

SOUTH AFRICAN VALUE-ADDED TAX IMPLICATIONS OF INTERACTIVE GAMBLING IN THE ABSENCE OF DETAILED PLACE OF SUPPLY RULES

by

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ABSTRACT

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Interactive gambling transactions take place over the internet, which is essentially a borderless environment. Typically, interactive gambling providers are located off-shore in tax-friendly destinations in order to maximise their profits. In the context of cross-border transactions, value-added tax (VAT) place of supply rules provide certainty regarding where a supply is deemed to take place in order to determine the correct treatment for VAT purposes.

In contrast to a number of other countries, South Africa has limited place of supply rules. This creates uncertainty regarding where the activities of a non-resident supplier is deemed to take place. The absence of detailed place of supply rules impacts on the determination of whether the transaction will be liable to VAT in South Africa and also creates uncertainty regarding whether or not a non-resident is liable to register for VAT in South Africa.

The main purpose of this study is to critically analyse the South African VAT implications of interactive gambling in the absence of detailed place of supply rules. This objective is achieved by analysing the South African VAT Act in the context of interactive gambling legislation to determine whether it succeeds in providing certainty regarding the place of supply of interactive gambling for purposes of the VAT Act. This analysis highlights the problems associated with the limited place of supply rules in South Africa.

This study also critically analyses the legislation in a number of countries with place of supply rules from a South African perspective.

The study concludes that the VAT place of supply rules in South Africa are not specific enough to create certainty regarding where the supplies of a non-resident interactive gambling supplier to a South African resident is deemed to take place and consequently whether the supply will be subject to VAT in South Africa. This may result in a failure to bring these transactions within the VAT net.

The study further concludes that the place of supply rules in the European Union are in line with the guidelines issued by the Organisation for Economic Co-operation and Development (OECD) as well as recent South African case law (albeit not specifically related to the place of supply for VAT purposes), which indicates that interactive gambling transactions should be taxed where the consumer is situated. By implementing place of supply rules based on European legislation, through amending the current legislation or by issuing interpretation guidance, the problems associated with the limited place of supply rules in South Africa can be alleviated. This will also ensure that South African providers of interactive gambling services can compete on an equal footing with off-shore providers.

OPSOMMING

SUID-AFRIKAANSE BELASTING OP TOEGEVOEGDE WAARDE GEVOLGE VAN INTER-AKTIEWE DOBBEL IN DIE AFWESIGHEID VAN GEDETAILLEERDE PLEK VAN LEWERING REËLS

deur

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Inter-aktiewe dobbel transaksies vind plaas oor die internet, wat in beginsel 'n grenslose omgewing is. Die verskaffers van inter-aktiewe dobbel dienste is tipies nie-inwoners wat gebaseer is in belastingvriendelike bestemmings om sodoende hulle winste te maksimeer. In die konteks van hierdie oorgrens transaksies, verskaf plek van lewering reëls duidelikheid oor waar lewering geag word plaas te vind om sodoende die korrekte behandeling in terme van belasting op toegevoegde waarde (BTW) vas te stel.

Anders is in verskeie ander lande, het Suid-Afrika beperkte plek van lewering reëls. Dit veroorsaak onduidelikheid oor waar die aktiwiteite van 'n nie-inwoner geag word plaas te vind. Die afwesigheid van gedetailleerde plek van lewering reëls gee ook aanleiding tot onsekerheid oor of die transaksies van die nie-inwoner onderworpe sal wees aan BTW in Suid-Afrika, asook oor die verpligting van die nie-inwoner om in Suid-Afrika vir BTW te registreer.

Hierdie studie het ten doel om die Suid-Afrikaanse BTW gevolge van inter-aktiewe dobbel in die afwesigheid van plek van lewering reëls krities te analiseer. Dit word bereik deur die BTW-wet in die konteks van inter-aktiewe dobbel te ontleed om sodoende vas te stel of die BTW-wet daarin slaag om duidelikheid te verskaf oor die plek van lewering van oorgrens

inter-aktiewe dobbel transaksies. Hierdie analise bring die probleme wat gepaard gaan met die beperkte plek van lewering reëls in Suid-Afrika na vore.

Die studie kom tot die slotsom dat die huidige BTW plek van lewering reëls in Suid-Afrika nie spesifiek genoeg is om duidelikheid te verskaf oor waar 'n nie-inwoner se lewering van inter-aktiewe dobbel dienste aan 'n Suid-Afrikaanse inwoner geag word plaas te vind nie. Gevolglik is daar onduidelikheid oor of hierdie transaksies onderworpe sal wees aan BTW in Suid-Afrika. Dit mag tot gevolg hê dat hierdie transaksies moontlik die Suid-Afrikaanse BTW-net ontglip.

Die studie kom verder tot die gevolgtrekking dat die plek van lewering reëls wat in die Europese Unie toegepas word, bepaal dat inter-aktiewe dobbel transaksies vir BTW doeleindes belasbaar is waar die klient geleë is. Dit is in ooreenstemming met die riglyne van die OECD, sowel as onlangse Suid-Afrikaanse regspraak (alhoewel die betrokke hofsaak nie spesifiek die plek van lewering vir BTW doeleindes aangespreek het nie). Deur soortgelyke plek van lewering reëls in Suid-Afrika te implementeer kan die probleme wat met die beperkte plek van lewering reëls gepaard gaan, verminder word. Dit kan vermag word deur bestaande wetgewing te wysig of deur interpretasie riglyne deur die Suid-Afrikaanse Inkomstediens uit te reik. Die implementering van plek van lewering reëls sal ook verseker dat Suid-Afrikaanse verskaffers van inter-aktiewe dobbel dienste op 'n gelyke voet met nie-inwoners kan kompeteer.

TABLE OF CONTENTS

CHAPTER 1.....	1
INTRODUCTION	1
1.1 BACKGROUND.....	1
1.2 RATIONALE FOR THE STUDY	3
1.3 PURPOSE STATEMENT	3
1.4 RESEARCH OBJECTIVES	3
1.5 SCOPE AND LIMITATIONS OF THE STUDY.....	4
1.6 ASSUMPTIONS	4
1.7 DEFINITION OF KEY TERMS.....	5
1.8 ABBREVIATIONS USED.....	7
1.9 RESEARCH DESIGN AND METHODS	7
1.9.1 Description of inquiry strategy and broad research design.....	7
1.10 BRIEF OVERVIEW OF CHAPTERS	8
CHAPTER 2.....	10
AN ANALYSIS OF THE CURRENT SOUTH AFRICAN LEGISLATION PERTAINING TO INTERACTIVE GAMBLING	10
2.1 INTRODUCTION.....	10
2.2 AN OVERVIEW OF INTERACTIVE GAMBLING IN SOUTH AFRICA.....	10
2.2.1 Legislative framework.....	10
2.2.2 Challenges in maintaining the current prohibition of interactive gambling	12
2.3 DEVELOPMENTS BROUGHT ABOUT BY A RECENT SUPREME COURT OF APPEAL DECISION	14
2.4 VAT LEGISLATION AND PLACE OF SUPPLY RULES IN THE SOUTH AFRICAN CONTEXT.....	15
2.4.1 Value-added tax principles and the charging provision	16

2.4.2	Definition of an enterprise for VAT purposes.....	18
2.4.3	Imported services	21
2.5	CONCLUSION.....	24
CHAPTER 3.....		25
PLACE OF SUPPLY RULES IN THE EUROPEAN UNION AND AUSTRALIA		25
3.1	INTRODUCTION	25
3.2	INTERACTIVE GAMBLING IN THE EUROPEAN UNION.....	26
3.2.1	Background to VAT in the European Union.....	26
3.2.2	Specific rules relating to the place of supply of electronic services in terms of the VAT Directive.....	27
3.3	SPECIFIC EU COUNTRIES	29
3.3.1	Interactive gambling in the United Kingdom	29
3.3.2	Interactive gambling in the Republic of Ireland.....	30
3.4	INTERACTIVE GAMBLING IN AUSTRALIA.....	32
3.5	CONCLUSION.....	33
CHAPTER 4.....		36
CONCLUSION AND VALUE OF THE STUDY		36
4.1	INTRODUCTION.....	36
4.1	SUMMARY OF FINDINGS RELATED TO THE RESEARCH OBJECTIVES.....	37
4.2	SUMMARY OF THE CONTRIBUTIONS OF THE STUDY	39
4.3	LIMITATIONS OF THE PRESENT RESEARCH AND RECOMMENDATIONS FOR FUTURE RESEARCH	39
4.4	CONCLUSION.....	40
LIST OF REFERENCES.....		42

LIST OF TABLES

Table 1: Abbreviations used in this document	7
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SOUTH AFRICAN VALUE-ADDED TAX IMPLICATIONS OF INTERACTIVE GAMBLING IN THE ABSENCE OF DETAILED PLACE OF SUPPLY RULES

CHAPTER 1

INTRODUCTION

1.1 BACKGROUND

The internet does not pay attention to national boundaries and interactive gambling is no exception (Baumann, 2010:1). This makes the current prohibition against interactive gambling in South Africa very difficult to regulate and police as it takes place in the virtual world (Rychlak, 2011:1231).

