The impact of the 2018 VAT rate increase on the South African tax policy on the zero-rating of merit goods

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Mini-dissertation submitted in partial fulfilment of the requirements for the degree Masters in South African Taxation at the University of Cape Town

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Word count: 22,298

Declaration

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Abstract

The 2018 Value-Added Tax (VAT) rate increase caused a national debate on the regressive nature of VAT and its impact on the poor. This study assessed whether an appropriate response is to include further zero-rated items and to analyse which items should be selected.

This study confirmed that VAT is regressive, and the instruments used to address this issue is to either introduce the zero-rating of 'merit goods' or to use cash transfers in a social grant system. Given that a significant portion of the South African government expenditure is already spent on the social grant system and has not yet resulted in a significant decline of income inequality, the appropriate response to the 2018 VAT rate increase is to expand the list of zero-rated items.

This study performed an analysis on the South African spending patterns per income group to identify the food items most consumed by the poor. The notable items included; poultry, beef, aerated soft drinks, white bread and white sugar, however these items would result in a significant loss of tax revenue, which is an inherent issue with a zero-rating amongst others. As the purpose of the 2018 VAT rate increase was to address the significant fiscal budget deficits over the last few years it would not be rational to introduce a zero-rating which would effectively eliminate the tax revenue needed to balance the fiscal budget. The government's response was to include sanitary pads, cake wheat flour and white bread wheat flour be zero-rated, which do not result in such a significant tax loss.

Therefore, the selection of items in the current South African economic environment would involve a balancing act between providing relief to the poor but not at the expense of a significant share of tax revenue.

Acknowledgements

I would like to express my gratitude to my supervisor Professor Jennifer Roeleveld for the useful comments, remarks and engagement through the learning process of this master thesis. Furthermore, I would like to thank colleagues for introducing me to the topic as well for the support on the way. I would also like to thank my family and friends, who have supported me throughout the entire process, and especially for all the words of motivation and encouragement.

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Glossary

Abbreviation	**Term**
BURS	Botswana Unified Revenue Service
CEMAC	Communauté Economique et Monétaire de l'Afrique Central
CEN–SAD	Community of Sahel–Saharan States
CIT	Corporate Income Tax
COMESA	Common Market for Eastern and Southern Africa
COSATU	Congress of South African Trade Unions
DRC	Democratic Republic of Congo
DTC	Davis Tax Committee
EAC	East African Community
ECCAS	Economic Community of Central African States
ECOWAS	Economic Community of West African States
FIRS	Federal Inland Revenue Service (Nigeria)
GST	General Sales Tax
HS or HBS[1]	Harmonized System
IBFD	International Bureau of Fiscal Documentation
IDRC	International Development Research Centre
IES	Income and Expenditure Survey
IGAD	Intergovernmental Authority on Development
IMF	International Monetary Fund
IVA	Imposto sobre o Valor Acrescentado*
KRA	Kenya Revenue Authority
LCS	Living Conditions Survey
LRA	Lesotho Revenue Authority
MRA	Mauritius Revenue Authority
OECD	Organization for Economic Co-operation and Development
PIT	Personal Income Tax

[1] HS and HBS refers to classifying goods with a six-digit code system for customs purposes. Source: United Nations Trade Statistics. (2019) *'Harmonized Commodity Description and Coding Systems (HS)'.* Available at: https://unstats.un.org/unsd/tradekb/Knowledgebase/50018/Harmonized-Commodity-Description-and-Coding-Systems-HS (Accessed: 20 August 2019).

REC	Regional Economic Community
SACU	Southern African Customs Union
SADC	Southern African Development Community
SARS	South African Revenue Service
SDL	Skills Development Levy
South Africa	Republic of South Africa
SRA	Swaziland Revenue Authority
SRC	Seychelles Revenue Commission
Stats SA	Statistics South Africa
TRA	Tanzania Revenue Authority
UMA	Arab Maghreb Union
VAT	Value-Added Tax
VAT Act	Value-Added Tax Act No 89 of 1991
VATCOM	Value-Added Tax Committee
ZIMRA	Zimbabwe Revenue Authority

Chapter 1: Introduction and background to this study

1.1 Introduction:

Taxes on income, wealth and sales, in some form or another have been around for centuries, whereas value-added tax (VAT) is a fairly modern concept.[2] During World War 1, the earlier stages of a VAT system was designed in the form of a consumption tax.[3] Subsequently the VAT system evolved with the first formalised system implemented in France in 1954. Before the introduction of VAT, most countries were utilising a form of sales tax to expand their national revenue base. Since its implementation, a global trend emerged over the last few decades with nations replacing their sales tax system with a modern VAT system.[4]

The Republic of South Africa[5] was no exception to this global trend and adopted its form of a VAT system in the 1990's. South Africa has six main categories of tax revenues which include; personal income tax (PIT), corporate income tax (CIT), skills development levy (SDL), taxes on property, VAT, and taxes on international trade and transactions.[6] Figure 1 illustrates the split of these South African tax revenues.

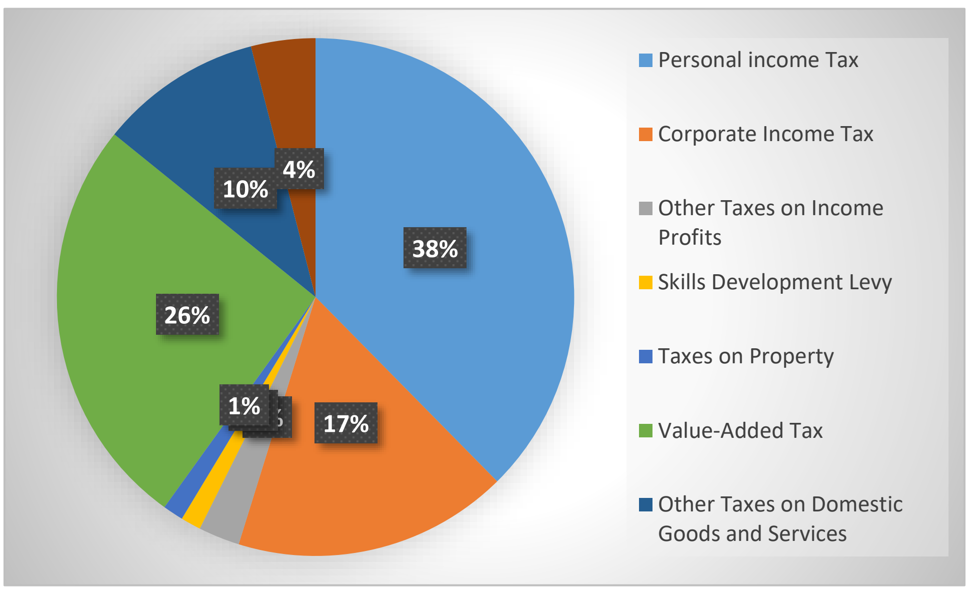

Figure 1. Budgeted tax revenue split per category. Source: Republic of South Africa (2018) National Treasury 2018 budget - www.treasury.gov.za.

[2] Charlet, A and Owens, J. (2010) '*An International Perspective on VAT',* Tax Notes International, 59(12), pp 943.
[3] Kearny, M. (2003) *'Restructuring Value-Added Tax in South Africa: A Computable General Equilibrium Analysis'*, pp 34. Available at: https://repository.up.ac.za/bitstream/handle/2263/27705/Complete.pdf?sequence=9&isAllowed=y (Accessed: 2 January 2019).
[4] Charlet, A and Owens, J. (2010) pp 943.
[5] Referred to as South Africa.
[6] Republic of South Africa. (2018) *'National Treasury Budget Speech 2018',* pp 11. Available at: http://www.treasury.gov.za/documents/national%20budget/2018/speech/speech.pdf (Accessed: 14 January 2019).

VAT is the second largest tax revenue source, and this has been increasing over the last few years, whereas the percentage increase for PIT has been decreasing (as evidenced by the trend analysis on tax revenues in Figure 2 and Figure 3 based on the Fiscal Budgets for 2014, 2015, 2016, 2017 and 2018).

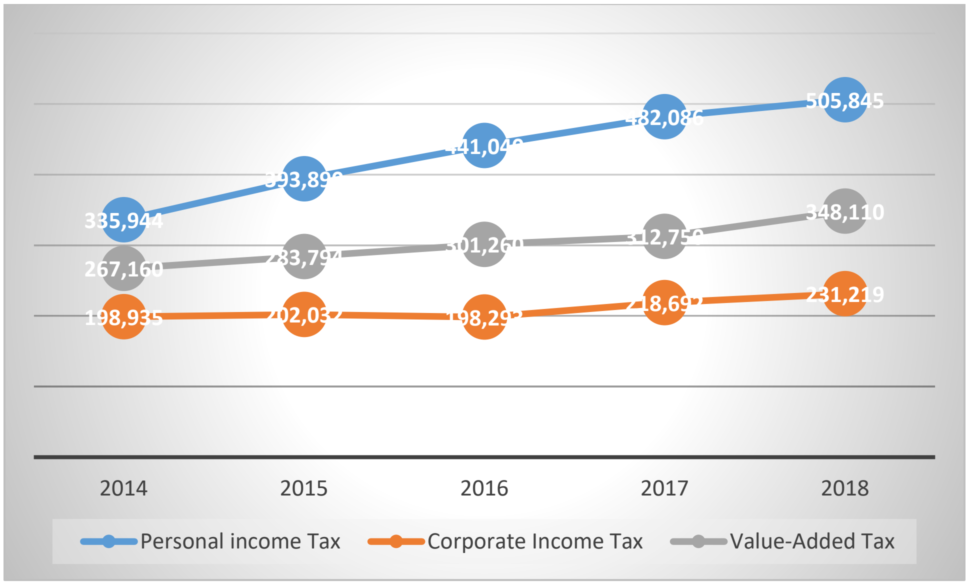

Figure 2. Tax revenue trend. Source: Adapted from National Treasury 2014, 2015, 2016, 2017 and 2018 Budget Review - www.treasury.gov.za

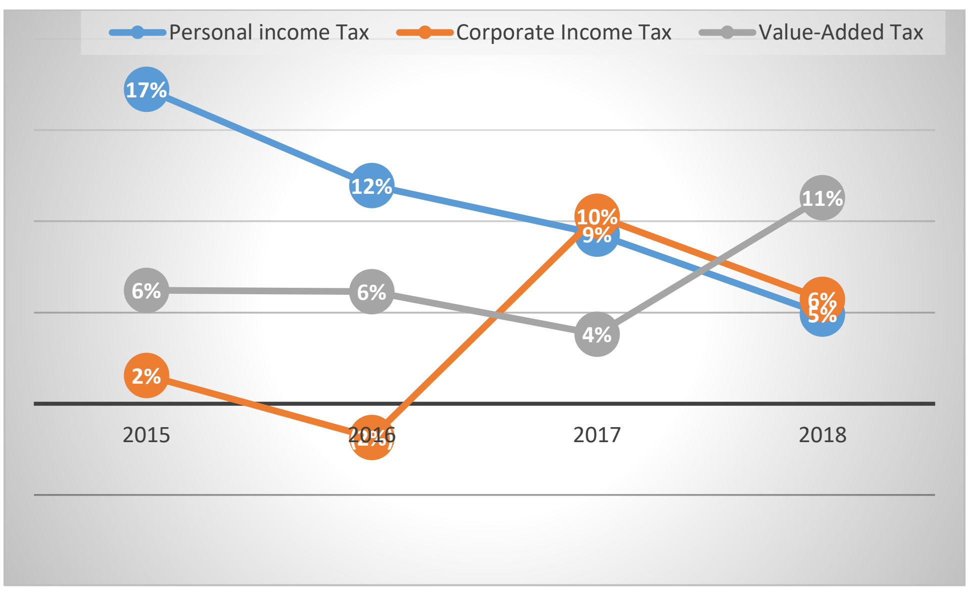

Figure 3. The percentage movement in CIT, PIT and VAT. Source: Adapted from National Treasury 2014, 2015, 2016, 2017 and 2018 Budget Review - www.treasury.gov.za

Poverty is one of the key issues in South Africa and a focus area for the South African government has been the redistribution of wealth.[7] Due to the design of VAT being that the end consumer bears the VAT cost,[8] VAT is

[7] Jansen, A. and Calitz, E. (2017) *'Considering the efficacy of value-added tax zero-rating as pro-poor policy: The case of South Africa',* Development Southern Africa, 34(1), pp. 56.

regarded as a regressive tax as the poor have a larger proportion of their income being taxed as opposed to the more wealthy where the tax is a smaller percentage of their disposable income.[9] Since its introduction VAT has been considered an emotional and political issue, especially given the income demographics of South Africa and trade unions such as COSATU are resistant to increases in the VAT rate.[10] Contrary to this view, academics and policy-makers have reiterated that a fiscal policy is not solely dependent on VAT as a revenue instrument but includes other taxes such as taxes on income and profits, and property amongst others and a fiscal policy may still be considered progressive irrespective of whether a portion of tax revenue is collected from VAT that in its design has elements of a regressive tax for some.[11]

Since VAT has been adopted policymakers have made some concessions specifically to support poorer households in South Africa. In the current VAT legislation, the following relevant zero-rated provisions are included:

- Section 11(1)(j): "goods consist of such foodstuffs as are set forth in Part B of Schedule 2"; and
- Section 11(1)(l): "goods consist of illuminating kerosene (marked) intended for use as fuel for illuminating or heating."[12][13]

1.2 Background:

1.2.1. The introduction of VAT:

Prior to the current VAT era, South Africa raised a portion of its revenue from prevailing general sales tax (GST), where the GST rate was 13% at the time[14]. A Commission of Inquiry, known as the Margo Commission, was established to consider the tax structure of South Africa, and in 1987/88 released its findings where it recommended that the current tax regime of GST should be abandoned, and a new tax known as VAT be introduced to replace it, due to the GST system having many inherent problems in respect of recovery of taxes and the common incidence of tax evasion.[15] Another contributing factor was the loss of tax revenue due to the many GST food exemptions.[16]

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8 Inchauste, G. et al (2015) *'The Distributional Impact of Fiscal Policy in South Africa'*, pp 40. Available at: http://worldbank.org/drm/documents (Accessed:16 May 2018).
9 Kearny, M. (2003) *'Restructuring Value-Added Tax in South Africa: A Computable General Equilibrium Analysis',* pp 45. Available at: https://repository.up.ac.za/bitstream/handle/2263/27705/Complete.pdf?sequence=9&isAllowed=y (Accessed: 20 January 2019).
10 Jansen, A., Stoltz, E. and Yu, D. (2013) *'The Targeting of Zero-Rated Basic Foodstuffs under Value-Added Tax (VAT) in South Africa',* Journal for Studies in Economics and Econometrics, 37(3), pp. 87.
11 Inchauste, G. et al (2015) pp 40.
12 "Referred to in Fuel Item Levy number 195.10.13 in Part 5A of Schedule No.1 to the Customs and Excise Act and are not mixed or blended with another substance." Extract from the Value-Added Tax Act, 1991.
13 Republic of South Africa. (1991) Value-Added Tax Act, 1991 (No. 89 of 1991). Government Gazette No. 13307 12 June 1991 (Published under Government Notice R1342).
14 Kleu, M. Prinsloo, J.W. and Venter, L. P. (1993) *'Notes on the value-added tax base of South Africa'* South African Reserve Bank Quarterly Bulletin No 188, pp 30. Available at: https://www.resbank.co.za/Lists/News%20and%20Publications/Attachments/5182/04Notes%20on%20the%20value-added%20tax%20base%20of%20South%20Africa.pdf (Accessed: 5 April 2018).
15 Kleu, M. Prinsloo, J.W. and Venter, L. P. (1993)
16 Republic of South Africa. (1988) *'White Paper on the Report of the Commission of Inquiry into the Tax Structure of the Republic of South Africa: (the Margo Report)'.* Govt. Printer, 1988.

The draft Value-Added Tax Bill (draft bill) was published on 18 June 1990 and was based on the VAT system introduced in New Zealand[17] with no mention of a prescribed rate. Refer to Annexure A for the evolution of the VAT rate. The draft VAT bill[18] included an exemption for medicine and medical services,[19] but did not contain any concessions in respect of food items.[20]

1.2.2 The establishment of the VATCOM:

A committee, known as the VATCOM, was appointed by the Minister of Finance at the time "to consider the comments and representations made by interested parties on the Government's draft Value-Added Tax Bill."[21] In 1991 the VATCOM concurred with the initial position that the most efficient and preferable VAT system is for all foodstuffs to be subject to VAT, but the report did acknowledge that in the South African context the VAT treatment of basic foods was a most sensitive and emotional issue to consider when introducing a VAT system.[22]

Basic Foodstuffs:

The VATCOM report commented that:

> "The use of a tax system to achieve social objectives, such providing relief to the needy by exemption of basic foodstuffs is a very inefficient means, unless the exemption is restricted to foodstuffs which are used predominantly or exclusively by the needy."[23]

The concept of zero-rating a list of basic food items suffers from the following shortcomings, namely;" difficulties in defining the goods, creating the opportunity for evasion, adding complexity to the system and costs to the vendor and inefficiency because the concession is not targeted to the needy."[24]

In addition, the VATCOM was hesitant in making its recommendations as it believed that if items were to be given special treatment (i.e. VAT zero-rate), it could set a precedent and may make it difficult to refuse any further special treatment requests or revoke the special treatment to the items included in such list in the future.

The VATCOM made the recommendations that:

> (i) "a limited number of goods which are presently exempted from GST such as maize products, rice, bread and milk powder, be zero-rated";[25]

[17] Marais, G. (1991) *'Report of the Value-Added Tax Committee (VATCOM)'.* Pretoria: Govt. Printer, pp 1.
[18] Draft Value-Added Tax Bill: Published in Government Notice 479 of 1990 in Government Gazette No. 12514 on 18 June 1990.
[19] This proposed exemption was deleted based on the views of the VATCOM.
[20] Republic of South Africa. (1991) *'Explanatory Memo on the Value-Added Tax Bill'.* Available at: http://www.osall.org.za/docs/2011/02/1991-VAT-Bill.pdf (Accessed: 1 September 2019).
[21] Marais, G. (1991) *'Report of the Value-Added Tax Committee (VATCOM)'.* Pretoria: Govt. Printer, pp 1.
[22] Marais, G. (1991) pp 17.
[23] Marais, G. (1991) pp 18.
[24] Marais, G. (1991) pp 18-19.
[25] Marais, G. (1991) pp 18-19.

(ii) “direct budgetary assistance be provided to the needy outside the tax system which will compensate them effectively for the increase of costs because of the introduction of VAT. The assistance outside the tax system to those persons in the welfare system could be best achieved by increasing social pensions, grants and subsidies to compensate for the effect of VAT.”[26]

1.2.3 The response to the VATCOM report:

In the Annual Fiscal Budget for 1991/92, the Minister of Finance announced that VAT at 12% would be introduced to replace GST with an effective date of 30 September 1991.[27] However, the VATCOM report suggested that the introductory percentage should be 10% to ensure public acceptance of the change in tax system.[28]

In addressing the concerns of stakeholders and to alleviate the burden of the poorer households, the Minister of Finance announced on the 17 July 1991 that brown bread and maize meal would be included in the zero-rating provisions in section11(1), and on the 21 August 1991 that the prescribed standard VAT rate would be reduced to 10%.[29] However, neither the concession in respect of brown bread and maize meal nor the reduction of the proposed VAT rate was enough to address the concerns of the stakeholders and interested parties, and protest action occurred.[30] The Minister of Finance responded by announcing on 29 September 1991, that additional basic food items would be included, until 31 March 1992. Nevertheless, the expiry date initially announced was later withdrawn and the zero-rating of food items became a permanent feature of the South African VAT system except for rice and fresh milk that were removed from the list in March 1992[31] but reinstated in 1993 (refer to Annexure A for the evolution of the list of basic food items).

The list in 1991 comprised of the following ten permanent items:

Item Number	Item Description
Item 1	“Brown bread”[32]
Item 2	“Maize meal”[33]
Item 3	“Samp”[34]
Item 4	“Mealie rice”[35]

[26] Marais, G. (1991) *‘Report of the Value-Added Tax Committee (VATCOM)’.* Pretoria: Govt. Printer, pp 18-19.
[27] Kleu, M. Prinsloo, J.W. and Venter, L. P. (1993) *‘Notes on the value-added tax base of South Africa’* South African Reserve Bank Quarterly Bulletin No 188, pp 30. Available at: https://www.resbank.co.za/Lists/News%20and%20Publications/Attachments/5182/04Notes%20on%20the%20value-added%20tax%20base%20of%20South%20Africa.pdf (Accessed: 5 April 2018).
[28] Marais, G. (1991) pp 13.
[29] Katz, M. (1994) *‘Interim report of the Commission of Inquiry into Certain Aspects of the Tax Structure of South Africa’.* Pretoria: The Commission, pp 104.
[30] Parliament Monitoring Group. (2011) 'Value-Added Tax 1991-2011' Presentation to the Standing Committee on Finance’ (23 March 2011), pp 7. Available at: http://pmg-assets.s3-website-eu-west-1.amazonaws.com/docs/110323VATSA.pdf (Accessed: 1 September 2019).
[31] Katz, M. (1994) pp 104.
[32] As defined in Regulation 1 of the Regulations in terms of Government Notice R.577 published in Government Gazette No. 13074 of 15 March 1991.
[33] “Graded as super maize meal, special maize meal, sifted maize meal or unsifted maize meal not further processed other than by addition of minerals and vitamins not exceeding one percent by mass of the final product, solely for the purpose of increasing the nutritional value.” Extract from the Value-Added Tax Act, 1991.
[34] “Not further prepared or processed.” Extract from the Value-Added Tax Act, 1991.
[35] “Not further prepared or processed.” Extract from the Value-Added Tax Act, 1991.

Item 5	"Dried silo screened mealies or dried mealies"[36]
Item 6	"Dried beans"[37]
Item 7	"Lentils"[38]
Item 8	"Pilchards or sardinella supplied in tins or cans"[39]
Item 9	"Milk powder"[40]
Item 10	"Dairy powder blend"[41]

Figure 4. Schedule 2 Part B list in 1991 (wording as in the 2019 VAT Act). Source: Value-Added Tax Act No 89 of 1991.[42]

1.2.4 The VAT rate increase in April 1993:

In early 1993 there were still public protests supported by trade unions such as the Congress of South African Trade Unions (COSATU) resisting the introduction of VAT due to its regressive nature.[43] In response a further nine items were added to the list of zero-rated foodstuffs in Part B of Schedule 2 as of the 7 April 1993. In addition, the VAT rate increased from the introductory rate of 10% to 14% on the same day.[44] The expanded list in 1993 included the following nine items:

Item Number	Item Description
Item 11	"Rice"[45]
Item 12	"Vegetables"[46]
Item 13	"Fruit"[47]
Item 14	"Vegetable oil"[48]
Item 15	"Milk"[49]

[36] "Not further prepared or processed or packaged as seed but excluding popcorn (zea mays everta)." Extract from the Value-Added Tax Act, 1991.
[37] "Whole, split, crushed or in powder form but not further prepared or processed or where packaged as seed." Extract from the Value-Added Tax Act, 1991.
[38] "Dried, whole, skinned or split." Extract from the Value-Added Tax Act, 1991.
[39] "Consisting mainly of such products regardless of whether flavoured, seasoned or preserved in oil, but excluding such products as are supplied as pet food or sardines supplied in tins or cans." Extract from the Value-Added Tax Act, 1991.
[40] "Unflavoured, being the powder obtained by the removal of water from milk and which falls under the following classifications determined by the Minister of Agriculture under the Agricultural Product Standards Act 1990 (Act No. 119 of 1990), or any regulation under that Act: High-fat milk powder, Full-fat milk powder, Medium-fat milk powder, Low-fat milk powder, Fat-free milk powder,
Provided the fat or protein content of such milk powder consists solely of milk fat or milk protein." Extract from the Value-Added Tax Act, 1991.
[41] "Being any diary powder blend, which falls under the following classifications determined by the Minister of Agriculture under the Agricultural Product Standards Act, 1990 (Act No. 119 of 1990), or any regulation under this Act: High-fat dairy powder blend, Full-fat dairy powder blend, Medium-fat dairy powder blend, Low-fat dairy powder blend, Fat-free dairy powder blend." Extract from the Value-Added Tax Act, 1991.
[42] Republic of South Africa. (1991) Value-Added Tax Act, 1991 (No. 89 of 1991). Government Gazette No. 13307 12 June 1991 (Published under Government Notice R1342).
[43]Jansen, A., Stoltz, E. and Yu, D. (2013) *'The Targeting of Zero-Rated Basic Foodstuffs under Value-Added Tax (VAT) in South Africa',* Journal for Studies in Economics and Econometrics, 37(3), pp. 88*.*
[44] Parliament Monitoring Group. (2011) *'Value-Added Tax 1991-2011'* Presentation to the Standing Committee on Finance' (23 March 2011), pp 7. Available at: http://pmg-assets.s3-website-eu-west-1.amazonaws.com/docs/110323VATSA.pdf (Accessed: 1 September 2019).
[45] "Whether husked, milled, polished, glazed, parboiled or broken." Extract from the Value-Added Tax Act, 1991.
[46] "Not cooked or treated in any manner except for the purpose of preserving such vegetables in their natural state, but excluding dehydrated, dried, canned or bottled vegetables or such vegetables as described under separate Items in this Part." Extract from the Value-Added Tax Act, 1991.
[47] "Not cooked or treated in any manner except for preserving such fruit in its natural state, but excluding dehydrated, dried, canned or bottled fruit and nuts." Extract from the Value-Added Tax Act, 1991.
[48] "Marketed and supplied for use in the process of cooking food but excluding olive oil." Extract from the Value-Added Tax Act, 1991.
[49] "Including high-fat, full-fat, low-fat or fat-free milk, being milk of cattle, sheep or goats that has not been concentrated, condensed, evaporated, sweetened, flavoured, cultured or subjected to any other process other than homogenisation or preservation by pasteurisation, ultra-high temperature treatment, sterilisation, chilling or freezing or addition of minerals, vitamins, enzymes and other similar additives not

Item 16	"Cultured milk"[50]
Item 17	"Brown wheaten meal"[51]
Item 18	"Eggs"[52]
Item 19	"Edible legumes and pulse of leguminous plants"[53]

Figure 5. Schedule 2 Part B additional list in 1993 (wording as in the 2019 VAT Act). Source: Value-Added Tax Act No 89 of 1991.[54]

1.2.5 The Katz Commission

In 1994 the Katz Commission in its First Interim Report of the Commission of Inquiry into certain aspects of the tax structure of South Africa dealt with the question of taxes and the role of non-tax instruments as poverty relief measures. The report concluded that:

(i) "The further erosion of the VAT base through zero-rating or exemptions should not be considered in view of the limited contributions which such measures make to the relief of poverty";[55]

(ii) "A higher tax on luxury goods or a multiple VAT rate system should not be adopted, in view of the limited contributions which such measures to reducing the regressivity of the VAT, the administration and compliance costs involved, and the limited potential for raising additional revenue thereby."[56]

Further, the Katz Commission recommended that, *"*revenue authorities should from time to time review the current basket of zero-rated goods, with reference, inter alia, to the distributional aspects."[57] In addition it stated that, "it might be possible, based on equity considerations, to improve on the present basket of zero-rated goods."[58]

exceeding one percent by volume of the final product, solely for the purpose of increasing the nutritional value." Extract from the Value-Added Tax Act, 1991.

[50] "Being cultured milk as classified under the Agricultural Product Standards Act 1990 (Act No. 119 of 1990), with the following class designation: Cultured high-fat milk, Cultured full-fat milk, Cultured low-fat milk, Cultured fat-free milk." Extract from the Value-Added Tax Act, 1991.

[51] "Being pure, sound wheaten meal, excluding separated wheaten bran, wheaten germ and wheaten semolina." Extract from the Value-Added Tax Act, 1991.

[52] "Being raw eggs laid by hens of species gallus domestics, whether supplied in their shells or in the form of egg pulp being raw pulp consisting of the yolk and white which is obtained from such eggs after the shells have been removed." Extract from the Value-Added Tax Act, 1991.

[53] "Dried, whole, split, crushed, skinned or in powder form, but not further prepared or processed or where packaged as seed or such pulse as are described under separate Item in this Part." Extract from the Value-Added Tax Act, 1991.

[54] Republic of South Africa. (1991) Value-Added Tax Act, 1991 (No. 89 of 1991). Government Gazette No. 13307 12 June 1991 (Published under Government Notice R1342).

[55] Katz, M. (1994) *'Interim report of the Commission of Inquiry into Certain Aspects of the Tax Structure of South Africa'.* Pretoria: The Commission, pp 133.

[56] Katz, M. (1994) pp 133.

[57] Katz, M. (1994) pp 133.

[58] Katz, M. (1994) pp 133.

1.2.6 The zero-rating of certain paraffin:

During the 2001 budget speech the Minister of Finance, Trevor Manuel, announced that illuminating paraffin will be included in the zero-rating provisions.[59] Therefore, section 11(1)(l)[60] was included in the VAT Act.

The purpose for including paraffin as a zero-rated item was to provide relief to poorer households. However National Treasury analysed the impact that this policy decision had on the poor and found that despite the zero-rating provision the price of paraffin was not reduced, and little benefit was derived by the poor.

The Chief Director of Economic Tax Analysis at National Treasury, Mr Cecil Morden, at the standing committee of finance meeting held on 22 March 2011 commented that:

> "The zero-rating of illuminating paraffin was a prime example of a zero rating that was well intended, but actually misguided. Most of the benefits of the VAT zero-rating of illuminating paraffin were captured by retailers, in the form of higher profit margins. The provision of relief in the form of reduced rates, and zero-rating for "merit" goods, might even worsen the 'regressivity' of a VAT system because these goods were mostly bought by individuals in the middle- and higher-income groups."[61]

1.2.7 The VAT rate increase in April 2018 and the impact thereof:

On the 21 February 2018, former Minister of Finance, Malusi Gigaba announced that the VAT rate will be increased from 14% to 15% as of 1 April 2018.[62] Given the current state of the economy and the government purse, the increase was viewed as an inescapable reality of the country's current state of affairs. Civil society, labour unions and other stakeholders raised concerns that the poor would be the most negatively affected by an increase in the VAT rate and this became a national debate.[63]

Following the announcement, there was an outcry for relief for the poor and the decision taken by the Minister of Finance was to establish a panel of experts[64] (referred to as the Panel) to consider the current fiscal policy in respect of the list of zero-rating of basic foodstuffs and to make any recommendations of items to be added or removed from the current list.[65] Initially the Panel's Terms of Reference, referred to the review of the current list

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[59] Republic of South Africa. (2001) *'National Treasury Budget Speech 2001',* pp 15-16. Available at: http://www.treasury.gov.za/documents/national%20budget/2001/speech/speech.pdf (Accessed: 5 April 2018).

[60] "Section 11(1)(l) states that goods consist of illuminating kerosene (marked) intended for use as fuel for illuminating or heating, referred to in Fuel Item Levy number 195.10.13 in Part 5A of Schedule No.1 to the Customs and Excise Act and are not mixed or blended with another substance." Extract from the Value-Added Tax Act, 1991.

[61] Parliament Monitoring Group. *'VAT rating on books: National Treasury briefing; Statistics SA Strategic Plan & budget 2011: Minister in Presidency and Stats SA briefing.' (22* March 2011). Available at: https://pmg.org.za/committee-meeting/12785 (Accessed: 1 September 2019).

[62] Republic of South Africa. (2018) *'National Treasury Budget Speech 2018'*, pp 11. Available at: http://www.treasury.gov.za/documents/national%20budget/2018/speech/speech.pdf (Accessed: 5 April 2018).

[63] Mail & Guardian. (2018) *'ANC caucus didn't want VAT hike.'* Available at: https://mg.co.za/article/2018-02-22-anc-caucus-didnt-want-vat-hike (Accessed: 5 April 2018).

[64] Referred to as the Panel.

