



Driving progress
Budget 2018/19

Consolidated Commentary
South Africa

Preface

The South African Minister of Finance, Malusi Gigaba, delivered his 2018 Budget Speech to Parliament on Wednesday, 21 February 2018.

In this summary, we highlight some of the tax proposals mentioned in his speech and set out in the detailed Budget Review document.

Please do not hesitate to contact us, should you require any additional information relating to any aspect covered in this summary.

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* Deloitte comments are indicated in *Blue Italics*

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Personal Income Tax

General

The marginal tax rates applicable to individuals remain unchanged across all tax brackets.

However, the first three income tax brackets (as well as the tax rebates) will see a below inflation adjustment of 3.1%, whilst the top four income tax brackets will remain unchanged (see tax tables in the Deloitte Quick Tax Guide 2018/19).

Comment: There is little benefit all round: the new tax tables provide no relief for higher income earners for fiscal drag, whilst the lower than inflation increase to the lower income tax brackets provide little respite to individuals who will utilise their net take-home cash salaries to fund basic commodities (which will rise in cost due to inflation and the higher VAT rate).

Changes to the medical scheme fees tax credit

In the prior year budget, it was cautioned that the medical scheme fees tax credit may be reduced in the future, as part of the funding framework for National Health Insurance.

This year we see a below inflation increase to the medical scheme fees tax credit (see tax tables in the Deloitte Quick Tax Guide 2018/19) for these purposes.

In addition, and in an attempt to curb abuse by taxpayers, it is proposed that the medical scheme fees tax credit (the medical scheme fees tax credit allowed for contributions made to a registered Medical Aid Scheme and the additional medical expenses tax credit) be apportioned in instances where multiple taxpayers contribute towards the medical aid or medical expenses.

Comment: The below inflation adjustment to the medical scheme fees tax credit is not matched with what is often an inflationary/above inflation increase in medical aid contributions. Taxpayers are thus obtaining little real benefit from the increase in the medical scheme fees tax credit.

In addition, whilst the proposed change to apportion the medical scheme fees tax credit seems fair, it will be administratively difficult for employers to effect such an apportionment where the medical scheme fees tax credit is claimed against the employees' tax payable, as employers would not be privy to the information required for such an apportionment.

Retirement reforms

The following amendments are proposed in relation to the retirement reforms:

- The interaction between the Income Tax Act and the Double Tax Agreements will be reviewed to ensure that a tax deduction is only allowed against pay-outs from foreign retirement funds which are taxable (and not against pay-outs where an exemption applies).
- Retrospective legislative changes will be made to correct unintended tax liabilities that arose in an employee's hands, due to the current wording of legislation in instances where funds were transferred between/within retirement funds of the same employer.
- When an individual formally emigrates from South Africa, such an individual may withdraw the full lump sum benefit of a retirement annuity. It is proposed that the tax treatment across the different retirement funds be aligned under these circumstances.
- In 2017, amendments were made to permit the tax efficient transfer from a retirement fund to a retirement annuity fund, subject to the fund rules, where individuals have elected to retire on a date other than normal retirement age. It is now proposed that such tax-free transfers also apply to transfers to a pension preservation fund or provident preservation fund.

Comment: The proposed alignment of the tax implications across various retirement funds is welcomed.

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Employee housing – removing the fringe benefit for low interest loans

In an attempt to promote the provision of housing to employees, it is proposed that no low interest/no interest loan fringe benefit be accounted for in instances where loans (of less than R450 000) are granted to employees to fund the acquisition of housing. However, it should be noted that the proposed amendment will only apply to lower income earners whose remuneration proxy does not exceed R250 000.

Comment: This proposed amendment is welcomed.

Adjusting the official rate of interest

It is proposed that the definition to the “official rate of interest” (which is, for instance, utilised to calculate the value of a low interest/no interest loan fringe benefit) be amended to reflect a rate closer to the prime rate of interest.

Comment: The proposed amendment will increase the fringe benefit on low interest loans and will also affect the amount of the deemed donation of individuals who have interest-free loans to trusts, which is also based on the official rate of interest.

Employment Tax Incentive

It is proposed that the employment tax incentive will be reviewed before it expires on 28 February 2019, as the impact of the incentive is currently greater in smaller firms when compared to larger firms.

In addition, it is proposed that the six special economic zones, which the Finance Minister will approve, will benefit from an employment tax incentive for workers of all ages.

Comment: The proposed amendments are welcomed.

Company Tax

Business (General)

Amendments resulting from the application of debt relief rules

In 2017, amendments were made to the Income Tax Act to address the tax consequences of applying debt relief rules. Concerns have been raised about the unintended consequences which may arise from the application of these tax amendments and it is proposed that further amendments be made to address these concerns.

Comment: Further amendments are urgently needed to address the ambiguities and uncertainties raised by the 2017 tax amendments. For example, the mere subordination of a debt or a minor change to the terms of a debt could now trigger a taxable debt benefit in the hands of the debtor. This is an undesirable situation and, apart from being inequitable, undermines tax certainty.

