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GENERAL NOTICE

NOTICE 1428 OF 2001**NATIONAL TREASURY**

PUBLICATION OF PROVINCIAL TAX REGULATION BILL, 2001

The Minister of Finance intends tabling the Provincial Tax Regulation Bill, 2001 in Parliament for consideration during the third parliamentary term. The Bill as approved by Cabinet is published in accordance with Rule 241(c) of the Rules of the National Assembly.

Interested persons and institutions are invited to submit written representation on the Bill to the Secretary to Parliament by no later than 3 August 2001.

All submissions must be addressed to:

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PROVINCIAL TAX REGULATION BILL

BILL

To regulate the exercise by provinces of their power in terms of section 228 of the Constitution to impose taxes, levies and duties and flat-rate surcharges on the bases of taxes, levies and duties imposed by national legislation; and to provide for related matters.

B E IT ENACTED by the Parliament of the Republic of South Africa, as follows:—

Definitions

1. In this Act, unless the context otherwise indicates—
- “**Budget Council**” means the Budget Council established by section 2 of the Intergovernmental Fiscal Relations Act, 1997 (Act No 97 of 1997); 5
 - “**Commission**” means the Financial and Fiscal Commission established by section 220 of the Constitution, 1996 (Act No 108 of 1996);
 - “**financial year**” means a year ending 31 March;
 - “**MEC for Finance**” means the member of an Executive Council of a province responsible for finance in the province; 10
 - “**Minister**” means the Minister of Finance;
 - “**national economic policy**” includes tax policy for the Republic as determined by the national government in pursuit of a tax system that is coherent, efficient, equitable, administratively simple and internationally competitive; 15
 - “**prescribe**” means prescribed by regulation in terms of section 7;
 - “**provincial tax**” means a compulsory payment to a provincial government, including a levy or duty, or a flat rate surcharge on the tax base of a tax, levy or duty that is imposed by national legislation, which may be assessed on a person, entity or assets and which a province may impose in terms of section 228 of the Constitution, but does not include a user charge; 20
 - “**user charge**” means an identifiable payment charged for a specific marketable good or service provided to a willing buyer and for which a direct benefit accrues, in exchange for the payment of such fee, to the person making the payment;

General principles applying to a provincial tax 25

2. (1) A provincial legislature may, in terms of section 228 of the Constitution and subject to the provisions of this Act, enact legislation to impose a provincial tax.
- (2) A provincial tax contemplated in subsection (1) must—
- (a) not materially or unreasonably prejudice—
 - (i) national economic policies; 30
 - (ii) economic activities across provincial boundaries; or
 - (iii) the national mobility of goods, services, capital or labour; and
 - (b) be consistent with the principles enshrined in Chapter 3 of the Constitution for the purposes of promoting co-operative governance between the national, provincial and local spheres of government. 35

Process regulating the introduction of a provincial tax

3. (1) A province which intends to impose a provincial tax which has not been previously determined as a provincial tax in accordance with the provisions of this Act must, at least ten months before the start of the next financial year, or such later date agreed with the Minister, submit particulars of the proposed provincial tax to the Minister. 40
- (2) The submission contemplated in subsection (1) must—
- (a) be made by the MEC for Finance;
 - (b) set out the reason for the imposition of the proposed provincial tax;
 - (c) identify and, where appropriate, describe for the proposed provincial tax— 45
 - (i) the tax base;
 - (ii) the desired tax rate;

- (iii) the person or body liable for the tax; and
 - (iv) any tax relief measures or exemptions;
 - (d) specify with regard to the administration of the proposed provincial tax—
 - (i) the tax collecting authority;
 - (ii) the person or body responsible for remitting the tax; 5
 - (iii) the methods and costs of enforcing compliance with that tax;
 - (iv) the compliance burden on taxpayers; and
 - (v) procedures for taxpayer assistance;
 - (e) describe the estimation methods and assumptions used to determine—
 - (i) the amount of revenue to be collected on a quarterly basis over three 10
fiscal years following the introduction of the tax;
 - (ii) the economic impact on individuals and businesses residing in the
province;
 - (iii) the economic impact on individuals and businesses residing outside the
province; and 15
 - (iv) the impact on economic development in the province;
 - (f) indicate consultations, including with other provinces, to establish the general
acceptability of the proposed provincial tax; and
 - (g) include such other particulars concerning the proposed tax as may be
prescribed. 20
- (3) If a submission contemplated in subsection (1) complies with subsection (2), the
Minister must, at the next meeting of the Budget Council—
- (a) table it so that it is dealt with in accordance with section 3 of the
Intergovernmental Fiscal Relations Act, 1997 (Act No 97 of 1997); and
 - (b) refer it to the Commission. 25
- (4) Any comments by the Commission and the provinces on the submission tabled in
the Budget Council in terms of subsection (3), must be provided to the Minister within
60 days of the date of that Budget Council meeting or such other date agreed upon by a
province with the Minister.
- (5) The Minister may consult any other interested persons or bodies on the submission 30
contemplated in subsection (2).
- (6) The Minister must indicate to the Budget Council the status of the evaluation of
the submission tabled in terms of subsection (3) at such time as may be appropriate, but
in advance of the fiscal year referred to in subsection (1).
- (7) The Minister must, after considering the comments of the Commission and after 35
consulting the Budget Council and other interested bodies or persons in accordance with
subsections (3) and (5), when the annual budget is introduced in the National Assembly,
also introduce regulatory national legislation which—
- (a) provides that the tax contained in the submission, together with such changes
effected as a result of the consultations contemplated in subsections (3) and 40
(5), may be imposed as a provincial tax; and
 - (b) must prescribe the manner and form which such provincial tax must take,
including—
 - (i) the tax base on which such provincial tax may be levied;
 - (ii) the rate band within which a province may impose such provincial tax; 45
 - (iii) the collecting agent for such provincial tax, if it is not the South African
Revenue Service; and
 - (iv) such other matters as may be prescribed.

