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May 2018 Newsletter

The Davis Tax Committee Concludes Its Work

The Davis Tax Committee (DTC) has announced the conclusion of its work and the publication of the following four final reports:

1. VAT (replaces the first VAT report);
2. Corporate income tax (CIT);
3. Public benefit organisations (PBO's);
4. Wealth tax.

The reports are based on the mandate of the DTC as per its Terms of Reference. The PBO and wealth tax reports were done in addition to the specified items in the Terms of Reference. The DTC does not require any further input on the four reports that have now been published as the reports have been finalised.

It is important to note that, as mentioned in the Terms of Reference of the DTC, "the Committee is advisory in nature, and will make recommendations to the Minister of Finance. The Minister will take into account the report and recommendations and will make any appropriate announcements as part of the normal budget and legislative processes. As with all tax policy proposals, these will be subject to the normal consultative processes and Parliamentary oversight once announced by the Minister."

This brings the DTC to the conclusion of its work within five years of being appointed by the Minister of Finance on 17 July 2013 to inquire into the role of the tax system in the promotion of inclusive economic growth, employment creation, development and fiscal sustainability.

Given the important nature and potential impact of these recommendations we have written abridged versions of the proposals on a wealth tax as well proposals regarding VAT for your perusal.

Davis Tax Committee recommendations on a Wealth Tax

Since 1994 South African fiscal policy has placed little emphasis on wealth taxes, save for recent increases in the rates of transfer duty and estate duty. Given the disturbing levels of wealth inequality in South Africa, a taxation system that would ignore such disparities of wealth will lack the important requirement of legitimacy in the tax system.

The process of creating a wealth tax in South Africa as a means to redress South Africa's levels of inequality would need to start with the consideration of a very simple form of an annual net wealth tax.

The decision on whether to implement an annual net wealth tax cannot be made without the following:

Consideration as to the appropriate tax base
The most important single question is whether retirement funds should fall within the scope of the tax. This is a controversial and complex issue which requires intensive engagement from Treasury, SARS and the relevant stakeholders, including the retirement industry and trade unions.

Comprehensive data on the pattern of wealth ownership
The DTC recommends that all taxpayers and beneficial owners of wealth (which includes control of trusts as well as beneficiaries thereof) that are required to submit an income tax return must be required to include the market value of all readily ascertainable wealth in a revised tax return for the 2020 year of assessment.

An evaluation as to the cost effectiveness of implementing a wealth tax
It is apparent from these recommendations that the introduction of a wealth tax cannot be implemented in the short term. Given the DTC's findings on the extent of wealth inequality and the importance of the legitimacy of the tax system there are interim measures that could be implemented to promote these objectives. For this reason, the DTC recommends that the focus should initially be on increasing estate duty collections given that the necessary administrative capacity already exists.

Finally, most of the wealth tax submissions received by the DTC point to the fact that progress could be made in reducing South Africa's levels of inequality by eradicating wasteful/corrupt government expenditure and curbing the levels of tax evasion that currently exist.

Davis Tax Committee final report on VAT

The terms of reference of the Davis Tax Committee (DTC) in general required the Committee "to inquire into the role of the tax system in the promotion of inclusive economic growth, employment creation, development and fiscal sustainability", and in particular as it relates to value-added tax ("VAT"), to give specific attention to:

"…efficiency and equity. In this examination, the advisability and effectiveness of dual rates, zero rating and exemptions must be considered"

Brief summary of recommendations.

Taxpayer compliance: The VAT gap

Essentially the tax gap in the VAT environment is the difference between the tax that is due under the VAT law, and the amount of actual tax collected. The magnitude of the gap **"can be seen as an indicator of the effectiveness of VAT enforcement and compliance measures, as it arises as a consequence of revenue loss through cases of fraud and evasion, tax avoidance, bankruptcies, financial insolvencies as well as miscalculations".**

The following observations and actions have been recommended to SARS:

- continue to monitor the VAT compliance gap as a means of evaluating its performance, and to inform strategic decisions about tax;
- take the opportunity of the release of the supply-use tables in February 2015 to update its estimate of the VAT gap, and its sectoral composition;
- consider broadening its tax gap analysis to include other major taxes and;
- further integrate its revenue and national compliance analyses, to support systemic compliance risk management. There is more scope for more detailed revenue analysis of revenues from individual industry sectors and taxpayer segments to support strategic risk analysis.

Zero-rating
The recommendation of the DTC is that no further zero-rated food items should be considered.

Dual (multiple) rates
The DTC recommends that multiple rates not be adopted.

Exemptions
This has been considered mainly from a financial services perspective and the DTC has suggested that the various approaches adopted in other jurisdictions should receive further urgent consideration by National Treasury and SARS.

Place of Supply Rules
Explicit place of supply rules have been adopted in most jurisdictions so as to fix the place in which supplies are to be taxed and accounted for. Given the magnitude of cross-border trade, in particular cross-border services, generally accepted place of supply rules are necessary to prevent double taxation and non-taxation. The OECD has issued the International VAT/GST Guidelines that seek to promote common place of supply rules.

The DTC recommends that the VAT Act be amended to ensure the inclusion of clearly stated 'place of supply rules', specifically rules that are in harmony with the OECD Guidelines and which are supported and adhered to by other VAT jurisdictions.

E-Commerce
The new frontier for VAT is its application in an electronic commerce ("e-commerce") environment, where the supply of electronic services across jurisdictional boundaries has given rise to many compliance challenges for governments. A significant number of foreign jurisdictions have sought to address this conundrum by adopting place of supply rules that apply specifically to e-commerce.

The Committee recommends that a number of technical amendments be made to the South African rules as regards the definition of "electronic services", while the Committee also recommends that a distinction be drawn between B2B and B2C supplies.

Macroeconomic impact of raising VAT
The recommendation was to not increase VAT, however if it was (as it now has been) the recommendation was that a range of compensatory mechanisms be considered for adversely affected consumers

Traditional Communities
The DTC recommends that the VAT Act be amended to place traditional communities who operate similarly to a municipality on the same footing as municipalities.

It is interesting that despite of the in depth analysis by the DTC, VAT was indeed raised to 15%. The most logical approach would be to close the "VAT Gap" by improving collections disclosure and the like. One can expect an increase in activity in this area as well.

Annual Employer Reconciliation for the period 1 March 2017 – 28 February 2018

Employers are required to submit their PAYE Employer Annual Reconciliations between 1 April and 31 May 2018 to SARS, confirming or correcting payroll tax amounts which were declared in respect of the 2017/2018 tax period.

Should you require professional assistance in this regard please do not hesitate to contact us.

Sincerely,

E M LUIZ
Chartered Accountants
Registered Auditors

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