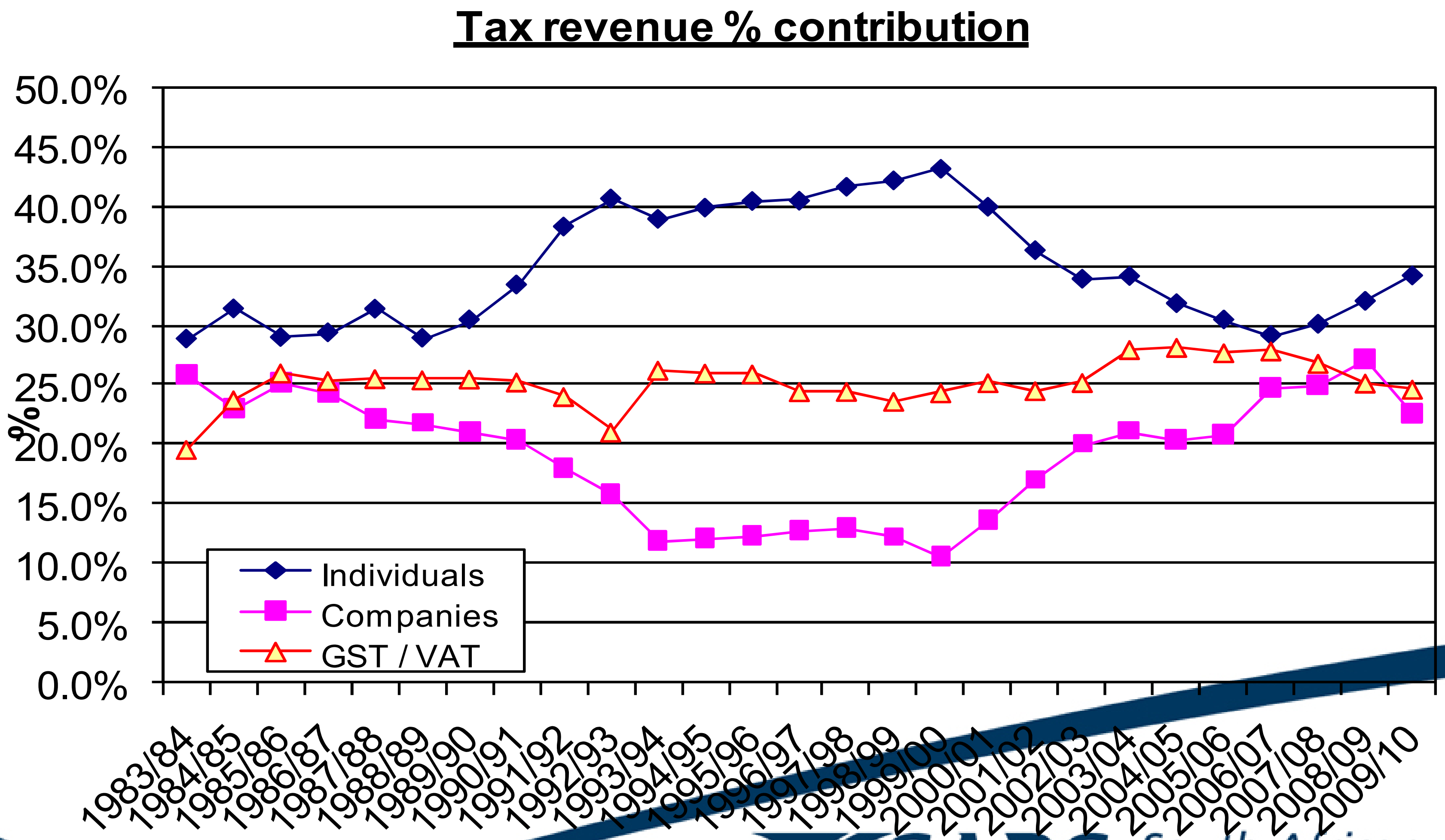
Key Revenue Sources

A Brief History of Income Tax and VAT

SARS South African Revenue Service

Key Revenue Sources



SARS South African Revenue Service

Income Tax - Origin

- Modern income tax was introduced in Britain on 9 January 1799, to finance the Napoleonic wars.
- Repealed in 1815 but reintroduced as a temporary measure in 1842.
- Board of Inland Revenue created in 1849.
- Two hundred years after its first imposition it was still a temporary tax, requiring new legislation every year.

