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Submission File

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National Treasury / South African Revenue Service

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Dear Majola and Ms Collins

**SAICA COMMENTS TO THE DRAFT RATES AND MONETARY AMOUNTS AND
AMENDMENT OF REVENUE LAWS BILL 2017**

The National Tax Committee on behalf of the South African Institute of Chartered Accountants (SAICA) welcomes the opportunity to make a submission to National Treasury (NT) and the South African Revenue Service (SARS) on the Draft Rates and Monetary Amounts and Amendment of Revenue Laws Bill 2017.

We cover the following matters in our submission -

1. Policy concerns relating to the increase in the dividend withholding tax (DWT) rate on 22 February 2017;
2. Practical implementation concerns relating to the increase in the DWT rate on 22 February 2017;
3. Resolution of the DWT concerns raised in this submission; and
4. Differences identified between the 2017 National Budget Speech and the Bill.



1. Policy concerns relating to the increase in the DWT rate on 22 February 2017

1.1. Policy reason for the increase in DWT

In the Minister's 2017 Budget Review (the Budget) on 22 February 2017, it was indicated that the increase in the dividends withholding tax (DWT) rate from 15% to 20% was to prevent arbitrage opportunities as a result of the increase in the personal tax rates between employees and business owners. However, if that was the motivation for the increase, then the increase in the tax rate should have been made effective on 1 March to coincide with the increase in the personal tax rates.

Therefore, by making the effective date of the DWT rate change the same day as the Budget Speech announcement, it becomes apparent that there was an additional 'anti-avoidance' policy imperative, namely to prevent businesses from declaring dividends during the period between 22 February and 1 March, purely in order to benefit from the lower DWT rate. This possible avoidance concern in our view remains speculative.

The Draft Rates and Monetary Amounts and Amendment of Revenue Laws Bill 2017 (the Bill) seeks to achieve the latter objective by virtue of the proposed amendment to section 64E of the Income Tax Act, 58 of 1962 (the Act), (subject to the discussion below in section 1.2. on the legality of the DWT rate change being effective on 22 February 2017).

However, given that National Treasury (NT) has reiterated that the National Development Plan (NDP) is the basis for the Budget proposals, it is unclear how this proposal supports that statement.

The NDP at pg. 140 states:

Small and expanding firms will become more prominent, and generate the majority of new jobs created. They will also contribute to changing apartheid legacy patterns of business ownership. They will be stimulated through public and private procurement, improved access to debt and equity finance, and a simplified regulatory environment.

Therefore, it seems clear that the NDP seeks to vest the growth of the small business industry as a key economic growth driver. However, given the economic challenges facing small business owners and the difficulties in forming a successful small business, as compared to just taking up employment, it is unclear what NT's strategy actually is when one considers the reason provided for this DWT rate increase.

The cause of the uncertainty is due to the continued lack of any real financial incentive in the Budget to individuals in opening a small business and earning dividends from the profits (which will also create employment when the small business hires employees) rather than taking up employment and earning a salary. This in our view directly contradicts NT's policy reason for increasing the DWT for all businesses.

Submission: It is submitted that NT should be offering a favourable dividends tax rate regime for small businesses to ensure that it becomes more favourable to start a small business rather than simply taking up employment. Applying a policy of equalised tax rates does not support such distinction.

Furthermore, should NT have concerns regarding the types of small businesses that should benefit from a favourable DWT rate, this could be addressed by excluding businesses or industries which do not contribute to the NDP objective. However, in our view, all small businesses which create jobs should be incentivised by this regime to ensure that there is 'uptake' by small business owners in all spheres of the economy.

1.2. Implementation of an unlegislated retroactive rate

In principle, SAICA does not support the retrospective implementation of tax rates, as it creates fiscal uncertainty and retroactive amendments should be frowned upon even more.

In this regard, we need to mention the 2016 amendment to section 5(2)¹ of the Act, which created new proxy legislative powers for the Minister of Finance, whereby public announcements altering "rates of tax chargeable in respect of taxable income" are lawful. This new rate will then apply even before the Act sanctioning such amendment is adopted by Parliament and signed into law, undermining Parliament's mandate to effect law changes. In considering extending this policy to DWT, it should also be noted that unlike the PAYE legislative equivalent which has been in the law for some time, DWT is a final tax whereas PAYE is an interim payment.

