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# COMPETITION ALERT

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**SMME Development: Considering Income Tax incentives for purposes of responding to the challenges posed by the new *buyer power and price discrimination* amendments of the Competition Act and the BEE Codes**

This article will consider the recent amendments to the Competition Act and its interaction with various other pieces of legislation, that seek to promote and protect the interests of small to medium-sized firms as well as previously disadvantaged firms, such as the BEE Codes and various Income Tax incentives that apply to supplier and enterprise development initiatives and SMMEs.

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## SMME Development: Considering Income Tax incentives for purposes of responding to the challenges posed by the new *buyer power and price discrimination amendments of the Competition Act and the BEE Codes*

The Competition Amendment Act, 2018, introduced new provisions that seek to advance and protect the interests of (SMMEs). These amendments took effect on 13 February 2020.

This article will consider the recent amendments to the Competition Act and its interaction with various other pieces of legislation, that seek to promote and protect the interests of small to medium-sized firms as well as previously disadvantaged firms, such as the BEE Codes and various Income Tax incentives that apply to supplier and enterprise development initiatives and SMMEs. In particular, this article discusses how dominant firms can use the amendments to the Competition Act as an opportunity with reference to the various tax incentives and provisions in the Income Tax Act, 1962 (the ITA).

The Competition Amendment Act, 2018 (Amendment Act), introduced new provisions that seek to advance and protect the interests of small and medium sized businesses (SMMEs). These amendments took effect on 13 February 2020.

In terms of the amendments to section 8 of the Competition Act, a dominant firm in certain sectors may not impose unfair prices or trading conditions on suppliers who are SMMEs and/or firms controlled by historically disadvantaged persons (HDPs), or may not refuse to and/or avoid purchasing goods and services from such firms.

The amendments to section 9 of the Competition Act provide that a dominant firm may not engage in price discrimination which impedes the ability of SMMEs and/or firms controlled or owned by HDPs, to participate effectively in the economy.

The Competition Act now provides that a contravention of these sections will attract penalties of up to 10% of the dominant firm's turnover in South Africa.

The unique nature of these provisions and the complex conceptual framework that is required to administer these sections of the Competition Act has attracted significant attention. It is evident that the Amendment Act strays beyond the traditional bounds of prohibiting exclusionary acts by dominant firms, and dominant firms now have a "positive duty" to favour certain firms in the market. i.e. if you have buyer power you have a positive duty not to use your buyer power in a way that treats SMMEs or HDPs unfairly.

National Treasury released a report titled 'Economic transformation, inclusive growth and competitiveness: towards an economic strategy for South Africa', which drew on six themes including modernising network industries to promote competitiveness and inclusive growth, lowering barriers to entry and addressing distorted patterns of ownership (Report).

The Report found that South Africa's lagging productivity growth and declining export performance have been partly attributed to a lack of competition both in upstream and downstream industries. Furthermore, while large businesses have the resources to navigate their way through difficult economic times, the combination of impediments such as a high regulatory burden, inflexible labour markets, and high levels of concentration, present significant

## SMME Development: Considering Income Tax incentives for purposes of responding to the challenges posed by the new *buyer power and price discrimination* amendments of the Competition Act and the BEE Codes ...continued

Many impediments faced by SMME and HDI firms are a function of weak economic growth, but the new Competition Act Amendments seek to penalise dominant firms, where dominant firms are at fault for the failure of these vulnerable firms to participate in the economy.

obstacles for SMMEs. However, the role of SMME's in creating employment remain very significant and, for this reason, the focus on their success in the economy is justified.

Many impediments faced by SMME and HDI firms are a function of weak economic growth, but the new Competition Act Amendments seek to penalise dominant firms, where dominant firms are at fault for the failure of these vulnerable firms to participate in the economy.

The BEE Act and Codes of Good Practice also seek to change the way that the private sector approaches the procurement of products and services. The amendments to the Competition Act, dealing with the buyer power and the price discrimination, have potential areas of overlap with the enterprise and supplier development provisions in the BEE Codes and dominant businesses have an opportunity to streamline and recalibrate their compliance efforts in this area.

In response to these developments dominant firms could focus on ways in which to promote compliance with the Competition Act by leveraging off existing initiatives, such as their BEE initiatives, and by seeking to

benefit from the various incentives which are currently available to them. From a tax perspective, dominant firms could consider implementing certain programmes, providing funding and developing initiatives with reference to the various tax incentives and provisions in the ITA.

For example, certain expenditure incurred in respect of enterprise development (ED) and socio-economic development (SED) could be deductible against income in terms of section 11(a) of the ITA, depending on the underlying facts and circumstances. In this manner, taxpayers should consider the principles enunciated in the preeminent case of *Warner Lambert SA Proprietary Limited v CSARS 65 SATC 346*, wherein a taxpayer incurred social responsibility expenditure for purposes of complying with the Sullivan Code in order to be able to continue trading in South Africa as a subsidiary of a United States company. Binding Private Ruling 282 (BPR 282) which dealt with the income tax consequences for the operator of a wind farm incurring ED and SED expenditure pursuant to obligations imposed and accordingly undertaken in terms of an electricity generation agreement and licence should also be considered.

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Dominant firms could also consider providing equity funding to certain section 12J venture capital companies (VCCs) that in turn invest in underlying SMMEs. Alternatively, they could leverage off the existing public benefit (PBO) regime whereby donations to such PBOs conducting relevant activities in support of certain SMMEs may be tax deductible in terms of section 18A of the ITA. Dominant firms could also consider utilising the section 30C small business funding entity provisions where donations to and by a small business funding entity are exempt from donations tax, amongst other benefits.

It should also be noted that SMMEs themselves may benefit from one or more of a variety of special taxation provisions, including for example the simplified Turnover Tax system for micro businesses (i.e. turnover of R1 million or less) that provides for progressive tax rates as opposed to the flat rate of 28% for companies in the ordinary course. Similarly, Small Business Corporations (as defined) with turnover of less than R20 million (SBCs) also potentially qualify for taxation as per the concessionary tax rates which follow a graduated marginal structure as opposed to the usual corporate tax rate of 28%. SBCs, as defined, may

also benefit from tax incentives including the section 12E accelerated depreciation allowance on certain capital assets acquired and brought into use by an SBC. Dominant firms engaged with SMMEs and SMMEs themselves would be well advised to consider the various special taxation regimes for purposes of maximising their benefits.

Efforts by dominant firms to lobby government to reduce red tape and barriers to entry and actively seeking to mitigate such impediments by participating in supplier and customer development programmes could assist in mitigating allegations that dominant firms have impeded the participation of vulnerable firms in the economy. The focus will be on dominant firms to demonstrate how they have been engaging constructively with small or HDI firms and refuting allegations that they have not impeded SMME firms and HDI firms from participating in the economy.

To the extent that vulnerable firms continue to fail despite these efforts, and the fault is placed at the door of dominant firms, difficult questions of causality and the reach of the recent amendments will need to be answered by the Competition Tribunal and the courts.

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