Refining anti-avoidance rules dealing with share buybacks and dividend stripping

Amendments to the dividend stripping and share buyback rules were brought about by the 2017 Taxation Laws Amendment Act, which have significantly widened the ambit of the anti-dividend stripping rules.

The corporate reorganisation rules, contained in sections 41 to 47 of the Income Tax Act would, in the past, have provided some protection from the anti-dividend stripping rules but this is no longer the case as the anti-dividend stripping rules now override the corporate rule provisions.

The amendments were made in order to prevent taxpayers from stripping out dividends of a target company resulting in a devaluation of the company before disposing of the company's shares.

Government has noted concerns that the above changes may affect some legitimate transactions and arrangements. As a result, it is proposed that the interaction of these anti-avoidance rules and the corporate reorganisation rules be reviewed. In

addition, anti-avoidance rules dealing with share buybacks and dividend stripping regarding preference shares should be clarified.

Comment: We agree that an urgent review of the 2017 tax changes are required as they are making it difficult, if not impossible, to rationalise and simplify corporate groups without triggering unwanted tax charges. For example, the liquidation or deregistration of group companies is now often not possible without triggering tax charges. This undermines the very purpose of the corporate reorganisation rules, which is to facilitate tax neutral corporate restructures.

Refining rules for debt-financed acquisitions of controlling interest in an operating company

Following the proposed suspension of intra-group transactions in 2012, a special interest deduction was introduced instead of allowing implementation of debt push-down structures, applicable where companies used debt funding to acquire a qualifying controlling interest in an operating company.

For this purpose, section 24O defines an "operating company" as a company of which at least 80% of the receipts and accruals constitute income in the hands of that company.

It is proposed that the provisions of section 24O will be amended to clarify when this test should be applied and whether this test should be applied when an operating company transfers its business as a going concern to a company that forms part of the same group of companies as that operating company.

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Addressing the abuse of collateral lending arrangement provisions

There are no income tax and securities transfer tax implications for a period of 24 months if a listed share is transferred as collateral in a lending arrangement. This means that if a foreign shareholder takes out a loan with a South African resident company using listed shares as collateral, the foreign shareholder can reduce its dividends tax rate to zero.

Under this arrangement, the resident company receives a tax-free dividend and pays an amount (called a manufactured dividend) based on the dividend received by that resident company to that foreign company.

It is proposed that the legislation be amended to prevent this form of abuse.

Business (financial sector)

Clarifying the tax treatment of doubtful debts

In 2015, the Commissioner's discretion in relation to the section 11(j) doubtful debts allowance was deleted with effect from a date to be announced. The Commissioner's discretion was deleted to allow for the allowance to be claimed according to criteria set out in a public notice issued by the Commissioner. No criteria have been formulated for the claiming of the allowance.

To provide certainty, it is proposed that the criteria for determining the allowance should instead be included in the Income Tax Act.

***Comment:** At present, different SARS offices apply different criteria in the amount that they will allow as a doubtful debts allowance. We welcome the certainty that this will give taxpayers on what would constitute a permissible allowance, assuming that the proposed criteria will be clear and unambiguous.*

Clarifying tax amendments relating to long-term insurers

The Income Tax Act was amended to introduce the risk policy fund for long-term insurers, effective from 2016. The tax treatment of long-term insurers was also amended due to the introduction of the solvency assessment and management framework (SAM). Recent amendments affecting the risk policy fund did not take effect when the fund was introduced.

It is proposed that the effective date of the relevant amendments be so changed.

Review of the provisions of the Income Tax Act referring only to the Johannesburg Stock Exchange

Certain provisions of the Income Tax Act refer to the Johannesburg Stock Exchange Limited or JSE Limited listing requirements.

Following the introduction of additional stock exchanges in South Africa, it is proposed that the relevant tax provisions be reviewed to include the newly introduced stock exchanges, subject to certain regulatory and transparency criteria.



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Tax treatment of amounts received by portfolios of collective investment schemes

In 2009, the Income Tax Act was amended to provide for collective investment schemes operating on behalf of investors with participatory interests. Amounts (other than capital amounts) are taxable in the portfolio of a collective investment scheme unless they are distributed to participatory interest holders within 12 months of accrual.

Some collective investment schemes are trading frequently and, according to National Treasury, are arguing, contrary to current case law, that the profits are of a capital nature.

It is, therefore, proposed that the current rules be clarified to provide certainty on the treatment of trading profits in this context.

Comment: It is not clear what form the proposed "clarity" will take. This could be contentious should it result in income treatment for gains that, in terms of established precedent, should be taxed on capital account. It could also lead to ancillary tax amendments insofar as the distribution of such income gains are concerned. One hopes that any proposals will be circulated in a timely fashion and that National Treasury will consult widely before enacting any changes.

Business (Incentives)

Review of venture capital company rules

There has been an increased utilisation of the venture capital company tax incentive regime. However, administrative and technical issues are hindering further uptake. It is proposed that the legislation be amended to address rules relating to the investment income threshold limitations in the qualifying company test, as well as when the controlled company test needs to be applied. The rules relating to the connected person test also need to be reviewed, specifically the rule for retroactive withdrawal of venture capital company status.

