



Tax Alert

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Let's talk

For a deeper discussion of how this issue might affect your business, please contact:

Matthew Besanko

Cape Town
+27 (0) 78 827 6376
m.besanko@pwc.com

Rodney Govender

Durban
+27 (0) 82 211 8568
rodney.govender@pwc.com

Juan Swanepoel

Johannesburg
+27 (0) 83 604 1028
juan.s.swanepoel@pwc.com

Annemarie Janse van Rensburg

Cape Town
+27 (0) 71 326 5925
annemarie.janse.van.rensburg@pwc.com

VAT on the supply of electronic services: Where are we now?

In brief

The fallout from the global pandemic, the economic hardship caused by lockdowns and restrictions have left most governments around the world with no option other than to prioritise revenue collection.

With this in mind, the importance of indirect taxes and the significant role they play in assisting in revenue collection has come to the forefront once again with the South African Revenue Service (SARS) identifying the electronic services sector and its compliance with the electronic services VAT regulations as a focus area.

In detail

Background

National Treasury first introduced VAT regulations on electronic services supplied by foreign suppliers in 2014. The application of these regulations was limited to a specific prescribed list of electronic services, which predominantly focused on electronic services acquired by private individuals.

When the regulations were amended with effect from 1 April 2019, it became clear that there was a policy shift within National Treasury to include as many foreign electronic service suppliers in the South African VAT net as possible.

These amendments broadened the scope of electronic services by defining 'electronic services' as any service supplied by means of an electronic agent, electronic communication or the internet for any consideration. The amendments also introduced intermediary rules and allowed a concession for intercompany supplies, amongst others. However, the amendments did not make a distinction between business-to-business (B2B) and business-to-customer (B2C) supplies, which would have aligned the South African VAT treatment of B2B and B2C supplies with many other international jurisdictions.

As a result, the South African VAT rules are applicable to all electronic services supplied by a foreign service provider, regardless of the status of the recipient of those services.

Currently, a foreign electronic services supplier will be required to register for VAT in South Africa if at least two out of the following three requirements are met and the registration threshold (ZAR 1 million) has been exceeded:

- the recipient of the services is a South African resident;
- payment for the service originates from a South African bank account; or
- the recipient of the services has a business, residential or postal address in South Africa.

The following services are, however, excluded from the definition of electronic services:

- educational services provided by a person regulated by an educational authority;
- telecommunications services; and
- certain intercompany services.

Recent developments

The concept of human intervention.

Due to the broad scope of electronic services envisaged above, National Treasury and SARS, by reference in policy and guidance documents issued, explained that electronic services that involve significant human intervention are not intended to fall within the scope of the definition of 'electronic services' and the regulations, notwithstanding the wide definition included in the regulations. This exception was, however, not specifically contained in the principal Act or the regulation and is merely stated in the Explanatory Memorandum to the regulations and SARS guidance documents.

The guidance set out in the Explanatory Memorandum and SARS publications would regard, for example, a legal opinion drafted and provided to a South African client via email as non-electronic in nature as substantial 'human intervention' is required in order to complete this service; that is, the service in its nature is not electronic but rather characterised as legal services provided.

It is our understanding that SARS' view regarding the concept of human intervention is contrary to the policy and guidance documents (these guidance documents were issued by SARS in the form of FAQs) issued alongside the regulations; that is, SARS still views services that involve significant human intervention as electronic services.

Notwithstanding the guidance available, the interpretation currently applied by SARS would require the non-resident supplier of legal services (or similar services) to register for VAT in South Africa.

This is currently being discussed with SARS and National Treasury with a view to have clarity on SARS' approach, and potentially amendments to the principal Act that will eliminate any doubt.

Intermediary rules

Prior to the promulgation of the intermediary rules in 2019 and during discussions and engagements with National Treasury, it was submitted that in order to assist with compliance and administration, the legislation should make provision for the intermediary (marketplace) to account for VAT in respect of all supplies made via its platform. This would have removed the VAT administration and compliance burden for foreign electronic services suppliers.

However, when the legislation was promulgated and came into effect, it was drafted in such a way that the intermediary will only be allowed to account for VAT in respect of supplies made on behalf of a foreign electronic services supplier who is not registered for VAT in South Africa. The intermediary is not allowed to account for VAT on supplies made on behalf of foreign electronic services suppliers that are registered or are required to be registered for VAT in South Africa. In this case, the foreign electronic services supplier will have to account for such supplies in its own VAT return rendered to SARS.

Practical difficulties have arisen in administering this arrangement, as most intermediaries are unaware of the distinction and merely assume the VAT rules are aligned with other territories around the world. In most cases, this has resulted in the double payment of output tax on the same supply, i.e. by the electronic services supplier and the intermediary. In addition to the aforementioned, this manner of VAT accounting is also not practical in the scenario and adds drastically to intermediaries' and principal electronic services suppliers' administrative burden in accounting for VAT in a foreign jurisdiction.

It is suggested that electronic services suppliers approach SARS on an individual basis where there are difficulties or impracticalities experienced.

SARS task team

SARS has identified the electronic services sector as an area of focus and established a specific division to review the sector and ensure compliance.

The division is actively pursuing foreign electronic services suppliers that failed to register for VAT in South Africa by approaching the South African Reserve Bank (SARB) and local businesses for information relating to foreign payments made from South Africa in order to identify suppliers.

Where payments made to non-registered electronic services suppliers are identified, SARS would issue requests for information and reasons as to why no VAT registration was obtained. Following this, SARS will register the foreign electronic services supplier for VAT and assess it for all VAT due on the past supplies of electronic services to South African recipients.

The takeaway

The absence of specific reference to the concept of human intervention in the principal Act has created uncertainty around the scope of the electronic services rules. The view taken by SARS, which appears to be contrary to the guidance provided, has added to this uncertainty and foreign electronic services providers are thus encouraged to investigate whether the services they render to South African recipients could be affected by this.

Foreign electronic services providers and intermediaries need to be made aware of the practical difficulties caused by the intermediary rules. While it is uncertain whether the principal Act will be amended to align the South African intermediary rules with other international jurisdictions, there is an opportunity for foreign electronic services providers to approach SARS on a case-by-case basis to seek dispensation to obtain approval to only account for VAT on supplies made via its own platform on the basis that the intermediary would account for VAT on supplies made via the intermediary's platform.

As SARS is now actively engaged in identifying non-compliance amongst foreign electronic services suppliers, it has become imperative for such suppliers to determine whether the services they supply to South African recipients fall within the 'electronic services' definition and whether they have met the VAT registration requirements.

Any delays by the foreign services provider to register for VAT and regularise its tax position may be costly due to additional penalties and interest arising.



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