Amendments, in the form of the National Gambling Amendment Act (10 of 2008), have been made to the existing legislation in order to licence and regulate the interactive gaming industry in South Africa. At the time of this study, these amendments were set to commence on a date determined by the South African state president and it is therefore anticipated that gambling on-line through licensed operators will be legal in the near future.

Regardless of the fact that interactive gambling in South Africa is, at the time of this study, not legalised, there are a number of websites that offer South Africans the option to participate in rand-based online casinos, for example www.randcasinos.com, www.randgambling.co.za, www.onlinecasinopicks.co.za, www.goinggambling.co.za to name but a few. Baumann (2010:1) quoting Puttergill, stated that the online gambling industry in South Africa was estimated at between R400 million and R1 billion in 2009. If the 6% tax on gross interactive gambling revenue proposed in the Interactive Gambling Tax Bill (2008) materialises, along with a potential 14% value-added tax (VAT), the industry, if properly regulated and taxed, is likely to generate considerable income for the South African fiscus.

South African VAT as imposed in terms of the Value-added Tax Act (89 of 1991) (hereafter referred to as the VAT Act) is a destination-based consumption tax, which implies that goods and services are taxed where consumption takes place, disregarding the place where the goods and services originate from (SARS, 2007:1). Interactive gambling may consequently have certain VAT implications, regardless of the legality thereof.

The limited place of supply rules in South Africa creates uncertainty regarding where the business activities of a non-resident supplier is deemed to take place. Consequently, where cross-border transactions are concerned, there is also uncertainty where the VAT on the supply is liable to be remitted. This situation has been exacerbated by the advent of e-commerce transactions (De Wet & Du Plessis, 2000: 271).

The VAT consequences may be twofold if the place of supply of services is deemed to be in South Africa: Firstly, VAT may be payable on the gambling transaction and secondly it may also result in non-resident online casino operators having to register as VAT vendors in South Africa (Niemand, De Swardt & Wiid, 2011: 35). In terms of the VAT Act, suppliers of goods and services in South Africa are required to register as vendors where taxable supplies are likely to exceed a specific amount (at the time of this study, this amount was R1 million) in any 12 month period (South African Revenue Service 2012: 9).

In contrast to a number of other countries, such as countries in the European Union and Australia (Schenk & Oldman: 196 & 210-219), South Africa's VAT legislation does not contain specific place of supply rules that determines where a supply is deemed to take place for VAT purposes (Niemand, de Swardt & Wiid, 2011: 35; Schneider 2009: 1). This may lead to uncertainty when determining whether a supply is taxable in South Africa and whether a supplier should be registered as a vendor for VAT in terms of the VAT Act.

An extensive search of leading electronic journal databases suggests that no academic research has directly examined the implications of interactive gambling in the context of the South African VAT act.

1.2 RATIONALE FOR THE STUDY

A recent Supreme Court of Appeals judgment, *Casino Enterprises (Pty) Ltd v Gauteng Gambling Board and Others*, 2011 (6) SA 614 (SCA), confirmed an earlier decision by the North Gauteng High Court that interactive gambling takes place where the participant takes part in the gambling activities. The consequence of this confirmation is that when a South African resident participates in online gambling from within the borders of South Africa, the gambling transaction is deemed to take place in South Africa. The ruling did not specifically address the place of supply for purposes of the requirements of the VAT Act, but the question can be posed whether this decision may have an implication in determining the place of supply of interactive gambling transactions.

From a theoretical perspective this study may contribute to the understanding of the place of supply of interactive gambling.

The study may also assist the legislature, the South African Revenue Service (SARS) and taxpayers with the interpretation of the VAT legislation as it applies to interactive gambling in South Africa.

1.3 PURPOSE STATEMENT

The main purpose of this study is to critically analyse the South African VAT implications of interactive gambling in the absence of detailed place of supply rules.

1.4 RESEARCH OBJECTIVES

The main purpose of this study is supported by the following research objectives:

- To critically analyse the applicable provisions of the South African VAT Act to determine whether interactive gambling transactions fall within the ambit of the VAT Act.

- To critically analyse place of supply rules and VAT (or goods and services tax (GST)) legislation in a number of countries with detail place of supply rules related to interactive gambling transactions, from a South African perspective.

1.5 SCOPE AND LIMITATIONS OF THE STUDY

This study addresses the VAT consequences of interactive gambling (gaming) in South Africa.

This study does not address:

- the income tax consequences of interactive gambling in terms of the Income Tax Act (58 of 1962) ;
- any effect of double taxation agreements or international tax rules;
- the tax consequences of other e-commerce transactions; or
- online betting transactions.

1.6 ASSUMPTIONS

Leedy & Ormrod (2010: 6) defines an assumption as “a condition that is taken for granted, without which the research project would be pointless”. Certain assumptions were made in the current study, which assumptions are set out below.

It is assumed that VAT will be applicable to an interactive gambling transaction when it falls within the requirements of the VAT Act, regardless of whether the transaction is legal or not (whether the interactive gambling provider is licensed or not).

For the purposes of this study the typical interactive gambler is assumed to be a private individual that is not registered as a VAT vendor.

According to Section 8(13) of the VAT Act, the person with whom a bet is placed is deemed to supply a service to the person placing a bet. Gambling is therefore deemed to be a supply of services to the gambler for VAT purposes. It is assumed that this will be

true, regardless of whether or not the gambling takes place online or in a land-based casino.

1.7 DEFINITION OF KEY TERMS

Electronic commerce

For the purposes of this study e-commerce will be defined as “commercial transactions occurring over open networks, such as the Internet” (OECD, 2012). It also incorporates similar transactions occurring over telecommunications networks.

Enterprise

“An enterprise or activity which is carried on continuously or regularly by any person in, or partly in South Africa in the course or furtherance of which goods or services are supplied to any other person for consideration, whether or not for profit, including any enterprise or activity carried on in the form of a commercial, financial, industrial, mining, farming, fishing, municipal or professional concern or any other concern of a continuing nature or in the form of an association or club” (Section 1 of the VAT Act).

Imported services

“A supply of services that is made by a supplier who is a resident or carries on business outside [South Africa] to a recipient who is a resident of South Africa to the extent that such services are utilised or consumed in [South Africa] otherwise than for the purpose of making taxable supplies” (Section 1 of the VAT Act).

Income Tax Act

Refers to the Income Tax Act of South Africa (Act 58 of 1962).

Interactive gambling

For the purposes of this study, interactive gambling means all forms of remote gambling taking place via the internet or other related forms of telecommunication (National Gambling Act, 7 of 2004).

Land-based gambling

Land-based gambling means traditional gambling taking place at a physical location, as opposed to interactive gambling.

Place of supply

Place of supply, for the purposes of this study, is the location where a supply is deemed to take place.

Online betting transactions

Online betting is where the bet is placed online, but the event that is bet on takes place separately from the online platform, such as a sports or racing event or a lottery. The online system therefore does not generate the result (Gambling Review Commission, 2010a: 175).

Services

“Anything done or to be done, including the granting, assignment, cession or surrender of any right or the making available of any facility or advantage, but excluding a supply of goods, money or any stamp, form or card contemplated in the definition of goods” (Section 1 of the VAT Act).

Supply

The “performance in terms of a sale, rental agreement and instalment credit agreement and all other forms of supply, whether voluntary, compulsory or by operation of law, irrespective of where the supply is effected” (Section 1 of the VAT Act).

Vendor

A person who is, or is required to be registered in terms of Section 23 of the VAT Act (89 of 1991).

VAT

Value-added Tax

VAT Act

Refers to the Value-added Tax Act (89 of 1991).

1.8 ABBREVIATIONS USED

Table 1 below clarifies the abbreviations used in this study.