Collection of provincial taxes

4. (1) The South African Revenue Service is the collecting agent for a provincial tax, 50
unless, in terms of the national legislation contemplated in section 3(7), another person
or body has been designated as such agent.
- (2) Despite subsection (1), a province may not impose a provincial tax unless it has
concluded an agreement with the South African Revenue Service or such other agent
designated to collect a provincial tax. 55

Transitional provisions

5. (1) Any tax, levy, duty or surcharge which was determined in terms of national or
provincial legislation and imposed by a province prior to 1 April 2002, and which in

terms of section 228(2)(b) of the Constitution should have been regulated in terms of this Act, is deemed to have been imposed in accordance with this Act.

(2) Despite subsection (1), any amendment of an Act of Parliament or a provincial legislature relating to such tax, levy, duty or surcharge contemplated in subsection (1) may be introduced only after the Minister has been consulted on the contents of such draft amendment. 5

(3) The Minister may, by notice in the *Gazette*, determine that the amendment contemplated in subsection (2) be subject to the provisions of this Act.

Amendments to this Act

6. Draft legislation directly or indirectly amending this Act, or providing for the enactment of subordinate legislation that may conflict with this Act, may be introduced in Parliament— 10

(a) by the Minister only; or

(b) only after the Minister has been consulted on the contents of the draft legislation. 15

Regulations

7. (1) The Minister may, by notice in the *Gazette*, make regulations regarding—

(a) anything which must or may be prescribed in terms of this Act; and

(b) any matter which is necessary to prescribe for the effective implementation of the provisions and objects of this Act. 20

(2) Without derogating from the generality of subsection (1), the Minister may make regulations establishing procedures, consistent with the principles of co-operative governance, for determining whether proposed provincial revenue is a tax or user-charge.

Short title and commencement 25

8. This Act is called the Provincial Tax Regulation Act, 2001, and takes effect on a date determined by the President by proclamation.

MEMORANDUM ON THE OBJECTS OF THE PROVINCIAL TAX REGULATION BILL

1. Section 228(1) of the Constitution of the Republic of South Africa, 1996 (Act No. 108 of 1996) (“the Constitution”) empowers provinces to impose certain taxes, levies and duties, but excluding an income tax, a value-added tax, general sales tax, and rates on property or customs duties. Provinces also have the power to impose a flat-rate surcharge on the tax bases of certain taxes, levies and duties, but not on corporate income tax, value-added tax, rates on property or customs duties. The power to impose any of these taxes is, however, subject to regulation by national legislation.

2. Section 228(2) of the Constitution assigns a co-ordinating and monitoring role to the national government with respect to provincial taxes. Section 228(2)(b) of the Constitution requires that an Act of Parliament regulate the process whereby provincial governments may implement tax powers granted to them by section 228 of the Constitution.

3. The Bill gives effect to the constitutional requirements of section 228 by defining the manner in which the national government, through the Minister of Finance, will exercise its policy oversight role and it establishes the process whereby provinces may exercise their taxation authority.

4. The Bill regulates the exercise by provinces of their power to impose taxes, levies and duties and flat-rate surcharges on the bases of taxes, levies and duties imposed by national legislation, by providing for the compliance by a proposed provincial tax, with the Constitution and the provisions of this Bill and to ensure that provincial proposals are dealt with in accordance with section 3 of the Intergovernmental Fiscal Relations Act, 1997 (Act No 97 of 1997).

5. The Bill does not set specific taxes that provinces may enact. Responsibility for initiating a provincial tax proposal rests with provinces and they may propose any tax not prohibited by the Constitution. Rather, the Bill regulates the process by which provincial taxes are imposed. It does not cover existing provincial taxes authorised under national legislation or provincial legislation prior to the date of the Act.

6. It also requires that the provincial legislature in the exercise of its power to impose taxes, levies, duties and surcharges, may not prejudice national economic policies, economic activities across provincial boundaries, or the national mobility of goods, services, capital or labour. The Bill also requires that provincial taxes do not impair coherence in the national tax system across all three spheres of government. It also provides for the enactment of national legislation which prescribes the manner and form which a proposed provincial tax must take.

APPROACH OF THE BILL

7. *Regulating introduction of a provincial tax.* A province intending to impose a new provincial tax will submit a proposal to the Minister of Finance.

8. *Calendar for submission.* A provincial tax proposal must be submitted to the Minister of Finance 10 months in advance of the start of the budget year, allowing for the possibility to include a new tax in the province’s budget for the next financial year.

9. *Submission package for provincial tax proposals.* When a province proposes a new provincial tax, its submission to the Minister of Finance must include a detailed analysis, including the following:

- (a) Reasons and motivation for the proposed tax
- (b) Identification of key aspects of the tax
 - Tax base or the economic activity or income to be subject to the tax.
 - Proposed tax rate expressed as a percentage rate applied to the value of the good or activity or as a fixed rate per unit of sale or consumption.
 - The person or body legally responsible for paying the tax.
 - Tax relief measures or exemptions to protect certain taxpayers or activities which otherwise would be included in the tax base.
- (c) Administration
 - Tax collection authority, including whether SARS or another agent would be the collecting agency.
 - Person or body responsible for actually remitting the tax and the timing of payments.
 - Methods and costs of administration and compliance enforcement.

- Description of the ease or difficulty for taxpayers to comply with the tax.
 - Procedures to assist taxpayers who request information or clarification and procedures for resolving taxpayer complaints.
- (d) Estimates of revenue and economic impact.
- Revenue analysis, including estimates of total revenue to be collected on a quarterly basis over three fiscal years.
 - Economic analysis of the impact on individuals and businesses in the province.
 - Economic analysis of the extent the tax will be paid by non-residents of the province.
 - Economic analysis of impact on the province's economic development.
- (e) Consultation with interested parties.