Income Tax – South Africa

- Income Tax Act, 1914
  - Based on New South Wales Act, 1895
- Income Tax (Consolidation) Act, 1917
- Income Tax Act, 1925
- Income Tax Act, 1941
- Income Tax Act, 1962

Income Tax - Legislation

- Both Personal Income Tax and Corporate Income Tax are levied in terms of the Income Tax Act, 1962.

- The same core rules apply across the board, although there may be special rules based on type of person or industry.

Income Tax – 1963

- Fourth Schedule dealing with pay as you earn (PAYE) and provisional tax introduced.
  - Match payment of taxes to availability of funds, provide more regular cash-flow for government, and reduce burden on collections process on assessment.

Income Tax – 1984

- Seventh Schedule dealing fringe benefits introduced.
  - Address difficulties in determining the value of fringe benefits provided to employees.
  - Ensure that fringe benefits are taxed on a similar basis to salaries and wages paid in cash.

Income Tax – 1995

- Removal of gender and marital status discrimination from the income tax system.
  - Alignment with Interim Constitution.
  - 1st Interim Katz Commission Report.

- Thin capitalisation and transfer pricing provisions introduced.
  - Protection of SA tax base in light of increased trade, international investment, and ongoing relaxation of exchange controls.
  - 2nd Interim Katz Commission Report.

Income Tax – 1997

- Passive income taxed on a residence basis and controlled foreign entity provisions introduced.
  - Protection of SA tax base in the light of increased opportunities for residents to invest offshore and ongoing relaxation of exchange control.
  - 5th Interim Katz Commission Report.

Income Tax – 2000

- Taxation of foreign dividends
  - Immediate measure to counter tax avoidance using off-shore companies.
- Revised regime for public benefit organisations
  - Introduced a unified regime that catered for a wide range of public benefit activities and extended section 18A deductible donations.
  - 9th Interim Katz Commission Report.

Income Tax – 2000

- Switch from source to residence (world-wide) basis of taxation from 1 January 2001
  - Under a pure source basis tax is levied on income earned from a source within the country.
  - Under pure residence basis tax is levied on the residents of a country.
  - In practice, tax systems contain elements of both.
  - Ever increasing capital investment offshore led to the view that it was time to move to the residence basis, as most countries around the world had done.

Income Tax – 2001

- Introduction of capital gains tax from 1 October 2001
  - The absence of a capital gains tax introduced many distortions into the economy, encouraging taxpayers to convert otherwise taxable income into tax-free capital gains, with negative implications for the efficiency and equity of the overall tax system.

- Group re-organisation relief
  - Permits the tax-free transfer of assets to the entity where they can be most efficiently used for business purposes.

SARS South African Revenue Service

VAT - Origin

- Value-added tax was introduced by France with effect from 10 April 1954 for large businesses and extended over time to all business sectors.

- Over 140 countries around the world now operate a VAT (also known as Goods and Services Tax) system, making it the fastest growing tax instrument internationally.

VAT – Predecessor

- The current VAT system was preceded by a sales tax (also known as a general sales tax or GST) system under the Sales Tax Act, 1978.

- It was imposed on the sales of goods and certain services to consumers and on capital and consumable goods to vendors.

SARS South African Revenue Service

The Switch to VAT

- Some factors that drove the switch to VAT were:
  - A broader base and improved neutrality due to the ability to tax a wider range of services.
  - Imposition of sales tax on business inputs led to cascading tax (or tax on tax), especially in capital intensive industries, and increased export prices compared to countries operating a VAT.
  - Exemption certificates were used to allow tax free purchases of goods for resale by businesses and were widely abused, especially given the poor audit trail the system provided.

VAT

- Value-added Tax Act, 1991
  - Based on New Zealand's Goods and Services Tax Act, 1985.
- 1996: VAT base extended to included most fee-based financial services.
  - 3rd Interim Report of the Katz Commission.
- 1999: Introduction of a threshold for registration
  - Counter claims on private or hobby expenses.