2017 Budget and Tax Update

March 2017

Workbook

Facilitated by ProBeta Training (Pty) Ltd

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2017 BUDGET AND TAX UPDATE

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PART 1-BUDGET 2017

The notes that follow draw extensively from the National Treasury Budget Review 2017.

HIGHLIGHTS

- A budget deficit of 3.4 per cent of GDP is expected for 2016/17, narrowing to 2.6 per cent in 2019/20.
- Debt stock as a percentage of GDP is expected to stabilise at 48.2 per cent in 2020/21.
- The main budget non-interest expenditure ceiling has been lowered by R26 billion over the next two years.
- R28 billion in additional tax revenue will be raised in 2017/18. Measures to increase revenue by a proposed R15 billion in 2018/19 will be outlined in the 2018 Budget.
- R30 billion has been reprioritised through the budget process to ensure that core social expenditure is protected.
- Real growth in non-interest spending will average 1.9 per cent over the next three years. Apart from debt-service costs, postschool education is the fastest-growing category, followed by health and social protection.

SPENDING PROGRAMMES

Over the next three years, government will spend:

- R490.4 billion on social grants.
- R105.9 billion on transfers to universities, while the National Student Financial Aid Scheme will spend R54.3 billion.
- R751.9 billion on basic education, including R48.3 billion for direct subsidies to schools, R42.9 billion for infrastructure, and R12.7 billion for learner and teacher support materials.
- R114.8 billion on subsidised public housing.
- R94.4 billion on water resources and bulk infrastructure.
- R189 billion on transfers of the local government equitable share to provide basic services to poor households.
- R142.6 billion to support affordable public transport.
- R606 billion on health, with R59.5 billion on the HIV/AIDS conditional grant.

INDIVIDUALS

TAX TABLES 2017/18

Taxable income R			Rate of tax				
0	-	189 880			18%		
189 881	-	296 540	34 178	+	26%	of the excess over	189 880
296 541	-	410 460	61 910	+	31%	of the excess over	296 540
410 461	-	555 600	97 225	+	36%	of the excess over	410 460
555 601	-	708 310	149 475	+	39%	of the excess over	555 600
708 311	-	1 500 000	209 032	+	41%	of the excess over	708 310
1 500 001	-	exceeding	533 625	+	45%	of the excess over	1 500 000

TAX TABLES 2016/17

Taxable income R			Rate of tax				
0	-	188 000			18%		
188 001	-	293 600	33 840	+	26%	of the excess over	188 000
293 601	-	406 400	61 296	+	31%	of the excess over	293 600
406 401	-	550 100	96 264	+	36%	of the excess over	406 400
550 101	-	701 300	147 996	+	39%	of the excess over	550 100
701 301	-	exceeding	206 964	+	41%	of the excess over	701 300

REBATES

	2017/18 R	2016/17 R	2015/16 R
Primary	13 635	13 500	13 257
Secondary (Age 65 and over)	7 479	7 407	7 407
Tertiary rebate (Age 75 and over)	2 493	2 466	2 466

TAX THRESHOLD

	2017/18 R	2016/17 R	2015/16 R
Below age 65	75 750	75 000	73 650
Age 65 to 74	117 300	116 150	114 800
Age 75 and over	131 150	129 850	128 500

The proposed changes to the tax tables and rebates partially compensates individuals for the effect of inflation on income tax liabilities. The impacts of these proposals are set below:

LOCAL INTEREST EXEMPTION

	2017/18 R	2016/17 R	2015/16 R
Natural persons below age 65	23 800	23 800	23 800
Age 65 and over	34 500	34 500	34 500

TAXABLE FOREIGN DIVIDEND EXEMPTION

	2017/18 R	2016/17 R	2015/16 R
Natural persons	25/45	26/41	26/41

MONTHLY MEDICAL SCHEME TAX CREDITS

	2017/18 R	2016/17 R	2015/16 R
Taxpayer and first dependant	303	286	270
Each additional dependant	204	192	181

CGT EXCLUSIONS (NATURAL PERSONS)

	2017/18 R	2016/17 R	2015/16 R
Annual exclusion for capital gains or losses	40 000	40 000	30 000
Annual exclusion in year of death for capital gains or losses	300 000	300 000	300 000
Primary residence exclusion for capital gains or losses	2 000 000	2 000 000	2 000 000
Disposal of a small business when a person is over age 55	1 800 000	1 800 000	1 800 000
Max assets to qualify as a small business above	10 000 000	10 000 000	10 000 000

TRAVEL ALLOWANCE: DEEMED EXPENDITURE TABLE WITH EFFECT FROM 1 MARCH 2018

Value of the vehicle R			Fixed cost R	Fuel cost c/km	Maintenance cost c/km
	-	85 000	28 492	91.2	32.9
85 001	-	170 000	50 924	101.8	41.2
170 001	-	255 000	73 427	110.6	45.4
255 001	-	340 000	93 267	118.9	49.6
340 001	-	425 000	113 179	127.2	58.2
425 001	-	510 000	134 035	146.0	68.4
510 001	-	595 000	154 879	150.9	84.9
595 001	-	and above	154 879	150.9	84.9

TRAVEL ALLOWANCE: DEEMED EXPENDITURE TABLE WITH EFFECT FROM 1 MARCH 2017

Value of the vehicle R			Fixed cost R	Fuel cost c/km	Maintenance cost c/km
	-	80 000	26 675	82.4	30.8
80 001	-	160 000	47 644	92.0	38.6
160 001	-	240 000	68 684	100.0	42.5
240 001	-	320 000	87 223	107.5	46.4
320 001	-	400 000	105 822	115.0	54.5
400 001	-	480 000	125 303	132.0	64.0
480 001	-	560 000	144 784	136.5	79.5
560 001	-	and above	144 784	136.5	79.5

Note:

- 80% of the travelling allowance must be included in the employee's remuneration for the purposes of calculating PAYE. The percentage is reduced to 20% if the employer is satisfied that at least 80% of the use of the motor vehicle for the tax year will be for business purposes.
- No fuel cost may be claimed if the employee has not borne the full cost of fuel used in the vehicle and no maintenance cost may be claimed if the employee has not borne the full cost of maintaining the vehicle (e.g. if the vehicle is the subject of a maintenance plan).
- The fixed cost must be reduced on a pro-rata basis if the vehicle is used for business purposes for less than a full year.
- The actual distance travelled during a tax year and the distance travelled for business purposes substantiated by a log book are used to determine the costs which may be claimed against a travelling allowance.

Alternative to the rate table:

Where the distance travelled for business purposes does not exceed 12 000 kilometers per annum, no tax is payable on an allowance paid by an employer to an employee up to the rate of 355 cents per kilometer, regardless of the value of the vehicle.This alternative is not available if other compensation in the form of an allowance or reimbursement (other than for parking or toll fees) is received from the employer in respect of the vehicle.

SUBSISTENCE ALLOWANCE: DEEMED EXPENDITURE DAILY LIMITS

The following amounts will be deemed to have been actually expended by a recipient to whom an allowance or advance has been granted or paid:

	2017/18 R	2016/17 R	2015/16 R
Where the accommodation, to which that allowance or advance relates, is in the Republic and that allowance or advance is paid or granted to defray:			
Incidental costs only	122 per day	115 per day	109 per day
The cost of meals and incidental costs	397 per day	372 per day	353 per day

Where the accommodation, to which that allowance or advance relates, is outside the Republic and that allowance or advance is paid or granted to defray the cost of meals and incidental costs, an amount per day determined in accordance with the following table for the country in which that accommodation is located:

DAILY AMOUNT FOR TRAVEL OUTSIDE THE REPUBLIC

Country	Currency	Amount
Albania	Euro	97
Algeria	Euro	110
Angola	US $	303
Antigua and Barbuda	US $	220
Argentina	US $	133
Armenia	US $	220
Austria	Euro	131
Australia	A $	230
Azarbaijani	US $	145
Bahamas	US $	191
Bahrain	B Dinars	36
Bangladesh	US $	79
Barbados	US $	202
Belarus	Euro	62
Belgium	Euro	146
Belize	US $	152
Benin	Euro	111
Bolivia	US $	78
Bosnia-Herzegovina	Euro	75
Botswana	Pula	826
Brazil	Reals	409
Brunei	US $	88
Bulgaria	Euro	91
Burkina Faso	CFA Francs	58,790
Burundi	Euro	73

Cambodia	US $	99
Cameroon	Euro	120
Canada	C $	177
Cape Verde Islands	Euro	65
Central African Republic	Euro	94
Chad	Euro	121
Chile	US $	106
China (People's Republic)	US $	127
Colombia	US $	94
Comoro Island	Euro	122
Cook Islands	NZ $	211
Cote D'Ivoire	Euro	119
Costa Rica	US $	116
Croatia	Euro	99
Cuba	US $	114
Cyprus	Euro	117
Czech Republic	Euro	90
Democratic Republic of Congo	US $	164
Denmark	Danish Kroner	2,328
Djibouti	US $	99
Dominican Republic	US $	99
Ecuador	US $	163
Egypt	Egyptian Pounds	873
El Salvador	US $	98
Equatorial Guinea	Euro	166
Eritrea	US $	109
Estonia	Euro	92
Ethiopia	US $	95
Fiji	US $	102
Finland	Euro	171
France	Euro	129
Gabon	Euro	160
Gambia	Euro	74
Georgia	US $	95
Germany	Euro	125
Ghana	US $	130
Greece	Euro	138
Grenada	US $	151
Guatemala	US $	114
Guinea	Euro	78
Guinea Bissau	Euro	59
Guyana	US $	118
Haiti	US $	109
Honduras	US $	186
Hong Kong	Hong Kong $	1,395
Hungary	Euro	92
Iceland	ISK	25,466

India	Indian Rupee	5,932
Indonesia	US $	86
Iran	US $	120
Iraq	US $	125
Ireland	Euro	139
Israel	US $	209
Italy	Euro	125
Jamaica	US $	151
Japan	Yen	16,424
Jordan	US $	201
Kazakhstan	US $	100
Kenya	US $	138
Kiribati	Australian $	233
Korea, Republic	Korean Won	184,642
Kuwait (State of)	Kuwait Dinars	51
Kyrgyzstan	US $	172
Laos	US $	92
Latvia	US $	150
Lebanon	US $	158
Lesotho	RSA Rand	750
Liberia	US $	112
Libya	US $	120
Lithuania	Euro	154
Macao	Hong Kong $	1,196
Macedonia (Former Yugoslav)	Euro	100
Madagascar	Euro	58
Madeira	Euro	290
Malawi	Malawi Kwacha	31,254
Malaysia	Ringgit	382
Maldives	US $	202
Mali	Euro	178
Malta	Euro	132
Marshall Islands	US $	255
Mauritania	Euro	97
Mauritius	US $	114
Mexico	Mexican Pesos	1,313
Moldova	US $	117
Mongolia	US $	69
Montenegro	Euro	94
Morocco	Dirhams	1,081
Mozambique	US $	101
Myanmar	US $	123
Namibia	RSA Rands	950
Nauru	Australian $	278
Nepal	US $	64
Netherlands	Euro	122
New Zealand	NZ $	206

Nicaragua	US $	90
Niger	Euro	75
Nigeria	US $	242
Niue	New Zealand $	252
Norway	NOK	1,753
Oman	Rials Omani	77
Pakistan	Pakistani Rupees	6,235
Palau	US $	252
Palestine	US $	147
Panama	US $	105
Papa New Guinea	Kina	285
Paraguay	US $	76
Peru	US $	139
Philippines	US $	122
Poland	Euro	88
Portugal	Euro	87
Qatar	Qatar Riyals	715
Republic of Congo	Euro	149
Reunion	Euro	164
Romania	Euro	83
Russia	Euro	330
Rwanda	US $	102
Samoa	Tala	193
Sao Tome & Pinciple	Euro	160
Saudi Arabia	Saudi Riyals	512
Senegal	Euro	113
Serbia	Euro	83
Seychelles	Euro	132
Sierra Leone	US $	90
Singapore	Singapore $	232
Slovakia	Euro	102
Slovenia	Euro	106
Solomon Islands	Sol Islands $	1,107
South Sudan	US $	146
Spain	Euro	112
Sri Lanka	US $	100
St. Kitts & Nevis	US $	227
St. Lucia	US $	215
St. Vincent & The Grenadines	US $	187
Sudan	US $	200
Suriname	US $	107
Swaziland	RSA Rand	1,367
Sweden	Swedish Kronor	1,317
Switzerland	S Franc	201
Syria	US $	185
Taiwan	New Taiwan $	4,015
Tajikistan	US $	97

Tanzania	US $	129
Thailand	Thai Baht	4,956
Togo	CFA Francs	64,214
Tonga	Pa'anga	251
Trinidad & Tobago	US $	213
Tunisia	Tunisian Dinar	198
Turkey	Euro	101
Turkmenistan	US $	125
Tuvalu	Australian $	339
Uganda	US $	111
Ukraine	Euro	131
United Arab Emirates	UAE Dirhams	699
United Kingdom	British Pounds	102
Uruguay	US $	133
USA	US $	155
Uzbekistan	Euro	80
Vanuatu	US $	166
Venezuela	US $	294
Vietnam	US $	91
Yemen	US $	94
Zambia	US $	119
Zimbabwe	US $	123
Other countries not listed	US $	215

RETIREMENT AND PRE-RETIREMENT LUMP SUM BENEFITS

PRE-RETIREMENT LUMP SUMS RETIREMENT FUND LUMP SUM WITHDRAWAL BENEFITS

Taxable lump sum R			Rate of tax		
0	-	25 000			0%
25 001	-	660 000	0		18% of the amount exceeding R 25 000
660 001	-	990 000	114 300	+	27% of the amount exceeding R660 000
990 001	-	and above	203 400	+	36% of the amount exceeding R990 000

Retirement fund lump sum withdrawal benefits consist of lump sums from a pension, pension preservation, provident, provident preservation or retirement annuity fund on withdrawal (including assignment in terms of a divorce order). Tax on a specific retirement fund lump sum withdrawal benefit (X) is equal to –

- Tax determined by applying the tax table to the aggregate of that lump sum X plus all other retirement fund lump sum withdrawal benefits accruing from March 2009 and all retirement fund lump sum benefits accruing from October 2007 and all severance benefits accruing from March 2011; less
- Tax determined by applying the tax table to the aggregate of all retirement fund lump sum withdrawal benefits accruing before lump sum X from March 2009 and all retirement fund lump sum benefits accruing from October 2007 and all severance benefits accruing from March 2011.

RETIREMENT AND DEATH LUMP SUMS AND SEVERANCE BENEFITS RETIREMENT FUND LUMP SUM BENEFITS TABLE

Taxable lump sum R			Rate of tax		
0	-	500 000			0%
500 001	-	700 000	0	+	18% of the amount exceeding R500 000
700 001	-	1 050 000	36 000	+	27% of the amount exceeding R700 000
1 050 001	-	and above	130 500	+	36% of the amount exceeding R1 050 000

Retirement fund lump sum benefits consist of lump sums from a pension, pension preservation, provident, provident preservation or retirement annuity fund on death, retirement or termination of employment due to redundancy or termination of employer's trade. Severance benefits consist of lump sums or by arrangement with an employer due to relinquishment, termination, loss, repudiation, cancellation or variation of a person's office or employment. Tax on a specific retirement fund lump sum benefit or a severance benefit (Y) is equal to:

- Tax determined by applying the tax table to the aggregate of that lump sum or severance benefit Y plus all other retirement fund lump sum benefits accruing from October 2007 and all retirement fund lump sum withdrawal benefits accruing from March 2009 and all other severance benefits accruing from March 2011; less
- Tax determined by applying the tax table to the aggregate of all retirement fund lump sum benefits accruing before lump sum Y from October 2007 and all retirement fund lump sum withdrawal benefits accruing from March 2009 and all severance benefits accruing before severance benefit Y from March 2011.

CORPORATE TAX RATES

COMPANIES

	Years of assessment ending between 1 April and 31 March	
	2017/18	2016/17
Non-mining companies	28%	28%
Close corporations	28%	28%
Employment companies (personal service provider)	28%	28%
Taxable income of a non-resident company (SA branch)	28%	28%

TAXABLE FOREIGN DIVIDEND EXEMPTION

	2017/18 R	2016/17 R	2015/16 R
Persons other than natural persons	8 28	13 28	13 28

TAX RATES FOR QUALIFYING SMALL BUSINESS CORPORATIONS

Years of assessment ending between 1 April 2017 and 31 March 2018							
Taxable income R							Rate of tax
0	-	75 750			0%		
75 751	-	365 000			7%	of the excess over	75 750
365 001	-	550 000	20 248	+	21%	of the excess over	365 000
550 001	-	and above	59 098	+	28%	of the excess over	550 000

Years of assessment ending between 1 April 2016 and 31 March 2017							
Taxable income R							Rate of tax
0	-	75 000			0%		
75 001	-	365 000			7%	of the excess over	75 000
365 001	-	550 000	20 300	+	21%	of the excess over	365 000
550 001	-	and above	59 150	+	28%	of the excess over	550 000

PRESUMPTIVE TURNOVER TAX ON MICRO BUSINESSES

The turnover tax regime was introduced to limit the compliance burden on micro businesses with annual turnover of up to R1 million.

Years of assessment ending between 1 March 2017 and 28 February 2018							
Taxable Turnover R							Rate of tax
0	-	335 000			0%		
335 001	-	500 000			1%	of the excess over	335 000
500 001	-	750 000	1 650	+	2%	of the excess over	500 000
750 001	-	1 000 000	6 650	+	3%	of the excess over	750 000

Years of assessment ending between 1 March 2016 and 28 February 2017							
Taxable Turnover R							**Rate of tax**
0	-	335 000			0%		
335 001	-	500 000			1%	of the excess over	335 000
500 001	-	750 000	1 650	+	2%	of the excess over	500 000
750 001	-	1 000 000	6 650	+	3%	of the excess over	750 000

DIVIDENDS TAX

Rate of Dividends tax on dividends declared and paid -	Rate
On or after 1 April 2012	15%
On or after 22 February 2017	20%

TRUSTS

The tax rate on trusts (other than special trusts which are taxed at rates applicable to individuals) increase to 45% (41%).