10. *Preliminary review by the Minister.* Provincial submissions to proposed taxes must comply with section 228(1) of the Constitution and must meet the procedural requirements of the Bill. The Minister will table such submissions at the next meeting of the Budget Council and refer them to the FFC for its recommendations.

11. *Calendar for comments.* Any recommendations made by provinces or the FFC must be available to the Minister of Finance within 60 days.

12. *Schedule for reporting by the Minister.* The Minister will report the status of provincial tax proposals to the Budget Council and provinces to ensure all parties are informed and so provinces can estimate impacts on their budgets for the next year.

13. *Schedule for introduction of national legislation.* If a proposal is consistent with section 228 of the Constitution, national economic policy, and the Bill, the Minister must introduce in Parliament national legislation at the time the Annual Budget of the national government is presented.

14. *Content of national legislation.* The national legislation will enable the province making the original request, as well as any other province, then or in the future, to enact the tax. It will prescribe the "manner and form" in which the tax can be implemented, including the tax base, rate band, and any other terms required. This legislation will serve as a template for provincial legislation to ensure the tax is implemented consistently, thereby maintaining coherence of the general tax system.

15. *Regulatory procedures.* The Bill defines additional regulations the Minister of Finance may issue by notice in the Gazette, as necessary for effective implementation.

BRIEF SUMMARY OF THE BILL

16. The following is a brief summary of the Bill:

- Section 1: definitions of words or expressions used in the bill.
- Section 2: restates section 228(2) of the Constitution, noting that a provincial tax must not materially or unreasonably prejudice national economic policies, economic activities across provincial boundaries or the national mobility of goods, services, capital or labour. It also requires provincial taxes to be consistent with co-operative governance as outlined in Chapter 3 of the Constitution.
- Section 3: regulates the process for the introduction of provincial taxes. It requires provinces to submit new tax proposals to the Minister of Finance at least ten months before the start of the financial year. The Minister must provide the submission to the Budget Council and the FFC for comment, which must be given to the Minister within 60 days. Section 3 also requires that if the tax proposal complies with section 2 of the Bill, the Minister must introduce national legislation for the tax. The national legislation must prescribe the manner and form of the provincial tax, including tax base, rate band and collecting agent.
- Section 4: states that the South African Revenue Services (SARS) is the collecting agent for a provincial tax, unless another agent is designated for this purpose in the national legislation contemplated in section 3.
- Section 5: clarifies that current provincial taxes are exempt from the Bill, and are deemed to have been imposed in terms of the Bill.
- Section 6: addresses amendments to the Act, once enacted, stating they can only be introduced in Parliament by the Minister of Finance or after consultation with the Minister.

Section 7: empowers the Minister of Finance to gazette regulations for implementation of the Act and to establish procedures to distinguish between user charges and taxes.

Section 8: provides for the date on which the Act takes effect.

17. *Parliamentary Procedure.* The National Treasury and State Law Advisers are of the opinion that the Bill must be dealt with in accordance with the procedure set out in section 76(1) of the Constitution as it provides for legislation required in Chapter 13 of the Constitution, and affects the financial interests of the provincial sphere as contemplated in section 76(4)(b) of the Constitution.

Guidelines for Provincial Tax Regulation Bill, 2001

The purpose of the Provincial Tax Regulation Bill is to define the process whereby provincial governments may implement the tax powers granted to them by section 228 of the Constitution. Under section 228(2)(b), an Act of Parliament is required to regulate these powers.

The purpose of these guidelines is to explain the provisions of the Provincial Tax Regulation Bill. The guidelines are intended to help the national and provincial governments implement their constitutional authority under section 228, and to explain the policy intent of the Constitution with regard to the intergovernmental assignment of revenue responsibility.

These guidelines to the Provincial Tax Regulation Bill are organised as follows:

- Part 1 summarises the provisions of section 228 of the Constitution, and the responsibilities for provincial taxes that the Constitution assigns to the provincial and national levels of government.
- Parts 2 — 5 provide more detailed explanations of the provisions of the Bill:
 - Part 2 provides an overview of the intent of the Bill and describes the process that provinces must follow in proposing new provincial taxes.
 - Part 3 discusses tax administration and collections issues.
 - Part 4 explains the provisions for future regulations, including procedures for distinguishing between user charges and taxes.
 - Part 5 defines the relationship of this Bill to existing provincial taxes.

Constitutional authority for provincial taxes

Public finance theory on allocation of tax authority

The Constitution authorises certain taxing powers for the provinces, but places limits on these powers according to specific local conditions as well as standard public finance theory.

The theory of public finance defines certain principles that guide the allocation of appropriate tax authority to the national and local levels of government, with some flexibility for middle levels of government. Taxes on international trade clearly belong at the national level. Taxes on any base that can move easily between subnational jurisdictions, and taxes that can be designed to further national macroeconomic or redistribution goals, should be assigned to that level of government. Thus, the taxes generally reserved for the national level are customs duties and tariffs, corporate and personal income taxes and VAT. At the local level, the most appropriate tax is the property tax, as property is an immobile tax base that cannot be easily moved from one jurisdiction to another, thereby reducing the potential for tax avoidance.

No taxing jurisdiction, local or national, has the right to tax property, income or goods of another jurisdiction. Where taxable activities or income cross jurisdictional lines, the allocation of tax authority may be determined by source-based or destination-based tax rules, or the tax base may be shared by a formula designed to avoid imposing “double-taxation”.

Limits on provincial taxes under section 228

The Constitution complies with standard public finance theory in granting limited tax authority to provincial governments, and barring the use of tax instruments best allocated to other levels of government.

Section 228(1)(a) authorises provinces to impose taxes, levies and duties *other than* an income tax, a value added tax, general sales tax, rates on property or customs duties.

Section 228(1)(b) authorises provinces to impose a flat-rate surcharge *on the tax bases* of any tax levy or duty imposed by national legislation *other than* the tax bases of corporate income tax, value added tax, rates on property or customs duties.

