

https://dspace.org/

The output value-added tax implications for South African vendors of purchases made by means of loyalty points

Maluleke, Mikateko

2018
https://hdl.handle.net/10539/27818

Downloaded from a DSpace repository. https://dspace.org/

SCHOOL OF ACCOUNTANCY

University of the Witwatersrand, Johannesburg

A research report submitted to the Faculty of Commerce, Law and Management in partial fulfilment of the requirements for the degree of Master of Commerce in the field of Taxation

The output Value-Added Tax implications for South African vendors of purchases made by means of loyalty points

Mikateko Maluleke

345878

.

Abstract

The use of loyalty programmes has in recent years become popular in South Africa. There has, however, been only one public document that has been issued by the South African Revenue Service ('SARS') which discusses the Value-Added Tax ('VAT') treatment of loyalty programmes that was published in August 2014.[1] Only one ruling has been issued to particular taxpayer on this subject.[2] Therefore, there is little guidance on this subject in South Africa. This report seeks to examine the VAT implications (specifically the VAT output implications) of loyalty programmes for VAT vendors who participate in South Africa's loyalty programmes. The report will explore some of the types of available loyalty programmes and explore the definition of 'consideration' as well as how other jurisdictions treat VAT output on loyalty programmes.

Key words: Value-Added Tax, loyalty programmes, consideration, VAT Vendor, South African Revenue Service (SARS), South Africa, output tax

1SARS, 2014:1, Discussion paper of the VAT treatment of Loyalty Programmes , (http://www.sars.gov.za/AllDocs/LegalDoclib/DiscPapers/LAPD-LPrep-DP-2014-01%20-%20Discussion%20Paper%20on%20VAT%20Treatment%20of%20Loyalty%20Programmes.pdf, (accessed 2017-03-25)

[2]SARS, BCR 055, (http://www.sars.gov.za/AllDocs/LegalDoclib/Rulings/LAPD-IntR-R-BCR-2016-07%20-%20BCR055%20Income%20tax%20and%20VAT%20consequences%20of%20a%20customer%20loyalty%20scheme.pdf) (accessed 2017-04-25). SARS gave a ruling on the Income Tax and Value-added Tax consequences of a loyalty scheme.

Declaration

I declare that this research report is my own unaided work. It is submitted for the degree of the Master of Commerce at the University of Witwatersrand, Johannesburg. It has not been submitted before for any other degree or examination at any other university.

_____

Mikateko Maluleke

Dedication

To the creator of heaven and the God I believe in, thank you for the strength you have given me to take on this project. To my family, va N'wnati, thank you for instilling in me the love for education at a very young age and for setting an example for me, I love you all. Sincere gratitude goes out especially to my brother Musa, thank you for always taking interest in this particular project and for always reminding me that I need to submit my research report. To my fiancé Jameson Mawila, thank you for all your support, for believing in me and for your constant encouragement, you have been such an awesome gladiator, I love you.

Acknowledgement

To Professor Alwyn de Koker and Roy Blumenthal, thank you for accepting me into the Tax Masters programme and for all the insightful information that has been provided to me in the form of guides and examples. Furthermore, thank you for arranging a dedicated lecture focusing on the writing of a research report. All your help and guidance is deeply appreciated.

Table of Contents

Abstract ..... **i**

Declaration ..... **ii**

Dedication ..... **iii**

Acknowledgement ..... **iv**

Table of Contents ..... **v**

List of Figures ..... **vi**

Chapter 1: Introduction **1**

1.1 The research problem 3
1.1.1 Statement of the problem 3
1.1.2 Sub-problems (Research questions) 5
1.2 Research methodology 6
1.3 Scope and limitation of the research report 6
1.4 Chapter outline 7

Chapter 2: Different loyalty programmes available in South Africa **8**

2.1 SARS Discussion Paper 8
2.2 Top six loyalty programmes in South Africa 11

Chapter 3: The definition of consideration for VAT purposes **22**

Chapter 4: Accounting for Output VAT by various vendors **28**

Chapter 5: Comparison to the current South African legislation on the VAT treatment of vouchers **38**

Chapter 6: International guidance **42**

6.1 The European Commission- Directorate for General Taxation and Customs Union 42
6.2 Economic Co-operation and Development (OECD) 44
6.3 Australia 46
6.3.1 GSTR 2012/1 47
6.4 New Zealand 49
6.4.1 Interpretation Statement 49
6.4.2 Technical Alert: Amendment to legislation 50

Chapter 7: Conclusion **53**

References **56**

List of Figures

Image 1. 1: Pick n Pay receipt 29
Image 1. 2: Clicks customer receipt 32
Image 1. 3: Edgars customer receipt 34
Image 1. 4: Dis-Chem customer receipt 35

Chapter 1: Introduction

According to CNBC Africa[3], the use of loyalty programmes is fast becoming popular in a variety of South African industries that include pharmaceutical stores, retailers, clothing and department stores.

Furthermore, merchants are realising that it yields good results to invest in consumer relationships. Over the last 20 years, loyalty programs have become prevalent publicity tools that companies use to collect information, ensure customer loyalty and to strengthen relationships.[4]

South African retailers have an issue of not offering differentiated products and little to low switching costs between them, loyalty programmes have therefore emerged as a vital means for customer retention and for forging sustainable customer loyalty through improved relationships.[5]

Brink[6] defined a client loyalty programme as one where eligible purchases by customers can enable customers to collect free points or miles based on the purchases of goods or services from a vendor. Upon accumulation of the points the customer is able to use the points for a variety of products including goods, services or a rebate on a next purchase transaction from the vendor. This is however, not an exhaustive definition of a loyalty programme as some rewards programmes such as the Absa one offers customers actual cashback.[7]

The loyalty programmes' primary objective is usually to gain a sale or market share.[8] Although the primary objective of most loyalty programmes is to attract and retain customers and to gain market share, it also brings about uncertainties relating to the VAT treatment of these loyalty programmes. This was highlighted in the SARS discussion

[3] CNBC Africa, 2016, (https://www.cnbcafrica.com/news/southern-africa/2016/07/15/retailing-in-south-africa-do-customer-loyalty-programs-really-work/) (accessed 2017-12-01).
[4] CNBC Africa, 2016, (https://www.cnbcafrica.com/news/southern-africa/2016/07/15/retailing-in-south-africa-do-customer-loyalty-programs-really-work/) (accessed 2017-12-01).
[5] CNBC Africa, 2016, (https://www.cnbcafrica.com/news/southern-africa/2016/07/15/retailing-in-south-africa-do-customer-loyalty-programs-really-work/) (accessed 2017-12-01).
[6] Brink 2013:796, The accounting treatment of single-company client loyalty programme', *Journal of Economic and Financial Sciences*, Vol. 6, no. 3, pp. 795-814.
[7] Absa cashback programme, (https://www.absa.co.za/personal/bank/absa-rewards/explore/) (accessed 01-20-2018).
[8] Sharp & Sharp, 1997:474, 'Loyalty Programs and their impact on repeat purchase loyalty patterns', *Journal of Research in Marketing*, Vol. 14, pp. 476-486.

paper, where the discussion paper intended amongst other things to list, identify and highlighted the current difficulties that are being experienced, in applying the provisions of the VAT Act.[9]

There has been no reported VAT court case in South Africa dealing with loyalty programmes. In terms of the Loyalty Whitepaper, the loyalty landscape in South Africa has grown exponentially over the past ten years, with accelerated activity within the last three to five years. It was estimated that in 2016, there were over 100 loyalty programmes in South Africa.[10]

Regardless of the increase in the popularity of loyalty programmes in South Africa, SARS has only issued two documents that relate to the programme, one being a discussion paper which acts as a guide for the VAT treatment of loyalty programmes as well as the Binding Class Ruling 055[11] on the income tax and value-added tax consequences of a loyalty scheme.

Therefore, there is currently a lot of uncertainty with regards to the correct VAT treatment of loyalty programmes in the hands of the VAT vendor.
The objective of the SARS discussion paper was to:

> *Promote discussion between SARS and stakeholders with a view to*:
> - Identify and understand the current challenges experienced, if any, in applying the provisions of the VAT Act;
> - Identify areas in the VAT Act which may require amendments to address the difficulties identified, if any; and
> - Adopt a policy which will result in the consistent application of VAT principles for all loyalty programmes.

Furthermore, in BCR 055, the applicants (referred to as the Class Members) sought to implement a customer loyalty scheme to protect their existing customer base and possibly expand their businesses. The scheme would involve loyalty bonus allocations to customers conducting business with the Class Members. SARS ruled that the allocation of the bonuses is not 'consideration' as defined in section 1(1) of the Value-

[9] SARS, 2014:1, Discussion paper of the VAT treatment of Loyalty Programmes , (http://www.sars.gov.za/AllDocs/LegalDoclib/DiscPapers/LAPD-LPrep-DP-2014-01%20-%20Discussion%20Paper%20on%20VAT%20Treatment%20of%20Loyalty%20Programmes.pdf, (accessed 2017-03-25)
[10] Truth, The 2016 truth loyalty whitepaper, 'The current state of loyalty programmes in South Africa', 2016:8-10, (http://truth.co.za/wp-content/uploads/Truth-Whitepaper-October-2016.pdf) (accessed 2016-11-12).
[11] SARS, BCR 055, (http://www.sars.gov.za/AllDocs/LegalDoclib/Rulings/LAPD-IntR-R-BCR-2016-07%20-%20BCR055%20Income%20tax%20and%20VAT%20consequences%20of%20a%20customer%20loyalty%20scheme.pdf) (accessed 2017-04-25)

added Tax Act 89 of 1991 ('the VAT Act'), in respect of any supply of goods or services made by the participating customer and the Class Member may not deduct any amount as input tax in relation to it.[12]

It should be noted that a BCR is not authoritative and is applicable only to the entities included in the BCR.[13] The focus of this ruling was on whether there will be any VAT implications for the vendor on the bonus allocation and nothing on the VAT implication when these points are used by the customer to purchase goods or services.

Current literature on the subject (loyalty programmes in South Africa) focuses on the possibility of the consumer paying too much VAT by virtue of them being part of a loyalty programme.[14] Me burgh (2016) argues that, the consumer pays VAT on the original purchase (assuming that the consumer is purchasing vatable goods or services) to earn points and when the consumer utilises the points they still pay VAT on the purchase using the points, that is, if the consumer is buying vatable goods or service.[15]

Other literature focuses on the taxability of the loyalty points in the hands of the loyalty programme's participating customers. For example, Brits[16] argued that loyalty points should be included in a taxpayer's income because, when the customers receive or accumulate loyalty points, those points have an economic value hence the suggestion to include the points in a taxpayer income for income tax purpose.

1.1 The research problem

1.1.1 Statement of the problem

There is currently no authoritative VAT legislation governing the output VAT treatment of purchases made by means of points earned through a loyalty programme. This creates

[12]SARS, BCR 055, (http://www.sars.gov.za/AllDocs/LegalDoclib/Rulings/LAPD-IntR-R-BCR-2016-07%20-%20BCR055%20Income%20tax%20and%20VAT%20consequences%20of%20a%20customer%20loyalty%20scheme.pdf) (accessed 2017-04-25).
[13] SARS, BCR 055, (http://www.sars.gov.za/AllDocs/LegalDoclib/Rulings/LAPD-IntR-R-BCR-2016-07%20-%20BCR055%20Income%20tax%20and%20VAT%20consequences%20of%20a%20customer%20loyalty%20scheme.pdf) (accessed 2017-04-25).

[14] Meyburgh, 2016, (https://www.sablog.kpmg.co.za/2016/04/vat-and-loyalty-programmes/) (accessed 2017-03-25).
[15] Meyburgh, 2016, (https://www.sablog.kpmg.co.za/2016/04/vat-and-loyalty-programmes/) (accessed 2017-03-25).
[16] Brits, (2013:5), The Taxation of Interest Earned in Customer Loyalty Award Programmes in South Africa.
.

a problem for VAT vendors when applying the current VAT legislation to account for output tax on these transactions.

In the SARS Interpretation Note 70, it was stated that:

> Although VAT legislation is generally broad-based and embraces all types of commercial activities, it does not include all the activities of all the entities in the economy. This distinction is attained by the use of definitions or specific legislative provisions which modify the effect of the broad-based definitions which describe the activities or persons who are intended to fall within the tax base. [17]

Therefore, the main research question is how VAT vendors should account for output VAT on transactions made by means of loyalty points? Due to the fact that there is no authoritative VAT legislation governing the VAT treatment of loyalty programmes in South Africa, different stakeholders operating loyalty programmes interpret the VAT treatment of loyalty programmes differently. This was also alluded to in the SARS Discussion Paper on the VAT treatment of loyalty programmes.[18]

Additionally, the following was noted in the National Treasury Budget (2016):

> Section 10(18), (19) and (20) of the Value-Added Tax Act deals with how issuing and redeeming tokens, vouchers or stamps are to be treated for VAT. There are no similar provisions in the act to deal with loyalty programmes and the VAT implications of redeeming loyalty points. It is proposed that loyalty programmes be analysed and legislative amendments be considered to provide clarity on their VAT treatment. The provisions relating to vouchers will also be reviewed to determine if they require amendments.

The above is from the 2016 Budget Review, where National Treasury announced that:

> The VAT treatment of loyalty programmes and the provisions relating to vouchers will be reviewed. This article looks at some of the more complicated aspects related to the implementation of VAT on loyalty programmes that ought to be considered as part of this review.

Brink[19] also concludes in the paper on the evaluation of the income tax treatment of loyalty programme transaction by South African suppliers that, there are gaps in the interpretation and application of the Income Tax Act in respect to client loyalty programme transactions. The author further noted that, there is also a lack of guidance from SARS

---

[17] SARS, Interpretation Note 70, purchases for no consideration, (2013:5) (http://www.sars.gov.za/Legal/Interpretation-Rulings/Interpretation-Notes/Pages/Numbers-61-80.aspx) (accessed 2017-09-12).

[18] SARS, 2014:1, Discussion paper of the VAT treatment of Loyalty Programmes, (http://www.sars.gov.za/AllDocs/LegalDoclib/DiscPapers/LAPD-LPrep-DP-2014-01%20-%20Discussion%20Paper%20on%20VAT%20Treatment%20of%20Loyalty%20Programmes.pdf, (accessed 2017-03-25).