Reviewing the write-off period for electronic communication cables

Companies providing telecommunications infrastructure have been moving from copper cabling to fibre optic cables. In order to align the write off periods with international practice and technological advances, it is proposed to reduce the period over which electronic communication lines and fibre optic cables are written off for tax purposes. Further alignment between taxpayers that own these assets and those with the right to use them will be considered.

Increasing the distribution period for small business funding entities

In order for the receipts and accruals of small business funding entities to be exempt from tax, these entities are required to distribute (or incur an obligation to distribute) 25% of all amounts received or accrued from assets held during the tax year, excluding amounts from disposing of any of the assets held during the same tax year.

Practical difficulties arise when a small business funding entity receives an amount on the last day of the tax year and is consequently required to distribute or incur an obligation to distribute on the same day.

It is, therefore, proposed that small business funding entities be required to distribute 25% of all amounts received or accrued from assets held during the tax year within 12 months of the end of the relevant tax year.

International tax

Transfer pricing

The Minister of Finance has pointed out that transfer pricing remains an area of keen focus for Government and SARS to ensure that the South African tax base is not eroded as a result of tax residents entering into non-arm's length arrangements with their foreign related parties.

He has specifically mentioned country-by-country reporting as part of the new mandatory transfer pricing documents which certain taxpayers are required to file with SARS.

Furthermore, the Minister has highlighted that inflated interest payments by local taxpayers to their related party lenders offshore should be prevented.

A technical amendment is also proposed relating to the secondary transfer pricing adjustment in the form of a deemed dividend in specie in terms of section 31 of the Income Tax Act.

As background, such deemed non-cash dividend gives rise to a dividends tax obligation in the hands of the company which is deemed to be paying the dividend. Technically, there is a potential overlap between the treatment of an actual dividend, as defined in section 1 of the Act, and the deemed dividend in specie provision under section 31 the Act.

Therefore, to prevent such overlap, it is proposed that an amount should be treated as a dividend in specie under section 31 of the Act, unless the amount already constitutes a dividend as defined in section 1 of the Act.

Comment: *It was widely expected that the Minister would focus on transfer pricing given our active participation in BEPS and all the regulations that have been issued around mandatory transfer pricing documentation to be prepared and filed with SARS, where applicable. Affected taxpayers are advised to prepare robust transfer pricing documentation in the form of a master file, local file and country-by-country reporting in order to be well-positioned to meet the new*

return filing deadlines. The additional administrative compliance in this regard should not be underestimated.

Regarding interest payments on cross-border loans between related parties, taxpayers are looking forward to the long-awaited guidance on thin capitalisation to be published by SARS. The Minister announced that a discussion document inviting comments will be published soon. Certainty in this area is crucial in attracting foreign investors to South Africa.

Lastly, the technical amendment above regarding the secondary transfer pricing adjustment in the form of a deemed dividend in specie only applying where an amount does not already constitute a "dividend", as defined in section 1 of the Act, is welcomed to avoid uncertainty in the treatment thereof.

Reversing exchange difference for exchange items disposed of at a loss

Following a proposal in the 2016 Budget, the Income Tax Act was amended to make it clear that previously taxed foreign exchange gains and losses on debts would be reversed if such debts became bad. The amendment did not extend to the case where an exchange item, e.g. a foreign denominated debt, had to be disposed of at a loss due to market forces.

It is therefore proposed that the application of the relief be clarified further.

Comment: *It is to be welcomed that the legislation also provide clearly for the reversal of previously taxed exchange differences on the disposal of an exchange item at a loss as a result of market related factors outside of the taxpayer's control.*

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Review of the definition of “international shipping income”

As background, a South African ship has to be registered as South African in terms of the above definition in order for a local shipping operator to qualify for the income exemption applying to international shipping.

However, in practice, the South African ship may at times not be operational temporarily and the local shipping company may only be able to find a foreign registered replacement ship on short notice.

Based on the current legislation, the operator will not qualify for the tax exemption while using the foreign registered replacement ship. Accordingly, it is proposed that the definition of “international shipping income” be extended to address the above scenario.

Comment: Shipping companies will welcome the proposed widening of the ambit of the tax exemption to circumstances where they have to use a foreign registered replacement ship temporarily due to unintended operational issues.

Taxation of short-term insurers

The current tax legislation on short-term insurance only applies to those resident in South Africa. However, the Insurance Act allows non-resident reinsurers to operate in South Africa through branches.

Accordingly, it is proposed that the tax legislation should be extended to apply similarly to foreign entities operating short-term insurance businesses through permanent establishments locally.

Comment: The alignment of the tax legislation on short-term insurance with the provisions of the Insurance Act on foreign reinsurers will be welcomed.