Table 1: Abbreviations used in this document

Abbreviation	Meaning
DTA	Double Taxation Agreement
E-commerce	Electronic commerce
EU	European Union
GST	Goods and Services Tax
OECD	Organisation for Economic Co-operation and Development
SA	South Africa
SARS	South African Revenue Service
UK	United Kingdom
VAT	Value-added Taxation
VAT Act	Value-added Tax Act, 1991 (89 of 1991)
WTO	World Trade Organisation

1.9 RESEARCH DESIGN AND METHODS

1.9.1 Description of inquiry strategy and broad research design

The research in this study comprises of an extensive literature review. Saunders, Lewis and Thornhill (2009: 590) define a critical literature review as a “detailed and justified analysis and commentary of the merits and faults of the literature within a chosen area, which demonstrates familiarity with what is already known about your research topic”. Mouton (2001:179) describes literature reviews as “studies that provide an overview of scholarship in a certain discipline through an analysis of trends and debates”.

Leedy and Ormond (2010: 66) refer to a number of benefits of performing a literature review, namely:

- It provides new ideas, perspectives and approaches to the researcher.
- It provides information about other researchers that conducted research in the area of your topic.
- It shows how the methodological and design issues were handled in similar studies.
- It can reveal additional sources of data.
- It reveals methods of dealing with problem situations and assists in the interpretation of findings.

According to Mouton (2001:180) a comprehensive literature review is vital to any study. Mouton (2001:180) highlights the strengths of a literature as follows:

- It provides a detailed background of the issues and debates in the particular field of study.
- It provides an understanding of the current theoretical thinking, as well as the definitions that are commonly used.
- It provides an awareness of previous studies and their results.

Mouton (2001:180) stated in contrast that the limitation of a literature review is the fact that a literature review cannot produce new empirical insights, although it often may lead to theoretical insights. Those insights will, however, still need to be tested using an empirical approach.

1.10 BRIEF OVERVIEW OF CHAPTERS

This chapter provided the background and rationale for the study and presented the research objectives of the study. It identified the scope and delimitations of the study and created awareness of certain assumptions that were made during the performance of the study. Chapter 1 also highlighted the benefits of the study and defined certain key terms and abbreviations used throughout the study. The research design and method is explained and brief overview of the chapters included in the study is provided.

Chapter 2 provides an analysis of the current South African legislation pertaining to interactive gambling, with a specific focus on the VAT legislation in South Africa as applicable in the context of interactive gambling.

Chapter 3 analyses the VAT place of supply rules in the European Union and Australia. Two specific countries in the European Union, namely the United Kingdom and the Republic of Ireland are also analysed to demonstrate the differences in the treatment of interactive gambling transactions between countries within the European Union.

Chapter 4 concludes the study, summarises the findings of the study and provides a conclusion to the study, in particular in the context of the research objectives of the study. The chapter highlights the contribution of the study and identifies areas for future research.

CHAPTER 2

AN ANALYSIS OF THE CURRENT SOUTH AFRICAN LEGISLATION PERTAINING TO INTERACTIVE GAMBLING

2.1 INTRODUCTION

The objective of this study is to critically analyse the South African VAT implications of interactive gambling in the absence of detailed place of supply rules. This chapter examines the legislative framework for interactive gambling in South Africa and analyses the provisions of the South African VAT Act in order to determine the applicability thereof to interactive gambling transactions. The legislation is then critically analysed in order to determine whether it succeeds in providing certainty regarding the place of supply of interactive gambling transactions for purposes of South African VAT.

According to Naicker (2010:8) there are no published rulings, tax court decisions or relevant publications or interpretation notes, at present, which addresses the VAT consequences of electronic commerce. This literature review attempts to assimilate the various sources in order to determine the correct treatment of interactive gambling transactions in terms of the VAT Act and to identify shortcomings in the legislation.

2.2 AN OVERVIEW OF INTERACTIVE GAMBLING IN SOUTH AFRICA

The purpose of this section is to clarify the legislative framework for interactive gambling in South Africa, as well as the challenges in maintaining the prohibition of interactive gambling in South Africa.

2.2.1 Legislative framework

Interactive gambling in South Africa is currently regulated in terms of the National Gambling Act (7 of 2004). This act was amended in 2008 by the National Gambling Amendment Act (10 of 2008), which defined online or interactive gambling for the first

time. Before the amendment, interactive gambling was not accepted as a legal form of gambling in South Africa. This amended legislation also aims to regulate the advertising of interactive gambling activities (Rahamim & Mthiyane, 2008: 14). The penalties for contravention of the legislation is a fine of up to R10 million or 10 years in prison (National Gambling Board, 2011: 1).

In terms of section 11 of the National Gambling Act, as amended, a person is prohibited from taking part in, facilitating or making available an interactive game, unless the interactive game is provided in terms of a licence issued under the National Gambling Act. To date, the National Gambling Board has not yet issued a single interactive gambling licence, and consequently all interactive gambling activities in South Africa are considered to be illegal (National Gambling Board 2011: 1).

Interactive Gambling Regulations (South Africa 2009) were published for comment during 2009; however, at the time of this study this has not resulted in legislation. The aim of these regulations is to regulate the industry in order to protect players from dishonest and unfair practices and to keep money from leaving the country (Collins, 2009:1).

The Department of Trade and Industry appointed the Gambling Review Commission in December 2009 to (Gambling Review Commission, 2010a: 8):

- review the development of the gambling industry since its legalisation;
- assess the social and economic impact of gambling (specifically problem gambling and gambling addiction, gambling demographics and youth gambling); and
- assess the success of current strategies to manage and alleviate the negative effects of gambling.

This resulted in the issuing of the Gambling Review Commission report: Review of the South African Gambling Industry and its Regulation. The Portfolio Committee on Trade and Industry, after consideration of the report of the Gambling Review Commission (GRC) agreed with all the recommendations made by the GRC in its report (Portfolio Committee on Trade and Industry, 2012:1).

Among other things, the GRC recommended that interactive gambling (or online or remote gambling) should be managed holistically by covering all the various ways in which it can be distributed, such as mobile phones.

2.2.2 Challenges in maintaining the current prohibition of interactive gambling

Despite the fact that interactive gambling has always been illegal in South Africa, the National Gambling Board (National Gambling Board 2011:1) stated that they have “identified an increase in the number of illegal online gambling operations nationally”.

A cursory search on the internet for rand-based casinos revealed that there are a large number of websites that advertise rand-based online gambling. Examples are: Rand Casinos (www.randcasinos.com), Rand Gambling (www.randgambling.co.za), Online Casino Picks (www.onlinecasinopicks.co.za) and Going Gambling (www.goinggambling.co.za), among others. These websites provide links to online gambling websites that offer Rand-based online casinos, which supports the fact that, despite the illegality of interactive gambling, there are still a number of interactive gambling websites that provide online gambling facilities to South Africans.

According to Mawson (2012a:1) referring to Tuxworth of the UK-based Betfair, if legalised, the interactive gambling industry could potentially contribute R1 billion in tax revenue in South Africa. According to Tuxworth, interactive gambling should be legalised as “any attempt to prohibit online gambling simply drives consumer demand into the offshore market”.

However, the difficulty in enforcing prohibition was stressed by the Gambling Review Commission in their report (Portfolio Committee on Trade and Industry, 2012: 21) which stated that the prohibition of interactive gambling will be very resource intensive. The National Gambling Board also agreed that there is a huge consumer demand for interactive gambling and that it is difficult to restrict access to websites offering this activity (Portfolio Committee on Trade and Industry, 2012: 21).

The current Chief Executive Officer of the National Gambling Board (Ms Baby Tyawa) confirmed that the board is only able to shut down an online casino's server if the server is located in South Africa. Otherwise the only recourse that the National Gambling Board has is to inform the operator that the board is compiling a blacklist which may limit their chances of being awarded a licence once interactive gambling is legalised (Mawson, 2012b:1).

The National Gambling Board has established a relationship with the South African Reserve Bank and local banks through the Banking Association of South Africa, through which transactions between online betting sites and banking customers are identified. If such a relationship is identified, the illegal winnings are seized and transferred to an "online gambling trust fund" (Aboobaker, 2012: 22).

The Banking Association of South Africa has raised the following concerns regarding the challenges that could be faced in identifying transactions linked to illegal online gambling activities (Portfolio Committee on Trade and Industry 2012: 24):

- Certain online gambling activities might be permitted and/or licensed in other countries;
- Existing licensed land-based casino operators might have integrated banking facilities with a consolidated payment structure, which may be difficult to distinguish from interactive gambling transactions where they could expand into this environment;
- Illegal service providers will attempt to conceal the true nature of the transaction.