[19] Brink, 2014:162, An evaluation of the Income Tax treatment of client loyalty programmes, *Journal of Economic and Financial Sciences*, Vol. 8, no. 1, pp. 145-164.

regarding the tax treatment of client loyalty programme transactions that requires serious attention.

Although the above mentioned research is related to the income tax deductibility relating to loyalty programmes, it is worth noting that the same gap exists when it comes to the VAT treatment of loyalty programmes.

In order for VAT output to be charged, there has to have been a supply made by a vendor in the furtherance of the vendor's enterprise for a consideration as defined[20]. Kruger *et al* (1992: §2.4) further stated in Juta's Value-Added Tax Manual stated that unless a charge is raised for supplied goods or services, they will not form part of the carrying on of an enterprise as defined below.

An 'enterprise' is defined in section 1(1) of the VAT Act as –

> The carrying on of continuous or regular activity in the Republic in the course or furtherance of which goods or services are supplied to any other person for consideration. (Emphasis added).

As it currently stands, the definition of consideration in relation to purchases made using 'points' earned through a loyalty programme is still uncertain as it is not accounted for in the VAT Act. Accordingly, the primary focus of this research report will be to explore the definition of consideration in the context of loyalty programmes (that is whether consideration can be interpreted to include 'payment' in the form of loyalty points).The report will therefore, attempt to establish the VAT output tax consequences for the VAT vendor of purchases made using loyalty programmes. The report will also suggest legislative changes where necessary to address the highlighted uncertainties.

1.1.2 Sub-problems (Research questions)

The report will attempt to answer the following questions:

- Do loyalty points that are used to purchase goods or services constitute consideration as defined in section 1(1) of the VAT Act?
- What differing interpretations of what is considered consideration for VAT purposes exist among loyalty programme providers/operators in South Africa? and

[20] . Kruger *et al,* (1992: §2.4) in Juta's Value-Added Tax Manual

- Is there a need to develop a policy or amend the existing provisions in the current VAT Act in order to mitigate against any challenges experienced by stakeholders in applying the VAT Act relating to loyalty programme transactions?

1.2 Research methodology

As highlighted in the SARS (2014) discussion paper on the VAT treatment of loyalty programmes, there is a range of different loyalty programmes that are currently available in the South African market and stakeholders operating loyalty programmes interpret and apply the relevant provisions in the VAT Act differently. [1]

Various South African and international authors that include but are not limited to Brink, (2013) Lee and Sharp have written extensively on the VAT treatment of loyalty programmes. A literature review of the fore mentioned authors as well as writings from SARS, National Treasury, and the South African Institute of Tax Professionals (SAIT) were examined to try and establish the principles to be applied in interpreting the VAT legislation in relation to accounting for output VAT on goods and/or services paid for by means of loyalty points.

1.3 Scope and limitation of the research report

This study will focus on the VAT output tax implications of loyalty points used to purchase goods and/or services. The study will aim to look at the top six loyalty programmes in South Africa in respect of the number of users on the loyalty programmes, as set out in the Truth 2017 Loyalty. Each of these programmes will be described in detail, setting out their terms and conditions as well as investigating how a transaction is treated when points are redeemed for goods and/or services.

This will be done by visiting some of the participating stores and making a purchase utilising accumulated loyalty points. This will assist in getting an idea on how the VAT on these purchases in accounted for on the customer receipt that will be issued after the purchase, The treatment will then be contrasted with what has been written on the treatment of loyalty programmes in order to establish if there is a need to amend the current VAT legislation or at least provide additional guidance to VAT vendors regarding the treatment of VAT on loyalty programmes.

The research report will also look at available international guidance on the VAT treatment of loyalty programmes. Guidance from different jurisdictions namely, New

Zealand and Australia will be explored to assist in attempting to answer the research question. The reason for choosing these jurisdictions is due to the similarities in the VAT legislation between South Africa and these jurisdictions.

This research report will not look at the input tax deductibility of any expenses incurred by the VAT vendors in awarding or dispensing the points to participants as well as any other costs related to the running and functioning of the loyalty programmes. The focus of this research report will be on the points allocated to loyalty programme members through an eligible purchase of goods or services; it will not focus on the points where members pay an extra fee for additional points to be allocated to them. The research paper will also mainly focus on exclusive programmes which are usually administered in-house without the involvement of any other third party except the customers. Furthermore, this research report will not look at the income tax implications of loyalty programmes.

1.4 Chapter outline

Chapter 2 will explore the top six loyalty programmes (in respect of the number of users on the loyalty programmes) available in South Africa as well as their various terms and conditions. Chapter 3 will examine the definition of ‘consideration’ using legislation and commentary. Chapter 4 will look at how various loyalty programme operators account for VAT output on purchases made using loyalty points. Chapter 5 will look at current legislation that may be used to draw inferences from it to develop legislation to address the current legislation uncertainty regarding loyalty programmes. Chapter 6 will also look at developments in other foreign jurisdiction in relation to legislation and/or commentary on the topic at hand.

Chapter 2:

Different loyalty programmes available in South Africa

This chapter will focus on the SARS Discussion Paper on VAT, loyalty points as well as the various South African loyalty programmes, more focus will be on loyalty programmes that have an exclusive programme structure. An exclusive programme is defined in the SARS Discussion Paper as a loyalty programme which is typically managed internally and where the entity of concerned acts as the only participant to the loyalty programme.[21] The top six loyalty programmes mentioned in chapter 1 above are administered in house although in some cases the is not only one stake holder, however, they do have elements of exclusivity.

The Consumer Protection Act 68 of 2008 in Section 1(1) defines a 'loyalty programme' as –

> any arrangement or scheme in the ordinary course of business, in terms of which a supplier of goods or services, association of such suppliers, or other person on behalf of or in association with any such suppliers, offers or grants to a consumer any loyalty credit or award in connection with a transaction or an agreement.

2.1 SARS Discussion Paper

This subsection will focus on the 2014 SARS Discussion Paper which was issued for public comment.

The following definitions as set out in the discussion paper and they will be relevant in the context of this subsection:

- "**Customer**" means any person who buys goods or services from a vendor;
- "**Loyalty partner**" means the vendor selling eligible goods or services to a member on which loyalty points are earned by the said member;
- "**Loyalty programme**" means a loyalty programme, reward scheme or any other similar scheme or programme;
- "**Loyalty points**" include miles, loyalty card points or any other similar items which are allocated to a customer and can be redeemed in future by a customer for a reward, but excludes any item that satisfies the definition of a "voucher", "token" or "stamp";
- The **Loyalty Programme Operator** "**LPO**" is the administrator of the loyalty programme;
- "**Member**" means a customer who is a participant in a loyalty programme;
- "**Redemption partner**" means the vendor responsible for making supplies of goods or services to the member in exchange for loyalty points;
- "**Relevant parties to a loyalty programme**" means any participant in a loyalty programme and includes the member, LPO, loyalty partner and the redemption partner;
- "**Section**" means a section of the VAT Act;

[21] SARS, Discussion paper of the VAT treatment of Loyalty Programmes ,(2014:6) (http://www.sars.gov.za/AllDocs/LegalDoclib/Rulings/LAPD-IntR-R-BCR-2016-07%20-%20BCR055%20Income%20tax%20and%20VAT%20consequences%20of%20a%20customer%20loyalty%20scheme.pdf) (accessed 2017-03-25)

- "**Stakeholders**" mean the relevant parties in to a loyalty programme excluding the member; [21]

The SARS Discussion Paper referred to two types of loyalty programmes that is the exclusive programmes and the multi-party programme. It further stated that, the loyalty programmes presently operational in the South African market contain different variations of these two types of programme structures [21]

These two types of loyalty programmes that will be discussed in detail below are set out in the SARS Discussion Paper.

> ***The exclusive programme***
>
> *This refers to a loyalty programme which is usually administered in-house where the relevant entity (the LPO) acts as the only stakeholder to the loyalty programme. It is the responsibility of the LPO to keep record of the loyalty points earned and subsequently redeemed by each member.*
> *A customer becomes a member of the loyalty programme by entering into an agreement with the LPO. For purposes of this discussion document, this agreement will be referred to as the Membership Agreement.*
> *Loyalty points may be earned on specific goods or services acquired from the LPO (eligible purchases) usually as a result of the member being in possession of a card verifying its membership to the specific loyalty programme. The member may then redeem these loyalty points by offering the said points as payment (or part payment) for acquisitions of goods or services at the LPO* [21]

The transactions relating to an exclusive programme would go as follows; the loyalty programme member could in certain occurrences be expected to pay a membership fee to the LPO in order to take part in the specific loyalty programme; the loyalty programme member makes eligible purchases at the loyalty partner; the loyalty partner is responsible for the allocation of loyalty points to the member based on the eligible purchases made by the said member; the member redeems the loyalty points by offering the loyalty points as payment (or part payment) for the acquisition of goods or supplied. **Error! Bookmark not defined.**

The multiple party programme

A multiple party programme is more multifaceted due to the the fact that there are more stakeholders partaking in the programme. Management of the loyalty programme can either be done by a separate unit or by a stakeholder to the loyalty programme (the LPO). The LPO has the responsibility to maintain record of the loyalty points earned and consequently redeemed by each member. [22]

A participating consumer becomes a member of the loyalty programme by entering into a Membership Agreement with the LPO. A loyalty programmes can include various entities as partners to the programme. The loyalty programme agreement needs to clearly set out the roles and responsibilities of each partner. [22]

Each member becomes entitled to loyalty points determined by the number of purchases made on goods or services from the loyalty partner that considered eligible per the rules of the loyalty programme. The association between the LPO and the loyalty partner is normally administered by an agreement which will be referred to as the Participation Agreement.[22]

The transactions relating to a multiple party programme would go as follows;

- For a member to take part in some specific loyalty programmes, the member may in certain occurrences be obligated to pay a membership fee;
- When a member makes eligible purchases from the loyalty partner or presents a loyalty card at the loyalty partner the member becomes entitled to loyalty points on the purchase of the applicable goods and/or services;

Additionally:

- The LPO is accountable for allotting loyalty points to the member based on the member's acquisitions at the loyalty partner; transactions that occur between the loyalty partner and the LPO may include:
    - The loyalty partner compensates the LPO with a management or administration fee, this may be done at any interval could be weekly, monthly or annually, for the administration of the loyalty programme;
    - The loyalty partner reimburses the LPO an amount equivalent to the worth of the loyalty points allotted to members as a consequence of the members' purchases at the loyalty partner;
    - The member redeems the loyalty points by contributing it as tender (or part tender) for the purchase of goods or services at the redemption partner;[23]

The SARS Discussion Paper focuses on the multiple partner type of loyalty programme. As noted in the scope and limitations, this paper will focus on exclusive loyalty programmes.

[22] SARS, Discussion paper of the VAT treatment of Loyalty Programmes ,(2014:8) (http://www.sars.gov.za/AllDocs/LegalDoclib/Rulings/LAPD-IntR-R-BCR-2016-07%20-%20BCR055%20Income%20tax%20and%20VAT%20consequences%20of%20a%20customer%20loyalty%20scheme.pdf) (accessed 2017-03-25)
[23] SARS, Discussion paper of the VAT treatment of Loyalty Programmes ,(2014:9) (http://www.sars.gov.za/AllDocs/LegalDoclib/Rulings/LAPD-IntR-R-BCR-2016-07%20-%20BCR055%20Income%20tax%20and%20VAT%20consequences%20of%20a%20customer%20loyalty%20scheme.pdf) (accessed 2017-03-25)

2.2 Top six loyalty programmes in South Africa

Oosthuizen (2014)[24] highlights that the playing field for loyalty programmes in the country has shown high improvements in terms of growth in the last few years as there are over 70 loyalty programmes in South Africa with approximately 10 million consumers participating in one or more loyalty programmes.

Furthermore, the purpose of many loyalty programme establishments in South African is to boost repeat purchases. Financial institutions have also been seen to be taking a bite of the loyalty programme market, as customers become more acquainted as to how loyalty programmes work, how to use them to their best benefit and who their information is safe with as this information is shared when engaging with these loyalty programme entities.[24]

As far as marketing tools go, loyalty points are unbeatable, repeat customers get rewarded and business enjoys increased revenues and profits.[25] Furthermore, the company listed Pick n Pay's Smart Shopper, Woolworths' Rewards, Clicks Club Card, Dis-Chem's Benefit and Edgars' Thank U as the top five most effective retail loyalty programmes.[25] This was determined by looking at various unique features offered by these loyalty programmes for example, pick n Pay has a mobile app that allows consumers to monitor their points balance, Wrewards members received instant savings on their purchases and extra savings if they purchase environmentally friendly products, with Clicks Club Card, members are able to earn double points every second Wednesday of the month and with Dischem's Benefit, a member is able to earn and spend eBucks at Dischem.[25]

According to the Loyalty Whitepaper a survey conducted in 2015 showed that economically active South African consumers belong to an average of 4.6 loyalty programmes. The paper further states that, conventionally, loyalty programmes are mostly limited to airline frequent flyers, retail and financial services industries. The demand for loyalty however continues to grow across other sectors of the market, including health and wellness, leisure and even corporate social responsibility.[26]

---

[24] Oosthuizen (2014), (http://www.bizcommunity.com/Article/196/458/115433.html) (accessed 2018-01-20).
[25] Loyalty Box 2015, (http://www.theloyaltybox.com/) (accessed, 2018-01-18).

[26] Truth, 2016:8. The 2016 truth loyalty whitepaper. 'The current state of loyalty in South Africa', (http://truth.co.za/wp-content/uploads/Truth-Whitepaper-October-2016.pdf) (accessed 2016-11-12).