OTHER TAXES

ESTATE DUTY

Rate of estate duty on the dutiable amount of an estate	
Death prior to 14 March 1996	15%
Death between 15 March 1996 and 30 September 2001	25%
Death or after 1 October 2001	20%
Primary abatement	R3 500 000 (R3 500 000) plus unused portion of the primary abatement of a pre-deceased spouse

DONATIONS TAX

Payable at a flat rate on the value of property donated by a resident	
Prior to 14 March 1996	15%
Between 15 March 1996 and 30 September 2007	25%
On or after 1 October 2007	20%
Annual exemption for natural persons	R100 000

CAPITAL GAINS TAX (CGT)

The effective CGT rates for disposal of assets in years of assessment commencing on or after 1 March 2017

Taxpayer	Inclusion Rate (%)	Statutory Rate (%)	Effective Rate (%)
Individuals	40	0 – 45	0 – 18
Trusts			
Special	40	18 – 45	7.2 – 18
Other	80	45	36
Companies			
Ordinary	80	28	22.4
Small business corporation	80	0 – 28	0 – 22.4
Employment company (personal service provider)	80	28	22.4
Foreign company (SA branch)	80	28	22.4
Micro-business subject to turnover tax	0	0	0
Life assurers			
Individual policyholders fund	40	30	12
Company policyholders fund	80	28	22.4
Untaxed policyholders fund	-	-	-
Corporate fund	80	28	22.4

TRANSFER DUTY

Transfer duty rates applicable to all persons on purchase agreements concluded on or after 1 March 2017							
Property value R							Rate of tax
0	-	900 000			0%		
900 001	-	1 250 000			3%	of the excess over	900 000
1 250 001	-	1 750 000	10 500	+	6%	of the excess over	1 250 000
1 750 001	-	2 250 000	40 500	+	8%	of the excess over	1 750 000
2 250 001	-	10 000 000	80 500	+	11%	of the excess over	2 250 000
10 000 001	-	and above	933 000	+	13%	of the excess over	10 000 000

Transfer duty rates applicable to all persons on purchase agreements concluded on or after 1 March 2016							
Property value R							Rate of tax
0	-	750 000			0%		
750 001	-	1 250 000			3%	of the excess over	750 000
1 250 001	-	1 750 000	15 000	+	6%	of the excess over	1 250 000
1 750 001	-	2 250 000	45 000	+	8%	of the excess over	1 750 000
2 250 001	-	10 000 000	85 000	+	11%	of the excess over	2 250 000
10 000 001	-	and above	937 500	+	13%	of the excess over	10 000 000

SECURITIES TRANSFER TAX

From 1 July 2008, STT replaced stamp duties and uncertificated securities tax on marketable securities. STT is levied at a flat rate of 0,25% on the taxable amount on any transfer of a security (listed and unlisted securities) including member's interests in close corporations.

BUDGET COMMENTARY

(Extracted from Annexure C and Chapter 4 of the National Treasury Budget Review 2017)

OVERVIEW

Economic growth is expected to remain in line with the October 2016 forecast. Tax revenue collections, however, have underperformed. Robust revenue collection depends on strong economic growth and effective tax administration. Tax revenues are estimated to grow by 7 per cent in 2016/17, compared with 9.8 per cent projected in the 2016 Budget. To maintain existing spending programmes, government proposes to raise tax rates, primarily at the upper end of the income spectrum, strengthening the progressive nature of the tax system. The measures will include a new top personal income tax bracket, a higher dividend withholding tax rate, and increases in fuel taxes and alcohol and tobacco excise duties. Government remains committed to maintaining a stable and transparent tax system.

The 2016 Budget estimated that government would receive total tax revenue of R1.175 trillion during 2016/17. The October 2016 Medium Term Budget Policy Statement (MTBPS) noted that revenue collection would fall well below estimates. The MTBPS projected a revenue shortfall of R22.8 billion, which is now revised to R30.4 billion, meaning an estimated R1.144 trillion will be collected. This is the largest tax revenue shortfall relative to budgeted estimates since 2009/10.

Projections have fallen short in three of the four main tax instruments. Personal income tax, value-added tax (VAT) and customs duties are down by an estimated R15.2 billion, R11.3 billion and R6.5 billion respectively relative to the 2016 Budget estimate. Lower wage increases and bonuses reduced personal income tax collection. The decline in import VAT has been partially offset by strong domestic VAT collection, but VAT refunds have been higher than anticipated, reducing net revenue. Corporate income tax collection is expected to exceed 2016 Budget estimates.

Tax collection projections are based on economic growth forecasts, the effectiveness of the tax administration in closing the compliance gap and tax policy changes. A protracted period of low economic growth has negatively affected job creation and tax bases. Although economic growth for 2016/17 remains in line with previous estimates, decreased imports and slower wage growth have contributed to lower revenues.

To ensure that the state has adequate resources to fund existing spending programmes, government proposes to raise tax rates for 2017/18. Raising taxes when the economy is struggling is undesirable, but unavoidable, given the current fiscal circumstances. Government is acutely aware of the difficult economic conditions facing the majority of South Africans, but deferring tax increases by accumulating more public debt would ultimately impose a greater burden on citizens. The main tax proposals are:

- A new top personal income tax bracket of 45 per cent for taxable incomes above R1.5 million.
- Limited relief for bracket creep.
- An increase in the dividend withholding tax rate to 20 per cent.
- A 30c/litre increase in the general fuel levy and a 9c/litre increase in the Road Accident Fund (RAF) fuel levy.

ECONOMIC GROWTH

In 2016/17, for the first time since 2009/10, tax revenues have not kept pace with economic growth. There is uncertainty regarding the path of revenue collection. Risks include weaker-than-expected economic growth, and concerns about tax morality, compliance and administration. Deterioration in any of these areas can hinder tax collection.

An efficient and trustworthy tax administration is one of South Africa's institutional strengths. The South African Revenue Service (SARS) has played an integral role in building the democratic state by ensuring that expected levels of revenue are available to fund spending programmes. SARS will continue to develop the skills and capacity needed to enforce legislation. It will strengthen its efforts to curb tax avoidance and evasion, and address transfer pricing – a component of illicit financial flows.

South Africa's democracy depends on the strength of its social compact. The payment of taxes is a legal obligation, but the effectiveness of the tax system relies to a large extent on the willingness of citizens to contribute. This cannot be taken for granted given rising public concerns about corruption, wastage of public funds and inefficiencies in service delivery. A marked decline in the culture of tax morality would have negative effects on the public finances and be exceptionally hard to reverse.

REDISTRIBUTION AND SOLIDARITY

Government is committed to maintaining a progressive, stable and transparent tax structure. Two foundational principles of the tax system are equity and efficiency. Equity means that all residents with the same level of income should pay the same in tax, and that residents

should contribute to the fiscus in proportion to their income level. Efficiency means raising revenue in a manner that does not deter economic growth, investment and job creation. Some tax instruments are progressive and promote equity; others are regressive, but more efficient.

REVENUE COLLECTION

In 2016/17, for the first time since 2009/10, tax revenues have not grown as fast as the economy.

Tax buoyancy describes the relationship between gross tax revenue collections and economic growth, including the revenue effects of policy changes. A value above one means that revenues are growing faster than the economy; below one means they fall below the rate of GDP growth. Although buoyancy fell below the rate of economic growth in the 2000s, this coincided with substantial tax relief. Tax buoyancy is expected to fall below one for 2016/17, even after tax measures proposed in the 2016 Budget raised an estimated R18 billion.

Budget estimates and revenue outcomes

	2015/16			2016/17			%
R million	**Budget**	**Outcome**	**Deviation**	**Budget**	**Revised**	**Deviation**	**change[2]**
Taxes on income and profits	**608 654**	**606 821**	**-1 833**	**668 387**	**660 586**	**-7 801**	**8.9%**
Personal income tax	392 000	388 102	-3 898	441 040	425 810	-15 230	9.7%
Corporate income tax	189 000	191 152	2 152	198 293	205 090	6 797	7.3%
Dividend witholding tax	23 650	23 934	284	25 031	25 710	679	7.4%
Interest witholding tax	216	219	2	218	450	232	105.9%
Other taxes on income and profits[3]	3 787	3 414	- 374	3 804	3 526	- 278	3.3%
Skills development levy	**15 800**	**15 220**	**- 580**	**17 640**	**15 462**	**-2 177**	**1.6%**
Taxes on property	**14 762**	**15 044**	**282**	**15 455**	**16 043**	**588**	**6.6%**
Domestic taxes on goods	**383 995**	**385 956**	**1 961**	**418 771**	**403 909**	**-14 862**	**4.7%**
Value-added tax	278 060	281 111	3 051	301 260	290 000	-11 260	3.2%
Specific excise duties	35 100	35 077	- 23	38 000	35 700	-2 300	1.8%
Ad valorem excise duties	3 037	3 014	- 23	3 276	3 385	109	12.3%
General fuel levy	56 700	55 607	-1 093	64 495	62 970	-1 525	13.2%
Other domestic taxes on goods and services[4]	11 098	11 146	49	11 739	11 854	114	6.3%
Taxes on international trade and transactions	**46 490**	**46 942**	**453**	**54 536**	**48 384**	**-6 152**	**3.1%**
Customs duties	46 000	46 250	250	54 043	47 500	-6 543	2.7%
Diamond export levy	120	127	7	122	142	20	12.2%
Miscellaneous customs and excise receipts	369	565	196	371	741	370	31.1%
Gross tax revenue	**1 069 700**	**1 069 983**	**283**	**1 174 788**	**1 144 382**	**-30 406**	**7.0%**
Non-tax revenue[5]	55 841	57 274	1 929	26 657	31 957	5 300	-44.2%
of which:							
Mineral royalties	*3 460*	*3 708*	247	*4 430*	*6 272*	*1 842*	*69.2%*
Less: SACU[6] payments	-51 022	-51 022	-	-39 448	-39 448	-	-22.7%
Main budget revenue	**1 074 519**	**1 076 234**	**2 212**	**1 161 996**	**1 136 891**	**-25 105**	**5.6%**
Provinces, social security funds and selected public entities	148 545	145 731	-2 814	162 343	160 404	-1 939	10.1%
Consolidated budget revenue	**1 223 064**	**1 221 965**	**- 602**	**1 324 339**	**1 297 295**	**-27 044**	**6.2%**

1. *A more disaggregated view is presented in Tables 2 and 3 of the statistical annexure*
2. *Percentage change between outcome in 2015/16 and revised estimate in 2016/17*
3. *Includes interest on overdue income tax and small business tax amnesty levy*
4. *Includes turnover tax for small businesses, air departure tax, plastic bags levy, electricity levy, CO_2 tax on motor vehicle emissions, incandescent light bulb levy and Universal Service Fund. Revised 2016/17 also includes tyre levy and international oil pollution compensation fund*
5. *Includes mineral royalties, mining leases, departmental revenue and sales of capital assets. 2016/17 revised includes proceeds from the sale of Vodacom shares*
6. *Southern African Customs Union. Amounts made up of payments and other adjustments Source: National Treasury*

The 2016 Budget estimate for gross tax revenue in 2016/17 was R1.175 trillion. The revenue shortfall is estimated to be R30.4 billion. The underperformance in tax revenues is largely due to weakening wage income and imports, both of which form a substantial part of the overall.

Budget revenue

R million	2013/14	2014/15	2015/16	2016/17	2017/18	2018/19	2019/20
		Outcome		Revised		Medium-term estimates	
Taxes on income and profits[2]	507 759	561 790	606 821	660 586	739 153	801 337	877 846
of which:							
Personal income tax	*309 834*	*352 950*	*388 102*	*425 810*	*482 086*	*527 299*	*581 934*
Corporate income tax	*177 324*	*184 925*	*191 152*	*205 090*	*218 692*	*233 023*	*251 660*
Skills development levy	12 476	14 032	15 220	15 462	16 641	17 968	19 454
Taxes on property	10 487	12 472	15 044	16 043	16 509	17 909	19 344
Domestic taxes on goods and services	324 548	356 554	385 956	403 909	439 539	473 152	509 487
of which:							
VAT	*237 667*	*261 295*	*281 111*	*290 000*	*312 750*	*337 714*	*364 671*
Taxes on international trade and transactions	44 732	41 463	46 942	48 384	53 647	59 034	65 090
Revenue measures - 2018 Budget	-	-	-	-	-	15 000	16 331
Gross tax revenue	**900 015**	**986 295**	**1 069 983**	**1 144 382**	**1 265 488**	**1 384 399**	**1 507 553**
Non-tax revenue[3]	30 726	30 900	57 274	31 957	32 880	29 053	28 489
of which:							
Mineral and petroleum	*6 439*	*5 422*	*3 708*	*6 272*	*6 688*	*7 127*	*7 697*
Less: SACU[4] payments	-43 374	-51 738	-51 022	-39 448	-55 951	-62 421	-64 527
Main budget revenue	**887 366**	**965 457**	**1 076 234**	**1 136 891**	**1 242 417**	**1 351 031**	**1 471 514**
Provinces, social security funds and selected public entities	120 685	133 409	145 731	160 404	171 684	184 198	197 016
Consolidated budget revenue	**1 008 051**	**1 098 866**	**1 221 965**	**1 297 295**	**1 414 101**	**1 535 229**	**1 668 531**
As percentage of GDP							
Tax revenue	*24.8%*	*25.5%*	*26.2%*	*26.0%*	*26.7%*	*27.0%*	*27.2%*
Main budget revenue	*24.5%*	*25.0%*	*26.3%*	*25.8%*	*26.2%*	*26.3%*	*26.5%*
GDP (R billion)	*3 624.3*	*3 863.1*	*4 086.8*	*4 409.8*	*4 741.2*	*5 129.2*	*5 545.5*
Tax buoyancy	*1.17*	*1.46*	*1.47*	*0.88*	*1.41*	*1.15*	*1.10*

1. *A more disaggregated view is presented in Tables 2 and 3 of the statistical annexure*
2. *Includes secondary tax on companies/dividend and interest withholding tax, interest on overdue income tax and small business tax amnesty levy*
3. *Includes mineral royalties, mining leases, departmental revenue and sales of capital assets*
4. *Southern African Customs Union. Amounts made up of payments and other adjustments. 2017/18 figures are preliminary Source: National Treasury and SARS*

TAX EXPENDITURE

Tax expenditures are estimates of tax revenue that government forgoes as a result of legislative provisions that deviate from standard tax treatment. This includes deductions, exemptions and rebates. Transparent reporting of tax expenditures is international best practice and encourages accountability. This annexure presents government's estimates of the fiscal cost of tax expenditures, and the methodology used to produce these estimates.

Government estimates that tax expenditures in 2014/15 – the latest year for which data is available – amounted to R139.1 billion, equivalent to 3.6 per cent of GDP. The four largest tax expenditures were deductions for pension and retirement annuity contributions, credits for medical contributions and qualifying expenses, value-added tax (VAT) relief for basic food items, and car manufacturer incentives.

Tax expenditures can advance specific policy goals. Tax incentives, for example, provide favourable tax treatment to individuals and businesses to encourage certain behaviour. Well-targeted incentives can promote investment and growth, but they also erode the tax base. Recent work by the International Monetary Fund, the Organisation for Economic Cooperation and Development, the United Nations and the World Bank shows that investors do not consider tax incentives to be a decisive factor when considering investments in developing countries. Incentives were often found to be redundant, meaning that investment would have taken place without them. This suggests that even well designed incentives may not be an effective way to address underlying problems that are not tax related. Tax expenditures can also undermine the principles of equity and simplicity, given that they target specific taxpayers and often require complicated rules to prevent abuse.

Spending decisions presented in the Budget are subject to extensive scrutiny and democratic oversight. In many jurisdictions, tax expenditures are subject to fewer controls and reviews. Good governance and regular, transparent evaluations are necessary to justify the

existence and continuation of incentives.

Personal income tax expenditures

Tax expenditures for personal income taxes are intended to promote savings for retirement, help individuals manage large and unexpected medical expenses, and provide relief for the elderly. Retirement fund, medical tax credit, and secondary and tertiary rebate tax expenditures are estimated based on anonymised individual tax returns. To estimate the tax expenditure, the relevant marginal tax based on SARS data by calculating the expected tax liability with and without each particular rebate.

The tax expenditure for retirement fund contributions should be interpreted with care, as the estimate represents only the reduction in tax liabilities in the tax year in which the contributions were made, and ignores that tax is paid on income received in retirement.

Corporate income tax expenditures

Government uses corporate income tax expenditures to promote small businesses development, stimulate investment and encourage job creation. Generally, corporate income tax expenditure estimates are calculated by multiplying the relevant tax measure by the headline corporate income tax rate (currently 28 per cent).

VAT expenditures

Concessions on taxpayers' VAT liability provide relief to low-income households and ease the administrative burden on specific economic sectors. The zero-rating of 19 basic food items assists low income households that spend a higher proportion of income on these items. Tax-exempt food items include brown bread, rice, milk, eggs, vegetables and samp. The tax expenditure on these basic food products represents a revenue loss that is calculated by applying 14 per cent on the estimated household spending on these items. Tax-exempt supplies include public road and rail transport, and educational services provided by
approved institutions.

VAT relief on fuel sales

Petrol, diesel and illuminating paraffin are zero rated for VAT. The difference to the standard rate is recorded as tax expenditure when these items are sold to final consumers. The main assumption used to calculate this item is that 20 per cent of petrol sales and 90 per cent of diesel sales were for business purposes (by VAT vendors) and would have qualified as an input VAT claim.

Customs duties and excise expenditures

Customs and excise expenditures aim to promote industrial development in the motor vehicle and textiles and clothing sectors. Expenditure reported in this category represents revenue lost on customs duties rebates on industry development programmes and excise duty refunds on diesel used in primary sectors of the economy.

