



**NATIONAL
TREASURY**

REPUBLIC OF SOUTH AFRICA

**SUPPLEMENTARY EXPLANATORY
MEMORANDUM**

TO THE

REVENUE LAWS AMENDMENT BILL, 2006



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SUPPLEMENTARY EXPLANATORY MEMORANDUM TO THE REVENUE LAWS AMENDMENT BILL, 2006

INTRODUCTION

The Revenue Laws Amendment Bill, 2006, introduces amendments to the Income Tax Act, 1962, the Customs and Excise Act, 1964, the Value-Added Tax Act, 1991, and the Revenue Laws Amendment Act, 2004.

2010 FIFA World Cup

Introduction

As part of the bid for the hosting of the 2010 FIFA World Cup the South African Government issued various guarantees to FIFA. Two of these guarantees, Government Guarantees No. 3 and 4, dealt with Customs duties and other taxes respectively and were supported by a Tax Ruling issued by SARS. Following the awarding of the 2010 FIFA World Cup to South Africa, representatives of Government, FIFA and the Local Organising Committee met to clarify the intent and scope of these two guarantees and the Tax Ruling. The proposed legislation gives effect to the agreement reached.

Definitions

A number of definitions are in addition to, or supersede those already contained in the FIFA List of Requirements and the Organising Association Agreement and apply only to Government Guarantees No. 3, No. 4 and the Tax Ruling.

Specific Concepts

Tax-free Bubble Concept

The provision for the concept of a “tax-free bubble” has been made and legislated accordingly. A tax-free bubble will be restricted to Sites for the periods specified. Practically, this means that the profit on goods (being consumable goods and semi-durable goods) sold or services rendered (provided the services so rendered (i) are intrinsic to the staging of the Championship, (ii) are enjoyed or partially utilised at a Site, and (iii) are paid for by individual members of the general public, FIFA or the Local Organising Committee) within Sites, as defined, will not be subject to any form of income tax and neither will VAT be applied at the standard rate. This applies to both non-residents as well as residents. Conversely, from an income tax perspective, expenses incurred in production of exempt income will not be permitted as deductions for income tax purposes. A reasonable allocation of expenses attributable to the exempt sales must be made and this is to be a matter between SARS and the taxpayer, where the taxpayer is otherwise subject to tax. VAT on supplies (goods and services) made in FIFA-designated Sites will be zero-rated and hence inputs will be claimable by the

vendors concerned. The only concessions that will apply in these tax-free bubbles are in respect of income tax and VAT.

The “tax-free bubble” will only be operative in respect of the following sub-components of a Site, as defined, as for the periods set out below –

- (i) The Stadia, any Exclusion Zone, any official Championship-related parking areas, Championship press and television centres (including the International Broadcast Centre), VIP Areas and any other areas or facilities as may be agreed in good faith by FIFA and SARS utilized for Official Events. The concession will be allowed for the period commencing one week before the 2009 FIFA Confederation Cup and ending immediately after the closing ceremony. A similar period will be allowed for the 2010 FIFA World Cup South Africa.
- (ii) Training sites, for official FIFA sanctioned training days at those sites only;
- (iii) Official host city public viewing venues, for Championship match days only; and
- (iv) The FIFA Flagship Store, for six months before the 2009 Confederations Cup until one month after the Closing Ceremony of the 2010 FIFA World Cup.

FIFA Retail Outlets

FIFA stores, store-in-store outlets and kiosk outlets outside of Sites, as defined, are not considered to be within tax-free bubbles and hence will be subject to the normal tax rules of the Republic. Concession operated outlets (for food and beverages, as well as merchandise) within Sites, as defined, will be within tax-free bubbles for income tax and VAT purposes. FIFA is permitted to nominate one FIFA Flagship Store which shall be considered to be a Site (and hence a tax-free bubble) for purposes of income tax and VAT provided that no tobacco products or cosmetics are sold at this store and that any alcoholic beverage sold may only be for consumption within an in-store restaurant.

Associated Persons

All references to natural persons or entities shall mean – (i) in the case of natural persons, that natural person; and (ii) in the case of entities, other than FIFA or FIFA Subsidiaries, that entity and any affiliated entity, if that entity holds at least 20% of the ordinary equity of the affiliated entity and the activities or services rendered by the affiliated entity are directly connected to the Championship.

