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Whose wishes were granted; who were denied??

In the run-up to the 2012 Budget many wishes and warnings were addressed to Minister Gordhan.

Let's see who got what they asked for (the haves) and who were denied (the have-nots):

- The SA Institute of Professional Accounts asked that individual taxpayers be spared. According to SAIPA they "*...had been contributing an ever-growing share of South Africa's revenues in the past five years.*"

  Verdict: Modest tax relief of R9.5 billion was proposed. This was "*... to ensure that the direct personal income tax burden on individuals remained reasonable.*" According to the Minister personal income tax was the basis for an equitable and progressive tax system. The top marginal tax rate for individuals remains at 40%. However, from 1 March 2012, the CGT inclusion rate for individuals and special trusts increases to 33.3% (from 25%) and for companies and other trusts to 66.6% (from 50%). So with the one hand the Minister gave and simultaneously took substantially with the other.

- Business Unity SA (BUSA) worried that SA's "*fiscal wiggle room was shrinking.*" It wanted the Minister to focus on "structural factors that could strengthen economic performance over the longer term." The focus had to be the promotion of growth and job creation.

  Verdict: "*To drive back unemployment*" got a mention right at the outset of the Minister's Budget Speech. The Minister's focus will be on the unemployed youth and therefore special employment initiatives had to be a priority in the present circumstances. On the financial side: a Budget deficit of the 4.6% of GDP is projected for 2012/13. That will reduce to 3% of GDP in 2014/15. Public debt will stabilise at 38% of GDP. Total spending will be R1.1 trillion next year, i.e. some 32% of GDP.

- BUSA and many others warned that "*welfare payments could not continue out of proportion with taxes.*" SA currently has 15 million recipients of social grants and this has grown 300% during the last decade.

  Verdict: Expenditure on social grants will grow from R105 billion in 2012/13 to R122 billion in 2014/15. In his speech the Minister mentioned that 16 million South Africans actually received social grants and that the increases given in the Budget would be reassessed if inflation continued to rise.

- Everyone wondered where money for the National Health Insurance (NHI) would come from? There were warnings that SA could not afford the NHI.

  Verdict: NHI will now be phased in over 14 years from 2012/13. It will require new funding sources. Options include an increase in VAT, a payroll tax on employers, a surcharge on income tax on individuals or a combination of these. The mention of a VAT increase is interesting seeing that VAT has always been viewed a politically-sensitive tax.

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- Economist Mike Shussler warned that "... *while SARS has become more effective, a high effective tax rate constrains companies from investing in a meaningful way.*" Government should learn to help companies otherwise SA would lose investment.

  Verdict: The Dividend Withholding Tax takes effect on 1 April 2012 and will be at 15% (5% higher than the STC it replaces). A whole section in the Speech was devoted to "Support to business sector growth". This included, amongst others, a simplified tax regime for small business, a draft policy framework and legislation that has been published for special economic zones and a venture capital incentive for junior mining companies.

- Numerous commentators asked that so-called "*stealth taxes*" should be curbed. This covered moans about the fuel levy, toll fees, administered prices, increases in electricity tariffs, a possible carbon tax, etc.

  Verdict: No relief in respect of sin taxes was to be expected. Excise duties on tobacco increases by between 5 and 8.2%. That on alcoholic beverages will increase between 6 – 20%. Following public consultation, government has revised its concept design for a carbon tax and a draft policy paper will be published for comment in 2012. The electricity levy will be increased by 1c/KWh to 3.5c/KWh. The general fuel levy increases by 20c/l and the Road Accident Fund levy by 8c/l (from 4 April 2012).

- Recently there was a lot of talk regarding "High Net Worth Individuals" (HNWI). Some mentioned a Warren Buffet-type "wealth tax."

  Verdict: A specific wealth tax on the ultra-rich did not happen. However, according to the Minister there is room to improve service to this segment. But, they will be a "*focus area for SARS in the coming year.*" Certain toys of the HNWI's will also become more expensive. Styled as a "Tax on luxury goods", there will be, from 1 October 2012, an *ad valorem* tax on certain aeroplanes and helicopters (at 7%) as well as on certain motorboats and sailboats (at 10%).