Tax expenditure estimates

R million	2011/12	2012/13	2013/14	2014/15
Personal income tax				
Pension and retirement annuity contributions[1]	23 346	26 038	27 773	25 915
Pension contributions – employees	*8 728*	*9 598*	*10 236*	*9 571*
Pension contributions – employers	*9 980*	*10 975*	*11 705*	*10 944*
Retirement annuity	*4 639*	*5 464*	*5 832*	*5 399*
Medical	16 413	19 887	21 297	18 493
Medical contributions & deductions	*16 413*	*3 849*	*4 284*	–
Medical tax credits [2]	–	*16 038*	*17 013*	*18 493*
Interest exemptions	1 939	1 965	2 160	2 106
Secondary rebate (65 years and older)	1 891	2 035	2 256	2 522
Tertiary rebate (75 years and older)	165	155	177	203
Donations	528	632	879	931
Capital gains tax (annual exclusion)	147	305	381	414
Total personal income tax	**44 429**	**51 018**	**54 923**	**50 584**
Corporate income tax[3]				
Small business corporation tax savings	1 561	1 953	2 515	2 294
Reduced headline rate	*1 539*	*1 926*	*2 484*	*2 266*
Section 12E depreciation allowance	*22*	*27*	*31*	*28*
Research and development	361	340	163	34
Learnership allowances	825	815	774	320
Strategic industrial projects[4]	130	169	438	7
Film incentive	228	353	13	1
Urban development zones	300	240	157	115
Employment tax incentive[5]	–	–	143	2 420

Total corporate income tax	**3 404**	**3 869**	**4 204**	**5 192**
Value-added tax				
Zero-rated supplies	40 763	46 139	49 611	51 123
19 basic food items [6]	*17 106*	*18 628*	*20 107*	*21 503*
Petrol [7]	*13 797*	*15 343*	*16 276*	*16 065*
Diesel [7]	*1 532*	*1 759*	*2 101*	*2 146*
Paraffin [7]	*585*	*611*	*702*	*659*
Municipal property rates	*7 568*	*9 598*	*10 209*	*10 522*
Reduced inclusion rate for commercial accommodation	*174*	*199*	*216*	*228*
Exempt supplies (public transport and education)	999	1 088	1 175	1 256
Total value-added tax	**41 763**	**47 228**	**50 786**	**52 379**
Customs duties and excise				
Motor vehicles (MIDP/APDP, including IRCCs)[8]	16 306	15 823	18 415	23 467
Textile and clothing (duty credits – DCCs)[8]	860	652	468	539
Furniture and fixtures	150	163	156	180
Other customs[9]	847	678	665	911
Diesel refund[10]	1 756	3 276	4 955	5 870
Total customs and excise	**19 919**	**20 592**	**24 659**	**30 967**
Total tax expenditure	**109 514**	**122 706**	**134 573**	**139 122**
Tax expenditure as % of total gross tax revenue	**14.7%**	**15.1%**	**15.0%**	**14.1%**
Total gross tax revenue	**742 650**	**813 826**	**900 015**	**986 295**
Tax expenditure as % of GDP	**3.6%**	**3.7%**	**3.7%**	**3.6%**

TAX PROPOSALS

SUMMARY OF THE MAIN TAX PROPOSALS

The 2017 tax proposals are projected to raise R28 billion, and increase the tax burden from 26 per cent of GDP in 2016/17 to 26.7 per cent in 2017/18. The new top marginal income tax bracket for individuals combined with partial relief for bracket creep is expected to contribute R16.5 billion, with R6.8 billion coming from the increased dividend withholding tax rate.

Bracket creep occurs when personal income tax tables are not fully adjusted for inflation, so that inflationary salary adjustments increase the effective tax rate, reducing real income. If no adjustments were made to the personal income tax tables in 2017/18, this would amount to an estimated R14.6 billion in additional revenue. The bracket creep adjustment for 2017/18 amounts to R2.5 billion in relief, leaving R12.1 billion as additional revenue.

Impact of tax proposals on 2017/18 revenue

R million	Effect of tax proposals	
Gross tax revenue (before tax proposals)		**1 237 464**
Budget 2017/18 proposals		**28 024**
Taxes on individuals and companies		
Personal income tax	**16 516**	
Revenue from not fully adjusting for inflation	12 148	
Revenue if no adjustment is made	*14 628*	
Bracket creep adjustment	*-2 480*	
New top marginal income tax bracket	4 369	
Dividend withholding tax	**6 822**	
Increase in dividend withholding tax rate	6 822	
Taxes on property	**-448**	
Transfer duty decrease	-448	
Indirect taxes	**5 133**	
Increase in general fuel levy	3 197	
Increase in excise duties on tobacco products	656	
Increase in excise duties on alcoholic beverages	1 280	
Gross tax revenue (after tax proposals)		**1 265 488**

In previous budget documentation, estimated revenue changes resulting from personal income tax, fuel levy and excise duty proposals were compared with no adjustment for inflation. These changes are now compared with full adjustment.

Source: National Treasury

PERSONAL INCOME TAX

Government proposes a new top personal income tax bracket of 45 per cent for taxable incomes above R1.5 million per year. The previous top bracket of 41 per cent was set at R701 301. The primary, secondary and tertiary rebates, and the levels of all the taxable income brackets, will be increased by 1 per cent from 1 March 2017. The tax-free threshold will increase from R75 000 to R75 750. However, since the increase is below the expected level of inflation, taxpayers will face a real increase in the effective personal income tax rate in 2017/18. This also requires a four-percentage point increase in the tax rate for trusts.

In combination, amendments to the personal income tax tables are expected to provide additional revenues of R16.5 billion. The budget proposals increase the proportion of tax paid by those earning R1.5 million and above from 25.5 per cent to 26.3 per cent, strengthening the progressivity of the personal income tax system.

Estimates of individual taxpayers and taxable income, 2017/18

Taxable bracket	Registered individuals		Taxable income		Income tax payable before relief		Income tax relief		Income tax from new top rate		Income tax payable after proposals	
	Number	%	R billion	%	R billion	%	R billion	%	R billion	%	R billion	%
R0 - R70 000[1]	6 582 884	-	159.8	0.0	–	0.0	0.0	0.0	–	0.0	–	0.0
R70 001 - R150 000	2 602 653	35.1	274.4	11.9	12.5	2.6	-0.3	13.5	0.0	0.0	12.1	2.5
R150 001 - R250 000	1 813 517	24.5	355.6	15.4	35.6	7.4	-0.4	16.6	0.0	0.0	35.2	7.3

R250 001 - R350 000	1 077 915	14.5	315.1	13.7	46.9	9.8	-0.4	15.9	0.0	0.0	46.5	9.6
R350 001 - R500 000	906 151	12.2	365.1	15.8	70.6	14.7	-0.5	19.5	0.0	0.0	70.1	14.5
R500 001 - R750 000	527 288	7.1	310.4	13.5	77.3	16.1	-0.4	16.1	0.0	0.0	76.9	16.0
R750 001 - R1 000 000	227 561	3.1	189.6	8.2	56.0	11.7	-0.2	8.7	0.0	0.0	55.8	11.6
R1 000 001 - R1 500 000	152 604	2.1	178.4	7.7	58.9	12.3	-0.1	5.8	0.0	0.0	58.7	12.2
R1 500 001+	103 353	1.4	319.0	13.8	122.6	25.5	-0.1	3.9	4.4	100.0	126.9	26.3
Total	**7 411 042**	**100.0**	**2 308**	**100.0**	**480.2**	**100.0**	**-2.5**	**100.0**	**4.4**	**100.0**	**482.1**	**100.0**
Grand total	**13 993 926**		**2 467**		**480.2**		**-2.5**		**4.4**		**482.1**	

Annual income tax payable and average tax rates, 2017/18 (taxpayers below 65)

Taxable income (R)	2016/17 rates (R)	Proposed 2017/18 rates (R)	Tax change (R)	% change	Average tax rates	
					Old rates	New rates
85 000	1 800	1 665	-135	-7.5%	2.1%	2.0%
90 000	2 700	2 565	-135	-5.0%	3.0%	2.9%
100 000	4 500	4 365	-135	-3.0%	4.5%	4.4%
120 000	8 100	7 965	-135	-1.7%	6.8%	6.6%
150 000	13 500	13 365	-135	-1.0%	9.0%	8.9%
200 000	23 460	23 174	-285	-1.2%	11.7%	11.6%
250 000	36 460	36 174	-285	-0.8%	14.6%	14.5%
300 000	49 780	49 347	-432	-0.9%	16.6%	16.4%
400 000	80 780	80 347	-432	-0.5%	20.2%	20.1%
500 000	116 460	115 824	-635	-0.5%	23.3%	23.2%
750 000	213 431	212 490	-941	-0.4%	28.5%	28.3%
1 000 000	315 931	314 990	-941	-0.3%	31.6%	31.5%
1 500 000	520 931	519 990	-941	-0.2%	34.7%	34.7%
2 000 000	725 931	744 990	19 059	2.6%	36.3%	37.2%

Source: National Treasury

Annual income tax payable and average tax rates, 2017/18 (taxpayers aged 65 to 74)

Taxable income (R)	2016/17 rates (R)	Proposed 2017/18 rates (R)	Tax change (R)	% change	Average tax rates	
					Old rates	New rates
120 000	693	484	-209	-30.2%	0.6%	0.4%
150 000	6 093	5 884	-209	-3.4%	4.1%	3.9%
200 000	16 053	15 693	-359	-2.2%	8.0%	7.8%
250 000	29 053	28 693	-359	-1.2%	11.6%	11.5%
300 000	42 373	41 866	-506	-1.2%	14.1%	14.0%
400 000	73 373	72 866	-506	-0.7%	18.3%	18.2%
500 000	109 053	108 343	-709	-0.7%	21.8%	21.7%
750 000	206 024	205 009	-1 015	-0.5%	27.5%	27.3%
1 000 000	308 524	307 509	-1 015	-0.3%	30.9%	30.8%
1 500 000	513 524	512 509	-1 015	-0.2%	34.2%	34.2%
2 000 000	718 524	737 509	18 985	2.6%	35.9%	36.9%

Source: National Treasury

Annual income tax payable and average tax rates, 2017/18 (taxpayers aged 75 and over)

Taxable income (R)	2016/17 rates (R)	Proposed 2017/18 rates (R)	Tax change (R)	% change	Average tax rates	
					Old rates	New rates
150 000	3 627	3 393	-234	-6.4%	2.4%	2.3%
200 000	13 587	13 203	-384	-2.8%	6.8%	6.6%
250 000	26 587	26 203	-384	-1.4%	10.6	10.5%
300 000	39 907	39 376	-531	-1.3%	13.3	13.1%
400 000	70 907	70 376	-531	-0.7%	17.7	17.6%
500 000	106 587	105 853	-734	-0.7%	21.3	21.2%
750 000	203 558	202 518	-1 039	-0.5%	27.1	27.0%
1 000 000	306 058	305 018	-1 039	-0.3%	30.6	30.5%
1 500 000	511 058	510 018	-1 039	-0.2%	34.1	34.0%
2 000 000	716 058	735 018	18 961	2.6%	35.8	36.8%

Medical scheme fees tax credit

To counter the effect of inflation, the medical tax credit will be increased for the first two beneficiaries from R286 to R303 per month, and for the remaining beneficiaries from R192 to R204 per month. Future adjustments will be balanced with the funding requirements of national health insurance.

Tax-free investments

Tax-free savings accounts were introduced on 1 March 2015 with an annual allowance of R30 000. The 2014 Budget stated that the allowance would be increased in line with inflation. Government proposes increasing the annual allowance to R33 000.

Bursaries and scholarships

The need for improved skills in the economy justifies additional support for bursaries. Currently, if an employee has an income of less than R400 000 and their employer provides a bursary to them or their relatives, the value of the bursary, up to a limit, will not be taxable in the hands of the employee. Government proposes to increase the applicable threshold and the monetary limits for bursaries. The effective date of implementation will be 1 March 2017.

Government proposes to increase the income eligibility threshold for employees from R400 000 to R600 000, and the monetary limits for bursaries from R15 000 to R20 000 for education below NQF level 7, and from R40 000 to R60 000 for qualifications at NQF level 7 and above.

Dividend withholding tax

Dividend income paid to shareholders is taxed at a rate of 15 per cent. After accounting for corporate income tax, which is paid before a distribution of dividends, the combined statutory tax rate on dividends is 38.8 per cent. Currently, South Africa’s combined statutory tax rate on dividend income falls below the OECD average.

To reduce the difference between the combined statutory tax rate on dividends and the top marginal personal income tax rate, government is increasing the dividend withholding tax rate to 20 per cent, effective 22 February 2017. The exemption and rates for inbound foreign dividends will also be adjusted in line with the new rate, effective for years of assessment commencing on or after 1 March 2017.

Withholding tax on immovable property sales

To align with the increased effective capital gains tax rate, government proposes to increase the withholding tax on immovable property sales by non-residents. Rates will be increased from 5 per cent to 7.5 per cent for individuals, 7.5 per cent to 10 per cent for companies and 10 per cent to 15 per cent for trusts.

Amending foreign employment income-tax exemption in respect of South African residents

Currently, if a South African resident works in a foreign country for more than 183 days a year, foreign employment income earned is exempt from tax, subject to certain conditions. This exemption is for employees of private-sector companies. In terms of the residence-based system of taxation, South African residents are taxed on their worldwide income. However, this exemption on foreign employment income appears excessively generous. If a resident works in a foreign country for more than 183 days with no tax payable in the foreign country, that foreign employment income will benefit from double non-taxation. It is proposed that this exemption be adjusted so that foreign employment income will only be exempt from tax if it is subject to tax in the foreign country.

TRUSTS

Refining measures to prevent tax avoidance through the use of trusts

In 2016, an anti-avoidance measure aimed at curbing the tax-free transfer of wealth to trusts through the use of low-interest or interest-free loans was introduced in the Income Tax Act (1962). This anti-avoidance measure deems any interest foregone in respect of low-interest or interest-free loans to a trust to be donations that are subject to donations tax at a rate of 20 per cent. However, some taxpayers have already attempted to circumvent the anti-avoidance measure by making low-interest or interest-free loans to companies owned by a trust. To counter abuse, it is proposed that the scope of this anti-avoidance measure be extended to cover these avoidance schemes. In addition, it is proposed that the anti-avoidance rule should not apply to trusts that are not used for estate planning, for example, employee share scheme trusts and certain trading trusts.

Corporate income tax revenue moves in line with the overall economy. Improving economic growth should result in a higher contribution from this tax. South Africa's corporate income tax rate of 28 per cent is higher than the Organisation for Economic Cooperation and Development (OECD) average of 25 per cent, leaving the fiscus vulnerable to base erosion and profit shifting – a term describing the channels used by multinational corporations to shift their reporting of income to low-tax countries. Corporate tax revenue can be increased by broadening the tax base. This can involve removing tax incentives, and introducing measures to curb tax avoidance through loopholes and schemes.

Clarifying the rules relating to the taxation of employee share-based schemes

In 2016, amendments were made to the Income Tax Act to introduce anti-avoidance measures dealing with schemes where restricted shares are allocated to employees through employee share-based incentive schemes. The shares are then liquidated in return for an amount qualifying as a dividend. However, the 2016 changes did not fully address the interaction between section 8C and the provisions of the Eighth Schedule that exclude gains arising from the vesting or disposal of a restricted equity instrument from capital gains tax. It is proposed that the interaction be clarified.

Tax implications of debt forgone

Alignment of the tax treatment of debt forgone for mining companies: Mining companies have a special tax regime in section 36 of the Income Tax Act that requires them to account for their capital expenditure differently from other companies. The current relief provided in paragraph 12A of the Eighth Schedule to the Income Tax Act, allowing a debtor to reduce the base cost of the allowance asset with the amount of a debt that is cancelled, waived, forgiven or discharged, does not apply to mining companies. As a result, mining companies are required to recoup debt that is cancelled, waived, forgiven or discharged without reducing their tax-deductible capital expenditure. To address this disparity, it is proposed that the tax treatment of debt forgone for mining companies be aligned with the tax treatment applied to companies in other sectors.

Alignment of the tax treatment of debt forgone for dormant group companies or companies under business rescue: Paragraph 12A of the Eighth Schedule to the Income Tax Act provides relief in respect of debt that is cancelled, waived, forgiven or discharged in respect of loans between companies within the same group. However, the intra-group relief does not extend to section 19 of the Income Tax Act dealing with debt used to finance tax-deductible operating expenditure. As a result, companies that used intra-group debt to finance tax-deductible operating expenses are required to recoup the debt. In the case of dormant group companies or companies under business rescue, not having this relief is cumbersome as such companies would not have the resources to pay tax on the debt recouped. It is proposed that the current relief for group companies available in paragraph 12A of the Eighth Schedule be extended to section 19.

Debt settled for consideration other than cash: In the current economic climate, debtors may make compromises with their creditors. This could include the issuing of shares where the issue price of the shares reflects the face value of the debt. It is proposed that the conversion of debt into equity be allowed. However, provision will be made to recoup capitalised interest on the debt in respect of which an interest deduction was previously claimed.

Addressing the circumvention of anti-avoidance rules

Addressing the abuse of disguised sale of shares using share buybacks: In the 2016 Budget Review, tax avoidance schemes involving share buybacks were highlighted for review. Such schemes involve a company buying back shares from its current shareholders to avoid the tax consequences of share disposals. The seller receives payment in the form of a dividend that may be exempt from normal tax and dividends tax, instead of paying tax on the sale of shares. Following the announcement in 2016, no specific countermeasures were introduced. It is therefore proposed that specific countermeasures be introduced to curb the use of share buyback schemes.

Addressing the abuse of artificial repayment of debt: Since the introduction of the current tax rules for debt forgiveness, it has come to government's attention that creditors and debtors are entering into short-term shareholding structures that attempt to circumvent income tax resulting from a recoupment triggered by the debt forgiveness rules. To achieve this, a creditor will subscribe for shares in its debtor and pay the debtor for those shares. The debtor will in turn use the subscription amount paid to settle its debt with the creditor. Soon after the payment is effected, the original shareholder of the debtor will buy the shares that the creditor subscribed for at a slight premium. This slight premium will cover the capital gains tax that the creditor will be liable for in respect of the shares in the debtor sold to the shareholder. This means the fiscus loses normal tax revenue on the recoupment and only receives the lower capital gains tax. It is proposed that measures be introduced to prevent these structures.

Interaction between the "in duplum" rule and the statutory tax legislation: The in duplum rule aims to protect debtors by limiting the amount of the total interest a creditor can charge. The effect of the rule is that interest on a debt ceases to accrue where the total amount of the interest equals

the outstanding principal debt. Various anti-avoidance provisions in the Income Tax Act may be undermined should the in duplum rule apply. Some taxpayers may be relying on this rule to distort the quantification of the tax benefit derived from low-interest or interest-free loans. These taxpayers aim to avoid income tax determined on the difference between the amount of interest actually incurred and the amount of interest that would have been incurred at the official rate. It is proposed that the tax rules dealing with low-interest or interest-free loans be amended to explicitly exclude the application of the in duplum rule to ensure their efficacy.