Provisions Relating Specifically to Guarantee No. 3 (Customs)

- 1 Clause 1 (persons qualifying for relief in respect of import taxes where such goods are re-exported) of Government Guarantee No. 3 shall only include the following qualifying persons –
 - (i) FIFA and FIFA subsidiaries;
 - (ii) FIFA National Associations;
 - (iii) FIFA Confederations;

- (iv) Media Representatives;
- (v) Commercial Affiliates;
- (vi) Merchandising Partners;
- (vii) Licencees;
- (viii) The FIFA Flagship Store operator;
- (ix) FIFA Designated Service Providers as well as the pitch importer, Concession Operators, Hospitality Service Providers, design servicers, event management and marketing operations servicers and office suppliers ;
- (x) The Host Broadcaster, Broadcasters and Broadcast Rights Agencies; and
- (xi) Any employee, not resident in the Host Country for income tax purposes, of any of the above entities who is temporarily seconded to the Host Country (in respect of household goods, motor vehicles or other goods normally associated with such relocation).

2 The following imports by a person contemplated in 1 above will be free from any import taxes –

- (i) Trading stock, being consumable or semi-durable goods, provided it is imported by a qualifying person with the intention of resale at a Site or re-export within the Re-export timeframe;
- (ii) Samples of trading stock, being consumable or semi-durable goods not for re-sale, provided they are imported by qualifying persons with the intention of distribution at a Site or re-export within the Re-export Timeframe;
- (iii) Capital goods, consumable goods and promotional materials, not for resale and individually of little value, for use by a person listed in 1 above in connection with the Championship or re-export within the Re-export Timeframe; and
- (iv) Household furniture and other household effects, one motor vehicle and equipment for the exercise of a trade by an employee of a qualifying person who is temporarily seconded to the RSA for the purposes of the 2010 FIFA World Cup.

3 Subject to 4 below, where goods imported free from any import taxes are not sold, distributed, used, or re-exported as contemplated in 2 above, customs duty and VAT (import taxes) will become payable on the lower of cost or market value for customs duty purposes on the earlier of the date of their disposal, use not in connection with the Championship or expiry of the Re-export Timeframe, and as if the goods were imported on that date.

4 Where goods imported free from any import taxes are not sold, distributed, used, or re-exported as contemplated in 2 above, but are donated to another person they must be treated as follows–

- (i) Where goods are donated to a person carrying on an income tax approved public benefit activity contemplated in Part I of the Ninth Schedule to Income Tax Act, 1962, and the goods are disposed of by the that person within five years of the donation, import taxes will become payable on the lower of cost or market value for customs duty purposes at the date of the donation to the income tax exempt person, and as if the goods were imported by the donee (recipient) on that date; and
- (ii) Where other goods are donated to any other person, import taxes will become payable on the lower of cost or market value for customs duty purposes at the date of donation, and as if that good was imported by the donee (recipient) on that date.

Provisions Relating Specifically to Guarantee No. 4 (Other Taxes, Duties and Levies)

- 1 In terms of this guarantee, the following entities are exempt from liability in respect of all South African taxes not covered by Government Guarantee No.3 unless specifically stated to the contrary –
 - (i) FIFA;
 - (ii) FIFA Subsidiaries; and
 - (iii) The Participating National Associations (excluding SAFA)

Furthermore, in respect of employees who are residents of the Republic of South Africa for tax purposes, FIFA and FIFA's subsidiaries will contribute and withhold Unemployment Insurance Contributions and will also contribute Skills Development Levies. Such returns and payments will be made as and when due. FIFA and FIFA's subsidiaries will, however not withhold employees' tax in respect of these same employees. FIFA and FIFA's subsidiaries will supply SARS with a list of these employees and the total remuneration paid annually to each employee.

- 2 In terms of this guarantee, regardless of residence of tax purposes, the following entities are exempt from income tax in respect of income derived from the sale of goods (being consumable goods and semi-durable goods) or services rendered (provided the services rendered are (i) intrinsic to the staging of the Championship, (ii) enjoyed or partially utilised at a Site, and (iii) paid for by individual members of the general public, FIFA or the Local Organising Committee) at Sites, as defined, and, where VAT is applicable, must levy VAT at the zero rate on all supplies of such goods or services at these Sites –
 - (i) Commercial Affiliates;
 - (ii) Licensees;
 - (iii) The Host Broadcaster, Broadcasters and Broadcast Rights Agencies;
 - (iv) Merchandising Partners;
 - (v) FIFA Designated Service Providers (see definition);
 - (vi) Concession Operators;

- (vii) Hospitality Service Providers; or
- (viii) The FIFA Flagship Store operator.

FIFA Designated Service Providers ((v) above) are the only entities that may sell goods or render services for consumption, usage or enjoyment outside of Sites, provided that such goods or services are directly connected to the Championship and are within the parameters for which such entity has been accredited by FIFA. This is in respect of income tax only.