The requirement that any surcharge be *on the tax base* of a national tax has been interpreted to mean that a province cannot impose a surcharge as a percentage of the national tax liability due (i.e. a surtax). Rather, the province must design its surcharge as a tax on the underlying income or activity that occurs within its borders. Thus, a province cannot automatically “piggyback” on a national tax.

Responsibilities of the national government

Although it gives some tax authority to the provincial level, the Constitution also complies with standard public finance theory by defining the priority of national economic interests, and the oversight role of the national government.

The country’s reintegration into the world economy and the need for prudent public debt management have made stability and fiscal discipline economic policy priorities. A problem in one part of the intergovernmental system is viewed by international markets as symptomatic of the system in general. In terms of fiscal policy, this has led to caution with regard to tax and borrowing powers at the provincial level. Government policy has first concentrated on expenditure assignment and improved administration to promote more accountable, effective and efficient use of funds.

Another objective of national economic policy is to maintain and strengthen the country’s competitive position in the world economy. One measure of competitiveness is the ratio of total taxes on individuals and businesses relative to total income (measured by gross domestic product, or GDP). Government has sought to reduce the tax:GDP ratio in line with the ratio of other countries. Increases in autonomous taxing powers at the provincial or local levels must be evaluated carefully, since a counterbalancing reduction in national government taxes might be required to comply with this national policy goal.

Another primary goal of national economic policy is to address imbalances of the past, and to promote redistribution and equity. This goal also argues for caution in assigning taxing powers to separate geographic locations until the country’s uneven economic development and basic infrastructure has been more equalised. The current formula for equitable share distributions to provinces takes these development factors into account. An increase in provincial tax authority would increase a province’s own-source revenues with which to address its development needs, and would require a re-evaluation of equitable share distributions.

For all of these reasons, the Constitution has further limited the authority it grants to the provinces by allocating a strong coordinating and monitoring role to the national government with respect to provincial taxes.

Section 228(2) requires that the power of a provincial legislature to impose taxes, levies, duties and surcharge:

- (a) may not be exercised in a way that materially and unreasonably prejudices national economic policies, economic activities across provincial boundaries, or the national mobility of goods, services, capital or labour
- (b) must be regulated in terms of an Act of Parliament, which may be enacted only after any recommendations of the Financial and Fiscal Commission have been considered.

The national government is responsible for maintaining coherence of the national tax system across the three spheres of government, as this is part of its responsibility to ensure the integrity of national economic policy. Fulfilling this responsibility requires adequate regulation of taxing powers exercised by the provincial and local spheres of government. In defining the ambit within which the word “regulate” should be interpreted, the Constitutional Court has suggested that “regulate” is normally associated with “control”, suggesting the power to “direct and command” that which must be regulated.

This Provincial Taxation Regulation Bill meets the constitutional requirements by defining the manner in which the national government, through the Minister of Finance, will exercise its policy oversight role, and the process whereby provinces may implement the constitutional authority granted to them.

New provincial taxes

Objectives of introducing the Provincial Tax Regulation Bill

The Provincial Tax Regulation Bill does not define the new taxes that provinces may enact. Responsibility for initiating a provincial tax proposal rests with the provinces.

Rather, the Bill regulates the process by which provincial taxes may be imposed, as required by section 228(2)(b). Over time, this regulatory process will result in an evolving list of provincial taxes.

Under the provisions of this Bill, a province may propose any tax not strictly prohibited by the Constitution. A National Treasury analysis outlined some of these tax options might be and which tax options are most compatible with standard public finance theory. This analysis also took into account the FFC and Katz Commission reviews of these issues. A province may propose any of these options, or any other tax option that it believes to be in accordance with section 228(1).

Options compatible with section 228(1)(a): taxes, levies, duties

Several taxes meet the criteria set out in the Constitution, including selective sales or excise taxes on specific services or goods and use and permission taxes.

Examples of a selective sales tax on services include a bed tax or a tax on other tourism services. Examples of selective sales taxes on specific goods are “sin taxes” on tobacco and alcoholic beverages, or “luxury taxes” on high-value consumer goods. Public finance theory and experience suggest caution in the use of selective taxes on goods at the provincial level, because the tax base is highly mobile and serious tax evasion problems exist at lower-than-national levels of government.

Other possible provincial taxes are environmental taxes; presumptive business taxes on small business activity that may not be captured by national income taxes; betterment taxes collected from a specific group of taxpayers for a specific infrastructure improvement project from which they will benefit; and taxes as a consideration on the right to extract mineral or petroleum products. Some of these taxes, like betterment taxes, may be more appropriate at the local level than the provincial level.

For many provinces, the tax options under section 228(1)(a) have limited applicability and are not likely to produce significant revenues.

Options compatible with section 228(1)(b): surcharges

The National Treasury analysis of provincial taxes reviews the surcharges on national taxes that a province might propose under section 228(1)(b). It focuses on the principal surcharge options — personal income tax and the fuel levy — compatible with the requirements of section 228(1)(b), which specifically excludes corporate income tax, VAT, property rates or customs duties from consideration.

With regard to a personal income tax surcharge, the National Treasury analysis raises a number of policy concerns. For instance, the narrowness of the personal income tax base would lessen its attractiveness as a provincial-level tax, where taxes with a wider revenue base that reflect a large cross-section of the population are more desirable. It is also questionable whether such a surcharge would not hinder Government’s equity and redistribution goals as well as foreclose or complicate other tax reform efforts.

The analysis also pointed out problems associated with administering a surcharge on the personal income tax, concerns that were highlighted by the Katz Commission. Section 228(1)(b) specifies that any provincial surcharge must be levied at a flat rate *on the base* of a national tax. In other words, the surcharge must be levied as a percentage of taxable income or activity within the province, not as an additional rate on each taxpayer’s national tax liability. The complexity of this requirement, given that a rebate system is used in South Africa, means that personal income tax surcharge will not be easy to implement. For instance, a provincial surcharge, which must be imposed at a flat rate for all income classes, may require provisions for low-income protection (exemptions, tax thresholds, credits, etc.) to ensure it does not fall unreasonably on the poor.