Extension of the application of controlled foreign company (CFC) rules to foreign companies held through foreign trusts and foundations

With effect from tax years commencing on or after 1 January 2018, the CFC rules have been extended to foreign companies held by foreign trusts and foundations, interposed between the foreign companies and South African residents. The draft legislation also contained related rules to classify distributions by discretionary foreign trusts or foreign foundations to resident individuals or trusts as income in their hands.

These draft rules did not come into effect and will be considered further in 2018.

Comment: The aim of the draft rules in question is to discourage the use of foreign trusts by local taxpayers to defer a tax liability or to recharacterise the nature of their income. For the final legislation in this regard to be effective, it should not be too complex or broad in its application.

Interest paid to the non-resident beneficiary of a trust

Based on current legislation, it is not clear who bears the obligation for the withholding tax on interest where interest is paid to a non-resident beneficiary of a trust. The related rules do not deem the trust to have paid the interest to the non-resident beneficiaries. It is proposed that this anomaly should be addressed.

Comment: It is advisable for the legislation to be amended for it to be applied effectively in this regard.

Controlled foreign company comparable tax exemption

South African investors with controlled companies operating in countries where tax payable is less than 75% of the tax that would be payable in South Africa are required to include the foreign net income in their South African income. This limit is to be reviewed in the light of lower corporate tax rates globally to determine whether a reduction is warranted.

Exchange Controls

The 2018 budget speech contained no dramatic exchange control announcements but the following three items were included and are of importance:

1) Increasing the prudential limit for institutional investors

The term “institutional investors” is a collective name for investment managers/fund managers, collective investment scheme management companies, the investment linked business of long-term insurers and retirement funds.

Institutions registered with the Financial Surveillance Department of the Reserve Bank as institutional investors have been able to make offshore investments in the past within a prudential limit.

The limit imposed on retirement funds and the underwritten policy business of long-term insurers has been 25%, whilst the institutional investors other than the aforementioned had a limit of 35%. In addition, these institutions could invest an additional 5% in the so-called African allowance, which enabled and restricted them to investments in Africa.

These limits have now been increased by a further 5%.

Comment: This development will certainly be welcomed by institutional investors as it provides them with additional capacity for foreign investment.

2) Relaxation of “loop structure” policy pertaining to companies and private equity funds

A loop structure is where a South African resident invests in South Africa via an entity outside South Africa.

To date, the only concession with regards to loop structures has been for South African companies investing abroad. Companies are permitted to invest in a foreign entity which holds an investment in South Africa provided that the South African investor holds a minimum of 10% and a maximum of 20% of the voting securities in the foreign company.

This has now been relaxed and the minimum holding of 10% is abolished, whilst the maximum of 20% has been increased to 40%.

Comment: The abolishment of the minimum 10% holding in foreign companies will probably be more appreciated by South African investors than the increase in the “loop” limit to 40%. This has been a stumbling block for many a South African company wishing to take up a small percentage holding in very large foreign companies in the past. The inclusion of private equity funds in this dispensation is a further welcome relaxation of the foreign investment policy.

3) Relaxations pertaining to the Holding Company regime (also known as Domestic Treasury Management Company)

The current limits applicable to transfers into holding companies are R2 billion for JSE-listed companies and R1 billion for unlisted entities. These limits have now been increased to R3 billion and R2 billion respectively, and the concession will be expanded to also include financial service companies.

Comment: Whether the increase in the limits now announced will have a material effect on the interest shown in this dispensation by local companies remains to be seen. The addition of financial service entities may, however, increase the number of interested parties.

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Strengthening tax morality

As announced in the State of the Nation Address, a commission of inquiry is to be established to examine the functioning and governance of SARS, with steps being taken to improve governance and accountability at this organisation. Government has also undertaken to strengthen the operational independence of the Tax Ombud, as recommended by the Davis Tax Committee.

Furthermore, to ensure proper governance and accountability at public entities, government proposes that fruitless and wasteful expenditure will not qualify for a tax deduction.

Comment: The above proposed measures will go a long way towards restoring tax morality, impacting tax compliance levels and revenue collection.

Estate duty and donations tax

Government proposes to increase the estate duty from 20% to 25% for estates worth R30 million and above. To limit abuse, any donations above R30 million in one tax year will also be taxed at 25%. Both measures will be effective from 1 March 2018.

Comment: The proposed amendment is in keeping with the approach of imposing a greater tax burden on the wealthy.

Repeal of requirement to submit dividends tax returns by persons receiving exempt dividends

The administrative burden for persons receiving exempt dividends is to be alleviated through the repeal of the requirement for such persons to submit dividends tax returns.

Notification of commencement of audit

In an effort to keep all parties informed, it is proposed that taxpayers be notified of the start of an audit.

Deregistration of non-compliant tax practitioners

It is proposed that amendments be introduced that allow for the deregistration by SARS of habitual non-compliant tax practitioners that do not correct their behaviour after being notified thereof.

Obligations of funds managed by bargaining councils

The correct tax treatment of employee and employer contributions to, and payments from bargaining council funds has been the subject of consultations with bargaining councils.

While it is felt that the majority of existing funds can be accommodated by withholding taxes at the employer level, transitory arrangements will be considered for a small minority of more complicated fund types to ensure smooth implementation.

