



## Guidance on Value Added Tax (VAT)

The purpose of this circular is to provide guidance to municipalities on how to budget, transact and report for Value Added Tax (VAT) using the Municipal Standard Chart of Accounts (*mSCOA*) chart. This circular must also be read in conjunction with:

- The VAT Act, 1991 (Act No. 89 of 1991), and its amendments;
- The VAT 419 Guide for Municipalities;
- The VAT Reference Guide for Foreign Donor Funded Projects;
- MFMA Circular No. 48 (dated 2 March 2009);
- MFMA Circular No. 55 (dated 07 March 2011);
- MFMA Circular No. 58 (dated 14 December 2011); and
- MFMA Circular No. 59 (dated 16 March 2012).

### Content

1. Background .....	2
2. Where are the VAT accounts in the <i>mSCOA</i> chart?.....	2
3. Nature of VAT transactions in terms of the <i>mSCOA</i> chart .....	4
4. VAT on conditional grants .....	9
5. Foreign Donor Funded Projects .....	11
6. Conclusion.....	12

## 1. Background:

In terms of the VAT Act, 1991 (Act No. 89 of 1991) and its amendments, municipalities must be VAT registered and must declare Output tax on the taxable supply of goods and services and claim Input tax credits on expenses incurred in the course or furtherance of the enterprise (the taxable supplies). The output tax is declared and the input tax claimed by completing a VAT 201 return.

The South African Revenue Services (SARS) have issued the **VAT 419 Guide for Municipalities** and the **VAT Reference Guide for Foreign Donor Funded Projects** to provide guidance to municipalities to meet their VAT obligations.

These guides are available on the SARS and National Treasury websites on the following links:

<https://www.sars.gov.za/wp-content/uploads/Ops/Guides/LAPD-VAT-G08-VAT-419-Guide-for-Municipalities.pdf>

<http://mfma.treasury.gov.za/Guidelines/Pages/default.aspx>

## 2. Where are the VAT accounts in the mSCOA chart?

VAT is recorded as Output, Input and Capital Input tax. These VAT categories can be defined as:

- Output tax refers to the tax levied at the standard rate by a municipality or municipal entity on the taxable supply of goods or services i.e. electricity, water, waste management and waste water management;
- Input tax refers to the tax charged on and/or paid by a municipality or municipal entity on the acquisition of goods or services for purposes of making taxable supplies. VAT can only be claimed if the Municipality is in possession of a valid tax invoice from a registered vendor (VAT registered supplier). SARS perform audits regularly to determine if the VAT claimed is valid and in accordance with the VAT prescripts; and
- Capital Input tax refers to the tax paid by a municipality or municipal entity on the acquisition of capital goods in the form of assets or the payment for contractors for the construction of assets to be used in providing taxable goods or services. Input tax on Capital must be reported in a separate area on the VAT 201 return.

The VAT 201 is a monthly or bi-monthly VAT declaration that must be submitted by all VAT registered vendors as per the registered tax period. This return reflects the VAT for which the entity is liable to declare output tax and the amounts that can be deducted as input tax.

**Importantly, when municipalities prepare their MTREF budgets, it must be exclusive of VAT and therefore the regulated budget Tables A4 and A5 must be VAT exclusive.**

It should also be noted that the accounts for Input and Output Tax on the mSCOA chart is named Input and Output VAT and irrecoverable debt is referred to as bad debt. Therefore, where reference is made to the VAT accounts in the chart in the examples used to explain the VAT transactions, Input and Output VAT and bad debt is used as per the mSCOA chart. These discrepancies in the terminology will be corrected in version 6.6 of the chart.