- Everybody in SA, without exception, asked on their wish-lists for taxpayers' monies to be spent wisely and in the right places. The wide-spread wasteful expenditure had to be addressed and those responsible taken to task. Otherwise "*...government would lose its moral right to tax.*"

  Verdict: The Budget proposals state: "*Government is taking steps to improve the efficiency of public expenditure and to root out corruption.*" In his speech the Minister said that "*we have to do more with less.*" The Minister emphasised that fraud and corruption would be combated through changes to procurement policies and practices and tough enforcement of the law. It's interesting that a whole section of the Budget Speech gave details as to how the wasteful expenditure would be stamped out going forward.

INCOME TAX RELATED PROPOSALS

Changes to the Dividends Tax regime

While companies and shareholders alike have been gearing up for the changeover on 1 April 2012 from Secondary Tax on Companies (STC) to Dividends Tax, National Treasury and SARS have had a card up their sleeve – one with some serious consequences.

It was announced by the Minister of Finance in his Budget Speech that the anticipated rate of 10% for purposes of Dividends Tax will increase to 15%. The change is very surprising for two reasons. Firstly, it has always been understood that, effectively, the net result of STC and Dividends Tax would be the same, being a tax of 10% in respect of dividends. This meant that Dividends Tax was never faced with much resistance. Secondly, the suggested change comes at the eleventh hour, while there has been ample opportunity to announce the change at an earlier stage. There has been no consultation with stakeholders in this regard.

SARS cites equity consideration as driving the change, there being an apparent equity mismatch in the way that income from interest, dividends and capital gains are taxed. SARS also makes no secret of the fact that high-income earners are targeted in that they usually earn large portions of their income through dividends.

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A further change in relation to Dividends Tax is the shortening of the period available for companies to use up any STC credit that they may have as on 1 April 2012. It is proposed that the period be changed from 5 years to 3 years. The reasons given are that the implementation of Dividends Tax has been delayed for too long, and that the proposed increase of the rate from 10% to 15% means that any STC credit will be used up quicker.

These changes are bound to leave interested parties at a loss, both in terms of words and their pockets.

Increase in capital gains tax rates

After more than 10 years of relatively modest and unchanged Capital Gains Tax (CGT) rates, the 2012 budget proposes an increase in the effective capital gains tax rates in order to enhance the equity, integrity and progressive nature of the South African tax system. These changes are scheduled to take effect on the disposal of qualifying capital assets from 1 March 2012.

It is proposed that the inclusion rate for individuals and special trusts will increase from 20% to 33.3%, resulting in a 13.3% increase in the effective rate with the inclusion rate for companies to increase from 50% to 66%, resulting in an effective rate increase of 18.6%. The inclusion rate for other trusts will increase to 66%, raising the effective rate to 26.7%.

As such, the tax burden on the disposal of qualifying assets has been increased significantly. This could have a detrimental impact on middle-income earners and such it is proposed that the exemption thresholds for individual capital gains and for primary residences be adjusted significantly. The following exemptions for individual capital gains are increased from 1 March 2012:

- The annual exclusion from R20 000 to R30 000;
- The exclusion amount on death from R200 000 to R300 000;
- The primary residence exclusion from R1.5 million to R2 million;
- The exclusion amount on the disposal of a small business when a person is over the age of 55 from R900 000 to R1.8 million; and
- The maximum market value of the assets allowed for a small business disposal for business owners over 55 years increases from R5 million to R10 million.

Furthermore, it was widely expected that the highest marginal tax rate for individuals would be increased from the current 40% to cater, inter alia, for funding of National Health Insurance. Surprisingly, the 40% highest marginal rate has remained intact, but with minimal tax relief for higher income earners.

Interaction between company law and income tax law

It seems that the legislative authorities have at last appreciated that a number of issues have arisen pursuant to the introduction of the new Companies Act 2008 on 1 May 2011. The introduction of the Companies Act has given rise to a number of anomalies and new concepts which have not been dealt with in the context of tax law to date. For instance, the Companies Act deals with a concept called "distributions", whereas the fiscal laws still refers to a "dividend" distributed to shareholders.

One of the issues that has not been addressed to date, relates to the ability of a company to issue so-called "sweat equity" to shareholders in circumstances where the initial subscription price is not paid for such subscription on day one. In terms of s40 of the Companies Act, the subscription price can be delayed or can be settled through means of the rendering of future services, future benefits or future payment by the shareholder. Unfortunately the ability to receive the shares immediately, results in an upfront tax liability for the subscriber to the extent that it is acknowledged that the shares are acquired for future services. Also it is not clear at this point in time whether the issue of shares by a company would actually constitute expenditure actually incurred by the company should these shares be issued for future services.