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Increase in the VAT rate

The VAT rate has finally been increased, with effect from 1 April 2018, from 14% to 15%. This increase is expected to generate an additional R22.9 billion revenue over the 12 month period. The previous increase was from 10% to 14% on 7 April 1993.

The new rate of 15% is still relatively low in comparison to African and European countries, and is now equivalent to the New Zealand VAT rate. The Minister indicated that the regressive nature of the increased rate would be alleviated by increased social grants and the existing zero-rated basic foodstuffs.

Although no additional zero-rated foodstuffs were proposed, there is an intention to remove products such as rye or low-GI bread from the existing list of zero-rated foodstuffs.

The increase in the VAT rate will result in additional administration for vendors in revised pricing, bearing in mind that any price advertised or quoted by a vendor is deemed to include any tax payable.

The VAT Act (sections 67 and 67A) contains transitional provisions in respect of existing contracts, statutory tariffs and fees, the supply of goods and services which straddle the period and the sale of fixed property. Anti-avoidance measures, which seek to prevent vendors manipulating the time of supply in order to avoid the increased VAT rate, are also included in these provisions.

Potential double deduction on written off debts

Vendors acquiring debts (which have previously been written off by the seller) on a non-recourse basis, have been seeking to claim a further input tax deduction, when they write off all or part of that debt. It is proposed that legislation will be introduced in order to prevent the claiming of such double deductions.

Housing subsidies

During 2015, amendments were introduced to remove the zero

rating on low cost housing subsidies. Amendments introduced in 2017, however, sought to postpone the abolition of such zero rating until 1 April 2019. It would now appear that, due to budgetary constraints, the abolition of the zero rating will take effect from an earlier date, which will be announced by the Minister.

Correction of tax invoices

It is intended that legislation will be introduced which clarifies the process in respect of cancelling incorrect tax invoices and re-issuing tax invoices containing the correct information.

Joint Venture – members jointly and severally liable

An amendment is proposed to clarify that members of a joint venture may be held jointly and severally liable for the VAT liabilities of that venture. In view of the interpretational difficulties surrounding the nature of a “joint venture”, it is hoped that the amendments will include a concise description of the term.

Electronic Services

In the 2017 Budget Speech, it was announced that in order to expand the tax base and to address base erosion and profit shifting, the scope of electronic services supplied by non-residents to residents, which were subject to VAT, would be expanded to include “cloud computing and services provided using online applications”.

In his 2018 Budget speech, the Minister has now announced that such amendments have been drafted.

The draft Regulation widens the definition of electronic services to include any services supplied by means of an electronic agent, electronic communication or the internet, other than –

- a) Educational services supplied by a person regulated by an educational authority in an export country; or
- b) Telecommunication services.



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VAT debts of branches and divisions

The VAT Act permits the separate registration of branches and divisions within a single juristic person. An amendment is proposed in order to clarify that any VAT debt incurred by a branch or division may be collected by SARS across all the branches or divisions.

Credit notes issued by a purchaser of a going concern

It is intended that legislation will be introduced which permits the purchaser of a going concern to issue credit notes in respect of goods sold by the seller of the going concern and returned to the purchaser of such going concern.

Cryptocurrency transactions

Digital currencies do not fall within the ambit of the definition of “money” contained in the VAT Act nor do they fall within the definition of “goods” as they are not “corporeal” things. They may fall within the definition of a “service”, which is extremely broad and includes “anything done or to be done”.

The issue then is whether they constitute “financial services” and are thus exempt from VAT. Although the definition of a financial service includes the exchange of currency, the definition of “currency” is restricted to “any banknote or other currency of any country”. Cryptocurrency would not appear to fall within this definition of currency.

A financial service also includes a “debt security” which in turn includes “an interest in or right to be paid money”. Although a typical cryptocurrency does not provide its owner with any inherent right to property or another currency, it may be said to include an “interest” in being paid money. On this broad interpretation, the acquisition of the cryptocurrency would not attract VAT.

The sale of goods or services by a vendor in return for a cryptocurrency would attract VAT but there could be issues around the time and value of the supply.

In any event, the Minister has recognised the difficulties surrounding cryptocurrencies and stated his intention to introduce amendments which would seek to clarify the tax treatment of cryptocurrency transactions. This follows a global trend of legislative bodies seeking to regulate these transactions.

Customs & Excise Duties and Levies

The Minister of Finance announced specific changes, and proposed others, to the current South African Customs and Excise legislation. These changes, discussed below, became effective immediately (unless specified otherwise).

Please note that simplified product descriptions and dutiable quantities are used below, and readers are advised to refer to the official product classifications and rates, as published by SARS, when actually classifying products and applying rates.