In terms of the Loyalty Whitepaper [27] there is good news for companies that currently have loyalty programmes, or those looking to enter the loyalty market, this is because overall loyalty usage in South Africa has increased by 8% from 2016 to 2017. This takes the new percentage of consumers using loyalty programmes, to be a significant 79%.[27]

This section will focus on the various loyalty programmes offered in South Africa. According to the Truth Report[26], the following are the top six most used loyalty programmes in South Africa:

- Pick n Pay Smart Shopper;
- Clicks Club Card
- Woolworths WRewards;
- Edgars Thank U;
- Dis-Chem Benefits and
- FNB eBucks

In terms of the survey conducted the per the 2016 Truth report, the survey shows that 68% of respondents belong to the Pick n Pay Smart Shopper programme. 59% belong to both the Edcon Thank U and Clicks Club card programmes with Woolworths WRewards placing 4th at 45%. Spur's Family Card is the only restaurant chain to make it onto the list with an impressive, 28% of respondents being a member of this programme. [28]

In 2016 Pick n Pay had 8.9 million member, Edgars Thank U with 12 million members, Clicks Club Card with 5 Million members and Woolworths WRewards with 3.1 Million member.[29]

[27] Truth, 2017:7. The 2017 truth loyalty whitepaper 'South African loyalty landscape', (http://truth.co.za/wp-content/uploads/Truth-Whitepaper-October-2017.pdf) (accessed 2018-03-23).
[28] Truth, 2016:10. . The 2016 truth loyalty whitepaper. 'The current state of loyalty in South Africa', (http://truth.co.za/wp-content/uploads/Truth-Whitepaper-October-2016.pdf) (accessed 2016-11-12).
[29] Truth, 2016:10, the 2016 truth loyalty whitepaper. 'The current state of loyalty in South Africa', (http://truth.co.za/wp-content/uploads/Truth-Whitepaper-October-2016.pdf) (accessed 2016-11-12).

According to the 2017 Truth report Clicks Club Card has overtaken Pick n Pay Smart Shopper as the most used loyalty programme in South Africa.[30]

CNBC Africa, reinforces the fact that the Pick n Pay Smart Shopper is one of the most popular loyalty programme points in South Africa.[31]

CNBC Africa states that in terms of existing assessments, Pick n Pay Smart Shopper is the largest supermarket rewards programmes in the country. The massive supermarket chain which is operational in most towns and cities across the country, operates one of the most popular (most used) loyalty programmes.[31]

The interesting shift according to the Truth 2017 Loyalty Whitepaper Survey is that the Clicks Club Card has passed the Pick n Pay Smart Shopper as the most utilised (meaning the highest number of members on the programme) loyalty programme in South Africa.[32] Other shifts that were observed comprise the drop of the Woolworths WRewards from the third most used loyalty programme in 2016 to being the fifth most used programme in 2017. Edgars Thank U Card and the Dis-Chem Benefits both have surpassed Woolworths and Dis-Chem has claimed its highest placed to date as the third most used loyalty programme in South Africa[33].

What does not change in the 2017 Loyalty Whitepaper is that the top six loyalty programme still remain although their position within the top six may have shifted. Another point to note is that in general, retail outlets still dominate the top six in 2017 and the only non-retail programme represented in the top six is the First National Bank's eBucks. It is the most used retail banking loyalty programme.

---

[30] Truth, 2017:11. The 2017 truth loyalty whitepaper 'South African loyalty landscape', (http://truth.co.za/wp-content/uploads/Truth-Whitepaper-October-2017.pdf) (accessed 2018-03-23).

[31] CNBC Africa, 2016, (https://www.cnbcafrica.com/news/southern-africa/2016/07/15/retailing-in-south-africa-do-customer-loyalty-programs-really-work/) (accessed 2017-12-01).

[32] Truth, 2017:13. The 2017 truth loyalty whitepaper 'South African loyalty landscape', (http://truth.co.za/wp-content/uploads/Truth-Whitepaper-October-2017.pdf) (accessed 2018-03-23).

[33] Truth, 2017:11. The 2017 truth loyalty whitepaper 'South African loyalty landscape', (http://truth.co.za/wp-content/uploads/Truth-Whitepaper-October-2017.pdf) (accessed 2018-03-23).

The top six loyalty programmes described above would be ideal to investigate and analyse as they are currently the country's top used programmes. Another reason for selecting these loyalty programmes is that they have differences and similarities in the way they function or work as well as how they operate. This will give an opportunity to identify different VAT issues that may arise with the respective loyalty programmes.

Each of these will be discussed below in order to identify the similarities and differences amongst them. Their terms and conditions will also be extensively scrutinised as the VAT output treatment may be guided by the terms and conditions of the programme.

Pick n Pay Smart Shopper

The Pick n Pay Smart Shopper allows participants to earn points when they shop at a Pick n Pay store. The customer presents their smart shopper card at the till point of sale in order to earn Smart Shopper points for transactions [34], for every For every R2 spent on point-eligible items, a Smart Shopper point will be earned. [34]

The Pick n Pay Smart Shopper Programme has further terms and conditions discussed below and these are also available on their website.

- A Pick n Pay Wallet pre-loaded in activated upon registration for the Smart Shopper programme. A customer can do a top-up (that is depositing money to the wallet) at a till point. The wallet can be used as a eligible for payment at Pick n Pay stores on all products and services but may not be exchanged for cash and no credit balance will be dispensed to a customer as cash;
- A customer is allowed a maximum wallet balance of R5000;
- Customers may only own one active Smart Shopper Card, which is connected to one Smart Shopper points account.
- In order to be able to utilise the Smart Shopper points as tender for purchases in store, donate their Smart Shopper points to a pre-selected charity organisation of one's choice or change to Avios, the customer will need to first accumulate 500 Smart Shopper points;
- Smart Shopper points can be converted to their monetary, or a redemption partner, or donated to a charity on any Pick n Pay digital channel;
- Smart Shopper points will be valid for 12 months. Money earned from Smart Shopper points' switches (that is smart shopper points that have been converted

[34] Pick n pay Smart Shopper programme as described on the pick n pay website, online (http://www.picknpay.co.za/smartshopper-terms-and-conditions, accessed, 2017-09-21).

to their monetary value and loaded on to the smart shopper card) will be valid on the Smart Shopper card for 3 years.

- Money accumulated from Smart Shopper point's conversions remains virtual money. No customer gift card will receive cash money from the Smart Shopper scheme. Monetary value is attached to the Smart Shopper card at which point the card assumes the function of a gift card;
- Smart Shoppers will receive instant savings on selected products in Pick n Pay stores. These promotions will be available for limited periods from time to time. Please note that not all products are available in all stores and special offers may change without notice.

The description of the loyalty points as taking on the function of a gift card is very important in helping to determine the appropriate VAT treatment upon redemption of the points to part or full settlement for the purchase of goods or services. A gift card is a form of payment and therefore, might fall within the ambit of consideration.

Clicks Club Card

With the Click Club Card, one can register at any of the Clicks stores by filling in a Club Card enrolment form and they will receive a plastic card immediately. For the customer's convenience, the customer may also enrol online or register a plastic card that they received in-store online.

Points are earned when one swipes the club card that is provided to the customer upon joining. The card can be used when shopping in stores or online. For every R5 spent at Clicks, one point is earned[35].

Customers can earn points at Clicks and at their Club Card affinity partner. Affinity partners are Clicks' partner where a customer can earn points on eligible purchases like they would if they were shopping at Clicks. The points are earned by presenting a club card to the cashier so that they can swipe it before cashing up to ensure that the points are indeed earned for the particular transaction, as they cannot be added after the sale has been concluded. With regards to the online Club Card purchases, affinity partners require that a customer enters their card number prior to concluding the transaction to enable them to earn points.[35]

A customer can check their points balance at the bottom of their till slip, by logging onto the My Rewards Activity on the Clicks website and by contacting the Customer Service Centre.[35]

[35] Clicks club card programme as described on the clicks website, online (https://clicks.co.za/clubCardPage, accessed, 2017-09-21).

Furthermore, in order to be able to redeem points, Club card members who earn at least 100 points need to convert their points to cashback by the expiry date and they will receive cashback loaded onto their Club Card every 2 months (Cashback is valid for 12 months). The cashback can be used for purchases in Clicks, The Body Shop, Claire's or GNC Concept store. The cashback loaded onto the Clicks Club card will expire 12 months from the date of issue. Rewards cannot be exchanged for cash or used to purchase Clicks, Musica, Claire's or The Body Shop gift cards.[35]

The terms and conditions of the Club Card state that a Clicks Club Card cannot be used as a credit or debit card, rewards cannot be exchanged for cash or used to purchase any gift cards sold in Clicks stores. Additionally, a Clicks Club Card is not transferable. Club card benefits will accordingly accrue to the named Club card member only.[35]

Unlike with the Edgars and Pick n Pay loyalty programmes, the Clicks Club Card does not give a clear indication of how the loyalty points (cashback) will be treated upon redemption, it does not state whether the cashback will take the form of a gift card or trade discount. Therefore, the categorisation of these cashback is open to interpretation. The terms and conditions do, however, sate that rewards may only be redeemed by a Club Card Member in the country in which the points were earned.[35] This requirement therefore, introduces a limitation on the cashback earned which might affect how the points are treated from a VAT perspective.

Woolworths WRewards

With WRewards one saves up to 20% instantly on thousands of items, from food, clothing, homeware, beauty products and more[36].

There are three levels to WRewards; one can either be a valued member, loyal member or a VIP member. These levels are discussed below as they are laid out on the WRewards website.

As a Valued Member, one will receive:

- Swipe a WRewards card and get an extra 10% off selected items. Pay with an account card and get a further 5% off selected items;
- Be the first to know about sales and special events.

[36] Woolworths WRewards as described on the Woolworths website, Online (http://www.woolworths.co.za/store/fragments/wrewards/wrewards-index.jsp?content=../lookbook/lookbook-multiple&contentId=cmp207958&context=how-it-works, accessed, 2017-09027).

As a Loyal Member, one will receive:

- Welcome tier voucher;
- Swipe a WRewards card and get an extra 10% off selected items. Pay with an account card and get a further 5% off selected items;
- Be the first to know about sales and special events;
- Exclusive WRewards savings vouchers throughout the year.

As our VIP Member, one will receive:

- Welcome tier voucher;
- Swipe a WRewards card and get an extra 10% off selected items. Pay with an account card and get a further 5% off selected items;
- Be the first to know about sales and special events;
- Exclusive WRewards savings vouchers throughout the year;
- Birthday voucher.

Unlike the other loyalty programmes, the Woolworths WRewards programme, offers discounts at the point of sale on selected WRewards products. Depending on the class of the reward programme, participants also get discount vouchers as well as birthday vouchers. It seems that there is no allocation of points that can be converted to be treated as a discount or gift card at a later stage. The VAT treatment of these rewards may therefore, be different from the ones where points are accumulated then redeemed at a later stage.

Edgars Thank U

The Edgars Thank U Programme, like the Pick n Pay and Click's Club Card, offers a person points when they swipe their loyalty card upon purchase of goods at all participating stores within the Edcon group[37]. The Edgars Thank U loyalty programme has further terms and conditions discussed below and they are also available on their website.

- Customers earn Thank U Points on purchases of all-inclusive products (these are all products that are approved per the loyalty programme terms and conditions as products that will enable customers to earn loyalty points);

[37] Edgars loyalty Programme describing the workings of the Edcon loyalty programme, Online (https://www.thanku.co.za/terms/, accessed 2017-10-31).

- In order for Thank U points to be earned by a customer a Thank U card must be presented at the point of sale. Thank U Points that will be lost or forfeited due to the 'card not being present' cannot be claimed retrospectively;
- The following specific conditions apply to on-line offers: The offer does not need to be printed out to be redeemed;
    - One needs to click on the "activate" button if they wish for the Thank U Points to be allocated to their account and purchase the selected product;
    - If one clicks the "activate" button but do not purchase the product, the Thank U Points will not be allocated;
    - If one purchases the product but they have not clicked the "activate" button, the Thank U Points will not be allocated;
    - Customer must go into a participating store and purchase the product on offer before the Thank U Points can be allocated to their account;
    - If the product is returned, the Thank U Points will be reversed;
    - There are selected goods or services in which Thank U points cannot be earned;
    - These includes; the purchase of gift card purchases, gift card top-ups, airtime, cigarettes, baby formula, insurance products, payments for third party services – including but not limited to – utility bills and purchase of lottery tickets (unless otherwise stipulated);
    - Purchases of third party partner products using a Thank U Account card are included in Thank U Points earning;
    - Base Thank U Points are earned on all-inclusive products at a rate of ten Thank U Points per net SA Rand spent;
    - In order to spend their Thank U points, a customer needs to reach a balance 10,000 Thank U Points, the points will be spent by presenting the Thank U Rewards Card at the point-of-sale in participating stores and informing the cashier that they wish to use their Loyalty Points as a trade discount against their cash or account purchase.

It is important to note that the Edgars Thank U Points as specifically stated in their terms and conditions will be utilised on redemption as a trade discount against a purchase of goods or services. This clear distinguishing characteristic might be helpful in determining the VAT treatment of this specific loyalty programme. A trade discount is excluded in the definition of consideration, in this regard, the vendor will not include the part payment in their consideration thereby excluding it from the output tax declared to SARS.

The vendor will therefore, not be left out of pocket in relation to a transaction where goods or services were paid for partly using loyalty points.

Dis-Chem Benefits

The Dis-Chem Benefit Programme also allows participants to earn points on the purchase of qualifying products. The loyalty points can be redeemed against a purchase at any time, the participant simply needs to inform the cashier at the store that they need to pay with their points. The Dis-Chem Programme also offers instant benefits in store when purchasing certain items and swiping a Dis-Chem Card one will receive an additional discount on the marked price of the item.[38]

[38] The Dis-Chem loyalty programme as described on the Dis-Chem website, Online (https://dischem.co.za/loyalty-terms-and-conditions, accessed 2017-11-18).

A Benefit Card and the rewards accruing thereto are not transferable. The Dis-Chem Benefit programme rewards will accrue to the Dis-Chem Benefit Programme Member only. Additionally, the points or rewards cannot be exchanged for cash. The value of points accumulated on the member's Benefit Card Profile can be used for payment of purchases at participating Dis-Chem Stores. Items purchased through redeemed points may not be returned or replaced for cash.

The terms of the loyalty programme clearly state that the value of accumulated points can be used as payment for goods or services at participating stores. This distinction is also very important in determining the VAT treatment of the points used as part or full payment on redemption. This could be read as Dis-chem suggesting that they will accept the points as consideration for the supply of goods or services, which may compel them to include the amount to the value of the points in their consideration for purposes of determining the output tax amount to be declared to SARS.

