

**A CRITICAL EVALUATION OF INTER-JURISDICTIONAL RULES IN THE
SOUTH AFRICAN VALUE-ADDED TAX SYSTEM**

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ABSTRACT

This study analysed the current inter-jurisdictional rules in the South African Value-Added Tax (VAT) system, identified shortcomings, and proposed legislative amendments or additions to address these shortcomings. The research was conducted within an interpretative post positivism paradigm, applied a qualitative research methodology, and a doctrinal research method. A detailed review of the literature was conducted to establish the theoretical basis of a good tax system and the theory underpinning indirect and consumption taxation. The literature review also included an in-depth analysis of the South African VAT system and its treatment of resident and non-resident businesses with a South African physical or economic reach, and its treatment of local and cross-border transactions, including imported services. The literature review also considered the international VAT treatment of these transactions. To obtain a wider range of expert opinions regarding shortcomings in inter-jurisdictional rules in the South African VAT system, data was collected through structured interviews with South African and global VAT and indirect tax experts, using a questionnaire that was specifically designed for this purpose.

This study proposed amendments and additions to the VAT Act, dealing with the VAT registration of non-resident suppliers; addressing various issues relating to the inter-jurisdictional VAT rate; proposing measures in connection with imported services; and legislating the intention of the legislator to tax final utilisation or consumption.

The study finally recommended the introduction of a general place of supply rule linked to residency; specific place of supply rules for electronic, broadcasting, and telecommunication services; and zero rating provisions for electronic, broadcasting, and telecommunication services provided to non-resident suppliers by resident suppliers for services initiated outside South Africa.

Key words: Value-Added Tax; Goods and Services Tax; Place of Supply rules; Zero rating; Worldwide VAT system; Territorial VAT system; Non-Resident VAT treatment; Inter-jurisdictional VAT rules; VAT on imported services; Reverse charging

PREFACE

Soli Deo Gloria

I would also like to extend my sincere appreciation to the following people:

- Professor Lilla (E.M.) Stack, my supervisor, for her positive energy, hard work, insightful contributions, superb knowledge of research methodology, and commitment to assist me in finishing this project;
- My parents who instilled in me an eagerness to learn; and
- My family and friends, but especially my wife Wilna, and my children, who have all humoured my academic endeavours over the years.

DEDICATION

Requiescat in pace

I dedicate this thesis to David Breetzke who, in his very short time of 23 years with us, demonstrated the power of living life to the fullest and with intensity and commitment.

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CHAPTER 1: INTRODUCTION

1.1 CONTEXT

A tax system typically comprises of direct and indirect taxes (Schneider, 1995:11). Direct tax is linked to characteristics of the person on whom the tax is imposed and includes income, capital, and wealth taxes. Indirect tax comprises “ad valorem” and specific taxes. VAT is generally an “ad valorem tax” imposed at differential rates (at least a standard rate and the zero rate), whereas customs and excise duties are ad valorem or specific taxes (Schneider, 1995:11).

As to the choice between direct and indirect taxation Gladstone, in his budget speech in 1861, concluded very appropriately that:

...two attractive sisters...introduced into the gay world of London; each with an ample fortune; both having the same parentage (...Necessity and Invention) differing only as sisters may differ...I cannot conceive any reason why there should be unfriendly rivalry between the admirers of these two damsels; and I would frankly own, whether it be due to a lax sense of moral obligation or not...I have always thought it not only allowable, but...an act of duty, to pay my addresses to them both. I am therefore, as between direct and indirect taxation, perfectly impartial (Cadman, 1969:3).

The origins of the VAT system, if considered to be a variant of sales tax or turnover tax, can be traced back to Ancient Greece, Hellenistic Egypt, and the Roman Empire (James, 2015:1). However, VAT considered as a modern fiscal innovation is often attributed to one of two people. Firstly, Dr Wilhelm Von Siemens, a German businessman proposed the VAT in 1918 as an improvement of the German turnover tax. (James, 2015:1 and Charlet and Owens, 2010:943). Secondly, the American economist T.S. Adams, proposed (in various writings from 1910 to 1921) an invoice-credit method VAT system as an alternative to corporate income tax (James, 2015:1). However, Maurice Lauré, acknowledged by some as the “father of VAT”, modified an existing turnover tax to become a predecessor to the VAT in 1954. The

European Union introduced VAT in member states in 1967, following the 1963 Neumark Committee's proposal (Peacock, 1981:120). The proliferation of VAT in Europe was driven by the fact that it is a prerequisite for membership of the European Economic Community (the ECC), predecessor to the European Union (the EU). VAT is also strongly supported by the International Monetary Fund. VAT systems have now been implemented in more than 160 countries, and account for about one-fifth of total tax revenue in the Organisation for Economic Cooperation and Development (the OECD) and worldwide (OECD, 2014a:14).

VAT systems are designed to tax final domestic consumption, which is generally done by freeing exports from VAT through zero rating whilst allowing related input tax deductions, and imposing VAT on importations (OECD, 2014b:5-6). Due to an increase in cross-border supplies of goods and services, the determination of the tax incidence and to which jurisdiction VAT revenue should accrue have become critical. Traditionally a supply could safely be assumed to take place at the supplier's location as cross-border supplies were limited. This is no longer the case. As a result, VAT place of taxation proxies to approximate the place of consumption were developed to address these shortcomings. The increase in global trade and defining when intangible property and services are exported also requires careful crafting of VAT rules relating to non-resident suppliers (OECD, 2014b:5-6).

The OECD and the EU developed consumption tax principles against which these proxies are measured. These proxies differentiate between internationally traded goods and services. The OECD and EU developed a set of main rules and certain special rules to deal with these proxies. Australia, Canada, and New Zealand, have all adopted specific inter-jurisdictional VAT rules. Australia's rules mainly use the concept of "connected with Australia" to determine the jurisdictional reach of its VAT system (OECD, 2014a:27). Australian VAT impacts non-residents extensively and requires the remittance of VAT for services performed in Australia, irrespective of whether the customer is a registered business or final consumer (OECD, 2014a:27). Canada adopted provincial and national rules, where the provincial place of supply rules mainly apply the origin basis and the national place of supply rules, the destination basis (Bird and Gendron, 2010:517). New Zealand adopted a different

approach to determine the VAT system's inter-jurisdictional reach, based on the residence of the supplier, and uses a combination of proxies (OECD, 2014a:27).

South Africa replaced its General Sales Tax (GST) with a VAT system in 1991. When VAT was introduced, South Africa was to a large extent still isolated from the world economy. Since the early 1990s, particularly since 1994 when South Africa had its first democratically elected government, the world economy started opening up to South Africa (Schneider, 2000:1). The South African VAT system can, in legal form, be described as a worldwide tax system (as opposed to a "territorial" VAT), which imposes tax on the worldwide supplies of persons (Schenk, 2009:9). The South African VAT net spans a substantial area of economic activity and, unlike most foreign VAT jurisdictions, does not have specific place of supply rules (MacKenzie and Kruger, 2009:67). As a result, a South African VAT registered vendor must report all supplies connected with his enterprise, wherever they occur (Schenk, 2009:9).

VAT practitioners have often expressed the need for place of supply rules to create certainty in respect of place of supply or consumption in cross-border transactions. Badenhorst (2007), for example, proposed certain place of supply rules in respect of foreign bank fees incurred and potentially consumed in South Africa, in response to the lack of place of supply rules. De Swardt (2011) acknowledged that the lack of place of supply rules gives rise to interpretational difficulties when considering whether a non-resident should register for VAT in South Africa. Parker (2011) observed that the lack of place of supply rules in the South African VAT system, especially in respect of electronic services, clearly illustrates that the VAT system lags well behind international VAT trends. Joubert (2010), in assessing the income tax and VAT implications of "cloud computing", made a plea for South Africa to introduce place of supply rules.

A limited number of comprehensive studies on South African inter-jurisdictional VAT rules have been carried out to date. The VAT sub-committee of the South African Fiscal Association (SAFA) drafted place of supply or activity rules in 2000 (SAFA, 2000). These suggested place of activity rules were never implemented. The VAT sub-committee of the South African Institute of Chartered Accountants (SAICA)

replaced the VAT subcommittee of SAFA and more recently revisited the need for VAT place of supply rules for South Africa (SAICA, 2009). The SAICA VAT subcommittee has not presented National Treasury with any recommendations on place of supply or place of activity rules. Schneider (2000) conducted a study on introducing VAT place of supply rules in South Africa, which included a fairly comprehensive theoretical discussion of the basis of taxation, VAT, consumption taxation, place of supply rules, and an international perspective. Janse van Rensburg (2011) conducted an explorative study of the introduction of VAT place of supply rules in South Africa, which also considered international experience. Some limited focus studies have also been undertaken on certain place of supply aspects. These studies include those by Krensel (2004) and Oosthuizen (2006) on the VAT treatment of electronic commerce, and de Swardt and Oberholzer (2006) on VAT compliance of digitised products.

These studies all, to varying degrees, considered certain aspects of inter-jurisdictional VAT rules, but mainly insofar as they relate to place of supply rules in the South African VAT system. The findings of these studies have not been implemented. None of these studies addressed inter-jurisdictional VAT rules comprehensively and either focused solely on the place of supply aspect, or on the activities of non-resident businesses in South Africa, or on selected aspects of one or these. None of these studies (except for SAFA to some extent) recommended detailed legislative changes. In 2004 the Minister of Finance acknowledged that the South African VAT Act does not have explicit place of supply rules (unlike most international VAT systems) and expressed the need for this to be reviewed to provide certainty with regard to the VAT on international transactions (South Africa, 2004:49). In 2005 National Treasury undertook to clarify VAT place of supply rules to provide certainty with regard to the responsibility and accountability for VAT in the case of certain international transactions (SARS, 2005b:17). Treasury, again in 2006, expressed the need to provide greater clarity in this area, especially for telecommunications, and that due consideration should be given to the work of the OECD in this regard (SARS, 2006b:17).

These studies and observations indicated two broad areas in the VAT system in need of further interrogation and potential revision. These two areas include:

- Uncertainty with regard to the VAT registration liability of non-residents; and
- The VAT rate applicable to cross-border supplies, especially supplies of services.

Any tax system should strive to satisfy certain principles of a “good tax system”. Adam Smith (1776:371) in his *“An Inquiry into the Nature and Causes of the Wealth of Nations”* formulated the properties of such a tax system. These properties are commonly referred to as the “canons” of taxation, although Smith used the word “maxims” (Ikeda, 2012). Various country studies have added to the debate on the principles of a “good tax system”, most notably that of the United Kingdom’s Meade Committee on Taxation (Meade, 1978), South Africa’s Margo Commission (Margo Commission, 1986) and the Australian Future Tax System (AFTS) Review Panel (AFTS Report, 2009). The most important property of a “good tax system” is that it must generate sufficient revenue to fund government expenditure. The other properties of a “good tax system” include equity, economic efficiency, administrative efficiency, and flexibility (Black, Calitz, and Steenekamp, 2012:165-167).

The present thesis, in attempting to propose legislative changes that will address the areas that appear to be problematic in the present VAT system, will be guided by these principles to which a “good” tax system should adhere.

1.2 GOALS OF THE RESEARCH

The goal of this research is to consider the current inter-jurisdictional rules in the South African VAT system, with a view to identifying current shortcomings in the system and to propose legislative changes or additions to address these shortcomings. The research considers shortcomings (or the lack thereof), not only in the traditional or so-called place of supply rules (aimed at determining where a supply takes place), but also considers the activities of non-resident businesses with activities or supplies that have a link or connection with South Africa. This is especially important if consumption occurs or could occur in South Africa.

In achieving the overarching goal of the research, the following sub-goals will be addressed:

- The research will initially create a theoretical foundation on which the remainder of the study can build.
- It will also consider the legislation and practical experience in selected countries and country groupings, with a view to applying these principles to address the shortcomings identified in the South African VAT system.
- The provisions of the South African VAT system governing non-residents, the inter-jurisdictional VAT rate and imported services will be considered in detail and analysed in the context of international experience in identifying shortcomings.
- Finally, the research sets out to make recommendations addressing the following aspects, collectively referred to as inter-jurisdictional VAT rules in the remainder of this thesis:
 - non-resident VAT registration;
 - the inter-jurisdictional VAT rate;
 - imported services; and
 - the place of supply rules.

The research will attempt to provide the legislator with specific technical and practical recommendations on inter-jurisdictional VAT rules and propose steps which might assist the legislator with the implementation.

1.3 RESEARCH METHODOLOGY

This study adopts an interpretative post positivism research paradigm as it seeks to understand, describe, design, and criticise the VAT consequences of inter-jurisdictional transactions and activities (Babbie and Mouton, 2009). The research methodology that will be applied can be described as qualitative and the research method as a doctrinal research method. This established method provides an orderly exposition of the rules directing a particular legal category (in this study: the legal rules relating to the VAT consequences of inter-jurisdictional transactions and

activities), analyses the interaction between these rules, explains areas of complexity, and is based entirely on documentary data (McKerchar, 2008). The research is conducted in the form of a natural language argument and will also include a comparative perspective with the view to propose reforms to the South African VAT system.

The first step in the research is a detailed review of literature to establish a theoretical basis of a good tax system, the theory underpinning indirect taxation and more specifically consumption taxation. The literature review also includes an in-depth analysis of the South African VAT system, particularly with regard to the treatment of resident versus non-resident businesses with a South African physical or economic reach, and its treatment of local and cross-border transactions, including imported services. The literature review also considers the international VAT treatment of non-residents and the treatment of cross border transactions and the use of inter-jurisdictional VAT rules to reduce interpretational uncertainty.

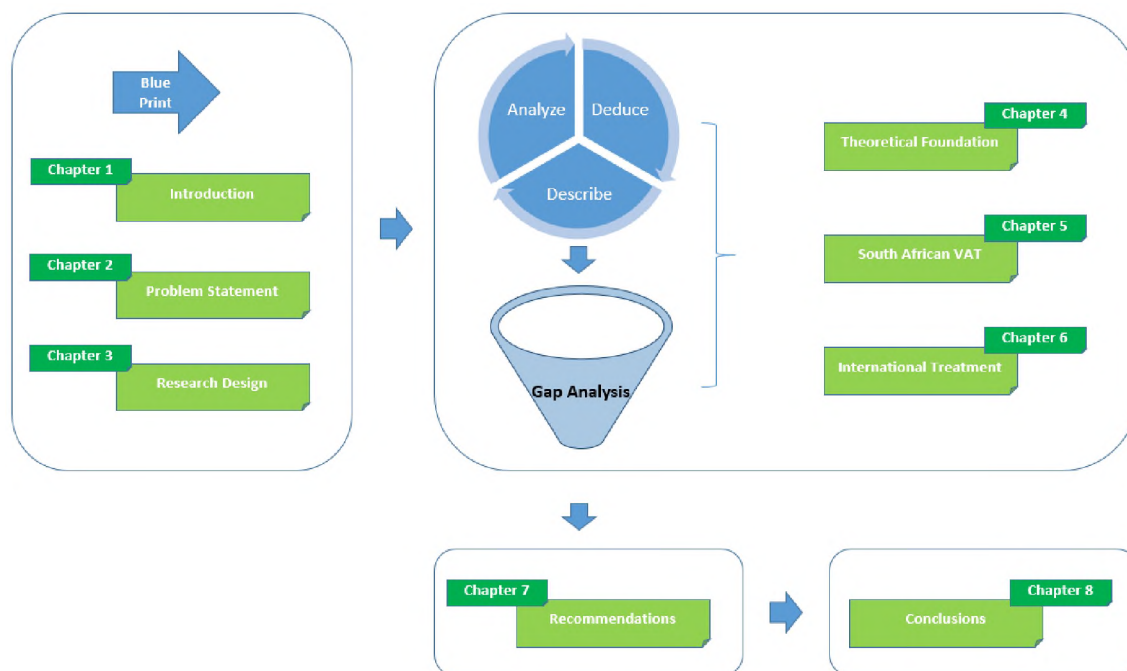
Data will also be collected through the administration of a questionnaire to a purposively selected panel of experts, consisting of various acknowledged South African and global VAT and indirect tax experts. The responses to the questionnaires will be complemented by detailed and carefully documented e-mail correspondence with respondents, to follow up and clarify issues where necessary. A questionnaire, specifically devised for this study, will be used. The research will not apply statistical hypothesis testing and, as such, is qualitative, with an interpretational orientation.

Informed written consent will be obtained from each participant. Approval will also be obtained from all the necessary parties, including the Ethics Committee of Rhodes University.

1.4 OVERVIEW OF CHAPTERS

The main outcomes of the study are presented in the format of a thesis. The structure and flow of the thesis can be illustrated diagrammatically as follows:

Table 1.1: The structure and flow of the thesis



The structure of the thesis is explained and summarised below.

Chapter 1 Introduction

Chapter I provides an introduction and context to the study, sets out the goals of the research, and provides a summary overview of the remaining chapters.

Chapter 2 Problem statement

Chapter 2 discusses the background to and the rationale for the study in the context of prior research undertaken. It briefly sets out the object of the research, and the value of the study in filling a niche in the body of research on the topic. It therefore sets out in detail the problem to be addressed in the research, which forms the basis of the goals set out in chapter 1 and guides the process of the research.

Chapter 3 Research design

Chapter 3 describes the theoretical underpinning of the research design, as it will be applied to the current study, not only as a guide to the researcher in conducting the study, but also as it may contribute to the research and knowledge of future researchers, especially in tax phenomena. It describes the research approach and provides a detailed discussion of the research method undertaken, including the data and the method of analysis and interpretation of the data.

Chapter 4 Theoretical framework of the study

Chapter 4 considers the theoretical basis of taxation, indirect taxation and value-added taxation. The economic nature, principles and consequences of a tax system and more particularly a VAT system receives specific consideration. The description of the shortcomings in the South African VAT system and the conclusions, and recommendations will be made with the theoretical basis in mind. Inter-jurisdictional VAT concepts which are considered include, amongst others, the basis of a consumption tax, double taxation and non-taxation in a VAT system, and the origin and destination principles of taxation. A thorough understanding of these concepts is important in assessing the current South African system and to make recommendations to address identified shortcomings. Chapter 4 sets out to ultimately develop an inter-jurisdictional VAT rule decision framework against which recommendations for the South African VAT system can be measured.

Chapter 5 Inter-Jurisdictional VAT rules in South Africa

Chapter 5 describes the current inter-jurisdictional VAT rules and differentiates specifically with regard to non-residents, the VAT rate applicable to inter-jurisdictional transactions, and imported services. The law should deal with these issues in a manner which results in certainty and simplicity and low cost of administration and compliance, and comply with the other principles of a good tax system, as considered in more detail in Chapter 4. The study seeks to identify shortcomings in the identified inter-jurisdictional VAT rules in the South African VAT system. Chapter 5 relies on a detailed analysis of the legislation and, to some extent, on data collected from the panel of experts who completed the Research

Questionnaire¹. Concepts such as imported services and non-residents doing business with or in South Africa are also considered.

Chapter 6 Inter-jurisdictional VAT rules in selected jurisdictions

Drawing on international experience to assist a country in assessing its own tax system and as a source from which to “borrow” is often used as a fiscal instrument to “sharpen” tax policy. The Margo (1986) and Katz (1994) Tax Commissions have relied extensively on international tax experience in assessing South Africa's tax system and the current South African VAT system is a prime example of exactly that, as it has been largely based and drafted on the New Zealand GST system (Morden, 2007). Chapter 4 considers specific inter-jurisdictional VAT rules used by other countries or country groupings. The OECD recommendations and rules used in Australia, Canada, the EU, and New Zealand are specifically considered. The study differentiates between inter-jurisdictional VAT rules applied to supplies of goods and services and rules determining foreign business VAT registration liability. This is contextualised against the background of the general principles in operation in these VAT systems. The various definitions of goods and services are also considered. The actual inter-jurisdictional VAT rules used in these countries or country groupings will be drawn on to assess whether they could address some or all of the South African identified VAT shortcomings.

Chapter 7 Recommendations

Chapter 7 considers, against the background of the theoretical basis (developed in Chapter 4), the extent to which the inter-jurisdictional VAT rules used in other VAT jurisdictions (considered in Chapter 6) could address some of the identified shortcomings in the inter-jurisdictional rules in the South African VAT system (as identified in Chapter 5). Chapter 7 proceeds by making recommendations on how these identified shortcomings could be addressed by proposing actual law amendments and additions.

Chapter 8 Conclusion

Chapter 8 concludes the study and summarises the findings in the other chapters,

¹ Appendix 1.

explains the contribution and limitations of the study, and makes certain recommendations.

CHAPTER 2: PROBLEM STATEMENT

2.1 INTRODUCTION

Inter-jurisdictional rules in the South African Value-Added Tax (VAT) system have, since the introduction of VAT in 1991, created interpretational difficulties. These difficulties in the inter-jurisdictional space mainly arose in the areas of non-resident VAT registration; application of the inter-jurisdictional VAT rate; imported services; and the implicit place of supply rules. The research sets out to identify and articulate these difficulties, conduct research to address them, and make certain recommendations or conclusions.

The objective of this research is to consider the current inter-jurisdictional rules in the South African Value-Added Tax (VAT) system. This is done with a view to identifying current shortcomings in the system and proposing legislative changes or additions to address these shortcomings. The study considers shortcomings (or the lack thereof) not only in the traditional or so-called place of supply rules (aimed at determining where a supply takes place) but also considers the activities of non-resident businesses with activities or supplies that have a link or connection with South Africa. This is especially important if consumption occurs or could occur in South Africa. The study initially creates a theoretical foundation on which the remainder of the study can build. It also considers the legislation and practical experience in selected countries and country groupings, with a view to applying these principles to address the shortcomings identified in the South African VAT system. The provisions of the South African VAT system governing non-residents, the inter-jurisdictional VAT rate and imported services are considered in detail and analysed in the context of international experience in identifying shortcomings. The research sets out to make recommendations addressing the following:

- non-resident VAT registration;
- the inter-jurisdictional VAT rate;
- imported services; and
- the place of supply rules.

This chapter presents a brief overview of the reason for the research, including research that has been carried out in this context, with a view to developing the problem statement for the research. The review of prior research will also demonstrate the gap in the existing body of knowledge that the present research aims to fill, and therefore its importance and value.

2.2 RATIONALE FOR THE STUDY

Due to an increase in cross-border supplies of goods and services, the determination of the tax incidence and to which jurisdiction tax revenue should accrue have become critical (OECD, 2014c:5-6). Traditionally a supply could safely be assumed to take place at the supplier's location as cross-border supplies were limited. This is no longer the case. As a result, place of taxation proxies to approximate the place of consumption were developed to address these shortcomings. The increase in global trade also required careful crafting of VAT rules relating to non-resident suppliers. VAT systems are designed to tax final domestic consumption, which is generally done by freeing exports from VAT through zero rating whilst allowing related input tax deductions, and imposing VAT on importations (OECD, 2014c:5-6).

The Organisation for Economic Cooperation and Development (OECD) and the European Union (EU) developed consumption tax principles against which these proxies are measured. Proxies to determine consumption differentiate between internationally traded goods and services. Rules for internationally traded services and intangibles differentiate further between business-to-business supplies and business-to-consumer supplies. The OECD and EU developed a set of main rules and recommended certain special rules to deal with these proxies. Australia, Canada, and New Zealand, have all adopted specific inter-jurisdictional VAT rules. Australia's rules mainly use the concept of "connected with Australia" to determine the jurisdictional reach of its VAT system (OECD, 2014b:27). Australian VAT impacts non-residents extensively and requires the remittance of VAT for services performed in Australia, irrespective of whether the customer is a registered business or final consumer (OECD, 2014b:27). Canada adopted provincial and national rules,

where the provincial place of supply rules mainly apply the origin basis (on sales in Canada) and the national place of supply rules, the destination basis. The Canadian provinces generally impose the Harmonised Sales Tax (HST) over and above the national Goods and Services Tax (GST) (Bird and Gendron, 2010:517). New Zealand adopted a different approach to determine the VAT system's inter-jurisdictional reach, based on the residence of the supplier. New Zealand uses a combination of proxies (OECD, 2014b:27).

South Africa replaced its General Sales Tax (GST) with a VAT system in 1991. When VAT was introduced, South Africa was to a large extent still isolated from the world economy. Since the early 1990s, particularly since 1994 when South Africa had its first democratically elected government, the world economy started opening up to South Africa (Schneider, 2000:1). The South African VAT system can, in legal form, be described as a worldwide tax system, which imposes tax on the worldwide supplies of persons (Schenk, 2009:9). This is in contrast to a "territorial" VAT which is imposed only on supplies in the taxing country (Schenk, 2009:9). The South African VAT net spans a substantial area of economic activity and, unlike most foreign VAT jurisdictions, does not have specific place of supply rules (MacKenzie and Kruger, 2009:67). As a result, a South African VAT registered vendor must report all supplies connected with its enterprise, wherever they occur (Schenk, 2009:9).

2.3 OVERVIEW OF PRIOR RESEARCH

A limited number of comprehensive studies on South African inter-jurisdictional VAT rules have been done to date. The VAT sub-committee of the South African Fiscal Association (SAFA) drafted place of activity (as opposed to supply) rules in 2000. These recommendations were never implemented. SAFA proposed defining when an "activity" (as contained in the definition of "enterprise" in section 1(1) of the Value-Added Tax Act, Act 89 of 1991 (the VAT Act)) carried on by a non-resident, will be deemed to be carried on in South Africa (SAFA, 2000b).

SAFA proposed that an activity of a non-resident supplier of goods be deemed to be carried on in South Africa, if that person supplies goods in terms of:

- a sale agreement of goods located in South Africa (not being goods in a licensed customs and excise warehouse), when the agreement is concluded; or
- an agreement for the supply of real rights in movable goods that are located in South Africa, when the agreement is concluded; or
- an agreement for the supply of real rights in fixed property that is located in South Africa; or
- an instalment credit agreement for goods located in South Africa, when the agreement is concluded; or
- a rental agreement, if the goods:
 - are used in South Africa; or
 - comprise of a foreign-going ship or aircraft which is operated by a resident (SAFA, 2000b).

The proviso to the proposal on goods excluded goods which are exempt from tax on importation in terms of section 13(3) of the VAT Act. It also deemed a sale or instalment credit agreement or an agreement for the supply of real rights in movable goods or fixed property, to be concluded at the time when the last party to the agreement accepts the terms and conditions of the agreement (SAFA, 2000b).

SAFA proposed that an activity of a non-resident supplier of services be deemed to be carried on in South Africa to the extent that a person or his agent:

- physically renders or performs services in South Africa; or
- supplies services, not capable of being physically rendered, from a fixed or permanent place in South Africa from where a business is carried on by the supplier or his agent (SAFA, 2000b).

SAFA also proposed that the Commissioner for SARS may, on request, deem any supply of services to be an activity carried on by any person to be supplies made in South Africa (SAFA, 2000b).

Shortcomings of SAFA's approach include:

- South African residents or non-residents can escape VAT registration and the "enterprise" requirements if their activities are deemed not be carried on in or partly in South Africa, although consumption may take place in South Africa;
- but for the proposed "activity" rule, a non-resident entity could be deemed to be carrying on an "enterprise" in South Africa and would have been entitled to zero-rate certain of its supplies and claim input tax deductions in respect of its expenses incurred in South Africa;
- adoption of the "activity" rule may, in certain instances, prevent registration of a non-resident entity in South Africa and deem all of its activities to be outside the South African VAT net, thereby denying the entity the benefits associated with zero-rating;
- SAFA's proposed rules applied only to non-residents, which narrowed the scope considerably, given the breadth of the definition of "resident of the Republic" in section 1(1) of the VAT Act. This limitation arguably rendered the proposed rules superfluous since it only covers the activities of persons that do not fall within the definition of "resident of the Republic". Since the proviso to the definition refers to "any enterprise or other activity", it envisages that such person will comply with one of the requirements of the definition of "enterprise" and that only if the person does not comply with that requirement will the person be regarded as not being a resident. The effect is that the proposed rules dictate when a person's activities will be deemed to be carried on in the Republic, with the knowledge that that person will not be conducting an enterprise in South Africa and as such will never be subject to VAT. This problem could potentially have been solved in one or two manners. Firstly, the proviso to the definition of "resident of the Republic" could be amended not to refer to the carrying on of any enterprise or other activity. The place of activity rules would then refer to "to the extent that such person or company carries on in the Republic any enterprise or other activity and has a fixed or permanent place in the Republic relating to such enterprise or other activity", as phrased in the proviso to the definition of "resident of the Republic". The second alternative would be to incorporate the proviso to the definition of "resident of the Republic" into the definition of

"enterprise".

Deloitte, on invitation by SAFA, commented as follows on the initial place of activity proposals on 31 July 2000 (as drafted by Schneider, 2000):

- place of supply and not place of activity rules should be introduced; the uncertainty regarding what constitutes an "enterprise or activity" should be addressed separately and this can be done by, for example, linking the definition of "enterprise" to the Income Tax concept of permanent establishment through a practice note, or a section 1(1) definition, or by some other means;
- place of supply rules linked to time of supply rules or date of acceptance of contractual conditions is open to manipulation, which is demonstrated by the various amendments to section 11(2) (l) of the VAT Act;
- various countries define goods as the transfer of ownership in tangible property or immovable property, whereas services are defined as any supplies not being supplies of goods; this distinction could be useful in defining place of supply;
- the European Union deems the supply of goods where the goods are dispatched or transported by the supplier, recipient or a third person to be the place where the goods are when the dispatch or transport to the recipient begins;
- if goods are installed or assembled by or on behalf of the supplier, the place of supply is deemed to be where the goods are installed or assembled;
- if goods are not dispatched or transported, the place of supply is deemed to be where the goods are located when the supply takes place;
- if goods are supplied under a sale agreement and placed at the disposal of the recipient in South Africa, the place of supply of the goods should be deemed to be in South Africa;
- if ownership in the goods remains with the foreign enterprise whilst the goods are used by a recipient in South Africa, the foreign enterprise should be required to register as a VAT vendor only if the recipient is a non-registered resident or partially taxable vendor or where the foreign enterprise has a permanent establishment in South Africa or owns fixed property;
- the place of supply of real rights in movable goods, or the supply of goods under an

instalment credit or rental agreement should be determined as if the supply is a supply of services, except where actual ownership of the goods passes;

- if real rights in fixed property are supplied under an agreement, the place of supply should be where the fixed property is located;
- the European Union generally deems the place of supply of services to be the where the supplier established his business or has a fixed establishment from which the service is supplied, or in the absence thereof, the place where he has his permanent address or usually resides, although specific rules also apply;
- the European Union deems the place of supply for certain services, such as services relating to fixed property, intellectual property rights, advertising, transport, hiring out of movable tangible property to be where the supply is used;
- the place of supply of services capable of being physically rendered or services not capable of being physically rendered should be where consumption takes place;
- if the supplier has a permanent establishment in South Africa, irrespective of nationality, the supplier should be liable to account for tax at the standard rate; if the supplier does not have a permanent establishment in South Africa then, irrespective of whether consumption takes place in South Africa, the supplier should not be required to register in South Africa, unless any of the recipients are not fully entitled to an input tax deduction (the compliance burden on SARS in applying the reverse charge mechanism if the supplier has no permanent establishment in South Africa would outweigh the benefits);
- discretion creates an administrative burden for SARS and should be avoided if possible;
- place of supply rules should consider the lack of resources of SARS and any alterations to the VAT Act should endeavour to limit the number of foreign enterprises registering as VAT vendors, except where non-registration would lead to a loss of revenue to the fiscus or to a lack of neutrality;
- place of supply rules should consider the nature of the supply; the place where the goods or services are made available and consumed; the place where the supplier operates his business from; as well as whether the supplier has a permanent establishment in South Africa;
- permanent establishment rules should be considered in designing place of supply rules. Whether the principal supplier operates through a dependent agent (who can

legally bind his principal) or an independent contractor who cannot legally bind the principal supplier should also be considered (Deloitte, 2000).

In conclusion, Deloitte (as drafted by Schneider, 2000) recommended that the following steps be followed to determine the place of supply and also a foreign enterprise's liability to register for VAT purposes in South Africa:

- determine the place of supply: if consumption takes place in South Africa, the place of supply is in South Africa;
- if it has been established that the place of supply is in South Africa, the nature of the supplier and recipient must be determined;
- if the supplier owns fixed property in South Africa, the foreign enterprise must register as a VAT vendor, and no further test is required; or
- if the supplier has a permanent establishment in South Africa, the foreign enterprise needs to register as a VAT vendor, and no further test is required; or
- if the recipient is a non-registered South African person or a partially taxable South African vendor, the foreign enterprise must register as a VAT vendor, and no further test is required; or
- if the recipient is a registered South African vendor, the foreign enterprise does not have to register as a VAT vendor, except if it has fixed property or a permanent establishment in South Africa; or
- if the place of supply is not in South Africa and the foreign enterprise is not a registered VAT vendor as a result of its other supplies, it should not be required to register as a VAT vendor (Deloitte, 2000).

The VAT sub-committee of the South African Institute of Chartered Accountants (SAICA) replaced the VAT subcommittee of SAFA and more recently revisited the need for VAT place of supply rules for South Africa (SAICA, 2009). The SAICA VAT sub-committee has not presented National Treasury with any recommendations on place of supply or place of activity rules.

Some other limited focus place of supply studies have been undertaken on certain place of supply aspects, including those by:

- Schneider (2000) on *introducing VAT place of supply rules in South Africa*, which included a fairly comprehensive theoretical basis of taxation, VAT, consumption taxation, place of supply rules, and an international perspective;
- Krensel (2004), De Wet and Du Plessis (2005), Oosthuizen (2006), and Fryer (2014) on *the VAT treatment of electronic commerce*;
- De Swardt and Oberholzer (2006) on *VAT compliance of digitised products*;
- Van Der Westhuizen (2006) on *place of supply rules, but predominantly those pertaining to telecommunication services*;
- Janse van Rensburg (2011) on *introducing VAT place of supply rules in South Africa*;
- Rourke (2012) on *the VAT implications of interactive gambling in the absence of detailed place of supply rules*;
- Van Zyl (2013a) on *the place of use or consumption of imported services for VAT purposes*;
- Van Zyl (2013b) on *the place of use or consumption for VAT purposes*;
- Van Zyl (2013c) on *the collection of VAT on online cross-border digital goods*;
- Davis Tax Committee: VAT sub-committee (2015b) on, amongst others, *VAT place of supply rules*;
- Schoeman, Steyn, and Homeier (2015) on *VAT on international mobile telecommunication services*; and
- Botha (2015) on *the meaning of “enterprise” in the South African VAT system*.

These studies all, to varying degrees, considered certain aspects of inter-jurisdictional VAT rules, but mainly insofar as they relate to place of supply rules in the South African VAT system. The findings of these studies have not been implemented. None of these studies addressed inter-jurisdictional VAT rules comprehensively and either focused solely on the place of supply aspect, or on the activities of non-resident businesses in South Africa, or on selected aspects of one of these. None of these studies (except for SAFA to some extent) recommended detailed legislative changes.

These studies and observations indicated two broad areas in the VAT system in need of further interrogation and potential revision. These two areas include:

- uncertainty with regard to the VAT registration liability of non-residents; and
- the VAT rate applicable to cross-border supplies, especially supplies of services.

In 2004 the Minister of Finance acknowledged that the South African VAT Act does not have explicit place of supply rules (unlike most international VAT systems) and expressed the need for this to be reviewed to provide certainty with regard to the VAT on international transactions (South Africa, 2004:49). In 2005 National Treasury undertook to clarify VAT place of supply rules to provide certainty with regard to the responsibility and accountability for VAT in the case of certain international transactions (SARS, 2005b:17). Treasury, again in 2006, expressed the need to provide greater clarity in this area, especially for telecommunications, and that due consideration should be given to the work of the OECD in this regard (SARS, 2006b:17).

Various VAT practitioners have also often expressed the need for place of supply rules to create certainty in respect of place of supply or consumption in cross-border transactions. Badenhorst (2007 and 2011), for example, proposed certain place of supply rules in respect of foreign bank fees incurred and potentially consumed in South Africa, in response to the lack of place of supply rules. Glyn-Jones (2006:8) and De Swardt (2011) acknowledged that the lack of place of supply rules gives rise to interpretational difficulties when considering whether a non-resident should register for VAT in South Africa. Parker (2011) observed that the lack of place of supply rules in the South African VAT system, especially in respect of electronic services, clearly illustrates that the VAT system lags well behind international VAT trends. Joubert (2010), in assessing the income tax and VAT implications of “cloud computing”, made a plea for South Africa to introduce place of supply rules.

Although the South African VAT system does not contain specific “place of supply rules”, jurisdictional or place of supply rules can to some extent be inferred through an assessment of the VAT Act. Millar (2011), in assessing the need for place of

supply rules in the South African VAT, observes that

...it is clear that South Africa has extensive place of taxation rules for one side of the place of taxation equation (the zero-rating rules that ensure that consumption outside South Africa is not taxed under the SA VAT).

Millar (2011) makes two comments on linking transactions to a jurisdiction in the South African VAT context, namely:

- South Africa does not "...give the name "place of supply"..."; and
- South Africa essentially only has one rule "...which is embodied in the words "in the Republic" in the definition of "enterprise", which forms an essential element of the imposition of tax on supplies...and of the definition of "imported services" (which also uses "residence")".

Millar (2011) is of also of the view that the notion of "in the Republic" as contained in the term "enterprise" is insufficiently defined, which creates uncertainty.

2.4 IMPORTANCE OF THE STUDY

The importance of the study is illustrated by the fact that the private sector and Government have often in the past pointed to the lack of specific place of supply rules as a particular shortcoming in the South African VAT system. In addition, the certainty with regard to the VAT treatment of cross-border trade and non-resident suppliers has often come under scrutiny.

A comprehensive and sound theoretical basis from which to assess current shortcomings with regard to cross-border transactions and non-resident suppliers, and the review of current legislation and introduction of new inter-jurisdictional rules, including specific place of supply rules in the South African VAT system, will assist the legislator to address these issues. An international perspective on the use of VAT place of supply rules and the success thereof will provide the legislator with the necessary international experience.

Recommending implementable, practical and well considered inter-jurisdictional VAT rules that address current shortcomings will ease implementation by the legislator. This will assist the legislator to address an important tax policy imperative, namely increased certainty in respect of inter-jurisdictional VAT rules in South Africa. Consideration of current shortcomings in the VAT Act and formulation of specific inter-jurisdictional VAT rules will require due consideration of:

- a framework for assessing current shortcomings and reviewing current legislation or including specific inter-jurisdictional rules;
- objectives that need to be achieved against which such assessment and definition should be measured;
- whether such assessment and definition should allow the Commissioner for the South African Revenue Service discretionary powers, or whether it should attempt to be so comprehensive as not to warrant any discretionary powers; and
- whether a general place of supply rule is required in addition to specific place of supply rules.

2.5 CONCLUSION

This chapter has discussed the background to and the rationale for the present study. It has briefly set out the object of the research, the rationale for the study and demonstrated the value of the study in filling a niche in the body of research on the topic. It has therefore set out in detail the problem to be addressed in the research. This problem forms the basis of the goals set out in chapter 1 and guides the process of the research.

The next chapter explains the research methodology and the research process to be followed in addressing the goals of the research.

CHAPTER 3: RESEARCH DESIGN

3.1 INTRODUCTION

This chapter describes the theoretical underpinning of the research design, as it was applied to the current study, not only as it guided the researcher in conducting the study, but also as it may contribute to the research and knowledge of future researchers, especially in tax phenomena. It describes the research approach or paradigm and provides a detailed discussion of the research method undertaken, including the data and the method of analysis and interpretation of the data.

The treatment of inter-jurisdictional VAT rules in a VAT system is described and dealt with extensively in tax literature. This thesis considers the current inter-jurisdictional rules in the South African Value-Added Tax (VAT) system and seeks to identify shortcomings and propose legislative changes or additions to address them. The study considers shortcomings, not only in the traditional place of supply rules, but also considers the activities or supplies of non-resident businesses with a link or connection to South Africa. The study initially creates a theoretical foundation on which the remainder of the study can build. It also considers the legislation and practical experience in selected countries (namely Australia, Canada, and New Zealand) and country groupings (namely the European Union (EU), and the Organisation for Economic Cooperation and Development (OECD)), to apply these principles to address the shortcomings identified in the South African VAT system. The provisions of the South African VAT system governing non-residents, the inter-jurisdictional VAT rate and imported services are considered in detail and analysed in the context of international experience in identifying shortcomings. The study sets out to make recommendations addressing the following inter-jurisdictional VAT rules:

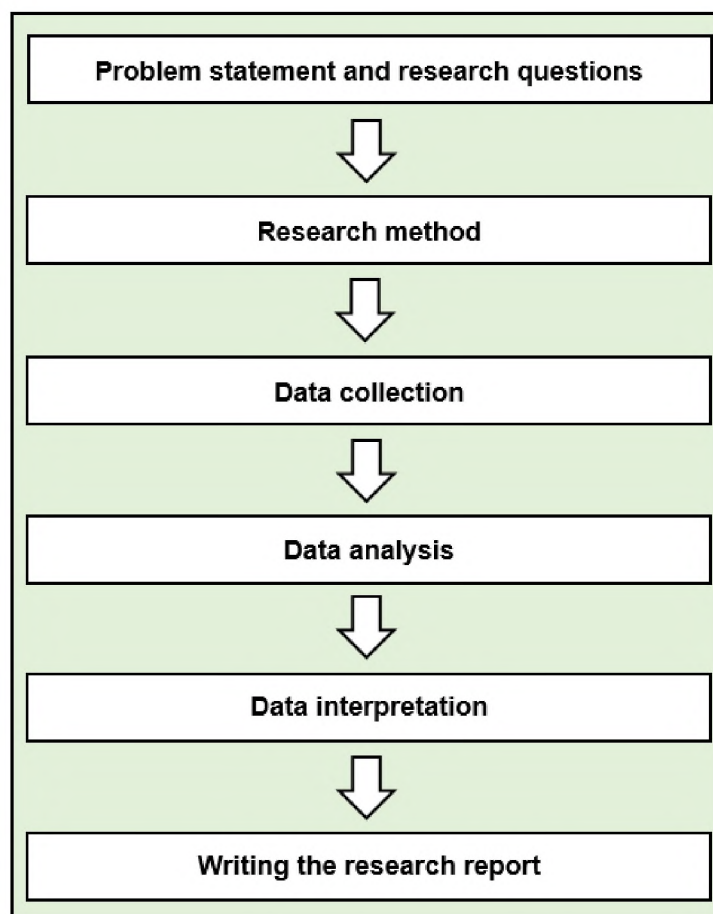
- non-resident VAT registration;
- the inter-jurisdictional VAT rate;
- imported services; and
- the place of supply rules.

The study will attempt to provide the legislator with specific technical and practical recommendations on inter-jurisdictional VAT rules.

3.2 RESEARCH PROCESS

Authors differ on the number of phases of the research process: some authors identify eight phases whilst others distinguish five or six phases (Strydom, 2011). The research process is illustrated in Table 3.1 below.

Table 3.1: The research process



Source: Strydom, 2011:5

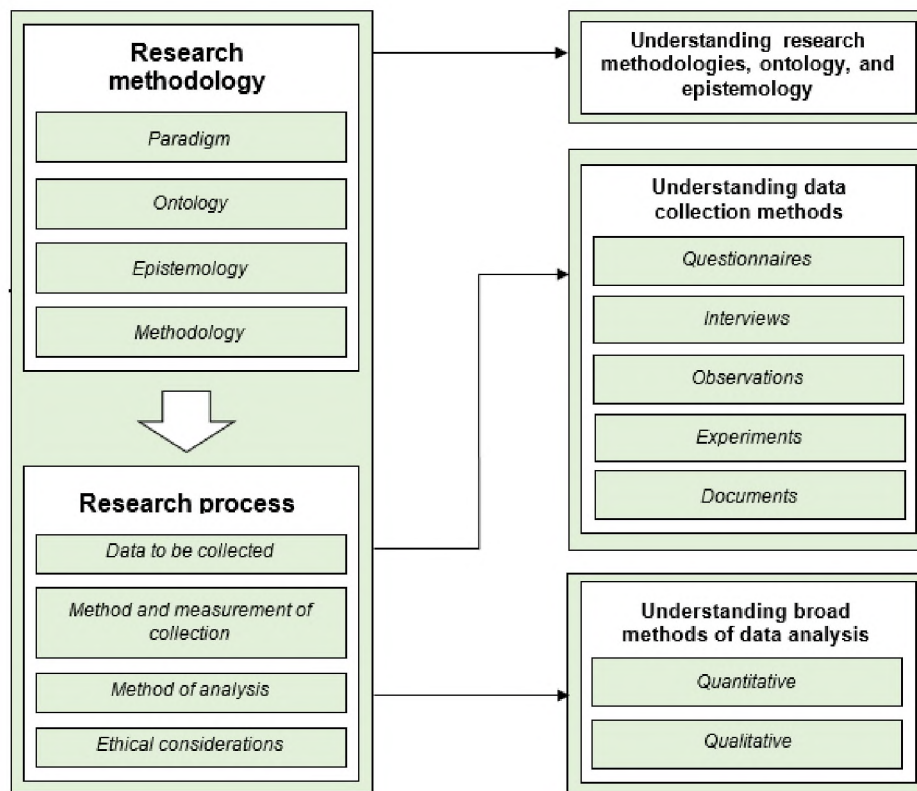
The problem statement and the goals and sub-goals of the research have been outlined briefly in chapter 1 and the literature review in chapter 2 provides a more detailed discussion of prior research carried out on the topic of the present research,

in order to identify the gap or niche that the present research attempts to fill, and therefore its relevance.

The first step in the research process of this study entailed a detailed review of available literature to establish the theoretical basis of a good tax system, the theory underpinning indirect taxation and more specifically consumption taxation. The literature review also included an in-depth analysis of the South African VAT system, particularly with regard to the treatment of resident *versus* non-resident businesses with a South African physical or economic reach, and its treatment of local and cross-border transactions, including imported services. The literature review also considered the VAT treatment of non-residents in selected foreign jurisdictions, the treatment of cross border transactions and the use of inter-jurisdictional VAT rules to reduce interpretational uncertainty.

The remainder of this chapter is dedicated to a critical descriptive analysis of the research design used in this study. The research design requires the researcher to decide on a suitable research methodology to be used to address the stated goals of the research. The design of the research process includes a consideration of the data to be collected; the method of collection and measurement of the data; the method of analysing the data; and ethical considerations (Stack, 2012). The research design is illustrated in Table 3.2 below.

Table 3.2: The research design



Source: Own formulation, based on Stack, 2012:27

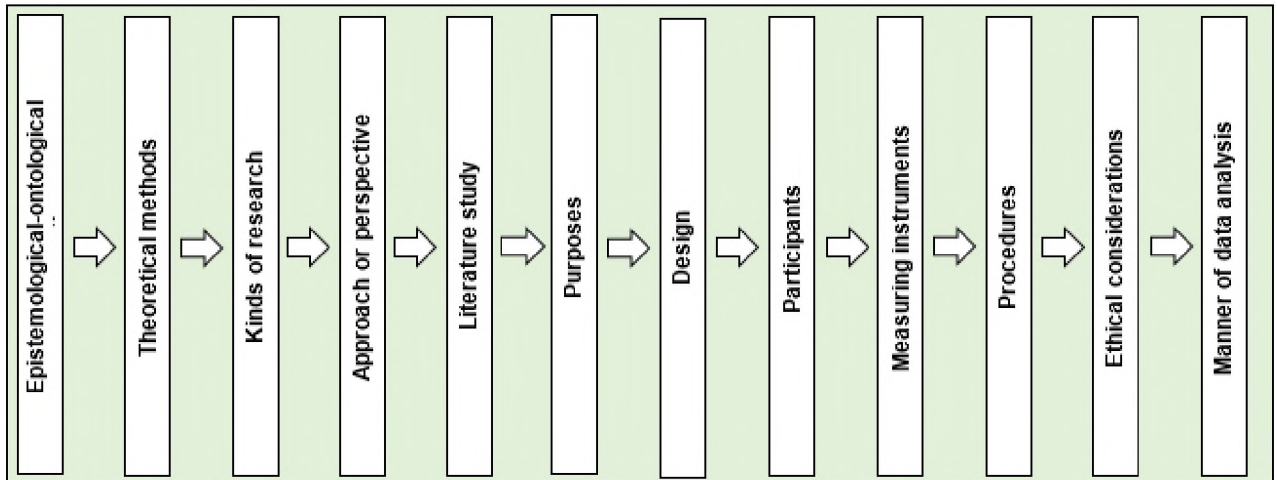
A detailed theoretical description of research design and how this was used to develop and describe the research carried out in this study is set out below.

3.3 RESEARCH METHODOLOGY

The term “research methodology” refers to the systematic manner in which a research problem is solved. It can be explained as a “science of studying how research is done scientifically” and involves various steps and methods that a researcher adopts in investigating a research problem, and the logic behind them. It includes not only the study of the methods used but also an explanation and justification of why certain research methods are used. Research methodology includes the philosophy of the entire research process and essentially is a set of rules or procedures to conduct research (Vibhute and Aynalem, 2009).

Table 3.3 below describes the research method applying in the research process.

Table 3.3: The research method



Source: Strydom, 2011: 8

Each of these components of the research method depicted in Table 3.3 is discussed below, together with the application to the present research.

3.3.1 Epistemological-ontological approach

This section describes the following associated components of the research method as depicted in Table 3.3 above:

- epistemological-ontological approach;
- theoretical methods;
- kinds of research; and
- the approach or perspective.

Research can be approached in a number of ways. Examples of research approaches (or paradigms) include:

- positivist, post-positivist or empirical research;
- interpretative research, also referred to as phenomenology;
- critical research; and

- post-structural research (Stack, 2012:28-29).

The researcher is required to document the epistemological-ontological assumptions that will be used for the study (Strydom, 2011).

To describe the research methodology in scientific terms requires an understanding of a number of research terms frequently used by researchers for this purpose. The broad research terminology is defined in Table 3.4 below.

Table 3.4: Definitions of research terms used in this study

	Definition
Paradigm	<i>A basis belief system based on ontological, epistemological, and methodological assumptions.</i>
Ontology	<i>A "world view" and particularly answering the question: What is the form and nature of reality?</i>
Epistemology	<i>The theory of knowledge and particularly answering the question: What is the relationship between the researcher and what is not known?</i>
Methodology	<i>Answers the question: What should the researcher do to establish what he/she believes can be known?</i>

Source: Stack, 2012:30

Research paradigms can be divided into two broad categories, namely positivist or post positivist or empirical; and non-empirical or interpretative (Stack, 2012). The ontology, epistemology, and methodology of these research paradigms is summarized in Table 3.5 below:

Table 3.5: Ontological-epistemological-methodological analysis of the research paradigms

	Ontology	Epistemology	Methodology
Positive/ post-positivist/ empirical	<i>Assumes a stable external reality which is “out there” and is rational and observable – “law” like.</i>	<i>Truth can be discovered by an objective detached observer.</i>	<i>Empirical, quasi-experimental, hypothesis-testing, quantitative.</i>
Interpretative	<i>An internal reality of shared experience, “truth” is a process of agreement; reality is a construct of mankind; created through shared cultural and social practices and shared beliefs. Multiple realities or understandings are created.</i>	<i>Observer inter-subjectivity, empathetic, observer closeness to the subject may affect what is observed.</i>	<i>Interactive, interpretative, and qualitative.</i>
Critical	<i>Truth is teleological (inherent in history), a socially constructed reality.</i>	<i>Observer-constructed versions, suspicious, political.</i>	<i>Deconstruction and textual analysis.</i>
Post-structural	<i>Worlds are created through language, discourses, plural, shifting realities</i>	<i>Transactional / subjective created findings</i>	<i>Discourse analysis</i>

Source: Stack, 2012:31-33

The present research can be categorized as falling within the interpretative paradigm for the following reasons.

- The ontological assumption underlying the research is that taxation represents a social phenomenon, where “truth” as represented in taxation law is a construct of the citizens of a particular country created through their shared cultural and social practices.
- The epistemological approach involves a process in which the researcher cannot claim to be wholly objective or detached, as the lens through which the tax law is interrogated is influenced by the researcher forming part of this community.
- The methodology to be adopted is interactive (in terms of the interviews with experts, based on a structured questionnaire), interpretative (in terms of the documentation and analysis of the questionnaire responses and the legislation applying to the “place of supply” rules in VAT legislation) and qualitative (as the analysis of the data is performed by way of natural language reasoning and the results expressed in words).

This study adopts an interpretative post-positivist research paradigm as it seeks to understand, describe, design, and criticise the VAT consequences of inter-jurisdictional transactions and activities (Babbie and Mouton, 2009). The research also includes a comparative perspective, with a view to proposing reforms to the South African VAT system.

Research types

Research comprises of various types, which typically includes descriptive and analytical research; applied and fundamental research; quantitative and qualitative research; and conceptual and empirical research (Vibhute and Aynalem, 2009). The research types are briefly described below.

Descriptive versus analytical research

Descriptive research describes the state of affairs as it exists, through description of the phenomenon and its characteristics and reports on what has transpired or is transpiring. Descriptive research does not analyse the causes of the phenomenon, whereas analytical research entails the critical evaluation of facts and information to produce a critical exposé of what was researched (Vibhute and Aynalem, 2009).

The present research is both descriptive and analytical. The existing legislation and the principles established in case law is initially described in various chapters. This data is then analysed with a view to pointing out problems or omissions and suggesting possible solutions.

Applied versus fundamental research

The objective of applied or action research is to derive a solution for an immediate problem through viewing the research in a practical context. Fundamental research concerns itself with the generalisation and formulation of theory, without being concerned with the practical context or use of the research (Vibhute and Aynalem, 2009).

The present research, with its objective of suggesting a solution to the practical problems relating to the inter-jurisdictional VAT rules in existing tax law, can be categorised as applied research.

Quantitative versus qualitative research

Quantitative research is based on a quantum and applies to a phenomenon that can be expressed in terms of the quantum. Quantitative research is therefore concerned with the scientific investigation of quantitative properties of a phenomenon and their inter-relatedness. The objective of quantitative research is to develop mathematical models, theories, and hypotheses in respect of the phenomenon being researched. The process of measurement is therefore essential to this research as it provides the fundamental relationship between empirical observation and mathematical expression of the quantitative relationship

Qualitative research, to the contrary, is concerned with qualitative phenomena, involving quality or kind. Unlike quantitative research, qualitative research relies on reason (Vibhute and Aynalem, 2009).

The researcher then needs to decide whether the study will apply a qualitative, quantitative, or a mixed method approach. In a quantitative paradigm study, the literature study precedes the empirical study, whilst in a qualitative paradigm study the literature study follows the empirical study, (the so-called literature control) (Strydom, 2011). The research methodology adopted in this study can be described as predominantly qualitative and the research method as doctrinal research. This established method provides an orderly exposition of the rules directing a particular legal category (in this study: the legal rules relating to the VAT consequences of inter-jurisdictional transactions and activities), analyses the interaction between these rules, explains areas of complexity, and is based entirely on documentary data (McKerchar, 2008).

Conceptual versus empirical research

Conceptual research relates to an idea or theory and is generally applied by philosophers and thinkers to develop new concepts or re-interpret existing ones. Empirical research, on the other hand, relies only on experience or observation (Vibhute and Aynalem, 2009). The present research, in the phase where a theoretical basis is developed for the purpose of designing a good tax system, represents conceptual research.

Basic, applied or integrated

It is necessary to determine the kind of research carried out, namely whether it is basic, applied, or integrated. Most social work research is done on an integrated level as social work research integrates theory and practice. As it has been argued above that the present research adopts the assumption that taxation is a social phenomenon; the kind of research adopted in this study can be described as integrated research, combining the theory and practice of taxation and in particular, indirect taxation.

Legal research

Legal research is broadly categorized into doctrinal legal research and non-doctrinal legal research. Doctrinal research can be defined as research into legal principles, rules, or doctrines through analysis of statutory provisions and case law by applying reason. Non-doctrinal research, on the other hand, can be defined as research into the relationship of law with other behavioural sciences and gives prominence to the interaction of law with people, social values, and social facts. Non-doctrinal research involves empirical research into the operation of the law. It researches the inter-relatedness between human behaviour and law. Doctrinal research is therefore “study in law” whereas non-doctrinal research is “research about law” (Vibhute and Aynalem, 2009). Legal research includes:

- Doctrinal research, which is research into legal rules, principles, concepts, and

doctrines. It involves a rigorous exposition, analysis, and critical evaluation of legal rules, principles, concepts, and doctrines and their inter-relatedness;

- Theoretical research, which is an inquiry into conceptual bases of legal rules, principles and doctrines, and stimulates and provides the intellectual framework for empirical research and advancements in law through legislative, judicial, and administrative processes;
- Empirical research, which is an assessment of the impact of law, reveals the gap between legal idealism and social reality. The researcher, in perceiving the law as a social phenomenon, explores the social, political, economic, and cultural dimensions or implications of law; and
- Reform oriented research, which, based on empirical study and critical evaluation of law, recommends changes in law and legal institutions (Vibhute and Aynalem, 2009).

The present research is a combination of:

- doctrinal research, where research deals with the legal rules, principles, concepts and doctrines relating to VAT legislation;
- theoretical research, where an inquiry is conducted into conceptual bases of a “good” legal system; and
- reform oriented research, where the existing law relating to the inter-jurisdictional rules in VAT legislation is critically evaluated and changes recommended.

3.3.2 Literature study

The literature study in the present research was documented in a number of chapters in the thesis and comprised the following:

- a brief review of existing research in the field of the present research, with the purpose of demonstrating the gap in the body of knowledge that the present

research aims to fill (chapter 2):

- the development of the theoretical framework to be used as a basis for the study, based on the philosophical work of acknowledged experts in the field, including the meaning of taxation, the composition of a tax system and the modern properties underpinning a “good” tax system (chapter 4);
- a detailed discussion of the VAT rules presently applying in South Africa (chapter 5); and
- a detailed discussion of the VAT rules presently applying in selected foreign jurisdictions (chapter 6).

3.3.3 Purpose of the research

With regard to the purpose of the research included in Table 3.3 above, four research purposes are generally distinguished, namely exploratory; descriptive; explanatory; and evaluative (Strydom, 2011). A combination of all four purposes are used in a study, or even all four purposes, separately. Explorative purpose research generally focuses on the “what” questions, whilst the descriptive purpose research generally focuses on the “how” and “who” questions. Explanatory purpose research generally answers the “why” questions and seeks to identify the causes and effects of human behaviour, and is generally experimental in nature. Evaluative purpose research focuses on program or practice evaluation and seeks to determine the effects of social policies, programs and interventions and essentially encompasses the other three purposes.

The present research addresses all four purposes – it has an initial exploratory component, followed by a descriptive and explanatory purpose, culminating in an evaluative purpose of critically evaluating existing legislation in order to make recommendations for its improvement.

3.3.4 The research design

The research methodology (referred to in Table 3.3 above) describes the design of the research and refers to the methods, techniques, or tools, which are used by a

researcher to conduct research. Research methods can be categorized into:

- data collection methods (if the available data is insufficient to derive the required solution);
- statistical techniques (used to establish relationships between the data and the unknowns); and
- evaluation methods to verify the accuracy of results obtained (Vibhute and Aynalem, 2009).

Research design seeks to plan or specify as clearly as possible what the researcher wants to establish and the best manner in which this can be achieved (Strydom, 2011).

Referring to Table 3.3 above, this section discusses:

- the data,
- the participants,
- the measuring instruments,
- the procedures, and
- the manner of analysis.

In describing the research process, the data and how it is collected, the nature of the participants and how they are selected, the measuring instruments and procedures to be used in the research and the manner in which the data generated by the research will be analysed, must be set out in detail.

Data collection and measurement

The various sources of information or data can be categorised into primary, secondary, and tertiary sources. Primary sources of information are those sources that contain original information and observations. Secondary sources of information furnish the information obtained and derived from primary sources of information. Secondary sources of information categorise, structure, or organise the information

in a systematic and planned manner. Tertiary sources list information such as directories and subject guides. The nature of the data collected and methods of collection used in this study are discussed below:

Collection of primary and secondary data

The data collected through the literature review of taxation theory primarily comprised secondary data, owing to the nature of theoretical tax data. The data collected through the literature review of the inter-jurisdictional VAT rules of South Africa and the selected country and country grouping VAT systems mainly comprised primary data, as primary data is generally more readily available given that it is found in legislation and case law. The data collected through the structured questionnaire was primarily secondary data interpreted by the respondents from primary data, namely the letter of the law.

In an exploratory phase of the research, data was collected through interviews with participants consisting of various South African and international VAT and indirect tax experts, using a questionnaire specifically developed for this study, as basis. These interviews were complemented and validated by a detailed and carefully documented e-mail correspondence with respondents. As the study does not apply statistical hypothesis testing but is qualitative with an interpretational orientation, the interviews and e-mail responses were analysed into themes, in order to be incorporated into the chapter dealing with the South African VAT system.

The researcher selected South African and international experts on VAT, indirect and fiscal economics as participants to assist in the explorative phase of the research. The participants selected comprised 12 South African and five global VAT and indirect tax experts. The participants were selected in order to obtain data from experts in the field of VAT, indirect taxes, and fiscal economics and to apply their experience and insights in VAT and more specifically to address the shortcomings in the inter-jurisdictional VAT rules of South Africa.

South African participants

The South African participants (12 in total) were selected to complement the researcher's own understanding and to use as sounding board for the South African technical component of the study, and to assist in the explorative phase of the study, in defining the current problems, gaps or shortcomings experienced with regard to inter-jurisdictional VAT rules in South Africa. Limiting the South African participants to 12 does not purport to represent the full potential population of experts.

The South African participants were selected from VAT experts at the big four audit firms (Ernst and Young (EY); Deloitte; KPMG; and PricewaterhouseCoopers (PWC)), selected medium size audit firms (BDO; Grant Thornton; PKF; and Mazars), selected recognised South African law firms (Edward Nathan Sonnenbergs; Webber Wentzel; Cliffe Dekker Hofmeyr; and Werksmans), the South African Revenue Service (SARS) and National Treasury.

The South African participants were selected if they complied with three or more of the following criteria:

- having specialised in or consulted on VAT, indirect taxes, or fiscal economics for at least ten years;
- having completed specialised VAT, indirect tax, or fiscal economics studies or having obtained a qualification in VAT, indirect taxes, or fiscal economics;
- a specialist at a senior level in VAT, indirect taxes, or fiscal economics at one of the selected categories;
- having published extensively on VAT, indirect taxes, or fiscal economics;
- having presented widely on VAT, indirect taxes, or fiscal economics; and
- a member of the South African Institute of Chartered Accountants (SAICA) or the South African Institute of Tax Practitioners (SAIT) VAT sub-committees.

The South African VAT, indirect taxes, or fiscal economics experts selected who agreed to participate in the study, in alphabetical order of first name, are reflected in Table 3.6 below.

Table 3.6: South African participants in the interviews

	Participant	Brief Curriculum Vitae
1	<i>Andre Meyburgh</i>	Director at KPMG, member of SAIT VAT sub-committee, VAT specialism exceeds ten years, published extensively on VAT, presented widely on VAT
2	<i>Antoinette Prinsloo</i>	Associate Director at Deloitte, member of SAICA VAT sub-committee, VAT specialism exceeds ten years, presented widely on VAT
3	<i>Charles de Wet</i>	Director at PWC, VAT specialism exceeds ten years, published extensively on VAT, presented widely on VAT
4	<i>Christo Theron</i>	Director at BDO, member of SAICA VAT sub-committee, VAT specialism exceeds ten years, published extensively on VAT, presented widely on VAT
5	<i>Cliff Watson</i>	Director at Grant Thornton, VAT specialism exceeds ten years, published extensively on VAT, presented widely on VAT
6	<i>Elsa Rudolph</i>	Associate Director at BDO, member of SAICA VAT sub-committee, VAT specialism exceeds ten years, published extensively on VAT, presented widely on VAT
7	<i>Geraldine Connell</i>	Director at Deloitte, member of SAICA VAT sub-committee, VAT specialism exceeds ten years, published extensively on VAT, presented widely on VAT
8	<i>Gerhard Badenhorst</i>	Director at ENS, member of SAICA VAT sub-committee, VAT specialism exceeds ten years, published extensively on VAT, presented widely on VAT
9	<i>National Treasury (collective response led by Seelan Moonsamy)</i>	Seelan Moonsamy (Team Leader): Director at National Treasury: Legal Policy Indirect Taxes, VAT specialism exceeds ten years, presented widely on VAT
10	<i>Richard Chauke</i>	Senior SARS official, VAT specialism exceeds ten years, presented widely on VAT
11	<i>Trevor van Heerden</i>	Specialist consultant to SARS, ex Commissioner for SARS, presented widely on VAT, VAT specialism exceeds ten years, published extensively on VAT
12	<i>Victor Terblanche</i>	Director at VATIT, presented widely on VAT, VAT specialism exceeds ten years, published extensively on VAT

International participants

The international participants (five in total) were selected on the same basis as the South African participants to provide input into the international comparative analysis of the study, and to assist in the final stages of the study, by contributing to applying international and theoretical experience in considering potential solutions to address South African inter-jurisdictional VAT rule problems, gaps or shortcomings. Some of the global participants were chosen as they also have extensive South African VAT knowledge, which could contribute to the South African technical component of the study as well. The selected five global participants do not purport to comprise the total potential population of international experts.

The global participants were selected from a universe of experts identified through a high-level literature survey of experts who regularly publish or present on VAT,

indirect taxes and fiscal economics, and referrals by experts already identified. The global experts on the panel were selected if they complied with three or more of the following criteria:

- having specialised in VAT, indirect taxes, or fiscal economics for at least ten years;
- having completed VAT, indirect tax, or fiscal economic studies or having obtained a qualification in VAT, indirect taxes or fiscal economics;
- a specialist at a senior level in VAT, indirect taxes, or fiscal economics at a recognised audit firm, law firm or university;
- having published extensively on VAT, indirect taxes or fiscal economics; and
- having presented widely on VAT, indirect taxes, or fiscal economics.

The international VAT, indirect tax, or fiscal economics experts selected who agreed to contribute to the study, in alphabetical order of first name, are reflected in Table 3.7 below.

Table 3.7: International participants in the interviews

	Participants	Brief Curriculum Vitae
1	<i>Alan Schenk</i>	Professor at Wayne State University, VAT or indirect tax specialism exceeds ten years, published extensively on VAT, presented widely on VAT
2	<i>Andra Glyn-Jones</i>	Director at Deloitte New Zealand, VAT specialism exceeds ten years, published extensively on VAT, presented widely on VAT
3	<i>Frank Nellen</i>	VAT Advisor at KPMG Netherlands, researcher at Maastricht University, VAT specialism exceeds ten years, published extensively on VAT
4	<i>Ian Blakeley</i>	Director at EY New Zealand, VAT specialism exceeds ten years, published extensively on VAT
5	<i>Rebecca Millar</i>	Associate professor at University of Sydney, VAT specialism exceeds ten years, published extensively on VAT, presented widely on VAT

Structured questionnaire

Questionnaires are useful as they determine attitudes and opinions, which enable the researcher to identify and describe the variability of the different phenomena (Saunders et al, 2012). A disadvantage of using a questionnaire is that it relies on

self-report data. In other words, respondents answer what they believe to be true or what they believe the researcher wants to hear (Leedy and Omrod, 2010:188). As the purpose of this exploratory phase of the research was specifically to obtain the opinions of the participants to supplement and support the researcher's own analysis of the problem, any disadvantage posed by the responses is likely to be negligible.