Specific Excise Duties

Alcoholic Beverages

The amended rates of excise duty on alcoholic beverages result in an increase in the duty-cost for the final consumer as follows:

	From:	To:	% Increase
Malt beer	R 1.47	R 1.62 per 340ml	10.2
Unfortified wine	R 2.71	R 2.93 per 750ml	8.1
Fortified wine	R 4.63	R 4.91 per 750ml	6.0
Sparkling wine	R 8.60	R 9.32 per 750ml	8.4
Other fermented beverages	R 1.47	R 1.62 per 340ml	10.2
Spirituous beverages	R 56.50	R61.30 per 750ml	8.5

The new rates of excise duty are effective immediately.

Tobacco Products

The amended rates of excise duty on tobacco products result in an increase in the duty-cost for the final consumer as follows:

	From:	To:	% Increase
Cigarettes	R 14.30	R 15.52 per 20	8.5
Cigarette tobacco	R 16.07	R 17.48 per 50g	8.8
Pipe tobacco	R 4.56	R 4.94 per 25g net	8.3
Cigars	R 75.86	R 82.32 per 23g net	8.5

The new rates of excise duty are effective immediately.

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Fuel Taxes

General Fuel Levy

The general fuel levy will increase by 22 cents per litre. Based on historic figures, the bio-diesel fuel levy stood at 50% of the diesel fuel levy and we have based the below figures on the assumption that the same percentage increase will occur in the 2018/19 financial year. This is, however, subject to confirmation as no reference has been made to this specific levy.

This will increase the general fuel levy rate to the following figures:

- Petrol R3.37 per litre
- Diesel R3.22 per litre
- Bio-diesel R1.61 per litre

The new fuel levy rates are effective on 4 April 2018.

Road Accident Fund (RAF) Levy

The RAF levy will increase by 30 cents per litre, resulting in a levy of R1.93 per litre.

The new RAF levy rates are effective on 4 April 2018.

Fuel Prices

The latest increase in fuel taxes shall lead to the following portion of tax forming part of the fuel price:

- Petrol R5.34 (Portion of tax based on current pump price: 38,4%)
- Diesel R5.19 (Portion of tax based on current pump price: 41,3%)

The diesel refund administration system

It was announced in the 2015 budget that the diesel refund administration system would be given a holistic reform, which would result in its separation from the Value-Added Tax (VAT) system under which it is currently administered. In February 2017, a discussion document was published for public comment which commentary has now been processed.

In 2018, National Treasury and SARS shall engage with industry and affected role players to further the reform process, the outcome of which will inform the design of the new system. This outcome will be announced within the 2019 Budget.

The introduction of a separate diesel refund system will supersede the provisions of the VAT Act specifically dealing with the diesel refund system. It is proposed that section 16(3)(l) of the VAT Act be repealed with effect from the date on which the new diesel refund system commences.



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Health and Environmental Levies

Health Promotion Levy

Government Gazette No. 41323, of 14 December 2017, confirmed that the Health Promotion Levy (Sugar Tax) will be implemented in South Africa on 1 April 2018.

The sugar tax / levy will apply to specified non-alcoholic beverages, and specified preparations for making such beverages, containing intrinsic or added sweeteners, imported into or manufactured in South Africa.

- Soft drinks (excluding un-flavored water);
- Diluted fruit and vegetable juices;
- Flavored milk; and
- Cocoa and other powders, as well as syrups and other concentrates, for making sweet beverages.

The levy will be assessed at a rate of 2.1 cents per gram of sugar / sweetener content above 4 grams per 100ml of the final beverage, and paid 'at source' (i.e. upon direct import or upon removal from a licensed import storage or local manufacturing warehouse) on the specified products intended to be consumed as a beverage in South Africa.

Certain deductions from the assessed or paid levy-amount (e.g. the levy assessed or paid on such specified exported product) will be allowed in order to ensure that the levy is effectively paid only on product actually consumed in South Africa.

***Comment:** We are of the view that if SARS adheres to the accepted 'tax-neutrality' principle, which prescribes that the administration of taxes should cause little disruption to business (and in order to achieve that, compliance requirements should consider and facilitate industry operational requirements), SARS will have to make further amendments to the current proposed regime for this levy.*

It is unlikely that such process will be completed before the current effective date of 1 April 2018 and, should the levy still be implemented, then it may have serious implications for industry's ability to comply as there is still uncertainty, in many areas, regarding the compliance requirements. Whilst a number of transitional requirements have to be complied with, the details of these requirements are still uncertain.

Plastic Bag Levy

The plastic bag levy will increase by 50% (to 12 cents per bag) with effect from 1 April 2018.

Incandescent Light Bulb Levy

The environmental levy on incandescent (non-energy saving) light bulbs will increase by 33% (to R8 per bulb) with effect from 1 April 2018.

Motor Vehicle CO2 Emissions Levy

The vehicle emissions tax will increase to R110 for every gram above 120 gCO₂/km for passenger vehicles, and to R150 for every gram above 175 gCO₂/km for double cab vehicles, with effect from 1 April 2018.

Carbon Tax

Cabinet adopted the Carbon Tax Bill in August 2017. Parliament has convened hearings following the release of the draft bill in December 2017. It is expected that the bill will be enacted before the end of 2018 and Government proposes to implement the tax from 1 January 2019 in order to meet its commitments under the 2015 Paris Agreement of the United Nations Framework Convention on Climate Change.