In the tax proposals issued by National Treasury it is indicated that an immediate focus area will also relate to company reorganisations and other share restructurings. Share-for-share recapitalisations of a single company will enjoy an immediate focus. Currently share-for-share transactions are dealt with in terms of s42 of the Income Tax Act on the basis that rollover relief is afforded to shareholders to the extent that a shareholder acquires a 20% equity shareholding in the acquiror company pursuant to the disposal of assets to the acquiror company. The amalgamation provisions of the Companies Act are also not consistent with those incorporated in s44 of the Income Tax Act, especially given the fact that s44 of the Income Tax Act does not deal with the transfer of liabilities whereas the amalgamation provisions in the Companies Act deal specifically with the merging of assets as well as liabilities of the merging companies.

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Transfer pricing and the use of quasi equity loans

It has often been a bone of contention between taxpayers and the revenue authorities as to whether a shareholders' loan should attract interest at market related rates in circumstances where the shareholders' loan has been intended to provide subordinated funding to the offshore company. More often than not such shareholders' loan is used to fund the start-up operations of the offshore entity and it is not expected that the loan will be serviced for the foreseeable future.

It has now been recognised by National Treasury that these types of loans more often than not function as additional share capital and that the purpose is to provide for a more flexible use of capital. One should therefore not automatically insist upon a market related interest rate that applies to these types of loans. In particular, it has been proposed that these types of loans should be treated as share capital in line with the decision to treat certain forms of debt as shares.

Contingent liabilities revisited

In the tax proposals for 2012, the issue of contingent liabilities has once again been the subject of reconsideration. In the 2011 budget it was proposed that new explicit rules would be introduced to clarify circumstances in which a deduction may be claimed in the case of the transfer of contingent liabilities pursuant to a sale of business. This proposal followed the judgment delivered in the *Ackermans Limited/Pep Stores (SA) Limited v the Commissioner* case delivered on 1 October 2010. The Supreme Court of Appeal considered if the expenditure had been actually incurred and concluded that no liability had been actually incurred by Ackermans having regard to the particular facts of the case.

On 10 May 2011, SARS issued a binding class ruling BCR29 concerning the deductibility of contingent liabilities taken over when buying the assets and liabilities of another company within the same group of companies. The context in which the ruling was issued was where two companies formed part of the same group of companies and that proposed transaction was to be implemented in accordance with the amalgamation provisions contained in s44 of the Income Tax Act.

The nature of the contingent liabilities included both employment related obligations such as leave pay and bonuses, sales related obligations such as warranty obligations and contract cost overruns. If the contingent liabilities were to materialise, they would ordinarily have been deductible. It was confirmed in the ruling that the purchaser will be entitled to deduct expenditure actually incurred in respect of the contingent liabilities transferred. The seller of the assets and liabilities will correspondingly not be entitled to a deduction of the contingent liabilities.

The approach in the ruling is consistent with the Ackermans case in that there is the necessity that the expenditure be actually incurred by the purchaser in order to qualify for the deduction of the contingent liabilities. There is the necessity of considering whether there has been an "undertaking of an obligation to pay" or "actual incurring of a liability" in order to satisfy the requirements of s11(a) read together with s23(g) of the Income Tax Act.

In the tax proposals for 2012 it is now indicated that after much debate no legislative provisions will be enacted. Rather, it is indicated that an interpretative approach will be favoured. Interpretative guidance, with legislative refinements, is expected later in the year. The question will be the form of such interpretative guidance and how the existing interpretation adopted in the Ackermans case and the ruling will be applied. It is of concern that there remains such degree of uncertainty with what appears to be an issue which is not uncommon.

Debt cancellation

In line with current economic trends of there being a weaker economic climate, National Treasury recognises that some taxpayers are at risk of becoming insolvent and will seek to reduce or restructure their debt. In the budget proposals for 2011, National Treasury announced its intention to consider the elimination of unintended tax consequences of debt reductions in circumstances where there is a debt work-out.

Legislative amendments were subsequently proposed to amend the definition of "gross income". However, the proposals were withdrawn following comments received that there was no co-ordination with recoupment rules. It was accepted that the isolated amendment was not appropriate.

