Overview

• Introduction
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• The small business landscape in South Africa
• Surveys to determine the impact of taxation on small businesses
• The simple turnover tax and associated VAT relief for small businesses
• The small business corporation tax system
• The venture capital tax incentive for small businesses
• Summary of the main tax products for small businesses
• Conclusion
Introduction

• Government recognises the vital role small businesses play in economic growth, job creation, poverty alleviation and the improvement of living standards of all in South Africa.

• Entrepreneurship is the key to making the New Growth Path successful.

• The tax system cannot serve as a driver to make people successful entrepreneurs.

• However, the tax system must be able to support and facilitate entrepreneurship and the growth of small businesses.

• With this in mind, various tax initiatives were introduced over the years to assist small businesses.
Previous Budget Announcements

2001:
Tax relief for small business corporations (close corporations and companies).

2005:
• 4-monthly VAT returns instead of general 2-monthly (1,300 registered);
• Exemption from Skills Development Levy if payroll < R500,000 pa;
• Small Retailers VAT Package (withdrawn – due to low uptake of less than 100);

2006:
• Small Business Amnesty (350,000 applications);
• Proposed further relief for small business corporations.

2007:
• Simplification of VAT registration process;
• Small business compliance cost study will be commissioned.

2008:
• Simplified tax system consisting of Turnover Tax and increase in VAT registration threshold from R300,000 to R1 million;
• Venture capital tax incentive for investments in small businesses.
The Small Business Landscape

South Africa is a unique country in that it has a dual economy i.e.

- A highly sophisticated formal economy – needs sophisticated tax system; and
- A typical informal economy - does not keep proper records and is marginalised – needs a simplified tax system.

Varying estimates of the number of small businesses:

- 1.8 million people and about 1 million businesses operate outside the formal economy (Small Business Project: 2005).
- Individuals in business with or without a partner – 1.4 million in informal sector and 568,000 in formal sector (Stats SA: LFS 2007).
- About 1.1 million informal small businesses in South Africa i.e. individuals with turnover of less than R300,000 p.a. (Stats SA LFS: 2009).
The Small Business Landscape

Finscope South Africa Small Business Survey 2010 (business owners > 16 years old with < 200 employees):

- 6 million small businesses in South Africa (1 in 6 people).
- 73% work from home for average of 63 hours per week.
- 67% have no employees, 27% have 1 to 4 employees. But 9 million jobs.
- 17% have registered businesses (formal) i.e. 5 million are informal.
- > 80% have turnover < R150 000 per annum.
- 79% are traders (retailers); 21% are service providers (5% professional).
- Obstacles to growth – space (16%), finance (14%), competition (13%), crime (7%), licensing (3%), customs/trade regulations (2%).
- 76% not aware of support organisations (5% aware of SARS). Tax???
- Bank account – 50% in urban areas and 40% in rural areas.
- Sole source of income for 67%.
National Treasury and SARS commissioned the following surveys to get a better understanding of the impact of taxation on small businesses:

- FIAS (World Bank) Survey - Tax compliance burden for small businesses in South Africa: A survey amongst tax practitioners (2007);

- Survey of formal small businesses (2008);

A business typically had to register for the following taxes:

- Income Tax (includes CGT) – 1 return;
- Provisional Tax – 3 returns;
- Value-Added Tax (VAT) – 6 returns.

A simplified tax system was introduced in 2009 to ease the tax compliance burden on micro businesses (turnover of up to R1 million per annum). It consists of the following:

- The Turnover Tax;
- An increase in the compulsory VAT registration threshold to R1 million.

The simplified tax system effectively replaces income tax, provisional tax, capital gains tax secondary tax on companies and VAT. It only requires one return instead of the usual ten or more returns.
Design of the Turnover Tax

- Align with usual tax system to promote equity and avoid cliff-edge drop;
- Extract similar amount of tax as usual tax system but on simplified basis;
- Single tax to replace various taxes – based on turnover – at low rates;
- Protect existing tax base;
- Aim relief at small start-up and informal businesses and not the more sophisticated businesses that require accounting, legal and tax services;
- Therefore need specific anti-avoidance provisions (disqualifications) to ensure that the relief is targeted and that it benefits only the intended recipients;
- In light of the low tax rates and the need to protect the employment income tax base, had to exclude professional services, which usually operate on high profit margins;
- The truly small, unsophisticated, start-up type of business shouldn’t run into major problems with the anti-avoidance provisions in the law;
- Align VAT registration threshold with turnover tax threshold;
- Simple tax guides and brochures.
The Turnover Tax

