

(21 November 2001 – to date)

INCOME TAX ACT 58 OF 1962

(Gazette No. 250, Notice No. 827, dated 29 May 1962. Commencement date: 1 July 1962)

REGULATIONS MADE UNDER SECTION 12G(7) OF THE INCOME TAX ACT, 1962 (ACT NO. 58 OF 1962)

Government Notice R1227 in Government Gazette 22848 dated 21 November 2001. Commencement date: 21 November 2001.

By virtue of the power vested in me by section 12G(7) of the Income Tax Act, 1962, I, Trevor Andrew Manuel, Minister of Finance, in consultation with the Minister of Trade and Industry, hereby make the regulations as set out in the Schedule hereto.

T A MANUEL
MINISTER OF FINANCE

SCHEDULE

TABLE OF CONTENTS

1. Definitions
2. Criteria for Strategic Industrial Project
3. Criteria for Qualifying Strategic Industrial Project With or Without Preferred Status
- 4.

1. Definitions

- 1.1. In these regulations, unless the context otherwise indicates, any word or expression to which a meaning has been assigned in the Income Tax Act, 1962, bears the meaning assigned thereto, and –

"date of commercial production" means the month in which the project reaches 50 per cent of its production capacity;

"the specified period" in relation to any condition that a strategic industrial project is required to meet, means the period beginning from the date of commercial production and continuing for a period of three years after that date, or such shorter or longer period approved by the Minister on recommendation of the adjudication committee;

"South African production" excludes for the purposes of regulations 2 and 3, any production of any other project which has been approved as a qualifying strategic industrial project under the provisions of section 12G of the Income Tax Act, 1962.

Computer and computer related activities as well as research and development activities

- 1.2 For the purposes of paragraphs (b) and (c) of the definition of "industrial project" in section 12G(1), "computer activities and computer related activities" and "research and development" shall have the same meaning as defined in terms of the most recent Standard Industrial Classification as issued by Statistics South Africa under the following headings –

(a) Computer and Computer Related Activities

<i>SIC-code</i>	<i>Industry description</i>
8610	Hardware consultancy
8620	Software consultancy and supply
8630	Data processing (other than standard secretarial services)
8640	Data base activities

(b) Research and Development

<i>SIC-code</i>	<i>Industry Description</i>
8710	Research and experimental development on natural sciences and engineering

2. Criteria for Strategic Industrial Project

Increase in production and displacement

- 2.1 In determining whether an industrial project will increase production of a South African industrial sector after taking into account any displacement within that industry sector, as contemplated in section 12G(4)(b), the Minister must be satisfied that –

- (a) the project will not result in a net reduction in jobs in the sector in which the project is classified;
and

- (b) the expected loss in production for other South African businesses within the same industry sector does not exceed 40 per cent of the production expected from that industrial project, and for this purpose –
 - (i) the 40 per cent limit must be complied with during each year of the specified period;
 - (ii) an industry sector to be measured is the lowest available sic-code major grouping, grouping or sub-grouping associated with the project as issued by Statistics South Africa;
 - (iii) production will be measured in units (or in gross sales if units are not available or do not provide an appropriately similar comparison); and
 - (iv) an applicant may prove that the industrial project will not exceed the 40 per cent limit for each year of the specified period by –
 - (aa) demonstrating that the total existing level of South African production does not exceed 40 per cent of the total production that is consumed by the relevant market and for this purpose, displacement of South African and other production will be deemed to take place in proportion to their relative percentages of the total market involved, as measured at the time of the application for approval as a qualifying strategic industrial project; or
 - (bb) demonstrating that the strategic industrial project will achieve a level of production of at least 250 per cent of the total existing level of South African production, as measured at the time of application for approval as a qualifying strategic industrial project; or
 - (cc) providing facts and circumstances that demonstrate that the displacement caused by the industrial project will not otherwise exceed 40 per cent of the total level of South African production which existed at the time of the application for approval as a qualifying strategic industrial project.

Expansion of existing industrial project

2.2 In determining whether an expansion of an existing industrial project will significantly increase production as compared to that of the existing industrial project, as contemplated in section 12G(4)(c), the production expected from the expansion and the existing industrial project must equal at least 135 per cent of the production generated from the existing industrial project operating at full capacity, and for this purpose –

- (a) production will be measured in units (or in gross sales if units are unavailable or do not provide an appropriately similar comparison); and

- (b) the 135 per cent threshold must be achieved and then maintained during the specified period.

Concurrent benefits

2.3 For the purposes of section 12G(4)(d), -

- (a) a company will be regarded as receiving a concurrent benefit under –
 - (i) section 37E of the Income Tax Act, 1962, if that company becomes entitled to any deduction as contemplated in that section after the date of approval of a project carried on by that company as a qualifying strategic industrial project in terms of section 12G(5); or
 - (ii) section 37H of the Income Tax Act, 1962, if the company carrying on the industrial project will enjoy tax holiday status after the date of approval of that project as a qualifying strategic industrial project in terms of section 12G(5); and
- (b) an industrial project will receive a concurrent investment incentive provided by the national sphere of government if that project, during any year in which the company carrying on the industrial project may be entitled to any additional industrial investment allowance in terms of section 12G(2), receives concurrent benefits under –
 - (i) the Regional Industrial Development Programme, which came into operation on 1 May 1991;
 - (ii) the Simplified Regional Industrial Development Programme, which came into operation on 1 October 1993;
 - (iii) the Motor Industry Development Programme, which initially came into operation on 1 September 1995;
 - (iv) the Small Medium Manufacturing Development Programme, which came into operation on 1 October 1996;
 - (v) the Productivity Asset Allowance, which came into operation in July 2000; or
 - (vi) the Small Medium Enterprise Development Programme, which came into operation on 1 September 2000;
- (c) previously allowed deductions or mere enjoyment of tax holiday status during any period before approval in terms of section 12G(5), must not be regarded as a concurrent benefit.