The internal validity of the questionnaire used in the exploratory phase of the research was assessed against a guideline used to design surveys or questionnaires on tax research, published by McKerchar (2008; obtained from De Vaus, 1990). In designing the questionnaire, the researcher attempted, as far as possible, to adhere to the following guidelines:

- language should be kept simple and free of jargon and technical terms;
- questions should be phrased to be as short as possible;
- questions should refrain from being double-barrelled;
- questions should not lead a participant to respond in a certain way;
- respondents should have the necessary knowledge to answer the questions;
- words used in the questionnaire should have the same meaning for everyone;
- questions should not artificially create opinions; and
- questions should not be ambiguous.

The questions included in the questionnaire are included as [Appendix 1](#).

Data analysis

The data generated by the interrogation and analysis of South African tax law relating to VAT and the tax law applying in the selected jurisdictions was presented in chapters 5 and 6.

With regard to the data obtained from the participants responding to the questionnaire, the researcher did not set out to simply present the data collected, but undertook an immersion process of repeated analysis and synthesis of the data.

Such immersion can be described as a process whereby the researcher engages in the data collected by reading or examining a portion or all of the data (Borkan, 1999). The immersion process allowed the data to develop structure as a step in the comprehensive understanding of the issue, the field, and the data (Flick, 2007). The result of the analysis and synthesis was not presented in a separate chapter in this thesis, but was used and integrated into the discussion of the legislation to enhance the description of the inter-jurisdictional VAT rules in South Africa and identify the current shortcomings (chapter 5).

3.3.5 Ethical considerations

This study used or generated two sources of data:

- data flowing from the literature reviews in chapters 2, 4, 5 and 6; and
- data generated through the interviews (that was integrated into chapter 5).

The data from the literature reviews are all in the public domain and therefore no ethical considerations relate to the use of this data.

Specific ethical procedures were followed in respect of the participants selected to respond to the structured questionnaire used as a research instrument in this study. In the case of research involving human subjects, most ethical issues in research fall into one or more of four categories, namely protection from harm, informed consent, the right to privacy and honesty with professional colleagues (Leedy and Omrod, 2010:101). The structured questionnaire relied mainly on the participants' informed consent. The researcher obtained written consent from all respondents before completion of the structured questionnaire, including their consent to reveal their names and the capacity in which they responded to the interview questions. The letter of consent, entitled "Consent for participation in a research study", is included as Appendix 2.

The researcher also obtained approval from the Research Ethics Committee of the University, before the fieldwork commenced. The ethical clearance is included as Appendix 3.

A researcher should evaluate his/her own conduct against ethical guidelines (de Vos et al, 2008:57). For the purpose of the present study, this implied, firstly, that the work of others was acknowledged by providing a full and accurate reference where their work was cited. The second implication is that the data was dealt with honestly. The researcher strove to avoid any form of bias in presenting and analysing the data and approached the research as objectively as possible. It is acknowledged that in any research relating to taxation, there may be an inherent bias on the part of the researcher against the Revenue Authority. The researcher was aware of this and did not permit this to cloud his judgement.

3.4 RELIABILITY AND VALIDITY

The researcher needs to ensure the validity and reliability of a research instrument, such as the structured questionnaire used in the present research. The validity of a qualitative study is measured against the proper collection and interpretation of the data to ensure that the conclusions accurately reflect the real world that formed the focus of the study (Yin, 2011:78). To enhance the validity of the data, interpretations, and conclusions relating to the current structured questionnaire, the following measures were taken:

- the questionnaire introduced the focus of the study and questions meticulously ;
- the questions contained detailed references to the primary source/s of data; and
- the inter-relatedness of the various questions was highlighted as far as possible to enhance understanding.

The reliability and validity of the results of the analysis and interpretation of the data – the interview responses and the provisions and principles of tax law – was ensured by presenting the relevant data and analysis completely and accurately, thus ensuring that the research can be replicated by other researchers.

3.5 CONCLUSION

This chapter provided a critical description of the research design. This thesis considers the current inter-jurisdictional rules in the South African Value-Added Tax (VAT) system and seeks to identify shortcomings and propose legislative changes or additions to address non-resident VAT registration; the inter-jurisdictional VAT rate; imported services; and the place of supply rules. The problem statement and the goals and sub-goals of the research have been outlined briefly in chapter 1 and the literature review in chapter 3 provides a more detailed discussion of prior research carried out on the topic of the present research, in order to identify the gap or niche that the present research attempts to fill, and therefore its relevance.

The first step in the research process of this study entailed a *detailed review of available literature* to establish the theoretical basis for this study. The literature review also included an in-depth analysis of the South African and selected foreign jurisdictions' VAT treatment of resident *versus* non-resident businesses, the treatment of local and cross-border transactions, and imported services, to reduce interpretational uncertainty in the South African VAT system. The *literature study* was documented in a number of chapters in the thesis. The present research addresses all four research purposes – it has an initial *exploratory* component, followed by a *descriptive and explanatory* purpose, culminating in an *evaluative* purpose of critically evaluating existing legislation in order to make recommendations for its improvement. The data collected through the literature review of taxation theory primarily comprised *secondary data*. The data collected through the literature review of the inter-jurisdictional VAT rules of South Africa and the selected country and country grouping VAT systems mainly comprised *primary data*. The data collected through the structured questionnaire was primarily secondary data interpreted by the respondents from primary data.

This study adopts an *interpretative post-positivist research paradigm* as it seeks to understand, describe, design, and criticise the VAT consequences of inter-jurisdictional transactions and activities (Babbie and Mouton, 2009). The research also includes a *comparative perspective*, with a view to proposing reforms to the

South African VAT system. The research is both *descriptive and analytical* and can be categorised as *applied research*. The *research methodology* adopted in this study can be described as *predominantly qualitative* and the *research method* as *doctrinal research*. The research, in the phase where a theoretical basis is developed for the purpose of designing a good tax system, represents *conceptual research*. This study adopts *integrated research*, combining the theory and practice of taxation and in particular, indirect taxation. The research is a combination of *doctrinal research; theoretical research; and reform oriented research*.

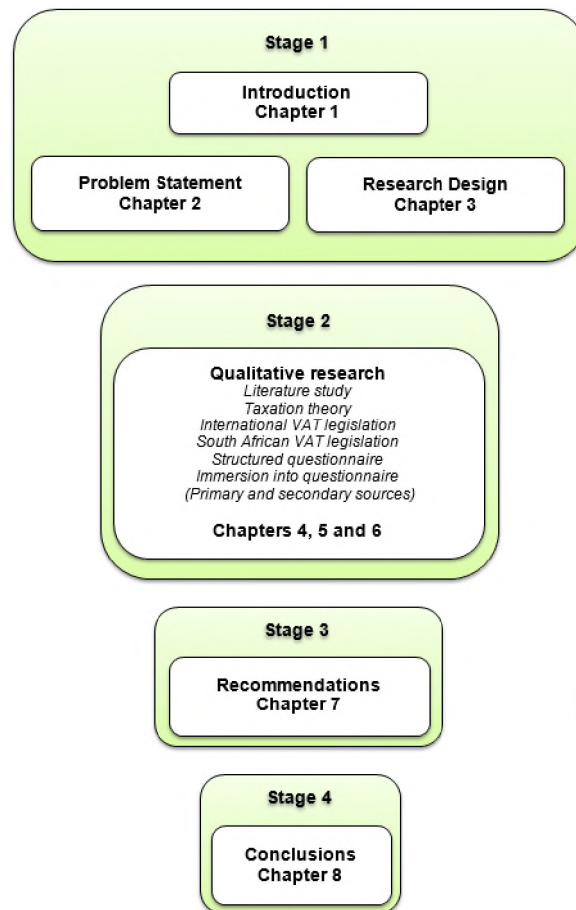
In an exploratory phase of the research, data was also collected through *interviews with participants* consisting of various South African and international VAT and indirect tax experts, using a questionnaire specifically developed for this study, as basis. These interviews were complemented and validated by a detailed and carefully documented e-mail correspondence with respondents. As the study does not apply statistical hypothesis testing but is qualitative with an interpretational orientation, the interviews and e-mail responses were analysed into themes, in order to be incorporated into the chapter dealing with the South African VAT system. The researcher selected South African and international experts on VAT, indirect tax and fiscal economics as participants to assist in the explorative phase of the research. The participants were selected in order to obtain data from experts in the field of VAT, indirect taxes, and fiscal economics and to apply their experience and insights in VAT and more specifically to address the shortcomings in the inter-jurisdictional VAT rules of South Africa. The *internal validity of the questionnaire* used in the exploratory phase of the research was assessed against a guideline used to design surveys or questionnaires on tax research, published by McKerchar (2008; obtained from De Vaus, 1990). The researcher did not set out to simply present the data collected through the questionnaire, but undertook an *immersion process* of repeated analysis and synthesis of the data. The immersion process allowed the data to develop structure as a step in the comprehensive understanding of the issue, the field, and the data (Flick, 2007). The result of the analysis and synthesis was not presented in a separate chapter in this thesis, but was used and integrated into the discussion of the legislation to enhance the description of the inter-

jurisdictional VAT rules in South Africa and identify the current shortcomings (chapter 5).

Specific *ethical procedures* were followed in respect of the participants selected to respond to the structured questionnaire used as a research instrument in this study. The researcher obtained *written consent* from all respondents before completion of the structured questionnaire or eliciting responses, including their consent *to reveal their names and the capacity in which they responded* to the interview questions. The researcher also obtained *approval from the Research Ethics Committee of Rhodes University*, before the fieldwork commenced. A researcher should *evaluate his/her own conduct against ethical guidelines* (de Vos et al, 2008:57). This implied, firstly, that the *work of others was acknowledged* by providing a full and accurate reference where their work was cited. The second implication is that the data was dealt with *honestly*. The researcher strove to *avoid any form of bias* in presenting and analysing the data and approached the research as objectively as possible. It is acknowledged that in any research relating to taxation, there may be an inherent bias on the part of the researcher against the Revenue Authority. The researcher was aware of this and did not permit this to cloud his judgement. The researcher needs to ensure the *validity and reliability of a research instrument*, such as the structured questionnaire used in the present research. The validity of a qualitative study is *measured against the proper collection and interpretation of the data* to ensure that the conclusions accurately reflect the real world that formed the focus of the study (Yin, 2011:78). To enhance the validity of the data, interpretations, and conclusions relating to the current structured questionnaire, the questionnaire introduced the focus of the study and questions meticulously; the questions contained detailed references to the primary source/s of data; and the inter-relatedness of the various questions was highlighted as far as possible to enhance understanding. The reliability and validity of the results of the analysis and interpretation of the data – the interview responses and the provisions and principles of tax law – was ensured by *presenting the relevant data and analysis completely and accurately, thus ensuring that the research can be replicated by other researchers*.

To place the present chapter in context and the link with chapters to follow, Table 3.8 below illustrates the stages and nature of each inquiry or research design of this study.

Table 3.8: Stages in the research process



Source: Own illustration

The research design can be based on the timing of collection of the qualitative and quantitative components and the order in which the data are used (Creswell and Plano Clark, 2011). The stages of this study were, to a large extent, executed sequentially as they appear in Table 3.8 above.

The research method used in each stage of the research is described below:

Stage 1

Stage 1 relied to a large extent on an extensive literature review on inter-jurisdictional VAT rules discussed in stage 2, to gain an understanding of and formulate the problem statement and the method of inquiry. Stage 1 applied a qualitative method.

Stage 2

Stage 2 comprised the main qualitative research phase of the study and was informed by Stage 1. Stage 2 applied a qualitative approach and had four objectives, namely to:

- describe the inter-jurisdictional VAT rules used in South Africa and identify current shortcomings;
- describe the relevant theoretical basis of taxation to create a theoretical foundation for the study;
- describe the inter-jurisdictional VAT rules used in selected other countries or country groupings; and
- formulate possible solutions to address the identified shortcomings;

Stage 2 included a survey which was conducted with a select few South African and international participants who specialise in VAT, indirect taxation, or fiscal economics. The questionnaire was sent to respondents electronically and then analysed. The results were then synthesised to use as data in the phase of the thesis that considered the South African inter-jurisdictional VAT rules and current shortcomings. The responses were integrated into the analysis, following the structure of that phase.

Stage 3

Stage 3 integrated the findings in Chapters 4, 5, and 6 and applied them to address the shortcomings identified and the problem statement outlined in Chapter 1; and

Stage 4

Stage 4 concluded the study and presented a summary of the approach followed and the findings.

CHAPTER 4: THEORETICAL FRAMEWORK OF THE STUDY

4.1 INTRODUCTION

In addressing the first sub-goal of the research, this chapter builds a theoretical framework for the study and considers the meaning and theory of taxation, indirect taxation and value-added taxation. The theoretical framework is used as basis for the remainder of the study. The chapter proceeds with a consideration of the meaning of taxation and the composition of a tax system. A discussion of the modern properties of a “good tax system”, namely fiscal adequacy, equity, economic efficiency, administrative efficiency and flexibility follows.

Tax incidence is then explored, as it underlies the determination of tax vesting of inter-jurisdictional activities and supplies in VAT. The theory, history, and design of VAT are the following considerations, which lead to a discussion of the doctrine of VAT “place of supply” rules. Place of supply rules are contextualised against inter-jurisdictional conflicts, tax incidence, and the destination principle which underpins modern VAT systems.

Then, consumption tax principles, which build on the Ottawa Taxation Framework, are presented. These principles include neutrality, efficiency, certainty and simplicity, effectiveness and fairness, and flexibility.

Finally, the chapter discusses “place of supply” proxies recommended by the OECD with regard to internationally traded goods and services, and intangibles. This section considers the essential differentiation between main rules that should apply to business-to-business, as opposed to business-to-consumer, supplies and special rules that could be applied where the main rules are lacking.

4.2 MEANING OF TAXATION

The word “tax” was first used in the 14th century and originates from the Latin “taxare”, which means “to assess” (New Internationalist, 2008). Prior to the use of “tax”, which requires money, the word “task” was used (originating from Old French), which requires labour. The word “tax” then developed the meaning of implying something wearisome or challenging (New Internationalist, 2008). Taxation is one of the strongest economic instruments in the hands of government to raise revenue (Steyn, 2012:23). The verb (to) “impose” is defined as (to) “force something to be accepted” (Oxford Dictionary and Thesaurus, 2009:465). The word “impose” describes a liability that government places on a taxpayer’s income, wealth, and/or consumption of commodities through legislation (Oxford Dictionary and Thesaurus, 2009:465). Almost two centuries ago, Jean-Baptiste Say (Say, 1821:450) defined a tax as:

the transfer of a portion of the national products from...individuals to...government, for purpose of meeting...public consumption or expenditure.

In *South African Reserve Bank and Another v Shuttleworth and Another* [2015] ZACC 17 (2015:26), the Court concluded that the dominant object of a statute needs to be identified to typify it as either fiscal or regulatory. The dominant object of enactment can either be to raise revenue (tax) or to regulate conduct (*South African Reserve Bank and Another v Shuttleworth and Another*: 26).

4.3 COMPOSITION OF A TAX SYSTEM

A tax system typically comprises of direct and indirect taxes. Direct tax is linked to characteristics of the person on whom the tax is imposed and includes income, capital, and wealth taxes. Income tax is generally progressive, whilst company and capital taxes are proportional. Capital taxes include capital transfer tax (donations tax and estate duty) and capital gains tax (Schneider, 1995:11).

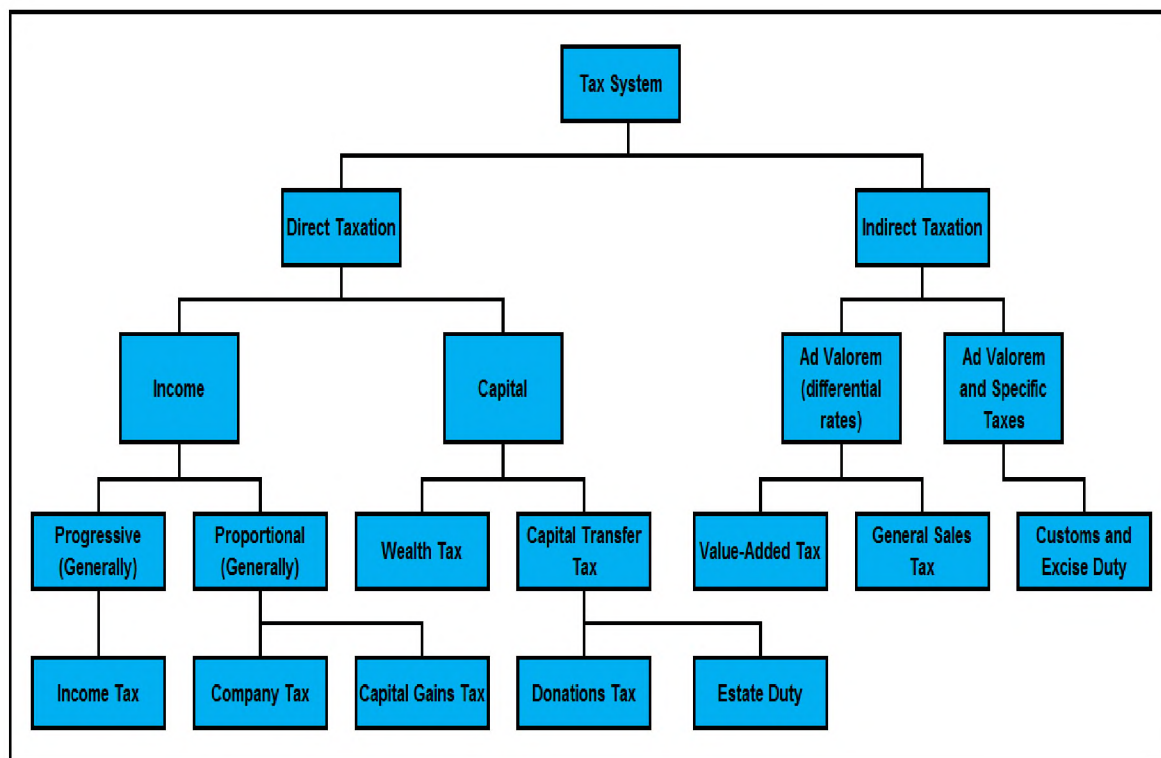
Indirect tax comprises “ad valorem” taxes and specific taxes. VAT is generally an “ad valorem tax” imposed at differential rates, whereas customs and excise duties are ad valorem or specific taxes. Ad valorem taxes are mostly expressed as a percentage of the selling price. If expressed as an amount per kilogram or similar measurement, it is a specific or unit tax (Schneider, 1995:11).

As to the choice between direct and indirect taxation Gladstone, in his budget speech in 1861, concluded very appropriately that:

...two attractive sisters...introduced into the gay world of London; each with an ample fortune; both having the same parentage (...Necessity and Invention) differing only as sisters may differ...I cannot conceive any reason why there should be unfriendly rivalry between the admirers of these two damsels; and I would frankly own, whether it be due to a lax sense of moral obligation or not...I have always thought it not only allowable, but...an act of duty, to pay my addresses to them both. I am therefore, as between direct and indirect taxation, perfectly impartial (Cadman, 1969:3).

Table 4.1 below sets out the typical composition of a tax system.

Table 4.1: Typical composition of a tax system



Source: Own design - from James and Nobes (2014) and Schneider (1995:12).

4.4 PROPERTIES OF A GOOD TAX SYSTEM

Adam Smith (1776:371) in his “*An Inquiry into the Nature and Causes of the Wealth of Nations*” formulated the properties of a “good tax system”. These properties are commonly referred to as the “canons” of taxation, although Smith used the word “maxims” (Ikeda, 2012). These maxims gave modern tax planners, practitioners and tax authorities guidelines and principles to develop and implement tax systems (Schneider, 2000:3).

Government activities and functions have increased significantly since Smith’s maxims were postulated (Akrani, 2010). Government is expected to maintain economic stability, promote full employment, reduce income inequality and encourage growth. The tax system should act as an enabler to meet these requirements. As a result, modern economists expanded on Smith’s maxims

(Akrani, 2010). Various country studies have added to the debate on the principles of a “good tax system”, most notably that of the United Kingdom’s Meade Committee on Taxation (Meade, 1978), South Africa’s Margo Commission (Margo Commission, 1986) and the Australian Future Tax System (AFTS) Review Panel (AFTS Report, 2009). The most important property of a “good tax system” is that it must generate sufficient revenue to fund government expenditure. The other properties of a “good tax system” include equity; economic efficiency; administrative efficiency; and flexibility (Black, Calitz, and Steenekamp, 2012:165-167). These properties are considered below.

4.4.1 Fiscal Adequacy

In modern society a tax system must primarily generate sufficient revenue to finance government expenditure (Black, Calitz, and Steenekamp, 2012:165-167). This can also be described as fiscal adequacy which requires a “good tax system” to yield enough revenue not to run into deficit (Akrani, 2010).

4.4.2 Equity

According to Smith, an ideal tax system should comply with the maxim of equity which requires that:

...(t)he subjects of every state ought to contribute towards the support of the government...in proportion to their respective abilities, that is in proportion to the revenue which they...enjoy under the protection of the state (Smith, 1776:371).

Tax equity requires equal sacrifice (Franzsen, 1990:20) and is generally divided into horizontal and vertical equity. Horizontal equity refers to treating like with like; vertical equity refers to the ability to redistribute between rich and poor (Meade, 1978:12). These principles may clash and require a balance between economic efficiency (which requires low marginal tax rates) and vertical redistribution (which requires high average tax rates on the rich). A good tax system minimises these

clashes and promotes redistribution, whilst minimising efficiency loss. The redistributive objectives of a tax system also involve basic value judgements on the nature of a good society with sufficient flexibility to allow for different political choices, such as variations in tax rates, etc. (Meade, 1978:12). As a result, taxes should (overall) result in an equitable distribution of income, considering that they can potentially be shifted (Black, Calitz, and Steenekamp, 2012:167). The equity principle is defended on the “ability-to-pay” and the “benefit” principles (Margo Commission, 1986:50-51). Different political systems and values impact the weight given to the “benefit” principle vis-à-vis the “ability-to-pay” principle in tax design (Davis Macro Analysis Report, 2015a:8). These concepts are considered below.

Ability-to-pay principle

Conventionally, tax equity is based on the “ability-to-pay” principle. The progressive² income tax system and capital gains tax are justified in terms of the ability-to-pay principle. The ability-to-pay principle regards tax as a sacrifice without a direct public service as a *quid pro quo*, based on an equitable burden for individual taxpayers, relative to their wealth (Davis Macro Analysis Report, 2015a:8). The ability-to-pay principle distinguishes between “horizontal equity” and “vertical equity” (Margo Commission, 1986:50-51). These concepts are considered below.

- Horizontal Equity

Horizontal equity mandates that similar tax subjects bear the same tax burden or that tax subjects in similar circumstances be treated equally (Margo Commission, 1986:50-51).

- Vertical Equity

Vertical equity mandates that tax subjects in different circumstances bear appropriately different tax burdens, i.e. the higher the level of economic well-being, the greater the tax burden (Margo Commission, 1986:50-51).

² The term “progressive” indicates that the tax system bears more heavily on those with higher incomes (Henry George Institute, *nd*).

Benefit principle

In terms of the benefit principle, taxation is based on the willingness of taxpayers to pay for benefits received (revealed through political mechanisms such as voting) (Davis Macro Analysis Report, 2015a:8). The benefit principle justifies the imposition of indirect taxes, such as VAT (Margo Commission, 1986:51). Thomas Hobbes in 1650 in his well-known “Leviathan” aptly defended the benefit principle as follows:

...when the Impositions are layd upon those things which men consume, every man payeth Equally for what he useth: Nor is the Common-wealth defrauded by the luxurious waste of private men (Rosen, 1985:453).

4.4.3 Economic Efficiency

Taxation results in administration costs for Government and compliance costs for the taxpayer (Franzsen, 1990:22). The cost to society of resource misallocation through economic distortions adds to the cost of taxation and is referred to as “dead-weight loss” (Schneider, 2000:5). Attempts to avoid tax result in “pure loss” to society. Compliance costs for taxpayers and administrative costs for tax authorities should be kept to a minimum (Margo Commission, 1986:51). A tax system should therefore:

...take out and keep out of the pockets of the people as little as possible, over and above what it brings into the public treasury of the State... (Smith, 1776:371).

A tax system impacts economic efficiency through effects on incentives and opportunities to work, save, invest, take risk and innovate, use resources efficiently; and allocate them to best serve society (Meade, 1978:7). An increased tax burden can have an “income effect” or “substitution effect”. If the tax burden leads to harder work to regain income lost to tax it is known as the “income effect”. If higher marginal tax rates reduce net disposable income for an additional hour’s work and leads to a preference towards leisure as opposed to work, it is known as the “substitution effect” (Meade, 1978:8).

An ideal tax system should minimise economic distortions (Steenekamp, in Black, Calitz, and Steenekamp, 2012:167), as they lead to the misapplication of the scarce resources available (Musgrave and Musgrave, 1984:225), and should:

...succeed in reducing a person's spending power...without leading him to behave any differently from the way in which he would have behaved if he had not been taxed at all, but his spending power had been correspondingly smaller: or in the words of Professor Pigou, a tax without announcement effects (Kaldor, 1965:81).

Designing a tax without “announcement effects” could be enhanced by increasing tax “invisibility” (Margo Commission, 1986:51). Invisibility is, strictly speaking, an approach to, and not a property of a “good tax” and relates to the notion that the best taxes are those perceived to be paid by others. This is close to being achieved through deductions at source and a VAT system, which has been described as *l'imput silencieux* (silent imposition) (Margo Commission, 1986:51). Tax invisibility can be questioned if it is argued that it is the privilege and obligation of a citizen to pay taxes and to call on Government to account for the application of the tax revenue (Franzsen, 1990:22-3).

4.4.4 Administrative Efficiency

Tax authority accountability can only be achieved if taxpayers understand their tax liabilities (Meade, 1978:18). Tax burdens should, for example, not be disguised in inflationary price movements, complexities in the formulation or administration of the tax, or its application (Meade, 1978:18). To minimise administration and compliance costs to ensure optimal efficiency, taxes should be “simple” and “certain” (Black, Calitz, and Steenekamp, 2012:167).

Simplicity

A tax system should be uncomplicated and easy to understand and administer with little need for interpretation and disputes (Akrani, 2010). The tax system should therefore be as transparent and simple as possible (Schneider, 1995:9).

Certainty

The nature and quantum of a taxpayer's taxes and compliance costs and the collection and administration costs of the *fiscus* should be simple to determine and observe (Franzsen, 1990:22). In the words of Smith (1776:371), in an ideal tax system:

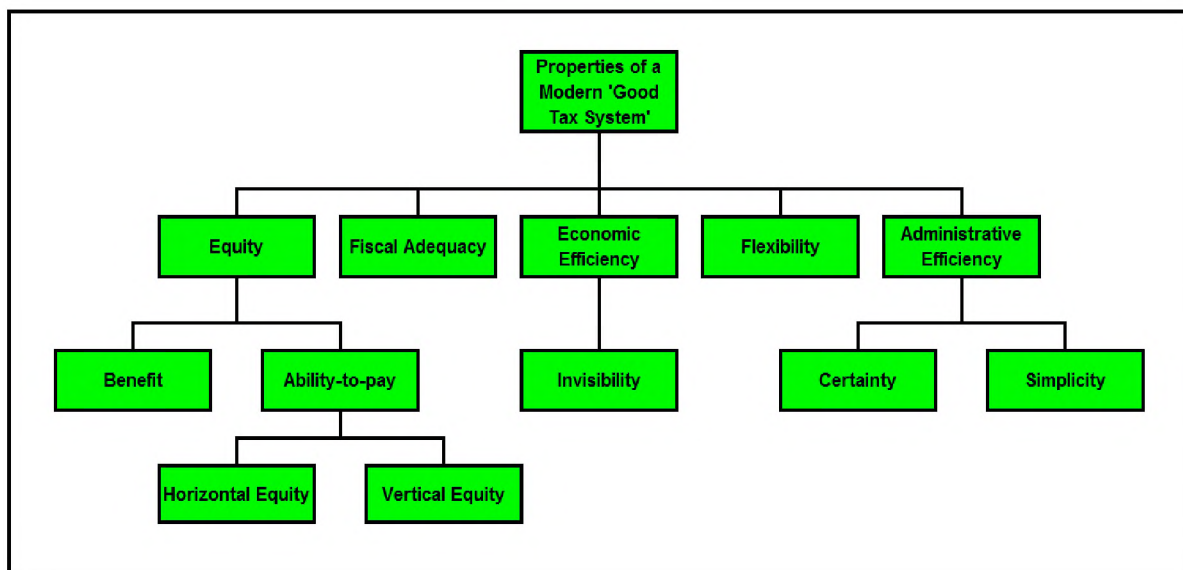
... (the) time of payment, the manner of payments, the quantity to be paid, ought all to be clear and plain to the contributor, and to every other person.

4.4.5 Flexibility

A good tax system should be economically and politically flexible (Meade, 1978:21). Economic flexibility ensures reasonably fast and frequent adjustments to total tax burdens to manage demand. Political flexibility, on the other hand, ensures that economic policy changes introduced by political changes are accommodated (Meade, 1978:21). Flexibility therefore aids and facilitates macroeconomic stability and economic development (Black, Calitz, and Steenekamp, 2012:167).

The properties of a good tax system are set out in Table 4.2 below.

Table 4.2: Properties of a good tax system



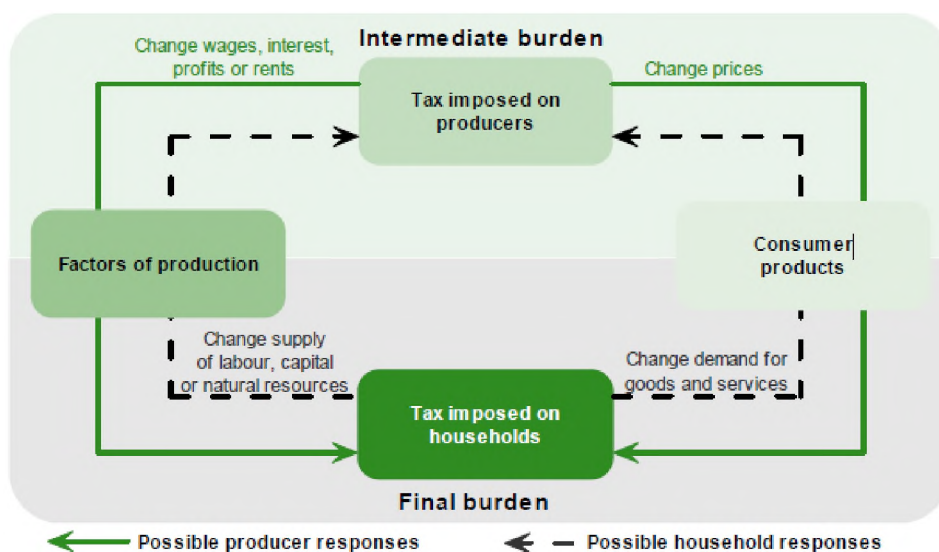
Source: Own formulation - from preceding analysis.

4.5 TAX INCIDENCE

Tax incidence determines who bears the tax burden, after taking into account changes in economic behaviour due to the imposition (Franzsen, 1990:15-16). In certain instances, tax may not be paid and borne by the same person (Franzsen, 1990:15-16). Tax can only be borne by natural persons. Legal and economic incidence should be distinguished from one another. Legal incidence of a tax refers to the tax burden imposed by the law, whereas economic incidence of a tax refers to the tax burden after taking into account changes in economic behaviour (Black, Calitz, and Steenekamp, 2012:171).

The economic incidence of a tax can be shifted through increased commodity prices or reduced costs in factors of production (AFTS Report, 2009:19). Market adjustments can also alter tax incidence. The tax burden is generally greater on a consumer of a product, or owner of a production factor for which the demand or supply is unresponsive to a change in price: thus a consumer of a product with no ready substitutes, or an owner of a production factor that is relatively immobile (AFTS Report, 2009:19).

Table 4.3: Tax incidence and shifting



Source: AFTS Report, 2009:20.

Legal tax incidence is the legal tax liability or tax burden imposed on the subject by statute or law. Economists are not only concerned with legal tax incidence since taxes affect economic behaviour which, in itself, can shift the tax incidence (Black, Calitz, and Steenekamp, 2012:171). Taxpayers and economists therefore concern themselves more with economic tax incidence as it determines who ultimately bears the burden (Black, Calitz, and Steenekamp, 2012:171).

4.5.1 Tax incidence of direct taxation

In practice, most countries apply a combination of source and residence principles of taxation for direct tax purposes, which can result in double- or non-taxation (Black, Calitz, and Steenekamp, 2012:200-201). To relieve double taxation, countries: (i) enter into trade-offs of taxing rights through bi-lateral or double taxation agreements; (ii) grant relief through domestic legislation; or (iii) harmonise tax treatment of cross-border income on a multi-lateral basis. Multi-lateral harmonisation is difficult as countries often do not view the benefits of each system similarly. Countries applying the residence (or worldwide) base of taxation generally grant tax relief unilaterally through deductions of income earned in the source country or grant

a tax credit for the tax paid in the source country. The source and residence principles are generally contained in tax laws and determine the legal tax incidence (Black, Calitz, and Steenekamp, 2012:200-201).

A tax neutral system should not distort locational decisions of businesses. Capital exporting countries applying the residence basis are neutral with regard to capital exports, as the investor is concerned with the tax rate in the country of residence. Capital importing countries applying the source basis are neutral with regard to capital imports where it does not discriminate between domestic and foreign investment, regardless of capital origination (Black, Calitz, and Steenekamp, 2012:202-203).

In terms of the source principle, income is taxed where earned or generated³. The person that earns income benefits from the provision of public goods and services at source. This is debatable as a resident who earns foreign-sourced income also benefits to some extent. Countries with high levels of foreign income (such as royalties, dividends, and interest) should consider the source base on revenue grounds (Black, Calitz, and Steenekamp, 2012:200-201). In terms of the revenue principle, the country where the person is resident should determine the tax liability and collect it. Legal persons are generally tax resident where the business is registered or has a fixed place of business. Income that can be allocated to these activities, whether at home or abroad, should attract tax⁴. Countries with low levels of foreign income should consider the revenue base on administrative expediency grounds (Black, Calitz, and Steenekamp, 2012:200-201).

³ This approximates the “benefit principle” of taxation. For a detailed discussion of the “benefit principle” see “Equity” discussed under “Properties of a Modern Good Tax System”.

⁴ This approximates the “ability-to-pay principle” of taxation and enables countries to tax worldwide income of residents on a progressive scale. For a detailed discussion of the “ability-to-pay” principle see “Equity” discussed under “Properties of a Modern Good Tax System”.

4.5.2 Tax incidence of indirect taxation

A VAT system (as representative of an indirect tax) generally relies on place of supply rules and VAT rates (inter-jurisdictional VAT rules) to determine the tax incidence of VAT on cross border transactions (Black, Calitz, and Steenekamp, 2012:200-201). These rules also curb double- or non-taxation (Terra, 1998:1). VAT systems generally zero rate exports and grant taxing rights to the recipient's tax jurisdiction. VAT systems generally also tax imports and domestic production⁵ (McLure, 1987:31).

Most VAT systems require (registered) VAT vendors to charge VAT on supplies and claim VAT on expenses incurred as input tax deductions (Tait, 1988:371). The requirement to register for VAT is often defined with reference to residency and the place of business. VAT systems often also define registration requirements by foreign persons and foreign branch/main business activities that have a physical or economic activity in that country, through deeming provisions (Tait, 1988:371). Worldwide VAT systems generally contain limited or no place of supply rules, which therefore increases reliance on these definitions. Territorial VAT systems, on the other hand, apply detailed place of supply rules which reduce reliance on these definitions (Schenk, 2009:4).

4.6 THEORY OF VALUE-ADDED TAX

VAT is justified in terms of the benefit principle, as economic subjects are taxed based on the benefit they derive from use or consumption of scarce economic resources (Schneider, 2000:6).

There has been a marked global shift towards implementing VAT systems. The rise in the implementation of VAT has, approximately three decades ago already, been

⁵ This follows the destination principle of taxation. For a detailed discussion of the destination principle of taxation, see "Worldwide versus Territorial" under "Classification of Value-Added Tax".

described as:

...an unparalleled phenomenon. The history of taxation reveals no other tax that has swept the world...from theory to practice, and has carried along with it academics who were once dismissive and countries that once rejected it...Various similes come to mind; VAT may be thought of as the Mata Hari of the tax world – many are tempted, many succumb, some tremble on the brink, while others leave only to return, eventually the attraction appears to be irresistible (Tait, 1988:3).

4.6.1 History of Value-Added Tax

Dr Wilhelm Von Siemens, a German businessman, is one of two people generally credited with the development of a VAT system in the 1920s (Charlet and Owens, 2010:943). The other is Thomas Adams, an American economist who suggested (in various writings from 1910 to 1921) the adoption of a credit-invoice method VAT, as an alternative to a corporate income tax system (James, 2015:1). Maurice Lauré, also considered by some as the “father of VAT”, took the idea and developed it into a tax system, which led to France implementing a predecessor of VAT in 1954. VAT systems at the manufacturing level were introduced in Cote d'Ivoire and Senegal in the 1960s. Brazil introduced a traditional VAT on all stages of production in 1965. The European Union introduced VAT in member states in 1967, following the 1963 Neumark Committee's proposal (Peacock, 1981: 120). The proliferation of VAT in Europe was driven by the fact that it is a prerequisite for membership of the European Union. VAT is also strongly supported by the International Monetary Fund. VAT systems have now been implemented in more than 160 countries, and account for about one-fifth of total tax revenue in the OECD and worldwide (OECD, 2014b:14).

4.6.2 Design of a Value-Added Tax system

The design of VAT systems differentiates between the economic base of imposition, inclusivity versus exclusivity, methods of calculation, treatment of capital goods, the

number of VAT rates used and whether it is a worldwide or territorial VAT. These designs are considered below.

Economic Base

VAT is a multistage sales tax levied on the value added at the different stages of production. Value added approximates the difference between sales and purchases of intermediate goods and services. The value added typically comprises salaries and wages, rent, interest, depreciation and profit (Steenekamp in: Black, Calitz, and Steenekamp, 2012:261).

VAT systems theoretically comprise broadly of three types, namely: (i) consumption type VAT systems; (ii) income type VAT systems; and (iii) VAT on gross product (Black, Calitz, and Steenekamp, 2012:262). The universal practice is a consumption-type VAT system. In a closed economy:

$$\text{GNP} = \text{C} + \text{I} = \text{W} + \text{P} + \text{D}$$

<i>Where:</i>	GNP	=	Gross National Product
	C	=	Consumption
	I	=	Gross Investment
	W	=	Wages
	P	=	Profit after depreciation
	D	=	Depreciation

The economic base of the consumption-type VAT is then:

$$\text{C} = \text{W} + \text{P} + \text{D} - \text{I} \text{ (Black, Calitz, and Steenekamp, 2012:262).}$$

Inclusivity versus Exclusivity

VAT systems can also be tax-inclusive⁶ or tax-exclusive⁷. Tax-inclusivity refers to a VAT system which requires prices to be quoted and advertised inclusive of VAT and

⁶ See also the section on "Methods of Calculation".

⁷ See also the section on "Methods of Calculation".

tax invoices to be inclusive of VAT. Tax-inclusivity requires calculating VAT by using the effective tax rate (or “te”) (Tait, 1972:4-5). Tax-exclusivity refers to a VAT which requires prices to be quoted and advertised exclusive of VAT and tax invoices to be exclusive of VAT, but VAT can be stipulated separately. Tax exclusivity requires calculating the VAT by using the nominal tax rate (or “tn”) (Tait, 1972:4-5). Although there is no theoretical difference between these two methods, they may impact the “economic efficiency” of a “good tax system” due to the impact of invisibility⁸.

Calculation

A VAT system can also be designed with reference to the method of calculation of the tax (Tait, 1972:2). The difference between the output and the input is equal to the payment of salaries and wages, and profit. The value added can either be calculated by using (i) the additive method [salaries and wages plus profit]; or (ii) the subtractive method [output less input] (Tait, 1972:4-5).

In terms of the *additive method*, the tax rate is applied in one of two ways, namely (i) directly [tax rate x ((salaries and wages) + profit)]; or (ii) indirectly [[tax rate x (salaries and wages)] + [tax rate x (profit)]] (Tait, 1972:4-5).

In terms of the *subtractive method*, the tax rate is applied in one of two ways, namely (i) directly [tax rate x (output – input)]; or (ii) indirectly [[tax rate x (output)] – [tax rate x (input)]] (Tait, 1972:4-5). The *subtractive-direct method* is known as the *accounts method*, and the *subtractive-indirect method* is known as the *credit-invoice method*. The credit-invoice method links the tax liability to the transaction value and is more desirable legally and technically and is most commonly used as the invoice is the proof of the transaction and tax liability and creates a clear audit trail, which ensures that input tax deductions are only made when the output tax has been or will be paid (Tait, 1972:4-5).

As VAT can be calculated on a tax exclusive or inclusive basis and could be calculated on either a direct or indirect basis under either the additive or subtractive methods, this results in eight methods of calculation. Table 4.4 below highlights these methods of calculation (Tait, 1972:4-5, and Schneider, 1995:27).

⁸ See the discussion of “economic efficiency” under “Properties of a ‘good tax system’”.

Table 4.4: Eight methods to calculate VAT

	Additive Method		Subtractive Method	
	Tax Exclusive	Tax Inclusive	Tax Exclusive	Tax Inclusive
Direct	$tn \times [W + P]$	$te \times [W + P]$	$tn \times [O - I]$	$te \times [O - I]$
Indirect	$[tn \times W] + [tn \times P]$	$[te \times W] + [te \times P]$	$[tn \times O] - [tn \times I]$	$[te \times O] - [te \times I]$

Where:

- tn = Nominal Tax Rate
- te = Effective Tax Rate
- W = Salaries and Wages
- P = Profit
- O = Output
- I = Input

Source: Tait (1972:4-5), and Schneider (1995:27).

Capital Goods

A VAT system can also be designed with reference to its treatment of capital goods. Firstly, certain VAT systems (those used in the European Union) allow VAT incurred on capital expenditure as an immediate input tax deduction. The immediate input tax deduction ensures that only consumables are subject to tax. Secondly, certain VAT systems limit VAT deductions on capital expenditure incurred to the depreciation of these capital assets. Thirdly, certain VAT systems limit VAT deductions on capital expenditure incurred to materials and parts, which physically form part of the manufactured goods (Schneider, 2000:8). Deductions on capital goods are therefore not granted on an ongoing or depreciation basis (Musgrave and Musgrave, 1984:442-3).

Destination versus Origin

VAT systems can also be designed in terms of the destination or origin bases (Schenk, 2009:4). A “destination based” VAT system taxes imports and domestic production and frees exports from VAT. The tax base of a destination based VAT system is consumption and is most commonly used (McLure, 1987:31). An “origin

based” VAT system taxes domestic supplies of goods and services by freeing imports from tax and taxing exports. No country operates a pure origin principle VAT (Schenk, 2009:4). The tax base of an origin based VAT system is production (McLure, 1987:31). The origin and destination principles can be distinguished as follows:

...between taxing at the place from which supplies are made (the origin principle) and taxing at the place to which supplies are made (the destination principle) (Krever, 2008:177). (emphasis added)

Worldwide versus Territorial

A VAT system imposes tax on supplies in the tax jurisdiction’s territory (territorial) or on all supplies by the registered person (worldwide). Countries operating worldwide or territorial VAT system decide independently how to tax international transactions (Schenk, 2009:4). A worldwide system initially imposes VAT on the vendor’s worldwide supplies, but then modifies the VAT base to enable the vendor to report on less than its worldwide supplies (Schenk, 2009:6). Most worldwide VAT systems apply the destination principle to international transactions by zero-rating exports and taxing imported goods. Imported services also follow the destination principle, irrespective of whether it is a worldwide or territorial VAT system (Schenk, 2009:4-6). Most VAT systems are territorial and apply a modified destination principle by taxing imported goods and some services, whilst zero rating exports of goods and certain services (Schenk, 2009:4-6). Territorial systems seek to limit the geographic scope to taxable supplies within the tax jurisdiction. As a result, the place of supply becomes critical and plays a central role in the tax system (Schenk, 2009:4-6).

4.7 DOCTRINE OF INTER-JURISDICTIONAL VAT RULES

4.7.1 Introduction

Place of supply rules for services were much simpler when services represented a smaller portion of consumer spending. The place of supply of most services was where the supplier was located. As these services increased, the location of the

supplier rule did not always provide a reasonable result. Countries re-examined and changed the place of supply rules for certain services (Schenk, 2009:4-6).

Growth in the volume of cross-border trade in services and intangibles makes the application of place of supply principles and the interaction between national VAT systems increasingly difficult. Monitoring these transactions and collecting taxes, especially where businesses supply services in jurisdictions where they do not have a physical presence, also pose difficulties. The OECD (2014c), in response, developed an international standard in respect of VAT and cross-border trade in services and intangibles to minimise double taxation and double non-taxation (OECD, 2014b:28).

The doctrine of inter-jurisdictional VAT rules does not impact on transactions or activities which take place in one tax jurisdiction between persons in that jurisdiction (Terra, 1998:1). It is then irrelevant where supplies take place and only two questions need answering. Firstly, where does the taxable person live or have a permanent establishment? And, secondly, which tax authority should collect the taxes (Terra, 1998:1)?

Transactions spanning more than one tax jurisdiction require a determination of where the supply takes place to allocate the tax revenue between the tax jurisdictions (Terra, 1998:1). Place of supply should adhere to tax neutrality and consider tax avoidance, and double or non-taxation and are essential to avoid double taxation (Terra, 1998:1).

Supplies of goods or services are generally subject to VAT if made in country. This requires defining “country” which generally includes the continental shelf and territorial sea and excludes free ports or zones (Tait, 1988:371).

The place of supply of services is generally determined through the application of a wide range of markers or proxies (OECD, 2014b:26). Proxies are used to determine the place of consumption which is often “like trying to get your hands around a piece of jelly” (Millar, 2004:286). These proxies include the place of performance, place of establishment or actual location of the supplier, residence or actual location of the

consumer, and the location of tangible property if the services are connected with tangible property. VAT systems often apply multiple proxies to determine the place of supply. Place of supply rules generally also distinguish between business-to-business and business-to-consumer supplies of services (OECD, 2014b:26).

4.7.2 Inter-Jurisdictional Conflicts

The different approaches to allocate tax inter-jurisdictionally exacerbate the potential for inter-jurisdictional conflict, which can result in double (or triple) taxation, inappropriate taxation, non-taxation, supply chain inefficiencies, barriers to market entry, distortions of competition, high compliance costs, non-compliance and general uncertainty (Millar, 2004:288-290).

VAT levied on a business-to-business supply can result in tax cascading, and cause one jurisdiction's tax to become a cost to supplies made in another (Millar, 2004:290). Different credit or deduction mechanisms and refund schemes for non-residents add further complexities. The main sources of inter-jurisdictional conflict include differing inter-jurisdictional treatment of the nature of supplies, bundled supplies, different proxies for the same supply types, interaction between time and place of supply rules, nature of effective use or enjoyment, when to measure effective use or enjoyment, and different interpretations of the same proxy (Millar, 2004:288).

4.7.3 Tax Incidence

VAT systems generally apply the destination principle and seek to tax final domestic consumption. VAT should vest with the final consumer. But, as consumption in the economic sense is difficult to determine, VAT place of supply rules are used to ensure that the tax incidence falls as closely as possible on the final consumer. VAT place of supply rules, as a result, also seek to address double and non-taxation (Terra, 1998:2).

Destination Principle

The last few years have seen a global shift towards the use of the destination principle (Millar, 2004:285-6). Most VAT systems apply the destination principle to international trade, which mandates that the tax jurisdiction where consumption occurs should levy tax (OECD, 2014c:3). The destination principle is justified in terms of the benefit principle (Terra, 1998:5). The jurisdiction where consumption takes place and supplies connected to that jurisdiction should be identified. VAT place of supply rules give effect to the destination principle in respect of business-to-consumer supplies, which should tax final consumption, and business-to-business supplies, which may not always tax final consumption (OECD, 2014c:3).

Cross-border supplies of goods apply the destination principle through border controls (OECD, 2014c:3). As internationally traded services and intangibles cannot be subject to border controls, the destination principle is more difficult to apply. The OECD developed guidelines relating to the destination principle and internationally traded supplies of services and intangibles, whilst adhering to core tax principles (OECD, 2014c:3-4).

The destination principle often applies differently to business-to-business supplies, as opposed to business-to-consumer supplies (OECD, 2014c:4). Place of supply rules should identify the actual place of business use for business-to-business supplies and the actual place of consumption for business-to-consumer supplies (OECD, 2014c:4). Place of supply rules for business-to-business supplies should also focus on the flow-through of the tax burden to the consumer, while maintaining neutrality and predicting where consumption is likely to take place (OECD, 2014c:4).

Consumption tax principles

The Committee on Fiscal Affairs of the OECD presented a report at the OECD Ministerial Conference on “*A Borderless World: Realising the Potential of Electronic Commerce*”, held in Ottawa in October 1998 (OECD, 1998:1). The Committee on Fiscal Affairs endorsed the Ottawa Tax Framework (or principles) and committed to develop inter-jurisdictional VAT rules on broad based consumption taxes (OECD, 2014a:4). Although the OECD initially articulated these general tax principles in the context of electronic commerce, they are now applied to the treatment of domestic

and international trade in VAT systems (OECD, 2014a:8-9). The OECD agreed core consumption tax elements on the back of the Ottawa Tax Framework, namely that cross-border trade should be taxed in the jurisdiction of consumption; digitised products should be treated as services; if persons in a country acquire services and intangible property from foreign suppliers, the use of reverse charge, self-assessment or equivalent mechanisms should be investigated if they would give immediate protection of revenue bases and the competitiveness of domestic suppliers; and countries should develop appropriate systems⁹ to collect tax on the importation of physical goods, which do not unduly impede revenue collection and the efficient delivery to consumers (OECD, 2001:18-19).

Determination of the place of supply should generally adhere to the destination principle (place of consumption) and comply with the tax principles of:

- neutrality;
- efficiency of compliance and administration;
- certainty and simplicity;
- effectiveness and fairness; and
- flexibility (OECD, 2014c:10).

These consumption tax principles are considered below.

Neutrality

Tax neutrality in domestic trade is achieved through the multi-stage payment system in which a business pays VAT to suppliers and receives VAT from customers. Input tax incurred is offset against output tax, resulting in a liability to pay or to be refunded the net amount. As a result, VAT normally “flows through the business” to the final consumer and is not borne by business (OECD, 2014a:10). Tax neutrality requires that tax collected in a particular supply chain should be proportional to the amount paid by the consumer, irrespective of the nature of the supply, the structure of the distribution chain, the number of transactions or economic operators involved and the technical means used (OECD, 2014a:10).

⁹ In co-operation with the World Customs Organization (WCO) and in consultation with carriers and interested parties.

Although VAT should not drive business it is often a consideration (OECD, 2014a:11). VAT rules that apply to international supplies should not produce a tax advantage when compared to domestic transactions. This includes the level of taxation, cost of collection and administration, and burdens on business and tax administrations (OECD, 2014a:12).

Table 4.5 below summarises the VAT neutrality guidelines discussed above.

Table 4.5: VAT guidelines on neutrality

	Description
2.1	<i>Taxable business should not bear VAT except if provided for in law</i> Foreign and local business should not bear the burden of the tax, except if provided in law.
2.2	<i>Businesses in “similar situations” doing “similar transactions” should have “similar tax levels”</i> “Similar tax levels” mean that the final tax burden needs to be considered, taking into account refunds and credits. If a business incurs irrecoverable tax in more than one jurisdiction on the same input, it does not bear a “similar level of taxation” compared to local business. Businesses acquiring services to support their taxable activities are not in a “similar situation” to businesses acquiring services to support exempt activities or that acquire services for personal use. Determining “similar transactions” for businesses in “similar situations” purchasing services or intangibles should focus on the nature of the supplies.
2.3	<i>Business decisions should not be influenced primarily by VAT considerations</i> VAT considerations include the tax amount paid to authorities, associated compliance burdens, and cash-flow impact of VAT. VAT should not drive decisions to operate in a jurisdiction, sell to customers in a jurisdiction, make purchases in a jurisdiction, and outsource activities such as production, manufacturing or other support services in a jurisdiction. It should also not influence structures of supply chain or use of intermediaries.
2.4	<i>Foreign businesses should be neutral with regard to tax levels, compared to local businesses</i> Foreign business should not incur unjustifiable discriminatory irrecoverable VAT compared to domestic business; VAT rules should not discriminate against foreign business; foreign business should not have a lower tax burden; and VAT should not distort competition between foreign and local business.
2.5	<i>Foreign businesses should not incur irrecoverable VAT and jurisdictions may use a number of approaches to achieve this</i> These approaches can include freeing supplies of VAT; specific foreign businesses refunding regimes; refunding foreign businesses through VAT registrations; shifting the responsibility to locally registered suppliers / customers, and granting purchase exemption certificates.
2.6	<i>Foreign businesses subject to specific administrative requirements should not bear a disproportionate or inappropriate compliance burden</i> Local business generally have fixed places from where they operate, local employees and contact persons, a local bank, links to local tax authorities and various identifications / registrations. Foreign business are less likely to have the same. Foreign business specific compliance requirements due to risk protection and administrative needs, should be proportionate and appropriate.

Source: OECD, 2014a:10-21

In addition to the *VAT Guidelines on Neutrality*, the OECD also formulated guiding principles of good tax administration for revenue authorities, which is encouraged.

These are summarised in Table 4.6 below.

Table 4.6: OECD VAT guidelines on good tax administration

	Guideline
1	Law application Fair, reliable and transparent application of tax laws.
2	Taxpayer rights Communicate taxpayer rights, obligations, and complaint procedures and redress mechanisms and provide accessible and dependable information service on taxpayer rights and obligations.
3	Service delivery Deliver quality information and accurate and timely treatment of taxpayer inquiries, requests and appeals.
4	Compliance costs Keep compliance costs to the minimum level required to achieve tax compliance.
5	Taxpayer input to policies Allow taxpayers to comment on administrative policies and procedures changes, where appropriate.
6	Taxpayer information Use taxpayer information to the extent permitted by law.
7	Working relationship Develop and maintain good working relationships with clients and the wider community.

Source: OECD, 2014a:14

Efficiency

Taxpayers' compliance costs and tax authorities' administrative costs should be kept to a minimum (OECD, 1998:4).

Certainty and simplicity

Tax rules should be clear and simple to enable taxpayers to anticipate the tax consequences of a transaction in advance, including knowing when, where and how the tax should be accounted for (OECD, 1998:4).

Effectiveness and Fairness

The tax system should produce the correct amount of tax at the correct time. Tax evasion and avoidance should be kept to a minimum, whilst maintaining anti-evasion and -avoidance measures proportionate to the associated risks (OECD, 1998:4). Fairness in a VAT system is achieved through the destination principle, which frees exports from VAT and taxes imports on the same basis and at the same rate as local supplies. The tax burden on imports should be equal to that of similar local supplies. The amount of export tax refunds should equate to the tax levied

(OECD, 2014a:12).

Flexibility

The tax system should be flexible and dynamic to ensure that it keeps pace with technological and commercial developments (OECD, 1998:5).

Table 4.7 below summarises the consumption tax principles.

Table 4.7: Consumption tax principles

Guideline	Description
Neutrality	<p>Taxable businesses should only bear VAT if provided for by law.</p> <p>Businesses in “similar situations” doing “similar transactions” should be subject to “similar tax levels”. Business decisions should not be driven by VAT considerations.</p> <p>Foreign businesses should not have favourable or unfavourable tax levels, compared to domestic businesses. Foreign businesses should not incur irrecoverable VAT, and jurisdictions may choose from a number of approaches to achieve this. Foreign businesses subject to specific administrative requirements should bear a proportionate or appropriate compliance burden.</p> <p>Good tax administration with regard to law application; taxpayer rights; service delivery; compliance costs; taxpayer input to policies; taxpayer information; and working relationship.</p>
Efficiency	<p>Taxpayers’ compliance costs and tax authorities’ administrative costs should be minimised.</p>
Certainty and simplicity	<p>Tax rules should be clear and simple to enable taxpayers to anticipate the tax consequences of a transaction in advance, including knowing when, where and how the tax should be accounted for.</p>
Effectiveness and Fairness	<p>The correct amount of tax should be produced at the correct time. Tax evasion and avoidance should be minimised, and anti-evasion or avoidance measures should be proportionate to the risk.</p>
Flexibility	<p>The tax system should be flexible and dynamic and keep pace with technological and commercial developments.</p>

Source: OECD, 1998:4-5 and OECD, 2014a:10-13

4.7.4 Place of supply proxies

VAT systems principally seek to tax final consumption, although each supply, supplier, and recipient of a supply is subject to the rules of law of the relevant jurisdiction. As a result, the term “consumption” for VAT purposes generally refers to the use of services or intangibles and not economic “consumption”, as economic consumption is difficult to legislate for (OECD, 2010:6-7). Establishing the exact place of consumption is often difficult, particularly for services and intangibles. To overcome this, VAT systems use proxies to deem place of consumption and allocate tax (OECD, 2010:7).

Traditionally consumers typically acquired services from local suppliers that could be expected to be consumed where performed (OECD, 2014c:5). Many VAT jurisdictions' place of supply rules were drafted primarily with reference to the supplier's location. These place of supply rules were often supplemented by place of performance rules if the supplier's location was a less reliable indicator of where the services were likely to be consumed (OECD, 2014c:5-6).

With the advent of digital services, inter-jurisdictional supplies increased exponentially, which rendered the use of the supplier's location or place of performance to approximate consumption insufficient to predict the place of consumption (OECD, 2014c:6). Applying the destination principle to ensure that the tax on services and intangibles is levied where consumption takes place is generally easier for business-to-consumer, as opposed to business-to-business supplies (OECD, 2014c:5).

Internationally traded goods

VAT systems operate on the underlying assumption that goods are consumed where they are located (Millar, 2004:291). As a result, a proxy to determine the place of consumption of supplies of immovable and movable goods based on the location of those goods at time of supply, is reasonable. Movable goods that are exported will generally be subject to VAT on importation (OECD, 2014c:15). The taxing rights are granted to the jurisdiction of consumption when the goods cross the border. VAT systems generally give VAT relief in the jurisdiction where movable goods are temporarily located, if they are subsequently exported (OECD, 2014c:15). Determining the place of supply of goods generally does not present practical or interpretational problems and this thesis will not consider it extensively.

Internationally traded services and intangibles

VAT neutrality in international trade is generally achieved through the destination principle. Applying the destination principle to supplies of internationally traded services and intangibles is more difficult than to goods since the former are not subject to border controls as are goods. The Guidelines developed by the OECD determine the jurisdiction of taxation for internationally traded services and intangibles that adhere to the destination principle. The destination principle often

requires that different approaches be applied to international business-to-business as opposed to business-to-consumer supplies (OECD, 2014a:23). As supplies should be taxed according to the destination principle they should follow the tax rules of the jurisdiction where consumption takes places (OECD, 2014c:3)¹⁰. Proxies should adhere to the consumption tax principles formulated by the OECD.

- *Business-to-business supplies – main rule*

The main rule for business-to-business supplies determines that supplies should be taxed at the customer's location (OECD, 2014c:5)¹¹. Customer identity is normally determined with reference to business agreements or contracts (OECD, 2014c:5)¹². Elements of the business agreement can include general correspondence, service level agreements, purchase orders, invoices, payment instruments and receipts (OECD, 2010:9). Elements of a business agreement can also include audio recordings of telephone conversations leading to conclusions of agreements, emails, on-line ordering records, payment and similar material and formats. Other agreements may provide the context of the supplies made under a particular business agreement. The business agreement in force at the time of supply governs the implementation of the main rule (OECD, 2010:9-10). In a business-to-business environment, suppliers will normally develop relationships with customers, especially if the supplies are on-going or their values warrant business agreements (OECD, 2010:11).

The customer should ideally be liable to account for tax due, which can be achieved through the reverse charge mechanism, if consistent with the design of the national consumption tax system. In terms of the reverse charge mechanism, better known in the South African VAT system as imported services, the supplier would then not be required to be identified for VAT or account for tax in the customer's jurisdiction as this would be done by the recipient in terms of the reverse charge mechanism (OECD, 2014a:31).

¹⁰ OECD Guideline 3.1.

¹¹ OECD Guideline 3.2.

¹² OECD Guideline 3.3.

Where supplies are made to customers with establishments in more than one jurisdiction, the supplies should be taxed where the establishments using the supplies are located (OECD, 2014c:5)¹³. Jurisdictions adopt a number of approaches to identify which establishment uses a service or intangible, including the direct use approach¹⁴; direct delivery approach¹⁵; or recharge method¹⁶ (OECD, 2014a:27).

- *Business-to-business supplies – special rules*

Using the customer location as a proxy in a business-to-business context may be inappropriate where services or intangibles are typically supplied to businesses and final consumers, services require the physical presence of the supplier and the customer, and services are used at a readily identifiable location (OECD, 2014c:12).

The general customer location rule may impose a significant compliance burden where services or intangibles are supplied to volumes of customers for relatively small amounts in a short period of time (for example restaurant services) (OECD, 2014c:12). Where customer location¹⁷ is inappropriate (as measured against the consumption tax principles), a special rule can be applied if it leads to a significantly better result if considered against the same criteria (OECD, 2014c:10)¹⁸.

The same could apply to the granting of access (to concerts, sport games, trade fairs or exhibitions) designed for businesses. Where a ticket is purchased at the entrance of the building it could be difficult to identify and establish the customer's status and location. Efficiency, certainty and simplicity, and fairness may be difficult to achieve. A special rule based on

¹³ OECD Guideline 3.4.

¹⁴ The establishment that uses the service or intangible.

¹⁵ The establishment to which the service or intangible is delivered.

¹⁶ The establishment that uses the service or intangible, determined on the basis of internal recharge arrangements, made in accordance with corporate tax, accounting or other regulatory requirements.

¹⁷ OECD Guideline 3.2.

¹⁸ OECD Guideline 3.7.

where the event takes place could meet the consumption tax principles and lead to a significantly better result (OECD, 2014a:44)

- *Business-to-consumer physically performed supplies – main rule*

The main rule for business-to-consumer physically performed supplies provides that the jurisdiction where the supply is physically performed should tax the supplies where they are physically performed at a readily identifiable location, are ordinarily consumed at the same time and place of performance and ordinarily require the physical presence of the person performing and the person consuming the supply at the same time and place of supply¹⁹.

The location of the person performing the supply can be used as an alternative, except for services comprising of consulting, accounting, legal, financial, insurance, telecommunication, and broadcasting services; long-term rental of movable property; online supplies of software, software maintenance, digital content, digital data storage and online gaming (OECD, 2014c:7-8).

Where the place of physical performance or the supplier's location is inappropriate to approximate the place of consumption of services and intangibles, the usual residence of the customer may be appropriate (OECD, 2014c:7). The usual residence of the customer is generally where the customer regularly lives or has a home, but excludes tourists or participants in training or conferences (OECD, 2014c:8).

The customer's usual residence will probably depend on the business model, the type and value of the supplies and the suppliers' delivery model (OECD, 2014c:8). E-commerce, for example, often involves high volume, low-value supplies with minimal interaction between suppliers and customers, which may make it difficult for suppliers to rely on single sources of information, such as contracts, to determine the customer's usual residence. Suppliers should have clear and realistic guidance on the information required to

¹⁹ OECD Guideline 3.7.

determine customers' usual residence. Suppliers should be allowed to rely, as far as possible, on customer information collected in the course of business that provides reasonably reliable evidence (OECD, 2014c:8).

- *Business-to-consumer non-physically performed supplies – main rule*

The main rule for business-to-consumer supplies not physically performed provides that the jurisdiction where the customer has its usual residence can tax the supplies (OECD, 2014c:7)²⁰.

- *Business-to-consumer supplies – special rules*

The general rules²¹ for business-to-consumer supplies may be inappropriate if they lead to an allocation of inefficient and administratively burdensome taxing rights, or are not sufficiently accurate to predict the place of consumption (OECD, 2014c:12-13). These may occur in the following instances:

- The place of physical performance²² for on-the-spot supplies of services²³ and intangibles may be inappropriate²⁴ where physical performance occurs and tax obligations arise in multiple jurisdictions, for example international transport of persons.
- The usual residence of the customer²⁵ for supplies of services and intangibles²⁶ may, in certain instances, be inaccurate to predict consumption. These could include services and intangibles performed at a readily identifiable location that require the physical presence of the

²⁰ OECD Guideline 3.8.

²¹ OECD Guidelines 3.7 and 3.8.

²² OECD Guideline 3.7.

²³ On-the-spot supplies are typically consumed immediately and at an identifiable place of performance, and include services physically performed on, or supplied to a person, such as hairdressing, beauty therapy, physiotherapy; accommodation; restaurant and catering services; theatre performances, trade fairs, museums, exhibitions, and parks; and attendance at sport events (OECD, 2014c:7).

²⁴ Measured against the criteria of OECD Guideline 3.7.

²⁵ OECD Guideline 3.8.

²⁶ Other than those falling under OECD Guideline 3.7.

consumer but not of the person performing it. Examples include internet access at an internet café or access to television for a fee in a hotel room. Such suppliers can arguably establish the location of the customer at time of consumption. The actual customer location at the time of supply can be used as a place of consumption proxy (OECD, 2014c:13).

A special rule, instead of the place of performance²⁷ or usual place of residence of the customer²⁸, should be used to allocate taxing rights in a business-to-consumer context where the customer location is inappropriate and a proxy other than customer location would give a significantly better result, if measured against the same criteria (OECD, 2014c:10)²⁹. Special rules³⁰ should be used sparingly as they may lead to interpretational and application differences between tax jurisdictions and increase double and unintended non-taxation (OECD, 2015:56). Special rules should be measured against the consumption tax principles and should be considered as interconnected (OECD, 2015:56).

VAT jurisdictions generally rely on the location of tangible property to determine the place of supply of services and intangibles connected with tangible property or with the supply of such property (OECD, 2015:58-59). A special rule allocating the taxing rights to the jurisdiction where immovable goods are located may be appropriate if internationally traded services and intangibles are directly connected with the immovable goods³¹ (OECD, 2015:59-60). Such services include transfer, sale, lease or right to use, occupy, enjoy or exploit immovable goods; supplies of services physically provided to immovable goods such as construction, alteration and maintenance³²; or supplies of services and intangibles not falling into those

²⁷ OECD Guideline 3.7.