- 3 Where any entity as contemplated in 2 above is exempt from income tax on income derived from the sales of goods (being consumable goods and semi-durable goods) sold or services rendered (provided the services so rendered are (i) intrinsic to the staging of the Championship, (ii) enjoyed or partially utilised at a Site, and (iii) paid for by individual members of the general public, FIFA or the Local Organising Committee) at Sites, as defined, any expenditure (whether direct or indirect) incurred in producing that exempt income will not be permitted as a deduction for income tax purposes.
- 4 No withholding tax is to be levied on Championship-related payments between FIFA, FIFA's Subsidiaries, the Commercial Affiliates, Licensees, the Host Broadcaster, Broadcasters, Broadcast Rights Agencies, Merchandising Partners or the FIFA Designated Service providers.
- 5 Income arising from any good sold for foreign consumption or service rendered outside of South Africa by persons who are not residents for tax purposes in South Africa will not be attributed on a source basis to having been derived in South Africa as a result of that person's sponsoring of the Championship or broadcasting of the Championship.
- 6 Where a qualifying natural person (as listed below) is not resident for income tax purposes in the Republic, that person will not be subject to South African income taxes with respect to income derived from activities connected to the Championship. Qualifying natural persons are as follows –
 - (i) All members of the FIFA Delegation;
 - (ii) Championship referees and assistant referees;
 - (iii) Participating National Association Officials;
 - (iv) FIFA Confederation Officials;
 - (v) Media Representatives;
 - (vi) All Commercial Affiliate staff;
 - (vii) All Merchandising Partner staff;
 - (viii) All FIFA Designated Service Providers staff; and
 - (ix) Host Broadcaster, Broadcast Rights Agency, and Broadcast staff

However, the following natural persons, not resident for income tax purposes in the Republic, are excluded from the exemption contemplated in 6 above –

- (i) Team members, as defined;
- (ii) Directors and personnel of SAFA; and
- (iii) Directors and personnel of the Local Organising Committee.

- 7 Withholding taxes are to be levied in respect of non-resident Team members in accordance with international practice.
- 8 FIFA, FIFA Subsidiaries and the Participating National Associations, excluding SAFA, are to be treated on the same basis as diplomatic missions for VAT purposes in respect of goods and services directly relating to the Championship.
- 9 Notwithstanding any other provision relating to VAT, ticket sales will be subject to VAT at the standard rate of 14%. Should FIFA, a FIFA subsidiary or any Participating National Association choose to sell tickets as the principal ticket seller or as one of the principal ticket sellers then FIFA, its subsidiary or any Participating National Association must account for output VAT in respect of these sales, but may be registered for VAT and be entitled to recoup input VAT. In other words, FIFA, its subsidiary or any Participating National Association will be liable to SARS for the payment of VAT collected on the sale of tickets in the aforementioned circumstances.
- 10 In respect of hospitality sales (excluding hospitality sales for hospitality within a Site), hotel and accommodation charges the standard VAT rate of 14% is to be applied. Should FIFA, a FIFA subsidiary or any Participating National Association choose to sell hospitality off-site or accommodation as the principal seller or as one of the principal sellers then FIFA, its subsidiary or any Participating National Association must account for output VAT in respect of these sales. In other words, FIFA, its subsidiary or any Participating National Association will be liable to SARS for the payment of VAT collected on the sale of off-site hospitality or accommodation in the aforementioned circumstances.
- 11 Government Guarantee No. 4 does not include the following embedded taxes –
 - (i) Fuel taxes;
 - (ii) Excise duties;
 - (iii) The Plastic Bag Levy;
 - (iv) Air Passenger Departure tax;
 - (v) Provincial taxes (gambling taxes and motor vehicle license fees)
 - (vi) Local Government taxes (Property rates)

Administrative Aspects

- 1 All aspects pertaining to the calculation of import taxes as contemplated in Government Guarantee No.3 and other taxes, duties and levies as contemplated in Government Guarantee No.4, shall be a matter between the South African Revenue Service and the taxpayer concerned.
- 2 Where any person abuses one or more of the exemptions or concessions contemplated in this agreement by misrepresenting the purpose of an import, overstating sales within a tax-free bubble, understating purchases or expenses in respect of sales in a tax-free bubble or by any other method, SARS may, in addition to any other remedies that may be available to it, withdraw that person's entitlement to any of the exemptions and concessions contemplated in this agreement, in whole or in part, with effect from the date that an exemption, waiver or concession was first claimed. Any such withdrawal will take place in consultation with FIFA.

Date of Implementation

The proposed legislation giving effect to the MOU agreed between FIFA and the South African Government will come into effect, retrospectively, as from 1 April 2006.

CLAUSE 1

Income Tax: Amendment of section 4 of the Income Tax Act, 1962

The proposed amendment extends the list of exceptions to the secrecy waiver to allow for greater disclosure of information to the National Treasury.