[65] Republic of South Africa. (2018) *'Media Statement: Establishment of an independent panel of experts to consider and review the current list of VAT zero-rated food items'.* Available at: http://www.treasury.gov.za/comm_media/press/2018/20180405%20Media%20statement%20-%20experts%20on%20VAT%20zero-rated%20items.pdf (Accessed: 3 April 2018).

of zero-rating of foodstuffs, but this was later expanded to also consider any non-food items which may be appropriate for inclusion. The Panel under the chair of Professor Ingrid Woolard provided their recommendations on the 6 August 2018.[66]

The Panel recommended that six items be included in the list of zero-rated items, namely: 'white bread', 'bread flour', 'cake flour'; 'sanitary products', 'school uniforms' and 'nappies'.[67]

After considering these recommendations, the government announced in the Medium-Term Budget Policy Statement that it proposes to zero-rate 'white bread flour', 'cake flour' and 'sanitary pads' from 1 April 2019.[68] On the 17 January 2019 the Rates and Monetary Amounts and Amendment of Revenue Law Act No 21 of 2018 states that effective from 1 April 2019 the following items will be added to Schedule 2 Part B.[69]

Item Number	Item Description
Item 20	'Cake wheat flour'[70]
Item 21	'White bread wheat flour'[71]
Item 22	'Sanitary towels (pads)'.

Figure 6. Schedule 2 Part B additional list in 1993 (wording as in the 2019 VAT Act). Source: Value-Added Tax Act No 89 of 1991

1.3 Problem statement and motivation for research:

The most concerning issue with an increase in the VAT rate is whether it will cause additional hardship for the poor due to the broad-based nature of a VAT system. This study aims to assess whether an appropriate response to the 2018 VAT rate increase, is to include the use of further zero-rating of basic goods as an instrument to combat the impact on poorer households.

Further this study will consider the recommendations put forth by the Panel and determine whether these recommendations are appropriate as well as noting the challenges and complexities associated with the concept of zero-rating.

[66] Republic of South Africa. (2018) *'Media Statement: Amendment to the terms of reference for the independent panel of experts for the review of the current list of VAT zero-rated food items'.* Available at: http://www.treasury.gov.za/comm_media/press/2018/2018052901%20Amendment%20to%20the%20terms%20of%20reference%20for%20the%20Independent%20panel%20of%20experts%20for%20the%20review%20of%20current%20list%20of%20VAT%20zero%20rated%20food%20items.pdf (Accessed: 20 January 2019).
[67] Republic of South Africa. (2018) *'Recommendations to Minister of Finance by the Independent Panel of Experts for the Review of Zero-Rating in South Africa'*, pp 63. Available at: http://www.treasury.gov.za/comm_media/press/2018/2018081001%20VAT%20Panel%20Final%20Report.pdf (Accessed: 21 September 2019).
[68] Republic of South Africa. (2018) *'Medium Term Budget Policy Statement 2018'*, pp 14. Available at: http://www.treasury.gov.za/documents/mtbps/2018/speech/speech.pdf (Accessed: 5 April 2018).
[69] Republic of South Africa. (2018) *'Rates and Monetary Amounts and Amendment of Revenue Law Act No 21 of 2018'.* Available at: http://www.treasury.gov.za/legislation/acts/2018/Rates%20and%20Monetary%20Amounts%20and%20Amendment%20of%20Revenue%20Laws%20Act%2021%20of%202018.pdf (Accessed: 20 January 2019).
[70] As defined in Regulation 1 of the Regulations in terms of Government Notice No. R.405 published in Government Gazette No. 40828 of 5 May 2017.
[71] As defined in Regulation 1 of the Regulation in terms of Government Notice No. R.405 published in Government Gazette No 40828 of 5 May 2017.

1.4 Research question:

The main question is whether the current zero-rating of further certain basic goods in light of both the globally accepted policies and principles, international trends and the current South African fiscal position is the most appropriate response to the 2018 VAT rate increase. A secondary question is how these basic goods suitable for zero-rating should be selected.

1.5 Research method:

This study will incorporate various research methodologies in order to reach an appropriate conclusion. Firstly, a literature view will be undertaken to determine the purpose and design of a VAT system, as well as to understand the view on whether VAT is progressive or regressive, especially in a South African context. The literature review will also include other views on the current zero-rating list and whether there are other viable alternatives for consideration as a response to a VAT rate increase.

Further this study will conduct an international comparison in an African context of which items are zero-rated, exempted or excluded from the VAT systems in other African countries to determine which goods are globally considered as a basic good for special VAT treatment.

Lastly an analysis will be performed on the spending patterns of the poor to determine which items should be incorporated in a list of zero-rated basic food items. The data used for this analysis was made available by the Income and Expenditure Survey and Living Conditions Survey of 2014/2015 published by Statistics South Africa.

1.6 Overview of chapters:

This first Chapter is an introduction to this study as well as providing the background to a VAT system and the evolution of zero-rating provisions for basic goods especially for the poor over the last two decades.

Chapter 2 will provide a brief evaluation of the South Africa's current fiscal policy and position and also provide the principles of a VAT system. It will also include the elements established to assess the appropriateness of a tax policy in light of the views of the International Monetary Fund (IMF) and other academics.

Chapter 3 will include a literature review, and briefly consider the debate on whether VAT is progressive or regressive, especially in a South African context. In addition, an in-depth analysis of the challenges and complexities of a zero-rating list will be discussed.

In Chapter 4 an international comparison will be conducted to determine whether there is other global precedent for South Africa's VAT system and especially whether the South Africa's zero-rating basic goods list is appropriate and effective.

An analysis of the economic considerations will be included in Chapter 5, where an evaluation of South Africa's spending patterns per the types of households will be observed. Lastly the final Chapter will be the conclusion.

Chapter 2: Concepts for adopting a tax policy and the structural elements in a VAT system

The purpose of this chapter is to investigate what elements need to be present for a sound tax policy. An understanding of a VAT system as well as the basic principles of VAT and understanding the international standards and trends of tax policies will enable an assessment on the appropriateness and possible effectiveness of zero-rating as the VAT treatment of basic goods.

2.1 Introduction:

There are various elements and instruments utilised by a government when it chooses to implement a fiscal policy. These elements include both direct taxes and indirect taxes. The South African Government has elected a mix of direct and indirect taxes in developing the South African Fiscal Policy. Direct taxes by definition are "paid by a person or organisation directly to the government",[72] and are usually "taxes on profits and income."[73] In South Africa direct taxes include: personal income tax; corporate income tax; dividends and interest withholding tax; tax on retirement funds; skills development levy; donations tax; securities transfer tax; and transfer duties.[74] On the other hand, indirect taxes are a tax levied on goods and services rather than on individuals and companies and the tax is added to the price of the goods and services.[75] Indirect taxes in South Africa include; value-added tax, customs duties, air departure tax, fuel levy, specific excise duties, and ad valorem excise duties.[76]

The Organization for Economic Co-operation and Development (OECD) considered the role of consumption taxes as an element of fiscal policy and stated that; ". . . the effects of consumption taxes on income distribution are only one element in reaching a decision on the desirability of increasing or decreasing reliance upon these taxes. Their effects upon economic efficiency, their administrative practicability and their role as revenue raisers, have also to be considered. Views taken on these other effects may outweigh distributional considerations."[77]

A zero-rating is a form of tax concession and there are various factors that governments consider before granting a tax concession. These include; the elected social policy, the concept of fairness, economic neutrality, the political objectives of the government, and easing the burden of administration.[78]

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[72] Collins Online Dictionary. (2019) *'Direct Taxes'.* Available at: https://www.collinsdictionary.com/dictionary/english/direct-tax (Accessed: 17 November 2019).
[73] See footnote 72.
[74] Republic of South Africa. (2018) *'National Treasury Budget Review 2018',* pp 39-40. Available at: http://www.treasury.gov.za/documents/national%20budget/2018/review/FullBR.pdf (Accessed: 5 April 2018).
[75] Collins Online Dictionary. (2019) '*Indirect Tax'.* Available at: https://www.collinsdictionary.com/dictionary/english/indirect-tax (Accessed: 20 January 2019).
[76] Republic of South Africa. (2018) pp 39-40.
[77] OECD. (1981) *'The Impact of Consumption Taxes at Different Income Levels',* OECD Studies in Taxation, OECD, Paris, pp 5.
[78] Republic of South Africa. (2007) *'The VAT Treatment of Merit Goods and Services',* pp 27. Available at: http://www.treasury.gov.za/publications/other/VAT%20Merit%20goods%20Final%20Report%20%20-%2015%20Oct%202007.pdf (Accessed: 25 April 2018).

In a South African context, at the beginning of the democratic South Africa, the government's purpose was to prompt redistribution and established a Growth, Employment, and Redistribution (GEAR) strategy. The GEAR policy document stated, "International experience confirms that it is on the expenditure side that the fiscus is most effectively able to contribute to redistribution. It is nonetheless important that the incidence of taxation should remain progressive, while at the same time impacting across a broad base to avoid excessive rates."[79]

2.2 The principles for developing a sound tax policy:

In examining the appropriateness of a tax policy, a consideration of the principles established in economic and tax theory is necessary. The first consideration is to determine the role of VAT in a tax system and to understand its design.

An ideal VAT model:

VAT in its design is intended to have a broad-based tax base, where the final consumption bears the actual tax cost.[80] This idealised broad-based VAT system is: "designed to bring within its charge every kind of economic transaction, subject to limited exemptions. This is normally achieved by drafting a very broad provision imposing VAT on an extremely wide range of business transactions and then removing by specific exception any transaction that is not liable."[81] Thus, a perfect VAT system exists where there are no exceptions or exemptions and allows for the VAT rate to be kept to the lowest acceptable rate.[82]

Bird commented, as reported in Keen (2009),[83] that an idealised design for a VAT system is one where: "the tax should avoid zero-rating other than for exports, and have minimal exemptions, a single positive rate, a fairly high threshold … rely on self-assessment (meaning taxpayers declare and pay tax due, subject to audit and penalty) and structure the tax administration along functional or taxpayer-segment lines to accommodate the requirements of the VAT."[84]

However, others have criticised the VAT system and found that although VAT in its perfect design is attractive, the political and social pressures that exist make it impractical to implement a pure system in practice as countries are forced to implement exemptions and multiple rates.[85]

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[79] Republic of South Africa. (1996) *'Macroeconomic strategy on growth, employment and redistribution.'* Pretoria: Government Printer.
[80] South African Revenue Service (SARS). (2019) *'The Value-Added Tax VAT404 Guide for Vendors',* pp 1. Available at: https://www.sars.gov.za/AllDocs/OpsDocs/Guides/LAPD-VAT-G02%20-%20VAT%20404%20Guide%20for%20Vendors.pdf (Accessed: 18 February 2019).
[81] Williams, D. (1996) *'Tax Law Design and Drafting'*, Chapter 6, pp 20. Available at: https://www.imf.org/external/pubs/nft/1998/tlaw/eng/ch6.pdf (Accessed: 15 February 2019).
[82] Charlet, A and Owens, J (2010) *'An International Perspective on VAT',* Tax Notes International, 59(12), pp 949; and Hagemann, R., B. Jones and R. Montador (1987), "Tax Reform in OECD Countries: Economic Rationale and Consequences", OECD Economics Department Working Papers, No. 40, OECD Publishing, Paris, pp 34-39. Available at: https://doi.org/10.1787/082177701741. (Accessed: 25 January 2019).
[83] Keen, M. (2009) *'What Do (and Don't) We Know about the Value Added Tax? A Review of Richard M. Bird and Pierre-Pascal Gendron's The VAT in Developing and Transitional Countries'*. Journal of Economic Literature 47(1), pp 160 - 161. Available at: https://doi.org/10.1257/jel.47.1.159 (Accessed: 25 January 2019).
[84] Bird, R. M. and Gendron, P. (2007) *'The VAT in Developing and Transitional Countries'.* Cambridge and New York: Cambridge University Press.
[85] Aaron, HJ. (1981) *'The Value-Added Tax: Lessons from Europe.'* Washington, DC. Brooklyn Institution, pp 16.

Principles for adopting a tax policy

As a pure VAT system is impractical, policymakers would adopt a tax policy that makes sense to its social and political endeavours. Therefore, it is important to assess whether the tax policy established or to be established, is appropriate within a conceptual framework of generally accepted principles. The concepts required in assessing whether a tax policy meets its desired effect are the concepts of 'equity' and 'efficiency'.[86]

The Concept of Equity:

Equity refers to the fairness of the tax imposed. Economic theory suggests that there are two forms of equity, namely; vertical equity and horizontal equity.

Vertical equity refers to the principle that taxes on individuals or households increase in line with the amount of income earned. The theory is that those who have the *ability to pay* should contribute more than those who do not.[87] Vertical equity introduces the notion of a tax system that encourages redistribution of wealth.[88]

On the other hand, ***horizontal equity*** refers to the economic theory that individuals with similar incomes and assets should be paying the same amount in taxes.[89] This speaks to a principle of neutrality, which is a principle established in the Ottawa Taxation Framework Conditions. The Ottawa Taxation Framework Conditions were adopted by the OECD, particularly in designing tax policies in respect of international transactions, such as e-commerce.[90]

Therefore, the concept of equity has two contrasting principles; that being the 'ability to pay' and 'fairness i.e. benefits received'. The 'ability to pay' concept is based on the level of wealth or income, suggesting that the more wealth or income individuals obtain the higher the probability that individuals can afford to pay the tax. In contrast the concept of 'benefit received' suggests that the individuals who benefit from government services should share in the tax burden.[91]

It is generally regarded that in countries where there is a significant gap in income between the rich and the poor, the principle of equity is best achieved through the proportionality of the tax. If a country does not have such significant economic equalities, then the concept of equity can be achieved through fairness.[92]

The perception is that indirect taxes, such as VAT, are horizontally equitable because the entire population, whether rich or poor, would pay taxes relative to their consumption of goods and services. However indirect taxes fail to be vertically equitable as the poor tend to spend more of their income on the consumption of goods

[86] Republic of South Africa. (2007) *'The VAT Treatment of Merit Goods and Services,'* pp 31. Available at: http://www.treasury.gov.za/publications/other/VAT%20Merit%20goods%20Final%20Report%20%20-%2015%20Oct%202007.pdf (Accessed: 25 April 2018).
[87] Investopedia. '*Vertical Equity'*. Available at: https://www.investopedia.com/terms/v/vertical_equity.asp (Accessed: 20 January 2019).
[88] Republic of South Africa. (2007) pp 33.
[89] Investopedia. '*Horizontal Equity'*. Available at: https://www.investopedia.com/terms/h/horizontalequity.asp (Accessed: 20 January 2019).
[90] OECD. (2017) *'International VAT/GST Guidelines'* OECD Publishing, Paris, pp 18. Available at: https://www.oecd-ilibrary.org/taxation/international-vat-gst-guidelines_9789264271401-en (Accessed: 23 March 2018).
[91] Republic of South Africa (2007) pp 32.
[92] Republic of South Africa (2007) pp 32.

and services than wealthier households and therefore in proportion more of their income is paid in tax. [93] Another similar concept is whether VAT is considered to be regressive, which will be considered further in Chapter 3.

Bird refers to the key principle of fairness and within such context, the concept of using zero-rating as a tool is a worthwhile exercise despite the loss of VAT revenue.[94]

The Concept of Efficiency:

Another feature that must be present for a good tax system is that the 'tax' must be efficient. Efficiency implies that the result of the tax should not be to cause distortions in the economy.[95] In assessing the concept of tax, policymakers need to consider that tax impacts households and individuals' disposable income and for businesses their profits. This may have a negative impact on the country's economic growth and other considerations such as an increase in the unemployment rate.[96]

The concept of efficiency is further divided into the following categories; simplicity, low administration costs, matching tax impact and incidence, diversity of the tax base, flexibility, moderate rates of progression, minimising excess burden, and maximising revenue.[97]

Simplicity:

A tax system should not be riddled with complexities that are difficult to understand and costs involved with the compliance and administration should be kept to a minimal level.[98] In a VAT context, this drives the reason for keeping zero-rating and exempt items to a minimum, so that vendors do not incur significant costs on ensuring compliance with a more complex system design.

Low administration costs:

This principle entails keeping the costs of collecting revenue as low as possible.[99]

Matching of tax impact and incidence:

When establishing a tax policy, its impact should not cause a substantial difference in terms of tax incidence. In economic theory, the term '***tax incidence***' refers to the "division of a tax burden between buyers and sellers."[100] This is viewed to be predicted and measured by virtue of price elasticities of supply and demand of a

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93 International Development Research Centre (IDRC) – Edited by Grown, C. and Valodia, I. (2010) *'Tax and Gender Equality: A Comparative Analysis of Direct and Indirect Taxes in Developing and Developed Countries'*, pp14. Available at: https://idl-bnc-idrc.dspacedirect.org/bitstream/handle/10625/43684/IDL-43684.pdf (Accessed: 18 January 2019).
94 Bird, R.M and Gendron P. (2006) '*Is VAT the best way to impose a general consumption tax in developing countries'.* IDEAS Working Paper Series from RePEc. Available at: http://search.proquest.com/docview/1697573215 (Accessed: 25 January 2019).
95 Republic of South Africa. (2007) *'The VAT Treatment of Merit Goods and Services'* pp 59 -60. Available at: http://www.treasury.gov.za/publications/other/VAT%20Merit%20goods%20Final%20Report%20%20-%2015%20Oct%202007.pdf (Accessed: 25 April 2018).
96 Republic of South Africa. (2007) pp 33.
97 Republic of South Africa. (2007) pp 33 - 34.
98 Republic of South Africa. (2007) pp 33.
99 Republic of South Africa. (2007) pp 33.
100 Investopedia. '*Tax Incidence'*. Available at: https://www.investopedia.com/terms/t/tax_incidence.asp (Accessed: 20 January 2019).

commodity. '***Price elasticity***' refers to the economic term, which relates to the measure of the change in the quantity of the commodity with a change in its price.[101] The economic principle of tax incidence states further that, when a supply (producers) of the commodity is more elastic (price elastic) than the demand (consumers) for the commodity, the tax burden will fall on the consumers. Whereas if the demand for a specific item is more elastic than the supply of a specific item, the producers will be the party to bear the cost of the tax.[102] Thus, tax shifting will occur for commodities where the price elasticity of demand is low, but the price elasticity of supply is high.[103] This means that the consumer will bear the cost of the tax. Therefore, policy makers should consider the relevant price elasticity of supply and demand as this will determine the impact of the tax burden and who will bear it.

The substitution effect:

Another economic behaviour a tax policy should avoid is the negative influence of the substitution effect of commodities, unless this is the desired effect. In VAT terms this involves consumer behaviour of substituting one food item that is standard rated for another food item that is zero-rated.[104] For example, should the government hypothetically decide to introduce butter as a zero-rated item, but margarine is still a standard-rated item due to butter being a healthier alternative, the substitution effect suggests that consumers may change their purchasing habits and purchase butter instead of margarine. In order to determine whether such substitutional effect would be substantial, an economic analysis of the elasticities should be assessed.

Diversity of the Tax Base:

A diverse tax base refers to the government receiving its revenue from numerous sources. The reason this is a preferable tax policy is that a dependency on one revenue stream opens the government to a risk that such revenue may experience an unexpected decline, i.e. corporates profitability declines and the tax revenue on the profits is less than budgeted. The more revenue sources the more robust the fiscal policy to unexpected circumstances where revenue has declined. Another benefit of a broad tax base is that the marginal tax rates are usually lower.[105]

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[101] Investopedia. '*Price Elasticity'*. Available at: https://www.investopedia.com/terms/p/priceelasticity.asp (Accessed: 20 January 2019).
[102] Investopedia. '*Tax Incidence'*. Available at: https://www.investopedia.com/terms/t/tax_incidence.asp (Accessed: 20 January 2019).
[103] Republic of South Africa. (2007) *'The VAT Treatment of Merit Goods and Services',* pp 33. Available at: http://www.treasury.gov.za/publications/other/VAT%20Merit%20goods%20Final%20Report%20%20-%2015%20Oct%202007.pdf (Accessed: 25 April 2018).
[104] Republic of South Africa. (2007) pp 33.
[105] Republic of South Africa. (2007) pp 34.

Flexibility:

This concept refers to policy makers making decisions on fiscal policy, such as tax rates and sources of revenue, based on current economic conditions enabling regular policy adjustments for the changing circumstances.[106]

Maximising revenue:

A government collects revenue for the provision of services and to cover the expenditure it incurs.[107] Therefore, an adopted tax policy attempts to maximise its tax revenue taking into account the other abovementioned principles and the economic conditions of the nation, in order for the government to meet all its expenditure commitments.

2.3 The structural elements of VAT

The VAT system is an efficient tax system as it collects tax at each stage in a series of transactions.[108] VAT is designed in such a manner as to have the final consumer bearing the VAT cost as producers and manufacturers as VAT vendors are entitled to claim the VAT costs on their expenditure during the production/ distribution chain.[109]

In order to consider a tax policy in respect of VAT and granting a food item or non-food item a tax concession such as a zero-rating or exemption, it is essential to acknowledge the implications thereof.

A VAT system is made up of output tax and input tax and the net is paid to or refunded by the South African Revenue Service (SARS). ***Output tax*** is defined in section 1 of the Value-Added Tax Act No 89 of 1991 (VAT Act) as *"*in relation to any vendor, means the tax charged under section 7(1)(a) in respect of the supply of goods and services by that vendor*.*"[110] Therefore section 7(1)(a) Act states that: "Subject to the exemptions, exceptions, deductions, and adjustments provided for in this Act, there shall be levied and paid … to be known as the value-added tax - on the supply by any vendor of goods and services supplied by him on or after the commencement date in the course or furtherance of any enterprise carried on by him."[111]

Additionally ***input tax*** is defined as *"*in relation to a vendor, means - tax charged under section 7 and payable in terms of that section by - a supplier on the supply of goods or services made by that supplier to the vendor…Where the goods or services concerned are acquired by the vendor wholly for the purpose of

[106] Republic of South Africa. (2007) *'The VAT Treatment of Merit Goods and Services'* pp 34. Available at: http://www.treasury.gov.za/publications/other/VAT%20Merit%20goods%20Final%20Report%20%20-%2015%20Oct%202007.pdf (Accessed: 25 April 2018).
[107] Republic of South Africa. (2007) pp 34.
[108] Katz, M. (1994). *'Interim report of the Commission of Inquiry into Certain Aspects of the Tax Structure of South Africa'.* Pretoria: The Commission, pp 120.
[109] South African Revenue Service (SARS). (2019) *'The Value-Added Tax VAT404 Guide for Vendors',* pp 2-3. Available at: https://www.sars.gov.za/AllDocs/OpsDocs/Guides/LAPD-VAT-G02%20-%20VAT%20404%20Guide%20for%20Vendors.pdf (Accessed: 18 February 2019).
[110] Republic of South Africa. (1991) Value-Added Tax Act, 1991 (No. 89 of 1991). Government Gazette No. 13307 12 June 1991 (Published under Government Notice R1342).
[111] Republic of South Africa. (1991) Value-Added Tax Act, 1991 (No. 89 of 1991).

consumption, use or supply in the course of making taxable supplies or, where the goods or services are acquired by the vendor partly for such purpose, to the extent (as determined in accordance with the provisions of section 17) that the goods or services concerned are acquired by the vendor for such purpose."[112]

A ***taxable supply*** "means any supply of goods or services which is chargeable with tax under the provisions of section 7(1)(a), including tax chargeable at the rate of zero per cent under section 11."[113]

Theoretically, where a government considers certain items as essential and should be granted a concession from VAT, it could elect to incorporate such item in the zero-rating provisions in section 11 or as an exemption in section 12. There are different implications depending on such election as a zero-rated supply is considered to be a taxable supply, but an exempt supply is not considered to be a taxable supply. A zero-rated supply is a taxable supply which is subject to VAT at 0%, and vendors making these supplies will be entitled to claim any input tax associated with its expenditure incurred.[114] The government will therefore forfeit the right to receive the revenue associated with the sale of these supplies, and the VAT that the producers or retailers of such goods have incurred on their expenditure is returned to them by way of refund.

In contrast, an exempt supply, not being a taxable supply, implies that a vendor making such supply will be prohibited from claiming any input tax to the extent it relates to the making of exempt or non-supplies.[115] In these circumstances, the fiscus will forfeit the revenue associated with exempt supplies, however, the producers and retailers of such supplies will bear the VAT incurred on their expenditure as an additional cost.

Structural elements of zero-rating and exemptions:

In the South African VAT system, most goods and services are subject to VAT at the standard rate of 15%, but there are a limited number of zero-rated and exempt goods and services.

Zero-Rating:

Firstly, international trade transactions i.e. exports in most jurisdictions are zero-rated, based on the destination principle promoted by the OECD, which achieves VAT neutrality and that the tax revenue should accrue in the country where there is final consumption.[116] Other goods such as diesel and petrol are zero-rated as they are subject to excise duties.[117] Further, a number of basic food items are zero-rated based on their merits for providing poverty relief.[118]

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[112] Republic of South Africa. (1991) Value-Added Tax Act, 1991 (No. 89 of 1991). Government Gazette No. 13307 12 June 1991 (Published under Government Notice R1342).
[113] Republic of South Africa (1991) Value-Added Tax Act, 1991 (No. 89 of 1991).
[114] South African Revenue Service (SARS). (2019) *'The Value-Added Tax VAT404 Guide for Vendors',* pp 41 and 55. Available at: https://www.sars.gov.za/AllDocs/OpsDocs/Guides/LAPD-VAT-G02%20-%20VAT%20404%20Guide%20for%20Vendors.pdf (Accessed: 18 February 2019).
[115] South African Revenue Service (SARS). (2019) pp 49.
[116] OECD. (2017) *'International VAT/GST Guidelines'* OECD Publishing, Paris, pp 20. Available at: https://www.oecd-ilibrary.org/taxation/international-vat-gst-guidelines_9789264271401-en (Accessed: 23 March 2018).
[117] South African Revenue Service (SARS). (2019) pp 42.
[118] Davis Tax Committee (DTC). (2018*) 'The Final Report on VAT for the Minister of Finance'* pp 5. Available at: https://www.sataxguide.co.za/wp-content/uploads/2018/05/20180329-Final-DTC-VAT-Report-to-the-Minister.pdf (Accessed: 10 February 2019).

Exemptions:

The most notable exempt services are education, financial services and passenger transport by road and rail. Education is exempt in most jurisdictions on the merit grounds that the institutions included in the exemption are mostly state funded and provide services to the public.[119] Financial services are exempt as these services are hard to tax.[120] Passenger transport by road and rail is exempt on the merit ground that the poor use busses, trains and taxis to commute to their workplace and VAT would increase these fares. A further reason is that it would be difficult to persuade mini taxi operators to register for VAT.[121]

Conclusion

This chapter summarises the essential elements to be considered by policy makers and other stakeholders when adopting tax policy. The theory suggests it is a generally accepted policy for a VAT system to be broad-based with few exceptions (i.e. zero-ratings and exemptions) with a single low rate. Given the design of the VAT system, when a tax concession is being considered, zero-rating is preferable to an exemption due to the cascading impact of denied input tax.[122]

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[119] Marais, G. (1991) *'Report of the Value-Added Tax Committee'* (VATCOM). Pretoria: Govt. Printer, pp 28-30.
[120] Inchauste, G. et al (2015) *'The Distributional Impact of Fiscal Policy in South Africa'*, pp 5. Available at: http://worldbank.org/drm/documents (Accessed: 16 May 2018).
[121] Inchauste, G. et al (2015) pp 5.
[122] Davis Tax Committee (DTC). (2018*) 'The Final Report on VAT for the Minister of Finance'* pp 6. Available at: https://www.sataxguide.co.za/wp-content/uploads/2018/05/20180329-Final-DTC-VAT-Report-to-the-Minister.pdf (Accessed: 10 February 2019).

Chapter 3: An analysis on addressing the regressivity of VAT

The purpose of this chapter is to consider conceptually the regressivity of VAT and the instruments used to address the regressive nature of VAT within the context of tax and economic theory literature. The zero-rating of basic goods is a potential instrument that policy-makers may elect to utilize, especially in developing countries. This chapter also considers a methodology for defining or classifying goods as basic goods. Further, the South African government has adopted the policy of limiting the number of zero-rating of goods in Schedule 2 Part A and to rather use social spending as a means to address the perceived regressivity of VAT.[123] A review of previous studies is performed to evaluate the effectiveness of this policy.

3.1 Is VAT regressive?

VAT is perceived as regressive and anti-poor[124] and this view has only intensified with the 2018 VAT rate increase as trade unions in particular believe that the poor are the most impacted by the increase of 1% in the VAT rate. The purpose of this section is to understand the underlying principles of regressivity and progressivity and to evaluate whether these sentiments are consistent with evidence from previous studies performed in this field. Firstly, we will consider what is meant by the term 'regressive'.

3.1.1. The concept of regressivity and progressivity:

The generally accepted definition for a regressive tax is where the lower income groups spend a larger proportion of their income on that tax, than higher income groups.[125] On the other hand, a tax is considered to be progressive if higher income earners pay a higher share of income in tax than lower income earners.[126] When considering the concept of regressivity it can be observed on three levels, the first is to consider whether a specific tax is regressive or progressive (i.e. VAT), the tax system is regressive or progressive (i.e. combined tax system of VAT, income taxes etc.), the tax system and government social expenditure (i.e. combined tax system and social spending such as income grants).[127]

When considering whether VAT is regressive, especially with regards to its vertical equity, it is incorrect to simply make such assessment in isolation as there is a larger tax system which incorporates progressive income taxes and other taxes. A tax system as a whole should be the basis for making this determination. Fourie and Owen (1993) refer to the concept of net tax regressivity or progressivity, which involves the entire

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[123] Republic of South Africa. (1996) 'Macroeconomic strategy on growth, employment and redistribution.' Pretoria: Government Printer and Republic of South Africa. (2007) *'The VAT Treatment of Merit Goods and Services'* pp 6. Available at: http://www.treasury.gov.za/publications/other/VAT%20Merit%20goods%20Final%20Report%20%20-%2015%20Oct%202007.pdf

[124]Jansen, A. Stoltz, E. and Yu, D. (2013) '*The Targeting of Zero-Rated Basic Foodstuffs under Value-Added Tax (VAT) in South Africa',* Journal of Econometrics, 37(3), pp. 87.

[125] Kearny, M. (2003) *'Restructuring Value-Added Tax in South Africa: A Computable General Equilibrium Analysis',* pp 45. Available at: https://repository.up.ac.za/bitstream/handle/2263/27705/Complete.pdf?sequence=9&isAllowed=y (Accessed: 20 January 2019).

[126] Republic of South Africa. (2018) *'Recommendations to Minister of Finance by the Independent Panel of Experts for the Review of Zero-Rating in South Africa',* pp 13. Available at: http://www.treasury.gov.za/comm_media/press/2018/2018081001%20VAT%20Panel%20Final%20Report.pdf (Accessed: 21 September 2019).

[127] Inchauste, G. et al (2015) *'The Distributional Impact of Fiscal Policy in South Africa',* pp. 15 - 21. Available at: http://worldbank.org/drm/documents (Accessed: 16 May 2018).

tax and expenditure system and assessing whether it achieves "the pattern of household income net of taxes and gross of transfers and government expenditures that society desires."[128] OECD researchers consider that the introduction of VAT arguably produced tax revenues which would otherwise not have occurred therefore the distribution of government expenditure should be taken into account.[129] Tait argued that the question is not one of whether VAT is regressive but whether "the overall mix of government taxes and expenditures has the desired effect on low- versus high-income households."[130]

Further Tait advocates that the strengths of the VAT system should be used to generate revenue (i.e. as a broad-based tax) that will enable a government to assist the poor in more effective ways, rather than "amending and distorting the VAT system" (i.e. with zero-rating and exemption). The use of higher tax revenues from VAT is "a more positive way to tackle the issue of regressivity than manipulating the new tax until its merits are eroded."[131]

VAT as a specific tax, is regarded to be regressive in nature, as it is a single rate of tax applied to a broad base of goods and services and increases with the level of consumption of goods and services.[132]

3.1.2 Other aspects in measuring the regressivity of VAT

As discussed earlier in this research there are two common perceptions in South Africa, firstly that VAT is perceived to be regressive and secondly that the 2018 VAT rate increase impacted the poor more than the rich. In this section and further in this chapter these perceptions will be addressed.