The mSCOA long codes that provides the classification for the transactions for the Output, Input and Capital Input tax accounts, the full item description, where these accounts are contained in the mSCOA chart as well as the movement accounts that portrays the use of the mSCOA chart are listed below:

### Output tax accounts in the mSCOA chart

Long code	Item description
<b>Accrual of Output tax</b>	
IL001009001	Liabilities: Current Liabilities: VAT Credit Output Accrual: Opening Balance
IL001009002	Liabilities: Current Liabilities: VAT Credit Output Accrual: Recognised
IL001009003	Liabilities: Current Liabilities: VAT Credit Output Accrual: Transfers
<b>Output Tax on Payments received from Debtors</b>	
IL001010001	Liabilities: Current Liabilities: Output VAT : Opening Balance
IL001010002	Liabilities: Current Liabilities: Output VAT : Recognised
IL001010003	Liabilities: Current Liabilities: Output VAT : T transfers
<b>Output Tax on the Provision for the impairment of Doubtful Debt (Contra Account)</b>	
IL001011001	Liabilities: Current Liabilities: Output VAT : Provision for Doubtful Debt Impairment: Opening Balance
IL001011002	Liabilities: Current Liabilities: Output VAT : Provision for Doubtful Debt Impairment: Recognised
IL001011003	Liabilities: Current Liabilities: Output VAT : Provision for Doubtful Debt Impairment: T transfers
<b>VAT 201 - VAT Control Account</b>	
IL001008001	Liabilities: Current Liabilities: VAT Payable Control: Opening Balance
IL001008002	Liabilities: Current Liabilities: VAT Payable Control: T transfers
IL001008003	Liabilities: Current Liabilities: VAT Payable Control: Payments

As shown above, in the mSCOA chart the Output tax account is represented by the VAT Credit Output Accrual, Output VAT, Output VAT: Provision for Doubtful debts impairment and the VAT Payable Control accounts.

## Input tax general and capital accounts in the mSCOA chart

Long code	Item description
<b>Accrual of Input tax</b>	
IA001011001001	Assets:Current Assets: VAT Receivable: Input Accrual: Opening Balance
IA001011001002	Assets: Current Assets: VAT Receivable: Input Accrual: Recognised
IA001011001003	Assets: Current Assets: VAT Receivable: Input Accrual: Transfers
<b>Input tax on payments made to creditors</b>	
IA001011002001	Assets: Current Assets: VAT Receivable: Input VAT General: Opening Balance
IA001011002002	Assets: Current Assets: VAT Receivable: Input VAT General: Recognised
IA001011002003	Assets: Current Assets: VAT Receivable: Input VAT General: T transfers
<b>Input tax on payments made to creditors on Capital purchases</b>	
IA001011003001	Assets: Current Assets: VAT Receivable: Input VAT Capital: Opening Balance
IA001011003002	Assets: Current Assets: VAT Receivable: Input VAT Capital: Recognised
IA001011003003	Assets: Current Assets: VAT Receivable: Input VAT Capital: T transfers
<b>VAT 201 - VAT Control Account</b>	
IA001011004001	Assets: Current Assets: VAT Receivable: VAT Control: Opening Balance
IA001011004002	Assets: Current Assets: VAT Receivable: VAT Control: T transfers
IA001011004004	Assets: Current Assets: VAT Receivable: VAT Control: Receipts

As shown above, in the mSCOA chart the Input tax account is represented by the VAT Receivable Input Accrual, VAT Receivable Input VAT General, the VAT Receivable Input VAT Capital and VAT Receivable VAT Control accounts. The principle of handling Input VAT General and Input VAT Capital items is the same with the distinction of what is purchased: goods and services versus capital items.

The VAT control account that is used to show whether a VAT liability or a VAT asset should be reflected at the end of the financial period is also listed in the Output and Input VAT accounts contained in the mSCOA chart. The net VAT result is calculated per reporting period and transferred to the VAT control account.

### 3. Nature of VAT transactions in terms of the mSCOA chart:

Accrual of transactions, cash movement and declaration of VAT all have different posting levels in the mSCOA chart. The recording of the VAT portion of transactions on the mSCOA chart, including movement accounting, is explained in the examples below.

