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13 December 2011

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Dear Mr Moodley

VALUE-ADDED TAX: CALCULATION OF PHARMACY DISPENSING FEES

I write with reference to your e-mail communication and the various attachments to that communication which were sent to Mr Ivan Pillay on 25 November 2011 regarding your question on VAT and the calculation of pharmacists dispensing fees.

1. BACKGROUND

Based on the information provided, it is understood that the position as you see it, is as set out below.

- 1.1. The National Department of Health (NDOH) published the amendments to the dispensing fee structure for pharmacists on the 19 November 2010 (per Government Notice R.1090 Gazette No 33775) in terms of the Medicines And Related Substances Act, 1965 (Act No 101 of 1965): Regulations Relating to a Transparent Pricing System for Medicines and Scheduled Substances.
- 1.2. An interpretation of the methodology to perform the calculation was circulated on the same day by the Director General of NDOH. The prescribed methodology requires that the medicine be identified according to a four-tiered structure. Depending on the structure in which the particular item appears, the Dispensing Fee is calculated as a percentage of the so-called "Single Exit Price" (SEP) of medicines dispensed, plus a fixed Rand amount.
- 1.3. The Dispensing Fee calculated in paragraph 1.3 above is prescribed to be a VAT-exclusive amount. VAT at the standard rate of 14% is therefore added as the final step to obtain the final VAT-inclusive dispensing fee in the case of a pharmacy that is registered for VAT.
- 1.4. Both the NDOH and Pharmacy Stakeholder's Forum are quite clear that the fee calculation as set out in the NDOH circular is correct. However, the medical schemes have chosen to ignore this interpretation until they get written clarity on a South African Revenue Service (SARS) letterhead confirming the NDOH interpretation.
- 1.5. The interpretation adopted by the medical schemes is that as the SEP is defined to include VAT, it must first be removed from the SEP before performing the calculation as described in paragraphs 1.3 and 1.4 above.

- 1.6. The Pharmacy Stakeholder's Forum considers that the view of the medical schemes on the calculation methodology is contrary to the Government Notice R.1090 and the circular from the NDOH explaining the methodology.

2. REQUEST

- 2.1. The solution proposed by the Pharmacy Stakeholder's Forum to resolve this impasse in the industry, is to obtain confirmation from SARS on a letterhead supporting the interpretation set out in the NDOH circular.
- 2.2. SARS is therefore requested to issue a letter confirming the calculation methodology as communicated in the circular by the NDOH dated to the 19 November 2010 to the industry. Alternatively, to provide the correct interpretation.

3. THE LAW

For ease of reference, the relevant sections of the VAT Act are quoted in Annexure A.

4. APPLICATION OF THE LAW

- 4.1 VAT is levied at the applicable rate on the value of a supply. The value of a supply is generally determined in accordance with the provisions of section 10(2) which provides that the value of a supply is determined by deducting the VAT from the consideration payable for the supply. In other words, the value of a supply is the VAT exclusive amount.
- 4.2 In the case of Dispensing Fees charged by pharmacies, it is clear that Government Notice R.1090 establishes the method for determining the value of the supply. In terms of the prescribed methodology, there is also nothing which would suggest that any element forming a component of the SEP (for example, VAT) can be excluded before performing the calculation.

5 CONFIRMATION

- 5.1 The view is held that the application of the pricing methodology for determining the value of Dispensing Fee payable to pharmacies which is set out in Government Notice R.1090 dated 19 November 2010 has been explained correctly in the NDOH circular dated 19 November 2010.
- 5.2 This confirmation is based solely on the information, documents, and representation of facts submitted or referred to in this document as being true and accurate.

Yours faithfully



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for THE COMMISSIONER FOR THE SOUTH AFRICAN REVENUE SERVICE

The Value-Added Tax Act, No. 89 of 1991 (the VAT Act)**Section 10(2)**

- (2) The value to be placed on any supply of goods or services shall, save as is otherwise provided in this section, be the amount of the consideration for such supply, as determined in accordance with the provisions of subsection (3), less so much of such amount as represents tax: Provided that—
- (i) there shall be excluded from such consideration the value of any postage stamp as defined in section 1 of the Post Office Act, 1958 (Act No. 44 of 1958), when used in the payment of consideration for any service supplied by the postal company as defined in section 1 of the Post Office Act, 1958;
 - (ii) where the portion of the amount of the said consideration which represents tax is not accounted for separately by the vendor, the said portion shall be deemed to be an amount equal to the tax fraction of that consideration.

The Value-Added Tax Act, No. 89 of 1991 (the VAT Act)

Section 10(2)