Industrial participation project

- 2.4 For the purposes of section 12G(4)(e) an industrial project will constitute an industrial participation project if that project or any company involved or associated with this project, during any year in which the company carrying on the industrial project may be entitled to any additional industrial investment allowance in terms of section 12G(2), claims any credits or benefits for this project under the National Industry Participation Program or Defence Industrial Participation Programme.

Long-term commercial viability

- 2.5 For the purposes of section 12G(4)(f), an industrial project must demonstrate long-term commercial viability by providing sufficient information to prove that the project's estimated pre-tax earnings to sales ratio equals or exceeds the domestic or international industry average for businesses within the lowest available sic-code major grouping, grouping or subgrouping associated with the project, as issued by Statistics South Africa, and for this purpose –
- (a) a pre-tax earnings to sales ratio is measured as the ratio of net income to sales turnover;
 - (b) the viability determination must be achieved within five years from the date of commercial production.

3. Criteria for Qualifying Strategic Industrial Project With or Without Preferred Status

Points system

- 3.1 The Minister of Trade and Industry must, in terms of section 12G(5), approve a strategic industrial project as a qualifying strategic industrial project –
- (a) where the strategic industrial project achieves at least 4 out of the 10 potential points in terms of the criteria contemplated in section 12G(5);
 - (b) having preferred status, where the strategic industrial project achieves at least 6 out of the 10 potential points in terms of the criteria contemplated in section 12G(5).

Factors and points allocation

3.2 Upgrading industry

A strategic industrial project must be regarded as upgrading an industry within the Republic and must be awarded the number of points indicated, where –

- (a) that project utilises a process or offers a product that is –
 - (i) previously unused in, or new to, the Republic when the company with the project submits its application for approval as a qualifying strategic industrial project and that process or product has material significance for the South African market; or
 - (ii) already used or available within South Africa to the extent that the process or product first arose from another industrial project that previously received approval in terms of section 12G(5) and that process or product has material significance for the South African market:

Provided that such process or product –

- (aa) demonstrates material significance in terms of delivery time, reduced cost or increased quality of function or of longevity; and
 - (bb) could not be introduced to the South African market without a substantial capital investment; **(1 point)**
- (b) that project acts as a key component in an industry cluster existing within South Africa, so as to improve the cluster's competitiveness as a whole, and in this regard –
- (i) the addition of the project at a point within an industry cluster will substantially reduce cost, add quality in terms of function or of longevity or improve the efficiency of the industry cluster; and
 - (ii) a project will be deemed to be a key component in an industry cluster, if the applicant demonstrates –
 - (aa) that the project fills an identified gap within a cluster diagram of the Department of Trade and Industry, which diagram is acceptable to the adjudication committee; or
 - (bb) that the project fills an identifiable gap in an industry cluster; **(1 point)**
- (c) that project contains a value-added process, which adds at least 35 per cent value under the formula contemplated in regulation 4(b), for each year of the specified period. **(1 point)**

3.3 Business linkages

A strategic industrial project must be regarded as providing general business linkages and must be awarded the number of points indicated, where –

(a) the project will acquire –

(i) at least 20 per cent; or **(2 points) or**

(ii) at least 10 per cent, **(1 point)**

of its raw materials, intermediate products and services, based on the annual cost to the industrial project (including direct and indirect operating costs), from small, medium and micro enterprises (excluding any small, medium or micro enterprise which is a connected person, as defined in section 1 of the Income Tax Act, 1962, in relation to the company carrying on that strategic industrial project), which must be measured in each year of the specified period;

(b) an amount equal to at least 5 per cent of the cost of qualifying industrial assets for the project is expended over the six year period after the date of approval in terms of section 12G(5), in respect of the acquisition, erection, construction or improvement of physical infrastructure in the Republic, including public roads, sewerage, underground telephone lines and other physical infrastructure which is freely available for general public use. **(1 point)**

3.4 Direct and indirect employment creation

A strategic industrial project must be regarded as creating direct or indirect employment within the Republic and must be awarded the number of points indicated where, before the end of the specified period, the project will create at least –

(a) 6 full-time jobs **(4 points)**

(b) 5 full-time jobs **(3 points)**

(c) 4 full-time jobs; or **(2 points) or**

(d) 3 full-time jobs **(1 point)**

for each R1 million in cost of industrial assets directly incurred for the project.

4. For the purpose of –

(a) regulation 3.2(b), an "industry cluster" –

(i) involves a concentrated subset of industries interconnected by a flow of purchases and sales that are stronger than the rest of the economy; and

- (ii) entails linkages throughout the value chain, from suppliers to end producers as well as support and specialised infrastructure;
- (b) regulation 3.2(c), the value-added shall be determined in accordance with the formula –

Gross Project Receipts - Material Inputs

Gross Project Receipts

where –

- (i) "gross project receipts" include all gross income other than income from investment and finance (such as interest, dividends, sales of financial instruments and currency transactions); and
 - (ii) "material inputs" include the direct cost of all raw materials, intermediate products, energy and water used to produce gross project receipts;
- (c) regulation 3.3(a), a business will not qualify as a small, medium or micro enterprise where –
- (i) more than 200 full-time employees are formally employed by that business; or
 - (ii) the annual turnover of that business exceeds R50 million; and
- (d) regulation 3.4, jobs created from indirect employment will be determined as jobs added due to the increased sale of goods and services directly acquired by the project.