In addition, under the PAYE system, the residence of taxpayers is not required information. A major problem is lack of data on a taxpayer’s province of residence, which is required to properly attribute income for provincial tax purposes. The Katz Commission also warned that other developing countries have encountered significant difficulties in attempting to apply regional or local surcharges on national income taxes, due to the burden on tax administration.

With regard to a fuel levy surcharge, the National Treasury analysis supports the Katz Commission’s finding that the administrative problems are less burdensome than for the personal income tax. However, administering a provincial fuel surcharge would add to the complexity of the current system and require significant cooperation by the oil industry.

The analysis also notes that provincial surcharges on fuel could have a significant impact on the national economy, given the key function of fuel as a factor in production and its importance for many different economic sectors.

Overall, the analysis supports the conclusion of the Katz Commission in advising against a surcharge on the personal income tax at this time. The Budget Council has also endorsed this position. The surcharge on the fuel levy has more potential as a viable option in future, but issues about consistency with national economic policy and administrative capacity would need to be addressed.

Provincial fees and taxes not covered by the Bill

The regulatory process included in this Bill covers neither provincial user charges nor existing provincial taxes authorised under other legislation, as discussed in the sections below.

User charges and fees

Section 228 of the Constitution refers to provincial revenues raised in a manner consistent with the standard public finance definitions of taxes, levies and duties. The provisions of the Constitution, and therefore the provisions of the Provincial Taxation Regulation Bill, do not apply to provincial user charges and fees to the extent they comply with the standard public finance definition of user charges.

The standard criteria defining user charges and fees are that they be characterised by excludability (i.e. only the payer receives the specific product or service), voluntary incidence (i.e. those who do not wish the good or service do not pay), and a reasonable compatibility between payment and benefit receipt in both value and timing.

If a provincially mandated payment is called a "fee" or "charge" but its application does not meet the criteria defined above, including a reasonable test of true intent, it will be subject to the provisions of section 228 and the Provincial Tax Regulation Bill.

Section 7.2 of the Bill envisages procedures for the review of provincial user charges, if necessary. Criteria for distinguishing between user charges and taxes are discussed in more detail in part 4 of these guidelines.

Existing taxes

The provisions of this Bill do not apply to provincial taxes and levies authorised under national legislation prior to the date of this Act. These include taxes imposed in terms of the Road Traffic Act of 1996, the National Gambling Act of 1996, or the provisions regarding liquor licence fees in Schedule A, Part 5 of the Constitution.

Regulating the introduction of a provincial tax

Overview

The Provincial Tax Regulation Bill defines the procedures by which the power of provinces to impose taxes is regulated, as required by section 228(2)(b) of the Constitution. Under these procedures, a province has control over both the initiation of a provincial tax proposal in accordance with the powers granted to it under section 228(1), and its ultimate enactment by the provincial legislature.

The national government has responsibility for reviewing the provincial proposal and determining whether it conforms with section 228(2)(a), i.e. that it will not prejudice:

- national economic policy
- economic activities across provincial boundaries
- the mobility of goods, services, capital and labour.

By the provisions of the Bill, any province wishing to impose a new provincial tax must make a submission to the Minister of Finance. The Minister will review the request for compliance with section 228 and with national economic policy, and hear recommendations from fiscal and policy staff, tax administration authorities and other interested parties.

If the Minister concludes a proposal is consistent with section 228, he must introduce separate national legislation to provide for provincial implementation of the tax proposal. The national legislation will enable the province making the original request, as well as any other province, at that time or in the future, to enact the tax. It will prescribe the “manner and form” in which the tax can be implemented, including the tax base, rate band, and any other terms required.

This national legislation will, in essence, be a template for provincial legislation to ensure the tax is implemented in a uniform and consistent manner across the provinces, thereby maintaining coherence of the general tax system. Allowable provincial differences, such as in rate or exemptions will be explicitly identified in the national legislation. The tax will become effective in a particular province only when imposed by provincial legislation, according to the terms prescribed by the national authorising legislation. This is in line with the Constitutional requirement that a province must have legislation for its own taxes and other revenues since these are money bills.

Each provincial tax that goes through the review process and that the Minister concludes meets constitutional requirements, will be provided for in national legislation. Over time, this national legislation will come to constitute a list of taxes that any province may impose. This body of provincial tax law (the so-called “allowed list”) may be reviewed and renewed annually by the Minister of Finance, at the time of the national budget, similar to the laws amending taxes at the national level.

The following sections explain the details of the submission process.

Calendar for submission of provincial tax proposals

A provincial tax proposal must be submitted to the Minister of Finance 10 months in advance of the start of the budget year. The intent of this schedule is to allow for the possibility of including a new tax in the province’s budget for the next financial year.

It should be noted, however, that approval — if granted — may not always coincide with the beginning of a fiscal year. The timing will ultimately depend on the details of each proposal, and the time needed for review and analysis. Other factors which may extend the review period could include the Minister’s need for further information or clarifications from the province, or national-provincial discussions on possible revisions, or alterations to the original submission recommended by the Budget Council, the FFC, the National Treasury, or SARS.

Submission package for provincial tax proposals

When a province is proposing a new provincial tax, it will be required to prepare a submission containing a detailed qualitative and quantitative analysis of various aspects of the tax. The analysis should be sufficiently detailed to enable a thorough assessment of the consistency of the tax with the Constitution and the imperatives of integrated tax policy. The Provincial Taxation Regulation Bill specifies several requirements regarding the contents of the provincial submission package.