From a South African perspective, VAT is generally considered by South African academics as regressive as the poor spend a larger proportion of their income on the consumption of goods, compared to more affluent households.[133] However there are alternative views on the interpretation of the consumer spending patterns and its impact on households. These views include differing opinions on the use of relative versus absolute basis for analysing consumer spending patterns and the analysis of the regressivity of VAT based on a single year versus a lifetime income approach.[134]

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[128] Aaron, HJ. (1981) *'The Value-Added Tax: Lessons from Europe.'* Washington, DC. Brooklyn Institution, pp 18.
[129] OECD. (1981) *'The Impact of Consumption Taxes at Different Income Levels',* OECD Studies in Taxation, OECD, Paris, pp 5.
[130] Tait, A.A. (1991) *'Value-Added Tax; Administrative and Policy Issues',* Occasional paper No 88, International Monetary Fund, Washington, D.C. pp 6.
[131] Tait, A.A. (1991) pp 7.
[132] Ebrill, L., Keen, M., Bodin, J. and Summers, V. (2001) *'The Modern VAT'.* International Monetary Fund, D.C., pp. 107.
[133] Kearny, M. (2003) *'Restructuring Value-Added Tax in South Africa: A Computable General Equilibrium Analysis'*, pp 45. Available at: https://repository.up.ac.za/bitstream/handle/2263/27705/Complete.pdf?sequence=9&isAllowed=y (Accessed: 20 January 2019).
[134] Republic of South Africa. (2018) *'Recommendations to Minister of Finance by the Independent Panel of Experts for the Review of Zero-Rating in South Africa',* pp 13. Available at: http://www.treasury.gov.za/comm_media/press/2018/2018081001%20VAT%20Panel%20Final%20Report.pdf (Accessed: 21 September 2019).

Did the VAT rate increase impact the poor more than the rich?

The Panel[135] also considered the consumer spending patterns in light of the VAT rate increase and whether the statement that the poor will be more impacted is accurate. In assessing the impact of the VAT increase it was held that; "The increase in the VAT across the entire population is not regressive; it is more or less proportional." [136] However as higher income households spend a lower percentage of their income on VAT, the Panel noted that the 2018 VAT rate increase largely impacted the lower four decile households compared to higher income households. The South African population is divided into 10 deciles, with the richest decile (Decile 10) representing households belonging to the upper 10 per cent in terms of per capita income, while the poorest decile represents households in the lower 10 per cent in terms of per capita income.[137] Figure 7 is a graph from the Panel's recommendation report evidencing that the VAT rate increase would have a larger impact on poorer households in relative terms.

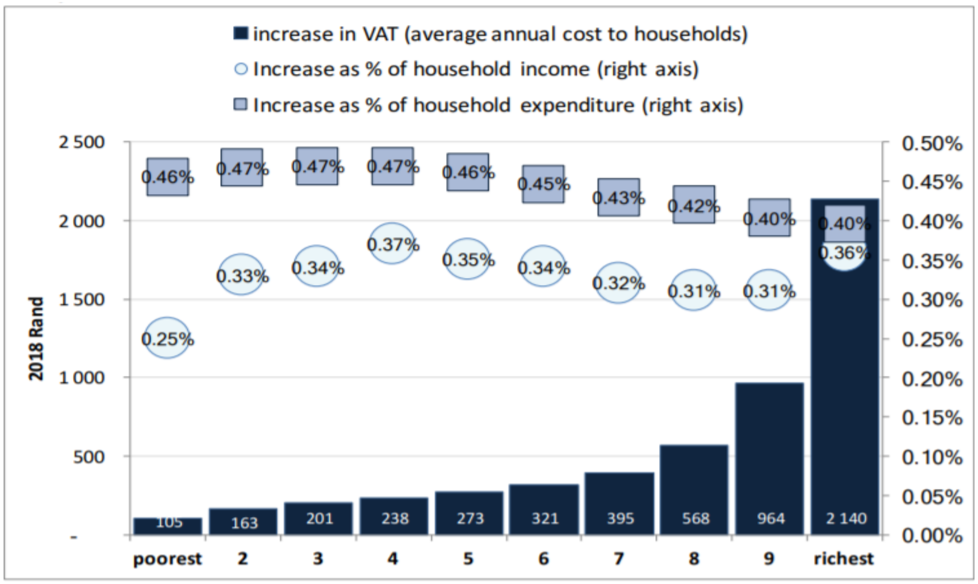

Figure 7. Incidence of the increase in VAT by households as a comparison of household income and expenditure. Source: Republic of South Africa (2018) Recommendations on Zero-Rating in the VAT system. [138]

VAT regressivity - relative versus absolute basis:

There is another school of thought that the issue of regressivity should not be considered solely on a relative basis (i.e. portion of income spent on expenditure subject to VAT) but consideration should also be given to the

[135] See footnote 64.
[136] Republic of South Africa. (2018) *'Recommendations to Minister of Finance by the Independent Panel of Experts for the Review of Zero-Rating in South Africa'*, pp 18. Available at: http://www.treasury.gov.za/comm_media/press/2018/2018081001%20VAT%20Panel%20Final%20Report.pdf (Accessed: 21 September 2019).
[137] Statistics South Africa. (2015) *'Living Conditions Survey'.* Available at: http://www.statssa.gov.za/publications/P0310/P03102014.pdf (Accessed: 18 January 2019).
[138] Republic of South Africa. (2018) pp 18.

absolute basis.[139] As illustrated in Figure 7 on an absolute basis, the more affluent households spend more in monetary value on basic goods than poorer households and therefore would receive a greater benefit with the zero-rating of these items.

VAT regressivity – single year versus lifetime income approach:

Another aspect is to consider an overall lifetime income approach as it is evident from the above studies that lower income households have a higher marginal propensity to consume, which implies that poorer households usually spend all their income with virtually no savings whilst the more affluent households save more of their income.[140] In the DTC final report on VAT, it was suggested that the extent to which VAT is regressive may be overstated, as accumulated savings are used to fund consumption expenditure during retirement.[141]

3.1.3. Economic measurement of the progressivity of a tax (Lorenz Curve)

In economic theory the Lorenz curve is used to measure income inequality. In 1905, the American economist Max Lorenz developed the Lorenz curve, which is a graphical representation of income or wealth inequality.[142] The curve is based on the horizontal axis, which is the cumulative proportion of the population and the vertical axis is the proportion share of the income. The concept of the curve was used to measure the equality of income for a specific country and is often used in conjunction with the similar economic concept of a 'Gini Coefficient'. The graph is a representation of the plotting of data points between 0% and 100%, and the shape of the curve depends on the proportion of the income at a specific proportion of the population, i.e. 20% of the population accumulates 50% or 60% of the income. The curve is accompanied with a 45° line, which is the linear presentation of perfect equality i.e. 50% of the population accumulates 50% of the income.[143]

A World Bank study performed by Inchaute et al, researched the progressivity of the main tax systems and social spending programmes in South Africa quantifying their impact on poverty and inequality. In reaching their conclusions, the Lorenz curve and a modified version described as concentration curves were used to determine the regressivity or progressivity of a tax or transfer (social grants). The approach taken was to determine the progressivity or regressivity of a tax or transfer by comparing the cumulative distribution of the tax burden or transfer benefit with the cumulative distribution of income, which are known as concentration curves. The measure of the progressivity or regressivity is determined by comparison to the Lorenz curve.[144] In Figure 8 is an illustration of the economic theory of the Lorenz curve and the concentration curves.

[139] Davis Tax Committee (DTC). (2018) *'The Final Report on VAT for the Minister of Finance'* pp 20 -21. Available at: https://www.sataxguide.co.za/wp-content/uploads/2018/05/20180329-Final-DTC-VAT-Report-to-the-Minister.pdf (Accessed: 10 February 2019).
[140] Davis Tax Committee (DTC). (2015) *'The Interim Report on VAT for the Minister of Finance'* pp 21. Available at: https://www.taxcom.org.za/docs/20150707%20DTC%20VAT%20First%20Interim%20Report%20-%20website.pdf (Accessed: 11 April 2018).
[141] Davis Tax Committee (DTC). (2018) *'The Final Report on VAT for the Minister of Finance'* pp 20. Available at: https://www.sataxguide.co.za/wp-content/uploads/2018/05/20180329-Final-DTC-VAT-Report-to-the-Minister.pdf (Accessed: 10 February 2019).
[142] Investopedia. '*Lorenz Curve*'. Available at: https://www.investopedia.com/terms/l/lorenz-curve.asp (Accessed: 20 January 2019).
[143] Investopedia. '*Lorenz Curve*'. Available at: https://www.investopedia.com/terms/l/lorenz-curve.asp (Accessed: 20 January 2019).
[144] Inchauste, G. et al (2015) *'The Distributional Impact of Fiscal Policy in South Africa',* pp 11. Available at: http://worldbank.org/drm/documents (Accessed: 16 May 2018).

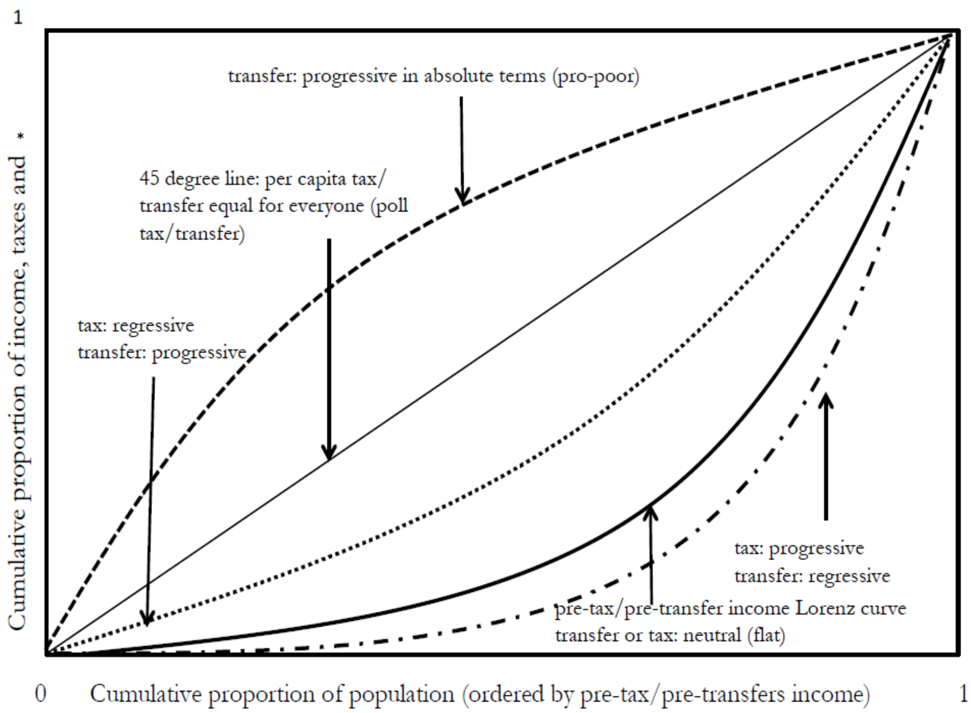

Figure 8. Illustration of the Lorenz curve and concentration curves. Source: Inchauste, G et al. (2015) The Distributional Impact of Fiscal Policy in South Africa. [145] [146]

Inchauste (et al) introduced a system of four classifications for which to evaluate the regressively or progressivity, namely; 'Absolutely progressive', 'Progressive', 'Neutral', and 'Regressive'. These classifications are defined as follows:

"***Absolutely progressive***: a transfer whose concentration curve lies everywhere above the diagonal (that is, the per capita transfer decreases with income) is globally progressive in absolute terms. An absolutely progressive transfer is frequently called 'pro-poor'.

Progressive: a tax whose concentration curve lies everywhere below the Lorenz curve for market income is globally progressive.

Neutral: a tax whose concentration curve coincides with the Lorenz curve of market income is neutral.

Regressive: a tax whose concentration curve lies everywhere above the Lorenz curve is globally regressive."[147]

In respect of indirect taxes, Inchauste (et al) concluded that for South Africa, its indirect taxes are slightly regressive. However, the concentration curve for VAT and the fuel levy is found to be progressive, and the cited

[145] *transfer benefit
[146] Inchauste, G. et al (2015) *'The Distributional Impact of Fiscal Policy in South Africa',* pp 11. Available at: http://worldbank.org/drm/documents (Accessed: 16 May 2018).
[147] Inchauste, G. et al (2015) pp 11.

reason for VAT being considered as progressive is due to the zero-rating of basic food items.[148] Figure 9 below provides an illustration of the concentration curve for South Africa's indirect taxes.

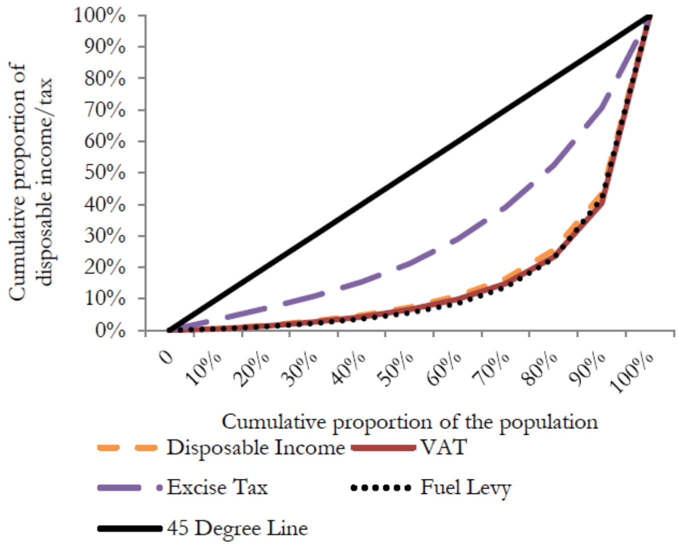

Figure 9. Concentration curves for indirect *taxes*. Source: Inchauste et al. (2015) The distributional impact of fiscal policy in South Africa.[149]

3.2 The alternatives to address the inequality of VAT

One of the first studies commissioned to research whether VAT is regressive in South Africa was undertaken by Fourie and Owen in 1993. The aim of the research was to build onto research used by the Margo Commission and to consider the distributional impact of VAT in South Africa since its introduction in 1991. Further the research was intended to consider the effectiveness of zero-rating of basic food stuffs and to comment on the theory that a higher VAT rate should be introduced on *'luxury'* goods.[150] Fourie and Owen concluded that VAT is indeed regressive but commented that: "The VAT structure should be judged, in the first place, in terms of the principles of a sound, efficient and equitable tax structure. In terms of the latter, zero-rating is beneficial, which explains its widespread use internationally to redress VAT regressivity."[151]

There are a number of approaches that may be used to address the issue that VAT has with the equity tax principle, and include; the zero-rating of basic necessary items mainly consumed by the poor, the introduction of a multiple tax rate VAT system (in addition to the zero-rate), the use of other indirect taxes such as excise duties, and the policy of redistribution of wealth through government transfers.[152] The use of exemptions has not been included as an approach as it is generally accepted globally to limit the use of exemptions due to the complexities it introduces to a tax system.

[148] Inchauste, G. et al (2015) *The Distributional Impact of Fiscal Policy in South Africa',* pp 11. Available at: http://worldbank.org/drm/documents (Accessed: 16 May 2018).
[149] Inchauste, G. et al (2015) pp 18.
[150] Fourie, F.C. and Owen, A. (1993) *'Value-Added Tax and Regressivity in South Africa'* South African Journal of Economics, 61(4), pp 296.
[151] Fourie, F.C. and Owen, A. (1993) pp 298.
[152] Jansen, A. and Calitz, E. (2017) *'Considering the efficacy of value-added tax zero-rating as pro-poor policy: The case of South Africa',* Development Southern Africa, 34(1), pp. 60 - 61.

Fourie and Owen cautioned that in their view, the issue of VAT and relief to the poor should be separated and rather make VAT an equitable form of taxation, in that it would be inappropriate to evaluate a zero-rating solely on its efficiency as a poverty relief measure. The same can be said for other taxes, such as CIT and PIT, which are not efficient poverty relief measures, but promote progressivity.[153]

Jansen (2016) discussed the Ramsey Rule and its relevance in optimizing the taxation of commodities.[154] It states that: "The deadweight loss is minimized when the rate of tax is inversely proportional to the price elasticity of demand for a good or service, given that all goods and services are subjected to the tax."[155]

This principle implies that all goods and services should be taxed differently if they have different price elasticities of demand. However, having a different taxing approach, reduces administrative efficiency, increases compliance risk and makes enforcement costlier; thus, advocating for a single universal rate approach.[156]

3.2.1 The zero-rating of basic items

3.2.1.1 The benefit and costs of zero-rating

The question to be addressed in this section is whether zero-rating as an instrument can be used to effectively mitigate to a certain degree the regressivity of VAT and contribute to a more equitable tax system. The elements of equity, efficiency and administrative costs are all important considerations, and VAT and zero-rating should be continuously evaluated to these tax principles.[157]

In order to determine whether zero-rating as an instrument provides the benefit of reducing the poor's VAT burden, the accepted approach is to consider consumer spending patterns. Jansen (2016) performed an economic analysis on household spending patterns for the 20 zero-rated items[158] per consumption decile based on the Income and Expenditure Survey: 2010/2011. The findings of this study concluded that lower income groups spent a higher percentage of their annual spending on the consumer goods basket for these zero-rated items, which confirmed that zero-rating of these items reduces the impact of VAT regressivity.[159] Figure 10 includes the calculations from the study which present on a proportionality basis the expenditure spent on the zero-rated items. The bottom four income groups (Decile 1 to 4) reflect the poor or needy that require tax relief.[160]

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153 Fourie, F.C. and Owen, A. (1993) *'Value-Added Tax and Regressivity in South Africa'* South African Journal of Economics, 61(4), pp 291 - 292.
154 Oxford University Press. '*Ramsey Rule'*. Oxford Reference. Available at: http://www.oxfordreference.com/view/10.1093/oi/authority.20110803100403456 (Accessed: 20 January 2019).
155 Rosen, H. S. and Gayer, T. (2014) *'Public Finance'.* 10th edition. McGraw-Hill Irwin.
156 Jansen, A. and Calitz, E. (2017) *'Considering the efficacy of value-added tax zero-rating as pro-poor policy: The case of South Africa',* Development Southern Africa, 34(1), pp 60 -61.
157 Fourie, F.C. and Owen, A. (1993) pp 298.
158 The items relate to a representation of the 19 food items in section 11(1)(j) and illuminating paraffin in section 11(1)(l).
159 Jansen, A. and Calitz, E. (2017) pp. 62 -65.
160 Jansen, A. and Calitz, E. (2017pp. 63.

Consumption decile	**1**	**2**	**3**	**4**	**5**	**6**	**7**	**8**	**9**	**10**
Zero-rated item	**Percentage of total consumption**									
Rice	1.83%	1.87%	1.72%	1.37%	1.16%	0.89%	0.61%	0.35%	0.17%	0.06%
Brown Bread	3.75%	2.85%	2.54%	2.12%	1.75%	1.41%	0.97%	0.60%	0.27%	0.10%
Maize Meal	4.70%	4.35%	3.55%	2.56%	1.96%	1.45%	0.84%	0.44%	0.14%	0.03%
Mealie Rice	0.01%	0.01%	0.02%	0.01%	0.01%	0.00%	0.00%	0.00%	0.00%	0.00%
Samp	0.36%	0.33%	0.26%	0.16%	0.16%	0.10%	0.05%	0.03%	0.01%	0.00%
Dried Beans	0.56%	0.45%	0.36%	0.24%	0.18%	0.10%	0.06%	0.03%	0.01%	0.00%
Dried Lentils	0.00%	0.00%	0.00%	0.01%	0.01%	0.01%	0.00%	0.00%	0.00%	0.00%
Canned Phichards	0.52%	0.50%	0.45%	0.37%	0.29%	0.30%	0.20%	0.11%	0.04%	0.01%
Powdered Milk	0.10%	0.13%	0.08%	0.10%	0.11%	0.09%	0.06%	0.04%	0.01%	0.01%
Sour Milk	0.55%	0.45%	0.40%	0.35%	0.26%	0.18%	0.14%	0.07%	0.03%	0.01%
Milk	0.94%	0.86%	0.86%	0.86%	0.91%	0.85%	0.70%	0.64%	0.49%	0.25%
Cooking fat (Vegetable)	0.01%	0.00%	0.02%	0.01%	0.01%	0.01%	0.00%	0.00%	0.00%	0.00%
Edible Oils	1.43%	1.33%	1.19%	0.93%	0.77%	0.57%	0.40%	0.24%	0.10%	0.04%
Eggs	0.60%	0.73%	0.65%	0.62%	0.57%	0.53%	0.42%	0.29%	0.17%	0.07%
Fruit	0.40%	0.42%	0.39%	0.38%	0.36%	0.35%	0.30%	0.29%	0.27%	0.20%
Vegetables	3.42%	2.86%	2.59%	2.14%	1.90%	1.57%	1.19%	0.87%	0.58%	0.36%
Paraffin	0.77%	0.60%	0.55%	0.43%	0.34%	0.23%	0.13%	0.06%	0.01%	0.00%

Figure 10. Spending on zero-rated goods as a proportion of total consumption, by consumption decile. Source: Jansen (2016) Considering the efficacy of value-added tax zero-rating as pro-poor policy: The case of South Africa', Development Southern Africa [161]

With reference to Figure 10, it is evident that the zero-rating of certain food items has provided a benefit in reducing the impact of VAT regressivity. Furthermore, Fourie and Owen conclude that there is an optimal selection of zero-rating goods to achieve an equity gain and to efficiently distribute the benefit to the households for which the benefit is intended, i.e. poorer households would receive the biggest relative relief.[162] More detail on the selection of the zero-rating goods is provided in Section 3.3.

Kearny recommended that the zero-rating of food could reduce poverty by lowering food prices, and reducing the regressiveness of VAT, if it is combined with a proportional increase in direct taxes i.e. PIT and CIT. Although the benefit of zero-rating of food would also be largely derived by the food industry as food is an intermediate in the production of the industries goods.[163]

However, it should be noted that the assumption in most studies is that food prices would be reduced by the VAT component, as South African food prices are not regulated the setting of food prices would be in the

[161] Jansen, A. and Calitz, E. (2017) *'Considering the efficacy of value-added tax zero-rating as pro-poor policy: The case of South Africa',* Development Southern Africa, 34(1), pp. 63.
[162] Fourie, F.C. and Owen, A. (1993) *'Value-Added Tax and Regressivity in South Africa'.* South African Journal of Economics, 61(4), pp 294.

control of the retailers who sell the goods to households. Other economic theory suggests that prices are influenced by the market structure and the relevant price elasticities of demand and supply.[164]

Further, it is important to bear in mind that the benefit of the zero-rating relief will not be solely focused on poorer households as the benefit would be spread across the whole income spectrum in varying degrees.[165] Zero-rating is not to provide an absolute poverty relief but it is an instrument that is available to promote poverty relief as it does promote vertical equity to a tax system and addresses the VAT structural issue by adjusting its regressivity.

Monetary and non-monetary costs associated with zero-rating:

Notwithstanding the above, it is recommended that the benefits of a zero-rating should be assessed and measured against its costs both from a monetary perspective and an administrative perspective.

Shrinking the tax base and the cost to the fiscus:

As discussed in Chapter 2, an ideal VAT system should not include any zero-ratings or exemptions, as this results in shrinking the tax base. When the tax base is reduced by introducing a zero-rating, it implies that the government would be forfeiting any VAT revenue from the supply of the zero-rated item. This results in a cost to the fiscus.[166] Most basic goods, such as food, are consumed by all households irrespective of their income, which is evident in the consumption patterns of zero-rated products which is quite broad, therefore when high income households consume this expenditure the government has forfeited the revenue it would have received. This benefit of not paying VAT on zero-rating items, such as food, would be a significant saving for the rich, which is counterintuitive to a progressive tax policy and the government's strategy of redistribution.

According to National Treasury the current zero-rating of basic food items contained in Schedule 2 accounts for a loss of R 22.794 billion in revenue,[167] which coincidentally is similar to the amount of additional revenue budgeted of R 22.9 billion from the 1% increase in the VAT rate.[168]

Loss of revenue will require compensation

It is unlikely that a government can afford to simply forfeit income and will identify alternative sources of revenue to compensate for the loss of revenue resulting from the zero-rating of an item.

[163] Kearney, M. and van Heerden, J. (2004) *'Zero-Rating Food in South Africa: A Computable General Equilibrium Analysis'.* South African Journal of Economics, 7(3) pp. 529.
[164] Republic of South Africa. (2018) *'Recommendations to Minister of Finance by the Independent Panel of Experts for the Review of Zero-Rating in South Africa',* pp 22. Available at: http://www.treasury.gov.za/comm_media/press/2018/2018081001%20VAT%20Panel%20Final%20Report.pdf (Accessed: 21 September 2019).
[165] Jansen, A. and Calitz, E. (2017) *'Considering the efficacy of value-added tax zero-rating as pro-poor policy: The case of South Africa',* Development Southern Africa, 34(1), pp. 68.
[166] Davis Tax Committee (DTC). (2018) *'The Final Report on VAT for the Minister of Finance'* pp 19. Available at: https://www.sataxguide.co.za/wp-content/uploads/2018/05/20180329-Final-DTC-VAT-Report-to-the-Minister.pdf (Accessed: 10 February 2019).
[167] Davis Tax Committee (DTC) (2018) pp 19.
[168] Republic of South Africa. (2018) *'National Treasury Budget Speech 2018'*, pp 11. Available at: http://www.treasury.gov.za/documents/national%20budget/2018/speech/speech.pdf (Accessed: 5 April 2018).

In 2004, Kearny studied the zero-rating of food in South Africa and used a computable general equilibrium (CGE) model, developed by Thurlow and van Seventer in 2002,[169] to analyse the combined effects of zero-rating food and using alternative revenue sources to compensate for the loss in tax revenue. The alternative revenue sources proposed included increasing direct taxes or applying a higher VAT rate to other goods and services.[170] Thurlow and van Seventer (2002) determined that high income groups spent a larger proportion of their income on business services and financial services compared to low income groups.[171] Therefore, it is arguable that increasing VAT on these items would contribute towards vertical equity. However, due to financial services being hard to tax, they are exempted from VAT in terms of section 12(a) of the VAT Act. The study[172] investigated the improvement of VAT regressivity from a broader economic perspective. The last alternative revenue source Kearny considered was to increase the VAT rate to 16%.[173]

The outcome of the study was that VAT on business services and financial services was not a realistic method to improve the regressivity of VAT, as the VAT rate on these items to compensate for the loss of revenue would need to be in excess of 42%.[174] Further, the CGE model does not measure administration and compliance costs, which has the potential to increase tax evasion.

In conclusion, Kearny stated that to make the zero-rating basic food item a viable option there would need to be a proportional increase in PIT and CIT.[175]

Administrative Issues:

As discussed in Chapter 1, the VATCOM noted that there are a number of administrative issues associated with zero-rating and include “difficulties in defining the goods, creating the opportunity for evasion, adding complexity to the system and costs to the vendor.”[176]

When an item has been identified for a tax concession, such as zero-rating, there are a number of administrative hurdles that must be considered to ensure a smooth transition. This includes the tax policy decision of what is included in the zero-rating provisions and which items fall outside the ambit of the zero-rating provision. Therefore, there is a need for a proper definition as an ambiguous definition is open to interpretation and easily leads to the abuse of the zero-rating provisions and thus tax evasion,[177] i.e. zero-rating the supply of goods which is intended to be subject to the standard VAT rate.

The government may change underlying Acts or Regulations from time to time, and should the list not be updated timely, it can cause confusion on whether an item is zero-rated or standard-rated and further provides

[169] Thurlow, J. and van Seventer, D. (2002) *‘A Standard Computable General Equilibrium Model for South Africa’,* pp. 1. Available at: http://ageconsearch.umn.edu/record/16279/ (Accessed: 1 December 2019).
[170] Kearney, M. and van Heerden, J. (2004) *‘Zero-Rating Food in South Africa: A Computable General Equilibrium Analysis’.* South African Journal of Economics, 7(3) pp 529.
[171] Thurlow, J. and van Seventer, D. (2002) pp 11.
[172] At the time of the study the VAT rate was 14%.
[173] Kearney, M. and van Heerden, J. (2004) pp 525.
[174] Kearney, M. and van Heerden, J. (2004) pp 525.
[175] Kearney, M. and van Heerden, J. (2004) pp 529.
[176] Marais, G. (1991) *‘Report of the Value-Added Tax Committee (VATCOM)’.* Pretoria: Govt. Printer, pp 18-19.
[177] Marais, G. (1991) ‘pp 18-19.

an opportunity for tax evasion. This illustrates that defining goods is very important and that zero-rating items pose many difficulties.

<u>Examples of the difficulties in definitions in practice:</u>

The issue of practice notes and binding general rulings to provide guidance:

1. VAT practice notes:

In the 1990's various VAT practice notes were issued to provide guidance on which items fall within the ambit of the zero-rating provisions. These items were usually defined in terms of a Regulation or an Act which contained such definition. The practice notes that are notable in this regard relate to dried maize and maize products and brown bread. These practice notes were later withdrawn as Schedule 2 had been updated to reflect such guidance.

No	Date	Title	Item	Description
6	13 Dec1991	The tax treatment of mealies supplied by producers and the maize board	Item 5	This practice provided guidance on mealies.
12	24 Nov 1993	The zero-rated supply of brown bread	Item 1	This practice note provided a definition for the term brown bread. Brown bread is defined in terms of Regulation 1 of the Regulations in terms of Government Notice Nr R.577.
15	07 Aug 1995	VAT treatment of supplies of dried maize and maize products	Item 5	This practice note replaced practice note 6. The reason for this practice note was to update the definition of maize to reflect the amendments made to the Summer Grain Scheme on 13 April 1995.

Figure 11. Table of Practice Notes issued by the South African Revenue Service (SARS). Source: www.sars.gov.za[178]

Milk and dairy products:

In 1998, the Taxation Laws Amendment Act No 30 of 1998 amended Item 9, 10 and 16 of Schedule 2 Part B to reflect the change in the underlying Act. Prior to the amendment these items were defined in terms of the Marketing Act No 59 of 1968. After the amendment these items were defined in terms of the Agricultural Product Standards Act No 119 of 1990.[179]

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[178] South African Revenue Service. (1993) '*Practice Note No. 12'*. Available at: https://www.sars.gov.za/AllDocs/LegalDoclib/Notes/LAPD-IntR-PrN-Arc-2016-06-Arc-06%20-%20VAT%20Practice%20Note%2012%20of%201993%20withdrawn%201%20April%202016.pdf (Accessed: 17 March 2019) and South African Revenue Service. (1995) 'Practice Note No. 15'. Available at: https://www.sars.gov.za/AllDocs/LegalDoclib/Notes/LAPD-IntR-PrN-Arc-2014-06%20-%20VAT%20Practice%20Note%2015%20of%201995%20withdrawn%201%20February%202010.pdf (Accessed: 17 March 2019).

[179] Republic of South Africa. (1998) Taxation Laws Amendment Act, 1998 (No. 30 of 1998). Government Gazette No.19013 29 June 1992 (Published under Government Notice R.884).

Brown bread:

Practice Note 12 provided guidance on the definition of brown bread, which was defined in light of the principles of Regulation 1 of the regulations[180] (1991 Regulation). The 1991 Regulation confirmed that brown bread, could be subject to the allowable deviations, but should consist of "a dough made from brown wheaten meal and water, with or without other ingredients that has been fermented by yeast or otherwise leavened and which has been baked in any form, size or shape."[181]

In terms of Practice Note 12:[182]
"The supply (other than in the course of the provision of a meal or refreshment) of any type of brown bread shall be subject to tax at the zero rate, provided -
(i) it is marketed and sold under the description brown bread;
(ii) the meal content of the dough consists of at least 50 per cent brown bread meal; and
(iii) the mass of the loaf exceeds 100 grams.

Products such as 'whole-wheat brown bread', 'high fibre brown bread', 'high protein brown bread' and 'brown health bread' which satisfy the above requirements will accordingly be subject to the zero rate."[183]

In 2008 the 1991 Regulation was repealed and replaced with the 2008 Regulation.[184] However, Item 1[185] was not amended until December 2017 and had still referred to the 1991 Regulation and Practice Note 12 was withdrawn on the 1 April 2016.

In 2017 a new regulation,[186] was introduced to replace the 2008 Regulation. There was a notable difference in the definition of brown bread introduced in the 2017 Regulation, which would result in certain brown bread such as; whole-wheat brown bread, high fibre brown bread, high protein brown bread and brown health bread being standard rated. Therefore, as Item 1 still referred to the outdated 1991 Regulation it caused issues for the industry in determining when it was appropriate to apply the zero-rate.[187] In addressing the confusion, SARS issued Binding General Ruling 46 on 27 November 2017, which stated that until the 31 March 2018; 'whole-wheat brown bread', 'high fibre brown bread', 'high protein brown bread' and 'brown health bread', may be zero-rated.

