BUDGET 2004

2004/5

Budget
Tax Proposals

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DIRECT TAX PROPOSALS

Personal income tax

South Africans have benefited from significant personal income tax relief since 1996. This relief has not only countered inflation-related fiscal drag but also provided a real reduction in the tax burden, particularly on low-income earners. These measures increased real disposable income for consumption and saving.

In 2004/05, personal income tax relief of R4 billion is proposed.

The main adjustments are:

- The primary rebate is raised to R5 800, increasing the income tax threshold by 7,4 per cent to R32 222.
- The tax threshold for taxpayers age 65 and over is raised to R50 000, or 6 per cent more than the current level.
- Brackets are adjusted to provide relief across the entire income spectrum.

The distribution of the tax relief is as follows:	
Threshold to R60 000	11%
R60 000 to R150 000	49%
R150 000 to R250 000	30%
R250 000 and above	10%

Personal income tax - bracket and threshold adjustments:

2003/04		2004/05	
Taxable income (R)	**Rates of tax**	**Taxable income (R)**	**Rates of tax**
0 – 70 000	18% of each R1	0 – 74 000	18% of each R1
70 001 – 110 000	R7 200 + 25% of the amount above R70 000	74 001 – 115 000	R13 320 + 25% of above R74 000
110 001 – 140 000	R17 200 + 30% of the amount above R110 000	115 001 – 155 000	R23 570 + 30% of the above R115 000
140 001 – 180 000	R26 200 + 35% of the amount above R140 000	155 001 – 195 000	R35 570 + 35% of the amount above R155 000
180 001 – 255 000	R47 200 + 38% of the amount above R180 000	195 001 – 270 000	R49 570 + 38% of the amount above R195 000
255 001 and above	R73 800 + 40% of the amount above R255 000	270 001 and above	R78 070 + 40% of the amount above R270 000
Rebates		**Rebates**	
Primary	R5 400	Primary	R5 800
Secondary	R3 100	Secondary	R3 200
Tax threshold		**Tax threshold**	
Below age 65	R30 000	Below age 65	R32 222
Age 65 and over	R47 222	Age 65 and over	R50 000

Income tax payable by individuals younger than 65

Taxable income (R)	2003 rates (R)	Proposed rates (R)	Tax reduction (R)
32,500	450	50	400
35,000	900	500	400
40,000	1,800	1,400	400
45,000	2,700	2,300	400
50,000	3,600	3,200	400
55,000	4,500	4,100	400
60,000	5,400	5,000	400
65,000	6,300	5,900	400
70,000	7,200	6,800	400
75,000	8,450	7,770	680
80,000	9,700	9,020	680
85,000	10,950	10,270	680
90,000	12,200	11,520	680
100,000	14,700	14,020	680
120,000	20,200	19,270	930
150,000	29,700	28,270	1,430
180,000	40,200	38,520	1,680
200,000	47,800	45,670	2,130
500,000	166,700	164,270	2,430
800,000	286,700	284,270	2,430
1,000,000	366,700	364,270	2,430

Income tax payable by individuals 65 years of age and older

Taxable income (R)	2003 rates (R)	Proposed rates (R)	Tax reduction (R)
50,000	500	–	500
55,000	1,400	900	500
60,000	2,300	1,800	500
65,000	3,200	2,700	500
70,000	4,100	3,600	500
75,000	5,350	4,570	780
80,000	6,600	5,820	780
85,000	7,850	7,070	780
90,000	9,100	8,320	780
100,000	11,600	10,820	780
120,000	17,100	16,070	1,030
150,000	26,600	25,070	1,530
180,000	37,100	35,320	1,780
200,000	44,700	42,470	2,230
500,000	163,600	161,070	2,530
800,000	283,600	281,070	2,530
1,000,000	363,600	361,070	2,530

Interest and dividend income exemption

The domestic interest and dividend exemption is currently R10 000 for taxpayers under age 65 and R15 000 for taxpayers age 65 and over. This exemption is an important benefit for those who rely on savings for their main source of income. In view of the significant reductions in interest rates, an increase is proposed. As from 1 March 2004, the interest exemption levels will be increased to R11 000 for taxpayers under 65 and to R16 000 for taxpayers age 65 and over. This change will result in an estimated revenue loss of R62 million.

Motor vehicle allowances

The number of taxpayers using the deemed expense schedule for motor vehicle allowances increased significantly over the past few years, resulting in significant revenue losses to the fiscus. A large number of taxpayers rely on the deemed expense schedule primarily as a result of the schedule's inherent overestimation of actual business cost. This overestimation in effect means that many taxpayers are able to deduct amounts that are effectively private expenses.

While recognizing that there are unavoidable compromises in these arrangements, it seems clear that the present provisions are unfair and unduly distort household choices. The deemed expense schedule will accordingly be reviewed, to explore the appropriateness of the deemed private and business kilometres travelled, the assumption that motor vehicles have a zero residual value after five years, the unintended encouragement of investment in higher valued vehicles and the 50 per cent PAYE withholding regime. The *ad valorem* duty structure on motor vehicles will also be reassessed, taking into account the findings of economic and distributional impact studies.

Transfer duty

The South African housing market has seen a notable recovery since 2000. This period coincided with significant personal income tax relief for low- and middle-income earners as well as transfer duty relief for the lower end of the property market. In this Budget, Government continues to grant effective tax relief for low-income earners by not only reducing the personal income tax relief around low- and middle-income groups, but also by adjusting the transfer duty brackets. The exempt threshold for the transfer duty will therefore be increased from the current R140 000 to R150 000 as from 1 March 2004, so that most houses affordable by low-income earners now fall under the tax threshold. The proposed new transfer duty threshold will reduce the tax burden on all property transactions by R500.

It is estimated that this proposal will result in a revenue loss of R100 million.

The new rate structure is set out below:

Property value	Rates of tax
R0 – R150 000	0%
R150 001 – R320 000	5% on the value above R150 000
R320 001 and above	R8 500 plus 8% on the value above R320 000

Property value	Current duty	% of value	Proposed duty	% of value
R150,000	R500	0.3%	–	0.0%
R200,000	R3,000	1.5%	R2,500	1.3%
R250,000	R5,500	2.2%	R5,000	2.0%
R300,000	R8,000	2.7%	R7,500	2.5%
R500,000	R23,400	4.7%	R22,900	4.6%
R750,000	R43,400	5.8%	R42,900	5.7%
R1,000,000	R63,400	6.3%	R62,900	6.3%

Corporate finance initiatives

Broad-based employee equity participation

Many countries have special tax incentives that promote broad-based employee equity participation. These schemes enhance productivity by providing employees with an economic stake in the company. In the South African context, the existence of these schemes could also serve as a useful means of promoting broad-based empowerment objectives.

Unfortunately, very few low-income employees hold shares in the company for which they work. One barrier to this form of ownership is the income tax. Any issue of shares to an employee at reduced or no cost triggers fringe benefit tax for the employee, which many people simply cannot afford. While tax strategies exist for reducing the tax costs through option, share and other equity-based schemes, these tax planning opportunities are typically available only for employees and directors earning higher incomes.

It is accordingly proposed that legislation be introduced to allow for the tax-free transfer of shares to employees (capped at a certain amount) in order to encourage broad-based employee participation in companies. These rules will facilitate long-term ownership rather than short-term profit taking by taxing any gains realised within a specified period as ordinary income and by allowing employers to provide certain restrictions to prevent short-term sales of shares by employees. Rules may also have to be explored as to the scheme's consequences for the employer company.

Adjustment of equity-based incentives for highly paid employees

Over the years, a number of equity-based incentives have been developed for top management that provide various forms of tax benefits. One example is share option schemes used to defer taxes or to convert ordinary salary income into capital gains. Some aspects of these incentives for top management conflict with the tax principle of vertical equity and create problems in respect of corporate governance. It is proposed that legislation be introduced to address equity-based incentives of this nature. Rules may also have to be explored as to the company consequences of equity-based issues in exchange for salary and other concerns.