FNB eBucks

The eBucks programme enables one to:

> earn eBucks for doing everyday things such as shopping, filling up with fuel or loading airtime[39]. One can spend the eBucks they earn on fuel, electronics and appliances, travel, books, CDs and DVDs, flowers, outdoor equipment or fashion. Depending on the status of the customer, a certain percentage of all purchases made is refunded by way of an award in the form of eBucks.

EBucks is a virtual currency with a monetary value which can be used by customers to buy goods and services online from third parties[40]. EBucks also has an eBucks shop which offers a variety of products to participants at supposedly discounted rates. As a participant, a person also has an opportunity to spend their eBucks at various partners available on the eBucks website.

The description of eBucks as a virtual currency may have a significant impact on the VAT treatment when the eBucks are used as part or full settlement for products or services.

A customer can also spend their eBucks at the eBucks shop in the following ways:

- Depending on the product you select to purchase you may make payment in either eBucks or Rand or split your payment in a combination of eBucks and Rand;
- The applicable payment options will be made available to you before checking out from the eBucks Shop;
- Payments for virtual vouchers using the EASYSPEND SMS SERVICE may only be in eBucks;

[39] eBucks programme as described on the eBucks website, Online (https://www.ebucks.com/web/eBucks/aboutus/, accessed 2017-09-20).
[40] Brits, (2013:6), The Taxation of Interest Earned in Customer Loyalty Award Programmes in South Africa

- Payment in Rand must be made with either any of your Qualifying Business Cheque Cards or your FNB Business Credit Card that has been registered for verified by Visa;
- If your FNB or RMB Private Bank credit card or cheque card has not been registered or verified by Visa you will have to log into FNB Online Banking to register and be verified by Visa before you are able to receive your OTP to purchase goods and services in the eBucks Shop, using your FNB or RMB Private Bank credit card or cheque card;
- If any of your Qualifying Business Cheque Cards or Your FNB Business Credit Card has not been registered for verified by Visa, you will have to log into Online Banking or Online Banking Enterprise™ and register as well as be verified by Visa before you are able to receive your One Time Pin (OTP) to purchase goods and services in the eBucks Shop, using any of your qualifying Business Cheque Cards or Your FNB Business Credit Card. No debit cards will be accepted and no credit cards or cheque account other than a qualifying Business Cheque Card or your FNB Business Credit Card will be accepted;
- Discounts will be restricted to products purchased with eBucks;
- Products paid for either in Rand or partly in Rand will not qualify for discounts[41]

In terms of the eBucks website, the purchaser has an option to make payment in either eBucks or Rand or split the payment in a combination of eBucks and Rand when shopping at an eBucks shop or selected partners.

The terms and conditions further state that, if a member does not earn or spend eBucks on their eBucks account for a period of 6 months, their eBucks account will be considered dormant. First national Bank will then deduct a dormancy administration penalty of eB85 (inclusive of VAT) from the customer's eBucks account every month until the customer has either earned or spent their eBucks, or until the members eBucks account reaches a zero balance, whichever occurs first. This dormancy administration penalty is used for, including but not limited to, covering the costs of maintaining the member's eBucks accounts on the First National Bank's system. Once the member has reached a zero balance, First National Bank may close the member's eBucks account.[41]

Additionally, there is something interesting to note in that there is a disclaimer on the website which says –

> First National Bank strongly recommends that members of the eBucks loyalty programme obtain independent professional advice regarding any tax implications arising from the receipt, accumulation, transfer or spend of any rewards, benefits, discounts or eBucks. Transfer refers to the transfer of rewards, benefits, discounts or eBucks to another person, business or entity. Furthermore, the member is fully responsible for any tax implications arising from or associated with any rewards, benefits, discounts or eBucks received, accumulated, transferred or spent due to them being a member of, or participating in, the eBucks Rewards Programme.*41*

This statement by First National Bank highlights the fact that there are tax issues that may arise as a result of being a member and participating in the eBucks programme or any other loyalty programmes for that matter.

The terms and conditions go on further to describe who the supplier is when an eBucks member makes a purchase using eBucks. The terms state the following-
First National Bank makes available a variety of products and services by way of the eBucks rewards programme.

---

[41] eBucks programmes as described on the eBucks website. (https://www.ebucks.com/web/eBucks/aboutus/, accessed 2017-09-20).

When one purchases vouchers via the eBucks Shop, First National Bank is regarded as a supplier, as defined in the Electronic Communications and Transactions Act 25 of 2002 (ECT Act).

When a member purchases any other product or uses any service via the eBucks Rewards Programme, the supplier, for the purposes of the ECT Act, is the party that provides the goods or services, unless expressly or by implication stated otherwise. Where a party is regarded as a supplier for the purposes of the ECT Act, that party may have its own terms and conditions.[42]

A 'supplier' is defined in the VAT act as-

> *In relation to any supply of goods or services, means the person supplying the goods or services.*

The following can be noted regarding the loyalty programmes described above:

- Some of the loyalty programmes are semi-exclusive programmes, exclusive in the sense that they are run internally. From the descriptions above, Pick n Pay, Edgars, and Dis-Chem operate an exclusive programme;
- The Woolworths WRewards programme, is a bit different from the others as it does not offer points to participants but instant discounts at the point of purchase. This will therefore, have different VAT implications;
- The eBucks and Clicks Club Card programmes are multiparty programmes. This is because the 'main participants' (that is First National Bank and Clicks) are not the only stakeholders in the programme. The customers are allowed or are able to redeem their points at participating partners.

As noted above, this report will focus on transactions with elements of an exclusive programme.

[42] eBucks programmes as described on the eBucks website. (https://www.ebucks.com/web/eBucks/aboutus/, accessed 2017-09-20).

Chapter 3:

The definition of consideration for VAT purposes

This chapter will explore the definition of consideration as it is broadly defined in Section 1(1) of the VAT Act, to include any payment made in relation to a supply of goods or services, whether using money or otherwise.

An important observation was made in the SARS Interpretation Note 70, that:

> the definition of the term 'consideration' merely determines whether certain payments, acts or forbearances are regarded as consideration. It does not determine the taxable nature or otherwise of a supply for which the consideration is received, nor the amount to be regarded as the consideration.

Section 7(1) of the VAT Act in the context of goods or services supplied is a section which is used to impose VAT output on the supply of goods or services made by a VAT vendor for purposes of the furtherance of an enterprise.

In terms of Section 7(1):

'Subject to the exemptions, exceptions, deductions and adjustments provided for in this Act, there shall be levied and paid for the benefit of the National Revenue Fund a tax, to be known as the value-added tax—

a) On the supply by any vendor of goods or 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 any 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 concerned or the importation, as the case may be'.

An enterprise is essentially defined in Section 1(1) of the VAT Act as, the carrying on of continuous or regular activity in the republic in the course or furtherance of which goods or services are supplied to any other person for consideration.

Consideration is defined in section 1(1)[43] of the VAT Act as –

> …in relation to the supply of goods or services to any person, includes any payment made or to be made (including any deposit on any returnable container and tax), whether in money or otherwise, or any act or forbearance, whether or not voluntary, in respect of, in response to, or for the inducement of, the supply of any goods or services, whether by that person or by any other person….

Furthermore, the definition of consideration in the VAT Act does not include:

> any payment made by any person as a donation to any association not for gain: Provided that a deposit (other than a deposit on a returnable container), whether refundable or not, given in respect of a supply of goods or services shall not be considered as payment made for the supply unless

[43] Consideration as defined in section 1 of the VAT Act

and until the supplier applies the deposit as consideration for the supply or such deposit is forfeited.[43]

It was stated in Interpretation Note 70 that:

> *The concept of "consideration" is one of the cornerstones of VAT and is defined in relation to the supply of goods or services. It contemplates the making of payments, the performance of certain acts and the carrying out of forbearances in relation to a supply.*[44]

Furthermore, the interpretation note emphasized that the consideration for a supply could be made up of a grouping of monetary amounts, reciprocal supplies or acts of forbearance. In such cases, a value must be attributed to each component of the consideration and must be combined to determine the final VAT-inclusive amount. [44]

This point in Interpretation Note 70 further highlights the fact that consideration does not only include money, but can include any other form of payment.

Other features of "consideration" as set out in Interpretation Note 70 are as follows:

- When the word is used with reference to a taxable supply, it is a VAT-inclusive concept. This means that any payment received by the supplier in respect of a supply of goods or services will include a component of VAT, whether payment has been made in part, or in full;
- It includes pre-payments for supplies as well as any past payments in the method of instalments, current payments, or payments which are still to be made in the future in respect of any supply;
- Payment of the consideration does not necessarily have to be made by the recipient of the supply. Consideration can also include payments received from a third party on behalf of the recipient. [44]

In a list of definitions provided by the Australian Tax Office (ATO), payment (consideration) for Goods and Services Tax ("GST") purposes is anything one receives for the provision of goods, services or anything else. Payment is usually done using money, but can be in the form of other goods or services, as in the case of barter transactions. Payment may also be made by way of refraining from doing something.[45]

---

[44] SARS, Interpretation Note 70, purchases for no consideration, (2013:15). (http://www.sars.gov.za/Legal/Interpretation-Rulings/Interpretation-Notes/Pages/Numbers-61-80.aspx) (accessed 2017-09-12).

[45] Consideration definitions per the ATO website (https://www.ato.gov.au/Business/GST/In-detail/Definitions/#Paymentconsideration, accessed 2018-02-20)

Other definitions included a definition in a glossary of terms provided on the New Zealand Inland Revenue (NZIR) website, it is stated that for GST, the term "consideration" has a broader meaning than the common usage:

> It includes any amount paid, or any act or forbearance, in return for a supply of goods or services. This means it:
>
> - Needs not be "compulsory";
> - Need not be in cash (such as barter);
> - May be a promise to not do something, for instance, in return for goods, a creditor may agree not to pursue a debt;
> - May be an stimulus offered to induce a supply;
> - May be paid by someone else, for example, if a parent pays for a child's haircut it does not include unconditional gifts made to non-profit bodies if the donor does not receive a direct benefit, for example, street appeals or bequests[46].

Furthermore, in the NZIR commentary on the GST Act, this was stated about the term consideration,

> This has been defined widely to include all amounts paid, or any act or forbearance, in respect of supplies of goods and services, whether made voluntarily or not. The term includes all Government charges, rates, and all contractual payments. The term is intentionally wider than its strict contractual meaning. "Consideration" also covers many Government grants and subsidies which are provided for the supply of goods and services, or where the supply is induced by the grant or subsidy. It also covers "payment in kind", barter, "trade-off" of debts and similar arrangements[47].

There are similarities that can be identified for these three definitions of consideration. The main being that consideration does not necessarily need to be in the form of money (cash), it can also take other forms like forbearance to induce the provision of gods or services.

Kruger et al (1992) also highlight that consideration received does not necessarily have to be in the form of a monetary payment. It was further stated that any kind of quid pro quo payment provided in return for the goods or services will constitute consideration for which the supplier must account for VAT.

In the SARS Interpretation Note 70[Error! Bookmark not defined.], it was stated that, in a normal business transaction, the consideration is usually determined with reference to an amount of money. However, consideration comprises of payment in any form and could be in money or in-kind.

In Chapter 2, the top six loyalty programmes in South Africa were discussed. One of the main characteristics of the loyalty programmes with exception to the Woolworths

[46] Consideration definitions per IR website (http://www.ird.govt.nz/gst/info-help/glossary/glossary.html#con, accessed 2018-02-20)

[47] IR commentary on the GST Act (http://www.ird.govt.nz/technical-tax/pib-review/pib-archived/archived-goods-and-services/goods-services-1983-vol-143.html, accessed 2018-01-20)

WRewards programme was that, the customers participating in the loyalty programmes can utilise the points earned as full or part payment for a purchase of goods or services. The use of loyalty points as a form of payment in exchange for the receipt of services or goods may need to be taken into account as consideration.

A further observation was made in Chapter 2 regarding some of the top six loyalty programmes. The Edgars Thank U programme makes reference to the fact that loyalty points accumulated by participants can be redeemed as a trade discount against a purchase. This would therefore mean that the Thank U points have no inherent value, other than providing the customer with an entitlement to a discount and cannot be transferred or traded in any way.

A further observation was made with regards to the Pick n Pay loyalty programme in that the converted accumulated points function as a gift card. This then follows that, the accumulated points have an intrinsic value and can be used as a form of payment. This could possibly mean that the points could be seen as consideration. The same inference can be drawn on the Dis-Chem and eBucks programmes respectively. The Dis-Chem terms state that the accumulated points can be used as payment. While the eBucks terms state that eBucks can be treated as virtual money. Although the vendors will not be getting actual money or value for the points redeemed, the fact that the consumer is able to pay in part or in full for the purchase of goods or services, could mean that the vendor is receiving consideration as defined.

These different interpretations by the loyalty programmes operators highlight the inconsistencies in the interpretation and application of the term consideration when accounting for output VAT on the sales made using loyalty points as part payment for goods or services. These inconsistencies will be explored further in Chapter 4.

As the definition of ‘consideration’ currently reads, the loyalty points that are used as a form of payment or as a gift card or as virtual money would not qualify as an exclusion. The normal rules relating to ‘consideration’ would therefore need to be applied. This could mean that such forms of payment could form part of consideration as defined for VAT purposes.

As noted above, consideration may include payment in any form and could be in money or in kind, the payment using points earned might fall within the definition of consideration as defined. The concept of using loyalty points as payments is, however, not that straight

forward. This is because, when the points are used as payment for most of the loyalty programmes discussed, the vendor does not receive any cash or any sort of tangible benefit for the portion of the transaction that was paid for using loyalty points.

For the reason that there is a transaction that was entered into for the purpose of furtherance of an enterprise and for which consideration was received (although not in cash), the VAT vendor might find themselves in a situation where they could have to account for output tax to be paid over to SARS. This might leave the vendor out of pocket. This is because, as highlighted above, they will not have received any benefit from the portion paid for in the form of loyalty points.

