

# TAX & EXCHANGE CONTROL ALERT

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### NEW ELECTRONIC SERVICES REGULATIONS: WIDENING THE INVISIBLE VAT NET

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Foreign suppliers of e-services are required to register for VAT in South Africa if at least two of the following circumstances are present:

- the recipient of the services is a South African resident;
- the payment for services originates from a South African bank account; or
- the recipient has a business, residential, or postal address in South Africa.

A foreign e-services supplier is currently required to register for VAT as soon as the value of the services exceeds R50,000. The current regulations list 'electronic services' as specific categories, including non-regulated educational services, games and games of chance, internet-based auction services, e-books, music and subscription services to websites and web applications.

## The new electronic services regulations

The Minister of Finance announced in his 2017 Budget Review that the regulations defining electronic services would be broadened. Following the revised draft regulations which were published on budget day 2018, National

Treasury published 'final' regulations which significantly broaden the definition of 'electronic services'.

The various categories of e-services have been removed and the revised regulations now define 'electronic services' to mean 'any services supplied by means of an *electronic agent*, *electronic communication* or the *internet* for any consideration'. These terms are in turn defined with reference to the Electronic Communications and Transactions Act, No 25 of 2002. The only exclusions are regulated educational services, telecommunication services (but not the content thereof) and certain supplies to wholly owned group companies.

Consequently, virtually all services that are supplied by way of electronic means are now 'electronic services'. The new definition will now include services such as cloud computing, computer software, online training, on-line data storage and broadcasting services.

## Business-to-business (B2B) transactions

Although the broadening of the definition of 'electronic services' *per se* is not problematic, the regulations make no distinction between B2B and

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business-to-consumer (B2C) transactions. Foreign e-services suppliers to South African customers will therefore be required to register for VAT in South Africa if their customers (including businesses) are located in South Africa.

National Treasury has indicated that the lack of distinction between B2B and B2C transactions is intentional, on the basis that this distinction does not exist in the VAT Act for local suppliers, and that introducing this concept for non-resident suppliers would create an unfair cash-flow advantage for such non-resident suppliers.

However, the regulations were first introduced to address concerns about non-compliance by recipients of imported services. The concept of 'imported services' specifically excludes services acquired for making taxable supplies. By including B2B transactions, the regulations create a disparity between supplies of e-services and supplies of any other services by foreign suppliers. The supplies of any other services are only taxed if they are acquired for purposes other than making taxable supplies.

The inclusion of B2B transactions is also contrary to the recommendations of the Davis Tax Committee (DTC), which carried out extensive research in this field

before making its recommendations. The Organisation for Economic and Co-operation and Development (OECD) also recommends that a distinction be drawn between B2B and B2C transactions, and many countries follow the OECD recommendations. The DTC warned that a deviation from OECD principles will cause increasing problems with administrative enforcement. The DTC thus recommended that the treatment of e-services should be aligned with international treatment and especially harmonised with OECD principles.

In addition to the concerns raised by the DTC, the inclusion of B2B transactions will place a significant administrative burden on both the supplier and SARS regarding the VAT registration process, and the subsequent on-going submission, processing and policing of VAT returns, with no additional revenue for the *fiscus*. Taxable businesses are entitled to deduct the total amount of VAT they pay as input tax, and partly taxable businesses account for the VAT by way of the imported services rules.

## **Intra-group transactions**

In order to limit the administrative burden, e-services supplied between companies in the same group are excluded. However,

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*The regulations have not been gazetted as yet but will come into operation on 1 April 2019.*



in terms of the definition of 'group of companies' in the regulations, the local recipient company must be a wholly owned subsidiary of the foreign group for the exclusion to apply. Consequently, if the local company has Black Economic Empowerment shareholders the exclusion will not apply.

The exclusion also does not apply where the foreign company procures e-services (such as IT services) from a third party for supply to the local company. To qualify for the exclusion, the foreign company must supply the services itself.

#### **Intermediaries**

Intermediaries who facilitate the supply of e-services or who provide their platforms to foreign suppliers for rendering the e-services to South African customers, and who are responsible for invoicing and collecting payment for the e-services, are also required to register for VAT in South Africa. Accordingly, where a foreign supplier supplies e-services via an intermediary, the intermediary will be deemed to be the supplier of the services where such intermediary facilitates the supply of the electronic services and is responsible for the issuing of the invoice and collection of the payment.

#### **Registration threshold**

A positive aspect is that the current registration threshold of R50,000 for foreign suppliers of e-services has been increased to R1 million for any 12-month period, which is now in line with local suppliers.

#### **Effective date**

The regulations have not been gazetted as yet but will come into operation on 1 April 2019.

#### **Implications**

Foreign suppliers of e-services to South African customers and local group companies and intermediaries who facilitate the supply of such services should consider their transactions in view of the new regulations. The scope of the revised definition of 'electronic services' is very broad, and the exclusions are limited. Many foreign suppliers of e-services to South African customers and e-services intermediaries will now fall within the scope of the revised regulations. They will have an obligation to register for VAT in South Africa and will be required to account for VAT on their e-services supplies with effect from 1 April 2019.

*Varusha Moodaley and  
Gerhard Badenhorst*

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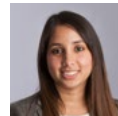
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