Addressing the tax treatment of hybrid financial instruments

The current tax differential between debt and equity leads to different cash flow results for taxpayers. For instance, debt provides interest deductions for issuers, but triggers a tax liability on interest earnings. On the other hand, dividend payments create secondary tax on companies for the distributing company, and the benefit of exemption for shareholders. Hybrid financial instruments combine both debt and equity characteristics. Such hybrid instruments may include convertible loans, perpetual debt, redeemable preference shares, and interest-yielding preference shares.

An urgent need exists to improve current anti-avoidance legislation relating to hybrid instruments. It is proposed that legislation be introduced that characterises hybrid instruments according to their underlying economic substance, along with other collateral anti-avoidance legislation. The main focus of proposed anti-avoidance legislation will be on:

- Convertible instruments
- Debt with principal that is effectively never repayable
- Shares with required repayment of capital
- Special rules addressing concerns surrounding domestic versus foreign hybrids.

Assisting deferred payment schemes

The purchase of property can be financed through various methods. In most cases, sellers demand their sale proceeds upfront with purchasers obtaining financing from other sources. In other cases, sellers can effectively finance purchases by allowing for deferred payment over several years. In the South African context, deferred payment schemes can also be used to shift ownership as part of the economic empowerment effort. However, current tax legislation arguably creates a barrier for this form of financing by triggering an immediate tax event, even though sale proceeds may be deferred over many years. Special additional problems exist when the deferred payments are based on contingencies (such as payments based on future profit streams) and when calculating gains on the sale of certain pre-1 October 2001 assets. Rules will accordingly be considered to accommodate some or all of the above concerns.

Investments into South Africa from counties within the Common Monetary Area

Foreign residents are generally not subject to tax on interest received from South African sources. However, this exemption does not apply to residents from countries within the CMA (i.e., Namibia, Lesotho, and Swaziland). This limitation for CMA residents was introduced in 1993 along with the exemption in order to protect the tax base before the 2001 introduction of the worldwide tax system.

It is proposed that the limitation applying to residents within the CMA be eliminated as obsolete (possibly subject to conditions). This proposal will also entail the technical realigning of the foreign interest exemption provisions and possibly certain situations in which CMA investment funds are subsequently repatriated to their respective home countries. Other collateral issues to be considered include an anti-avoidance rule that prevents the exemption from applying in the case of debts originating between domestic parties.

Government grants and exempt entities

Government grants

In 2003, government grants to Public Private Partnerships (PPP) for infrastructure development became eligible for income tax relief. These tax preferential grants to PPPs were justified only in cases where the physical infrastructure reverts to Government ownership by close of the concession period. It is proposed that tax relief be extended to other entities receiving grants of this nature. It has also come to Government's attention that the 2003 tax proposals require further refinement, including provision for capital expenditure items associated with physical infrastructure.

In addition, private stakeholders may expend their own funds to construct or improve infrastructure on Government's behalf. However, these stakeholders cannot claim tax depreciation on related expenditure for this form of capital expenditure because, among other reasons, the infrastructure is not technically "owned" by them (i.e., the infrastructure affixes to land that belongs to Government). It is proposed that this form of capital expenditure and related expenses become tax deductible, subject to anti-avoidance concerns.

Financial exchanges and other specialised exempt entities

The Income Tax Act currently contains exemptions for specialised entities (such as the JSE Securities Exchange, Chambers of Commerce and social clubs) if approved by the Commissioner subject to regulatory conditions imposed by the Minister. Many of these exemptions currently need review in light of recent legislative changes and past practice. Of special note is the JSE Securities Exchange, which may be subject to overall regulatory change in terms of the impending Securities Services legislation. It is accordingly proposed that the exempt status of these entities be reviewed in law and/or regulation. These changes may provide the Minister with authority to provide for partial exemptions if circumstances so warrant and for rules addressing changes from tax-exempt to taxable status.

Stamp duties

Removal of stamp duties on mortgage bonds

Under current law, taxpayers acquiring real property are subject to stamp duty if they incur a mortgage to finance the property acquisition. Hence, the stamp duty creates a second duty on top of the transfer duty for an actual property transfer. The stamp duty is especially inequitable when one considers the fact that most persons of limited means (and first-time home buyers) more heavily rely on mortgage debt to acquire their homes. It is accordingly proposed that the stamp duty on mortgages be repealed from 1 March 2004. The estimated cost of this proposal is R250 million.

Removal of stamp duties on negotiable certificates of deposit

Government continued its gradual elimination of stamp duties on debts in 2003 with the removal of stamp duties on fixed deposits and non-convertible debentures. With the proposed removal of the stamp duty on mortgage debts as outlined above, the only stamp duty on debt remaining

is on NCDs. Continued stamp duty solely on this form of debt creates unwarranted economic distortions with the duty being avoided through various forms of arbitrage. It is accordingly proposed that the stamp duty on NCDs be repealed from 1 April 2004, at an estimated cost of R20 million.

Stamp duty on leases

Transfer duty generally applies when real property rights are transferred, and stamp duty generally applies when real property rights are leased. However, the long-term lease of real property is taxed at vastly lower amounts than the transfer of real property. No economic justification exists for this discrepancy. The stamp and the transfer duties will accordingly be reviewed in order to close this arbitrage opportunity in respect of long-term leases.

Stamp duties also raise enforcement concerns. Parties to an agreement, especially a lease, often fail to stamp their documents or only stamp their documents when an aggrieved party wishes to initiate litigation. The current penalty for this form of late stamping fails to act as a deterrent because the maximum penalty is often insufficient in relation to the total stamp duty owed. Late stamping allows an agreement to become enforceable with retrospective effect. Measures will accordingly be introduced to prevent these abuses and to align the penalty structure with other Acts.

INDIRECT TAX PROPOSALS

Excise duties on tobacco products

For the past seven years, the excise duties on tobacco products were aimed at effecting a total indirect tax incidence of 50 per cent of the retail selling price of the most popular brands. Evidence clearly suggests that this tax incidence has contributed towards Government's policy of discouraging the consumption of tobacco products. However, the policy of raising retail prices of tobacco products through an excise tax intervention must be balanced against the risk of smuggling and production of counterfeit cigarettes.

In an attempt to reinforce the efforts of the Department of Health, it is proposed to increase the total indirect tax incidence (i.e excise duties and VAT) on tobacco products to 52 per cent with immediate effect. In order to provide certainty to the industry, Government proposes to maintain the 52 per cent tax incidence target for three fiscal years.

The proposed increases in excise duties on tobacco products are expected to raise about R794 million in additional revenue in 2004/05. Based on the current retail selling prices of the most popular brands of tobacco products, the 52 per cent total tax incidence target translates into the following proposed excise duty increases:

• Cigarettes	16,55% to R4,53 per 20 cigarettes
• Cigarette tobacco	11,70% to R139,04 per kg
• Cigars	15,67% to R1 233,04 per kg
• Pipe tobacco	17,30% to R68,32 per kg.

Excise duties on alcoholic beverages

Adjustments in the excise duties of alcoholic beverages are based on a targeted total tax burden (excise duties and VAT), expressed as a percentage of the weighted average retail selling prices of spirits, clear beer and wine respectively. Currently, the tax burden on spirits, clear beer and wine is approximately 38, 32 and 18-19 per cent, respectively. Government in consultation with stakeholders has agreed to target a total tax burden as a percentage of the weighted average retail selling price for spirits, clear beer and wine of 43, 33 and 23 per cent. This will be phased in over three years.

The proposed increases in the excise duties for the different types of alcoholic beverages, with immediate effect, are as follows:

• Natural unfortified wine	30,7%
• Sparkling wine	28,0%
• Fortified wine	16,0%
• Spirits	13,5%
• Clear/malt beer	9,0%
• Alcoholic fruit beverages	7,1%

Excise duties on Traditional African Beer and beer powder will remain unchanged. Alcohol excises will raise approximately R660 million in additional revenue in 2004/05.