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Acid mine drainage levy

Government will publish a discussion document outlining design options for the proposed acid mine drainage levy to make polluters pay for the cost of environmental damages, and to help fund treatment of acid mine water.

An environmental fiscal reform policy brief will be published in the near future. The paper will examine fiscal and regulatory options to improve water resource management, mitigate the emission of pollutants and reduce waste.

Ad Valorem duties on luxury goods

Government proposes to increase the current ad valorem excise rate on luxury goods (as a substitute to applying a higher VAT rate to these products) which are consumed mainly by wealthier households.

Examples of luxury products listed comprise cosmetics, electronics and golf balls. It has been noted that the associated tax revenue potential is not significant, but aligns with the current progressive tax structure.

The tariff classification of cellular telephones will be updated to include smart phones to ensure ad valorem duties are paid thereon. Government intends commencing with a consultation process to replace the current flat rate on cellphones to that of a progressive rate structure based on the value of the phone.

The following ad valorem rate changes will take effect on 1 April 2018:

	From:	To:	% increase:
Motor vehicles	25%	30%	20%
Other Luxury products (current rate of 5%) Examples: fireworks, eye and lip makeup preparations	5%	7%	40%
Other luxury products (current rate of 7%) Examples: Perfumes, cellphones, yachts, golf balls.	7%	9%	29%



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Diamond Export Levy

The Diamond Export Levy Act, No. 15 of 2007 distinguishes between large, medium and small producers, based on turnover thresholds. The larger the producer, the more stringent the requirements for sales to local cutters and polishers. To avoid penalties, specified percentages of the value of the various producers must be sold to diamond beneficiation licence holders (local cutters and polishers).

As a result of diamonds being traded solely in US dollars, the rand depreciation against the dollar has effectively halved the turnover thresholds in US dollar terms since 2007.

It was proposed that the thresholds be adjusted in order to reflect the original US dollar equivalents to retain the policy intent.

Customs General

Customs Modernisation

Government aims to take steps to implement the customs modernisation programme (as implemented under current legislation) in order to give effect to the new customs and excise legislation passed in 2014.

Measures to enhance tax administration

Amendments to the Customs and Excise Act will be considered to prevent “forestalling” – a practice through which abnormal volumes of products are moved from warehouses into the market to avoid increases in excise duty rates.

Legislative changes will be made to extend the use of “fiscal markers”, which are required under the tracking and tracing obligations of the World Health Organisation’s Protocol to Eliminate Illicit Trade in Tobacco Products. The extension will enable fiscal marking of other products

Investment and Innovation Incentives

Incentives Regime

A review of the incentive ecosystem was announced during the Medium Term Budget Policy Statement and this was intended to assess performance, determine value for money, and analyse how the system as a whole supports the economy and job creation. In line with this, no significant change was expected in the current budget and the funds allocated to incentives confirm this.

Three key incentive reviews have been announced –

- a review of business incentives by the Department of Planning, Monitoring and Evaluation;
- a review of section 12I by the Department of Trade and Industry and National Treasury; and
- a review of the Automotive Production Development Programme (this is the largest tax expenditure item).

These reviews will inform the structure, scale and focus of all future incentives.

Carbon Tax

Although the Bill has not yet passed through Parliament, government intends to start the Carbon Tax from 1 January 2019. The second Draft Carbon Tax Bill was submitted to Parliament on 12 February 2018 although comments can still be made on the draft bill until 9 March 2018. It is expected that Parliament will hold public hearings and make a decision on the Carbon Tax during 2018.

The Carbon Tax will, effectively, levy a tax of between R6 and R48 per tonne of Carbon Dioxide equivalent emissions.

Comment: In our opinion, there are still many practical problems that have not been resolved in the second draft Carbon Tax Bill. In addition, a lot of the regulations and rules surrounding the tax are still outstanding. Of significant concern is the large number of entities that have been caught in the Carbon Tax net in the new draft, which would not originally have been taxed. This includes most companies that are liable for the Department of Environmental Affairs' Mandatory Greenhouse Gas reporting. We do not believe the full extent of this scope change has been explored yet, and there is the potential of significant unintended consequences.

Venture Capital Incentive

The Venture Capital Incentive has been in place since 2008 and provides a tax deduction for buying shares in venture capital companies. These venture capital companies need to invest the funds in qualifying small businesses in order to enable small businesses to expand and contribute to economic growth and job creation.

Following recent amendments, there has been a substantial increase in the use of the Venture Capital Incentive. The window for establishing new Venture Capital Companies terminates on 30 June 2021.

Changes in the legislation are expected in order to address rules relating to the investment income threshold limitations in the qualifying company test, as well as when the controlled company test needs to be applied.

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Research & Development

South Africa aspires to be a preferred destination for foreign investment in research and development (R&D) although it faces tough competition. South Africa's 150% super deduction is matched by most developed countries.