#### ***Invoice versus Payment basis for VAT***

The invoice basis means that Output tax must be paid to SARS in the month falling within the tax period that the account was issued to a consumer. Invoices for cash payments will attract output tax and this is payable at the earlier date of payment being received or an invoice being issued by the municipality. The municipality will not accrue for output tax but will transfer all output tax raised during billing to the output VAT liability and declare the

amount billed per tax period. The VAT liability is likely to be higher if a municipality operates on the invoice basis, depending on the circumstances. However, only a few municipalities are currently registered on the invoice basis.

The payment basis means that only the portion of the VAT received or paid must be declared to SARS in the period that the payment is made or received.

The treatment for invoice basis and payment basis applies to Output and Input tax.

The VAT Act allows municipalities and only those municipal entities that are supplying water, electricity, refuse removal and waste water services to register for VAT on the payment basis. Once payment for services rendered has been received will the municipality or municipal entity become liable to declare and pay VAT to SARS.

The VAT credit accrual account is used for all billing transactions where the amount owed to SARS is accrued to keep record of the VAT liability. When payment is received from debtors, the amount will be transferred from the VAT credit accrual (liability) to the VAT output account, and at the end of the tax period the amount received from the debtors' transactions and from any other VAT on cash received will be declared. The full amount is transferred from the VAT output account to the VAT control account. This process of transferring amounts to the different control accounts is utilised to ensure that the municipality or municipal entity keeps track of VAT payable and what amount will remain as a liability until payment is received from the consumers.

### **Output tax transactions**

#### *Example 1: Raising a receivable and receiving payment*

The municipality provides an account for electricity services sold to a consumer. The electricity sold is billed on the account of the consumer for R1 150 of which the VAT is R150 (currently 15 per cent). The total amount will be billed on the account and the electricity revenue will exclude the VAT amount. The billing and partial receipt of the account with the output tax treatment is explained in step 1 and step 2 below:

#### **STEP 1: Billing Transaction**

Account Description	Long code	AMOUNT (R)
DR: Assets: Trade Services and Customer Service Debtors: Electricity: Monthly billing	IA001010003001002	1150
CR: Revenue: Exchange Revenue:Service Charges: Electricity:Electricity Sales : Commercial Conventional	IR002006001008001	-1000
CR: Liabilities: Current Liabilities: VAT Credit Output Accrual: Recognised	IL 001009002	-150

#### **STEP 2: Receipting Transaction**

Account Description	Long code	AMOUNT (R)
DR: Assets: Current Assets: Cash and Cash Equivalents: Cash at Bank:Deposits	IA001001001001002	575
CR: Assets: Trade Services and Customer Service Debtors: Electricity: Collections	IA001010003001005	-575
DR: Liabilities: Current Liabilities: VAT Credit Output Accrual: Transfers	IL 001009003	75
CR: Liabilities: Current Liabilities: Output VAT : Recognised	IL 001010002	-75

The amount received at the end of the tax period is transferred to the VAT Control account as shown in step 3 and this amount will be used to complete the VAT 201 return with the total Output tax due to SARS.

**STEP 3: Transfer the output tax liability to the VAT control account**

Account Description	Long code	AMOUNT (R)
DR: Liabilities: Current Liabilities: Output VAT: Transfers	IL 001010003	75
CR: Liabilities: Current Liabilities: VAT Payable Control: Transfers	IL001008002	-75

At the end of the tax period the amount Output tax forms part of the VAT 201 declaration as a payable amount. Depending on, whether the Output tax or Input tax is higher, a payment will either be made to SARS, or a refund will be payable by SARS. Output and Input tax are offset in the VAT 201 return. For illustration purposes the VAT control account is explained in conjunction with the Input tax examples.