In this regard, the researcher concurs with the suggestion brought forward in the SARS Discussion Paper that relief must be granted to the vendor and how this would be achieved is if loyalty points accepted as payment for goods or services by a vendor in an exclusive programme should be excluded from the consideration of the supply SARS[48]. To achieve this, the definition of consideration in section 1(1) of the VAT Act would need to be amended.

It should be noted that changes might need to be made within the systems of the different vendors taking part in loyalty programmes. This is because as it will be seen in Chapter 4, the different VAT vendors have set up their systems to account for VAT output differently.

There are certain forms of payment that are specifically excluded from the definition of consideration as defined in the VAT Act and they exclude certain forms of payment. These include:

- Donations received by associations not for gain. This includes cash payments as well as the open market value of any donated goods or services where the donor does not expect or receive anything of value in return;
- A deposit (other than a deposit on a returnable container), whether refundable or not, which is given in respect of a supply of goods or services. If the supplier however applies the deposit as consideration for a taxable supply, or the deposit

[48] SARS, 2014:13, Discussion paper of the VAT treatment of Loyalty Programmes , (http://www.sars.gov.za/AllDocs/LegalDoclib/DiscPapers/LAPD-LPrep-DP-2014-01%20-%20Discussion%20Paper%20on%20VAT%20Treatment%20of%20Loyalty%20Programmes.pdf, (accessed 2017-03-25)

is forfeited at a later date, only on the happening of that event will the amount constitute consideration. **Error! Bookmark not defined.**

Loyalty points could be added as one of the forms of payment that are specifically excluded from the definition of consideration as defined in the VAT Act. This as noted above could offer some form of relief to VAT vendors taking part in the loyalty programmes.

Chapter 4:
Accounting for Output VAT by various vendors

This chapter will look at how different vendors account for VAT in the calculation of the total output VAT due to be declared by a vendor to SARS. This was done by going to some of the stores in the top six loyalty programmes (as discussed in chapter 3 above), making a purchase utilising loyalty points and inspecting the customer receipt to try and see how the different vendors treat purchases made using points earned through a loyalty programme.

The treatment will then be contrasted with the literature available on the treatment of loyalty programmes in order to establish if there is a need to amend the current VAT legislation or at least provide additional guidance to VAT vendors regarding the treatment of VAT on loyalty programmes.

It should be noted that the stores visited or the analysed receipts were chosen based on the availability of membership in these loyalty programmes offered by the stores. The loyalty programme store receipts to be analysed in this study include, Pick n Pay Smart Shopper, Clicks Club Card, Edgars Thank U and Dis-Chem Benefits.

Pick n Pay Smart Shopper

The customer receipt is displayed below as Image 1.1.



Image 1. 1: Pick n Pay receipt

As noted in the image above, a purchase was made for a product with the selling price of R9.99 there was an option to partly for the product using smart shopper points. The value of the smart shopper points was R9.99. The full value of the smart shopper points was utilised in full as payment for the purchase.

As it has been established in Chapter 3 above, consideration does not necessarily have to be in the form of money. It can also include any other form of payment other than money. As discussed in Chapter 2, part of the terms and conditions of the Pick n Pay Smart Shopper Loyalty Programme is that the accumulated points can be switched to cash to spend in-store. Additionally, on conversion of the points, the monetary value is attached to the Smart Shopper Card at which point the card assumes the function of a gift card.

The R10 which was used as part settlement for a product purchased by swiping the loyalty card (which in terms of the terms and conditions takes the form a gift card) could be perceived as a form of consideration. Based on the receipt displayed above as Image

1.1, the R10 smart shopper points redemption, which could be seen as a form of consideration was not treated as a form of consideration. This is because the R10 was excluded from the value of supply as seen on the receipt.

Based on the above customer receipt, the VAT was accounted for as follows. The value of the supply before taking into account the R10 smart shopper points is R8.69 which is the sale price excluding VAT. The total VAT based on the value of the supply is R1.30. Therefore, the consideration would be R9.99 which would be the value of the supply plus VAT. If the manner in which the VAT was accounted for on the above customer receipt. The total VAT of R1.30 was reduced by the amount of R1.30, which is R10 *15/115.

Based on receipt, it seems that the VAT amount related to the smart shopper points utilised will be excluded from the VAT declared to SARS. Therefore, consideration for the transaction excludes the payment made utilising the smart shopper points.

As noted in Chapter 2, unlike with the Clicks Club Card , the Pick n Pay Card, outlines the terms and conditions to give a clear indication of how the loyalty points will be treated (that is, the time when the accumulated points are redeemed they take the form of a gift card). As things stand in the current VAT legislation, the treatment displayed above can be a valid interpretation of the law. This is because the current definition of the consideration does not specifically include loyalty points or specifically exclude loyalty points.

On the other hand, it is noted that consideration could be money or any other form of payment. Another interpretation might look at the use of the smart shopper points as part of the consideration for the supply of goods. This highlights the differences that may arise in the interpretation of the law when loyalty points are utilised as part payment for the supply of goods and services. These differences will be explored in the other store receipts analysed below.

An additional observation was made with regards to Pick n Pay, please see Image 1.2 below. The image will be described below in more detail as it is unclear.

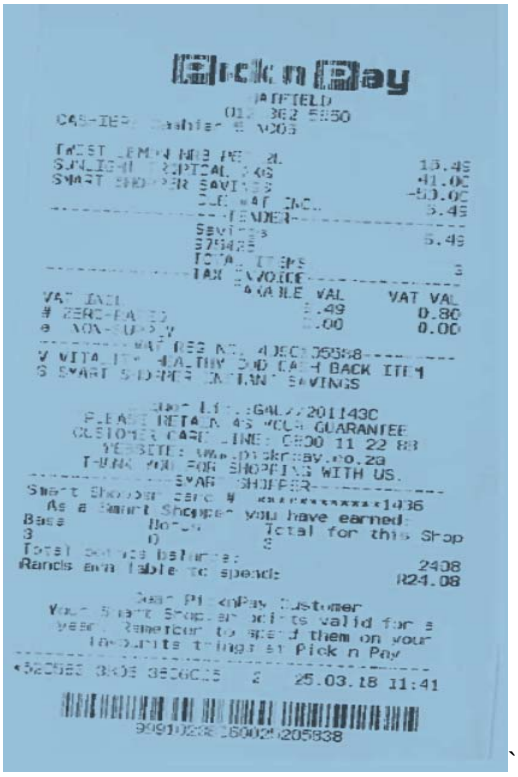


Image 1. 2: Pick n Pay receipt (apologies for the unclear image)

With regards to Image 1.2 above, a purchase was made at a Pick n Pay store. The payment of the product received was a smart shopper gift credit of R50. Image 1.2 shows a purchase which was made and paid for by utilising a voucher issued to the customer. The voucher was awarded to the customer.

A voucher or gift card is awarded as follows, a customer makes a purchase and presents their loyalty card at the till, based on the purchases made, a voucher will be awarded to the customer which will be separate from the loyalty points that may have been earned by the customer on the purchase.

As noted above, the award was made based on the purchases made by a customer and the customer presented their smart shopper card and got an instant discount voucher. This voucher would be described as a multi purposes voucher as it was not specified on the voucher which items should be purchased using it. It therefore meant the voucher could be used to purchase any product.

The distinguishing factor between the information in Image 1.1 and Image 1.2 is that with regards to Image 1.2 the customer did not have to accumulate qualifying points then convert the points in order to use the points to pay for goods or services, the voucher or

gift card was generated instantly at the point of sale and the customer could use the voucher immediately (that is there is no waiting period).

Another distinguishing factor is the way VAT is accounted for on the customer's receipt. With regards to Image 1.2, the full VAT portion related to the transaction was accounted for, however, in Image 1.1 as noted above; the VAT amount was reduced by the portion of VAT that related to smart shopper points. This then follows that the VAT accounting for payments made using loyalty and payments made using a voucher is different. The treatments are different although the terms and conditions of the Pick n Pay smart shopper programme say that the redeemed accumulated points can be treated as gift card/ voucher.

Clicks Club Card

The customer receipt is displayed below as Image 1.3.


CLICKS
Pharmacy
CLICKS CLUBCARD
CALL 0860 254 257
www.clicks.co.za

WELCOME TO
ROSEBANK MALL

ESS L/L EYEPENCIL 01 R29.95

10% Off Colour Cosme -R3.00
Cash Back Reward -R18.30

Total Savings R21.30

1 BALANCE DUE R8.65
Debit card R8.65
EXP. DATE: 12/2018
Auth Code = 351698
CHANGE R0.00

TOTAL BEFORE VAT R7.59
TOTAL VAT R1.06
TOTAL AFTER VAT R8.65

TAX-CODE	TAXABLE-VAL	TAX-VALUE
14% VAT	R8.65	R1.06

CLUBCARD STATEMENT
CLUBCARD NUMBER 020054154544b
Cashback Opening Balance R18,30
Cashback Spent R18,30
Cashback Balance R0,00
Points Balance (Midnight) 286 points

Image 1. 3: Clicks customer receipt

As noted in the image above, a purchase was made, for a product with the selling price of R29.95. There was a 10% once-off discount of R3.00. Additionally, there was an option to partly pay for the product using the cashback rewards. The value of the cashback rewards was R18.30. The full value of the v rewards was utilised in full as part payment

for the purchase. The remainder of the purchase price amounting to R8.65 was paid for using cash.

Based on the receipt displayed above as Image 1.3, it seems the R18.30, which could be seen as a form of consideration was not treated as a form consideration. Based on the customer receipt above, the VAT was accounted for as follows, the value of the transaction was R7.59 which is the sale price excluding VAT, the 10% discount and the R18.30 cashback rewards. The consideration would therefore be the value of the supply plus the VAT at 14%. In this regard, VAT was only accounted for on the customer receipt on the amount net off the cashback reward and the 10% discount.

As noted in Chapter 2, unlike with the Edgars and Pick n Pay loyalty programmes, the Clicks Club Card does not give a clear indication of how the loyalty points (cashback) will be treated as. Therefore, the categorisation of these cashbacks is open to interpretation. Moreover, as things stand in the current VAT legislation, the treatment displayed above as with the Pick n Pay treatment can be a valid interpretation of the law.

The treatment of the loyalty points by Clicks seems to be the same with that of the treatment in the Pick n Pay loyalty programme. It is important to note that although these treatments are similar, the terms and conditions of the respective loyalty programmes are different in that Pick n Pay is clear as to what form the accumulated points take when redeemed and Clicks is silent. This then raises the question on whether the terms and conditions of a particular loyalty programme have any impact on the VAT treatment thereof.

Edgars Thank U



CASH CARD SALE TAX INVOICE

Edcon Limited
Private Bag 1, Crown Mines, 2025
VAT#:4460236773
Edgars Rosebank Mall
Shop 238-239 and Shop 326,The, 50,Bath Avenue,Rosebank,
TEL#:0112147740

S/N :22092017 01824 00030 117078 11:48:49
CASHIER :Tswanelo Bucibo 2315561
CASH CARD:**********0173

ITEM	QTY	VALUE
1 .*2101011936567	1	99.95
3PH PLAIN OPAQUE BLACK		
THANK U REDEEM(11000 P)		-11.00
TOTAL Excl VAT		87.68
VAT@14.00%		12.27
TOTAL Incl VAT		99.95
TOTAL PAID		88.95
EFT [400974******4822]		88.95
THANK U BALANCE		11,045.00
THANK U BALANCE VALUE		11.84

TaxRate	Consideration	Tax
Item 14.00%	99.95	12.27
THANK U REDEEM 14.0	-11.00	-1.35
Total Tax		10.92
ITEMS PURCHASED	1	

Image 1. 4: Edgars customer receipt

As noted in the image above, a purchase was made, for one product with the total selling price of R99.95. As with the Clicks receipt displayed in image 1.3, there was an option to partly pay for the product using the loyalty rewards (‘Thank U points‘). The value of the loyalty points was R11.00. The full value of the loyalty points was utilised in full as part payment for the purchase. The remainder of the purchase price amounting to R88.95 was paid for using cash.

The customer receipt together with the Edgars’ terms and conditions referred to in Chapter 2, makes it clear that when redeemed, the member utilises their loyalty points to obtain a trade discount by reflecting the total tax after the discount has been taken into consideration.

In this regard, the R11 as seen in the customer receipt is excluded from consideration, the consideration only shows the amount of R88.95. Furthermore, the VAT on the receipt is reduced by 14/114 of R11. In this regard, the VAT output declared to SARS will exclude the amount of VAT relating to the loyalty points. Again this treatment is similar to the treatment applied by Clicks and Pick n Pay but the terms and conditions are different.

Dis-Chem



DIS-CHEM ROSEBANK PHARMACY

*ORIGINAL*ORIGINAL*

SHOP 327/328 CASH SALE
ROSEBANK MALL 01479624
51 BATH AVENUE 2017/09/22
ROSEBANK, JHB
Tel: 011 772 1210
Fax: 011 880 1806

TAX INVOICE V.A.T REG. NO: 4820223024
CASHIER: TSHOLOFELO PHETHLE
TILL NO: 0007

DISCO EYEBROW PENCIL BROWN W/BRUSH
6009511131122 1 x 15.95 15.95 T1
BT CONCEALER CRAYON
676768316013 1 x 39.95 39.95 T1

Total>>>: 55.90
(Rounding): 0.00
(Incl.VAT @14%): 6.86

LOYALTY 12.56
CRCARD 43.34
Time: 12:01:27 ********2.000 ITEM/S

*VIT:Discovery Vitality members get up to 25% cash back on HealthyCare items.
www.discovery.co.za

Thank You for Swiping your Card Today.
By doing so, you have contributed to
The Dis-Chem Foundation.

Image 1. 5: Dis-Chem customer receipt

As noted in the image above, a purchase was made, for two products with the total selling price of R55.90. As with the Clicks receipt displayed in Image 1.3, there was an option to partly pay for the product using the loyalty rewards. The value of the loyalty points is R12.56. The full value of the loyalty points was utilised in full as part payment for the purchase. The remainder of the purchase price amounting to R43.34 was paid for using cash.