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180 Government Notice R.577 published in Government Gazette No 13074 of 15 March 1991.
181 South African Revenue Service. (1993) *'Practice Note No. 12'.* Available at: https://www.sars.gov.za/AllDocs/LegalDoclib/Notes/LAPD-IntR-PrN-Arc-2016-06-Arc-06%20-%20VAT%20Practice%20Note%2012%20of%201993%20withdrawn%201%20April%202016.pdf *(*Accessed: 17 March 2019).
182 South African Revenue Service (1993).
183 South African Revenue Service (1993).
184 Government Notice R.186 published in Government Gazette 30782 of 22 February 2008, (2008 Regulation).
185 Item 1 of Schedule 2 Part B of the VAT Act.
186 Government Notice R.405 published in Government Gazette No 40828 of 5 May 2017 (2017 Regulation).
187 South African Revenue Service. (2017) '*Binding General Ruling (VAT) 46: Supply of Brown Bread'.* Issued on 27 November 2017. Available at: https://www.sars.gov.za/AllDocs/LegalDoclib/Rulings/LAPD-IntR-R-BGR-2017-09%20-%20BGR46%20Supply%20of%20brown%20bread.pdf (Accessed: 17 March 2019).

In the Taxation Laws Amendment Act No 17 of 2017, Item 1[188] was updated to refer to the 2017 Regulation and Tax Laws Amendment Act No 21 of 2018, amended Item 1[189] to read 'brown bread and whole wheat brown bread as defined respectively in Regulation 1 of the Regulations in terms of Government Notice No. R.405 published in Government Gazette No. 40828 of 5 May 2017' therefore from 1 April 2018; 'high fibre brown bread', 'high protein brown bread' and 'brown health bread' became standard-rated .

2. Binding General Rulings ("BGRs") issued to provide guidance on the zero-rating of other items in Schedule 2.

There are a number of BGRs which were issued by SARS as there were uncertainties on whether VAT at the zero-rate could be applied to various categories of goods, i.e. vegetables, fruit and sanitary towels. These BGRs provided detailed guidance on which products would fall within the ambit of the zero-rating provisions. Refer to the table in Annexure B for more details on the BGRs issued in this regard.

In conclusion it is evident from the practical examples mentioned that the introduction of zero-rating provisions increases the administrative burden, as the legislation could cause confusion, i.e. what items fall within the zero-rating provisions, and the need to update legislation should it refer to another Regulation or Act.

3.2.2 Multiple VAT rate system

In order to address the regressivity of VAT, multiple VAT rates could be introduced to soften its regressivity. Although the zero-rate is applicable a multiple VAT rate system is usually where there is a reduced rate applicable to goods and services that are consumed by lower income households or considered as essential goods which on a merit basis requires a special tax treatment. A feature of this system that may be controversial is that the government is in effect deciding the products that should be consumed by the poor by implementing a reduced rate.[190]

This is opposite to the current global trend of moving towards a single rate. The OECD advocates for a single tax rate and the global trend is that countries adopting VAT since the early 1990s have introduced a single VAT rate.[191] Figure 12 provides a table of the global trends in adopting a single VAT rate.

[188] Item 1 of Schedule 2 Part B of the VAT Act.
[189] Item 1 of Schedule 2 Part B of the VAT Act.
[190] Jansen, A. and Calitz, E. (2017) *'Considering the efficacy of value-added tax zero-rating as pro-poor policy: The case of South Africa',* Development Southern Africa, 34(1), pp. 60.
[191] Jansen, A. and Calitz, E. (2017) pp 69.

	Number of countries introducing VAT for the first time	Percentage with a single rate at introduction
Before 1990	48	25%
1990-1999	75	71%
1999-2011	31	81%

Figure 12. VAT systems with a single rate at time of introduction. Source: Keen (2012) Targeting, Cascading and Indirect Tax Design.[192]

In addition to a standard and zero rate, a third rate is envisioned to be introduced on goods deemed to be a 'luxury'. The purpose of this luxury VAT rate is to address the vertical equity issues, but other research has found that this alternative does little to contribute to poverty relief as the amount of revenue required from these luxury goods to cover the loss in revenue from the reduced VAT rate is too high i.e. the VAT rate on luxury goods would need to be significantly higher than the current VAT rate.[193]

Further this luxury rate becomes unattractive when you consider the additional complexities it introduces into a VAT system, especially in the manner of administering multiple VAT rates and compliance with respect to a definition for such goods.[194] In Jansen's study it was determined that typical luxury goods such as mobile phones and televisions are also purchased by low-income households. It was established that there are only a number of items that would solely be recommended for a luxury good treatment and include; four-wheel drive vehicles, boats, aircrafts and go carts.[195] Therefore, the likelihood that this luxury tax would provide a sustainable and sufficient revenue stream is very low.

Keen (2012) commented that "the amount of redistribution that can be achieved by differentiating rates of indirect taxation will generally be quite limited… because variation in the share of income spent on particular goods is generally just not enough to make this an effective way to distinguish between poor and rich."[196]

It is accepted that even in a VAT system where there is a single VAT rate, such as South Africa, opposed to countries which have differential rates or reduced VAT rates for certain products, there is still a place for zero-rating.[197]

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[192] Jansen, A. and Calitz, E. (2017) *'Considering the efficacy of value-added tax zero-rating as pro-poor policy: The case of South Africa',* Development Southern Africa, 34(1), pp. 69.
[193] Davis Tax Committee (DTC). (2018) *'The Final Report on VAT for the Minister of Finance'* pp 26. Available at: https://www.sataxguide.co.za/wp-content/uploads/2018/05/20180329-Final-DTC-VAT-Report-to-the-Minister.pdf (Accessed: 10 February 2019).
[194] [194] Jansen, A. and Calitz, E. (2017) pp. 69 - 70.
[195] Jansen, A. and Calitz, E. (2017) pp 70.
[196] Keen, M. (2012) *'Targeting, Cascading, and Indirect Tax Design'*, Indian Growth and Development Review, pp. 183.
[197] Jansen, A. and Calitz, E. (2017) pp 71.

3.2.3 VAT in the context of all indirect taxes

Another approach to address the regressivity of VAT is to evaluate its regressivity in the context of all indirect taxes. Excise duties is also an indirect tax and in South Africa excise duties are included in the price of goods which are subject to VAT.[198] Therefore, if excise duties are applied to 'luxury goods' consumed by middle- and higher- income groups, this is a step-in promoting redistribution. The problem with this approach is that it still suffers from the issues promoting an optimal VAT system, i.e. compliance issues, enforcement costs, little real increase in tax revenue.[199]

3.2.4 Combination of tax and government expenditure

In this approach the total fiscal impact on households is considered and the expenditure side of the budget should be used to undertake a fiscal redistribution.[200] Historically South Africa has mostly adopted this approach in addressing VAT regressivity except for the zero-rating of basic foodstuffs. This approach is assessed in further detail in the rest of this chapter.

3.3 Zero-rating versus government transfers

As a poverty relief measure, a zero-rating may not be the most efficient, compared to targeted expenditure programmes (transfers), as there will be a loss of revenue to the fiscus from more affluent households. However, it is important to determine whether the South African expenditure system is efficient enough to reduce the reliance on zero-rating as relief for the poor and whether the current list of zero-rated foodstuffs should be entirely removed.

Fourie and Owen (1993) believed it is impractical to remove the current VAT zero-ratings and exemptions in the South African context as it would not be politically responsible to the extent that the social security system is ineffective.[201]

Van der Berg (2009)[202] was commissioned to perform a study on the fiscal incidence of social spending in South Africa by National Treasury, which related to the effectiveness of South Africa's expenditure on its socio-economic objectives. The outcome was that between the period 2000 and 2006, government spend made a significant contribution to reducing income inequalities, and the fiscal redistribution effect strengthened. The measure used to determine the level of inequality in a country is referred to as a Gini coefficient. A Gini coefficient is a statistical measure of distribution and is commonly used for determining income distribution.[203]

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[198] Davis Tax Committee (DTC). (2018) *'The Final Report on VAT for the Minister of Finance'* pp 19. Available at: https://www.sataxguide.co.za/wp-content/uploads/2018/05/20180329-Final-DTC-VAT-Report-to-the-Minister.pdf (Accessed: 10 February 2019).
[199] Jansen, A. and Calitz, E. (2017) *'Considering the efficacy of value-added tax zero-rating as pro-poor policy: The case of South Africa',* Development Southern Africa, 34(1), pp. 69.
[200] Keen, M. (2012) *'Targeting, Cascading, and Indirect Tax Design',* Indian Growth and Development Review, pp. 184.
[201] Fourie, F.C. and Owen, A. (1993) *'Value-Added Tax and Regressivity in South Africa'.* South African Journal of Economics, 61(4), pp 285.
[202] Van der Berg, S. (2009) *'Fiscal incidence of social spending in South Africa, 2006'.* Stellenbosch Working Paper Series No. WP10/2009, pp 1 and 22. Available at: http://www.ekon.sun.ac.za/wpapers/2009 (Accessed: 26 January 2019).
[203] Investopedia. '*Gini Index'.* Available at: https://www.investopedia.com/terms/g/gini-index.asp (Accessed: 20 January 2019).

The study used a primary Gini coefficient which is income distribution for South Africa and an adjusted Gini coefficient, which accounted for net fiscal transfers (consisting of social spending benefits and direct and indirect taxes).

Gini coefficient	1995	2000	2006
Gini coefficient – Income excluding grants	0.67	0.71	0.69
Gini coefficient – Income plus social spending benefits	0.58	0.58	0.53
Gini coefficient – Income minus taxes plus social spending benefits	0.53	0.53	0.47

Figure 13. Gini coefficient between 1995 and 2006. Source: Van der Berg (2009) Fiscal incidence of social spending in South Africa, 2006 [204]

Van der Berg (2009) concluded that even though there has been an increase in social spending, i.e. social grants, it has only had a limited impact in addressing the broader issue of inequality in South Africa.[205] According to the World Bank, South Africa's Gini coefficient in 2015 is 0.63,[206] which is a similar result to Van der Berg's study.

Jansen (2016) stated that for the purposes of tax analysis a balanced budget approach should be utilised. This implies that when a tax concession is made, i.e. an item is zero-rated, the loss in revenue must be compensated for by other taxes, which in her view will have different distributional features.[207] It is important to reflect that the tax system in place and distributional effect today has been shaped by the decision of zero-rating certain goods in 1991 and 1993 and should these items now be removed from the list of zero-rating partially or in totality. Jansen argues that *"the impact on the economy goes much further than that of the removal because a new set of distributional relations will be effected."*[208] The effect will be dependent on how the government utilizes the potential extra revenue from the supply of the previously zero-rated goods. It is arguable that if this extra VAT revenue received from the low-income groups that would be most impacted by the removal of the zero-rating, is channelled wholly into financing or extending existing income support programmes then the government could utilize the extra revenue from the other higher income groups for its other fiscal priorities. Notwithstanding, this approach would depend on whether the same poorer individuals who bear the extra VAT cost are the same beneficiaries of the income support programmes.[209]

Jansen argued that should the zero-rating items be removed, the question shifts to "How well targeted do public spending measures have to be for the poor to be best served not by taxing at a particularly low or zero-rate

[204] Van der Berg, S. (2009) *'Fiscal incidence of social spending in South Africa, 2006'.* Stellenbosch Working Paper Series No. WP10/2009, pp 22. Available at: http://www.ekon.sun.ac.za/wpapers/2009 (Accessed: 26 January 2019).
[205] Van der Berg, S. (2009) pp 22.
[206] World Bank Group (2019) '*South Africa – Overview*'. Available at: https://www.worldbank.org/en/country/southafrica/overview (Accessed: 4 January 2020).
[207] Jansen, A. and Calitz, E. (2017) *'Considering the efficacy of value-added tax zero-rating as pro-poor policy: The case of South Africa',* Development Southern Africa, 34(1), pp. 65.
[208] Jansen, A. and Calitz, E. (2017) pp 65.
[209] Jansen, A. and Calitz, E. (2017) pp 65 - 66.

those commodities that account for an especially large part of their budget, but taxing them and using the proceeds to increase that public spending?"[210]

Jansen performed a benefit to cost ratio for social assistance and zero-rating, and concluded based on the benefit to cost ratio, that social spending is more effective. However, the issue of price inflation impacts on this benefit to cost analysis. Jansen states the benefits of zero-rating to the poor is that: "zero-rating adjusts automatically with inflation; transfers are cash amounts that require discretionary inflation adjustments."[211] The implication is that zero-rating is a better option for the poor if the cash transfers they receive from the state are not updated in line with price inflation on a frequent basis.[212] These cash transfer increases usually only take place once or twice a year and are announced during the national budget speech or the medium-term budget policy statement.

In 2016 Jansen calculated an estimate should zero-ratings be abolished, and all items are taxed at the standard VAT rate, including an adjustment for the delivery and admin costs providing social grants. A change in tax policy by abandoning the zero-rating of basic items would eliminate the VAT leakage in the VAT system, therefor promoting tax efficiency. However, given the poverty in South Africa there would need to be compensation to the poor that is efficient and well targeted.[213]

Another test Jansen introduced when evaluating whether a zero-rating or cash transfer system is more effective is whether this is means-tested. Means-tested refers to the circumstances that those who are in need receive the benefit.[214] In the 1990's when South Africa introduced VAT there was no sophisticated welfare system, and the poor were significantly affected, however, since then a more sophisticated cash transfer system has been developed, which involves means testing. This includes old age pensions, disability grants, and child support grants, where the benefit decreases as income increases. Zero-rating lacks a means-testing as it is an absolute benefit experienced by all, rich and poor.[215]

When it comes to targeted expenditure there is the possibility that the existing beneficiary of the cash transfer may not be the rightful beneficiary.[216] Although South Africa has made significant progress in the development of a welfare system, the removal of current zero-rating would be a thorny issue and given the high level of inequality as evidenced by the high Gini coefficient it would be difficult to conclude that the zero-rating of basic food items should be abandoned.

[210] Jansen, A. and Calitz, E. (2017) *'Considering the efficacy of value-added tax zero-rating as pro-poor policy: The case of South Africa',* Development Southern Africa, 34(1), pp. 66.
[211] Jansen, A. and Calitz, E. (2017) pp. 66.
[212] Jansen, A. and Calitz, E. (2017) pp 66.
[213] Jansen, A. and Calitz, E. (2017) pp 66.
[214] Jansen, A. and Calitz, E. (2017) pp 68.
[215] Jansen, A. and Calitz, E. (2017) pp 68.
[216] Jansen, A. and Calitz, E. (2017) pp 68.

3.4 The definition of essential or merit goods and basic foodstuffs and the selection or targeting of zero-rated items

Given the 2018 VAT rate increase and its impact on the poor, there have been calls to increase the items on the zero-rating list. The question, therefore, resolves to one of what is the definition of a merit good (good requiring a tax concession) and what is the justification for providing a special tax treatment? Another term to describe these goods is 'essential' and are usually considered goods that are necessary as opposed to luxury goods. Prior to the VAT rate increase, mostly food items were included as basic items, except for illuminating paraffin.

It is not an easy task to select which goods should be considered as basic[217] and the definition of essential goods will likely differ between countries.[218]

Tait (1988) distinguished between essential and luxury goods for the purposes of zero-rating as a distinction between processed and unprocessed foods.[219] On the other hand Jansen mentioned from Calcaterra and Kirsten's unpublished research (2003),[220] that this distinction of basic goods should include the differentiation between products undergoing minimal processing and staple foods which are traditionally included in the diets of poorer households, with the latter being considered basic. Cnossen (2003) stated that if the spending patterns between poor and rich are distinctly different then goods can be separated into sub-groups that could be zero-rated, which makes it easier to select these goods.[221] However, in the South African context there is no clear or significant distinction between the spending patterns of the rich and poor on certain goods.

Due to poverty and other social issues, the inclusion of zero-rating provisions may be unavoidable, therefore the task is to determine the optimal selection of the zero-rated basket of goods.[222] This causes a range of difficulties; such as administrative concerns (i.e. ease of definition), problems of substitution, the existence of hard-to-tax goods or services, the promotion of 'merit goods', and the achievement of equity.[223] Therefore, the question is what method should be used to determine which goods should be considered as basic goods and be selected for zero-rating. Fourie and Owen (1993) concluded that a method in selecting zero-rating must be rational.[224]

Fourie and Owen developed a methodology for selecting a rational basis, which is to use data supplied in the household expenditure survey conducted regularly by STASA. The first step would be to determine whether a particular product is consumed mainly by the poor, and secondly whether or not the product is an important

[217] Fourie, F.C. and Owen, A. (1993) *'Value-Added Tax and Regressivity in South Africa'.* South African Journal of Economics, 61(4), pp 284.
[218] Jansen, A. Stoltz, E. and Yu, D. (2013) *'The Targeting of Zero-Rated Basic Foodstuffs under Value-Added Tax (VAT) in South Africa',* Journal of Econometrics, 37(3), pp 92 and Cnossen, S. (2003). *'The Incidence of Consumption in Member Countries of the South Africa* Development Community'. Paper prepared for the Southern African Conference on Excise Taxation, Centurion Lake Hotel, Gauteng, South Africa, 11-13 June 2003, referred to Khalilzadeh-Shirazi, J. and Shah, A. (1991). *'Tax Policy in Developing Countries'.* A World Bank Symposium. Washington: World Bank.
[219] Tait, A.A. (1988) *'Value-Added Tax; International Practice and Problems'*, International Monetary Fund, Washington, D.C.
[220] Calcaterra, M. and Kirsten, J. (2003) *'An Economic Assessment of Zero Rating of VAT on Red Meat'*. Pretoria: University of Pretoria.
[221] Jansen, A. Stoltz, E. and Yu, D. (2013) pp 90 and Cnossen, S. (2003).
[222] Fourie, F.C. and Owen, A. (1993) pp 284.
[223] Fourie, F.C. and Owen, A. (1993) pp 284 - 285.
[224] Fourie, F.C. and Owen, A. (1993) pp 295.

element in the budget of a poor household. However, this methodology does not take into account other considerations, such as administrative and compliance issues.[225] The methodology introduced an 'equity gain ratio' in order to evaluate whether products meet the rational criteria discussed above. It explained that the ratio between two such percentages indicates the relative weight of the benefit from zero rating a particular product for a lowest income household compared to a highest income household.[226] The equity gain ratio is as follows:

$$\frac{(percentage\ of\ lowest\ income\ budget\ spent\ on\ good)^2}{percentage\ of\ highest\ income\ budget\ spent\ on\ good}$$

It is not appropriate to select products for zero-rating by merely ranking products. The selection of products should be a combination of ranking goods by the equity gain ratio and the relevance of the product's importance to the poor.[227]

Subsequently an estimate of the tax revenue forfeited, should products be zero-rated, should be calculated. It recommended that the government should consider a maximum amount of tax revenue it is prepared to forgo and use the list of equity ratios per product ranked per highest to lowest, and together with the estimate, select products that together reach the cumulative loss to the fiscus.[228] This could imply that a government could purposely not select a product which has a high equity ratio purely on the basis that such product is too costly and results in too significant a loss in tax revenue.

As not to confuse a government's policy, non-basic goods like cigarettes, tobacco and beer should be excluded, given these items are traditionally labelled as 'sin goods' and subject to excise duties.[229]

Fourie and Owen commented that economic, industry-specific, administrative and other considerations, including lobbying and political pressure from interest groups, could considerably influence an eventual selection of goods for zero-rating.[230]

Jansen (2012) argued that there could be improvement made in targeting of the zero-rated basket.[231] As a case study the food category of vegetables was investigated to determine whether changes in the tax treatment should be made to the sub-categories of vegetables to have a more direct impact on the cost of food for low income households. [232]

Jansen analysed the spending patterns for the different categories of vegetables, namely; fresh, frozen and canned vegetables, to determine which of these types are disproportionally consumed by the poor. It was

[225] Fourie, F.C. and Owen, A. (1993) *'Value-Added Tax and Regressivity in South Africa',* South African Journal of Economics, 61(4), pp 295.
[226] Fourie, F.C. and Owen, A. (1993) pp 295. Kindly note the 2 for the quoted equation reflects the mathematical concept of being squared.
[227] Fourie, F.C. and Owen, A. (1993) pp 295.
[228] Fourie, F.C. and Owen, A. (1993) pp 296.
[229] Fourie, F.C. and Owen, A. (1993) pp 296.
[230] Fourie, F.C. and Owen, A. (1993) pp 296.
[231] Jansen, A. Stoltz, E. and Yu, D. (2013) *'The Targeting of Zero-Rated Basic Foodstuffs under Value-Added Tax (VAT) in South Africa',* Journal of Econometrics, 37(3), pp. 88.
[232] Jansen, A. Stoltz, E. and Yu, D. (2013) pp. 88.

expected that the poorest income groups did not own or have access to refrigerators and therefore would not spend much on frozen vegetable products.[233]

For all vegetables (no sub-categories) it was illustrated that in relative terms the poorest income group spend proportionally more than richer income groups. In the case of frozen vegetables, the results were similar to all vegetables, i.e. the poorest income group spend proportionally more than richer income groups. Canned vegetables which are not included in the current zero-rating provision was found to be regressive, therefore Jansen argues it should have been included in the zero-rating list contained in Schedule 2. In the fresh vegetable category, results where again similar to the above two categories.[234]

However, when the fresh vegetables were split into further sub-categories, i.e. individual types of vegetables, there was a clear distinction between 'basic vegetables' and 'other or luxury vegetables'. The 'basic vegetables' included; spinach, cabbage, green mealies, tomatoes, green beans, pumpkin/ butternut, green/ red/ yellow peppers, chilies, mixed vegetables, onions, carrots, beetroot, potatoes, and sweet potatoes. The 'other vegetables' included; lettuce, cauliflower, broccoli, marrow, gem squashes, cucumber, mushrooms and other vegetables.[235]

The recommendation from Jansen is that investigations should be done on a regular basis as small changes in the tax treatment could impact the relative position of the poorer households.[236]

The Panel provided that a good should only be considered for zero-rating on the grounds of being a merit good if , "increased consumption would benefit, or at least not harm, economic and social development."[237] It introduced the economic principles of external costs and benefits where consumption of goods bears costs and has benefits to society that are not borne by the consumers. Government should consider goods on its merits of benefiting society as a whole rather than increasing the costs borne by society. The first example is the increased consumption of tobacco and sugar which has an additional health cost in that society ultimately bears the cost. This implies these goods should not be considered based on the increased health costs. However, the increased consumption of food, healthcare and education would benefit society by improving individuals' well-being and promoting increased productivity which reduces the reliance and demands on the government for service delivery of these goods.[238] The question the Panel attempted to assess was whether a zero-rating is the best incentive to increase consumption that benefits society as a whole. In reaching a conclusion the Panel noted that based on past experience the government does not have a great track record at implementing social spending programmes and therefore it would be preferable to include additional zero-rated items. The Panel

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233 Jansen, A. Stoltz, E. and Yu, D. (2013) *'The Targeting of Zero-Rated Basic Foodstuffs under Value-Added Tax (VAT) in South Africa',* Journal of Econometrics, 37(3), pp. 95.
234 Jansen, A. Stoltz, E. and Yu, D. (2013) pp 99.
235 Jansen, A. Stoltz, E. and Yu, D. (2013) pp 94.
236 Jansen, A. Stoltz, E. and Yu, D. (2013) pp 101.
237 Republic of South Africa. (2018) '*Recommendations to Minister of Finance by the Independent Panel of Experts for the Review of Zero-Rating in South Africa',* pp 20. Available at: http://www.treasury.gov.za/comm_media/press/2018/2018081001%20VAT%20Panel%20Final%20Report.pdf (Accessed: 21 September 2019).
238 Republic of South Africa. (2018) pp 20.

performed an in-depth analysis and their recommendations are the most appropriate in considering the current South African situation.

Chapter 4: International Comparison

4.1 Introduction

The purpose of this chapter is to consider the VAT treatment of basic items from a global context. Most countries generate their tax revenues from generally the same sources, i.e. income tax, tax on property, sales or consumption tax, but the tax system differs to some degree depending on each country's specific history, legal tradition, political structure and economic base.[239] Furthermore the tax structure differs globally depending on the level of national income, i.e. developed economies and developing economies. It has been observed that countries with low income collect roughly two thirds of their tax revenue from indirect taxes, whereas high income countries collect one third of their tax revenue from indirect taxes.[240]

According to the World Bank Study on South Africa and its fiscal policy used to combat poverty and inequality, South Africa receives relatively more tax revenue from PIT and less tax revenues from indirect taxes, such as VAT, compared to other countries. This comparison was based on calculations performed using the methodology developed by the Commitment to Equity (CEQ) Institute. The other CEQ countries include; Ethiopia, Bolivia, Guatemala, El Salvador, Armenia, Indonesia, Peru, Costa Rica, Brazil, Uruguay and Mexico.[241] Figure 14 below represents the results observed in this study.

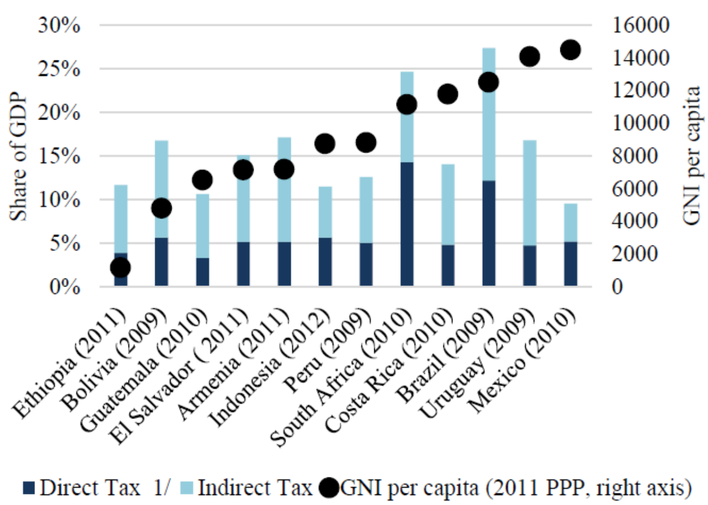

Figure 14. Distributional Impact amongst CEQ countries. Source: Inchauste, G. et al (2015) The Distributional Impact of Fiscal Policy in South Africa.[242]

[239] Bahl, R and Bird, R. (2008) *'Tax Policy in Developing Countries: Looking Back and Forward'.* National Tax Journal. 61, pp 283 -284.
[240] International Development Research Centre (IDRC) – Edited by Grown, C. & Valodia, I. (2010) *'Tax and Gender Equality: A Comparative Analysis of Direct and Indirect Taxes in Developing and Developed Countries',* pp 3. Available at: https://www.idrc.ca/en/book/taxation-and-gender-equity-comparative-analysis-direct-and-indirect-taxes-developing-and (Accessed: 18 January 2019).
[241] Inchauste, G. et al (2015) *'The Distributional Impact of Fiscal Policy in South Africa',* pp 7. Available at: http://worldbank.org/drm/documents (Accessed: 16 May 2018).
[242] Inchauste, G. et al (2015) pp 4.

4.2 Basket of merit goods and tax treatment in the African Countries

4.2.1 Introduction

In considering the appropriateness of South Africa's list of VAT free basic items an international comparison has been conducted to identify the trends amongst developing economies in Africa. In 2015, Cnossen performed a study on 'Mobilizing VAT revenues in Africa'[243] and established that the best practice for comparison purposes is to group African countries in their Regional Economic Community (REC).[244]

In Africa there are eight REC's which include;[245]

- Arab Maghreb Union (UMA);
- Common Market for Eastern and Southern Africa (COMESA);
- Community of Sahel–Saharan States (CEN–SAD);
- The East African Community (EAC);
- Economic Community of Central African States (ECCAS) / Communauté Economique et Monétaire de l'Afrique Central (CEMAC) ;
- Economic Community of West African States (ECOWAS);
- Intergovernmental Authority on Development (IGAD); and
- The Southern African Development Community (SADC).

Note: Annexure C includes details of the member states for each of the RECs.

Further the International Monetary Fund (IMF) released a list of the biggest African economies,[246] the list has been included in Figure 15.

[243] Cnossen, S. (2015) *'Mobilizing VAT revenues in African countries'.* International Tax and Public Finance, 22(6), 1077–1108. Available at: doi:10.1007/s10797-015-9348-1 (Accessed: 7 July 2018).
[244] According to the African Union, "The Regional Economic Communities (RECs) are regional groupings of African states. The RECs have developed individually and have differing roles and structures. Generally, the purpose of the RECs is to facilitate regional economic integration between members of the individual regions and through the wider African Economic Community (AEC), which was established under the Abuja Treaty (1991)." Extract from the African Union website. 'Regional Economic Communities (RECs)'. Available at: https://au.int/en/organs/recs (Accessed: 15 August 2019).
[245] African Union website. 'Regional Economic Communities (RECs)'. Available at: https://au.int/en/organs/recs (Accessed: 15 August 2019).
[246] Independent Online IOL. (2018) '*These are the biggest economies in Africa – IMF'*. Available at: https://www.iol.co.za/business-report/economy/these-are-the-biggest-economies-in-africa-imf-15929339 (Accessed: 8 July 2019).

	Country	GDP	REC
1	Nigeria	$376.3 billion	ECOWAS
2	South Africa	$349.3 billion	SADC
3	Egypt	$237.1 billion	COMESA
4	Algeria	$178.3 billion	UMA
5	Angola	$124.2 billion	SADC
6	Morocco	$109.8 billion	UMA
7	Ethiopia	$80.9 billion	IGAD
8	Kenya	$79.5 billion	EAC

Figure 15. The list of biggest economies in Africa. Source: IOL, IMF and Annexure C[247]

For the purposes of the international comparison for this study, we will consider the VAT free list of basic items for the SADC region as South Africa is a member of SADC as well as a few countries in Africa with the biggest economies from a few of the other REC's, namely Nigeria, Egypt and Kenya. Figure 16 is a list of countries included in the international comparison and references the current VAT rate in each country.

Countries	VAT introduced	VAT rate
Botswana	2002 [248]	12%
DRC	2012 [249]	16%
Egypt	2016 [250]	14%
Kenya	1990 [251]	16%
Lesotho	2003 [252]	15%
Madagascar	1994 [253]	20%
Malawi	2005 [254]	16.5%
Mauritius	1998 [255]	15%
Mozambique	1998 [256]	17%
Namibia	2000 [257]	15%
Nigeria	1993 [258]	5%

[247] Independent Online IOL. (2018) '*These are the biggest economies in Africa – IMF'*. Available at: https://www.iol.co.za/business-report/economy/these-are-the-biggest-economies-in-africa-imf-15929339 (Accessed: 8 July 2019).
[248] PwC. (2017) '*Helping you navigate Africa's VAT landscape',* pp 2. Available at: https://www.pwc.co.za/en/assets/pdf/vat-in-africa-2017.pdf (Accessed: 5 May 2019).
[249] IBFD. (2019) *'Congo (Dem. Rep.) – VAT & Sales Tax Table',* Quick Reference Tables IBFD. Available at: https://research-ibfd-org.ezproxy.uct.ac.za/#/doc?url=/document/vatst_cd (Accessed:4 May 2019).
[250] PwC. (2016) '*Egypt VAT Law'*. Available at: at https://www.pwc.com/m1/en/tax/documents/pwc-newsalert-egypt-vat-law-sept2016.pdf (Accessed: 25 August 2019).
[251] IBFD. (2019) '*Kenya - VAT & Sales Tax Table'*, Quick Reference Tables IBFD. Available at: https://research-ibfd-org.ezproxy.uct.ac.za/#/doc?url=/document/vatst_ke (Accessed: 9 May 2019).
[252] PwC. (2017) pp 64 and PwC (2018) '*Tax Alert Indirect Taxes – Lesotho VAT rate increase'*. Available at: https://www.pwc'.co.za/en/assets/pdf/vat-alert-lesotho-regulation.pdf (Accessed: 15 September 2019).
[253] IBFD. (2019) '*Madagascar – VAT & Sales Tax Table'*, Quick Reference Tables IBFD. Available at: https://research-ibfd-org.ezproxy.uct.ac.za/#/doc?url=/document/vatst_mg (Accessed: 4 May 2019).
[254] IBFD. (2019) '*Malawi – VAT & Sales Tax Table'*, Quick Reference Tables IBFD. Available at: https://research-ibfd-org.ezproxy.uct.ac.za/#/doc?url=/document/vatst_mw (Accessed: 4 May 2019).
[255] Republic of Mauritius. (2018) *'The Value-Added Tax Act'.* Available at: http://mra.mu/download/VATAct.pdf (Accessed: 4 May 2019).
[256] PwC. (2017) pp 83.
[257] PwC. (2017) pp 92.
[258] PwC. (2017) pp 98.