**Example 2: Impact on Output tax when Impairment of receivables**

In the event where a municipality provides for Impairment on Trade and other Receivables, the Output tax transaction will be recorded as indicated in the example below where the receivable (billing) is reduced by R230, the loss on impairment is R200 and R30 relates to a provision for doubtful debt on the Output tax. This is a control account that will be used to impair the Output tax liability figure in the reporting period. This does not affect the Output tax liability. Only once irrecoverable debt is written off in terms of the requirement of section 22 of the VAT Act will the Output tax liability be reduced.

**Impairment of Debt**

Account Description	Long code	AMOUNT (R)
DR: Gains and Losses: Trade and other Receivables from Exchange Transactions: Ele	IZ005007001	200
DR: Current Liabilities: Output VAT: Provision for Doubtful Debt Impairment: Recognise	IL001011002	30
CR: Current Assets: Trade Services and Customer Service Debtors: Impairment: Recog	IA00101000300100800	-230

**Example 3: Irrecoverable Debt written off**

When irrecoverable debt is written off, the Output tax accrual account must be reduced by the amount that was levied on the irrecoverable debt that is approved by Council to be written off. In the example below, R115 is written off as irrecoverable debt. The Trade Services account will be debited with R115, the irrecoverable debt to be written off is R100 and Output tax of R15 will be reversed on the VAT Credit Output Accrual account which means that the liability on the Output tax that is accrued will be reduced.

**Output Tax reduced when Irrecoverable debt is written of**

Account Description	Long code	AMOUNT (R)
DR: Expenditure: Bad Debts written off	IE001	100
DR: Liabilities: Current Liabilities: VAT Credit Output Accrual: Recognised	IL 001009002	15
CR: Assets: Trade Services and Customer Service Debtors: Electricity: Debt write off	IA001010003001006	-115

Irrecoverable debts relate to amounts actually written off and leads to output tax adjustments if the conditions in section 22 of the VAT Act are met. The VAT Act does not recognise "provisions" as supplies or adjustments to be made in respect of supplies.

The Output tax transaction for impairment of trade receivables and the irrecoverable debt written off does not form part of the calculation for the VAT 201 return. The above examples explain how these accounts will form part of the accounting for Trade receivables and how Output tax must be treated for irrecoverable debt written off as well as for the impairment of Trade receivables.

The Output tax accrual account presents the full amount that the municipality or municipal entity owes SARS, but only the portion paid by the consumers must be declared and paid to SARS at the end of each VAT reporting period. Municipalities will net-off the Output tax and the Input tax to determine if a payment must be made to SARS or if a refund must be claimed from SARS.

**Input tax transactions:**

Input tax consists of Input VAT General and Input VAT Capital. The VAT 201 return requires that Input tax on goods or services purchased for operational (taxable supply) and capital purchases must be declared separately under Input tax. The examples below explain the recording of Input tax when an invoice is received, and the expense is accrued. It should be noted that all Input tax transactions will be recorded against the six prescribed mSCOA segments. However, to simplify the guidance provided in this circular, only the transactions against the item segment will be explained.

Input tax will be accounted for during the process of accrual and when the payment occurs. The VAT that is paid to the supplier must be transferred to the Input tax account that can be claimed back from SARS.

**Example 4. Capturing an invoice**

The municipality receives an account from Eskom for electricity supplied. The municipality accrues for the expense in step 1 and then payment is made in step 2. The transaction for VAT is shown in step 1 and 2 below.

**STEP 1: Accrual of Input tax**

Account Description	Long code	AMOUNT (R)
DR: Bulk Purchase : Electricity: ESKOM	IE 002	200
DR: Assets: Current Assets: VAT Receivable: Input Accrual: Recognised	IA001011001002	30
CR: Current Liabilities: Trade and other Payables Exchange Transactions: Electricity Bulk purchase : Deposits	IL001006008002	-230

**STEP 2: Payment of the invoice**

Account Description	Long code	AMOUNT (R)
DR: Current Liabilities: Trade and other Payables Exchange Transactions: Electricity Bulk purchase : Withdrawals	IL 001006011003	230
CR: Assets: Current Assets: Cash and Cash Equivalents: Cash at Bank: Withdrawals	IA00100100100100100	-230
DR: Assets: Current Assets: VAT Receivable: Input VAT General: Recognised	IA001011002002	30
CR: Assets: Current Assets: VAT Receivable Input Accrual: T ransfers	IA001011001003	-30

As shown in the example below, a similar process is followed for *Input tax capital* on capital purchases where Input tax capital is accrued on the purchase of capital assets and is then transferred from the Input VAT Capital accrual to the Input VAT: Capital once the payment is made.