Addressing circumvention of dividend-stripping rules: The Income Tax Act has rules that target dividend- stripping avoidance schemes. If a company borrows money from a party it is selling shares to and the company declares a dividend that is tax-free before the sale of the shares, such dividends are subject to income tax or capital gains tax in the hands of the seller. For these anti-avoidance rules to apply, the debt funding for the shares must be provided by the purchaser or be guaranteed by any connected person in relation to the purchaser. Government has identified schemes whereby loans for the purchase of the shares are raised from another party, such as a loan from a bank. It is proposed that additional measures be introduced to curb circumvention of dividend-stripping rules.

Changes to the definition of contributed tax capital: The definition of "contributed tax capital" was introduced in the Income Tax Act in 2008, when the Companies Act came into effect. It is a notional amount derived from contributions made to a company by shareholders in respect of a certain class of shares. It is reduced by any capital that is subsequently transferred by the company to one or more of the shareholders and is commonly known as a capital distribution. Government has identified a mechanism whereby companies with foreign parents increase their contributed tax capital, thus arguably avoiding the payment of dividends tax through capital distributions. These capital distributions are not subject to capital gains tax in the hands of the foreign parent if the underlying investment is not in immovable property in South Africa. It is proposed that amendments be made in the tax legislation to prevent the abuse of the definition of contributed tax capital.

Corporate reorganisation rules

Tax implication on the assumption of contingent debt: The Income Tax Act provides for the tax-free transfer of assets for corporate restructuring purposes, subject to certain limitations on how the transfer is funded. The only acceptable means of funding the transfer of assets is by obtaining shares in the buyer of assets or the buyer assuming the debts of the seller. Cash or other assets are not acceptable. With respect to debt, only unconditional obligations are currently catered for. However, a seller and buyer may negotiate a selling price after considering and taking into account some of the future contingent liabilities of the seller. Where the parties agree that the buyer will assume some of the future contingent liabilities of the seller, there is a real economic effect on the sale as the seller will be freed from future costs relating to those contingent liabilities. It is proposed that the assumption of future contingent liabilities be considered as an acceptable consideration under the corporate reorganisation rules.

Interplay between real estate investment trusts (REITs) and corporate reorganisation rules: Section 25BB of the Income Tax Act stipulates that REITs are not entitled to claim certain capital allowances. This is because REITs are subject to a special tax dispensation that allows them to deduct their shareholder distributions against rental income as the shareholders bear the tax liability. The REIT is precluded from claiming allowances on its assets, which means that an anomaly arises when a REIT is party to a reorganisation transaction, because its assets would not qualify as allowance assets. This anomaly means the rules on reorganisation do not apply to transactions involving REITs. It is proposed that the legislation be amended to make provision for corporate reorganisation rules to apply to transactions involving REITs.

Extension of collateral and securities lending arrangement provisions

Government has been gradually introducing measures to address concerns about the limited scope of tax relief provisions dealing with collateral and securities lending arrangements. In 2016, legislative changes were made to include listed government bonds as allowable instruments for securities lending and collateral arrangements. In light of the ongoing review, it is proposed that changes be made to extend the current provisions of collateral and securities lending arrangements to include listed foreign government bonds.

Amendments to third-party backed shares provisions

Currently, all dividends arising directly or indirectly from transactions and arrangements involving preference shares guaranteed by third parties are deemed ordinary revenue, subject to "qualifying purpose" exemptions, to which the anti-avoidance rules do not apply. The qualifying purpose exemptions are too narrow, and may impede legitimate transactions. It is proposed that the current exemption on third-party backed shares with regard to asset-backed securities be further refined to cover all qualifying purposes.

RETIREMENT REFORMS

Preservation of benefits after reaching normal retirement dates: In 2014, amendments were made to the Income Tax Act to allow individuals to elect to retire, and the date on which the lump sum benefit accrued to the individual depended on the date on which the individual elected to

retire and not on the normal retirement age. Currently, once the individual elects to retire, the Income Tax Act does not cater for the transfer of lump sum benefits from one retirement fund to another. It is proposed that transfers of retirement interests be allowed from a retirement fund to a retirement annuity fund, subject to fund rules.

Tax-exempt status of pre-March 1998 build-up in public-sector funds: Currently, the Income Tax Act makes provision for the tax-free transfer of pre-March 1998 lump sum benefits from a public-sector fund to a pension fund. It is proposed that subsequent transfers of these lump sum benefits to another pension fund be tax free.

Removing time limit to join an employer umbrella fund: Existing employees who do not join a newly established employer umbrella fund have 12 months within which to join the fund, after which they are unable to join. To encourage employees to contribute towards their retirement and remove practical difficulties, it is proposed that the 12-month limit be removed and that employees be allowed to join without time restriction, subject to the rules of the fund.

TAX INCENTIVES

Government is re-evaluating existing items that narrow the corporate tax base, including tax incentives and deductions for excessive debt financing. Tax incentives provide favourable treatment to encourage investment, with costs borne by the public. However, a healthy business environment, and political and policy certainty, have a much greater influence on investment decisions. Reviews of tax incentives should regularly assess their effect on investment, job creation and growth. Where the costs outweigh the benefits, consideration should be given to removing these incentives.

Government reviewed the urban development zone tax incentive in 2012, and the learnership and employment tax incentives in 2016. Reports on the latter two were published on the National Treasury website.

The learnership tax incentive supports training and skills development. It has been revised to provide more support for scarce skills, particularly for artisans, and extended until 2022.

Between 1 January 2014 and 31 January 2017, more than 50 000 firms took up the employment tax incentive. The incentive has had modest positive effects on the growth of youth employment in participating firms, and no notable negative outcomes. The incentive has been extended until 2019 to allow for further evaluation.

The tax incentive for qualifying industrial policy projects comes to an end this year. Government will review the programme before taking a decision on its future.

Over the medium term, government will continue to work on a sustainable method of funding higher education

VALUE ADDED TAX

Expanding the VAT base

Government will look to expand the VAT base in 2018/19. It is proposed that the zero-rating on fuel be removed. This will be subject to consultation leading up to the 2018 Budget. To mitigate the effect on transport costs, government will consider combining this with either a freeze or a decrease in the fuel levy.

To address base erosion and profit shifting, businesses providing foreign electronic services to South African consumers have been required to register for VAT since 1 June 2014. In line with the 2015 Budget announcement, the regulations are being updated to broaden the scope of electronic services that are subject to VAT and to remove some uncertainties and practical difficulties. Taxable services will now include cloud computing and services provided using online applications.

The proposed changes will be published for public comment during 2017.

Clarifying the VAT treatment on leasehold improvements

The VAT Act (1991) does not currently provide guidelines in respect of the VAT treatment of leasehold improvements effected by the lessee to the leasehold property during the period of a lease agreement. It is proposed that amendments be made to the act to clarify the VAT treatment in respect of the time and value of supply of leasehold improvements on leasehold property.

VAT vendor status of municipalities

The local government elections of 3 August 2016 have led to the disestablishment or merger of certain municipalities. As a result, the affected

municipalities had to either cancel their VAT registrations or apply for new VAT registrations. It is proposed that transitional measures be provided to address this.

Amending the definition of "resident of the republic" for VAT purposes

The VAT Act contains a definition of "resident of the republic" for VAT on cross-border supplies based on the definition of "resident" in the Income Tax Act. However, if a foreign company is effectively managed from South Africa, it will be regarded as a resident of South Africa. This implies that goods or services supplied by a South African company to the foreign company will be subject to VAT and no zero- rating provisions are applicable. If the foreign company is not required to register for VAT but bears South African VAT because it is a resident, the VAT that is borne will become a business cost, as that company cannot deduct that VAT as input tax. The definition of "resident in the republic" in the VAT Act will be amended to provide for such situations.

Repealing the 2011 amendment dealing with the value to be placed on inter-warehouse sales

If goods are imported into South Africa and entered for home consumption, the goods are subject to VAT. The VAT is calculated by taking into account the value for customs duty purposes, plus any customs duty levied thereon, plus 10 per cent of the value of the goods. However, when goods are imported into the country and entered for storage in a licenced warehouse, but have not been entered for home consumption, and such goods are then sold from one warehouse to another, the value to be placed on such goods is the higher of the above calculation, or the actual amount in money paid, or the open market value of the goods. This was determined in terms of a 2011 amendment to the VAT Act. Prior to 2011, the value was deemed to be the lower of these amounts. The 2011 amendment was never implemented due to administrative and compliance complexities and it is proposed that it should be repealed with retrospective effect.

Postponing the 2015 amendment dealing with the VAT treatment of the national housing programme

In 2015, amendments were made to the VAT Act to abolish the zero rating of the supply of goods and services for government's national housing programme, with effect from 1 April 2017. However, both the National Treasury and municipalities are not ready to make the VAT amendments. It is proposed that the effective date for this amendment be postponed for two years.

Clarifying the zero rating of international travel insurance

It is proposed that the zero-rating provision pertaining to international travel be clarified, including, for example, while the traveller is still in the country of departure, while the traveller is still being transported to or from the original point of departure in South Africa, and while the traveller is not actually travelling, but is in a hotel room.

Clarifying the VAT treatment of services supplied in connection with particular movable property situated in an export country

The term "movable property" is not defined in the VAT Act. In terms of the Companies Act, movable property includes securities or shares. Securities or shares in a foreign incorporated company that is listed on the JSE could be interpreted to mean movable property that is situated in an export country. The VAT Act makes provision for the zero rating of services (fees charged) that are supplied directly in connection with movable property that is situated in an export country at the time the services are rendered. This implies that services supplied relating to securities or shares in a foreign incorporated company listed on the JSE should be subject to zero-rated VAT. It is proposed that changes be made to the VAT Act to clarify the tax treatment of these services.

TRANSFER DUTY

To provide relief for lower- and middle-income households, government proposes to raise the duty-free threshold on purchases of residential property from R750 000 to R900 000, effective 1 March 2017.

TAX ON SUGAR-SWEETENED BEVERAGES

Government proposes to implement a tax on sugary beverages, as soon as the necessary legislation is approved by Parliament and signed by the President. The tax will be administered through the Customs and Excise Act (1964). The National Treasury's preliminary socioeconomic impact assessment shows a relatively small effect on job losses, most of which can be prevented if companies reformulate their products.

Over the past year, the National Treasury published a draft policy paper and consulted with industry associations and other interested parties on the tax. Following this process, the design of the tax has been revised:

- A broader World Health Organisation definition will be applied to cover both intrinsic and added sugars in sugary beverages.
- The sugar content will remain the base on which the tax is applied because it is well suited to public health goals.

- The proposed tax rate will be 2.1c/gram for sugar content in excess of 4g/100ml.
- Of the proposed rate, 50 per cent will apply to concentrated beverages.

Some of the revenue will be used to support health-promotion interventions as part of a strategy to fight non-communicable diseases.

EXCISE DUTIES ON TOBACCO AND ALCOHOL

The targeted excise tax burdens for wine, beer and spirits are 11 per cent, 23 per cent and 36 per cent of the weighted average retail price, respectively. Since the implementation of the current excise regime in 2002, tax rates on most alcoholic beverages have consistently increased above inflation annually. The 2017 Budget continues this trend with proposed excise duty rate increases of between 6.1 per cent and 9 per cent. This will lead to excise tax burdens that are slightly higher than the targets for beer and spirits.

The targeted excise tax burden as a percentage of the retail selling price of the most popular brand within each tobacco product category is currently 40 per cent. The consumption of cigars has moved towards more expensive brands, requiring a higher than inflationary increase to maintain the targeted tax burden. Government proposes to increase the excise duty rate by between 8 per cent and 9.5 per cent.

Product	Current excise duty rate	Proposed excise duty rate	Percentage Nominal	Real percentage change
Malt beer	R79.26 / litre of absolute alcohol (135c / average 340ml can)	R86.39 / litre of absolute alcohol (146.9c / average 340ml can)	9.0	2.9
Traditional African beer	7,82c / litre	7,82c / litre	–	-6.1
Traditional African beer powder	34,70c / kg	34,70 / kg	–	-6.1
Unfortified wine	R3.31 / litre	R3.61 / litre	8.8	2.7
Fortified wine	R5.82 / litre	R6.17 / litre	6.1	–
Sparkling wine	R10.53 / litre	R11.46 / litre	8.8	2.7
Ciders and alcoholic fruit beverages	R79.26 / litre of absolute alcohol (135c / average 340ml can)	R86.39 / litre of absolute alcohol (146.9c / average 340ml can)	9.0	2.9
Spirits	R161.47 /litre of absolute alcohol (R52.07 / 750ml bottle)	R175.19 / litre of absolute alcohol (R56.50 / 750ml bottle)	8.5	2.4
Cigarettes	R13.24 / 20 cigarettes	R14.30 / 20 cigarettes	8.0	1.9
Cigarette tobacco	R14.88 / 50g	R16.07 / 50g	8.0	1.9
Pipe tobacco	R4.16 / 25g	R4.56 / 25g	9.5	3.4
Cigars	R69.28 / 23g	R75.86 / 23g	9.5	3.4

FUEL TAXES

General fuel levy

Government proposes to increase the general fuel levy and the RAF levy, effective 5 April 2017. South Africa has three main fuel taxes – the general fuel levy, the customs and excise levy on petrol, diesel and biodiesel, and the RAF levy. They fund general government expenditure, support environmental goals and finance the RAF. The general fuel levy's proposed increase of 30c/litre contributes to the additional revenue requirement for 2017/18. After a large increase in the RAF levy in 2015/16 and no increase last year, it is proposed that the RAF levy be increased by 9c/litre.

Total combined fuel taxes on petrol and diesel

	2015/16		2016/17		2017/18	
Rands/litre	93 octane petrol	Diesel	93 octane petrol	Diesel	93 octane petrol	Diesel
General fuel levy	2.55	2.40	2.85	2.70	3.15	3.00
Road Accident Fund levy	1.54	1.54	1.54	1.54	1.63	1.63
Customs and excise levy	0.04	0.04	0.04	0.04	0.04	0.04
Total	**4.13**	**3.98**	**4.43**	**4.28**	**4.82**	**4.67**
Pump price[1]	10.09	9.26	12.15	9.43	13.38	11.63

Taxes as percentage of pump price	*40.9%*	*43.0%*	*36.5%*	*45.4%*	*36.0%*	*40.2%*

PROFIT SHIFTING AND BASE EROSION

In November 2015, the Group of 20 (G20) governments endorsed a package of measures to curb base erosion and the shifting of profits to low-tax countries. The base erosion and profit shifting project is now being implemented. Many countries, including South Africa, have begun incorporating the preventative measures into domestic legislation.

South Africa worked with more than 100 jurisdictions in crafting the multilateral instrument that will swiftly modify and implement tax treaty-related measures without the need to renegotiate each tax treaty bilaterally. It was adopted on 24 November 2016 and governments, including South Africa, are expected to sign the multilateral instrument on 7 June 2017. Government has also committed to the automatic exchange of financial account information from 1 September 2017. Large multinational companies will be required to file country-by-country transfer-pricing reports with SARS from 31 December 2017.

Government is strengthening its efforts to curb excessive debt financing, which erodes the tax base, and will review the current regime in light of OECD recommendations. Table C.5 in Annexure C shows progress in implementing the standards and recommendations.

CARBON TAX

During 2016, following comments received on the draft Carbon Tax Bill, government held additional public consultations. A revised Carbon Tax Bill will be published for public consultation and tabled in Parliament by mid-2017. The latest developments include the following:

- During the first phase of the tax (until 2020), there will be no impact on the price of electricity.
- A revised regulation for the carbon offset allowance, enabling firms to reduce their carbon tax liability, will be published by mid-2017.

By the end of this year, government expects to provide clarity on the alignment of the carbon tax and carbon budget after 2020.

INTERNATIONAL TAX

Tax treatment of foreign member funds

The South African government will be establishing foreign member funds to enable local and foreign fund managers to establish and manage funds targeted for investments into the rest of Africa and the world. To make foreign member funds attractive, they will benefit from a special tax dispensation. Foreign investors investing in the funds for onward investment into the rest of Africa or elsewhere will be exempt from withholding tax on interest. However, fees earned by local asset managers and collective investment scheme managers for investment management services will be subject to tax in South Africa.

Changes to the tax treatment of domestic treasury management companies

In 2013, amendments were made in the Income Tax Act to make provision for qualifying domestic treasury management companies to be eligible for tax relief in respect of foreign currency gains and losses. The qualifying criteria for domestic treasury management companies in relation to tax residence will be reviewed as they are overly restrictive.

Tax implications of acquisition of foreign intellectual property by South African multinationals

The Income Tax Act does not allow deductions for payments made to a foreign person in respect of the use or right to use tainted intellectual property. This is to prevent erosion of the tax base resulting from assigning South African intellectual property to foreign entities subject to lower effective tax rates in the foreign country, followed by the licensing of that intellectual property back to South African taxpayers. As these anti-avoidance measures may affect legitimate commercial transactions and discourage the use of South African-based group infrastructure to further develop offshore intellectual property, relaxation of the policy will be considered without losing sight of the initial policy intent, which is to prevent tax base erosion.

Tax implications of controlled foreign companies and offshore foreign trusts

In 2015, the Budget Review announced that measures would be introduced on the treatment of foreign companies held by interposed trusts. However, no specific countermeasures were introduced in this regard. It is therefore proposed that specific countermeasures be introduced to curb abuses.

PART 2 – TAX UPDATE

These notes cover tax developments over the last year, including SARS' documentation and regulations released during 2016 and the 2016 Amendment Acts promulgated on 19 January 2017. The list is not exhaustive. You will recognise edited versions of the Explanatory Memoranda which make up the bulk of these notes.