Specific excise duties

It is proposed that the customs and excise duties in Section A of Part 2 of Schedule No.1 of the Customs and Excise Act, No.91 of 1964, be amended with effect from 18 February 2004 to the extent shown below:

Tariff item	Tariff heading	Description	Present rate of duty 2003/04		Proposed rate of duty 2004/05	
			Excise	Customs	Excise	Customs
104.00		Prepared foodstuffs; beverages, spirits and vinegar; tobacco				
104.01	19.01	Malt extract; food preparations of flour, grouts, meal starch or malt extract, not containing cocoa or containing less than 40 per cent by mass of cocoa calculated on totally defatted basis, not elsewhere specified or included; food preparations of goods of headings 04.01 to 04.04, not containing cocoa or containing less than 5 per cent by mass of cocoa calculated on totally defatted basis not elsewhere specified or included:				
.10		Traditional African beer powder as defined in Additional Note 1 to Chapter 19	34.7c/kg	34.7c/kg	34.7c/kg	34.7c/kg
104.10	22.03	Beer made from malt				
.10		Traditional African beer as defined in Additional Note 1 to Chapter 22	7.82c/l	7.82c/l	7.82c/l	7.82c/l
.20		Other	2 819.30c/l of absolute alcohol	2 819.30c/l of absolute alcohol	3 073.04c/l of absolute alcohol	3 073.04c/l of absolute alcohol

Tariff item	Tariff heading	Description	Present rate of duty 2003/04		Proposed rate of duty 2004/05	
			Excise	Customs	Excise	Customs
104.15	22.04	Wine of fresh grapes, including fortified wines; grape must, other than that of heading no. 20.09				
	22.05	Vermouths and other wine of fresh grapes flavoured with plants or aromatic substances				
.02		Sparkling wine	252.60c/l	252.60c/l	323.32c/l	323.32c/l
.04		Unfortified wine	89.6c/l	89.6c/l	117.10c/l	117.10c/l
.06		Fortified wine	200.75c/l	200.75c/l	232.87c/l	232.87c/l
104.17	22.06	Other fermented beverages, (for example, cider, perry and mead); mixtures of fermented beverages and mixtures of fermented beverages and non-alcoholic beverages, not elsewhere specified or included:				
.05		Traditional African beer as defined in Additional Note 1 to Chapter 22	7.82c/l	7.82c/l	7.82c/l	7.82c/l
.15		Other fermented beverages, unfortified	143.55c/l	143.55c/l	153.74c/l	153.74c/l
.17		Other fermented beverages, fortified	254.54c/l	254.54c/l	295.27c/l	295.27c/l
.22		Mixtures of fermented beverages and mixtures of fermented beverages and non-alcoholic beverages	143.55c/l	143.55c/l	153.74c/l	153.74c/l
.90		Other	254.54c/l	254.54c/l	295.27c/l	295.27c/l
104.20	22.07	Undenatured ethyl alcohol of an alcoholic strength by volume of 80 per cent volume or higher; ethyl alcohol and other spirits, denatured, of any strength				
	22.08	Undernatured ethyl alcohol of an alcoholic strength by volume of less than 80 per cent volume; spirits, liqueurs and other spirituous beverages:				
.10		Wine spirits, manufactured by the distillation of wine	4 038.10c/l of absolute alcohol	3 942.10c/l of absolute alcohol	4 583.65c/l of absolute alcohol	4 487.65c/l of absolute alcohol
.15		Spirits, manufactured by the distillation of any sugar cane product	4 038.10c/l of absolute alcohol	3 942.10c/l of absolute alcohol	4 583.65c/l of absolute alcohol	4 569.65c/l of absolute alcohol
.25		Spirits, manufactured by the distillation of any grain product	4 038.10c/l of absolute alcohol	3 942.10c/l of absolute alcohol	3 942.10c/l of absolute alcohol	4 583.65c/l of absolute alcohol
.29		Other spirits	4 038.10c/l of absolute alcohol	4 038.10c/l of absolute alcohol	4 583.65c/l of absolute alcohol	4 583.65c/l of absolute alcohol
.40		Liqueurs and other spirituous beverages	4 038.10c/l of absolute alcohol	4 038.10c/l of absolute alcohol	4 583.65c/l of absolute alcohol	4 583.65c/l of absolute alcohol
104.30	24.02	Cigars, cheroots, cigarillos and cigarettes, of tobacco or of tobacco substitutes				
.10		Cigars, cheroots and cigarillos, of tobacco or of tobacco substitutes	106 600c/kg net	106 600c/kg net	123 304c/kg net	123 304c/kg net
.20		Cigarettes, of tobacco or of tobacco substitutes	194.25c/10 cigarettes	194.25c/10 cigarettes	226.40c/10 cigarettes	226.40c/10 cigarettes
104.35	24.03	Other manufactured tobacco and manufactured tobacco substitutes; "homogenised" or "reconstituted" tobacco; tobacco extracts and essences:				
.10		Cigarette tobacco and substitutes thereof	12 447c/kg	12 447c/kg	13 903c/kg	13 903c/kg
.20		Pipe tobacco and substitutes thereof	5 824c/kg net	5 824c/kg net	6 832c/kg net	6 832c/kg net

Changes in specific excise duties - 2004/05

Product	Current excise duty rate	Proposed excise duty rate	Estimated additional revenue R million	Change in excise duty Nominal	Real
Malt beer	R28,19c / litre of absolute alcohol (47,9c / average 340ml can)	R30,73c / litre of absolute alcohol (52,24c / average 340ml can)	303.2	9.0%	3.8%
Traditional African beer	7,82c / litre	7,82c / litre	–	0.0%	(5.2%)
Traditional African beer powder	34,7c / kg	34,7c / kg	–	0.0%	(5.2%)
Unfortified wine	89,6c / litre	117,1c / litre	98.2	30.7%	25.5%
Fortified wine	200,7c / litre	232,87c/ litre	10.6	16.0%	10.8%
Sparkling wine	252,6c / litre	323,32c / litre	6.0	28.0%	22.8%
Ciders and alcoholic fruit beverages	143,6c / litre	153,74c / litre (52,27c / average 340 ml can)	21.0	7.1%	1.9%
Spirits	R40,38c / litre of absolute alcohol (R13,02c / average 750ml bottle)	R45,84c / litre of absolute alcohol (R14,78 / average 750ml bottle)	220.3	13.5%	8.3%
Cigarettes	388,5c / 20 cigarettes	452,8c / 20 cigarettes	730.7	16.6%	11.4%
Cigarette tobacco	622,4c / 50g	695,17c / 50g	0.4	11.7%	6.5%
Pipe tobacco	145,6c / 25g	170,79c / 25g	61.7	17.3%	12.1%
Cigars	2452c / 23g	2836c / 23g	0.7	15.7%	10.5%

General fuel levy

It is proposed that the general fuel levy on petrol and diesel be increased by 10 cents per litre to R1,11 and R0,95 per litre respectively with effect from 7 April 2004. This increase will be a first step towards narrowing the fuel tax differential between petrol and diesel.

To minimise the impact on primary producers of the proposed increases, the diesel fuel concession to such producers (agriculture, forestry and mining) will be increased from 31,6 per cent (26,86 cents per litre) to 38,8 per cent (36,86 cents per litre) of the general fuel levy on diesel. This concession will take effect from 7 April 2004.

The proposed increase in the fuel levy will raise approximately R900 million in additional revenue for 2004/05.

Liquid petroleum gas (LPG) is being used in South Africa for transport purposes as a substitute for either petrol or diesel. Although the environmental advantage of LPG is given as a reason for its use, the main reason appears to be the lower price of LPG stemming from the absence of a fuel levy. However, recent studies suggest that LPG has no real environmental benefits over alternative clean fossil fuels, such as unleaded petrol or low-sulphur diesel used in vehicles with

catalytic converters. The significant fuel tax differentiation in favour of LPG therefore cannot be justified. Accordingly, it is appropriate to subject LPG used for transport purposes to all the transport fuel related levies. The administrative feasibility of this will be investigated during the next few months.