**STEP 1: Accrual of Input tax Capital**

Account Description	Long code	AMOUNT (R)
DR: Assets: Non Current assets: Electrical Infrastructure: In use: HV Switching station: Cost: Acquisitions	IA00201500100300100	2000
DR: Assets: Current Assets: VAT Receivable: Input Accrual: Recognised	IA001011001002	300
CR: Current Liabilities: Trade and other Payables Exchange Transactions: Payables and Accruals: Deposits	IL 001006011002	-2300

**STEP 2: Payment of the invoice on Capital purchase**

Account Description	Long code	AMOUNT (R)
DR: Current Liabilities: Trade and other Payables Exchange Transactions: Payables and Accruals : Withdrawals	IL 001006011003	2300
CR: Assets: Current Assets: Cash and Cash Equivalents: Cash at Bank: Withdrawals	IA00100100100100100	-2300
DR: Assets: Current Assets: VAT Receivable: Input VAT Capital: Recognised	IA001011003002	300
CR: Assets: Current Assets: VAT Receivable Input Accrual: Transfers	IA001011001003	-300

At the end of a VAT period the total amount of Input tax must be Transferred to the VAT Control Account: Current Assets: VAT Control.

**STEP 3: Transfer Input tax General and Capital to the VAT Control account**

Account Description	Long code	AMOUNT (R)
DR: Assets: Current Assets: VAT Receivable: VAT Control: Transfers	IA 001011004002	330
CR: Assets: Current Assets: VAT Receivable: Input VAT General: Transfers	IA001011002003	-30
CR: Assets: Current Assets: VAT Receivable: Input VAT Capital: Transfers	IA001011003003	-300

The final step in the VAT cycle is where the municipality either pays SARS the net VAT due (where output tax exceeds input tax and other deductions for the tax period) or receives the net amount of VAT claimed from SARS as a refund (where input tax and other deductions exceeds the output tax for the tax period).

Using the information above, the municipality owes SARS R75 Output tax and claims back R30 Input tax general and R300 Input tax capital. The net of these three amounts is (R255). The VAT 201 return will be completed using this information and a Current Asset will be reflected in the books of the municipality. Once SARS refunds or reimburse the municipality with the net amount of R255, the amount will be received as per the transaction below.

**VAT Control - Receivable**

Account Description	Long code	AMOUNT (R)
DT: Assets: Current Assets: Cash and Cash Equivalents: Cash at Bank: Deposits	IA 001011004002	255
CR: Assets : Current assets: VAT Control: Receipts	IA 001011004004	-255

Providing an example for payment to SARS, the following transaction will be recorded:

The municipality declared R450 Output tax and claims back R30 Input tax general and R300 Input tax Capital. The net of these three amounts is R120. The VAT 201 return will be completed using this information and a current liability will be reflected in the books of the municipality. Once the municipality pays SARS the net amount of R120, the transaction will be reflected as indicated below:



**VAT Control - Liability**

Account Description	Long code	AMOUNT(R)
DT: Liabilities: Current Liabilities: VAT Payable Control: Payments	IL001008003	120
CR: Assets: Current Assets: Cash and Cash Equivalents: Cash at Bank: Withdrawals	IA001011004004	-120

Most financial systems provide the functionality to perform the above accounting treatment with limited user intervention. Normally a report is run where the VAT 201 report for the period is created. The municipality will then complete the VAT 201 with the information extracted from the system and either make payment or claim the VAT refund from SARS. If the municipality has a claim for a refund against SARS, the amount would be reflected as an asset. If the municipality is required to pay SARS, the amount would be reflected as a liability.