However, within the current legislative framework, not even the amendment to section 5(2) of the Act provides for the legal immediate implementation of the DWT rate increase as announced on 22 February 2017, as the section only applies to the alteration of rates on "taxable income", which DWT is not.

Consequently, it would appear that NT has required businesses to implement the 20% increased DWT rate without business having a legal mandate to do so. However, despite this deficiency, corporate SA has responded favourably to the Minister's announcement and should be applauded for the spirit in which this DWT rate increase was embraced.

¹ Section 5(a) The Minister may announce in the national annual budget contemplated in section 27(1) of the Public Finance Management Act, 1999, (Act No. 1 of 1999), that, with effect from a date or dates mentioned in that announcement, the rates of tax chargeable in respect of taxable income will be altered to the extent mentioned in the announcement.

(b) If the Minister makes an announcement of an alteration contemplated in paragraph (a), that alteration comes into effect on the date or dates determined by the Minister in that announcement and continues to apply for a period of 12 months from that date subject to Parliament passing legislation giving effect to that announcement within that period of 12 months.

The existence of the Minister's powers to effect tax rate changes, as announced in the Budget, from a date mentioned in that announcement, rather than on promulgation of the legislation, is concerning. Whilst we appreciate the need for this dispensation from a practical perspective in limited instances, e.g. to allow for personal income tax rates to change on an annual basis from the first day of the new tax year for individuals, when it is applied in the current manner it makes the implementation of such a rate change problematic (please refer below to section 2.), especially when also retrospective (please also refer below to section 1.3.). This policy may also create the impression to investors that SA is not a viable investment destination due to the lack of certainty of one's return on investment on any given day, because the Minister may amend the effective date of a rate change applicable to that return in such a way that does not allow an investor to predict their return. In our view the existence of this power and the principle it underpins is questionable.

Submission: Despite the fact that corporate SA embraced the DWT rate change announced in the Budget, we express concern in respect of this policy and practice, that tax rate increases are imposed without the existence of an apparent legal mandate by the legislature to do so.

If the amendment of tax rates other than those applying to "taxable income" is a policy requirement of NT going forward, then the law should be amended to accommodate such policy (and extend the Minister's powers in this regard). SAICA does not support such extension and harbours concerns in respect of the legality of the executive having de facto legislative powers. We are also concerned regarding the impact of the uncertainty such powers create.

Furthermore, NT needs to acknowledge the difficulties faced by industry in applying this policy by requiring industry to implement immediate rate changes. This creates fiscal uncertainty (and the resultant negative sentiment towards SA for foreign investors) if such power is arbitrarily invoked on an annual basis.

1.3. Retroactive legislation

In terms of the South African common law it is generally understood that statutes are not to be construed to operate retroactively unless an express or implied intention exists to the contrary²

In case of *Bellairs v Hodnett and Another*³ the following was stated by the court:

² *Adampol (Pty) Ltd v Administrator, Transvaal* [1989] 4 All SA 776 (AD) on page 783, *Unitrans Passenger (Pty) Ltd t/a Greyhound Coach Lines v Chairman, National Transport Commission* [1999] 3 All SA 365 (A) at paragraph 12, *Curtis v Johannesburg Municipality* 1906 TS 308 on page 311, *Mohamed NO v Union Government* 1911 AD 1 at 8 and *Bellairs v Hodnett and Another* 1978 (1) SA 1109 (A) 1148F-G). Also see Taljaard, J. C. (2001) *Geld die gewone reëls en beginsels van wetsuitleg by die uitleg van belastingwetgewing* M.Comm (Taxation) Stellenbosch University at 2.4.1 and the reference therein to *Principal Immigration Officer v Pushotam* 1928 AD 435 443, *Jockey Club of SA v Transvaal Racing Club* 1959 1 SA 441 A 451 and *Edwards v Tuckers Land and Development Corporation (Pty) Ltd* 1983 1 SA 577 A 580.

'There is a general presumption against a statute being construed as having retroactive effect and even where a statutory provision is expressly stated to be [retroactive] in its operation it is an accepted rule that, in the absence of contrary intention appearing from the statute, it is not treated as affecting completed transactions and matters which are the subject of pending litigation.'