Seychelles	2013 [259]	15%
South Africa	1991 [260]	15%
Swaziland	2012 [261]	15%
Tanzania	1998 [262]	18%
Zambia	1995 [263]	16%
Zimbabwe	2004 [264]	15%

Figure 16. Table of the VAT rates and year of VAT's introduction for the countries included in the international comparison. Source: http://taxsummaries.pwc.com/ID/Value-added-tax-(VAT)-rates[265]

4.2.2 The Southern African Development Community

Firstly, we will consider the VAT treatment of basic and necessary items for the member states of SADC.[266] This REC can be grouped into two categories; the Southern African Customs Union (SACU) and the other SADC countries.

Southern African Customs Union (SACU)

In addition to South Africa, SACU includes the following countries; Botswana, Lesotho, Namibia and Swaziland.[267]

Botswana:

The Botswanan Government introduced VAT in 2002 with an effective date of 1 July 2002.[268] There are many similarities between the South African and Botswanan VAT Acts due to being members of the same Customs Union. However, the VAT rate in Botswana is only 12%[269] and did not increased in April 2018 such as its neighbouring Customs Union members. Figure 17 below includes the basic items that are zero-rated in the Botswanan VAT Act.

[259] IBFD. (2019) '*Seychelles – VAT & Sales Tax Table'*, Quick Reference Tables IBFD. Available at: https://research-ibfd-org.ezproxy.uct.ac.za/#/doc?url=/document/vatst_sc (Accessed: 4 May 2019).
[260] PwC. (2017) 'Helping you navigate Africa's VAT landscape', pp 115. Available at: https://www.pwc.co.za/en/assets/pdf/vat-in-africa-2017.pdf (Accessed: 5 May 2019).
[261] Swaziland Revenue Authority. Available at: http://www.sra.org.sz/vat/swaziland-vat.php (Accessed: 5 April 2018).
[262] PwC. (2017) pp 124.
[263] PwC. (2017) pp 143.
[264] PwC. (2017) pp 149.
[265] PwC website. '*Value-added tax (VAT) rates'*. Available at: http://taxsummaries.pwc.com/ID/Value-added-tax-(VAT)-rates (Accessed: 6 January 2020).
[266] The 15-member states; Angola, Botswana, Democratic Republic of Congo, Lesotho, Madagascar, Malawi, Mauritius, Mozambique, Namibia, Seychelles, South Africa, Swaziland, Tanzania, Zambia and Zimbabwe. Independent Online IOL. (2018) '*These are the biggest economies in Africa – IMF'*. Available at: https://www.iol.co.za/business-report/economy/these-are-the-biggest-economies-in-africa-imf-15929339 (Accessed: 8 July 2019).
[267] Southern African Customs Union website. Available at: https://www.sacu.int/ (Accessed: 7 January 2020).
[268] Botswana Unified Revenue Service (BURS). Available at: http://www.burs.org.bw/index.php/tax/value-added-tax (Accessed: 5 April 2018).
[269] See footnote 261.

Chapter 50:03 Value-Added Tax Act[270]

In terms of section 10 of the VAT Act, items included in the First Schedule are subject to VAT at the rate of zero.

Basic food items introduced as zero-rated in the First Schedule from commencement in 2002.	Additional food items introduced as zero-rated in the First Schedule in the amendments made in 2015[271].
"(q) a supply of **sorghum** or **maize meal** for human consumption"[272]	"(x) the supply of – (i) Brown bread;[273]
"(s) a supply of – leaded petrol, unleaded petrol, diesel oil and illuminating paraffin"[274]	(ii) Fresh vegetables;[275]
"(t) a supply of -	(iii) Fresh fruits;[276]
(i) Millet grain;	(iv) Rice;[277]
(iii) Millet meal;	(v) Samp;[278]
(vi) Wheat grain;	(vi) Milk;[279] and
(vii) Maize cobs;	(vii) Bread flour,"[280]
(viii) Flour;	
(ix) Sugar; and	
(x) Setswana beans.	
in their natural state and not mixed with other products, to the extent provided in the Regulations."	

Figure 17. Basic Food Items in Botswana. Source: Botswanan Unified Revenue Service - www.burs.org.bw[281]

[270] Republic of Botswana. (2002) *'Chapter 50:03 Value-Added Tax Act'*. Available at: http://www.burs.org.bw/index.php/tax/tax-downloads (Accessed: 5 April 2018).

[271] Republic of Botswana. (2015) *'Value-Added Tax Amendment Act No 1 of 2015'*. Available at: http://www.burs.org.bw/index.php/tax/tax-downloads?download=362:2015-vat-amendment-act (Accessed: 5 April 2018).

[272] "But does not include maize meal for human consumption when it is furnished or served as a meal, or as cooked or prepared food Maize meal." Extract from Chapter 50:03 Value-Added Tax Act.

[273] "As specified under the Customs Tariff Heading 1905.90.40." Extract from Value-Added Tax Amendment Act No 1 of 2015.

[274] "Which consist of fuel levy goods as defined in section 2 of the Customs and Excise Duty Act." Extract from Chapter 50:03 Value-Added Tax Act.

[275] "Vegetables as specified under Customs Tariff Headings 0701.90, 07.02, 07.03, 07.04, 07.05, 07.06, 07.07, 07.09 and 07.10, not cooked or treated in any manner except for the purpose of preserving such vegetables in their natural state, but excluding dehydrated, dried, canned or bottled vegetables." Extract from Value-Added Tax Amendment Act No 1 of 2015.

[276] "Fruit as specified under Customs tariff Headings 0803.10.10, 0803.90.10, 0804.10.10, 0804.20.10, 0804.30.10, 0804.40.10, 0804.50.10, 0805.10.10, 0805.20.10, 0805.40.10, 0805.50.10, 0805.90.10, 0806.10 and 0807 – 0810, not cooked or treated in any manner except for the purpose of preserving such fruits in its natural state, but excluding dehydrated, dried, canned or bottled fruit and nuts." Extract from Value-Added Tax Amendment Act No 1 of 2015.

[277] "As specified under the Customs Tariff Heading 1006, whether husked, milled, polished, glazed, parboiled, or broken." Extract from Value-Added Tax Amendment Act No 1 of 2015.

[278] "As specified under Customs Tariff Heading 1104.23.10, not further prepared or processed." Extract from Value-Added Tax Amendment Act No 1 of 2015.

[279] "As specified under the Customs Tariff Heading 0401, including high-fat, full-fat, low-fat or fat-free milk, being the milk of cattle, sheep or goats that has not been concentrated, condensed, evaporated, sweetened, flavoured, cultured or subjected to any other process other than homogenization or preservation by pasteurization ultra-high temperature treatment, sterilization, chilling or freezing or the addition of minerals, vitamins, enzymes, and other similar additives solely for the purpose of increasing the nutritional value." Extract from Value-Added Tax Amendment Act No 1 of 2015.

[280] "As specified under Customs Tariff Headings 1101.10 and 1109.90, whether white, brown or whole wheat." Extract from Value-Added Tax Amendment Act No 1 of 2015.

Lesotho:

In 2003 the Lesotho Finance Minister introduced VAT to replace GST with an effective date of July 2003.[282] Similarly, to South Africa, prior to 1 April 2018, the VAT rate was 14% and increased to 15%.[283] As supported by the Southern African Customs Union, there are a few basic food items that are zero-rated for VAT purposes, however, these are not a carbon copy of South Africa's list as included in Figure 18.

Value-Added Tax Act No 9 of 2001

In terms of Section 6A[284] of the VAT Act, items included in the Forth Schedule are subject to VAT at the rate of zero.

The items as listed in the IV Schedule:
"(b) Beans";
"(c) "Bread";
"(d) Lentils";
"(e) Livestock feed and poultry feed";
"(f) Maize (grain)";
"(g) Maize meal";
"(h) Milk";
"(i) Paraffin intended for use as fuel for cooking, illuminating or heating";
"(j) Peas";
"(k) Sorghum meal";
"(l) Unmalted sorghum grain";
"(m) Wheat (grain)"; and
"(n) Wheat flour."

Figure 18. Basic Food Items in Lesotho. Source: Lesotho Revenue Authority - www.lra.org.ls[285]

It is notable that Lesotho's list is shorter than that of South Africa, but it does not have definitions as restrictions and includes a wider range of item inclusions, such as all types of bread and wheat flour, whereas South Africa strictly includes brown bread and flour as defined in a Regulation.

[281] Republic of Botswana. (2002) and Republic of Botswana. (2015).
[282] Lesotho Revenue Authority (LRA). Available at: http://www.lra.org.ls/value-added-tax-vat (Accessed: 5 April 2018).
[283] PwC. (2018) *'Tax Alert Indirect Taxes – Lesotho VAT rate increase'.* Available at: https://www.pwc.co.za/en/assets/pdf/vat-alert-lesotho-regulation.pdf (Accessed: 15 September 2019).
[284] Kingdom of Lesotho. (2003) *'Amendments introduced in Value Added Tax (Amendment) Act No 6 of 2003'.* Available at: https://lesotholii.org/ls/legislation/act/2003/15/value_added_tax_amendment_act_no_6_of_2003_pdf_48730.pdf (Accessed: 5 April 2018).
[285] Kingdom of Lesotho. (2003).

Namibia:

Namibia was the first of South Africa's neighbouring countries to introduce VAT, which was implemented in 2000 with three VAT rates; 30% on certain luxury items, a standard rate of 15% and a zero-rate for certain basic commodities.[286] In the Amendment Act No 6 of 2002, the 30% luxury VAT rate was removed and the standard rate of 15% has been in place since 2000.[287]

However, the list of merit items which are zero-rated in terms of Section 9 of the Value-Added Tax Act No 10 of 2000[288] is notably different to that of South Africa as included in Figure 19.

Value Added Tax Act No 10 of 2000

In terms of Section 9 of the VAT Act, items included in the Third Schedule are subject to VAT at the rate of zero.

The items as listed in the III Schedule:
"(r) a supply of - (i) petrol, leaded; or (ii) petrol, unleaded; or (iii) distillate fuels (for example gas oil and diesel oil); or (iv) mixtures of illuminating or heating kerosene with lubricity agents, being goods subject to the fuel levy as defined in section 1 of the Customs and Excise Act";
"(s) a supply of **mahango, mahango meal** or **maize meal**, but does not include these items when furnishing or served as a meal, or as cooked or prepared food";
"(w) a supply of **electricity, water, refuse removal** and **sewerage** to a residential account";
"(aa) a supply of **livestock** (other than game)";
"(ee) a supply of **fresh and dried beans** (excluding canned and frozen beans), **sunflower cooking oil**, fried out or processed **animal fat** used for the preparation of food, **bread and cake flour** (sifted and unsifted) and **bread**, but does not include these items when furnished or served as a meal, or as cooked or prepared food"; and
"(ff) a supply of dry white or wet or dry brown granular **sugar**, and of **fresh milk**."

Figure 19. Basic zero-rated items in Namibia. Source: Namibian Parliament - https://laws.parliament.na[289]

Similarly, to Lesotho and Botswana, Namibia has included a zero-rated list, which is less comprehensive compared to South Africa's list of basic food items. However, there are additional items such as residential use of electricity and water, sugar, any type of bread and flour.

[286] Odhiambo, O. and Odada, J. (2015) *'Effects of zero rating value added tax on government revenue in Namibia',* African Journal of Economic and Management Studies, Vol. 6 No. 4, pp. 343-355. Available at: https://doi.org/10.1108/AJEMS-04-2013-0035 (Accessed: 22 September 2019) and Independent Online IOL (2000) *'SA Exporters get ready for Namibian VAT pinch'.* Available at: https://www.iol.co.za/news/south-africa/sa-exporters-get-ready-for-namibian-vat-pinch-50801 (Accessed: 22 September 2019).
[287] Odhiambo, O. and Odada, J. (2015), pp. 343-355.
[288] Republic of Namibia. (2010) '*Value-Added Tax Act 10 of 2000'*. Available at: https://laws.parliament.na/cms_documents/value-added-tax-dc6ffd6d86.pdf (Accessed: 5 April 2018).
[289] Republic of Namibia. (2010) '*Value-Added Tax Act 10 of 2000'.*

Swaziland:

Swaziland was the last member of SACU to introduce VAT in 2012 which replaced Sales Tax, with an effective date of 1 April 2012.[290] Similarly, Swaziland increased its VAT rate from 14% to 15% with an effective date of 1 August 2018.[291] Further Swaziland has included a list of zero-rated items, which is included in Figure 20.

Value-Added Tax Act of 2011[292]

In terms of Section 24 of the VAT Act, items included in the Second Schedule are subject to VAT at the rate of zero.

The items as listed in the II Schedule:
"(c) Maize meal";[293]
"(d) Maize";[294]
"(e) Beans";[295]
"(g) Paraffin";[296]
"(h) Dairy products";[297]
"(i) Brown bread";[298]
"(k) Samp";[299]
"(l) Fresh fruit and vegetables";[300]
"(m) Fresh eggs";[301]
"(n) Rice";[302]
"(o) Vegetable oil";[303]

[290] Swaziland Revenue Authority. Available at: http://www.sra.org.sz/vat/swaziland-vat.php (Accessed: 5 April 2018).
[291] KPMG (2018) *'Eswatini - Indirect Tax Guide'.* Available at: https://home.kpmg/xx/en/home/insights/2019/02/eswatini-formerly-swaziland-indirect-tax-guide.html (Accessed: 15 September 2019).
[292] Kingdom of Swaziland. (2011) *'Value-Added Tax Act of 2011'.* Available at: http://www.sra.org.sz/documents/1498486033.pdf (Accessed: 5 April 2018).
[293] "(Tariff Heading 1102.20), where it is graded as super maize meal, special maize meal, sifted maize meal or unsifted maize meal." Extract from Value-Added Tax Act of 2011.
[294] "(Tariff Heading 1005.00), where it is dried maize or dried seed of the plants zea mays indurate and zea mays inderata or any one or more crossings thereof of a mixture of the dried seed of such plants but excluding popcorn (zea mays everta) or green mealies for human consumption." Extract from Value-Added Tax Act of 2011.
[295] "(Tariff Heading 0713.00), provided that they are dried, whole split, or crushed, but not further prepared or processed, or where packaged as seed." Extract from Value-Added Tax Act of 2011.
[296] "(Tariff Heading 2710.11) intended for cooking, illuminating and heating is zero rated provided it is not mixed or blended with any other substance for any purpose other than cooking, illuminating or heating." Extract from Value-Added Tax Act of 2011.
[297] "The supply of dairy products, being milk of all kinds; fermented milk, emasi, buttermilk, fresh or UHT cream or sour cream; yoghurt, sip, buttermilk powder; condensed milk, powdered milk and milk substitutes (e.g. cremora etc); baby milk formulas, dessert, ice cream and other edible ice, mixtures and dairy blends; butter and margarine; whey cheese (cheddar, gouda or other) and curd; honey (natural or artificial) and animal products of animal origin not elsewhere specified or included in the Tariff Book." Extract from Value-Added Tax Act of 2011.
[298] "(Tariff Heading 1905.10). For purposes of interpretation only brown bread made from brown wheaten meal and water that has been fermented by yeast and which has been baked in the standard form shall be zero rated." Extract from Value-Added Tax Act of 2011.
[299] "(Tariff heading 1005.90) not further prepared or processed." Extract from Value-Added Tax Act of 2011.
[300] "(Tariff headings 0701.10 – 0709.90 & 0801.11 – 0810.90) Vegetables, not cooked or treated in any manner except for the purpose of preserving such vegetables in their natural state, but excluding dehydrated, dried, canned or bottled vegetables. Fruit. not cooked or treated in any manner except for the purposes of preserving such fruit in its natural stale. but excluding dehydrated, dried, canned or bottled fruit and nuts." Extract from Value-Added Tax Act of 2011.
[301] "(Tariff heading 0407.00) being raw eggs laid by hens of the species gallus domesticus, whether supplied in their shells or in the form of egg pulp being raw pulp consisting of the yolk and white which is obtained from such eggs after the shells have been removed." Extract from Value-Added Tax Act of 2011.
[302] "(Tariff heading 1006.20) whether husked, milled, polished, glazed, parboiled or broken." Extract from Value-Added Tax Act of 2011.

“(p) Medicines and drugs supplied”;[304]
“(q) The supply of school text books”; and
“The supply of petrol, diesel and liquid gas.”

Figure 20. Zero-rated goods and services in Swaziland. Source: Swaziland Revenue Authority - http://www.sra.org.sz[305]

In contrast to South Africa, Swaziland has a wide inclusion of diary products and has also included medicines and the supply of school books. Proposals in respect of the school books and medicines being included in the list of zero-rating has previously been made to the South Africa’s National Treasury, however, these proposals were rejected.[306]

Other SADC countries

Angola:

In 2018 the Angolan Government proclaimed that VAT will be introduced from 1 July 2019. Prior to VAT Angola had a Consumption Tax in place which taxes internally generated goods, imports and a wide range of services.[307]

Democratic Republic of Congo (DRC):

The DRC introduced VAT in 2012 by Law 10/001 of 20 August 2010 at a rate of 16%,[308] and unlike South Africa it has adopted implementing exemption for certain necessary items rather than zero-rating specific basic items. The exemptions are contained in Section 3 of Law 10/001.[309] Figure 21 below includes a list of basic items that have been classified as items exempt form VAT.

[303] “Except olive oil (tariff heading 1512.11 – 1512.21, marketed and supplied for use in the process of cooking food.” Extract from Value-Added Tax Act of 2011.
[304] “For use in a qualified medical facility; to the Government Medical Stores; or to an individual, subject to submission by that individual, of a prescription issued by a registered medical practitioner within sixty (60) days prior to the supply and in such quantities as prescribed by the registered medical practitioner.” Extract from Value-Added Tax Act of 2011.
[305] Kingdom of Swaziland. (2011) *‘Value-Added Tax Act of 2011’.* Available at: http://www.sra.org.sz/documents/1498486033.pdf (Accessed: 5 April 2018).
[306] Republic of South Africa. (2007) ‘*The VAT Treatment of Merit Goods and Services’* pp 7. Available at: http://www.treasury.gov.za/publications/other/VAT%20Merit%20goods%20Final%20Report%20%20-%2015%20Oct%202007.pdf (Accessed: 25 April 2018).
[307] EY. (2018) *‘Indirect Tax Alert. Angola to implement VAT in 2019’.* Available at: https://www.ey.com/gl/en/services/tax/international-tax/alert--angola-to-implement-vat-in-2019 (Accessed: 5 May 2019).
[308] Yay & Associates. (2012) ‘*Understanding how Value Added Tax (VAT) is applied in the Democratic Republic of Congo*. Available at: https://www.legavox.fr/blog/yav-associates/understanding-value-added-applied-democratic-7388.htm (Accessed: 7 January 2020).
[309] IBFD. (2019) ‘*Congo (Dem. Rep.) – VAT & Sales Tax Table’,* Quick Reference Tables IBFD. Available at: https://research-ibfd-org.ezproxy.uct.ac.za/#/doc?url=/document/vatst_cd (Accessed: 4 May 2019).

The Items in Section 3 of Law 10/001 of 20 August 2010:
"Importation and supply of blood and human organs by medical institutions and prostheses";
"Importation and acquisition of pharmaceutical products, pharmaceutical inputs and medical equipment and materials";
"Importation and sale of mosquito nets";
"Imports and domestic sales of wheat, maize, wheat flour and corn flour"; and
"Domestic sales of bread."

Figure 21. List of Exempt items in the DRC. Source: KPMG indirect tax guide - https://home.kpmg/[310]

Madagascar:

VAT has been adopted in Madagascar since 1994 at a rate of 20%, legislated in Finance Law 1994.[311] Similarly, to the DRC Madagascar has also adopted the policy to exempt basic items rather than the use of zero-rating. Figure 22 includes a list of specific basic items, contained in Article 6,[312] that are exempt from VAT in Madagascar.

Basic exempt items contained in Article 6 of the General Tax Code:
"Electricity and water for domestic use (up to 10 cubic metres for water and 100 kWh for electricity)";
"Sales and imports of medicines";
"Health services";
"Imports and sales of postage stamps, brochures (for educational purposes), paraffin, spectacles, inputs for agricultural use";
"Local sales and imports of instruments and appliances for hemodialysis";
"Imports and sales of ready-to-use therapeutic food"; and
"Sale of corn, import and sale of wheat and soya bean seeds."

Figure 22. List of exempt basic items in Madagascar. Source: IBFD (2019)[313]

Malawi:

In 2005 the Malawian parliament introduced the Value Added Tax Act 7 of 2005 at a rate of 17.5%,[314] which includes various exemptions in the First Schedule. Similarly, the use of an exemption as a tool of a tax concession is the preferred option for the Malawian Government. Figure 23 includes a number of notable exempt items.

[310] KPMG. (2019) '*Democratic Republic of the Congo (DR Congo or DRC) - Indirect Tax Guide*'. Available at: https://home.kpmg/xx/en/home/insights/2019/03/democratic-republic-of-the-congo-indirect-tax-guide.html (Accessed: 5 May 2019).
[311] PwC. (2017) *'Helping you navigate Africa's VAT landscape',* pp 70. Available at: https://www.pwc.co.za/en/assets/pdf/vat-in-africa-2017.pdf (Accessed: 4 May 2019) and Bird, R. M. and Gendron, P. (2007) 'The VAT in Developing and Transitional Countries', pp 225. Cambridge and New York: Cambridge University Press.
[312] IBFD. (2019) '*Madagascar – VAT & Sales Tax Table',* Quick Reference Tables IBFD. Available at: https://research-ibfd-org.ezproxy.uct.ac.za/#/doc?url=/document/vatst_mg (Accessed: 4 May 2019).
[313] IBFD. (2019).
[314] Malawi Legal Information Institute. (2005) *'Value Added Tax, 2005'.* Available at: https://malawilii.org/mw/legislation/act/2005/7 (Accessed: 1 December 2019) and Malawi College of Accountancy. (2010) *'A Study of the Malawi Taxation System'*. Available at: http://www.cfscmalawi.org/pdf/CFSC%20TAX%20RESEARCH%20REPORT.pdf (Accessed: 9 January 2020).

Basic exempt items in the First Schedule:[315]
"Certain animal products";[316]
"Animal or vegetable fats and oil and their cleavage products, prepared edible fats and animal or vegetable waxes";
"Vegetable products in a raw state";[317] and
"All medical equipment or medical services."

Figure 23. List of exempt basic items in Malawi. Source: IBFD (2019) and Malawi Legal Information Institute - https://malawilii.org/mw/legislation/act/2005/7[318]

Mauritius:

The island nation of Mauritius adopted a VAT regime in 1998 at a rate of 10%.[319] Mauritius like South Africa uses a combination of exemptions and zero-rating as tools for tax concessions. However, Mauritius has a more extensive list than South Africa and has chosen to exempt certain food items from VAT.

Value Added Tax Act[320]

Basic exempt supplies contained in First Schedule:	Basic zero-rated supplies contained in the Firth Schedule:
Item 2: "Wheat; cereal flours (excluding wheat flour)";	**Item 2(a):** "Rice, wheat flour and wheat bran";
Item 3: "Bread";	**Item 2(b):** "Edible oils"**;**
Item 4: "Animal or vegetable fats and oils";[321]	**Item 2(c):** "Margarine and butter";
Item 7: "Food of a kind used for human consumption - primary agricultural and horticultural produce";[322]	**Item 2(d):** "Milk and cream, buttermilk, whey, kephir and other fermented or acidified milk and cream; cheese and curd";
Item 8: "Food preparations for infant use";[323]	**Item 2(e):** "Sugar, sugar cane, molasses and bagasse";
Item 8A: "Breakfast cereals";	**Item 2(f):** "Live poultry, meat of poultry, edible offal of poultry and birds' eggs in the shell";[324]

[315] IBFD. (2019) *'Malawi – VAT & Sales Tax Table',* Quick Reference Tables IBFD. Available at: https://research-ibfd-org.ezproxy.uct.ac.za/#/doc?url=/document/vatst_mw (Accessed: 4 May 2019).
[316] "Including meat and fish, dairy produce (including fresh milk and infant's milk), birds' eggs and natural honey." Extract from Value Added Tax, 2005.
[317] "Including live trees and other plants, bulbs and roots, edible vegetables and certain roots and tubers, edible fruit and nuts, coffee and tea, cereals, products of the milling industry, including malt, starch, oil seeds and oleaginous fruit." Extract from Value Added Tax, 2005.
[318] Malawi Legal Information Institute. (2005) 'Value Added Tax, 2005'. Available at: https://malawilii.org/mw/legislation/act/2005/7 (Accessed: 1 December 2019) and IBFD. (2019).
[319] Bird, R. M. and Gendron, P. (2007) 'The VAT in Developing and Transitional Countries', pp 225. Cambridge and New York: Cambridge University Press.
[320] Republic of Mauritius. (2018) *'The Value-Added Tax Act'.* Available at: http://mra.mu/download/VATAct.pdf (Accessed: 4 May 2019).
[321] "Other than ghee produced in Mauritius and edible oils." Extract from (Mauritius) The Value-Added Tax Act.
[322] "(Including tomatoes, potatoes, onions and other vegetables, fruits, coffee, cocoa beans and nuts but excluding tea, honey and spices) which have not been processed except for reaping, threshing, husking, crushing, winnowing, trimming, drying and packaging to put them into marketable condition and bird's eggs in the shell." Extract from (Mauritius) The Value-Added Tax Act.
[323] "Put up for retail sale." Extract from (Mauritius) The Value-Added Tax Act.
[324] For the purposes of "items 2(f), (fa) and (o) of this Schedule, "fish", "meat of poultry" and "edible offal of poultry" -

Item 9: "Common salt other than common salt produced in Mauritius";	**Item 2(fa):** "Edible meat and edible meat offal, fresh, chilled or frozen";[325]
Item 10: "Live animals";[326]	**Item 2(fb):** "Soya bean cakes or chunks";
Item 11: "Unprocessed agricultural and horticultural produce";	**Item 2(fc):** "Meat-free vegetable burgers and vegetable sausages";
Item 12: "Medical, hospital and dental services";[327]	**Item 2(fd):** "Tea";
Item 53: "Blood glucose strip";[328]	**Item 2(fe):** "Honey";
Item 54: "Lancets";[329]	**Item 2(ff):** "Spices";
Item 55: "Equipment for medical, surgical and dental uses;"[330] and	**Item 2(n):** "Common salt produced in Mauritius";
Item 55A: "Equipment for medical, surgical and dental uses."[331]	**Item 2(o):** "Fish";[332]
	Item 2(p): "Ghee produced in Mauritius";
	Item 2(q): "Kerosene including kerosene jet type fuel";
	Item 7(a): "Electricity";[333]
	Item 7(b): "Water";[334]
	Item 26: "Antibiotics";[335]
	Item 27: "Pharmaceutical products";[336]
	Item 34: "Sanitary towels (pads) and tampons"; and
	Item 35: "Menstrual cups."

Figure 24. List of zero-rated and exempt items in Mauritius. Source: Mauritius Revenue Authority - http://mra.mu[337]

(a) include food preparations containing more than 20% by weight of fish, sausage, meat "(including meat of poultry) and an edible offal (including offal of poultry)", or any combination thereof; but
(b) exclude caviar and caviar substitutes of heading 16.04 and stuffed products of
Heading 19.02 or the preparations of heading No. 21.03 or 21.04." Extract from (Mauritius) The Value-Added Tax Act.

[325] Refer to definition above.

[326] "Of a kind generally used as, or yielding or producing, food for human consumption other than live poultry." Extract from (Mauritius) The Value-Added Tax Act.

[327] "Including clinical laboratory services, services provided in a health institution, veterinary services and a residential care home registered with the Ministry responsible for the subject of social security." Extract from (Mauritius) The Value-Added Tax Act.

[328] "Of H.S. Code 3822.00.10." Extract from (Mauritius) The Value-Added Tax Act.

[329] "Of heading 90.18 and glucometer of H.S. Code 9027.80.10." Extract from (Mauritius) The Value-Added Tax Act.

[330] "Of heading 90.18 and of H.S. Codes 3701.10.00", "3702.10.00", "8419.20.00, 9006.30.10, 9019.10.50, 9019.20.00, 9022.12.00, 9022.13.00, 9022.14.00, 9022.21.00, 9022.30.00, 9022.90.10, 9022.90.20, 9022.90.90, 9027.80.10, 9402.10.10, 9405.10.30 and 9405.40.30." Extract from (Mauritius) The Value-Added Tax Act.

[331] "Of heading 94.03 and of H.S. Codes 8414.60.00, 8414.80.00, 8419.89.00 and 9011.80.00 when imported for use in a health institution." Extract from (Mauritius) The Value-Added Tax Act.

[332] Refer to the definition above.

[333] "Supplied by the Central Electricity Board and the renting out of a meter, the reconnecting of electricity supply and the carrying out of infrastructure works, by the Board." Extract from (Mauritius) The Value-Added Tax Act.

[334] "Supplied by the Central Water Authority and the renting out of a meter and the carrying out of infrastructure works by the Authority." Extract from (Mauritius) The Value-Added Tax Act.

[335] "Of heading No. 29.41." Extract from (Mauritius) The Value-Added Tax Act.

[336] "Of heading Nos. 30.01 to 30.06." Extract from (Mauritius) The Value-Added Tax Act.

[337] Republic of Mauritius. (2018) *'The Value-Added Tax Act'.* Available at: http://mra.mu/download/VATAct.pdf (Accessed: 4 May 2019).

Mozambique:

VAT[338] was originally introduced in Mozambique in 1999, however in 2007, new VAT law was adopted at a rate of 17%,[339] and the 1998 law was repealed.[340] Mozambique has adopted a system of introducing exempt supplies with and without credit. Exempt with credit supplies has a similar effect as zero-rating. The exemptions are contained in Chapter 2, Section 1, and Article 9 of Law 32/2007 of 31 December 2007.[341]

Article 9: Basic exempt without credit supplies:	**Article 9: Basic exempt with credit supplies:**
Item 1 "(a): Medical and sanitary services";[342]	Item 10 includes: "Maize and maize flour";
Item 1 "(c): Human organs, blood and milk";	"Rice";
Item 1 "(l): Medicines";	"Bread";
Item "13: Alimentary oil and soaps"; and	"Iodised salt";
"Sugar."	"Powdered milk for infants up to one year";
	"Wheat and wheat flour";
	"Fresh or refrigerated tomatoes";
	"Potatoes";
	"Onions";
	"Frozen horse mackerel";
	"Lighting petrol";
	"Jet fuel";
	"Mosquito nets";
	"Common bicycles"; and
	"Condoms."
	Item 13 includes: "Farming goods and services for sugarcane production"; and
	"Goods to be used as raw material in alimentary oil and soap industry."

Figure 25. List of exemption items in Mozambique. Source: Autoridade Tributária de Moçambique - http://www.at.gov.mz[343]

[338] Mozambique legislation is in Portuguese, VAT is known as Imposto sobre o Valor Acrescentado (IVA).
[339] Bird, R. M. and Gendron, P. (2007) 'The VAT in Developing and Transitional Countries', pp 225. Cambridge and New York: Cambridge University Press.
[340] PwC. (2017) *'Helping you navigate Africa's VAT landscape',* pp 83. Available at: https://www.pwc.co.za/en/assets/pdf/vat-in-africa-2017.pdf (Accessed: 4 May 2019).
[341] Publicacao Oficial da Republica de Mocambique [Official Publication of the Republic of Mozambique] (2007) 'Lei *[Law] 32 of 2007 - Código do Imposto sobre o Valor Acrescentado [Value-Added Tax Code].* Available at: http://www.salcaldeira.com/index.php/pt/publicacoes/artigoss/cat_view/32-legislacao/68-tributacao/117-iva (Accessed: 5 May 2019) and Autoridade Tributária de Moçambique. Available at: http://www.at.gov.mz (Accessed: 5 May 2019).
[342] "And strictly connected operations, carried out by hospitals, clinics and dispensaries." Extract from Publicacao Oficial da Republica de Mocambique [Official Publication of the Republic of Mozambique] (2007) 'Lei *[Law] 32 of 2007 - Código do Imposto sobre o Valor Acrescentado [Value-Added Tax Code].*
[343] Publicacao Oficial da Republica de Mocambique [Official Publication of the Republic of Mozambique] (2007) 'Lei *[Law] 32 of 2007 - Código do Imposto sobre o Valor Acrescentado [Value-Added Tax Code].*

Seychelles:

The Seychelles implemented a VAT regime with an effective date of 1 January 2013 at a rate of 15%.[344] The exemptions are contained in the First Schedule of the Value Added Tax Act of 2010.[345] Figure 26 includes the list of relevant exempt items.