The penalties for contravention of the current prohibition against interactive gambling is a fine of up to R10 million or 10 years in prison (National Gambling Board, 2011: 1). In spite of this, to date no one has been arrested for illegal online gambling although certain penalties have been imposed (Tyawa in Mawson, 2012b:1). According to the National Gambling Board illegal gambling winnings of R3.5 million has been seized over the last three to four years with the help of local banks (Aboobaker, 2012: 22).

When determining the legality of interactive gambling, a distinction has to be drawn between interactive gambling and online betting, as online betting is currently legal in South Africa in terms of the National Gambling Act (Gambling Review Commission, 2010a: 175). Online betting is where the bet is placed online, but the event that is bet on takes place separately from the online platform, such as a sports or racing event or a lottery. The online system therefore does not generate the result.

This is different from interactive gambling (or gaming) in an online casino, for example, where the online system will determine the outcome (Gambling Review Commission, 2010a:175).

This section provided an overview of the legislative framework for interactive gambling in South Africa. Although interactive gambling has been legalised in terms of the National Gambling Act (7 of 2004) as amended, the fact that no licences have been issued to date effectively means that interactive gambling is currently still illegal in South Africa. The next section will explore the developments brought about by case law in South Africa related to the place of supply of interactive gambling.

2.3 DEVELOPMENTS BROUGHT ABOUT BY A RECENT SUPREME COURT OF APPEAL DECISION

Despite the fact that interactive gambling is deemed to be illegal in accordance with the current South African legislation, many foreign-based interactive gambling providers actively marketed their online casino websites to South Africans. Most notable of these providers were Piggs Peak (www.piggspeak.com), Silver Sands (www.silversandscasino.com) and African Palace (www.africanpalacecasino.com), amongst others. This practice culminated in a court case between the Gauteng Gambling Board and Casino Enterprises (Casino Enterprises v Gauteng Gambling Board 2010 (6) SA 38).

Casino Enterprises operates Piggs Peak online casino which is legally licensed in Swaziland (Casino Enterprises (Pty) Ltd v Gauteng Gambling Board and Others, 2011 (6) SA 614 (SCA)). The Gauteng Gambling Board instructed radio stations broadcasting in

Gauteng to cease broadcasting advertisements for Piggs Peak internet casino, as Casino Enterprises was not licenced to operate a casino in the Gauteng Province. The radio stations withdrew the advertisements as a result. Casino Enterprises then sought an order to declare its online casino legal. Casino Enterprises contended that the gambling activity takes place where the servers are situated, in this case in Swaziland, and therefore the company was not contravening South African legislation by engaging with South African gamblers through interactive gambling. The North Gauteng High Court found in favour of the Gauteng Gambling Board and determined that the gambling takes place where the gambler is situated, regardless of the location of the servers. Casino Enterprises (Pty) Ltd appealed this decision.

The subsequent Supreme Court of Appeal decision in *Casino Enterprises v The Gauteng Gambling Board* confirmed that the gambling takes place where the gambler is situated (*Casino Enterprises (Pty) Ltd v Gauteng Gambling Board and Others*, 2011 (6) SA 614 (SCA)). The uncertainty regarding legality of interactive gambling by South Africans on foreign-based websites was therefore eliminated and the legal position confirmed.

A question can be posed as to whether or not the decision may have any implication in determining the place of supply of interactive gambling transactions for VAT purposes. However, it is possible to argue that this court case decision does not necessarily clarify the place of supply for purposes of the requirements of the VAT Act.

2.4 VAT LEGISLATION AND PLACE OF SUPPLY RULES IN THE SOUTH AFRICAN CONTEXT

VAT is a main source of revenue of the state. In 2011, VAT contributed 27.2% of the total tax revenue collected by the state, or R183,571 million (National Treasury & SARS:15). Only personal income tax contributed more than VAT to the government revenue. Despite the relative importance of VAT to the state, the specific VAT implications of interactive gambling have as yet not been explored by the revenue authorities.

In response to the impending regulation of interactive gambling in terms of the National Gambling Amendment Act (10 of 2008), which called for a tax to be imposed on interactive

gambling, the Interactive Gambling Tax Bill was made public for comment during 2008. In terms of the Interactive Gambling Tax Bill, a tax will be imposed at the national level on interactive gambling at a rate of 6% of all gross gambling revenue from an interactive source. Gross gambling revenue is determined as the aggregate amount debited to player accounts, less certain deductions (Section 4 of the Interactive Gambling Tax Bill). The Interactive Gambling Tax Bill (Section 4) states that the gross gambling revenue should be “determined without regard to any input tax or output tax as defined in section 1 of the Value-Added Tax Act, 1991 (Act No. 89 of 1991)”. The fact that the treatment of VAT is explicitly addressed in the Bill can be construed as an indication that the legislature intends interactive gambling to be subject to VAT.

Currently the VAT consequences of land-based gambling transactions are addressed by Interpretation Note 41 (SARS, 2007), which constitutes a binding general ruling. As a result of the inherent nature of gambling transactions, casinos find it very difficult to separately keep record of the amounts of bets placed versus the amounts paid out in the form of winnings (SARS, 2007:11). It is therefore difficult to determine the exact amounts due in respect of output VAT and input VAT. Interpretation Note 41 allows casinos to account for VAT by calculating the VAT amount due on the net betting transactions, which is the “amount remaining after winnings have been deducted”.

The next sub-section will examine the extent to which the existing VAT legislation is applicable to online gambling transactions.

In order to determine the possible VAT consequences of interactive gambling transactions, the VAT Act has to be analysed to determine its application to interactive gambling.

2.4.1 Value-added tax principles and the charging provision

Value-added tax (VAT) in South Africa is a destination-based consumption tax. This implies that an activity is taxed where consumption takes place (Steyn 2010:239). In order to determine whether VAT will be chargeable in South Africa, it is important to determine where “consumption” is deemed to take place. This is very difficult when dealing with e-

commerce transactions taking place in the virtual world, especially in the context of the limited VAT place of supply rules in South Africa (Steyn: 240).

The determination of whether VAT should be levied and paid is set out in Section 7 of the VAT Act. Section 7(1) of the VAT Act states the following:

“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.”

In terms of Section 7 of the VAT Act, two instances can therefore be identified where the supply of services may be subject to VAT at the standard rate of 14%, namely:

- where a vendor supplies services in the course or furtherance of any *enterprise* carried on by him; and
- on the supply of any imported services by any person.

According to Section 8(13) of the VAT Act, the person with whom a bet is placed is deemed to supply a service to the person placing a bet. Gambling is therefore deemed to be a supply of services to the gambler for VAT purposes. The VAT Act does not distinguish between traditional and electronically supplied betting transactions and it is therefore assumed that this will be true, regardless of whether or not the gambling takes place online or in a land-based casino.

Hence the supply of interactive gambling services will be subject to VAT at 14% where the interactive gambling provider constitutes a vendor supplying services in the furtherance of an enterprise. Where an off-shore interactive gambling provider does not constitute a vendor, the interactive gambling transaction may still be subject to VAT at the standard rate where the interactive gambling services are imported by any person.

Consequently it is necessary to clarify the concept of what an enterprise is and what imported services are in terms of the VAT Act, as it relates to interactive gambling.

2.4.2 Definition of an enterprise for VAT purposes

An entity has to register for VAT in South Africa if it carries on an enterprise and if its taxable supplies exceeds, or is likely to exceed, the registration threshold, which is currently set at R1 million (Section 23(1) of the VAT Act). An “enterprise” is defined in Section 1 of the VAT Act as “an *enterprise or activity* which is carried on *continuously or regularly, in or partly in* South Africa in the course...of which *goods and services* are *supplied...for consideration...*” (own emphasis).

The definition does not require a fixed place of business in South Africa, but that a person or company will be regarded to be carrying on an enterprise if goods or services are supplied in the course of activities conducted continuously or regularly, in or partly in South Africa (Niemand, de Swardt & Wiid, 2011: 35; Steyn, 2010: 244). The fact that a foreign supplier does not have a permanent establishment in South Africa therefore does not necessarily mean that the supplier is not conducting an enterprise in South Africa and hence the supplier might still be required to register as a vendor for VAT purposes (De Wet & Du Plessis, 2000: 263).

