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TAX AND EXCHANGE CONTROL ALERT

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WHERE THERE'S SMOKE THERE'S FIRE (AND CARBON TAX) – NATIONAL TREASURY RELEASES THE DRAFT REGULATIONS: CARBON OFFSETS

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GOOD NEWS FOR EMPLOYERS: INCREASE IN THRESHOLDS FOR EXEMPTION OF EMPLOYER-PROVIDED BURSARIES

On 8 July 2016, the National Treasury (Treasury) released the draft Taxation Laws Amendment Bill 2016 (TLAB). The TLAB aims to give effect to the various tax proposals announced in the 2016 National Budget.

CUSTOMS AND EXCISE HIGHLIGHTS

Below are this week's selected highlights in the Customs and Excise environment.

CDH
CLIFFE DEKKER HOFMEYR

WHERE THERE'S SMOKE THERE'S FIRE (AND CARBON TAX) – NATIONAL TREASURY RELEASES THE DRAFT REGULATIONS: CARBON OFFSETS

Any taxpayer who is liable for carbon tax can reduce their carbon tax liability by making use of the allowances mentioned in the Bill, including a carbon offset allowance of either 5% or 10%.

A carbon offset is an external investment that allows a firm to access GHG mitigation options at a lower cost than investment in its current operations.

In November 2015, the Draft Carbon Tax Bill (Draft Bill) was published by National Treasury, setting out the framework within which carbon tax would be levied. We reported on the main tenets of the Draft Bill in our Tax Alert of 20 November 2015 (Carbon tax in South Africa). On 20 June 2016, flesh was given to this framework with the release of the Draft Regulations: Carbon Offsets (Draft Regulations), which were published in terms of clause 20(b) of the Draft Bill. The Explanatory Note for the Draft Regulations on Carbon Offset (Explanatory Note) was released at the same time.

Section 4 of the Draft Bill states that carbon tax will be levied in respect of greenhouse gas (GHG) emissions resulting from:

- the combustion of fossil fuels;
- fugitive emissions in respect of commodities, fuel or technology; and
- industrial processes, and product use.

Any taxpayer who is liable for carbon tax can reduce their carbon tax liability by making use of the allowances mentioned in the Bill, including a carbon offset allowance of either 5% or 10%. Schedule 2 of the Bill sets out the percentage allowance that will be applicable to taxpayers in different sectors. The Draft Regulations set out the requirements to qualify for the carbon offset allowance and the documentation that a taxpayer would have to submit to the South African Revenue Service (SARS) in this regard.

Policy rationale and purpose of the carbon offset system

The Explanatory Note describes carbon offsets as investments in specific projects that reduce, avoid or sequester emissions. A carbon offset is an external investment that allows a firm to access GHG mitigation options at a lower cost than investment in its current operations. The carbon offset system also aims to incentivise mitigation in sectors or activities that are not directly covered by the carbon tax or are benefiting from other government incentives, especially transport, agriculture, forestry and other land use (AFOLU) and waste.

Eligibility – when will a taxpayer qualify for a carbon offset allowance?

Carbon offsets can only be generated by an approved project. The Draft Regulations define an approved project as a Clean Development Mechanism (CDM) project, a Verified Carbon Standard (VCS) project, a Gold Standard (GS) project or a project that complies with another standard approved by the Minister of Energy or a delegated authority. CDM, VCS and GS are existing accepted international carbon offset standards, each with their own associated institutional and market infrastructure. During the initial stage of the carbon offset scheme, it is envisaged that it will rely primarily on these existing standards and any offset project will need to be approved by one of these standards.

In terms of Regulation 1 of the Draft Regulations, an offset will be allowed in terms of s20 of the Draft Bill, in respect

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of any certified emission reduction (CER) derived from the furtherance of an approved project that is carried on by a taxpayer on or after 1 January 2017 if that project is wholly undertaken in South Africa or if that project is in respect of an activity that is not subject to the carbon tax. Where a project has been registered prior to the implementation of the carbon tax and offset credits issued in terms of the project have not been retired, those credits will be eligible, provided they are transferred from an international registry (CDM, GS or VCS) to the South African registry within 12 months of the implementation of the carbon tax. Projects that are currently under development and which will be registered before the start date of the tax and credits issued following the introduction of the carbon tax will have to be transferred from an international registry to the South African registry within 6 months of their issuance.

In terms of Regulation 4 of the Draft Regulations, projects benefitting from other government incentives, such as projects registered for the Energy Efficiency Savings Tax Incentive in terms of s12L of the Income Tax Act, No 58 of 1962 (Act), will not be eligible for the carbon offset allowance or activities conducted in terms of the Renewable Energy Independent Power Producers Procurement Programme (REIPPPP).

For how long may a carbon offset be used?

