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Standing Committee on Finance
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Dear Sirs

CALL FOR COMMENT: 2011 TAX RELATED BUDGET PROPOSALS

We would like to firstly thank you for the invitation to present both written and oral comments to the Standing Committee on Finance ("SCoF") on the fiscal framework and revenue proposals as was announced by the Minister of Finance on 23 February 2011.

It is difficult to provide meaningful feedback on the tax amendments proposed in the budget review, because the budget review merely advises of the areas identified for amendment, but does not provide details on how the amendments will be implemented.

GENERAL COMMENTS

We are of the opinion that the Budget was well balanced. We welcome the following proposals submitted by SAICA:

- learnership tax incentives;
- termination of the capital gain foreign currency rules;
- transfer of contingent liabilities;
- relief for outstanding debt between group companies.

We note however that there were no specific incentives for small business corporations (SBC's). For example the R14 million threshold for the taxation of SBC's at a more favourable rate than other corporations has last been altered in 2007, so an inflation-related adjustment was clearly necessary. In addition, SBC's begin paying 28% corporate tax when their taxable income exceeds R300 000. This taxable income threshold also needed to be increased to reflect inflation.

RELIEF FOR INDIVIDUALS

1. Personal income tax relief

SAICA welcomes the Minister's R8.1 billion in tax cuts to individuals which will partially assist consumers for the current inflationary pressure, including increased rates and taxes, electricity costs etc.

2. National health insurance

We welcome his further clarification on the National Health Insurance but are concerned as to the funding of this. Although this is planned to be phased in over 14 years, the 3 methods of proposed funding will create severe hardship on taxpayers, employers and consumers.

The proposal of National Health Insurance refers to payroll tax, an increase in VAT rate and a surcharge on individual's taxable income as possible funding options. Consideration should be given for alternative funding.

3. Savings

SAICA welcomes the Minister increasing the exempt portion of interest for taxpayers. However, these increases of between 2.24% and 3.12% are insufficient to encourage taxpayers to save in these tough economic times.

One assumes that the proposal to encourage people to save towards specific goals such as housing and education may take the form of an interest deduction incurred on the funding of such expenditure. These options should not replace the current tax free interest exemptions.

4. Social security and retirement

4.1. Tax treatment of contributions to retirement funds

Current non-contributory funds whereby employers have an obligation to make contributions to employee's retirement as per the fund rules will be regarded as a fringe benefit. Employers will then merely restructure to ensure that employee's has the obligation to pay the contributions to the retirement fund. It is unclear as to whether the employee's deduction includes employer contributions.

Employee contributions to provident funds are currently not tax deductible, but the budget proposes that as from 1 March 2012 employees will be entitled to deduct up to 22,5% of their taxable income for their contributions to pension funds, provident funds and retirement annuities. Employees will be able to deduct a minimum

amount of R12000 per annum (even if R12 000 is more than 22,5% of the specific employee's taxable income) and a maximum amount of R200 000 per annum. These changes effectively caps contributions of employees with taxable incomes in excess of R 888 888, both in regard to pension/provident funds and retirement annuity funds (if the employee has high non-retirement funding income). This will have a major impact on the funding for retirement of such taxpayers and will not incentivise retirement savings at this level.

5. Adjustment of monetary thresholds

We welcome the proposal to increase the CGT (Capital Gain Tax) exclusions but note that the primary residence exclusion has not been increased.

6. Gambling

Generally if you are a professional gambler (trade) then winnings should in any event be taxed as gross income. Will this type of gross income also be subject to the proposed 15% withholding tax?

Consideration should be given on practicalities of implementing the 15% withholding taxes. Upon cashing in chips with cashier, how will the cashier know whether these were winnings or the persons own cash?

7. Business taxes

7.1. Dividends Tax

SAICA welcomes the fixing of the date for the introduction of the dividends tax. However, it is unclear whether the 3 months notice required will be provided by December 2011 (proposed date 1 April 2012).

Inbound dividends: The wording implies that inbound dividends will be taxed at 10%, in line with the local dividends. However, where Double Taxation Agreements apply to reduce the rate the local tax will be more than the offshore tax. Is this the intention? Furthermore, currently where the shareholding is greater than 20% the dividend is tax free (subject to certain provisos). This is based on the fact that controlled foreign company legislation may apply etc. This should surely remain.

7.2. Closure of dividend scheme

In closing the alleged dividend schemes involving preference shares, the cost of the preference share funding for valid BEE transactions should not be increased by taxing the preference share dividends.

Will investors be given time to move their investments should they be deemed to be income?

8. Research and development tax incentive

The proposal that the Department of science and Technology (DST) approve research and development (R&D) submissions prior to the return being submitted may give rise to significant delays in submission of the return. This will, of course depend on at what point DST must approve. However, the process may lead to the allowance becoming unwieldy to claim and taxpayers 'not bothering' which defeats the objective of the incentive. Perhaps if SARS is concerned about the validity of claims, it should rather engage DST in the audit process, to ensure DST agrees that claims are technically valid. A further proposal is to implement a threshold limit that requires DST approval.

9. Fuel tax

The increase in the Fuel levy of 10 cents per litre and 8 cents in the RAF (Road Accident Fund) will further exacerbate the current inflationary pressures consumers are experiencing. This in itself will have a multiplied inflationary effect on the economy and affect food prices amongst other costs.

10. Value Added Tax

10.1. Input tax on fixed property

We welcome the de-linking of the transfer duty liability from the VAT treatment. The limitations placed on the input tax deduction. The proposed bases of limiting the *quantum* of the input tax deduction does not support the general concept of only taxing value added in the overall supply chain. Especially the proposed limitation linked to (1) the current municipal value of the property and (2) the VAT-inclusive acquisition price, including improvements, by the non-vendor selling the property bears no resemblance to the true value of the property supplied. If any limitations are to be imposed, it should only apply to transaction between connected parties and the limitation should be linked to market value.

10.2. Synchronising VAT and customs for temporary import relief

The proposed amendment is welcomed and reflects recognition of changes in the operating environment.

10.3. Minimum exemption for imported services

The proposal is welcomed and will legitimize/de-criminalize many day-to-day transactions by individuals.

10.4. Relief for outstanding debt between group members

The proposed amendment is welcomed on the condition that it is enacted this time round.

10.5. Revised starting date for alternative apportionment methods (administration)

While we understand the rationale for the proposed amendment, from a practical point of view this would be very difficult to administer. We recommend that a more meaningful approach would be to treat such amounts as recoveries or recoupment in terms of section 8 of the Income Tax Act, taxing such amounts in the fiscal year in which it occurs.

Please do not hesitate to contact us, should you have any questions regarding the above.

Yours faithfully

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The South African Institute of Chartered Accountants