CLAUSE 2

Income Tax: Amendment of section 11(hB) of the Income Tax Act, 1962

The proposed amendment introduces parity into the income tax system by configuring a once-off lump sum payment in respect of mining royalties to be akin to the expenditure incurred for payment of mining royalties over successive years. However, this deduction is limited to transactions that empower only tribal communities envisaged by the Mineral and Petroleum Resources Development Act, 2002 (Act No. 28 of 2002).

This proposed amendment will be effective for years of assessment ending on or after 31 December 2006.

CLAUSE 3

Income Tax: Amendment of section 24I of the Income Tax Act, 1962

Section 24I provides a comprehensive mark-to-market regime for foreign currency gains and losses that are largely designed to match generally

accepted accounting practice (“GAAP”). However, anomalies continue to arise where section 24I is not in line with accounting because section 24I predates recent changes to GAAP. One area of concern involves currency hedges for the acquisition of shares. Currency gains and losses to hedge these acquisitions often trigger tax consequences even though these gains and losses often go unrecognized in terms of income statements required by GAAP. The proposed amendment (section 24I(11A)) seeks to remedy significant situations of this kind.

More specifically, the new provision exempts currency gains and losses stemming from forward exchange contracts and foreign currency option contracts used to hedge foreign company acquisitions by residents. The acquisition must be of foreign shares amounting to at least 20 per cent of equity share capital of the foreign company to be acquired and the foreign company must qualify as a controlled foreign company in relation to the acquiring resident after the acquisition. However, given the elective nature of the GAAP rules in this area, the exemption from gain or loss will only apply to the extent the gain or loss is not reflected in the income statement for GAAP purposes.

The new provision also applies to controlled groups of companies. This situation would arise if one party in the group enters into a hedge so that another company within the group can acquire foreign shares. The basic conditions of this exemption are the same as a direct acquisition, except for the GAAP treatment. Exemption will be available in these cases even if the resident performing the hedge recognizes the gain or loss on its own independent income statement as long as that gain or loss would not be considered in the income statement when the resident company is viewed as part of the group.

CLAUSE 4

Income Tax: Amendment of paragraph 20 of the Eighth Schedule to the Income Tax Act, 1962

This amendment is consequential to the currency gain or loss exclusion described in proposed section 24I(11A). If any resident acquires shares in connection with a currency hedge and that currency hedge gain or loss is excluded by virtue of section 24I(11A), this exclusion must be reflected in the share (much like a rollover). Excluded currency gain will require a reduction in the base cost of the share, and excluded currency loss will trigger an increase in the base cost of the share.

CLAUSE 5

Customs and Excise: Amendment of section 1 of the Customs and Excise Act, 1964

A definition of “customs controlled area” is inserted as a result of the proposed amendment to section 6 of the Act which empowers the Commissioner to designate such areas.

CLAUSE 6

Customs and Excise: Amendment of section 6 of the Customs and Excise Act, 1964

Subsection (6)(1)(aA) is inserted to empower the Commissioner to designate any area where goods or person may enter or leave the Republic as a “Customs Controlled Area” in order to more effectively control such movement through specifically designated areas. The proposed amendment is as a result of the activities of the Border Control Co-ordinating Committee (BCOCC) regarding the formulation of a new border control strategy for the Republic.

Subsection (6)(1)(h) empowers the Commissioner to prescribe entrances and exits to or from any dock or wharf area or customs and excise airport. The proposed amendment is consequential to the designation of customs controlled areas in section 6(1)(aA). The proposed amendment now empowers the Commissioner to further secure the movement of goods and persons into and from the Republic by prescribing entrances and exits in respect of any port, land border and customs controlled area.

CLAUSE 7

Customs and Excise: Insertion of section 6A of the Customs and Excise Act, 1964

Section 6A is consequential to the insertion of section 6(1)(aA). The proposed amendment empowers the Commissioner to control the movement of goods and persons in, into, or from a customs controlled area and to determine, in consultation with the relevant person or authority, how such areas must be secured and signposted. The Commissioner is further empowered to specify the limits of any customs controlled area by rule and to make further rules relating to access control, identification of persons entering or leaving such areas, or any other matter that may be necessary to achieve the effective control over goods or persons in customs controlled areas.

CLAUSE 8

Value-Added Tax: Amendment of section 6 of the Value-Added Tax, 1991

The proposed amendment extends the list of exceptions to the secrecy waiver to allow for greater disclosure of information to the National Treasury.

CLAUSE 9

Income Tax: Amendment of section 62 of the Revenue Laws Amendment Act, 2004

Subclause (b): Subsection (1) shall come into operation on 1 September 2007