To address the issue of permanence pertaining to certain offset projects, the crediting period for carbon offset projects will require periodic reviews to ensure, most importantly that the baseline assumptions of the project are still valid. To give effect to this, Regulation 2 states that an offset generated by a CDM project may be used for a non-renewable 10 year period or for a 7 year period which is twice renewable, constituting a period of 21 years in total. The same crediting periods apply to any GS project. In the case of a VCS project, all non-AFOLU projects will have a 10 year crediting period which may be renewed twice and all other AFOLU projects may be credited for a minimum period of 20 years and a maximum period of 100 years which may be renewed four times. Any project approved under another standard will have a crediting period specified by the Minister of Energy or a delegated authority.

How does a taxpayer claim the carbon offset allowance?

Regulation 7 merely states that a taxpayer that intends to utilise an offset as a carbon tax allowance must register that offset with the administrator in the form and manner and at the place that the administrator may determine. In terms of Regulation 5, the Designated National Authority (DNA) within the Department of Energy will fulfil the role of administrator. The Explanatory Note summarises the envisaged process whereby the transfer of carbon credits and generation of carbon-offset certificates will take place as follows:

- Once emissions reductions are verified, the project developer may request the issuance of carbon credits, being CERs under the CDM, Verified Carbon Units (VCUs) under the VS and GS credits under the GS.

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- Upon approval of the project by the issuing bodies, the credits are deposited into the project developer's account in the relevant registry (CDM, VCS or GS).
- For the credits to be used to offset a tax liability under the South African carbon tax scheme, offset developers or entities responsible under the carbon tax will have to request credits to be cancelled in the international registry and then transferred to the South African registry.
- This will be a mirror system where one tonne CO_2 is transferred as such into the South African registry. These carbon credits will have to meet the local eligibility criteria and then are registered in the South African registry only after the DNA has received confirmation that the same credits have been cancelled in the respective international registry. Offset developers or entities must obtain a carbon-offset certificate from the DNA.

Record keeping

In order to administer the scheme, an offset registry will be created in terms of Regulation 8. The registry must reflect a number of things, including any offsets registered in terms of Regulation 5 and any offsets transferred in terms of Regulation 3.

From the taxpayer's perspective it will be crucial to obtain a certificate from the DNA, proving its entitlement to claim the carbon offset allowance. The Explanatory Note states that in order to obtain a certificate, project developers would apply to the DNA for a pre-screening letter that a proposed project would be eligible against the domestic eligibility requirements of the carbon tax. The project developers apply for an Extended Letter of Approval (ELOA) from the DNA to confirm domestic eligibility approval before a project is undertaken. The project is then undertaken under the rules and modalities of the international offset standard (CDM, VCS or GS) or an approved methodology for South African specific projects and then issued with credits under the respective standard. The project developer would then request for the international programme credits to be transferred into the domestic registry.

The DNA would then assess each request for transfer against the domestic eligibility criteria and would either accept or reject the transfer. If the transfer is accepted, the DNA will issue corresponding domestic carbon offset into the nominated account of the transferee in the domestic offset registry. The units issued into the domestic registry could be either linked to the specific CER, if this is a CDM project, or simply represent an undifferentiated CER held in the national account. Entities liable for carbon tax will have to surrender their carbon offset credits to SARS should they wish to use the offset credits to reduce their carbon tax liability. If SARS decides to carry out an audit or a specific carbon tax liable entity, the DNA will work with SARS to provide information on the offset credits used by an entity to reduce its tax liability. This will be achieved

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In the 2016 Budget announced by the Minister of Finance in February, it was stated that "given the economic outlook, the carbon tax has been designed to ensure that its overall impact will be revenue neutral up to 2020..." and that 90 comments on the Draft Bill had been received up until that point.

through providing SARS access to the offset registry/database, which should contain proof of retirement of the carbon offsets. The certificate issued by the DNA must contain specific information, which is detailed in Regulation 10 of the Act. In terms of Regulation 9, the taxpayer will have to retain this certificate for a minimum period of 15 years.

Comment

In the 2016 Budget announced by the Minister of Finance in February, it was stated that "given the economic outlook, the carbon tax has been designed to ensure that its overall impact will be revenue neutral up to 2020..." and that 90 comments on the Draft Bill had been received up until that point. The 2016 Budget further stated that the Draft Bill will be revised, taking into account public comments and further consultation. Although Treasury has not issued a revised version of the Draft Bill, it is very possible that the carbon tax will come into effect at the beginning of 2017. Taxpayers that could be liable for carbon tax in terms of Section 4 of the Draft Bill, are advised to understand what their carbon tax liability will be once it comes into effect and to take steps to make use of the allowances offered by the Draft Bill to the greatest extent possible. Persons wishing to submit written comments or requesting clarifications on the Draft Regulations, should submit them to Treasury by 29 July 2016.

Louis Botha and Heinrich Louw

GOOD NEWS FOR EMPLOYERS: INCREASE IN THRESHOLDS FOR EXEMPTION OF EMPLOYER-PROVIDED BURSARIES

Section 10(1)(q) of the Income Tax Act, No 58 of 1962 (Act) exempts from taxable income, any "bona fide" scholarship or bursary granted to assist or enable any person to study at a recognised educational or research institution.

