

## **BINDING GENERAL RULING (VAT) 39 (Issue 2)**

DATE: 26 July 2018

**ACT : VALUE-ADDED TAX ACT 89 OF 1991**

**SECTION : SECTION 8(28)**

**SUBJECT : VAT TREATMENT OF MUNICIPALITIES AFFECTED BY CHANGES TO MUNICIPAL BOUNDARIES**

### ***Preamble***

For the purposes of this ruling, unless the context indicates otherwise –

- **“BGR”** means a binding general ruling issued under section 89 of the Tax Administration Act 28 of 2011;
- **“existing municipality”** means a municipality in the form in which it existed before any municipal boundary change;
- **“municipal boundary change”** means any change or re-determination of municipal boundaries from the effective date published by way of a Notice in a Provincial *Government Gazette* under section 12 of the Local Government: Municipal Structures Act 117 of 1998;
- **“Structures Act”** means the Local Government: Municipal Structures Act 117 of 1998;
- **“superseding municipality”** means a municipality into which an existing municipality or part thereof is merged, or a new municipality that has been created to supersede an existing municipality or municipalities, or parts thereof as a result of a municipal boundary change;
- **“VAT”** means value-added tax;
- **“VAT Act”** means the Value-Added Tax Act 89 of 1991; and
- any other word or expression bears the meaning ascribed to it in the VAT Act.

### **1. Purpose**

This BGR –

- explains the VAT treatment of the transfer of any assets, liabilities, rights and obligations pursuant to the merger, creation and disestablishment of municipalities as a result of any municipal boundary change as contemplated under section 8(28);<sup>1</sup> and

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<sup>1</sup> Read together with section 31 of the Local Government: Municipal Demarcation Act 27 of 1998 and sections 12 and 14 of the Local Government: Municipal Structures Act 117 of 1998.

- withdraws the first issue of BGR 39 dated 27 January 2017 with effect from 1 April 2018.

## 2. Background

From time-to-time the Municipal Demarcation Board may consider applications to change municipal boundaries under the Structures Act.

The municipal boundary changes, which affect so-called “existing municipalities”, are dealt with under section 31 of the Local Government: Municipal Demarcation Act 27 of 1998. In terms of that Act, the legal, practical and other consequences resulting from the area of a municipality being wholly or partially incorporated in or combined with the area of another municipality must be dealt with under the Structures Act.

Section 14 of the Structures Act regulates the effects of the establishment of a municipality on existing municipalities and provides, amongst others, that –

- a municipality established under section 12 of the Structures Act supersedes the existing municipality or municipalities to the extent that the existing municipality or municipalities fall within that area;
- the superseding municipality becomes the successor in law of the existing municipality (subject to certain provisions dealing with the sharing of functions between local municipalities and district municipalities); and
- the notice required under section 12 of the Structures Act must contain certain information about the disestablishment as well as the various aspects relating, for example, to staff matters and the transfer of administrative records, assets, liabilities, rights and obligations from the existing municipality to the superseding municipality or municipalities.

As the VAT Act did not previously have a comparable provision to section 14 of the Structures Act, which deals with the potential supplies of goods or services that may occur as a result of any municipal boundary change, the first issue of BGR 39 was issued on the basis of an arrangement under section 72 to deal with such matters. The VAT Act was subsequently amended<sup>2</sup> by the insertion of section 8(28), rendering the arrangement under section 72 redundant. However, as there is still a need to explain the application of section 8(28), this BGR has been amended accordingly.

## 3. Ruling

- 3.1 In the case of the transfer of all assets, liabilities, rights and obligations of an existing municipality (transferor) to a superseding municipality (transferee) as a result of a municipal boundary change, such municipalities are deemed to be one and the same person for the purposes of section 8(28), provided that such municipalities are merged into a single municipality.
- 3.2 In the case of the transfer of only some of the assets, liabilities, rights and obligations as a result of the municipal boundary change, where the municipalities concerned continue to exist as separate persons, then the existing municipality (transferor) is deemed not to have made a supply to the superseding municipality (transferee) in that regard.

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<sup>2</sup> Amended by section 78(1)(b) of Act No. 17 of 2017 with effect from 1 April 2018.

3.3 The effect of the ruling in **3.1** and **3.2** is that as at the effective date of the municipal boundary change –

- no supply of any goods or services is made by the existing municipality for the purposes of section 7(1)(a), and consequently, there will be no output tax payable by the existing municipality under section 16(4);
- no goods or services are acquired by the superseding municipality from the existing municipality, and consequently, no input tax deduction will be allowed under section 16(3) to the superseding municipality;
- no change of use adjustments under section 18 will be allowed to, or required by, either the existing municipality or the superseding municipality;
- an output tax or input tax adjustment may be required as contemplated in section 15(5) in a case where the existing and superseding municipalities do not account for VAT on the same accounting basis;
- the provisions of section 8(2) will not apply to the existing municipality upon its disestablishment and subsequent deregistration for VAT purposes unless any goods or rights capable of assignment, cession or surrender are not transferred to the superseding municipality as a result of the municipal boundary change, in which case, section 8(2) shall only apply to that extent;
- for the purposes of sections 16(2), 16(3), 17(1), 20 and 21, any valid tax invoice, debit or credit note or other prescribed document that has been issued in the name of the existing municipality, may be used as acceptable documentary proof for the purposes of deducting input tax or other allowable deduction in the name of the superseding municipality for a period of six months after the effective date of the municipal boundary change, provided such deduction has not previously been allowed to the existing municipality;
- for the purposes of calculating the superseding municipality's apportionment percentage as prescribed by section 17(1) and the related annual adjustment, symbols (a), (b) and (c) in the Formula in BGR 4 (Issue 3) shall be the aggregate of the values of those symbols for the existing and superseding municipalities for the financial year concerned;<sup>3</sup> and
- as a superseding municipality becomes the successor in law of the existing municipality in the event of a complete merger, the superseding municipality is liable to account to SARS for any VAT liability or outstanding VAT returns in relation to the activities of the existing municipality that arose before the effective date of the municipal boundary change.

This ruling constitutes a BGR issued under section 89 of the Tax Administration Act 28 of 2011.

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<sup>3</sup> This rule applies only in the case where the existing municipality is taken over in its entirety by the superseding municipality.

**4. Period for which this ruling is valid**

This BGR applies with effect from 1 April 2018 and shall remain in force until it is withdrawn, amended or the relevant legislation is amended.

To the extent that this BGR does not provide for a specific scenario in respect of the municipal boundary changes contemplated in this document, vendors may apply for a VAT ruling or VAT class ruling in writing by sending an e-mail to **VATRulings@sars.gov.za** or by facsimile to 086 540 9390. In this regard a clearly motivated application complying with the provisions of section 79 of the Tax Administration Act 28 of 2011 excluding section 79(4)(f) and (k) and (6), must be submitted.

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