Unlike the Clicks cash back loyalty points, the terms of the Dis-Chem loyalty programme clearly state that the value of points accumulated can be used as payment for goods or services at participating stores. This could have certain VAT consequences for this particular vendor.

Based on the customer receipt in Image 1.5 above, the VAT was accounted for as follows: The consideration for the transaction is R55.90 which is the value of the supply plus the VAT. VAT is therefore accounted for on the R55.90 and not R55.90 less 12.56 (loyalty points). This is clearly different from the Clicks, Pick n Pay and Edgars treatment highlighted above.

Based on this customer receipt, the loyalty points were clearly treated as part of consideration and not as a “discount”. This could be due to the fact that the terms and conditions for this particular loyalty programme specifically state that loyalty accumulated points can be used as part settlement for the purchase of goods or services.

The terms and conditions of this particular loyalty programme might have been drafted to explicitly say that the loyalty points can be used for payment of goods and or services due to the vendor’s interpretation of the current VAT legislation or the main focus in drafting the terms and conditions was not the VAT legislation. It is clear that in the case of Dis-Chem, a payment made by way of loyalty points should form part of consideration based on their terms and conditions.

The differences identified above further highlight how different loyalty programme providers interpret the VAT Act as it currently reads. Section 7 of the Act levies VAT on the supply of any goods or services in the course or furtherance of the carrying on of an enterprise, calculated as 14% of the value of the supply.

In terms of Section 10(2) of the Act, the ‘value of a supply’; is the consideration for it less the tax included in it.

Consideration as defined in Section 1 of the Act includes any payment made or to be made in respect of, in response to, or for the inducement of the supply of any goods or services. The difficulty in the interpretation of this consideration definition has hopefully been clearly illustrated through the analysis of the different customer receipts displayed and analysed above.

There is no denying that the treatments of the different VAT vendors identified above are all valid, although some of the treatments might leave some of the VAT vendors in an out of pocket situation, for example in the Dis-Chem transaction. The vendor only receives a portion of the sales value of the product as part of the purchase but the customer is funded by way of loyalty points. The vendor however, still has to declare to SARS VAT on the full sales price.

Another consequence could be that SARS might feel that they are left out of pocket in relation to those vendors who only declare VAT on sales amounts net of loyalty points. Depending on how this is interpreted, SARS may contend that VAT be declared on the full sales value of the products sold. Either way, as the legislation currently reads, the

vendors and SARS are left with uncertainties as to what the correct treatment of transactions in which loyalty points are utilised as part payment is.

To further emphasise the point of uncertainty, it was noted in the introduction that Brink[19] also concluded in the paper on the evaluation of the income tax treatment of loyalty programme transaction by South African suppliers that, there are gaps in the interpretation and application of the Income Tax Act in respect to client loyalty programme transactions. The same applies for the VAT treatment of loyalty programmes and guidance is required from the tax authorities in this regard.

SARS in their Discussion Paper (2014) also alluded to the existing uncertainties as displayed in this chapter using the customer receipt exercise.

Chapter 5:
Comparison to the current South African legislation on the VAT treatment of vouchers

The current VAT legislation makes provision for the VAT treatment of vouchers. These provisions are set out in section 10(18), (19) and (20).

The Oxford Concise Dictionary defines a voucher as a small printed piece of paper that entitles the holder to a discount, or that may be exchanged for goods or services[49]. As defined in the introduction above.

The Consumer Protection Act 68 of 2008 in section 1(1) defines a loyalty programme as:

> any arrangement or scheme in the ordinary course of business, in terms of which a supplier of goods or services, association of such suppliers, or other person on behalf of or in association with any such suppliers, offers or grants to a consumer any loyalty credit or award in connection with a transaction or an agreement.[50]

Vouchers and loyalty points are similar in the sense that a customer is granted the right or benefit to acquire goods and/or services at a consideration other than money. Although vouchers and loyalty points are not necessarily the same, inferences can be drawn from the current VAT legislation on vouchers to assist in drafting legislation on the VAT treatment of loyalty programmes in South Africa.

In terms of the SARS draft interpretation note on the VAT treatment of vouchers, the legislation makes provision for the VAT treatment of three specific categories of vouchers, namely monetary vouchers, product-specific vouchers and discount vouchers[51] These will discussed in detail below in reference to the vouchers' time of supply as well as if the voucher will be vatable on sale, that is VAT will be charged at the point of sale where the voucher is utilised to purchase vatable goods or services.

Monetary vouchers

In terms of Section 10(18) of the VAT Act:

> Where a right to receive goods or services to the extent of a monetary value stated on any token, voucher or stamp (other than a postage stamp as defined in Section 1 of the Postal Services Act,

[49] 2 Ed (Oxford University Press Southern Africa (Pty) Ltd: Cape Town 2010) 1336.
[50] Consumer Protection Act 68 of 2008
[51] SARS draft interpretation note on the VAT treatment of vouchers, (2014:1) (http://c.ymcdn.com/sites/sait.site-ym.com/resource/resmgr/2014_SARS/LAPD-LPrep-Draft-2014-19_-_D.pdf) (accessed 2018-02-20).

> 1998), and any token voucher or stamp contemplated in subsection (19) is granted for a consideration in money, the supply of such token, voucher or stamp is disregarded for the purposes, of this Act, except to the extent (if any) that such consideration exceeds such monetary value.[52]

In terms of the draft interpretation note on the VAT treatment of vouchers, the VAT on the sale of the voucher should be nil, this is because the nature of the goods or services to be supplied on redemption of the voucher is not known at the time of the sale of the voucher, the rate of tax that should be applicable to the supply cannot be determined.[53]

It then follows that the supply of these vouchers is not a supply for VAT purposes and no VAT should be levied when the voucher is sold to a customer. VAT (output VAT) will therefore only be levied when the voucher is used as a payment for goods and/or services, the VAT will be levied on the goods sold and not on the voucher.

What this means in relation to loyalty points is that when a monetary voucher is sold to the customer, the nature of goods or services to be acquired using the voucher is not known at the time of sale and therefore, the VAT rate is unknown at that point.

The same principle as set out in Section 10(18) of the VAT Act should be followed, in that there should be no VAT levied on that transaction. With regards to whether VAT should be levied on the redemption of the points as payments for goods and/or services, the terms of the loyalty programme should be analysed to determine the nature of the payment. As seen in Chapter 2, some VAT vendors treat it as a trade discount, some as a gift card or as cash to spend at a store.

Product specific vouchers

In terms of Section 10(19) of the VAT Act:

> where any token, voucher or stamp (other than a postage stamp as defined in Section 1 of the Postal Services Act, 1998) is issued for a consideration in money and the holder thereof is entitled on the surrender thereof to receive goods or services specified on such token, voucher or stamp or which by usage or arrangement entitles the holder to specified goods or services, without any further charge, the value of the supply of the goods or services made upon the surrender of such token, voucher or stamp is regarded as nil.[54]

In terms of the Draft Interpretation Note on the VAT treatment of vouchers[51], these vouchers will be subject to VAT at the time the voucher is sold. This is because the goods or services to be supplied are specified on the voucher and the vendor is able to establish

[52] Section 10(18) of the VAT Act 89 of 1991
[53] SARS draft interpretation note on the VAT treatment of vouchers, (2014:1) (http://c.ymcdn.com/sites/sait.site-ym.com/resource/resmgr/2014_SARS/LAPD-LPrep-Draft-2014-19_-_D.pdf) (accessed 2018-02-20).
[54] Section 10(19) of the VAT Act 89 of 1991

the nature of the goods or services to be supplied as well as the applicable VAT rate. As a result of the VAT being accounted for when the voucher is sold, the value of the goods or services actually supplied upon the surrender of the voucher is regarded as nil [5155].

When it comes to the loyalty programmes that were discussed above, it does not seem as if any of them would fall into this type of category. Many of the loyalty points allow one to earn points on the purchase of specific products, however, those points can be utilised to obtain any other goods or services offered by the vendor.

Discount vouchers

The draft interpretation note defines a discount voucher as a token that provides the holder with the right to a discount on specified goods or services. In practice, the supplier of the goods or services (that is, not the issuer of the voucher) must give the discount when it supplies the goods or services to its customer who presents the voucher. [56]

Furthermore, the Draft Interpretation Note on the VAT treatment of vouchers (2014) states that the supplier, being a vendor, who supplies the goods or services, must not reduce the value of the supply by the discount being given to its customer. In other words, the supplier is liable to levy VAT on the full value of the goods or services before the discount is taken into account and such VAT must be paid over to SARS.[56]

If this type of voucher is compared to one of the loyalty programmes discussed in Chapter 2, for example the Edgars Thank U loyalty points, the Edgars Thank U points specifically state in their terms and conditions that the points earned will be utilised on redemption as a trade discount against a purchase of goods or services.

In this regard, Edgars would be seen as the supplier making the supply of goods or services who in terms of the Draft Interpretation Note on the VAT treatment of vouchers (2014) may not reduce the value of the supply by the discount given. Edgars is however, also the issuer of the voucher in this case. Unlike the description given in the interpretation draft note, there is no third party involved in the issuing of the discount

[55] SARS draft interpretation note on the VAT treatment of vouchers, (2014:3) (http://c.ymcdn.com/sites/sait.site-ym.com/resource/resmgr/2014_SARS/LAPD-LPrep-Draft-2014-19_-_D.pdf) (accessed 2018-02-20).
[56] SARS draft interpretation note on the VAT treatment of vouchers, (2014:3) (http://c.ymcdn.com/sites/sait.site-ym.com/resource/resmgr/2014_SARS/LAPD-LPrep-Draft-2014-19_-_D.pdf) (accessed 2018-02-20).

voucher. Edcon should then be able to reduce the value of the supply by the amount on the discount voucher when it is utilised.

It is noted that various other types of vouchers are discussed in the draft interpretation, however, only the ones that were deemed to be of relevance to this research report were discussed. As noted at the beginning of this chapter, the Draft Interpretation Note on the VAT treatment of vouchers (2014) sets out the VAT treatment of vouchers and the hope is to draw some inference from the VAT treatments suggested in the draft interpretation note on the VAT treatment of vouchers to try and determine the VAT treatment of loyalty points.

Chapter 6: International guidance

6.1 The European Commission- Directorate for General Taxation and Customs Union

The European Commission- Directorate for General Taxation and Customs Union has released a Summary of Results Report on 21 May 2007 on the public consultation on, "Modernising the Value-added Tax treatment of vouchers and related issues"[57].

The consultation was based on an analysis on the VAT treatment of vouchers across the European Union (EU). The report on modernising the Value-added Tax treatment of vouchers and related issues noted that the development of some vouchers in terms of functionality and lack of clear rules has contributed to an inconsistent VAT treatment of vouchers.[58] This is similar to the objectives noted in the SARS Discussion Paper on the VAT treatment of loyalty programmes (2014), which essentially sought to promote a discussion between SARS and the key stakeholders regarding any difficulties experienced in applying and interpreting the provisions of the VAT Act in treating loyalty points. In specific reference to this research report, uncertainties in the VAT output implications of loyalty programmes exist.

The report on modernising the value-added tax treatment of vouchers and related issues proceedings on page 2 to note that some member states treat the supply of a voucher as a supply of goods or services while others treat its purchase as a payment on account for future supplies. Other member states only tax goods and services supplied at the redemption of the voucher.

The report notes that any possible legislative change would require a description and definition of the main features of a voucher and their functioning. This statement would be relevant to loyalty programmes as well. There is a need for legislation to define and describe the salient features of loyalty programmes from a VAT perspective.

---

[57] Although the summary discusses vouchers, it is noted that inferences can still be drawn from the principles established regarding vouchers in order to assist in establishing the treatment of VAT on loyalty programmes.

[58] European Commission- Directorate for General Taxation and Customs Union, 2007:2. Modernising the Value-added Tax treatment of vouchers and related issues, (http://ebiz.pwc.com/wp-content/uploads/2014/12/summary_report_consultation_vouchers_en.pdf) (accessed, 2017-10-12)

In terms of the report, the consultation proposed a description of free vouchers, so-called single- purpose vouchers and so-called multi-purpose vouchers together with their corresponding VAT treatment.

The reports on modernising the value-added tax treatment of vouchers and related issues notes the following on the different vouchers noted above.

> **Free voucher**- A free voucher is issued without charge, normally with the intention of promoting a product or service. Discount vouchers and business gifts are a subcategory of free vouchers.[59]

The difference between a single voucher and a multi-purpose voucher can be explained as follows, a single purpose voucher would be a voucher that is issued to grant the holder of voucher the right to acquire a discount to exchange the voucher for goods or services that are identified at the time of issue. In this regards, the VAT rate of the goods or services to be purchased using the voucher is known at the time of issue. A multi-purpose voucher on the other hand gives the holder a right to acquired goods or services which are not know at the time of issue, this then means that the VAT rate of the goods or services to be acquired are not known at the time of issue.[59]

In this regard, the time of supply, for a single purpose voucher should be taxed at the time of issuance of the voucher because the nature and the VAT rate of the goods or services to be obtained is known. With regards to a multi-purpose voucher, the tax should be charged at the time of the redemption, this is because, the nature and therefore the VAT rate of the goods or services obtained using the voucher will only be known on redemption.

The report on modernising the value-added tax treatment of vouchers and related issues further notes that a free voucher does not have a taxable amount. The taxable amount of goods or services supplied against a multi-purpose voucher is equal to the value of the multi-purpose voucher used to acquire these goods and services. Finally, the taxable amount of the single-purpose voucher is equal to the consideration paid by the customer to acquire the voucher.

[59] European Commission- Directorate for General Taxation and Customs Union, 2007:3. Modernising the Value-added Tax treatment of vouchers and related issues, (http://ebiz.pwc.com/wp-content/uploads/2014/12/summary_report_consultation_vouchers_en.pdf) (accessed, 2017-10-12).

An attempt can be made to apply the guidelines set out in the report discussed above to the South African context. Depending on the terms of the loyalty programme, multi-purpose voucher and free vouchers seem to be the main categories that could apply in the South African loyalty points context.