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In the 2012 budget proposals, the issue of debt cancellation is highlighted as one of the tax amendments for the forthcoming year. It is indicated specifically that –

"*The goal would be to create a simplified regime to determine the tax impact on the debtor when debt unilaterally reduced or cancel without full consideration, and to eliminate adverse tax consequences when the debt relief merely restores the debtor to solvency.*"

No specific indication is provided as to how this goal will be achieved, although it is noted in the 2012 budget proposals that specific rules will be required to regulate the situations where creditors agree to convert their debt interests into an equity stake as partial compensation. It remains unclear as to what form these rules will take as well as what other matters will be addressed in any legislative amendments required to eliminate the so-called unintended tax impact of debt reductions.

Continued focus on excessive debt in business operations

Since the suspension of the application of s45 (intra-group transactions) and s47 (liquidations) to corporate restructuring rules during June and July 2011 there has been a continued focus on the use of excessive debt in corporate restructuring transactions. It has now been mentioned that the main problem is the erroneous classification of certain instruments as debt to generate interest deductions for the debtor, where these types of instruments more accurately represent equity. This would for instance be the case with reference to so-called subordinated shareholders loans or so-called junior loans that are made available to companies.

It has also been indicated that, should the creditor be a non-resident, there is currently a tax mismatch given the fact that the debtor can deduct the interest whereas the creditor would not be subject to tax. One of the consequences is the introduction of a withholding tax on interest at the rate of 15% on 1 January 2013.

It has also been indicated that, in 2013, National Treasury will consider a so-called "across-the-board" percentage ceiling on interest deductions, relative to earnings before interest and depreciation. This will limit excessive debt financing.

Related to the aforegoing, it has long been a bone of contention that no interest deduction is afforded to taxpayers in circumstances where debt is raised to acquire shares. The reason is that the shares are only expected to render exempt returns in the form of dividends thus prohibiting the interest deduction.

Pursuant to the introduction of s23K to the Income Tax Act in circumstances where taxpayers had to make application to have transactions approved, including the level of debt, it has now been announced that the use of debt to acquire controlling share interests of at least 70% be allowed. The interest associated with this form debt acquisition is still subject to the same controls applied to s45 acquisitions. In other words, even though there may be an interest deduction pursuant to the acquisition of shares, one will still have to make application to the Revenue Authorities so as to have the level of debt and equity approved, the rate of interest, the identity of the debtor and the fact that non-South African residents will effectively not be able to fund these types of transactions.

The question as to whether debt can be used to fund share acquisitions, has been the subject matter of much debate between taxpayers and the Revenue Authorities over the years. To the extent that an interest deduction will now be allowed, it is interesting to establish whether dividends will also become taxable in these circumstances so as to provide for reciprocity. Ultimately, however, taxpayers will have to realise that these types of transactions will be subject to a pre-approval process, apart from the fact that they will have to be reported to the Revenue Authorities. Apart from the fact that certain shareholders loans may in future be treated as equity, especially if they are subordinated in favour of senior lenders, the actual rate applicable to loans will also be closely scrutinised. The moment a premium is attached to an interest rate in view of the fact that the loan is subordinated in favour of other lenders, it may well at some stage be treated as equity, resulting in a non-deduction of interest by the debtor.

The focus of SARS shifts to insurance companies

It seems that the focus of the legislator and the revenue authorities has shifted from financial institutions to insurance companies. Apart from the elimination of so-called captive cell arrangements, it has also been mentioned that specific focus

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will be given on scenarios where premiums are paid by a parent company at increased rates on the basis that the excess so paid back to the company by way of tax-free preference share dividends, will be specifically addressed.

However, pursuant to a number of assessments issued to insurance companies over the last few months, it has been indicated that the solvency requirements applicable to insurance companies are not currently consistent with the tax treatment thereof. In the case of short-term insurance companies, it has been specifically indicated that the recognition of certain reserves have had both a positive and negative effect for short-term insurers.

In the context of long-term insurance companies, it seems that the so-called forefront trustee system of taxation is to be reconsidered. Essentially the business of a long-term insurance company is divided into an untaxed policyholder fund, a company policyholder fund, an individual policyholder fund and a corporate fund. Different tax principles apply to each fund and the assets accounted for by each fund. For instance, the untaxed policyholder fund is not subject to any tax. The different treatment has also given rise to mismatches from an accounting perspective. For instance, at one stage reinsurance liabilities were not recognised even though reinsurance assets were recognised for tax purposes, resulting in substantial anomalies.

