National Treasury consults on proposed changes to tax regime

Theo Boshoff

Head: Legal Intelligence
Tel: +27 12 807 6686
Email: theo@agbiz.co.za

www.agbiz.co.za

National Treasury recently published a number of draft Bills that would amend the tax regime in South Africa, and more specifically the taxation mechanisms designed to attract investment into SMEs and special economic zones (SEZ). At a recent consultation session held at the SARS offices in Pretoria, industry had the opportunity to interact with the policymakers and gain insight into the implications which these would have for their members.

Venture capital companies

Amendments to the tax regime for the so-called section 12J venture capital companies came sharply into the spotlight. The current tax regime is designed to encourage investment into SMEs that lack access to formal financing channels via the s12J mechanisms. The proposed amendments would introduce a cap of R2,5 million rand per investment within the qualifying period. This, it was stated, was an attempt to strike a balance between encouraging venture capital investment without depriving the fiscus of revenue unduly.

Industry stakeholders were amenable to a cap in principle. However, it was suggested that the cap make a distinction between personal investments and corporate companies, with a much higher cap recommended for the latter. If a cap of R2,5 million be applied to corporates, it could result in less corporates choosing to invest their Enterprise Development Funds into s12J companies. Similarly, a cap which is too low could result in the s12J companies no longer being favoured by fund managers. A R2,5 million cap would prevent a corporate from acting as the 'anchor' investor and would entail significantly more work for fund managers for less returns. Put differently, a manager would need to attract 40 investors contributing R2,5 m each opposed to a single investor willing to crowd in R100 million into a venture capital company. National Treasury would consider these proposals before the Bill is finally submitted to Parliament.

Special economic zones

The latest set of draft amendments was intended to align the tax incentives for SEZs with the policy document emanating from the DTI. SEZs offer a reduced corporate tax rate of 15% (compared to 28%) for companies who set up their businesses in SEZs. The policy was designed to encourage new investments into strategic areas through the creation of new companies or expansion of companies into SEZs.

The latest amendments propose a 'new business test' as well as the requirement that a business must expand by 100% within the first year for its expansion (based in an SEZ) to qualify for the tax benefits. These amendments were put in place to prevent the situation whereby existing businesses simply move from their current base to an

SEZ to make use of the benefits without creating new job opportunities or growing the economy.

Whilst the policy imperative is well understood, industry representatives questioned the 100% threshold for qualifying expansions as the first year of an expansion into an SEZ is typically used to construct the premises, recruit and train staff. The feasibility of a 100% increase in value terms is therefore called into question.

Alternatives to measure the legitimacy of the expansion were proposed including the use of a three-year average and measurements other than gross value, for example an increase in employment or product volumes.

National Treasury will consider the proposals before the Bills are finally tabled in Parliament.