

15 December 2017

**Final Response Document on the 2017 Rates and Monetary Amounts
and Amendment of Revenue Laws Bill (excluding response to the
proposed introduction of the Health Promotion Levy to be imposed on
Sugary Beverages)**

**(Based on report-back hearings to the Standing Committee on Finance
and Select Committee on Finance in Parliament)**



**NATIONAL
TREASURY**



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1. BACKGROUND

1.1. PROCESS

The 2017 Draft Rates and Monetary Amounts and Amendment of Revenue Laws Bill (Draft Rates Bill) gives effect to the major tax proposals that were announced by the Minister in the 2017 Budget on 22 February 2017. The 2017 Draft Rates Bill was first released for public comment on Budget Day, 22 February 2017. The major tax changes contained in the 2017 Draft Rates Bill include an increase in the dividends tax rate from 15 per cent to 20 per cent, effective from Budget Day, 22 February 2017 as well as the new 45 per cent rate on taxable income above R1.5 million, effective from 1 March 2017. The 2017 Draft Rates Bill also contains changes in other tax rates and monetary thresholds, excise duties on alcohol beverages and tobacco products, and SARS reporting requirements. Further, the 2017 Draft Rates Bill also proposed a Health Promotion Levy to be imposed on Sugary Beverages.

National Treasury and SARS briefed the Standing Committee on Finance (SCoF) on the Draft Rates Bill on 23 May 2017. Public comments to the SCoF on the 2017 Draft Rates Bill (excluding comments on the proposed introduction of the Health Promotion Levy to be imposed on Sugary Beverages) were presented at hearings that were held on 6 June 2017. On 14 June 2017, National Treasury and SARS presented a draft response document to the SCoF containing a summary of responses to comments received on the 2017 Draft Rates Bill (excluding comments to the proposed introduction of the Health Promotion Levy to be imposed on Sugary Beverages). On 28 November 2017, National Treasury and SARS briefed the Select Committee on Finance on the key issues contained in the 2017 Rates Bill.

The purpose of this Final Response Document is to explain the pertinent changes made to the 2017 Draft Rates Bill (excluding proposed changes to the proposed Health Promotion Levy to be imposed on Sugary Beverages) published for public comment on 22 February 2017 that have been included in the 2017 Rates Bill introduced by the Minister of Finance in the National Assembly on 25 October 2017.

1.2. PUBLIC COMMENTS

With regard to the proposed changes to the Draft Rates Bill, excluding proposed changes to the proposed Health Promotion Levy to be imposed on Sugary Beverages, the National Treasury and SARS received responses from 4 organisations and individuals (see Annexure A attached). There were 3 organisations that presented their responses orally during the public hearings hosted by the SCoF on 6 June 2017.

1.3. POLICY ISSUES AND RESPONSES

Provided below are the responses to the policy issues raised by the public comments received, both written and during the public hearings. These comments were taken into account in making changes to the 2017 Draft Rates Bill. Comments that fall

wholly outside the scope of the Draft Rates Bill have not been taken into account for purposes of this response document.

1.4. SUMMARY

This draft response document includes a summary of the main written comments received on the 2017 Draft Rates Bill, excluding proposed changes to the proposed Health Promotion Levy to be imposed on Sugary Beverages, as well as the issues raised during the public hearings held by the SCoF.

The main comments that were raised during the public hearings and the other main issues in the 2017 Draft Rates Bill, excluding proposed changes to the Health Promotion Levy to be imposed on Sugary Beverages, relate to:

- The increase in the Dividends Tax rate
- Tax rates and monetary thresholds:
 - Increasing annual limit for tax free savings account;
 - Increasing the fringe benefit exemption ceiling for employer provided bursaries
- SARS reporting requirements
- Enabling better public consultation

The response document does not take into account proposals raised that were not part of the Budget proposals and the 2017 Draft Rates Bill. Should taxpayers and tax advisors wish to raise issues that are not included in the 2017 Draft Rates Bill, they are welcome to write to the Minister of Finance through a separate process.

2. DRAFT RATES AND MONETARY AMOUNTS AND AMENDMENT OF REVENUE LAWS BILL

2.1 DIVIDENDS TAX (DT)

2.1.1 Policy rationale for the increase in DT

(Main reference: Section 64E of the Income Tax Act : Clause 11)

On 22 February 2017, the Minister made an announcement in the Budget to increase the DT rate from 15% to 20% with effect from 22 February 2017, in order to reduce the difference between the effective statutory tax rate on companies and distributed dividends and the proposed top marginal personal income tax rate of 45%.

