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BUSINESS UNITY SOUTH AFRICA COMMENTS ON THE DRAFT TAXATION LAWS AMENDMENT BILL, 2024 (DTLAB)

1. Business Unity South Africa ("BUSA") is a confederation of business organisations, including chambers of commerce and industry, professional associations, corporate associations, and sectoral organisations. It represents South African ("SA") business on macroeconomic issues that affect it at the national and international level. BUSA's function is to ensure that business plays a constructive role in the country's economic growth, development, and transformation and to create an environment where businesses of all sizes and sectors can thrive, expand and be competitive.

2. BUSA welcomes the opportunity to submit comments on the draft Taxation Laws Amendment Bill, 2024 ("DTLAB") which was published on 1 August 2024 and to engage in a consultation process with the National Treasury to ensure a robust, coordinated, and aligned policy framework.

3. BUSA asserts that a stable economic environment is essential for fostering economic growth. Tax policy and legislation play a crucial role in this stability when

they carefully balance the protection of South Africa's tax base with the need to create an enabling environment for domestic businesses to thrive and expand. Consistency in tax policy, which informs legislative changes, is key to maintaining this stability. However, there is concern that the proposed amendments may undermine this stability, introducing uncertainty and potentially leading to significant unintended economic consequences.

Amendment to Section 9D: Controlled Foreign Companies (CFCs)

4. The amendment to Section 9D seeks to tighten the taxation rules for Controlled Foreign Companies (CFCs) by further restricting the income that South African taxpayers must include in their taxable income. This amendment could increase the administrative burden on South African companies with foreign subsidiaries, requiring more complex tax calculations and potentially higher tax liabilities.

5. While the objective of protecting the South African tax base is recognised, the business community is concerned that this amendment may discourage outward investment and expansion by South African companies. The increased complexity and potential costs associated with compliance could deter businesses from pursuing international growth opportunities. We propose that the government consider implementing transitional arrangements or providing additional guidance to minimise the disruption to businesses and maintain South Africa’s attractiveness as a base for multinational operations.

6. **Recommendation:** To mitigate the increased compliance burden, it is recommended that the government provide clear guidance, possibly including a grace period for companies to adjust their structures to comply with the new CFC rules. Implementing de minimis thresholds to exempt small or incidental amounts of CFC income could reduce the administrative impact on smaller businesses and minimise disruption, helping to maintain South Africa's attractiveness as a base for multinational operations.

Amendment to Section 12J: Phasing Out of Venture Capital Company (VCC) Incentives

7. The proposed phasing out of the Section 12J incentive, which has been pivotal in encouraging investment in small and medium-sized enterprises (SMEs) through Venture Capital Companies (VCCs), could harm the availability of capital for emerging businesses. This change could slow down the growth of SMEs, which are essential for job creation and economic development.

8. The business community is concerned that the removal of the VCC incentive could reduce the flow of much-needed capital into the SME sector, particularly in a challenging economic environment. Instead of an outright removal, we propose that the government consider refining the incentive to address any abuses while continuing to support SMEs. This could include targeted incentives for specific sectors or extending the incentive with stricter oversight.

9. **Recommendation:** Rather than completely phasing out the VCC incentive, the government should explore refining the scheme to prevent abuse while continuing to support SME growth. This could involve setting more stringent criteria for qualifying investments or focusing the incentive on specific sectors where capital is most needed. A phased reduction in the incentive, with regular impact assessments, could also help balance the need for fiscal prudence with the ongoing support for SMEs.

Amendment to Section 11D: Research and Development (R&D) Incentives

10. The amendment to Section 11D introduces stricter criteria for qualifying Research and Development (R&D) activities eligible for tax incentives. This change may limit the ability of businesses to claim R&D tax deductions, particularly for incremental innovations that do not meet the revised definitions. The result could be a reduction in South Africa's attractiveness as a hub for R&D activities, leading businesses to consider relocating their R&D functions to more favourable jurisdictions.

11. Business is concerned that the stricter criteria could stifle innovation, particularly in industries where R&D is a key driver of competitiveness. We recommend that the government adopt a more flexible approach that recognises the diverse nature of R&D across different sectors. By maintaining a supportive R&D tax incentive framework, South Africa can continue to attract and retain innovative companies, thereby enhancing its global competitiveness.

12. **Recommendation:** The government should consider introducing sector-specific R&D incentives that recognise the varying nature of innovation across industries. Furthermore, broadening the definition of qualifying R&D activities to include incremental innovations could encourage a wider range of businesses to invest in R&D. Clear guidelines on qualifying activities and expenditures should also be provided to reduce uncertainty and ensure more consistent application of the incentive.