The intent of these requirements is to facilitate the national review of provincial tax proposals required by section 228(2). The submission requirements will assist National Treasury officials, as well as the Budget Council and the FFC and other interested parties, in their review of the proposal. The submission requirements should also assist the province in fully analysing the impact of the tax proposal on both revenue and economic development. Overall, these requirements support transparency and cooperative governance, as envisaged in Chapter 3 of the Constitution.

For the reasons specified above, a provincial tax proposal submission to the Minister of Finance for review must include the following:

Reasons and motivation for the proposed tax

The first item in the submission package will include a brief description of the tax proposal, and the reasons and motivation for its implementation. This would include the constitutional authority, and a brief rationale for the tax, whether for revenue or other reasons (e.g. regulatory, use or permission taxes).

Identification of key aspects of the tax

The second section of the submission package will include the identification of the key aspects of the tax. The requirements here are intended to clarify the important statutory details of the tax proposal. These are as follows:

Tax base

What is the economic activity or income intended to be subject to the tax? For example, for a bed levy, the tax base may be defined as the rental of a bed in a hotel or other lodging. Any qualifications that define the terms (such as the duration of stay) and other factors (such as the threshold rental price) should be included in the definition of the tax base. The broader the tax base, i.e. the larger the number of taxpayers included in the base, the lower will be the tax burden on any one taxpayer and the greater will be the tax revenue (for a given tax rate). A tax with a very narrow tax base may not be worth the effort; the revenue potential of such a tax is likely to be limited. Moreover a tax with a narrow base would, more than likely, require a high rate that could result in increased efforts of tax avoidance and even tax evasion.

Proposed tax rate

Is the tax rate *ad valorem* (i.e. expressed as a percentage rate applied to the value of the good or activity) or is the rate specific (i.e. a fixed rate per unit of sale or consumption)? Is there a single rate or is there a schedular rate structure with different rates for different categories within the base (e.g. different classes of hotels)? A simple design of the rate structure generally makes the task of both the tax administrator and the taxpayer easier.

The person or body liable for the tax

The statutory taxpayer is the person or entity legally responsible to pay the tax. The statutory taxpayer of a business income tax is the business, even though the business may simply “pass along” the cost of the tax in higher prices to its customers. The statutory taxpayer of a sales tax is the consumer, who pays an extra amount at the time of purchase, even though the store remits the tax payment to the tax authorities on behalf of the consumer.

Tax relief measures or exemptions

Relief measures and exemptions are special provisions designed to protect certain taxpayers or activities which otherwise would be included in the tax base. Any such measures should be explained and justified.

Administration

The third section should contain a description of how the proposed tax will be administered, to enable assessment of administrative feasibility of the proposal. This section of the submission should define the following:

Tax collection authority

Section 4 of the Provincial Taxation Regulation Bill stipulates that SARS is the default collection authority, though in some instances a province may designate another person or body. In its submission, the province should indicate whether it is requesting SARS to be the collection agency or designating another collection agent. The submission must indicate the extent to which the province has consulted the prospective collection agency regarding the administrative feasibility of the tax in the format proposed.

Provinces are required to enter into an agreement with SARS before they can impose a tax. This would take place after a tax is approved in national legislation, as the detail the legislation would have a bearing on the formulation of such an agreement.

Person or body responsible for remitting the tax

The province should define who will remit the tax, and the timing of payments. For example, for a bed levy, the hotel or lodging establishment would remit the tax. This person or body need not be the statutory taxpayer.

Methods and costs of enforcing compliance

The province should summarise its procedures for ensuring that a tax, once enacted, can be enforced. It should also indicate that it has considered the costs of enforcing compliance of the proposed tax in its revenue estimates. A tax with an unduly high enforcement cost is not worth implementing.

Estimates would be required of the administrative costs associated with the tax, irrespective of whether the tax is administered and collected by SARS. This is essential to minimise collection and enforcement costs associated with the tax (which increase with tax complexity).

Compliance burden

This section should provide an evaluation of the ease or difficulty with which a taxpayer can comply with the tax, e.g. how much time or effort taxpayers will be required to spend following tax payment procedures (filling out forms, waiting in queues, obtaining receipts, etc). This part of the submission would also outline measures that will be taken to reduce compliance costs of the tax, e.g. allowing for electronic filing of tax returns, providing taxpayer advice and assistance. As a general rule, taxes that citizens may view as more of a “nuisance” than is merited by the value of the services they will finance should be avoided.

Procedures for taxpayer assistance

Taxes are payments by citizens to their government in return for services. In this sense, the taxpayer is the “client” who must be satisfied. The province should explain what procedures it will use to satisfy taxpayer requests for information or clarifications regarding the proposed tax, as well as procedures for resolving taxpayer complaints.

Estimates of revenue and economic impact

The fourth section of the submission package should contain estimates of revenue and the economic impact, and the methods used to arrive at these estimates, even if the data and methods are rudimentary. The requirements in this section are intended to facilitate evaluation of the economic and fiscal impact of the proposed tax. This section should include the following:

Revenue analysis

The province should provide estimates of the amount of revenue to be collected on a quarterly basis over three fiscal years, and the methods used to make these estimates. A key issue is whether the tax option will generate stable and predictable revenues for the province.

Economic impact analysis — residents

The province should define the impact of the tax on individuals and businesses residing in the province. For example, for a bed levy, the tax burden on residents of the province would be expected to be minimal. Whereas in the case of a surcharge on the fuel levy, the residents and businesses of the province are expected to bear most of the tax burden.

Economic impact analysis — non-residents

The province should estimate the extent to which the proposed tax will be “exported”, i.e. paid by non-residents of the province. This information will be important to the province and Minister of Finance in ensuring the tax proposal complies with section 228(2)(a), namely that the tax “may not ... materially and unreasonably prejudice ... economic activities across provincial boundaries”.