Comment: It is submitted that National Treasury (NT) should be offering a favourable dividends tax rate regime for small businesses to ensure that it becomes more favourable to start a small business rather than simply taking up employment. Applying a policy of equalised tax rates does not support such distinction. Furthermore, should NT have concerns regarding the types of small business that

should benefit from a favourable DT rate, this could be addressed by excluding businesses or industries that do not contribute to the NDP objective. The increase in the DT rate contradicts the NDP stated objective to encourage and incentivise small business development. All small businesses that create jobs should be incentivised by this regime to ensure that there is 'uptake' by small business owners in all spheres of economy.

Response: Not accepted. While it is acknowledged that tax has an impact on the returns to shareholders, the rate of taxation of dividends is not the long-run determinant of investment in enterprises. It is primarily determined by the profitability of the enterprise, and influenced by the dividend policy of the enterprise. Tax policy relief is a blunt instrument to use for incentivising focussed business development. It has a broad impact by design, and is therefore not a good instrument for limited intervention. The dividends tax applies to dividends received by shareholders, and a carve-out for dividends received from a subset of companies would be inequitable.

In addition, the South African tax system already offers several incentives for small businesses. These include the turnover tax regime for micro businesses, to simplify tax compliance, and the Small Business Corporation (SBC) regime, which offers favourable income tax rates to small enterprises. In addition, there is also a Venture Capital Company (VCC) regime, which is aimed at incentivising equity funding for small businesses.

2.1.2 Rationale for effective date of rate increase (Retrospective effect)

(Main reference: Section 64E of the Income Tax Act: Clause 11)

Comment: Despite the fact that corporate South Africa has accepted the DT rate increase, concerns are reiterated regarding the apparent lack of legal mandate under which the DT rate increase has been achieved and the need for resolution in this regard. It is submitted that there exists no reason to implement a retrospective rate change and even less so, a retroactive rate increase as any avoidance concerns are speculative at best. It should be NT policy to adhere to the principle of prospective legislative amendments at all times, including instances relating to rate changes, except in exceptional circumstances such as material tax evasion practices, which is not applicable in the current instance.

In addition, the DT rate increase is imposed without the existence of an apparent legal mandate by the legislature to do so. If the amendment of tax rates other than those applying to 'taxable income' is a policy requirement of NT going forward, then the law should be amended to accommodate such policy (and extend the Minister's powers in this regard). SAICA does not support such extension and harbours concerns in respect of the legality of the executive having *de facto* legislative powers and is also concerned regarding the uncertainty such powers create.

The DT proposal is retroactive as it will apply to dividends declared before the Rates and Monetary Amounts and Amendment of Revenue Laws Bill is enacted. This pre-empted Parliaments' adoption of the proposal and hinges on whether the Minister's announcement creates a legal obligation.

The SCoF should be cognisant of the Minister's *quasi* legislative powers for final taxes and should not support the principle of retroactive tax rate change. Given that business has already adopted the DT rate increase current condonation should be noted by SCoF as an exceptional case.

Response: Not accepted. The tax liability for DT is triggered when the dividend is paid to the shareholder. With regard to the meaning of "paid", section 64E of the Income Tax Act draws a distinction between listed and unlisted companies. With regard to listed companies, paid means the date in which the dividends are actually paid. With regard to unlisted companies, paid means the earlier of the date on which the dividend is "actually paid" or becomes "due and payable".

On 22 February 2017, the Minister made an announcement in the Budget to increase the DT rate from 15 per cent to 20 per cent with effect from 22 February 2017. This implies that the new 20 per cent DT rate will be triggered when dividends are paid to shareholders on or after 22 February 2017.

South African law distinguishes between retroactive legislation and retrospective legislation. Retroactive legislation means legislation that changes the law with effect from a date in the past, in respect of events or transactions irrespective of whether they occurred before the date of announcement, typically where legislation provides that from a past date, the new law shall be deemed to have been in operation. On the other hand, retrospective legislation means legislation that affects an event that occurred prior to the date on which the legislation was promulgated but on or after the date on which the proposed change in the law was first announced.

Applying the above to the given circumstances, the proposed increase of the DT rate from 15 per cent to 20 per cent with effect from 22 February 2017 is not retroactive as it does not seek to tax dividends that were paid before 22 February 2017. The proposal was effective from the date of the announcement, not from a date before then. However, the proposed increase can be viewed as retrospective as it has been implemented before the legislation has been promulgated. Other proposals in the Draft Rates Bill, such as changes to personal income taxes, can be characterised in the same manner. In fact, most rates and threshold changes take place after the announcement on Budget Day, and are implemented before the tax laws are enacted (normally around December, about ten months after the announcement). Given the market sensitivity of tax announcement, this practice is the norm in order to ensure that taxpayers do not rush to restructure their tax affairs to lower or avoid paying the full amount of the expected tax.