USEFUL GUIDES ISSUED OR REVISED BY SARS DURING 2016 AND EARLY 2017

Issue date	Subject
19 September 2016	Basic guide to income tax exemption for public benefit organisations (Issue 2)
19 September 2016	Basic guide to tax-deductible donations (Issue 2)
29 March 2016	Guide for tax rates/duties/levies (Issue 12)
26 January 2017	Tax exemption guide for public benefit organisations in South Africa (Issue 5)
29 February 2016	Tax guide for recreational clubs (Issue 3)
1 February 2017	Guide on the US Foreign Account Tax Compliance Act (FATCA) (Issue 2)
5 December 2016	SARS FAQ Guide: Common Reporting Standard
30 June 2016	Guide on the determination of medical tax credits (Issue 7)
21 July 2016	Guide on the taxation of franchisors and franchisees
16 August 2016	Guide to the employment tax incentive
18 November 2016	Guide to the exemption from normal tax of income from films
18 November 2016	Guide to the urban development zone (UDZ) tax incentive (Issue 5)
10 February 2017	ABC of capital gains tax for individuals (Issue 9)
10 February 2017	ABC of capital gains tax for companies (Issue 7)
28 September 2016	Transfer duty guide
26 January 2017	Tax guide for micro businesses (2016/17)
12 December 2016	Quick reference guide on VAT ruling application procedure
24 January 2017	VAT 404 – Guide for vendors
27 September 2016	VAT 409 – Guide for fixed property and construction
28 September 2016	VAT 420 – Guide for motor dealers
12 December 2016	VAT 421 – Guide for short-term insurance

INTERPRETATION NOTES ISSUED OR REVISED DURING 2016 AND EARLY 2017

Issue date	No.	Subject
19/12/2016	IN 94	Contingent liabilities assumed in the acquisition of a going concern
24/11/2016	IN 93	The taxation of foreign dividends
24/10/2016	IN 92	Documentary proof prescribed by the Commissioner
21/10/2016	IN 91	Reduction of debt

Issue date	No.	Subject
15/08/2016	IN 90	Year of assessment of a company: Accounts accepted to a date other than the last day of a company's financial year
01/03/2016	IN 89	Maintenance orders and the tax-on-tax principle
19/02/2016	IN 88	Tax deduction for amounts refunded

DRAFT DOCUMENTS ISSUED DUE FOR COMMENTS

Comment date	Subject
3 March 2017	Draft BGR on associations: funding requirement
31 March 2017	Draft IN 67 (Issue 3) on connected persons
31 March 2017	Draft Interpretation Note on classification of risk policy and the once-off election to transfer certain policies or classes of policies issued before 2016 to the risk policy fund
31 March 2017	Draft Rates and Monetary Amounts and Amendment of Revenue Laws Bill, 2017
13 April 2017	Draft IN 60 (Issue 2) on loss on disposal of depreciable assets
28 April 2017	Draft IN on the exemption from income tax: remuneration derived by a person as an officer or crew member of a South African ship

BINDING PRIVATE RULINGS ISSUED OR REVISED DURING 2016 AND EARLY 2017

Note: Binding Private Rulings (BPR) are published in terms of section 87 of the Tax Administration Act. A BPR does not have any binding effect upon the Commissioner unless that ruling applies to a person in accordance with section 83 of the Tax Administration Act. In addition, a BPR may not be cited in any proceedings before the Commissioner or the courts other than a proceeding involving the applicant or co-applicant for that ruling. Thus, you cannot rely upon a binding private ruling that has been issued to someone else, even if the facts of your own transaction are similar to those described in the published ruling. These rulings are therefore published for general guidance only.

BPR No.	Subject
BPR225	Hybrid debt instruments
BPR225	Transfer of the long-term insurance business, partly to a third party and partly intra-group
BPR225	Share subscription transaction followed by two share repurchase transactions
BPR226	Whether an investment of preference share funding in a newly established business is for a "qualifying purpose"
BPR227	Employer provided accommodation to employees
BPR228	Disposal of an asset in terms of an asset-for-share transaction within 18 months of its acquisition in terms of an intra-group transaction
BPR229	Corporate restructuring by way of asset-for-share and amalgamation transactions
BPR230	Disposal of an asset in terms of an asset-for-share transaction within 18 months of its acquisition in terms of an intra-group transaction
BPR231	Corporate restructuring by way of asset-for-share and amalgamation transactions
BPR232	Equity shares to be issued by resultant company as part of an amalgamation transaction

BPR No.	Subject
BPR233	Transfer of a part of a business to a fellow subsidiary
BPR234	Asset-for-share and unbundling transactions not regulated by sections 42 and 46
BPR235	Income tax consequences for parties to an unbundling transaction
BPR236	Set-off of a loan account arising from an intra-group transaction to acquire equity shares
BPR237	Reinstatement of a deregistered company to transfer immovable properties
BPR238	Taxation of receipts by or accruals to a programme of activities of a clean development mechanism project
BPR239	Cash contributions made to a special purpose vehicle established to provide housing to mine workers
BPR240	Taxation of parties to share index linked notes
BPR241	Award received for a black economic empowerment (BEE) training initiative
BPR242	Venture capital company investment in qualifying companies carrying on business as hotel keepers
BPR243	Termination of a subcontracting agreement and implementing of a toll manufacturing arrangement
BPR244	Disposal of an undivided interest in immovable property by way of an amalgamation transaction
BPR245	Time of accrual of short-term insurance premiums and time of supply of security provided to the Master of the High Court
BPR246	Debt reduction and capitalisation
BPR247	Employer contributions to foreign social and pension funds in respect of a non-resident
BPR248	Deduction of interest on asset backed notes
BPR249	Corporate group restructuring involving multiple transactions
BPR250	Risk policies
BPR251	Cancellation of reinsurance agreement
BPR252	Donations tax and capital gains tax consequences of the part waiver of a loan and reduction of the interest rate
BPR253	Donations tax consequences of a transaction to introduce a BEE shareholder into a group
BPR254	Consequences of cross-border and domestic asset-for-share transactions
BPR255	Debt reduction by means of set-off
BPR256	Mining rehabilitation
BPR257	Islamic financing arrangement
BPR258	Corporate group restructuring
BPR259	Capital gains tax implications for an employee share trust
BPR260	Interest on loans used to acquire shares

BINDING CLASS RULINGS ISSUED OR REVISED DURING 2016

Note: Binding Class Rulings (BCR) are published in terms of section 87 of the Tax Administration Act. A BCR does not have any binding effect upon the Commissioner unless that ruling applies to a class member in accordance with section 83 of the Tax Administration Act. In addition, a BCR may not be cited in any proceedings before the Commissioner or the courts other than a proceeding involving the applicant or a class member for that ruling. Thus, you cannot rely upon a binding class ruling that has been issued to someone else, even if the facts of your own transaction are similar to those described in the published ruling. These rulings are therefore published for general guidance only.

BCR No.	Subject
BCR052	Income tax and securities transfer tax consequences for the shareholders of a listed company following an unbundling transaction
BCR053	Programme of activities of a clean development mechanism project
BCR054	Employer-provided accommodation
BCR055	Income tax and value-added tax consequences of a customer loyalty scheme

BINDING GENERAL RULINGS ISSUED OR REVISED DURING 2016

Note: Binding General Rulings (BGR) are published in terms of section 89 of the Tax Administration Act regarding interpretation of a tax Act or the application of a tax Act in respect of a particular set of facts and circumstances or transaction as defined in section 75 of the Tax Administration Act.

BGR No.	Subject
BGR31	Interest on late payment of benefits
BGR32	VAT treatment of specific supplies in the short-term re-insurance industry
BGR33	The value-added tax treatment of the supply and importation of vegetable oil
BGR34	Management of superannuation schemes: Long-term insurers
BGR35	The value-added tax treatment of the supply and importation of frozen potato products
BGR36	Circumstances prescribed by the Commissioner for the application of section 16(2)(*g*)
BGR37	Zero-rating of international travel insurance
BGR38	The value-added tax treatment of the supply and importation of vegetables and fruit
BGR39	VAT treatment of municipal affected by changes to municipal boundaries

INTEREST RATE CHANGES

Date of change	Prescribed interest rate payable to SARS	Prescribed interest rate payable by SARS	Official interest rate for fringe benefits purposes
01.03.2008	14%	10%	12%
01.07.2008	15%	11%	
01.09.2008			13%
01.03.2009			11.5%
01.05.2009	13.5%	9.5%	
01.06.2009			9.5%
01.07.2009	12.5%	8.5%	8.5%
01.08.2009	11.5%	7.5%	
01.09.2009	10.5%	6.5%	8%
01.07.2010	9.5%	5.5%	
01.10.2010			7%
01.03.2011	8.5%	4.5%	6.5%
01.08.2012			6%

01.02.2014			6.5%
01.05.2014	9%	5%	
01.08.2014			6.75%
01.11.2014	9.25%	5.25%	
01.08.2015			7%
01.11.2015	9.5%	5.5%	
01.12.2015			7.25%
01.02.2016			7.75%
01.03.2016	9.75%	5.75%	
01/04/2016			8.00%
01/05/2016	10.25%	6.25%	
01/07/2016	10.5%	6.50%	

AMENDMENTS TO THE LEGISLATION

2016 AMENDMENT ACTS

- The Rates and Monetary Amounts and Amendment of Revenue Laws Act No. 13 of 2016 – 19 January 2017
- The Rates and Monetary Amounts and Amendment of Revenue Laws (Administration) Act No. 14 of 2016 – 19 January 2017
- Taxation Laws Amendment Act No. 15 of 2016 – 19 January 2017
- Tax Administration Laws Amendment Act No. 16 of 2016 - 19 January 2017
- Unemployment Insurance Amendment Act 10 of 2016 – 19 January 2017

Most of these amendments are explained in the notes below. In the preparation of these notes extensive use has been made of the Explanatory Memorandum on the Taxation Laws Amendment Bill, 2016 and the Memorandum on the Objects of the Tax Administration Laws Amendment Bill, 2016.

INDIVIDUALS, EMPLOYMENT AND SAVINGS

RETIREMENT FUND CONTRIBUTION DEDUCTION AGAINST PASSIVE INCOME

[Applicable provision: Section 11(k) of the Income Tax Act No.58 of 1962 ('the Act')]

Background

From 1 March 2016, the tax treatment of contributions to retirement funds was amended to be harmonized across all retirement funds. Previously, deductions to retirement annuity funds were only allowed to be set off against "non-retirement funding income" (which included passive income such as interest or royalties, but excluded taxable capital gains), while deductions to pension funds could only be set off against "retirement funding income" (which represented income from employment and did not include passive income).

Reasons for change

The harmonisation of the tax treatment of contributions in section 11(k) allowed for a deduction against income from "carrying on a trade", which unintendedly excluded passive income. This resulted in members of retirement annuity funds who were using the deduction against passive income to no longer able to deduct their contributions against the passive income.

Amendment

To correct this anomaly and to allow retirement annuity members to continue to receive a deduction and fully align the treatment between all retirement fund members, the deductions for contributions to all retirement funds should be allowed to be set off against passive income. For the section 11(k) deductions, the passive income does not include taxable capital gains.

Effective date

The amendments are deemed to have come into operation on 1 March 2016.

CLARIFYING SOURCE RULES FOR RETIREMENT ANNUITY FUNDS

[Applicable provisions: Sections 9(2)(i) and 9(3) of the Act]

Background

Sections 9(2)(i) and 9(3) of the Act deems the portion of the lump sum and annuity payments from a pension fund and provident fund to be from a source outside South Africa, if the amounts received are in respect of services rendered outside South Africa.

Reasons for change

There is a view within the industry that the exclusion from South Africa source rule referred to in sections 9(2)(i) and 9(3) of the Act also includes payments made from retirement annuities. However, contributions to retirement annuities are not linked to employment and should not be associated with any type of services rendered, whether they are within South Africa or outside of South Africa.

Amendment

Changes were made to section 9(2)(i) of the Act to remove the ambiguity and clarify that the exclusion from South Africa source rule in section 9(2)(i) does not apply to lump sum, or annuities received from retirement annuity funds. Section 9(3) of the Act is repealed as it created ambiguity.

Effective date

The amendments will come into operation on 1 March 2017.

FORMULA TO DETERMINE THE FRINGE BENEFIT FOR DEFINED BENEFIT CONTRIBUTIONS

[Applicable provision: Paragraph 12D of the Seventh Schedule of the Act]

Background

The new paragraph 12D of the Seventh Schedule (dealing with the valuation of contributions made by employers to certain retirement funds) inserted a formula to calculate the taxable fringe benefit for contributions to a retirement fund that has a defined benefit component. The provisions of paragraph 12D of the Seventh Schedule stated the formula would cover contributions by the employer to the retirement fund.

Reasons for change

The formula in paragraph 12D of the Seventh Schedule to the Act assumes that the value "A" represents the income that the retirement fund uses to calculate the required level of contributions given the expected liabilities of the fund. However, the wording of the provision currently refers to "remuneration" which is a different income figure. Remuneration may also differ for two individuals depending on the level of travel allowance, leading to a situation where two identical members of the same defined benefit fund would have a different fringe benefit value for the employer contribution.

This wording also refers only to employer contributions and is silent on contributions made on behalf of the employer by the fund. These types of contributions may be interpreted to be exempt from the formula, creating a potential loophole.

Amendment

Changes were made in paragraph 12D of the Seventh Schedule to adjust the definition of income to determine the value "A" in the formula and to include contributions made by the fund on behalf of the employer.

Effective date

The amendment in respect of the adjustment of the definition of income to determine the value "A" in the formula will come into operation on 1 March 2017 and applies in respect of contributions made on or after that date.

The amendment in respect of inclusion of contributions made by the fund on behalf of the employer is deemed to have come into operation on 1 March 2016 and applies in respect of contributions made on or after that date.

EXEMPTION FOR A RETIRMENET LUMP SUM THAT IS LOCATED WITHIN THE REPUBLIC

[Applicable provision: Section 10(1)(gC)(ii) of the Act]

Background

When the residence based system was introduced in 2001, section 10(1)(gC) was included in the Act to exempt the receipt of foreign pensions arising from employment outside of the Republic. The provisions of section 10(1)(gC) allows a South African tax resident who is employed outside of the Republic to receive those retirement benefits (that they earned while outside the country) free from tax.

Reasons for change

There is uncertainty regarding the interpretation of the current provisions of section 10(1)(gC). The consequence is that South African tax residents who work outside of the Republic can receive a tax deduction on contributions made to the South Africa retirement fund (local retirement fund). The deduction can either be made in the same tax year if they have other forms of taxable income or worked partially within that year or the amounts can be rolled over to be deducted in a future year of assessment. However, upon receipt of the retirement benefits the amount that accrued while the South African tax resident was employed outside the Republic will be free from tax.

Amendment

To ensure a fair tax treatment of retirement benefits received by South African residents, the Act is amended so that the exemption provided in section 10(1)(gC)(ii) only applies to retirement benefits from foreign retirement funds or amounts relating to foreign retirements funds that were transferred to a local retirement fund i.e. retirement benefit from a pension fund, pension preservation fund, provident fund, provident preservation fund or retirement annuity fund as defined in section 1 of the Act (where members are eligible for deductible contributions) will not qualify for the exemption in section 10(1)(gC)(ii).

Effective date

The amendments will come into operation on 1 March 2017 and apply in respect of years of assessment commencing on or after that date.

WITHDRAWALS FROM RETIREMENT FUNDS

[Applicable provision: Definition of "retirement annuity fund" in section 1 of the Act]

Background

In 2015, changes were made in the Act to allow individuals to withdraw a lump sum from the retirement annuity fund when they cease to be tax

resident or when they leave South Africa at the end of their work visa.

Reasons for change

The 2015 Draft Taxation Laws Amendment Bill (2015 Draft TLAB), which was released for public comments on 22 July 2015 made provision for the following criteria to be met for individuals to be able to withdraw a lump sum from their retirement annuity fund:

- When the individual emigrated from the Republic and that emigration is recognised by the South African Reserve Bank for purposes of exchange control;
- When the individual ceases to be a tax resident;
- When the individual leaves South Africa at the expiry of the work visa contemplated in the Immigration Act, 2002; or
- Is not regarded as a resident by the South African Reserve Bank for purposes of exchange control.

Based on the public comments received on the 2015 Draft TLAB, changes were made in the 2015 TLAB to limit the criteria to be met for the individuals to be able to withdraw a lump sum from their retirement annuity fund to only the following:

- When the individual ceases to be tax resident; or
- When the individual leaves South Africa at the expiry of the work visa contemplated in the Immigration Act No. 13, of 2002.

It has come to Government attention that exclusion of the requirement that an individual must emigrate from the Republic and that emigration must be recognised by the South African Reserve Bank for purposes of exchange control creates a loophole for South African nationals or tax residents to be able to make an early withdrawal from their retirement annuity funds, without formally emigrating. This was not the original policy intention.

Amendment

To align the current provisions of the Act allowing individuals to withdraw a lump sum from their retirement annuity fund to the underlying policy objectives, the following amendment is made:

- The definition of the “retirement annuity fund” in section 1(b)(x)(dd) should be amended to include the requirement that an individual must emigrate from the Republic and that emigration must be recognised by the South African Reserve Bank for purposes of exchange control as one of the criterion to be met in order for individuals to be able to withdraw a lump sum from their retirement annuity fund.

INTEREST FREE OR LOW INTEREST LOANS TO A TRUST

[Applicable provision: New sections 7C]

Background

The transfer of wealth by a person through the use of trusts can be achieved in a number of ways. These alternatives all have their resultant tax consequences.

In the first instance, a person may donate his or her assets to a trust and trigger donations tax at a rate of 20 per cent of the fair market value of the assets in the hands of the donor. If the donor does not pay the donations tax due, then that donor and the donee (the trust) become jointly and severally liable for the donations tax due. A person may sell his or her assets to a trust on loan account, the loan being subject to interest at a market related rate. The person will be fully taxed on the interest portion of the loan repayments paid to him or her by that trust.

A person may sell his or her assets to a trust on loan account and the loan may be subject to interest that is below market rates or charge no interest on the loan. The result is that donations tax is not triggered as the transaction is a sale and not a donation. Income tax is also not paid by that person on the forgone interest as a result of not charging interest at market rates.

Lastly, a person may advance an interest free loan or a loan with interest below market rates to a trust in order to enable that trust to acquire assets or to simply retain that advance and avoid donations tax and income tax on the forgone interest as a result of the person not charging interest at market rates.

Reasons for change

At issue is the avoidance of estate duty and donations tax when a person transfers wealth through the use of an interest free loan or a loan with

interest below market rates. These loans are either used to facilitate the transfer of assets or assist the trust to acquire an asset. This is done in order to avoid donations tax as no donation arises on the sale of an asset or on advancing loan funding to a trust.