Road Accident Fund levy

In order to adjust for the impact of inflation and to assist the Road Accident Fund to implement a restructuring programme and begin to reduce its accrued deficit, the Road Accident Fund levy on petrol and diesel will be increased by 5 cents per litre with effect from 7 April 2004. Further increases of 5 cents per litre in April 2005 and April 2006 are proposed, subject to the Board of the Fund taking decisive action to put it on a sustainable financial footing, taking into account recommendations of the Satchwell Commission.

Total combined fuel levy on leaded petrol and diesel

	2002/03 93 Octane		2003/04 93 Octane		2004/05 93 Octane	
	Petrol	**Diesel**	**Petrol**	**Diesel**	**Petrol**	**Diesel**
General fuel levy	98.0	81.0	101.0	85.0	111.0	95.0
Road Accident Fund levy	18.5	18.5	21.5	21.5	26.5	26.5
Customs and Excise levy	4.0	4.0	4.0	4.0	4.0	4.0
Equalization Fund levy	–	–	–	–	–	–
Illuminating Paraffin marker	–	0.2	–	0.2	–	0.2
Total	**120.5**	**103.7**	**126.5**	**110.7**	**141.5**	**125.7**
Pump price: Gauteng (as in June)[1]	419.0	383.2	361.0	315.9	378.0	345.0
Taxes as % of pump price	**28.8%**	**27.0%**	**35.0%**	**35.0%**	**37.4%**	**36.4%**

1. *For 2004/05, the pump price is listed as of January 2004.*

Ad valorem customs and excise duties

An *ad valorem* duty exemption currently applies to vehicles with a carrying capacity of at least ten persons. Although this exclusion was intended to benefit only minibus taxis, the exemption unintentionally applies to other vehicles. It is accordingly proposed that the minimum carrying capacity be increased to at least fifteen persons with effect from 1 April 2004. Once the taxi re-capitalisation programme is implemented, an increase in the carrying capacity exemption to a minimum of eighteen persons will be considered.

In the 2003 Budget, *ad valorem* customs and excise duties on computers and some printers were removed. It is now proposed to remove duties on all computer printers, recorded and prepared unrecorded media (including magnetic tapes and stripes), certain cosmetic products, print film, photo copying apparatus and watches and clocks with effect from 1 April 2004.
It is proposed that the relevant sections in Section B of Part 2 of Schedule No.1 of the Customs and Excise Act, No.91 of 1964, be deleted with effect from 1 April 2004 to the extent shown on the next page:

Tariff item	Tariff heading	Description
118.25	33.05	Preparations for use on hair: shampoos, etc.
118.30	33.07	Pre-shave, shaving, or after-shave preparations, personal deodorants, bath preparations, etc
118.35	37.01	Photographic plates & film, etc.
118.40	37.02	Photographic film in rolls, sensitised, unexposed, etc
124.10	84.43	Printing machines
124.60	85.23	Prepared unrecorded media: magnetic tapes, discs, cards incorporating a magnetic stripe, etc.
124.65	85.24	Records, tapes & other recorded media e.g. CDs, DVDs, magnetic tapes, magnetic strips, etc.
128.40	90.09	Photo copying apparatus
128.55	91.03	Clocks with watch movements
128.60	91.05	Other clocks

VAT and transfer duty

The VAT and transfer duty have been linked to minimise and or prevent the likelihood of double taxation. The current provisions that link the VAT to the transfer duty result in certain inequities and will therefore be reviewed.

2003 BUDGET TAX PROPOSALS – IMPLEMENTATION

Foreign exchange amnesty and accompanying tax treatment

In 2003, an exchange control amnesty with accompanying tax measures was enacted to provide an opportunity for South Africans to regularise illegal offshore income and assets. Amnesty applicants can disclose or repatriate offshore amounts subject to prescribed levy payments of 0, 5 or 10 per cent, with an additional 2 per cent for accompanying domestic tax violations. The amnesty window period was initially 1 June 2003 to 30 November 2003, but was extended to 29 February 2004 in view of various changes to the regulations and the strong growth in applications received in October and November 2003. The total number of applications received exceeded 14 250 by the end of January 2004.

Expanding number of public benefit organisations eligible for tax deductible donations

In the 2003 Budget, the scope of tax preferences for PBOs was further expanded. Most notably, the list of public benefit activities eligible for tax-deductible donations was extended to include almost all PBOs involved in the areas of welfare and humanitarian aid, health care, land and housing, education and development.

In addition, the list of activities eligible for tax-exempt status was expanded to promote media access, low-income housing and bids for hosting international events. Tax rules were also changed so that local PBOs can utilise foreign donations anywhere in the region without losing their exempt status.

Stimulating development for urban development zones

In last year's Budget Speech the Minister of Finance announced a tax incentive in order to address the problem of inner city decay. This incentive allows taxpayers to receive accelerated depreciation allowances for investment in under-utilised urban development zones. Taxpayers refurbishing existing buildings within a demarcated zone will now receive a 20 per cent straight-line depreciation allowance over a 5-year period. The construction of new buildings within such a zone will benefit from a 17-year write-off period (20 per cent in the first year and 5 per cent in subsequent years).

The 2003 Budget Review identified 15 municipalities and the final legislation also provides for the Emfuleni municipality to benefit from the tax preference. The legislation requires municipalities to demarcate one or possibly two urban areas based on qualifying criteria, including population size and other special circumstances. Each tax preferential area is restricted to an overall hectare size limitation.

Pension fund reform

The National Treasury has been reviewing the taxation of retirement funds since 2002. Last year the retirement fund tax rate was reduced from 25 to 18 per cent. It is an important objective of public policy that individuals should face a compelling inducement to provide for their retirement. The task is how to find the optimal mix between policy instruments (such as taxes) and institutional provisions (such as compulsory contributions to pension funds). Also, tax policy interventions need to ensure some degree of neutrality between discretionary and contractual savings, which requires complex comparative analyses.

With a view to exploring options for reform, taking into account realistic household budget constraints and preferences, a holistic review is being conducted. National Treasury intends, together with all stakeholders involved in South Africa's saving industry, to develop policy proposals on savings and pension fund tax reform in 2004.

Mineral Royalty Bill and mining tax review

After extensive consultation with all stakeholders, the Minister announced several refinements to the Mineral and Petroleum Royalty Bill. These include a delay in the introduction of the royalty to five years after introduction of the Mineral and Petroleum Resources Development Act as well as the removal of the fiscal stabilisation clause. The Minister also reconfirmed Government's preference for a revenue-based royalty.

Government is mindful of potential adverse impacts on investment, employment and output from a royalty. The Treasury's assessment suggests that economic costs can be minimised if the royalty regime takes adequate cognisance of the sector's diverse production dynamics. Due to different market structures, the impact of the royalty will vary across the mining sectors, requiring a differentiated royalty rate. This rate differentiation will be refined to account for these diverse economic impacts. Other issues that still need review include the handling of marginal mines, the elimination of potential double royalties, continuation of current royalties during the transition period and possible adjustments to other revenue charges in respect of the issuance of new order mineral rights.

The new regulatory system for mining rights and accompanying royalty dispensation for the mining and petroleum industry has made it imperative to holistically reassess the current fiscal regime, including tax depreciation, rate differentiation for mining sectors, allowable deductions and STC exemptions in terms of the income tax regime.

Also due for review is the gold mining tax formula, which provides income tax exemption and STC relief for certain gold mines despite the existence of profit. While a special dispensation is arguably required for marginal mines, any tax preference in this regard is more appropriate fir a royalty regime than the corporate profit tax, which by its very nature automatically adjusts for profit levels. Other issues of concern include the special 40 per cent surcharge for companies engaged in natural oil extraction, as South Africa is keen to attract more investment into its fledgling natural oil and gas industry.

MEASURES TO ENHANCE TAX ADMINISTRATION

Enhanced tax administration is achieved through a balanced approach of improving enforcement and easing compliance. The following proposals are designed to promote both of these goals.