Economic development impact

The province should indicate its evaluation of the overall impact of the tax proposal on its economy. Taxes can affect many facets of economic activity, including savings, investment and labour supply. This section should consider the impact the tax could have on economic activity within the province imposing the tax, on neighbouring provinces, and on national economic activity. In this analysis, provinces would also take account of the public services they provide.

Consultation with interested parties

The fifth section of the submission package should indicate whether the province has informed and discussed its proposal with interested parties or, if appropriate, has held public hearings. Interested parties might include other provinces or affected private-sector representatives. This information is important for the province and Minister of Finance to ensure there has been opportunity for input from affected taxpayers and other jurisdictions. The proposal should also contain a synopsis of any comments received from the parties consulted.

In general, it is envisaged that provinces will consult early in the process with other provinces and the National Treasury. Such consultations can occur in the context of the Budget Council. Consultation should occur at the formative stages of developing provincial tax proposals to ensure proper coordination and to avoid duplication of effort if more than one province is investigating a particular proposal.

Other considerations

The sixth and last section of the submission package should include any specific considerations unique to the tax being proposed, and any additional information determined by the Minister of Finance to be necessary for national review of the proposal.

Preliminary review by the Minister

In addition to defining the responsibilities of provinces, the Provincial Tax Regulation Bill also defines the responsibilities of the national government.

The intent of the Bill (section 3, subsections 3-7) is to define the process whereby the national government will perform the oversight and review function required by the Constitution.

When a province submits its tax proposal to the Minister of Finance, it will first be screened to ensure it does not violate the restrictions of section 228(1) and meets the procedural requirements described above, including that the submission package is complete. Necessary changes or additions, emerging through discussions with the province, may take place at this stage. Once the proposal has passed this initial screening, the Regulation Bill requires that the Minister:

- table the submission at the next meeting of the Budget Council and
- refer the submission to the FFC for its recommendations.

The purpose of this requirement is to allow consideration of the impact of the proposal on national economic policy and interprovincial economic activity, transparency of the decision-making process, and an opportunity for comments from other provincial governments and the FFC.

Calendar for comments

Any recommendations made by provinces or the FFC must be available to the Minister of Finance within 60 days, unless the Minister agrees to a later date.

The intent of this schedule is to ensure the review process is not unduly extended, and that a decision on the provincial proposal is made in a timely fashion.

Consultation with other parties

The Minister is authorised by the Bill to consult with any other interested bodies or persons for their views on the provincial tax proposal, to ensure democratic participation in decision-making.

Schedule for reporting by the Minister

The Bill mandates that the Minister of Finance indicate the status of the provincial tax proposal review to the Budget Council prior to the start of the next fiscal year. This schedule is intended to ensure that all parties are informed of the status of the Minister's review, including any requests for additional information and/or discussions on revisions to a province's original submission.

Under the current budget process, the Minister indicates to the provinces in the *Medium Term Budget Policy Statement* (MTBPS) the anticipated equitable share for the next financial year. The MTBPS has also presented, although in somewhat less detail, the anticipated conditional grants. The timing of the MTBPS in late October or early November is intended to allow the provinces sufficient time to make budget decisions and prepare budget documentation. Consistent with this process, it is envisaged that the Minister would inform provinces of the status of a tax proposal so they are able to plan for the impact of the proposal on their budgets for the next financial year.

Schedule for introduction of national legislation

Once the Minister has decided a proposed provincial tax, including any revisions, is in compliance with the provisions of section 228 of the Constitution and the procedures of the Provincial Tax Regulation Bill, the Minister must seek Cabinet approval and, if granted, introduce national legislation allowing for the provincial tax. The legislation must be introduced in the National Assembly at the time that the Annual Budget of the national government for the next fiscal year is presented.

The national legislation will permit the province that submitted the proposal, as well as any other province, to enact the tax. The tax does not become valid in a province until it has been enacted by that province's legislature.

As noted previously, the Minister is not required by the Bill to complete his review of a provincial tax proposal by a certain date or within a specified time period. Although provinces must make their submissions at least 10 months before the start of the next financial year, to be considered for that year, it may not be possible for the Minister to finish his review by that time. Ten months is the minimum time needed for such a review and for drafting the authorising legislation, however a more complex may not be sufficient time for a complicated tax proposal may require a longer period for review.

Content of national legislation

The national legislation will prescribe a provincial tax for enactment by any province. For reasons of administrative simplicity and economic efficiency, the national legislation will define the form, manner and content of the particular tax that has been approved. Specifically, the national legislation will define a uniform tax base to be used by any province enacting the tax, and a rate band from which a province may decide its tax rate. Other matters may also be included in the national legislation to avoid a proliferation of differences in the way in which different provinces implement the tax. Any province wishing to impose the tax would copy the relevant portions of the national law into its own legislation.

The intent of this provision is to ensure South Africa avoids a proliferation of different versions of a tax across provinces. Different versions of a tax could have a negative impact on the economy as a whole, and would be administratively difficult and costly.

Collection of provincial taxes

Effective tax administration is central to a coherent and internationally competitive national tax policy. Any divergence between the tax policy as advanced in legislation and the manner in which it is administered can compromise the efficiency and integrity of national tax policy. It is in this context that the Provincial Taxation Regulation Bill contains stringent requirements regarding the administration of provincial tax legislation.

Section 4 of the Provincial Tax Regulation Bill establishes that the South African Revenue Service (SARS) be the collecting agent for a provincial tax approved under this process, unless the Minister designates another person or body for that purpose. The Minister will only designate another agency to be the collecting agent when the province submitting the tax proposal proves that such other agency will be able to collect the tax more efficiently and cost-effectively than SARS.

In terms of the Bill, a province must conclude an agreement for the administration and collection of a tax with SARS or other agent before implementing the tax. The administrative implications of taxes include the information systems requirements, the personnel requirements, and the related collection costs associated with these proposals.

