national treasury

Department:
National Treasury
REPUBLIC OF SOUTH AFRICA

REQUEST FOR PUBLIC COMMENTS - THE SOUTH AFRICAN TONNAGE TAX PROPOSAL

South Africa is an open economy and its economic growth, prosperity and welfare depend on fully accessing global trade opportunities. Consequently, government continuously seek to improve the country's trade and investment environment. This is to be achieved through a host of interventions to reduce the cost of doing business and investing in South Africa. These measures include the introduction of an industrial policy framework, establishment of a robust and predictable tax system, customs administration and tariff reforms, and the stepping up of investments in road, rail and ports infrastructure.

South Africa significantly depends on maritime trade for its international transport needs; however, mostly foreign registered vessels provide this service. The non-South African registered vessels which transport the country's imports and exports translates into significant transport service payments by South Africa to the rest of the world. This amounted to more than R38 billion in 2007. It represents an opportunity cost to South Africa as ships transporting commodities and goods to and from a jurisdiction, create wealth for the country in which the vessels and the ship-owning company are registered. A sound economic argument thus exists to revive the declining domestic shipping industry.

In the 2005 Budget, government announced its intention to investigate the possible introduction of a tonnage tax regime in keeping with long-term trade facilitation initiatives. This notional or presumptive corporate income tax system would align South Africa's shipping tax regime with the fiscal systems of other major maritime nations. The tonnage tax will also form an integral part of Government's Maritime Transport Agenda: 2010 which, *inter alia*, seeks to arrest the decline of the domestic shipping register. By potentially bringing shipping companies' key strategic management decisions back to South Africa the scope of secondary support activities will broaden. This includes a growth in crewing opportunities for South African seafarers. It also has the potential of reducing the sizable transport service payments to the rest of the world, which in turn would have a positive impact on the current account.

KEY DESIGN FEATURES OF THE TONNAGE TAX

The proposed South African tonnage tax regime is based on the ‘Dutch model’, due to its design and administrative simplicity. It is an elective system, taxing shipping companies at fixed rates according to the size of their ships and days operated during an accounting period, and not according to the company’s business income results. Tonnage tax regimes have been successfully implemented in other countries such as Belgium, India, Ireland, the United Kingdom and the Netherlands.

Tonnage tax rate

In terms of the tonnage tax proposal a notional profit is computed based on the number and size of ships operated during a year. The proposed tonnage rate or fixed profit per day rate (used for calculating the notional profit) is as follows:

Fixed Profit Rates: Proposed scale of charges based on vessels net tonnage	Fixed profit per day in R
For each 100 tons up to 1 000 net tons	R4.00
For each 100 tons between 1 000 and 10 000 net tons	R3.00
For each 100 tons between 10 000 and 25 000 net tons	R2.00
For each 100 tons above 25 000 tons	R1.00

As a second step the graduated formula of fixed profit per day is applied to the net registered tonnage (NRT) of the vessel, which takes into account only its carrying capacity, and not its gross registered tonnage (GRT). For example, this calculation will result into the following notional profit figure for a vessel with a net tonnage of 10,000t (assuming the ship was used for 365):

Net tons	Calculation 1	Calculation 2	Notional profit
0 – 1 000	1 000/100 = 10	10* R4.00*365 days	R14 600
1 000 – 10 000	9 000/100 = 90	90* R3*365 days	R10 950
10 000 – 25 000	15 000/100 = 150	0* R2*365 days	R00
t > 25 000	163 000/100 = 1,630	0* R1*365 days	R00
		Annual taxable tonnage profit	R25 550

Thirdly, in calculating the corporate tax liability, the current corporate tax rate is applied to the notional profit, i.e., R25 550 @28% (i.e. the CIT rate), translating into an annual tax bill of R7 154. The proposed tonnage tax differs materially from so-called registration fees payable in Flags of Convenience registers, where a very low and flat rate is applied to the tonnage of the registered vessel. It is important to note that the tonnage tax qualifies as a creditable tax in terms of concluded bilateral tax treaties.

Transitional and anti-avoidance matters

The discussion document proposes further a range of adjustments to standard corporate income tax rules. These changes were informed by the need to draw a very clear, unambiguous and easy-to-administer ring-fence around qualifying tax-preferential tonnage tax activities on the one hand, and secondary and incidental shipping activities on the other. The suggested ring-fence anti-avoidance rules and reform proposals regarding core and secondary/incidental shipping transport activities compare well with international practices in Denmark, the United Kingdom and various other countries.

Key corporate tax aspects for consideration in the tonnage tax design are as follows:

- The tax treatment of profit distribution streams received in the hands of a qualifying tonnage tax company;
- The parallel recording of capital gains as a company operates within the tonnage tax regime with possible roll-over relief as tonnage tax assets are realised;
- The tax treatment of capital allowances that cannot be accessed whilst in the tonnage tax regime;
- Election-in and election-out processes with an internationally highly attractive proposal of locking tonnage tax companies in for only five years in lieu of the international standard 10-year lock-in periods;
- Rules pertaining to tonnage tax company mergers, demergers and amalgamations; and
- Anti-avoidance rules for loss deductions, finance costs, thick capitalisation rules, intra-group and inter-company loans, treatment of investment income, adapted transfer pricing rules, thin-capitalisation and CFC regulations.

National Treasury invites the public to submit comments on the draft tonnage tax proposal. Comments should be submitted via e-mail to marie.bertrand@treasury.gov.za or by fax to 012 323 2917 by 31 October 2008.

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