When the definition of an enterprise in the VAT Act is analysed in the context of foreign-based interactive gambling websites, the following important aspects emerge:

- An “*enterprise*” or an “*activity*”:

These terms have been very broadly defined in the VAT Act and include any enterprise or activity carried on in the form of a commercial, financial, industrial, mining, farming, fishing, municipal or professional concern, whether for profit or not (Section 1 of the VAT Act). The term “activity” is not specifically defined in the VAT Act.

SARS defines an enterprise as “any business activity in the broadest sense” (SARS 2012:103) and has indicated that an enterprise basically follows a business activity test subject to certain exclusions (SARS 2012:27). As the supply of gambling services is a business activity, this will constitute an “enterprise” or an “activity” for purposes of the VAT Act.

- “*Continuously*” or “*regularly*”:

The term “continuously or regularly” is not defined in the VAT Act and hence the ordinary meaning of the words will apply. These terms have been interpreted by the Court of Appeal in New Zealand in *Newman v CIR* (1995) 17 NZTC 12. According to the New Zealand Court of Appeal an activity is deemed to be “continuous” if there is no significant cessation or interruption in the activity, this excludes any temporary interruptions. An activity is deemed to be “regular” if it is repeated at reasonably fixed intervals (New Zealand Inland Revenue 1995:9). It is also important to note here that it is the “activity” and not the supply that must be continuous or regular and that the activity need only be *either* “continuous” or “regular” (New Zealand Inland Revenue 1996:6). The fact that interactive gambling services are provided to South Africans on an on-going basis will therefore constitute a continuous or regular activity.

- “Goods or services supplied”:

In accordance with Section 8(13) of the VAT Act a person taking a bet is deemed to be supplying a service to the person making the bet. The interactive gambling provider is therefore supplying a service to the interactive gambler. This supply takes place in the course of the interactive gambling provider’s enterprise.

- “In or partly in South Africa”:

There is some uncertainty as to whether the supply of the gambling facilities takes place in or partly in South Africa. This is not easily determinable in the absence of detailed place of supply rules in the South African legislation.

Schneider (2009:1), Niemand, de Swardt & Wiid (2011: 35) and De Wet & Du Plessis (2000: 260) agree that the limited place of supply rules in the South African VAT Act poses problems in determining whether the supply takes place in or partly in South Africa.

According to De Swardt & Oberholzer (2006: 21) “the lack of clarity regarding the question of when a foreign supplier is regarded as carrying on an enterprise in South Africa is a major deficiency in the current South African VAT system, specifically with regard to the imposition of VAT on the supply of digitised products”.

Schneider (2009:1) has further indicated that the fact that the services are consumed within South Africa does not necessarily indicate that the activities are carried on in South Africa.

The Casino Enterprises judgement ruled that interactive gambling takes place where the punter is situated, regardless of where the gambling equipment/server is situated (National Gambling Board, 2010: 1). This judgement did not, however, specifically address the place of supply for VAT purposes. The question can, however, be posed whether this decision can form the basis of a VAT place of supply rule for interactive gambling.

- “For a consideration”:

Section 1 of the VAT Act defines “consideration” 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, but does not include any payment made by any person as a donation to any association not for gain.”

The interactive gambling provider supplies goods or services for a consideration in the form of the wager in terms of the gambling transaction.

It can therefore be concluded that the elements of an enterprise is reasonably easily identifiable, with the exception of the determination of where the transaction takes place.

The next section looks at the scenario where the gambling services are supplied by a non-resident who is not a vendor in terms of the VAT Act. It will then have to be determined whether the services fall within the definition of “imported services”.

2.4.3 Imported services

The VAT Act defines imported services as (Section 1 of the VAT Act):

“A supply of services that is made by a supplier who is a resident or carries on business *outside the republic* to a recipient *who is a resident of the republic* to the extent that such services are *utilised or consumed in the Republic* otherwise than for the purpose of making taxable supplies.”

Supplies utilised or consumed for the purpose of making taxable supplies are specifically excluded from the definition of imported services. Judge Waglay, in delivering judgement in VAT Case 144 (2005) summed up the reason for this exclusion by stating that a person that acquires a service for the purpose of making taxable supplies will be entitled to claim the VAT portion as an input tax credit, whereas a person that does not make taxable supplies is unable to claim the VAT as an input tax credit. Consequently, a non-resident supplier obtains an unfair advantage when supplying services to a local recipient utilising

the services for making non-taxable supplies, as they will be able to supply the services at 14% less than a local supplier. In order to offset this advantage, VAT is levied on “imported services” in the hands of the local recipient of the services. As the recipient making taxable supplies is in any event entitled to claim the VAT as an input credit, these are excluded from the definition of imported services.

A resident of the republic is defined in Section 1 of the VAT Act as:

“A resident as defined in Section 1 of the Income Tax Act: Provided that any other person or any other company shall be deemed to be a resident of the Republic to the extent that such person or company carries on in the Republic any enterprise or other activity and has a fixed or permanent place in the Republic relating to such enterprise or other activity.”

In accordance with Section 1 of the Income Tax Act, a resident means a natural person who is ordinarily resident in the Republic, or a company which is incorporated in, or has its place of effective management in South Africa.

Where the supplier of the service is a foreign-based interactive gambling website, which is not registered as a VAT vendor in South Africa, the transaction will therefore be deemed as the importation of a service to the extent that the services are “utilised or consumed in the Republic” in terms of the VAT Act.

Where a transaction is utilised or consumed is a little more problematic to establish as the terms “utilised” and “consumed” are not defined in the VAT Act. The online Oxford Dictionaries (not dated) define the term “consume” as “eat, drink or ingest (food or drink), completely destroy (of a fire), use up (a resource), buy (goods or services), completely fill the mind of someone (of a feeling)”. This definition, although useful in determining what the term consume means, does not clarify where the consumption takes place in respect of services.

The determination of where services are utilised or consumed is especially difficult in relation to electronic transactions that take place across borders. The absence of detailed

place of supply rules in South Africa means that the place of supply (or consumption) is not specifically defined in relation to e-commerce in general, and interactive gambling transactions in the specific. Consequently these types of transactions may escape the South African VAT net.

The Organisation for Economic Co-operation and Development (OECD) has laid down a principle in respect of consumption tax rules for cross-border transactions, which recommends that the rules should result in taxation being payable where consumption of the goods or services takes place (OECD, 2001:10). In respect of business-to-consumer transactions, the place of consumption for cross-border supplies of services are defined as the jurisdiction in which the customer has his or her usual place of residence (OECD 2001:24; De Swardt & Oberholzer, 2006: 19).

Using the OECD principles as a point of reference it is possible to state that the services related to interactive gambling transactions will be regarded as being consumed in South Africa. However, the lack of place of supply rules in the South African context may result in these transactions escaping the VAT net. The reason for this being that, in accordance with section 7(1)(c) of the VAT Act, VAT has to be levied and paid on the supply of imported services at the rate of 14% on the value of the supply concerned. The value of the supply is determined in accordance with section 14(3) of the VAT Act, which states that the value of an imported service is the highest of the open market value of the supply or the actual consideration paid. Also, in terms of section 14(1) of the VAT Act, this VAT has to be paid over by the recipient of the services within 30 days of the receipt of the invoice or any payment made in respect of the services, whichever is the earliest.

In the case of interactive gambling transactions, the recipient will more than likely be a private individual that is not registered for VAT. As the responsibility for accounting for the VAT lies at the door of the recipient of the service, this casts a shadow over the enforceability of this provision (Naicker, 2010:9) and there is therefore a high probability that the individual consumer will not pay over the VAT to SARS (Steyn, 2011:235). The administrative burden of submitting a return every time a gambling transaction is entered into also has to be taken into account.

2.5 CONCLUSION

The critical analysis of the current VAT legislation in South Africa and its applicability to interactive gambling highlights the problems associated with the limited place of supply rules in South Africa, particularly in the e-commerce environment. Hence, it was deemed necessary to critically analyse the place of supply rules pertaining to interactive gambling in other countries from a South African perspective. The purpose of the analysis was to critically examine possible solutions from these countries' place of supply rules which may contribute in finding a solution for the VAT problems identified in South Africa.

The next section will provide a critical analysis of the VAT/GST consequences of interactive gambling transactions in the European Union and Australia.

CHAPTER 3

PLACE OF SUPPLY RULES IN THE EUROPEAN UNION AND AUSTRALIA

3.1 INTRODUCTION

The objective of this study was to critically analyse the South African VAT implications of interactive gambling in the absence of detailed place of supply rules. The previous chapter examined the legislative framework for interactive gambling in South Africa and analysed the specific provisions of the South African VAT Act in order to determine the applicability thereof to interactive gambling transactions. It also highlighted the problems associated with the limited place of supply rules in South Africa.