²⁸ OECD Guideline 3.8.

²⁹ OECD Guideline 3.7.

³⁰ That differ from the main rules in OECD Guidelines 3.2, 3.7, and 3.8.

³¹ OECD Guideline 3.8.

³² These services aim to change or maintain the physical status of the immovable property.

categories but with a direct link with immovable goods³³ (OECD, 2015:59-60). A special rule contemplates a close link between the supply and the immovable goods and a restrictive application (OECD, 2015:60). The immovable goods must be clearly identifiable, particularly with regard to composite supplies. Where the connection with immovable goods is only a part of the supply it will not result in the supply falling into one of the three categories (OECD, 2015:60). In addition to the use of immovable goods and services physically performed to or on the immovable goods, other services and intangibles may have a close link to the immovable goods (OECD, 2015:60). Taxation where the immovable goods are located could lead to a significantly better result than the general rule. A special rule, in addition to the close link, should also be more manageable and enforceable (OECD, 2015:60).

Services and intangibles connected with movable goods include services that are physically carried out on specific movable property such as repairs, alterations or maintenance of the property, and the rental of specific movable goods if it is considered to be a service (OECD, 2015:61). A place of supply rule based on the location of the movable goods to which the supply is connected may be more appropriate. VAT systems generally give temporary VAT relief in the jurisdiction where the supply is performed and the movable goods are located, if the goods are subsequently exported (OECD, 2014c:15). Applying the customer location rule will generally give an appropriate result for business-to-business supplies of services and intangibles connected with movable goods (OECD, 2015:61).

Table 4.8 below contains the place of internationally traded services and intangibles.

³³ Certain intellectual services, such as architectural services that relate to clearly identifiable, specific immovable property, could have a sufficiently close connection with immovable property.

Table 4.8: Place of internationally traded services and intangibles

Guideline	Description
3.1	<p align="center">Destination principle</p> <p>Supplies should be taxed in terms of the rules of the jurisdiction of consumption.</p>
3.2	<p align="center">Main rule for business-to business</p> <p>Supplies should be taxed at the customer location in applying the destination principle.</p>
3.3	<p align="center">Customer identity</p> <p>Customer identity, in determining customer location, is normally determined with reference to the business agreement.</p>
3.4	<p align="center">Customer established in more than one jurisdiction</p> <p>Supplies made to customers with establishments in more than one jurisdiction should be taxed where the establishments using the supplies are located, in determining customer location.</p>
3.5	<p align="center">Main rule for business-to-consumer supplies -Place of physical performance-</p> <p>The jurisdiction where the supply is physically performed, in applying the destination principle, should tax supplies (i) physically performed at a readily identifiable location, (ii) ordinarily consumed at the same time and place where physically performed, and (iii) which ordinarily require the physical presence of the person performing the supply and the person consuming the supplies at the same time and place where the supply is physically performed.</p>
3.6	<p align="center">Main rule for business-to-consumer supplies -Customer's usual residence-</p> <p>The jurisdiction where the customer has its usual residence, in applying the destination principle, should tax supplies not physically performed.</p>
3.7	<p align="center">Special rules</p> <p>Customer location should not be used to allocate taxing rights of business-to-business supplies where it is (i) inappropriate if measured against the consumption tax principles, and (ii) another proxy would have a significantly better result if measured against the same criteria.</p> <p>Where the taxing rights for business-to-consumer supplies can be allocated with reference to a proxy other than the place of performance and usual residence of the customer, when both the conditions above are met.</p>
3.8	<p align="center">Supplies directly connected with immovable property</p> <p>Supplies directly connected with immovable property, should be taxed in the jurisdiction where the immovable property is located.</p>

Source: OECD, 2014c:3-10

The place of supply of services or intangibles should not be affected by (i) onward supplies; (ii) provision of the services or intangibles to a third party business other than the customer; or (iii) the direction of the payment flows and the identity and location of the payer (OECD, 2014a:34).

The supplier's jurisdiction should be allowed to make supplies VAT-free to foreign customers identified in the business agreement and the customer's jurisdiction should ensure that the customer accounts for tax on the foreign supply, using the reverse charge mechanism, even if the services or intangibles are directly provided

by a local third party business (OECD, 2014a:34-35).

4.7.5 Collecting VAT from non-resident suppliers

VAT compliance is generally more burdensome on non-resident suppliers than on resident suppliers (OECD, 2014c:8). The reverse charge mechanism should apply to cross-border business-to-business supplies of services and intangibles that are taxable in the jurisdiction where the customer is located, where it is consistent with the overall VAT design. This minimises the administrative burden and complexity for non-resident suppliers and shifts the tax liability from the supplier to the customer, and relieves the non-resident supplier of foreign VAT obligations (OECD, 2014c:8). Compliance with reverse charging is generally low in business-to-consumer supplies and therefore not appropriate (OECD, 2014c:9).

Reverse-charging³⁴ has a number of advantages, namely (i) the tax authority in the jurisdiction of consumption can verify and ensure compliance since it has jurisdiction over the customer; (ii) if the compliance burden is shifted from the supplier to the customer it is minimised as the customer has full access to the details of the supply; (iii) administration costs for the tax authority are lower as the supplier is not required to meet local tax obligations; and (iv) reverse charging reduces the revenue risks associated with tax collection from non-resident suppliers (OECD, 2014a:34).

The most effective and efficient approach to collect VAT on supplies made by non-residents is to require the non-resident supplier to register for VAT in the foreign tax jurisdiction. A simplified registration and compliance regime can aid compliance by non-resident suppliers (OECD, 2014c:9). Greater international cooperation between revenue authorities and reciprocal and regular exchanges of information can enhance compliance of non-resident suppliers with their VAT obligations (OECD, 2015:76-77).

³⁴ The reverse charge mechanism is known as “imported services” in South Africa. South African “imported services” provisions only apply to business-to-consumer and non-taxable business-to-business supplies and differs from many other VAT systems.

4.8 SUMMARY

This chapter builds the theoretical framework of the study.

Taxation is generally considered to be an imposition on subjects to generate revenue for government, as opposed to regulate economic behaviour. Tax systems generally comprise of direct taxation (which imposes tax on persons) and indirect taxation (which imposes tax on transactions). Tax systems are evaluated against and should adhere to well-established properties of a good tax system. These properties include, first and foremost, fiscal adequacy or revenue generating capacity to fund government expenditure; equity (or fairness) which justifies tax imposition through the “ability-to-pay” or “benefit” principles; economic efficiency which mandates that taxation should not unduly create economic distortions; administrative efficiency which requires that the compliance cost of the taxpayer and the administration cost of government should be kept to a minimum and should not be disproportionate to the revenue collected. This requires that taxes should be, as far as possible, certain and simple to understand and comply with and flexible, to ensure that the tax system can adapt to changes required due to demand or changes in the political or economic environment.

Determining the incidence of tax is critical to ensure that the properties of a good tax system are complied with. Tax incidence differentiates between legal and economic incidence where legal incidence refers to the person on whom the tax is legally imposed. Economic incidence is of more importance to taxpayers and economists as it refers to the person who ultimately and economically bears the tax burden. These two incidences differ as taxes can be shifted from the person on whom the tax is legally imposed to another. The tax incidence of direct taxes on natural persons is less likely to be shifted, whereas the tax incidence of indirect taxes, such as VAT, is generally shifted away from the business that collects the tax to the consumer.

Moving to VAT, as the foremost indirect tax globally, it should be noted that forms of VAT were developed in Germany in the 1920s and implemented in France in the 1950s. VAT is now the most popular indirect tax system used globally and accounts

for approximately 1/5th of the tax revenue generated in the OECD and worldwide. The design of VAT systems differentiates between many factors, most notably including its economic base, whether it levies VAT inclusively or exclusively; how the VAT is calculated (which is a choice between at least eight methods); the treatment of capital goods; whether it is in terms of the destination or origin base; and finally whether it is a worldwide or territorial VAT system. Generally VAT systems apply VAT to final domestic consumption, levy VAT on the credit-invoice method; and apply the destination principle (which mandates taxation of final domestic consumption). Many VAT systems allow a choice between VAT inclusivity and exclusivity. Treatment of capital goods varies. Territorial VAT systems seek to tax supplies in their territory and start off with a narrower base than worldwide VAT systems. Worldwide VAT systems subject vendors' worldwide supplies to VAT and then narrow the base through exclusions and exceptions, some of which include zero rating provisions and provisions relating to foreign branches or main businesses.

Due to increased inter-jurisdictional supplies of goods and services, the necessity to determine the tax incidence or where a supply should be taxed and to which jurisdiction the tax revenue should accrue have become critical. Traditionally it was assumed that a supply takes place where the supplier is located, as cross-border supplies were limited. This is no longer the case. The concepts of proxies for the place of supply and consumption to determine or deem the place of consumption were developed to address these shortcomings. A lack of internationally harmonised and well-articulated place of supply rules can result in inter-jurisdictional conflicts, and double- or non-taxation. It is generally accepted that VAT systems should adhere to the destination principle, which mandates that they should seek to tax final domestic consumption. To this end, the OECD developed consumption tax principles (on the back of the Ottawa Taxation Framework), against which these proxies can be measured. The consumption tax principles include:

1. neutrality;
2. efficiency;
3. certainty and simplicity;
4. effectiveness and fairness; and

5. flexibility.

Place of supply proxies to determine consumption differentiate between internationally traded goods and services. Internationally traded goods do not pose significant problems as supplies of both movable and immovable goods are deemed to be supplied and consumed at the place of location of the goods at the time when the supply is made. Internationally traded services and intangibles, on the other hand, often present problems in determining where consumption takes place.

Place of supply rules for internationally traded services and intangibles differentiate between business-to-business supplies and business-to-consumer supplies. The main premise for both is that they should follow the destination principle, which seeks to tax consumption. The OECD has developed main rules, in acknowledgement of certain inadequacies (resulting from the nature of supplies), and recommended when special rules should be used and, in certain instances, recommend the nature of these special rules. These rules all presuppose adherence to the consumption tax principles.

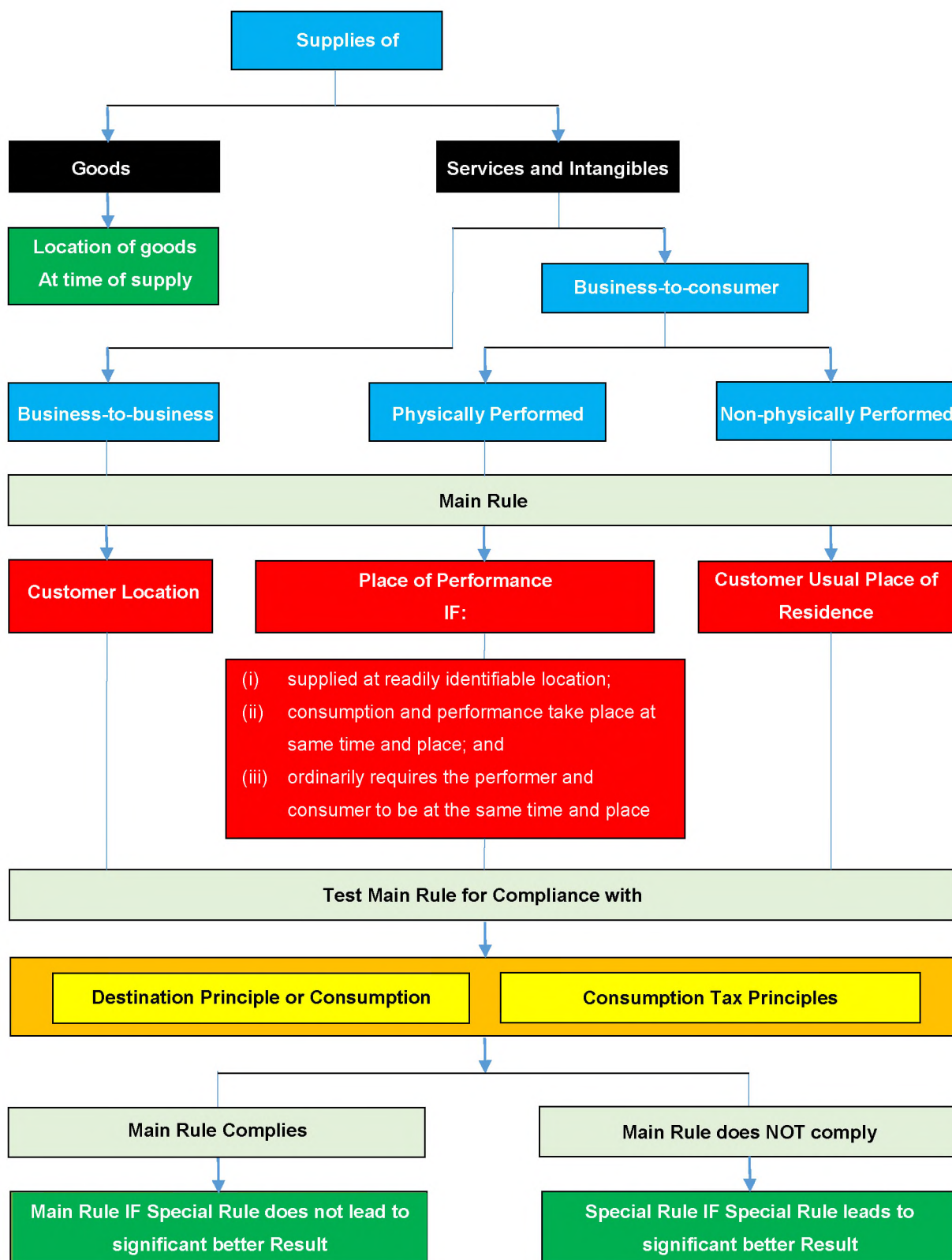
The main place of supply rule for business-to-business supplies provides that the supply should be taxed where the customer is located. Customer identity is determined with reference to business agreements entered into between the supplier and recipient. Where the customer has an establishment in more than one jurisdiction, the jurisdiction where the supply is used should prevail and tax the supply. Where the main place of supply rule for business-to-business supplies does not provide an appropriate approximation of place of consumption, does not adhere to the consumption tax principles, and where a special rule would give a significantly better result than the main rule and adheres to the consumption tax principles, a special rule should be used. The main rule may be inappropriate where services or intangibles are typically supplied to businesses and final consumers, services require the physical presence of the supplier and the customer and services are used at an identifiable location. The main rule may, in certain instances, impose a significant compliance burden where services or intangibles are supplied to volumes of customers for relatively small amounts in a short period of time, for example restaurant services. The main rule may also be inappropriate for the granting of

access (to concerts, sport games, trade fairs or exhibitions) designed for businesses. A special rule based on where the event takes place could meet the consumption tax principles and lead to a significantly better result.

The place of supply for business-to-consumer supplies has two main rules, differentiating between supplies physically performed and non-physically performed supplies. The main place of supply rule for business-to-consumer physically performed supplies provides that the jurisdiction where the supply is physically performed should tax the supplies if performed at a readily identifiable location; are ordinarily consumed at the same time and place of performance; and ordinarily require the physical presence of the person performing and the person consuming the supply at the same time and the same place of supply. The main place of supply rule for business-to-consumer non-physically performed supplies provides that the jurisdiction where the customer has its usual place of residence should tax the supplies. Where customer location for business-to-consumer supplies does not provide an appropriate approximation for place of consumption, does not adhere to the consumption tax principles, and where a special rule other than place of performance and usual residence of the customer would give a significant better result than the main rules and adheres to the consumption tax principles, a special rule should be used.

VAT can be collected from non-residents in a number of manners. The reverse charge mechanism should ideally be used for cross-border business-to-business supplies of services and intangibles that are taxable in the jurisdiction where the customer is located, where it is consistent with the overall VAT design. As compliance with reverse charging is generally low for business-to-consumer supplies it is inappropriate. The most effective approach is to require the non-resident supplier to register for VAT in the foreign tax jurisdiction through a simplified registration and compliance regime. Greater international cooperation between revenue authorities and reciprocal and regular exchanges of information should be explored to enhance compliance of non-resident suppliers with their VAT obligations. Table 4.9 below illustrates the decision tree to follow in determining the place of supply rules that apply to goods and services and intangibles.

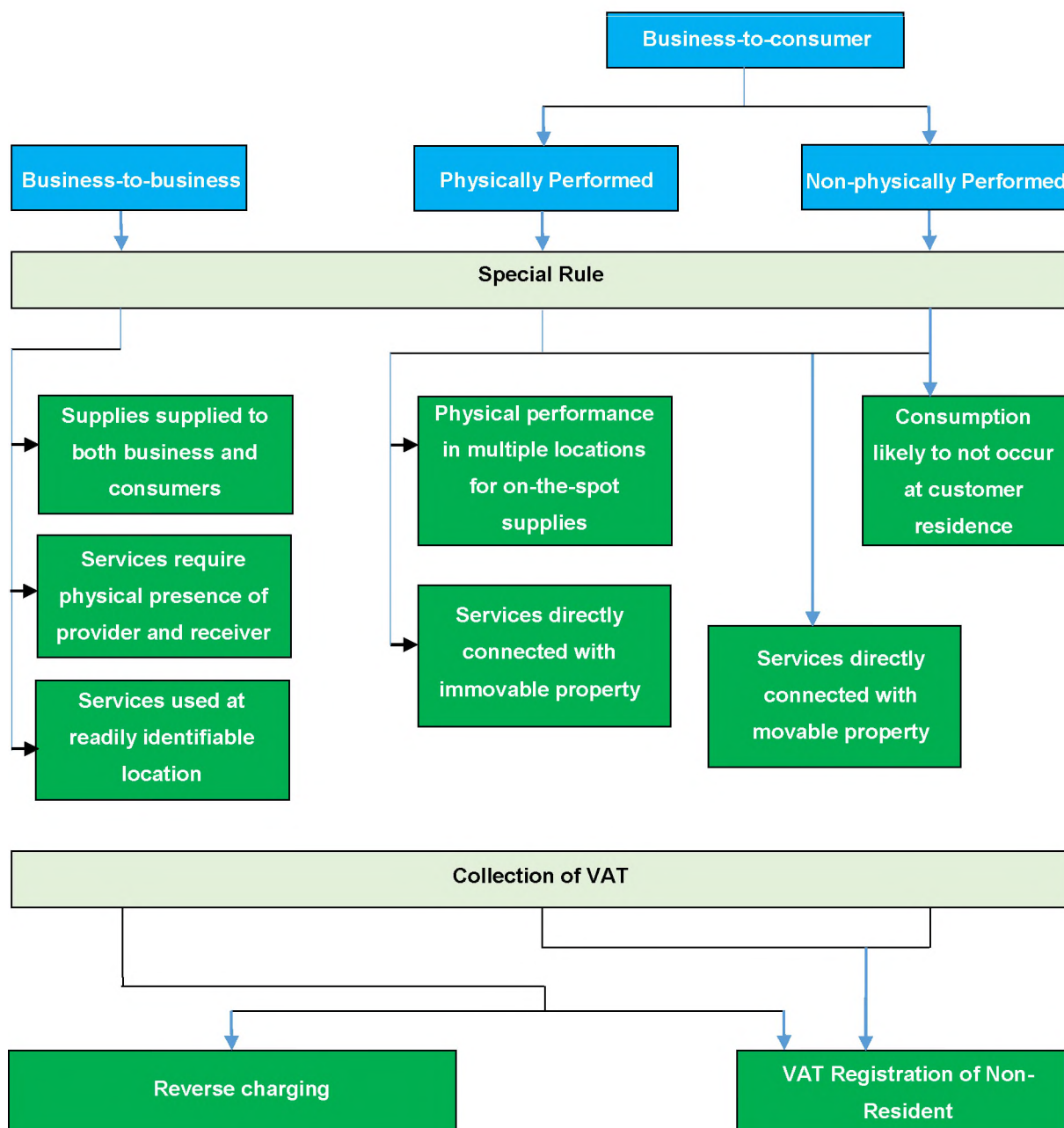
Table 4.9: Place of supply decision framework



Source: Own design - from OECD place of supply rules

Table 4.10 below illustrates the decision tree to follow in determining when special place of supply rules should be applied to services and intangibles and how VAT should be collected.

Table 4.10: Special rules for services and intangibles and VAT collection



Source: Own design - from OECD place of supply rules

This chapter has provided a detailed discussion of the theoretical basis for levying VAT on the supply of goods and services, both nationally and internationally. The

supply of goods within a jurisdiction poses few place-of-supply problems. The focus of this thesis is primarily on the broader concept of inter-jurisdictional rules in a VAT system and place-of-supply of services as a sub-set thereof. To this end, the following chapter deals with inter-jurisdictional VAT rules in South Africa.

CHAPTER 5: INTER-JURISDICTIONAL VAT RULES IN SOUTH AFRICA

5.1 INTRODUCTION

As stated in chapter 2 of this study, the objective of the research is to consider the current inter-jurisdictional rules in the VAT system of South Africa, with a view to determine shortcomings and propose legislative changes or additions to address these shortcomings. The study specifically sets out to make recommendations addressing the following:

- non-resident VAT registration;
- inter-jurisdictional VAT rate;
- imported services; and
- place of supply rules.

As a result, the objective of this chapter is to describe the current inter-jurisdictional VAT rules in the South African VAT system and determine the shortcomings in order to ultimately make detailed recommendations in Chapter 7. The various concepts and definitions, especially where they relate to cross-border transactions and a VAT enterprise, are dealt with in detail. The chapter specifically considers the current rules applicable to non-residents and their obligations to register for VAT purposes, or not to register. The chapter proceeds to consider the current inter-jurisdictional VAT rules applicable to supplies of goods and services and also considers current shortcomings in the VAT system. The introduction of specific place of supply rules in the South African VAT system is considered further, particularly a framework for defining place of supply rules, non-resident VAT registration, and rules governing VAT rates applicable to supplies of goods and services. The chapter relies to some extent on responses received from a panel of VAT experts (in South Africa, and to a limited extent outside of South Africa) on a questionnaire devised for purposes of this study, as described in detail in Chapter 3 (the Research Design chapter).

The South African VAT system is a tax on final domestic consumption, which taxes

imported goods and certain imported services and zero rates most exports of goods and services (Schneider, 2012). The VAT Act imposes tax on a vendor's worldwide supplies and then narrows the scope of the tax without relying on specific place of supply rules used in "territorial" VAT systems (Schenk, 2012). The VAT system can, as a result, be described as a worldwide tax system. The VAT system uses two base-reduction measures to align its worldwide scope more closely to a territorial VAT system, namely the definition of "enterprise" and the zero rating provisions³⁵. The VAT system requires a registered vendor³⁶ to report supplies connected with its enterprise, wherever they occur³⁷ (Schenk, 2009:6-9). The VAT system levies VAT on four broad categories of taxable supplies or events, namely:

- supplies of goods or services made by a vendor in the course or furtherance of an enterprise³⁸;
- importation of goods³⁹;
- use or consumption of certain imported services⁴⁰; and
- certain deemed supplies⁴¹.

As place of supply rules flow naturally from a territorial VAT system, adoption of place of supply rules in South Africa could be done by converting the VAT into a territorial VAT (Schenk, 2012). The entire VAT system should be considered to determine whether legislative changes should be effected to convert VAT into a

³⁵ The exclusion from the VAT net of supplies between a branch and main business outside the country is an example of a mechanism to eliminate some supplies from the scope of the worldwide tax net (de Wet, 2012 and Schenk, 2012).

³⁶ Section 1(1) of the Value-Added Tax Act, Act 89 of 1991 (the VAT Act) defines a "vendor" as a person who is registered or is required to register. A person is required to register if that person conducts an enterprise and, in connection with that enterprise, makes taxable supplies exceeding a threshold amount.

³⁷ VAT is imposed by section 7(1) of the VAT Act. These rules, although not "place of supply" rules, impact the scope of VAT (Schenk, 2009:9).

³⁸ Section 7(1)(a) of the VAT Act.

³⁹ Section 7(1)(b) of the VAT Act.

⁴⁰ Section 7(1)(c) of the VAT Act.

⁴¹ Section 8, proviso (ii) to the definition of "enterprise" in section 1(1), and section 18(3) of the VAT Act.

territorial system. Whether Government has the political will and public support to convert the South African VAT system to a territorial VAT system is a critical success factor (Schenk, 2012). VAT principles should be harmonised internationally and place of supply rules should be clear and unambiguous (Davis VAT Report, 2015:77-86). The Davis VAT Committee recommended that South Africa adopt a main place of supply rule. The Davis VAT Committee also recommended that consideration be given to implementing an effective VAT refund mechanism for non-resident suppliers to enable them to claim input tax deductions in respect of taxable goods and services acquired, similar to recent New Zealand VAT amendments (Davis VAT Report, 2015:77-88).

The next section is dedicated to a description of the inter-jurisdictional VAT rules in South Africa.

5.2 CURRENT INTER-JURISDICTIONAL VAT RULES

The VAT Act, when introduced in 1991, arguably contained relatively adequate zero rate rules to compensate for the lack of formal place of supply rules (Terblanche, 2012). However, as the world economy globalised it resulted in increased cross-border transactions and an increase in “difficult to tax” types of supply, such as intangible property. The South African VAT system applies the destination principle and aims to tax final domestic consumption. The VAT system contains various inter-jurisdictional VAT rules, which relate to cross-border supplies of goods and of services, and also deal with foreign persons and their liability to register for VAT or not. However, South Africa has not yet adopted formal place of supply rules termed as such. The place of consumption, where a supply takes place, or where an activity or enterprise is conducted, is generally used to determine the VAT rate and whether a VAT registration obligation is created. These “places” are not expressly stated in the VAT Act and often need to be assumed through a study of the legislation. This is not ideal as it creates uncertainty. This uncertainty is exacerbated in case of “virtual” supplies, such as supplies of electronic commerce, telecommunication services, intellectual property services and other intangible property services. This is substantiated by the large number of applications to SARS for rulings, the number of

rulings issued by the SARS, and the number of disputes with regard to the taxability of supplies or the application of the rate of zero percent (Badenhorst, 2011). The definition of a VAT “enterprise”, the exemption and zero rating provisions relating to certain cross border transactions, and the VAT on imported services provisions give some guidance on the place of consumption, supply, or enterprise or activity. The place of consumption, supply, or “enterprise or activity” rules in respect of goods in the VAT Act generally provide clear guidance, but this is not without exceptions. For example, the VAT Act intends to zero rate consumption of movable goods by foreign businesses in South Africa⁴², but SARS arguably holds the view that the provision only applies to goods which are physically used outside South Africa (Terblanche, 2012). The South African VAT system, for example, also does not cater effectively for foreign aircraft and ships with South African ties (van Heerden, 2012).

A description follows of the South African VAT provisions that directly or indirectly pertain to inter-jurisdictional rules.

5.2.1 Enabling legislation

The VAT Act contains certain enabling definitions used in respect of enterprise activities and the supply of goods and services, which are considered below. Definitions specific to inter-jurisdictional supplies of goods and services, non-resident VAT registration, and reverse charging, are discussed in sections elsewhere in this chapter.

Taxable supply

A “taxable supply”⁴³ is a supply of goods or services which is subject to VAT at the standard rate⁴⁴ or zero rate⁴⁵. VAT is levied on:

...the supply by any vendor of goods or services supplied by him...in the course or furtherance of any enterprise carried on by him...calculated at the

⁴² In terms of section 11(1)(d) of the VAT Act.

⁴³ Section 1(1) of the VAT Act.

⁴⁴ Section 7(1)(a) of the VAT Act.

⁴⁵ Section 11 of the VAT Act.

rate of 14 per cent on the value of the supply...⁴⁶

It can therefore be deduced that a supply is subject to VAT, if the following requirements are met:

- a supply,
- by a vendor,
- of goods or services,
- in the course or furtherance of an enterprise⁴⁷.

Certain deeming provisions widen the scope of the term “supply”, including⁴⁸:

- Where a single supply consists of more than one element and if separate considerations had been payable, some of the elements would have been charged at the standard rate, whilst others would have been charged at the zero rate, each element is deemed to be a separate supply⁴⁹.
- An agent who is a registered VAT vendor and acts for a non-vendor foreign principal, is entitled to claim VAT paid on goods imported into South Africa on behalf of the foreign principal as an input tax deduction if the goods are imported by the foreign principal to make a supply to a person in South Africa and the foreign principal does not reimburse the agent for the VAT⁵⁰. The agent is deemed to make a supply of the imported goods to the principal's customer in South Africa⁵¹.

⁴⁶ Section 7(1)(a) of the VAT Act, which is known as the charging section.

⁴⁷ Section 7(1)(a) of the VAT Act.

⁴⁸ Mainly through sections 8, 18(3), and proviso (ii) to the definition of “enterprise” in section 1(1) of the VAT Act.

⁴⁹ Section 8(15) of the VAT Act.

⁵⁰ Section 54(2A) of the VAT Act.

⁵¹ Section 8(20) of the VAT Act.

Non-taxable supply

Supplies made by non-vendors⁵² are not subject to VAT in South Africa, other than for VAT on imported services. Certain supplies are subject to exemption and although no VAT is charged on exempt supplies, VAT becomes an inherent cost in the provision of such supplies as suppliers are not entitled to claim VAT on expenses incurred as input tax deductions⁵³. Although supplies which are subject to the zero rate are also not subject to a VAT charge (other than 0%), VAT is removed from the supply as the registered vendor making the supply is entitled to claim VAT on expenses incurred relating to such supply as an input tax deduction⁵⁴.

Taxable importations

The South African VAT system subjects most imports of goods⁵⁵ and certain imports of services to VAT⁵⁶. The importation of goods and certain services into South Africa is a taxable event, irrespective of whether the importer is registered for VAT purposes or the nature of the goods or services. VAT is levied on the importation of goods into South Africa by a person at 14% on the value of the importation⁵⁷. Only goods which are considered to be entered for home consumption are deemed to be imported and subject to VAT⁵⁸. Where goods are imported and entered into a licensed Customs and Excise warehouse (a bonded warehouse), but have not been entered for home consumption, VAT only becomes payable when the goods are removed from bond⁵⁹. Only a registered vendor can potentially claim the VAT incurred on the importation of goods into South Africa as an input tax deduction⁶⁰.

⁵² As opposed to a non-registered vendor.

⁵³ Section 16(3) read with the definition of "input tax" in section 1(1) of the VAT Act prohibits the claiming of VAT incurred on expenses to make supplies other than taxable supplies.

⁵⁴ The prohibition on VAT incurred on expenses to make exempt supplies does not apply to the making of zero rating supplies.

⁵⁵ Section 7(1)(b) of the VAT Act.

⁵⁶ Section 7(1)(c) of the VAT Act.

⁵⁷ Section 7(1)(b) read with section 13 of the VAT Act.

⁵⁸ Section 13(1) of the VAT Act.

⁵⁹ Section 13 of the VAT Act.

⁶⁰ The extent of the input tax deduction is determined by the definition of "input tax" in section 1(1) of the VAT Act, read with section 16 and 17 which contain specific denials.

Liability to pay VAT

A supply is only subject to VAT if made by a vendor. A “vendor” is defined as “any person who is or is required to be registered”⁶¹. Supplies made by a vendor in the course or furtherance of an enterprise are subject to VAT. The person who conducts the enterprise is liable to account for VAT and not the enterprise. This is important when considering the VAT registration threshold. All the taxable supplies made by a person are taken into account, even though they may be made in the course of different enterprises, in determining whether the person should be VAT registered. When a person becomes liable to register, all of its business activities or enterprises are subject to VAT. A person only becomes liable to account for tax if it makes supplies of goods or services in the course or furtherance of an enterprise and its taxable supplies exceed the VAT registration threshold. A vendor is, therefore, a person conducting an enterprise or enterprises in the course of which it makes taxable supplies of goods or services exceeding the VAT registration threshold⁶². A person can also voluntarily register for VAT purposes if its turnover exceeds the voluntary registration threshold⁶³. VAT registration does not depend on the supplier's place of residence. A foreign person is, as a result, obliged to register as a vendor if it conducts an enterprise in or partly in South Africa, irrespective of whether it is a resident of South Africa.

Supply

The term “supply” is an integral part of the imposition of VAT and is defined in broad terms to include:

performance in terms of a sale, rental agreement, instalment credit agreement and all other forms of supply, whether voluntary, compulsory or by operation of law, irrespective of where the supply is effected, and any derivative of ‘supply’ shall be construed accordingly⁶⁴

⁶¹ Section 1(1) of the VAT Act.

⁶² Section 23 of the VAT Act. The compulsory VAT registration threshold is where taxable supplies exceed or are expected to exceed R1 000 000 per annum.

⁶³ Section 23 of the VAT Act. The voluntary registration threshold is R50 000 per annum. Special rules apply to suppliers of electronic services in terms of section 1(1) and section 23 of the VAT Act.

⁶⁴ Section 1(1) of the VAT Act.

South Africa places reliance, to some extent, on foreign VAT precedent (De Koker and Jenkinson, 2011). New Zealand and United Kingdom courts have often interpreted the term “supply”, and the following general conclusions can be applied in the South African VAT context:

- The ordinary meaning of “supply” is to furnish or to serve.
- A supply requires at least two parties, namely a supplier and a recipient.
- A person cannot self-supply, unless legislation permits.
- A supply of goods comprises the passing of possession in goods by agreement in terms of which the supplier agrees to part with and the recipient agrees to take possession. Possession refers to control over the goods or immediate access to their use, which may or may not involve the physical removal of the goods.
- The provision of consignment goods does not constitute a supply, as possession or ownership does not pass to the consignee. A supply includes a sale but does not have to be a sale.
- If a sale occurs and the contract is void, VAT must still be charged.
- The sale of illegal items is subject to VAT.
- A supply includes sales, gifts, rental agreements, instalment credit agreements, financial leases, the provision of goods and services, and goods and services which have been applied for the vendor’s private use, the vendor’s family or an employee, subsequent to acquisition for business purposes. Most transactions therefore constitute supplies (De Koker and Jenkinson, 2011).

5.2.2 Non-resident VAT registration

Enterprise

An area of uncertainty in the VAT Act is what constitutes an “enterprise”, particularly for non-residents without a fixed place of business in South Africa (Theron, 2012). Supplies made in the course or furtherance of a vendor’s enterprise, constitute taxable supplies⁶⁵. Unless a person meets the VAT threshold requirement to be registered for VAT, or registers voluntarily for VAT, and carries on an enterprise and

⁶⁵ Section 7(1)(a) of the VAT Act.

makes supplies in the course or furtherance of that enterprise, the person may not register and account for output tax or claim VAT on expenses incurred as an input tax deduction⁶⁶. VAT is therefore not levied on supplies made outside of the course or furtherance of an enterprise.

The New Zealand courts have stated the following regarding the phrase “in the course of furtherance of a taxable activity”, which is the New Zealand equivalent of an “enterprise”:

...it is a question of fact and degree as to whether a supply is in the course of furtherance of a taxable activity carried on by the person concerned. There must obviously be a discernible relationship between the supply and the activity in the form of a nexus for the supply to be in the course or furtherance of the activity (New Zealand, 1988).

...An act done for the purpose or object of furthering the taxable activity, or achieving its goal, can be to help, achieve, or advance, and thus a ‘furtherance’ of a taxable activity, although it may not necessarily be always in the course of that taxable activity (New Zealand, 1991).

The term “enterprise” is defined, firstly, by way of a general provision and, secondly, by way of specific inclusions and exclusions⁶⁷. To some extent, the definition of “enterprise” contains an equivalent of “place of supply rules”. The concept of when an activity is carried on continuously or regularly in South Africa is not defined. The general definition of “enterprise” provides that:

...in the case of any vendor other than a local authority, any enterprise or activity which is carried on continuously or regularly by any person in...or partly in the Republic...in the course or furtherance of which goods or services are supplied to any other person for a consideration, whether or not for profit...⁶⁸

⁶⁶ Section 7(1)(a) read with section 23 of the VAT Act.

⁶⁷ Section 1(1) of the VAT Act.

⁶⁸ Paragraph (a) of the definition of “enterprise” in section 1(1) of the VAT Act.

It can therefore be concluded that an “enterprise” comprises of seven components, namely:

- an enterprise or activity carried on
- continuously or regularly
- by a person
- in or partly in South Africa
- in the course of which goods or services are supplied
- to another person
- for a consideration, whether or not for profit.

These components are discussed in more detail below.

Enterprise or activity

The first and primary defining requirement of the definition of enterprise is that an “enterprise or activity” must be carried on. The following factors established by the Courts and Tribunals of the United Kingdom have been used in South Africa as guidance as to whether an “enterprise or activity” exists:

- Is it a serious undertaking earnestly pursued or a serious occupation, not confined to commercial undertakings?
- Is it an occupation or function actively pursued with reasonable or recognizable continuity?
- Does the undertaking have substance, as measured by the value of taxable supplies?
- Is the undertaking properly organized in a regular manner, using recognized business principles?
- Is the undertaking mainly concerned with supplies made to customers for a consideration?
- Does the undertaking involve the making of taxable supplies, commonly made by others with a view to making a profit? (De Koker and Jenkinson, 2011: paragraph 4.4.1)

These factors, although important, are not conclusive in determining the existence of an enterprise. The activity and its nature must be examined in its entirety to

establish whether an enterprise exists (De Koker and Jenkinson, 2011: paragraph 4.4.1). A person's worldwide supplies are arguably drawn into the VAT net only to the extent that the supplies are generated by the "enterprise or activity" in South Africa (Meyburgh, 2011). However, where a person conducts an "enterprise" (e.g. a main business), its worldwide supplies would arguably then emanate from this enterprise and would be included in the definition of "enterprise" (Prinsloo, 2012). The VAT Act does not define "enterprise or activity" and does not prescribe whether the "activity" consists of physical, economic or legal activities. The use of "enterprise" in the definition of "enterprise" potentially creates a circular reference⁶⁹. According to Glyn-Jones (2012) consideration could be given to substituting the word "enterprise" used in the definition of "enterprise" with "business" or "business activity". Although it could be argued that only a physical activity in South Africa should give rise to a VAT "enterprise",⁷⁰ it is likely that a contractual or economic activity would also give rise to a VAT enterprise (Rudolph, 2011). The phrase "enterprise or activity"⁷¹ should therefore be interpreted more widely (and be given its normal meaning) than the definition of "enterprise" and may be construed as encompassing both physical and economic activities (van Heerden, 2012)⁷².

The word "enterprise" means a project or undertaking, especially one that requires effort, whereas "activity" means the state or quality of being active, lively action or movement, any specific action, pursuit, etc.⁷³. The word "enterprise" also suggests a large project, a business or a company and "activity" includes a situation in which things happen or are done, involving busy or energetic action or movement⁷⁴. The

⁶⁹ The use of the word "enterprise" in the definition of "enterprise" in section 1(1) of the VAT Act can only be relied on to the extent that the context does not indicate otherwise, which is the case. As such, the ordinary meaning of "enterprise", where used in the definition of "enterprise", should be used.

⁷⁰ New Zealand uses the term "taxable activity". A principle similar to the New Zealand "force of attraction" principle should be considered for South Africa (Glyn-Jones, 2012).

⁷¹ Glyn-Jones (2012) argues that substituting "taxable activity" with "enterprise" will increase uncertainty.

⁷² Connell (2011), Chauke (2011) and Watson (2011) all support the contention that "activity" should be given a wider all encompassing, including economic, meaning.

⁷³ The New Collins Concise Dictionary.

⁷⁴ The Compact Oxford English Dictionary.

Oxford Dictionary⁷⁵ defines “activity” as “being active; being busy; actions” or “taking part in activities; functioning; in operation”. As the terms “enterprise” or “activity” are integral components of, and wider than “enterprise” they cannot merely be substituted by “business activity”, whether physical or economic, as “business activity” only envisages an activity carried on for profit, whereas “enterprise or activity” includes activities that are not necessarily only carried on for profit (National Treasury, 2012). Should “activity” include physical and non-physical (such as economic) actions or the making available of rights to use intellectual property, this could result in an enterprise conducted in or partly in South Africa. Where the view is adopted that the making available of a right for consideration, whether it be through formal registration, patent or license, is not a physical activity and does not comprise an “enterprise or activity” for purposes of the definition of “enterprise”, such interpretation (if adopted globally) could lead to double non-taxation of the rights for VAT purposes. The making available of intellectual property rights is generally done through the registration of a patent or trademark. If such patent or trademark is registered in South Africa and results in royalty income, these circumstances could arguably give rise to an “enterprise” for VAT purposes.

SARS’ VAT News 13 of December 1999 provided that foreign licensors receiving royalty income from South Africa (as a result of making rights available in South Africa) could become subject to VAT registration (SARS, 1999). SARS (2011b) ruled (on 8 June 2011) that a foreign franchisor with no fixed place of business or activities in South Africa, other than the franchise agreement with a local franchisee in terms of which royalty payments were paid to the foreign franchisor, did not constitute an “enterprise”. SARS, in VAT News 37 of February 2011 (SARS, 2011a), held the view that intangible property made available by a foreign enterprise for use in South Africa is a passive activity and that the foreign enterprise would not be required to register for VAT. However, the making available of intangible property in South Africa by a foreign business without a place of business in South Africa could in certain instances potentially create a VAT “enterprise” (National Treasury, 2012). A distinction could potentially also be drawn between intellectual property situated or registered in South Africa and situated or registered in a foreign jurisdiction (Theron,

⁷⁵ The Compact Oxford English Dictionary.

2012). Intellectual property situated or registered in South Africa and owned by a non-resident, could arguably result in supplies originating from South Africa, as the intellectual property is made available or exploited from South Africa. This may constitute an “activity” and create an “enterprise”. Intellectual property situated or registered outside of South Africa and owned by a non-resident, and made available for use in South Africa would arguably not create a VAT “enterprise” if the non-resident has no other activities in South Africa. The making available of the use of the foreign registered intellectual property would arguably also not constitute an “activity” in South Africa (Theron, 2012). Assuming that the intangible property is made available where the grantor is located⁷⁶, the continuous making available thereof in South Africa by a foreign business would not create a VAT “enterprise”⁷⁷ (Badenhorst, 2011). It should then be explored whether a South African based enterprise that owns intangible property in a foreign country and makes it available for use in South Africa with no other activities in South Africa, would create an “enterprise” in South Africa.

Continuously or regularly

The second requirement of “enterprise” is that the “enterprise or activity” must be carried on “continuously or regularly”. The VAT Act does not define “continuously or regularly”. The New Zealand Taxation Review Authority in Case N27 (1991) 13 NZTC 3,229, interpreted the word “continuously” with regard to activity, as one that:

...has not ceased in a permanent sense, or has not been interrupted in a significant way (CCH New Zealand Limited, 1998:21-200).

⁷⁶ VAT Case 179.

⁷⁷ On the assumption that the foreign enterprise does not:

- (i) have a presence in South Africa; and
- (ii) carry on an enterprise or activity in or partly in South Africa by making available intellectual property for use in South Africa.

The New Zealand Taxation Review Authority interpreted the word “regularly” with regard to activity, as:

...a steadiness or uniformity of action, or occurrence of action, so that it recurs or is repeated at fairly fixed times, or at generally uniform intervals, to be of a habitual nature and character... (CCH New Zealand Limited, 1998:21-200).

The words “continuously” and “regularly” arguably complement one another, where “regularly” is concerned with repeated actions and “continuously” with an ongoing assignment or assignments (De Koker and Jenkinson, 2011:paragraph 4.4.1). A once-off transaction, project, or supply that comprises continuous or regular activities can create a VAT “enterprise”⁷⁸. The phrase “continuously or regularly” refers to the activity carried on, which should result in the supply of goods and services, and not to the supply in itself (Meyburgh, 2011). An occasional “enterprise or activity” may, in certain instances, not create a VAT “enterprise” (Badenhorst, 2011). The nature of a once-off event (for example a once-off concert), must be considered carefully as the actions surrounding the event may entail continuous or regular activities and create a VAT “enterprise” (Theron, 2012). An activity is “continuous” if there is no significant cessation or interruption of the activity (Badenhorst, 2011). Temporary interruptions in the activity for holiday or health reasons, for example, should not disqualify the activity from being “continuous”. An activity is “regular” if it is repeated at reasonably fixed intervals. To constitute an “enterprise”, the activity needs only be “continuous” or “regular”. An occasional activity can, as a result, be carried on “regularly” if it is repeated at reasonably fixed intervals, taking into account the type of supply and the time it took to complete the activities associated with the supply (Badenhorst, 2011).

Person

The third requirement of the definition of enterprise is that the enterprise or activity carried on continuously or regularly must be carried on by a “person”. The term

⁷⁸ All the respondents to the questionnaire agreed that a once-off transaction or event with continuous or regular activities could create a VAT “enterprise”.

“person” includes:

...any public authority, any local authority, any company, any body of persons (corporate or unincorporate), the estate of any deceased or insolvent person and any trust fund...⁷⁹

A body of persons, corporate or unincorporate, other than a company, is treated as a person separate from its members, and should register for VAT purposes in respect of any enterprise activity carried on independently from its members. Where a partnership carries on an enterprise it, and not its partners, is required to register for VAT purposes⁸⁰.

The activities of an agent in South Africa could arguably draw a foreign supplier into the VAT net⁸¹ (Theron, 2012). In *South African Rugby Football Union v Commissioner for SARS*⁸² the Supreme Court of Appeal held that the foreign entity complied with the definition of “resident of South Africa” and that it:

...was physically represented in South Africa through accredited employees and agents to enable it to carry on its business of exploiting commercial rights at the various venues in South Africa for the duration of the tournament...

A foreign principal can therefore, arguably, by virtue of its agent’s activities and supplies, create a VAT “enterprise” if it is a dependent agent that can conclude contracts and effect supplies for and on behalf of the principal (van Heerden, 2012). Where a non-resident with no direct activities in South Africa outsources certain activities to a sub-contractor these activities, in isolation, would not create a VAT “enterprise” for the non-resident (Meyburgh, 2011).

In or partly in South Africa

The fourth requirement of the definition of “enterprise” is that the person who carries

⁷⁹ Section 1(1) of the VAT Act.

⁸⁰ Section 51(1), read with the definition of “person” in section 1(1) of the VAT Act.

⁸¹ Or, alternatively, through a specific rule introduced into section 54 of the VAT Act.

⁸² [1999] 4 All SA 444 (A), 61 SATC 406.

on the “enterprise or activity” continuously or regularly must carry it on in or partly in South Africa (the Republic). The term “Republic” in the definition of “enterprise” is used with reference to the “enterprise or activity” that is carried on⁸³. To comply with this requirement of the definition of “enterprise”, an “enterprise or activity” must be carried on “in...or partly in the Republic” in the course or furtherance of which goods or services are supplied. Supplies made anywhere in the world could therefore potentially attract VAT if made through an enterprise or activity carried on continuously or regularly in or partly in South Africa. The term “Republic” is defined in the geographical sense to mean:

...the territory of the Republic of South Africa and includes the territorial waters, the contiguous zone and the continental shelf...⁸⁴

Although the wording of the definition of “Republic” is clear and unambiguous, it may be difficult to attribute certain activities and supplies to a specific geographical area (Theron, 2012). Examples of such activities and supplies include:

- activities in cyber space (Theron, 2012);
- satellites situated directly above South Africa (Badenhorst, 2011);
- goods supplied in a duty free area to non-residents qualify for the zero rate, but services do not⁸⁵ (Badenhorst, 2011);
- certain services supplied directly in respect of movable property situated in an export country at the time the services are rendered can be zero rated⁸⁶; the VAT Act does not provide guidance as to when movable property (which includes intangible property) is deemed to be situated outside South Africa; and
- services supplied locally by a local supplier to a “resident” (albeit the foreign branch of a local main business) cannot be zero rated⁸⁷, irrespective of where the supply is consumed (Badenhorst, 2011); the problem could be addressed by excluding from the ambit of “resident of the Republic” the foreign “branch or main

⁸³ This was the unanimous view of all the participants in the questionnaire.

⁸⁴ Section 1(1) of the VAT Act.

⁸⁵ SARS General Written Ruling 440 (withdrawn).

⁸⁶ Section 11(2)(g)(i) of the VAT Act.

⁸⁷ Section 11(2)(l) of the VAT Act.

business” of a local concern⁸⁸ (Meyburgh, 2011).

The term “resident of the Republic” means:

a person (other than a company) who is ordinarily resident in the Republic or a... domestic company as defined in section 1(1) of the Income Tax Act: Provided that any other person or any other company shall be deemed to be a resident of the Republic to the extent that such person or company carries on in the Republic any enterprise or other activity and has a fixed or permanent place in the Republic relating to such enterprise or other activity⁸⁹.

The term “resident of the Republic” does not assist in determining when a person conducts an “enterprise” and becomes liable to register as a vendor. It only serves to categorise persons to whom certain supplies may be zero-rated (Theron, 2012). However, the definitions of “Republic” and “resident of the Republic” define, to some extent, the jurisdictional reach of VAT (Schenk, 2012)⁹⁰. The word “enterprise” used in the definition of “resident of the Republic” should be ascribed its defined meaning⁹¹, whereas the word “enterprise” used in the definition of “enterprise” should be given its ordinary meaning (Rudolph, 2012)⁹².

The VAT Act does not define the term “fixed or permanent place in the Republic”, which may create ambiguity in certain instances (Meyburgh, 2011). SARS could consider publishing guidelines similar to those of the HM Customs and Excise on what comprises a fixed or permanent establishment⁹³ (Badenhorst, 2011).

⁸⁸ If proviso (ii) to the definition of “enterprise” applies.

⁸⁹ Section 1(1) of the VAT Act.

⁹⁰ The term “resident of the Republic” is mainly defined for purposes of sections 11(2)(l) and 14 and VAT on imported services by a “resident” (Badenhorst, 2011).

⁹¹ As in section 1(1) of the VAT Act.

⁹² Section 1(1) of the VAT Act provides definitions, subject to “unless the context otherwise indicates”.

⁹³ See VAT Notice 741A (United Kingdom, 2010).

Alternatively, it could be considered to adopt the Income Tax treatment of a fixed or permanent place of business (van Heerden, 2012).

The term “resident of the Republic” could be linked to the place of supply of foreign suppliers to determine the VAT treatment of cross-border supplies and the VAT registration in South Africa. This would make the place of supply dependent on the VAT residency status of the supplier (Rudolph, 2012). However, if the term “enterprise” is clearly defined to determine when a person becomes liable to register for VAT, the definition of “resident of South Africa” would not have to be linked to the definition of “enterprise” since the use of the word “enterprise” in the definition of “resident of South Africa” would then revert to the defined term (Badenhorst, 2011).

Goods or services

The fifth requirement of the definition of enterprise is that the person must carry on the enterprise or activity continuously or regularly in or partly in South Africa “in the course of which goods or services are supplied”.

Other person

The sixth requirement of the definition of enterprise is that the person must carry on the enterprise or activity continuously or regularly in or partly in South Africa in the course of which goods or services are supplied “to any other person”.

Consideration

The seventh requirement of the definition of enterprise is that the person must carry on the enterprise or activity continuously or regularly in or partly in South Africa in the course of which goods or services are supplied to any person “for a consideration, whether or not for profit”. The term “consideration”, in relation to the supply of goods or services to a person, includes:

...any payment made or to be made...whether in money or otherwise, or any act or forbearance, whether or not voluntary, in respect of, in response to, or for the inducement of, the supply of any goods or services, whether by that person or by any other person...⁹⁴

⁹⁴ Section 1(1) of the VAT Act.

The term “consideration” does not include payment made by a person as a donation to an association not for gain. A deposit, whether refundable or not, in respect of a supply of goods or services is not seen as payment for a supply until the supplier applies it as consideration for the supply or the deposit is forfeited.

Inclusions, exclusions and exceptions

In addition to the general definition of “enterprise”⁹⁵, the definition also contains certain inclusions, such as:

...any enterprise or activity carried on in the form of a commercial, financial, industrial, mining, farming, fishing or professional concern or any other concern of a continuing nature or in the form of an association or club...

Other special rules in the definition of “enterprise” include, for example, that:

- The rendering of services as employee, to the extent that the employee receives remuneration, is excluded from “enterprise”⁹⁶.
- Exempt supplies are excluded from “enterprise”⁹⁷.
- Goods and services supplied outside South Africa by a separately identifiable branch or main business of a South African concern, permanently located at premises outside South Africa, which maintains a separate, independent accounting system, are deemed to be supplied by a separate person⁹⁸.
- Underwriting insurance business by Underwriting Members of Lloyd's of London, to the extent that the contracts are concluded in South Africa, is deemed to be an “enterprise”⁹⁹.
- Certain supplies of electronic services by foreign suppliers are deemed to be an “enterprise”¹⁰⁰.

⁹⁵ Section 1(1) of the VAT Act.

⁹⁶ Proviso (iii) to the definition of “enterprise” in section 1(1) of the VAT Act.

⁹⁷ Proviso (v) to the definition of “enterprise” in section 1(1) of the VAT Act. Section 12 of the VAT Act contains a list of exempt supplies.

⁹⁸ Proviso (ii) to the definition of “enterprise” in section 1(1) of the VAT Act.

⁹⁹ Proviso (vi) to the definition of “enterprise” in section 1(1) of the VAT Act.

¹⁰⁰ Proviso (vi) to paragraph (b) of the definition of “enterprise” in section 1(1) of the VAT Act.

Certain vendors are specifically deemed to be an “enterprise”. These include public authorities; local authorities; welfare organisations and share block companies. The legislator also published proposed legislation to amend the definition of “enterprise” to include certain supplies of telecommunication services. Telecommunication services and foreign underwriting insurance business by underwriting members such as those of Lloyd’s of London are discussed below.

Telecommunication services

In the mid-1990s, the legislator proposed an amendment to the definition of “enterprise” to deem continuous or regular supplies of telecommunication services used in South Africa to constitute an “enterprise”, irrespective of residence or whether the supplier had a permanent establishment or place of business in South Africa. Promulgation would have required many telecommunication service providers to register for VAT, if the value of these services exceeded the compulsory VAT registration threshold. The proposed amendment¹⁰¹ read as follows:

the activities of any person who continuously or regularly supplies telecommunication services to any person who utilizes such services in the Republic...

The Explanatory Memorandum on the Taxation Laws Amendment Bill, 1997 (South Africa, 1997) mentioned that, although imported telecommunication services are covered by the general imported services provisions, tax is seldom paid by the person using the services, other than for making taxable supplies. Since telecommunication services are imported on a large scale, the amendment intended to provide an alternative to tax these services. The main target of the amendment was the so-called call-back operators, but without a definition of “telecommunication services” it would have resulted in a much wider application. The proposed amendment was never promulgated¹⁰². Some years ago, the VAT Act denied the zero rating of telecommunication services physically rendered outside South

¹⁰¹ The proposal was to be effected by inserting paragraph (b)(iv) in the definition of “enterprise”.

¹⁰² Subparagraph (b)(iv) to the definition of “enterprise”, as introduced by Act 27 of 1997, may have been repealed (Badenhorst, 2011).

Africa¹⁰³ (Meyburgh, 2011).

The Davis VAT Committee proposed that the VAT Act be amended to include provisions to address supplies of telecommunication services (Davis VAT Report, 2015:78-94). Such amendments should be harmonious with other VAT jurisdictions and in accordance with the Melbourne Convention. Addressing telecommunication services should also ensure that the OECD Ottawa Taxation Framework Conditions are adhered to. The OECD acknowledged the need to update these conditions, although it is envisaged that the core OECD principles of neutrality, flexibility and the like, will prevail (Davis VAT Report, 2015:78-94).

Amendments to introduce rules for supplies of telecommunication services would have to address various aspects, including:

- international roaming by residents outside South Africa; these services are currently standard rated, which does not adhere to the destination principle as foreign consumption is taxed (Rudolph, 2012);
- non-residents who lease network capacity locally to provide telecommunication services in South Africa; these suppliers will create a VAT “enterprise”, irrespective of whether they have physical activities in South Africa (Meyburgh, 2011);
- the use of telecommunication infrastructure in South Africa; such use should arguably comprise an activity for “enterprise” purposes (National Treasury, 2012);
- defining “telecommunication services”; consideration should be given to defining such services in the VAT Act (Badenhorst, 2011);
- defining consumption of telecommunication services in South Africa, which could be done with reference to where the debtors reside (Connell, 2011); and
- competitive inequity between domestic and foreign suppliers should be addressed by amendments (Schenk, 2012).

Specific guidance is required on, for example, whether the use of a server, antenna, and cable or satellite network in South Africa will be considered to be an activity carried on in South Africa (Meyburgh, 2011).

¹⁰³ Section 11(2)(k) of the VAT Act.

Intangible property

In VAT Case 179 it was held that a contractual right is located in the jurisdiction where the owner of the right or grantor resides (Badenhorst, 2011)¹⁰⁴. The Minister of Finance noted that VAT registration of nominal or certain wholly passive activities of foreign persons is impractical when the supply is made to domestic VAT vendors. Relief from VAT registration could be considered in order not to discourage direct foreign investment¹⁰⁵ (Badenhorst, 2011). VAT case 179 may not have provided enough clarity on the place of supply of the making available of intangible rights, especially in light of SARS' VAT News of 13 December 1999 (SARS, 1999), which provided that the granting by a foreign enterprise of the use of intellectual property in South Africa over a period of time is regarded as an enterprise carried on partly in South Africa (National Treasury, 2012).

The place of supply with regard to intellectual property which results in royalties should be determined with reference to the place of consumption (location of the recipient) or alternatively with regard to the location of the owner of the intellectual property (Prinsloo, 2012). Government should refrain, as far as possible, from registering foreign licensors for VAT purposes who receive royalty income from South African licensees where the fiscus will not benefit monetarily (van Heerden, 2012).

Specific place of supply rules should be introduced to provide clarity in respect of certain tourism-related services such as inbound arrangement services; vouchers and certain imported services¹⁰⁶ (Blakeley, 2012). Certain other activities or supplies, such as royalties and cross border leasing, can be dealt with under a general place of supply rule (Blakeley, 2012).

Place of supply rules in respect of or changes to domestic accommodation may also be required (Terblanche, 2012). Certain jurisdictions refund VAT incurred by a

¹⁰⁴ This does not necessarily imply that the activity of making available the rights takes place where the owner of the rights resides. It could be argued that the activities concerning the rights (albeit economic) reside where the rights are used or made available.

¹⁰⁵ Budget Tax Proposals 2007/2008.

¹⁰⁶ The New Zealand GST Act can be used as a basis.

foreign business on accommodation, although this has become an issue in many jurisdictions due to its close connection with VAT on “entertainment”. South Africa could consider also offering tax relief to foreign businesses for accommodation. South Africa currently does not have VAT reciprocity with Germany, which means that South African businesses that incur German VAT cannot claim it back. Israel and Canada amended their VAT laws to zero rate accommodation provided to foreign businesses to obtain reciprocity with Germany (Terblanche, 2012).

Foreign Underwriting Insurance Business

The definition of “enterprise” was amended to include, with effect from 1 January 2001, the following:

the activity of underwriting insurance business by Underwriting Members of Lloyd’s of London, to the extent that contracts of insurance are concluded in the Republic, shall be deemed to be the carrying on of an enterprise...¹⁰⁷

The Lloyd’s of London (Lloyd’s) insurance business differentiates between cover holder business (also referred to as “binder business”) and open market business (also referred to a “worldwide business”) (Meyburgh, 2011). This inclusion in “enterprise” is based on the “activities” carried on “continuously or regularly” in South Africa¹⁰⁸. In terms of cover holder business a person enters into an agreement with Lloyd’s which entitles it to market and sell certain insurance policies, without further approvals. Cover holders are referred to as underwriting management agents (UMAs) for Lloyd’s and binds Lloyd’s in South Africa. In terms of open market business, a South African insurance intermediary promotes business for and on behalf of Lloyd’s and charges a fee or commission for these services. The agreement and insurance cover are entered into and provided outside South Africa (Meyburgh, 2011).

¹⁰⁷ Paragraph (vi) to the definition of “enterprise” in section 1(1) of the VAT Act.

¹⁰⁸ Read with section 54 of the VAT Act, which deems supplies made by an agent on behalf of a principal to be made by the principal.

To the extent that other foreign insurers conclude contracts of insurance in South Africa and are entitled to do so in terms of the Short-term Insurance Act, 1998, they should arguably be required to register as vendors (Glyn-Jones, 2012; Meyburgh, 2011; National Treasury, 2012; and Prinsloo, 2012). Such an extension should arguably not apply to reinsurers as the Short Term Insurance Act contains adequate safeguards to limit it to South African business (de Wet, 2012). Place of supply rules for insurance services are very important and could be determined with reference to the location of the insured, the insurer, or the insured risk (Prinsloo, 2012).

Foreign branch or main business

The term “enterprise” in its original form specifically excluded supplies of goods or services outside South Africa by the foreign branch of a local concern or its main business permanently located outside South Africa, if the foreign branch or main business:

- could be identified separately; and
- had an independent system of accounting¹⁰⁹.

As a result, these supplies did not constitute taxable supplies, as the foreign branch or main business was deemed not to have a VAT “enterprise” and only supplies made in South Africa by the local concern were subject to VAT. Supplies by the local branch or main business to its foreign operation were deemed to be in the course or furtherance of the local VAT “enterprise”¹¹⁰. Without such a deeming provision, the VAT Act would not have recognised such “supplies” as they would happen within one legal entity and would technically not constitute supplies. Supplies from South Africa (other than from the local branch or main business) to the foreign branch or main business potentially did not qualify for the zero rate, as the foreign branch or main business arguably was a “resident of the Republic” and was present in South Africa when the services were rendered¹¹¹ (Prinsloo, 2012).

The law, as it relates to foreign branches and main businesses and the concept of

¹⁰⁹ Proviso (ii) to the definition of “enterprise” in section 1(1) of the VAT Act.

¹¹⁰ Section 8(9) of the VAT Act.

¹¹¹ Section 11(2)(l)(iii) of the VAT Act.

“enterprise”, was amended in 2005. The VAT Act now provides that any branch or main business permanently situated at premises outside South Africa shall be deemed to be carried on by a person separate from the vendor, if the foreign branch or main business:

- can be identified separately; and
- has an independent system of accounting.

The legislator changed the law with the intention to deem supplies made by a foreign branch or main business of an “enterprise” not to be supplies made by the South African “enterprise”¹¹². The foreign branch or main business is now regarded as a separate person for VAT purposes, which ensures that the normal rules relating to exports and imports and the supply of services apply to foreign branches or main businesses. As a result, the VAT Act now limits the previous jurisdictional reach of the VAT system from worldwide supplies to supplies of the South African VAT “enterprise” and excludes the supplies of its foreign branches and main businesses¹¹³.

The consignment or delivery of goods or the provision of services by a vendor to its “independent” foreign branch or main business¹¹⁴ is deemed to be a supply of such goods or service in the course or furtherance of its enterprise¹¹⁵. These supplies can¹¹⁶ generally be zero-rated¹¹⁷. As the VAT Act now deems the foreign branch or main business to be carried on by a person separate from the South African vendor it acknowledges, as a result, that supplies can be made between the local and foreign “branch or main business” which is part of the same legal entity. The need for the VAT Act to still deem “transactions” between the local and foreign counterparts to be supplies, is seemingly unnecessary as the normal provisions,

¹¹² Explanatory Memorandum on Revenue Laws Amendment Bill, 2004:Clause 92(e) (South Africa, 2004a).

¹¹³ Explanatory Memorandum on Revenue Laws Amendment Bill, 2004:Clause 92(e) (South Africa, 2004a).

¹¹⁴ If paragraph (ii) of the proviso to “enterprise” in section 1(1) of the VAT Act applies.

¹¹⁵ Section 8(9) of the VAT Act.

¹¹⁶ If paragraph (ii) of the proviso to “enterprise” in section 1(1) of the VAT Act applies.

¹¹⁷ Section 11(1)(i) and 11(2)(o) of the VAT Act.

which govern transactions between separate legal personae, now apply.

A South African business that conducts a VAT “enterprise” would be “resident of the Republic”¹¹⁸, which would render its foreign branch or main business also to be “resident of the Republic” as “they” form part of one legal entity. General provisions which zero rate supplies to non-residents would therefore not apply, which necessitates special zero rating provisions¹¹⁹. The legislator could consider amending the current zero rating provisions (other than those relating to foreign branches or main businesses) to specifically include supplies between local and foreign branches or main businesses. Alternatively, non-vendor foreign branches or main businesses could be excluded from the definition of “resident of the Republic”.

Prior to the amendment of “enterprise”, the VAT Act only recognised supplies from South Africa to its foreign branch or main business. The VAT Act now recognises supplies between the local and foreign “branch or main business”, irrespective of the directional flow of these supplies. This can, for example, lead to tax on “imported services” payable by the local vendor in respect of services supplied by its foreign branch or main business¹²⁰.

In practice, the current legislation dealing with local and foreign “branches or main businesses” potentially creates various interpretational and practical difficulties, including:

- determining the nature or extent of the separate accounting system that should be maintained (Meyburgh, 2011); the main operating entity’s accounting system generally contains the accounting records of the branch, although the activities of

¹¹⁸ The term “resident of the Republic”, as defined in section 1(1) of the VAT Act, includes a person to the extent that the person carries on an enterprise or activity and has a fixed or permanent place in South Africa relating to the enterprise or activity.

¹¹⁹ Sections 11(1)(i) and 11(2)(o) of the VAT Act applies specifically to supplies by a local branch or main business to its foreign branch or main business.

¹²⁰ See also section 14(4) of the VAT Act.

the branch or main business would generally be accounted for as separately identifiable profit centres (Badenhorst, 2011)¹²¹;

- attributing supplies to the enterprise or activity of the local as opposed to the foreign “branch or main business;” determining which supplies emanate from activities carried on in South Africa and outside South Africa, especially where a non-resident carries on similar activities inside and outside South Africa (Meyburgh, 2011);
- identifying a branch or main business as “separate”, as it is subjective and creates uncertainty¹²²; the VAT Act is unclear whether this requirement indicates separate identification with regard to geography, activities and operations, or some other means (Badenhorst, 2011);
- determining the meaning of an “enterprise permanently situated at premises outside the Republic” and whether the enterprise must be carried on from these premises outside South Africa; it can, for instance, be questioned whether an intermediary’s premises outside South Africa (neither owned nor rented by the vendor) from which the vendor carries on an enterprise, would fulfil this requirement (Badenhorst, 2011);
- determining whether a foreign branch or main business can have more than one South African VAT registration for the same legal entity (Connell, 2011); and
- incurring costs and significant actions to “carve-out” supplies made outside South Africa from the scope of VAT and keep an independent accounting system, due to the worldwide nature of the VAT system (Schenk, 2009:12).

Electronic services

Increased development of electronic services may impact the tax base and collection of tax revenue adversely (South Africa, 2000:36). This is the result of the difficulty inherent in defining the tax jurisdiction in the cyber world, linked with administration and enforcement difficulties. The tax system should be fair,

¹²¹ The intention of the legislator could potentially provide guidance. If it is assumed that the intention is to “ring-fence” local and foreign activities, an “independent system of accounting” would not necessarily require a completely separate system and could envisage a worksheet or spreadsheet to enable SARS to differentiate between local and foreign activities.