Amendment to Section 9: Employment Tax Incentive (ETI)

13. The proposed amendment in the Taxation Laws Amendment Bill aims to modify Section 9(4) of the Employment Tax Incentive (ETI) Act, 2013. The amendment introduces a significant change by replacing the existing provision, which currently allows employers to roll over excess ETI amounts up to a cap of R6,000 per qualifying employee, with a new rule that deems any such excess amount as nil. This change impacts amounts as contemplated in subsections (2) and (3), unlike the original provision which only applied to subsection (1).

14. Removal of the R6,000 Cap: The amendment eliminates the R6,000 cap on the excess ETI amount that can be rolled over. Under the current law, any excess amount beyond the employees' tax could be carried forward, up to this limit. The proposed amendment entirely removes this possibility, effectively resetting the excess amount to zero.

15. Application to Subsections (2) and (3): The amendment broadens the scope by applying to amounts considered under both subsections (2) and (3), whereas the original only applied to subsection (1). This expansion may have wider implications for businesses calculating their ETI.

16. Elimination of Rollover Provisions: The proposed amendment would eliminate the ability for businesses to carry over any excess ETI amounts between tax periods. This feature previously provided flexibility in managing tax liabilities.

17. While it is understood that the amendment may be aimed at reducing potential abuse of the ETI, there is concern about unintended negative consequences, particularly for Small, Medium, and Micro Enterprises (SMMEs). The amendment could inadvertently create barriers to participation, particularly discouraging SMMEs from utilising the ETI, which is designed to incentivise job creation. Given that SMMEs are critical to economic growth and employment in South Africa, this could undermine the broader objective of the ETI.

18. An Impact Assessment focusing on SMMEs should be conducted before any further consideration of the proposed amendments. This assessment would help to gauge the potential impact on SMMEs and ensure that the ETI remains a viable tool for promoting employment.

19. Call for Further Enhancements to the ETI: To ensure that the ETI continues to be an effective incentive for job creation and access to employment, business stakeholders strongly advocate for additional amendments to the ETI. These enhancements could build on the current successes of the ETI by making it more inclusive and better aligned with current economic realities.

20. Increase in the Remuneration Threshold: It is proposed that the remuneration threshold be increased from the current **R6,500 to R9,000**. This adjustment would

encourage higher earnings and better reflect the cost of living, which has not been adequately considered under the existing threshold.

21. Increase in the Age Threshold: The current age threshold of 18 to 29 years should be increased to 35 years. This change would align the ETI with other government employment programmes, such as the Youth Employment Service (YES) programme, and address the growing number of unemployed individuals beyond the age of 29 who are currently excluded from the benefits of the ETI.

22. Sector-Specific Incentives: In line with government employment creation initiatives such as Operation Vulindlela, additional sector-specific incentives could be introduced. For example, the ETI could be extended or enhanced for sectors like Tourism, Global Business Services (GBS), and Manufacturing. These sectors are strategically important for job creation, and incentivising them, possibly without age limitations, could further stimulate employment opportunities.

23. The proposed amendment to the ETI Act has the potential to significantly alter the landscape of employment tax incentives in South Africa. While the intention to curb abuse is acknowledged, any changes must not stifle the ability of SMMEs to participate in and benefit from the ETI. Additionally, further enhancements to the ETI, including increases in remuneration and age thresholds and sector-specific incentives, could help maintain and enhance its effectiveness as a tool for job creation in South Africa.

Amendments to Section 19C: Carbon Tax Act

24. The Carbon Tax Act, 15 of 2019, plays a pivotal role in South Africa's efforts to reach its net-zero goals by addressing carbon-intensive sectors and incentivising a shift towards lower-carbon production and technologies. As part of this ongoing effort, on 1 August 2024, the National Treasury and SARS published the draft Taxation Laws Amendment Bill (TLAB) for public comment, which includes

proposed amendments to the Carbon Tax Act. Additionally, amendments to the Carbon Offset Regulation were also published, prescribing carbon offsetting in terms of Section 19(c) of the Carbon Tax Act.

25. The purpose of this amendment is to ensure alignment between the Carbon Tax Act and the Department of Forestry, Fisheries and the Environment's Methodological Guidelines for Quantification of Greenhouse Gas Emissions (the Methodological Guidelines), changes to the carbon dioxide emission factors and net calorific values for the relevant fuel types are necessary, as announced in the 2023 Budget and updates to the Schedule 1 fuel combustion emissions factors and net calorific values and additional of new fuel types are necessary.

26. Coal Mining Fugitive Emissions: In the Draft Explanatory Memorandum, 2024 it is stated: *"To ensure alignment between the Carbon Tax Act and the methodological guidelines, changes to the Schedule 1 fugitive emissions tables are necessary to include the new fugitive emission factors."* The Methodological Guideline for Quantification of Greenhouse Gas Emissions (Gazette No 47257, dated 7 October 2022) indicates the fugitive emissions below for coal mining.