This chapter provides an analysis of the literature related to the VAT legislation applicable in the European Union (EU) and Australia with reference to electronic commerce in general, and with specific reference to interactive gambling.

The European Union was selected for the analysis as the European Union has detailed place of supply rules in relation to electronically supplied services, which include interactive gambling. Gambling transactions (including interactive gambling transactions) are exempt from VAT in most European countries, therefore the VAT legislation pertaining to electronically supplied services was analysed as these transactions, if not exempt, would have fallen under the definition for electronically supplied services. As the implementation of the EU VAT legislation and the legislation governing gambling differs between EU states, the situation pertaining to the taxing of gambling activities in the United Kingdom and the Republic of Ireland was analysed to determine where the supply of the gambling services is deemed to take place in these specific countries.

In addition, the VAT legislation in Australia was also examined to determine whether Australia has specific place of supply rules in respect of electronically supplied services in general and interactive gambling services in the specific. This provides a perspective from a country outside the European Union.

3.2 INTERACTIVE GAMBLING IN THE EUROPEAN UNION

The European Commission (2011a:1) stated that there were almost 15,000 interactive gambling websites on the internet. As internet gambling legislation has not been harmonised within the EU, each member country within the EU can regulate interactive gambling independently. Consequently interactive gambling may be legal and regulated in one EU country whereas it may be restricted or prohibited in another EU country. The European Court of Justice confirmed that member states are entitled to prohibit interactive gambling within their own borders (Court of Justice of the European Union, 2010: 1).

There have been calls for a common set of rules related to interactive gambling at the EU-level (European Commission, 2011a: 1). However, there are differing views between the member countries regarding the extent of the required intervention by the EU (Gambling Compliance, 2012: 8). The European Commission has responded by issuing a Green Paper on on-line gambling for consultation, which paper might eventually lead to legislation being issued by the EU (European Commission 2011b).

3.2.1 Background to VAT in the European Union

Since VAT is a consumption tax, the VAT legislation in Europe is geared towards taxing electronic services in the country of destination, or where consumption takes place (European Commission (not dated):1). This section clarifies the VAT legislation in Europe relating to interactive gambling, as well as betting taxes on interactive gambling, to determine the consensus in Europe relating to the agreed place of supply of these cross-border activities.

VAT in the EU is a consumption-based tax system and the VAT is harmonised between the countries within the EU VAT area (European Union 2006:3). This area consists of all member countries of the EU and certain other countries, such as the Isle of Man, which follow the EU's rules on value added tax. VAT is not collected by the EU itself, but all member countries of the EU have to implement a VAT system that is harmonised with that prescribed by the EU. This does not mean that the rules are similarly applied in all countries within the EU VAT, since countries have certain discretion regarding the

application of the rules. Consequently, VAT rates may differ between countries and specific items may be exempted or fall within a lower rate between the different member countries. Where goods or services are sold between member countries within the European Union, this may complicate the VAT treatment of the transaction. For example, where a supplier situated in Sweden sells goods to a customer in Germany, the German buyer will pay VAT at the Swedish VAT rate, which is 6% higher than the VAT rate in Germany (European Commission 2012b: 3).

VAT in the EU generally applies to all goods and services that are consumed within the EU. Consequently, no VAT is generally levied on goods that are exported or services that are rendered to customers situated outside the EU. Goods and services imported into the EU are, however, subject to VAT. This ensures that suppliers within the EU can compete with other suppliers outside the EU on equal terms (European Commission (not dated): 1).

Since 17 May 1977 VAT in the EU was governed by the Sixth VAT Directive. The Sixth VAT Directive was replaced by the VAT Directive (Council Directive 2006/11/EC) on 1 January 2007. This has also subsequently been amended by Council Directive 2008/8/EC in order to ensure that supplies of services will be taxed in the place where actual consumption takes place (European Union, 2008:1).

3.2.2 Specific rules relating to the place of supply of electronic services in terms of the VAT Directive

The VAT treatment of electronically supplied services was laid out in Council Directive 2002/38/EC, adopted on 7 May 2002, which required non-EU vendors that provide electronic services to non-taxable customers in the EU to charge VAT, and consequently to register in the EU for VAT purposes (European Commission 2012a: 1). These provisions have also been included in the VAT Directive. VAT on electronically supplied services is levied based on where the customers reside. However, in the case of EU vendors supplying electronic services to customers from a different state within the EU, the place of supply will be where the supplier is located (Van der Paardt 2009: 525). This will be the case until 1 January 2015, when electronic services supplied by EU vendors to a non-taxable person situated within the EU will be taxed in the country in which the

customer is established (European Commission 2012a:1). Hence, the same rules will apply to EU vendors and non-EU vendors and this will “prevent distortions of competition between Member States operating different VAT rates” (Van der Paardt 2009:527).

Where non-EU suppliers provide electronic services to taxable businesses within the EU, the VAT is payable by the customer under a reverse charge mechanism (European Commission 2012a: 1). This effectively means that it is the VAT registered customer, and not the supplier, that will have the liability to submit the VAT return and pay the VAT to the relevant authorities.

The VAT Directive (European Union 2006) contains specific rules relating to the place of supply of electronic services. According to Annex II to the VAT Directive, which contains an “indicative list” of electronically supplied services, these services include “games of chance and gambling games” (European Union 2006:145). Article 135(1)(i) of the VAT Directive does however exempt “betting, lotteries and other forms of gambling, subject to the conditions and limitations laid down by each Member State”. According to Van der Paardt (2009:526) the fact that the exemption is limited to betting, lotteries and gambling, implies that all other types of gaming, such as internet games, will be subject to VAT.

The VAT Committee Guidelines (VAT Committee 2003) issued to provide guidance on what is included or excluded from the term “electronically supplied services” in the context of the Sixth VAT Directive, stated that electronically supplied services will be exempt from VAT, if the supply in the traditional manner is exempt from VAT (VAT Committee 2003:5). Similar guidance was, however, not issued in respect of the current VAT Directive.

In *Leo Libera GmbH v Finanzamt Buchholz in der Nordheide* (ECJ C-58-09) the European Court of Justice ruled that member states are allowed to only exempt certain forms of gambling from VAT (Lycka 2011:194). This means that in practice member states have a discretion not to exempt certain forms of gambling in terms of Article 135(1)(i) of the VAT Directive. The forms of gambling that are not exempted from VAT will consequently be subject to VAT in the country where the recipient of the services are established. This treatment is in line with the guidelines issued by the OECD, which recommends that taxation should be payable where the consumption of goods or services takes place (OECD, 2001:10). From a South African perspective this treatment will result in VAT being

payable in South Africa in terms of the VAT Act. However, the question remains as to how the collection of the VAT will practically be achieved by SARS. The OECD has come to the conclusion that a simplified online registration scheme is the only viable option for taxing e-commerce sales by non-resident traders (European Commission 2012a:2).

3.3 SPECIFIC EU COUNTRIES

The application of EU legislation in the different countries differs to some degree. Furthermore, the regulation of interactive gambling currently takes place at national level. As a result, the treatment of interactive gambling transactions differs between the different countries. This study will summarise the treatment of interactive gambling transactions in two EU countries, namely the United Kingdom and Ireland.

3.3.1 Interactive gambling in the United Kingdom

The United Kingdom allows its residents to participate in interactive gambling and allows interactive gambling operators to legally operate in the UK in terms of the Gambling Act, 2005. The act was instituted to promote and regulate the gambling industry in the UK, while protecting the customers (Gambling Review Commission 2010b: 22). The act also instituted a Gambling Commission to oversee the regulation of the industry and the licencing of interactive gambling providers in the UK. The Gambling Commission requires locally based interactive gambling service providers to be licensed in the UK, while off-shore providers can advertise their services to UK customers without a UK licence if they are situated within the EU, or a so-called “white-listed” country (Gambling Review Commission 2010a: 96).

Gambling and betting transactions are exempt from VAT in the UK, however, a 15% gambling tax is currently levied on the net gambling revenues of interactive gambling operators situated and licenced within the UK (Van Deventer, 2010: 50). Currently, therefore, the place of supply for interactive gambling is the place where the operator is established and consequently foreign operators fall outside the tax net.

The fact that interactive gambling providers can offer their services to UK citizens from a white-listed territory, resulted in a number of providers moving their operations off-shore in order to avoid the 15% gambling tax. By moving their operations to a tax-efficient white-listed destination, these operators could generate substantial savings.