In terms of the Edgars Thank U points discussed in Chapter 2, a member may redeem points at the point-of-sale in any of the participating stores as a trade discount against purchases. This could be categorised for example as a free voucher in the sense that, the consumer/ customer did not have to pay any consideration (i.e. it was issued without charge and as one of the main characteristics of loyalty programmes), it is issued with the intention of promoting a product or business. It could also be seen as an MVP as it carries the right to receive a discount when acquiring goods or services.

With regards to treatment as set out in the report, if categorised as a free voucher, there would be no VAT consequences on the redemption of the voucher as a free voucher does not have a taxable amount. An example would be the discount vouchers given to employees of a retail company at no extra cost to the employees (that is employees get a 20% discount on any purchases made).

6.2 Economic Co-operation and Development (OECD)

In addition to the European Commission- Directorate for General Taxation and Customs Union Report, additional guidance can also be sought form other international bodies such as the OECD to assist in drafting guidelines or legislation for the VAT treatment of loyalty programmes in the South African context.
In 2015 the OECD issued international VAT /GST Guidelines. It is important to note that the international guidance mainly focused on dealing with cross-border trade but the principles set out in the report can be applicable to the topic at hand.

The OECD guidelines allude to the fact that basic VAT principles are generally the same across jurisdictions in so far as they are designed to tax final consumption in the jurisdiction where it occurs according to the destination principle.[60]

[60] The OECD international VAT /GST Guidelines 2015:10

It was further stated in the guidelines that the overarching purpose of VAT is to impose a broad-based tax on consumption, which is understood by the various jurisdictions to mean final consumption by households as well as businesses.[61]

Based on the above statement, it is therefore, an acceptable principle that VAT should be a tax on final consumption. As seen in Chapter Four, some of the VAT vendors end up bearing the cost of VAT on sales made utilising loyalty points.

> The central design feature of a VAT, and the feature from which it derives its name, is that the tax is collected through a staged process. Each business in the supply chain takes part in the process of controlling and collecting the tax, remitting the proportion of tax corresponding to its margin, i.e. on the difference between the VAT imposed on its taxed inputs and the VAT imposed on its taxed outputs. Thus, the tax is in principle collected on the "value-added" at each stage of production and distribution.[62]

The OECD international guidelines further reiterate that the fundamental principle is that the tax burden should not rest on businesses, it requires a mechanism for relieving businesses of the burden of the VAT they pay when they acquire goods, services, or intangibles.[63] This statement highlights the importance of ensuring that the VAT consequences of selling goods and/or services using loyalty points need to be established.

The OECD international guideline set out the generally accepted principles of tax policy applicable to consumption taxes that were welcomed by Ministers from across the globe[64]. As noted above, although these principles were set out in the context of electronic services, they could be applied in the devising of a VAT guideline or legislation for VAT on loyalty programmes. These principles are set out below as described in the OECD guide.

- Neutrality: Taxation should seek to be neutral and equitable between forms of electronic commerce and between conventional and electronic forms of commerce. Business decisions should be motivated by economic rather than tax considerations. Taxpayers in similar situations carrying out similar transactions should be subject to similar levels of taxation. Efficiency: Compliance costs for businesses and administrative costs for the tax authorities should be minimised as far as possible.
- Certainty and simplicity: The tax rules should be clear and simple to understand so that taxpayers can anticipate the tax consequences in advance of a transaction, including knowing when, where, and how the tax is to be accounted.
- Effectiveness and fairness: Taxation should produce the right amount of tax at the right time. The potential for tax evasion and avoidance should be minimised while keeping counteracting measures proportionate to risks involved.
- Flexibility: The systems for taxation should be flexible and dynamic to ensure that they keep pace with technological and commercial developments. [64]

[61] The OECD international VAT /GST Guideline 2015:12
[62] The OECD international VAT /GST Guidelines 2015:13
[63] The OECD international VAT /GST Guideline 2015:10
[64] The OECD international VAT /GST Guideline 2015:15

The neutrality principle was defined in the guidelines to include the absence of discrimination in a tax environment that is unbiased and impartial and the elimination of undue tax burdens as well as disproportionate or inappropriate compliance costs for businesses.

If the neutrality principle is applied in the context of VAT output on loyalty programmes, it would follow that in order to achieve neutrality, there should be clear guidance from the tax authority on how output VAT should be accounted for by a VAT vendor. Devising guidelines that achieve this can prove to be very challenging given the multitude of loyalty programmes that exist within the South African market.

With regards to the application of the efficiency principle in devising guidelines or legislation for the treatment of output VAT relating to loyalty programmes, there should not be an added administration or compliance cost to VAT vendors.

As noted above, legislation should be clear and simple to understand in order for VAT vendors to know what the output VAT consequences are of making sales of goods and/or services utilising loyalty points. Currently, as seen in Chapter 4, VAT vendors have different VAT consequences relating to these transactions.

In respect to effectiveness and fairness, the legislation or guidelines should ensure that the right VAT is calculated and declared to SARS at the correct point of the loyalty programme transaction cycle.

In terms of flexibility, the legislation or guidelines, need to take into account the diversity of loyalty programmes in the South African market. These loyalty programmes have not all been discussed in this paper because of the limitation addressed in the introduction of the paper. The guidelines will need to cater for the different terms and characteristics of the loyalty programmes to achieve flexibility.

6.3 Australia

There similarities in the VAT legislation between South Africa and Australia. Additionally, Australia also has loyalty programmes operating in the country and they have attempted to issue guidance on treatment of loyalty programmes which are going to be explored in this section.

6.3.1 GSTR 2012/1

The ATO issued a ruling on GST implications for loyalty programmes, goods and services tax: Loyalty programs ("GSTR 2012/1") in 2012.

The aim of the ruling as set out GST 2012/1 was to consider:

(a) Whether it is necessary to apportion some consideration to the supply of points, when a member pays the consideration to purchase goods or services and as a consequence has points allocated to them;
(b) Whether a payment from a program partner to the loyalty program operator is consideration for a supply;
(c) The extent that such a payment is consideration for a supply, how is that supply characterised? Specifically, the ruling considers the implications of such characterisation in determining whether the supply is to any extent GST-free or input taxed;
(d) Whether the provision of a reward to the member (upon redemption of points by them) is a supply to the member for consideration;
(e) Whether any payments made by the loyalty program operator to a redemption partner is consideration for a supply made by the redemption partner to the loyalty program operator, or is instead consideration for the supply of the reward made to the member; and
(f) Whether the redemption partner makes a supply to the program member, even if it also makes a supply to the loyalty program operator.[65]

The contents of the ruling will be discussed to determine whether they can apply to the South African context. It should be noted that only sections of the ruling that are relevant for purposes of this paper will be discussed. In order to do this, it is important to also set forth some definitions defined in the ruling:

- A 'program member' or 'member' means an individual that joins a loyalty program pursuant to a loyalty program membership agreement between them and the loyalty program operator;
- A 'loyalty program operator' or 'operator' means the entity responsible for the operation of the loyalty program, which has agreements with members and (where applicable) program partners and redemption partners. In some cases, the operator may administer the loyalty program; in other cases it may outsource the administration to a third party;
- A 'points fee' means a fee charged by a loyalty program operator to a program partner for the allocation of points (or bonus points) to customers of the program partner. The fee is charged on a periodic basis and calculated by reference to the number of points or bonus points provided to the program partner's customers. In some loyalty programs, a program partner may be charged other fees in addition to, or instead of, a points fee;
- A 'program partner' means an entity that participates in a loyalty program run by the loyalty program operator, upon payment of a points fee. In some cases a program partner is also a redemption partner;
- A 'redemption partner' means an entity that is engaged by the loyalty program operator to provide rewards to members of the loyalty program. In some cases a redemption partner is also a program partner;
- 'Loyalty points' is a reference to any record-keeping mechanism (usually, but not necessarily, called points) which is used to ascertain the member's eligibility for rewards. However, it does not include rights to goods or services in the form of vouchers within the meaning of section 100-25; and
- 'Redemption of points' is a reference to the exchange by a member of loyalty points for goods or services. The goods or services may be provided by a redemption partner or the loyalty program operator.[65]

[65] Goods and Services ruling loyalty program, (2012) (http://law.ato.gov.au/atolaw/view.htm?DocID=GST/GSTR20121/NAT/ATO/00001#P44) (accessed 2017-12-15)

GSTR2012/1 applies to loyalty programme operators, members, programme partners and redemption partners. It also applies to loyalty programmes that have been established by a loyalty programme operator.

Additionally, the loyalty must have the following features according to the ruling; the loyalty programmes operator must grant loyalty points to a loyalty programme member as a result of the loyalty programme member making an eligible purchase of goods and services. The price paid by the loyalty programme member for making the eligible purchase is the same as the price that a non-member would pay, the loyalty points cannot be transferred for cash or redeemed as cash, the loyalty programme operator can track the points earned by the loyalty programme member. The value of the points earned when purchasing goods or services is lower than the value of the goods or services and when the points are redeemed, the reward must depend on the number of points earned.[66]

The description of the loyalty programme structure described above is similar to the description in Chapter 2 as defined in the Consumer Protection Act as well as in the different loyalty programmes described in the same chapter. This indicates the importance of this ruling in the pursuit to find answers to the research question.

It ruled that when a loyalty programme member pays consideration for goods or services and gets allocated points as a result, the payment is consideration for the acquired goods or services and there should not be an apportionment between the goods or services and the points [66].

Per the ruling, the redemption of points by a member is not consideration for the supply of a reward to the member. Accordingly, the supply of the reward can only be a taxable supply by the operator or redemption partner to the member where some consideration is provided, for example under a points plus pay arrangement.[66]

The ruling goes further to say,

> when a redemption partner provides goods or services to the member upon redemption of points (or upon redemption of points plus additional consideration) under a contractual arrangement between the

[66]Goods and Services ruling loyalty program, (2012) (http://law.ato.gov.au/atolaw/view.htm?DocID=GST/GSTR20121/NAT/ATO/00001#P44) (accessed 2017-12-15)

redemption partner and the loyalty program operator, the redemption partner also makes a supply to the loyalty program operator. A payment from the loyalty program operator to the redemption partner, in return, is consideration for this supply.[66]

What the ruling is unclear on is whether a purchase made by the loyalty programme member subsequent to the redemption of the points will constitute consideration for goods or services obtained by the member. In other words, will payment for goods or services using loyalty points would constitute consideration.

6.4 New Zealand

New Zealand has a more established VAT system with the legislation being established in 1985, guidance was sought from New Zealand's VAT legislation in the drafting of the South African VAT legislation.

6.4.1 Interpretation Statement

The New Zealand Inland Revenue Authorities (NZIR) issued an interpretation statement relating to multiple or single supplies in relation to Goods and Services Tax. Although this interpretation was not issued to exclusively and specifically deal with issues relating to GST on loyalty points, there are contents in the interpretation statement which may be essential in providing guidance for the topic at hand.

There is an example provided for in the interpretation statement which is as follows:
Loyalty points with a credit card

- Electronics Ltd (an electronics retail chain) operates a customer loyalty programme in its retail stores. Registered customers receive loyalty points for shopping at Electronics Ltd and these loyalty points entitle them to future discounts at Electronics Ltd;
- New Bank wants to expand its credit card business. It decides to enter into an arrangement with Electronics Ltd. Under the terms of the arrangement, New Bank and Electronics Ltd intend to provide additional loyalty points in Electronics Ltd's loyalty programme to registered customers who use the New Bank credit card to purchase goods from Electronics Ltd.

Electronics Ltd wants to know how it should treat the services it supplies to New Bank for GST purposes.[67]

[67] New Zealand Inland Revenue, Interpretation Statement: IS 17/03: Goods and Services Tax-Single supply or multiple supply, 2017:18 (https://www.ird.govt.nz/resources/a/9/a9ef4aac-bff1-4e12-9415-804a3041e921/is1703.pdf) (accessed 2017-11-23).

It is noted that this example not only deals with loyalty programmes but also deals with how the transaction described above should be treated as a single or double supply.

Should any of the services be exempt as a separate supply of financial services?
No. The services are all part of a single composite supply of standard-rated marketing and promotional services. The contract between New Bank and Electronics Ltd provides for the supply of several services from Electronics Ltd to New Bank. The focus must be on what is supplied to the recipient. The recipient of these services is New Bank, despite the fact some of the services are supplied directly to New Bank's customers (for example, answering questions about the loyalty programme) (NZIR, 2017:18).

The supply could be broken down into separate elements (some taxable at the standard rate and some exempt). However, this would not appropriately reflect what is supplied to the recipient, New Bank. The supply from Electronics Ltd to New Bank is a supply of all the elements. From New Bank's perspective, it has contracted with Electronics Ltd for the supply of all those elements as a single package of marketing and promotional services. It is helpful to consider the relationship between the different elements of the supply when deciding whether Electronics Ltd has made one composite supply or multiple separate supplies to New Bank (NZIR, 2017:19).
This example shows what was confirmed by the Australian GSTR 12/1, that the payment made by a loyalty programme partner to a redemption partner / loyalty programme operator is consideration in return for a supply.
The question that this example does not answer is what happens when the Electronics Ltd customers eventually earn enough points and redeem those points to utilise them in part settlements of purchases made at Electronics Ltd stores. Is the payment made using those points treated as consideration for the supply of the goods?

6.4.2 Technical Alert: Amendment to legislation

In 2009, New Zealand made amendments to its Goods and Services Tax Act 1985 ("GST Act") to allow particular loyalty programme operators to postpone the charging of GST until the redemption of loyalty points to ensure that GST is being paid at the accurate rate.[68]

[68] New Zealand Inland Revenue, Technical Area Tax Area: GST and loyalty points. (2009) (http://www.ird.govt.nz/technical-tax/legislation/2009/2009-34/2009-34-other-policy-matters/2009-34-op-gst-and-loyalty/) (accessed 2017-10-20)

In a technical alert found on the NZIR website, the NZIR explained the reasons for the need for a change in legislation. In the background, it highlighted the fact that:

> GST is charged on goods and services consumed in New Zealand. Since exported goods and services are consumed outside of New Zealand, as a general rule, exports of goods and services are zero-rated. Zero-rating allows a supplier of goods and services not to charge GST, but to still be able to claim input tax deductions.[69]

It was indicated in the alert that:

> before the current amendment to the GST Act, because of the involvement of an intermediary, supplies of what are normally considered zero-rated goods or services could be subject to GST at the standard rate. For example, a loyalty programme operator (such as an airline) could enter into a transaction with a purchaser whereby the purchaser paid consideration to the loyalty programme operator for crediting loyalty points to a customer. The customer would later redeem the loyalty points for a zero-rated reward supplied by the loyalty programme operator. By imposing GST on the loyalty points at the time they were issued, GST was in effect imposed on what would normally be a zero-rated supply. This anomaly would not exist if the supply was acquired directly from the operator for a monetary consideration instead of through the use of loyalty points.[69]

In terms of the NZIR, the amendment to the GST Act allows certain loyalty programme operators to defer the imposition of GST until such time as the nature of the reward and the normally applicable GST rate is known.