Improving compliance

Improving information quality

SARS will develop, test and implement procedures to improve the reliability of information from third parties. The aim is to utilise existing data warehousing and data mining systems to cross reference information collected from third parties and to reduce information requested from individual taxpayers. Consideration will also be given to extending tax reporting requirements to other third parties. This latter initiative may require minor legislative amendments.

General administration

Taxpayers are not required to inform SARS of changes in personal details, especially changes in mailing addresses. This failure creates an administrative burden for SARS, and it is proposed that taxpayers be required to inform SARS of any changes in this regard.

SARS will build on its successful 2003 filing season by launching an intensive taxpayer education campaign in 2004. These measures will be balanced with initiatives to simplify tax returns and a more stringent extension policy aimed at curtailing unreasonable delays in submitting returns.

In late 2002, SARS issued a discussion paper regarding the proposed registration of tax practitioners. Numerous comments were received from the legal and accounting professions. The most appropriate mechanism of regulation is being considered along with possible incorporation into legislation.

Corporate compliance

The low effective tax rates in specific sectors of the economy have continued to act as a catalyst for discussions between SARS and these sectors to understand the causes of the low rates and to collaborate in addressing them. As an example, the banking sector has agreed to look into its effective tax rate following discussions with SARS. Discussions with this and other sectors have yielded fruitful results but much remains to be done.

The low effective tax rates in certain sectors essentially transfer the costs of infrastructure and government services that the sectors depend on to others. This approach to doing business is unsustainable. It should become the active concern of CEOs, chairpersons and members of company boards who must increasingly make tax compliance and the effective tax rates paid by their companies a central issue in corporate governance.

Real property transactions involving residential property holding entities and foreigners

Two years ago, measures were introduced to prevent the use of residential property holding entities as instruments to avoid transfer duty. Under these measures, the change of ownership in a residential property holding entity became subject to transfer duty as if the ownership transfer directly involved residential property. It appears that these enforcement measures are still insufficient (especially when ownership changes hands between foreign parties) because the usual reporting mechanism for transfer duty does not apply. In order to protect the transfer duty base further, it is proposed that special reporting requirements be added for third parties involved in these transactions.

Enforcement problems also exist in terms of capital gains tax in respect of disposals by foreign parties. Foreign parties disposing of domestic real estate are subject to tax on capital gains, including sales of companies mainly holding domestic real estate. However, no effective enforcement mechanism exists to collect this tax. It is proposed that a capital gains withholding requirement be imposed to ensure proper collection from foreign persons.

Easing compliance

Simplification of forms and procedures

SARS is committed to improving service delivery for tax return filers and will introduce two new

individual income tax returns in 2004 – a simplified return for basic salary earners and a second return for salaried individuals with various forms of passive income.

The project to transform the existing Corporate Tax Centre into the SARS Corporates' Office (SCO) was launched in 2002. The SCO will provide comprehensive coverage (pre-filing, filing, risk assessment, compliance inspections and examinations) for all taxes imposed on companies. The SCO will be established through a phased approach in 2004/05. These services will ensure compliance and reduce the corporate tax gap.

SARS will continue to explore with other Government departments, the necessity of a single business number (SBN) that will provide a single point of access for information on business across all Government departments. Security of information will be increased and record keeping will be more efficient. For SARS, this new number would mean broadening the tax base in order more easily to register businesses for related taxes, including VAT, PAYE, Skills Development Levy and Unemployment Insurance Fund Contributions.

As stated in the 2003 Budget, SARS has been actively reviewing the possibility of introducing formal advance rulings, including the release of a comprehensive discussion document for public comment by 27 February 2004. The proposed advance ruling system is aimed at providing taxpayers with certainty as to the tax consequences of certain complex transactions. To the extent required, legislation will be developed during 2004.

The current system of purchasing adhesive stamps as proof of purchase for enforcement of the stamp duty is anachronistic. It is accordingly proposed that an e-stamping system be introduced.

Fiscal and administrative measures in support of small business

As illustrated in the accompanying textbox, Government has evidenced a long-standing commitment to dealing with small business concerns. Renewed focus this year is on improved administration.

First, the VAT retail scheme is scheduled for introduction in 2004. This scheme will provide a practical alternative for calculating the VAT liability if the vendor does not have a cash register that can distinguish between zero and standard rated sales. The VAT retail scheme will simplify compliance and administration for many retail small businesses that sell both standard and zero-rated goods.

Second, small businesses continue to have general administrative concerns, such as understanding SARS' requirements, submitting returns and time spent dealing with SARS. In recognition of these concerns, a task team of academics, representatives from various government departments and the private sector (including small businesses) will be established to review administrative aspects of small business interactions with SARS.

Measures in support of SMMEs

Tax policy changes

- *Incentives for small business companies:*
  Small companies with a turnover of less than R5 million qualify for a 15 per cent income tax rate on the first R150 000 of taxable income as well as immediate expensing for plant and machinery.
- *CGT incentives for the disposal of small business assets:*
  Taxpayers receive a one-time exclusion for the first R500 000 of capital gains for the disposal of small business assets within a two-year period.
- *Start-up expenses:*
  Costs incurred before commencement of trade are now deductible from the first year that trading commences. In addition, provision is made for a double deduction of start-up costs up to R20 000.
- *Deferral for business reinvestment:*
  Taxpayers can now defer gains/ income on the sale of business assets if they fully reinvest the sale proceeds in other business assets.
- *Increased mandatory VAT threshold:*
  The mandatory VAT registration threshold increased from R150 000 to R300 000 in 1999 to ease the compliance burden of small businesses.
- *Cash basis (for VAT purposes) for individual investors:*
  Small businesses registered as individuals can choose to register on the payment basis if sales are less than R2,5 million per annum.

Administration

- *Easing of the compliance burden:*
  SARS has reviewed the application of the penalty provisions, introduced colour-coded tax forms and reduced the number of returns that must be filed with respect to different tax instruments.
- *Service Monitoring Office (SMO):*
  Aggrieved taxpayers can now seek assistance from the SMO if they are not satisfied with the service provided to them at SARS branch offices. This office is especially useful for small businesses.
- *Dispute resolution processes:*
  Provision has been made for formal and informal dispute resolution. The dispute resolution process will provide for time periods for both SARS and tax-payers within which each step of the process must be completed. Informal dispute resolution is a form of dispute resolution other than court litigation, which is less formal and adversarial as well as more cost effective in resolving a dispute with SARS.
- *Tax guidance:*
  A tax guide for small businesses has been published by SARS

Trade facilitation – VAT deferment

The deferment of VAT payable on imports intended for re-export applies only to goods stored

inside bonded warehouses. Hence, as protective customs duties are phased out, fewer goods are kept in bonded warehouses, thereby eliminating VAT deferment opportunities. Such VAT payments result in cash-flow problems for businesses. Consideration is being given to remedy the cash-flow impact of VAT payments on duty-free goods intended for re-export. The removal of tax barriers in this area is important in order to facilitate South Africa's growth as a distributional hub to the rest of Africa.

Customs transformation

The Customs transformation project aims to optimise revenue collection, facilitate South African trade as well as provide accurate and timely trade statistics. The transformation process involves the following:

- Enhanced recruiting to address critical staffing requirements
- Improved technology integration between the Customs and Revenue offices
- Improved facilitation of intergovernmental information transfers
- The creation of effective transactional interfaces with commercial traders
- The provision of an in-depth policy document for a revised customs act
- Improved customs accreditation, including the effective management of accredited clients, tracking and managing client compliance records, accrediting compliant importers and exporters as well as improving training and stakeholder education.

MISCELLANEOUS AMENDMENTS

In addition to the Budget Proposals already described, the 2004 legislation will contain a number of miscellaneous amendments to the various tax acts. These amendments stem from various problem areas identified in the current legislation as detected over the course of the year through internal review and public comment. Some of these amendments eliminate perceived loopholes while others ensure that tax legislation does not inadvertently hinder legitimate non-tax motivated transactions. These amendments are expected to have only a small revenue impact for the Fiscus. This full listing of lesser amendments provides taxpayers with certainty in terms of expected legislative changes for the upcoming year.