It has been indicated that the tax system for calculating short-term insurance reserves will be addressed during 2012, with the long-term insurance industry being considered during 2013. One can expect far-reaching amendments, especially given the aggressive attitude that has been displayed by the revenue authorities towards insurers of late. However, recognition will have to be given that reserves play a critical role in this context, especially with reference to claims that are to be submitted in the future and the way in which insurance companies have to recognise same.

Mark-to-market taxation of financial instruments

Currently some financial traders utilise the provisions of s24J(9) to effectively provide for the taxation of their interest-bearing instruments on a mark to market basis linked to the accounting treatment of those instruments in their accounts.

The Minister has indicated that he is keen to commence moving towards taxing financial instruments on this basis, that is aligning the tax treatment to the accounting treatment, in order to simplify the audit and compliance requirements for both taxpayers and SARS. Firstly he wants to move the provisions of s24I dealing with foreign currency instruments closer to the accounting standards. Secondly he is wanting to expand and revise the mark to market treatment of other financial instruments. The Budget Tax Proposals say that these changes will include expanding the provisions of s24J(9) to cover a wider set of financial assets and liabilities. He says that the revised system will be subject to explicit SARS approval so that those parties electing to move into this regime will be fully controlled during the pilot phase of the project.

The Minister makes it clear in his Budget Proposals that these legislative provisions will be changed as they are tested over the next few years based on the practical experience that flows from using them. Be warned!

Renewable energy tax allowances

Section 12B of the Income Tax Act allows for the deduction of plant and machinery used in the generation of electricity from renewable resources on a 50/30/20 basis. A contentious issue that arises under similar accelerated allowance provisions is whether supporting structures in fact form part of or can be regarded as plant or machinery qualifying for deduction. Case law on this aspect is not always necessarily helpful.

For renewable energy structures the problem is particularly acute as they are capital intensive projects with most structures affixed to the ground not always capable of being removed. It is welcomed that National Treasury will extend the 50/30/20 allowance under s12B of the Income Tax Act to supporting structures to provide clarity to Independent Power Producers bidding to the Department of Energy. However, until such time that the legislation is promulgated it appears that the Advance Tax Ruling process must be favoured for current projects to obtain certainty on the tax treatment on supporting structures.

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Reduction of tax rate for foreign companies

It is proposed that the corporate income tax rate for foreign companies with domestic income be reduced from the current 33% to 28%. The move was widely expected with the abolishment of Secondary Tax on Companies and the introduction of the Dividends Tax. It was long regarded that the higher foreign company tax rate of 33% was discriminatory under the provisions of certain Double Tax Agreements entered into by South Africa.

Given the unexpected jump in the Dividends Tax rate from 10% to 15% the effective tax rate of a foreign company in South Africa may be more beneficial than that of a locally incorporated entity. Could we see a surge in branch operations in South Africa as a result of this amendment?

Conclusion of tax information exchange agreements

True to its word, the South African Government has concluded a number of exchange of information agreements with so-called perceived tax havens so as to address the perceived risk that amounts may be hidden by South African residents in these types of countries. Of late, agreements have been published with the Cayman Islands, Jersey, Guernsey as well as San Marino. A number of other agreements are in the process of being ratified.

These agreements provide for the exchange of information between countries party to such an agreement upon request. Should the information in the possession of a specific country not be sufficient to enable such country to comply with the request for information, the country is obliged to use at its own discretion the information gathering measure it considers relevant to provide the other country with the information so requested. This is notwithstanding the fact that the requested party may not need the information for its own tax purposes. Recently a scenario arose where the Australian Government requested information from the South African Government in relation to the affairs of an Australian tax resident. Even though the request did not relate to the tax position of the taxpayer in South Africa, it was held that the information still had to be provided.

The information to be provided, extends to information held by banks, financial institutions and any other person acting in an agency or fiduciary capacity. It includes information about settlors, trustees, beneficiaries and protectors of a trust, units issued by a collective investment scheme and the like.

Taxpayers should appreciate that the world has become very small and that it would no longer be possible to hide assets in perceived tax havens without the ability of the South African fiscus to obtain information about that.

Property Loan Stock Company & Trusts

The Property Loan Stock Association and the Association of Collective Investment Schemes in Property have been in negotiations with National Treasury for some years now, regarding the implementation of blanket legislation for both variable loan stock companies and Collective Investment Schemes in Property, under the banner of Real Estate Investment Trusts (so called REIT's).