In some instances, the lender reduces or waives the loan capital which is supposed to be paid back to him/her (whether as settlement for an outstanding asset disposal consideration or the settlement of loan funding that was advanced to a trust for its own use). This further avoids estate duty through the reduction or waiver of the asset base of the lender in respect of the loan capital.

Due to the fact that the loan is an interest free loan or a loan with interest below market rates, no interest is paid to the seller or interest paid is less than market rates, the seller will not be liable for income tax on the interest that is forgone. This results in a further reduction of the tax base.

Amendment

In order to limit taxpayers' ability to transfer wealth to a trust without being subject to tax, new rules focusing on affected loans were introduced in section 7C of the Act. For purposes of section 7C, affected loans will encompass interest free loans or loans with interest below market rates that are made to a trust directly or indirectly by:

- A natural person, or
- A company that is a connected person in relation to that natural person, i.e. a company in which that natural person, either individually or together with a connected person or persons, holds an interest of at least 20 per cent.

The anti-avoidance measure under the new section 7C will with effect from 1 March 2017 apply to all loans, including loans currently in existence, that meet this criterion if the person or company involved, or any person that is a connected person in relation to that person or company, is a connected person in relation to that trust. This will include loans or credit provided directly to a trust as well as loans or credit routed through other persons or entities.

Example:

Facts

Mr Planner's spouse and three children are beneficiaries of the Quattuor Trust. The Quattuor Trust is the only beneficiary of the Tempus Fugit Trust.

Mr Planner advances a loan of R 5 million to a business associate, Grabbitt,that is not a connected person in relation to any of the trusts. The loan is non-interest bearing, payable on demand and is subject to an arrangement in terms of which Grabbitt will in turn advance an interest-free loan of R5 million that is repayable on demand to the Tempus Fugit Trust and cede the claim for repayment thereof to Mr Planner as security for the repayment of the amount owed by Grabbitt. The Tempus Fugit Trust utilises those funds to acquire a range of shares and interest-bearing assets.

Result

The loan used by the Tempus Fugit Trust was advanced indirectly by Mr Planner. The rules will therefore apply in respect of the loan to the Tempus Fugit Trust.

The proposed rules will apply only in respect of loans advanced or provided by a natural person or, at that person's instance, by a connected company. An amount that is vested irrevocably by a trustee in a trust beneficiary and that is used or administered for the benefit of that beneficiary without distributing or paying it to that beneficiary will not qualify as a loan or credit provided by that beneficiary to that trust if

- The vested amount may in terms of the trust deed governing that trust not be distributed to that beneficiary, e.g. before that beneficiary reaches a specific age; or
- That trustee has the sole discretion in terms of that trust deed regarding the timing of and the extent of any distribution to that beneficiary of such vested amount.

An amount vested by a trust in a trust beneficiary that is not distributed to that beneficiary will, however, qualify as a loan or credit provided by that beneficiary to that trust if that non-distribution results from an election exercised by that beneficiary or a request by that beneficiary that the amount not be distributed or paid over, e.g. if the beneficiary has reached the age at which a vested amount must be paid over or distributed to him or her and

- The trustee accedes to a request by that beneficiary that this not be done; or

- The beneficiary enters into an agreement with the trustee in terms of which the amount may be retained in the trust.

Treatment of interest forgone as a donation

Interest foregone in respect of low interest loans or interest free loans that are made to a trust will be treated as an ongoing and annual donation made by the natural person to the trust on the last day of the year of assessment of that trust. For purposes of this anti-avoidance measure, interest foregone will be determined as the difference between the interest charged by the lender or holder of the loan and the interest that would have been payable by the trust had the interest been charged at the official rate of interest as defined in the Seventh Schedule to the Act).M

Multiple natural persons as shareholders

It is acknowledged that in some instances, an affected loan under these rules may be advanced by a company to a trust at the instance of more than one natural person who are shareholders in that company. To address such scenarios, each person will treated as having made a donation in proportion to their equity interests in the company during the year of assessment that the deemed donation arose.

Denial of tax deduction or losses

There is also concerns around the cancellation or waiver of loan accounts that are assets of the lenders. Often, lenders that advance low interest or interest free loans will cancel or waive the loan. This results in the diminution of the asset base of the lender for estate duty purposes. To counter such practices that avoid estate duty, no deduction, loss, allowance or capital loss may be claimed in respect of interest free loans or low interest loans made to trusts.

The interaction between section 7C and section 31

This anti-avoidance measure seeks to curb the unfair advantage of using loans that are not subject to interest at market rates have. Similarly, the transfer pricing rules in the Act also apply to counter the mispricing of cross-border loan arrangements. In order to ensure that there is no overlap or double taxation in respect to low or no interest loans made to foreign trusts, the anti-avoidance measure under section 7C will not apply to a loan that is subject to the transfer pricing rules in section 31 of the Act.

Exclusions from the application of section 7C

As trusts are used for a myriad of other purposes other than that of estate planning, various exclusions are proposed from the application of these rules. These exclusions include the following:

Vesting trusts:

Loans by trust beneficiaries to vesting trusts that comply with the requirements listed in subsection (5)(b) will be excluded from the proposed rules. The vested interest of a beneficiary in the assets and receipts or accruals of such a trust will form part of that beneficiary's estate during his or her life and upon death or when ceasing to be a resident. The interest that remains subject to normal tax as well as estate duty represents, in effect, a fixed stake in the assets disposed of to or acquired by that trust and in the gains made by that trust. An interest-free or a low-interest loan made to that trust by a beneficiary should therefore not result in estate duty avoidance if that beneficiary's vested stake in the trust assets is proportionate to that beneficiary's contributions, including that loan, to that trust.

Examples:

- Loans to a trading trust that meets all the requirements set out in subsection (5)(b).
- A loan by a trust beneficiary to a trust that qualifies as a bewind trust, i.e. a trust that holds and administers assets, the ownership of which vests in that beneficiary, for and on behalf that beneficiary.

Trusts that hold a primary residence:

A loan made by or at the instance of a natural person to a trust will be excluded to the extent to which that loan was used by that trust to fund the acquisition of a residence that is used by that person or that person's spouse as a primary residence.

Examples:

Facts

Mr Law made an interest-free loan of R5 million to the Law Family Trust during 2010. The trust used R3 million of the funds to acquire a house in which Mr Law and his spouse have resided and used as their primary residence ever since. The remaining R2 million was used to fund the

acquisition of other assets.

Result:

The anti-avoidance rule will be applied only in respect of the R2 million not used for purposes of acquiring the house.

Other exclusions from this targeted anti-avoidance rule include the following:

- Special trusts that are created solely for the benefit of minors with disability as defined in paragraph (a) of the definition of "special trust" in section 1 of the Act;
- Trusts that fall under public benefit organisations as contemplated in section 30 of the Act;
- Small Business Funding entities contemplated in section 30C of the Act;
- Loans that constitute an affected transaction and subject to the provisions of section 31 of the Act;
- Loans provided to the trust in terms of a sharia compliant financing arrangement; and
- Loans that are subject to the anti-value extraction provisions of section 64E(4) of the Act.

Effective date

The amendments will come into operation on 1 March 2017 and apply in respect of any amount owed by a trust in respect of a loan, advance or credit provided to that trust before, on or after that date.

EMPLOYER PROVIDED BURSARIES

[Applicable provision: Section 10(1)(q) of the Act]

Background

Currently, the Act makes provision for tax exemption for all "bona fide" bursaries or scholarships granted by employers to employees or relatives of qualifying employees, subject to certain monetary limits and other requirements.

If a bursary or scholarship is awarded to a relative of the employee, the exemption will apply only if the employee's remuneration does not exceed R250 000 during the year of assessment. In addition, the amount of the bursary or scholarship will only be exempted up to a limit of R10 000 for studies from Grade R to 12 including qualifications in NQF levels 1 to 4 and R30 000 for qualifications in NQF levels 5 to 10.

Reasons for change

The monetary limits associated with bursaries and scholarships granted to relatives were last revised in 2013. To support skills development and to encourage the private sector (employers) in the provision of education and training.

Amendment

The monetary limits are increased for bursaries and scholarships granted by employers to employees or relatives of qualifying employees.

The monetary limit in respect of remuneration for qualifying employees are increased from R250 000 to R400 000.

The monetary limits in respect of exempt bursary or scholarship are increased from R10 000 to R15 000 and from R30 000 to R40 000 respectively.

Effective date

The amendments are deemed to have come into operation on 1 March 2016 and apply in respect of years of assessment commencing on or after that date.

EMPLOYEE BASED SHARE INCENTIVE SCHEMES

[Applicable provisions: Section 8C and section 10(1)(k) of the Act]

Background

Amounts in cash or in kind which are received or accrued in respect or by virtue of services or employment are treated, as a point of departure, as ordinary revenue. Section 8C (dealing with taxation of directors and employees on vesting of equity instruments) forms part of a set of anti-avoidance measures aimed at preventing the characterisation of an amount that relates to services or employment as a capital gain or as an exempt amount subject only to dividends tax.

For example, dividends that are received or that accrue in respect of services or by virtue of employment or the holding of an office are treated as ordinary revenue.

Section 8C governs schemes that are based on equity shares. A restricted equity instrument represents an interest in the equity shares underlying the scheme that is held either directly or through a derivative mechanism. The retention or acquisition, by a scheme beneficiary, of the benefits flowing from the scheme, e.g. dividends, is subject to suspensive or resolutive terms or conditions. These benefits are dependent, in essence, on continued employment or the rendering of services for a specified period.

The distributions derived from a restricted equity instrument and the growth in value of the underlying shares until the date the restrictions fall away constitute, in effect, benefits that arise in respect of services and form part of the reward for services rendered. Dividends in respect of a restricted equity instrument will be exempt only if that instrument complies with specific requirements.

Taxation under section 8C is as a general rule triggered when the restrictions in respect of the interest in the underlying equity shares fall away, i.e. when the employee can, in broad terms, freely dispose of or deal with those shares on the same basis as any shareholder who is not an employee, or is entitled to an amount equal to their value. The amount subject to section 8C is determined with reference to the value of those shares at that time, thus treating the growth in value of that payment in kind as revenue.

Section 8C is based on the implicit assumption that the full value of the equity shares underlying a restricted equity instrument will vest in the employee when the restrictions fall away. The value derived from the underlying shares may, however, be liquidated in full or in part by means of distributions that are effected before these restrictions fall away, e.g. distributions resulting from the disposal or redemption of the underlying shares or resulting from a return of capital in respect of the underlying shares. Distributions qualifying as a return of capital or a foreign return of capital in respect of the underlying equity shares are treated as revenue. The current inclusion does not extend, however, to a return of capital by way of a distribution of an equity instrument.

Distributions in the form of dividends may also impact negatively on the value of the underlying shares. The policy intent underlying the inclusion, in the income of a holder of a restricted equity instrument, of a return or foreign return of capital was expressed as follows in the Explanatory Memorandum on the Taxation Laws Amendment Bill, 2010: "Capital distribution will generally trigger ordinary revenue in recognition of this partial cash-out. However, if the capital distribution consists of another restricted equity instrument, the capital distribution will be treated as a non-event."

The current exclusion of a return or foreign return of capital does not reflect this policy clearly. A return of capital in the form equity shares that are not restricted will erode the value of the equity shares from which the value of a restricted equity instrument is derived.

The above-mentioned exclusion should apply only in respect of an equity instrument that qualifies as a restricted equity instrument subject to section 8C, i.e. if the gain or loss in respect of that instrument will be treated as being of a revenue nature. Other receipts or accruals in respect of a restricted equity instrument that are not treated as dividends and that are not taken into account in determining the gain or loss in respect of the restricted equity instrument may also erode the value of the underlying shares and result in a leakage of the gains that should be treated as income in terms of section 8C. The current requirements regarding dividends in respect of restricted equity instruments that are exempt from normal tax do not deal adequately with dividends consisting of or derived from the proceeds from the disposal or redemption of:

- The underlying equity shares; or
- Shares from which those equity shares derive their value; or
- The liquidation of a company from which those equity shares derive their value.

The treatment, as an exempt dividend, of an amount that reduces or liquidates the gain subject to section 8C converts, in effect, an amount that should be taxed at marginal rates to an amount that is taxed at a lower rate. This conflicts with the policy objective underlying section 8C (i.e. that there should be parity of treatment of amounts in cash and in kind).

Amendment

Targeted measures that deal adequately with some schemes where restricted shares are held by employees and liquidated in return for an amount qualifying as dividend be introduced as follows:

Inclusion in section 8C

The provisions of subsection (1A) of section 8C is extended to include any amount received by or accrued to a taxpayer during a year of assessment in respect of a restricted equity instrument in the taxpayer's income for that year of assessment if that amount does not constitute:

- A return of capital or foreign return of capital by way of a distribution of a restricted equity instrument;
- A dividend or foreign dividend in respect of that restricted equity instrument; or
- An amount that must be taken into account in determining the gain or loss, in terms of section 8C, in respect of that restricted equity instrument.

Exclusion from dividend exemption in section 10(1)(k)(i)

The exemption in section 10(1)(k)(i) is amended to specifically exclude certain dividends in respect of a restricted equity instrument scheme. Such dividends will be treated as ordinary revenue.

A new paragraph (jj) is introduced as a proviso to section 10(1)(k)(i) specifically excluding, from the current exemption, any dividend in respect of a restricted equity instrument as defined in section 8C that was acquired in the circumstances contemplated in section 8C if that dividend is derived directly or indirectly from, or constitutes:

- An amount transferred or applied by a company as consideration for the acquisition or redemption of any share in that company;
- An amount received or accrued in anticipation or in the course of the winding up, liquidation, deregistration or final termination of a company; or
- An equity instrument that is not a restricted equity instrument as defined in section 8C, that will, on vesting be subject to that section.

Examples

Facts:

Mr Eager, an executive director of Last Hope Ltd, holds a restricted equity instrument in the Last Hope Employee Share Trust that will remain restricted for a period of 5 years after that instrument was awarded to Mr Eager. It entitles him to dividends derived from 10 000 of the equity shares in Real Hope (Pty) Ltd that are held by the trust while the restrictions governing that equity instrument apply and the transfer of those shares once those restrictions fall away. Real Hope (Pty) Ltd is a subsidiary of Last Hope Ltd.

Real Hope buys back 90 per cent of the shares held in it by the trust at R200 per share 4 years after the award of that restricted equity instrument. The trust distributes an amount of R1 800 000 to Mr Eager as a dividend in respect of his restricted equity share.

Result:

The dividend of R1 800 000 will not be exempt as it is derived from the consideration paid by Real Hope in respect of the share buy-back. This result will apply irrespective of whether the consideration in respect of the share buy-back consists of cash or an asset in kind.

Facts:

Ms Sharp, an executive director of Tower Projects, holds a restricted equity instrument in the Tower Group Employee Share Trust that will remain restricted for a period of 5 years after that instrument was awarded to her. It entitles her to dividends derived from 10 000 of the equity shares in Mini Tower that are held by the trust while the restrictions governing that equity instrument apply and the transfer of those shares once those restrictions fall away. Mini Tower holds 100 per cent of the class B equity shares in Tower Software while Tower Projects holds all the class A equity shares in Tower Software.

Tower Software redeems 80 per cent of the class B equity shares at R200 per share 4 years after the award of that restricted equity instrument. Mini Tower distributes this amount as a dividend to the trust. The trust distributes an amount of R1 600 000 to Ms Sharp as a dividend in respect of her restricted equity instrument scheme.

Result

The dividend of R1 600 000 will not be exempt as it is derived from the consideration in respect of the redemption of the class B equity shares.

Effective date

The amendments will come into operation on 1 March 2017 and apply in respect of amounts received or accrued on or after that date.

CORPORATE

THIRD-PARTY BACKED SHARES

[Applicable provision: Sections 8E and 8EA of the Act]

Background

Third-party backed share anti-avoidance rules were introduced by Government during 2012 to deal with identifiable concerns regarding preference shares with dividend yields backed by third parties. These anti-avoidance rules deem dividend yields of third-party backed shares to be treated as ordinary revenue unless the funds derived from the issue of the third-party backed shares are used for a qualifying purpose.

The rules target share instruments (typically preference shares) with debt like features, i.e. where the dividends in respect of those shares are guaranteed by unrelated third parties. The holder of the share is in effect not exposed to the risks associated with the issuer that would normally be faced by the holder of an equity stake.

For purposes of these specific anti-avoidance rules, section 8EA of the Act defines third-party backed shares as preference shares in respect of which an enforcement right or obligation exists for the benefit of the holder of the preference shares. An enforcement right means, in broad terms, a right of the holder of the share that is enforceable against a third person (who therefore bears the corresponding obligation) in terms of which that person may be required to:

- Acquire that share from that holder;
- Make any payment in respect of that share in terms of a guarantee, indemnity or similar arrangement; or
- Procure, facilitate or assist with any of the above.

A subordination agreement entered into with a third party creditor of the issuer of that share in terms of which the payment of any amount owing to that creditor is conditional upon the prior payment, to the holder of that share, of any amount owed in accordance with the terms governing that share would, for example, be an arrangement that would facilitate or assist with the making of such payment to that holder.

Reasons for change

Over the past 2 years, changes have been effected to the third-party backed share antiavoidance rules to address adverse tax consequences affecting legitimate business transactions not aimed at avoidance. Concerns have been raised that certain provisions in these rules still impede certain historic arrangements and transactions that were entered into before the introduction of these anti-avoidance rules in the Act in 2012.These historic arrangements and transactions were often entered into with guarantees and obligations being bolted on by lenders as standard practice, thus effectively trapping parties to these transactions and arrangements within the ambit of the targeted anti-avoidance rules.

Taxpayers who entered into the historic arrangements and transactions could restructure them so as to remove the excessive guarantees and obligations but at issue is the fact that in absence of any commercial reasons for restructuring other than to avoid the provisions of section 8E or section 8EA of the Act, such restructuring could attract the application of the general anti-avoidance rule.

A further issue that has been raised relates to the definition of qualifying purpose. The use of funds derived from a preference share issue to acquire shares in a company will in terms of the current wording constitute a qualifying purpose only if that company is an operating company at that time, i.e. a company carrying on a business in the course of which it provides goods or services. This requirement does not cater for the acquisition of shares in start-up companies that have not yet commenced the carrying on of a business, e.g. a company that is still erecting the plant that is required for the provision of goods or services.