The Chancellor of the Exchequer has, however, indicated in his 2012 budget speech that the place of supply will change to the place of consumption in the future (Grant Thornton, 2012:1). In terms of the planned legislation, operators will have to pay the 15% betting tax on gross gambling profits generated from UK residents, regardless of where the operator is situated. UK-based operators, that currently pay tax on all gambling profits, whether generated within the UK or from abroad, will get relief as they will now not be taxed on gambling revenues generated from non-UK residents (HM Treasury 2012:7).

This will bring the UK gambling tax within the guidelines issued by the OECD.

GamblingData (2012:4) estimated the interactive gambling market in the UK to be worth approximately £1.71bn during 2011. This means that the change to a point of consumption tax in future can generate tax revenues of up to £242m on the 2011 estimates (GamblingData 2012:4).

3.3.2 Interactive gambling in the Republic of Ireland

In Ireland sports betting, betting on horse races, betting exchanges, poker and skill games are currently offered online (Williams & Wood, 2007:13). Irish residents can participate in interactive gambling hosted by local or off-shore operators. However, to the date of this study interactive gambling has not been specifically regulated or taxed in Ireland and off-shore bookmakers can offer interactive gambling services to Irish residents without a valid Irish bookmaking licence (Merrionstreet 2012:1).

The intention of the Irish government to bring interactive bookmakers and betting exchanges into the tax net culminated in amendments to the Finance Act 2002 (5 of 2002) brought about by section 49 of the Finance Act 2011 (6 of 2011). These amendments provide specifically for the taxation of interactive bookmakers and betting exchanges, but

the commencement of this section is subject to an order by the Minister of Finance (Section 49(3) of the Finance Act 2011), as a licencing regime is not yet in place in respect of interactive gambling specifically.

This is set to change when the Betting (Amendment) Bill 2012 is enacted. This bill aims to ensure that all interactive bookmakers and betting service providers offering interactive gambling services from Ireland or to persons in Ireland are regulated and brought within the tax net (Merrionstreet 2012:1). The bill addresses bookmaking and betting services, but does not address other gaming services. Consequently, those interactive gambling service providers that do not provide online betting services, but do provide other interactive gambling games such as poker, blackjack and roulette, will still not be regulated in terms of any act and will therefore fall outside the Irish tax net (Murray 2012:1).

As is the situation in South Africa, Irish law distinguishes between gaming and betting transactions. Betting is regulated in terms of the Betting Act, 1931 (27 of 1931), whereas gaming is regulated in terms of the Gaming and Lotteries Act, 1956 (2 of 1956) (hereafter referred to as the Gaming and Lotteries Act).

“Gaming” is defined in the Gaming and Lotteries Act as “playing a game (whether of skill or chance or partly of skill and partly of chance) for stakes hazarded by the players” (Section 2 of the Gaming and Lotteries Act). The player therefore participates in the game. When “betting”, however, the person making the bet on a particular event does not influence the outcome of the event. Section 4 of the Gaming and Lotteries Act prohibits games where the chances of all players are not equal or where a portion of the stakes is retained by the operator, which seems to prohibit most casino-type games (Thompson 2010: 121). However, a number of loopholes in the law have allowed casino type facilities to be operated in Ireland in the form of “private members clubs” and amusement halls (Thompson 2010:121-122; Department of Justice, Equality and Law Reform 2008:2,4). Regardless of the fact that the services provided by interactive gambling operators might be illegal, interactive gambling provided by off-shore operators have not been clamped down on by Irish authorities (The art of iGaming (not dated): 1)

The distinction between gambling and betting has relevance as betting transactions that are subject to excise duty, or that are exempted from excise duty in terms of the Finance Act 2002 (5 of 2002) are exempted activities in terms of the Value-added Tax Consolidation Act, 2010 (31 of 2010) (hereafter referred to as the VAT Consolidation Act). As the Finance Act 2002 only addresses betting transactions, only betting transactions are exempted from VAT, whereas other gambling activities are not exempted and are therefore taxable at the standard rate (Revenue Commissioners 2010:1). Interactive gambling may therefore be subject to VAT depending on where the customer is situated.

Section 34 of the VAT Consolidation Act clarifies the place of supply of electronic services, which include games of chance and gambling games (Section 2 of the VAT Consolidation Act). The place of supply of electronic services that are supplied by a non-resident taxable person to a non-taxable person in Ireland is deemed to be in Ireland (Section 34(l) of the VAT Consolidation Act). Where the electronic services are supplied to a person outside of Ireland, then the place of supply is deemed to be where that person is established (Section 34(m) of the VAT Consolidation Act).

Although the supply of interactive gambling services by foreign operators seems to fall within the VAT net in Ireland on the face of the legislation, it could not be determined whether this is in fact enforced by the Irish Revenue Commissioners.

3.4 INTERACTIVE GAMBLING IN AUSTRALIA

The Australian Interactive Gambling Act 2001 prohibits local and off-shore interactive gambling providers from offering interactive gambling services to players physically located in Australia (Department of Broadband Communications and the Digital Economy 2012: 20). By contrast, locally licensed interactive gambling operators may offer its interactive gambling activities to residents from foreign countries, provided that it is permitted in that specific country (Van Deventer, 2010: 47). Customers physically located within Australia are, however, not prohibited from taking part in interactive gambling. Although foreign-based interactive gambling providers are also prohibited from providing services to Australian customers, this is very difficult to enforce, with the consequence that Australian customers solely gamble online with interactive gambling companies situated

off-shore and therefore regulated in a different jurisdiction (Productivity Commission 2010:15.18).

The Australian Taxation Office levies a goods and services tax (GST) (similar to VAT) of one eleventh of the net gambling revenue of interactive service providers registered in the country, however, no tax is levied on service providers rendering services from outside the country. Gambling services supplied to gamblers situated outside of Australia are also deemed to be GST-free exports. Gambling operators situated within Australia have to record details (residential address and contact details as a minimum) in order to prove to the revenue authorities that the gambling sale is GST-free. (Australian tax office: not dated).

The Australian GST system is territorially or destination-based and has specific place of supply rules (Schenk & Oldman 2007: 196). The place of supply rules under Australian GST is basically determined based on the “connected with Australia” principles. Under the place of supply rules a supply of services will be connected with Australia if the service is performed in Australia, or if the supplier has an enterprise in Australia carried on through a permanent establishment in Australia (Schenk & Oldman 2007: 196).

In general, the Australian GST system aims to tax goods and services where consumption takes place. This principle is sometimes waived for practical or administrative reasons. For example: where services are supplied over the internet by an off-shore supplier to private customers that are not registered, or required to be registered for GST, these services are not subject to GST (Board of Taxation 2009:13). Interactive gambling services offered by off-shore interactive gambling providers will therefore fall outside the Australian VAT net.

3.5 CONCLUSION

In this chapter the literature related to the VAT legislation pertaining to interactive gambling in the European Union and Australia was analysed. In most European countries gambling transactions are exempt from VAT, however, as interactive gambling falls within the

definition of electronically supplied services, the applicable place of supply rules related to electronically supplied services were analysed.

This chapter specifically analysed the situation pertaining to the taxing of interactive gambling activities in the UK and Ireland to determine where the supply of the gambling services is deemed to take place.

The UK was selected as it was one of the first countries to legalise and regulate interactive gambling. Although interactive gambling is exempt from VAT in the UK, a 15% gambling tax is currently levied on the net gambling revenues of interactive gambling operators situated and licenced within the UK. This system will change to a destination-based system in future which means that the place of supply of interactive gambling transactions will now be deemed to be where the gambler is situated.

Ireland is an interesting case study as it is one of the only European countries that have not exempted all forms of gambling from VAT. Betting and lotteries are exempt from VAT, however, other gambling transactions have not been exempted. To the date of this study interactive gambling transactions have also not been regulated in Ireland, however, as certain interactive gambling transactions have not been exempted from VAT, the application of the Irish VAT legislation to these interactive gambling transactions would indicate that these transactions should be subject to VAT. This does not appear to be enforced and consequently no VAT is levied on off-shore based interactive gambling operators providing services to Irish residents.

Similarly to South Africa, Australia prohibits interactive gambling service providers from offering services to persons physically present in Australia. Individuals are, however, not prohibited from gambling online. Since off-shore interactive gambling service providers are difficult to regulate (and Australia has not enforced the prohibition related to off-shore providers), Australian individuals gamble online with interactive gambling service providers situated off-shore.