Part II of the First Schedule – Exempt supplies items
Item 1(e): "Supply of a government hospital, medical or dental services";[346] and
Item 1(i): "Fresh bread."[347]

Figure 26. List of exempt items (Part II) in the Seychelles. Source. Seychelles Revenue Commission - https://www.src.gov.sc[348]

In the 2018 set of VAT amendments of the schedules, the Seychelles Government introduced Part III to the First Schedule, which stated that imported or locally produced goods i.e. the goods imported or produced in the Seychelles which all have the following HBS codes will be exempt from VAT.[349] Figure 27 includes the list of exempt items in the Seychelles.

Part III of the First Schedule – Imported or locally produced items	
1.	"Meat of bovine animals";[350]
2.	"Meat of sheep or goats";[351]
3.	"Meat and edible offal of poultry";[352]
4.	"Fish";[353]
5.	"Milk and cream";
6.	"Cheese and curd";
7.	"Birds egg";
8.	"Potatoes";[354]
9.	"Tomatoes": [355]
10.	"Onions, shallots, garlic, leeks and other alliaceous vegetables";[356]
11.	"Cabbages, cauliflowers, kohlrabi, kale, and similar edible brassicas"; [357]
12.	"Lettuce and chicory";[358]

[344] IBFD. (2019) '*Seychelles – VAT & Sales Tax Table',* Quick Reference Tables IBFD. Available at: https://research-ibfd-org.ezproxy.uct.ac.za/#/doc?url=/document/vatst_sc (Accessed: 4 May 2019).
[345] Republic of Seychelles. (2010) '*Value Added Tax, 2010*'. Available at: https://www.src.gov.sc/pages/resources/VATAct.aspx (Accessed: 5 May 2019).
[346] Republic of Seychelles. (2012) *'Value Added Tax (Amendment' of Schedules) Regulations, 2012, Statutory Instrument 65 of 2012'*. Available at: https://www.src.gov.sc/resources/SI/2018/SI33of2018.pdf (Accessed: 5 May 2019).
[347] Republic of Seychelles. (2012).
[348] Republic of Seychelles. (2012).
[349] Republic of Seychelles. (2018) *'Value Added Tax (Amendment' of Schedules) Regulations, 2018, Statutory Instrument 33 of 2018'*. Available at: https://www.src.gov.sc/resources/SI/2018/SI33of2018.pdf (Accessed: 4 May 2019).
[350] "Fresh, chilled or frozen." Extract from Statutory Instrument 33 of 2018.
[351] "Fresh, chilled or frozen." Extract from Statutory Instrument 33 of 2018.
[352] "Fresh, chilled or frozen." Extract from Statutory Instrument 33 of 2018.
[353] "Fresh, chilled or frozen and specific types of fish listed." Extract from Statutory Instrument 33 of 2018.
[354] "Fresh or chilled." Extract from Statutory Instrument 33 of 2018.
[355] "Fresh or chilled." Extract from Statutory Instrument 33 of 2018.
[356] "Fresh or chilled." Extract from Statutory Instrument 33 of 2018.
[357] "Fresh or chilled." Extract from Statutory Instrument 33 of 2018.

13.	"Carrots, turnips, salad beetroot, salsify, celeriac, radishes, and similar edible roots";[359]
14.	"Cucumbers and gherkins, fresh or chilled"; [360]
15.	"Leguminous vegetables, fresh or chilled"; [361]
16.	"Other vegetables";[362]
17.	"Dried leguminous vegetables"; [363]
18.	"Manioc, arrowroot, salep, Jerusalem artichokes, sweet potatoes and similar roots and tubers";[364]
19.	"Bananas, including plantains";[365]
20.	"Dates, figs, pineapples, avocados, guavas, mangoes and mangosteens";[366]
21.	"Citrus fruit";[367]
22.	"Grapes";[368]
23.	"Melons (including watermelons) and papaws (papayas)";[369]
24.	"Apples, pears and quinces";[370]
25.	"Apricots, cherries, peaches (including nectarines), plums and sloes";[371]
26.	"Other fruits";[372]
27.	"Coffee";
28.	"Tea";
29.	"Mate";
30.	"Rice";
31.	"Wheat and meslin flour";
32.	"Cereal groats, meal and pellets";
33.	"Cereal grains";[373]
34.	"Soya-bean oil and its fractions";[374]
35.	"Olive-oil and its fractions"; [375]
36.	"Sunflower-seed, safflower or cotton-seed oil and the fractions thereof";[376]

[358] "Fresh or chilled." Extract from Statutory Instrument 33 of 2018.
[359] "Fresh or chilled." Extract from Statutory Instrument 33 of 2018.
[360] "Fresh or chilled." Extract from Statutory Instrument 33 of 2018.
[361] "Shelled or unshelled, fresh or chilled." Extract from Statutory Instrument 33 of 2018.
[362] "Fresh or chilled." Extract from Statutory Instrument 33 of 2018.
[363] "Shelled, whether skinned or split." Extract from Statutory Instrument 33 of 2018.
[364] "With high starch and insulin content, fresh, chilled, frozen or dried, whether or not sliced or in the form of pellets; sago pits." Extract from Statutory Instrument 33 of 2018.
[365] "Fresh or dried." Extract from Statutory Instrument 33 of 2018.
[366] "Fresh or chilled." Extract from Statutory Instrument 33 of 2018.
[367] "Fresh or dried." Extract from Statutory Instrument 33 of 2018.
[368] "Fresh or dried." Extract from Statutory Instrument 33 of 2018.
[369] "Fresh." Extract from Statutory Instrument 33 of 2018.
[370] "Fresh." Extract from Statutory Instrument 33 of 2018.
[371] "Fresh." Extract from Statutory Instrument 33 of 2018.
[372] "Fresh." Extract from Statutory Instrument 33 of 2018.
[373] "Otherwise worked (for example, hulled, rolled, flaked, pearled, sliced or kibbled, except rice of heading 10.06, germ of cereals, whole, rolled, flaked or grounded." Extract from Value Added Tax (Amendment' of Schedules) Regulations, 2018, Statutory Instrument 33 of 2018.
[374] "Whether or not refined or but not chemically modified." Extract from Statutory Instrument 33 of 2018.
[375] "Whether or not refined or but not chemically modified." Extract from Statutory Instrument 33 of 2018.

37.	“Coconut (copra), palm kernel or babassu oil and the fractions thereof”;[377]
38.	“Rape, colza or mustard oil and the fractions thereof”;[378]
39.	“Other fixed vegetable fats and oil (including jojoba oil) and the fractions thereof”;[379]
40.	“Margarine, edible mixtures or preparations of animal or vegetables fats or oils”; [380]
41.	“Other prepared or preserved meat, or meat offal or blood”;
42.	“Malt extract, food preparations of flour, groats, meal, starch or malt extract”;[381]
43.	“Prepared foods obtained by swelling or roasting of cereals or cereal products”;[382]
44.	“Other vegetables prepared or preserved”;[383]
45.	“Extracts, essences and concentrates, of coffee, tea or mate”;[384]
46.	“Sauces and preparations thereof, mixed condiments and mixed seasonings, mustard flour and meal and prepared mustard”;
47.	“Soups and broths and preparations thereof, homogenised composite food preparations”;
48.	“Food preparations not elsewhere specified or included”;
49.	“Vegetable materials and vegetable waste, vegetable residues and by-products”;[385]
50.	“Salt (including table salt and denatured salt) and pure sodium chloride”;[386]
51.	“Petroleum oils and oils obtained from bituminous minerals”;[387] and
52.	“Ketones and quinones.”[388]

Figure 27. List of exempt items (Part III) in the Seychelles. Source. Seychelles Revenue Commission - https://www.src.gov.sc[389]

Tanzania:

VAT in Tanzania was originally introduced in 1998 at a rate of 20%,[390] however a new VAT Act (Value-Added Tax Act No 10 of 2014) was adopted in 2014, with an effective date 1 July 2015.[391] Unlike South Africa, the Tanzanian Government has decided to exempt basic food items from VAT rather than using the zero-rating

[376] “Whether or not refined or but not chemically modified.” Extract from Statutory Instrument 33 of 2018.
[377] “Whether or not refined or but not chemically modified.” Extract from Statutory Instrument 33 of 2018.
[378] “Whether or not refined or but not chemically modified.” Extract from Statutory Instrument 33 of 2018.
[379] “Whether or not refined or but not chemically modified.” Extract from Statutory Instrument 33 of 2018.
[380] “Or of fractions of different fats or oils of this Chapter; other than edible fats or oils or their factions under heading 15.16.” Extract from, Statutory Instrument 33 of 2018.
[381] “Not containing cocoa or containing less than 40% by weight of cocoa calculated on a totally defatted basis, not elsewhere specified or included; food preparations of goods headings 04.01 to 04.04, not containing cocoa less than 5% weight of cocoa calculated on a totally defatted basis, not elsewhere specified or included.” Extract from Statutory Instrument 33 of 2018.
[382] “(For example, corn flakes), cereals (other than maize (corn) in grain form or in the form of flakes or other worked grains (except flour, groats and meal), pre-cooked, or otherwise prepared, not elsewhere specified or included.” Extract from Statutory Instrument 33 of 2018.
[383] “Otherwise than vinegar or acetic acid, not frozen, other than products of heading 20.06.” Extract from Instrument 33 of 2018.
[384] “Preparations with a basis of these products or with a basis of coffee, tea or mate; roasted chicory and other roasted coffee substitutes, and extracts, essences, and concentrations thereof.” Extract from Statutory Instrument 33 of 2018.
[385] “Whether or not in the form of pellets, of a kind used in animal feeding, not elsewhere specified or included; Preparations of a kind used in animal feeding.” Extract from Statutory Instrument 33 of 2018.
[386] “Whether or not aqueous solution or containing added anti-caking or free-flowing agents, sea water.” Extract from Statutory Instrument 33 of 2018.
[387] “Other than crude, preparations not elsewhere specified or included, containing by weight 70% or more of petroleum oil or of oils from bituminous minerals, these oils being the basic constituents of the preparations, waste oils.” Extract from Statutory Instrument 33 of 2018.
[388] “Whether or not with oxygen function, and their halogenated, sulphonated, nitrated or nitrosated derivatives.” Extract from *Value Added Tax (Amendment' of Schedules) Regulations, 2018, Statutory Instrument 33 of 2018.*
[389] Republic of Seychelles. (2018) *‘Value Added Tax (Amendment' of Schedules) Regulations, 2018, Statutory Instrument 33 of 2018’.* Available at: https://www.src.gov.sc/resources/SI/2018/SI33of2018.pdf (Accessed: 4 May 2019).
[390] Bird, R. M. and Gendron, P. (2007) ‘The VAT in Developing and Transitional Countries’, pp 226. Cambridge and New York: Cambridge University Press.

instrument. However, as with other African countries items which are deemed necessary for its citizens' basic needs have been included as an exemption. The common exemptions are namely; water, medical services and certain medicines. These VAT exemptions are contained in Part I of the Schedule, which has been included in Figure 28 and Figure 29.

Schedule (made under Section 6(1)) Part 1[392] – Supplies and imports exempt from VAT	
3	"Livestock, basic agricultural products and foods for human consumption";
7	"Medicine or pharmaceuticals products, not including food supplements or vitamins; including Sanitary Pads";[393]
8	"Articles designed for people with special needs";
10	"Health care";
15	"Petroleum products"; and
16	"Supply of water, except bottled or canned water or similarly presented water."

Figure 28. List of exempt items in Tanzania. Source: Tanzania Revenue Authority - https://www.tra.go.tz[394]

Further details of the basic food items are included below:

Item 3 - Livestock, basic agricultural products and foods for human consumption	
No	Food item
1	"Live cattle";
2	"Live swine";
3	"Live sheep";
4	"Live goats";
5	"Live poultry";
6	"Unprocessed edible animal products";
7	"Unprocessed edible eggs";
8	"Unpasteurised or pasteurised cow milk except with additives and long life milk";
9	"Unpasteurised or pasteurised goat milk except with additives and long life milk";
10	"Unprocessed fish";
11	"Unprocessed edible vegetables";
12	"Unprocessed fruits";
13	"Unprocessed nuts";
14	"Unprocessed bulbs";

[391] PwC. (2017) *'Helping you navigate Africa's VAT landscape'*, pp 124. Available at: https://www.pwc.co.za/en/assets/pdf/vat-in-africa-2017.pdf (Accessed: 4 May 2019).
[392] The United Republic of Tanzania. (2014) *'The Value-Added Tax No 10 of 2014'*. Available at: https://www.tra.go.tz/tax%20laws/THE%20VALUE%20ADDED%20TAX%20ACT,%202014.pdf (Accessed: 8 May 2019).
[393] The United Republic of Tanzania (2018) '*Finance Act No 4 of 2018'*. Available at: https://www.tra.go.tz/images/uploads/FINANCEACT2018.pdf (Accessed: 8 May 2019).
[394] The United Republic of Tanzania. (2014) *'The Value-Added Tax No 10 of 2014'*. Available at: https://www.tra.go.tz/tax%20laws/THE%20VALUE%20ADDED%20TAX%20ACT,%202014.pdf (Accessed: 8 May 2019).

15	“Unprocessed tubers”;
16	“Unprocessed cereals”;
17	“Wheat or meslin flour”;
18	“Maize flour”;
19	“Tobacco, not stemmed/stripped”;
20	“Unprocessed cashew nuts”;
21	“Unprocessed coffee”;
22	“Unprocessed tea”;
23	“Soya beans”;
24	“Ground nuts”;
25	“Sunflower seeds”;
26	“Oil seeds”;
27	“Unprocessed pyrethrum”;
28	“Unprocessed cotton”;
39	“Unprocessed sisal”;
30	“Unprocessed sugarcane”;
31	“Seeds and plants thereof”;
32	“Preparations of a kind used in animal feeding”;
33	“Fertilized eggs for incubation”;
34	“Oil-cake of soya beans”;
35	“Oil-cake and other solid residues of cotton seeds”;
36	“Oil-cake and other solid residues of sunflower seeds”;
37	“Maize bran”;
38	“Wheat bran”;
39	“Lysine”;
41	“Mycotoxin binders”;
42	“Pollard”;
43	“Rice bran”; and
44	“Cotton cake.”

Figure 29. List of exempt food items in Tanzania. Source: Tanzania Revenue Authority - Source: https://www.tra.go.tz[395]

[395] The United Republic of Tanzania. (2014) '*The Value-Added Tax No 10 of 2014*'. Available at: https://www.tra.go.tz/tax%20laws/THE%20VALUE%20ADDED%20TAX%20ACT,%202014.pdf (Accessed: 8 May 2019); The United Republic of Tanzania. (2016) '*Finance Act No 2 of 2016*'. Available at: https://www.tra.go.tz/images/uploads/statistics/Finance-Act-2016--2.pdf (Accessed: 23 August 2019); The United Republic of Tanzania. (2017) '*Finance Act No 4 of 2017*'. Available at: https://www.tra.go.tz/Images/headers/THE-FINANCE-ACT-2017-CHAPA-Final.pdf (Accessed: 23 August 2019); and The United Republic of Tanzania. (2018) '*Finance Act No 4 of 2018*'. Available at: https://www.tra.go.tz/images/uploads/FINANCEACT2018.pdf (Accessed: 23 August 2019).

Zambia

Zambia introduced a VAT regime with an effective date of 1 July 1995 at the rate of 20%[396] in terms of its VAT Act, which is Chapter 331 of the Laws of Zambia.[397] In terms of its VAT Act[398] the following goods and services of a basic nature is included in Figure 30.

Basic exempt supplies:	**Basic zero-rated supplies:**[399]
"Health services";	"Fresh vegetables";
"Water";	"Medical supplies and drugs";
"Sewerage";	"Bread";
"Paraffin"; and	"Wheat";
"Books and newspapers."	"Fruit";
	"Nuts";
	"Maize";
	"Mealie meal";
	"Sorghum";
	"Soya beans";
	"Millet";
	"Flour (except wheat flour)";
	"Meat (beef, sheep, goats, swine)";
	"Poultry";
	"Eggs";
	"Milk";
	"Fish";
	"Cereals"; and
	"Infant cereals."

Figure 30. List of zero-rated and exempt items in Zambia. Source: Zambian VAT Act - http://www.parliament.gov.zm[400]

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[396] Bird, R. M. and Gendron, P. (2007) '*The VAT in Developing and Transitional Countries*', pp 226. Cambridge and New York: Cambridge University Press.

[397] PwC. (2017) *'Helping you navigate Africa's VAT landscape'*, pp 143. Available at: https://www.pwc.co.za/en/assets/pdf/vat-in-africa-2017.pdf (Accessed: 4 May 2019).

[398] Republic of Zambia. (1995) *'The Value-Added Tax Act: Chapter 331 of the Laws of Zambia'.* Available at: http://www.parliament.gov.zm/sites/default/files/documents/acts/Value%20Added%20Tax%20Act.pdf (Accessed: 5 May 2019).

[399] EY. (2019) *'Worldwide VAT, GST and Sales Tax Guide'.* Available at: https://www.ey.com/Publication/vwLUAssets/ey-2019-Worldwide-VAT-GST-and-Sales-Tax-Guide/$FILE/ey-2019-Worldwide-VAT-GST-and-Sales-Tax-Guide.PDF (Accessed: 7 May 2019).

[400] Republic of Zambia. (1995) *'The Value-Added Tax Act: Chapter 331 of the Laws of Zambia'.* Available at: http://www.parliament.gov.zm/sites/default/files/documents/acts/Value%20Added%20Tax%20Act.pdf (Accessed: 5 May 2019).

Zimbabwe

VAT was introduced in Zimbabwe with effect from 1 January 2004 at a rate of 15% to replace the previous sales tax regime.[401] The VAT legislation is known as the Value Added Tax Act (Chapter 23:12).[402] The zero-rated basic food items are contained in the Second Schedule and the list of VAT exemptions are contained in the First Schedule of the VAT Regulations published in Statutory Instrument No 273 of 2003.[403]

In 2017 the Zimbabwean Government was of the opinion that the list of zero-rated and exempt food items was too large and in Statutory Instrument No 20 of 2017 (SI 20)[404] the following food items were deleted from the Schedules; potatoes, rice, margarine and mahewu from the First Schedule (exemptions) and raw meats and fish from the Second Schedule (zero-ratings). Public outcry was experienced,[405] and the government responded by repealing SI 20 and in terms of Statutory Instrument 65A of 2017 (SI 65A) incorporated raw meats and fish items in the First Schedule i.e. exempt from VAT.[406] Therefore, reducing the list of basic food items that are zero-rated and increased the list of VAT exemptions. This illustrated that once a zero-rating concession has been made it is very difficult for a government to reverse such concession in the future.

Figure 31 includes the list of exempt and zero-rated basic items:

First Schedule - Basic exempt supplies:	**Second Schedule - Basic zero-rated supplies:**
“Medical services”;	“Bread”;
“Water for domestic use”;	“Milk”;
“Fuel”;	“Mealie meal”;
“Rice”;	“Sugar”;
“Margarine”;	“Prescription medicines”;
“Cereals”;	“Salt”;
“Mahewu”;	“Supply of electricity”; and
“Pork”;	“Livestock.”
“Beef”;	
“Fish”;	

[401] PwC. (2017) ‘*Helping you navigate Africa’s VAT landscape’,* pp 149. Available at: https://www.pwc.co.za/en/assets/pdf/vat-in-africa-2017.pdf (Accessed: 4 May 2019) and Bird, R. M. and Gendron, P. (2007) ‘The VAT in Developing and Transitional Countries’, pp 226. Cambridge and New York: Cambridge University Press.
[402] IBFD. (2019) ‘*Zimbabwe - VAT & Sales Tax Table'*, Quick Reference Tables IBFD. Available at: https://research-ibfd-org.ezproxy.uct.ac.za/#/doc?url=/document/vatst_zw (Accessed: 7 May 2019).
[403] Republic of Zimbabwe. (2002) *'Chapter 23:12: Value Added Tax Act'*. Available at: https://www.zimra.co.zw/downloads/category/17-acts?start=20 (Accessed: 5 May 2019).
[404] Republic of Zimbabwe. (2017) *'Statutory Instrument 20 of 2017 - Value-Added Tax (General) (Amendment) Regulations No 42 of 2017'.* Available at: https://www.zimra.co.zw/downloads/category/25-2017 (Accessed: 5 May 2019).
[405] Zimbabwe Independent. (13 February 2017) *‘VAT: Consumer power prevails’.* Available at: https://www.theindependent.co.zw/2017/02/13/vat-consumer-power-prevails/ (Accessed: 29 September 2019).
[406] Republic of Zimbabwe. (2017) *‘Statutory Instrument 26A of 2017 - Value-Added Tax (General) (Amendment) Regulations No 43 of 2017'.* Available at: https://www.zimra.co.zw/downloads/category/25-2017 (Accessed: 5 May 2019).

"Chicken";	
"Potatoes";	
"Eggs";	
"Vegetables";	
"Fruit";	
"Protective clothing (i.e. gloves, raincoats and gumboots)"[407]; and	
"Mineral water."	

Figure 31. List of zero-rated and exempt items in Zimbabwe. Source: IBFD, PwC, EY and Zimbabwe VAT Regulations - https://www.zimra.co.zw[408]

4.2.3 Top African Economies

Nigeria (ECOWAS):

The Nigerian Government announced VAT to replace Sales Tax in 1993, with an effective date of 1 January 1994 at a rate of 5%.[409] In Value-Added Tax Act No 102 of 1993, Section 3 states that certain goods and services as specified in the First Schedule will be exempt from VAT.[410] Basic food items are included in the list of exempt items, which is the opposite of the decision taken by South Africa on its adoption of VAT a few years previously.

The list of exempt goods and services included in the First Scheduled is detailed in the Tax Information Circular No 9701: Detailed list of items from Value-Added Tax,[411] and the relevant items for the purposes of this study is included in Figure 32.

First Schedule – Part I

Item 1: *All medical and pharmaceutical products*

Item 2: *Basic food items*

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407 Zimbabwe Revenue Authority. (2016) *'Statutory Instrument 9 of 2016 - Value-Added Tax (General) (Amendment) Regulations No 40 of 2016'.* Available at: https://www.facebook.com/ZIMRA.11/posts/did-you-knowvat-zero-rated-goods-zero-rated-supplies-are-supplies-of-goods-and-s/1051117251613555/ (Accessed: 5 May 2019).
408 Republic of Zimbabwe. (2017) *'Statutory Instrument 20 of 2017 - Value-Added Tax (General) (Amendment) Regulations No 42 of 2017'.* Available at: https://www.zimra.co.zw/downloads/category/25-2017 (Accessed: 5 May 2019) and Republic of Zimbabwe. (2017) *'Statutory Instrument 26A of 2017 - Value-Added Tax (General) (Amendment) Regulations No 43 of 2017'.* Available at: https://www.zimra.co.zw/downloads/category/25-2017 (Accessed: 5 May 2019) and IBFD. (2019) '*Zimbabwe - VAT & Sales Tax Table*', Quick Reference Tables IBFD. Available at: https://research-ibfd-org.ezproxy.uct.ac.za/#/doc?url=/document/vatst_zw (Accessed: 7 May 2019).
409 PwC. (2017) *'Helping you navigate Africa's VAT landscape',* pp 98. Available at: https://www.pwc.co.za/en/assets/pdf/vat-in-africa-2017.pdf (Accessed: 4 May 2019) and Bird, R. M. and Gendron, P. (2007) 'The VAT in Developing and Transitional Countries', pp 225. Cambridge and New York: Cambridge University Press.
410 Federal Republic of Nigeria. (1993) *'Value-Added Tax Act No 102 of 1993'.* Available at: https://www.firs.gov.ng/sites/Authoring/contentLibrary/035860b3-9ecf-400f-8d03-4335e4be5d19Value%20Added%20Tax%20(VAT).pdf (Accessed: 5 April 2018).
411 Federal Republic of Nigeria. (1997) *'Federal Inland Revenue Service: Information Circular No 9701 – Detailed list of items exempted from Value Added Tax'.* Available at: https://www.firs.gov.ng/sites/Authoring/contentLibrary/cee0422b-7305-48d6-f76c-81dcbf3776ec11.DETAILED%20LIST%20OF%20ITEMS%20EXEMPTED%20FROM%20VALUE%20ADDED%20TAX%20-9701.pdf (Accessed: 5 April 2018).

BASIC FOOD ITEMS *(For the purpose of VAT, basic food is defined as any unprocessed staple food item, whether or not it is packaged).*	
02.04	"Meat of sheep or goats, fresh, chilled or frozen."
02.07	"Meat and edible offal, of the poultry of heading No. 01.05, fresh, chilled or frozen."
03.02	"Fish - Fish, fresh or chilled, excluding fish fillets and other fish meat of heading No. 03.04."
03.03	"Fish, frozen, excluding fish fill fillets and other fish meat and heading No. 03.04."
03.05	"Fish, dried, salted, or in brine smoke fish, whether or not cooked before or during the smoking process; fish meal fit human consumption."
07.13	"Dried leguminous vegetables, shelled, whether or not skinned or split."
07.14	"Manioc, arrowroot, salep, Jerusalem artichokes, sweet potatoes and similar roots an tubers."
10.06	"Rice"
11.04	"Cereal grains otherwise work except rice of heading No.10.06."

INFANT FOOD	
19.01	"Malt extract, food preparations of flour, meal, starch or malt extract"[412]

Item 4: *Baby products*

BABY PRODUCTS	
39.23	"Feeding bottles and related products for babies use."
48.18	"Sanitary towels and tampons napkins and napkin liners for babies and sanitary articles."
61.11	"Babies garments and clothing accessories knitted or crotched."
62.09	"Babies garments and clothing accessories."
87.15	"Baby carriages and parts."

Figure 32. List of exempt items in Nigeria. Source: Tax Circular No 1907 - https://www.firs.gov.ng[413]

First Schedule – Part II

Item 1: *Medical and health care services*

In addition to item 1 the following have been deemed to fall within the exemption in accordance with Tax Circular No 9701, which include edible or table salt and water.

[412] "Not containing Cocoa powder or containing Cocoa powder or containing cocoa powdered in proportion by weight less than 50% not elsewhere specified or included; Food preparation of goods of heading Nos. 04.01 to 04.04, not containing Cocoa powder in a proportion by weight of less than 10% not elsewhere specified or included." Extract from Federal Inland Revenue Service: Information Circular No 9701 – Detailed list of items exempted from Value Added Tax.

[413] Federal Republic of Nigeria. (1997) *'Federal Inland Revenue Service: Information Circular No 9701 – Detailed list of items exempted from Value Added Tax'.* Available at: https://www.firs.gov.ng/sites/Authoring/contentLibrary/cee0422b-7305-48d6-f76c-81dcbf3776ec11.DETAILED%20LIST%20OF%20ITEMS%20EXEMPTED%20FROM%20VALUE%20ADDED%20TAX%20-9701.pdf (Accessed: 5 April 2018).

Egypt (COMESA):

Prior to 2016 Egypt had GST and on the 31 August 2016 the Egypt Parliament approved the introduction of VAT with an effective date of 8 September 2016 at a rate of 13%.[414] Similarly to Nigeria, the Egyptian Government decided to use an exemption instrument rather than a zero-rating instrument to provide relief to the poor.

Value-Added Tax Law No. 67 of 2016

There is a list of 57 goods that are exempt from VAT,[415] and the relevant items for the purposes of this study, which is included in Figure 33.

Exempt goods and services:	
1	"Baby milk and dairy products";
2	"Baby formula";
3	"Egg";
4	"Tea, sugar and coffee";
5	"Grain mills products, except super flour and imported self-rising flour";
6	"Bread";
7	"Pasta, except pasta with semolina";
8	"Frozen or fresh poultry and livestock";
9	"Meat processed products";
10	"Frozen or fresh fish and seafood";
11	"Processed and smoked renga fish, except caviar and other smoked fish";
12	"Agricultural products in its raw nature, except tobacco seedlings";
13	"Honey, molasses, halva, tahini (sesame paste)";
14	"Locally manufactured fruits and vegetables except potatoes and juices and its concentrates";
15	"Legumes, grains, salt and manufactured spices";
16	"Foods manufactured or sold to the end consumer from restaurants or non-tourist shops which fulfilling the requirements to be determined by a decision from the Minister";
17	"Water purifying, desalting, or distribution except the packed water";
18	"Crude oil";
19	"Natural gas and butane gas";
22	"Electricity production, transmission, selling or distribution";

414 PwC. (2016) *'Egypt VAT Law'.* Available at: https://www.pwc.com/m1/en/tax/documents/pwc-newsalert-egypt-vat-law-sept2016.pdf (Accessed: 25 August 2019).

415 Salah, F. Riad, E. Elkady, H. & Mohsen, A. (23 October 2016) *'A Guide to Egypt's VAT Law'.* Available at: http://www.riad-riad.com/en/publications/guide-egypts-vat-law (Accessed: 25 August 2019).

23	"Residues and wastes of food industries and wastes of papers";
24	"Foods prepared for animals, birds and fishes (forage) except those used for feeding cats, dogs and ornamental fishes";
32	"Seats with wheels and their spare parts, and the artificial members of the body, hearing aids, dialysis machines and children incubation";
39	"Healthcare services except weight loss services and plastic surgeries for non-medical purposes";
52	"Cars specialized for disabled persons";
54	"Devices and software specialized for blind persons"; and
55	"(a) Local medicines and their effective components. (b) Imported medicines and their effective components."

Figure 33. List of exempt items in Egypt. Source: http://www.riad-riad.com/en/publications/guide-egypts-vat-law[416]

Kenya (EAC):

Prior to 1990, Kenya had a Sales Tax Regime, however the Kenyan Government decided to implement a VAT system with an effective date of 1 January 1990 at a rate of 17%.[417] Furthermore, the legislation was substantially changed in 2013 and noted in the Value-Added Tax Act No 35 of 2013.[418] The VAT exemptions are contained in Annexure A and the zero-rated items are contained in Annexure B and C.[419] The relevant items for this study are set out in Figure 34 and Figure 35. In contrast to South Africa, Kenya has a wider list of basic food items with a tax concession, which is exempt from VAT rather than zero-rated.

Basic exempt items (Annexure A of Value-Added Tax Act No 35 of 2013)[420]
Item 1 – 3: "Bovine and animal semen, and fish eggs and roes";
Item 4 – 17: "Soya beans, groundnuts, copra, linseed, rape or colza seeds, sunflower seeds, cotton seeds, sesamum seeds, mustard seeds, safflower seeds, other oil seeds and oleaginous fruits and pyrethrum flower";
Item 17A: "Sugarcane";
Item 17B: "Unprocessed produce of plant species camellia sinensis";
Item 18: "Live animals";

[416] Salah, F. Riad, E. Elkady, H. & Mohsen, A. (23 October 2016) *'A Guide to Egypt's VAT Law'.* Available at: http://www.riad-riad.com/en/publications/guide-egypts-vat-law (Accessed: 25 August 2019).
[417] Omondi, F. (2013) '*VAT Reforms and Revenue Productivity in Kenya (1990 – 2010*)', pp 4. Available at: http://erepository.uonbi.ac.ke/bitstream/handle/11295/63135/Omondi%20Francis_Vat%20Reforms%20and%20Revenue%20productivity%20in%20Kenya%20%281 (Accessed: 1 December 2019) and Bird, R. M. and Gendron, P. (2007) 'The VAT in Developing and Transitional Countries', pp 225. Cambridge and New York: Cambridge University Press.
[418] PwC. (2017) *'Helping you navigate Africa's VAT landscape',* pp 55. Available at: https://www.pwc.co.za/en/assets/pdf/vat-in-africa-2017.pdf (Accessed: 4 May 2019).
[419] The Republic of Kenya. (2018) *'Value-Added Tax Act No 34 of 2013'.* Available at: https://www.kra.go.ke/images/publications/ValueAddedTax_ActNo35of2013.pdf (Accessed: 9 May 2019).
[420] The Republic of Kenya. (2018).