Income Tax Act

- *Removing foreign anomalies involving trusts:*
  A number of foreign anomalies exist involving trusts. These anomalies include issues relating to the flow-through principle of foreign income and the treatment of foreign beneficiaries. The rules will be clarified in order to ensure that funds retained off-shore through trusts remain fully within the tax net and to ensure that foreign holdings of this type are not subjected to any unintended additional tax charges.
- *Clarifying the meaning of "participation rights" in a foreign company without share capital:*
  The Income Tax Act triggers the inclusion of income for South African residents having participation rights in a controlled foreign company if those residents have a stake of at least 10 per cent. At issue is how to apply these rules when a foreign company does not have

share capital (such as a captive insurance mutual fund). It is accordingly proposed that the law be clarified in this regard.

- *Adopting an annualised average foreign currency exchange rate for purchased annuities:* As a result of recent amendments, the income tax rules for calculating currency profits and losses now generally apply on an annual averaging (rather than spot) basis. The shift to averaging was inadvertently omitted from the purchased annuity-formula. This omission will accordingly be rectified.
- *Clarifying the 50:30:20 depreciation write-off for bio-fuel processing:* Last year Government stressed the importance of bio-fuels (bio-diesel and bio-ethanol) to support sustainable development. A preferential tax depreciation write-off regime of 50:30:20 was highlighted to encourage investment in bio-fuel related processing. It has subsequently come to Government's attention that not all bio-fuel projects may qualify for this preferential tax regime as was intended. It is proposed that the law be clarified to allow a 50:30:20 tax depreciation write-off for all investment in bio-fuel related processing.
- *Deleting the special entertainment deduction for amounts incurred by commission-based employees and entrepreneurs:* Commission-based employees and entrepreneurs can claim a limited amount of entertainment deductions if incurred directly in connection with a trade (and these expenses do not satisfy the general deduction formula). This deduction for additional entertainment expenses will be deleted in order to reduce confusion and to reduce possible claims for disguised personal expenses.
- *Denying deductions for interest and penalties made pursuant to the Unemployment Insurance Contributions Act:* Taxpayers generally cannot deduct interest and penalties paid pursuant to the various tax laws. Express provision will be made to deny deductions for comparable payments made pursuant to the Unemployment Insurance Contributions Act.
- *Removing the reference to Generally Accepted Accounting Practice (GAAP) in interest rate agreements:* Taxpayers must calculate their income and expense arising from interest rate agreements on a day-to-day basis, which conforms to GAAP and is consistently applied for all financial reporting purposes. With the adoption of AC 133, parties subject to mark-to-market accounting no longer use day-to-day calculations. It is accordingly proposed that the reference to GAAP be deleted.
- *Eliminating anomalies to the secondary tax on companies (STC):* Last year's amendment included changes to the STC to co-ordinate the rules for actual and deemed dividends. Further review may be needed to ensure that the recent changes work as intended. In addition, problems have emerged with certain administrative provisions, including the rules for additional taxes and the prescription period for assessments. Lastly, the dividend exemption for intra-group dividends needs to be limited so that the exemption does not apply when dividends are paid to exempt companies.
- *Modifying the provisions for pension payouts to divorced/separated spouses:* The current rules involving pension payouts to divorced/separated spouses contain unintended anomalies when a fund member's benefit is awarded to the former spouse. These rules will accordingly be clarified for consistency.

- *Creating rules for the conversion of real estate companies to share block companies:*
  A number of uncertainties exist when a real property company converts to a share block company. Special concerns exist as to whether this conversion causes a deemed distribution to the shareholders. It is accordingly proposed that these uncertainties be clarified.
- *Ongoing revisions concerning 1 October 2001 implementation issues for capital gains tax:*
  Special time-apportionment rules apply with respect to assets held before 1 October 2001 that ensure capital gains/losses are restricted to the post-1 October 2001 period. As in prior years, issues continually arise in this area that need to be addressed.
- *Clarifying the calculations for the learnership deduction:*
  Calculating the size of the learnership deduction depends on certain ratios involving the "annual equivalent" of a learner's wage. Unfortunately, the term "annual equivalent" is creating multiple interpretation problems. It is accordingly proposed that the learnership calculations be clarified either administratively or legislatively.
- *Administration – removing duplicate record keeping requirements:*
  Two sets of rules currently exist for essentially the same record keeping requirements. These rules will accordingly be streamlined.
- *Administration – providing optional pay-as-you-earn (PAYE) relief for disability insurance premiums paid by employees:*
  Under current law, employers may deduct employee-contributions to retirement annuity funds from the PAYE base if elected by the employee. No deduction from the PAYE base exists for employee-premiums paid for disability insurance. Consideration will accordingly be given to provide optional deductions from the PAYE base in these circumstances.
- *Administration – liberalising the definition of labour broker for PAYE:*
  Parties paying remuneration to a labour broker must withhold PAYE unless that labour broker receives a certificate of exemption. Similar to the waiver for the anti-avoidance personal service company rules, it is proposed that PAYE withholding be waived if a labour broker employs more than three full-time employees.
- *Administration – co-ordinating the R10 000 threshold for provisional tax with other thresholds:*
  The R10 000 threshold for payment of provisional tax has not been synchronised with other thresholds, such as the income threshold for paying tax. As a result, certain taxpayers are forced to file provisional tax returns even if no taxes are ultimately due. It is accordingly proposed that the provisional tax threshold be modified to eliminate this and other anomalies.
- *Administration – providing the Financial Services Board (FSB) with the authority to approve various forms of tax-exempt pension plans:*
  Tax-free pension plans currently need approval from both the FSB and SARS. This dual process is cumbersome, especially when the requirements of both agencies are often aimed at the same concerns. In order to simplify administration, consideration is being given to providing SARS with the authority to delegate the tax approval process to the FSB.
- *Administration – prescription period for re-assessments:*
  SARS generally cannot re-assess a taxpayer after three years have passed from original assessment. This three-year rule becomes a hindrance to negotiations when transactions under investigation are questioned by SARS. It is accordingly proposed to allow taxpayers

to elect to extend the prescription period by agreement for, these marginal circumstances, to facilitate the negotiation process.

Value-Added Tax Act

- *Extending the list of preferential domestic goods and services:*
  Commercial accommodations (e.g., hotels, old age homes) providing certain listed domestic goods and services are subject to VAT under a preferential formula subject to certain conditions. This list includes cleaning, maintenance, electricity, telephone, television and meals. The proposal is to extend the list to laundry and frail care services (including nursing services) provided by housing schemes for retired persons.
- *Extending the list of motor vehicles eligible for VAT input credits:*
  VAT vendors generally do not receive VAT input credits for motor vehicles, even for business use, because vehicles often contain a private consumption element. However, some exceptions exist for vehicles if the nature of the vehicle is such that private usage is doubtful (e.g., single-cab bakkies, ambulances). It is accordingly proposed to add hearses and game viewing vehicles as additional exceptions.
- *Clarifying the minimum VAT registration threshold for commercial accommodation:*
  It has always been intended that a commercial accommodation enterprise has to make annual taxable supplies exceeding R60 000 in order to be eligible to register as a VAT vendor. However, a technical anomaly exists between the general minimum registration rule of R20 000 and the commercial accommodation rule that arguably permits an "accommodation" enterprise to register voluntarily at the R20 000 general minimum. It is accordingly proposed that this technical anomaly be eliminated.
- *Clarifying derivatives as an exempt financial service:*
  Uncertainty exists as to whether the current generation of derivatives are adequately covered as an exempt financial service. It is accordingly proposed to extend the list of exempt financial services to include derivatives.
- *Clarifying the type of foreign leased goods eligible for zero-rating:*
  Zero-rating for lease, rental or charter agreements conducted outside South Africa was initially intended solely for the benefit of foreign utilised movable goods. However, this zero-rating could be misconstrued as also applying to "fixed property" (thereby triggering unintentional VAT inputs) because the definition of "goods" literally includes "fixed property." It is accordingly proposed to eliminate this anomaly.
- *Providing for zero-rating when enterprises of the same legal entity are combined:*
  A single legal enterprise can have multiple VAT registration numbers for its branches or divisions if those branches or divisions qualify as separate enterprises. As a rule, any combination of these separate enterprises creates a VAT liability, even though all activities remain within the same legal entity. It is accordingly proposed that enterprise combinations of this kind be zero-rated.
- *Clarifying the circumstances when zero-rating applies to services for foreign residents:*
  Services performed in South Africa for a foreign resident are generally zero-rated if that foreign resident (or representative) is located outside South Africa at the time of performance. However, certain foreign residents are attempting to claim zero-rating even though the

services at issue are wholly received by a VAT registered enterprise within South Africa (where standard rating is the only appropriate policy result). It is accordingly proposed that the rules involving zero-rating for services to foreign residents be clarified.