It is not clear in what form the dispensation will come, however, it does appear as though there concerns have not fallen on deaf ears. It has been proposed in the tax proposals to the 2012 budget speech that the governance of property loan stock entities will be placed on a par with property unit trusts. It is proposed that the rental income from these entities will fall under the pass-through regime that currently applies to property unit trust. It is our understanding that the intention is to ensure that both variable loan stock companies and Collective Investment Schemes in Property are effectively placed in a tax neutral position *vis-à-vis* the distribution of the rental income.

It is noted that Treasury appears to be concerned that other taxpayers (ie taxpayers other than variable loan stock companies) may use the linked unit structure (eg a R10 linked unit of which R0.01c is linked to the equity component and the remaining R9.99 linked to the debenture component) in order to avoid tax by relying on an excessive interest deduction. Taxpayers issuing linked units should thus be mindful of Treasury's view on these types of structures.

Household Saving Initiatives

As part of the Government's drive to increase the rate of savings in South Africa, the Government is proposing to introduce tax-preferred saving and investment vehicles (Saving Vehicles) by April 2014. A discussion document will be published by May 2012 to facilitate the consultation process and refine its proposals.

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It is proposed that the returns generated from these Savings Vehicles (eg interest, dividends, capital gains, etc) and the withdrawals from same will be exempt from normal tax. However, the aggregate annual contributions to these saving vehicles could be limited to R30 000 per year per taxpayer, with a lifetime limit of R500 000. These Saving Vehicles are clearly aimed at low income earners and it is anticipated that they will provide little incentive for middle-to-high income earners to utilise these Saving Vehicles.

Share Incentive Schemes

Share incentive schemes are once again in the spot light in this year's tax budget proposals. We have previously highlighted in our weekly Tax Alerts that previous amendments to the Income Tax Act have triggered adverse tax consequences for share incentive schemes (eg amendments to s10(1)(k)(i)(dd) and paragraph 38(2)(d) of the Eighth Schedule to the Income Tax Act).

It appears that these previous amendments have not satisfied National Treasury's concerns on share incentive schemes and will be undertaking a review of the various types of share incentive schemes to eliminate purported loopholes and possible double taxation concerns (as indicated in previous Tax Alerts).

The review will also consider the interrelationship between employer deductions and employee share scheme income. SARS may be concerned that taxpayers currently argue that the contributions to the employee share scheme for their employees are deductible (see Provider v Commissioner of Taxes, 17 SATC 40), while the contributions received by the Trust are capital in nature on the basis that the trust is not engaged in a profit making scheme (see *CIR v Pick 'n Pay Employee Share Purchase Trust 54 SATC 271*).

It also appears that the broad-based employee share plan contemplated in s8B of the Income Tax Act will be reviewed and possibly merged into a single employee share scheme regime. Section 8B schemes are not used by many taxpayers owing to the onerous requirements. If the s8C and s8B share scheme provisions are combined, it is anticipated that it will be to the detriment of high-net worth individuals. However, this process is said to take two years and we will have to wait and see what is proposed.

Share Issue Mismatches

It has come to Government's attention that certain taxpayers have been relying on the fact that the issue of shares by a company does not give rise to ordinary or capital gains tax consequences for the company (ie merely representing a cash contribution to company), to shift value to new shareholders without paying the full tax due. Apparently the scheme relies on the shares being issued by the company for a consideration in excess of the value of the shares. For example, the company issues a share with a market value of R100 to a shareholder for R200.

The proposal made by the Treasury is for the R100, being the market value of the share, to remain free from any ordinary or capital gains tax treatment. Whereas, the additional R100 paid by the shareholder, in excess of the market value of the shares, will be subject to tax in the hands of the company.

It is noted that there may well be circumstances where a shareholder is willing to subscribe for shares in a company in excess of the market value. It will therefore be interesting to see whether the proposed legislation requires some form of collusion (for want of a better word) between the shareholders (ie the show that there is an intention to shift value between the shareholders) before triggering the additional tax treatment contemplated.

EMPLOYEE'S TAX RELATED PROPOSALS

Reduction in rate for Personal Service Providers

The flat tax rate of 33% applicable to Personal Service Providers will be reduced to 28%, without much reasoning from National Treasury. The move to reduce the flat rate is welcomed, but seemingly carries no correlation to the marginal rate of tax for individuals which was unmoved at 40%. Given that the Personal Service Provider legislation is an anti-avoidance provision aimed at discouraging individuals from rendering services through incorporated entities one would have expected some link to the individual tax rates.