The agreements between the province and SARS (or the alternatively designated collecting agent) should provide for, inter alia, the following:

- The resources required to administer the tax, e.g. IT resources and staff.
- The procedure for paying the tax to the collecting authority and the transfer of tax revenues to the provincial treasury.
- The manner in which the province will pay the collecting authority for its tax collection costs.
- The management information system and data-sharing arrangements with the National Treasury to account fully on an annual basis for all taxes collected at the provincial sphere of government. It remains the National Treasury's prerogative to determine the format in which provincial tax revenue data is reported to enable the National Treasury to report on provincial tax powers periodically, consistently and in a transparent manner.
- Any other matter required for the effective collection of the revenue.

Regulatory procedures

The Provincial Tax Regulation Bill, in section 7, defines additional regulations that the Minister of Finance may issue by notice in the *Gazette*.

Supporting regulations for the Bill

The Minister of Finance may issue regulations regarding any matter in the Bill, or any matter necessary for its effective implementation.

Procedures to distinguish taxes from user charges

Section 7(2) of the Bill empowers the Minister to make regulations establishing procedures to determine whether a proposed revenue option is a tax or user charge. This distinction is important, as it determines whether a proposed revenue source must be regulated by the Bill.

Provinces are empowered to impose user fees to recover costs reasonably associated with the provision of services set out in schedules 4 and 5 of the Constitution. Such user fees will not fall within the ambit of the Provincial Taxation Regulation Bill, as they do not constitute taxes. The Constitution prescribes the submission of a Money Bill to Parliament by the Minister of Finance when taxes, levies or duties are imposed. This is not the case with user charges, as such fees do not constitute taxes and are therefore not subject to the direct supervision of the Minister of Finance. However, it is sometimes difficult to distinguish a user fee from a tax or levy. A "user fee" must adhere to the standard criteria defined below. Otherwise, it will be considered to be a tax that must be regulated in terms of the Bill and follow the procedures set out therein.

The procedures to distinguish between user charges and taxes are intended to be consistent with the principles of co-operative governance, with the goal of clarifying issues before disputes arise. This consultation process could prevent legal challenges to provincial user fees.

Criteria to distinguish a tax or levy from a user charge

Standard public finance theory and international best practice provide guidance in distinguishing user fees and charges from taxes and levies. The following definition of a user charge is taken from the 1993 System of National Accounts:

- a marketable service is provided to identifiable beneficiaries;
- direct benefits accrue to beneficiaries in exchange for payments made; and
- transactions take place in a willing buyer market.

In contrast, taxes or levies result in no direct benefit in exchange for payments. Taxes and levies are general obligations which can be identified in terms of the following criteria:

- payments are compulsory and are enforced in terms of legislation;
- no direct benefits accrue to taxpayers in exchange for payments made; and
- benefits are returned to groups of people, not identifiable individuals.

As a guideline, user charges are a sound form of financing (partial or total) when costs can be associated directly with beneficiaries. On economic efficiency and fairness grounds, provinces should seek to utilise user charges to finance service provision in appropriate circumstances. For example, user charges may prove especially suitable for recovering the costs associated with regulatory services, like inspections and permitting.

The imposition of taxes and levies, on the other hand, must be carefully evaluated to ensure they are appropriate for the provincial sphere of government and that the process set out in the Bill has been followed. Taxes should be considered when it is not feasible or not desirable for equity reasons to impose the costs of a service directly on the group that benefits.

Where a levy financing arrangement proves necessary, it may be possible to design the levy" in such a way to maintain some of the economic and equity advantages of user charges. charges" are essentially levies that imitate user charges. The individual elements of the levy arrangement are formulated to approximate the standard criteria for user charges. For example: A levy is a compulsory statutory charge, however but it can incorporate an element of a willing buyer market by empowering the group who bears the burden of the levy to directly influence the levy determination process.

These definitions provide guidance to distinguish user charges from levies or taxes. The key element of a user charge is choice in consuming a public good or service, which confers direct benefits on the individual purchasing it and for which the individual pays appropriate compensation. The term 'appropriate compensation' is critical, as efficient user charges must be set at a level that will at most cover the costs of providing the service. Charges over and above the costs of providing the service received do not reflect the true benefits to the individuals who bear the charge. A charge that includes such additional payments does not meet the definition of a user charge. In other words, if a charge were set at a level that would generate more revenue than required to recover the costs of the service, it would be a tax.

In some instances it is easy to identify a user charge, for example, a fee for entry into national parks and museums. However, in other instances, the distinction between a user charge and a tax becomes blurred. In such cases, the intent of the government imposing the charge will be a key factor.

Provinces may impose user charges without following the process set out in the Provincial Taxation Regulation Bill. However, where the user charge or fee is in fact a tax, as discussed above, it must follow the provisions of the Bill. In situations of doubt, the provincial treasury should consult with National Treasury on whether a proposed charge is a user fee or is a tax that requires approval. This consultation process could prevent legal challenges against legitimate user charges.

Provincial governments are encouraged to utilise user charges in appropriate conditions. The Minister of Finance has the responsibility to regulate provincial taxes in terms of the Constitution and thus must ensure that a provincial tax or levy is not introduced under the guise of a user charge. The sections above are therefore intended to provide guidance to the provinces as to the distinction between a user charge or fee and a levy or tax.

Exclusion of existing provincial taxes

Provinces already have certain taxing powers. The Provincial Taxation Regulation Bill will not apply to these taxes, which include taxes imposed in terms of the Road Traffic Act of 1996, the National Gambling Act of 1996, or the provisions regarding liquor licence fees in Schedule A, Part 5 of the Constitution. In effect, these taxes will be “deemed” to have been implemented in terms of the Bill.

However, it must be recognised that some regulatory limits are required to govern the manner and form of amendments to existing provincial taxes. Amendments may be introduced only after consultation with the Minister of Finance. During this consultation, the Minister may determine a proposed amendment to an existing provincial taxing power is substantial enough to warrant following the procedures set out in the Provincial Taxation Regulation Bill.

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