All over the world, it is not uncommon for taxation measures to be enacted with retrospective operation and for those measures to commence from the date of the budget announcement, rather than the date of a transaction or enactment of legislation. Generally, there is acceptance that amendments to tax legislation may apply retrospectively, where the Government has made an announcement of its intention to introduce legislation with sufficient detail of the proposal and subsequent legislation providing for commencement with effect from the date of announcement. It is international practice for countries to accept that retrospective amendments may be appropriate where a retrospective provision (i) corrects an unintended consequence of a provision, (ii) addresses tax avoidance and (iii) might otherwise lead to a significant behavioural change that would create undesirable consequences. This also accords with the views expressed in the recent North Gauteng High Court, Pretoria judgement handed down on 29 May 2017 in the matter between Pienaar Brothers Ltd and Commissioner for the South African Revenue Service and the Minister of Finance.

In South Africa, similar to other countries, this happens regularly when the Minister of Finance makes an announcement in the Budget for that announcement to take effect on the date of the Budget or 1 March of the same year, but before Parliament passes the Rates and Monetary Amounts and Amendment of Revenue Laws Bill, for example announcements relating to the changes to the personal income tax tables, tax rebates, medical tax credits, excise duties and transfer duties.

However, if Parliament does not accept the proposal regarding the increase in the rate of DT with effect from the date of the Budget, Government (through SARS) will have to refund the difference between the DT paid in accordance with this proposal and the DT that is payable in terms of the law after the Rates and Monetary Amounts and Amendment of Revenue Laws A Bill has been passed by Parliament.

Comment: One reason given for the increase of DT rate is to address arbitrage opportunities for individuals who could pay themselves with dividends rather than salaries. The individual tax rates were only increased with effect from 1 March 2017. Therefore, increasing the DT rate from 1 March 2017 would largely have addressed this risk. Therefore, no need exists to impose the DT rate change before 1 March 2017.

Response: Not accepted. The primary risk that informed the immediate effective date is the risk of accelerating dividend payments to benefit from the lower 15 per cent rate that applied before the announcement.

2.1.3 Practical Implementation concerns relating to the increase on 22 February 2017

Comment: NT needs to be cognisant of the manner in which both industry and SARS are required to respond to an immediate tax rate change, with the attendant risk of errors for industry due to lack of adequate testing systems. Consequently, NT should

not resort to such immediate tax rate changes as a matter of policy and should rather entertain such a practice on an exceptional basis. Furthermore, where such rate changes are viewed as being merited due to exceptional circumstances, it is assumed that SARS will be consulted with sufficient lead time to ensure that they can practically consider and resolve implementation challenges.

Response: Noted. NT and SARS considered and discussed the practical implementation of the proposal before and after the announcement by the Minister in order for SARS to be ready to administer the increased DT rate. The first dividends tax returns to be submitted with the new 20 per cent rate were due by the end of March 2017 and payment of dividends tax for the month of February 2017 was also only due by the end of March 2017. SARS updated the dividends tax returns and its systems on 10 March 2017, in time for the end of March due date for the submissions of returns and payment of dividends tax that included dividends tax on dividend payments from Budget Date to the end of February. Information on the SARS website regarding dividends tax was updated on 24 February 2017 to reflect the Budget announcement.

2.2 TAX AND MONETARY INCOME TAX (PERSONS AND INDIVIDUALS)

2.2.1 Tax free savings accounts

(Main reference: Section 12T(4)(a) of the Income Tax Act : Clause 9)

Tax free savings accounts were introduced on 1 March 2015, with an annual allowance of R30 000. The 2014 Budget stated that the allowance would be increased in line with inflation. In the 2017 Budget, Government proposes to increase the annual allowance to R33 000.

Comment: The increase in the annual contribution limit was welcomed. It is requested that the lifetime limit also be increased.

Response: Noted. The current lifetime limit of R500 000 far exceeds the potential amount that could have been invested in tax free savings account since its introduction. An increase will push the date at which the lifetime limit could possibly be reached still further into the future. An increase is not necessary at this early stage of the incentive.

2.2.2 Fringe benefit taxation: bursary limit changes

(Main reference: Section 10(1)(g) of the Income Tax Act: Clause 7)

Annexure C of the 2017 Budget Review includes a proposal to increase the fringe benefit exemption for employer provided bursaries.

Comment: There is a discrepancy between the thresholds applicable to different NQF levels referred to in Annexure C of the Budget Review (NQF 7 and above), and the Draft Rates Bill (above NQF 4). Payroll software providers are hesitant to build changes into payroll systems due to this uncertainty.

Response: Accepted. The threshold stated in the Draft Rates Bill is correct, since that is also the current threshold. There was a mistake in Annexure C of the Budget Review.