¹²² Glyn-Jones (2012) recommends that the New Zealand GST definition of “non-resident” be implemented.

predictable and not distort business decisions. The challenge is to develop a tax policy that is not isolated from its e-commerce partners (South Africa, 2000:36).

On 27 February 2013 the Minister of Finance announced (as part of his 2013 Budget Speech) that foreign suppliers of electronic services would be required to register for South African VAT purposes (Schneider, 2013). The term “electronic services”¹²³ is defined to mean those electronic services prescribed as such by the Minister by regulation, in terms of the VAT Act. National Treasury published the final Electronic Services Regulations on 28 March 2014 (the Regulation) in Government Gazette No. 37489, which took effect on 1 June 2014. The Regulation includes the following services:

- *educational services*, including the supply of distance teaching programmes; educational webcasts; internet-based courses; internet-based education programmes; or webinars, if the person making the supply is not regulated by an educational authority in the export country;
- *games and games of chance*, including the supply of electronic games (including internet-based games; or multiplayer role-playing games); interactive games (where they are games of chance; games where the result is influenced by the skill of the player; or games which is a combination of chance and skill); or electronic betting or wagering, where it constitutes the acceptance of a bet or wager (on the outcome of a race; or any other event or occurrence);
- *internet-based auction service facilities*;
- *miscellaneous services*, including the supply of e-books, which means digitised content of any book; or electronic publication;
- *audio visual content*, which means any set of moving visual images or other visible signals, with or without accompanying sounds, where the sequences of the visual images are seen as moving pictures; and any right to view the visual images or visible signals;
- *still images*, which means desktop themes; photographic images; pictorial images; or screensavers, and any right to view any item listed above;
- *music*, which means audio clips; broadcasts not simultaneously broadcast over

¹²³ Section 1(1) of the VAT Act.

any conventional radio network in the Republic; jingles; live streaming performances; ringtones; songs; or sound effects, and any right to listen to any item listed in the regulation; and

- *subscription services*, including subscription services to blogs; journals; magazines; newspapers; games; internet-based auction services; periodicals; publications; social networking services; webcasts; webinars; web sites; web applications; or web series.

The definition of “enterprise” was amended¹²⁴ to include foreign suppliers of “electronic services” as follows:

the supply of electronic services by a person from a place in an export country, where at least two of the following circumstances are present:

- (aa) [t]he recipient...is a resident of the Republic;
- (bb) ...payment to that person in respect of such...services originates from a bank...in terms of the Banks Act...;
- (cc) the recipient...has a business address, residential address or postal address in the Republic.¹²⁵

With effect 1 April 2015¹²⁶ the supply by foreign suppliers of electronic services may no longer be zero rated¹²⁷. Foreign suppliers of “electronic services” are required to register¹²⁸ and account for VAT in South Africa if their taxable turnover exceeds the

¹²⁴ By inserting proviso (vi) to paragraph (b) of “enterprise” in the VAT Act.

¹²⁵ This section was amended with effect 1 April 2015 and previously required (aa) or (bb) to be present to constitute an “enterprise” activity.

¹²⁶ The VAT Act was amended to exclude “electronic services” envisaged by section 11(2)(k) from the zero rating afforded by section 11(2).

¹²⁷ SARS also issued BGR 28 (26 March 2015) which covers: (i) the minimum information that tax invoices, debit or credit notes issued by non-resident suppliers of electronic services must contain to allow input tax deductions; (ii) acceptable sources of exchange rate information to convert the VAT charged at the time of supply into Rand; and (iii) permission for a non-resident electronic services suppliers to advertise or quote VAT-exclusive prices if their websites indicate that VAT will be charged at the standard rate to South African recipients.

¹²⁸ Section 23(1A) of the VAT Act.

VAT registration threshold of R50 000¹²⁹. The Davis VAT Committee recommended that the registration threshold for foreign electronic service suppliers be reconsidered in light of the OECD neutrality principle¹³⁰ (Davis VAT Report, 2015:93). As the requirement to issue tax invoices is not an industry norm, SARS issued Binding General Ruling 28 (BGR 28) on 26 March 2015. BGR 28 sets out the information that must be contained in tax invoices, debit, and credit notes; the exchange rate that must be applied to determine the VAT charged in Rand; and the manner in which prices must be advertised or quoted, for the supply of electronic services by an electronic services supplier. The OECD recommendations will need to be analysed and compared to the South African tax system and assessed to establish whether they are appropriate for South Africa. A recommendation should not be implemented if it results in contravention of an OECD principle (Davis VAT Report, 2015:84-85).

The Davis VAT Committee recommended that the default legal position should require a vendor to adopt the invoice basis but that the option to use the payments basis, subject to the legal requirements, should be retained (Davis VAT Report, 2015:84).

As many foreign businesses that only supply electronic services to other group companies would be caught in the VAT net and be required to register for VAT on intra-group supplies, the Davis VAT Committee recommended that consideration be given to exclude supplies within a “group of companies” as defined in section 1 of the Income Tax Act, 58 of 1962, from the ambit of the e-commerce provisions (Davis VAT Report, 2015:93). However, listing qualifying electronic services, as the Regulation does, may not be flexible enough to adapt to developments. Electronically supplied services could be categorised and explained in a guide or, alternatively, if an exhaustive list is preferred, the Regulation should be reviewed and updated regularly, for example every two years. Attaching specific place of supply rules to actual facilities should be avoided, to ensure flexibility in this changing environment (Davis VAT Report, 2015:93).

¹²⁹ The compulsory threshold is R1 000 000 (section 23 of the VAT Act).

¹³⁰ Neutrality between local and foreign supplies.

The Regulation does not distinguish between business-to-business and business-to-consumer supplies (Davis VAT Report, 2015:89). The OECD recommended a distinction between business-to-business and business-to-consumer supplies where the treatment “is consistent with the overall design of the national consumption tax system”. The following should be taken into account in respect of South Africa:

- the reverse charge mechanism may not be consistent with the overall design of the VAT system as it has been introduced for specific circumstances and supplies¹³¹;
- compliance with the OECD principles is more important than granting favourable treatment to EU jurisdictions;
- distinguishing between business-to-business and business-to-consumer supplies requires that the identity of the recipient be determined, which increases the compliance burden of suppliers and can lead to manipulation and evasion (Davis VAT Report, 2015:89-90).

Distinguishing between business-to-business and business-to-consumer supplies ensures that only foreign suppliers of electronic services supplied to final consumers are registered, to counter consumers’ non-compliance with the reverse charge mechanism (Davis VAT Report, 2015:85-90). However, the Regulation lists electronic services that are viewed as business-to-consumer supplies. Not differentiating between business-to-business and business-to-consumer supplies may arguably lead to the exclusion of certain business-to-consumer supplies, such as supplies of software. International VAT harmonisation of cross-border transactions may counter double taxation or double non-taxation. Distinguishing between business-to-business and business-to-consumer supplies may arguably be in contravention of the OECD principle of neutrality. Although the tax revenue is neutral, such a distinction arguably grants a cash flow benefit. Distinguishing between business-to-business and business-to-consumer supplies allows business-to-business supplies to be VAT neutral and renders VAT registration unnecessary. Most domestic business-to-business supplies are also tax neutral. It is arguable that if a foreign electronic service supplier is excluded from VAT registration for

¹³¹ Although argued by Davis (Davis VAT Report, 2015:89), this is debatable.

business-to-business supplies, local suppliers of business-to-business supplies should also not be required to register for VAT, which would change the core VAT system globally (Davis VAT Report, 2015:85-90).

The Davis VAT Committee recommended against a distinction between business-to-business and business-to-consumer suppliers (Davis VAT Report, 2015:90). Business-to-consumer transactions should be reconsidered when the OECD publishes its guidelines and commentary relating to business-to-consumer supplies to assess whether changes are required to ensure harmonisation with the OECD principles (Davis VAT Report, 2015:93).

The recent Base Erosion and Profit Shifting (BEPS) review done in respect of South Africa, raised the concern that the VAT amendments relating to electronic services do not address online advertising, which certain foreign companies engage in to avoid paying taxes in foreign jurisdictions (Davis VAT Report, 2015:90-92). Rule 6 of the Regulation includes the “supply of any... still image... and any right to view...”, which could arguably include on-line advertising, depending on the manner in which the advertising is supplied. These interpretational issues may not necessarily require legislative changes but could be addressed by a guide. The “subscription service to a web site” could arguably also include certain types of advertisements. The Regulation defines “website” as “any website as defined in section 1 of the Electronic Communications and Transactions Act (ECTA)”. The ECTA defines “web site” as “any location on the Internet containing a home page or web page”. A “website” is not a “web page” but “a collection of web pages” (TechTerms.com). It must still then be determined whether the payments satisfy the definition of “subscription”. The Regulation defines “subscription” broadly. The Oxford English Dictionary defines “subscription” as “the action of making or agreeing to make an advance payment in order to receive or participate in something or as a donation...; an arrangement by which access is granted to an online service; ...an advance payment made to receive or participate in something...” If it can be argued that a subscription fee is paid (through a “cost per click”) for an advertisement on a “website”, it may fall within the ambit of the Regulation. The Davis VAT Committee argues that the Regulation may not necessarily require amendment, as it could be argued that it includes on-line advertising, but that SARS should publish a guide to

clarify this issue for purposes of the Regulation (Davis VAT Report, 2015:91-92).

The “enterprise” enquiry is central to South Africa’s VAT taxing rights (Theron, 2012). Determining non-residents’ VAT registration liability and VAT rate issues present practical challenges resulting from the subjective nature of the “enterprise or activities” conducted in or partly in South Africa and should ideally be clarified (Theron, 2012). Determining where an “enterprise or activities” are conducted is critical in establishing whether a foreign person has a VAT registration liability and attributing supplies to these activities (Meyburgh, 2011). Legislation should provide clarity on a person’s liability to register for VAT and who should levy and account for tax (Nellen, 2012).

The legislator should consider introducing provisions to allow foreign businesses not to register for VAT purposes, where non-registration will ultimately not result in VAT leakage, to keep tax compliance costs for foreign persons and SARS to the minimum (Terblanche, 2012)¹³². Such provisions should ideally differentiate between business-to-business and business-to-consumer transactions (Terblanche, 2012). The uncertainty created by a lack of sufficient rules with regard to VAT registration requirements of foreign persons is exacerbated by the fact that junior SARS officials attend to VAT registrations (van Heerden, 2012). Technically, the VAT registration provisions in the VAT Act¹³³ have created problems in practice (van Heerden, 2012).

This section considered the provisions of the VAT Act relating to non-residents with a link or connection to South Africa, the possible liability to register for VAT purposes, and potential shortcomings in these provisions. To analyse this meaningfully it was necessary to assess the components of the definition of “enterprise” in section 1(1) of the VAT Act as they relate to non-residents. This section also considered specific types of foreign enterprises, including foreign

¹³² Provisions similar to section 54(2A)(b) in respect of goods and section 11(2)(l)(ii) with respect to services could be considered to keep certain foreign persons outside of the VAT net (Terblanche, 2012).

¹³³ Specifically section 23(3)(d) of the VAT Act.

branches and main businesses and also suppliers of telecommunication services, intangible property, insurance services, and electronic services. The section below considers the VAT rate applicable to inter-jurisdictional supplies and potential shortcomings in the legislation relating to the exemption or zero-rating of these supplies.

5.2.3 VAT rate applicable to inter-jurisdictional supplies

VAT exemptions and zero ratings

Certain supplies are exempt from VAT¹³⁴, including supplies of certain financial services (not subject to the zero rate). These are residential accommodation and related leasehold land; transport of fare-paying passengers by road or rail; educational services; and certain supplies by associations not for gain; employee organization services to members recovered through membership contributions; goods supplied by non-residents in South Africa that have not been entered for home consumption; goods supplied by bargaining councils and political parties in return for membership contributions; and certain supplies made in the course of the management of predetermined bodies or persons. Registered vendor suppliers are not entitled to charge VAT on exempt supplies, and are not entitled to claim VAT on expenditure incurred relating to the making of exempt supplies as an input tax deduction¹³⁵.

Taxable supplies of goods or services¹³⁶ can, if they comply with certain criteria, be zero rated¹³⁷. The zero rate applies mainly to the following categories of supplies:

- certain supplies of goods based on location, destination, or consumption¹³⁸;
- sales of going concerns between separate legal entities and between branches

¹³⁴ Proviso (v) to the definition of “enterprise” read with section 12 of the VAT Act.

¹³⁵ Proviso (v) to the definition of “enterprise” in section 1(1) of the VAT Act deems any activity, to the extent that it involves the making of exempt supplies, not to be the carrying on of an enterprise.

¹³⁶ Subject to VAT in terms of section 7(1) of the VAT Act.

¹³⁷ Sections 11(1) or 11(2) of the VAT Act. Section 11(1) deals with the zero rating of goods and section 11(2) deals with the zero rating of services.

¹³⁸ For a detailed discussion see “Inter-jurisdictional VAT rules applicable to ‘goods’”.

or divisions¹³⁹;

- certain supplies of gold and gold coins to Government and banks¹⁴⁰;
- certain supplies for use in agriculture¹⁴¹;
- supplies of fuel levy goods¹⁴²;
- supplies of certain foodstuffs¹⁴³;
- supplies of illuminating kerosene for illumination or heating¹⁴⁴;
- supplies of certain old order mining rights converted into new rights¹⁴⁵;
- compensation by public authorities for supplies of controlled animals or things¹⁴⁶;
- certain supplies of fixed property to the Cabinet member responsible for land reform or restitution¹⁴⁷; and
- certain supplies of fixed property to the extent that the consideration is an advance or subsidy in respect of land assistance¹⁴⁸.

A supply of services is subject to the zero rate if it falls into one of a number of categories, including:

- certain supplies of services, based on location, destination, or consumption¹⁴⁹;
- certain deemed services relating to welfare activities, government, horse owners, and grants¹⁵⁰; and
- municipal rates¹⁵¹.

Zero-rated supplies are taxable supplies, although they are charged with tax at 0%.

¹³⁹ Section 11(1)(e) and 11(1)(p) of the VAT Act.

¹⁴⁰ Section 11(1)(f) and 11(1)(k) of the VAT Act.

¹⁴¹ Section 11(1)(g) of the VAT Act.

¹⁴² Section 11(1)(h) of the VAT Act.

¹⁴³ Section 11(1)(j) of the VAT Act.

¹⁴⁴ Section 11(1)(l) of the VAT Act.

¹⁴⁵ Section 11(1)(n) of the VAT Act.

¹⁴⁶ Section 11(1)(r) of the VAT Act.

¹⁴⁷ Section 11(1)(s) of the VAT Act.

¹⁴⁸ Section 11(1)(t) of the VAT Act.

¹⁴⁹ For a detailed discussion see “Inter-jurisdictional VAT rules applicable to ‘services’”.

¹⁵⁰ Sections 11(2)(q); 11(2)(n); 11(2)(s); 11(2)(t); 11(2)(u); and 11(2)(x) of the VAT Act.

¹⁵¹ Section 11(2)(w) of the VAT Act.

Registered vendors are entitled to claim VAT on expenditure incurred relating to the making of zero rated supplies as an input tax deduction.

Inter-jurisdictional VAT rules generally differentiate between goods and services, and between tangible and intangible goods (Badenhorst, 2011; Glyn-Jones, 2012¹⁵²; and van Heerden, 2012). Although these differentiations can reduce legislative uncertainty (Prinsloo, 2012), they should not be overly complex as this would defeat the objective (de Wet, 2012).

The place of consumption of or “enterprise or activity” relating to tangible goods is generally relatively easy to determine, but not without exception. For example, a sales contract concluded at a place different from the place of delivery poses the question of where the places of “enterprise or activity” and consumption are¹⁵³. This could result in a legal enquiry involving the law of contract and when and where the sale was concluded, for example, where the taxing rights would be if the *essentialia* of a contract of sale are fulfilled in more than one jurisdiction (Theron, 2012). Tangible goods are generally consumed where they are supplied, unless subsequently exported (Badenhorst, 2011). Consumption of intangible goods, by their nature, is more problematic to determine. In the Gallo Africa case¹⁵⁴, it was held that South African law distinguishes between movable and immovable incorporeal property, and that intellectual property rights are territorial in nature. As a result, it is imperative that the VAT rules clearly distinguish between the supply of goods, services and intangibles (Badenhorst, 2011). The place of consumption of goods is generally where the goods are situated when supplied and the place of consumption of services is generally where the recipient is located (Rudolph, 2012). The place of consumption and supply of intellectual property may differ and should be catered for in the VAT Act (Rudolph, 2012).

¹⁵² See NZ GST section 11A(2) and NZ Telecoms section 8(6) – 8(9).

¹⁵³ See for example ARO Lease BV v Inspecteur de Belastingdienst Grote Ondernemingen, Amsterdam Case C-190/95 regarding cross-border leasing.

¹⁵⁴ Gallo Africa v Sting Music [2011] 1 All SA 449 (SCA).

Inter-jurisdictional VAT rules applicable to goods

The term “goods” is defined in broad terms to mean:

corporeal movable things, fixed property and any real right in any such thing or fixed property, but excluding money; any right under a mortgage bond or pledge of any such thing or fixed property; and any stamp, form or card which has a money value and has been sold or issued by the State for the payment of any tax or duty levied under any Act of Parliament, except when subsequent to its original sale or issue it is disposed of or imported as a collector's piece or investment article¹⁵⁵.

The term “fixed property” is defined to mean:

land (together with improvements...), any unit...in...the Sectional Titles Act..., any share in a share block company which confers a right to or an interest in the use of immovable property, and, in relation to a property timesharing scheme, any time-sharing interest...in...the Property Time-sharing Control Act...; and any real right in any such land, unit, share or time-sharing interest¹⁵⁶.

The following is also deemed to be a supply of goods:

...a supply of the use or right to use or the grant of permission to use any goods (whether with or without a driver, pilot, crew or operator) under any rental agreement, instalment credit agreement, charter party, agreement for charter or any other agreement under which such use or permission to use is granted...¹⁵⁷

The VAT Act zero rates certain supplies of goods, based on intended location, destination, or consumption, including:

- movable goods supplied in terms of a sale or instalment credit agreement and

¹⁵⁵ Section 1(1) of the VAT Act.

¹⁵⁶ Section 1(1) of the VAT Act.

¹⁵⁷ Section 8(11) of the VAT Act.

directly “exported”¹⁵⁸, or exported by the recipient in terms of an indirect export¹⁵⁹, if the supplier elects to apply the zero rate¹⁶⁰;

- goods supplied to repair, renovate, modify, or treat temporarily admitted exempt goods or supplied to repair, maintain, clean or recondition a foreign going ship or aircraft¹⁶¹; or
- movable goods supplied under a rental agreement, charter party or chartering agreement, used exclusively in an export country or by a customs controlled area enterprise or an Industrial Development Zone (IDZ) operator in a customs controlled area¹⁶²;
- movable goods supplied under a rental agreement, charter party or chartering agreement, used exclusively in a commercial, financial, industrial, mining, farming, fishing or professional concern in an export country if payment of rent or other consideration is effected from the export country¹⁶³;
- goods supplied to foreign branches or main businesses under the special rules¹⁶⁴ that apply¹⁶⁵;
- movable goods supplied in terms of a sale or instalment credit agreement to a customs controlled area enterprise or an IDZ operator if physically delivered to the customs controlled area enterprise or IDZ operator in a customs controlled area by the supplier or a VAT registered cartage contractor, whose main activity is transporting goods and who is engaged by the supplier to deliver the goods and the supplier is liable for the full cost of delivery¹⁶⁶;
- use of fixed property, situated in a customs controlled area, supplied to a customs controlled area enterprise or an IDZ operator¹⁶⁷;

¹⁵⁸ Paragraphs (a), (b) or (c) of the definition of “exported” in section 1(1) of the VAT Act.

¹⁵⁹ Part 2 of the Export Incentive Scheme referred to in paragraph (d) of the definition of “exported” in section 1(1) of the VAT Act.

¹⁶⁰ Section 11(1)(a) of the VAT Act.

¹⁶¹ Section 11(1)(b) of the VAT Act.

¹⁶² Section 11(1)(c) of the VAT Act.

¹⁶³ Section 11(1)(d) of the VAT Act.

¹⁶⁴ Section 8(9) of the VAT Act.

¹⁶⁵ Section 11(1)(i) of the VAT Act.

¹⁶⁶ Section 11(1)(m) of the VAT Act.

¹⁶⁷ Section 11(1)(mA) of the VAT Act.

- goods supplied to a non-resident non-vendor who has contracted with the vendor to deliver the goods to another vendor if the goods form part of a supply by the non-resident non-vendor to the other vendor if they will be used by the recipient to make only taxable supplies¹⁶⁸; or
- goods supplied, other than by an inbound duty and tax free shop, which have been imported and entered into a licensed Customs and Excise storage warehouse before entry for home consumption¹⁶⁹; and
- goods supplied by an inbound duty and tax free shop¹⁷⁰.

The VAT Act defines “exported”¹⁷¹ in relation to movable goods supplied by a vendor in terms of a sale or instalment credit agreement, to mean:

- (a) consigned or delivered by the vendor to the recipient at an address in an export country...; or
- (b) delivered by the vendor to the owner or charterer of any foreign-going ship...or to a foreign-going aircraft when...going to...an export country and such goods are for use or consumption in such ship or aircraft...; or
- (c) delivered by the vendor to the owner or charterer of any foreign-going ship...for use in such ship; or
- (d) removed from the Republic by the recipient for conveyance to an export country in accordance with...an export incentive scheme...

It can be concluded that movable goods destined for a place outside South Africa are only “exported” for VAT purposes if the goods are supplied in terms of a sale or instalment credit agreement. The VAT Act defines “export country”¹⁷² as a country other than the Republic and any place which is not in South Africa. The President may by notice in the Government Gazette deem a specific country or territory not to be an export country, from a date and to the extent indicated in the notice. The zero rating of goods destined for use outside South Africa or in certain designated areas

¹⁶⁸ Section 11(1)(q) of the VAT Act.

¹⁶⁹ Section 11(1)(u) of the VAT Act.

¹⁷⁰ Section 11(1)(v) of the VAT Act.

¹⁷¹ Section 1(1) of the VAT Act.

¹⁷² Section 1(1) of the VAT Act.

(such as IDZs) is generally clear and can be applied with relative ease. These rules usually adhere to the destination principle and ensure that tax is levied on final domestic consumption. Some of these rules may have practical shortcomings, such as the time limits in which to obtain documentary proof to substantiate direct or indirect exports, in the absence of which the standard rate applies. The VAT Act and various SARS guidelines and rulings do not necessarily provide alternatives to ensure adherence to the destination principle, where it can be clearly demonstrated that the goods are consumed outside South Africa or in a designated area, but the time limits or documentary requirements have not been met.

Areas of particular importance that may require amendment are discussed below.

Supplies of foreign land by way of sale or lease

The exemption of supplies (by way of sale or lease) of land situated outside South Africa narrows the jurisdictional reach of the tax¹⁷³ (Schenk, 2012) and removes these supplies from the ambit of the definition of “enterprise”¹⁷⁴ (Theron, 2012). The categorisation of a specific supply of goods as exempt if made outside South Africa and so disallowing the benefits associated with making zero-rated supplies¹⁷⁵, is contrary to the general structure of the VAT Act and inequitable when compared to the VAT treatment of exports of movable goods (de Wet, 2012). It is also inequitable when compared to services supplied by local suppliers to foreign recipients, which qualify for the zero rate¹⁷⁶ (Badenhorst, 2011). This exemption is contrary to the destination principle, as the fixed property is located and used outside South Africa. However, the VAT incurred on goods or services acquired by a vendor from South African suppliers to construct, repair, maintain, insure, etc., the property, may be insignificant (Meyburgh, 2011). The legislator should consider deleting the exemption and could replace it with a provision that zero rates supplies (by way of sale or lease) of land situated outside South Africa (Glyn-Jones, 2012).

¹⁷³ Section 12(e) of the VAT Act.

¹⁷⁴ Section 1(1) of the VAT Act, through the working of proviso (v) to the definition of “enterprise”.

¹⁷⁵ SARS general written VAT Ruling 419, withdrawn on 1 August 2009.

¹⁷⁶ Section 11(2)(l) of the VAT Act.

Supplies of goods by non-residents before entry for home consumption

South Africa has designated areas that are treated as being outside South Africa, even though these areas are geographically in South Africa. Pre-entry sales among non-residents often arise in South African territorial waters before entry for home consumption. A non-resident that continuously or regularly supplies goods that enter South African territorial land and waters may be required to register for VAT, even if the non-resident does not have a permanent establishment or place in South Africa. Non-residents without a permanent establishment or place in South Africa generally want to avoid the compliance burden of registering for VAT¹⁷⁷. As a result, the VAT Act exempts¹⁷⁸ the supply of goods in South Africa by a non-resident non-vendor (excluding goods supplied by an inbound duty and tax free shop), which have not been entered for home consumption. The non-resident may apply to the Commissioner for SARS who may direct that the exemption will not apply.¹⁷⁹ The supply of goods (excluding goods supplied by an inbound duty and tax free shop), which have been imported and entered for storage in a licensed Customs and Excise storage warehouse but have not been entered for home consumption, is subject to the zero rate¹⁸⁰. The VAT Act¹⁸¹ does not provide enough clarity on whether certain supplies (or sales) are made inside or outside South Africa (Rudolph, 2012), for example, where a “sale”¹⁸² is made whilst the goods are outside South Africa, i.e. the non-resident transacts or acts in consequence of which ownership will pass to another person, but the actual transfer of ownership is delayed until after importation into South Africa (Rudolph, 2012).

¹⁷⁷ Explanatory Memorandum on the Taxation Laws Amendment Bill, 2012: clause 147.

¹⁷⁸ Section 12(k) of the VAT Act.

¹⁷⁹ Glyn-Jones (2012) suggested that the South African VAT Act could move closer to the NZ GST Act – see section 8(4) of GST Act.

¹⁸⁰ Section 11(1)(u) of the VAT Act.

¹⁸¹ Section 13 of the VAT Act.

¹⁸² Section 1(1) of the VAT Act defines “supply” to include “performance in terms of a sale”. Section 1(1) of the VAT Act defines “sale” as meaning “an agreement of purchase and sale and includes any transaction or act whereby or in consequence of which ownership of goods passes or is to pass from one person to another”.

Inter-jurisdictional VAT rules applicable to services

The term “services” is defined as:

anything done or to be done, including the granting, assignment, cession or surrender of any right or the making available of any facility or advantage, but excluding a supply of goods, money or any stamp, form or card contemplated in paragraph (e) of the definition of “goods”¹⁸³

The term “financial services” includes certain activities which are deemed to be financial services¹⁸⁴. These activities include the exchange of currency; certain dealings in cheques or letters of credit, debt securities, participatory securities; the provision of credit, long term insurance, an interest in superannuation schemes; and certain dealings in derivatives and options. Certain financial service activities are deemed to be subject to tax if a fee, commission, merchant’s discount or similar charge, excluding any discounting cost, is charged¹⁸⁵. Although financial services comprise “services”, they are generally exempt from VAT¹⁸⁶, except if zero rated¹⁸⁷.

The VAT Act zero rates certain supplies of services, based on intended location, destination, or consumption, including:

- international transport of passengers or goods and related services¹⁸⁸;
- insuring, arranging of insurance, or arranging of international transport of passengers or goods¹⁸⁹;
- services directly in connection with land or improvements outside South Africa¹⁹⁰;
- services supplied directly in respect of:
 - movable property outside South Africa when the services are rendered;

¹⁸³ Section 1(1) of the VAT Act.

¹⁸⁴ Section 1(1) read with section 2(1) of the VAT Act.

¹⁸⁵ Certain fee-based financial services became subject to VAT on 1 October 1996 (with the deletion of section 2(1)(n) of the VAT Act).

¹⁸⁶ Section 12 read with section 2 of the VAT Act.

¹⁸⁷ Section 11(2) of the VAT Act.

¹⁸⁸ Section 11(2)(a), (b), (c), (e) of the VAT Act.

¹⁸⁹ Section 11(2)(d) of the VAT Act.

¹⁹⁰ Section 11(2)(f) of the VAT Act.

- goods temporarily admitted into South Africa which are exempt from VAT on importation;
- certain goods “exported”¹⁹¹; or
- repair, maintenance, cleaning or reconditioning of a foreign going ship or aircraft¹⁹²;
- services comprising of:
 - handling, pilotage, salvage or towage of any foreign going ship or aircraft situated in South Africa;
 - services in connection with the operation or management of any foreign going ship or aircraft; or
 - storage, repair, maintenance, cleaning, management or arranging the provision of certain containers¹⁹³, or arranging those services, where the services are supplied directly to a non-resident non-vendor, not through an agent or another person;
- services of arranging:
 - the supply of certain “exported” goods¹⁹⁴;
 - the supply of repair, maintenance, cleaning or reconditioning, handling, pilotage, salvage or towage of a foreign going ship or aircraft or certain containers; or
 - transport of goods and ancillary transport services in South Africa for a non-resident non-vendor¹⁹⁵;
- repair, maintenance, cleaning or reconditioning of a railway train operated by a non-resident non-vendor¹⁹⁶;
- services physically rendered outside South Africa or to a customs controlled area enterprise or an IDZ operator in a customs controlled area¹⁹⁷;
- services supplied to a non-resident, except if:
 - supplied directly in connection with land or improvements or movable

¹⁹¹ Paragraph (b) or (c) of the definition of “exported” in section 1(1) of the VAT Act.

¹⁹² Section 11(2)(g) of the VAT Act.

¹⁹³ Those referred to in paragraph (1)(i) of Schedule 1(1) to the VAT Act.

¹⁹⁴ Paragraph (b) or (c) of the definition of “exported” in section 1(1) of the VAT Act.

¹⁹⁵ Section 11(2)(i) of the VAT Act.

¹⁹⁶ Section 11(2)(j) of the VAT Act.

¹⁹⁷ Section 11(2)(k) of the VAT Act.

property (excluding debt; equity; or participatory securities) in South Africa when the services are rendered, except movable property exported to that person after the supply of the services, or which forms part of a supply by that person to a registered vendor and the services are supplied to that person for purposes of the supply to the registered vendor; or

- supplied directly to that person or another person, except services which form part of a supply by that person to a registered vendor and the services are supplied to that person for purposes of the supply to the registered vendor, if that person or another person is in South Africa when the services are rendered; and
- it comprises of the acceptance of an obligation to refrain from carrying on any enterprise, to the extent that the carrying on of that enterprise would have occurred in South Africa¹⁹⁸;
- services comprising:
 - filing, prosecution, granting, maintenance, transfer, assignment, licensing or enforcement, including the incidental supply by the supplier of such services or any other services necessary for the supply of the services, of intellectual property rights, including patents, designs, trademarks, copyrights, knowhow, confidential information, trade secrets or similar rights;
 - acceptance of an obligation to refrain from pursuing or exercising in whole or in part any such rights, to the extent that the rights are used outside South Africa¹⁹⁹;
- services supplied by a vendor for purposes of his foreign branch or main business²⁰⁰, except if:
 - supplied directly in connection with land or improvements or movable property (excluding debt; equity; or participatory securities) in South Africa when the services are rendered, except movable property consigned or delivered to that person at an address in an export country after the supply of the services or which forms part of a supply by that person to a registered vendor and the services are supplied to that person for purposes of the

¹⁹⁸ Section 11(2)(l) of the VAT Act.

¹⁹⁹ Section 11(2)(m) of the VAT Act.

²⁰⁰ As contemplated in section 8(9) of the VAT Act.

- supply to the registered vendor; or
- supplied directly to that person or another person, except services which form part of a supply by that person to a registered vendor and the services are supplied to that person for purposes of the supply to the registered vendor, if that person or another person is in South Africa when the services are rendered²⁰¹;
- vocational training of employees (not educational services) for a non-resident non-vendor employer²⁰²; and
- services relating to goods under warranty to the extent that the services are provided for consideration in terms of the warranty and supplied to a non-resident non-vendor warrantor who is outside South Africa when the services are rendered, if the goods were subject to tax upon importation²⁰³.

Insuring or arranging of insurance relating to cross-border supplies

The VAT Act zero rates the insurance or arranging of insurance, or arranging of international transport of passengers or goods²⁰⁴. Services supplied directly in connection with land (and improvements thereto) situated outside South Africa are also subject to the zero rate²⁰⁵. This zero rate would arguably not apply to insurance services on the basis that insurance services cannot be supplied directly in connection with land²⁰⁶ (Rudolph, 2012). Services supplied directly in respect of movable property situated outside South Africa when the services are rendered; goods temporarily admitted into South Africa which are exempt from VAT on importation; certain goods “exported”²⁰⁷; and repair, maintenance, cleaning or

²⁰¹ Section 11(2)(o) of the VAT Act.

²⁰² Section 11(2)(r) of the VAT Act.

²⁰³ Section 11(2)(v) of the VAT Act.

²⁰⁴ Section 11(2)(d) of the VAT Act.

²⁰⁵ Section 11(2)(f) of the VAT Act.

²⁰⁶ This issue and other questions relating to the VAT effects of short term insurance has, to a large extent, been clarified as SARS in consultation with a SAIA established VAT Committee, represented by VAT specialists and the insurance industry to finalise a general written ruling, (reconfirming a ruling which the industry relied on since 1991) and a “Value-Added Tax Guide for Short Term Insurance”.

²⁰⁷ Paragraph (b) or (c) of the definition of “exported” in section 1(1) of the VAT Act.

reconditioning of a foreign going ship or aircraft; are also subject to the zero rate²⁰⁸. Insurance services could arguably be zero-rated in terms of these provisions (Rudolph, 2012).

Certain financial services are arguably supplied directly in respect of movable property situated outside South Africa and subject to the zero rate in terms of these provisions. Clarification of the differences (if any) in meaning of the phrases “directly in respect of”²⁰⁹ and “directly in connection with”²¹⁰ would enhance legislative clarity (Rudolph, 2012).

Services directly in connection with land or improvements outside South Africa

The VAT Act zero rates services supplied directly in connection with land or improvements situated outside South Africa²¹¹. This zero rating provision deems the consumption of services supplied directly in connection with land or improvements to be where the land is located.

Services directly in connection with movable goods outside South Africa or goods temporarily admitted into South Africa

The VAT Act zero rates services supplied directly in respect of movable property outside South Africa when the services are rendered, or goods temporarily admitted into South Africa which are exempt from VAT on importation, or certain goods “exported”²¹², or repairs, maintenance, cleaning or reconditioning of a foreign going ship or aircraft²¹³. The zero rating provision deems consumption of services supplied directly in connection with movable goods to be where the goods are situated when the services are rendered. The zero rate provision also approximates consumption of services supplied directly in connection with goods temporarily admitted into South Africa not to be in South Africa.

²⁰⁸ Section 11(2)(g) of the VAT Act.

²⁰⁹ Section 11(2)(g) of the VAT Act.

²¹⁰ In, for example, sections 11(2)(f) and 11(2)(l) of the VAT Act.

²¹¹ Section 11(2)(f) of the VAT Act.

²¹² Paragraph (b) or (c) of the definition of “exported” in section 1(1) of the VAT Act.

²¹³ Section 11(2)(g) of the VAT Act.

Services relating to “exported goods”, foreign going ships or aircraft, containers, and foreign owned railway trains

The VAT Act zero rates certain services relating to foreign going ships or aircraft, and certain containers²¹⁴ situated in South Africa; services of arranging the supply of certain “exported” goods²¹⁵ and transport of goods and ancillary transport services in South Africa for a non-resident non-vendor²¹⁶. Repairs, maintenance, cleaning or reconditioning of a railway train operated by a non-resident non-vendor are also subject to the zero rate²¹⁷. This zero rating provision deems the consumption of services relating to foreign going ships or aircraft, and certain containers, to be outside South Africa. This zero rating provision further deems the consumption of repairs, maintenance, cleaning or reconditioning of a railway train operated by a non-resident non-vendor to be outside South Africa.

Services physically rendered outside South Africa or to a customs controlled area enterprise or an IDZ operator in a customs controlled area

Services which are physically rendered elsewhere than in South Africa or to a customs controlled area enterprise or an IDZ operator in a customs controlled area can be zero rated²¹⁸. Services that are supplied to the non-resident or any other person whilst the non-resident or the other person is in South Africa, cannot be zero rated. This zero rating provision deems the consumption of services physically rendered elsewhere than in South Africa, or to a customs controlled area enterprise, or an IDZ operator in a customs controlled area to be outside South Africa. It can be concluded that the VAT Act attributes the place of consumption, in this instance, to the place of performance²¹⁹. This can be justified if consumption in the particular

²¹⁴ Those referred to in paragraph (1)(i) of Schedule 1(1) to the VAT Act.

²¹⁵ Paragraph (b) or (c) of the definition of “exported” in section 1(1) of the VAT Act.

²¹⁶ Section 11(2)(i) of the VAT Act.

²¹⁷ Section 11(2)(j) of the VAT Act.

²¹⁸ Section 11(2)(k) of the VAT Act.

²¹⁹ The European model applies this proxy²¹⁹ to a designated list of services that would be expected to be consumed where they are performed (Millar, 2008:201/202). New Zealand imposes a limitation by reference to the underlying principle, namely the place of performance only results in zero-rating if the nature of the services is such that they can only be physically received at the time and place where they are physically performed.

circumstances can only occur where performance happens.

Services capable of physical performance should be taxed in the jurisdiction where they are performed, as they are generally consumed in such jurisdiction (Badenhorst, 2011). Services capable of physical performance include cultural performances, sporting events, conferences, meetings, entertainment, construction services, training and education (Badenhorst, 2011). Clarification regarding whether the services must be capable of being physically rendered and what is meant by physically rendered may add to legislative certainty. This provision arguably does not apply to insurance and certain financial services which are not capable of being physically rendered. SARS apparently interprets this provision to apply only if the services are consumed outside South Africa, irrespective of where the services are actually rendered (Prinsloo, 2012). SARS is also of the view that a vendor cannot rely on this provision if the supplies are made to a South African recipient where the supplier has subcontracted the services physically supplied elsewhere than in South Africa (van Heerden, 2012).

Consumption of services not capable of being physically rendered should arguably not be determined with reference to a person's "fixed or permanent place in the Republic", but with reference to the location of the recipient, which can be assumed to be where the services are consumed (Badenhorst, 2011). Attributing consumption of intangible or virtual services to the location of the recipient approximates where the profit or income is earned from those services (Connell, 2011). Although consumption of services not capable of being physically rendered should be assumed to be where the recipient is located, it should not necessarily give rise to VAT registration of a foreign supplier in South Africa (Badenhorst, 2011). This is so since the location of "enterprise or activity" as envisaged in the definition of "enterprise" may differ from the place of consumption²²⁰ (Badenhorst, 2011).

Services to non-residents outside South Africa

The VAT Act zero rates the supply of services to a non-resident, except if:

²²⁰ In accordance with the judgement in VAT Case 179 and the authorities quoted in that case.

- supplied directly in connection with land or improvements or movable property (excluding debt; equity; or participatory securities) in South Africa when the services are rendered, except movable property exported to that person after the supply of the services or which forms part of a supply by that person to a registered vendor and the services are supplied to that person for purposes of the supply to the registered vendor; or
- supplied directly to that person or another person (except services which form part of a supply by that person to a registered vendor and the services are supplied to that person for purposes of the supply to the registered vendor) if that person or another person is in South Africa when the services are rendered; and
- it comprises the acceptance of an obligation to refrain from carrying on any enterprise, to the extent that the carrying on of that enterprise would have occurred in South Africa²²¹.

This zero rating provision mainly deems the consumption of services supplied to a non-resident, to be outside South Africa. This provision then attributes consumption of services supplied directly in connection with land or improvements or movable property (excluding debt; equity; or participatory securities) in South Africa when the services are rendered, to be in South Africa. Consumption of services directly in connection with movable property exported after the supply, or which forms part of a supply to a registered vendor is assumed to be outside South Africa²²². This provision also attributes the consumption of services supplied directly to a person in South Africa when the services are rendered (except services which form part of a supply by that person to a registered vendor and the services are supplied to that person for purposes of the supply to the registered vendor) to South Africa.

The wording used in this provision is ambiguous and consideration should be given to providing more legislative certainty in respect of the terms “directly” and “directly in connection with” (as opposed to “directly in respect of”) and the reference to “other person” (van Heerden, 2012). The reference to “other person” adds further interpretational difficulties as it seems to imply a differentiation by the legislator

²²¹ Section 11(2)(l) of the VAT Act.

²²² See also SARFU case.

between the contractual and beneficial recipient of a supply (de Wet, 2012). This is one of the most relied on provisions to zero rate services to non-residents (Schneider, 2012). The section has been the subject of many debates and has been amended a number of times since the introduction of VAT. It has also been the subject of many court cases over the past 25 years. The evolution of the provision may give an indication of its ultimate objective and potentially its current meaning and purpose (Schneider, 2012).

The provision, when first introduced, was mainly adapted from New Zealand's GST (Schneider, 2012). The 1991 wording was fairly basic and, in effect, zero rated services supplied to and for a non-resident who was outside South Africa when the services were rendered, if the services were not supplied directly in connection with land or improvements in South Africa or movable property in South Africa when rendered. The legislator soon realised that the wording did not adequately cater for many scenarios (Schneider, 2012).

The most significant change to this provision was made in 1997 (Schneider, 2012). The 1997 change provided context to the wording of the provision in that it changed the wording supplied "to and for" a non-resident to read "for the benefit of and contractually to" a non-resident. The amendment also addressed the denial of the zero rate where the services were supplied directly in connection with movable property in South Africa when the services were rendered. The amendment introduced an exception (to the movable property exception) by allowing the zero rate to apply even though the services are supplied directly in connection with movable property in South Africa as long as the movable property was exported to the non-resident subsequent to the services, or where the movable property formed part of supply by the non-resident to a registered vendor and the services were supplied to the non-resident for purposes of its supply to the vendor. Although the 1997 amendment may have complicated the provision it also created a clear "proxy" to ensure that foreign consumption is not subject to VAT and that final domestic consumption is taxed. The Explanatory Memorandum inferred that the legislator may have adopted the principles established in the New Zealand GST case of

Wilson and Horton, as it provided that:

...any incidental benefit derived by a person...in...(South Africa) should (not) disqualify the supply of the service from being zero-rated. Where...a local newspaper contracts with a foreign advertiser to publish an advertisement, the local newspaper will supply the service to the foreign advertiser at the zero rate. The fact that local readers of the newspaper may also benefit from reading the advertisement is...incidental and will not require the service to be supplied at the standard rate. The word “directly”...ensures that an incidental benefit will not affect the zero-rating... (Schneider, 2012).

In the New Zealand case, *Wilson and Horton Ltd* (1994 and 1995), the Court considered whether advertising space supplied by a resident company to non-residents was “directly in connection with” goods situated in New Zealand (Schneider, 2012). Wilson and Horton placed advertisements in the *New Zealand Herald* directed at foreign clients, which they zero-rated. The Court held that “(t)he supply of space and the services rendered by Wilson and Horton are directly connected with the advertising but not with the goods advertised. The goods are... at least one step removed from the services supplied...” (Schneider, 2012).

The current wording originates from the 1998 amendment, which replaced the words “for the benefit of and contractually to” a non-resident with “to” a non-resident (Schneider, 2012). The Supreme Court of Appeal handed down two important VAT judgments in this regard. In *Commissioner for SARS v De Beers Consolidated Mines Limited* (1 June 2012) the Court followed a practical approach to determine the “place of consumption” of services and concluded *in casu* that services consumed by the board of directors are consumed where the board meets to consider and decide issues and where transactions are implemented. *Stellenbosch Farmers' Winery v Commissioner for SARS*²²³ (25 May 2012) addressed two

²²³ In 1991 United Distillers (UD), a UK based company, and SFW signed a distribution agreement. In terms of the agreement UD granted SFW an exclusive distribution right to resell Bell's, Haig, and Dimple Scotch whisky in Southern Africa for 10 years. Due to group restructuring in 1997 UD sought early termination of the distribution agreement. In 1998 the parties dissolved the agreement and UD agreed to pay SFW an amount in respect of the termination.

important principles. Firstly, the Court confirmed that the early termination of a distribution right occurred in the course or furtherance of Stellenbosch Farmers' Winery's VAT enterprise and was integral to "...the furtherance of the enterprise carried on..." and constituted a taxable supply of a service. The service was held not to have been supplied directly in connection with movable property situated in South Africa (Schneider, 2012). Secondly, the Court confirmed that an incorporeal right is located where the grantor resides, thereby clarifying the place of supply of a contractual right for VAT purposes (Badenhorst, 2011).

In *Master Currency (Pty) Ltd v Commissioner for SARS* (unreported judgment, VAT case number 712) it was held that currency or money is not movable property for VAT purposes since "goods" include corporeal movable things and exclude money, and "services" exclude the supply of money (Schneider, 2012). The Court also held that foreign currency exchange services in a duty free area are consumed in South Africa and do not constitute exports. The Court held that a company in a duty-free area of an airport is located in South Africa for VAT purposes and that the zero rate cannot be applied.

In ITC 1646 it was held that the supply of tickets to non-residents for the Rugby World Cup 1995 in South Africa did not qualify for the zero-rate²²⁴. In *South African Rugby Football Union (SARFU) v Commissioner for SARS* (the appeal from ITC 1646), the Court held that section 11(2)(l) did not apply as SARFU failed to prove that the overseas organisers were not residents of South Africa at the time of supply. It also held that it was likely that they conducted activities and had a fixed place of business in South Africa.

SARS Interpretation Note 42, which deals with travel agents who sell packaged tours to non-residents, treats the constituent parts of tour packages as separate supplies²²⁵. The provision of hotel accommodation in South Africa to a foreign tourist is standard-rated, irrespective from where or through whom it was booked or paid for, on the basis that the accommodation is used and enjoyed in South Africa. A

²²⁴ Section 11(2)(l) of the VAT Act.

²²⁵ Section 8(15) of the VAT Act.

travel agent's fee for arranging the accommodation prior to arrival of the tourist in South Africa, however, is subject to the zero-rate (Schneider, 2012).

Intangible property

The VAT Act²²⁶ zero rates the supply of filing, prosecution, granting, maintenance, transfer, assignment, licensing and enforcement in respect of intellectual property rights (including patents, designs, trademarks, copyrights, know-how, confidential information, trade secrets or similar rights) to any person, where the rights are used outside South Africa. This zero rating of intellectual property rights used outside South Africa attributes consumption to a place outside South Africa. South Africa should consider introducing rules²²⁷ to ensure that foreign enterprises do not have to register if they supply intangible property to a South Africa vendor for purposes of carrying on taxable supplies, if the South Africa vendor will be entitled to a full input tax deduction (Prinsloo, 2012). The foreign enterprise should be deemed to conduct an enterprise activity in South Africa where the foreign enterprise is making available intangible property in South Africa to a non-registered South Africa person or to a vendor who utilises the intangible services wholly or partially to make exempt supplies (Prinsloo, 2012).

Services to foreign branches or main businesses

The VAT Act zero rates²²⁸ services deemed to be supplied²²⁹ by a vendor to or for the purposes of its foreign branch or main business. This zero rating provision attributes consumption of services supplied by a vendor to or for the purposes of his foreign branch or main business to a place outside South Africa.

Services relating to cross-border warranties

The VAT Act zero rates services relating to goods under warranty to the extent that the services are provided for consideration in terms of a warranty and supplied to a non-resident non-vendor warrantor who is outside South Africa when the services

²²⁶ Section 11(2)(m) of the VAT Act.

²²⁷ Similar to section 8(4) of the New Zealand GST Act.

²²⁸ Section 11(2)(o) of the VAT Act.

²²⁹ Section 8(9) of the VAT Act.

are rendered, if the goods were subject to tax upon importation²³⁰. This provision attributes consumption of services relating to goods under warranty supplied to a non-resident non-vendor warrantor who is outside South Africa when the services are rendered, if the goods were subject to tax upon importation, to be outside South Africa.

The above section critically considered the VAT rate provisions relating to inter-jurisdictional supplies with a view to identifying potential shortcomings. This entailed a detailed consideration of the VAT consequences of exemptions and zero ratings; inter-jurisdictional supplies of goods; supplies of foreign land; and goods supplied by non-residents before entry for home consumption. The section also considered the VAT treatment of inter-jurisdictional supplies of services; including insurance; services connected with land or movable goods outside South Africa; services connected with goods temporarily admitted into South Africa; services relating to “exported goods”, foreign ships or aircraft, containers, and foreign owned railway trains; services physically rendered outside South Africa or to a customs controlled area enterprise or an IDZ operator in a customs controlled area; services to non-residents outside South Africa; intangible property; services to foreign branches or main businesses; and services relating to cross-border warranties. The section that follows contains a detailed consideration of the VAT provisions relating to imported services with a view to documenting current shortcomings.

5.2.4 Imported services

The imported service provisions impose VAT on certain imported services and act as an anti-avoidance section (Badenhorst, 2006). The imported service provisions theoretically ensure that consumption of imported services and consumption of local supplies receive the same VAT treatment. In the absence of the imported service provisions a VAT exempt entity or non-registered person who acquires services from abroad would pay less VAT, compared to when buying from a VAT registered person (Badenhorst, 2006). The VAT Act imposes VAT at 14% on the importation of

²³⁰ Section 11(2)(v) of the VAT Act.

certain services²³¹. The term “imported services” is defined as:

...a supply of services that is made by a supplier who is resident or carries on business outside the Republic to a recipient who is a resident of the Republic to the extent that such services are utilized or consumed in the Republic otherwise than for the purpose of making taxable supplies²³².

The concept “imported services”²³³ contains the following elements:

- a supply of services made;
- by a supplier who is resident or carries on business outside South Africa;
- to a recipient who is resident in South Africa;
- to the extent that such services are utilised or consumed in South Africa;
- otherwise than for the making of taxable supplies.

A person who acquires services from a non-resident is required to account for VAT on imported services or if the services are acquired for purposes other than making taxable supplies. The VAT on imported service provisions are wide enough to mandate that all individuals and non-vendors and vendors that import services to make non-taxable supplies should account for output tax. A foreign person that falls into the definition of “resident of the Republic” can also be liable for VAT on imported services, irrespective of whether it is a vendor (Badenhorst, 2011). Although the taxation of “imported services” is arguably not a place of supply rule²³⁴, rules that give guidance on whether imported services are consumed or utilized in South Africa will add to legislative certainty (Rudolph, 2012). One of the main problems in the South African VAT environment with regard to “imported services” is that Government itself has not, until recently, accounted for VAT on imported services (van Heerden, 2012). The recipient of imported services is required to calculate the tax payable²³⁵ and remit payment to the SARS within 30 days of the time of

²³¹ Section 7(1)(c) of the VAT Act.

²³² Section 1(1) of the VAT Act.

²³³ Section 7(1)(c) of the VAT Act.

²³⁴ This view is shared unanimously by all respondents who completed the questionnaire.

²³⁵ Section 7(1)(c) of the VAT Act.

supply²³⁶.

The VAT Act exempts²³⁷ from imported services VAT, a supply which:

- is subject to the general charging section²³⁸;
- if made in South Africa, would be zero-rated²³⁹; or
- if made in South Africa, would be exempt²⁴⁰.

As a result, if a supplier outside South Africa provides services to a resident in South Africa that is subject to VAT in terms of the general charging section or zero rated or exempt if it had been provided in South Africa, VAT on imported services does not become payable. The VAT Act exempts investment income earned in South Africa from VAT. Investment income earned from foreign investments is subject to the zero rate, as the zero rate overrides the exemption²⁴¹. As a result, investment income earned on foreign investments constitutes consideration for a taxable supply, and is subject to the zero rate. It can be argued that a foreign financial institution's services are utilized and consumed where the services are physically performed, and where the funds and investments to which they directly relate, are located (Badenhorst, 2007). The services are physically performed outside South Africa and the underlying funds and investments are located outside South Africa. In the absence of specific "place of supply rules", the services provided by a foreign financial institution would then arguably be utilized or consumed outside South Africa. The fact that the South African resident may benefit from the services rendered by the foreign financial institution, does not render the services utilized or consumed in South Africa. This is an interesting observation which, if correct, could potentially result in non-taxation as the foreign jurisdiction may also zero rate the foreign financial institution's services on the basis that the supply is to a non-resident not present in the foreign jurisdiction when the services are rendered.

²³⁶ Section 14(1) of the VAT Act.

²³⁷ Section 14(5) of the VAT Act.

²³⁸ Section 7(1)(a) of the VAT Act.

²³⁹ Section 11 of the VAT Act.

²⁴⁰ Section 12 of the VAT Act.

²⁴¹ Section 12(a) of the VAT Act.

Services supplied by a foreign financial institution can be directly attributed to zero-rated foreign investment income earned by the South African resident from the foreign investment. To that extent, the foreign financial institution's services will be utilized or consumed for the purpose of making taxable supplies (namely earning zero rated foreign investment income) and should not be subject to VAT on imported services, even if the services are utilized or consumed in South Africa.

SARS (2005a) published VAT General Written Ruling 442 in March 2005, which held that where a South African resident invests monies abroad and incurs fees, charges or commissions from the foreign financial institution for administering the foreign investments, these services are considered to be consumed in the foreign country, and are not regarded as imported services. The South African resident was, as a result, not required to account for imported services VAT. SARS' amended VAT General Written Ruling 442²⁴² provided that the consumption of the services provided by a foreign financial institution takes place in South Africa, which required the South African investor to account for VAT on imported services. In light of the revised VAT General Written Ruling 442, not only foreign bank related services became subject to VAT on imported services but also foreign portfolio management fees, which has major cost implications for financial institutions investing funds abroad. SARS subsequently withdrew all VAT general written rulings, including VAT General Written Ruling 442.

In VAT case 144²⁴³ a life insurance company acquired services from various overseas consultants and suppliers. The Court confirmed that a supply cannot be subject to the general charging section and to VAT on imported services simultaneously. Where a foreign supplier regularly and continuously supplies services in South Africa, the foreign supplier conducts a VAT "enterprise" and is required to register and account for VAT. Failure to register does not render the recipient liable to account for VAT on imported services. To assess whether VAT on imported services is payable it needs to be determined where the South African

²⁴² Effective 1 March 2006.

²⁴³ VAT 144 [2006] JOL 17138 (TC).

resident utilizes or consumes the services supplied by the foreign financial institution. The VAT Act does not provide guidance on where these services are consumed. Services supplied by a foreign financial institution will typically include administration of the foreign investments, investing funds transferred by the South African resident, the withdrawal of funds, the calculation of investment returns, the preparation and submission of regular investment statements, the acquisition and disposal of investments, and transferring of funds into and from investment portfolios. The foreign financial institution physically renders the administration services in the country where the bank or investment account is located, by staff located outside South Africa. The services are rendered in respect of underlying investments located outside South Africa. The investments are acquired or disposed of outside South Africa (Badenhorst, 2007).

Up to this point this chapter set out to describe the current VAT provisions relating to non-resident persons with a link or connection to South Africa, the VAT rate applicable to inter-jurisdictional supplies; and VAT on imported services. This section also set out to identify and describe the current shortcomings. The following section will attempt to suggest broad guidelines on what specifically should be addressed (in detail) and how this could be addressed, without actually going so far as to actually provide recommended wording for legislative changes.

5.3 ADDRESSING INTER-JURISDICTIONAL SHORTCOMINGS

5.3.1 A framework for addressing inter-jurisdictional VAT rule shortcomings

VAT systems generally seek to tax local or territorial consumption of goods and services (Theron, 2012). Tax authorities must, as a result, be able to allocate taxing rights to supplies. The South African VAT system subjects to tax, supplies made through “activities...conducted...in South Africa or partially in the Republic” (contained in the definition of “enterprise”). The allocation of these taxing rights is impacted by the destination principle²⁴⁴, which seeks to tax domestic “consumption”

²⁴⁴ Report of the Value-Added Tax Committee, 19 February 1991, at p 2; Guide for Vendors (VAT 404) 6 September 2011, par 1.1.

of goods or services (Meyburgh, 2011), regardless of where the goods are produced or where the services are rendered. Certain zero rate provisions ensure that only domestic consumption remains standard rated (Meyburgh, 2011). Inter-jurisdictional VAT rules should allocate VAT to the country where consumption takes place (National Treasury, 2012).

The remainder of this chapter considers the shortcomings in the inter-jurisdictional VAT rules (treatment of non-resident VAT registrations and VAT rates applicable to cross border supplies) in South Africa; formulates, in tabular format, high level proposals to address these shortcomings; and considers, on a high level basis, the introduction of certain specific place of supply rules in the South African VAT system.

Meaning of inter-jurisdictional VAT rules

Inter-jurisdictional VAT rules can be defined as rules which govern where supplies are made and how taxing rights are allocated between tax jurisdictions (Blakeley, 2012). In the South African context, these would be the rules which determine the applicable VAT rate and when a person would be conducting a VAT “enterprise” (Terblanche, 2012).

Objectives of inter-jurisdictional VAT rules

The objectives of place of supply and other inter-jurisdictional VAT rules should be to provide:

- protection from intra-jurisdictional double taxation or non-taxation;
- certainty for suppliers and recipients on the jurisdictional allocation of taxing rights;
- certainty for suppliers and recipients on the VAT rate applicable to a supply;
- certainty on a person’s obligation to register for VAT; and
- increased equity in the tax system (Nellen, 2012).

Introducing refined rules governing inter-jurisdictional transactions which guide the place of consumption, supply, and “enterprise or activity” and explicit place of supply rules, should be considered for the following reasons:

- Taxpayers have the right to fair administrative action in terms of the Constitution.
- A tax system should provide certainty, especially in a self-assessment environment such as VAT.
- A tax system should ensure global VAT harmonisation.
- A tax system should promote (or not discourage) foreign direct investment and trade between South Africa and other countries (Terblanche, 2012 and Theron, 2012).

Allowing for discretion in defining inter-jurisdictional VAT rules

Discretionary powers should be limited as far as possible as they could create uncertainty (Chauke, 2012). Discretionary powers could potentially empower the Commissioner for SARS to broaden or narrow the reach of the VAT system (Glyn-Jones, 2012 and Meyburgh, 2011). However, in so far as practically possible, comprehensive inter-jurisdictional VAT rules may render it unnecessary to grant the Commissioner for SARS discretionary powers except for services or activities not included in the rules (Chauke, 2012)²⁴⁵. Since the Commissioner for SARS is responsible for administering the VAT Act and National Treasury is responsible for tax policy, it can be argued that all deeming provisions should be part of the VAT Act (National Treasury, 2012).

Developing a proxy for “utilised or consumed”

Defining the terms “utilised” or “consumed” could be an appropriate mechanism for determining the incidence of VAT on a supply (National Treasury, 2012). The place of consumption of intangible services should deem the services to be supplied where the recipient is located, due to the practical difficulty of determining the actual place of consumption (Badenhorst, 2011). This may not always be the case, for example, if computer software is provided by a non-resident to a resident, the computer software can be used in South Africa or outside South Africa if the recipient travels (Badenhorst, 2011). Place of consumption, “enterprise or activity”, or supply rules should provide specific guidance in respect of insurance services (for

²⁴⁵ Although the majority of respondents to the questionnaire agreed that discretion should be limited as far as possible, Connell (2011) and Schenk (2012) favour discretionary powers, the latter arguing the need for this in a worldwide VAT system.

example, based on location of the risk and the insured, etc.) (Meyburgh, 2011). A general rule could be introduced which clarifies that the South African VAT system seeks to tax final domestic consumption (van Heerden, 2012).

Method of introducing inter-jurisdictional VAT rules

Inter-jurisdictional VAT rules will become increasingly important as South Africa develops and integrates globally and electronic transacting increases (Chauke, 2012). The VAT Act should define place of “enterprise or activity” rules to provide clarity with regard to the obligation of a person, especially non-South African residents, to register for VAT purposes in South Africa (Badenhorst, 2011). A definition of “enterprise or activity” would provide clarity with regard to the extent to which the activity will give rise to a VAT registration in South Africa²⁴⁶. For example, once-off projects which extend over a period, begs the question whether a non-resident has an obligation to register for VAT purposes if it conducts a once-off activity or project in South Africa that is expected to be completed within a limited time frame. The legislator could clarify the time frame that would necessitate VAT registration (Badenhorst, 2011).

Defining place of “consumption” rules to assist with the VAT rate could be done through an interpretation note or a regulation that forms part of the law, drafted and agreed upon by industry, National Treasury and SARS (Rudolph, 2012). Place of consumption, “enterprise or activity”, and supply rules should preferably be introduced as law and not by way of an interpretation note (de Wet, 2012 and Theron, 2012). This could be done by insertion of a separate section in the VAT Act as a single point of reference which would increase interpretational certainty (Theron, 2012; Connell, 2011; and de Wet, 2012).

The VAT Act should contain a general place of supply rule with a general definition and regulations for different types of supplies (Badenhorst, 2011).

²⁴⁶ This recommendation could imply introducing a certain degree of subjectivity that will allow SARS to exclude limited activities from the liability to register in certain instances.

5.3.2 Non-resident VAT registration

One of the major shortcomings in VAT policy is arguably that Government has not made a firm policy decision on how to treat supplies made in South Africa by foreign businesses, in the absence of a fixed or permanent place of business (van Heerden, 2012). Inter-jurisdictional VAT rules should serve to establish what to tax, whilst endeavouring to reduce the need for tax compliance and attract foreign domestic investment where possible (Glyn-Jones, 2012). Inter-jurisdictional VAT rules should also provide clarity with regard to when a foreign principal who conducts business through an agent (binding agent) or a sub-contractor (non-binding agent) in South Africa would be creating an “enterprise” for VAT purposes (Rudolph, 2012). Where goods or services are supplied through agents or sub-contractors in South Africa, the services should not give rise to an obligation to register for VAT in South Africa. The supply of goods will, in any event, be taxable on importation into South Africa, and the supply through agents or subcontractors should qualify for the zero rate²⁴⁷ if provided to registered vendors (Badenhorst, 2011).

In addition to clearly defining “enterprise or activity” as contained in the definition of “enterprise”, the provision relating to local and foreign “branches or main businesses” should be clarified. Introducing inter-jurisdictional VAT rules to narrow the obligation of foreign entities to register for VAT in South Africa, to activities carried on within South Africa from a fixed or permanent place of business in South Africa²⁴⁸ could be considered (Badenhorst, 2011). Such place of activity rules would therefore not result in a loss of revenue to the State. The legislator could consider allowing foreign businesses not to register for VAT purposes where non-registration will not result in VAT leakage. This will reduce the cost of tax compliance of foreign persons and SARS²⁴⁹.

²⁴⁷ Section 11(2)(l)(ii)(bb) of the VAT Act.

²⁴⁸ Refer to the examples in VAT Notice 741A of HM Customs and Excise.

²⁴⁹ Provisions similar to section 54(2A)(b) in respect of goods and section 11(2)(l)(ii) with respect to services could be considered in order to keep certain foreign persons outside of the VAT net (Terblanche, 2012).

The most significant shortcomings in the South African VAT system with regard to foreign business activities in South Africa which could be addressed by law changes or introducing specific place of supply rules are captured in Table 5.1 below.

Table 5.1: Place of supply and foreign business activities in South Africa

	Illustrations and Shortcomings	Potential Solutions
<i>Intangible property</i>	<p>The law and various communications of SARS on the subject make it unclear whether a foreign business that makes intellectual property (owned and registered offshore) available to residents on a continuous basis or supplies services via the internet could create a VAT “enterprise”, even if the non-resident has little or no physical activities or may not use any equipment or facilities locally.</p> <p>This uncertainty is exacerbated as the intellectual property could legally be made available in or outside South Africa.</p>	<ol style="list-style-type: none"> 1 Physical activities (which need to be defined) and not only supplies, should be a pre-requisite to create a VAT “enterprise” (Meyburgh, 2011). 2 Rules²⁵⁰ could be introduced to ensure that foreign enterprises are not required to register if they supply intangible property to a vendor if the vendor will be entitled to a full input tax deduction (Prinsloo, 2012). 3 A foreign enterprise can be deemed to conduct an “enterprise” in South Africa if it makes intangible property available in South Africa to a non-registered person or a vendor who uses the services wholly or partially to make exempt supplies (Prinsloo, 2012). 4 The meaning of an “enterprise or activity” (physical, contractual, or economic) should be clarified (Rudolph, 2012).
<i>Turnkey projects</i>	<p>Where a foreign supplier designs and constructs goods and makes</p>	<ol style="list-style-type: none"> 5 Proviso (ii) to “enterprise” could provide more guidance on how

²⁵⁰ Similar to section 8(4) of the New Zealand GST Act.