Determination of the value of fringe benefits

The Seventh Schedule of the Income Tax Act provides for the value of certain non-cash benefits received by virtue of employment to be subject to PAYE on a monthly basis. Depending on the type of benefit in question, the valuation thereof may be subject to a formula calculation, such as housing benefits.

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The valuation methods in the Seventh Schedule to the Income Tax Act do not always correlate to the actual cost of the benefit which in many instances can be objectively determined by an employer. Treasury has proposed where possible and practical, an employer would be allowed to use actual costs to determine the value of a fringe benefit. This is an attempt to create a better match between the deduction of employee's tax and the tax calculation on assessment. Caution is necessary on this proposal, as actual costs may in fact push up the value of fringe benefits in certain cases.

SECURITIES TRANSFER TAX PROPOSALS

End of the broker's exemption

Currently South Africa has a Securities Transfer Tax which is payable on the change of the beneficial ownership of both listed and unlisted shares. Currently there is an exemption for brokers in the market – technically this is applicable to any "authorised user" as defined in s1 of the Securities Services Act 2004, who provides those services as the rules of the exchange regulate the buying and selling of listed securities. The Minister of Finance has announced that this exemption will be removed where brokers acquire shares for their own benefit. He says that the current blanket exemption will be abolished and where brokers do acquire securities as a principal, the tax will be applied at an "appropriate lower rate". He says that this reduced rate will also cover the purchases of shares utilised in support of derivative hedging (which we suspect encompasses a "lending arrangement"). That is where parties have borrowed listed securities from another which they have delivered to a buyer pursuant to a short sale in order to hedge a long position of their own.

The Minister has said that these amendments will come into effect on 1 April 2013. However, he has also said that the Department will investigate the feasibility of widening the Securities Transfer Tax to cover derivatives.

Carbon Tax proposals

The National Treasury circulated a comprehensive Policy Paper weighing up the various options and consequences of introducing a Carbon Tax in December 2010. We have keenly awaited an indication of what the National Treasury's thinking is on implementing such a carbon tax, if indeed such a tax is truly socially beneficial. When Cabinet approved its Climate Change Response White Paper, they did indicate that the need to price carbon emissions and to bring in a tax instrument for this purpose was accepted as a policy initiative.

In the tax proposals the Minister says that a "modest carbon tax" will begin to price carbon dioxide emissions so that the external costs resulting from such emissions start to be incorporated into production costs and consumer prices. He said that subsequent to the consultation following the previous paper, a further draft policy paper will be published for comment this year. However he does indicate that the design features of this tax that it will be on a percentage basis rather than absolute emissions thresholds, below which the tax will not be payable. It stipulates that a tax free threshold for process emission, will be involved in the tax, with consideration given to the industries of cement, iron and steel, aluminium and glass to mitigate the impact of the tax on them over the near term; there will be additional relief for trade exposed sectors. There will also be the ability to use offsets by companies to reduce their carbon tax liability. There will be a basic tax free threshold of 60% and maximum offset percentages of 5% or 10% until 2019/2020. They will look at additional relief for firms that reduce their carbon intensity during the first phase of the tax. The reduction in carbon intensity will be measured with reference to a base year or to an industry bench mark. The tax-free thresholds will be reduced during the second phase (that is from 2020 to 2025) and may be replaced with absolute emission thresholds thereafter. Treasury will seek to align the proposed carbon budgets as per the National Climate Change Response White Paper (2011).

Government is looking at pricing a carbon emission at a R120 per ton of CO^2, but of course the taxing only starts at above the suggested threshold of 60%. It is proposed that this will take effect during 2013/14, with annual increases of 10% until 2019/2020. They are not proposing to earmark the revenues derived from carbon tax, but they will give consideration on spending to address environmental concerns. Government commits themselves to support incentives such as energy efficiency and measures to assist low income households. The tax proposals have printed a table summarising the proposed emission thresholds for all sectors, with further adjustments

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to account for the trade exposure of a firm (up to a maximum) and indicating the allowances for sector process emissions. One can expect the figures in this table to change as Government seeks to ensure that all industries are shouldering the burden of carbon reduction.