2.3 SARS REPORTING REQUIREMENTS PROPOSALS

(Main reference: Section 107 of the Income Tax Act and section 74 of the Value Added Tax: Clauses 12 and 20)

The 2017 Draft Rates Bill proposes amendments to section 107 of the Income Tax Act and section 74 of the VAT Act to make provision for the Minister of Finance to make Regulations in relation to information the Minister deems necessary to obtain from the Commissioner in order to ensure transparency and reporting on tax collection.

Comment: The proposed amendment is a welcome development and could be used to harness greater transparency and accountability (in line with administrative justice principles). The current weakness in legislation is that section 70(1) of the Tax Administration Act that allows SARS to disclose certain information to National Treasury is too narrow. Firstly, the term “may provide” makes it at the discretion of SARS whether or not to provide information, weakening accountability in reporting actual revenue collected for any tax. Secondly, the extent of the information that SARS may provide is limited to taxpayer or SARS information in respect of: (i) a taxpayer which is an institution referred to in section 3(1) of the Public Finance Management Act, (ii) An entity referred to in section 3 of the Local Government Municipal Finance Management Act to the extent necessary for Treasury to perform their functions and exercise their powers under these two Acts, (iii) a class of taxpayers to the extent necessary for the purpose of tax policy design or revenue estimation. Other agencies such as the South African Reserve Bank must fully share information. The Financial Intelligence Centre and the South African Reserve Bank should also be allowed a much freer flow of information between each other as enforcement agencies, especially in terms of offshore transactions (e.g. Panama Papers).

Response: Noted. The proposed amendments to section 107 of the Income Tax Act and section 74 of the VAT Act seek to ensure transparency and reporting on tax collection. These two amendments will give the Minister of Finance powers to make Regulations in this regard.

Currently, with regard to the general sharing of information between SARS and NT for policy making purposes, SARS is in terms of section 70(1) of the Tax

Administration Act empowered to share information with NT in respect of PFMA institutions, Local Government MFMA entities and a class of taxpayers to the extent necessary for the purposes of tax policy design or revenue estimation.

In addition, section 70(3) of the Tax Administration Act allows SARS to disclose information to the South African Reserve Bank and the Financial Intelligence Centre, as may be required for the purpose of exercising a power or perform a function or duty under the South African Reserve Bank Act or for the purpose of carrying out the duties and functions under the Financial Intelligence Centre Act, respectively. With regard to sharing of information between the South African Reserve Bank and Financial Intelligence Centre, the Tax Administration Act deals with the sharing of information by SARS to other entities and does not deal with the sharing of information between Financial Intelligence Centre and the South African Reserve Bank.

2.4 ENABLING BETTER PUBLIC CONSULTATION PROCESS

2.4.1 Lack of NT feedback

Comment: It is submitted that to enable a proper public consultative process, NT should engage with the public on their submissions, provide structured policy positions or discussions preceding finalisation of proposals. NT should also give feedback on why submissions are accepted or rejected, prior to the SCoF hearings to address matters raised so that the SCoF is only required to consult on matters where information needs to be shared. It also means that any changes or solutions resulting from NT consultation process have themselves been subject to consultation.

Response: Noted. NT and SARS published the Draft Rates Bill for public comment on 22 February 2017. NT and SARS briefed the SCoF on the Draft Rates Bill on 23 May 2017. Public comments to the SCoF were presented at hearings that were held on 31 May 2017 and 6 June 2017. The first report back to the SCoF on proposed amendments in the Draft Rates Bill, excluding on the proposed Health Promotion Levy to be imposed on Sugary Beverages was on 14 June 2017. In terms of the process, it would open up the process to bilateral negotiations between taxpayers, NT and SARS if feedback were to be provided on the reasons why submissions are accepted or rejected, prior to the SCoF public hearings. Besides making the process for each tax proposal less transparent and opening the process to undue pressure from taxpayers that are adversely affected, it could also undermine the parliamentary process, which must take its own course during which NT and SARS provide a formal response to Parliament and the public (in a transparent manner) as to why a comment is accepted or rejected.

The policy rationale for proposals is included in the annual Budget Reviews and the Explanatory Memoranda, while discussion documents are published, further consultation is done, for more significant policy proposals such as retirement reform and the carbon tax.

2.4.2 SCoF time period for submissions

Comment: It is requested that the period for submitting comments to the SCoF should be sufficient to enable broad participation, but also allow sufficient time for the public to properly prepare written or oral submissions that substantively inform often challenging policy and technical positions. This will substantially increase once NT habitually engages the public on comments made on the Draft Tax Bills prior to the SCoF public hearings.

Response: Noted. (Parliament to respond)

3. Annexure A - Public Comments

2017 Rates and Monetary Amounts and Amendment of Revenue Laws Bill

Name of Company	Contact Person
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