Item 19: "Meat and edible meat offals";
Item 20: "Fish and crustaceans, muluscs and other quanticiveterbrates";
Item 21: "Unprocessed milk";
Item 22: "Eggs";
Item 23: "Edible vegetables and certain roots and tubers";
Item 24: "Edible fruits and nuts, peal of citrus fruits or melon";
Item 25: "Cereals";
Item 26: "Fertilizers";
Item 28: "Maize (corn) seed";
Item 33 - 39: "Certain medical equipment and medicines";
Item 39 (9619.00.10 tariff number): "Sanitary towels (pads) and tampons";
Item 39 (0402.99.10 tariff number): "Milk, specially prepared for infants";
Item 39 (1006.30.00 tariff number): "Semi-milled or wholly milled rice";
Item 41: "Mosquito nets";
Item 44: "Unprocessed green tea";
Item 45: "Specialised solar equipment and accessories, including solar water heaters and deep cycle-sealed batteries which exclusively use or store solar power";
Item 52, 52A and 52B: "Plastic biogas digesters, biogas and the leasing of biogas producing equipment";
Item 53: "Parts imported or purchased locally for the assembly of primary school laptop tablets, subject to approval by the Cabinet Secretary for the National Treasury, on recommendation by the Cabinet Secretary responsible for matters relating to information technology";
Item 95: "The supply of natural water, excluding bottled water, by the government";
Item 98: "The supply of maize (corn) flour, cassava flour, wheat or meslin flour and maize flour containing cassava flour by more than ten per-cent in weight";
"Medical, veterinary, nursing and dental services";
"Public passenger transportation";
"Parts imported or sold locally for the assembly of computers"; and
"Fuel (exemption terminated 1 September 2018, a reduced rate of 8% applicable)."

Figure 34. List of exempt items in Kenya. Source: Kenya VAT Act - https://www.kra.go.ke

Basic zero-rated items (Annexure B and C of Value-Added Tax Act No 35 of 2013)
Item 11: "Inputs or raw materials (either produced locally or imported) supplied to pharmaceutical manufacturers in Kenya for manufacturing medicaments, as approved from time to time by the Cabinet Secretary in consultation with the Cabinet Secretary responsible for matters relating to health";
Item 13: "The supply of maize (corn) flour, ordinary bread and cassava flour, wheat or meslin flour and maize flour containing cassava flour by more than ten per-cent in weight";

Item 13A: "The supply of ordinary bread";
Item 15: "Milk and cream, not concentrated nor containing added sugar or other sweetening matter, of tariff numbers – 0401.10.00—of a fat content, by weight, not exceeding 1%; 0401.20.00—of a fat content, by weight, exceeding 1% but not exceeding 6%; 0401.40.00—of a fat content, by weight, exceeding 6% but not exceeding 10%; 0401.50.00—of a fat content, by weight, exceeding 10%";
Item 16: "All inputs and raw materials whether produced locally or imported, supplied to manufacturers of agricultural pest control products upon recommendation by the Cabinet Secretary for the time being responsible for agriculture";
Item 18: "Inputs or raw materials for electric accumulators and separators including lead battery separator rolls whether or not rectangular or square supplied to manufacturers of automotive and solar batteries in Kenya"; and
Annexure C: "Medicaments with certain HS Codes."

Figure 35. List of zero-rated items in Kenya. Source: Kenya VAT Act - https://www.kra.go.ke[421]

4.3 Conclusion

It is evident from this international comparison performed on several African countries that there is a wide application of VAT exemptions and zero-ratings and that there is limited consensus amongst the countries on determining a tax policy of goods deemed to be necessary or basic for its citizens. In Jean-Paul Bodin's Article, "The Rise of VAT in Africa", it is stated that the features of the VAT systems of the African countries vary and depend on traditions and the date of introduction of the tax and there are often many exemptions which is observed in the results of the international comparisons in an African context. The common exemptions include the agricultural sector, unprocessed foodstuffs, medical and healthcare goods and services, foreign aid projects, utilities such as water and electricity, and education.[422] The list has also been increased in countries such as Kenya to include sanitary pads. However, the challenge for these African counties is to re-broaden its tax base and reduce the number of exemptions.

Some critics of VAT in developing countries, such as those in Africa, have suggested that due to the large-scale poverty and other challenges of operating a VAT system, it is unwise to adopt VAT in developing countries and a sales tax system would be more beneficial.[423]

Given the level of economic growth and the large number of exemptions in other African countries, it would be tempting to argue that South Africa's list is too limited and other basic foods, water and electricity and medicines and medical services should be included. However, it is interesting to note that SADC has adopted a policy to

[421] The Republic of Kenya. (2018) *'Value-Added Tax Act No 34 of 2013'.* Available at: https://www.kra.go.ke/images/publications/ValueAddedTax_ActNo35of2013.pdf (Accessed: 9 May 2019).
[422] Bodin, J.P. and Koukpaizan, V. (2009) *'The Rise of VAT in Africa – Impact and Challenges'.* International VAT Monitor, IBFD, May/ June 2009, pp 178 – 189. Available at: https://research-ibfd-org.ezproxy.uct.ac.za/#/doc?url=/document/ivm030902 (Accessed: 23 July 2019).
[423] Bodin, J.P. and Koukpaizan, V. (2009) pp 178 – 189.

limit VAT exemptions and zero-ratings to an absolute minimum and to have a broad base of tax.[424] South Africa as a member is likely to share this view, which is evident by the restraint of policy makers to make drastic changes to the VAT legislation in this regard. However, given the vast wealth inequality in South Africa and the impact of the 2018 VAT rate increase, it is unlikely that the use of zero-rating certain items would be eliminated. Although many African countries use exemptions as relief for the poor, it is not recommended that exemptions be introduced. The reason for this was explored in Chapter 2 as exemptions introduce complexities and a cascading of VAT effect[425] (i.e. VAT blockage on input tax, thus VAT is charged on VAT). However, the use of zero-rating as an equality instrument is preferable as there is no cascading VAT impact as there is with an exemption. Chapter 5 will consider which items would be appropriate to include in the list of zero-rated items in the context of South Africa's consumer patterns and economic conditions.

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[424] *South African Development Community (2016) 'Guidelines for Co-Operation in Value Added Taxes in the SADC Region'.* Available at: https://www.sadc.int/files/4114/7618/6109/SADC_VAT_Guidelines_and_Commentary_Published_October_2016_English.pdf (Accessed: 5 April 2018).

[425] *"*Cascading effect is when there is tax on tax levied on a product at every step of the sale. The tax is levied on a value which includes tax paid by the previous buyer, thus, making the end consumer pay tax on already paid tax.*"* Cleartax. Available at: https://cleartax.in/s/differences-between-gst-and-vat (Accessed: 21 September 2019).

Chapter 5: Assessment of South Africa's spending patterns

5.1 Introduction

Chapter 3 introduced various methodologies for selecting or targeting an optimal list of basic items that should be included in the zero-rating basket. The purpose of this Chapter is to apply these methodologies to determine which commodities should be included in a zero-rated list within the South African context. In essence, these methodologies centre on evaluating the consumer expenditure patterns of the population and making a comparison between the expenditure spending patterns of the rich and poor.

5.2 Analysis of spending patterns

The first step is to determine the spending patterns of the population and assess the consumption figures to understand on which expenditure items the poor spend their income.

Statistics South Africa (Stats SA) at regular intervals performs an Income and Expenditure Survey (IES) and Living Conditions Survey (LCS). These surveys research the income spread and source as well as the expenditure items of households. The most recent survey available is the LCS 2014/2015. The types of expenditure sources are as follows; (1) Food and non-alcoholic beverages; (2) Alcoholic beverages, tobacco and narcotics; (3) Clothing and footwear; (4) Housing, water, electricity, gas and other fuels; (5) Furnishings, household equipment, and routine maintenance of the house; (6) Health; (7) Transport; (8) Communication; (9) Recreation and culture; (10) Education; (11) Restaurants and hotels; (12) Miscellaneous goods and services; and (13) Other unclassified Expenses.[426]

As described in Chapter 3, the South African population is split into ten deciles, representing each 10% of the population based on households' annual income. The income categories for each decile are outlined in Figure 36 below.

Decile	Income
Decile 1	Below R 11,788 p.a.
Decile 2	R 11,779 - R 20,281 p.a.
Decile 3	R 20,282 - R 29,758 p.a.
Decile 4	R 29,759 - R 40,694 p.a.
Decile 5	R 40,695 - R 54,348 p.a.
Decile 6	R 54,349 - R 77,502 p.a.
Decile 7	R 77,503 - R 113,946 p.a.
Decile 8	R 113,947 - R 186,214 p.a.
Decile 9	R 186,215 - R 358,695 p.a.
Decile 10	Above R 358,696 p.a.

Figure 36. The income categories for each of the ten deciles of the South African population. Source: Statistics South Africa. (2015) 'Living Conditions Survey' - www.statssa.gov.za.

[426] Statistics South Africa. (2015) 'Living Conditions Survey'. Available at: http://www.statssa.gov.za/publications/P0310/P03102014.pdf (Accessed: 20 January 2019).

As discussed by Jansen (2016), it is universally considered amongst economists that the first four deciles represent the poor community in South Africa.[427]

In determining on which expenditure category, the poor, middle-class and rich spend most of their income, the proportional spend of the total spend has been calculated, and the results are observed in Figure 37. The methodology used for this calculation is based on the following formula for each data point; i.e. the 28.9% calculated for Decile 1 in the Food and non-alcoholic beverages category:

$$\% = \frac{Decile\ 1\ spend\ on\ Food\ and\ non{-}alcoholic\ beverages}{Total\ spend\ by\ Decile\ 1}$$

Expenditure Category	Decile 1	Decile 2	Decile 3	Decile 4	Decile 5	Decile 6	Decile 7	Decile 8	Decile 9	Decile 10
Food and non-alcoholic beverages	28.9%	30.9%	29.5%	26.4%	25.0%	22.0%	18.3%	13.0%	9.2%	6.1%
Alcoholic beverages, tobacco	2.9%	1.7%	1.5%	1.7%	1.5%	1.4%	1.2%	1.0%	0.7%	0.4%
Clothing and footwear	7.6%	7.2%	8.1%	7.8%	8.0%	7.7%	6.9%	5.4%	4.1%	2.9%
Housing, water, electricity, gas and other fuels	25.3%	25.0%	24.7%	25.5%	26.0%	27.5%	28.9%	31.0%	32.6%	37.3%
Furnishings, household equipment	3.7%	4.8%	4.9%	5.8%	4.9%	4.6%	4.2%	4.4%	5.2%	5.8%
Health	0.9%	0.8%	0.8%	0.8%	0.9%	0.9%	0.7%	0.9%	1.0%	0.9%
Transport	11.3%	11.4%	11.1%	11.6%	13.4%	14.6%	16.9%	19.4%	18.7%	16.2%
Communication	4.5%	3.8%	3.8%	4.0%	4.0%	4.0%	3.9%	3.6%	3.3%	2.9%
Recreation and culture	2.7%	2.3%	2.5%	3.2%	3.0%	3.4%	3.6%	4.0%	4.1%	4.1%
Education	1.8%	0.9%	1.2%	1.6%	1.6%	1.5%	1.9%	2.1%	2.6%	3.1%
Restaurants and hotels	2.6%	2.6%	2.2%	2.1%	1.9%	2.1%	1.9%	1.9%	2.0%	2.2%
Miscellaneous goods and services	7.6%	8.6%	9.7%	9.3%	9.6%	10.3%	11.4%	13.2%	16.3%	17.9%
Other unclassified Expenses	0.1%	0.0%	0.1%	0.1%	0.1%	0.1%	0.1%	0.0%	0.0%	0.0%

Figure 37. The proportion of spending on consumption types per each decile in the South African population. Own calculations based on the data available in LCS 2014/ 2015. Source: www.statssa.gov.za

The observations of the proportional spend per each decile demonstrates that for the poorer households in South Africa, their highest expenditure spend relates to the following categories; Food and non-alcoholic beverages, Housing, water, electricity, gas and other fuels, and Transport. In comparison the more affluent household's highest expenditure categories are; Housing, water, electricity, gas and other fuels, Transport, and Miscellaneous goods and services. Therefore, on a proportional basis of expenditure the poor spend most of their income on food, which would imply that tax concessions, such as zero-rating, should be focussed on this area.

[427] Jansen, A. and Calitz, E. (2017) *'Considering the efficacy of value-added tax zero-rating as pro-poor policy: The case of South Africa', Development Southern Africa,* 34(1), pp. 64.

However, as discussed in Chapter 3, experts debate whether this analysis should be done on an absolute or proportional basis. Therefore Figure 38 includes the absolute values (in Rands rounded to millions) of expenditure spend per expenditure category for each Decile.

Consumption type	1	2	3	4	5	6	7	8	9	10
Food and non-alcoholic beverages	11,387	14,097	15,754	17,764	19,838	21,309	23,331	25,379	30,048	41,985
Alcoholic beverages, tobacco and narcotics	1,159	764	781	1,166	1,204	1,381	1,569	2,031	2,280	2,797
Clothing and footwear	2,990	3,279	4,303	5,264	6,375	7,427	8,804	10,491	13,529	19,609
Housing, water, electricity, gas and other fuels	9,948	11,404	13,185	17,190	20,631	26,614	36,919	60,419	107,066	255,423
Furnishings, household equipment	1,442	2,202	2,599	3,925	3,909	4,438	5,342	8,593	17,168	39,981
Health	360	354	451	565	728	883	901	1,751	3,158	6,383
Transport	4,457	5,216	5,923	7,781	10,596	14,124	21,494	37,831	61,499	110,703
Communication	1,769	1,743	2,015	2,683	3,141	3,900	5,003	6,922	10,973	20,174
Recreation and culture	1,061	1,071	1,323	2,168	2,389	3,316	4,624	7,788	13,586	28,036
Education	724	400	646	1,088	1,237	1,429	2,475	4,112	8,682	21,277
Restaurants and hotels	1,034	1,179	1,201	1,437	1,502	2,057	2,486	3,658	6,450	15,234
Miscellaneous goods and services	2,979	3,931	5,186	6,233	7,626	9,934	14,515	25,679	53,516	122,450
Other unclassified Expenses	25				81	74	66	76	107	329
Total	39,335	45,659	53,402	67,359	79,257	96,886	127,529	194,730	328,062	684,381

Figure 38. The absolute spending on consumption types per each decile in the South African population. Source: www.statssa.gov.za

Figure 38 illustrates that although Decile 1, Decile 2, Decile 3 and Decile 4 spend proportionally more of their income on food, Decile 10 spends more in absolute terms, i.e. their Rand spend is significantly more than the poor. Therefore, a zero-rating of food in absolute terms would have a larger benefit in tax savings for the wealthy.

5.3 Top 40 food items consumed by the poor

As discussed, the selection of zero-rated items should be based on items that are mostly consumed by the poor. Based on the data collected by Stats SA, the poor would receive the most relief i.e. the tax savings benefit, from the zero-rating of food. However, should food in its entirety be zero-rated the cost of VAT revenue lost by the government would be significantly large and thus impractical to recommend for implementation. Therefore, a method of targeting specific items should be utilised to identify a selection of items that would benefit the poor and have a minimal cost to the fiscus.

In order to make such selection of additional zero-rated items the proportion of the 40 largest food items consumed by the poor[428] have been identified by analysing the consumer spending patterns from the data collected in LCS 2014/2015. Further consideration has been given to which food items are already subject to the zero-rate. Figure 39 details the results of the top 40 food items consumed by the poor.

No	Type	1	2	3	4	Average of Decile 1- 4 (Poor)	10	Comments
1	Poultry (incl heads and feet)	13.92%	14.10%	14.98%	14.44%	14.36%	9.36%	Standard-rated
2	Mealie meal/Maize flour	11.30%	12.52%	12.21%	10.79%	11.70%	1.60%	Zero-rated
3	Brown bread	7.93%	6.91%	7.59%	7.28%	7.43%	3.00%	Zero-rated
4	Rice	5.62%	5.59%	4.50%	4.33%	5.01%	1.55%	Zero-rated
5	Beef and veal (incl heads and feet)	4.58%	4.17%	4.34%	5.37%	4.62%	10.53%	Standard-rated
6	Aerated cold drinks	4.15%	3.53%	3.53%	3.83%	3.76%	3.61%	Standard-rated
7	Edible oils (eg cooking oils)	3.67%	3.86%	3.49%	3.05%	3.52%	0.91%	Zero-rated
8	White bread	3.66%	3.59%	3.35%	3.20%	3.45%	2.49%	Standard-rated
9	White sugar	3.15%	3.72%	3.36%	3.26%	3.37%	0.86%	Standard-rated
10	Potatoes	2.85%	2.92%	2.72%	2.45%	2.73%	0.96%	Zero-rated
11	Fresh full cream milk	2.22%	1.85%	2.22%	2.39%	2.17%	3.45%	Zero-rated
12	Cake flour	1.64%	1.79%	1.83%	1.99%	1.81%	0.53%	Zero-rated[429]
13	Canned pilchards	1.92%	1.78%	1.85%	1.54%	1.77%	0.47%	Zero-rated
14	Boerewors	1.64%	1.68%	1.73%	1.94%	1.75%	2.26%	Standard-rated
15	Large eggs	1.69%	1.66%	1.47%	1.46%	1.57%	1.30%	Zero-rated
16	Tomatoes fresh	1.64%	1.39%	1.36%	1.31%	1.43%	0.82%	Zero-rated
17	Sour milk/maas	1.47%	1.45%	1.42%	1.33%	1.42%	0.31%	Standard-rated
18	Brown sugar	1.07%	1.35%	1.29%	1.21%	1.23%	0.38%	Standard-rated
19	Unclassified food items	0.95%	0.58%	0.96%	2.35%	1.21%	3.55%	Standard-rated
20	Food hampers	0.79%	0.91%	1.11%	1.52%	1.08%	2.55%	Standard-rated
21	Onions	1.08%	0.98%	1.02%	1.03%	1.03%	0.61%	Zero-rated
22	Cabbage fresh	0.98%	0.95%	1.09%	0.93%	0.99%	0.20%	Zero-rated
23	Baby food Predominantly milk	0.99%	0.71%	0.86%	1.37%	0.98%	0.09%	Standard-rated
24	Powder soup	0.85%	0.90%	0.74%	0.85%	0.84%	0.34%	Standard-rated
25	Beans dried	0.73%	0.83%	0.77%	0.89%	0.81%	0.13%	Zero-rated
26	Longlife Full cream milk	0.78%	0.82%	0.81%	0.77%	0.80%	1.21%	Zero-rated
27	Baked beans in tomato sauce	0.77%	0.83%	0.73%	0.73%	0.76%	0.45%	Standard-rated
28	Polony	0.76%	0.84%	0.74%	0.64%	0.75%	0.71%	Standard-rated
29	Medium eggs	0.83%	0.74%	0.64%	0.56%	0.69%	0.23%	Zero-rated
30	Potato crisps	0.48%	0.36%	0.48%	1.36%	0.67%	0.90%	Standard-rated
31	Bread flour	0.62%	0.75%	0.60%	0.69%	0.66%	0.06%	Zero-rated[430]

[428] Average of Decile 1, Decile 2, Decile 3 and Decile 4.
[429] Included in Schedule 2 Part B in 2018 after the VAT panel report.
[430] Included in Schedule 2 Part B in 2018 after the VAT panel report.

32	Fruit juices not from food service places	0.75%	0.54%	0.65%	0.63%	0.64%	1.88%	Standard-rated
33	Other processed meat (Russians)	0.63%	0.62%	0.68%	0.60%	0.64%	0.75%	Standard-rated
34	Whiteners (Cremora, Ellis Brown)	0.54%	0.64%	0.60%	0.50%	0.57%	0.19%	Standard-rated
35	Tag less tea bags	0.58%	0.54%	0.56%	0.55%	0.55%	0.26%	Standard-rated
36	Medium fat margarine spread	0.37%	0.64%	0.42%	0.70%	0.53%	1.20%	Standard-rated
37	Flavoured yogurt	0.56%	0.43%	0.49%	0.57%	0.51%	1.06%	Standard-rated
38	Instant coffee	0.57%	0.47%	0.50%	0.49%	0.51%	1.34%	Standard-rated
39	Concentrates and drink powders	0.46%	0.47%	0.51%	0.50%	0.49%	0.48%	Standard-rated
40	Samp	0.46%	0.57%	0.43%	0.43%	0.47%	0.09%	Zero-rated

Figure 39. Top 40 food items consumed by the poor. Own calculations based on the data collected in the LCS 2014/2015. Source: www.statssa.gov.za.

As observed in Figure 39, five of the top ten food items are currently included in the schedule of zero-rating,[431] these big spend items are; Mealie meal, Brown bread, Rice, Cooking oils, and Potatoes. The other five items which are currently standard-rated include; Poultry, Beef and veal, Aerated cold drinks, White bread and White sugar. Given the spending patterns it is tempting to state that these top five standard-rated items should be zero-rated and incorporated in Schedule 2 Part B. However, as Fourie and Owen commented, the list of zero-rated items must also take into account the costs to the fiscus i.e. the loss in VAT revenue associated with zero-rating these items.[432] Therefore, a cost analysis has been performed to estimate the monetary impact of zero-rating these additional five items. The resultant monetary impact of zero-rating (in Rands rounded to millions) these additional food items is contained in Figure 40.

Food Item	Amount of Revenue Forgone
Poultry	4,316
Beef and veal	2,951
Aerated cold drinks	1,600
White bread	1,277
White sugar	800
Total monetary impact	10,944

Figure 40. The monetary impact of zero-rating the additional five food items. Own calculations based on the data collected in LCS 2014/2015 and the consumer price indexes for 2016,2017,2018 and 2019. Source: www.statssa.gov.za

As calculated in Figure 40, the monetary value of the loss of revenue for the South African government is estimated to be approximately R 10,944 million. This amount is approximately half of the R 22 billion additional revenue estimated to be collected by the 2018 VAT rate increase.

[431] Schedule 2 Part B of the VAT Act.
[432] Fourie, F.C. and Owen, A. (1993) '*Value-Added Tax and Regressivity in South Africa*'. South African Journal of Economics, 61(4), pp 284 - 285.

5.4 Economic condition of South Africa

The South African economy is under severe pressure which was the message of the 2019 Budget Speech, where the National Treasury has released the economic snapshot and outlook. Further it acknowledged that the preceding decade was plagued with a weak economy, with little investment growth.[433] The forecasted GDP growth is estimated to be 1.5% and the current budget deficit is estimated to be R 204.3 billion, which is serviced by government debt.[434] The economic performance and projections suggest that the South African government and tax policymakers would be considering policies that would increase the tax base rather than policies that will result in significant loss in revenue.

5.5 Conclusion

This Chapter provided a summary of the South African economy and the expenditure spending patterns of the South African population, with the view to assess the differences in the spending of the poor versus the rich. Most food items mostly consumed by the poor are also consumed by the rich as observed in Figure 39. Arguably, poultry and white bread are two items that should be zero-rated and included in Schedule 2 Part B. The VAT panel had recommended white bread as an item to be included in the zero-rating food basket.[435] Further, the VAT panel considered the inclusion of poultry but mentioned that "the cost in terms of forgone VAT would be relatively high."[436] This would also be difficult to motivate given the state of the South African economy. An option to offset the revenue forgone is to remove the blanket inclusion of fruit and vegetables included in the zero-rated schedule[437] and use the above consumer patterns to identify individual fruits and vegetables,[438] which should be included in the zero-rated basket. Figure 39 reveals that potatoes, tomatoes, onions and cabbage are amongst the vegetables mostly consumed by the poor.

[433] Republic of South Africa. (2018) *'National Treasury Budget Speech 2018',* pp 13. Available at: http://www.treasury.gov.za/documents/national%20budget/2019/review/FullBR.pdf (Accessed: 5 April 201).
[434] Republic of South Africa. (2018) pp 7 and 8.
[435] Republic of South Africa. (2018) *'Recommendations to Minister of Finance by the Independent Panel of Experts for the Review of Zero-Rating in South Africa',* pp 43. Available at: http://www.treasury.gov.za/comm_media/press/2018/2018081001%20VAT%20Panel%20Final%20Report.pdf (Accessed: 21 September 2018).
[436] Republic of South Africa. (2018) pp 64.
[437] Schedule 2 Part B of the VAT Act.
[438] Jansen, A. Stoltz, E. and Yu, D. (2013) *'The Targeting of Zero-Rated Basic Foodstuffs under Value-Added Tax (VAT) in South Africa',* Journal of Econometrics, 37(3), pp. 101.

Chapter 6: Conclusion

The question this study aimed to answer is whether the 2018 VAT rate increase negatively impacted on the poor, and whether further zero-rated items should be added to the list of Schedule 2 Part B of the VAT Act, is the most appropriate response in this regard.

Given the budget deficit, the 2018 VAT rate increase may have been unavoidable, as the National Treasury needed to source additional tax revenues. After the announcement there was adverse public reactions and the Panel of Experts appointed by the Minister of Finance were tasked with identifying the impact on the poor and whether additional items should be added to the list of basic food items in Schedule 2 Part B of the VAT Act or whether items should be removed. The Panel concluded that the poor were impacted more than the rich, and that six items should be added to the list of basic food items.

In Chapter 2 the basic principles of VAT and a sound tax policy were discussed as well as the appropriate manner to assess a tax policy. A tax concession for VAT purposes, would be a reduced VAT rate, zero VAT rate or an exemption. An exemption is not preferable due to the cascading effect of the restriction of input tax associated with exempt supplies.

Chapter 3 included a literature review, which revealed that VAT is considered regressive and that it is impracticable to not have any food items as zero-rated. The concept of basic goods or 'merit' goods suggest that certain items deserve a tax concession and that the use of the zero-rating is a means to balance the regressive nature of VAT. Previous studies provided methodologies on the selection of these 'merit' goods, which involved assessing the spending patterns of the poor. However, the selection of a food item is dependent on its affordability for the government, as the trade-off is VAT revenue forgone, therefore, there are basic items which may be excluded based on its cost to the national purse.

Economists have advised that consumer spending patterns may change over time and the list of 'merit' goods should be reviewed at regular intervals. Notwithstanding, there are disadvantages of zero-ratings, other than the loss of tax revenue, and these include adding complexities into the VAT system and rendering it vulnerable to tax evasion. The South African Revenue Service has, however, used the practice of issuing practice notes and interpretation notes to manage these risks.

There have been many studies on the efficiency of South Africa's fiscal policy and its economic position. The results of these studies were that, irrespective of the use of social grants, South Africa's Gini Coefficient is relatively high (in the region of 63%), which suggests that South Africa has a high-income inequality and an unequal society and therefore questioned the effectiveness of the social spending and its distributional impact.

An international comparison was undertaken with a focus on African economies in Chapter 4. The results infer that many other African nations have granted tax concessions on food items with some countries having further extended the concessions to non-food items such as electricity, water and medicine and medical services.

These tax concessions are a mix of exemptions and zero-ratings. Some academics have suggested that developing economies with a large proportion of a poor population will struggle to limit these exceptions to a minimum and others have suggested a VAT system is not ideal for such economies.

The last chapter involved applying the methodology outlined in the literature review to the current South African spending patterns and to evaluate whether the current list of basic food items[439] is relevant and identifying the most consumed food items of the poor. A review of the top 40 items consumed by the poor was performed and the majority of the items in the list of zero-rated items contained in Schedule 2 Part B made up half of the top 40 list. However, the other strong contenders to include would be; poultry, beef, aerated soft drinks, white bread and white sugar, but would result in a significant cost to the fiscus.

In conclusion, South Africa has a high-income inequality and using a social grant system has not yet resulted in a decline of this income inequality. In ideal circumstances where government spending is effective in balancing the poverty gap, the use of zero-rating can be avoided, as the adverse impact of the regressive nature of VAT is offset by increasing social grants. However, this would need to be a balancing act for the National Treasury when setting the annual fiscal budget to ensure the cash payments to the poor through the social system is enough to offset the regressive nature of VAT.

However, in societies with significant inequality and where government spending on the social grant system is already a significant portion of the budget, a VAT concession in the form of a zero-rating may prove necessary to provide relief in combatting the impact of a VAT rate increase on the poor. It is important to note that the 2018 VAT rate increase was presumably a result of the significant budget deficit, and therefore the selection of food items for zero-rating would need to factor in the economic conditions. Therefore, items which on a merit basis should be included on the list of basic food items may be rejected due to its unaffordability. It would not be rational to introduce a zero-rating which would effectively wipe out the tax revenue needed to balance the fiscal budget.

This study has provided evidence that the 2018 VAT rate increase did negatively impact the poor, and that as the Panel recommended, the list of basic food items should be expanded. However, the items that were included based on the Panel's recommendations are expected to provide limited relief to the poor. This is an area for future studies to identify the actual relief these inclusions had on the poor based on the next income and expenditure survey data.

[439] Part B of Schedule 2 of the VAT Act.

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Annexures

Annexure A

Table 1 of Government Gazettes – The evolution of the South African VAT rate

Date of Issue	Government Notice	Government Gazette No	Notice Title	Description
18 June 1990	R. 479	12514	Proposed Introduction of Value-Added Tax (VAT Bill)	1. Proposed Section 7 (1) states: Subject to exemptions, exceptions, deductions and adjustments provided for in this Act, there shall be levied and paid for the benefit of the State Revenue Fund a tax, to be known as the value-added tax – (a) On the supply by any vendor of goods and services supplied by him on or after the commencement date in the course or furtherance of any enterprise carried on by him; (b) On the importation of any goods into the Republic by any person on or after the commencement date; and (c) On the supply of imported services by any person on or after the commencement date, calculated at the rate of **x** per cent on the value of the supply in question or the importation, as the case may be.
12 June 1991	R. 1342	13307	No 89 of 1991: Value-Added Tax Act, 1991	1. Section 1 – Definitions “Prescribed tax rate” means the rate of tax, expressed as a percentage, fixed by Parliament; 2. Section 7 (1) states: Subject to exemptions, exceptions, deductions and adjustments provided for in this Act, there shall be levied and paid for the benefit of the State Revenue Fund a tax, to be known as the value-added tax – (a) On the supply by any vendor of goods and services supplied by him on or after the commencement date in the course or furtherance of any enterprise carried on by him;

				(b) On the importation of any goods into the Republic by any person on or after the commencement date; and (c) On the supply of imported services by any person on or after the commencement date, calculated at the **prescribed tax rate** on the value of the supply in question or the importation, as the case may be.
17 July 1991	R. 1662	13412	No 136 of 1991: Taxation Laws Amendment Act, 1991	1. The deletion of “prescribed tax rate” definition. 2. Section 7(1) states: Subject to exemptions, exceptions, deductions and adjustments provided for in this Act, there shall be levied and paid for the benefit of the State Revenue Fund a tax, to be known as the value-added tax – (a) On the supply by any vendor of goods and services supplied by him on or after the commencement date in the course or furtherance of any enterprise carried on by him; (b) On the importation of any goods into the Republic by any person on or after the commencement date; and (c) On the supply of imported services by any person on or after the commencement date, calculated at the **rate of 12 per cent** on the value of the supply in question or the importation, as the case may be.
8 November 1991	R. 2695	13627	Value-Added Tax Act (89/1991): Amendments to sections 1, 2, 7, 8, 10, 11, 12, 15, 17, 18, 20, 21, 22, 27, 28, 39, 40, 41, 64, 65, 67, 75 and 78 and of Schedules 1 and 2	1. Section 7(1) states: Subject to exemptions, exceptions, deductions and adjustments provided for in this Act, there shall be levied and paid for the benefit of the State Revenue Fund a tax, to be known as the value-added tax – (a) On the supply by any vendor of goods and services supplied by him on or after the commencement date in the course or furtherance of any enterprise carried on by him; (b) On the importation of any goods into the Republic by any person on or after the commencement date; and

				(c) On the supply of imported services by any person on or after the commencement date, calculated at the **rate of 10 per cent** on the value of the supply in question or the importation, as the case may be. Note: The amendments effected shall be deemed to have come into operation on **30 September 1991**.
2 April 1993	R. 598	14731	Value-Added Tax Act (89/1991): Increase in rate of tax specified in section 7	1. "Under section 77 of the Value-Added Tax Act, 1991 (Act No. 89 of 1991), I, Theodorus Gerhardus Alant, Deputy Minister of Finance, hereby make known for general information that in terms of a taxation proposal tabled in Parliament on 17 March 1993 the rate of value-added tax specified in section 7 of the said Act is to be increased to the rate of **14 per cent**, as set forth in that proposal, for the purpose of determining amounts of value-added tax which are or are deemed to have become payable on the supply of goods or services on or after **7 April 1993** or on the importation of goods into the Republic on or after that date."
9 July 1993	R. 1193	14936	No. 97 of 1993: Taxation Laws Amendment Act, 1993	1. Section 7(1) states: Subject to exemptions, exceptions, deductions and adjustments provided for in this Act, there shall be levied and paid for the benefit of the State Revenue Fund a tax, to be known as the value-added tax – (a) On the supply by any vendor of goods and services supplied by him on or after the commencement date in the course or furtherance of any enterprise carried on by him; (b) On the importation of any goods into the Republic by any person on or after the commencement date; and (c) On the supply of imported services by any person on or after the commencement date, calculated at the **rate of 14 per cent** on the value of the supply in question or the importation, as the case may be.