The rationale behind the South African common law presumption against retroactivity is the need for legal certainty.⁴

The rationale can also be said to be that those subject to legislative provisions should be treated fairly, irrespective of the prospective or retroactive nature of the legislative provision in question^[4] and retroactivity should be viewed by the legislature with extreme prejudice and a direct imposition on the concept of legality and fair administration i.e. unless exceptional circumstances justify its use e.g. extreme evasion, it should not be tolerated.

Given these extreme repercussions in relation to the use of retroactive legislation, understanding the difference as to what constitutes retrospectively and what is its extreme form, namely retroactivity, is very important.

In *NDPP v Carolus and others*⁵ the court explains retrospectivity as legislation that operates prospectively but imposes a new result for a past event that took place before the enactment. For example, where the law imposes a different tax treatment to interest on a pre-existing loan but only to the interest after the enactment of the law (i.e. past transaction with prospective consequence).

In contrast, a retroactive statute operates as of a time prior to its enactment i.e. operates backwards and changes how the law applied to the past transaction. For example, where the law imposes a different tax treatment to interest on pre-existing loans in respect of interest taxable before enactment of the law (i.e. past transaction with back dated consequence).

The characteristics for retroactivity have been stated in *Bareki and Another v Gencor*⁶ as:

- Legislation invalidates what was previously valid
- Affects transactions already completed
- It enacts that as a past date the law shall be taken to be that which it was not at such time.

³1978 (1) SA 1109 (A) 1148F-G).

⁴Louw, H. **Retrospective application** Without Prejudice September 2012 on page 08

⁵2000 (1) SA 1127 (SCA)

⁶2006 (1) SA 432 (T)



In context of the proposed DWT rate change on 22 February 2017, two scenarios apply depending on whether the Budget announcement results in a legal basis for the change or not.

1.3.1. The Minister's announcement creates lawful quasi enactment

If the Minister's announcement does create a legal basis for the rate increase on 22 February 2017 (which we do not believe is the case), then the application to listed share dividends declared before but paid after is retrospective as it creates amended implications (increased rate) from a legislated date (i.e. quasi enactment) in respect of past declared dividends. However, the tax is only effected on determination after the legal change i.e. on actual payment which is prospective.

For unlisted share dividends, the new rate only applies to dividends declared after 22 February 2017 in accordance with the definition of "paid" in section 64E(2) of the Act. Therefore, this will neither be retrospective nor retroactive as all changes only apply prospectively to both dividend declaration and its subsequent payment after the quasi enactment.

1.3.2. The Minister's announcement does not create lawful quasi enactment

Should the Minister's Budget announcement not create quasi enactment as we have submitted, then the application of the increased DWT rate of 20% to dividends actually paid (listed shares) or due and payable (unlisted shares) before enactment (possibly only June or July 2017) will be retroactive as it would change the tax rate of 15% which legally applied at such date to 20%. This essentially requires a redetermination of the historical tax liability by applying the increased future legislated rate.

Submission: Despite the fact that corporate SA has embraced the DWT rate increase, we re-iterate our concerns regarding the apparent lack of legal mandate under which this DWT rate increase has been achieved and the need for resolution in this regard. We submit that in our view, there exists no reason to implement a retrospective rate change and even less so, a retroactive rate increase as any avoidance concerns are speculative at best. It should be NT's policy to adhere to the principle of prospective legislative amendments at all times, including instances relating to such a rate change, except in exceptional circumstances such as material tax evasion practices, which is not applicable in the current instance.

2. Practical implementation concerns relating to the increase in the DWT rate on 22 February 2017

The immediate implementation of this DWT rate increase on announcement of the Budget has resulted in a multitude of practical problems, as it is apparent that neither SARS nor business had sufficient time to implement the rate increase.

We understand that business (including the JSE) and SARS experienced difficulties in implementing this rate change, since system changes were required 'overnight'. There is a

serious risk for business in such circumstances because system changes were required immediately and in many instances without sufficient time to thoroughly test all system implications relating to such a change in the tax rate. Complex systems are not necessarily configured for immediate rate changes.

