



March 2019

Employment Tax Incentive (ETI): To employment and beyond!

Recent changes to the ETI landscape

1. The ETI has been extended for an additional 10 years, to 29 February 2029¹.
2. As from 1 August 2018², employers can claim ETI in respect of SEZ qualifying employees. This is as a result of the broadening of the ETI from a “youth employment incentive”, to also apply as an additional incentive for Special Economic Zones (SEZs).
3. With effect from 1 January 2019³, the new National Minimum Wage (NMW) requires employers to remunerate employees at a minimum of R20 per hour.
4. As from 1 March 2019⁴, employers will be able to claim the maximum value of R1 000 per month for employees earning up to R4 500 monthly (previously R4 000), with the incentive tapering to zero at the maximum monthly income of R6 500. The value of the incentive halves during the second twelve-month period where an employer claims the ETI in respect of a specific employee.

Summary of the ETI

- The ETI is primarily a government incentive, aimed at encouraging the private sector to employ young people (from 18 to 29), earning below R6500/month (from 1 March 2019).
- The ETI can operate in conjunction with Skills Development Levy (SDL) claims, the section 12H tax incentive, and the Youth Employment Scheme (YES).
- ETI is limited to 24 ‘claiming’ months per qualifying employee.
- ETI claims are predominantly facilitated as part of the employees’ tax reporting process, wherein employers utilise the ETI that they claim, by setting it off against the employees’ tax payable.
- Significant benefits may be available to industries that employ individuals at below R6500.

The status of the ETI

The ETI is now 5 years old. From the perspective of the average tax instrument, it means that the ETI is still in its infancy. It follows that practical situations still arise often that may require policy direction, legislative amendments, interpretational clarity or system development.

SARS has issued a Guide⁵ that has gone a long way towards managing taxpayer interpretation queries and concerns. The biggest stumbling block currently is the ETI administration, both from the side of the employer, and from SARS.

The original limited timeframe of the ETI (initially a 3-year and then a further 2-year period), led to an understandable reluctance on the part of the private sector, Government, and SARS to expend any more than absolutely necessary on system infrastructure and general marketing to maintain and manage the risks associated with the ETI.

Risk areas

Employers have a number of risk areas that must be addressed in order to ensure that their ETI claiming process is robust from a risk perspective. Amongst the most common concerns are employer tax non-compliance, incorrect payroll mapping, retrospective payroll transactions, payroll tracking of the relevant claiming month, and the non-capturing of pertinent details (e.g. hours, terminations, etc.).

On SARS' side, it appears that some of the SARS systems are not fully aligned with the ETI Act.

Practically, ETI claims can be denied at the point of submission of the EMP501 reconciliation wherein the ETI is claimed, or after that reconciliation has been submitted (e.g. due to SARS' risk analysis of the data submitted or following an audit finding). Currently, any ETI that is denied (whether legitimately or not), leads to an underpayment being indicated against PAYE, SDL, and UIF. These seeming 'debts' are open for debt collection action and can lead to an employer being unable to obtain a Tax Clearance Certificate to indicate a positive tax compliance status.

The legitimate denial of an ETI claim after submission, and the resultant interest and penalties flowing from an underpayment of employees' tax are risks that any employer claiming ETI must contend with. The greatest concern currently, is the effective denial of ETI, through blocks on the e@syFile TM software that prevent employers from claiming ETI at the point of submission of the annual and bi-annual reconciliation (EMP501).

In practice, an employer may not be able to submit its EMP501 reconciliation, because the SARS system currently blocks the claiming of ETI on the basis that the quantum of the ETI as per the EMP501 reconciliation:

1. May not differ from the quantum of the total ETI claims reported as per the IRP5 tax certificates. This block is legitimate in our view, since the reconciliation between tax certificates and the EMP501 is paramount in any tax reporting system.
2. May not be in excess of the quantum of the ETI claimed on the employer's monthly EMP201 returns. In our view, this block is not legislatively sound, since the employer is effectively systematically prevented from correcting an ETI reporting error, whilst at the same time being legislatively required to fix an employment tax reporting error, based on the same underlying cause.
3. May not utilise (as opposed to claim, but not utilise against employees' tax), ETI previously claimed in the employer's monthly EMP201 returns. However, legislatively employers that are tax compliant, may utilise ETI claimed in a previous tax period, subject to certain conditions.

Conclusion

The reach of the ETI has thus far been limited, and according to our experience it is mostly large employers with big potential ETI claims that justify the resources required to adequately risk manage ETI claims. Unfortunately it appears that for those employers reliant on payroll or manual calculations, who cannot afford a tax expert to monitor and manage the process, the risks often outweigh the benefits. The result, we believe quite unintentionally, is that small and medium sized businesses (SMEs) are indirectly being excluded from participation due to a lack of scale

In various analyses conducted⁶, the ETI has proven to be successful as an incentive aimed at combatting unemployment and, in particular, youth unemployment. However, in our experience, the barriers discussed above result in the effectiveness of the ETI being restricted.

We hope that the additional 10 year timeframe will provide the necessary certainty to all stakeholders to jumpstart and justify their significant investment in the ETI, and in particular its uptake in the SME sector.

SMEs are often referred to as the 'life-blood of our economy'. As such, we should all work towards enabling every small business in South Africa to absorb one young person (partly funded through the incentive), so that the person, now employee, may be up-skilled, and/or allowed access to education. The effect of such a common goal would be the gradual reduction of youth unemployment, creating hope for our future.

Endnotes

1. Section 102 of the Taxation Laws Amendment Act, No. 23 of 2018.

2. On 6 July 2018, the Minister of Finance published Gazette No. 41759, designating six SEZs for the purposes of section 6(ii) of the Employment Tax Incentive Act, No. 23 of 2016 (the ETI Act). A number of requirements must be met before an employee will be considered to be a qualifying employee for purposes of the ETI Act. Where the age requirement is not met, the SEZ requirement states in section 6(a)(ii), that the employee must be employed by an employer operating through a fixed place of business located within a designated SEZ, and that employee renders services to that employer mainly within that SEZ.

3. An employer may not claim the ETI if the relevant employee is not paid in accordance with any "wage regulating measure" applicable to that employer. Although the NMW is effective from 1 January 2019, it does not qualify as a "wage regulating measure" for the purposes of the ETI Act. It is expected that the ETI Act will be amended accordingly.

4. Clause 5 of the Rates and Monetary Amounts and Amendment of Revenue Laws Bill, 2019 published on 20 February 2019.

5. Guide to the Employment Tax Incentive (Issue 2), dated 4 June 2018 - <http://www.sars.gov.za/AllDocs/OpsDocs/Guides/LAPD-ETI-G01%20-%20Guide%20to%20the%20Employment%20Tax%20Incentive.pdf>

6. The Effects of the Tax Incentive on Youth Employment – Amina Ebrahim, Murray Leibbrandt & Vimal Ranchhod;

Quantitative Analysis of the Tax Incentive Act – Development Policy Research Unit; Employment Tax Incentive Evaluation – by Singizi Consulting (noting that these are preliminary findings in that the research has not yet been concluded).

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