Government is looking at pricing a carbon emission at a R120 per ton of CO^2, but of course the taxing only starts at above the suggested threshold of 60%. It is proposed that this will take effect during 2013/14, with annual increases of 10% until 2019/2020. They are not proposing to earmark the revenues derived from carbon tax, but they will give consideration on spending to address environmental concerns. Government commits themselves to support incentives such as energy efficiency and measures to assist low income households. The tax proposals have printed a table summarising the proposed emission thresholds for all sectors, with further adjustments to account for the trade exposure of a firm (up to a maximum) and indicating the allowances for sector process emissions. One can expect the figures in this table to change as Government seeks to ensure that all industries are shouldering the burden of carbon reduction.

The percentage thresholds will be used to quantify the carbon tax liability of a firm based on its absolute emissions for the year. A formula of $Z = \frac{Y}{X}$ is proposed to adjust that basic percentage tax free threshold to take into account efforts being made by the firm to reduce its emissions. X is the average measured and verified carbon intensity of the output of a firm; Y is the agreed benchmark carbon intensity for the sector. The basic percentage threshold below which the tax will not be payable may be adjusted using a carbon emissions intensity factor for output compared to an agreed sector benchmark. The adjustment to the tax free threshold is then determined by multiplying the original percentage threshold by the resultant Z. The ethos of this is that where a company has carbon emission intensity the same as the benchmark figure, its basic tax free threshold remains the same. A company doing better than the intensity benchmark, then qualifies for a higher basic percentage tax free threshold. A firm doing worse than the carbon emission intensity benchmark will be penalised for its excessive carbon emissions.

Proposed emissions thresholds for sectors

Sector	Basic tax free threshold (%) below which no carbon tax will be payable during the first phase (2013 to 2019)	Maximum Additional allowance trade exposure	Additional allowance for "process" emissions	Total	Maximum offset percentage
Electricity	60%	-	-	60%	10%
Petroleum (coal to liquid)	60%	10%	-	70%	10%
Petroleum – oil refinery	60%	10%	-	70%	10%
Iron and steel	60%	10%	10%	80%	5%
Aluminium	60%	10%	10%	80%	5%
Cement	60%	10%	10%	80%	5%
Glass & ceramics	60%	10%	10%	80%	5%
Chemicals	60%	10%	10%	80%	5%
Pulp & paper	60%	10%	-	70%	10%
Sugar	60%	10%	-	70%	10%
Agriculture, forestry and land use	60%	-	40%	100%	-
Waste	60%	-	40%	100%	-
Fugitive emissions: coal	60%	10%	10%	80%	5%
Other	60%	10%	-	70%	10%

VALUE-ADDED TAX PROPOSALS

Value-Added Tax Registration Clarification

Currently, s23 of the Value-Added Tax Act No. 89 of 1991 (VAT Act) provides that a person becomes liable to register for value-added tax (VAT) at the end of the month where the total value of taxable supplies made by that person in the period of 12 months ending at the end of that month in the course of carrying on all enterprises has exceeded R1 million. Such a person must compulsorily apply to be registered as a VAT vendor within 21 days.

Until that person is registered as a VAT vendor by SARS, that person cannot charge VAT on any supplies made it in the course of carrying on its enterprise. Unfortunately, it has taken some vendors months to be registered as a VAT vendor and there are no provisions in the VAT to address this transition from a non-vendor to a VAT vendor (ie the person may not levy VAT on any of its supplies during this period). Accordingly, it has been proposed in the Budget Speech that the liability date for registration as a VAT vendor will be clarified (ie presumably to allow a vendor to charge VAT during this transition period).

OTHER

Introduction of toll fees in Gauteng

It has now been announced that toll fees will become payable in Gauteng with effect from 30 April 2012. Even though the Government agreed to fund SANRAL with a once-off payment of R5,75 billion, a decision was taken to introduce the levy even though at reduced rates. Essentially cars with e-tags will pay 30cent per kilometre. Taxis and other public transport operators are still exempt from paying any levy. It has also been indicated that a so-called frequent user cap of R550 a month will be introduced for light vehicles and motorcycles. Depending on when heavy vehicles make use of the toll roads, a so-called time of day saving of 20% will apply.

It is disappointing that a decision was taken to continue with the implementation of the tolling system. Ultimately the question arises how the improvement of roads should be funded, especially in circumstances where a fuel levy is paid by motorists.

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