The manner in which DWT is reported to SARS, i.e. via the monthly submission of the DTR01 forms, was not taken into account before this immediate rate change was announced. As a result, changes were required to such forms to allow for more than one DWT tax rate in a single month.

Submission: We submit that NT needs to be cognisant of the manner in which both industry and SARS are required to respond to an immediate tax rate change, with the attendant risk of errors for industry due to the lack of adequate testing of systems. Consequently, NT should not resort to such immediate tax rate changes as a matter of policy and should rather entertain such a practice on an exceptional basis.

Furthermore, where such rate changes are necessitated due to exceptional circumstances, it would be assumed that SARS would be consulted with sufficient lead time to ensure that they can practically consider and resolve implementation challenges.

3. Resolution of the DWT concerns raised in this submission

SAICA acknowledges that NT proposed the DWT rate increase to increase revenues required by the state to fund its budgeted activities.

However, it is difficult to support the policy intent behind this rate increase, as -

- It does not support the NDP statement of intent in relation to incentivising small businesses;
- It has occurred in the apparent absence of a legal mandate to effect such a change which would then render the rate change as being retroactive, as opposed to being retrospective for listed companies;
- It adds to the creation of an environment of fiscal uncertainty which can only negatively impact foreign direct investment into SA; and
- It has created undue practical difficulties in implementation which were only overcome due to corporate SA's commitment to embracing this rate change without question, despite the apparent lack of legal mandate on NT's part.
- It creates substantial tax rate arbitrage between returns on investment from local capital compared to foreign capital i.e. most foreign outbound dividends will attract a 5% reduced rate due to the application of double taxation agreements. In our view, this has

the potential to incentivise bad fiscal behaviour by local investors through tax avoidance schemes.

Submission: We believe that it is imperative that the above concerns are addressed by NT. Accordingly, SAICA is willing to participate in discussions with NT in this regard with a view to furthering any 'thought leadership' initiatives which may assist NT going forward.

4. Differences identified between the 2017 National Budget Speech and the Bill

When the Budget was announced and the relevant budget documentation was released, Chapter 4 (page 46) of the 2017 Budget review indicated an increase in thresholds and exempt values for bursaries. Readers were directed to Annexure C for the detail.

Annexure C (on page 139) then provided the necessary detail and indicates the following:

Increasing the fringe-benefit exemption for employer-provided bursaries

Government proposes to increase the income eligibility threshold for employees from R400 000 to R600 000, and the monetary limits for bursaries from R15 000 to R20 000 for education below NQF level 7, and from R40 000 to R60 000 for qualifications at NQF level 7 and above.

The existing R15 000 exemption was applicable to grades R to 12 and NQF levels 1 to 4 (inclusive) and the R40 000 exemption was applicable to NQF levels 5 and above. The introduction of a new distinction in the Budget announcement moving the applicable NQF levels to below 7 or above 7 without any explanation created some concern.

The Bill however, provides for the amendment of section 10(1)(q) of the Act with an increase in the remuneration proxy, as well as increases in the exempt values for bursaries, with no mention of NQF level 7.

The proposed amendment to section 10(1)(q) of the Act again references the distinction between NQF levels 1 to 4 (inclusive) and NQF levels 5 and above to determine which exempt value is applicable.

The proposed amendment is in line with the existing section 10(1)(q) of the Act provision. However, the discrepancy between the Annexure C proposal and the draft Bill creates uncertainty.

The impact of this uncertainty is that payroll software providers are hesitant to build the amendments into the payroll systems until promulgation of the legislation, as the Budget announcements differ from the draft legislation. If the Budget announcement reflects the intention and policy of NT, the amendment is more complex than a simple value change. If, however, the Bill reflects the true intention of NT, the amendment is simple and logical and is simply an amendment of values to reflect the higher exemption.



The delay by payroll software providers is creating uncertainty for employers, as they are unable to implement the new thresholds and exempt value in their own bursary processes and this impacts the beneficiaries of the bursaries.

Submission: Clarity is required on the true intention of the amendment as to whether it is merely a value increase as per the Bill or a substantive amendment to section 10(1)(q) of the Act, as per Annexure C of the Budget.

Please do not hesitate to contact us should you have any queries in relation to anything contained in this submission.

Yours sincerely

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