	<p>supplies in and outside South Africa, the VAT treatment creates uncertainty. This arises due to difficulty in determining which activities are carried out inside and which outside of South Africa and, if outside South Africa, what the value of the supplies are that were generated from the offshore activities. These difficulties often arise if the delivery price is not split between local and foreign activities.</p>	<p>to split activities and attribute values to these activities in and outside of South Africa (Meyburgh, 2011).</p>
<p><i>Supplies made through Agents</i></p>	<p>The law is unclear as to whether a foreign business that subcontracts the supply of services to a local subcontractor and the non-resident entity imports goods into South Africa for this purpose, would create a VAT “enterprise”. Goods imported are deemed to be imported by the agent (and not the foreign principal) in terms of section 54(2A) (b), read with section 8(20).</p> <p>The law does not differentiate between a foreign business appointing a local binding agent, as opposed to an independent agent, to render services for and on its behalf.</p>	<p>6 It should be clarified whether a foreign business conducts an “enterprise” through an agent making supplies on its behalf in South Africa (Rudolph, 2012).</p> <p>7 A foreign business should be permitted not to register as a VAT vendor if it supplies services through a local agent and the agent assumes its VAT obligations (Prinsloo, 2012).</p>
<p><i>Enabling activities resulting in supplies</i></p>	<p>The law is unclear on whether a foreign business that has activities in South Africa purely to enable the making of supplies outside South Africa would create an “enterprise” for VAT purposes, for example, where a foreign news agency sends reporters to South Africa on a continuous and regular basis to gather information. The information is used offshore by the main business to compile news programmes which</p>	<p>8 It should be clarified whether supplies emanating from enabling activities in South Africa are made in South Africa and whether the off-shore supplier would carry on a VAT “enterprise” (Connell, 2011).</p>

	<p>are then broadcasted across the world, including locally.</p>	
<p><i>Electronically provided services</i></p>	<p>Specific potential shortcomings in the current electronic services VAT provisions include the registration threshold; the need to issue tax invoices; applying the provisions to supplies in a group of companies; listing electronic services versus differentiating between business-to-business and business-to-consumer services; and certain interpretational shortcomings.</p>	<p>9 The registration threshold for foreign electronic service suppliers should be reconsidered in light of the OECD neutrality principle (Davis VAT Report, 2015:93).</p> <p>10 The OECD recommendations in respect of the issuing of invoices need to be compared to the South African VAT system to establish their appropriateness. The default legal position should require a vendor to adopt the invoice basis whilst retaining the option to use the payments basis, subject to the legal requirements (Davis VAT Report, 2015:84).</p> <p>11 Consideration should be given to exclude supplies in a “group of companies” (as defined for Income Tax purposes) from the ambit of the e-commerce provisions (Davis VAT Report, 2015:93).</p> <p>12 Listing qualifying electronic services, as the Regulation does, may not be flexible enough to adapt to developments. Electronically supplied services could be categorised and explained in a</p>

		<p>guide (Davis VAT Report, 2015:93).</p> <p>13 If an exhaustive list is preferred, the Regulation should be reviewed and updated regularly, for example every two years. Attaching specific place of supply rules to actual facilities should be avoided to ensure flexibility (Davis VAT Report, 2015:93).</p> <p>14 It should be considered whether the Regulation should distinguish between business-to-business and business-to-consumer supplies (Davis VAT Report, 2015:89).</p> <p>15 Interpretational shortcomings in the Regulation should be addressed, for example “still image”; “subscription service to a web site”; and “subscription” (Davis VAT Report, 2015:91-92).</p>
<p>Limited duration supplies</p>	<p>The law is not clear on whether a foreign supplier who enters South Africa for a once-off predetermined time period to make a supply/ies would create a VAT “enterprise”?</p>	<p>16 It should be clarified at which point limited duration ventures or supplies would create a VAT “enterprise” (Glyn-Jones, 2011).</p>
<p>Supplies of goods before entry for home consumption</p>	<p>The law seems to indicate that a “sale” of goods made whilst the goods are outside South Africa, i.e. the non-resident transacts or acts in consequence of which ownership will pass to another person, but the actual transfer of ownership is delayed until after importation into South Africa (Rudolph, 2012), may create an “enterprise” for the non-resident.</p>	<p>17 The law should be amended or guidance provided to address whether supplies made outside South Africa, but ownership passes in South Africa, would create an “enterprise”.</p>

<p>Consignment goods</p>	<p>The VAT Act is not clear on whether a foreign consignor would create a VAT “enterprise” in South Africa in consequence of ownership in goods passing whilst in South Africa, although it seems plausible. It is also doubtful whether the local consignee would be entitled to claim the VAT incurred on importation as an input tax deduction where the consignment agreement is continuous.</p>	<p>18 It should be clarified whether a consignor creates a VAT “enterprise” and whether the consignee would be entitled to claim an input tax deduction on the goods imported (Glyn-Jones, 2012).</p>
<p>Telecommunication services</p>	<p>Foreign telecommunication suppliers who make supplies of telecommunication services in South Africa without establishing a local presence are currently arguably not conducting an “enterprise” and not required to register for VAT purposes. Arguments could potentially be advanced to the contrary, although it may require some technical supporting evidence to do so. In addition, the VAT Act contained legislation relating to foreign telecommunication service providers, but the legislation never became effective. As a result, the VAT Act currently does not contain any provisions relating to foreign telecommunications.</p>	<p>19 Telecommunication services should be defined and included in the definition of “enterprise” (de Wet, 2012). Various aspects should be clarified or defined, including:</p> <ul style="list-style-type: none"> ▪ international roaming by residents outside South Africa; ▪ non-residents leasing network capacity locally to provide telecommunication services in South Africa; ▪ use of telecommunication infrastructure in South Africa; ▪ consumption of telecommunication services in South Africa; ▪ competitive inequity between domestic and foreign suppliers; and ▪ specific guidance on, for example, whether the use of a server, antenna, cable or satellite network in South Africa will constitute an activity in South Africa.

<p>Foreign Insurance Services</p>	<p>Foreign insurance underwriters writing insurance business in South Africa through binding agents would arguably not carry on an “enterprise”. This is contrary to the provisions that apply to Lloyd’s of London, which is specifically included in the definition of “enterprise”.</p>	<p>20 To the extent that foreign insurers conclude contracts of insurance in South Africa permitted by the Short-term Insurance Act, 1998, they should be required to register as vendors. This should arguably not apply to reinsurers as the Short Term Insurance Act contains adequate safeguards to limit registration to South African business.</p>
<p>Foreign branch or main business</p>	<p>Deeming “transactions” between the local enterprise and its foreign counterpart to be supplies is seemingly unnecessary as the normal provisions which govern transactions between separate legal personae apply. The nature or extent should be determined of the “separate accounting system” that should be maintained (Meyburgh, 2011). Which supplies emanate from activities carried on in South Africa and outside South Africa should be established, especially where a non-resident carries on similar activities inside and outside South Africa (Meyburgh, 2011). A branch or main business as “separate”²⁵¹ should be identified (Badenhorst, 2011). The VAT Act is unclear whether this requirement indicates separate identification with</p>	<p>21 Introducing inter-jurisdictional VAT rules to narrow the obligation of foreign entities to register for VAT in South Africa to activities carried on within South Africa from a fixed or permanent place of business in South Africa²⁵², could be considered (Badenhorst, 2011). Such place of activity rules would therefore not result in a loss of revenue to the State.</p>

²⁵¹ Glyn-Jones (2012) recommended that the New Zealand GST definition of “non-resident” could be implemented.

²⁵² Refer to the examples in VAT Notice 741A of HM Customs and Excise.

	<p>regard to geography, activities and operations, or some other means. The meaning of an “enterprise permanently situated at premises outside the Republic” and whether the enterprise must be carried on from these premises outside South Africa must be clarified. It can, for instance, be questioned whether an intermediary’s premises outside South Africa (neither owned nor rented by the vendor) from which the vendor carries on an enterprise, would fulfil this requirement (Badenhorst, 2011).</p> <p>Whether a foreign branch or main business can have more than one South African VAT registration for the same legal entity must be determined (Connell, 2011).</p> <p>Whether incurring costs and significant action to “carve-out” supplies made outside South Africa from the scope of VAT and keep an independent accounting system must be clarified, due to the worldwide nature of the VAT system (Schenk, 2009:12).</p>	
<p><i>Services supplied to foreign entities consumed in South Africa</i></p>		<p>22 Consideration could be given to zero rate services supplied to, and consumed by, foreign businesses in South Africa. Exceptions, such as accommodation (for example with respect to tour operators), can be addressed through specific exclusions in the zero rating provisions, as was done in Namibia (Terblanche, 2012).</p>
<p><i>Clarification of</i></p>		<p>23 Consideration should be given</p>

important terms		to clarify certain terms used in the VAT Act, associated with “supply” such as “performed”, “rendered”, “supplied, “utilised”, or “consumed” (Prinsloo, 2012).
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The potential solutions derived in this chapter, illustrated in Table 5.1 (above) and Table 5.4 (below), have been analysed and then classified using three colours, as described in Table 5.2 below.

Table 5.2: Colour classification of potential solutions

Colour code	Classification description
<i>Red</i>	<i>The researcher is of the view that the solution suggested is either not justified, or the researcher does not agree that the current legislation contains sufficient uncertainty that requires addressing</i>
<i>Orange</i>	<i>The researcher is of the view that the solution suggested may have merit but implementation is not critical to enhance certainty, or the problem would be addressed elsewhere</i>
<i>Green</i>	<i>The researcher is of the view that the proposed solution needs to be implemented to enhance certainty</i>

Table 5.3 below illustrates the researcher’s classification of the potential solutions in respect of the foreign business activities contained in Table 5.1 above, by making use of Table 5.2 above.

Table 5.3: Place of supply rules in respect of foreign business activities in South Africa – suggested solutions evaluated

	Potential Solutions
Intangible property	1 Physical activities (which need to be defined) and not only supplies, should be a pre-requisite to create a VAT “enterprise”.
	2 Rules ²⁵³ could be introduced to ensure that foreign enterprises are not required to register if they supply intangible property to a vendor if the vendor will be entitled to a full input tax deduction.
	3 A foreign enterprise can be deemed to conduct an “enterprise” in South Africa if it makes intangible property available in South Africa to a non-registered person or a vendor who uses the services wholly or partially to make exempt supplies.
	4 The meaning of an “enterprise or activity” (physical, contractual, or economic) should be clarified.
Turnkey projects	5 Proviso (ii) to “enterprise” could provide more guidance on how to split activities and attribute values to these activities in and outside of South Africa.
Supplies made through Agents	6 It should be clarified whether a foreign business conducts an “enterprise” through an agent making supplies on its behalf in South Africa.
	7 A foreign business should be permitted not to register as a VAT vendor if it supplies services through a local agent and the agent assumes its VAT obligations.
Enabling activities resulting in supplies	8 It should be clarified whether supplies emanating from enabling activities in South Africa are made in South Africa and whether the off-shore supplier would carry on a VAT “enterprise”.
Electronically provided services	9 The registration threshold for foreign electronic service suppliers should be reconsidered in light of the OECD neutrality principle.
	10 The OECD recommendations in respect of the issuing of invoices need to be compared to the South African VAT system to establish their appropriateness. The default legal position should require a vendor to adopt the invoice basis whilst retaining the option to use the payments basis, subject to the legal requirements.
	11 Consideration should be given to exclude supplies in a “group of companies” (as defined for Income Tax purposes) from the ambit of the e-commerce provisions.

²⁵³ Similar to section 8(4) of the New Zealand GST Act.

	12 Listing qualifying electronic services, as the Regulation does, may not be flexible enough to adapt to developments. Electronically supplied services could be categorised and explained in a guide.
	13 If an exhaustive list is preferred, the Regulation should be reviewed and updated regularly, for example every two years. Attaching specific place of supply rules to actual facilities should be avoided to ensure flexibility.
	14 It should be considered whether the Regulation should distinguish between business-to-business and business-to-consumer supplies.
	15 Interpretational shortcomings in the Regulation should be addressed, for example “still image”; “subscription service to a web site”; and “subscription”.
Limited duration supplies	16 It should be clarified at which point limited duration ventures or supplies would create a VAT “enterprise”.
Supplies of goods before entry for home consumption	17 The law should be amended or guidance provided to address whether supplies made outside South Africa, but ownership passes in South Africa, would create an “enterprise”.
Consignment goods	18 It should be clarified whether a consignor creates a VAT “enterprise” and whether the consignee would be entitled to claim an input tax deduction on the goods imported.
Telecommunication services	19 Telecommunication services should be defined and included in the definition of “enterprise”. Various aspects should be clarified or defined.
Foreign Insurance Services	20 To the extent that foreign insurers conclude contracts of insurance in South Africa permitted by the Short-term Insurance Act, 1998, they should be required to register as vendors. This should arguably not apply to reinsurers as the Short Term Insurance Act contains adequate safeguards to limit registration to South African business.
Foreign branch or main business	21 Introducing inter-jurisdictional VAT rules to narrow the obligation of foreign entities to register for VAT in South Africa to activities carried on within South Africa from a fixed or permanent place of business in South Africa ²⁵⁴ , could be considered.
Services supplied to foreign entities consumed in South Africa	24 Consideration could be given to zero rate services supplied to, and consumed by, foreign businesses in South Africa. Exceptions, such as accommodation (for example with respect to tour operators), can be addressed through specific exclusions in the zero rating provisions, as was done in Namibia.
Clarification of important terms	25 Consideration should be given to clarify certain terms used in the VAT Act, associated with “supply” such as “performed”, “rendered”,

²⁵⁴ Refer to examples in VAT Notice 741A of HM Customs and Excise.

5.3.3 VAT rate applicable to inter-jurisdictional supplies and imported services

The most significant shortcomings in the South African VAT system with regard to the VAT rate applicable to inter-jurisdictional supplies and imported services which could be addressed by law changes or the introducing specific place of supply rules are captured in Table 5.4 below.

Table 5.4: Place of supply rules to determine the VAT rate and imported services

	Shortcomings	Potential Solutions
Composite supplies	It is unclear whether sections 11(1), 11(2) or both apply to composite supplies. This is important as certain zero rating provisions deal with services supplied “in respect” of or “in connection with” “goods” or “services” “inside” or “outside” South Africa, for example, sections 11(2)(f); (g); (k); (l) and (m). This can be illustrated by a local company that makes composite supplies, i.e. goods and services which form part of a single supply.	<ol style="list-style-type: none"> 1 It should be clarified when a supply is deemed to be “goods” or “services”. 2 Concepts such as “directly in respect of”, “directly in connection with” and “use” or “consumption” should be clarified for purposes of zero rating (Meyburgh, 2011).

Management, consulting, and related services	<p>Section 11(2)(l) does not apply to certain services, even though they are not consumed in South Africa, for example, where a local company provides management and related services to a foreign company. Two senior managers of the foreign company die. As a result, the foreign company becomes effectively managed locally and becomes “resident” for VAT purposes. If the deceased managers are replaced by foreign managers, the foreign company will not be effectively managed in South Africa, and section 11(2)(l) applies again.</p> <p>Services rendered to non-residents, (including a service not capable of physical performance, such as consulting services or management services) supplied to a person who is in South Africa at the time the service is rendered could strictly be consumed outside South Africa when the non-resident returns to the foreign country.</p> <p>Also, if a firm consults to a non-resident via phone, video conference, electronic mail or some other electronic means whilst the non-resident is outside South Africa, the service is zero rated in terms of section 11(2)(l). If the non-resident travels to South Africa for the consultation, SARS is of the view that the zero rate does not apply as the person is present in South Africa at the time of the consultation in terms of section 11(2)(l)(iii).</p>	<p>3 Management services should be deemed to be supplied where the recipient is located (Badenhorst, 2011).</p>
	<p>4 All consulting services should be treated in the same manner for VAT purposes, irrespective of the medium through which they are provided (Badenhorst, 2011).</p>	
Local services provided to foreign business operations of local company with no presence	<p>Certain services supplied by local suppliers cannot be zero rated in terms of section 11(2)(l) although the services are consumed outside South Africa, since the services are supplied to a “resident”. For example, a locally incorporated company</p>	<p>5 These services could be deemed to be supplied where the recipient has established its business operations (Badenhorst, 2011).</p>

<i>in South Africa</i>	with no physical presence locally, that only has foreign operations, with its head office established in a foreign country, engages local suppliers to supply services in respect of its foreign business operations.	
<i>Local services provided to foreign branch of local vendor</i>	Certain services cannot be zero rated in terms of section 11(2)(l) as they are rendered to a “resident”. If the South African vendor supplies the services directly, they can be zero rated in terms of section 11(2)(o). Where a foreign company has a local branch, the services rendered to the foreign company's offshore operations could be zero rated as the services are not rendered to a “resident”.	6 These services could be deemed to be supplied where the recipient has established its business operations (Badenhorst, 2011).
<i>Supplies of foreign land by way of sale or lease</i>	Supplies of foreign land by way of sale or lease are categorised as exempt and the benefits associated with zero-rated supplies are disallowed ²⁵⁵ . This is contrary to the general structure of the VAT Act and inequitable when compared to the VAT treatment of exports of movable goods (de Wet, 2012).	7 The law should be amended to allow supplies of foreign land by way of sale or lease to be subject to the zero rate, if done in the course or furtherance of an “enterprise”.
<i>Services to non-residents outside South Africa</i>	Wording, such as “directly” and “directly in connection with” (as opposed to “directly in respect of”) and the reference to “other person”, used in section 11(2)(l) is ambiguous. The reference to “other person” seems to imply a legal differentiation between the contractual and beneficial recipient of a supply (de Wet, 2012).	8 Consideration should be given to enhancing legislative certainty in respect of the terms “directly” and “directly in connection with” (as opposed to “directly in respect of”) and the reference to “other person” (van Heerden, 2012).

²⁵⁵ SARS general written VAT Ruling 419, withdrawn on 1 August 2009.

Foreign Underwriting Insurance Business	<p>The meaning of the phrases “directly in respect of”²⁵⁶ and “directly in connection with”²⁵⁷ as they, for example, are contained in section 11 and relate to insurance services creates uncertainty (Rudolph, 2012).</p> <p>The meaning of services “physically rendered” (section 11(2)(k) of the VAT Act) creates uncertainty.</p>	<p>9 Clarification of the differences in meaning of the phrases “directly in respect of”²⁵⁸ and “directly in connection with”²⁵⁹ would enhance legislative certainty (Rudolph, 2012).</p>
		<p>10 Clarification of whether the services must be capable of being physically rendered and what is meant by physically rendered would add to legislative certainty.</p>
		<p>11 Consumption of services not capable of being physically rendered should not be determined with reference to a person’s “fixed or permanent place in the Republic” but with reference to the location of the recipient, which can be assumed to be where the services are consumed (Badenhorst, 2011).</p>
Foreign branch or main business	<p>As a branch and its main business are part of the same legal person; either of them, in falling within the definition of “Resident of the Republic” would draw the other one into the definition. As a result, the general zero rate provisions that apply to independent parties, where it relies on “Resident of the Republic”, would not entitle the local vendor to zero rate</p>	<p>12 Non-vendor foreign branches or main businesses could be excluded from the definition of “Resident of the Republic”, to the extent that they do not have an “enterprise or activity” in South Africa.</p>

²⁵⁶ Section 11(2)(g) of the VAT Act.

²⁵⁷ In, for example, sections 11(2)(f) and 11(2)(l) of the VAT Act.

²⁵⁸ Section 11(2)(g) of the VAT Act.

²⁵⁹ In, for example, sections 11(2)(f) and 11(2)(l) of the VAT Act.

	supplies to its foreign “VAT person”.	
Imported Services	One of the main problems in the South African VAT environment with regard to “imported services” is that Government itself does not self-assess and pay over VAT on imported services (van Heerden, 2012). The concepts of “utilized” or “consumed” are not defined terms and, as such, create interpretational difficulty (Rudolph, 2012). A specific example that would need clarification is whether fees charged by foreign financial institutions managing foreign investments for South African persons would attract VAT on imported services (Badenhorst, 2007).	13 SARS should enforce compliance by Government of the imported services legislation, which, if not complied with, should be subject to penalties and interest. Alternatively, National Treasury should seek to revise the policy in this regard.
		14 The terms “utilized” and “consumed” should be clarified in law or by way of Guidelines.
		15 Specific clarification would be required for foreign financial institution fees charged to South African persons in respect of foreign investments.

Table 5.5 below illustrates the researcher’s classification of the potential solutions in respect of foreign business activities contained in Table 5.4 above, by making use of Table 5.2 above.

Table 5.5: Place of supply rules to determine the VAT rate and imported services – suggested solutions evaluated

	Potential Solutions
Composite supplies	1 It should be clarified when a supply is deemed to be “goods” or “services”.
	2 Concepts such as “directly in respect of”, “directly in connection with” and “use” or “consumption” should be clarified for purposes of zero rating.
Management, consulting, and related services	3 Management services should be deemed to be supplied where the recipient is located.

	4	All consulting services should be treated in the same manner for VAT purposes, irrespective of the medium through which they are provided.
Local services provided to foreign business operations of local company with no presence in South Africa	5	These services could be deemed to be supplied where the recipient has established its business operations.
Local services provided to foreign branch of local vendor	6	These services could be deemed to be supplied where the recipient has established its business operations.
Supplies of foreign land by way of sale or lease	7	The law should be amended to allow supplies of foreign land by way of sale or lease to be subject to the zero rate, if done in the course or furtherance of an “enterprise”.
Services to non-residents outside South Africa	8	Consideration should be given to enhancing legislative certainty in respect of the terms “directly” and “directly in connection with” (as opposed to “directly in respect of”) and the reference to “other person”.
Foreign Underwriting Insurance Business	9	Clarification of the differences in meaning of the phrases “directly in respect of” ²⁶⁰ and “directly in connection with” ²⁶¹ would enhance legislative certainty.
	10	Clarification of whether the services must be capable of being physically rendered and what is meant by physically rendered would add to legislative certainty.
	11	Consumption of services not capable of being physically rendered should not be determined with reference to a person’s “fixed or permanent place in the Republic” but with reference to the location of the recipient, which can be assumed to be where the services are consumed.
Foreign branch or main business	12	Non-vendor foreign branches or main businesses could be excluded from the definition of “Resident of the Republic”, to the extent that they do not have an “enterprise or activity” in South Africa.

²⁶⁰ Section 11(2)(g) of the VAT Act.

²⁶¹ In, for example, sections 11(2)(f) and 11(2)(l) of the VAT Act.

Imported Services	13 SARS should enforce compliance by Government of the imported services legislation, which, if not complied with, should be subject to penalties and interest. Alternatively, National Treasury should seek to revise the policy in this regard.
	14 The terms “utilized” and “consumed” should be clarified in law or by way of Guidelines.
	15 Specific clarification would be required for foreign financial institution fees charged to South African persons in respect of foreign investments.

5.4 SUMMARY

This chapter described the current inter-jurisdictional VAT rules in the South African VAT system and determined their shortcomings, in order to ultimately make detailed recommendations in Chapter 7. The chapter describes the various concepts and definitions, especially where they relate to cross-border transactions and a VAT enterprise, in detail. The chapter relies to some extent on responses received from a panel of VAT experts (in South Africa, and to a limited extent outside of South Africa) to a questionnaire devised for purposes of this study, as described in detail in Chapter 3 (the Research Design chapter).

This chapter specifically described the current inter-jurisdictional VAT rules in the South African VAT system and potential shortcomings and addressed the following:

- non-resident VAT registration;
- the inter-jurisdictional VAT rate;
- imported services; and
- place of supply rules.

The analysis and recommendations that emanated from this chapter were presented in tabular format, broadly categorised into two main areas, namely the VAT rules that apply to non-resident businesses and the VAT rate applicable to inter-jurisdictional supplies. These two main categories encompass the four broad themes bulleted immediately above. These findings were then assessed using a colour coding system to conclude on which potential solutions should be taken forward into Chapter 7 of this study.

The following chapter, Chapter 6, assesses the inter-jurisdictional VAT rules used in Australia, Canada, New Zealand, and the European Union. The findings in Chapter 6 will further inform potential shortcomings in the South African VAT system and will, in conjunction with the findings in this chapter, be used in Chapter 7.

CHAPTER 6: INTER-JURISDICTIONAL VAT RULES IN SELECTED JURISDICTIONS

6.1 INTRODUCTION

The objective of this chapter is to assess the inter-jurisdictional VAT rules used in Australia, Canada, New Zealand, and the European Union. The findings of this chapter will, in addition to those in Chapter 5, inform potential shortcomings in the South African VAT system and be used in Chapter 7 to make recommendations regarding inter-jurisdictional VAT rules in a South African context. International tax experience supports the need to assess carefully the institutional features and tax cultures in individual countries (World Bank, 1991:7). The jurisdictions were selected for the present research as they represent worldwide and territorial VAT systems. In addition, New Zealand was also selected as South Africa's VAT system is based on that of New Zealand (Roeleveld and De Wet, 2012:463). These jurisdictions also have prominent economic standings and are strong trade partners of South Africa. The selected jurisdictions all apply a broad based VAT of the credit-invoice type, following the destination principle by freeing exports from VAT through zero rating and subjecting imports of goods (on crossing the border) and certain services (mainly imported services) to VAT. All the jurisdictions have imported services provisions and apply the reverse charge mechanism to some extent (to account for VAT on imported services). These jurisdictions all apply similar definitions of "enterprise" or "taxable activity", "goods", "resident", "services", "supply", and "taxable supply". All the jurisdictions assign either the zero rate or exemption to certain supplies seen as meritorious or difficult to tax. As these concepts and treatment are similar in the selected VAT jurisdictions they will not be considered in detail, except to the extent that certain nuances may apply to the South African VAT regime.

Most VAT jurisdictions recognise the necessity for refined inter-jurisdictional VAT rules. Global harmonisation of inter-jurisdictional rules aims to prevent double or non-taxation (Davis VAT Report, 2015b:65). A number of countries (for example, Australia, Canada, New Zealand, South Africa, and Singapore) have adopted a

model different to that of the European Union, which is often referred to as a worldwide or “New World” VAT system (OECD, 2014b:27). The New World VAT system applies a series of proxies for place of consumption to all categories of services in a stepped approach. A connection with the country is firstly established (for example, where the supplier is established; the service performed; or the service acquired). A number of proxies are then applied to determine the actual place of supply. Under the European Union model (a territorial VAT system) “place of supply” is determined for each category of supply according to its nature and the customer’s (business or consumer) status. The place of supply is also the place of taxation (OECD, 2014b:27).

The chapter proceeds with a consideration of the VAT treatment in the chosen jurisdictions to the extent meaningful in adding to or addressing the shortcomings identified in the South African VAT system in Chapter 5.

6.2 INTER-JURISDICTIONAL VAT RULES IN AUSTRALIA

6.2.1 Introduction

Australia enacted its Goods and Services Tax (GST) in the GST Act entitled “A New Tax System (Goods and Services Tax) Act 1999”, which took effect on 1 July 2000 (OECD, 2014b:28) and replaced a federal wholesale sales tax (WST) and a number of inefficient state and territorial indirect taxes (Millar and McCarthy, 2012:21-22). The GST Act defines its place of supply rules with reference to supplies “connected with Australia”²⁶². A supply is subject to GST if it is connected with Australia. In terms of the “connected to Australia” proxy, supplies of services performed in Australia, provided through an Australian enterprise, or consisting of rights to receive supplies in Australia are potentially taxable in Australia (OECD, 2014b:28). The concept of a supply connected with Australia is relevant to determine whether it is a taxable supply, GST-free or a zero rated export. A taxable supply is a supply connected with Australia and made for consideration by a registered person (or a person required to be registered) in the course or furtherance of an enterprise²⁶³.

²⁶² Section 9-25 of the GST Act.

²⁶³ Section 9-5 of the GST Act.

The GST Act also caters for supplies that are partly connected with Australia. Where supplies comprise of more than one kind that are partly connected with Australia, the actual supply is treated as separate supplies to ensure that the portion of the supply connected with Australia is taxed appropriately (Australia, 2012a:21). If a supply is not connected with Australia or is GST-free, a supplier is not required to pay GST. To the extent that supplies are GST-free or input taxed, they are not taxable supplies. A supply is input taxed if there is no entitlement to an input tax credit for the things that are acquired or imported to make the supply²⁶⁴.

An enterprise is carried on in Australia if the enterprise is carried on through a permanent establishment²⁶⁵ or a place that would be a permanent establishment²⁶⁶ in certain instances²⁶⁷. A “permanent establishment”²⁶⁸ is defined as a place where (or through which) a person carries on a business, including a place where the person carries on a business through an agent; uses or installs substantial equipment or machinery; or engages in a construction project. It is also a place where a person sells goods manufactured, assembled, processed, packed or distributed by another person for, at, or to the first-mentioned person and one of them or another person participates in the management, control or capital of the other, and is the place where the goods are manufactured, assembled, processed, packed or distributed. To establish whether a supply is made through a permanent establishment guidance can be taken from existing case law and commentaries such those on the “OECD Model Tax Convention on Income and on Capital” (Australia, 2012a:18-22). Whether a supply is made through a permanent establishment, can also be indicated by whether the permanent establishment can sign contracts or accept purchase orders for the supply; can make important decisions in respect of the supply; physically makes, manufactures or produces, the supply; provides the service; provides the advice or information; or grants, creates, assigns, transfers or surrenders the right. A supply of a thing not connected with

²⁶⁴ Section 9-30(2) of the GST Act.

²⁶⁵ As defined in subsection 6(1) of the Income Tax Assessment Act, 1936.

²⁶⁶ If paragraph (e), (f) or (g) of that definition did not apply.

²⁶⁷ Section 9-25(6) of the GST Act.

²⁶⁸ Section 6(1) of the Income Tax Assessment Act, 1936.

Australia (as it is not done in Australia), is connected with Australia if the supplier makes the supply through an enterprise that the supplier carries on in Australia²⁶⁹. The supply connected with Australia must have a connection with the Australian permanent establishment. An enterprise is defined broadly to mean an activity, or series of activities done in a particular manner²⁷⁰. If only a part of an actual supply is connected with Australia, the supply is treated as if it were separate supplies²⁷¹. The part of the actual supply that is connected with Australia is treated as if it were a separate supply that is connected with Australia²⁷². The part of the actual supply not connected with Australia is treated as a separate supply that is not connected with Australia²⁷³. If a part of a supply can be reasonably regarded as incidental to another part of a supply, and its value is below the threshold, the incidental supply is treated similar to the other part of the supply²⁷⁴. A part of a supply is regarded as incidental to another part if it is minor relative to the other part. Certain supplies and acquisitions made for a period or on a progressive basis²⁷⁵ are treated as if each progressive or periodic component is a separate supply or acquisition. Taxable supplies made for a period or on a progressive basis and made for consideration to be provided on a progressive or periodic basis, if the progressive or periodic component would not be connected with Australia if it was a separate supply, is treated as a separate supply not connected with Australia (Australia, 2012a:18-22).

6.2.2 VAT Treatment of non-residents

VAT registration of non-residents

Non-resident entities that make supplies that are connected with Australia must register for GST purposes if they meet the registration threshold. A resident is a person who is a resident of Australia for the purposes of the Income Tax

²⁶⁹ Section 9-25(5)(b) of the GST Act.

²⁷⁰ Section 9-20 of the GST Act.

²⁷¹ In terms of section 96-5, and as a result of the application of section 9-25 of the GST Act.

²⁷² In terms of section 96-5(2) of the GST Act.

²⁷³ In terms of section 96-5(3) of the GST Act.

²⁷⁴ Section 96-5(4) of the GST Act.

²⁷⁵ Section 156-15 of the GST Act.

Assessment Act 1936, whereas a non-resident is a person that is not a resident.

Reverse charging

The GST Act contains voluntary²⁷⁶ and compulsory²⁷⁷ reverse charge mechanisms. In terms of the voluntary reverse charge mechanism, GST payable on taxable supplies made by non-residents can, by agreement with the recipients, be “reverse charged” to the recipients²⁷⁸. The GST on a taxable supply is payable by the recipient if the supplier is a non-resident; the supplier does not make the supply through an enterprise which it carries on in Australia; the recipient is registered (or required to be) for GST purposes; and the supplier and recipient agree that the GST on the supply is payable by the recipient, with certain exceptions²⁷⁹. In terms of the compulsory reverse charge mechanism, the supply of a thing (other than goods or real property) that takes place outside Australia and constitutes a taxable supply must be “reverse charged” to the recipient of the supply²⁸⁰. A supply of anything (other than goods or real property) not connected with Australia; or connected with Australia but neither done in Australia nor done through an enterprise of the supplier in Australia, where the thing is a right or option to acquire another thing which would be connected with Australia²⁸¹, is a taxable supply²⁸² (and the tax is payable by the recipient)²⁸³ if the supply is for consideration and the recipient:

- acquires the thing solely or partly for purposes of its enterprise carried on in Australia, but not solely for a creditable purpose; and
- is registered (or required to be)²⁸⁴.

²⁷⁶ Division 83 of the GST Act.

²⁷⁷ Division 84 of the GST Act.

²⁷⁸ Section 83-1 of the GST Act.

²⁷⁹ Section 83-5(1) of the GST Act.

²⁸⁰ Section 84-1 of the GST Act.

²⁸¹ Section 9-25(5)(c) of the GST Act.

²⁸² The supply is not a taxable supply to the extent that it is GST-free or input taxed.

²⁸³ Section 84-10 of the GST Act.

²⁸⁴ Section 84-5 of the GST Act.

*The recipient is required to account for output tax and can claim input tax to the extent that it was incurred for the purposes of making taxable supplies, subject to the apportionment method already in use*²⁸⁵. For purposes of compulsory reverse charging²⁸⁶, if an entity carries on an enterprise in Australia and also carries on that enterprise or another outside Australia, then the transfer or doing of anything by the enterprise outside Australia to the enterprise in Australia, is regarded as a supply that is not connected with Australia. This provision does not apply to a transfer of the services of an employee, to the extent that payments (relating to the transfer made from the enterprise in Australia to the enterprise outside Australia) would be withholding payments if they were made from the enterprise in Australia to the employee²⁸⁷. Withholding payments refer to amounts collected on account of income tax payable by the recipient of the payment, alienated personal services payment, non-cash benefit or capital proceeds.

Branches

Separate branch registration requires that independent branch accounts be kept; the branch is identifiable through its location or activities; and an enterprise is conducted through the branch. GST group entities cannot register separately. Companies within a 90% owned group, and certain other entities can form a GST group and then one member of the group deals with all the GST liabilities and entitlements (except for GST on most taxable importations) of the group, and (in most cases) intra-group transactions are excluded from the GST²⁸⁸. Transfers between separately registered branches are deemed to be supplies and acquisitions (Millar and McCarthy, 2012:40-41). The GST Act, in certain instances, deems a supply to be made between an offshore branch and Australian branch. Inbound intra-entity dealings are subject to GST if the registered entity would not have been entitled to full input tax on the services transferred between the branches. The supply is deemed to be made if a registered (or required to be registered) entity has

²⁸⁵ Sections 84-12 and 84-13 of the GST Act.

²⁸⁶ Section 84-1 of the GST Act.

²⁸⁷ Section 84-15 of the GST Act.

²⁸⁸ Section 48-1 of the GST Act.

permanent establishments in and outside Australia through which it carries on one or more enterprise/s; the offshore establishment transfers to or does something for the Australian establishment; the onshore establishment acquires the “thing” transferred or done for purposes of its Australian enterprise but is not entitled to full input tax; the “thing” transferred or done would not be GST-free or input taxed; and there is consideration. The GST Act does not assume consideration between branches if there is no monetary or non-monetary payment provided for the “services”. It also does not deem the two enterprises to be “connected” and does not apply an arm’s length market value rule. The internal transfer of funds could arguably amount to consideration for the deemed supply. Following the application of the reverse charge, the entity should apply the normal GST rules to determine the extent of claimable input tax (Millar and McCarthy, 2012:40-41).

6.2.3 Place of supply rules

Various place of supply rules apply to different categories of supply.

Place of supply of goods

- Supplies of goods wholly in, from, or to Australia

A supply of goods is connected with Australia if the goods are delivered, or made available, in Australia to the recipient²⁸⁹. Goods are delivered in Australia if the goods are physically delivered in Australia. Goods are made available in Australia if the goods are physically made available in Australia (Australia, 2012a:12). Where the recipient imports the goods into Australia, the supply is not connected with Australia since the goods are not delivered, or made available, to the recipient in Australia. A supply of goods removed from Australia is connected with Australia²⁹⁰. Removal of goods from Australia is a supply from Australia and means that the goods are physically taken out of Australia. A supply of goods brought to Australia is connected with Australia if the supplier imports the goods into or installs or assembles the goods in

²⁸⁹ Section 9-25(1) of the GST Act.

²⁹⁰ Section 9-25(2) of the GST Act.

Australia²⁹¹. The import of the goods into or the installation or assembly thereof in Australia is a supply of goods to Australia. A supply connected with Australia may result in a taxable supply and a taxable importation if the supplier imports the goods into Australia. This does not apply to a supply of goods brought to Australia if the recipient imports the goods. As a result, the supplier is either an exporter from outside and importer into Australia, or an exporter from outside and installer or assembler in Australia. A supply of goods may be partly connected with Australia and partly not. The extent to which a supply of goods is connected with Australia must then be determined (Australia, 2012a:13)²⁹².

- *Supplies of real property*

A supply of real property is connected with Australia if the real property, or the land to which it relates, is in Australia²⁹³. Land for these purposes means the physical land (Australia, 2012a:13). The reference to “land to which the real property relates” means that an interest in, or right over land, is connected with Australia if the physical land is in Australia. A supply of real property is connected with Australia if it involves, for example, the sale of land situated in Australia; the grant, assignment or surrender of any interest in or right over land in Australia; a personal right to call for or be granted any interest or right over land in Australia; a licence to occupy land in Australia; or any other contractual right exercisable over or in relation to land in Australia. A supply of real property consisting of real property in and outside Australia is connected with Australia to the extent that the supply of real property, or land to which it relates, is in Australia. The supply is not connected with Australia to the extent that the supply is not in Australia (Australia, 2012a:14)²⁹⁴.

Table 6.1 below summarises when supplies of goods are “connected with Australia”.

²⁹¹ Section 9-25(3) of the GST Act.

²⁹² By applying sections 9-25(1), 9-25(2) and 9-25(3) of the GST Act to the relevant parts of the supply.

²⁹³ Section 9-25(4) of the GST Act.

²⁹⁴ Section 9-25 of the GST Act.

Table 6.1: Supply of goods “connected with Australia”

Supply of	Supply connected with Australia if:
<i>Goods wholly in Australia</i>	Goods are delivered or made available to the recipient in Australia
<i>Goods from Australia</i>	Goods are removed from Australia
<i>Goods to Australia</i>	Supplier imports, installs, or assembles the goods in Australia
<i>Real property</i>	Real property or land to which the real property relates is in Australia

Source: Own formulation, from the GST Act

Place of Supply of Services

Subjecting services to tax in Australia is determined through the interaction of three sets of rules, namely the “connection with Australia” rules; the GST-free rules for services supplied for consumption outside Australia; and the compulsory reverse charge mechanism (Millar and McCarthy, 2012:57).

- *Supplies of anything else*

A supply of a thing²⁹⁵, other than goods or real property, is connected with Australia if done²⁹⁶ in Australia or made through the supplier’s enterprise in Australia. A supply of a thing, other than goods or real property, is also connected with Australia if not done in Australia and the supplier does not make the supply through its enterprise in Australia, the thing is a right or option to acquire another thing, and the supply of the other thing would be connected with Australia²⁹⁷. The supply of a thing other than goods or real property is partly connected with Australia if done partly in Australia or the supplier makes the supply partly through an enterprise of the supplier in Australia. A supply is connected with Australia to the extent that the thing is done in Australia. The part of the supply not connected with Australia may still be connected with

²⁹⁵ “Thing” refers to anything that can be supplied or imported, such as a service, advice, information or a right, and is the subject of the supply (Australia, 2012a:14).

²⁹⁶ What is meant by “done” depends on the nature of the “thing” supplied. “Done” can mean performed, executed, completed, finished, etc. depending on what is supplied (Australia, 2012a:15).

²⁹⁷ Section 9-25(5) of the GST Act.

Australia if the supply is made through an enterprise that the supplier carries on in Australia²⁹⁸. If one part of a thing done is reasonably regarded as incidental to the doing of another, the incidental part is done where the part to which it is incidental is done. If a supplier makes a supply partly through an enterprise it carries on in Australia, the supply is connected with Australia to the extent made through that enterprise. The part of the supply not connected with Australia may still be connected with Australia if the thing is done in Australia (Australia, 2012a:20-21).

- *Supply of a service*

A supply of a thing²⁹⁹, other than goods or real property, is connected with Australia if done³⁰⁰ in Australia or the supply is made through an enterprise of the supplier in Australia. If the “thing” supplied is a service, the supply is typically done where the service is performed. If the service is performed in Australia, the service is done in Australia and the supply is connected with Australia³⁰¹. A supply of a service to an offshore recipient may be GST-free.

- *Provision of advice or information*

Advice or information provided which involves work to create, develop or produce the information or advice for the recipient, is a supply of services. The advice or information is provided where prepared, produced, or created. The supply of advice or information is connected with Australia if the advice or information is prepared, created or produced in Australia (Australia, 2012a:16).

²⁹⁸ Section 9-25(5)(b) of the GST Act.

²⁹⁹ “Thing” refers to anything that can be supplied or imported, such as a service, advice, information or a right, and is the subject of the supply (Australia, 2012a:14).

³⁰⁰ What is meant by “done” depends on the nature of the “thing” supplied. “Done” can mean performed, executed, completed, finished, etc. depending on what is supplied (AUSTRALIA, 2012A:15).

³⁰¹ Section 9-25(5)(a) of the GST Act.

- *Instantaneous supply of advice or information*
If advice or information provided is instantaneous, the supply is done where the advice or information is provided. The meaning of provided depends on the facts. Depending on the circumstances, the supply may be GST-free (Australia, 2012a:16).

- *Creating, granting, transferring, assigning or surrendering of a right*
The granting, transfer or assignment of a right to another, or the surrender of that right, is done where the right is created, granted, transferred or assigned to that other person, or surrendered. The act that creates that right will depend on the facts of each individual case (Australia, 2012a:17). If the agreement is made outside Australia, the supply is not connected with Australia³⁰². If the supplier makes the supply through an enterprise that it carries on in Australia, even if the agreement is made outside Australia, the supply is connected with Australia³⁰³.

- *Entry into, or release from, an obligation*
A supply of the entry into, or release from, an obligation to do anything, or to refrain from an act, or to tolerate an act or situation, is made where the obligation is entered into or the release is effected (Australia, 2012a:17).

- *Supply of a right or option to acquire another thing and the supply of the other thing would be connected with Australia*
A supply not done in Australia³⁰⁴, of a right or option to acquire another thing if the supplier does not make the supply through an enterprise that it carries on in Australia (supply is not connected with Australia), is connected with Australia³⁰⁵ if the supply of the other thing would be connected with Australia. This may apply to an overseas tour operator who does not carry on an enterprise in Australia, and makes a supply overseas of an Australian holiday package to a

³⁰² Section 9-25(5)(a) of the GST Act.

³⁰³ Section 9-25(5)(b) of the GST Act.

³⁰⁴ Not connected with Australia in terms of section 9-25(5)(a) of the GST Act.

³⁰⁵ In terms of section 9-25(5)(c) of the GST Act.

non-resident tourist that gives the non-resident tourist rights or options to acquire goods, services or other things which would be connected with Australia³⁰⁶. The supply of the rights or options is connected with Australia (Australia, 2012a:19-20). The supply of a right or option to acquire another thing may be partly connected with Australia³⁰⁷. To the extent that the goods, services or other things are not connected with Australia, the supply of the right or option should not be connected with Australia. A supply of the right or option to acquire another thing is partly connected with Australia if the supply of the other thing would be partly connected with Australia. The use or enjoyment rule deems advertising services to be supplied at the location of the entity to which they are provided, whether it is the recipient or a third party. Use or enjoyment of advertising services is not considered to be where broadcast or published (Millar and McCarthy, 2012:70-71).

- *Telecommunication services*

A “telecommunication supply” is a supply³⁰⁸:

...relating to the transmission, emission or reception of signals, writing, images, sounds or information of any kind by wire, radio, optical or other electromagnetic systems. It includes:

- (a) the related transfer or assignment of the right to use capacity for such transmission, emission or reception; and
- (b) provision of access to global information networks.

Telecommunication services are connected with Australia if the recipient uses or enjoys the supply in Australia. A telecommunication supply or telecommunication supply included in a class of telecommunication supplies is not connected with Australia if the supply is made through an enterprise not carried on in Australia; and the collection of GST would not be administratively

³⁰⁶ In terms of section 9-25 of the GST Act.

³⁰⁷ In terms of section 9-25(5)(c) of the GST Act.

³⁰⁸ Section 85-10 of the GST Act.

feasible³⁰⁹. Telecommunication services are connected with Australia if performed in or supplied through a permanent establishment in Australia (Millar and McCarthy, 2012:70). This brings telecommunications supplied outside Australia into the GST net. A ruling can be requested (which has mostly been granted) not to apply the place of use or enjoyment rule to telecommunication services supplied through a permanent establishment outside Australia (Millar and McCarthy, 2012:38).

Table 6.2 below summarises when supplies of anything else are connected with Australia.

Table 6.2: Supply of a thing “connected with Australia”

Supply of	Supply connected with Australia if:
<i>Anything else</i>	Done in Australia or made through the supplier’s enterprise in Australia
<i>A service</i>	Performed in Australia
<i>Provision of advice or information</i>	The advice or information is prepared, created or produced in Australia
<i>Instantaneous advice or information</i>	The advice or information is provided in Australia
<i>Creating, granting, transferring, assigning or surrendering of a right</i>	The right is created, granted, transferred or assigned or surrendered in Australia. The act that creates the right will depend on the facts of each individual case. If the agreement is made outside Australia, the supply is not connected with Australia. If the supply is made through an enterprise carried on in Australia, even if the agreement is made outside Australia, the supply is connected with Australia.
<i>Entry into, or release from, an obligation</i>	The obligation is entered into or the release is effected in Australia
<i>A right or option to acquire another thing and the supply of the other thing would be connected with Australia</i>	The supply of the other thing would be connected with Australia, even if the supply is not done in Australia and the supply is not done through an enterprise carried on in Australia (supply is not connected with Australia)
<i>Telecommunication services</i>	The recipient uses or enjoys the supply in Australia; or performed in or supplied through a permanent establishment in Australia

Source: Own formulation, from the GST Act

- *GST-free supplies of things, other than goods or real property, for consumption outside Australia*

A supply of services is GST-free if the supply is directly connected with goods or real property situated outside Australia, or if the supply is a supply of work physically performed on goods in Australia when the work is done or if the

³⁰⁹ Section 85-5 of the GST Act.

supply is directly connected with real property situated in Australia (Australia, 2012a:15). It may also need to be determined whether the recipient is in Australia in relation to the supply. Although a service may involve work done and the creation of a product for the recipient, this does not alter the nature of the supply as one for the performance of a service (Australia, 2012a:15). A supply of tooling for use in Australia to manufacture goods for export is GST-free even without leaving Australia, as the non-resident customer would have been entitled to register for GST and claim input tax (Millar and McCarthy, 2012:55).

Table 6.3 below summarises GST-free supplies of things, other than goods or real property.

Table 6.3: GST-free supplies of things, other than goods or real property

<i>Item</i>	<i>Supply</i>	<i>GST-free supplies</i>
1	<i>Connected with property outside Australia</i>	A supply directly connected with goods or real property outside Australia
2	<i>To a non-resident outside Australia</i>	A supply made to a non-resident not in Australia when the thing supplied is done, and: <ul style="list-style-type: none"> ▪ the supply is neither work physically performed on goods situated in Australia when the work is done nor a supply <i>directly connected with real property</i>³¹⁰ in Australia; or ▪ the non-resident acquires the thing in carrying on the non-resident's enterprise, but is not registered (nor required to be)
3	<i>Used or enjoyed outside Australia</i>	A supply made to a recipient not in Australia when the thing supplied is done and the effective use or enjoyment takes place outside Australia; other than work physically performed on goods in Australia when the thing supplied is done, or a supply directly connected with real property in Australia
4	<i>Of rights</i>	A supply made in relation to rights if the rights are for use outside Australia; or the supply is to a non-resident entity that is outside Australia when the thing supplied is done
5	<i>Of services to goods destined for outside Australia</i>	A supply of repair, renovation, modification or treatment of goods from outside Australia destined for outside Australia

Source: Australia, 2012a:6

³¹⁰ "Directly connected with" land requires a close link between the supply and the real property, which can include if the supply physically changes or affects the real property; physically interacts with the real property without changing it; establishes the physical attributes or value of the real property; affects or protects the nature or value of the real property; or affects the ownership of the real property (Australia, 2012b:8-9).

Item 1 to 5 supplies in Table 6.3 above are not GST-free if it is a supply of a right or option to acquire something which would be connected with Australia and would not be GST-free³¹¹. Item 2 to 4 supplies in Table 6.3 above are not GST-free if the acquisition of the supply relates (directly or indirectly, or wholly or partly) to the making of a supply of real property situated in Australia that would be input taxed.³¹² Item 2 supplies are not GST-free if the supply is made in terms of an agreement entered into, directly or indirectly, with a non-resident; or the agreement requires it to be made, to another entity in Australia³¹³. Item 3 supplies are deemed to be made to a recipient not in Australia if the supply is made in terms of an agreement entered into, whether directly or indirectly, with an Australian resident; or the agreement requires it to be made to another entity outside Australia³¹⁴.

A supply of a thing for consideration³¹⁵, other than goods or real property, not connected with Australia, or in certain instances supplies connected with Australia³¹⁶, is a taxable supply and subject to GST to the extent that the supply is neither GST-free nor input taxed, if the recipient acquires the thing solely or partly for purposes of its enterprise carried on in Australia, but not solely for creditable purposes³¹⁷ and the recipient is registered, or required to be³¹⁸. If the acquisition of the thing (other than goods or real property) by the recipient relates to making supplies that would be input taxed or the acquisition is partly of a private or domestic nature, the supply is treated³¹⁹ as a taxable supply. The GST on that taxable supply

³¹¹ Section 38-190(2) of the GST Act.

³¹² Section 38-190(2A) of the GST Act.

³¹³ Section 38-190(3) of the GST Act.

³¹⁴ Section 38-190(4) of the GST Act.

³¹⁵ Section 84-5(1)(d) of the GST Act.

³¹⁶ In terms of section 9-25(5)(c) of the GST Act. Section 9-25(5)(c) of the GST Act deems a supply of anything other than goods or real property to be connected with Australia if the thing is not done in Australia and the supplier does not make the supply through an enterprise that the supplier carries on in Australia; and the thing is a right or option to acquire another thing; and the supply of the other thing would be connected with Australia.

³¹⁷ Section 84-5(1)(c) of the GST Act.

³¹⁸ Section 84-5(1)(e) of the GST Act.

³¹⁹ In terms of Division 84 of the GST Act.

is payable by the recipient, or reverse-charged for GST purposes (Australia, 2012a:10).

The section above considered the inter-jurisdictional VAT rules in the GST system of Australia. Concepts such as “connected to Australia” and “things” are central to the place of supply and inter-jurisdictional VAT rules in Australia. Transposing these concepts into the South African VAT Act may not be ideal as they are foreign concepts and would require a substantial rewriting of the South African VAT Act. Australia’s treatment of “imported services or reverse charging”, which is also followed by many other jurisdictions, may be beneficial if adopted in South Africa. In terms of the Australian GST, the recipient is required to account for output tax and can claim input tax to the extent that it was incurred for the purposes of making taxable supplies, subject to the apportionment method in use. Certain definitions used in the Australian GST system may also be useful in the South African context. The inter-jurisdictional VAT rules used in Canada will be considered next.

6.3 INTER-JURISDICTIONAL VAT RULES IN CANADA

6.3.1 Introduction

Canada enacted The Goods and Services Tax (GST) in the Excise Tax Act (ETA) on 1 January 1991. The GST replaced the main Federal Sales Tax (FST). Most provinces levy a provincial sales tax (PST) (Abbas and Cockfield, 2012:110). GST is harmonized with PSTs in a number of provinces, resulting in the Harmonized Sales Tax (HST). The federal government generally administers the HST and shares revenue with each provincial government to reduce PST administration costs. Quebec’s sales tax (QST) is also largely harmonized with the GST (Abbas and Cockfield, 2012:110).

The GST term “commercial activity”³²⁰ includes a business carried on by a person. The term “business”³²¹ includes a profession, calling, trade, manufacture or

³²⁰ Section 123(1) of the ETA.

³²¹ Section 123(1) of the ETA.

undertaking, whether for profit or not, and an activity engaged in on a regular or continuous basis involving the supply of property by way of lease or licence. A “permanent establishment” is a fixed place of business, including a place of management, branch, office, factory or workshop, and a mine, oil or gas well, a quarry, timberland or place of extraction of natural resources, through which the person makes supplies; or a fixed place of business of another person (other than a broker, general commission agent or other independent agent acting in the ordinary course of business) who is acting in Canada on behalf of that person and through whom that person makes supplies in the course of business (Sherman, 1999:62). Place of supply rules apply to cross-border provincial supplies and international supplies in or outside a participating province (Davis VAT Report, 2015:73). Place of supply rules determine if a supply is made in Canada.

6.3.2 VAT Treatment of non-residents

Non-residents must determine whether they have a permanent establishment in Canada. Non-resident businesses with permanent establishments in Canada are treated in a manner similar to resident businesses and are generally required to register for GST. Non-residents without permanent establishments may also be required to register if they carry on businesses in Canada. Generally, a person will be considered to carry on a business in Canada if it has a regular or continuous business activity. Non-residents who are not required to register³²² are permitted to register³²³ voluntarily if the non-resident, in the course of business outside Canada, regularly solicits orders for the supply of tangible personal property for export or delivery to Canada. Non-residents may also register voluntarily if they enter into an agreement to perform services in Canada or supply intangible personal property for use in or that relates to real property in Canada; or tangible personal property ordinarily in Canada. A supply of personal property or a service made in Canada by a non-resident is deemed to be made outside Canada, unless the supply is made in the course of a business carried on in Canada or the person is registered at time of

³²² In terms of sections 240(1)(c) and 240(2) of the ETA.

³²³ In terms of section 240(3) of the ETA.

supply³²⁴. Non-residents who enter Canada to make taxable supplies of admission in respect of a place of amusement (for example sport events, concerts and stage performances), public speaking engagements, seminars, and other activities and events are required to register, irrespective of whether or not carrying on a business in Canada³²⁵. A permanent establishment is treated as a separate person. A permanent establishment of a non-resident in Canada is treated as a resident and a permanent establishment of a resident outside Canada is treated as a non-resident³²⁶. The supply of goods or services by a permanent establishment to another permanent establishment of the same person is deemed to be made between separate persons dealing at arm's length (Abbas and Cockfield, 2012:120).

6.3.3 Place of supply rules

Various place of supply rules apply to different categories of supply.

Place of supply of goods

The place of supply of real property is deemed to be where the real property is located³²⁷. The place of supply of tangible personal property, by way of a sale, is deemed to be where the property is located, or is delivered, or made available to the recipient. The place of supply of tangible personal property, not by way of a sale, is

³²⁴ Section 143(1) of the ETA.

³²⁵ Section 240(2) of the ETA.

³²⁶ Sections 123(1); 132 and 220 of the ETA. In terms of section 132(2) of the ETA where a non-resident has a permanent establishment in Canada, the person is deemed to be resident in respect of its activities carried on through that establishment. In terms of section 132(3) "where a person who is resident...has a permanent establishment in a country other than Canada, the person shall be deemed to be a non-resident person in respect of...activities of the person carried on through that establishment." Section 123(4) of the ETA provides that "where a person carries on a business through a permanent establishment ... in Canada and through another permanent establishment ... outside Canada", (a) the transfer of personal property or rendering of a service by the establishment in Canada to the establishment outside Canada is deemed to be a supply of the property or service; and (b) in respect of that supply, the permanent establishments are deemed to be separate persons who deal at arm's length.

³²⁷ Section 142 of the ETA.

deemed to be where possession or use is given or made available to the recipient (Sherman, 1999: 139).

The place of supply of goods rules are summarised in Table 6.4 below³²⁸.

Table 6.4: Place of supply of goods in Canada

<i>A supply of</i>	<i>Supply is in Canada if:</i>
<i>Sale of tangible personal property</i>	The property is or will be delivered or made available in Canada to the recipient ³²⁹
<i>Supply of tangible personal property not by sale</i>	Possession or use of the property is given or made available in Canada to the recipient ³³⁰
<i>Supply of real property</i>	The real property is in Canada ³³¹

Source: Own formulation, from the ETA.

Place of Supply of Services

The place of supply of services, excluding intangible property and telecommunications, is deemed to be in Canada if the service is performed wholly or partly in Canada³³² (Abbas and Cockfield, 2012:127). The place of supply of intangible personal property is deemed to be in Canada if (i) the property may (or is allowed to) be used in whole or in part in Canada; or (ii) the property relates to real property in Canada; to tangible personal property ordinarily situated in Canada; or to a service to be performed in Canada (Sherman, 1999:139). Although the term “performed” is not defined, the place of performance has traditionally been the geographic location of the individual who is doing the work (Canada, 2002:16). The following factors guide whether a service is performed in or partly in Canada:

- an individual is required to perform a task whilst in Canada; or
- the supplier’s computer equipment located in Canada performs operations (Canada, 2002:30-31).

³²⁸ From section 142(1) and subject to sections 143, 144 and 179 of the ETA.

³²⁹ Section 142(1)(a) of the ETA.

³³⁰ Section 142(1)(b) of the ETA.

³³¹ Section 142(1)(d) of the ETA.

³³² Section 142 of the ETA.

The GST Act arguably includes enhanced cross-border e-commerce trade and other international transactions (Canada, 2002). Entities that buy and sell electronic goods and services need to address three main factors, namely “carrying on business in Canada”; “permanent establishment”; and “taxable supplies”. This multi-factor approach determines whether a non-resident business should be GST registered. For example, a United States based online retailer supplies downloadable audio files to Canadian consumers through a web site hosted on a United States server. Advertisements are directed to Canada and the contract is entered into in Canada. The non-resident will arguably not carry on a business in Canada. Foreign taxpayers are subject to GST if they own or lease servers in Canada and perform integral aspects of the cross-border transaction through the server. For example, a foreign e-commerce company which has a website on a Canadian-based server and takes orders from Canadian consumers, and processes payment for digital goods and transmits them to consumers, is likely to be required to register for GST. A supply of intangible personal property to a non-resident is zero rated if the non-resident is not registered at the time of supply and it is a supply of intellectual property, a right, license or privilege to use such property³³³. A supply of intangible personal property that relates to tangible personal property ordinarily situated in Canada is not zero rated (Canada, 2002).

The GST Act defines a “telecommunication service”³³⁴ as:

- (a) ...emitting, transmitting or receiving signs, signals, writing, images or sounds or intelligence of any nature by wire, cable, radio, optical or other electromagnetic system, or by any similar technical system, or
- (b) making available for such emission, transmission or reception telecommunications facilities of a person who carries on the business of supplying services referred to in paragraph (a).

A “telecommunications facility”³³⁵ is a facility, apparatus or other thing (including wire, cable, radio, optical or other electromagnetic system, or any similar technical

³³³ Section 10 of the ETA.

³³⁴ Section 123(1) of the ETA.

³³⁵ Section 123(1) of the ETA.

system, or part thereof) used or capable of being used for telecommunications.

The Canadian Revenue Authority (CRA) applies the guidelines in Table 6.5 below to distinguish between intangible personal property and electronic services¹⁹⁰:

Table 6.5: Intangible personal property versus electronic services

Supply of Intangible Personal Property	Electronic services
A right in or to use a product for personal or commercial purposes, including: <ul style="list-style-type: none"> ▪ Intellectual property (e.g. copyright); or ▪ Rights of a temporary nature (e.g. a right to view, access or use a product while on-line) 	A supply which does not include the provision of rights (e.g. technical know-how) or if rights are supplied, they are incidental to the supply
A product created, developed, or in existence	The supply involves specific work that is performed by a person for a specific customer
A product created or developed for a customer, where the supplier retains ownership	The supply requires human involvement
A right to make a copy of a digitised product	

Source: Canada, 2012:4.

The place of supply of a telecommunication service is in Canada if payment is for a terminal or station situated in Canada. The place of supply of long distance telephone charges is in Canada if two or more of the following three places are in Canada:

- the place of origin;
- the place of termination; and
- the billing location³³⁶.

The billing location of a telecommunication service supplied is in Canada if the consideration charged or applied to the recipient's account is from a business that supplies telecommunication services and the account relates to a telecommunications facility used (or available for use) by the recipient to obtain telecommunication services, and the telecommunications facility is ordinarily located in Canada. In any other case, the telecommunications facility which initiates the

³³⁶ Section 142 of the ETA.

service is located in Canada³³⁷.

Notwithstanding the above, a supply of a telecommunication service is in Canada if it comprises the making available of telecommunications facilities that are (or part thereof of are) located in Canada. In any other case, the supply is in Canada if the telecommunication is emitted and received in Canada, or the telecommunication is emitted or received in Canada and the billing location is in Canada³³⁸.

The place of supply rules for services in Canada are summarised in Table 6.6 below³³⁹.

Table 6.6: Place of supply of services in Canada

Supply of	Supply is in Canada if:
Intangible personal property	The property: <ul style="list-style-type: none"> may be used in or partly in Canada, or relates to real property in Canada; to tangible personal property ordinarily in Canada; or a service to be performed in Canada³⁴⁰
A service relating to real property	The real property is in Canada ³⁴¹
A prescribed service	The supply complies with the definition of prescribed service ³⁴²
Any other service	The service is or will be performed in or partly in Canada ³⁴³
Electronic services	Supplied through a business carried on in Canada, or through a permanent establishment, and it constitutes a taxable supply
Telecommunication service	<p>Payment is for a terminal or station situated in Canada. The place of supply of long distance telephone charges is in Canada if two or more of the following three places are in Canada:</p> <ul style="list-style-type: none"> The place of origin; The place of termination; and The billing location; or <p>It comprises the making available of telecommunications facilities that are (or part thereof of are) located in Canada.</p> <p>In any other case, the supply is in Canada if the telecommunication is emitted and received in Canada, or the telecommunication is emitted or received in Canada and the billing location is in Canada.</p>

Source: Own formulation, from the ETA.

³³⁷ Section 142 1(1) of the ETA.

³³⁸ Section 142.1(2) of the ETA, notwithstanding section 142 and subject to section 143.

³³⁹ Deduced from section 142(1) and subject to sections 143, 144 and 179 of the ETA.

³⁴⁰ Section 142(1)(c) of the ETA.

³⁴¹ Section 142(1)(d) of the ETA.

³⁴² Section 142(1)(f) of the ETA.

³⁴³ Section 142(1)(g) of the ETA.

The section above considered the inter-jurisdictional VAT rules in the GST system of Canada. Definitions developed in Canada, such as electronic services and telecommunication services, may be of use to South Africa. The inter-jurisdictional VAT rules used in the European Union will be considered next.

6.4 INTER-JURISDICTIONAL VAT RULES IN THE EUROPEAN UNION

6.4.1 Introduction

The “Treaty establishing the European Economic Community” (Treaty of Rome) established the European Economic Community (EEC) which came into effect on 1 January 1958 (EU, 1957)³⁴⁴. The Treaty of Rome also provided for the harmonisation of turnover taxes, excise duties and other forms of Indirect Tax in the European Economic Community (EU, 1957)³⁴⁵. The First Council Directive (Council Directive 67/227/EEC) came into effect on 1 January 1970 and provided for the adoption by all Member States of a common VAT system. The Sixth Directive (Council Directive 77/388/EEC) on the Common VAT system came into effect on 1 January 1978 and replaced the First Council Directive. The Single European Act, 1987 revised the Treaty of Rome to add momentum to European integration and complete the creation of the internal market. The Single European Act came into effect on 1 July 1987. The “Treaty on European Union” (Treaty of Maastricht) came into effect on 1 January 1993 and established the European Union as a Common Market by creating the European Union and replacing the European Economic Community with the European Community. The Common Market did away with the completion of border documentation and the presentation of goods to the customs office for inspection. It also minimised stock financing requirements and introduced a simple control system based on consignment notes (European Union, 1992). The Treaty of Lisbon (which amended the Treaty on European Union) replaced the European Community with the European Union and re-allocated competencies between the European Union and Member States and came into effect on 1 December 2009. Council Directive 2006/112/EC replaced the Sixth Directive

³⁴⁴ Article 1 of the Treaty of Rome (EU, 1957).

³⁴⁵ Article 99 of the Treaty of Rome (EU, 1957).

(Council Directive 77/388/EEC) and repealed the First Council Directive (Council Directive 67/227/EEC). Council Directive 2008/8/EC (the VAT Directive) replaced Council Directive 2006/112/EC and came into effect on 1 January 2007. The VAT Directive provides the legislative framework for the common VAT system and a legal framework to avoid inter-jurisdictional conflict in the European Union and with third countries. Member states are required to incorporate the VAT Directive into their national law, which is often done through place of supply proxies.

The meaning of “permanent establishment” for VAT is not the same as for income tax. As the term is not defined, a Member State can define a permanent establishment for VAT purposes. The Court of Justice of the European Communities defined a permanent establishment as a facility for carrying on a business that has a permanent presence in the form of personnel and technical resources required to supply the services where it is inappropriate to link those services with the supplier’s principal place of business (Kogels, 1999:118-9). The place of supply rules were changed a number of times between 2010 and 2015. The 2010 changes included two general place of supply of services rules, which differentiated between supplies of business-to-business services and business-to-consumer services. Place of supply rules also changed with effect 1 January 2015 with regard to supplies of telecommunications, broadcasting and electronic services. The January 2015 changes did not cover supplies of goods (including distance selling) ordered electronically and supplies other than telecommunications, broadcasting and electronic services.

6.4.2 VAT treatment of non-residents

In terms of the VAT Directive, several operations result in payment of VAT by the person to whom the goods or services are supplied. This primarily applies to intra-community supplies of goods between taxable persons and supplies of services between taxable persons if the services are supplied by a taxable person not established in a Member State (OECD, 2014b:80). The VAT Directive seems not to be prescriptive with regard to reverse charging by Member States, other than certain

disclosure requirements with regard to invoices³⁴⁶.

6.4.3 Place of supply rules³⁴⁷

Various place of supply rules apply to different categories of supply.

*Place of supply of goods*³⁴⁸

- *Goods not dispatched or transported*
The place of supply of goods not dispatched or transported is where the goods are located at the time of supply³⁴⁹.

- *Goods dispatched or transported*
The place of supply of goods dispatched or transported is where the goods are located at the time when dispatch or transport to the customer begins. If dispatch or transport begins in a third territory or country, the place of supply by the importer designated or liable to pay the VAT and the place of subsequent supplies are deemed to be in the Member State of importation³⁵⁰.

- *Goods dispatched or transported, and installed or assembled (by the supplier, the customer or a third person)*
The place of supply of goods dispatched or transported, and installed or assembled (by the supplier, the customer or a third party) is where the goods are installed or assembled. If the installation or assembly is in a Member State other than that of the supplier, that Member State must ensure that there is no double taxation in that Member State³⁵¹.

³⁴⁶ Article 226 of the VAT Directive.

³⁴⁷ Articles 31-39 of the VAT Directive deal with the place of acquisition of goods other than intra-Community acquisitions.

³⁴⁸ Articles 40-42 of the VAT Directive deal with the place of an intra-Community acquisition of goods.

³⁴⁹ Article 31 of the VAT Directive.

³⁵⁰ Article 32 of the VAT Directive.

³⁵¹ Article 36 of VAT Directive.

- *Goods sold on ships, aircraft or trains during passenger transport in the European Union*

The place of supply of goods on board ships, aircraft or trains during passenger transport in the European Union is the place of departure of the passenger transport³⁵².

- *Goods supplied through distribution systems*

The place of supply of goods supplied through distribution systems is where the taxable dealer has established his business or has a fixed establishment for which the goods are supplied, or, in the absence of such a place, his permanent address or usual residence³⁵³. A “taxable dealer” is a taxable person that mainly buys gas or electricity for resale with negligible own consumption. If a supply is not covered above the effective use and enjoyment rules apply³⁵⁴. In the absence of a place of business or fixed establishment, the customer is deemed to have used the goods where he has his permanent address or usual place of residence.

The place of supply rules for goods are summarised in Table 6.7 below³⁵⁵.

³⁵² Article 37 of the VAT Directive. Passenger transport refers to transport without a stopover outside the European Union, between the departure and arrival points.

³⁵³ Article 38 of the VAT Directive.

³⁵⁴ Article 39 of the VAT Directive.

³⁵⁵ From section 142(1) and subject to sections 143, 144 and 179 of the ETA.

Table 6.7: Place of supply of goods in the European Union

A supply	Place of supply where:
<i>Not dispatched or transported</i>	The goods are located at the time of supply
<i>Dispatched or transported</i>	The goods are located when dispatch or transport to the customer begins. If dispatch or transport begins in a third territory or country, the place of supply by the importer designated or liable to pay the VAT and the place of subsequent supplies are deemed to be in the Member State of importation
<i>Dispatched or transported, and installed or assembled (by the supplier)</i>	The goods are installed or assembled. If the installation or assembly is in a Member State other than that of the supplier, that Member State must ensure that there is no double taxation in that Member State
<i>Sold on board ships, aircraft or trains during passenger transport in the European Union</i>	The passenger transport begins
<i>Supplied through distribution systems</i>	The taxable dealer has established his business or has a fixed establishment for which the goods are supplied, or, in the absence of such a place, his permanent address or usual residence. If a supply is not covered above the effective use and enjoyment rules apply. In the absence of a place of business or fixed establishment, the customer is deemed to have used the goods where he has his permanent address or usual place of residence.