The amendments of the GST Act included the amendment of sections 9(9), 9(10), and 11C. The keys features of the amendments were follows:

- New section 9(9) of the GST Act allows certain loyalty programme operators to defer the imposition of GST on a sale of loyalty points to another person until such time that the loyalty points are redeemed;
- New section 11C specifies the requirements which have to be satisfied before a loyalty points operator can defer the imposition of GST under section 9(9). A loyalty programme operator is able to use the rules if it makes supplies for consideration under an arrangement with another person to provide loyalty points to a third person and the following conditions are satisfied:
    - 25% or more of the loyalty programme operator's or its associated person's business involves the provision of zero-rated goods or services;
    - The operator or its associated person has a business activity outside the activity of operating a loyalty programme (the main business activity) and the loyalty points are able to be redeemed for rewards supplied by the operator or associate as part of the main business activity;
    - The loyalty programme operator is able to identify, at the time of the redemption of loyalty points, whether GST was imposed on the points in

[69] New Zealand Inland Revenue, Technical Area Tax Area: GST and loyalty points. (2009) (http://www.ird.govt.nz/technical-tax/legislation/2009/2009-34/2009-34-other-policy-matters/2009-34-op-gst-and-loyalty/) (accessed 2017-10-20)

question when they were issued or whether the GST liability was deferred until the redemption of points under proposed section 9(9).[70]

Although the change in the NZIR, allows for the deferral of GST on the sale of loyalty points, this change by the NZIR to the VAT Act to allow the deferral of charging GST on certain loyalty programme transactions shows that there is a possibility to make a policy change in the VAT legislation in South Africa to accommodate loyalty programmes in the current VAT legislation.

The alert goes on to further explain that, a new section 11C(6) of the GST states that the second requirement will still be satisfied if, in addition to being redeemable for rewards supplied by the operator's or associated person's main business activity, the loyalty points are able to be redeemed for a reward supplied by an operator's partner under an associated loyalty programme. [70]

What can be gathered from these changes instituted by the NZIR is that, after extensive consultation and robust research, the South African legislation is also capable of being amended to accommodate the various loyalty programmes available in the country and that if proper research is done, all the unique features that exist in these programmes will be catered for in the legislation.

The changes and commentary provided by the NZIR can also be used as guidance by the policy makers and stakeholders in enacting the change in the current VAT legislation to deal with the output VAT and other VAT implications on loyalty programmes in South Africa.

[70] New Zealand Inland Revenue, Technical Area Tax Area: GST and loyalty points. (2009) (http://www.ird.govt.nz/technical-tax/legislation/2009/2009-34/2009-34-other-policy-matters/2009-34-op-gst-and-loyalty/) (accessed 2017-10-20)

Chapter 7: Conclusion

Loyalty programmes are an integral part of South Africa's economy, especially within the retail market. They are used by companies to incentivise loyalty and build stronger relationships with customers. That being said, VAT has a huge impact in the loyalty programme landscape of South Africa.

As seen in this research report, there are differences amongst stakeholders in the application and interpretation of the current VAT legislation relating to VAT on loyalty points. As it stands, the guidance in terms of legislation relating to the treatment of VAT on loyalty points is very limited. This poses a risk in different stakeholders interpreting and applying the current VAT principles differently when accounting for output VAT on transactions that are entered into using loyalty programmes. Four years down the line, there has not been any feedback from SARS regarding the last discussion paper issued in 2014.

The research problem stated at the beginning of the research report was that there is currently no authoritative VAT legislation governing the output VAT treatment of purchases made by means of points earned through a loyalty programme. This creates a problem for VAT vendors in applying the current VAT legislation to account for output VAT on aforementioned transactions. In this regard, the main research question that needed to be answered was how VAT vendors should account for output VAT on transactions made by means of loyalty points?

The report looked at the top six loyalty programmes in South Africa and of those six, four were further investigated to try and understand how they account for VAT output on transactions made using loyalty points. The results of that exercise highlighted the uncertainty and differences that exists in the South African market regarding the application of the current legislation in these kinds of transactions.

After all the facts and arguments set out in this report with the exception of the Dischem Benefit programme, the conclusion is that, payments made by the utilisation or redemption of loyalty points should not be included in consideration for purposes of determining the amount of output VAT to be declared by a VAT vendor to SARS. The argument is that when goods or services are paid for in part using loyalty points, the VAT vendor does not receive any fundamental monetary or tangible value for the portion paid for in loyalty points. In this regard, the vendor will need to declare a higher output value to SARS which will leave the vendor out of pocket.

Given the above information the following proposals are made:

- Further consultation should be done with the relevant stakeholders (including retailers, loyalty programme operators , loyalty programme partners, tax advisors, legal advisor), in order to understand the underlying issues that are faced by the various stakeholders;
- Feedback on the 2014 discussion paper on which public comment was requested needs to be given by SARS to the public. This might shed some light on what the way forward is regarding the VAT treatment of loyalty programmes;
- If legislative changes are required, the definition of consideration as defined in the VAT Act should be amended to insert the exclusion of loyalty points. This will specifically exclude loyalty points from the definition of consideration for reasons stated above;
- In order to promote the principles of neutrality, efficiency, certainty, flexibility, fairness and effectiveness and as promised in the 2016 national budget, specific provisions dealing with the VAT treatment of loyalty points should be drafted and included in the VAT Act. To give certainty to the stakeholder on how the transactions should be treated;
- The various stakeholders might need to relook at the terms and conditions of their loyalty programmes, some of the terms and conditions may push them into having to account for loyalty points as consideration as it is currently defined, SARS could also provide guidance to the stakeholders in this regard.

As noted in the introduction, this research report is limited in its scope and further research areas need to be conducted to explore further aspects of VAT implications of loyalty programmes in South Africa. These areas include the following:

- For entities in multiple loyalty programmes, whether an entity or a loyalty program operator, is making a taxable supply to a program partner where it allocates points to nominated customers of the loyalty program partner in return for a points fee;
- Whether fees paid to a loyalty points redemption partner by a loyalty points operator for the redemption of loyalty points can be claimed as an input from SARS (that is as part of a marketing expense as loyalty programmes can be seen as a way to encouraging customer loyalty and even building a new customer base);
- In addition to the points fees, whether any other costs related to the running and functioning of the loyalty programmes can be claimed as input tax.

References

Books

- Kruger, D, Bennett, A, Divaris, C and Stein, M. (1992). *Juta's Value-Added Tax Manual*. Cape Town: Juta and Company Limited.
- *Oxford concise dictionary, 2 ed.* (2010). Cape Town: Oxford University Press Southern Africa (Pty) Ltd.

Journal articles

- Brink, S.M. (2013). 'The accounting treatment of single-company client loyalty programme', *Journal of Economic and Financial Sciences*, Vol. 6, no. 3, pp. 795-814.
- Brink, S.M. (2014). 'An evaluation of the Income Tax treatment of client loyalty programmes transactions by South African suppliers', *Journal of Economic and Financial Sciences*, Vol. 8, no. 1, pp. 145-164.
- Sharp, A. and Sharp B. (1997). 'Loyalty Programs and their impact on repeat purchase loyalty patterns', *Journal of Research in Marketing*, Vol. 14, pp. 476-486.
- Van Zyl, S.P. (2013). 'The VAT treatment of vouchers: a comparative study between South Africa and the European Union', *The Comparative and International Law Journal of Southern Africa*, Vol. 46. no.2, pp 234-256.

Statues

Australia

- Goods and Services Tax Act 1999 (as amended).

South Africa

- Consumer Protection Act 68 of 2008 (as amended).
- Value-added Tax Act 89 of 1991(as amended).

Government reports

- National Treasury Republic of South Africa. (2016) *Budget Review,* Online (http://www.treasury.gov.za/documents/national%20budget/2016/review/default.aspx) (accessed 2016-12-13).

Discussion Papers

- Brits, P. (2013.) 'The Taxation of Interest Earned in Customer Loyalty Award Programmes in South Africa' Athens: ATINER'S Conference Paper Series, No: LAW2013-0872.
- South African Revenue Services. (2014). 'Discussion paper on the VAT treatment of Loyalty Programmes', (http://www.sars.gov.za/AllDocs/LegalDoclib/DiscPapers/LAPD-LPrep-DP-2014-01%20-%20Discussion%20Paper%20on%20VAT%20Treatment%20of%20Loyalty%20Programmes.pdf) (accessed 2017-03-25).

Online Resources

- Australian Tax Authorities. (2012). Goods and Services Tax Ruling: Loyalty programs, (http://law.ato.gov.au/atolaw/view.htm?DocID=GST/GSTR20121/NAT/ATO/00001#P44) (accessed 2017-12-15).
- Australian Tax Authorities. (2012). Goods and Services Tax and points fee in a loyalty program, ATO ID 2013/1 (http://law.ato.gov.au/atolaw/view.htm?docid=%22AID%2FAID20131%2F00001%22) (accessed, 2017-12-15).
- Clicks club card programme as described on the clicks website, (https://clicks.co.za/clubCardPage) (accessed, 2017-09-21).
- CNBC Africa. (2016). Retailing in South Africa: Do customer loyalty programs really work?, (https://www.cnbcafrica.com/news/southern-africa/2016/07/15/retailing-in-south-africa-do-customer-loyalty-programs-really-work/) (accessed 2017-12-01)
- De wet, C. (2016). 'The VAT treatment of loyalty programmes', (http://www.thesait.org.za/news/304977/The-VAT-Treatment-of-Loyalty-Programmes-.htm) (accessed 2016-12-13).
- Dis-Chem loyalty programme as described on the Dis-Chem website, Online (https://dischem.co.za/loyalty-terms-and-conditions) (accessed 2017-11-18).
- eBucks programmes as described on the eBucks website. (https://www.ebucks.com/web/eBucks/aboutus/, accessed 2017-09-20).
- Edgars loyalty programme, Online (https://www.thanku.co.za/terms/) (accessed 2017-10-31).

- European Commission- Directorate for General Taxation and Customs Union. (2007). Modernising the Value-added Tax treatment of vouchers and related issues, (http://ebiz.pwc.com/wp-content/uploads/2014/12/summary_report_consultation_vouchers_en.pdf) (accessed, 2017-10-12).
- Grobbelaar, C and Swanepoel, J. (2014). 'VAT Treatment of loyalty programmes', (http://www.thesait.org.za/news/news.asp?id=180533) (accessed 2016-12-13).
- Loyalty box. (2015) (http://www.theloyaltybox.com/blog/loyalty-ideas/what-you-can-learn-from-south-african-loyalty-programs/) (accessed 2018-01-17).
- Meyburgh, A. (2014). 'VAT and loyalty programmes', Online (https://www.sablog.kpmg.co.za/2016/04/vat-and-loyalty-programmes/) (accessed 2017-03-25).
- New Zealand Inland Revenue, Interpretation Statement: IS 17/03: Goods and Services Tax- Single supply or multiple supply. (2017) (https://www.ird.govt.nz/resources/a/9/a9ef4aac-bff1-4e12-9415-804a3041e921/is1703.pdf) (accessed 2017-11-23).
- New Zealand Inland Revenue, Technical Area Tax Area: GST and loyalty points. (2009) (http://www.ird.govt.nz/technical-tax/legislation/2009/2009-34/2009-34-other-policy-matters/2009-34-op-gst-and-loyalty/) (accessed 2017-10-20).
- OECD International guidance on VAT/GST. (2015). (http://www.oecd.org/tax/consumption/international-vat-gst-guidelines.pdf) (accessed 2018-01-20).
- Oosthuizen J. (2014). Loyalty programmes expand in South Africa (http://www.bizcommunity.com/Article/196/458/115433.html) (accessed 2018-01-20).
- South Africa Revenue Service, 'Value-added tax treatment of voucher', Draft Interpretation. (2014). (http://c.ymcdn.com/sites/sait.site-ym.com/resource/resmgr/2014_SARS/LAPD-LPrep-Draft-2014-19_-_D.pdf) (accessed 2018-02-20).
- South African Revenue Service, 'income tax and Value-added Tax consequences of a customer loyalty scheme', *Binding Class Ruling 055. (2016).* (http://www.sars.gov.za/AllDocs/LegalDoclib/Rulings/LAPD-IntR-R-BCR-2016-07%20-%20BCR055%20Income%20tax%20and%20VAT%20consequences%20of%20a%20customer%20loyalty%20scheme.pdf) (accessed 2017-03-25).

- South African Revenue Services, ‘Supplies made for no consideration’, Interpretation note No. 70. (2013) (http://www.sars.gov.za/AllDocs/LegalDoclib/Notes/LAPD-IntR-IN-2013-03%20-%20IN70%20Supplies%20made%20for%20no%20consideration.pdf) (accessed 2017-09-12).
- Truth, The 2016 truth loyalty whitepaper (2016) ‘The current state of loyalty programmes in South Africa’. ‘The current state of loyalty in South Africa’, (http://truth.co.za/wp-content/uploads/Truth-Whitepaper-October-2016.pdf) (accessed 2016-11-12).
- Truth, The 2017 truth loyalty whitepaper (2017) ‘South African loyalty landscape’, (http://truth.co.za/wp-content/uploads/Truth-Whitepaper-October-2017.pdf) (accessed 2018-03-23).
- Woolworths WRewards as described on the Woolworths website, Online (http://www.woolworths.co.za/store/fragments/wrewards/wrewards-index.jsp?content=../lookbook/lookbook-multiple&contentId=cmp207958&context=how-it-works) (accessed 2017-09-27).