- Presumptive tax - indirect calculation of tax, based on certain assumptions, to arrive at a tax liability that is similar to what is chargeable in the usual tax system.
- Available to individuals, companies, close corporations (CC’s) and co-operatives..
- Is a stand-alone tax i.e. will not be combined with other income.
- Elective i.e. it is an alternative to the standard tax system.
- Cash basis.
- Calculated by applying a tax rate to taxable turnover.
- Use of progressive tax rates per tax table.
- First R100,000 of turnover is exempt from tax;
- Liability in upper turnover range is relatively higher to encourage migration to the standard tax system.
- Minimal record-keeping.
VAT Implications

Registration threshold increased from R 300,000 to R1 million i.e. not compulsory to register if taxable supplies do not exceed R1 million in a 12-month period. Voluntary.

A micro business that is registered for VAT will not be permitted to register for TT.

The rule on de-registration from VAT is that “exit VAT” is payable on the lesser of cost or open market value of the assets held.

If vendor deregisters from VAT to apply for the TT, will get the following relief:

• Up to R100,000 deductible from the value of assets to calculate “exit VAT”.
• Can pay “exit VAT” in instalments.
# Turnover Tax: Before and After

<table>
<thead>
<tr>
<th>BEFORE</th>
<th>AFTER</th>
</tr>
</thead>
<tbody>
<tr>
<td>Detailed record keeping and costs.</td>
<td>Minimal record keeping and costs.</td>
</tr>
<tr>
<td>Typically submit <strong>10 or more returns</strong>:</td>
<td>Submit <strong>1 annual return</strong> with two six-monthly payments.</td>
</tr>
<tr>
<td>Provisional Tax (3 returns);</td>
<td></td>
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<tr>
<td>Income Tax (IT) (1 return);</td>
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<tr>
<td>Capital Gains Tax (with IT);</td>
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<tr>
<td>Secondary Tax on Cos (variable);</td>
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<tr>
<td>VAT (variable – usually 6).</td>
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<tr>
<td><strong>VAT - intensive recordkeeping.</strong></td>
<td></td>
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<tr>
<td><strong>Generic Income Tax computation:</strong></td>
<td></td>
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<tr>
<td>Total Income</td>
<td></td>
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<tr>
<td>Less: capital receipts =</td>
<td></td>
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<tr>
<td>Gross Income</td>
<td></td>
</tr>
<tr>
<td>Less: exemptions =</td>
<td></td>
</tr>
<tr>
<td>Income</td>
<td></td>
</tr>
<tr>
<td>Less: allowable tax deductions (records) =</td>
<td></td>
</tr>
<tr>
<td>Taxable Income (include taxable capital gains)</td>
<td></td>
</tr>
<tr>
<td><strong>No VAT</strong></td>
<td></td>
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<tr>
<td><strong>Generic Turnover Tax computation:</strong></td>
<td></td>
</tr>
<tr>
<td>Turnover</td>
<td></td>
</tr>
<tr>
<td>Add: 50% of sales of business assets =</td>
<td></td>
</tr>
<tr>
<td>Taxable Turnover (minimal records)</td>
<td></td>
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</tbody>
</table>
Turnover Tax Uptake

- About 8,000 businesses registered.
- Less than 1,000 new registrations.
- Split between companies and individuals more or less 50:50.
- Less than 3,000 out of a potential 131,000 businesses de-registered for VAT.

NB: More than 50% of the VAT register are small businesses with a turnover of less than R300,000 – high volume of refunds – they remain registered on a voluntary basis – businesses registered for VAT cannot register for turnover tax.
Turnover Tax Survey

• Businesses aware of tax obligations did not want to comply as they did not have time or money or they did not want to part with hard earned money or they felt that the way that the Government is spending tax money does not justify them paying taxes.

• Felt that only big businesses with offices pay taxes.

• Felt it was too costly to deregister from VAT or they (about 50%) would lose clients that prefer to deal with VAT registered businesses.