Source: Own formulation, from the VAT Directive.

*Place of Supply of Services*³⁵⁶

In 2010 the European Union introduced two new general rules for the place of supply of services. Supplies of business-to-business services became taxable where the customer is established³⁵⁷. Supplies of business-to-consumer services became taxable where the supplier's business is established³⁵⁸. The place of supply of business-to-consumer services by an intermediary that acts in the name and on behalf of another person is where the underlying transaction is supplied³⁵⁹. The

³⁵⁶ Articles 43-59 of the VAT Directive.

³⁵⁷ Article 44 of the VAT Directive. The place of supply to a fixed establishment of the taxable person not where it is established, is where the fixed establishment is located. In the absence of a place of establishment or fixed establishment, the place of supply is where the taxable person has its permanent address or usually resides.

³⁵⁸ Article 45 of the VAT Directive. The place of supply from a fixed establishment of the supplier not where it is established, is where the fixed establishment is located. In the absence of a place of establishment or fixed establishment, the place of supply is where the supplier has his permanent address or usually resides.

³⁵⁹ Article 46 of the VAT Directive.

place of supply of services connected with immovable property³⁶⁰ is deemed to be where the property is located³⁶¹. The place of supply of passenger transportation services is where the transport takes place, proportionate to the distances covered³⁶². The place of supply of business-to-consumer goods transportation services, other than the intra-Community transport of goods³⁶³, is where the transport takes place, proportionate to the distances covered³⁶⁴. The place of supply of business-to-business services of admission to cultural, artistic, sporting, scientific, educational, entertainment or similar events, such as fairs and exhibitions, and related ancillary services, is where the events actually take place³⁶⁵. The place of supply of business-to consumer services and ancillary services, relating to cultural, artistic, sporting, scientific, educational, entertainment or similar activities, such as fairs and exhibitions, including the supply of services of the organisers, is where the activities actually take place³⁶⁶. The place of supply of the business-to-consumer ancillary transport activities³⁶⁷ and valuations of and work on movable tangible property is where the service is physically carried out³⁶⁸. The place of supply of restaurant and catering services (not physically carried out on board ships, aircraft or trains during passenger transport in the European Union) is where the services are physically carried out³⁶⁹. The place of supply³⁷⁰ of restaurant and catering services physically carried out on board ships, aircraft or trains in the European

³⁶⁰ These include services of estate agents and experts, and services to prepare and coordinate construction work, and services of architects and firms providing on-site supervision.

³⁶¹ Article 47 of the VAT Directive. This includes expert and estate agent services, accommodation in the hotel or similar sectors, such as holiday camps or sites developed for use as camping sites, the granting of rights to use immovable property and services for the preparation and coordination of construction work, such as the services of architects and on-site supervision.

³⁶² Article 48 of the VAT Directive.

³⁶³ Articles 50-52 of the VAT Directive.

³⁶⁴ Article 49 of the VAT Directive.

³⁶⁵ Article 53 of the VAT Directive.

³⁶⁶ Article 54 of the VAT Directive.

³⁶⁷ Such as loading, unloading, handling and similar activities.

³⁶⁸ Article 54 of the VAT Directive.

³⁶⁹ Article 55 of the VAT Directive.

³⁷⁰ Article 57 of the VAT Directive.

Union, is at the point of departure of the passenger transport³⁷¹. The place of short-term hiring of a means of transport is where it is put at the disposal of the customer³⁷². The place of business-to-consumer hiring of a means of transport services, other than short-term, is where the customer is located³⁷³. The place of business-to-consumer hiring of a pleasure boat, other than short-term hiring, is where it is put at the disposal of the customer, where the service is actually provided by the supplier from his place of business or a fixed establishment situated in that place. The place of supply³⁷⁴ of business-to-consumer telecommunications³⁷⁵, broadcasting³⁷⁶, and electronic services³⁷⁷ is where the customer is located³⁷⁸. Table 6.8 below illustrates the application of the place of supply rules that apply to supplies of telecommunications, broadcasting, and electronic services.

³⁷¹ Passenger transport refers to transport without a stopover outside the European Union, between the departure and arrival points.

³⁷² Article 56 of the VAT Directive, with effect 1 January 2013. Short-term means the continuous possession or use of the means of transport in a period not exceeding thirty days and, in the case of vessels, not more than ninety days.

³⁷³ Where the customer is established, has his permanent address or usually resides.

³⁷⁴ Article 58 of the VAT Directive, with effect 1 January 2014.

³⁷⁵ Service referred to in the first subparagraph of Article 56(2) of the VAT Directive, with effect 1 January 2013.

³⁷⁶ Services listed in Article 58 of the VAT Directive, with effect 1 January 2015.

³⁷⁷ In particular those referred to in Annex II of the VAT Directive.

³⁷⁸ Where the customer is established, has its permanent address or usually resides.

Table 6.8: Place of supply of telecommunications, broadcasting, and electronic services

Telecommunications, broadcasting, and electronic services supplied by/to	<i>EU consumer in EU country 1</i>	<i>EU consumer in EU country 2</i>	<i>Non-EU consumer²</i>
<i>EU supplier (EU country 1)</i>	Taxed in EU country 1	Taxed in EU country 2 ¹	No EU VAT
<i>Non-EU supplier</i>	Taxed in EU country 1 ¹	Taxed in EU country 2 ¹	No EU VAT

Notes:

¹ Special Schemes available (Articles 358a-369, and 369a-369k of the VAT Directive).

² Unless effective use and enjoyment rules apply (Article 59a of the VAT Directive).

Source: Articles 58, 59a, 358a-369, and 369a-369k of the VAT Directive

The place of supply of the following services to a non-taxable person who is established or has his permanent address or usually resides outside the European Union, is where the customer is located³⁷⁹:

- transfers and assignments of intellectual property rights;
- advertising services;
- consulting, engineering and similar services, data processing and the provision of information;
- obligations to refrain from pursuing or exercising a business activity or a right in terms of this rule;
- banking, financial and insurance, except the hire of safes;
- supply of staff;
- hiring out of movable tangible property, except any means of transport;
- access to, and of transport or transmission through, natural gas and electricity distribution systems and other directly linked services³⁸⁰.

³⁷⁹ Where the customer is established, has its permanent address or usually resides.

³⁸⁰ Article 59 of the VAT Directive.

Member States may, in order to prevent double taxation, non-taxation or competitive distortion, treat the place of supply of business-to-business services³⁸¹; business-to-consumer services³⁸²; hiring of a means of transport³⁸³; telecommunication, broadcasting, and electronic services³⁸⁴; and services to non-taxable persons outside the European Union³⁸⁵, as the place where the customer is located³⁸⁶, if:

- located in the Member State, if effective use and enjoyment takes place outside the European Union, as outside the European Union;
- located outside the European Union, if effective use and enjoyment takes place in the Member State, as in the Member State (from 1 January 2015)³⁸⁷.

Customer location for telecommunications, broadcasting or electronic services³⁸⁸ supplied at a location such as a telephone box, telephone kiosk, Wi-Fi hot spot, an internet café, a restaurant or hotel lobby, where the recipient's physical presence is needed for the service to be provided to him or her, is presumed to be there and also presumed to be used and enjoyed there. If the location is on board a passenger ship, aircraft or train in the European Union, the location is the country of departure³⁸⁹. Customer location for telecommunications, broadcasting or electronic services³⁹⁰ supplied to a non-taxable person is presumed to be:

- if supplied through his or her fixed land line, where the fixed land line is installed;
- if supplied through mobile networks, in the country identified by the mobile country code of the SIM card used to receive the services; and
- if the place is not known, where the viewing card is sent for use, or if a decoder

³⁸¹ Article 44 of the VAT Directive.

³⁸² Article 45 of the VAT Directive.

³⁸³ Article 56 of the VAT Directive.

³⁸⁴ Article 58 of the VAT Directive.

³⁸⁵ If the customer is established or has its permanent address or usually resides outside the European Union.

³⁸⁶ Where the customer is established, has its permanent address or usually resides.

³⁸⁷ Article 59a of the VAT Directive.

³⁸⁸ For the application of Articles 44, 58 and 59a of the VAT Directive.

³⁸⁹ Article 24a of the VAT Implementing Regulation (EU, 2013).

³⁹⁰ For the application of Article 58 of the VAT Directive.

or similar device or a viewing card is needed and a fixed land line is not used, where the decoder or similar device is located.

Customer location for telecommunications, broadcasting or electronic services supplied in any other circumstances³⁹¹ is presumed to be at the place identified by the supplier on the basis of two items of non-contradictory evidence³⁹². A non-taxable legal person is established³⁹³ where its central administration functions are carried out; or at any other establishment with a sufficient degree of permanence and structure in terms of resources to receive and use services supplied³⁹⁴. A supplier can regard a customer established in the European Union as non-taxable if he can demonstrate that the customer has not communicated his VAT identification number to him, unless he has information to the contrary³⁹⁵. The term “*telecommunication services*” is defined as:

...services relating to the transmission, emission or reception of signals, words, images and sounds or information of any nature by wire, radio, optical or other electromagnetic systems, including the related transfer or assignment of the right to use capacity for such transmission, emission or reception, with the inclusion of the provision of access to global information networks³⁹⁶.

Telecommunications services include:

- fixed and mobile telephone services for transmission and switching of voice, data and video, and telephone services with an imaging component (videophone services);
- internet telephone services, including voice over Internet Protocol (VoIP);
- voice mail, call waiting, call forwarding, caller identification, three-way calling and

³⁹¹ Not covered by Articles 24a and 24b of the VAT Implementing Regulation (EU, 2013).

³⁹² As listed in Article 24f of the VAT Implementing Regulation. Article 24b of the VAT Implementing Regulation (EU, 2013).

³⁹³ For purposes of the first subparagraph of Article 56(2) and Articles 58 and 59 of the VAT Directive.

³⁹⁴ Article 13a of the VAT Directive.

³⁹⁵ Article 18(2) of the VAT Directive.

³⁹⁶ Article 24(2) of the VAT Directive.

- other call management services;
- paging services;
- audio text services;
- facsimile, telegraph and telex;
- access to the Internet, including the World Wide Web; and
- private network connections providing telecommunications links for the exclusive use of the client³⁹⁷.

Telecommunications services exclude broadcasting and electronic services. “*Electronic services*”³⁹⁸ include automated services delivered over the Internet or an electronic network that require minimal human intervention, and are impossible to provide without information technology³⁹⁹. Electronic services⁴⁰⁰ specifically include⁴⁰¹:

- websites, web-hosting, distance maintenance of programmes and equipment⁴⁰²;
- software and updating thereof⁴⁰³;

³⁹⁷ Article 6a(1) of the VAT Implementing Regulation (EU, 2013).

³⁹⁸ Article 7 of the VAT Implementing Regulation (EU, 2011).

³⁹⁹ Electronic services specifically include supplies of digitised products, software, and changes or upgrades; services of providing a business or personal presence on an electronic network such as a website or webpage; automated services generated from a computer via the Internet or an electronic network, in response to specific data input by the recipient; transfer for consideration of the right to sell goods or services on an online market type Internet site on which buyers bid through an automated process and the parties are notified of a sale by automatic electronic mail generated from a computer; and Internet Service Packages (ISP) of information if the telecommunications component forms an ancillary and subordinate part (i.e. packages going beyond mere Internet access, which include elements such as content access to news, weather or travel reports; playgrounds; website hosting; access to online debates, etc.) (Article 7 of the VAT Implementing Regulation (EU, 2011)).

⁴⁰⁰ As referred to in Article 58 and Article 56(1)(k) of the VAT Directive.

⁴⁰¹ Annex II (Indicative List) to the VAT Directive.

⁴⁰² Includes automated, online and distance programme maintenance; remote systems administration; online data warehousing, storing and retrieving data electronically; and online supply of on-demand disc space (Annex I of VAT Directive).

⁴⁰³ Includes accessing, downloading, and updating software, including procurement, accounting and anti-virus software; software to block banner adverts showing (“banner blockers”); download drivers,

- images, text and information and making available of databases⁴⁰⁴;
- music, films and games, including games of chance and gambling games, and political, cultural, artistic, sporting, scientific and entertainment broadcasts and events⁴⁰⁵; and
- distance teaching⁴⁰⁶.

Electronic services specifically exclude broadcasting and telecommunications services and services which seemingly (although electronic) are incidental or ancillary to the underlying supply. These exclusions cover electronic ordering and processing of goods, correspondence course teaching, CDs, cassettes, DVDs, CD-ROMs, etc.⁴⁰⁷. If a taxable person acts in his own name and takes part in a supply of

such as software that interfaces computers with peripheral equipment (such as printers); online automated installation of filters on websites; and online automated firewall installations (Annex I of VAT Directive).

⁴⁰⁴ Includes accessing or downloading desktop themes; accessing or downloading photographic or pictorial images or screensavers; digitised content of books and other electronic publications; subscription to online newspapers and journals; weblogs and website statistics; online news, traffic information and weather reports; online information generated automatically by software from specific data input by the customer, such as legal and financial data, (specifically continuous real time updated stock market data); provision of advertising space, including banner ads on a website/web page; and use of search engines and Internet directories (Annex I of VAT Directive).

⁴⁰⁵ Includes accessing or downloading music on computers and mobile phones; accessing or downloading jingles, excerpts, ringtones, or other sounds; accessing or downloading of films; downloading of games on computers and mobile phones; accessing automated online games dependent on the Internet or similar electronic networks, where players are geographically remote from one another; receiving radio or television programmes distributed via a radio or television network, the Internet or similar electronic network for listening or viewing programmes at the moment chosen by the user and at the user's individual request on the basis of a catalogue of programmes selected by the media service provider such as TV or video on demand; receiving radio or television programmes via the Internet or similar electronic network (IP streaming), unless the programmes are broadcast simultaneously over traditional radio and television networks (Annex I of VAT Directive).

⁴⁰⁶ Includes automated distance teaching dependent on the Internet or similar electronic network to function and which requires limited or no human intervention, including virtual classrooms, except where the Internet or similar electronic network is used as a tool for communication between the teacher and student; workbooks completed online and marked in an automated fashion without human intervention (Annex I of VAT Directive).

⁴⁰⁷ Electronic services also exclude goods ordered and processed electronically; CD-ROMs, floppy

services on behalf of another person, he is deemed to have received and supplied the services⁴⁰⁸. A taxable person taking part in a supply of electronic services supplied through a telecommunications network, an interface⁴⁰⁹ or a portal⁴¹⁰ such as a marketplace for applications, is presumed to act in his own name and on behalf of the provider of the services, unless the taxable person explicitly indicates the provider as the supplier⁴¹¹ and their contractual arrangements reflect this. A taxable person may not explicitly indicate another person as the supplier if the taxable person authorises the charge to the customer or the delivery of the services, or sets the general terms and conditions of the supply. This could apply if internet provided telephone services, including voice over Internet Protocol (VoIP), are supplied through a telecommunications network, an interface or a portal such as a marketplace for applications and are supplied under similar conditions⁴¹². Telecommunications networks are networks that can be used to transfer voice and data, including cable networks, telecom networks and ISP (Internet Service Provider) networks, and should cover any facility which allows access to telecommunications, broadcasting or electronic services (EU, 2014). The terms

disks and similar tangible media; printed matter, including books, newsletters, newspapers or journals; CDs and audio cassettes; video cassettes and DVDs; games on CD-ROM; professional consulting services by e-mail; teaching services, where the course content is delivered by a teacher over the Internet or an electronic network; offline physical computer repair services; offline data warehousing; advertising, particularly in newspapers, on posters or television; telephone helpdesk services; correspondence course teaching such as postal courses; conventional auctioneer services reliant on direct human intervention, irrespective of the nature of bidding; tickets to cultural, artistic, sporting, scientific, educational, entertainment or similar events booked online; and accommodation, car-hire, restaurant services, passenger transport or similar services booked online (Article 7 of VAT Implementing Regulation (EU, 2011)).

⁴⁰⁸ Article 28 of the VAT Directive.

⁴⁰⁹ Includes a portal but is a wider concept. In computing it should be understood as a device or a program which allows two independent systems or the system or the end user to communicate.

⁴¹⁰ Any type of electronic shop, website or similar environment that offers electronic services directly to the consumer without diverting them to another supplier's website, portal, etc. to conclude the transaction, including app stores, electronic marketplaces and websites offering e-services for sale.

⁴¹¹ The supplier can regard the provider of the services as the supplier if the invoice of each taxable person taking part in the supply identifies the services and the supplier thereof; and the bill or receipt to the customer identifies the services and the supplier thereof.

⁴¹² Article 9a of the VAT Implementing Regulation (EU, 2013).

“telecommunications networks” and “communication networks” are interchangeable for VAT purposes, but “mobile networks” is a wholly contained subset of telecommunications networks (EU, 2014).

“*Broadcasting services*” include services consisting of audio and audio-visual content, such as radio or television programmes provided to the general public via communications networks by and under the editorial responsibility of a media service provider, for simultaneous listening or viewing, on the basis of a programme schedule. Broadcasting services, in particular, include radio or television programmes transmitted or retransmitted over a radio or television network; or distributed via the Internet or similar electronic network (IP streaming), if broadcasted simultaneously with transmission or retransmission over a radio or television network. Broadcasting services exclude telecommunications or electronic services; provision of information on particular programmes on demand; transfer of broadcasting or transmission rights; leasing of technical equipment or facilities to receive broadcasts; radio or television programmes distributed via the Internet or similar electronic network (IP streaming), unless broadcasted simultaneously with traditional radio or television networks⁴¹³.

Taxable suppliers not established in the European Union that supply electronic services to non-taxable persons belonging in a Member State⁴¹⁴, are permitted to participate in a *special scheme for telecommunications, broadcasting or electronic services* supplied by taxable persons not established within the Community⁴¹⁵. The Member State of identification must allocate a VAT identification number to the supplier and notify him of the number electronically. Member States of consumption may have recourse to their own identification systems based on the information used for identification⁴¹⁶. The VAT return must indicate the identification number and, for each Member State of consumption, where VAT is due, the value (exclusive

⁴¹³ Article 6b of VAT Implementing Regulation (EU, 2013).

⁴¹⁴ If the customer is established or has his permanent address or usually resides in the European Union.

⁴¹⁵ Articles 358a-369 of the VAT Directive.

⁴¹⁶ Article 362 of the VAT Directive.

of VAT) of the services supplied during the tax period, the total VAT amount, and the VAT rate⁴¹⁷. Suppliers that use this scheme are not entitled to deduct VAT⁴¹⁸. The taxable person will be refunded in terms of Directive 86/560/EEC, but for certain exceptions. Taxable suppliers established in the European Union but not in the Member State of consumption that supply electronic services to non-taxable persons belonging in a Member State⁴¹⁹, are permitted to participate in a special scheme for telecommunications, broadcasting or electronic services supplied by taxable persons established within the Community but not in the Member State of consumption⁴²⁰. Similar provisions that apply to the special scheme for telecommunications, broadcasting or electronic services supplied by taxable persons not established within the Community, apply to this special Scheme as well. If the taxable person also carries out other activities in the Member State of consumption in respect of which he is obliged to be registered for VAT purposes, he must deduct VAT in respect of his taxable activities which are covered by this scheme in his VAT return⁴²¹. The place of supply of services rules are summarised in Table 6.9 below.

⁴¹⁷ Article 365 of the VAT Directive.

⁴¹⁸ Article 368 of the VAT Directive. VAT deductions are generally made in terms of Article 168 of the VAT Directive.

⁴¹⁹ If the customer is established or has his permanent address or usually resides in the European Union.

⁴²⁰ Articles 369a-369k of the VAT Directive.

⁴²¹ Article 369j of the VAT Directive.

Table 6.9: Place of supply of services in the European Union

A supply of		Place of supply where:
Business-to-business services	<i>general Rule</i>	Customer is established
	<i>admission to cultural, artistic, sporting, scientific, educational, entertainment or similar events, such as fairs and exhibitions, and related ancillary services</i>	Events actually take place
Business-to-consumer services	<i>general Rule</i>	Supplier is established
	<i>by an intermediary that acts in the name and on behalf of another person</i>	Underlying transaction is supplied
	<i>goods transportation services, other than the intra-Community transport of goods</i>	Transport takes place, proportionate to the distances covered
	<i>services and ancillary services relating to cultural, artistic, sporting, scientific, educational, entertainment or similar activities, such as fairs and exhibitions, including the supply of services of the organisers</i>	Activities actually take place
	<i>ancillary transport activities and valuations of and work on movable tangible property</i>	Service is physically carried out
	<i>hiring of a means of transport services, other than short-term</i>	Customer is located
	<i>hiring of a pleasure boat, other than short-term hiring</i>	Put at the disposal of the customer, where the service is actually provided by the supplier from his place of business or a fixed establishment situated in that place
	<i>telecommunications</i>	Customer is located
	<i>broadcasting</i>	Customer is located
	<i>electronic services</i>	Customer is located
Services connected with immovable property		Property is located
Passenger transportation services		Transport takes place, proportionate to the distances covered
Restaurant and catering services	<i>not physically carried out on board ships, aircraft or trains during passenger transport in the European Union</i>	Services are physically carried out
	<i>physically carried out on board ships, aircraft or trains in the European Union</i>	Passenger transport begins
Short-term hiring of a means of transport		Put at the disposal of the customer

Source: Own formulation, from the VAT Directive.

The section above considered the inter-jurisdictional VAT rules in the European Union. The European Union’s distinction between business-to-business and business-to-consumer transactions can be considered further for incorporation into the South African VAT system. The European Union’s distinction between telecommunication services, electronic services and broadcasting services is thorough and could be considered for implementation in the South African context. The inter-jurisdictional VAT rules used in New Zealand will be considered next.

6.5 INTER-JURISDICTIONAL VAT RULES IN NEW ZEALAND

6.5.1 Introduction

New Zealand enacted The New Zealand Goods and Services Tax (GST) Act 1985 (the GST Act), with effect from 1 October 1986, which replaced a wholesale sales tax. The standard GST rate was increased to 15% on 1 October 2010 (Deloitte, 1998:77). Supplies by non-residents are governed by special rules and although supplies by non-residents made outside New Zealand are generally not subject to VAT, certain exceptions exist⁴²². The GST begins with a worldwide tax base with respect to New Zealand residents but does not impose GST on a worldwide base with respect to non-residents (Schenk, 2009:7). The general place of supply rule for supplies made by non-residents deems the supplies to be outside New Zealand, except where the service is physically performed in New Zealand and the recipient is a final consumer or registered business that has agreed that the transaction can be treated as being made in New Zealand⁴²³ (OECD, 2014b:27). The place of a supply made by a resident is presumed to be in New Zealand, unless the supply is a zero-rated export of services. The inclusion of a supply by a resident requires extensive zero-rating of services, which includes most situations where consumption is likely to be outside New Zealand (OECD, 2014b:27). The New Zealand GST combines proxies such as:

- location of the provider;
 - location of the customer;
-

⁴²² A supply by a non-resident is generally made in New Zealand if the goods are in New Zealand at the time of the sale, or if the services are rendered in New Zealand (Schenk, 2009:7). Where the sale is to a registered person for use in a taxable activity, the sale is made outside New Zealand, unless the supplier and the recipient agree to the contrary (section 8(8) of the GST Act). Most countries that apply a modified destination principle do not tax the import of all services. Consumers and businesses that cannot recover GST on services purchased domestically may import services from non-resident suppliers free of GST. New Zealand amended its GST to counter the competitive disadvantage to local businesses. Some services supplied by non-residents are treated as supplies in New Zealand (a place of supply rule).

⁴²³ Section 8(2) of the GST Act.

- relationship with the tangible world (goods or land); and
- intended use of the supply and physical performance (OECD, 2012:37).

The GST Act was changed with effect 1 April 2014 to allow non-residents to claim back tax in certain instances (New Zealand, 2014). To claim tax back, a non-resident must qualify as a non-resident GST business claimant, which requires that the non-resident should expect a GST refund claim in its first GST taxable period of more than \$500; and in its country or territory of residence:

- be registered for a consumption tax; or
- have a consumption tax which it is not required to register for and should be carrying on a taxable activity with a turnover exceeding NZ\$60,000 in a 12-month period, or
- should not have a consumption tax, and should be carrying on a taxable activity with a turnover exceeding NZ\$60,000 in a 12-month period, and

the non-resident should not:

- carry on or intend to carry on a taxable activity in New Zealand, and should not be a member or intend to become a member of a GST group carrying out a taxable activity in New Zealand; or
- have a taxable activity that includes providing services, where it can be reasonably foreseen that the service will be received in New Zealand by a non-registered person (New Zealand, 2014).

Non-residents that perform services in New Zealand under a contract constitute non-resident contractors. Non-resident contractors are not entitled to register as non-resident GST business claimants (New Zealand, 2014). The New Zealand GST does not distinguish between “telecommunications services” and services supplied via the Internet. The term “telecommunications services” is defined⁴²⁴ to mean:

the transmission, emission or reception, and the transfer or assignment of the right to use capacity for the transmission, emission or reception, of signals,

⁴²⁴ Section 2 of the GST Act.

writing, images, sounds or information of any kind by wire, cable, radio, optical or other electromagnetic system, or by a similar technical system, and includes access to global information networks but does not include the content of the telecommunication.

Examples of “telecommunications services” include telephone calls, accessing the internet via an internet service provider, video conferences, or facilities such as a leased lines agreement, website hosting or server hosting (New Zealand 2006:13). Examples of telecommunications content (excluded from the definition of “telecommunication services”) include information obtained via a 0800 toll free number and images downloaded from an internet server. A “telecommunications supplier” is defined⁴²⁵ to mean “a person whose principal activity is the supply of telecommunications services”. The term “content of the telecommunication” is defined⁴²⁶ to mean:

...the signals, writing, images, sounds or information of any kind that are transmitted, emitted or received by telecommunications service.

The term “resident” is defined to mean resident for Income Tax purposes⁴²⁷, subject to the following provisos:

- A person is deemed to be resident to the extent that it carries on a taxable or other activity in New Zealand and has a fixed or permanent place in New Zealand relating to that taxable or other activity.
- An unincorporated body is deemed to be resident if its centre of administrative management is in New Zealand⁴²⁸.

A company is “resident” in New Zealand for Income Tax purposes if:

- it is incorporated in New Zealand; or
- its head office is located in New Zealand; or

⁴²⁵ Section 2 of the GST Act.

⁴²⁶ Section 2 of the GST Act.

⁴²⁷ In terms of sections YD 1 and YD 2, excluding section YD 2(2) of the Income Tax Act, 2007.

⁴²⁸ Section 1 of the GST Act.

- its centre of management is in New Zealand; or
- control of the company by the directors, acting in that capacity, is exercised in New Zealand, whether or not decision-making is confined to New Zealand (Schenk, 2009:8).

An unincorporated body is resident in New Zealand if it has its centre of administrative management in New Zealand. For Income Tax purposes, an individual is deemed to be resident of New Zealand if:

- the person has a permanent place of abode in New Zealand; or
- if the person is personally present in New Zealand for one or more periods exceeding 183 days in aggregate in any 12-month period (Schenk, 2009:8).

A resident individual who is absent from New Zealand for one or more periods exceeding 325 days in aggregate in any 12-month period is deemed not be resident of New Zealand (Schenk, 2009:8). A supply of services is deemed to be in New Zealand⁴²⁹ if the services are supplied by a non-resident to a resident and the supply would have been a taxable supply if made in New Zealand by a registered person in the course or furtherance of a taxable activity carried on by the registered person, and the recipient:

- estimates at the time of acquisition that the intended use is less than 95%; or
- determines at the end of an adjustment period that the actual use is less than 95%.

The concept “percentage intended use”⁴³⁰ is defined for a registered person to mean the extent to which the goods or services are intended to be used to make taxable supplies, estimated at the time of acquisition and expressed as a percentage of total use⁴³¹. The concept “percentage actual use”⁴³² is defined for a registered person and an adjustment period to mean the extent to which the goods or services are actually used to make taxable supplies and is calculated for the period that starts

⁴²⁹ In terms of section 8(4B) of the GST Act, despite section 8(2).

⁴³⁰ Section 21G(1)(b) of the GST Act.

⁴³¹ Section 21G(1)(b) of the GST Act.

⁴³² Section 21G(1)(a) of the GST Act.

when the goods or services are acquired and finishes at the end of the adjustment period, and is expressed as a percentage of total use⁴³³. An allocation of costs by a non-resident to a resident is deemed to be a supply of services⁴³⁴ and the amount provided to the non-resident by the resident under the allocation is deemed to be the consideration for the supply⁴³⁵.

6.5.2 VAT Treatment of Non-Residents

Reverse charging

The GST Act uses the term “imported services” instead of “reverse charging” commonly used in many other jurisdictions. In terms of the GST Act, output tax is payable on a supply of imported services⁴³⁶. A supply of services that is not treated as made in New Zealand in certain instances⁴³⁷ is deemed to be made in New Zealand if supplied by a non-resident to a resident; and the supply would be a taxable supply if made in New Zealand by a registered person in the course or furtherance of a taxable activity carried on by the registered person⁴³⁸; and the recipient:

- estimates at acquisition that the intended use is less than 95%; or

⁴³³ Section 21G(1)(a) of the GST Act.

⁴³⁴ If it satisfies sections 8(4B)(a) and 8(4B)(c) of the GST Act.

⁴³⁵ Section 8(4C) of the GST Act.

⁴³⁶ Charged in terms of section 5B of the GST Act, where the supply of services is treated by section 8(4B) of the GST Act as being made in New Zealand, having been made by the recipient of the supply in the course or furtherance of a taxable activity carried on by the recipient.

⁴³⁷ In terms of sections 8(3)(b) and 8(4). In terms of section 8(3)(b) of the GST Act services are deemed to be supplied in New Zealand if the supplier is a non-resident and the services are physically performed in New Zealand by a person who is in New Zealand when the services are performed. In terms of section 8(4) of the GST Act if a non-resident supplier supplies services to a registered person for the purposes of carrying on the registered person’s taxable activity, the services are deemed to be supplied outside New Zealand unless the supplier and the recipient of the supply agree the contrary. This is an administrative concession to allow the non-resident supplier not to register for New Zealand GST where no net GST would be collected on the supply.

⁴³⁸ Section 8(4B) of the GST Act.

- determines at the end of an adjustment period that the actual use is less than 95%.

For purposes of “imported services”⁴³⁹, where a person carries on activities inside and outside New Zealand through branches:

- Each branch is treated as a separate person.
- A branch inside New Zealand is deemed to be a resident.
- A branch outside New Zealand is deemed to be a non-resident.
- An activity carried on by a branch is deemed to be carried on separately by the branch⁴⁴⁰.

Branches

A resident registered person does not report supplies which relate to the foreign activities of its foreign branches as taxable supplies (Schenk, 2009:9). The New Zealand GST base is, in general terms, determined with reference to residency. For GST purposes a branch of a New Zealand company (branch of a New Zealand resident) operating outside New Zealand is a non-resident. Generally only New Zealand activities of non-residents are subject to GST whereas supplies by a branch outside New Zealand are generally outside the scope (Schenk, 2009:9). A head office of a company is deemed to be a branch or division of the company.

6.5.3 Place of supply rules

Various place of supply rules apply to different categories of supply.

Place of supply of goods

A supply of goods is deemed to be made in New Zealand if the supplier is resident in New Zealand and is deemed to be supplied outside New Zealand if the supplier is a non-resident, irrespective of the physical place of the supply⁴⁴¹. Goods are

⁴³⁹ As envisaged by section 8(4B) of the GST Act.

⁴⁴⁰ Section 56B of the GST Act.

⁴⁴¹ Section 8(2) of the GST Act.

deemed to be supplied in New Zealand if the supplier is a non-resident and the goods are in New Zealand at the time of the supply⁴⁴². Where a non-resident supplies goods to a registered person for the purposes of carrying on the registered person's taxable activity, the goods are deemed to be supplied outside New Zealand, unless the supplier and the recipient agree the contrary⁴⁴³. Table 6.10 below contains the place of supply rules for goods in New Zealand.

Table 6.10: Place of supply of goods in New Zealand

Goods supplied	Place of supply
By a resident	New Zealand ⁴⁴⁴
By a non-resident	Outside New Zealand ⁴⁴⁵
IF the goods are:	New Zealand – the default position ⁴⁴⁶
▪ <i>In New Zealand at the time of supply</i>	Outside New Zealand, IF supplied to a registered person for use in its taxable activity ⁴⁴⁷
	New Zealand, IF the supplier and recipient elect ⁴⁴⁸
▪ <i>Outside New Zealand at the time of supply</i>	Outside New Zealand ⁴⁴⁹

Source: Own formulation, from section 8 of the GST Act

Place of Supply of Services

A supply of services is deemed to be supplied in New Zealand if the supplier is resident in New Zealand, and is deemed to be supplied outside New Zealand if the supplier is a non-resident⁴⁵⁰. To the extent to which a supply of services consists of the facilitation of inbound tour operations it is subject to tax⁴⁵¹, without the option to zero rate⁴⁵². Tourism products and services include accommodation, meals, transport, and other activities. Services are deemed to be supplied in New Zealand if

⁴⁴² Section 8(3)(a) of the GST Act, despite section 8(2).

⁴⁴³ Section 8(4) of the GST Act.

⁴⁴⁴ Section 8(2) of the GST Act.

⁴⁴⁵ Section 8(2) of the GST Act.

⁴⁴⁶ Section 8(3)(a) of the GST Act.

⁴⁴⁷ Section 8(4) of the GST Act.

⁴⁴⁸ For section 8(4) of the GST Act not to apply.

⁴⁴⁹ Section 8(3)(a) of the GST Act.

⁴⁵⁰ Section 8(2) of the GST Act.

⁴⁵¹ In terms of section 8(1) and section 8(2B) of the GST Act.

⁴⁵² In terms of section 11A.

the supplier is a non-resident and the services are physically performed in New Zealand by a person who is in New Zealand at the time the services are performed⁴⁵³. If a non-resident supplier physically performs services for a registered person for the purposes of carrying on the registered person's taxable activity, the services are deemed to be supplied outside New Zealand, unless the supplier and the recipient agree to the contrary⁴⁵⁴. Table 6.11 below contains place of supply rules for services in New Zealand, excluding telecommunication services and certain deeming provisions.

Table 6.11: Place of supply of services (excluding telecommunication services) in New Zealand⁴⁵⁵

Services supplied	Place of supply
By a resident	New Zealand ⁴⁵⁶
By a non-resident	Outside New Zealand ⁴⁵⁷
<ul style="list-style-type: none"> ▪ <i>Physically performed in New Zealand</i> 	New Zealand – the default position ⁴⁵⁸
	Outside New Zealand ⁴⁵⁹ , IF supplied to a registered person for use in its taxable activity
	New Zealand ⁴⁶⁰ , IF the supplier and recipient elect that the supply is not outside New Zealand
<ul style="list-style-type: none"> ▪ <i>Physically performed outside New Zealand</i> 	Outside New Zealand ⁴⁶¹
<ul style="list-style-type: none"> ▪ <i>Deemed outside New Zealand⁴⁶²</i> 	New Zealand ⁴⁶³ , IF: <ul style="list-style-type: none"> ▪ Supplied to a resident; and ▪ The recipient estimates at time of acquisition the intended use to be less than 95% or determines at the end of an adjustment period that the actual use is less than 95%; and ▪ The supply would be a taxable supply if made in New Zealand by a registered person in the course or furtherance of a taxable activity carried on by that person.

Source: Own formulation, from section 8 of the GST Act.

⁴⁵³ Section 8(3)(b) of the GST Act, despite section 8(2).

⁴⁵⁴ Section 8(4) of the GST Act.

⁴⁵⁵ Table 6.11 above excludes the deeming provision contained in section 8(4C) of the GST Act which is discussed immediately above.

⁴⁵⁶ Section 8(2) of the GST Act.

⁴⁵⁷ Section 8(2) of the GST Act.

⁴⁵⁸ Section 8(3)(b) of the GST Act.

⁴⁵⁹ Section 8(4) of the GST Act.

⁴⁶⁰ Section 8(4) of the GST Act.

⁴⁶¹ Section 8(3)(b) of the GST Act.

⁴⁶² In terms of sections 8(3)(b) or 8(4) of the GST Act.

⁴⁶³ Section 8(4B) of the GST Act.

The GST Act does not distinguish between “telecommunication services” and services supplied via the Internet⁴⁶⁴. Telecommunications services supplied by a non-resident are deemed to be supplied in New Zealand⁴⁶⁵ if a person, physically in New Zealand, initiates the supply from a telecommunications supplier, whether or not the person initiates the supply on behalf of another person⁴⁶⁶. Telecommunications services supplied by a non-resident to a registered person for the purposes of carrying on the registered person’s taxable activity are deemed⁴⁶⁷ to be supplied outside New Zealand, unless the supplier and the recipient agree that this will not apply. The person who initiates a supply of telecommunications services is deemed⁴⁶⁸ to be the person identified by the supplier who:

- controls the commencement of the supply;
- pays for the services; or
- contracts for the supply⁴⁶⁹.

Where a telecommunications supplier cannot apply⁴⁷⁰ the above as it is impractical for the supplier to determine the physical location of a person due to the type of service or the class of customer to which the person belongs, the supplier must treat a supply of telecommunications services as supplied in New Zealand if the person’s address for receiving invoices from the supplier is in New Zealand⁴⁷¹. For this provision to apply the telecommunications supplier must⁴⁷² satisfy this provision⁴⁷³ for all supplies of telecommunications services made for the type of service or the

⁴⁶⁴ In terms of section 8(5), sections 8(3), 8(4) and 8(4B) of the GST Act do not apply to supplies of telecommunications services.

⁴⁶⁵ By section 8(6) of the GST Act, despite section 8(2).

⁴⁶⁶ In terms of section 8(7) of the GST Act, section 8(6) does not apply to supplies made between telecommunications suppliers.

⁴⁶⁷ By section 8(8) of the GST Act, despite section 8(6) and section 8A.

⁴⁶⁸ By section 8(9) for purposes of sections 8(6) and 11AB of the GST Act.

⁴⁶⁹ If more than one person satisfies the criteria: the person who appears highest on the list.

⁴⁷⁰ Section 8(6) of the GST Act.

⁴⁷¹ Section 8A (1), despite section 8(2) of the GST Act.

⁴⁷² In terms of section 8A(3) of the GST Act.

⁴⁷³ Section 8A(1) of the GST Act.

class of customer. This provision⁴⁷⁴ does not apply to supplies made between telecommunications suppliers⁴⁷⁵. Address means the physical residential or business address of a person to which invoices are sent, and excludes a post office box number⁴⁷⁶. As “content of the telecommunication” is excluded from the definition of “telecommunications services” the special place of supply rule does not apply to “content” but the general place of supply rules apply (Davis VAT Report, 2015:81). A supply of services that is chargeable with tax⁴⁷⁷ is subject to the zero rate⁴⁷⁸, where the telecommunications services are supplied:

- by a resident telecommunications supplier to an overseas telecommunications supplier; or
- to a person, other than an overseas telecommunications supplier, and the telecommunications service was initiated outside New Zealand⁴⁷⁹.

Table 6.12 below summarises the place of supply rules for telecommunication services in New Zealand.

⁴⁷⁴ Section 8A(1) of the GST Act.

⁴⁷⁵ In terms 8A(2) of the GST Act.

⁴⁷⁶ In terms of section 8A(4) of the GST Act.

⁴⁷⁷ In terms of section 8 of the GST Act.

⁴⁷⁸ Section 11AB of the GST Act.

⁴⁷⁹ In terms section 8(9) of the GST Act.

Table 6.12: Place of supply of telecommunication services in New Zealand

Telecommunications services supplied	Place of supply
By a resident	New Zealand ⁴⁸⁰
By a non-resident	Outside New Zealand ⁴⁸¹
<ul style="list-style-type: none"> ▪ <i>If a person, physically in New Zealand, initiates the supply from a telecommunications supplier, whether or on behalf of another person</i> 	New Zealand ⁴⁸² , <i>Except</i> for supplies between telecommunications suppliers.
<ul style="list-style-type: none"> ▪ <i>If impractical to determine the physical location of person due to type of service or class of customer</i> 	New Zealand ⁴⁸³ , <i>IF</i> the person's address for receiving invoices from the supplier is in New Zealand, <i>Except</i> for supplies between telecommunications suppliers ⁴⁸⁴
<ul style="list-style-type: none"> ▪ <i>To a registered person for purposes of carrying on its taxable activity</i> 	Outside New Zealand, subject to exception ⁴⁸⁵

Source: Own formulation, from GST Act

The section above considered the inter-jurisdictional VAT rules in New Zealand. New Zealand's use of the terms "resident" and "non-resident" to define the scope of the VAT net can be of much value to South Africa as a general place of supply rule, especially considering that the South African VAT system emanated from the New Zealand GST. The chapter is summarised in the section that follows.

6.6 SUMMARY

This chapter analysed the inter-jurisdictional VAT rules used in Australia, Canada, New Zealand, and the European Union, with a view to inform potential shortcomings in the South African VAT system to be discussed in Chapter 7.

Permanent establishments

The selected jurisdictions treat *foreign businesses with permanent establishments in their countries as resident businesses*. Foreign businesses without permanent

⁴⁸⁰ Section 8(2) of the GST Act.

⁴⁸¹ Section 8(2) of the GST Act.

⁴⁸² Section 8(6) and 8(7) of the GST Act.

⁴⁸³ Section 8A(1), despite sections 8(2), 8A(2), and 8A(3) of the GST Act.

⁴⁸⁴ Where section 8A(1) applies it must be satisfied for all telecommunications services supplies made for the type of service or the class of customer.

⁴⁸⁵ Unless the supplier and the recipient agree that section 8(8) will not apply, despite sections 8(6) and 8A of the GST Act.

establishments may, in certain instances, also be required to register if they carry on businesses in the country. Foreign taxable persons supplying goods or services in a country are generally required to register for VAT purposes, except where the reverse charge mechanism applies. A permanent establishment is generally a fixed place of business, although not all the countries selected for the purpose of this research use the term. Permanent establishment also includes a fixed place of business of agents acting on behalf of that person through whom that person makes supplies. A permanent establishment generally excludes a non-commercial entity, such as a representative office, and VAT registration is not allowed. Certain countries apply a regularity test in respect of persons not established in their country, which takes into account the totality or duration of the activities carried on in the country. The term business generally includes any trade, profession or vocation and any continuing activity that involves making supplies of goods or services, even if made irregularly or on a non-profit basis. Foreign enterprises may recover VAT incurred in some of the selected countries and in many European Union Member States, provided they do not have a permanent establishment in that country and the tax paid would have been deductible by the resident entrepreneur in that country.

Definitions used in other jurisdictions

The selected jurisdictions *define a number of terms that can be of assistance for South Africa, namely permanent establishment; resident and non-resident; telecommunication services; telecommunications supplier; content of the telecommunication; telecommunications facility; telecommunications networks; electronic services; and broadcasting services.* These definitions are reflected in Table 6.13 below.

Table 6.13: Definitions that could be applied in the South African VAT Act

Term	Meaning
Permanent establishment	<p>A place where (or through which) a person carries on a business, including a place where the person carries on a business through an agent; uses or installs substantial equipment or machinery; engages in a construction project; and sells goods manufactured, assembled, processed, packed or distributed by another person for, at, or to the first-mentioned person and one of them or another person participates in the management, control or capital of the other, is the place where the goods are manufactured, assembled, processed, packed or distributed (Australia)</p> <p>A fixed place of business, including a place of management, branch, office, factory or workshop, and a mine, oil or gas well, a quarry, timberland or place of extraction of natural resources, through which the person makes supplies; or a fixed place of business of another person (other than a broker, general commission agent or other independent agent acting in the ordinary course of business) who is acting in Canada on behalf of that person and through whom that person makes supplies in the course of business (Canada)</p> <p>Permanent establishment for VAT is not the same as for income tax. A permanent establishment is a facility for carrying on a business that has a permanent presence in the form of personnel and technical resources required to supply the services where it is inappropriate to link those services with the supplier's principle place of business (European Union)</p>
Resident	<p>A person who is a resident for Income Tax purposes (Australia)</p> <p>A permanent establishment of a non-resident in country is treated as a resident and a permanent establishment of a resident outside country is treated as a non-resident (Canada)</p> <p>The term "resident" is defined to mean resident for Income Tax purposes, provided that a person is deemed to be resident to the extent that it carries on a taxable or other activity in and has a fixed or permanent place in country relating to that taxable or other activity; and an unincorporated body is deemed to be resident if its centre of administrative management is in country. A company is "resident" for Income Tax purposes if it is incorporated in the country; its head office is located in the country; its centre of management is in the country; or control of the company by the directors, acting in that capacity, is exercised in the country, whether or not decision-making is confined to the country (New Zealand)</p>
Non-resident	<p>A person that is not a Resident (Australia)</p>
Telecommunication services	<p>A supply relating to the transmission, emission or reception of signals, writing, images, sounds or information of any kind by wire, radio, optical or other electromagnetic systems. It includes the related transfer or assignment of the right to use capacity for such transmission, emission or reception; and provision of access to global information networks (Australia)</p> <p>Emitting, transmitting or receiving signs, signals, writing, images or sounds or intelligence of any nature by wire, cable, radio, optical or other electromagnetic system, or by any similar technical system, or making available for such emission, transmission or reception telecommunications facilities of a person who carries on the business of supplying such services (Canada)</p> <p>Services relating to the transmission, emission or reception of signals, words, images and sounds or information of any nature by wire, radio, optical or other electromagnetic systems, including the related transfer or assignment of the right to use capacity for such transmission, emission or reception, with the inclusion of the provision of access to global information networks (European Union)</p> <p>The transmission, emission or reception, and the transfer or assignment of the right to use capacity for the transmission, emission or reception, of signals, writing, images, sounds or information of any kind by wire, cable, radio, optical or other electromagnetic system, or by a similar technical system, and includes access to global information networks but does not include the content of the telecommunication (New Zealand)</p>
Telecommunications supplier	<p>A person whose principal activity is the supply of telecommunications services (New Zealand)</p>
Content of the telecommunication	<p>The signals, writing, images, sounds or information of any kind that are transmitted, emitted or received by telecommunications service (New Zealand)</p>
Telecommunications	<p>A facility, apparatus or other thing (including wire, cable, radio, optical or other electromagnetic system, or any similar technical system, or part thereof) used or</p>

facility	capable of being used for telecommunications (Canada)
Telecommunications networks	Networks that can be used to transfer voice and data, including cable networks, telecom networks and ISP (Internet Service Provider) networks, and should cover any facility which allows access to telecommunications, broadcasting or electronic services. The terms “telecommunications networks” and “communication networks” are interchangeable for VAT purposes , but “mobile networks” is a wholly contained subset of telecommunications networks (European Union)
Electronic services	A supply which does not include the provision of rights (e.g. technical know-how) or if rights are supplied, they are incidental to the supply. The supply involves specific work that is performed by a person for a specific customer. The supply requires human involvement (Canada) Include automated services delivered over the Internet or an electronic network that require minimal human intervention, and are impossible to ensure without information technology. Electronic services specifically include websites, web-hosting, distance maintenance of programmes and equipment; software and updating thereof; images, text and information and making available of databases; music, films and games, including games of chance and gambling games, and of political, cultural, artistic, sporting, scientific and entertainment broadcasts and events; and distance teaching (European Union)
Broadcasting services	Include services consisting of audio and audio-visual content, such as radio or television programmes provided to the general public via communications networks by and under the editorial responsibility of a media service provider, for simultaneous listening or viewing, on the basis of a programme schedule. Broadcasting services, in particular, include radio or television programmes transmitted or retransmitted over a radio or television network; or distributed via the Internet or similar electronic network (IP streaming) if broadcasted simultaneous with transmission or retransmission over a radio or television network (European Union)

Source: Own formulation

Place of supply of goods

Most jurisdictions define “goods” to include tangible personal or real property and the right to dispose thereof and exclude money. Place of supply rules in the selected jurisdictions demonstrate that tangible goods do not present serious problems in defining place of supply rules.

Australia generally taxes a supply of goods with reference to the location to which the goods are supplied or at which they are used. Australia applies a number of proxies to determine the place of supply of goods, including where the goods are delivered or made available; from where the goods are delivered; where the goods are installed or assembled; where the goods are used (only in respect of outbound leases); and whether a direct connection exists with goods to be exported (in respect of tooling and goods imported temporarily into Australia used in repairs or treatment).

Canada deems the place of supply of tangible personal property, by way of a sale,

to be where the property is, or where it is to be delivered or made available to the recipient of the supply. The place of supply of tangible personal property, not by way of a sale, is deemed to be where possession or use of the property is made available to the recipient. The place of supply of intangible personal property is deemed to be in Canada if the property may be used in whole or in part in Canada; or if the property relates to real property in Canada, to tangible personal property ordinarily in Canada or to a service to be performed in Canada. The place of supply of intangible personal property is deemed to be outside Canada if the property may not be used in Canada; or if the property relates to real property outside Canada, to tangible personal property ordinarily outside Canada or to a service to be performed wholly outside Canada. The place of supply of real property or a service in relation to real property is deemed to be where the real property is situated.

The European Union (through its VAT Directive) deems the place of a supply of goods not dispatched or transported to be where the goods are located at the time of supply; for goods dispatched or transported to be where the goods are located at the time when dispatched or transported; for goods sold on board ships, aircraft or trains to be the place of departure of the passenger transport operation; for gas through the natural gas distribution system, or electricity to be where the customer is located; for intra-Community acquisitions of goods to be where the transport of the goods to the person acquiring them ends; and for goods imported to be the Member State where the goods are located when they enter the European Union.

New Zealand deems the place of supply of goods to be in New Zealand if the supplier is resident in New Zealand, irrespective of the physical place of supply. The determination of the residence of a company follows the normal income tax provisions. In addition, two overriding rules determine residence for VAT purposes. Firstly, a person is resident in New Zealand to the extent that the person carries on an activity in New Zealand, which has a fixed or permanent place of business in New Zealand. Secondly, an unincorporated body of persons, partnership, joint venture or trust is resident in New Zealand if its centre of administration is in New Zealand. A foreign company is resident under this rule to the extent that its activities relate to that fixed or permanent place. The determination of residence of individuals

looks to a permanent place of abode in New Zealand or personal presence in New Zealand for certain predetermined periods per 12-month period. If the supplier is a non-New Zealand resident the place of supply of goods is deemed to be in New Zealand only if the goods are in New Zealand at the time of supply. However, if the non-New Zealand resident makes a supply to a registered person in New Zealand for use in a taxable activity it will be deemed to be supplied outside New Zealand, unless the supplier and recipient agree otherwise. The supplier will therefore not be able to charge or recover VAT. As an alternative, the supplier can agree with the recipient and have the supply treated as if it was made in New Zealand. The supplier might then be required to register for VAT. If a non-New Zealand resident provides goods, which are in New Zealand at the time of supply, to a person in New Zealand for use outside of or partially outside of that person's taxable activity, the non-New Zealand resident will be deemed to be making a supply in New Zealand. Table 6.14 below contains a summary of the place of supply of goods used in the selected countries.

Table 6.14: Place of supply of goods in the selected countries

A supply of	Place of supply:
Tangible personal property	
▪ <i>Goods made available, removed, installed, assembled (General)</i>	Where made available, removed, installed, assembled (General)
▪ <i>Not by way of a sale</i>	Where possession is given or made available (Canada)
▪ <i>Not dispatched or transported</i>	Where located at time of supply (EU)
▪ <i>Dispatched or transported</i>	Where dispatch or transport begins (EU)
▪ <i>Sold on ships, aircraft, or trains</i>	Where passenger transport begins (EU)
▪ <i>Supplied through distribution systems</i>	At supplier's business or fixed establishment or permanent address or usual residence or at customer's permanent address or usual residence (EU)
▪ <i>Supply by Resident</i>	Country of residence (NZ)
▪ <i>Supply by Non-Resident</i>	Generally outside country of consumption (NZ)
- <i>Goods in Country at time of supply</i>	In country – default position (NZ)
- <i>IF supplied to a registered person for use in its taxable activity</i>	Outside Country, or in Country IF supplier and recipient elect (NZ)
- <i>Goods Outside Country at time of supply</i>	Outside Country (NZ)
Real property	Location of real property

Source: Own formulation

Place of supply of services

Most jurisdictions define services as anything that is neither a good nor money, and done for a consideration. The supply of services generally includes the granting, assignment or surrender of the whole or part of any right, which is done for a consideration. Services usually consist of the obligation to perform or refrain from performing acts or the granting of permission to perform acts. Australia (and the three other jurisdictions) defines telecommunication services in addition to services. Canada defines a “telecommunications facility” separately as a facility, apparatus or other thing used or capable of being used for telecommunications. This is done as “facility” is used to define the place of supply rule for telecommunication services. The European Union’s VAT Directive, in addition to defining telecommunication services, uses the term “electronic services” and its indicative list of electronic services include website supply, web-hosting, distance maintenance of programmes and equipment; supply of software and updating thereof; supply of images, text and information and making available of databases; supply of music, films and games, including games of chance and gambling games, and of political, cultural, artistic, sporting, scientific and entertainment broadcasts and events; and supply of distance teaching. New Zealand, in addition to the above, also defines “content of the telecommunication” to mean the signals, writing, images, sounds or information of any kind that are transmitted, emitted or received by telecommunications service. The purpose being that the “content” is subject to the standard place of supply of services rule and not to the rule that applies to telecommunications services. The selected jurisdictions generally define telecommunication services as the transmission, emission or reception of data, signals, sounds and images by electronic means, wire, radio, optical or other electromagnetic systems. Telecommunication services include telephone, facsimile and telegraphic services, call and call-back services, telephone cards, as well as e-mail and access to and use of electronic databases, such as the Internet.

Traditional services do not present problems in defining place of supply rules. The place of supply rules in the selected jurisdictions demonstrate that the areas of complexity in defining place of supply of services rules include electronic services, telecommunication services, and other intangible property or services. The reverse

charge mechanism is often used. The reverse charge mechanism is not effective in business-to-consumer type transactions and is impractical to police.

Canada deems the place of supply of services, excluding intangible property and telecommunication services, to be in Canada if the service is performed wholly or in partly in Canada. Canada deems the place of supply of intangible personal property to be in Canada if (i) the property may be used in whole or in part in Canada; or (ii) the property relates to real property in Canada, to tangible personal property ordinarily in Canada or to a service to be performed in Canada (Sherman, 1999:139). Canada deems the place of supply of intangible personal property to be outside Canada if (i) the property may not be used in Canada; or (ii) the property relates to real property outside Canada, to tangible personal property ordinarily outside Canada or to a service to be performed wholly outside Canada (Sherman, 1999:139). The transfer of digital goods and services is generally considered to be the supply of intangible personal property or services. Canada deems the place of supply of making telecommunication facilities available to be in Canada if the facilities or part thereof are located in Canada. The place of supply is also deemed to be in Canada if the telecommunication is emitted and received in Canada, or the telecommunication is emitted or received in Canada and the invoicing is done in Canada.

The European Union's general place of supply rule deems the place of supply of services to be where the supplier has established its business or has a fixed establishment from where the service is supplied. In the absence of a place of business or fixed establishment, the place of supply is deemed to be where the supplier has its permanent address or usually resides. The European Union deems the place of supply of telecommunications and electronic services (amongst other services) to customers established outside the European Union, or to taxable persons established in the European Union but not in the same country as the supplier, to be the place where the customer has established its business or has a fixed establishment for which the service is supplied, or, in the absence of such a place, where it has its permanent address or usually resides. The European Union generally deems the place of supply of cultural, artistic, sporting, scientific, and

educational or entertainment services; services relating to exhibitions, conferences or meetings; and the valuation of, or work performed on, goods to be where the supplies are physically carried out.

New Zealand deems the place of supply of services, if the supplier is not resident in New Zealand, to be in New Zealand only if the services are physically performed in New Zealand. The converse also applies. If a non-New Zealand resident provides services, which are physically performed in New Zealand, to a person in New Zealand for use outside of or partially outside of that person's taxable activity, the non-New Zealand resident will be deemed to be making a supply of services in New Zealand. Table 6.15 below contains a summary of the place of supply of services used in the selected countries.

Table 6.15: Place of supply of services in the selected countries

A supply of	Place of supply where:
Business-to-business services	
<i>General Rule</i>	Customer is established (EU)
<i>Admission to cultural, artistic, sporting, scientific, educational, entertainment or similar events, such as fairs and exhibitions, and ancillary services</i>	Events actually take place (EU)
Business-to-consumer services	
<i>General Rule</i>	Supplier is established (EU)
<i>By an intermediary that acts in name and on behalf of another person</i>	Underlying transaction is supplied (EU)
<i>Goods transportation services</i>	Transport takes place, proportionate to distances covered (EU)
<i>Services and ancillary services, relating to cultural, artistic, sporting, scientific, educational, entertainment or similar activities, such as fairs and exhibitions, including supply of services of organisers</i>	Activities actually take place (EU)
<i>Passenger transportation services</i>	Transport takes place, proportionate to distances covered (EU)
<i>Ancillary transport activities and valuations of and work on movable tangible property</i>	Service is physically carried out (EU)
<i>Hiring of a means of transport services, other than short-term,</i>	Customer is located (EU)
<i>Hiring of pleasure boats, other than short-term hiring,</i>	Put at disposal of the customer, where service is actually provided by supplier from his place of business or a fixed establishment situated there (EU)
<i>Telecommunications</i>	Customer is located (EU); or performed in or supplied through a permanent establishment (Australia) Payment is for a terminal or station in Country. Place of supply of long distance telephone charges is in Country if 2 or more of the following 3 places are in Country:

		<ul style="list-style-type: none"> ▪ Place of origin; ▪ Place of termination; and ▪ Billing location; or <p>It comprises the making available of telecommunications facilities that are (or part thereof of are) located in Country (Canada).</p> <p>In any other case, the supply is in Country if telecommunication is emitted and received in Country, or telecommunication is emitted or received in Country and billing location is in Country (Canada).</p> <p><i>By a resident</i> – In Country (New Zealand) <i>By a non-resident</i> – Outside Country (New Zealand)</p> <ul style="list-style-type: none"> ▪ <i>IF a person, physically in Country, initiates the supply from a telecommunications supplier, whether or on behalf of another person</i> – In Country, <i>Except</i> for supplies between telecommunications suppliers. ▪ <i>IF impractical to determine the physical location of person due to type of service or class of customer</i> – In Country, <i>IF</i> the person's address for receiving invoices from supplier is in Country, <i>Except</i> for supplies between telecommunications suppliers ▪ <i>To a registered person for purposes of carrying on its taxable activity</i> – Outside Country, subject to exception (New Zealand)
	<i>Broadcasting</i>	Customer is located (EU)
	<i>Electronic services</i>	Customer is located (EU) or supplied through a business carried on in Country, or through a permanent establishment, and it constitutes a taxable supply (Canada)
Restaurant and catering services		
	<i>Not physically carried out on ships, aircraft or trains during passenger transport</i>	Services are physically carried out (EU)
	<i>Physically carried out on ships, aircraft or trains</i>	Passenger transport begins (EU)
Services connected with immovable property		
Short-term hiring of a means of transport		
Rights to acquire a thing and the supply of the thing would be connected with Country		
Rights		
Intangible personal property		
		Property: <ul style="list-style-type: none"> ▪ may be used, or ▪ relates to real property in Country; to tangible personal property ordinarily in Country; or a service to be performed in Country (Canada)
Entry into, or release from, an obligation		
Advice or information		
Instantaneous advice or information		
Anything else		
A service physically performed		
By a resident		
By a non-resident		
	<i>Physically performed in Country</i>	In Country – the default position (New Zealand)
		Outside Country, <i>IF</i> supplied to a registered person for use in its taxable activity (New Zealand)

		In Country, IF the supplier and recipient elect that the supply is not outside Country (New Zealand)
	<i>Physically performed outside Country</i>	Outside Country (New Zealand)
	<i>Deemed outside Country</i>	In Country, IF: <ul style="list-style-type: none"> ▪ Supplied to a resident; and ▪ Recipient estimates the intended use to be less than 95% or determines at the end of an adjustment period that the actual use is less than 90%; and ▪ Supply would be a taxable supply if made in Country by a registered person in the course or furtherance of a taxable activity carried on by that person (New Zealand)

Source: Own formulation

The definitions used in the selected jurisdictions; specific and general place of supply rules; treatment of non-residents, imported services, and cross-border business-to-business and business-to-consumer transactions, described in this chapter will be considered and where appropriate be applied in making recommendations in the following chapter, Chapter 7, to make recommendations to address the inter-jurisdictional VAT rule shortcomings in South Africa, identified in Chapter 5.

CHAPTER 7: RECOMMENDATIONS

7.1 INTRODUCTION

This chapter consolidates the research findings of chapters 4 – 6 and applies the data, shortcomings identified and recommendations made in these chapters to propose changes to current legislation and suggest new legislation to increase certainty in the VAT treatment of inter-jurisdictional activities and supplies in the South African VAT system.

This study does not only consider place of supply rules in the narrow sense but looks more widely into the VAT treatment of activities and supplies spanning the borders of South Africa. The two underlying aspects which underpin cross-border consequences in the VAT system are considered in detail, namely activities of non-resident persons with a South African “reach” or “connection”, particularly if consumption takes place in South Africa. Secondly, the study considers the VAT rate applicable to cross-border supplies.

The findings in Chapters 4 – 6 are used in the sections that follow to propose legislation to address current gaps and shortcomings and introduce specific “place of supply” rules to better address the VAT treatment of inter-jurisdictional transactions and enhance certainty. The proposed legislation applies the methods adopted by the South African legislator in amending or adding legislation, namely:

- *Indented underlined text in italics* denotes legislative additions or insertions; and
- [*Indented text in brackets in italics*] denotes legislative deletions.

7.2 NON-RESIDENT VAT REGISTRATION

A study of the impact of inter-jurisdictional supplies or activities would be incomplete without a comprehensive consideration of how non-residents are treated for VAT purposes. This section of the chapter proposes changes to the law to enhance legislative certainty.

7.2.1 Dependent Agents

Paragraph (a) of the definition of “enterprise” in section 1(1) of the Value-Added Tax Act, Act 89 of 1991 (the VAT Act) does not provide guidance as to whether it includes the activities of a non-resident enterprise acting through a local agent or dependent agent (as opposed to an independent agent) in the course of furtherance of which it makes supplies of goods or services⁴⁸⁶. Although the VAT Act is arguably clear on the VAT consequences of a foreign person conducting an “enterprise or activity” through an agent who acts for and on behalf of that person in South Africa, it nevertheless creates uncertainty in VAT circles as demonstrated by the replies of the panel of experts to the questionnaire developed for purposes of this study⁴⁸⁷. This should be clarified through various amendments to the VAT Act.

A definition of “dependent agent” can be derived from the Articles 5(4) and 5(5) of the OECD Model (OECD, 2014d) and would read as follows:

a person, other than an agent of an independent status, who acts on behalf of an enterprise and has, and habitually exercises an authority to conclude contracts in the name of the enterprise, except if the person’s activities are

⁴⁸⁶ Goods imported are deemed to be imported by the agent (and not the foreign principal) in terms of section 54(2A) (b) read with section 8(20).

⁴⁸⁷ This uncertainty could partly be ascribed to the fact that section 54 of the VAT Act deals with agents who make or receive supplies on behalf of a principal. Section 54 does not specifically address activities conducted by an agent on behalf of a principal which, as result, cannot directly be linked to the definition of “enterprise” in section 1(1) of the VAT Act.

limited to the following:

- (a) the use of facilities solely for the purpose of storage, display or delivery of goods or merchandise belonging to the enterprise;
- (b) the maintenance of the stock of goods or merchandise belonging to the enterprise solely for the purposes of storage, display or delivery;
- (c) the maintenance of a stock of goods or merchandise belonging to the enterprise solely for the purposes of processing by another enterprise;
- (d) the maintenance of a fixed place of business solely for the purpose of purchasing goods or merchandise or of collecting information, for the enterprise;
- (e) the maintenance of a fixed place of business solely for the purpose of carrying on, for the enterprise, any activity of a preparatory or auxiliary character;
- (f) the maintenance of a fixed place of business solely for any combination of activities mentioned in subparagraphs a) to e), provided that the overall activity of the fixed place of business resulting from this combination is of a preparatory or auxiliary character.

The VAT Act does not define “agent” or “dependent agent”. As a result, the term “agent” should be ascribed its general meaning. A definition of “dependent agent” should be inserted into section 1(1) as follows:

Dependent agent means:

an agent who acts for and on behalf of a principal as envisaged in section 54 of this Act⁴⁸⁸.

⁴⁸⁸ The legislator could also consider applying the principle of a Dependent Agent Permanent Establishment (DAPE) as addressed by Article 5(5) of the OECD Model Tax Convention on Income and Capital (the OECD Model) (OECD, 2014d).

Paragraph (a) of the definition of “enterprise” in section 1(1) of the VAT Act should be amended as follows:

(a) in the case of a vendor, or a vendor acting through a dependent agent who acts for and on behalf of such vendor, any enterprise or activity which is carried on continuously or regularly by any person in the Republic or partly in the Republic and in the course or furtherance of which...;

The VAT Act arguably requires a foreign enterprise to register as a vendor if it makes and receives supplies through a dependent agent and the agent assumes the foreign enterprise’s VAT obligations. This leads to uncertainty and creates additional compliance costs for the foreign person and SARS. To address this, proviso (xiv) should be inserted into the definition of “enterprise” in section 1(1) of the VAT Act as follows:

(xiv) A non-resident person who carries on activities in South Africa through a dependent agent who acts for and on behalf of such vendor and such agent assumes all such person’s obligations imposed under this Act is deemed not to be carrying on an enterprise if such non-resident person applies in writing to, and receives confirmation from, the Commissioner that this proviso applies to such non-resident person;

7.2.2 Foreign branch or main business

The VAT Act deems “transactions” between a branch or main business⁴⁸⁹ to be supplies, which is arguably unnecessary as the normal provisions which govern transactions between separate legal *personae* apply.

⁴⁸⁹ Section 8(9) of the VAT Act. It is arguable that, since proviso (ii) to the definition of “enterprise” in section 1(1) of the VAT Act deems the foreign branch or main business to be carried by a person separate from the vendor (if (aa) and (bb) are complied with), section 8(9) would only be required where the proviso (ii) deeming provision would not create supplies and supplies that need to be deemed by section 8(9). For example, cross-border cost recoveries in respect of salaries or

The VAT Act does not provide guidance as to what is meant by whether a branch or main business can be “separately identified”⁴⁹⁰. Proviso (iiA) should be inserted into the definition of “enterprise” in section 1(1) of the VAT Act, following proviso (ii), as follows:

(iiA) for purposes of proviso (ii)(aa) above, “separately identified” shall mean separate identification with regard to geography, activities and operations, a fixed or permanent place, or by some other means;

The VAT Act does not provide guidance as to what is meant by an “independent system of accounting”⁴⁹¹ that should be maintained in respect of the branch or main business. Proviso (iiB)⁴⁹² should be inserted into the definition of “enterprise” in section 1(1) of the VAT Act, following proviso (iiA), as follows:

(iiB) for purposes of proviso (ii)(bb) above, “independent system of accounting” shall mean separate identification with regard to records, books of account, or accounting systems, or by some other means;

Proviso (iiC)⁴⁹³ should be inserted into the definition of “enterprise” in section 1(1) of the VAT Act, following proviso (iiB), as follows:

(iiC) for purposes of proviso (ii) above, if a person carries on activities inside and outside of the Republic through branches and a main business -
(a) each branch or the main business is treated as a separate person;

overheads. However, as the definition of “supply” has been drafted in a wider and not narrower sense, such situations are also likely to constitute supplies.

