VAT on the supply of “electronic services” (hereafter “e-services”).

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In the 4th industrial revolution, digital trade allows for firms to bring in new products and services to a larger pool of digitally connected customers located anywhere in the world. It allows for digitally enabled transactions of goods and services which can either be digitally or physically delivered. Most noteworthy examples include the purchase of a book through an online marketplace such as Amazon, booking a stay in an apartment through a matching digital application such as Airbnb, hailing a taxi through the application Uber and accessing online course material from a foreign tertiary institution at the convenience of your own home.

The efficiency and convenience of digital-enabled but physically delivered transactions of goods and services poses new challenges in the way international trade and investment policies are made. As digitalisation undermines the traditional structure, in which businesses normally had some sort of physical presence (referred to as a “permanent establishment”) in a given jurisdiction, which gave tax authorities, such as SARS, a tangible basis against which to secure tax compliance.

In terms of the Value Added Tax Act 89 of 1991 (hereafter “VAT Act”) of South Africa (hereafter referred to as “RSA”) these digitally enabled transactions blur the already grey line of what constitutes a “good” and a “service”.
It was, therefore, necessary that the OECD delivered guidance on how to collect VAT on cross-border sales of digital goods and services, beginning with the International VAT Guidelines, released in 2015 and updated in 2017. The guidelines state that non-resident suppliers must register for, charge, collect and remit VAT/GST in the jurisdiction where the customer is located, generally via a form of simplified registration process. This is consistent with the 'destination principle', in that the jurisdiction of consumption is entitled to impose indirect tax on the supply.

In terms of the registration requirements of an “e-service provider” found in section 23(1A) of the VAT Act, a person must register by completing a VAT 101 form if that person carries on or intends to carry on an “enterprise” as defined in section 1 of the VAT Act and exceeds the

registration threshold of ZAR 1 million in any consecutive 12-month period. The foreign suppliers of e-services and intermediaries who facilitate the supply of e-services are required to account for VAT on the payment's basis.

The framework of the "destination principle" in RSA is encapsulated in section 1(1)(b)(vi) of the VAT Act (effective from 1 April 2015) and is triggered when at least two of the following three requirements are present from a place in an export country (i.e., any place outside the RSA):

(1) the supply of e-services is to a person who is a RSA resident or
(2) the recipient of those e-services has a business address, residential address or postal address in the RSA or
(3) any payment to that person in respect of such e-services originates from a RSA bank.

Therefore, if a foreign e-service provider qualifies the destination principle then it will be regarded as carrying on an "enterprise" for VAT purposes in the RSA.

The scope of services that qualified as "e-services" in section 1 of the VAT Act was **significantly broadened** by the amended regulations effective from 1 April 2019.

The amended regulations define "e-services" to be those services supplied using an:

(a) electronic agent
(b) electronic communication or
(c) the internet.

The qualifying test in this regard is if:

i. These services are dependent on information technology,
ii. They are automated and
iii. They involve minimal human intervention.

However, supplies of services by electronic means, which are exempt under section 12 of the VAT Act, (which includes financial services) are not subject to VAT under these Regulations.

The SARS has published FAQs in respect of the anomalies that occur in the supply of e-services.

What is understood by these anomalies are:

1. **What is not an "e-service":**
   - A legal opinion that is issued by a non-resident legal practitioner in a foreign jurisdiction for example the UK and thereafter emailed to a RSA client. The supply of online training programmes if the training director actively presents the course to a student via an online streaming platform.
     - This is because the service, although transmitted using electronic communication (i.e., via email, Zoom, Microsoft teams), is not dependent on information technology and involves substantial human intervention.

   - Limited inter-group supplies exclusion: The inter-group exclusion applies where a non-resident company and a resident company form part of the same "group of companies" and the non-resident company itself supplies the e-services exclusively for the purposes of consumption of those services by the resident company. A "group of companies" for this purpose means two or more companies where one company directly or indirectly holds at least 70% of the equity shares of the other company.

However, the e-service must be exclusively discovered, devised, developed, created, or produced by the non-resident. If any of the elements of the service is acquired or procured from another party and not exclusively produced by the non-resident entity, the group company exclusion may not apply.

- Regulated foreign educational services exclusion.
- Telecommunication services exclusion.

2. What is an "e-service":

- The supply of online training programmes, which may have involved extensive human intervention during the development stages but are subsequently supplied online.
- The supply of a mobile applications.
- This is because the online training programmes and mobile applications are ultimately supplied via the internet and are not dependent on further human intervention at the time of supply.

However, it was found in the Supreme Court of Appeal in the case of ***Diageo South Africa (Pty) Ltd v Commissioner for the South African Revenue Service (330/2019) [2020] ZASCA 34*** that section 8(15) of the VAT Act requires that a single supply of goods or services comprising parts that would each, if they had been supplied separately, have attracted a different rate of tax be deemed to be a separate supply of goods or services. In this regard, the anomaly exists when considering the aspect of "minimal human intervention" in whether for example the online training program would fall outside the ambit of "e-services "if a client has access to the training director either during or after consuming the course material online. In this regard, the supply of supplementary services by the training director could be regarded as a "separate supply" that could have its own VAT implications outside the e-service VAT framework for example such as the importation of services in terms of section 7(1)(c) of the VAT Act. This stems from the principle found in terms of section14(5)(*a*) of the VAT Act which states that imported services cannot be chargeable to VAT twice (that is to say, under s 7(1)(*a*) and (*c*)). Shortly put, in the case when a service falls outside the ambit of "e-services", one needs to consider if the imported service which is not an e-service is either standard or zero rated in terms of the general provisions of VAT Act pertaining thereto.

An enterprise in terms of section 20(5B) of the VAT Act must therefore be careful and account for the value and VAT chargeable implications of a composite supply. This is done separately on a VAT invoice in line with the requirements as set out in the 10 December 2021 SARS regulations. The SARS regulations amongst others require that the VAT invoice reflect the consideration in money for the e-supply in the currency of any country and states:

If reflected in South African Rand (ZAR):

a. the amount of VAT charged or
b. a statement that the consideration includes a charge for VAT and the rate at which VAT was charged.

If reflected in any currency other than ZAR:

a. the amount of tax charged in ZAR or
b. a separate document issued by the e-services supplier to the e- services recipient reflecting the amount of tax charged in ZAR.

In both scenarios the value of the supply (VAT-exclusive amount) is also required to be reflected in ZAR.

The exchange rate applicable is that of:

a. The South African Reserve Bank (SARB).
b. Bloomberg, or
c. European Central Bank

Generally, for suppliers of e-services, the issuing of the invoice and the payment will be on the same date. However, time of supply rules when accounting for the supply of e-services is the earlier of the time an invoice is issued, or payment is received as determined in section 9(1) of the VAT Act.

We further draw reference to section 143(a) of the Tax Administration Act, No. 28 of 2011 (hereafter "TAA"), which states a person who wilfully and without just cause fails or neglects to register as a VAT Vendor is guilty of a criminal offence and is liable on conviction to a fine or to imprisonment for a period not exceeding two years. In terms of section 22(5) of TAA where a taxpayer fails to register as a VAT Vendor, SARS may register the taxpayer for one or more tax types, as is appropriate under the circumstances. Furthermore, a person may also be subject to further penalties for the failure to register, as well as up to 200% penalties of tax payable for non-compliance with RSA VAT obligations and interest on output tax not accounted for from the time such person first became liable to register. Foreign suppliers of e-services should therefore carefully consider their VAT registration obligations in the RSA and should ensure that they comply with the revised Regulations and VAT legislation by consulting our network.

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