- *Providing VAT inputs for meals to offshore crews:*
  Enterprises providing meals as part of their services to clients generally cannot claim VAT inputs for meals consumed by employees (because employee meals could act as a fringe benefit). In 2003, an exception to this rule was added so that VAT inputs could be claimed for meals consumed by employees on board passenger transportation (who have no option but to eat at their worksite). It is now proposed that a comparable exception be added for meal costs consumed by crew employees of shipping vessels and those engaged in similar activities.
- *Eliminating VAT avoidance schemes using artificial non-vendor intermediaries:*
  A small class of VAT vendors are illegally attempting to avoid paying VAT on sales by utilising non-vendor intermediaries as agents. In schemes of this kind, a VAT vendor transfers goods to a non-vendor, and the non-vendor (acting as agent) sells the goods to another VAT vendor with VAT outputs illegally left unpaid. The buying VAT vendor then claims deemed VAT inputs for the purchase of second-hand goods (thereby being indifferent to the use of the intermediary). In addition to ongoing audits to prevent this practice, it is proposed that the declaration required for the deemed input be reviewed.
- *Defining the term "bad debts":*
  Special rules apply for bad debts, but the term "bad debts" is left wholly undefined, with the issue left solely to existing practice. It is accordingly proposed that the term "bad debts" be defined in statute in accordance with existing practice.
- *Reviewing changes to intergovernmental transfers and grants:*
  In 2003, changes were made to the operation of VAT in terms of transfer payments and governmental subsidies. These changes are set to go into effect on the date of Presidential proclamation. Consideration will be given to revisit the proposed treatment of grants to businesses in order to address any unintended consequences.
- *Administration - moving the location of VAT payments on imports:*
  In order to align the VAT Act with the Customs and Excise Act, it is proposed that VAT payments on imports be made at the port of entry or at the nearest local Customs office (rather than at the local SARS office).
- *Administration – clarifying the rules for tax invoices:*
  It is intended that all VAT vendors issue either full or abridged VAT invoices as part of their general reporting obligations. In addition, it is intended that all VAT vendors rely on a full VAT invoice when claiming inputs for supplies above R1 000 and may alternatively rely on an abridged VAT invoice when claiming VAT inputs for supplies not exceeding R1 000. The current literal wording is confusing and apparently contradictory in this regard. It is accordingly proposed that this wording be clarified.
- *Administration – requiring farmer notification for changes in VAT registration status:*
  Farmers who account for VAT on a six monthly cycle are not required to notify SARS when their income exceeds R1 million per annum, even though this change in income requires a shift to a bi-monthly cycle. Notification requirements will be added for this circumstance as a matter of consistency.

- *Administration – imposing a penalty for failing to notify SARS of an enterprise's cessation:* A vendor who ceases to carry on a VAT registered enterprise is required to notify SARS, but currently no penalty exists to enforce this notification. Consistent with other current notification penalties, it is accordingly proposed that this failure be made an offence.

Customs and Excise Act

- *Excise – refining duty at source:* Since 2002, duty at source has been phased in for the tobacco, spirit and fuel industries. Possible consequential amendments may be required to eliminate unintended anomalies uncovered during the implementation process.
- *Excise – refining the biofuels preference:* In 2002, a legislative preference was introduced for the manufacture, storage, distribution and use of biofuels. Consequential legislative amendments to this biofuel preference may be required to facilitate rule implementation.
- *Excise – clarifying the diesel fuel refund:* Diesel fuel concessions have recently been extended to certain off-land non-passenger operators. Further clarifications will be required in this regard, as well as extending it to other small off-land categories of non-passenger operators.
- *Ad valorem excise – Eliminating misuse of the R50 000 threshold:* Manufacturers are currently misusing the R50 000 threshold by artificially dividing their activities in order to multiply the value of the exemption. This misuse allows manufacturers to escape licensing and *ad valorem* excise duties. This provision will accordingly be reviewed to eliminate these concerns.
- *Ad valorem excise– eliminating category splitting of air conditioning machines:* Importers are attempting to reduce the *ad valorem* excise duty on air conditioners by artificially dividing the machine into two parts. Specific anti avoidance techniques will be introduced.
- *Environmental plastic bag levy – providing consequential amendments to the enabling legislation:* Enabling legislation was introduced in 2003 for the enactment of an environmental (plastic bag) levy. SARS will commence collection of the levy during the course of 2004. Consequential amendments might be needed to facilitate rule implementation.
- *Customs - Industrial Development Zones:* A revised set of enabling legislation for Industrial Development Zones was introduced in 2003. Gradual implementation of Industrial Development Zones may necessitate further legislative changes to facilitate smooth implementation, including collateral changes to the VAT Act, and may possibly include some policy shifts to account for changing realities.
- *Customs – refining enforcement in light of possible Constitutional concerns:* Customs enforcement requires that customs officials have the power to enter premises, gather information as well as detain and seize goods. Consideration will be given to reviewing these powers in order to eliminate any possible violation of the Constitution.
- *Customs – providing the Commissioner the power to readjust the value of exported goods:* The Customs and Excise Act currently provides that the value of exported goods is equal to

the free-on-board value. The Commissioner does not have any power to adjust this value in favour of true economic realities, even though the Commissioner normally has this power in other areas as a standard measure to prevent avoidance. The Commissioner will accordingly be provided with this power to address these concerns.

- *Customs – continuing the refinement of Siyakha initiatives:*
  The Siyakha initiatives are still ongoing. Consequential amendments may still be required for implementation.
- *Customs – adjusting legislation in light of the new South African Customs Union ("SACU") Agreement:*
  The new SACU agreement is expected to enter into force at the end of April 2004. This new agreement will necessitate changes to customs legislation and will include the updating of cross-references.
- *Customs – refining the shift of the General System of Preferences ("GSP") function to SARS:*
  In 2003, legislation was promulgated that shifted the function of GSP to SARS. Possible consequential amendments may be required to eliminate unintended anomalies uncovered during the process of implementation.
- *Customs – adding an absolute final prescription period for Section 75 refund claims:*
  Section 75(14) of the Customs and Excise Act provides that the Commissioner may, in exceptional circumstances, pay a refund or drawback after the expiration of the relevant period within which it has to be submitted. It is therefore proposed that final prescription period be added even for exceptional circumstances.
- *Customs - refining the dispute resolution, appeals and settlement procedures:*
  A revised set of dispute resolution, appeals and settlement procedures were added in 2003. Possible consequential amendments may be required to eliminate unintended anomalies.
- *Customs – prescribing the payment of salvage pursuant to the Wreck and Salvage Act No. 94 of 1996:*
  The Wreck and Salvage Act requires the Commissioner to pay salvage to the person salvaging a wreck. The Customs and Excise Act prescribes how payment is made for most situations but omits to make reference to salvage payments. It is accordingly proposed that salvage payments be included in the Act.

