
MEDIA STATEMENT

PUBLICATION OF THE DISCUSSION DOCUMENT ON THE REVIEW OF THE DIESEL FUEL TAX REFUND SYSTEM FOR PUBLIC COMMENT

The National Treasury today publishes the Discussion Document on the Review of the Diesel Fuel Tax Refund System for public comment and further consultation. This paper follows on announcements in Budget 2015 to undertake a review of the diesel refund administration to address anomalies in the system related to qualifying activities and beneficiaries. National Treasury and the SARS committed to explore alternative, more equitable rules and administrative procedures in consultation with affected industries.

Government currently imposes a suite of fuel taxes in terms of the Customs and Excise Act, No. 91 of 1964 (C&E Act), namely the fuel levy (FL), Road Accident Fund (RAF) levy, and excise duty. The diesel refund system provides full or partial relief for the FL and RAF levy to primary producers in the agriculture, forestry, fishing and mining sectors. It was introduced from 2000 in a phased approach and is aimed at protecting international competitiveness of local industries and reducing the road-related tax burden of the RAF levy for certain non-road users.

The diesel refund system has faced several technical administrative and legal challenges. Some eligible firms are unable to benefit from the system, while others appear to be making disproportionate refund claims. The main administration concerns relate to the shared VAT administration, logbook compliance and authorisation of primary production.

To address these concerns, this discussion paper outlines the main options for a simplified administration system and proposals for reform which ensure that the policy intent of the diesel refund system is maintained. The paper is structured as follows:

- Overview of the diesel refund system
- Policy context – Fuel taxation and inefficient fossil fuel subsidies
- Current diesel refund administration
- Key challenges with the administration system
- Proposals for reforms

This paper was jointly developed by the National Treasury and the South African Revenue Service (SARS).

Background - Structure and Administration of the diesel refund system

The diesel refund system consists of a refund in respect of the FL and RAF levy and is provided for in terms of sections 75(1A) to (1D), 4A and 7A read with Part 3 of Schedule No.6 to the C&E Act.

Diesel refunds are claimed based on the type of usage and include on land (farming, forestry and mining), and offshore activities (commercial fishing, coasting vessels, offshore mining, NSRI vessels, vessels conducting research in support of the marine industry, coastal patrol vessels, vessels servicing fibre optic telecommunications cables), harbour vessels, rail freight and peak power electricity generation plants (with a capacity of more than 200 MW).

Beneficiaries of the diesel refund qualify as follows:

- Primary producers on land (farming, forestry and mining) qualify for a refund amounting to 100 per cent of the RAF levy and 40 per cent of the FL in respect of 80 per cent of their eligible diesel fuel purchases.
- Rail freight (but not passenger rail) and harbour vessels are fully refunded the RAF levy only.
- Full refunds of both the FL and RAF levy apply to offshore activities whilst peak power electricity generation plants get full refunds of the RAF levy and 50 per cent of the FL since 1 April 2016.

The diesel refund system is administered through the C&E Act and the VAT Act, No. 89 of 1991. Diesel refunds are currently processed through the VAT refund system and are offset against any VAT which may be payable for the tax period concerned. Enterprises conducting eligible activities must be registered for VAT purposes in order to claim the refund. The system also requires that a fuel purchaser who is registered for the diesel refund must maintain a record of supporting documents including purchase invoices, sales invoices and logbooks.

Technical Challenges

The main challenges facing the system include:

- *Shared VAT Administration* – Potential diesel refund beneficiaries such as small scale primary producers that are not required to register for VAT purposes are inadvertently excluded from the diesel refund system. This also affects those joint ventures that share production output between members without making taxable supplies, which may not register for VAT and therefore cannot access the diesel refund.
- *Lack of logbook compliance* - to qualify for the refund, taxpayers need to maintain accurate logbooks including information on diesel storage and volumes eligible for the refund. Certain taxpayers, especially in the agriculture, forestry and mining sectors currently claim refunds without maintaining the detailed logbook verification required by law.
- *Authorisation of primary production* – Commercial fishing and mining operations may only qualify for diesel refunds if authorised through a fishing permit or mining right in

terms of the relevant legislation. Qualifying fishing and mining operations that fall within the intended scope of the diesel refund system have therefore in some instances been denied refunds where authorisation was outsourced to contractors, pooled in joint venture partnerships or had their fishing permits or mining rights delayed by the Departments of Agriculture, Forestry and Fisheries or Mineral Resources respectively.

- *Outsourcing of operations.* Primary producers in the agriculture, forestry, fishing and mining industries regularly outsource a range of operational activities. Under the current rules of the diesel refund system, only primary producers can claim diesel refunds where the primary producer provides the diesel to the contractor for dry contracting while any diesel that is obtained by the contractor itself, referred to as wet contracting, is disallowed.

Proposed reforms to the diesel refund system

To address these concerns and limitations of the current system, the following reforms are proposed.

Interim Diesel Refund Amendments

Whilst the holistic review of the system was underway, interim amendments were necessary ahead of the longer term reforms to address outstanding assessments, disputed cases and pending litigation. These interim amendments to the current diesel refund system became effective on 1 April 2016. This included:

- Qualification for refunds by ceded mining right holders, contract and small-scale farmers in sugarcane production, on-going mining rehabilitation; and
- Reducing the FL benefit rate from 100 per cent to 50 per cent of the FL for peaking electricity generation plants.

Qualifying primary production activities rather than users:

The systemic problems confronting the current administration of the diesel refund system are due to the emphasis on eligible diesel purchases by qualifying users, rather than on qualifying activities and use.

- It is proposed that the basis of the diesel refund administration be shifted from the current emphasis on allowed users to qualifying primary production activities. An indicative list of the type and nature of qualifying activities and use by primary producers is provided in the discussion paper and this will be finalised through the public comment consultative process.

Inclusion of contractors

The inclusion of contractors is proposed in the revised diesel refund system to allow smaller producers and new entrants who lack the necessary funding or experience to benefit from the system. This proposal might also require a suitable diesel use threshold, possibly by sector, to address possible administrative complexities for SARS and the taxpayer.

Standalone Diesel Refund Administration System

A standalone diesel refund administration is proposed separate from the VAT system. This will address limitations around intended beneficiaries that cannot claim the diesel refunds due to not being VAT registered. To ease the compliance burden on taxpayers and administrative burden on SARS, the new system will be phased in through the initial confirmation of current diesel refund registrants followed by the re-registration of all beneficiaries anew over time.

Linking qualifying activities to physical location

The need to link the qualifying activities to a physical location has also been identified, which will enable easier definition of primary activities and monitoring of diesel use to prevent double claims and help curb abuse of the system. The proposed exclusion of all off-site transport and any processing activities, as well as stricter registration and enforcement measures, would also significantly curb the potential for abuse.

Due date for comments

Written comments should be submitted by close of business on **15 May 2017** to:

- National Treasury email: dieselrefundcomments@treasury.gov.za; or queries to Memory.Machingambi@treasury.gov.za and
- SARS email: [C&E legislativecomments@sars.gov.za](mailto:C&E_legislativecomments@sars.gov.za)

The *Diesel Refund System Review Discussion Paper* is available on the National Treasury website: www.treasury.gov.za and the SARS website www.sars.gov.za

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