From a BRICS perspective, Russia and China also offer a 150% super deduction. India offers a 200% deduction and Brazil 175%. Singapore and the United Kingdom, both established markets where global R&D takes place, offer a 400% and 350% deduction respectively.

Given the country's inability to achieve a 1% of GDP spend on R&D and to ensure that at least 1.5% of GDP is spent on R&D in the future, the Minister of Science and Technology appointed a task team in 2016 to advise on the improvement of R&D incentives. Various changes were proposed to ease the administrative burden of claiming the incentive, to simplify the incentive and to provide clarity on what type of R&D will be incentivised.

The Minister of Science and Technology is hosting a breakfast on 2 March 2018 to discuss enhancements made to the R&D tax incentive, which is a clear indication that there will indeed be changes to the incentive programme.

Additionally, a new incentive to support small and medium business in the start-up phase has been announced. A budget of R2.1 billion has been allocated over the medium term.

Infrastructure Investment

Infrastructure Investment Support provides grants for two industrial infrastructure initiatives:

- The Special Economic Zones (SEZ)
- The Critical Infrastructure Programme

These are aimed at enhancing infrastructure and industrial development, and increasing investment and exports of value-added commodities.

Government's aim is to stimulate investment growth by supporting infrastructure projects that are critical, thereby lowering costs of doing business in South Africa.

In 2018 budget speech, the Minister allocated R4.9 billion, a 17% increase from prior year, over the medium term for industrial infrastructure projects. Of this, R4.2 billion has been allocated to SEZ, increasing the SEZ budget significantly by 56%.

The Minister of Finance has approved a 15% reduced corporate tax rate for qualifying companies in the six special economic zones (Coega, Dube Trade Port, East London, Maluti-a-Phofung, Richards Bay and Saldanha Bay). Over the next medium term, three additional SEZ sites (the proposed sites are Nkomazi, Atlantis and Mogwase) will be approved. These SEZs will benefit from additional tax incentives, including an employment tax incentive for workers of all ages.

Manufacturing Investment

In the State of the Nation Address, government committed to tackle the decline in manufacturing capacity by promoting greater investment in key manufacturing sectors through strategic use of incentives. A total of R3.6 billion has been allocated to the manufacturing sector in 2018/19.

It is expected that the majority of this will be targeted at the automotive sector, agro-processing sector as well as a program targeted at promoting the economic competitiveness of manufacturers.

Despite the stated focus on manufacturing, there has been a steep decline in support for the manufacturing sector since 2016. The current allocation is less than budgets that were made available in the sector in 2014/2015.



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Agriculture

Agriculture is seen as one of the key sectors that has the opportunity to create the greatest number of jobs. It is one of the few sectors where grant-funding support shows a growth trajectory.

An estimated R581.7 million has been budgeted for the reprioritisation of the black producer commercialisation programme thereby creating opportunities for black agricultural producers.

Furthermore, the Comprehensive Agricultural Support Programme aims to support newly established and emerging farmers, particularly subsistence, smallholder and previously disadvantaged farmers.

Over the next three years, government expects to spend more than R4 024 million on infrastructure under the Comprehensive Agricultural Support Programme. In addition, the Department of Agriculture, Forestry and Fisheries will over the next five years focus on creating and supporting 450 profitable black commercial producers enabling the participation in prioritised value chains as one of the key outcomes from Operation Phakisa.

Black Industrialisation

The 2018 State of the Nation Address reiterated the importance of transformation as part of the process of industrialisation. The funding for the Black Industrialists Scheme is provided under the DTI's manufacturing incentives and is an important measure towards developing a new generation of black industrialists that can produce at scale.

The Financial Sector Codes have been gazetted and a R100 billion Black Business Growth Fund has been created through the code. The fund will assist black entrepreneurs to finance big deals, an intervention that is crucial to transforming capital allocation in the economy.

Tourism

In the 2018 State of the Nation Address, Tourism was identified as another area which provides South Africa with incredible growth opportunities. Tourism currently sustains 700 000 direct jobs and is performing better than most other growth sectors.

The focus is to support key tourism markets, reduce regulatory barriers and develop emerging tourism businesses. R198 million has been allocated to tourism incentive programmes for the 2018/19 year. The tourism incentive programmes are aimed at developing an all-inclusive economy of tourism enterprises.

Jobs Fund

With government's focus on job creation other than the Expanded Public Works Program, the only existing job creation focused incentive programme is the Jobs Fund.

It was allocated R9 billion in June 2011. R2.9 billion of this is available and we are expecting the 8th round of the Jobs Fund to open at the end of February / beginning of March this year. The 50% grant ranges from R10 million up to R100 million and it will continue to focus on supporting initiatives that create jobs at scale i.e. any project that creates jobs at a low cost per job.

This guide is based on the Budget proposals tabled in Parliament by the Minister of Finance on 21 February 2018. These proposals are, however, subject to approval by Parliament. The information contained in this guide is for general guidance only and is not intended as a substitute for specific advice in considering the tax effects of particular transactions. While every care has been taken in the compilation of the information contained herein, no liability is accepted for the consequences of any inaccuracies contained in this guide.