⁴⁹⁰ Proviso (ii)(aa) to the definition of “enterprise” in section 1(1) of the VAT Act.

⁴⁹¹ As provided for in proviso (ii)(bb) to the definition of “enterprise” in section 1(1) of the VAT Act.

⁴⁹² The wording of proposed proviso (iiB) is mainly deduced from section 129. (3)(b) of Canada’s Excise Tax Act, 1985.

⁴⁹³ The wording of proposed proviso (iiC) is adopted mainly from section 56B of New Zealand’s Goods and Services Tax Act, 1985.

- (b) each branch or the main business inside the Republic is treated as a resident of the Republic;
- (c) each branch or the main business outside the Republic is treated as a non-resident; and
- (d) an activity carried on by a branch or the main business is treated as carried on separately by the branch or the main business; and
this proviso:
 - (i) treats the main business as a branch; and
 - (ii) applies, irrespective of whether a branch or the main business is registered (or required to be registered) in terms of section 23 of this Act.

Proviso (ii) to the definition of an “enterprise” in section 1(1) of the VAT Act does not provide guidance on which supplies emanate from activities carried on inside and outside South Africa, particularly if a non-resident carries on similar activities inside and outside South Africa. Goods or services that are to be used or supplied whilst outside of South Africa but that will form part of a supply by a registered branch or main business in South Africa should be deemed to be part of the envisaged supplies by the branch or main business. Proviso (iiD) should be inserted into the definition of “enterprise” in section 1(1) of the VAT Act, following proviso (iiC), as follows:

- (iiD) for purposes of proviso (ii) above, goods or services originating from an export country that form an integral part of a supply by a registered branch or main business in South Africa are deemed be part of that supply by branch or main business;

7.2.3 Internationally traded services and intangibles

The VAT Act does not provide adequate guidance as to whether a non-resident person that only supplies intangible property for use or consumption without any physical activities in South Africa conducts an “enterprise” as defined in section 1(1) of the VAT Act. To address this, proviso (xiii) should be inserted into the definition of

“enterprise” in section 1(1) of the VAT Act⁴⁹⁴ to deem a foreign enterprise not to be carrying on an enterprise if the foreign enterprise only supplies intangible property to a registered vendor and if the vendor would have been entitled to a full input tax deduction in respect of the supply made to it:

(xiii) A person that makes supplies solely of intangible property from an export country to a registered vendor, if the vendor would have been entitled to a full input tax deduction in respect of the supply to it, is deemed not to be carrying on an enterprise;

The VAT Act does not define “enterprise or activity” as contained in the definition of “enterprise” in section 1(1) of the VAT Act. A definition should be inserted into section 1(1) as follows:

Enterprise or activity for purposes of the definition of “enterprise” includes *physical, contractual, or economic activities*⁴⁹⁵;

7.2.4 Foreign underwriting insurance business

Proviso (vi) to the definition of “enterprise” in section 1(1) determines when the activity of underwriting insurance business by Underwriting Members of Lloyd’s of London would constitute an “enterprise” for VAT purposes. The VAT Act, however, does not provide adequate direct guidance in respect of other non-resident insurers.

To the extent that other non-resident insurers⁴⁹⁶ conclude contracts of insurance in South Africa, they should also be required to register as vendors⁴⁹⁷.

⁴⁹⁴ Similar to section 8(4) of the New Zealand GST Act.

⁴⁹⁵ This would be in line with intangible and electronic services.

⁴⁹⁶ This should arguably not apply to reinsurers as the Short Term Insurance Act contains adequate safeguards to limit to South African business.

⁴⁹⁷ Foreign insurance underwriters writing insurance business in South Africa through binding agents could arguably not constitute an “enterprise” activity. This is contrary to the provisions that apply to Lloyds of London, which is specifically catered for in the definition of “enterprise”.

Proviso (vi) to the definition of “enterprise” in section 1(1) of the VAT Act should be amended as follows:

- (vi) *the supply of insurance services by a non-resident person from an export country, including the activity of underwriting insurance business by Underwriting Members of Lloyd’s of London, to the extent that contracts of insurance are concluded in the Republic, shall be deemed to be the carrying on of an enterprise;*

7.2.5 Electronic services

The current compulsory VAT registration threshold of non-resident suppliers of electronic services is R50 000, which is not aligned with the R1 million registration threshold that applies to other persons. The registration threshold for foreign electronic service suppliers should be aligned with local suppliers to comply with the OECD neutrality principle to ensure that local and foreign persons in similar circumstances are treated similarly. Section 23(1A) of the VAT Act should be amended as follows:

- 23(1A) *Every person who carries on any enterprise as contemplated in paragraph (b) (vi) of the definition of “enterprise” in section 1 and is not registered becomes liable to be registered at the end of any month where the total value of taxable supplies made by that person has exceeded [R50 000] R1 million.*

Section 15(2)(a)(vii) of the VAT Act provides that non-resident electronic service suppliers should account for VAT on the payments basis. Non-resident electronic service suppliers should be required to apply the invoice basis of accounting for VAT to bring them into line with domestic suppliers of electronic service suppliers. This would require deletion of section 15(2)(a)(vii) of the VAT Act:

- [(vii) carrying on an enterprise as contemplated in paragraph (b)(vi) of the definition of “enterprise” in section 1; or]*

Supplies to recipients in a “group of companies” (as defined for Income Tax purposes) are not excluded from the ambit of the electronic services provisions. Paragraph (b)(vi) of the definition of “enterprise” should be amended as follows:

(b)(vi) the supply of electronic services, other than a supplier who solely supplies electronic services to recipients in a “group of companies” as defined in section 1 of the Income Tax Act, 1958, by a non-resident person [from a place in an export country]-

(aa) to a recipient that is a resident of the Republic; or

(bb) where any payment to that person in respect of such electronic services originates from a bank registered or authorised in terms of the Banks Act, 1990:

The electronic services Regulation contains a finite list of qualifying electronic services⁴⁹⁸, which would be less flexible in adapting to continuous developments in the field of electronic services than a more principled approach or differentiation. The list of electronic services also does not differentiate between business-to-business and business-to-consumer supplies.

The legislator should differentiate between business-to-business and business-to-consumer supplies and only seek to legislate and tax business-to-consumer supplies in terms of the recently introduced electronic services provisions⁴⁹⁹. The

⁴⁹⁸ An exhaustive list would require the Regulation to be reviewed and updated regularly, for example every two years.

⁴⁹⁹ In theory, the current electronic services provisions contained in the VAT Act, assuming no special provisions for non-resident suppliers of electronic services were enacted, would effectively levy tax through the imported services provisions on (i) persons who are not registered or required to be registered for VAT purposes, and (ii) vendors (persons who are registered or required to be registered) who are not entitled to a full input tax deduction (partly taxable and partly exempt vendors). As per the OECD (2014c:9), compliance with the imported services provisions by persons in category (i) above is low, which limited tax revenue collected historically. Consequently, the most effective approach is to require the non-resident supplier to register for VAT in the foreign tax jurisdiction. As compliance with the imported services provisions by vendors in category (ii) above is subject to SARS’ monitoring and systems, compliance is more likely. As a result, the main objective

legislator could consider the adoption of a *de minimus* rule (for example, 95 per cent or more) to allow non-resident electronic services suppliers whose business-to-business supplies in relation to total supplies are equal to or exceed the *de minimus* threshold not to register for VAT purposes. This would keep compliance costs to a minimum.

The Regulation makes reference to but does not define various terms, for example “still image”; “subscription service to a web site”; and “subscription”. The legislator should address these definitional shortcomings.

The legislator should consider excluding from the ambit of “electronic services”, supplies that include the provision of rights (e.g. technical know-how) or if rights are supplied, they are incidental to the supply, as was done in Canada’s Excise Tax Act, 1985. Electronic services should ideally also exclude supplies that involve specific work performed by a person for a specific customer.

7.2.6 Telecommunication services

The VAT Act does not contain specific provisions relating non-resident suppliers of telecommunication services in South Africa. A number of years ago the legislator proposed an amendment to the VAT Act to include foreign suppliers of telecommunication services in the definition of “enterprise” in section 1(1) of the VAT Act. The amendment⁵⁰⁰ proposed read as follows:

...the activities of any person who continuously or regularly supplies telecommunication services to any person who utilizes such services in the Republic...

with the introduction of the non-resident supplier of electronic services provisions would have been to collect tax in respect of category (i) above.

⁵⁰⁰ The proposal was to be effected by the addition of paragraph (b)(iv) to the definition of “enterprise”, but was never promulgated.

Telecommunication services supplied by non-residents that are utilised or consumed in South Africa should be subject to VAT and these suppliers should fall within the definition of “enterprise”. Sub-paragraph (vii) should be added to paragraph (b) of the definition of “enterprise” in section 1(1) of the VAT Act as follows:

(b)(vii) the supply of telecommunication services by a non-resident telecommunication supplier to a recipient that is a resident of the Republic:

The VAT Act does not define telecommunication services. A definition of “telecommunication services”⁵⁰¹ should be inserted into section 1(1) as follows:

Telecommunication services include:

- (a) services of transmitting, emitting or receiving; or the transfer or assignment of the right to use capacity for transmitting, emitting or receiving; or the making available of telecommunication facilities of a person who carries on the business of supplying such services for emitting, transmitting or receiving of signs, signals, words, writing, images or sounds, information or intelligence of any nature; and*
- (b) providing access to global information networks by wire, cable, radio, optical or other electromagnetic system, or by any similar technical system.*
- (c) but does not include the content of the telecommunication;*

The VAT Act does not define “telecommunication supplier”. A definition of

⁵⁰¹ The proposed definition is adopted from those used by Australia, Canada, the European Union, and New Zealand.

“telecommunication supplier”⁵⁰² should be inserted into section 1(1) as follows:

Telecommunication supplier means:

A person whose principal activity is the supply of telecommunication services;

The VAT Act does not define “telecommunication content”. A definition of “telecommunication content”⁵⁰³ should be inserted into section 1(1) as follows:

Telecommunication content means:

the signs, signals, words, writing, images or sounds, information or intelligence of any kind, that are transmitted, emitted or received by telecommunication services;

The VAT Act does not define “telecommunication facility”. A definition of “telecommunication facility”⁵⁰⁴ should be inserted into section 1(1) as follows:

Telecommunication facility means:

a facility, apparatus or other thing (including wire, cable, radio, optical or other electromagnetic system, telecommunication network, or any similar technical system, or part thereof) used or capable of being used for telecommunication;

The VAT Act does not define “telecommunication network”. A definition of

⁵⁰² The proposed definition is adopted from those used by Australia, Canada, the European Union, and New Zealand.

⁵⁰³ The proposed definition is adopted from those used by Australia, Canada, the European Union, and New Zealand.

⁵⁰⁴ The proposed definition is adopted from those used by Australia, Canada, the European Union, and New Zealand.

“telecommunication network”⁵⁰⁵ should be inserted into section 1(1) as follows:

Telecommunication network includes:

networks that can be used to transfer voice and data, including cable networks, telecommunication networks and ISP (Internet Service Provider) networks, and covers any facility which allows access to telecommunications, broadcasting or electronic services; the terms “telecommunication networks” and “communication networks” are interchangeable for VAT purposes, but “mobile networks” is a wholly contained subset of telecommunication networks;

7.2.7 Broadcasting services

The VAT Act does not contain specific provisions relating to non-resident suppliers of broadcasting services in South Africa. Broadcasting services supplied by non-residents that are utilised or consumed in South Africa should be subject to VAT and the activities of these suppliers should fall into the definition of “enterprise”. Sub-paragraph (vii) should be added to paragraph (b) of the definition of “enterprise” in section 1(1) of the VAT Act as follows:

(b)(viii) the supply of broadcasting services by a non-resident broadcasting services supplier to a recipient that is a resident of the Republic:

The VAT Act does not define broadcasting services. A definition of “broadcasting services”⁵⁰⁶ should be inserted into section 1(1) as follows:

Broadcasting services includes:

services consisting of audio and audio-visual content, including radio and television programmes provided to the general public through

⁵⁰⁵ The proposed definition is adopted from those used by the European Union.

⁵⁰⁶ The proposed definition is an adaptation of the one used in the European Union.

communications networks by and under the editorial responsibility of a media service provider, for simultaneous listening or viewing, on the basis of a programme schedule; broadcasting services, in particular, include radio and television programmes transmitted or retransmitted over a radio or television network; or distributed via the Internet or similar electronic network (IP streaming) if broadcast simultaneously with transmission or retransmission over a radio or television network;

7.2.8 Goods imported on behalf of a foreign principal

The VAT Act does not clarify a local consignee's entitlement to claim VAT incurred on importation as an input tax deduction where the consignment agreement is continuous⁵⁰⁷. The consignee's input tax entitlement in terms of section 16(3) is arguably justified in terms of section 54(2A) (b) of the VAT Act but cannot be relied on in circumstances where the foreign principal continuously or regularly supplies to the local consignee and, as a result, should be VAT registered. Section 54(2A) (b) of the VAT Act should be amended to address its current shortcomings, as follows:

54(2A)(b) ...where any goods are imported into the Republic by an agent who is acting on behalf of another person who is the principal for the purposes of that importation, and-

- (i) the agent is a registered vendor; and
- (ii) the principal is [not a resident of the Republic] a non-resident person and is not a registered vendor and has applied in writing to, and received confirmation from, the Commissioner that proviso (xv) to the definition of

⁵⁰⁷ The local consignee could, in once-off situations, be entitled to claim the VAT incurred on importation in terms of section 54(2A)(b) read with section 8(20) of the VAT Act. However, where the local consignee regularly acquires consignment stock from the same foreign supplier, the supplier would be required to register for VAT and once registered, section 54(2A)(b) of the VAT Act would no longer apply. The local consignee may arguably not be party to another person not fulfilling its obligations imposed under the VAT Act.

“enterprise” in section 1(1) of this Act applies to such non-resident person;

(iii) *the goods are imported by the principal for the purposes of a supply made or to be made by him to a person in the Republic; and*

(iv) *the agent obtains and retains documentary proof, as is acceptable to the Commissioner, that-*

(aa) *he paid the tax on importation on behalf of that principal;*

(bb) *such agent and that principal agree in writing that the said tax has not and will not be reimbursed to such agent by that principal;*

that importation shall for the purposes of this Act be deemed to be made by such agent and not by that principal,

The VAT Act does not permit a foreign enterprise or consignor not to register as a vendor if it solely supplies goods on consignment to a consignee in the Republic. Proviso (xv) should be inserted into the definition of “enterprise” in section 1(1) of the VAT Act as follows:

(xv) *The supply of consignment goods by a non-resident person (consignor) from a place in an export country to a consignee in the Republic is deemed not to be carrying on an enterprise if the consignor solely makes supplies of consignment goods in circumstances contemplated in section 54(2A)(b) of this Act, if such non-resident person has applied in writing to, and received confirmation from, the Commissioner that this proviso applies to such non-resident person;*

Section 8(20) of the VAT Act deems the agent to make a supply to the foreign principal’s recipient. As section 8(20) should be read in conjunction with section 54(2A)(b) of the VAT Act no amendment is required.

7.2.9 Obiter dicta

This section highlights views expressed on a number of issues related to inter-jurisdictional VAT treatment and potential uncertainty in the VAT Act.⁵⁰⁸ Although these views have merit, it is submitted that they do not pose major interpretational problems. For sake of comprehensiveness and potential further consideration, these views have been reproduced.

Foreign branch or main business

It has been suggested that the VAT Act is unclear as to whether a foreign branch or main business can have more than one South African VAT registration for the same legal entity (Connell, 2011). The view is held that a foreign enterprise can have more than one branch or main business in South Africa. The legislator should consider whether the definition of “enterprise” should provide further clarity.

Goods imported on behalf of a foreign principal

It has been suggested that the VAT Act is unclear as to whether a foreign consignor would create a VAT “enterprise” in South Africa in consequence of ownership in goods passing whilst in South Africa (Glyn-Jones, 2011). The view is held that a foreign enterprise who sells goods in respect of which the ownership passes in South Africa could create a VAT “enterprise”. The legislator should consider whether the definition of “enterprise” should exclude these activities if the non-resident supplier has no activities in South Africa other than the transfer of ownership in the consignment goods.

Local enabling activities resulting in foreign supplies

It has been suggested that the VAT Act is unclear as to whether a foreign enterprise with activities in South Africa purely to enable the making of supplies outside South Africa creates an “enterprise” for VAT purposes⁵⁰⁹ (Connell, 2011). The view is held

⁵⁰⁸ These views were obtained through the questionnaire (see Appendix 1) sent to the respondents.

⁵⁰⁹ For example, if a foreign news agency sends reporters to South Africa on a continuous and regular basis to gather information. The information is used offshore by the main business to compile news programmes which are then broadcasted globally and locally.

that a foreign enterprise with activities in South Africa purely to enable the making of supplies outside South Africa creates an “enterprise” for VAT purposes. The legislator should consider whether the definition of “enterprise” should be limited to exclude the mentioned activities.

Limited duration supplies

It has been suggested that the VAT Act is unclear as to whether and if so, when, a foreign supplier that enters South Africa for a once-off predetermined time period to make a supply or supplies would create a VAT “enterprise” (Glyn-Jones, 2011). The view is held that a foreign enterprise that enters South Africa for a once-off predetermined time period to make a supply or supplies would create a VAT “enterprise”. The legislator should consider whether the definition of “enterprise” should be limited to exclude these activities if the activities do not exceed a limited time period or the resultant supplies do not exceed a certain monetary threshold.

Supplies of goods before entry for home consumption

It has been suggested that the VAT Act is unclear as to whether a “sale”⁵¹⁰ of goods made by a non-resident whilst the goods are outside South Africa with delayed transfer of ownership, could create an “enterprise” for the non-resident⁵¹¹ (Rudolph, 2012). The view is held that a foreign enterprise that “sells” goods whilst outside South Africa if ownership is transferred after the goods have entered South Africa could create a VAT “enterprise”⁵¹². The legislator should consider whether the

⁵¹⁰ Section 1(1) of the VAT Act defines “sale” as “an agreement of purchase and sale and includes any transaction or act whereby or in consequence of which ownership of goods passes is or is to pass from one person to another”. The term “supply”, on the other hand, is defined in section 1(1) of the VAT Act as including “performance in terms of a sale, rental agreement, instalment credit agreement and all other forms of supply, whether voluntary, compulsory or by operation of law, irrespective of where the supply is effected, and any derivative of “supply” shall be construed accordingly”.

⁵¹¹ In effect, the non-resident transacts or acts in consequence of which ownership passes to another person, but the actual transfer of ownership is delayed until after importation into South Africa,

⁵¹² Since, in terms of the definition of “enterprise” in section 1(1) of the VAT Act “any enterprise or activity carried on continuously or regularly in...the Republic in the course of which goods or services are supplied...” would constitute an “enterprise”. The transfer of ownership in goods would comprise

definition of “enterprise” should be amended to exclude these activities if the non-resident supplier has no activities in South Africa other than the transfer of ownership in the goods.

Local services provided to a foreign branch of a local vendor

It has been suggested that inter-jurisdictional VAT rules could be introduced to narrow the obligation of foreign entities to register for VAT in South Africa, to activities carried on within South Africa from a fixed or permanent place of business in South Africa⁵¹³ if such rules would not create a loss of revenue for the State (Badenhorst, 2011).

7.3 INTER-JURISDICTIONAL VAT RATE

In addition to a consideration of how non-residents are treated for VAT purposes, inter-jurisdictional VAT rules are significantly impacted by the VAT rate that applies. This section of the chapter proposes changes to the law to enhance legislative certainty in this regard.

7.3.1 Double taxation agreements

The OECD Model (Double Tax Agreement) does not apply to consumption taxes, but applies to taxes on income and capital (OECD, 2014d). The legislator could consider implementing a model similar to the OECD Model that applies to VAT. This could be effected in one of at least two manners:

- the South African government officials that negotiate the OECD Model with other countries can endeavour to include a Model that applies to VAT; or
- the legislator could enact the principles of the OECD Model in the VAT Act to apply to the VAT regime.

an “activity”, albeit an economic activity, and if followed by a supply of those goods, would constitute an “enterprise” if done in the Republic.

⁵¹³ Refer to the examples in VAT Notice 741A of HM Customs and Excise.

Irrespective of the method chosen, the purpose of such implementation would be to reach agreement with the treaty or trading country that:

- inter-jurisdictional supplies subject to the zero rate in one country should be subject to the standard rate in another country, and *vice versa*, on the assumption that the VAT regimes of both treat the specific transaction similarly for domestic VAT purposes, namely subject domestic supplies to VAT or exempt such supplies from VAT; and
- that the country where the supply originates should zero rate the supply and the country of destination should apply the standard rate.

7.3.2 Services to non-residents outside South Africa

Section 11(2)(l) of the VAT Act is the section used in most instances to zero rate services supplied to non-residents. Section 11(2)(l) zero rates services supplied to a non-resident person, except where the services "...are supplied directly in connection with..." land or movable property or supplied directly to that or any "other person" if that or the other person is in the Republic. The words and phrases "directly" and "directly in connection with" (as opposed to "directly in respect of") and any "other person" used in section 11(2)(l) and elsewhere in the VAT Act are ambiguous (van Heerden, 2012). Although the phrase to any "other person" could potentially imply a legal differentiation between the contractual and beneficial recipient of a supply, the VAT Act does not provide guidance.

Section 11(2)(l) of the VAT Act was mainly an adaptation of section 11A(1)(k) (previously section 11(2)(e)) of the New Zealand Goods and Services Tax Act, 1985 (the GST Act, 1985), read with certain other sections, most notably sections 11A(2) and 11A(3).

In *Wilson and Horton v CIR* (1995) 17 NZTC 12,325 (*Wilson and Horton* (1995)) advertising space was held to be directly in connection with the advertisement and not directly in connection with what is advertised. The advertising space and the subject matter of the advertisement or advertising message is at least one step

removed (*Wilson and Horton v CIR* (1994) 16 NZTC 11,221 (at 11,224) (*Wilson and Horton* (1994))). In Case S88 (1996) 17 NZTC 7,551 it was held that motor vehicle repair services are directly in connection with the vehicle as the repair service could not be performed without the vehicle⁵¹⁴.

The VAT Act does not define the phrase “directly in connection with”⁵¹⁵. A definition of “directly in connection with”⁵¹⁶ should be inserted into section 1(1) as follows:

Directly in connection with should be interpreted by taking the following into account:

- (i) for two things to be “in connection with” each other, a sufficient relationship between the things is a matter of fact, degree and impression and requires a common sense assessment of the facts;
- (ii) the word “directly” indicates a close connection between a service and land or movable property, for the service to be “directly in connection with” the land or movable property;
- (iii) a direct relationship between the service and the land or movable property does not require the non-resident to own or be entitled to the use or possession of the land or movable property;
- (iv) the recipient of the service does not need to have a legal interest in the land or movable property for the service to be “directly in connection with” the land or movable property;
- (v) services that are “directly in connection with” land or movable property include services that have a physical effect on the land or movable property, such as gardening or repairs;

⁵¹⁴ These principles were confirmed by the New Zealand Tax Revenue Authority in Public Ruling – BR Pub 03/03, dated 28 April 2003.

⁵¹⁵ Although the phrase “directly in connection with” is used only three times in the VAT Act, the ambiguity that it creates warrants further clarification by the legislator.

⁵¹⁶ The proposed definition is an adaptation of the New Zealand Tax Revenue Authority’s (NZTRA) Public Ruling – BR Pub 10/09, dated 2 September 2010, in which the NZTRA ruled on whether legal services provided to non-residents were directly in connection with land in New Zealand, and formulated principles on the interpretation of the phrase “directly in connection with”.

- (vi) services that merely bring about or facilitate a transaction that has a direct effect on the land or movable property and that are one step removed from a transaction that has a direct effect on the land or movable property are not “directly in connection with” the land or movable property;
- (vii) services that could not have been performed but for the existence of the land or movable property may suggest that they are “directly in connection with” the land or movable property, but this is not conclusive;
and
- (viii) the services must be supplied directly in connection with specific land or movable property;

Section 11A(3) of the GST Act, 1985 for purposes of, amongst others, section 11A(1)(k) provides that “outside New Zealand” includes, for a company or an unincorporated body that is not a resident, a minor presence in New Zealand, or a presence that is not effectively connected with the supply.

In *Wilson and Horton* (1995), the New Zealand Tax Court of Appeal held that the word “to” in the phrase “supplied to a person” means “contractually to” and does not infer “beneficially for”. The ambiguity created by the use of the word “to” in the phrase “supplied to a person”, and by the use of any “other person” in section 11(2)(l) of the South African VAT Act can be addressed as follows:

- (l) *the services are contractually supplied to a person who is not resident of the Republic, not being services which are supplied directly-*
 - (i) *in connection with land or any improvement thereto situated inside the Republic; or*
 - (ii) *in connection with movable property (excluding debt securities, equity securities or participatory securities) situated inside the Republic at the time the services are rendered, except movable property which-*
 - (aa) *is exported to the said person subsequent to the supply of such services; or*

- (bb) *forms part of a supply by the said person to a registered vendor and such services are supplied to the said person for purposes of such supply to the registered vendor; or*
- (iii) *to the said person or any other person, other than in circumstances contemplated in subparagraph (ii) (bb), if the said person or such other person is in the Republic and effectively connected with the supply⁵¹⁷ at the time the services are rendered and receives the services supplied, including-*
- (aa) an employee of the said person; or*
- (bb) if the said person is a company, a director of the company;*

and the other person will not receive the services supplied in the course of making taxable or exempt supplies and⁵¹⁸ not being services which are the acceptance by any person of an obligation to refrain from carrying on any enterprise, to the extent that the carrying on of that enterprise would have occurred within the Republic

7.3.3 Services supplied directly in respect of goods or movable property exported or destined for export

Section 11(2)(g) of the VAT Act zero rates certain services supplied directly in respect of movable property or goods exported or destined for export. Section 11(2)(g)⁵¹⁹ of the VAT Act contains the only use in the VAT Act of the expression “directly in respect of” as opposed to “directly in connection with”, which occurs more commonly in the VAT Act. The use of “directly in connection with” and “directly in

⁵¹⁷ Addressed by an adaptation of section 11A(3) of the GST Act, 1985.

⁵¹⁸ Addressed by an adaptation of section 11A(2) of the GST Act, 1985.

⁵¹⁹ Section 11(2)(g) zero rates services supplied directly in respect of (i) movable property situated in an export country at the time the services are rendered; or (ii) goods temporarily admitted into the Republic from an export country which are exempt from tax on importation under Items 470 and 480 of paragraph 8 of Schedule 1 of the VAT Act; or (iii) goods in respect of which the provisions of paragraph (b) or (c) of the definition of “exported” in section 1 of the VAT Act apply; or (iv) the repair, maintenance, cleaning or reconditioning of a foreign-going ship or aircraft.

respect of” could potentially create interpretational difficulties. Various dictionaries indicate that “directly in connection with” and “directly in respect of” are synonyms⁵²⁰. As a result, it is suggested that the use of “directly in respect of” in section 11(2)(g) of the VAT Act be replaced with “directly in connection with”.

7.3.4 Services physically rendered outside the Republic

The VAT Act⁵²¹ zero rates the supply of services physically rendered elsewhere than in the Republic or to a customs controlled area enterprise or an IDZ operator in a customs controlled area. The study recognised two technical or interpretative issues in applying section 11(2)(k) of the VAT Act in practice, namely:

- the meaning of the phrase “physically rendered”; and
- SARS’ apparent application of section 11(2)(k) to deny the zero rate if the supplier sub-contracts the provision of the services to be rendered elsewhere than in the Republic.

Regarding the phrase “physically rendered”, in *Wilson and Horton v VCIR* (1995) 17 NZTC 12,325 (*Wilson and Horton* (1995)) the New Zealand Tax Court of Appeal held that the word “to” in the phrase “supplied to a person” means “contractually to”. The phrase “physically rendered” therefore stands in contrast to a contractual supply and denotes a physical rendition of services.

Regarding SARS’ purported application of section 11(2)(k) to deny the application of the zero rate unless the supplier itself physically renders the supply elsewhere than in the Republic, it should be noted that such interpretation would fall foul of the destination or consumption principle of taxation. In addition, section 11(2)(k) of the

⁵²⁰ Cambridge Dictionaries Online accessed on 19 March 2016 at <http://dictionary.cambridge.org/dictionary/english/in-respect-of-sth>; and Oxforddictionaries.com accessed on 19 March 2016 at http://www.oxforddictionaries.com/definition/english-thesaurus/respect?q=in+respect+of#in_respect_of.

⁵²¹ Section 11(2)(k) of the VAT Act.

VAT Act should be clarified as follows:

(k) the services are physically rendered elsewhere than in the Republic, or are the arranging of services that are physically rendered elsewhere than in the Republic, or to a customs controlled area enterprise or an IDZ operator in a customs controlled area⁵²²

The words “performed” and “rendered” are used in the VAT Act in many instances, particularly in the zero rating provisions. The use in the VAT Act of the concepts “performed” and “rendered” and their derivatives (such as perform or render) creates interpretational difficulty. The word “perform” is defined as “carry out, accomplish, or fulfil (an action, task, or function)” or “to do an action or piece of work”, whereas the word “render” is defined as “to cause someone or something to be in a particular state”, or “provide or give”. Some dictionaries indicate “perform” and “render” as synonyms⁵²³. The use of the words (or their derivatives) “perform” or “render” in the VAT Act of is often linked or in direct reference to a “supply” and mostly (if not always) infer a similar meaning, application, or use. The word “performance” is also used in the definition of “supply” in section 1(1) of the VAT Act, but in this sense it is used in a more legal or contractual sense. To enhance clarity and interpretation, the legislator could review the VAT Act to ensure a more consistent use of these two terms and their derivatives.

7.3.5 Foreign branch or main business

As a branch and its main business as envisaged in proviso (ii) to the definition of “enterprise” in section 1(1) of the VAT Act are part of the same legal person, if either of them falls into the definition of “resident of the Republic”, the remaining one would be a “resident of the Republic”. As a result, the general zero rate provisions that

⁵²² This is an adaptation of section 11A(1)(j) of the New Zealand GST Act, 1985.

⁵²³ Cambridge Dictionaries Online accessed on 21 March 2016 at <http://dictionary.cambridge.org/dictionary/english/in-respect-of-sth>; and Oxforddictionaries.com accessed on 21 March 2016 at http://www.oxforddictionaries.com/definition/english-thesaurus/respect?q=in+respect+of#in_respect_of.

apply to independent parties, to the extent that it relies on “resident of the Republic”⁵²⁴, would preclude a local vendor to zero rate supplies to the foreign “VAT person”. If the South African vendor supplies the services directly to the non-resident branch or main business, the services can be zero rated in terms of section 11(2)(o) of the VAT Act.

To address this shortcoming, non-vendor non-resident branches or main businesses as envisaged in proviso (ii) to the definition of “enterprise” in section 1(1) of the VAT Act should be excluded from the definition of “resident of the Republic”, to the extent that it does not have an “enterprise or activity” in South Africa. This should be effected by introducing a clearly articulated definition of “non-resident” into the VAT Act.

7.3.6 Non-resident

The VAT Act does not define “non-resident”, which impacts on the verbosity and complexity of legislation, for example, the zero rating provisions relating to supplies made to non-residents have been drafted to refer to “a person who is not a resident of the Republic”, and could have referred to “a non-resident person”⁵²⁵. A definition

⁵²⁴ For example, section 11(2)(l) of the VAT Act.

⁵²⁵ Adding a definition of “non-resident” will impact the VAT Act in 17 places, namely paragraph (b) of the definition of “foreign going ship” in section 1(1); sections 11(1)(q); 11(2)(e); 11(2)(h); 11(2)(i); 11(2)(j); 11(2)(l); 11(2)(r); 11(2)(v); 12(k); 16(3)(c); 23(2); 44(3)(d); 45(1)(iii); 46(f); 54(2A)(b)(ii); and section 54(6) (a). Such addition will also address the shortcoming that supplies (other than section 8(9) deemed supplies) by a local branch or main business (as envisaged by proviso (ii) to the definition of “enterprise” in section 1(1)) to its foreign branch or main business do not currently qualify to be zero rated (in terms of section 11(2)(l)), as the foreign “person” is a “resident of the Republic” by virtue of the fact that the local “enterprise” is a “resident of the Republic” and both “persons” are part of the same legal entity.

of a “non-resident”⁵²⁶ should be inserted into section 1(1) as follows:

Non-resident means a person to the extent that the person is not a resident of the Republic;

The consequential changes to the VAT Act should be effected which, amongst others, would entail replacing the phrase “a person who is not a resident of the Republic” with “a non-resident person”⁵²⁷.

7.3.7 Non-resident refunds

The South African VAT system does not refund non-resident enterprises the VAT incurred in South Africa in respect of consumption that would effectively take place outside of South Africa⁵²⁸.

New Zealand’s GST Act was changed with effect 1 April 2014 to allow non-residents who do not carrying on a VAT enterprise in New Zealand and do not provide services to non-vendors, to claim back tax in certain instances (New Zealand, 2014)⁵²⁹. To claim tax back a non-resident must expect a GST refund claim exceeding a minimum amount in its first GST tax period. Non-residents that perform services in New Zealand under a contract constitute non-resident contractors and

⁵²⁶ The proposed definition of “non-resident” is an adaptation from New Zealand (section 2 of the Goods and Services Tax Act, 1985), after consideration of similar definitions enacted by Australia and Canada.

⁵²⁷ These changes should be effected to paragraph (b) of the definition of “foreign going ship” in section 1(1); sections 11(1)(q); 11(2)(e); 11(2)(h); 11(2)(i); 11(2)(j); 11(2)(l); 11(2)(r); 11(2)(v); 12(k); 16(3)(c); 23(2); 44(3)(d); 45(1)(iii); 46(f); 54(2A)(b)(ii); and section 54(6)(a).

⁵²⁸ The VAT system allows refunds to certain tourists in respect of certain goods acquired to be taken outside of South Africa through the VAT Refund Administrator.

⁵²⁹ Section 54B of the GST Act, 1985. See also section 19(1B) – accounting basis; section 20(3L), 20(3LB), 20(3M), – calculation of tax payable; section 46(1B) – Commissioner’s right to withhold payments, section 51(4)(a) – persons making supplies in the course of taxable activity to be registered, section 51B(1)(d) – persons treated as registered; 52(7) – cancellation of registration, section 54C – non-residents: cancellation of registration, section 55(1B) – group of companies.

are not entitled to register for the refund scheme (New Zealand, 2014).

Section 23(1B)⁵³⁰ should be inserted into the VAT Act, following section 1(2) as follows:

- 23(1B)(1) Notwithstanding section 23(1), the Commissioner may register a non-resident person that is not liable to register under section 23(1) if the Commissioner is satisfied that the person meets the following requirements:
- (a) the person-
- (i) is registered for a consumption tax in an export country in which it is resident; or
 - (ii) if the export country in which the person is resident does not have a consumption tax, or has a consumption tax that does not apply to the person's activities, is carrying on an enterprise, and has a level of taxable activity in a country or territory that would require it to be registered under section 23(1) if it carried on the enterprise in the Republic; and
- (b) the amount of the person's input tax for the first tax period after the date of registration in the Republic is likely to exceed R10 000⁵³¹; and
- (c) the person's enterprise does not involve the rendering of services that are reasonably foreseeable to be received in the Republic by a person who is not a vendor; and
- (d) the person is not carrying on an enterprise in the Republic, or intending to carry on an enterprise in the Republic.

⁵³⁰ The proposed section 23(1B) is an adaptation of section 54B of the New Zealand GST Act, 1985.

⁵³¹ New Zealand fixed this amount at \$500, which as a ratio to its compulsory registration threshold of \$60 000, equates to 0.83%. Applying the 0.83% to the R1000 000 compulsory registration threshold amounts to R8 333, which rounded to the nearest R10 000, amounts to R10 000. This amount needs to be set to ensure the compliance burden for SARS does not outweigh the refund.

(2) If a non-resident person that is not registered under this section commences making taxable supplies, it is deemed to be registered on the date specified by the Commissioner under subsection (1), and not from the date on which it commences making taxable supplies.

7.3.8 Fixed or permanent place

The VAT Act defines “resident of the Republic” in section 1(1) to include:

...any other person...to the extent that such person...carries on in the Republic any enterprise or other activity and has a *fixed or permanent place* in the Republic relating to such enterprise or other activity (own emphasis)

The VAT Act does not define “fixed or permanent place”. A definition of a “fixed or permanent place”⁵³² should be inserted into section 1(1) as follows:

Fixed or permanent place for purposes of the definition of “resident of the Republic” includes a place or facility where (or through which) a person:

- (a) carries on a business that has a permanent presence in the form of personnel and technical resources required to make supplies, where those supplies cannot be linked with the supplier’s principal place of business;
- (b) carries on a business through a dependent agent that acts on behalf of that person (other than through an independent agent);
- (c) uses or installs equipment or machinery;
- (d) engages in a construction project;
- (e) sells goods manufactured, assembled, processed, packed or distributed by another person for, at, or to the first-mentioned person and one of them or another person participates in the management, control or capital of the other;
- (f) manufactures, assembles, processes, packs or distributes goods; and

⁵³² The proposed definition of “fixed or permanent place” is adopted from the definitions of permanent establishment used in Australia, Canada, and the European Union.

(g) includes a place of management, branch, office, factory or workshop, and a mine, oil or gas well, a quarry, timberland or place of extraction of natural resources.

7.3.9 Supplies of foreign land by way of sale or lease

The VAT Act exempts supplies of foreign land by way of sale or lease, thereby disallowing the benefits associated with zero-rated supplies⁵³³. This exemption does not adhere to the destination principle and is inequitable when compared to the zero rating of goods or services destined for consumption outside of South Africa. Section 14 of New Zealand Goods and Services Tax Act, 1985 (GST Act, 1985), which deals with exempt supplies, does not contain a similar exemption. In fact, sections 11A(1)(e) and 11A(1)(f) of the GST Act zero rate services supplied directly in connection with land (or any improvement thereto) or movable property, respectively, situated outside New Zealand. Section 11(2)(f) of the South African VAT Act contains a similar zero rating provision.

The VAT Act should be amended to remove the exemption that applies to supplies of foreign land by way of sale or lease, by deletion of section 12(e)⁵³⁴ as follows:

[(e) the supply of land (together with any improvements to such land existing on the date on which the supplier became contractually obliged to supply such land and such existing improvement to the recipient) where such land is situated outside the Republic and such supply is made by way of sale or by way of letting;]

⁵³³ SARS general written VAT Ruling 419, withdrawn on 1 August 2009.

⁵³⁴ The legislator could consider introducing an option to the supplier of the foreign land, similar to that contained in section 12(k) of the VAT Act, to have the exemption apply or not.

7.4 IMPORTED SERVICES

VAT generally places a heavier compliance burden on non-resident than on resident suppliers (OECD, 2014c:8). In the case of imported services, reverse charging should also apply to business-to-business internationally traded services and intangibles that are taxable in the jurisdiction where the customer is located, where it is consistent with the overall VAT design. This minimises the administrative burden and complexity for non-resident suppliers, shifts the tax burden from the supplier to the customer, and relieves the non-resident supplier of foreign VAT obligations (OECD, 2014c:8).

It is understood that the State and governmental bodies in South Africa may not all account for and pay over VAT on imported services, where they are supposed to do so (van Heerden, 2012). Whether this is done inadvertently through a lack of effective policing or through an internal policy applied by SARS and/or National Treasury is uncertain. As the State and governmental bodies presumably account for a substantial portion of domestic expenditure, which would include the importation of services, such non-compliance could have a substantial impact on the effectiveness of the VAT system and could also distort price competitiveness between non-resident and local suppliers. It is a commonly accepted principle that a VAT system is most effective with the fewest exceptions or the least incidences of non-compliance.

SARS should actively enforce compliance by the State and governmental bodies with the imported services legislation, which, if not complied with, should be subject to penalties and interest. Alternatively, the legislator should revise the policy and VAT Act in this regard in a neutral manner which adheres to the OECD consumption tax principles⁵³⁵.

⁵³⁵ The Auditor General of South Africa's (AGSA's) *Consolidated general report on national and provincial audit outcomes (2014-2015 PFMA)* (November 2015) issued SARS with an *unqualified with no findings* report. SARS could itself be partly liable to account for VAT on imported services and is also responsible for administering the VAT Act as it applies to all vendors and persons that should account for VAT on imported services, including the State and governmental bodies.

Reverse charging is generally not an effective instrument to collect tax on cross-border business-to-consumer supplies as levels of compliance are low (OECD, 2014c:9). The most effective approach is to require the non-resident supplier to register for VAT in the foreign tax jurisdiction. A simplified registration and compliance regime can aid compliance by non-resident suppliers (OECD, 2014c:9).

In South Africa many transactions escape the VAT net due to non-compliance or under-reporting of VAT on imported services. A number of countries (including some in the European Union and Australia) (see also Chapter 6) apply the reverse charge mechanism successfully to business-to-business transactions (Van Zyl, 2013a). This is done by requiring domestic VAT vendors to account for output tax in full on imported services and allowing an input tax deduction to the extent that the services will be used to make taxable supplies. This can be fairly easily achieved in the South African VAT Act by amending the definition of “imported services” in section 1(1) of the VAT Act as follows:

“imported services” means a supply of services that is made by a supplier who is resident or carries on business outside the Republic to a *[recipient] person [who is a resident of the Republic to the extent that such services are utilized or consumed in the Republic otherwise than for the purposes of making taxable supplies]*

The definition of “input tax” in section 1(1) of the VAT Act would need to be amended as follows:

“input tax”, in relation to a vendor, means-

- (a) tax charged under section 7 and payable in terms of that section by-
 - (i) ...;
 - (ii) ...; *[or]*
 - (iii) ...; or
 - (iv) the recipient of imported services

7.5 INTENTION OF THE LEGISLATOR

The VAT Act does not contain a general rule that clarifies that the South African VAT system seeks to tax final domestic consumption. Section 1(3)⁵³⁶ should be inserted into the VAT Act, following section 1(2) as follows:

1(3) This Act levies a tax on final utilisation or consumption that occurs in the Republic, imposed under the destination principle of taxation which seeks to tax importation and free exportation from tax.

The use in the VAT Act of the concepts “utilised” or “consumed” and their derivatives (such as use or consume) creates interpretational difficulty. The word “utilised” is defined as “the action of making practical and effective use of something” or “the use of something”, whereas the word “consumption” is defined as “the action of using up a resource”, “an amount of something which is used up or ingested”, or “the act of using, eating, or drinking something”. Various dictionaries indicate “utilised” and “consumed” as synonyms⁵³⁷.

To address this shortcoming in the VAT Act, a definition of “utilised or consumed” should be included into section 1(1) of the VAT Act as follows:

Utilised or consumed, shall be used interchangeably, and the terms and any derivatives thereof, shall include the action of making use of something or the action of using up a resource

⁵³⁶ The proposed section 1(3) is adopted from the work of the OECD (2014c:23-24).

⁵³⁷ Cambridge Dictionaries Online accessed on 21 March 2016 at <http://dictionary.cambridge.org/dictionary/english/in-respect-of-sth>; and Oxforddictionaries.com accessed on 21 March 2016 at http://www.oxforddictionaries.com/definition/english-thesaurus/respect?q=in+respect+of#in_respect_of).

7.6 PLACE OF SUPPLY RULES

Internationally traded goods do not pose significant problems as supplies of movable and immovable goods are deemed to be supplied and consumed at the place of location of the goods when the supply is made. Internationally traded services and intangibles, on the other hand, often present problems in determining where consumption takes place.

The place of supply of goods that are made available, removed, installed or assembled, is generally deemed to be where the goods are made available, removed, installed, or assembled. Canada deems the supply of goods not by way of a sale to be where possession in the goods is given or made available. The European Union deems the supply of goods not dispatched or transported to be where the goods are located at the time of supply. If goods are dispatched or transported, the European Union deems the place of supply to be where the dispatch or transport of the goods begins. Goods sold on ships, aircraft, or trains are deemed to be supplied where the passenger transport begins. Goods supplied through distribution systems are deemed to be supplied at the supplier's business or fixed establishment or permanent address or usual residence or at customer's permanent address or usual residence. The place of supply of real property is generally deemed to be the where the real property is located.

New Zealand's general place of supply of goods and services rule deems goods and services supplied by residents to be in New Zealand and if supplied by non-residents to be outside New Zealand, irrespective of the physical place of supply⁵³⁸. Supplies of goods and services in New Zealand by a non-resident to a registered person for use in its taxable activity are deemed to be supplied outside New Zealand⁵³⁹, unless the supplier and recipient elect for it to be deemed to be supplied in New Zealand⁵⁴⁰. Supplies by a non-resident of goods and services outside New Zealand are deemed to be outside New Zealand⁵⁴¹.

⁵³⁸ Section 8(2) of the GST Act.

⁵³⁹ Section 8(3) (a) of the GST Act.

⁵⁴⁰ Section 8(4) of the GST Act.

To address the lack of place of supply of goods and services rules in the VAT Act a number of law changes are required. The place of supply “anchor” in the VAT Act should be the charging section, namely section 7(1)(a). To incorporate place of supply rules and use the charging section as an anchor, section 7(1)(a) of the VAT Act should be amended⁵⁴² as follows:

(1)(a) on the supply in the Republic by any vendor of goods or services supplied by him on or after the commencement date in the course or furtherance of any enterprise carried on by him;

7.6.1 General place of supply rule

A general place of supply rule in respect of goods and services should be inserted into the VAT Act in relation to which exceptions and deviations could be introduced. A general place of supply rule, section 7(1A), should be introduced into the VAT Act, following section 7(1)⁵⁴³, as follows:

7(1A) Goods and services shall be deemed to be supplied in the Republic if the supplier is a resident of the Republic, and shall be deemed to be supplied outside the Republic if the supplier is a non-resident.

7.6.2 Main exception to the general rule

The most important exception to the general place of supply rule should cater for supplies where it is obvious from the nature of the supply that it cannot merely follow the general place of supply rule. Supplies which by their nature potentially warrant a treatment that differs from the main place of supply rule include the supplies of goods which are in the Republic at the time of supply, and services physically rendered by a person who is in the Republic at the time the services are rendered.

⁵⁴¹ Section 8(3)(a) of the GST Act.

⁵⁴² Following an adaptation of section 8(1) of the New Zealand GST Act, 1985.

⁵⁴³ Following an adaptation of section 8(2) of the New Zealand GST Act, 1985.

The main exception to the general place of supply rule, section 7(1B), should be introduced into the VAT Act, following section 7(1A)⁵⁴⁴, as follows:

7(1B) Notwithstanding section 7(1A), goods and services shall be deemed to be supplied in the Republic if the supplier is a non-resident and-
(a) the goods are in the Republic at the time of the supply; or
(b) the services are physically rendered⁵⁴⁵ in the Republic by a person who is in the Republic at the time the services are rendered⁵⁴⁶.

7.6.3 Narrowing of the main exception to the general rule

A number of countries and country groupings such as the OECD, EU, and New Zealand have designed their place of supply rules by differentiating between business-to-business and business-to-consumer supplies. This differentiation then often allows them to keep non-resident suppliers who make business-to-business supplies out of the VAT net. In addition, many countries further differentiate between supplies of goods made in the country and services physically rendered in the country, and other supplies of goods and services.

The width of the main exception is such that it could require many non-resident persons to register for VAT purposes in South Africa. This could create a substantial compliance burden on non-resident persons and also on the tax administration. To address the impact on compliance, the application of the main exception should be

⁵⁴⁴ Following an adaptation of section 8(3) of the New Zealand GST Act, 1985.

⁵⁴⁵ The EU has special place of supply rules for restaurant and catering services, and for cultural, artistic, sporting, scientific, educational, entertainment or similar events, such as fairs and exhibitions, and ancillary services, including supplies of services by the organisers, which deem the place of supply to be where the activities are actually carried out or the events actually take place.

⁵⁴⁶ This rule would give effect to the EU's place of supply rules in respect of goods and passenger transportation services; ancillary transport activities and valuations of and work on movable tangible property; services connected with immovable property; hiring of a means of transport services (other than short-term); and hiring of pleasure boats, (other than short-term hiring), which effectively deems the place of supply to be where the services take place or are physically carried out or where the services are put at the disposal of the customer.

narrowed, with the caveat that such narrowing should not negatively impact revenue collections. This should be done by limiting the application of the main exception to exclude supplies made by non-residents to vendors who use such goods or services to make taxable supplies. This will effectively subject business-to-consumer supplies to taxation and exclude business-to-business supplies from taxation. The non-resident suppliers should be entitled, if this is done in agreement with the local recipient vendor, to retain the option for this exclusion not to apply. To narrow the application of the main exception without reducing revenue collections, section 7(1C) should be introduced into the VAT Act, following section 7(1B)⁵⁴⁷, as follows:

7(1C) Notwithstanding section 7(1B), if a non-resident supplier supplies goods and services to which section 7(1B) would apply, but for this section, to a vendor for the purposes of carrying on the vendor's enterprise, the goods and services are deemed to be supplied outside the Republic, unless the supplier and the recipient of the supply agree that this section will not apply to the supply.

7.6.4 De minimus rule

To limit tax leakage, a *de minimus* rule should be introduced. Section 7(1D) should be introduced into the VAT Act, following section 7(1C)⁵⁴⁸, as follows:

7(1D) Notwithstanding section 7(1B), a supply of services that is not deemed to be made in the Republic by sections 7(1B)(b) or 7(1C) is deemed to be made in the Republic if-

- (a) the services are supplied by a non-resident to a resident;
- (b) the intended use by the recipient of the supply in the course of making taxable supplies is less than 95% of the total intended use;

⁵⁴⁷ Following an adaptation of section 8(4) of the New Zealand GST Act, 1985.

⁵⁴⁸ Following an adaptation of section 8(4B) of the New Zealand GST Act, 1985.

(c) the supply would be a taxable supply if made in the Republic by a vendor in the course or furtherance of an enterprise carried on by the vendor.

7.6.5 Electronic services, broadcasting services, and telecommunication services

To address the lack of “place of supply” rules in respect of electronic services, broadcasting services, and telecommunication services in the VAT Act a number of law changes are required. As electronic services, broadcasting services, and telecommunication services do not constitute the supply of goods or the supply of services physically rendered, the general place of supply rules outlined in the proposed sections 7(1B), 7(1C), and 7(1D) would not find application. Section 7(1E) should be introduced into the VAT Act, following section 7(1D)⁵⁴⁹, as follows:

7(1E) Sections 7(1B), 7(1C), and 7(1D) do not apply to supplies of electronic services, broadcasting services, and telecommunication services.

Due to the unique nature of supplies of electronic services, broadcasting services, and telecommunication services, the general place of supply rule contained in the proposed section 7(1A) would not deal with these supplies if they are initiated in the Republic. Section 7(1F) should be introduced into the VAT Act, following section 7(1E)⁵⁵⁰, as follows:

7(1F) Notwithstanding section 7(1A), electronic services, broadcasting services, and telecommunication services supplied by a non-resident are deemed to be supplied in the Republic if a person, physically in the Republic, initiates the supply from an electronic services supplier, a broadcasting services supplier, or a telecommunication supplier.

⁵⁴⁹ Following an adaptation of section 8(5) of the New Zealand GST Act, 1985.

⁵⁵⁰ Following an adaptation of section 8(6) of the New Zealand GST Act, 1985.

whether or not the person initiates the supply on behalf of another person⁵⁵¹.

To increase legislative certainty, in applying the proposed sections 7(1F) and 11(2)(y) of the VAT Act, section 7(1G)⁵⁵² should be introduced into the VAT Act, as follows:

7(1G) For the purposes of section 7(1F) and section 11(2)(y), the person who initiates a supply of electronic services, broadcasting services, or telecommunication services is the person who-

- (a) is identified by the supplier as the person who-
 - (i) controls the commencement of the supply;
 - (ii) pays for the services;
 - (iii) contracts for the supply; and
- (b) if paragraph (a) applies to more than one person, the person who satisfies the requirements of paragraph (a)(i) or, failing that, (a)(ii), and failing that, (a)(iii).

The place of supply rules applicable to non-resident suppliers who initiate supplies of electronic services, broadcasting services, and telecommunication services

⁵⁵¹ The telecommunication services place of supply rules used in Canada are also of interest. The place of supply is deemed to be in Canada if payment is for a terminal or station situated in Canada. The place of supply of long distance telephone charges is in Canada if two or more of the following three places are in Canada: (i) the place of origin; (ii) the place of termination; and (iii) the billing location. The billing location of a telecommunication service is in Canada if the consideration charged or applied to the recipient's account is from a business that supplies telecommunication services and the account relates to a telecommunications facility used (or available for use) by the recipient to obtain telecommunication services, and the telecommunications facility is ordinarily located in Canada. In any other case, the telecommunications facility which initiates the service is located in Canada. Irrespective of the above, a supply of a telecommunication service is in Canada if it comprises the making available of telecommunications facilities that are (or part thereof of are) located in Canada. In any other case, the supply is in Canada if the telecommunication is emitted and received in Canada, or the telecommunication is emitted or received in Canada and the billing location is in Canada.

⁵⁵² Following an adaptation of section 8(9) of the New Zealand GST Act, 1985.

physically from such suppliers in the Republic should *not apply* to supplies between suppliers belonging to such categories. To *exclude these supplies*, section 7(1H) should be introduced into the VAT Act, following section 7(1G)⁵⁵³, as follows:

7(1H) Section 7(1F) does not apply to supplies made between:

- (a) electronic services suppliers; or
- (b) broadcasting services suppliers; or
- (c) telecommunication suppliers⁵⁵⁴.

To reduce the compliance burden, the place of supply rules for electronic services, broadcasting services, and telecommunications services should generally only apply to business-to-consumer supplies and should exclude business-to-business supplies from taxation. The non-resident suppliers can, if this is done in agreement with the local recipient vendor, retain the option for this exclusion not to apply. To narrow the application of the main exception without reducing revenue collections, section 7(1I) should be introduced into the VAT Act, following section 7(1H)⁵⁵⁵, as follows:

7(1I) Notwithstanding section 7(1F) and section 7(1J), electronic services, broadcasting services, or telecommunication services supplied by a non-resident to a vendor for the purposes of carrying on the vendor's enterprise are deemed to be supplied outside the Republic, unless the supplier and recipient of the services agree that this section will not apply to the supply⁵⁵⁶.

The VAT Act should cater for situations where the application of section 7(1F) is not possible due to the practical problem for the supplier of determining the physical location of a person as a result of the type of service or class of customer. As a

⁵⁵³ Following an adaptation of section 8(4) of the New Zealand GST Act, 1985.

⁵⁵⁴ Following an adaptation of section 8(7) of the New Zealand GST Act, 1985.

⁵⁵⁵ Following an adaptation of section 8(4) of the New Zealand GST Act, 1985.

⁵⁵⁶ Following an adaptation of section 8(8) of the New Zealand GST Act, 1985.

result, the VAT Act should be amended to introduce section 7(1J)⁵⁵⁷ into the VAT Act, as follows:

7(1J)(1) Notwithstanding section 7(1A), if an electronic services supplier, a broadcasting services supplier, or a telecommunication supplier cannot apply section 7(1F) because it is impractical for the supplier to determine the physical location of a person due to the type of service or class of customer, the supply of the electronic services, broadcasting services or telecommunication services is deemed to be made in the Republic, if the person's address for receiving invoices from the supplier is in the Republic.

(2) Subsection (1) does not apply to supplies made between:

- (a) electronic services suppliers; or
- (b) broadcasting services suppliers; or
- (c) telecommunication suppliers.

(3) If subsection (1) applies, the electronic services supplier, broadcasting services supplier, or telecommunication supplier must satisfy subsection (1) for all supplies of electronic services, broadcasting services, or telecommunication services, respectively, made for the type or class of customer.

(4) In this section, "address" means the physical residential or business address of the person to which invoices are sent, and does not include a post office box number.

Due to the uniqueness of the nature of electronic, broadcasting, and telecommunication supplies, a specific zero rating provision should be introduced into the VAT Act to zero rate these supplies if made to non-resident suppliers by resident suppliers or supplies made by resident suppliers, if the services are initiated

⁵⁵⁷ Following an adaptation of section 8A of the New Zealand GST Act, 1985.

outside the Republic. As a result, the VAT Act should be amended to introduce section 11(2)(y)⁵⁵⁸ into the VAT Act, as follows:

11(2)(y) electronic services, broadcasting services, or telecommunication services supplied to a-
(a) non-resident electronic, broadcasting, or telecommunication services supplier by a resident electronic, broadcasting, or telecommunication supplier; or
(b) resident electronic, broadcasting, or telecommunication supplier, for an electronic, broadcasting, or telecommunication service that is initiated outside the Republic in terms of section 7(1G).

7.7 SUMMARY

This chapter consolidates the research findings of chapters 2 – 6 and uses the findings in these chapters to propose changes to current legislation and suggest new legislation to address the VAT treatment of inter-jurisdictional activities and supplies in the South African VAT system. This study does not only consider place of supply rules in the narrow sense but looks wider into the VAT treatment of activities and supplies spanning the borders of South Africa. The two underlying aspects which underpin cross-border consequences in the VAT system are considered in detail, namely activities of non-resident persons with a South African “reach” or “connection”, particularly if consumption takes place in South Africa. Secondly, the study considers the VAT rate applicable to cross-border supplies. If the legislative amendments recommended in this chapter are considered by the legislator and to the extent that the legislator accepts the proposed legislation in full or in part, the amendments would follow the normal legislative process, namely publication of a Taxation Laws Amendment Bill for commentary and final enactment. The legislative process could be preceded by a workshop/s facilitated by the writer of this thesis and attended by the legislator and other stakeholders, during which the rationale for and detail of the proposals are explained and discussed. The proposed

⁵⁵⁸ Derived from an adaptation of section 11AB of the New Zealand GST Act, 1985.

changes and additions to the VAT Act in this regard are summarised below.

7.7.1 Non-resident VAT registration

A study of the impact of inter-jurisdictional supplies or activities would be incomplete without a comprehensive consideration of how non-residents are treated for VAT purposes. This chapter proposed changes to the VAT Act to enhance legislative certainty.

Dependent Agents

The concept of agent is important in any VAT system as supplies by and the activities of an agent could be attributed to a principal. To enhance legislative clarity the recommended changes put it beyond doubt that a dependent or binding agent (as opposed to independent agent) could create an enterprise, through specific inclusion in the definition of enterprise. The concept is also defined and provision made for certain situations to allow activities that a dependent agent assumes on behalf of a principal to be accounted for by the agent.

Foreign branch or main business

Non-resident persons can conduct their activities through branches or main businesses, and a number of provisions in the VAT Act cater specifically for these taxpayers. To enhance legislative certainty, definitions are proposed for concepts such as “separately identified” and “independent system of accounting”. To address uncertainty relating to the VAT rate, it is proposed that branches or main businesses are treated as separate persons and assume opposing residence statuses. The effect is that if a branch and main business (or other branch) are treated as separate persons for VAT purposes, they will not share the same “residence” status. If the one “person” is a “resident of the Republic”, the other “person” will be a “non-Resident”. In addition, it is proposed that supplies made in South Africa that partly comprise of components sourced from outside South Africa, be deemed to be part of the final supply in South Africa.

Internationally traded services and intangibles

The VAT treatment of goods traded cross-border is generally straight forward. To reduce compliance and streamline the VAT consequences, it is proposed to deem that non-resident suppliers of intangible property to fully taxable vendors do not carry on an enterprise. In addition, to increase interpretative certainty, a definition of “enterprise or activity” as envisaged by the definition of enterprise is proposed.

Foreign underwriting insurance business

The VAT Act does not cater for non-resident insurers other than for Underwriting Members of Lloyd’s of London (UMAs) (binder business). UMAs of Lloyd’s of London that conduct binder business in South Africa conduct an enterprise to the extent that contracts of insurance are signed in South Africa. To ensure fair treatment with regard to other non-resident insurers, it is proposed that they also conduct enterprises to the extent that contracts are concluded in South Africa.

Electronic services, telecommunication services, broadcasting services

In 2014 the legislator introduced VAT legislation in respect of certain non-resident suppliers of electronic services which seeks to tax local consumption. The changes did not extend to non-resident telecommunication or broadcasting service suppliers. These three classes of service conceptually pose similar challenges for VAT purposes, which can be addressed through similar changes to the VAT system. As the South African VAT legislation already caters for non-resident suppliers of electronic services, potential shortcomings and gaps in this regard are addressed as a first step, followed by a widening of the VAT net to include telecommunication and broadcasting services supplied by non-resident suppliers, to the extent that consumption takes place in South Africa. With regard to electronic services supplied by non-residents in South Africa, the following specific proposals are made to enhance legislative certainty or increase neutrality:

- aligning the registration threshold for foreign electronic service suppliers with that of local suppliers;

- requiring non-resident electronic service suppliers to apply the invoice basis of accounting for VAT to bring them into line with domestic suppliers of electronic services;
- excluding supplies to recipients in a “group of companies” (as defined for Income Tax purposes) from the ambit of the electronic services provisions as these are not typically and commercially provided on the same footing as electronic services;
- differentiating between business-to-business and business-to-consumer supplies and only seeking to legislate to tax business-to-consumer supplies in terms of the recently introduced electronic services provisions;
- adopting a *de minimus* rule (for example, 95 per cent or more) to allow non-resident electronic service suppliers whose business-to-business supplies in relation to total supplies are equal to or exceed the *de minimus* threshold not to register for VAT purposes;
- addressing definitional shortcomings;
- excluding from the ambit of “electronic services”, supplies that include the provision of rights (e.g. technical know-how) or if rights are supplied, they are incidental to the supply; and
- excluding from the ambit of “electronic services” supplies that involve specific work performed by a person for a specific customer.

It is further proposed to subject to VAT telecommunication services supplied by non-residents which are utilised or consumed in South Africa and that these suppliers’ activities should be included in the definition of “enterprise”. Enabling legislation requires that concepts such as telecommunication services, telecommunication supplier, telecommunication content, telecommunication facility, telecommunication network, be defined. In addition, it is proposed to include broadcasting services supplied by non-residents that are utilised or consumed in South Africa in the definition of “enterprise”. As a result, “broadcasting services” is defined.

Goods imported on behalf of foreign principal

The VAT Act does not effectively cater for consignment goods supplied by a non-resident to a resident to the extent that the non-resident does not have any other

activities or supplies in South Africa. In this regard, the following proposals are made:

- addressing a local consignee's entitlement to claim VAT incurred on importation as an input tax deduction where the consignment agreement is continuous;
- amending section 54(2A) (b) of the VAT Act to address its current shortcomings, to allow a non-resident person that is not a registered vendor to apply in writing to the Commissioner not to have an enterprise; and
- permitting a foreign enterprise or consignor not to register as a vendor if it solely supplies goods on consignment to a consignee in the Republic.

Obiter dicta

The study also revealed certain potentially problematic areas identified by the respondents to the questionnaire as being in need of addressing, although the researcher did not necessarily see the need for this. These include whether:

- a foreign enterprise can have more than one branch or main business in South Africa;
- a foreign consignor would create a VAT "enterprise" in South Africa in consequence of ownership in goods passing whilst in South Africa;
- a foreign enterprise with activities in South Africa purely to enable the making of supplies outside South Africa creates an "enterprise" for VAT purposes;
- a foreign supplier who enters South Africa for a once-off predetermined time period to make a supply or supplies would create a VAT "enterprise";
- a "sale" of goods made by a non-resident whilst the goods are outside South Africa with delayed transfer of ownership, could create an "enterprise" for the non-resident; and
- the introduction of inter-jurisdictional VAT rules to narrow the obligation of foreign entities to register for VAT in South Africa to activities carried on within South Africa from a fixed or permanent place of business in South Africa, if such rules would not create a loss of revenue for the State.

7.7.2 Inter-jurisdictional VAT rate

In addition to a consideration of how non-residents are treated for VAT purposes, inter-jurisdictional VAT rules are significantly impacted by the VAT rate that applies. This section of the chapter proposes changes to the law to enhance legislative certainty in this regard.

Double taxation agreements

The legislator could consider implementing a model similar to the OECD Model that applies to VAT. The purpose of such implementation would be to reach agreement with the country with which trading takes place, to avoid double or non-taxation.

Services to non-residents outside South Africa

The main section relied upon to zero rate services supplied to non-resident is section 11(2)(l) of the VAT Act. To enhance legislative certainty and curtail abuse, the following changes to section 11(2)(l) are proposed:

- defining “directly in connection with”;
- changing “the services are supplied to a person” to “the services are *contractually* supplied to a person”;
- clarifying the meaning of “directly to” the person or any other person, by “effectively” connecting the persons with the supply and ensuring that they are the recipients of the supply;
- clarifying that the zero rate will not apply to services supplied to an employee or director of the “said person”; and
- clarifying that the zero rate will not apply if the other person intends to use the services received to make taxable or exempt supplies.

Services supplied directly in respect of goods or movable property exported or destined for export

The phrase “directly in respect of” only occurs once in the VAT Act, namely in section 11(2)(g). The phrase “directly in connection with” is used more commonly in the VAT Act. These phrases literally mean more or less the same thing, but their

arguably interchangeable use may create confusion. As a result, it is proposed that the phrase “directly in respect of” be replaced with “directly in connection with” to enhance certainty and create conformity.

Services physically rendered outside the Republic

The study observed two technical or interpretative issues in applying section 11(2)(k) of the VAT Act in practice, namely (i) the meaning of the phrase “physically rendered”; and (ii) SARS’ disallowance of the zero rate if the supplier sub-contracts the provision of the services to be rendered elsewhere than in the Republic. The following proposals are made:

- clarifying that the zero rate extends to the arranging of services that are physically rendered elsewhere than in the Republic; and
- to enhance clarity and interpretation, the legislator could review the VAT Act to ensure a more consistent use of the terms and “performed” and “rendered” and their derivatives.

Foreign branch or main business

The VAT Act does not cater effectively for the application of the zero rate to foreign branches or main businesses with local activities. It is proposed that this should be addressed by introducing a clearly articulated definition of “non-resident” into the VAT Act which excludes the activities of the local branch or main business.

Non-resident refunds

The South African VAT system does not refund non-resident businesses the VAT incurred in South Africa in respect of consumption that would effectively take place outside of South Africa. New Zealand’s GST Act was changed with effect from 1 April 2014 to allow non-residents who do not carry on a VAT enterprise in New Zealand and do not provide services to non-vendors, to claim back tax in certain instances. It is proposed that a similar provision should be included in the VAT Act.

