



# PROVINCIAL TREASURY

Provincial Government of the Western Cape

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THE HEAD: BRANCH GOVERNANCE AND ASSET MANAGEMENT (MR TC ARENDSE)  
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THE PROVINCIAL AUDITOR

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THE HEAD OF DEPARTMENT: LOCAL GOVERNMENT

THE CHIEF DIRECTOR: LOCAL GOVERNMENT BUDGET ANALYSIS - NATIONAL TREASURY (MR J HATTINGH)

# CLARITY ON THE TREATMENT OF VAT ON GRANTS BASED ON THE VAT 419 GUIDE TO MUNICIPALITIES

## 1. Purpose

- 1.1 The purpose of this circular is to provide clarity to municipalities on the VAT treatment of grants based on the VAT 419 guide to municipalities.

## 2. Background

- 2.1 Prior to 1 April 2005, the term grant was not defined in the VAT act instead; the VAT legislation referred to, and defined the term transfer payment.
- 2.2 One of the main issues faced by municipalities was that the appropriations made to them by government under the annual Division of Revenue Act for example, equitable share grants, did not comply with the definition of transfer payment. Therefore these receipts did not qualify as a zero rated supply under section 11(2)(p) of the VAT act as it read at the time. This created a problem in that, public authorities and municipalities were generally under the impression that such payments qualified to be zero rated and did not budget for the VAT, which should have been included at the standard rate.
- 2.3 Amendments was therefore introduced to the VAT Act and the amendments included amongst others the following:
- The definition of transfer payment was replaced with the definition of a grant. The definition of a grant included in its meaning any appropriations made by government under the annual Division of revenue act.
  - The deeming provisions of section 8(5) of the VAT act were amended to now only apply to a designated entity.
  - The zero rating provision under section 11(2)(p) was replaced with section 11(2)(t) of the VAT act. This new provision allowed the deemed supply under section 8(5A) of the VAT act in respect of grants made to municipalities as well as grants made by municipalities to be zero-rated.
- 2.4 After careful consideration of amongst other the above, South African Revenue Services (SARS) issued the Value-Added Tax Guide - **VAT 419 – Guide for Municipalities** dated 31 October 2008, which relates to the application of the Value-Added Tax (VAT) law in respect of municipalities.
- 2.5 The main purpose of this guide is to provide guidance and clarity on the VAT treatment of supplies made by municipalities from 1 July 2006.

### **3. Discussion**

- 3.1 An extract from the VAT 419 Guide, ...."A grant is a means of assistance from the State or a municipality being a gratuitous or unrequited payment by the grantor, where no exchange is expected in the form of a supply of goods or services of corresponding value. Where the recipient is required to perform minor actions in regard to the grant, such as providing the grantor with a report or information on how the grant funds were spent, those actions are not regarded as constituting an actual taxable supply of services by the grantee to the grantor in terms of section 7(1) (a) of the VAT Act."
- 3.2 Grants can be either grants made for taxable supplies or grants made for exempt supplies.
- 3.3 Grants received for the purposes of making taxable supplies are zero rated supplies. A grant is subject to VAT at a zero rate only where the municipality has not actually supplied any goods or services to the public authority, municipality or constitutional institution making the payment. Where there is an actual supply of goods or services by the municipality, the supply will be subject to Vat at the standard rate.
- 3.4 Where a grant is received by a municipality from a public authority, constitutional institution, or another municipality, the receipt gives rise to a deemed supply of services in terms of section 8(5A) of the VAT Act. This deemed supply is zero-rated in terms of section 11(2) (t) of the VAT Act, provided that the grant is for the purpose of assisting the municipality to make taxable supplies of goods or services in the course of its enterprise.
- 3.5 If a grant is received for the purposes of exempt or other non-taxable purposes, the municipality will not be entitled to claim any input tax in respect of any goods or services acquired in this regard.
- 3.6 A grant must be attributed and declared on the VAT 201 return according to whether it relates to taxable, exempt or other non-taxable supplies. Where the grant is for both taxable and non-taxable purposes, the receipt must be attributed accordingly. For example, if 30% of a grant is for subsidizing the municipality's public transport business (exempt supply) and 70% is for subsidising the supply of water and electricity to customers (taxable supplies), 30% of the grant will not be taxable, and the other 70% will be subject to VAT at the zero rate.

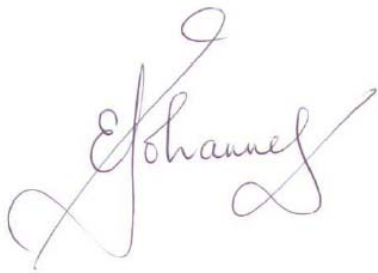
### **4. Way forward**

- 4.1 The VAT 419 guide should be used as guidance only as it does not constitute a general rule and is based on the VAT legislation as at 31 October 2008.
- 4.2 For detailed information on the VAT treatment of grants it is advised to refer to Interpretation Note No. 39 – VAT Treatment of Public Authorities, Grants and Transfer Payments which is available on the SARS website: [www.sars.gov.za](http://www.sars.gov.za).

4.3 If you have any further enquiries, please do not hesitate to contact the relevant officials at the National and Provincial Treasuries:

<b>National Treasury:</b>	<b>Provincial Treasury:</b>
1. Mr Sello Mashaba Tel: 012 – 315 5183 E-mail: <a href="mailto:Sello.Mashaba@treasury.gov.za">Sello.Mashaba@treasury.gov.za</a>	1. Mr Elton Johannes Tel: 021 – 483 4229 E-mail: <a href="mailto:mfma@pgwc.gov.za">mfma@pgwc.gov.za</a>
2. Mrs Kavitha Ruplal Tel: 012 – 315 5700 E-mail: <a href="mailto:Kavitha.Ruplal@treasury.gov.za">Kavitha.Ruplal@treasury.gov.za</a>	2. Mr Msimelelo Slgabi Tel: 021 – 483 4101 E-mail: <a href="mailto:mfma@pgwc.gov.za">mfma@pgwc.gov.za</a>

Yours faithfully



**MR EJ JOHANNES**

**ACTING SENIOR MANAGER: LOCAL GOVERNMENT FINANCE**

**DATE:** 23 AUGUST 2010