

VAT registration of foreign online suppliers not limited to supplies of e-books

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The recent amendments to the VAT legislation introduced by the Taxation Amendment Act, No 31 of 2013, gives effect to government's proposal that all foreign businesses supplying e-books, e-music and other digital goods and services in South Africa be required to register as South African value-added tax ("VAT") vendors. Government indicated that the proposal is in line with international trends such as regulations adopted by the European Union requiring such suppliers to register for VAT in the country where the consumer resides.

The amendment has the effect that from 1 April 2014, all persons supplying electronic services from a place outside of South Africa will be required to register as VAT vendors where they make supplies of electronic services to South African customers who are either tax resident in South Africa, or where payment for the services by such customers originates from South African banking accounts. Suppliers of electronic services will be considered to be carrying on an enterprise in South Africa and will be required to register as VAT vendors if they makes taxable supplies in excess of R50 000 in a 12 month period. Once registered, they will be required to levy and account for VAT on supplies made by them.

The amendments were introduced mainly to address the concerns of local publishers and booksellers with respect to VAT not being declared and paid on purchases of e-books by South African consumers from foreign suppliers. This placed the local industry at a competitive disadvantage owing to the fact that the foreign suppliers enjoying an effective 14% VAT

discount on their prices as compliance with the reverse charge mechanism was virtually non-existent.

The Minister of Finance recently released draft regulations in terms of which he prescribes what constitutes 'electronic services' for purposes of the VAT Act and for which foreign suppliers must register for VAT in South Africa. The scope of these draft regulations is, however, far reaching and much wider than originally anticipated.

In terms of the draft regulations, it is not only the suppliers of e-books, e-music or similar digital products to South African consumers who will be required to register for VAT. The draft regulations also include the provision of "information system services" as defined in the Electronic Communications and Transactions Act No. 25 of 2002. This definition is extremely broad and includes the provision of connections, the operation of facilities for information systems, the provision of access to information systems, the transmission or routing of data messages between points and the processing and storage of data. This means that all forms of electronic supplies such as information system services; internet based courses; webinars; the administration, maintenance and technical support of a web site, database or information system; data storage and the supply of software are all included.

Examples of foreign businesses that will be drawn into the VAT net in addition to suppliers of e-books and digital music or videos are the following:

Foreign entities that arrange video conferencing facilities for South African businesses to communicate with their foreign customers, branches, divisions, or head offices;

Foreign entities that provide South African business customers the facility to store digital data offsite; and

Foreign holding or group companies that have a centralised

service function, supplying information technology services, credit vetting, back-up and support services, etc.

The draft regulations therefore not only apply to Business-2-Consumer (B2C) transactions but it also apply to Business-to-Business (B2B) transactions. It is questionable as to what benefit would accrue to the fiscus on B2B transactions if the net impact on the fiscus is nil, as any VAT charged by the supplier will be deductible as input tax by the recipient, coupled with the increased administration for both the South African Revenue Service ("SARS") and the foreign supplier. No concern has been expressed by the SARS regarding the compliance with the current reverse charge mechanism in the case of partially taxable recipients who need to account for VAT on the imported services.

A further challenge is the implementation date of 1 April 2014 in view of the uncertainty as to which foreign entities are required to be registered for VAT whilst the regulations are not yet finalised. The current wide reach of the draft Regulations will potentially bring an innumerable number of foreign entities into the South African VAT net. In light of the current onerous registration process, particularly for foreign entities, it is questionable whether SARS will be able to cope with all of the VAT registration applications in time for the 1 April 2014 implementation date. A further impediment with the registration of foreign entities lies in the opening of a South African bank account, which is a requirement before an entity can even apply for VAT registration in South Africa. This is owing to the requirement of South African banks to comply with the Financial Intelligence Centre Act, 2001.

It is not an option for a foreign entity supplying electronic services to South African entities not to register for VAT in South Africa. A person who is liable to register and fails to do so is guilty of an offence and is liable to a fine or imprisonment for a period not exceeding two years.

Furthermore, a person may also be subject to further penalties for failure to register, as well as penalties and interest on output tax not accounted for from the time such person first became liable to register. Once the regulations listing the type of electronic services that are to be subject to VAT in South Africa are finalised, foreign suppliers should carefully consider their VAT registration obligations in South Africa, and apply for registration timeously.