The payment or receipt of a refund requires the municipality to use the fund segment as follows. For the payment of VAT and the receiving of VAT refund claimed, the fund segment that must be utilised is Operational: Revenue: General Revenue: Taxes: Taxes and Surcharges (FD001001001009002). Municipalities must ensure that their system setup is corrected to reflect this funding source. Currently, some municipalities use “non-funding” which is incorrect. Using Taxes and Surcharges as the fund will populate the cash flow statement.

#### 4. VAT on conditional grants:

In addition, MFMA Circulars No. 48, 55 and 58 provides guidance on the required treatment of VAT on conditional grants, namely:

*“When a municipality uses conditional grant funds to purchase goods and services, input VAT is included in the price of such goods and services, which municipalities are required to pay, using conditional grant funding. In the normal course of managing their VAT, municipalities are able to reclaim this input VAT from SARS.*

*...municipalities must treat this ‘reclaimed VAT’ as ‘own revenue’ and its use by the municipality is not subject to any conditions that were applicable to the original conditional grant.”*

Examples of the accounting treatment of conditional grants and how the VAT must be treated is contained in MFMA Circular No. 58.

In accordance with MFMA Circular No. 59: Municipalities should distinguish between transfers and subsidies received as part of non-exchange transactions and agency payments received as exchange transactions.

Generally, agency payments from national and provincial government to local government are unlikely to be regarded as grants for VAT purposes. The municipality is performing a service for the relevant national or provincial department in terms of an agency agreement and so agency payments from relevant national or provincial department to the municipality are subject to the normal VAT provisions. Guidance on this is also provided in the VAT guide for municipalities and Interpretation Note No. 39 on VAT treatment of public authorities and grants.

From a VAT perspective, there is a distinction between:

- An unrequited payment (grant) which is given to the municipality to carry out its mandated functions (where a deemed supply arises to the extent that they make taxable supplies); and
- Payments which the municipality receives from any person which constitutes consideration for actual supplies made in return and which would usually be taxable at the standard rate.

### ***National Housing Programme***

In terms of the VAT Act, a public authority (e.g. The National or Provincial Department of Human Settlements) is considered as an end consumer that cannot register for VAT or be a vendor. Therefore, all the VAT costs incurred in acquiring goods and services will be a cost to the public authority. However, the VAT Act makes provision for the zero-rating of services deemed to be supplied to a public authority or municipality to the extent of any payment made to, or on behalf of, that vendor in terms of a national housing programme contemplated in the Housing Act, 1997 (Act No.107 of 1997). Under normal circumstances, these services will be supplied at a standard rate and the VAT costs borne by the public authority (i.e. Department of Human Settlements). These provisions (i.e. section 8(23) and section 11(2)(s) of the Housing Act) have caused a lot of difficulties in terms of its interpretation and application for all role-players in the implementation of the housing programmes by the Department of Human Settlements.

In 2015, the government announced its intention to review these provisions and continued to amend the VAT Act to abolish the zero-rating by deleting these sections in the VAT Act to make the supplies on the housing programme VAT standard rated. The amendments were intended to take effect from 01 April 2017, to allow the departments and municipalities involved in the housing programme time to make budgetary allowance for the additional VAT costs related to standard rating. However, both the National Treasury and municipalities were not ready to make the transition to standard rate on 01 April 2017.

Budget 2017 proposed that the effective date for this amendment be postponed for two years, and therefore reinstated these provisions from 01 April 2017. It still remains National Treasury's intention to abolish the zero-rating of services related to the National Housing Programme and subject it to the VAT standard rate to address the difficulties currently experienced.