Amendment

Pre-2012 legitimate transactions

To provide relief in respect of pre-2012 legitimate transactions, the following is amended:

- To allow any parties that entered into any arrangement or transaction the terms of which were finally agreed to before 01 April 2012, (earliest effective date of the third-party backed share anti-avoidance rules) that fall foul of the provisions of section 8EA be allowed to cancel any enforcement obligation or right;
- Cancellation of any enforcement obligation or right be made within a proposed window period, i.e, the period from the date of introduction of

the TLAB on 26 October 2016 to 31 December 2017; and

- Relief be prospective. There will be no refunds of tax in respect of amounts received or that accrued in respect of the affected shares prior to the cancellation of the enforcement rights in question.

Start-up companies

The definition of a qualifying purpose is amended to cater for the investment, in shares of start-up companies, of funds derived from preference share issues by applying the test whether the company is an operating entity only at the time of the receipt or accrual of any dividend in respect of those preference shares.

Effective Date

- The amendments in respect of pre-2012 legitimate transactions will come into operation on the date of promulgation of the Taxation Laws Amendment Act, 2016.
- The amendment in respect of start-up companies will come into operation on 1 January 2017 and will apply in respect of years of assessment ending on or after that date.

ANTI-AVOIDANCE RULES DEALING WITH THIRD PARTY BACKED SHARES

[Applicable provisions: Sections 8E and section 8EA of the Act]

Background

The anti-avoidance measures introduced during 2012 in respect of instruments with debt-like features targeted, firstly, share issues the dividends in respect of which were guaranteed by unrelated third parties. Secondly, the legislation targeted share issues the dividends in respect of which were fully secured by financial instruments (i.e. the secured financial instrument served as the basis for the dividend yield as opposed to a mix of assets associated with the issuing company as a whole).

Reasons for Change

Several schemes have been identified where investors structure transactions to circumvent the hybrid equity anti-avoidance rules. These anti-avoidance schemes are even marketed and sold as tax beneficial products to investors. These schemes include, for example, the formation of trust holding mechanisms whereby investors acquire participation rights in trusts and the underlying investments of those trusts are preference shares. The main aim of these schemes is for the trusts to invest in preference shares in order to generate income in the form of dividends.

The interposition of a trust between the investor and the underlying preference shares is aimed at avoiding the anti-avoidance measures in order to preserve the benefit, for the holder of the instrument, of being taxed at the lower dividend withholding tax rate as opposed to the normal tax rate which applies on interest income.

Amendment

In order to curb the circumvention of these specific anti-avoidance measures section 8E as well as section 8EA will be extended to include any right or interest where the value of that right or interest is directly or indirectly determined with reference to a share or an amount derived from a share.

Effective Date

The amendments will come into operation on or after 1 January 2017 and apply in respect of years of assessment ending on or after that date.

CROSS-BORDER HYBRID DEBT INSTRUMENTS

[Applicable provisions: Sections 8F and 8FA of the Act]

Background

Specific anti-avoidance rules dealing with hybrid debt instruments and hybrid interest were introduced during 2013. The anti-avoidance rules reclassify amounts incurred as interest as dividends in specie that cannot be deducted by the company that incurred them. The antiavoidance rules embedded in section 8F focus on the equity-like features of the debt instrument itself, while section 8FA focuses on the nature of the yield (i.e. the method of determining the amount that is labelled as interest).

Section 8F targets, in broad outline, debt instruments that are subject to an arrangement in terms of which

- The instrument must or can be converted into or exchanged for shares;
- The payment of an amount owing in respect thereof is conditional upon the solvency of the issuer; or
- The issuer owes an amount to a connected person and is not obliged to redeem that instrument within 30 years from its date of issue.

Section 8FA focuses on the nature of the yield and targets amounts that are not determined with reference to a rate of interest or the time value of money or that are determined with reference to profits or gains.

These anti-avoidance rules are aimed at preventing the artificial generation of interest deductions by an issuer if the debt instrument qualifies as a hybrid debt instrument because of its equity features, or if the yield is determined not to constitute bona fide interest. In addition, the issuer is furthermore liable for dividends tax at a rate of 15 per cent.

Reasons for change

The 2013 Draft Taxation Laws Amendment Bill (2013 Draft TLAB) which was released for public comments on 4 July 2013 made provision for these specific anti-avoidance rules to apply only in respect of debt that was issued by South African tax resident companies. Based on the public comments received on the 2013 Draft TLAB, changes were made in the 2013 Draft TLAB to extend the application of these rules to debt issued by both resident and non-resident companies.

It has come to Government's attention that the current dispensation creates opportunities for tax arbitrage by allowing non-resident issuers of debt instruments to issue debt instruments that include any of the targeted equity features to resident holders in order to take advantage of the re-classification feature of these anti-avoidance rules.

The resident holder of the debt instrument will benefit from the re-classification of interest as dividends in specie as that holder will be deemed to have received a dividend in specie that is exempt from normal tax. However, the anti-avoidance rules will as a general rule not be effective by denying the non-resident issuer an interest deduction as the non-resident issuer would in most instances not be subject to the South African anti-hybrid debt rules. The non-resident issuer would be subject to a dividend withholding tax of 15 per cent (subject to various exemptions and treaty benefits).

Amendment

In order to curb this mismatch and discourage non-resident issuers from structuring their loans by including equity features that trigger the re-classification of their interest payments for South African tax purposes, both sets of anti-avoidance rules should be limited to instances under which the intended denial of the interest deduction will apply.

The following anti-avoidance rules should only apply:

- In instances where the issuer is a resident company;
- Where the issuer is a non-resident company, if the interest in respect of that instrument is attributable to a permanent establishment in South Africa; or
- Where that issuer is a controlled foreign company, if the interest in respect of that instrument must be taken into account in determining the net income of that company in terms of section 9D.

Effective date

The amendments are deemed to have come into operation on 24 February 2016 and apply in respect of amounts incurred in respect of an instrument on or after that date.

HYBRID DEBT INSTRUMENTS SUBJECT TO SUBORDINATION AGREEMENTS

[Applicable provision: Section 8F of the Act]

Background

An amount of interest that is incurred in respect of a debt instrument is recharacterised in terms of section 8F of the Act as a dividend in specie declared and paid by the issuer if that debt instrument has specific equity-like or dividend like features. The issuer may not deduct the interest so incurred and becomes liable for dividend withholding tax at a rate of 15 per cent in respect of such dividend in specie.

The anti-avoidance rules will be triggered by any arrangement in terms of which the obligation to repay any amount owing in respect of the debt instrument (i.e. the corpus or interest) is conditional upon the solvency of the debtor (i.e. the market value of the issuer's assets not being less than its liabilities).

Reasons for change

Timing of the re-characterisation of the yield on an instrument that is subject to a subordination arrangement Debt instruments that are subject to section 8F must be tested for the specified equity-like features that trigger the avoidance rules on a continuous basis (i.e. not once off at the date of issue but at any time thereafter). The re-characterisation of the interest labelled yield was intended to apply in respect of the period during which an instrument exhibits these equity-like features. Currently, paragraph (b) of the definition of a "hybrid debt instrument" in terms of which an instrument that is subject to subordination is subject to the re-characterisation rule does not clearly express this intention. The current wording is ambiguous as to whether the recharacterisation rule will apply from the date of issue of the instrument that is subject to a subordination arrangement or only in respect of the period during which a payment of an amount owing was deferred in terms of that arrangement.

The impact of applying the re-characterisation rule in respect of an instrument subject to a subordination arrangement where the issuer is in financial distress In the current economic climate, it is not uncommon for companies to find themselves going through periods of varying levels of financial distress. These periods of financial distress may be short-term or may be fairly sustained. As a result, many companies revert to entering into subordination agreements aimed at subordinating their related party loans in favour of third party borrowings. A subordination arrangement may also result from an audit of the company if its auditors require that shareholder loans be subordinated to ensure that the company's annual financial statements not be qualified regarding whether it can continue as a going concern.

Typically, a subordination agreement provides that the company will not make any payments in respect of a debt until such time as the assets of the company fairly valued exceed the liabilities of the company. The re-classification of the interest as a result of the subordination agreement gives rise to added pressures for the company. In the first instance, the company will be treated as having paid a dividend in specie in respect of any interest incurred in respect of the subordinated loan. It will, secondly, be denied a deduction in respect of the incurred interest charges.

Amendment

Timing of the re-characterisation of an instrument due to subordination: In order to clarify that the re-characterisation of an instrument by virtue of that instrument being or becoming subject to a subordination agreement will only apply for the period that the instrument is subject to subordination, technical changes are proposed to paragraph (b) of the definition of a "hybrid debt instrument".

The intention is to confirm that an instrument will be regarded as a "hybrid debt instrument" if the obligation of a company to pay an amount during a year of assessment has been deferred conditional upon the assets of that company exceeding its liabilities. In addition, that instrument will be regarded as a "hybrid debt instrument" only for that period.

Exclusion from re-characterisation of an instrument subject to subordination This exclusion for related party debt that is subordinated in favour of third party creditors will result in the company continuing to claim its interest deduction of the debt. In addition, as there will be no re-classification of the interest as dividends in specie, the company will not suffer the added burden of a dividends withholding tax. For purposes of this exclusion, relief will be provided so that subornation agreements entered into in respect of debt between connected persons as defined in section 1 of the Income Tax Act. As a condition of this relief, the subordination of the envisaged debt must be subject to a request by a registered auditor, as contemplated in the Auditing Profession Act (Act No. 26 of 2005), who or which has certified that the payment, by a company, of an amount owed in respect of that instrument has been or is to be deferred by reason of the market value of the assets of that company being less than the amount of the liabilities of that company.

It is envisaged that the auditor's certification of the subordination of the related party debt for purposes of this exclusion should be evidenced in a separate letter.

Effective date

The amendments are deemed to have come into operation on 1 January 2016 and apply in respect of years of assessment commencing on or after that date.

OUTRIGHT TRANSFER OF COLLATERAL PROVISIONS

[Applicable provisions: Section 1, 22 and paragraph 11 of the Eighth schedule of the Act and section 1 of the Securities Transfers Act No. 25 of 2007]

Background

In 2015, changes were made in the tax legislation to provide relief in respect of an outright transfer in beneficial ownership of collateral. As a result, there are no capital gains tax and securities transfer tax implications if a listed share is transferred as collateral in a collateral arrangement, provided that the identical shares are returned to the borrower by the lender within a limited period of 12 months from the date in which the collateral arrangement was entered into.

The 2015 tax dispensation that was introduced in the tax legislation for the outright transfer of collateral is similar to the tax dispensation applicable to securities lending arrangements.

The above-mentioned new tax dispensation for collateral arrangements necessitated the introduction of a concept of "identical share" in the tax legislation as well as changes to the provisions dealing with amalgamation transactions in section 44 of the Act, to take into account the impact of amalgamation transaction on the ability of a party to the arrangement to return a share of the same class in the same company as that share originally transferred in terms of that arrangement.

Reasons for change

The tax relief on collateral arrangements has been welcomed by industry and taxpayers but concerns have been raised about certain of the restrictions and potential shortcomings not addressed in the current legislation. These restrictions include the following:

12 Month limitation

The limitation of a collateral arrangement to a period of 12 months or less without the ability to re-post collateral due to the underlying obligation is unduly restrictive and would have the effect that it can only be applied in a context of a short term debt and would severely restrict the ability of banks to benefit from collateral arrangements in terms of meeting the regulatory requirements in so far as it relates to high quality liquid assets.

Corporate Actions

The 2015 changes to the definitions of "identical share" and "identical security" in the Act only recognize the impact of specific corporate actions on the ability of parties to both collateral and lending arrangements to return an identical share or security only to the extent of amalgamation transactions as envisaged in section 44 of the Act. These changes do not cater for situations outside of the control of a party to a securities lending/collateral arrangement that could possibly result in an identical share or security being unable to be returned in terms of securities lending/collateral arrangements. In practice, corporate actions and its impact on the ability to deliver an identical share or security in relation to these arrangements can be separated into two categories where a corporate action can either:

- Impact the listed status of the share through the following actions (list not exhaustive nor definitive):
  - Suspension/termination or withdrawal of share listing on a recognized exchange;
  - Winding up/insolvency of issuer of shares; or
  - Unbundling transactions; or
- Result in additional or different shares being returned through the following actions (list not exhaustive nor definitive):
  - Rights offers;
  - Scrip dividends;
  - Capitalization issues; or
  - Unbundling transactions.

These categories or actions could potentially impact the securities lending/collateral arrangement definition post implementation of the securities lending/collateral arrangement, by no fault of the parties to the securities lending/collateral arrangement, which would result in the application of both capital gains tax and securities transfer tax to such securities lending/collateral arrangement.

Listed shares

The special tax dispensation for securities lending/collateral arrangement only applies to the instruments listed in paragraph (a) of "security" as defined in the Securities Transfer Tax Act that is listed on an exchange. This limits the exemption on securities lending/collateral arrangement to listed shares only to be transferred as collateral. As a result, if bonds and other instruments not listed in paragraph (a) of the definition of security are transferred as collateral, they will not qualify for this special tax dispensation.

Amendment

Extending the 12 Month limitation to a 24-month limitation

Government is still concerned that the 2015 changes made in the tax legislation to provide relief in respect of an outright transfer in beneficial ownership of collateral moves away from common law principles in regard to a change of beneficial ownership. As a result, the 12-month limitation in respect of collateral arrangement was introduced to assist in limiting tax avoidance scenarios where either the sale of shares is disguised as collateral transactions or transactions where the collateral is used against rolling debt positions that are designed to keep a collateral position open for extended periods of time or even indefinitely.

Due to the fact that collateral arrangements support financial stability objectives because of the role they play in mitigating credit risk, it is proposed that the legislation be amended to extend the allowable period within which the identical shares are returned to the borrower by the lender from the date on which the collateral arrangement was entered into from 12 to 24 months.

Broadening the definitions of "identical share" and "identical security" to cater for other specified corporate actions

The legislation, as it relates to an 'identical security' and 'identical share' for purposes of a security lending/collateral arrangement, is broadened to cater for corporate actions in relation to situations outside of the control of a party to a securities lending/collateral arrangement that could possibly result in an identical security or identical share being unable to be returned in terms of that securities lending/collateral arrangement. The legislation should only recognize corporate actions announced and released, post finalisation of the securities lending/collateral agreement, by a Stock Exchange News Service (SENS) announcement if it specifically relates to the allowable security/collateral within that securities lending/collateral arrangement.

Including listed government bonds as allowable instruments on security lending and collateral arrangements

Government is concerned that the extension of security lending/collateral arrangements to other instruments, for example bonds, has little merit due to the fact that bonds are not subject to securities transfer tax and will only be subject to capital gains tax if and when bonds are traded in the secondary market at a capital gain. The value of bonds generally only increases when the market has low inflation or disinflationary expectations, which would see increased demand for fixed instruments such as bonds. The vast majority of bonds in South Africa are held until maturity, meaning that there will be no gains or losses at maturity, regardless of market conditions.

However, Government recognises that the use of government bonds as collateral is embedded in the financial markets industry and affects all its participants and transactions. Based on the above, the provisions of securities lending/collateral arrangement are extended to include listed government bonds. As a result, listed government bonds that are transferred as collateral, will qualify for the abovementioned special tax dispensation.

Effective Date

The amendments will come into operation on 1 January 2017 and apply in respect of any securities lending arrangement or collateral arrangement entered into on or after that date.

PERSONAL LIABILITY COMPANIES

[Applicable provision: Section 12E of the Act]

Background

In 2001, a special dispensation for qualifying business corporations was introduced. In order to qualify for the special dispensation, the entity had to meet the definition of a "small business corporation" as defined in the Act. The Act required that an entity qualifying as a small business corporation had to either be a close corporation or a company registered as a private company in terms of the then applicable Companies Act, 1973 (Act No. 61 of 1973). Furthermore, the scope of the definition of small business corporation was intentionally limited to curb the disguise of passive income and remuneration as business earnings. Such a disguise would otherwise have allowed persons rendering professional services to take advantage of the concessionary tax rates that apply to small business corporations instead of taxing the disguised passive income and remuneration at the normal company tax rate.

The limitation measure provides that an entity that has more than 20 per cent of its revenue receipts and accruals and capital gains being made up of passive income and income earned by the entity for rendering certain professional services which are performed by a person who holds an interest in the entity (i.e. personal services) could not qualify as a small business corporation.

In 2005 the abovementioned measure in respect of personal services was relaxed. As a result, entities that rendered personal services could

qualify as small business corporations provided that they employ at least three full-time employees who do not have an interest in the entity and are not connected persons (i.e. relatives) in relation to those that have an interest in the entity.

Reasons for change

In 2009, the new Companies Act, 2008 (Act No. 71 of 2008) was promulgated and is administered by the Department of Trade and Industry. Many provisions of the Act depended or referred to company law principles and definitions contained in the old Companies Act, 1973 (Act No. 61 of 1973). Over the past years' subsequent technical corrections have been made in the Act due to the commencement of the 2008 Companies Act in 2011.

It has come to Government's attention that amendments made to the provisions dealing with small business corporations as a result of the Companies Act No. 71 of 2008 did not adequately take into account some of the issues related to small business corporations, for example, under the 2008 Companies Act the definition of a private company expressly excludes a personal liability company. As the definition of a small business corporation in the Act includes a private company, the resultant anomaly is that personal liability companies which typically render personal services are currently automatically excluded from being small business corporations for tax purposes.

Amendment

To correct this anomaly created by the exclusion of personal liability companies from the definition of a private company in the 2008 Companies Act, personal liability companies should be expressly included in the definition of a "small business corporation" contained in the Act. However, these personal liability companies would be subject to the requirement to employ at least three full-time employees who do not have an interest in the entity and are not connected persons in relation to those that have an interest in the entity. This amendment will come into effect in line with the date that the 2008, Companies Act came into effect on 1 May 2011.

Effective date

The amendment is deemed to have come into operation on 1 May 2011 and applies in respect of years of assessment ending on or after that date.