Fixed or permanent place

The VAT Act defines “resident of the Republic” with reference to a fixed or permanent place in the Republic relating to such enterprise or other activity, but

does not define what is meant with “fixed or permanent place”. This creates uncertainty. A definition of “fixed or permanent place” is proposed.

Supplies of foreign land by way of sale or lease

The VAT Act exempts supplies of foreign land by way of sale or lease. This is contrary to the destination principle and the overall design of the South African VAT system. It is proposed that this exemption be deleted.

7.7.3 Imported Services

The OECD recommends that imported services (reverse charging) should apply to business-to-business internationally traded services and intangibles that are taxable in the jurisdiction where the customer is located, where it is consistent with the overall VAT design. Reverse charging is generally not an effective instrument to collect tax on cross-border business-to-consumer supplies as compliance is low. The most effective approach is to require the non-resident supplier to register for VAT in the foreign tax jurisdiction. The State and governmental bodies in South Africa may not all account for VAT on imported services, although they are required to do so. It is proposed that SARS should actively enforce compliance. The legislator could, in the alternative, revise the policy and VAT Act in this regard in a neutral manner. South Africa should apply the reverse charge mechanism to business-to-business transactions and require domestic VAT vendors to account for output tax in full on imported services and permit an input tax deduction, to the extent that the services will be used to make taxable supplies.

7.7.4 Intention of the legislator

The VAT Act does not contain specific provisions which make it clear that the intention of the legislator is to tax final utilisation or consumption in South Africa in the VAT Act. To enhance certainty it is proposed that such intention be inserted into the VAT Act. It is also proposed that the concepts of “utilised or consumed” be clearly defined.

7.7.5 Place of supply rules

Internationally traded goods do not pose significant problems as supplies of movable and immovable goods are deemed to be supplied and consumed at the place of location of the goods when the supply is made. Internationally traded services and intangibles, on the other hand, often present problems in determining where consumption takes place. Incorporating place of supply rules and using the charging section as an anchor, section 7(1)(a) of the VAT Act should be amended. Schenk's classification of worldwide and territorial VAT systems as highlighted in Chapters 1 and 2 could be indicative that the South African VAT system would be moving away from the worldwide VAT system towards a territorial system, if the recommendations of this study are implemented, particularly as they relate to "resident" and "non-resident" to define the VAT scope. It is submitted New Zealand's VAT system also moved closer to a territorial VAT system.

General place of supply rule

It is proposed that a general place of supply rule for goods and services linked to residency status be introduced into the VAT Act. A main exception to the general place of supply rule should be introduced to cater for supplies where it is obvious from their nature that they cannot merely follow the general place of supply rule. Such supplies include the supplies of goods which are in South Africa at the time of supply, and services physically rendered by a person who is in South Africa at the time the services are rendered. The place of supply of these supplies should be deemed to be in South Africa. The main exception should be to exclude supplies made by non-residents to vendors that will use such goods or services to make taxable supplies, which will effectively subject business-to-consumer supplies to taxation and exclude business-to-business supplies from taxation. The non-resident suppliers should be entitled to retain the option for this exclusion not to apply. To limit tax leakage, a *de minimus* rule should be introduced.

Electronic services, broadcasting services and telecommunication services

Due to the unique nature of supplies of electronic services, broadcasting services, and telecommunication services it is proposed that these services be excluded from

the general place of supply rules. It is proposed that the general place of supply of these services supplied by a non-resident is in South Africa if a person, physically in South Africa, initiates the supply from such suppliers, whether or not the person initiates the supply on behalf of another person. This requires defining the person who initiates such services. It is further proposed to narrow the place of supply rules applicable to non-resident suppliers who initiate supplies of these services physically from such suppliers in South Africa, to exclude supplies between suppliers belonging to such categories. To reduce the compliance burden, the place of supply rules for these services should generally only apply to business-to-consumer supplies and should exclude business-to-business supplies. These non-resident suppliers should still have the option for this exclusion not to apply. The VAT Act should cater for the impracticality of determining the physical location of a person, as a result of the type of service or class of customer, by deeming such supplies to take place in South Africa if the person's address for receiving invoices from the supplier is in South Africa. Due to the uniqueness of the nature of these supplies, a specific zero rating provision should be introduced into the VAT Act to zero rate these supplies, if they are made to non-resident suppliers by resident suppliers or are supplies made by resident suppliers, if the services are initiated outside South Africa.

7.7.6 Concluding remarks

This chapter considered the research findings of chapters 4 – 6. This was done to achieve the ultimate objective of this research as set out in Chapter 1, namely to consider the current inter-jurisdictional rules in the South African VAT system, identify current shortcomings, and propose legislative changes or additions to address these shortcomings, in line with the “Problem Statement” in Chapter 2 and in adherence to “Research Method” formulated in Chapter 3. This chapter specifically addressed one of the sub-goals articulated in Chapter 1, namely to provide the legislator with specific technical and practical recommendations addressing the following:

- non-resident VAT registration;

- the inter-jurisdictional VAT rate;
- imported services; and
- the place of supply rules.

The next chapter, Chapter 8, concludes the study by highlighting:

- the theoretical constructs, the research methodology, and the research implications of the study;
- the findings and conclusions of the study, specifically those contained in this chapter; and
- the contribution of the study, its limitations, and considering the way forward.

CHAPTER 8: CONCLUSION

8.1 INTRODUCTION

This chapter provides a conclusion for the study. The study considered the inter-jurisdictional VAT rules in place in South Africa with a view to identifying shortcomings and to recommending solutions to address these shortcomings. The study was not confined to a consideration of only so-called “place of supply”, rules but extended to a more holistic consideration of most inter-jurisdictional rules in the South African VAT system.

8.2 IDENTIFYING AND DEFINING THE THEORETICAL CONSTRUCTS

Theory in research is very important as research requires a sound theoretical basis and strong methodology (Udo-Akang, 2012:89-97). Theory is important for three reasons, namely (a) it provides a framework for analysis; (b) it provides an efficient method for field development; and (c) it provides a clear explanation for the pragmatic world (Wacker, 1998:361-385). Theories should describe and explain a phenomenon effectively, should place a limit on what would be examined, and should be highly generative and heuristically stimulate further research or investigation (Gelso, 2006).

In Chapter 4 an in-depth discussion was presented of the theoretical basis of a good tax system and, in particular, the principles to which a consumption tax should adhere. The following guiding principles for the present research were established:

- neutrality;
- efficiency;
- certainty and simplicity;
- effectiveness and fairness; and
- flexibility.

The inter-relatedness between theory, practice, and research is central to the discussion of theory as a conceptualised cycle of development and facilitation

(Wacker, 1998), and the one directs the other (Usha, 2007). Thus the theoretical construct underlying the present research guided the practical collection of the data, their analysis and interpretation, in a cycle designed to develop recommendations flowing from the research. The conceptualisation of theoretical constructs can be approached by either using a “theoretical”, or by using an “operational” or “observational” approach. The theoretical approach starts from a “theoretical construct” which is defined in a particular manner, which is then “operationalised” and subsequently measured on that basis. The observational approach starts with observations or measurements and subsequently attempts to relate these to each other in terms of “models” or “functions”, within a particular empirical domain. These two approaches need to be synthesised by explicating the theoretical constructs to enable the operationalization of the construct which is closely linked to the definition of the construct itself (Middendorp, 1991:235-252). This study used a synthesised approach and identified and defined the theoretical constructs of the inter-jurisdictional VAT rules in South Africa, informed by a description of the theory of taxation, specifically consumption taxation, the inter-jurisdictional VAT rules used in Australia, Canada, New Zealand, and the European Union, and the principles formulated by the Organisation for Economic Cooperation and Development in this regard.

Research must be used to collect and analyse new information and data that will enhance the body of knowledge (Ellis and Levy, 2008:18-33). It is submitted that this thesis has demonstrated that the present research does add to the present body of knowledge.

8.3 RESEARCH METHODOLOGY

This study adopted an interpretative post positivist research paradigm and applied a qualitative research methodology and a doctrinal research method. The research included an international comparative perspective with the view to proposing reforms to the South African VAT system.

The first step of the research entailed a detailed review of literature to establish a theoretical basis of a good tax system, the theory of indirect taxation and of

consumption taxation. The literature review then presented an in-depth analysis of the South African VAT system and its treatment of resident versus non-resident businesses with a South African physical or economic reach, and its treatment of local and cross-border transactions, including imported services. The literature review also considered the international VAT treatment of non-residents and the treatment of cross border transactions and the use of inter-jurisdictional VAT rules to reduce interpretational uncertainty.

Additional data was collected through interviews with a panel of experts, consisting of various South African and global VAT and indirect tax experts. A questionnaire was specifically devised for this study and was used as a basis for the respondent interviews, conducted through correspondence. Informed written consent was obtained from each participant and approval was obtained from all the necessary parties, including the appropriate Ethics Committees.

As described above, this study effectively made use of triangulation, which is often used in the social sciences to indicate that two (or more) research methods (methodological triangulation) are used in a study in order to check the results of the same subject (Nokleby, 2011:141). Triangulation increases the reliability of the research results. Triangulation can be used in quantitative and qualitative research and is a method-appropriate strategy of increasing the credibility of qualitative analyses. By combining multiple methods, the researcher decreases the weakness or intrinsic biases and the problems associated with single method, single-observer and single-theory studies (Thurmond, 2001:254). Thus, the present research, in applying methodological triangulation, used a literature survey together with expert opinions of participants to triangulate the findings of the research, in order to make recommendations for amendments to the South African VAT Act.

8.4 RESEARCH IMPLICATIONS

The descriptions, analyses, and interpretations of data are very important components of research or a study. However, the implications of the research, or what will be done with the findings, are equally important (George Mason University, online). The research should provide clarity on the “why” and “how” of analyses and interpretations and the manner in which these concepts evolved. The research

should inform the reader of unexpected findings or patterns that emerged from the data and should support assertions or interpretations presented (Stainback and Stainback, 2003). Implementation of the research recommendations flowing from the present research could have far-reaching consequences. This study makes various recommendations regarding the inter-jurisdictional rules in the South African VAT system through proposing amendments to the law. These amendments originate from a consideration of the South African VAT Act and selected other VAT systems and take the form of proposing changes to current legislation and also introducing new legislation. Implementation of these proposals will result in (a) enhanced interpretative certainty with regard to the law and (b) decreased compliance costs, for both taxpayers and SARS.

Research should also “look for those critical incidents in your data, the “aha” or “oh no” moments, when you had a breakthrough in answering your research question...” (Hubbard and Power, 2003). This study had at least two “eureka” moments. Although these moments impacted the end result, they are shared here almost as *obiter dicta*. The first and most notable eureka experience involved the researcher’s deviation from the original research question, namely to research “place of supply rules” in the South African VAT system. Through a process of immersion in the theory of tax and VAT in South Africa and certain international VAT jurisdictions, the researcher realised that the South African VAT system is not only in need of a study of VAT “place of supply rules” (in a rather one-dimensional manner), but would benefit from a more holistic study of most inter-jurisdictional VAT rules applicable in South Africa. The second eureka experience was the realisation by the researcher that unless well-considered wording for legislation is proposed, that the effort of the research process will not “reach its full potential”.

8.5 FINDINGS AND CONCLUSIONS

This study identified and described a number of shortcomings in the inter-jurisdictional rules in the South African VAT system and proposed the following changes and additions to the VAT Act:

8.5.1 Non-resident VAT registration

- defining “dependent agents”;
- refining the provisions relating to foreign branch or main business;
- deeming certain non-resident suppliers of internationally traded services and intangibles to fall outside of the VAT net;
- extending the provisions relating to Underwriting Members of Lloyd’s of London to certain foreign underwriting insurance businesses;
- refining the provisions relating to foreign suppliers of electronic services;
- providing for foreign suppliers of telecommunication services and broadcasting services in a manner similar to electronic services; and
- clarifying the VAT treatment of goods imported on behalf of foreign principals.

8.5.2 Inter-jurisdictional VAT rate

- introducing measures similar to the OECD Tax Model on double taxation;
- introducing definitions of “non-resident” and “fixed or permanent place”;
- introducing a New Zealand-type non-resident refund mechanism;
- clarifying provisions relating to services supplied to non-residents outside South Africa, supplied directly in respect of goods or movable property exported or destined for export and physically rendered outside the Republic; and
- reclassifying supplies of foreign land by way of sale or lease;

8.5.3 Imported Services

- enforcing the imported services provisions applicable to government or revising the policy and VAT Act in this regard;
- applying the imported services provisions to business-to-business transactions; and
- requiring domestic VAT vendors to account for output tax in full on imported services and permit an input tax deduction, to the extent that the services will be used to make taxable supplies.

8.5.4 Intention of the legislator

- legislating the intention of the legislator to tax final utilisation or consumption; and
- defining the concepts of “utilised or consumed”.

8.5.5 Place of supply rules

The study finally recommended the introduction of a general place of supply rule linked to residency; specific place of supply rules for electronic, broadcasting, and telecommunication services; and zero rating provisions for electronic, broadcasting, and telecommunication services made to non-resident suppliers by resident suppliers for services initiated outside South Africa.

8.6 CONTRIBUTION OF THE STUDY

This study applied a holistic approach to the inter-jurisdictional VAT rules, their shortcomings, and recommendations to address these shortcomings and did not limit the research question to a consideration of place of supply rules only. Although other limited focus South African place of supply studies have been undertaken on certain place of supply aspects, the research did not attempt to consider these phenomena holistically and in an all-encompassing manner and can, to a certain extent, be described as following a piece-meal approach. As outlined in Chapter 2 of this study, these studies include those by:

- the VAT Committee of the South African Fiscal Association (SAFA) on *introducing place of activity rules in South Africa*;
- Schneider (2000) on *introducing VAT place of supply rules in South Africa*, which included a fairly comprehensive theoretical basis of taxation, VAT, consumption taxation, place of supply rules, and an international perspective;
- Krensel (2004), De Wet and Du Plessis (2005), Oosthuizen (2009), and Fryer (2014) on *the VAT treatment of electronic commerce*;
- De Swardt and Oberholzer (2006) on *VAT compliance of digitised products*;
- Van Der Westhuizen (2006) on *place of supply rules but predominantly those pertaining to telecommunication services*;

- Janse van Rensburg (2011) on *introducing VAT place of supply rules in South Africa*;
- Rourke (2012) on *the VAT implications of interactive gambling in the absence of detailed place of supply rules*;
- Van Zyl (2013a) on *the place of use or consumption of imported services for VAT purposes*;
- Van Zyl (2013b) on *the place of use or consumption for VAT purposes*;
- Van Zyl (2013c) on *the collection of VAT on online cross-border digital goods*;
- Davis Tax Committee: VAT sub-committee (2014) on, amongst others, *VAT place of supply rules*;
- Schoeman, Steyn, and Homeier (2015) on *VAT on international mobile telecommunication services*; and
- Botha (2015) on *the meaning of “enterprise” in the South African VAT system*.

These studies mostly considered certain aspects only of inter-jurisdictional VAT rules, and mainly insofar as they relate to place of supply rules. The legislator has not implemented the findings of these studies. None of these studies (except for SAFA to some extent) recommended detailed legislative changes.

8.7 LIMITATIONS OF THE STUDY

This study is limited to the extent that it did not attempt to present:

- a detailed consideration of previous South African studies done on inter-jurisdictional VAT rules, other than deducing main focal points raised in these studies and addressing major shortcomings of these studies; or
- a consideration of international experience of countries or country groupings, other than the OECD, the EU, Australia, Canada, and New Zealand.

Future research can include a refinement of the recommendations made in this study, and can test whether these recommendations will fully or partly convert the South African VAT system from a worldwide or New World VAT system to a territorial VAT system (European Model).

The contribution made by this study will not be nullified should the legislator not consider the recommendations made and not implement them. The contribution of this study will, however, lie more in the sparking of debate in tax technical circles, including National Treasury, SARS, and tax practitioners, particularly as the VAT Act has not been reviewed holistically since its inception in 1991. The study will hopefully also serve as motivation for future higher level research in tax in South Africa, a perceived need.

8.8 CONCLUDING REMARKS

The study considered the inter-jurisdictional rules in the South African VAT system with a view to identifying shortcomings and addressing these through making detailed legislative recommendations. To that extent it is submitted that the study achieved its overall objective. In attaining the overall objective of the study, it is submitted that the study also achieved the following sub-goals of the study:

- to create a theoretical foundation on which the remainder of the study could be built;
- to consider the legislation and practical experience in selected countries and country groupings, and apply these principles to address the shortcomings identified in the South African VAT system;
- to consider the provisions of the South African VAT system governing non-residents, the inter-jurisdictional VAT rate and imported services in detail and analyse them in the context of international experience in identifying shortcomings; and
- to make recommendations addressing the following:
 - non-resident VAT registration;
 - the inter-jurisdictional VAT rate;
 - imported services; and
 - the place of supply rules.

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GLOSSARY OF TERMS

Where abbreviations have been used in this study the following meaning should be given to them:

Abbreviation	Meaning
AFTS	Australia's Future Tax System
Davis Macro Analysis Report	Refers to "The tax system and inclusive growth in South Africa: towards an analytical framework for the Davis Tax Committee" Discussion Document. (see List of References).
Davis VAT Report	Refers to the "First Interim Report on Value-Added Tax for the Minister of Finance" of the Davis Tax Committee (see List of References)
ENS	Edward Nathan Sonnenbergs Law Firm
EU	European Union
EY	Ernst and Young Accountants and Auditors
Government	South African Central Government which, in certain instances, could include National Treasury and SARS
GST	Goods and Services Tax, also used to describe a Value-Added Tax system
IBFD	International Bureau of Fiscal Documentation
IMF	International Monetary Fund
Income Tax Act	Income Tax Act 58 of 1962
Katz Commission	Commission of Inquiry into the Tax Structure of the Republic of South Africa, appointed by the President and chaired by Professor Michael Katz. The Katz Tax Commission first reported in 1994
KPMG	The South African firm of the Global Firm of Accountants and Auditors KPMG

Margo Commission	Commission of Inquiry into the Tax Structure of the Republic of South Africa, appointed by the President and chaired by Judge Cecil Margo. The Margo Tax Commission reported in 1986.
National Treasury	National Treasury Office of South Africa which forms part of the Department of Finance and reports directly to the Minister of Finance and is responsible for tax policy and design
OECD	Organisation for Economic Cooperation and Development
PE	Permanent establishment, a term often used for Corporate Income Tax purposes to indicate a tax presence in a country.
PWC	PriceWaterhouseCoopers
SAFA	South African Fiscal Association
SAICA	South African Institute of Chartered Accountants
SARS	South African Revenue Service
South Africa	Used to denote the Republic of South Africa, and in certain instances used as reference for publications by the South African government, and referred to in full in the "List of References"
USA	United States of America
VAT	Value-Added Tax
VAT Act	Value-Added Tax Act 89 of 1991
VATCOM	Value-Added Tax committee appointed by Government to consider comments and representations by interested parties on the draft Value Added Tax Bill that was published for comment on 18 June 1990. See also South Africa. 1991b.

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APPENDICES

APPENDIX 1: QUESTIONS POSED TO PANEL OF EXPERTS

PLACE OF SUPPLY QUESTIONNAIRE

SA operates a destination based VAT, i.e. the VAT system taxes final domestic consumption by standard rating domestic consumption and importation and zero-rating rating exports.

Some observers are of the view that although South Africa may not have rules called “place of supply” rules, it effectively has place of supply or inferred place of supply rules which effectively addresses any “place of supply” difficulties.

Other observers are of the view that South Africa’s lack of actual place of supply rules is a definite shortcoming in the South African VAT system which needs to be addressed.

The purpose of this questionnaire is to obtain your view as an expert on various aspects relating to place of supply rules which will be used as input in a doctoral study, the results of which will be presented to the National Treasury and/or SARS.

References in the questionnaire to place of supply should be construed to also refer to place of activity rules, except where the context clearly indicates otherwise.

Question1

How would you define VAT place of supply rules?

Question 2

Do you believe the South African VAT system has (sufficient) (direct or inferred) place of supply rules?

PLEASE MOTIVATE.

Question 3

Do you believe South Africa needs to introduce specifically defined:

- (i) VAT place of supply rules, or
- (ii) Place of activity rules?

PLEASE MOTIVATE.

Question 4

If you believe that place of supply rules should be introduced into the South African VAT system, should the place of supply rules:

- (i) Differentiate between goods and services, and, if so, between tangible and intangible goods, or
- (ii) Not differentiate between goods and services?

PLEASE MOTIVATE.

Question 5

Do you believe that place of supply rules should be introduced to provide more certainty on:

- (i) The VAT registration liability of non-residents,
- (ii) The VAT rate applicable to specific supplies,

- (iii) The Vat registration liability of non-residents and the VAT rate applicable to specific supplies, or
- (iv) Issues not addressed above.

Question 6

Do you believe that proviso (ii) to the definition of “enterprise” in section 1 of the VAT Act is worded to:

- (i) Create any interpretational shortcomings, or
- (ii) Address any interpretational shortcomings?

PLEASE MOTIVATE.

Question 7

Do you believe that the last amendment to proviso (ii) to the definition of “enterprise”:

- (i) Clarified the application of section 8(9) of the VAT Act, or
- (ii) Rendered section 8(9) superfluous?

PLEASE MOTIVATE.

Question 8

Do you believe section 13 and the corresponding section 11 zero ratings contain:

- (i) Inferred place of supply rules,
- (ii) Add to certainty with regard to the VAT registration liability of non-residents in South Africa, or
- (iii) No reference or clarity with regard to place of supply rules?

PLEASE MOTIVATE.

Question 9

Should place of supply rules give guidance on areas such as:

- (i) E-commerce,

- (ii) Telecommunications,
- (iii) Insurance,
- (iv) Rental companies (e.g. AVIS and cross border leasing),
- (v) Royalties,
- (vi) Other?

PLEASE MOTIVATE.

Question 10

How do you believe place of supply rules should be introduced

- (i) To form part of the definition of "enterprise",
- (ii) In a separate section,
- (iii) As a separate schedule to the Act,
- (iv) By defining "activity" as envisaged in the definition of "enterprise" could instead of creating separate rules, or
- (v) A Practice Note or legislatively incorporated Regulation agreed and drafted by the major consulting firms, National Treasury and SARS.

PLEASE MOTIVATE

Question 11

Should the Commissioner for SARS have the discretion to, on request:

- (i) Deem certain activities to take place in South Africa, or
- (ii) Deem certain activities not to take place in South Africa?

PLEASE MOTIVATE

Question 12

Should the terms fixed or permanent place of business be defined to provide more clarity?

PLEASE MOTIVATE

Question 13

Does the differentiation of "Lloyds of London" cover-holder business and worldwide business present and insurance provided by other global insurers present any difficulties?

PLEASE MOTIVATE

Question 14

Should the place of supply of services differentiate between services capable of being physically rendered and those not capable of being physically rendered?

PLEASE MOTIVATE

Question 15

Should the place of supply in respect of services not capable of being physically rendered be determined with reference to place of fixed or permanent business and not services capable of being physically rendered?

PLEASE MOTIVATE

Question 16

How would place of supply rules impact section 54 transactions?

PLEASE MOTIVATE

Question 17

Please provide the 3 most important practical examples which illustrate shortcomings in the current South African VAT system which could be addressed by the introduction of place of supply rules.

PLEASE MOTIVATE

Question 18

Do you agree that the phrase “enterprise or activity” as used within the concept of “enterprise” can be seen as a “place of business” proxy linking what the supplier does and where? In other words, where a non-resident has a “place of business” in South Africa, it automatically has a VAT presence.

PLEASE MOTIVATE

Question 19

It has been argued that the question of “activity” as in “enterprise or activity” gives rise to most uncertainty. Do you believe that the original drafters meant it:

- (i) In a narrow sense, or
- (ii) In a broader sense.

PLEASE MOTIVATE

Question 20

Is the use of “Republic” in the definition of “enterprise” used with reference to the phrase “enterprise or activity” or the supply of “goods or services”?

PLEASE MOTIVATE

Question 21

Are you of the view that worldwide supplies of goods and services are drawn into the South African VAT net where the business has an “enterprise or activity” in or partly in South Africa (before exclusions, exemptions, etc.)?

PLEASE MOTIVATE

Question 22

How does “enterprise” (main definition) link to the charging section, section 7(1)(a)?

PLEASE MOTIVATE

Question 23

Do you view “imported services” in section 7(1)(c) as an inferred place of supply rule?

PLEASE MOTIVATE

Question 24

Do you consider the phrase “enterprise or activity” to be an integral component of “enterprise”?

PLEASE MOTIVATE

Question 25

Do you consider the reach of the VAT net:

- (i) Wider than the “place of business” of an entity, or
- (ii) Narrower than the “place of business” of an entity?

PLEASE MOTIVATE

Question 26

Do you consider the making available of intellectual property in South Africa by a foreign business without a “place of business” in South Africa to:

- (i) Constitute an “enterprise” in South Africa, or
- (ii) Not constitute an “enterprise” in South Africa?

PLEASE MOTIVATE

Question 27

Do you consider the phrase “enterprise or activity” to:

- (i) Include an economic activity, or
- (ii) Not include an economic activity (as opposed to a physical activity)?

PLEASE MOTIVATE

Question 28

Are you of the view that the South African VAT legislation:

- (i) Lacks additional rules regarding supplies by non-residents (as used, for example, by New Zealand), or
- (ii) Has sufficient rules regarding supplies by non-residents?

PLEASE MOTIVATE

Question 29

Regarding the definitions of "Republic" and "resident of the Republic", do you consider:

- (i) These definitions to contain shortcomings, especially with regard to place of supply, or
- (ii) These definitions to be fairly strong and tested definitions.

PLEASE MOTIVATE

Question 30

The definition "resident of the Republic" deems a person to be resident if that person carries on "any enterprise or activity" in the Republic from a fixed or permanent place in the Republic. The phrase "enterprise or activity" is contained in both "enterprise" and "resident of the Republic". What do you consider the relevance of this to be?

PLEASE MOTIVATE

Question 31

Do you consider that occasional "enterprise or activity":

- (i) Falls out of "enterprise" as the "enterprise or activity" must be carried on "continuously or regularly", or
- (ii) Could comprise an "enterprise"?

PLEASE MOTIVATE

Question 32

A recent South African court case (VAT Case 179) dealt with the discontinuation of intellectual property rights made available from outside of South Africa for use in South Africa. Do you believe that VAT Case 179:

- (i) Established the place of supply regarding intellectual property made available to be where the owner of the property reside,
- (ii) Established the place of supply regarding intellectual property made available to be where the acquirer or user of the property reside, or
- (iii) Did not provide any more clarity regarding the place of supply regarding intellectual property made available?

PLEASE MOTIVATE

Question 33

A recent South African court case (VAT Case 382) dealt with the restructuring of a South African mining and diamond company which involved share buy-backs and cancellations and the creation of a foreign holding company. Do you believe that VAT Case 382:

- (i) Correctly held that the activities surrounding the restructuring were not part of the company's VAT enterprise, or
- (ii) Incorrectly held that the activities surrounding the restructuring were not part of the company's VAT enterprise?

PLEASE MOTIVATE

Question 34

Do you believe that a once-off transaction or supply which comprise of a continuous or regular set of activities could fall within the definition of "enterprise"?

PLEASE MOTIVATE

Question 35

Do you agree with the following statement of a well-known global VAT expert:

“I have always thought that when South Africans say ‘we have no place of supply rules’ the real complaint is that the notion of ‘in the Republic’ in the enterprise rule is insufficiently well defined, leaving lots of scope for argument. It clearly isn’t referring to residence. Carrying on business from a fixed place of establishment clearly would be carrying on an enterprise in the Republic. Just making an occasional supply would not. But the real problem is what level of activity is sufficient to fall within that phrase?”

PLEASE MOTIVATE

Question 36

With regard to the VAT place of supply rules in the **UK VAT system**, can you please provide the following:

- (i) The actual and current wording of the VAT place of supply rules,
- (ii) Any material changes effected to the VAT place of supply rules, and when and why these were made,
- (iii) Whether the VAT place of supply rules enhance certainty,
- (iv) Why the VAT place of supply rules were originally introduced. For example, to address the VAT rate applicable to certain transactions or to address the potential VAT liability of foreign businesses.

Question 37

With regard to the VAT place of supply rules in the **Canadian VAT system**, can you please provide the following:

- (i) The actual and current wording of the VAT place of supply rules,
- (ii) Any material changes effected to the VAT place of supply rules, and when and why these were made,
- (iii) Whether the VAT place of supply rules enhance certainty,

- (iv) Why the VAT place of supply rules were originally introduced. For example, to address the VAT rate applicable to certain transactions or to address the potential VAT liability of foreign businesses.

Question 38

With regard to the VAT place of supply rules in the ***New Zealand VAT system***, can you please provide the following:

- (i) The actual and current wording of the VAT place of supply rules,
- (ii) Any material changes effected to the VAT place of supply rules, and when and why these were made,
- (iii) Whether the VAT place of supply rules enhance certainty,
- (iv) Why the VAT place of supply rules were originally introduced. For example, to address the VAT rate applicable to certain transactions or to address the potential VAT liability of foreign businesses.

Question 39

With regard to the VAT place of supply rules in the ***Australian VAT system***, can you please provide the following:

- (i) The actual and current wording of the VAT place of supply rules,
- (ii) Any material changes effected to the VAT place of supply rules, and when and why these were made,
- (iii) Whether the VAT place of supply rules enhance certainty,
- (iv) Why the VAT place of supply rules were originally introduced. For example, to address the VAT rate applicable to certain transactions or to address the potential VAT liability of foreign businesses.

Question 40

With regard to the VAT place of supply rules in the ***EU VAT system***, can you please provide the following:

- (i) The actual and current wording of the VAT place of supply rules,

- (ii) Any material changes effected to the VAT place of supply rules, and when and why these were made,
- (iii) Whether the VAT place of supply rules enhance certainty,
- (iv) Why the VAT place of supply rules were originally introduced. For example, to address the VAT rate applicable to certain transactions or to address the potential VAT liability of foreign businesses.

**APPENDIX 2: LETTER OF CONSENT SENT TO PANEL OF EXPERTS TO
PARTICIPATE IN STUDY**

Consent for participation in a research study

Title of the study: “PLACE OF SUPPLY RULES IN THE SOUTH AFRICAN VALUE-ADDED TAX SYSTEM”

Research conducted by:

Mr Ferdinand Dirk Schneider

Telephone number: +27 82 771 4157

E-mail: fschneider@bdo.co.za

Dear respondent

You are invited to participate in a research study conducted by Ferdie Schneider, (doctoral student from the Department of Accounting of the Rhodes University).

The purpose of the study is to examine the desirability of implementing VAT place of supply rules in the South African VAT system. The results will be presented to National Treasury, and possibly SARS, to provide them with reasons for and recommendations on the possible introduction of place of supply rules.

Your participation in this research is very important as it would, through the output of this study, provide National Treasury or SARS with sound specialist input into a very important aspect of national VAT policy.

Please note the following:

- Please answer the questions below as honestly and comprehensively as possible.
- Your participation will form part of a survey of selected South African and global VAT, indirect tax and fiscal economics specialists. Your participation will be in your capacity as a specialist in the mentioned field and not as a representative of your employer. Your views may be quoted in the study and referenced to you in person.

- Your participation in this study is very important. You may, however, choose not to participate and you may also stop participating at any time without any negative consequences.
- The results of the study may be used for future research purposes.
- Please e-mail Ferdie Schneider at fschneider@bdo.co.za if you have any questions or comments regarding the study.

Please indicate that:

- You have read and understand the information provided above.
- You give your consent to participate in the study on a voluntary basis.

Kind regards

Ferdie Schneider

APPENDIX 3: ETHICAL CONSENT



RHODES UNIVERSITY

DEPARTMENT OF ACCOUNTING

APPLICATION NUMBER
ACC 2016 001

NATURE OF THE REVIEW:

An original review	x
A re-review	

At a meeting of the Department of Accounting Ethics Sub-Committee held on:

11 July 2016

the Committee resolved to:

Approve the application	x
Approve the application, with stipulations	
Modifications required	
The project is to be monitored	
No approval required	
Not approved	

The committee noted that this application was extremely unusual in light of the fact that the applicant had recently transferred from the University of Pretoria and the research had already been conducted. The committee further noted, however, that the applicant had obtained ethical clearance from the University of Pretoria Faculty of Commerce and Economic Management Sciences Committee for Research Ethics prior to the research having been conducted.

Chair/Acting Chair: Professor J Arendse

Member: Professor J Williams

APPENDIX 4: SAFA's INITIAL DRAFT PLACE OF ACTIVITY RULES

Place of Activity Rules

For the purposes of the definition of "enterprise" as defined in section 1 of the Act, an activity shall be deemed to be carried on in or partly in the RSA where:

1. *In the case of goods supplied by any person under:*
 - a) *a sale agreement, the goods are situated in the RSA, excluding goods located in a licensed customs and excise warehouse, at the time the sale agreement is concluded; or*
 - b) *an agreement for the supply of any real right in movable goods, such movable goods is located in the RSA at the time the agreement for the supply of such rights is concluded; or*
 - c) *an agreement for the supply of any real right in fixed property, such fixed property located in the RSA at the time the agreement for the supply of such rights is concluded; or*
 - d) *an instalment credit agreement, the goods are situated in the RSA at the time the instalment credit agreement is concluded; or*
 - e) *a rental agreement:*
 - (i) *the goods are used wholly or partly in the RSA; or*
 - (ii) *the goods consist of a foreign going ship or a foreign going aircraft which is operated by a resident of the RSA.*

Provided that this subsection shall not apply in respect of goods which are exempt from tax on importation as envisaged in section 13(3) of this Act.

Provided that for purposes of this section, a sale agreement, an instalment credit agreement and an agreement for the supply of a real right in movable goods or fixed property, shall be deemed to be concluded at the time when the last party to the agreement accepts the terms and conditions of the agreement.

2. *In the case of services supplied by any person where the services are:*
- a) *capable of being physically rendered or performed, to the extent that such services are physically rendered or performed by the supplier or his agent in the RSA; or*
 - b) *not capable of being physically rendered or performed to the extent that the supplier or his agent supplies the services from a fixed or permanent place in the RSA from where a business is carried on by the supplier or his agent.*

Notwithstanding any of the provisions in this section, the Commissioner may on request, deem any supply of services to be an activity carried on by any person to be supplies made in the RSA.

Source: SAFA (2000a)

**APPENDIX 5: DELOITTE COMMENTARY ON SAFA'S INITIAL DRAFT PLACE OF
ACTIVITY RULES**

Deloitte and Touché Commentary on the Value-Added Tax (VAT) Place of Activity Rules Proposed by SAFA

We would like to express our appreciation for the opportunity to give our comments on the proposed place of activity rules drafted by your committee.

We proceed in Part A by introducing some of the problems experienced in the South African VAT field, which could possibly be addressed by the introduction of place of supply rules and guidelines that we believe should be followed. We allude in Part B to specific areas of concern. In Part C we have summarised our commentary on the actual proposals, in seriatim. We give a recommended approach in Part D of how we believe place of activity (or supply) rules can and should address these and more generic problems and conclude in part E.

A Introduction

We are of the view that the primary reason for introducing place of supply (or activity) rules should be to alleviate the current legislative uncertainty experienced by VAT consultants and commercial enterprises alike in interpreting the South African VAT provisions as it relates to cross-border transactions and foreign enterprises with some South African connection.

Due to the resource constraints experienced by the South African Revenue Service (SARS), we would like to propose that any amendments to the current VAT system should be done in such a manner to rather alleviate the resource problem than to add to the administrative burden of SARS. In this respect we propose that foreign enterprises not conducting a business in South Africa should not unnecessarily be burdened with VAT registration requirements, except where non-registration would lead to a loss of revenue to the fiscus.

B Specific Examples

We highlight below various examples of problems experienced in practice, which could possibly be solved by the introduction by place of supply (or activity) rules.

B1 Movable Goods Rented to a South African Person by a Foreign Enterprise and Made Available Outside the Republic of South Africa (SA)

Movable goods made available outside SA by a foreign enterprise (who retains ownership) and subsequently imported by a person present in SA into SA could, in terms of current interpretation of the VAT legislation render the foreign enterprise liable to register for SA VAT purposes.

B2 Royalty Payments

In the SARS' VAT News No. 13 of December 1999 the view was expressed that the granting of the right of use in SA of any trade mark or intellectual property by a foreign enterprise over a period of time is regarded as the carrying on of an enterprise in or partly in SA for VAT purposes. It was argued that foreign enterprises that regularly receive royalties, franchise or agency fees are required to register as VAT vendors if their annual receipts exceed R300 000.

Should this be the official view of SARS in future, it would lead to the registration of many foreign enterprises in SA without necessarily any material revenue gain to the fiscus, and an additional administrative burden to the fiscus and the foreign enterprise alike.

B3 Telecommunication Services

The amendment to "enterprise" (albeit not promulgated yet) provides that the place of supply of telecommunication services is where the services are consumed and, if it is proposed, would not have been captured in the definition of "enterprise", had it not been for the amendment.

This amendment seems to cater for the fact that most of the recipients of telecommunication services are not registered for VAT purposes. The amendment

would seem to contradict, to some extent, the application of the reverse charge procedure provided for in section 7(1)(c) and the definition of "imported services" in section 1 of the VAT Act.

B4 Insurance

With effect from 1 January 2001, the recent amendment to "enterprise" provides that the place of supply in respect of services rendered by Underwriting Members of Lloyd's of London is where the contracts of insurance are concluded.

This amendment caters for the unique nature of the business of the Underwriting Members of Lloyd's of London, but does not address the insurance industry's VAT treatment in general.

B5 Service Contracts Executed by Foreign Enterprises in South Africa through Agents or Employees

Foreign enterprises often conclude contracts with South African residents to perform or render services physically in South Africa. The nature, duration and continuity of these services might vary. Clear guidelines as to when the foreign enterprise needs to register for VAT in South Africa has not officially been made available.

C Summary of Deloitte and Touché (D&T) Commentary (please refer to main document for detailed commentary) on the SAFA of Activity Rules

Proposed SAFA Place of Activity Rule	D&T Commentary and Suggestions
<p><i>For the purposes of the definition of “enterprise” as defined in section 1 of the Act, an activity shall be deemed to be carried on in or partly in the RSA where:</i></p>	<p><i>We recommend that place of supply rules rather be introduced and that the current uncertainty regarding what constitutes an “enterprise” or “activity” be addressed as a distinct separate issue. This could be done by, for example, linking the definition of “enterprise” to the Income Tax concept of permanent establishment (PE) via practice note or a section 1 definition or by some other means.</i></p> <p><i>We proceed with suggestions based on place of supply rules with reference to the PE concept:</i></p>
<p><i>1. In the case of goods supplied by any person under:</i></p>	<p><i>As a general comment we would like to stress that we believe that affixing place of supply rules to the time when a contract is signed and the location of the goods at that time to be very open to manipulation.</i></p> <p><i>It should be noted that various countries and also the European Union (EU) defines goods as meaning the transfer of ownership in tangible property or immovable property, whereas services</i></p>

	<p><i>mean supplies not being supplies of goods. This distinction could be useful in defining place of supply.</i></p>
<p><i>a) a sale agreement, the goods are situated in the RSA, excluding goods located in a licensed customs and excise warehouse, at the time the sale agreement is concluded; or</i></p>	<p><i>The EU deems the supply of goods where the goods are dispatched or transported by the supplier, recipient or a third person to be the place where the goods are at the time when the dispatch or transport to the recipient begins.</i></p> <p><i>Where the goods are installed or assembled by or on behalf of the supplier, the place of supply is deemed to be where the goods are installed or assembled, i.e. where consumption takes place.</i></p> <p><i>Where the goods are not dispatched or transported, the place of supply is deemed to be where the goods are when the supply takes place.</i></p> <p><i>We recommend that where goods are placed at the disposal of the recipient at a place in SA, the place of supply of the goods should be deemed to be in SA. We further recommend that in the event that ownership of the goods remains in the hands of a foreign enterprise, whilst the goods are used by a recipient at a place in SA,</i></p> <p><i>The foreign enterprise be required to</i></p>

	<i>register for SA VAT purposes only where the recipient is a non-registered SA person or partially taxable SA VAT vendor or where the foreign enterprise has a PE in SA or owns fixed property.</i>
<i>b) an agreement for the supply of any real right in movable goods, such movable goods is located in the RSA at the time the agreement for the supply of such rights is concluded; or</i>	<i>We recommend that the place of supply should be determined as if the supply of goods in these instances is a supply of services, except where actual ownership of the goods passes.</i>
<i>c) an agreement for the supply of any real right in fixed property, such fixed property is located in the RSA at the time the agreement for the supply of such rights is concluded; or</i>	<i>It is generally accepted that the place of supply of services relating directly to fixed property in a country is deemed to take place in that country.</i> <i>Real rights in fixed property would, as a rule, be consumed in the country where the fixed property is located, and should consequently be taxed in that country.</i>
<i>d) an instalment credit agreement, the goods are situated in the RSA at the time the instalment credit agreement is concluded; or</i>	<i>We recommend that the place of supply should be determined as if the supply of goods in these instances is a supply of services, except where actual ownership of the goods passes.</i>
<i>e) Rental agreement:</i> <i>(i) The goods are used wholly or partly in the RSA; or</i> <i>(ii) The goods consist of a foreign going ship or a foreign going aircraft, which is operated by a resident of the RSA.</i> <i>Provided that his subsection shall not</i>	<i>We recommend that the place of supply should be determined as if the supply of goods in these instances is a supply of services, except where actual ownership of the goods passes.</i>

<p><i>apply in respect of goods which are exempt from tax on importation as envisaged in section 13(3) of this Act.</i></p>	
<p><i>Provided that for purposes of this section, a sale agreement, an instalment credit agreement and an agreement for the supply of a real right in movable goods or fixed property, shall be deemed to be concluded at the time when the last party to the agreement accepts the terms and conditions of the agreement.</i></p>	<p><i>The danger of linking place of supply or activity rules to the superficial time of supply rules in the VAT Act or date of acceptance of conditions is that it invites manipulation. This principle is demonstrated by the various amendments to section 11(2)(1) over the last years.</i></p>
<p><i>2. In the case of services supplied by any person where the services are</i></p>	<p><i>The EU generally deems the supply of services to be the place where the supplier established his business or has a fixed establishment from which the service is supplied, or in the absence thereof, the place where he has his permanent address or usually resides.</i></p> <p><i>Specific rules also apply. The EU also deems the place of use to be the place of supply for certain services, such as services relating to fixed property, intellectual property rights, advertising, transport, hiring out of movable tangible property.</i></p>
<p><i>a) capable of being physically rendered or performed, to the extent that such services are physically rendered or performed by the supplier or his agent in the RSA.</i></p>	<p><i>We recommend that the place of supply should be determined by considering where the consumption takes place. If the consumption takes place in SA, the supply should be deemed to take place in SA.</i></p>

	<p><i>Where the supplier has a PE in SA, irrespective of nationality, the supplier should be liable to account for VAT at the standard rate. Where the supplier has no PE in SA, then notwithstanding that consumption takes place in SA, the supplier should not be required to register in SA unless any of the recipients are not fully entitled to make an input tax deduction (e.g. individuals or financial institutions).</i></p> <p><i>We have considered whether SA should consider the reverse charge mechanism where the supplier has no PE in SA, but are of the view that the compliance burden on SARS would outweigh the benefits.</i></p>
<p><i>b) not capable of being physically rendered or performed to the extent that the supplier or his agent supplies the services from a fixed or permanent place in the RSA from where a business is carried on by the supplier or his agent.</i></p>	<p><i>We recommend that the place of supply should be determined by considering where the consumption takes place. If the consumption takes place in SA, the supply should be deemed to take place in SA.</i></p> <p><i>Where the supplier has a PE in SA, irrespective of nationality, the supplier should be liable to account for VAT at the standard rate. Where the supplier has no PE in SA, then notwithstanding that the consumption takes place in SA, the supplier should not be required to</i></p>

	<p><i>register in SA unless any of the recipients are not fully entitled to an input tax deduction (i.e. individuals or financial institutions).</i></p> <p><i>We have considered whether SA should consider the reverse charge mechanism where the supplier has no PE in SA, but are of the view that the compliance burden on SARS would outweigh the benefits.</i></p>
<p><i>Notwithstanding any of the provisions in this section, the Commissioner may on request, deem any supply of services to be an activity carried on by any person to be supplies made in the RSA.</i></p>	<p><i>Discretion generally creates an enormous administrative compliance burden for SARS and should be avoided as far as possible.</i></p>

D Suggested Approach

D1 General

Place of supply rules should ideally take into account:

- *The lack of resources of the South African Revenue Service (SARS) and in this regard any alterations to the VAT Act should endeavour to limit the number of foreign enterprises registering in South Africa for VAT purposes, except where non-registration would lead to a loss of revenue to the fiscus or to a lack of neutrality*
- *The nature of the supply, i.e. a distinction between tangible and intangible goods and services;*
- *Where specifically the goods or services are made available;*
- *Where the goods or services are consumed;*
- *Where the supplier operates his business from;*

- *Whether the supplier has a permanent establishment (PE) in South Africa PE rules as used in the OECD or the UN Model Tax Treaties or used in some VAT systems such as Greece, Italy or the UK should be considered in designing place of supply rules for South Africa; and*
- *Whether the principal supplier operates through a dependent agent (who can legally bind his principal) or an independent contractor who cannot legally bind the principal supplier.*

D2 Suggested Place of Supply Rule - Goods (see Annexure A)

We are of the view that the place of supply of movable goods placed at the disposal of the recipient (or made available) outside SA should be deemed to be outside SA and, other things being equal, the owner of the goods should not, by reason of this initial supply of these goods on its own, be required to register in SA for VAT purposes.

Should the place of supply rules cater for this, the South African fiscus would be in a neutral position as regards the once-off and physical making available of the goods. Should the goods subsequent to the placing at the disposal of the recipient outside SA, be imported into SA, it would give rise to SA VAT. The importer would be charged with VAT on importation and physical entry of the goods into SA. The importer should be entitled to claim an input tax deduction on the importation of the goods if it will be used to make taxable supplies.

In the case where the ownership of the goods are retained by a foreign enterprise (such as an instalment credit or rental agreement), who made the goods available outside SA and was not responsible for the importation, the VAT Act needs to charge the domestic consumption of the goods (e.g. the use in SA under a rental) to VAT at the standard rate. In this regard, SARS would have two options of taxing the rental stream in SA.

Firstly, the SA importer could be expected to reverse charge (on the principles of imported services). This option would be impractical and would result in the exact same compliance issues currently experienced in the field of self-supply in respect of imported services and would consequently place an enormous administrative

burden on SARS.

The second option would be to deem the foreign enterprise to conduct an enterprise activity in SA, where the foreign enterprise is making available any goods to a non-registered SA person or to a vendor who utilises the goods wholly or partially for making exempt supplies. Should the foreign enterprise make its SA supplies (i.e. the making available of the goods) solely to SA VAT vendors, the foreign enterprise should not be required to register for SA VAT purposes and these supplies should not attract SA VAT, since the SA VAT vendor would be entitled to an equal input tax deduction. This option seems viable since the objective should be to not register foreign enterprises in SA, except where non-registration would lead to a loss of revenue to the fiscus. The only degree of a lack in neutrality (cross-border) could be that goods supplied in SA to a VAT vendor under a rental agreement or the like by a foreign enterprise would not have the possible adverse cash flow consequences associated with domestic supplies, where tax is paid in advance of claiming an input tax deduction.

Should the foreign enterprise have a permanent place of business, permanent establishment (using the OECD or UN Model Double Tax Treaty definitions) or place of belonging (as in UK VAT legislation), any supplies made by the foreign enterprise and consumed in SA should be charged with VAT by the foreign enterprise, irrespective of the VAT status of the recipient.

D3 Suggested Place of Supply Rule - Services (see Annexure B)

The place of supply should be where the supplier has established his business or has his PE from which the service is supplied, or in the absence thereof, the place where he has his permanent address or usually resides. Should this place of supply rule be adopted, again, the South African fiscus would not be adversely affected. Non-registered persons or partially taxable registered SA VAT vendors could be required to reverse-charge if the services are acquired to make exempt supplies.

We would again suggest, as in D2 above, that the foreign enterprise should be deemed to conduct an enterprise activity in SA, where the foreign enterprise is

making available any rights to a non-registered SA person or partially taxable registered SA VAT vendor. Should the foreign enterprise make its SA supplies (e.g. the making available of rights) only to SA VAT vendors, the foreign enterprise should not be required to register for SA VAT purposes and these supplies should not attract SA VAT, since the SA VAT vendor would be entitled to an equal input tax deduction. Again, this option seems viable since the objective should be to not register foreign enterprises in SA, except where non-registration would lead to a loss of revenue to the fiscus. The only degree of a lack in tax neutrality (cross-border) could be that services used in and made available in SA to a registered SA VAT by a foreign enterprise would not have the possible adverse cash flow consequences associated with domestic supplies, where tax is normally paid in advance of claiming an input tax deduction.

Should the foreign enterprise have a permanent place of business, permanent establishment (using the OECD or UN Model Double Tax Treaty definitions) or place of belonging (as in UK VAT legislation), any supplies made by the foreign enterprise and consumed in SA should be charged with VAT by the foreign enterprise, irrespective of the nature of the recipient.

E Conclusion

We recommend that the place of supply rules be introduced together with a clarification of "enterprise or activity" as contained in the definition of "enterprise" in section 1 of the VAT Act. We recommend that "enterprise or activity" be given the meaning of a general physical commercial activity, by using the definition of "permanent establishment as used in either the OECD or UN model tax treaties.

We further recommend that the following steps be followed in determining the place of supply and also a foreign enterprise's responsibility to register for VAT purposes in SA:

1. Determine the place of supply:

- if consumption takes place in SA - place of supply is in SA.*
- If place of supply is in SA:*

2. Determine the nature of the supplier and recipient:

- 1 If the supplier owns fixed property in SA - foreign enterprise needs to register in SA for VAT purposes - no further test; or*
- 2 If the supplier has a PE in SA - foreign enterprise needs to register in SA for VAT purposes - no further test; or*
- 3 If the recipient is a non-registered SA person or partially taxable SA VAT vendor – foreign enterprise needs to register in SA for VAT purposes - no further test; or*
- 4 If the recipient is a registered SA VAT vendor - foreign enterprise do not need to register in SA for VAT purposes, except where 3.1 or 3.2 above apply.*

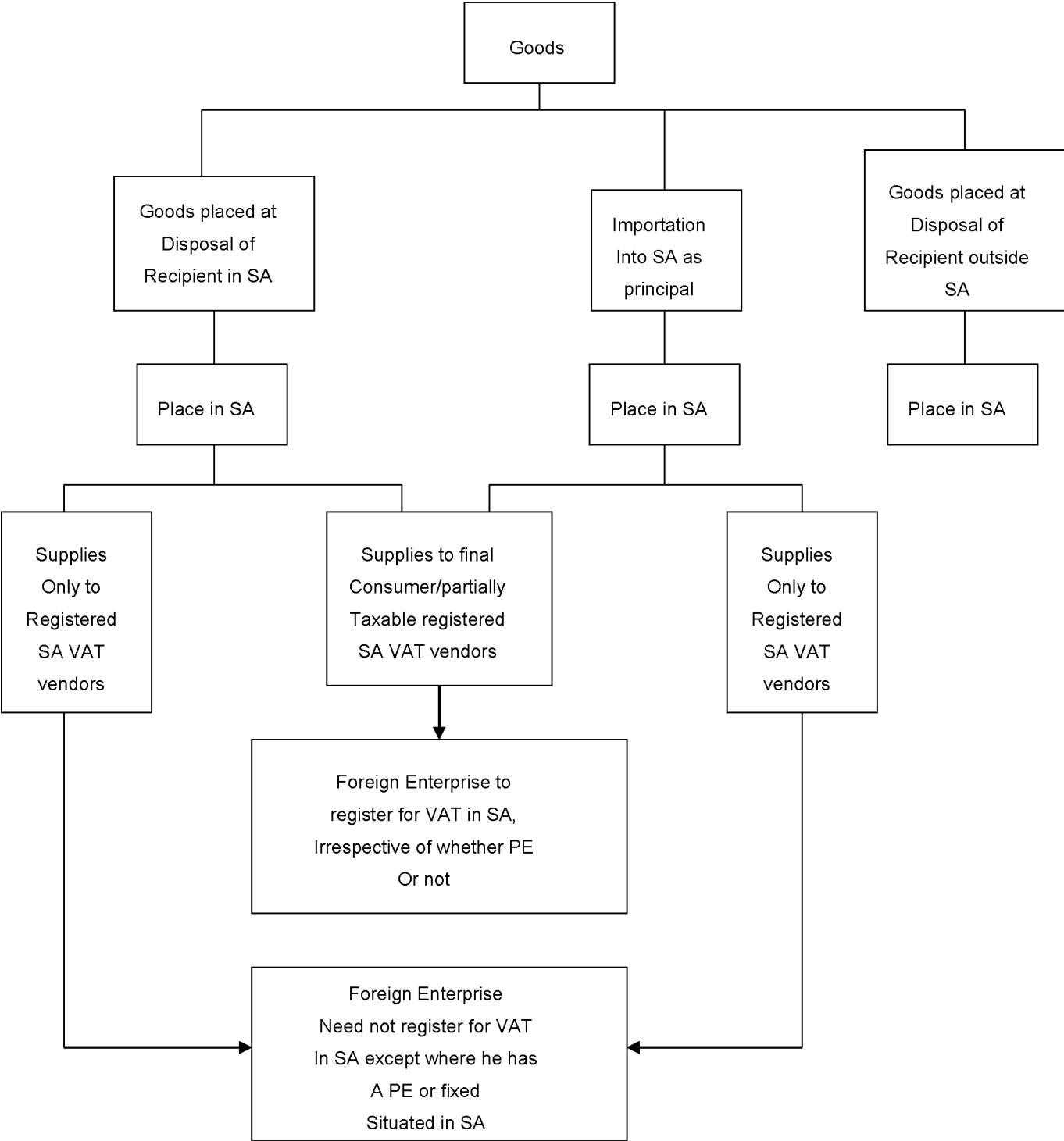
3. If place of supply is not in SA:

- and foreign enterprise is not registered in SA for VAT purposes due to any of its other supplies, no need to register in SA for VAT purposes.*

Yours faithfully

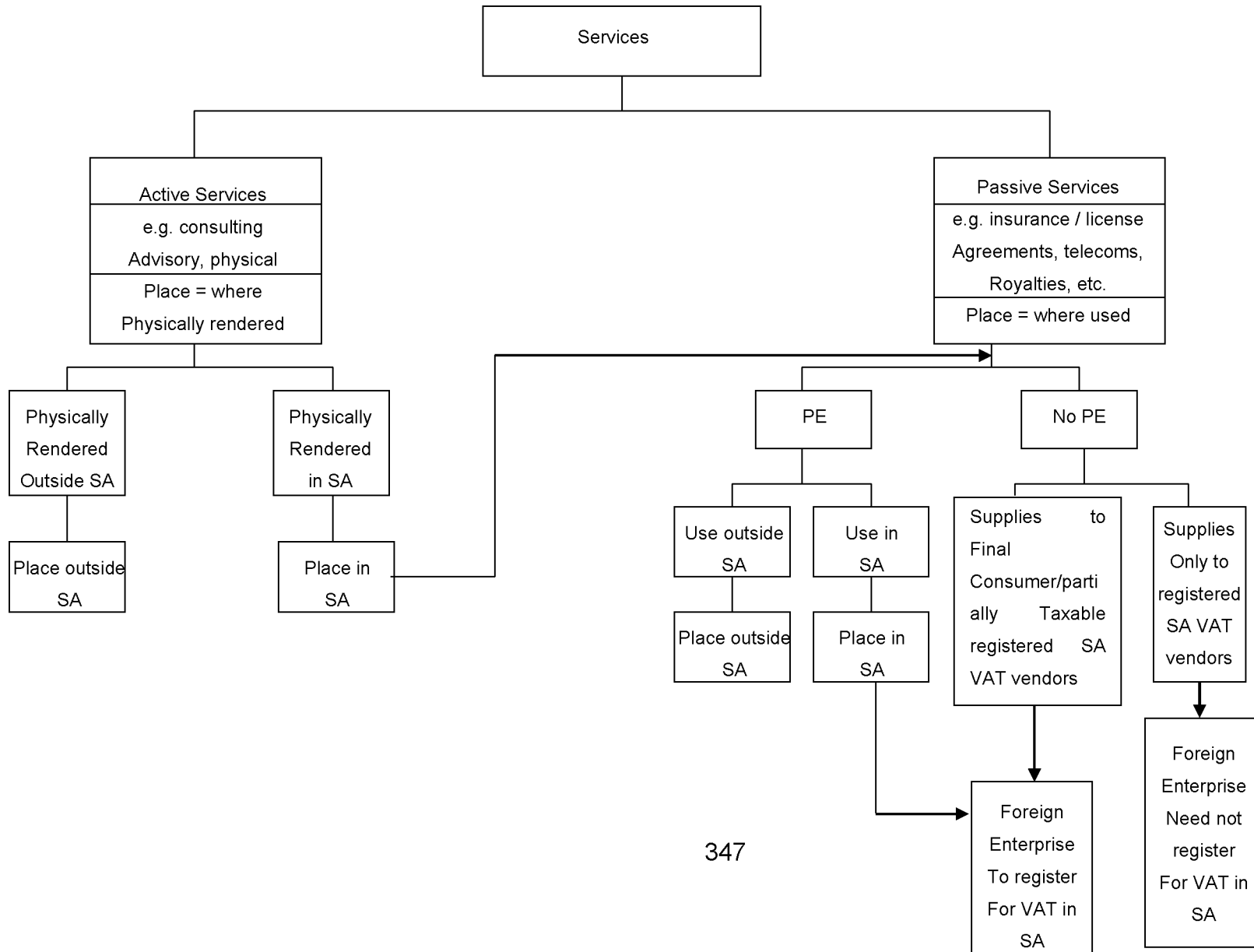
Deloitte and Touché

Source: Deloitte (2000)



Place of Supply Services

Annexure B



APPENDIX 6: SAFA'S REVISED DRAFT PLACE OF ACTIVITY RULES

Place of Activity Rules - Final Draft (September 20, 2000)

For the purposes of the definition of "enterprise" as defined in section 1 of the Act, a person that is not a resident shall be deemed to carry on an activity in or partly in the RSA where:

1. *In the case of goods supplied by that person under:*
 - a) *a sale agreement, the goods are situated in the RSA, excluding goods located in a licensed customs and excise warehouse, at the time the sale agreement is concluded; or*
 - b) *an agreement for the supply of any real right in movable goods, such movable goods is located in the RSA at the time the agreement for the supply of such rights is concluded; or*
 - c) *an agreement for the supply of any real right in fixed property, such fixed property is located in the RSA; or*
 - d) *an instalment credit agreement, the goods are situated in the RSA at the time the instalment credit agreement is concluded; or*
 - e) *a rental agreement:*
 - (i) *the goods are used wholly or partly in the RSA; or*
 - (ii) *the goods consist of a foreign going ship or a foreign going aircraft which is operated by a resident of the RSA.*

Provided that this subsection shall not apply in respect of goods which are exempt from tax on importation as envisaged in section 13(3) of this Act.

Provided that for purposes of this section, a sale agreement, an instalment credit agreement and an agreement for the supply of a real right in movable goods or fixed property, shall be deemed to be concluded at the time when the last party to

the agreement accepts the terms and conditions of the agreement.

2. *In the case of services supplied by any person where the services are:*
 - a) *capable of being physically rendered or performed, to the extent that such services are physically rendered or performed by the supplier or an agent in the RSA acting for or on behalf of that supplier; or*
 - b) *not capable of being physically rendered or performed to the extent that the supplier or an agent acting for or on behalf of that supplier supplies the services from a fixed or permanent place of business in the RSA from where a business is carried on by the supplier or his agent.*

Notwithstanding any of the provisions in this section, the Commissioner may on request by such person, deem any supply of services to be an activity carried on by any person to be supplies made in the RSA.”

Source: SAFA (2000b)

**APPENDIX 7: SAFA'S GUIDELINES ON THE PROPOSED PLACE OF ACTIVITY
("SUPPLY") RULES**

Proposed Place of Activity ("Supply") Rules

In view of the current interpretative uncertainty in the South African Value-Added Tax (VAT) system, especially with regards to cross-border transactions the SAFA VAT Committee has drafted proposed "place of supply" rules or what we have termed "place of activity" rules for South Africa.

Please consider the rules in light of, amongst others, the guidelines and/or questions listed below. We would appreciate if the individual firms can provide us with their consolidated and motivated views on the issues raised.

1 Final Domestic Consumption

SA operates a destination based VAT, i.e. the VAT system taxes final domestic consumption by standard rating domestic consumption and importation and zero-rating rating exports.

Would the proposed rules add certainty to these principles or alter the VAT basis in any way?

2 Definition of "enterprise"

Would the rules add clarity to the current definition of "enterprise" or is the definition contradicted in any way?

Does the current definition of "enterprise" cater for all possible scenarios addressed by the proposed rules?

3 Deeming provisions and export provisions

Would the rules contradict any of the deeming provisions in the VAT Act (e.g. section 8(9)) or the zero-rating provisions or even sections 13 (e.g. section 13(3)) and 14?

4 Specific types of transactions

Although the rules do not seek to address all possible specific types of transactions, would the proposed rules give enough guidance on the more common problem areas such as e-commerce, insurance, rental companies (e.g. AVIS and cross border leasing), royalties, etc.?

Would the rules in any way contradict the traditional wisdom regarding the treatment of the specific types of transactions mentioned above and imported goods and/or services?

Should the rules not cater for more specific types of transactions?

5 Place of "activity" as opposed to place of "supply"

Would the term "activity" provide more clarity than the term "supply"?

6 Incorporating the Rules into the Act

How should the rules be incorporated into the Act? A few alternatives are:

- the rules can form part of the definition of "enterprise" (e.g. as was done for telecommunication services) by extending the "SA-use deems enterprise" proviso of telecommunication services*
- in a separate section (e.g. section 1A)*
- as a separate schedule to the Act (e.g. Schedule 3 or 4)*
- "activity" as envisaged in the definition of "enterprise" could be defined instead of creating separate rules*
- would a Practice Note or legislatively incorporated Regulation agreed and drafted by the major consulting firms and SARS under the banner of SAFA suffice in addressing the current uncertainty?*

7 Telecommunication services

The proviso in the definition of "enterprise" in section 1 referring to "telecommunication services" and its use in South Africa forming part of an enterprise is effectively a place of supply rule deeming the place of supply to be in South Africa if the consumption takes place in South Africa.

Should it be decided that the proposed rules not form part of the definition of "enterprise" (as posed in paragraph 5 above) in the same manner as telecommunication services, should the proviso relating to telecommunication services be moved contextually to form part of the "place of activity" rules.

8 Commissioner for SARS' discretion

Should the Commissioner for SARS have the discretion to deem certain activities to take place in South Africa on request?

Should the Commissioner for SARS have the discretion to deem certain activities not to take place in South Africa? If in the affirmative, should this discretion also only be exercisable upon request?

Would the insertion of one or both of the discretions nullify the objective of introducing place of activity rules, i.e. to enhance interpretative certainty?

9 Fixed or permanent place of business

Should the terms fixed or permanent place of business be defined to provide more clarity?

10 "Lloyds of London" and "telecommunication services"

Would the removal of the terms "Lloyds of London" and "telecommunication services" from the definition of "enterprise" alter the width of the South African VAT net?

11 Place of activity of services

Should the place of activity of services distinguish between services capable of being physically rendered and those not capable of being physically rendered?

If in the affirmative, should the place of activity in respect of services not capable of being physically rendered be determined with reference to place of fixed or permanent business and not services capable of being physically rendered?

12 Agent Vs Principal

Would any of the place of activity rules in any way alter section 54? Should the rules in respect of services refer to agents as well?

13 Practical Examples

Please consider and provide us with some practical examples and test them against the proposed rules.

14 Explanatory Memorandum

Should thought be given to drafting a comprehensive explanatory memorandum, which explains the various provisions by way of practical examples?

Please direct your comments to any of the following people:

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Source: SAFA (2000)

**APPENDIX 8: COMPARATIVE ANALYSIS OF PLACE OF SUPPLY RULES IN
SOUTH AFRICA**

Nature of Supply	Place of Supply		
	Current Legislation	SAFA Proposals	Deloitte Proposals
<p><i>Services Physically Rendered in South Africa (SA) by Foreign Enterprise or Agent Acting on its behalf</i></p>	<p>SA (s7(l)(a))</p>	<p>SA</p>	<p><i>Where consumed; or if supplier has PE in SA the place is deemed to be in SA; or if supplier has no PE in SA, but consumed in SA and the recipients can claim full input tax deduction, the place of supply is deemed to be outside SA</i></p>
<p><i>Rights made available by Foreign Enterprise and used in South Africa (SA)</i></p>	<p><i>Where consumed (SARS' interpretation- VAT News 13 of December 1999)</i></p>	<p><i>Where supplier 's or agent's fixed or permanent place of business is from where services are supplied</i></p>	<p><i>Where consumed; or if supplier has PE in SA the place is deemed to be in SA; or if supplier has no PE in SA, but consumed in SA and the recipients can claim full input tax deduction, the place of supply is</i></p>

			deemed to be outside SA
Foreign Telecommunication Services Used in South Africa (SA)	SA (not promulgated)	Where supplier 's or agent's fixed or permanent place of business is from where services are supplied	Where consumed; or if supplier has PE in SA the place is deemed to be in SA; or if supplier has no PE in SA, but consumed in SA and the recipients can claim full input tax deduction, the place of supply is deemed to be outside SA
Underwriting Insurance Business by Underwriting Members of Lloyd's of London	Where contract is signed (1/1/2001)	Where supplier 's or agent's fixed or permanent place of business is from where services are supplied	Where consumed; or if supplier has PE in SA the place is deemed to be in SA; or if supplier has no PE in SA, but consumed in SA and the recipients can claim full input tax deduction, the place of supply is deemed to be outside SA

<i>Importation of Services into South Africa (SA)</i>	<i>Non-supply: reverse charging may apply (s7(l)(c))</i>	<i>Not addressed</i>	<i>Not addressed</i>
<i>Supplies of Goods in South Africa (SA) by Foreign Enterprise</i>	<i>SA (s7(l)(a))</i>	<i>Where goods are situated at time sale agreement is concluded</i>	<i>Where goods are placed at the disposal of the recipient</i>
<i>Importation of Goods into South Africa (SA) by Foreign Enterprise</i>	<i>Non-supply: look to subsequent supply (s7(l)(b))</i>	<i>Not addressed</i>	<i>Not addressed</i>
<i>Exportation of Goods from South Africa (SA) by Foreign Enterprise</i>	<i>SA (s7(l)(a))</i>	<i>Where goods are situated at time sale agreement is concluded</i>	<i>Where goods are placed at the disposal of the recipient</i>

Source: Deloitte (2000)