sait South African Institute of Tax Professionals

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The National Treasury

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The South African Revenue Service

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Additional comments on Special Economic Zones (SEZs)

Thank you for the opportunity to participate in the Annexure C workshop on Business Tax Incentives on 5 December 2016. We would like to expand on our comments made in our Annexure C submissions regarding SEZs.

Ten-year sunset clause

Our concern is that many start-up companies make losses for a number of years before they start making profits. In addition, most of these SEZ companies would also be entitled to accelerated capital allowances (S12C), additional tax allowances (S12I) and to the 10% allowance in respect of buildings in the SEZ (S12S). Consequently, these companies could be in a tax loss position for many years from the time that they commence business in an SEZ. It will only be once they start becoming tax paying that they would benefit

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from the reduced tax rate of 15%. Therefore, allowing the reduced tax rate only for the first 10 years from commencing business in an SEZ could largely negate the benefit. Hence our recommendation that the SEZ tax rate should continue for 10 years once the qualifying company becomes taxable.

Limitation on connected person transactions

The connected person limitation is likely to be a significant stumbling block in the way of the success of the SEZ regime. Many potential investors who buy or sell into their own supply chain will not be willing to locate any of their operations in an SEZ in order to address the connected person anti-avoidance rule especially as a new legal entity is needed to benefit from S12R. While we acknowledge the 20% allowance gives companies some space to buy from connected parties, this is a fixed percentage and creates uncertainty from a measurement perspective over the S12R period. They would rather not locate any of their operations in an SEZ.

Another concern is that investors who do not obtain good tax advice upfront, may not realise that they will be disqualified from the SEZ tax benefits due to the limitation on connected person transactions. Practically we have found that the investment promotion agencies and the DTI administering the programme are not aware of these specific tax rules as they are focused on attracting investment.

As suggested in our Annexure C submission, applying a section 31 transfer pricing rule to prevent perceived avoidance would be more appropriate.

We would be pleased to engage further in this regard.

Yours sincerely

Duane Newman

Chair of the Business Incentives Work Group