27. The Draft 2024 TLAB still indicates the fugitive emissions for coal mining which are not aligned with the emission factors presented in the Methodological Guideline for Quantification of Greenhouse Gas Emissions (Gazette No 47257 dated 7 October 2022).

28. As business, we have previously commented on this issue in the 2023 Draft TLAB and yet it was not addressed by the National Treasury. This gap requires rectification to ensure policy implementation alignment as the result of which creates incongruencies in carbon disclosure and transparency reporting.

Annexure B: Fugitive Emissions – Emission Factors

Solid Fuels

Table B.1: Country specific emission factors for fugitive emissions from coal mining (Lloyd and Cook, 2005)

Mining method	Activity	GHG	South African specific Emission Factor (m^3 $tonne^{-1}$)
Underground Mining	Coal Mining	CH_4	0.77
	Post-mining (handling and transport)		0.18
Surface Mining	Coal mining		0
	Post-mining (storage and transport)		0
Underground Mining	Coal mining	CO_2	0.077
	Post-mining (storage and transport)		0.018
Surface Mining	Coal mining		0
	Post-mining (storage and transport)		0

(Table 1: proposed changes to schedule 1 fugitive emission factors)

29. In the case of Iron and Steel, the inclusion of 1B1ci coke production (per coke produced) (tonne GHG/tonne coke) <u>is only applicable when using a Tier 1 methodology as per the Intergovernmental Panel on Climate Change (IPCC).</u>

30. IPCC is very clear indicating that in cases where a Tier 2/3 method is used to quantify process CO2 emissions, then CH4 emissions should not be estimated separately from the carbon balance method used. CH4 calculation is not applicable in these cases, to the Iron and Steel industry when quantifying GHG emissions using higher tier methods.

31. Country-specific factors and alignment of schedule 1 of the carbon tax with the updated factors on the methodological guidelines for quantification of greenhouse gas emissions: In the case of the iron and steel industry, which utilises the available Tier 2 emission factors under Section 3.7 of the Technical Guidelines, it is important to note that other factors for GHG emission quantification are also specified within the Technical Guidelines under various sectors, not just in

Schedule 1. These emission factors and methodologies are approved by the Department of Forestry, Fisheries, and the Environment (DFFE) for GHG quantification.

32. **Recommendation**: BUSA recommends aligning the Carbon Tax Act with the Technical Guidelines. This would help prevent misinterpretations among taxpayers, the Department of Forestry, Fisheries, and the Environment (DFFE), and the National Treasury, and reduce the need for constant updates to the Carbon Tax Act and the Customs and Excise Act. BUSA suggests that this alignment should specifically include consistency with the DFFE-approved methodology and the most recent version of the Technical Guidelines.

33. Increased threshold for eligible renewable energy projects from 15 to 30 megawatts for the carbon offset allowance: BUSA welcomes the increase in the threshold for eligible renewable energy projects from 15MW to 30MW for the carbon offset allowance and considers this a positive development. However, the offset regulations still reflect an excessively limited approach to project eligibility, which negatively impacts the available offset supply, increases the cost of offsets, and limits the potential to meet offset demand.

Way Forward

34. **Engage in Consultation:** The business community strongly recommends that the government further consult industry stakeholders before finalising the amendments. This dialogue should focus on assessing the real-world impacts of the proposed changes and exploring alternative approaches that could achieve policy goals without stifling economic growth.

35. **Conduct Impact Assessments:** Comprehensive impact assessments, particularly for SMMEs, should be conducted for all significant amendments, including those affecting the ETI, Section 12J, and Section 9D. These

assessments would provide valuable insights into how the changes might affect different sectors and business sizes, helping to fine-tune the amendments to minimise negative consequences.

36. **Phased Implementation:** Consider implementing the amendments in a phased manner, allowing businesses time to adjust and ensuring that any unintended consequences can be addressed promptly. Phased implementation would also allow for periodic reviews and adjustments based on real-time feedback from the business community.

37. **Provide Clear Guidance and Support:** The government should issue detailed guidance and support to businesses, particularly regarding the technical aspects of the new CFC rules and the updated R&D incentive criteria. This could include training sessions, online resources, and dedicated support channels to assist businesses in understanding and complying with the new requirements.

Conclusion

38. The 2024 Taxation Laws Amendment Bill introduces changes that could significantly impact the South African business landscape. While the intent to protect the tax base and align with international standards is clear, the business community is concerned about the potential for these amendments to create additional burdens and discourage investment.

39. To ensure that the amendments support economic growth, it is crucial that they are carefully designed and implemented with input from industry stakeholders. By engaging in further consultations, conducting thorough impact assessments, and considering phased implementation, the government can strike a balance between fiscal responsibility and fostering a conducive environment for business development.

40. Ultimately, a collaborative approach between the government and the business community will be key to ensuring that South Africa’s tax framework remains competitive, fair, and supportive of long-term economic growth.

Yours faithfully,

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