The study determined that there are GST place of supply rules in place in Australia that addresses services supplied over the internet, which will include interactive gambling

services. Where these services are supplied to private consumers by an off-shore provider, these transactions are not subject to GST. This results in off-shore interactive gambling service providers falling outside the Australian GST net.

CHAPTER 4

CONCLUSION AND VALUE OF THE STUDY

4.1 INTRODUCTION

Transactions are increasingly taking place over the internet which is essentially a borderless environment. In this context in particular, VAT place of supply rules provide certainty regarding where a supply is deemed to take place in order to determine the correct treatment for VAT purposes.

The limited place of supply rules in South Africa creates uncertainty regarding where the business activities of a non-resident supplier is deemed to take place. Consequently, where interactive gambling transactions take place across borders there is also uncertainty where the transaction will be liable to VAT.

The main objective of this study was to critically analyse the South African VAT implications of interactive gambling in the absence of detailed place of supply rules. This study consisted of an extensive literature review which comprised of an analysis of the legislative framework for interactive gambling in South Africa and an analysis of the provisions of the South African VAT Act in order to determine the applicability thereof to interactive gambling transactions. The legislation was critically analysed to determine whether it succeeds in providing certainty regarding the place of supply of interactive gambling transactions for purposes of South African VAT. The results from this analysis are presented in chapter 2.

The legislation related to interactive gambling transactions in the European Union and Australia, which have place of supply rules, was critically analysed from a South African perspective. The results from this analysis are presented in chapter 3 of the present study.

The current chapter summarises the findings and presents the conclusions related to the main objective of the study.

4.1 SUMMARY OF FINDINGS RELATED TO THE RESEARCH OBJECTIVES

The following specific research objectives guided this study:

- To critically analyse the applicable provisions of the South African VAT Act to determine whether interactive gambling transactions fall within the ambit of the VAT Act.
- To critically analyse place of supply rules and VAT or goods and services tax (GST) legislation in a number of countries with detail place of supply rules related to interactive gambling transactions, from a South African perspective.

The South African VAT Act was analysed in detail in chapter 2 of the study. From an analysis of Section 7(1) of the VAT Act it was determined that a supply of services may be subject to VAT where a vendor supplies services in the course or furtherance of any enterprise or where services are imported by any person. The concepts “enterprise” and “imported services” were then further analysed as it relates to interactive gambling (see Section 2.4).

In relation to the definition of an “enterprise” it was found that it was the concept of “in or partly in South Africa” that created the biggest uncertainty regarding where interactive gambling services are deemed to take place. If the supply of gambling facilities takes place in or partly in South Africa, then the interactive gambling provider may be deemed to carry on an enterprise in South Africa, provided that the other elements of the definition of an “enterprise” are met. The other elements, however, do not present the same problems in interpretation as “in or partly in South Africa” in the absence of place of supply rules (see Section 2.4.2).

The Supreme Court of Appeal ruling in *Casino Enterprises v Gauteng Gambling Board and Others* confirmed that interactive gambling takes place where the punter is situated, however, as the judgement did not specifically address the place of supply for VAT purposes, it remains to be seen whether this decision can form the basis of a VAT place of supply rule for interactive gambling in future (see Section 2.3).

In determining whether a supply of interactive gambling services by a foreign vendor to a consumer in South Africa constitutes an “imported service”, difficulties were also identified in determining where the services are utilised or consumed (see Section 2.4.3).

The conclusion reached in Chapter 2 was that the analysis of the current VAT legislation in the context of interactive gambling highlighted the problems associated with the limited place of supply rules in South Africa.

In chapter 3 the VAT place of supply rules and VAT or GST legislation in the European Union and Australia were analysed with reference to interactive gambling transactions. The place of supply rules in the European Union related to electronically supplied services, which includes interactive gambling services, directs that such a supply is deemed to take place where the consumer is situated (see Section 3.2.2). The European VAT legislation also requires foreign suppliers that supplies electronic services to a private consumer within the European Union to register as a VAT vendor in the European Union. Gambling transactions are, however, exempt from VAT in most countries in the European Union (see Section 3.2.2).

Two specific countries in the European Union, namely the United Kingdom and the Republic of Ireland were also analysed to demonstrate the differences in the treatment of interactive gambling transactions within the European Union.

Interactive gambling is exempt from VAT in the United Kingdom however a 15% gambling tax is levied on net gambling revenues. Currently, the place of supply of interactive gambling is deemed to be where the supplier of the services is situated however, in future the place of supply will change to the place of consumption in future, which will be where the consumer is situated. This will bring the UK gambling tax within the guidelines issued by the OECD (see Section 3.3.1).

Unlike the situation in the United Kingdom, Ireland has not exempted all gambling transactions from VAT. A review of the literature indicates that interactive gambling transactions supplied by off-shore providers should be subject to VAT. However, due to

the fact that interactive gambling is not regulated in Ireland, it does not appear that this is enforced by the revenue authorities (see Section 3.3.2).

The Australian place of supply rules regarding interactive gambling transactions were analysed in order to obtain a perspective from outside the European Union. In contrast to the other countries analysed, Australia has elected not to subject supplies of services over the internet by an off-shore provider to a private consumer to GST, because of practical or administrative difficulties (see Section 3.4).

4.2 SUMMARY OF THE CONTRIBUTIONS OF THE STUDY

Prior research has focussed on the income tax consequences of interactive gambling transactions in South Africa, however, the applicability of South African VAT legislation on interactive gambling transactions have not been researched.

The study contributes to an understanding of the place of supply of interactive gambling transactions in the context of the South African VAT Act and highlights the problems associated with the limited place of supply rules in South Africa. It also investigated the place of supply rules in the European Union and Australia that can assist in formulating place of supply rules in South Africa.

4.3 LIMITATIONS OF THE PRESENT RESEARCH AND RECOMMENDATIONS FOR FUTURE RESEARCH

If the place of supply of interactive gambling transactions are deemed to take place where the consumer is situated, this treatment may result in VAT being payable in South Africa in terms of the VAT Act and may also result in the non-resident company being liable to register as a VAT vendor in South Africa. However, this study does not address the question of how the collection of the VAT from the non-resident supplier will practically be achieved by SARS. The OECD has come to the conclusion that a simplified online registration scheme is the only viable option for taxing e-commerce sales by non-resident traders. Future research can focus on the specific mechanisms required to implement the collection of VAT related to interactive gambling services.

This study did not address the income tax consequences of interactive gambling as well as the consequences of double taxation agreements on the deemed place of supply of interactive gambling activities, which may provide an area for future study.

The study also did not consider the implication of illegal interactive gambling transactions on the taxability thereof in terms of the VAT Act. This can be further researched in the context of the case of MP Finance Group CC (In Liquidation) v CSARS (69 SATC 141), where the Supreme Court of Appeal ruled that the income received by a taxpayer from illegal activities should be taxable in the hands of the taxpayer. Although this case specifically addressed the income tax consequences of illegal transactions, the applicability thereof on the liability of an illegal supplier of interactive gambling services for South African value-added tax can be researched.

4.4 CONCLUSION

This study highlighted the fact that the absence of detailed place of supply rules in respect of electronic services creates uncertainty regarding where the supplies of a non-resident interactive gambling supplier to a South African resident is deemed to take place and consequently whether the supply will be subject to VAT in South Africa. The VAT place of supply rules in South Africa are not specific enough to clear the uncertainty surrounding the taxability of interactive gambling transactions in South Africa, which may result in a failure to bring these transactions within the South African VAT net.

The introduction of place of supply rules in South Africa related to the electronic supply of services in general and interactive gambling specifically will go a long way to clear any uncertainty regarding where a transaction is deemed to take place. The place of supply rules in the European Union are in line with the guidelines issued by the OECD, which indicates that interactive gambling transactions should be taxed where the consumer is situated. This also does not contradict the decision reached by the Supreme Court in the Casino Enterprises-case. The problems associated with the limited place of supply rules in South Africa can therefore be alleviated by amending the existing legislation, or by issuing interpretation guidance through SARS, that sets out the place of supply of e-

commerce transactions in general and interactive gambling transactions specifically. This will also ensure that South African interactive gambling service providers are able to compete on equal terms with foreign interactive gambling service providers, once interactive gambling licences are issued.

The Australian option of exempting electronic services provided by non-resident suppliers to private consumers situated in the country does not appear to be fair to local service providers, whose services will be 14% more expensive than those supplied by a non-resident supplier.

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