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Treasury invokes the S12J sunset clause

The National Treasury has decided to invoke the sunset clause and not extend the Section 12J tax incentive scheme.

The industry's disappointment has been palpable, with various surveys yielding 100% response rates of the opinion that the scheme should be extended. But the industry's opinion on whether it has met its objectives is not so decided.

Alternative investment options

This clause will mean that investments in approved Venture Capital Companies (VCC), before the end of June, will be 100% deductible from the investor's taxable income, but not thereafter. The returns and potential for attractive returns, as the funds mature, will determine whether investors will stay put in VCCs or seek alternative investment options. This will no doubt put pressure on fund managers to keep costs in check and offer value against the backdrop of the investment landscape.

The maturity of the underlying positions will prop up these comparatives, with many section 12J funds having worked through the "hockey stick" hook and now yielding an attractive internal rate of return. There is also a significant base of investors that chose to invest not only for the tax break, but also for the Environmental, Social, and Corporate Governance (ESG) benefits. Investors now want their money to not only work for them, but have a further positive impact, and this incentive has helped bolster the benefits of impact investments.

Snowball effect on job creation

But has it been effective in its primary goal of mobilising funding for new ventures and thereby ensuring job creation?

Statistics show over 5 000 permanent jobs having been created and over 5 000 additional temporary positions. The number of permanent jobs created almost matches the number of participating investors 1:1. More importantly, the benchmark data from the Industrial Development Corporation indicates that the cost to create a job through other incentives was almost twice as much as the actual cost to create a job through this mechanism.

The R10 billion raised to date could be seen as an indication of success, but some question the productivity, as well as the sustainability of this mechanism. One of the main reasons why the sunset clause was invoked is that even though these 12J structures are compliant, the capital raised is not always going towards new ventures and rather towards the refinancing of existing models or asset-based finance for things like office equipment.

However, with many of these businesses now having received their required funding, the hope is that the snowball effect on job creation will accelerate and create a positive delayed result. Not to mention, it has given investors an avenue to receive the allowed tax break, while being more purposeful in their investment decisions and looks to contribute to SME upliftment.

A handy tax incentive

Come July, investors will still have the option to invest in these underlying VCC assets, albeit outside of the beneficial tax ambit, and if tax efficiency is still a high priority, then other more traditional endowment structures still exist. Perhaps keeping with the conscious investment approach, a less mainstream but equally compelling option exists with the section 12B tax allowance, which is targeted at specific assets such as farms, business premises and small manufacturing. This act allows for an accelerated capital allowance of the assets used in the generation of electricity from wind power, solar power, and hydropower. As of 1 January 2016, section 12B of the tax act was amended to accommodate a 100% depreciation allowance in year one. This not only encourages investment in renewable energy but acts as a handy tax incentive.

So, even though there may be some unanswered questions concerning the effectiveness of Section 12J and its outcomes, it would have hopefully highlighted the benefits of conscious investing. Investors will now be looking at the options available to increase their returns and make a greater positive impact. ●

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