On 8 July 2016, the National Treasury (Treasury) released the draft Taxation Laws Amendment Bill 2016 (TLAB). The TLAB aims to give effect to the various tax proposals announced in the 2016 National Budget. One of these proposals relates to the increase of the monetary thresholds for the exemption of employer-provided scholarships or bursaries.

Increasing these thresholds will most likely support skills development and encourage the private sector (employers) to provide education and training.

By way of background, s10(1)(q) of the Income Tax Act, No 58 of 1962 (Act) exempts from taxable income, any "bona fide" scholarship or bursary granted to assist or enable any person to study at a recognised educational or research institution. However, if such scholarship or bursary has been granted by an employer to an employee or relative of such employee, the exemption will not apply:

- if the bursary or scholarship has been granted to enable or assist any such employee, unless the employee agrees to reimburse the employer if the employee fails to complete their studies for reasons other than death, ill-health or injury; or
- in the case of a scholarship or bursary granted to enable or assist any relative of an employee:
    - if the annual remuneration derived by the employee for a year of assessment exceeds R250,000;
    - the scholarship or bursary in respect of studies from Grade R–12 or a qualification to which a NQF level from 1 up to and including 4 has been allocated exceeds R10,000; and/or
    - the scholarship or bursary in respect of a qualification to which a NQF level from 5 up to and including 10 has been allocated, exceeds R30,000.

The monetary limits associated with bursaries and scholarships to relatives of qualifying employees were last revised in 2013 and Treasury has realised that it has become necessary to align the monetary limits with the ever-changing economy. Increasing these thresholds will most likely support skills development and encourage the private sector (employers) to provide education and training.

The TLAB proposes that the monetary limits be increased for bursaries and scholarships granted by employers to employees or relatives of qualifying employees as follows:

- remuneration for qualifying employees will be increased from R250,000 to R400,000; and
- exempt bursaries or scholarships will be increased from R10,000 to R15,000 and from R30,000 to R 40,000 respectively.

GOOD NEWS FOR EMPLOYERS: INCREASE IN THRESHOLDS FOR EXEMPTION OF EMPLOYER-PROVIDED BURSARIES

CONTINUED

This is a meaningful and viable way in which employers may continue to make a long lasting positive contribution to alleviating the socio-economic challenges faced by our society.

It is clear from the above that the aim of the proposal is to assist low-income earners in providing their dependants and relatives with the necessary education, skills and training. This in turn will enable them to enter the job market and participate in growing the economy. This is also a meaningful and viable way in which employers may continue to make a long lasting positive contribution to alleviating the socio-economic challenges faced by our society, as well as bridging the gap between unemployment and poverty levels in a sustainable manner.

In conclusion, any "bona fide" scholarship or bursary granted to enable or assist any person to study at a recognised educational or research institution is exempt from normal tax. However, this exemption is subject to certain conditions, particularly where the scholarship or bursary is granted by an employer (or an associated institution to that employer) to an employee or relative of such employee.

The TLAB is available for public comment prior to its formal introduction in Parliament. Comments must be submitted by 8 August 2016.

Mark Morgan and Gigi Nyanin

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CUSTOMS AND EXCISE HIGHLIGHTS

Please note that this is not intended to be a comprehensive study or list of the amendments, changes and the like in the Customs & Excise environment, but merely selected highlights which may be of interest.

In the event that specific advice is required, kindly contact our Customs and Excise specialist, Director, Petr Erasmus.

Below are this week's selected highlights in the Customs and Excise environment.

The Draft Rates and Monetary Amounts and Amendment of Revenue Laws Bill intends to amend the Customs legislation as follows (not a comprehensive list):

1. In Schedule 1 Part 1:

   1.1 Substitution in Chapter 22 of Additional Notes relating to products of tariff headings ("TH") 2206.00.05 & 2206.00.19 and insertion of Additional Notes for TH2208.20.11 and 2208.20.91;

   1.2 Deletion of TH2208.20.10 and 2208.20.90;

   1.3 Substitution of TH2206.00.05 and 2206.00.19;

   1.4 Insertion of TH's in heading 22.06 and 22.08;

Heading 22.06 is titled "Other fermented beverages (for example, cider, perry, mead); mixtures of fermented beverages and mixtures of fermented beverages and non-alcoholic beverages, not elsewhere specified or included" and heading 22.08 is titled "Undenatured ethyl alcohol of an alcoholic strength by volume of less than 80 per cent vol.; spirits, liqueurs and other spirituous beverages".

2. Amendment of Schedule 1 Part 2A relating to tariff item 104.00 (being "Prepared Foodstuffs; Beverages, Spirits and Vinegar; Tobacco", and certain of its sub-items); and

3. Insertion of Schedule 1 Part 3E entitled "Environmental Levy on Tyres".

Petr Erasmus

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Cliffe Dekker Hofmeyr is very pleased to have achieved a Level 3 BBBEE verification under the new BBBEE Codes of Good Practice. Our BBBEE verification is one of several components of our transformation strategy and we continue to seek ways of improving it in a meaningful manner.

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