There also seems to be difficulties related to the interpretation and application of the VAT Act regarding the treatment of payments related to rental stock. It should be noted that the VAT Act in section 12(c)(i) makes provision for the exemption of the supply of a dwelling under an agreement for the letting and hiring thereof. This has implications for the housing programme that provides rental units to beneficiaries of the programme, whether provided directly by municipalities or through social housing institutions. The institutional housing subsidy programme was introduced to provide capital grants to social housing institutions which construct and manage affordable rental units. The municipality will be earning exempt rental income from these properties. Hence, any VAT incurred directly in connection with these properties, whether in the construction or in the maintenance thereof, will be a cost to the municipality and cannot be claimed as input tax credits.

In summary:

- If the municipality receives such a payment to act as developer to build low cost houses to be handed over to beneficiaries, then they are deemed to make a supply to the department concerned (Department of Human Settlements). Such supply is zero rated under Section 8(23) read with Section 11(2)(s) of the VAT Act;
- If a municipality then engages sub-contractors to carry out some or all of the work, then the normal standard rate will apply. The sub-contractor will levy VAT on the supply to the municipality. The VAT registered municipality will be entitled to claim Input tax credits; and
- If the payment from the National Department of Human Settlements is used to build rental stock, then the payment is intended to be out of scope of VAT with no VAT consequences. Municipalities will be earning exempt rental income once the property has been developed and leased out. Hence, all VAT incurred directly in the building and maintenance of those property will be a cost to the municipality. The municipality will not be entitled to claim the Input tax credits.

## **5. Foreign Donor Funded Projects:**

Over the years there has been a proliferation of Foreign Donor Funded Projects (FDFP) in the country with uncertain tax status and treatment including for VAT purposes. The VAT legislation has also gone through a number of changes to streamline the governance and administration of FDFP to realise the VAT zero-rating for qualifying FDFP. In this regard, the 2019 amendments which came into effect on 01 April 2020, provides further clarification of the qualifying criteria for FDFP. The FDFP must be established in terms of an official development assistance agreement (ODAA) to which the government of South Africa is constitutionally bound as a party; and the agreement must stipulate that the international donor funding will not be subject to tax; and the Minister of Finance must have accordingly approved the project as a FDFP for VAT purposes.

Importantly, a definition of an implementing agency has been introduced to further enhance the governance of FDFP with regards to the operation, administration, implementation, and management of the FDFP. The implementing agency is responsible for the accounting of the receipt of funding and distribution of such funding received from the foreign donor.

In the past the FDFP was recognised as a “person” for VAT purposes, and it was the FDFP that was registered for VAT in order to claim back all input tax incurred. In terms of the 2019 amendments (applicable only to new FDFP registrations), the FDFP is no longer recognised as a “person” for VAT purposes. The implementing agency is the “person” and for VAT purposes, must register the FDFP as a branch of the implementing agency. The VAT incurred on expenses can still be claimed back by the FDFP through its branch VAT registration. In this way, VAT will never be a cost to the project. Donations received by the foreign donor are treated as zero-rated income. Hence, there is no output tax due.

Municipalities must ensure that the setup in their financial systems and the reporting of VAT for a FDFP is correctly implemented. By using the project and fund segments optimally the reporting could be managed for the separate VAT submission as required in the VAT Reference Guide for Foreign Donor Funded Projects.

The VAT Reference Guide for Foreign Donor Funded Projects provides further guidance on this issue.

## 6. Conclusion:

Municipalities should ensure that they stay up to date with the latest directives by SARS with regards to changes in the VAT Act. A review of payments received from government should be undertaken to ensure that the VAT treatment on grants and agency services is recorded correctly. The explanation of the use of input and output tax must be checked to ensure that the reporting is aligned to the VAT account provided in the mSCOA chart as explained to reduce the risk of incorrectly reporting on VAT.

Any queries relating to VAT transactions on the mSCOA chart must be logged on the mSCOA Frequently Asked Questions (mSCOA FAQ) Database. The database can be accessed on the mSCOA website on the following link:

<http://mscoafaq.treasury.gov.za>

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