• Conflict of interest on the part of the tax practitioners.

• Lack of confidence was the strongest driver for not registering.

• More innovative advertising needs to be used to reach the target.

• Turnover Tax uptake will be successful in the long run based on its simple objectives.
Small Business Corporations

Companies, close corporations and co-operatives that have a turnover of up to R14 million per annum can register for income tax with the following incentives:

- Accelerated wear and tear – 100% on assets used for manufacturing and 50:30:20 for other assets;
- Graduated income rates (compared to flat 28%) for the 2010-2011 tax year:

<table>
<thead>
<tr>
<th>Taxable Income</th>
<th>Tax Rate</th>
</tr>
</thead>
<tbody>
<tr>
<td>R0 to R57 000</td>
<td>Nil</td>
</tr>
<tr>
<td>R57 001 to R300 000</td>
<td>10% of amount over R57 000</td>
</tr>
<tr>
<td>R300 001 and over</td>
<td>R24 300 + 28% of amount over R300 000</td>
</tr>
</tbody>
</table>

About 70,000 on register in 2010.
Venture capital tax incentive was implemented in 2009 to promote venture capital equity investments in SME’s.

Aim of the incentive is to encourage **Investors** to invest in approved **Venture Capital Companies** (VCC’s), which will, in turn, invest in qualifying **Investee** companies (i.e. small and medium-sized businesses and junior mining companies).

**Investors** → **VENTURE CAPITAL COMPANY** → Small/Medium/Junior Mining Companies

To retain its SARS approval, a VCC must invest the following minimum amounts within three years:

- R150 million in junior mining companies (assets must not exceed R10 million);
- R30 million in small businesses (assets must not exceed 10 million and must not be engaged in certain trade activities).
Venture Capital Tax Incentive

Provides for the following tax deductions in the hands of the investors (individuals and listed companies) in venture capital companies (VCC’s):

**Individuals** - 100% deduction of the amount invested for newly issued shares in an approved VCC up to limits:

- Annual deduction limit: R750,000
- Cumulative lifetime deduction limit (adjusted for recoupments): R2.25 million

**Listed companies (and their group subsidiaries)** - 100% deduction of amounts invested in a VCC to the extent that its investments, together with investments of its group companies, do not exceed 40% of the shares of the VCC i.e. although it is allowed to invest in more than 40% of the shares of the VCC, it will not get a deduction in respect of the amount in excess of the 40%.

Only one company on register in 2010 (implemented in midst of recession).
## Summary of Main Tax Products

<table>
<thead>
<tr>
<th>Micro Business</th>
<th>Small Business Corporation</th>
<th>Venture Capital Company Tax Incentive (VCC)</th>
</tr>
</thead>
<tbody>
<tr>
<td>Turnover up to R1 million</td>
<td>Turnover up to R14 million</td>
<td></td>
</tr>
<tr>
<td>• Individuals, CC’s, companies; and co-operatives</td>
<td>• CC’s, companies and co-ops;</td>
<td>• Tax deductions for investors;</td>
</tr>
<tr>
<td>• Turnover Tax;</td>
<td>• No tax up to R57,000 of taxable income ;</td>
<td>• Individuals: R750,000 pa up to 2,25 million over lifetime;</td>
</tr>
<tr>
<td>• No VAT;</td>
<td>• 10% tax up to R300,000 taxable income;</td>
<td>• Listed companies: up to 40% of equity in a VCC;</td>
</tr>
<tr>
<td>• 1 return instead of 10 or more;</td>
<td>• 28% tax on taxable income&gt; R300,000 (2011);</td>
<td>• VCC must invest in small businesses and junior mining companies, which must meet certain requirements.</td>
</tr>
<tr>
<td>• No tax up to R100,000 turnover;</td>
<td>• 100% wear and tear for manufacturing assets;</td>
<td></td>
</tr>
<tr>
<td>• Minimal record keeping and costs.</td>
<td>• 50:30:20 wear and tear for other assets</td>
<td></td>
</tr>
</tbody>
</table>

- SDL exemption if payroll < R500 000 per annum.
- Option to file VAT returns on 4 – monthly basis.
Conclusion

SARS will continue to look into ways and means of easing the tax compliance burden on small businesses to facilitate entrepreneurship and the growth of small businesses.

Questions???