				Note: The amendments effected shall be deemed to have come into operation on **7 April 1993**.
17 January 2019	R. 18	42171	No. 21 of 2018: Rates and Monetary Amounts and Amendment of Revenue Laws Act, 2018	1. Section 7(1) states: Subject to exemptions, exceptions, deductions and adjustments provided for in this Act, there shall be levied and paid for the benefit of the National[440] Revenue Fund a tax, to be known as the value-added tax – (a) On the supply by any vendor of goods and services supplied by him on or after the commencement date in the course or furtherance of any enterprise carried on by him; (b) On the importation of any goods into the Republic by any person on or after the commencement date; and (c) On the supply of imported services by any person on or after the commencement date, calculated at the **rate of 15 per cent** on the value of the supply in question or the importation, as the case may be. Note: The amendments effected shall be deemed to have come into operation on **1 April 2018**.

Figure 41. Table of Government Gazettes - The evolution of the South African VAT rate. Source: https://www.sabinet.co.za/

Table 2 of Government Gazettes – The evolution of section 11 (1) (j) and Schedule 2 Part B

1. Government Notice 1662 of 1991 in Government Gazette No. 13412 on 17 July 1991

Section 11 (1) (j)
The goods consist of (i) Brown bread as defined in Regulation 1 of the Regulations in terms of Government Notice No. R.577 published in Government Gazette No. 13074 of 15 March 1991; or (ii) Maize meal graded as super maize meal, special maize meal, sifted maize meal or unsifted maize meal.

Figure 42. Government Notice 1662 of 1991 in Government Gazette No. 13412 on 17 July 1991. Source: https://www.sabinet.co.za/

2. Government Notice 2695 of 1991 in Government Gazette No. 13627 on 8 November 1991

Section 11 (1) (j)

[440] The term ‘State’ was changed to ‘National’ in respect of the amendment published in Government Notice 1102 of 1996 in Government Gazette No. 17311 on 3 July 1996.

The goods consist of such foodstuffs as are set forth in Part B of Schedule 2, but subject to such conditions as may be prescribed in the said Part;

Schedule 2 Part B - Zero Rate: Supply of Goods consisting of Certain Foodstuffs	
1. The goods in respect of the supply of which the rate of zero per cent shall apply under the provisions of section 11 (1) (j) of this Act shall, subject to the provisions of paragraph 2, be as hereinafter set forth:	
Item 1	Brown bread as defined in Regulation 1 of the Regulations in terms of Government Notice No. R. 577 published in Government Gazette No. 13074 of 15 March 1991
Item 2	Maize meal, graded as super maize meal, special maize meal, sifted maize meal or unsifted maize meal
Item 3	Samp, not further prepared or processed
Item 4	Mealie rice not further prepared or processed
Item 5	Dried-silo screened mealies or dried mealies for human consumption not further prepared or processed or packaged as, seed, but excluding popcorn (zea mays everta)
Item 6	Dried beans, whole, split, crushed or in powder form but not further prepared or processed or where packaged as seed
Item 7	Lentils, dried, whole, skinned or split
Item 8	Pilchards or sardinella supplied in tins or cans consisting mainly of such products regardless of whether flavoured, seasoned or preserved in oil, but excluding such products as are supplied as pet food or sardines supplied in tins or cans
Item 9	Milk, being the milk of cattle sheep or goats that has not been concentrated, condensed, evaporated, sweetened, flavoured, cultured or subjected to any other process other than homogenization or preservation by pasteurization ultra-high temperature treatment, sterilization, chilling or freezing
Item 10	Milk powder: unflavoured being the powder obtained by the removal of water from milk and which falls under the following classifications determined by the Minister of Agriculture under the Marketing Act, 1968 (Act No. 59 of 1968) or any regulation under that Act: High-fat milk powder Full-fat milk powder Medium-fat milk powder Low-fat milk powder Fat-free milk powder, provided that fat or protein content of such milk powder consists solely of milk fat or milk protein
Item 11	Dairy powder blend, being any dairy powder blend which falls under the following classifications determined by the Minister of Agriculture under the Marketing Act, 1968 (Act No.59 of 1968), or any regulation under that Act: High-fat dairy powder blend Full-fat dairy powder blend Medium-fat dairy powder blend Low-fat dairy powder blend Fat-free dairy powder blend
Item 12	Rice, whether husked, milled, polished, glazed, parboiled or broken
2. The provisions of paragraph 1 shall not apply where any goods mentioned in that paragraph are supplied in the course of carrying out any agreement for the furnishing or serving of any meal, refreshment, cooked or prepared food or any drink, as the case may be, so as to be ready for immediate consumption when so supplied.	
3. The provisions of paragraph 1 shall only apply in relation to the goods referred to under Items 3 to 12 of that paragraph for the period commencing on 30 September 1991 up to and including 31 March 1992.	

Figure 43. Government Notice 2695 of 1991 in Government Gazette No. 13627 on 8 November 1991. Source: https://www.sabinet.co.za/

3. **<u>Government Notice 1923 of 1992 in Government Gazette No. 14139 on 15 July 1992 (Act No 136 of 1992)</u>**

Schedule 2 Part B - Zero Rate: Supply of Goods consisting of Certain Foodstuffs	
1. The goods in respect of the supply of which the rate of zero per cent shall apply under the provisions of section 11 (1) (j) of this Act shall, subject to the provisions of paragraph 2, be as hereinafter set forth:	
Item 1	Brown bread as defined in Regulation 1 of the Regulations in terms of Government Notice No. R. 577 published in Government Gazette No. 13074 of 15 March 1991
Item 2	Maize meal, graded as super maize meal, special maize meal, sifted maize meal or unsifted maize meal
Item 3	Samp, not further prepared or processed
Item 4	Mealie rice not further prepared or processed
Item 5	Dried-silo screened mealies or dried mealies for human consumption not further prepared or processed or packaged as, seed, but excluding popcorn (zea mays everta)
Item 6	Dried beans, whole, split, crushed or in powder form but not further prepared or processed or where packaged as seed
Item 7	Lentils, dried, whole, skinned or split
Item 8	Pilchards or sardinella supplied in tins or cans consisting mainly of such products regardless of whether flavoured, seasoned or preserved in oil, but excluding such products as are supplied as pet food or sardines supplied in tins or cans
Item 9	Milk powder: unflavoured being the powder obtained by the removal of water from milk and which falls under the following classifications determined by the Minister of Agriculture under the Marketing Act, 1968 (Act No. 59 of 1968) or any regulation under that Act: High-fat milk powder Full-fat milk powder Medium-fat milk powder Low-fat milk powder Fat-free milk powder, provided that fat or protein content of such milk powder consists solely of milk fat or milk protein
Item 10	Dairy powder blend, being any dairy powder blend which falls under the following classifications determined by the Minister of Agriculture under the Marketing Act, 1968 (Act No.59 of 1968), or any regulation under that Act: High-fat dairy powder blend Full-fat dairy powder blend Medium-fat dairy powder blend Low-fat dairy powder blend Fat-free dairy powder blend
2. The provisions of paragraph 1 shall not apply where any goods mentioned in that paragraph are supplied in the course of carrying out any agreement for the furnishing or serving of any meal, refreshment, cooked or prepared food or any drink, as the case may be, so as to be ready for immediate consumption when so supplied.	
3. Items 3 to 10 of paragraph 1 shall cease to have effect as from such date as the Minister may fix by notice in the Gazette	
Note: These provisions are deemed to have come into operation on 1 June 1992.	

Figure 44. Government Notice 1923 of 1992 in Government Gazette No. 14139 on 15 July 1992 (Act No 136 of 1992). Source: https://www.sabinet.co.za/

4. **<u>Government Notice 1193 of 1993 in Government Gazette No. 14936 on 9 July 1993 (Act No 97 of 1993)</u>**

Schedule 2 Part B - Zero Rate: Supply of Goods consisting of Certain Foodstuffs
1. The goods in respect of the supply of which the rate of zero per cent shall apply under the provisions of section 11

(1) (j) of this Act shall, subject to the provisions of paragraph 2, be as hereinafter set forth:	
Item 11	Rice, whether husked, milled, polished, glazed, parboiled or broken[441]
Item 12	Vegetables, not cooked or treated in any manner except for the purpose of preserving such vegetables in their natural state, but excluding dehydrated, dried, canned or bottled vegetables or such vegetables as are described under separate Items in this PART.
Item 13	Fruit, not cooked or treated in any manner except for the purposes of preserving such fruit in its natural state, but excluding dehydrated, dried, canned or bottled fruit and nuts.
Item 14	Vegetable oil, marketed and supplied for use in the process of cooking food, but excluding olive oil.
Item 15	Milk, being the milk of cattle, sheep or goats that has not been concentrated, condensed, evaporated, sweetened, flavoured, cultured or subjected to any other process other than homogenization or preservation by pasteurization, ultra-high temperature treatment, sterilization, chilling or freezing.[442]
Item 16	Cultured milk, being cultured milk as classified under the Marketing Act, 1968 (Act No. 59 of 1968), with the following class designation: Cultured high-fat milk Cultured full-fat milk Cultured low-fat milk Cultured fat-free milk.
Item 17	Brown wheaten meal, being pure, sound wheaten meal, but excluding separated wheaten bran, wheaten germ and wheaten semolina.
Item 18	Eggs, being raw eggs laid by hens of the species gallus domesticus, whether supplied in their shells or in the form of egg pulp being raw pulp consisting of the yolk and white which is obtained from such eggs after the shells have been removed.
Item 19	Edible legumes and pulse of leguminous plants, dried, whole, split, crushed, skinned or in powder form, but not further prepared or processed or where packaged as seed or such pulse as are described under separate Items in this PART; and
2. The provisions of paragraph 1 shall not apply where any goods mentioned in that paragraph are supplied in the course of carrying out any agreement for the furnishing or serving of any meal, refreshment, cooked or prepared food or any drink, as the case may be, so as to be ready for immediate consumption when so supplied.	
3. Deleted.	
Note: These provisions are deemed to have come into operation on 7 April 1993.	

Figure 45. Government Notice 1193 of 1993 in Government Gazette No. 14936 on 9 July 1993 (Act No 97 of 1993). Source: https://www.sabinet.co.za/

5. **<u>Government Notice 884 of 1998 in Government Gazette No. 19013 on 29 June 1998 (Act No 30 of 1998)</u>**

Schedule 2 Part B - Zero Rate: Supply of Goods consisting of Certain Foodstuffs	
Item 8	Milk powder: unflavoured being the powder obtained by the removal of water from milk and which falls under the following classifications determined by the Minister of Agriculture under the **~~Marketing Act, 1968 (Act No. 59 of 1968)~~** **Agricultural Product Standards Act, 1990 (Act No. 119 of 1990)**, or any regulation under that Act: High-fat milk powder Full-fat milk powder Medium-fat milk powder Low-fat milk powder Fat-free milk powder, provided that fat or protein content of such milk powder consists solely of milk fat or milk protein
Item 9	Dairy powder blend, being any dairy powder blend which falls under the following classifications

[441] Previously this was Item 12.
[442] Previously this was Item 9.

	determined by the Minister of Agriculture under the ~~**Marketing Act, 1968 (Act No. 59 of 1968)**~~ **Agricultural Product Standards Act, 1990 (Act No. 119 of 1990)**, or any regulation under that Act: High-fat dairy powder blend Full-fat dairy powder blend Medium-fat dairy powder blend Low-fat dairy powder blend Fat-free dairy powder blend
Item 16	Cultured milk, being cultured milk as classified under the ~~**Marketing Act, 1968 (Act No. 59 of 1968)**~~ **Agricultural Product Standards Act, 1990 (Act No. 119 of 1990)**, with the following class designation: Cultured high-fat milk Cultured full-fat milk Cultured low-fat milk Cultured fat-free milk.

Figure 46. Government Notice 884 of 1998 in Government Gazette No. 19013 on 29 June 1998 (Act No 30 of 1998). Source: https://www.sabinet.co.za/

6. **Government Notice 709 of 2001 in Government Gazette No. 22532 on 27 July 2001 (Act No 19 of 2001)**

Schedule 2 Part B - Zero Rate: Supply of Goods consisting of Certain Foodstuffs	
Item 2	Maize meal, graded as super maize meal, special maize meal, sifted maize meal or unsifted maize meal, **not further processed other than by the addition of minerals and vitamins not exceeding one per cent by mass of the final product, solely for the purpose of increasing the nutritional value.**
Item 15	Milk, **including high-fat, full-fat, low-fat or fat-free milk**, being the milk of cattle, sheep or goats that has not been concentrated, condensed, evaporated, sweetened, flavoured, cultured or subjected to any other process other than homogenization or preservation by pasteurization, ultra-high temperature treatment, sterilization, chilling or freezing, **or the addition of minerals, vitamins, enzymes and other similar additives not exceeding one per cent by volume of the final product, solely for the purpose of increasing the nutritional value**.

Figure 47. Government Notice 709 of 2001 in Government Gazette No. 22532 on 27 July 2001 (Act No 19 of 2001). Source: https://www.sabinet.co.za/

7. **Government Notice 39 of 2007 in Government Gazette No. 30656 on 8 January 2008 (Act No 35 of 2007)**

Schedule 2 Part B - Zero Rate: Supply of Goods consisting of Certain Foodstuffs	
Item 5	Dried-silo screened mealies or dried mealies ~~**for human consumption**~~ not further prepared or processed or packaged as, seed, but excluding popcorn (zea mays everta)

Figure 48. Government Notice 39 of 2007 in Government Gazette No. 30656 on 8 January 2008 (Act No 35 of 2007). Source: https://www.sabinet.co.za/

8. **Government Notice 1451 of 2017 in Government Gazette No. 41342 on 18 December 2017 (Act No 17 of 2017)**

Schedule 2 Part B - Zero Rate: Supply of Goods consisting of Certain Foodstuffs	
Item 1	Brown bread as defined in Regulation 1 of the Regulations in terms of Government Notice No. ~~**R. 577**~~ **R405** published in Government Gazette No. ~~**13074 of 15 March 1991**~~ **40828 of 5 May 2017**

Figure 49. Government Notice 1451 of 2017 in Government Gazette No. 41342 on 18 December 2017 (Act No 17 of 2017). Source: https://www.sabinet.co.za/

9. Government Notice 18 of 2019 in Government Gazette No. 42171 on 17 January 2019 (Act No 21 of 2018)

Schedule 2 Part B - Zero Rate: Supply of Goods consisting of Certain Foodstuffs	
Item 20	Cake wheat flour as defined in Regulation 1 of the Regulations in terms of Government Notice No. R.405 published in Government Gazette No. 40828 of 5 May 2017.
Item 21	White bread wheat flour as defined in Regulation 1 of the Regulations in terms of Government Notice No. R.405 published in Government Gazette No. 40828 of 5 May 2017
Item 22	Sanitary towels (pads)

Figure 50. Government Notice 18 of 2019 in Government Gazette No. 42171 on 17 January 2019 (Act No 21 of 2018*).* Source: https://www.sabinet.co.za/

Annexure B

VAT Binding General Ruling ("BGR")				
No	**Title and description of issue.**	**Item**	**Zero-rated supplies**	**Standard-rated supplies**
26[443]	**<u>The VAT treatment of the supply and importation of herbs.</u>** The term 'vegetable' is not defined in the VAT Act. The BGR provides guidance on whether herbs are vegetables for the purposes of item 12. According to BGR 26, herbs are included in the meaning of 'vegetables'.	12	The supply of herbs that have not been cooked or treated in any manner except for the purpose of preserving such herbs in their natural state, is zero-rated under section 11(1)(j) read with Item 12. Fresh and frozen herbs sold in the following forms qualify for zero-rating: - Cut; - Diced; or - Shredded. Subject to the standard-rated supplies provisions, the zero-rating applies regardless of whether the herbs are sold individually (for example, a packet of curry leaves or a packet of angelica) or mixed with other vegetables (for example, mixed cucumber and parsley or mixed lettuce and fresh dill) provided all other vegetables are zero-rated.	The supply of herbs in the following instances is specifically excluded from Item 12 and is therefore subject to VAT at the rate of 14% under section 7(1)(a): (a) Cut, diced or shredded herbs, to which any other substance has been added (other than for the purpose of preserving such herbs in their natural state). (b) Minced or pureed herbs. (c) Fresh or frozen herbs that have been treated with an additive for the purpose of adding colour or flavour (for example, glucose, dextrose, sugar or salt). (d) Herbs supplied in the course of the furnishing or serving of any meal, refreshment, cooked or prepared food or any drink, so as to be ready for immediate consumption when supplied.

[443] South African Revenue Service (2015) '*Binding General Ruling (VAT) 26: The VAT treatment of the supply and importation of herbs'.* Issued on 12 March 2015. Accessed on 17 March 2019 at https://www.sars.gov.za/AllDocs/LegalDoclib/Rulings/LAPD-IntR-R-BGR-2015-01%20-%20BGR26%20VAT%20treatment%20of%20supply%20and%20importation%20of%20herbs.pdf.

33[444]	**<u>The VAT treatment of the supply and importation of vegetable oil.</u>** This BGR provides guidance on what is meant by the term 'vegetable oil'.	14	The supply of certain vegetable oil (excluding olive oil), is zero-rated under section 11(1)(j) read with Item 14, provided the vegetable oil is marketed and supplied for use in the process of cooking food. In order for the zero rate to apply, the oil must be a 'vegetable oil' that is marketed and supplied for use in the process of cooking food. There is no specific legislation that requires vegetable oil to be labelled as oil for use in the process of cooking food. As a result, vegetable oil that is normally displayed with other cooking oils will be regarded as being supplied and marketed for use in the process of cooking food.	The supply of vegetable oil in the following instances is excluded from Item 14 and is therefore subject to VAT at the rate of 14%: (a) Vegetable oil not marketed and supplied for use in the process of cooking food, for example, coconut oil displayed where toiletries are sold. (b) Olive oil. (c) Vegetable oil blends that contain olive oil. (d) Any vegetable oil to which a standard-rated item has been added, for example, canola oil and butter blend. (e) Any of the vegetable oils or blends marketed and supplied as salad dressing. (f) Any vegetable oil to which another vegetable, in its natural state or processed, is added for purposes of flavouring, that is, a whole garlic clove or chilli added to canola oil. (g) Vegetable oils supplied in the course of carrying out any agreement for the furnishing or serving of any meal, refreshment, cooked or prepared food, as the case may be, so as to be ready for immediate consumption when so supplied.
35[445]	**<u>The VAT treatment of the supply and importation of frozen potato products.</u>** This BGR provides guidance on which frozen potato products fall within the ambit of the zero-rating provisions.	12	The supply of the following frozen potato products is subject to VAT at the zero rate under section 11(1)(j) read with Item 12: (a) Potato products that are blanched in hot water, steam or oil for the purpose of preserving the product in its natural state. For purposes of this BGR, blanching of potato products in order to – (i) stop the action of enzymes that can cause loss of flavour, colour and texture;	The supply of the following frozen potato products is specifically excluded from Item 12 and is subject to VAT at the rate of 14% under section 7(1)(a), irrespective of whether such products have also been treated in the same manner as the products listed in the zero-rating provision: - Potato products that have been treated with an additive, excluding dextrose, for a purpose other than to preserve the potato product in its natural state, such as flavourings, sweeteners, spices and salt. - Potato products that are coated with a

[444] South African Revenue Service (2016) '*Binding General Ruling (VAT) 33: The VAT treatment of the supply and importation of vegetable oil'. Issued on 24 March 2016.* Accessed on 17 March 2019 at https://www.sars.gov.za/AllDocs/LegalDoclib/Rulings/LAPD-IntR-R-BGR-2016-04%20-%20BGR33%20The%20VAT%20treatment%20of%20the%20supply%20or%20importation%20of%20vegetable%20oil.pdf.
[445] South African Revenue Service (2016) '*Binding General Ruling (VAT) 35: The VAT treatment of the supply and importation of frozen potato products'.* Issued on 27 May 2016. Accessed on 17 March 2019 at https://www.sars.gov.za/AllDocs/LegalDoclib/Rulings/LAPD-IntR-R-BGR-2016-06%20-%20BGR35%20VAT%20treatment%20of%20the%20supply%20and%20importation%20of%20frozen%20potato%20products.pdf.

			(ii) make the potato product safer for the end-user from a microbiological aspect; (iii) brighten the colour and help to prevent the loss of the natural sugars and vitamins present in the potato product; (iv) soften the potato product and make it easier to pack; or (v) prepare the potato product for freezing, is regarded as being performed for the purpose of preserving the product in its natural state. (b) Potato products that have been treated with a preservative to prevent the potato product from naturally darkening.	layer of batter in order to increase the crispiness. - Formed potato products, such as hash browns and röstis.
38[446]	**<u>The VAT treatment of the supply and importation of vegetables and fruit.</u>** This BGR provides guidance on which vegetables and fruits fall within the ambit of the zero-rating provisions. This BGR replaces BGR 18 which provided guidance on the zero-rating of various types of dates.	12 & 13	The supply of vegetables and fruit that have not been cooked or treated in any manner except for the purpose of preserving such vegetables and fruit in their natural state, is zero-rated under section 11(1)(j) read with Item 12 and Item 13 respectively. Fresh and frozen vegetables and fruit supplied in the following manner are regarded as not having been "treated" as envisaged in the said Item numbers, and therefore qualify for zero-rating: - Cut (including vegetables and fruit cut into specific shapes); - Diced; - Sliced; - Shredded; - Crushed; - Minced; - Pureed; - Peeled; - De-pitted; or - Compressed. Subject to standard-rated supplies proviaions, the	Vegetables and fruit supplied in the following manner are specifically excluded from Items 12 and 13 respectively, and the supply of such vegetables and fruit is subject to VAT at the rate of 14% under section 7(1)(a): (a) Cut, diced, sliced or peeled vegetables or fruit to which any other substance has been added whether or not separately packed in the same container (other than for purposes of preserving the vegetables or fruit in their natural state). Examples are – (i) a sachet of spices added to sliced mushrooms; (ii) fruit juice added to sliced fruit or a mixture of vegetable and fruit; and (iii) salad dressing and/or cheese added to a green salad (for example, a mixture of slices of lettuce, cucumber and tomato). (b) Fresh or frozen vegetables and fruit that have been treated with an additive for the purpose of adding colour or flavour (for example, glucose, sugar or salt). (c) Dehydrated, dried, canned or bottled vegetables or fruit. (d) Vegetables or fruit smoothies or

[446] South African Revenue Service (2017) '*Binding General Ruling (VAT) 38: The VAT treatment of the supply and importation of vegetables and fruit'.* Issued on 23 January 2017. Accessed on 17 March 2019 at https://www.sars.gov.za/AllDocs/LegalDoclib/Rulings/LAPD-IntR-R-BGR-2017-01%20-%20BGR38%20The%20VAT%20treatment%20of%20the%20supply%20and%20importation%20of%20vegetables%20and%20fruit.pdf.

			aforementioned zero-rating applies regardless of whether the vegetables and fruit are sold individually (for example, a punnet of strawberries or a pocket of potatoes) or mixed (for example, mixed diced carrots and potatoes or mixed chopped strawberries and kiwi fruit). Frozen vegetables and fruit that have been blanched in hot water are regarded as having been "treated" for the purpose of preserving the vegetables and fruit in their natural state, and therefore, the supply of such frozen vegetables and fruit qualify for the zero rating. The supply of a mix or a combination of vegetables and fruit by a store or similar establishment, whether or not at the delicatessen section of the establishment, may be zero-rated unless the vegetables and fruit fall under the standard-rated supplies provisions.	juices, and any similar products. The supply of vegetables and fruit in the course of carrying out any agreement for the furnishing or serving of any meal, refreshment, cooked or prepared food or any drink, so as to be ready for immediate consumption when supplied, is subject to VAT at the rate of 14% under section 7(1)(a). The supply of vegetables and fruit by a restaurant or similar establishment, or in the course of providing catering services, is therefore subject to VAT at the rate of 14% under section 7(1)(a), irrespective of whether they fall under the zero-rating provisions.
49[447]	**Supply of and Importation of sanitary towels (pads).** This BGR sets out the general VAT treatment of the supply and importation of sanitary towels (pads) under Item 22.	22	The supply of sanitary towels (pads) under Item 22 is zero-rated under section 11(1)(j). A sanitary towel (pad) is a female hygiene product specifically designed to absorb menstrual or vaginal blood. Absorption is by means of a towel or pad, which may be scented, unscented, disposable or reusable. The following products fall under Item 22: - Menstrual pads (all types – for example, light, medium and heavy flow, mini, super, sports, overnight, wings and no wings); - Maternity pads designed for use in pre and post birth bleeding;	The following products do not fall under Item 22: - Tampons (all types, with or without an applicator); - Menstrual cups; - Feminine sanitary wipes; - Period or leak-proof underwear; and - Any incontinence towels or pads.

[447] South African Revenue Service (2019) '*Binding General Ruling (VAT) 49: Supply of and Importation of sanitary towels (pads)'.* Issued on 15 March 2019. Accessed on 17 March 2019 at https://www.sars.gov.za/AllDocs/LegalDoclib/Rulings/LAPD-IntR-R-BGR-2019-01%20-%20BGR49%20The%20supply%20and%20importation%20of%20sanitary%20towels%20(pads).pdf.

			and - Panty liners which are similar to menstrual pads and are lighter and thinner.	

Figure 51. List of Binding General Rulings that provide guidance on items zero-rated or standard compiled from the relevant BGRs available on the SARS website. Source: www.sars.gov.za

Annexure C

Regional Economic Community ("REC") Member States in Africa

1. The Southern African Development Community ("SADC")

	Member States
1	Angola
2	Botswana
3	Democratic Republic of Congo
4	Lesotho
5	Madagascar
6	Malawi
7	Mauritius
8	Mozambique
9	Namibia
10	Seychelles
11	South Africa
12	Swaziland
13	Tanzania
14	Zambia
15	Zimbabwe

Figure 52. List of the SADC member states. Source: The South African Development Community website - https://www.sadc.int/

2. The East African Community (“EAC”)

	Partner States
1	Burundi
2	Kenya
3	Rwanda
4	South Sudan
5	Tanzania
6	Uganda

Figure 53. List of EAC member states. Source: East African Community website - https://www.eac.int/

3. Economic Community of Central African States (“ECCAS”) Communauté Economique et Monétaire de l’Afrique Central (“CEMAC”)

	Member States
1	Angola (ECCAS only)
2	Burundi (ECCAS only)
3	Cameroon (ECCAS & CEMAC)
4	Central African Republic (ECCAS & CEMAC)
5	Congo (ECCAS & CEMAC)
6	Gabon (ECCAS & CEMAC)
7	Equatorial Guinea (ECCAS & CEMAC)
8	Chad (ECCAS & CEMAC)
9	Democratic Republic of Congo (ECCAS only)
10	Sao Tome and Principle (ECCAS only)
11	Rwanda (ECCAS only)

Figure 54. List of ECCAS and CEMAC member states. Source: Communauté Economique et Monétaire de l'Afrique Central website - http://www.cemac.int

4. Economic Community of West African States ("ECOWAS")

	Member States
1	Benin
2	Burkina Faso
3	Cabo Verde
4	Cote D'Ivoire
5	The Gambia
6	Ghana
7	Guinea
8	Guinea Bissau
9	Liberia
10	Mali
11	Niger
12	Nigeria
13	Senegal
14	Sierra Leone
15	Togo

Figure 55. List of ECOWAS member states. Source: Economic Community of West African States website - https://www.ecowas.int/member-states/

5. Arab Maghreb Union (“UMA”)

	Member States
1	Algeria
2	Libya
3	Mauritania
4	Morocco
5	Tunisia

Figure 56. List of UMA member states. Source: United Nations Economic Commission for Africa website - https://www.uneca.org/oria/pages/amu-arab-maghreb-union

6. Intergovernmental Authority on Development (“IGAD’)

	Member States
1	Djibouti
2	Eritrea

3	Ethiopia
4	Kenya
5	South Sudan
6	Sudan
7	Somalia
8	Uganda

Figure 57. List of IGAD member states. Source: Intergovernmental Authority on Development website - https://igad.int/about-us/the-igad-region

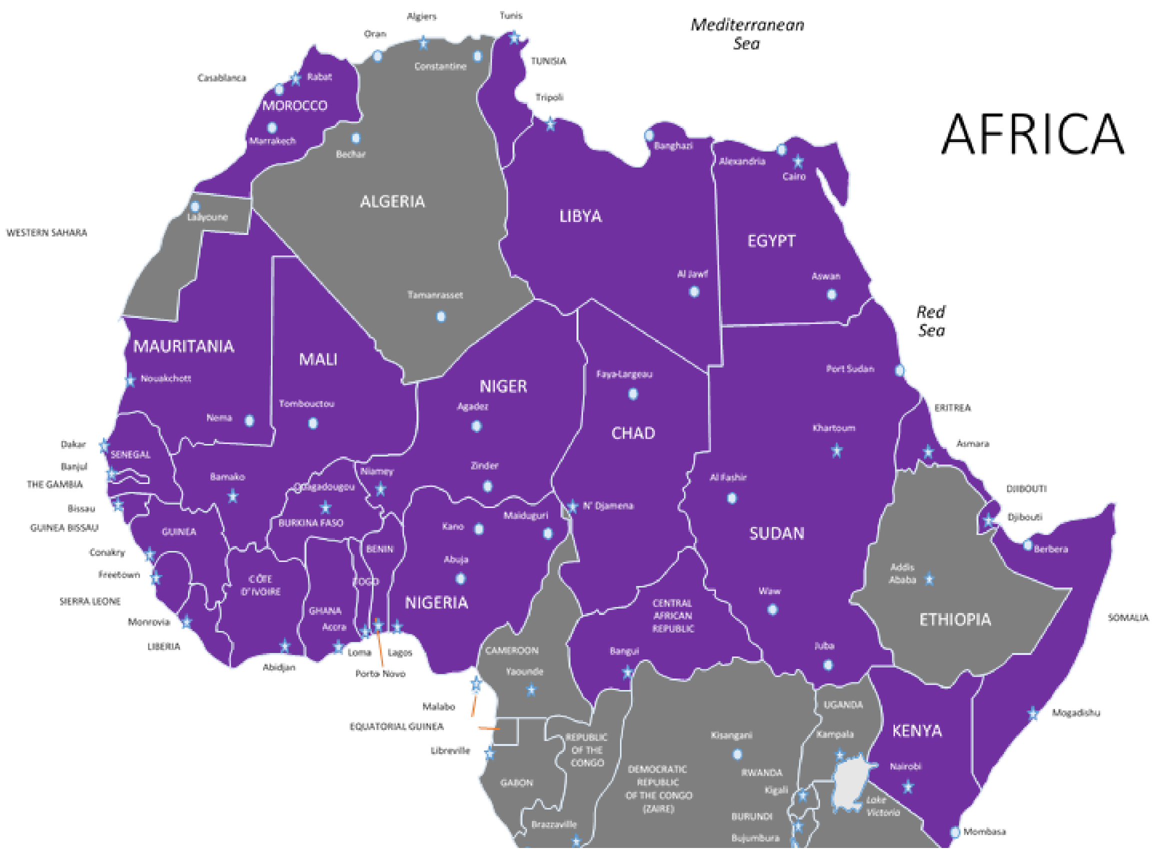
7. Common Market for Eastern and Southern Africa ("COMESA")

	Member States
1	Burundi
2	Comoros
3	Democratic Republic of Congo
4	Djibouti
5	Egypt
6	Swaziland
7	Eritrea
8	Ethiopia
9	Kenya
10	Libya
11	Madagascar

12	Malawi
13	Mauritius
14	Rwanda
15	Seychelles
16	Somalia
17	Sudan
18	Tunisia
19	Uganda
20	Zambia
21	Zimbabwe

Figure 58. List of COMESA member states. Source: COMESA website - https://www.comesa.int/comesa-members-states/

8. Community of Sahel–Saharan States ("CEN-SAD")



	Member States
1	Burkina Faso
2	Chad
3	Libya
4	Mali
5	Niger
6	Sudan
7	Central African Republic
8	Eritrea
9	Djibouti
10	Gambia

11	Senegal
12	Egypt
13	Morocco
14	Nigeria
15	Somalia
16	Tunisia
17	Benin
18	Togo
19	Ivory Coast
20	Guinea-Bissau
21	Liberia
22	Ghana
23	Sierra Leone
24	Comoros
25	Guinea
26	Kenya
27	Sao Tome and Principe
28	Mauritania
29	Cape Verde

Figure 59. List of CENSAD member states. Source: The AU website - https://au.int/en/recs/censad