Tax on Retirement Funds Act

- *Administration – providing interest for refunds:*
  Taxpayers entitled to a refund from SARS with respect to retirement funds taxes are not entitled to any interest. This failure to provide interest is unfair and differs from the principles of other taxes. It is accordingly proposed that refund interest provisions be added for the tax on retirement funds.

Unemployment Insurance Contributions Act

- *Clarifying the interaction between the Unemployment Insurance Contributions Act and the Unemployment Insurance Act:*
  Some anomalies remain between the contributions act and the main act. It is proposed that the provisions of the Unemployment Insurance Contributions Act be aligned with the Unemployment Insurance Act.

Transfer Duty Act

- *Clarifying the exemption from transfer duty for partial public benefit organisation (PBO) activities:* PBOs are exempt from transfer duty when acquiring property wholly or substantially for PBO activities. However, since confusion exists as to how this exemption applies when property is only partly used for these purposes, the law will be clarified.

Stamp Duties and Uncertificated Securities Tax Acts

- *Administration – imposing late interest charges:*
  Taxpayers who fail to pay the stamp duty are subject to penalties but no late interest charges. Taxpayers consequently have little incentive to pay stamp duty on time. It is accordingly proposed that late interest charges be imposed that are consistent with other tax acts.
- *Administration – eliminating penalty stamps in favour of additional duties:*
  Stamp duty penalties are currently enforced through the anachronistic system of late penalty stamps. It is proposed that this penalty system be eliminated in favour of an additional duty.
- *Clarifying the definition of interest-bearing securities:*
  Stamp duties and uncertificated securities tax do not apply to interest-bearing securities unless convertible into shares. As part of the overall review of hybrid instruments, consideration will be given to clarify the meaning of "interest-bearing." Consideration will also be given to ensure that the exclusion of convertible securities from the exemption is consistent for both stamp duty and uncertificated securities tax purposes.

Skills Development Levies Act

- *Administration – reviewing in-kind salary:*
  Administration and compliance difficulties exist when applying the skills development levy if employers can only make salary payments in-kind rather than cash. Consideration will be given to review these concerns.

General Administration

- *Addressing administrative difficulties when applying interest rates set in terms of the Public Finance Management Act ("PFMA"):*
  Interest charges under the various tax acts are set with reference to PFMA. While this result makes sense from a policy viewpoint, process issues arise in terms of application, especially during periods immediately following rate changes. It is proposed that administrative leeway be provided to accommodate these process issues.
- *Reviewing the system of taxpayer accounts:*
  Taxpayers often have multiple tax accounts for various taxes. Consideration is being given for an improved accounting system possibly entailing minor legislative changes.
- *Reviewing Government interest for refund payments:*
  Although taxpayers are entitled to interest on refunds, the circumstances triggering interest can be unclear. It is accordingly proposed that these circumstances be clarified.

Other

- *Clarifying the circumstances when the 35 per cent branch rate applies:*
  The 35 per cent rate for South African branches or agencies could literally be read to apply to all companies with foreign located effective management. As a matter of clarity, the 35 per cent rate will be adjusted so that the rate applies only when a non-resident company maintains a South Africa branch or agency.
- *Reviewing tax acts relating to the former self-governing territories:*
  Some special tax acts and provisions for former self-governing territories inadvertently still remain on the books. Consideration will be given to the removal of these tax acts and provisions as they come to Government's attention.

TECHNICAL CORRECTIONS

In addition to the miscellaneous amendments above, the 2004 legislation will contain ongoing technical corrections. These technical corrections will address typing and grammatical issues, incorrect or misleading headings, misplaced cross-references, differences between the English and Afrikaans text, obsolete provisions, cross references incorporating regulations into law and problems relating to effective dates. These technical corrections may also occasionally include legislation clearly at odds with legislative intent as well as obvious ambiguities and omissions (especially with respect to recent legislative changes). These changes are not intended to have any policy or revenue impact. Technical corrections will be made during the upcoming year only if time permits.

INTERNATIONAL TAX AGREEMENTS

International tax agreements are important for encouraging investment and trade flows between countries. Agreements reached on the allocation of taxing rights between residence and source countries of international investors, international tax agreements provide a solid platform for growth in international trade and investment.

In the 2003/04 fiscal year, considerable progress was once again made in reaching agreements with other countries for the avoidance of double taxation and prevention of fiscal evasion. The present position is as follows:

Comprehensive agreements (53) are in force with Algeria, Australia, Austria, Belarus, Belgium, Botswana, Canada, Croatia, Cyprus, the Czech Republic, Denmark, Egypt, Finland, France, Germany, Greece, Hungary, India, Indonesia, Iran, Ireland, Israel, Italy, Japan, Korea, Lesotho, Luxembourg, Malawi, Malta, Mauritius, Namibia, the Netherlands, Norway, Oman, Pakistan, the People's Republic of China, Poland, Romania, the Russian Federation, the Seychelles, Singapore, the Slovak Republic, Swaziland, Sweden, Switzerland, Taiwan, Thailand, Tunisia, Uganda, the United Kingdom, the United States of America, Zambia and Zimbabwe. An older

agreement with the United Kingdom (1946) applies also to Grenada and Sierra Leone.

New comprehensive agreements (26) are in the process of negotiation or being finalised with Bangladesh, Brazil (ratified by South Africa), Bulgaria, Cuba, Estonia, Ethiopia, Gabon, Ghana, Kuwait, Latvia, Lithuania, Malaysia, Morocco, Mozambique, New Zealand (ratified by South Africa), Nigeria (ratified by South Africa), Portugal, Qatar, Rwanda (ratified by South Africa), Saudi Arabia, Spain, Sri Lanka, Tanzania, Turkey, Ukraine (signed but not ratified) and the United Arab Emirates.

Old comprehensive agreements (7) are in the process of renegotiation or being finalised with Botswana (signed but not ratified by South Africa), Germany, Malawi, the Netherlands, Swaziland (signed but not ratified), Zambia and Zimbabwe. Where agreements are being renegotiated, the existing agreements remain effective until new agreements are entered into force.

Limited sea and air transport agreements (3) are in force with Brazil, Portugal and Spain.

Note: Further information on the current status of the agreements is available on the SARS website under Income Tax / DTAs.

AGREEMENTS FOR MUTUAL ADMINISTRATIVE ASSISTANCE BETWEEN CUSTOMS ADMINISTRATIONS

Agreements covering all aspects of assistance, including exchange of information, technical assistance, surveillance, investigations and visits by officials are as follows:

Agreements (4) are in force with France, the Netherlands, the United Kingdom and the United States of America.

New agreements (9) are in the process of negotiation or being finalised with Algeria (ratified by South Africa), Angola, Iran, Norway, the Czech Republic (ratified by South Africa), Mozambique (ratified by South Africa), Norway, Turkey and Zambia (ratified by South Africa).

AGREEMENTS FOR MUTUAL AND TECHNICAL ASSISTANCE IN RESPECT OF VAT

New agreements (4) with Botswana, Lesotho, Namibia and Swaziland are in the process of negotiation or being finalised.

SUMMARY OF THE EFFECTS OF THE TAX PROPOSALS

	Effect of tax proposals
Direct tax proposals	**(4,432)**
Personal income tax:	**(4,062)**
Adjust personal income tax rate structure	(4,000)
Increase in interest and dividend exemption under 65 years	(50)
Increase in interest and dividend exemption age 65 years and over	(12)
Financial transaction taxes:	**(370)**
Adjust table for transfer duties	(100)
Remove stamp duty on mortgage loans	(250)
Remove stamp duty on NCDs	(20)
Indirect tax proposals	**2,132**
Specific excise taxes:	**1,453**
Increase in duties on beer	303
Increase in duties on fortified wine	11
Increase in duties on sparkling wine	6
Increase in duties on unfortified wine	98
Increase in duties on cider	21
Increase in duties on spirits	220
Increase in duties on tobacco products (52% incidence)	794
Increase in fuel levy	**909**
Remove *ad valorem* duties on certain products	**(230)**
Budget 2004/05 tax proposals	**(2,300)**