INCOME TAX: BUSINESSES (FINANCIAL INSTITUTIONS AND PRODUCTS)

INTERACTION BETWEEN REITS AND SECTION 9C

[Applicable provisions: Sections 9C and 25BB of the Act]

Background

In 2007, section 9C was introduced in the Act which currently makes provision for amounts in respect of equity shares that are held for a period of at least three continuous years to be deemed to be of a capital nature.

Section 9C(5) provides that when the equity share, held for at least 3 years, is disposed of there must be included in the taxpayer's income any expenditure or losses allowed as a deduction in terms of section 11 in any previous year of assessment, provided that this subsection does not apply in respect of any expenditure or loss to the extent that the amount was recouped in terms of section 8(4)(a) or section 19.

Dividends received from a resident REIT or controlled company, as defined in section 25BB(1), are not exempt from tax in terms of paragraph (aa) of the proviso to section 10(1)(k)(i) but expenditure incurred to produce these taxable dividends and allowed as a deduction may be recouped on disposal of the equity shares in the REIT or controlled company.

Reasons for change

The current provisions of section 9C are inappropriate for equity shares in REITs and controlled companies that are residents. Dividends received from a REIT or a controlled company (as defined in section 25BB(1) that is a resident), form part of taxable income but allowable expenditure incurred to produce these taxable dividends that is recouped under section 9C(5) is then effectively not deductible. It is therefore proposed that a proviso be added to section 9C that subsection (5) does not apply to shares in a REIT or controlled company, as defined in section 25BB, that is a resident.

Amendment

In order to remove this anomaly, amendments are made in section 9C(5) to clarify that this section does not apply to shares in REITs or controlled companies that are residents.

Effective date

The amendment is deemed to have come into operation on 1 January 2016 and applies in respect of years of assessment ending on or after that date.

REITS - QUALIFYING DISTRIBUTION RULE

[Applicable provision: Section 25BB(1) of the Act, definition of "rental income"]

Background

As from 1 April 2013, a special tax dispensation for a listed company that is a Real Estate Investment Trust ("REIT") or a company that is a subsidiary of a REIT ("controlled company") that is a resident was introduced in section 25BB of the Act. Under this special tax regime, a REIT or a controlled company that is a resident is entitled to deduct from its income the amount of any "qualifying distribution" incurred during that year of assessment by that REIT or controlled company that is a resident. "Qualifying distribution" is defined in section 25BB of the Act to include any dividend declared or interest incurred in respect of a debenture forming part of a property linked unit by a REIT or a controlled company, during a year of assessment, if more than 75 per cent of the gross income received by or accrued to such REIT or controlled company consists of rental income.

Based on this specific tax dispensation of a REIT or controlled company, a REIT or controlled company is not entitled to claim specific allowances in respect of immovable property in terms of sections 11(g), 13, 13bis, 13ter, 13quat, 13quin, or 13sex of the Act.

Reasons for change

At issue is the fact that a REIT or controlled company that is a resident may have claimed the above-mentioned specific allowances in respect of immovable property before it become a REIT or a controlled company that is a resident. On disposal of such immovable property the general

recoupment provisions of section 8(4) of the Act will apply to a REIT or controlled company in so far as that entity claimed the above-mentioned allowances in respect of immovable property. In terms of paragraph (n) of the definition of gross income in section 1 of the Act, the REIT or controlled company that is a resident will therefore have to include the amount of recoupments in respect of allowances previously claimed in its gross income in the year of disposal. The inclusion of the amount of recoupment in the gross income of the REIT or controlled company could affect the 75 per cent rental income analysis for purposes of the qualifying distribution rule.

Example:

Facts:

The REIT or controlled company disposes of property A, on which it had previously claimed commercial building allowances of R30 million during the 2016 financial year. The REIT or controlled company earns rental income of R70 million during the 2016 financial year.

Results:
Based on current legislation

Gross income = R70 million + R30 million = R100 million

Rental income = R70 million

Qualifying distribution threshold = Rental income/Gross income = R70 million

R100 million = 70 per cent

The net effect is that a REIT or controlled company that is a resident will not qualify for the qualifying distribution deduction (75 per cent).

Amendment

In order to assist those REITs or controlled companies that are residents and that may have claimed the above-mentioned specific allowances in respect of immovable property before they obtained the status of a REIT or controlled company, the amount of recoupments in respect of allowances previously claimed must be included in the "rental income" definition of section 25BB and form part of the 75 per cent rental income analysis for purposes of the qualifying distribution rule.

The changes will only apply to those REITS or controlled companies that may have claimed the above-mentioned specific allowances in respect of immovable property before qualifying as a REIT or controlled company.

Effective date

The amendments are deemed to have come into operation on 1 January 2016 and apply in respect of years of assessment ending on or after that date.

SHORT-TERM INSURERS

[Applicable provision: Section 28(3) of the Act]

Background

Cell captive arrangements refer to cases where an insurance company enters into a contractual arrangement with a cell shareholder. Cell shareholders are generally companies that wish to self-insure their own risks (first-party cells) or their customers' risks (third-party cells) in a capital efficient way without the cost and regulatory burden of running a complete insurance company.

The insurance company pledges to provide insurance and financial management of the cell in exchange for a fee. This contractual arrangement includes access to an insurer's insurance licences and underwriting, reserving, reinsurance, claims management, actuarial investment and accounting services.

Under International Financial Reporting Standards (IFRS) 10, a standard on Consolidated Financial Statements, a cell can only be consolidated by the cell owner if it first meets the definition of "deemed separate entities". Cell captive insurers are not legally ring-fenced and therefore do not meet the definition of a "deemed separate entity".

IFRS 4 defines an insurance contract and the measurement of liabilities as dependent on the classification of contracts as an insurance or investment contract. Due to IFRS 10 standard and the fact that the shareholders agreement is read in conjunction with insurance contract, the impact is that first party cell arrangements are not recognised in the income statement (statement of profit or loss and other comprehensive

income).

Third party cell arrangements are recognised but the inclusion of cell underwriting profits and expenses do not impact the company's net results, as the result of cell activities that are transferred back to the cell owner (reinsured third party cell owner resulting in a nil profit for third party cell arrangements in the Income Statements).

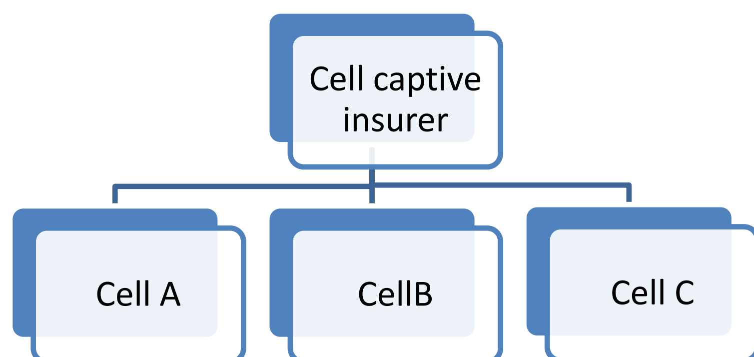
Reasons for change

In terms of IFRS 4, an insurance contract is defined as a contract when one party (the insurer) accepts significant insurance risk from another party (the policyholder) by agreeing to compensate the policyholder or other beneficiary if a specified uncertain future event (the insured event) adversely affects the policyholder or other beneficiary. Where there isn't sufficient insurance risk transfer, contracts are classified as investment contracts.

First party cell captive arrangements are arrangements where the cell shareholder and the policyholder are considered the same person. Where more than one contract is entered into with a single counterparty, it is considered to be a single contract, and the shareholder and insurance agreement are considered together for risk transfer purposes. As these contracts are a single contract there is no significant risk transfer and those cell captive facilities are accounted for as investment contracts.

The accounting effect of treating first party cell captive arrangements as investment contracts is that the net profit is excluded from the income statement (statement of profit or loss and other comprehensive income) and the insurance liabilities are excluded from the balance sheet (statement of financial position).

Currently, the cell captive insurance company reports on the total company's profit including cells for tax and for statutory reporting purposes however, in terms of IFRS the cells are excluded as stated above.



Amendment

All insurance contracts reported on in the audited annual financial statements of the short-term insurer as investment contracts that relate to short-term insurance business as defined in the Short-term Insurance Act for regulatory purposes should utilize section 28(3) but the effect of IFRS 4/IFRS 10 on the cell captive arrangement should be ignored.

Effective date

The amendments will come into operation on the date on which the Insurance Act, 2016, comes into operation and apply in respect of years of assessment ending on or after that date.

LONG-TERM INSURERS

[Applicable provisions: Section 29A(1); new subsections 14, 15 and 16 of section 29A of the Act]

Background

The insurance industry is undergoing changes to the manner in which it is regulated and the manner in which financial reporting will need to be done, due to the introduction of the Solvency Assessment and Management (SAM) framework and the anticipated standard for insurance

contained in International Financial Reporting Standards (IFRS), known as IFRS 4 Phase II. The current taxation method for determining taxable profits of a long-term insurer from insurance business is effectively based on transfers from the Untaxed Policyholder fund, Individual Policyholder fund, Company Policyholder fund and Risk Policy fund to the Corporate fund. The taxable profits are determined as the difference between the market value of the assets allocated to the policyholder funds and the value of the liabilities of these funds. The value of liabilities is currently calculated on the basis determined by the Chief Actuary of the Financial

Services Board (FSB) in consultation with the Commissioner for the South African Revenue Service. This basis of determination is based on the Statutory Valuation Method (SVM) with some adjustments.

In 2015, an announcement was made in the Budget Review to cater for the tax treatment of the long term insurance industry as a result of the introduction of the SAM Framework and the new Insurance Act, which will replace the current regulatory regime for the long term insurance industry. As a result, changes were proposed in the 2015 Draft TLAB that was released for public comment on 22 July 2015 and submitted to Parliament. During the parliamentary legislative process, Parliament recommended that due to the fact that the Insurance Bill enabling SAM still requires to be considered by Parliament, proposals relating to the tax treatment of long term insurers due to the introduction of SAM Framework should be removed from the 2015 TLAB and be considered in the 2016 TLAB.

Reasons for change

The introduction of the SAM framework will render the current adopted concept of the valuation of policyholder liabilities for tax purposes to be obsolete. More-over the SAM framework recognizes all future income on a policy upfront and is therefore not suitable as a basis for calculating tax where the Income Tax Act generally includes amounts in gross income when the income is received by or accrued to a taxpayer.

In addition, the International Accounting Standards Board is currently reviewing the policy liability valuation basis for long term insurers contained in IFRS and it is expected that the new IFRS 4 Phase II will only be effective for financial years commencing on or after 1 January 2020.

It is expected that that IFRS 4 Phase II will provide relevant and accurate recognition of insurance profit and insurance liabilities. The use of current IFRS to value long-term insurer's liabilities is in line with comparable country experience and practice. Effectively, the differences that currently exist between the valuation of liabilities on the statutory basis that is reported to FSB and the current IFRS basis that is reported by the insurer to shareholders in their audited financial statements will be significantly reduced. Furthermore, eventually there will be even greater alignment between insurers when they all apply IFRS 4 Phase II as a basis.

Amendment

In order to cater for the tax treatment of the long-term insurance industry as a result of the introduction of the SAM Framework and the new Insurance Act, the following is amended:

Definition of "value of liabilities"

Currently, the Act has two separate rules in the definition of "value of liabilities", one applicable to the Untaxed Policyholder fund, Individual Policyholder fund and Company Policyholder fund and the other one applicable only to the Risk Policy fund. There is no policy rationale to have two separate rules of "value of liabilities" one applicable to the risk policy fund and the other one applicable to the three policyholder funds. The definition of the "value of liabilities" sets out a single rule for both risk policy fund and the three policyholder funds and the current rule in the definition of "value of liabilities" applying to the three policyholder funds should be extended to apply to the risk policy fund.

Definition of "adjusted IFRS value"

Anew definition of "adjusted IFRS value" should be made applicable to both the risk policy fund and the three policyholder funds and will take into account the following:

The IFRS policy liabilities amount is net of reinsurance (gross amount of liabilities less reinsurance amount) determined in accordance with IFRS as annually reported in the audited financial statements. It should be stated that this IFRS policy liabilities amount takes into account cases where policyholder liabilities are determined and reported on a gross basis and a corresponding reinsurance asset is reflected as an asset in the annual financial statements. In this scenario, IFRS policyholder liabilities will be reduced by the amount reflected as a reinsurance asset (see examples for further clarification).

The IFRS policy liabilities amount is also net of negative liabilities (gross amount of liabilities less all negative liabilities irrespective of whether they are disclosed as a reduction of liabilities or as an asset) determined in accordance with IFRS as annually reported in the audited financial statements The amount of liabilities in respect of policies of the insurer net of reinsurance and negative liabilities is determined with reference to

the amounts disclosed in accordance with IFRS. The amounts disclosed in accordance with IFRS should be disaggregated in order to allocate the amounts to the relevant policyholder fund or risk policy fund. After the allocation, a single net amount of liabilities in respect of all policies allocated to a fund is determined.

If the determination under the previous three paragraphs results in a net “negative liability” the amount under paragraph (a) of the definition is limited to nil. The reason therefore is that the transfer mechanism under subsection (7) operates on the assumption that the value of liabilities cannot be a number less than zero. See examples for further clarification.

Although the “adjusted IFRS value” applies to the risk policy fund and the three policyholder funds, only the policyholder funds should include the deferred tax liabilities in respect of assets allocated to those funds in the “adjusted IFRS value”.

This stems from the fact that unrealised gains on assets allocated to the risk policy fund are not earned for the benefit of specific policyholders as in the case of policyholder funds under the trustee basis of taxation.

Transitional rules: Phasing in amount and period of phasing in

A phasing in amount and a phasing in period of 6 years are introduced as a transitional measure aimed at stabilising tax collections by SARS and reducing the financial impact on certain long term insurers due to these proposed changes. These rules are intended to cater for the difference in treatment of negative liabilities under the new regime (coming into effect when the Insurance Act of 2016 and SAM come into effect) and the previous rules, which applied before the coming into effect of the proposed definition of “adjusted IFRS value”, in so far as it relates to negative liabilities. Negative liability means the amount by which the expected present value of future receipts from a policy exceeds the expected present value of future claims and expenses in respect of a policy – effectively expected profit from a policy. This fixed amount representing the difference relating to policies allocated to a fund between the liabilities for tax purposes and the liabilities disclosed in the insurer’s published annual financial statements for 2016 will be phased in over a period of six years.

The amount of negative liabilities will be reduced by the negative liabilities that are recognized as an asset on the balance sheet (statement of financial position) by insurers that are in a net asset position (total negative liabilities exceeds total positive liabilities to policyholders). The reason for the exclusion is to avoid a significant negative impact on the liquidity of insurers that have a net negative liability for policies allocated to a specific tax fund.

Anti-avoidance measures for calculating the phasing in amount

The introduction of transitional rules is intended to stabilise tax collections by SARS and reduce the financial impact on certain long term insurers flowing from the treatment of negative liabilities. However, some insurance companies may change the manner of disclosure of negative liabilities for either or both tax and financial reporting purposes in 2016 in order to benefit from a deferral of tax payable as a result of the phasing in rules.

Negative liabilities as disclosed for tax and financial reporting in 2016 is adjusted to the manner of disclosure that applied in 2015.

Examples of calculating the phasing in amount:

Example 1

Facts:

Assuming the year of assessment ends after 30 June 2017 and after the Insurance Act, 2016, came into effect.

In respect of the 2016 year of assessment the accounting net liabilities in respect of policies were R100 (taking into account negative liabilities of R20). However, for reporting to shareholders, liabilities in respect of policyholders were disclosed as R104, which mean negative liabilities of R16 have been recognised. In 2016 for statutory reporting and also for tax purposes the value of liabilities was R120 – therefore no negative liabilities have been taken into account. It is assumed the manner of disclosure for financial reporting and tax reporting did not change from 2015 to 2016. The phasing-in amount is R16 (R16 – R0).

Results:

In respect of the first year of assessment after the Insurance Act, 2016 came into effect the new value of liabilities definition (without the phasing in) results in an amount of R110. After applying the phasing in rules the value of liabilities is R123.3= (R110 + (0.833 x 16)).

In respect of the second year of assessment after the Insurance Act, 2016 came into effect the new value of liabilities definition (without the phasing in) results in an amount of R125. After applying the phasing in rules the value of liabilities is R135.7 = (R125 + (0.667 x 16)).

In respect of the third year of assessment after the Insurance Act, 2016 came into effect the new value of liabilities definition (without the phasing

in) results in an amount of R150. After applying the phasing in rules the value of liabilities is R158 = (R150 + (0.5x 16)).

In respect of the fourth year of assessment after the Insurance Act, 2016 came into effect the new value of liabilities definition (without the phasing in) results in an amount of R165. After applying the phasing in rules the value of liabilities is R170.3 = (R165 + (0.333x 16)).

In respect of the fifth year of assessment after the Insurance Act, 2016 came into effect the new value of liabilities definition (without the phasing in) results in an amount of R180. After applying the phasing in rules the value of liabilities is R182.7 = (R180 + (0.167x 16)).

In respect of the sixth year of assessment after the Insurance Act, 2016 came into effect the new value of liabilities results in an amount of R200.

The negative liabilities have been fully phased in and no further adjustment applies.

Example 2

Facts:

Assuming the year of assessment ends after 30 June 2017 and after the Insurance Act, 2016, came into effect.

In respect of the 2016 year of assessment the accounting net liabilities in respect of policies were R80 (taking into account negative liabilities of R20). However, for reporting to shareholders, liabilities in respect of policyholders were disclosed as R94, which mean negative liabilities of R6 have been recognised. In 2016 for statutory reporting and also for tax purposes the value of liabilities was R82 – therefore R18 negative liabilities have been recognised. It is assumed the manner of disclosure for financial reporting and tax reporting did not change from 2015 to 2016.

The phasing-in amount is R12 (R18 – R6).

Results:

In respect of the first year of assessment after the Insurance Act, 2016 came into effect the new value of liabilities definition (without the phasing in) results in an amount of R110. After applying the phasing in rules the value of liabilities is R100 = (R110 – (0.833x 12)).

In respect of the second year of assessment after the Insurance Act, 2016 came into effect the new value of liabilities definition (without the phasing in) results in an amount of R125. After applying the phasing in rules the value of liabilities is R117 = (R125 – (0.667x 12)).

In respect of the third year of assessment after the Insurance Act, 2016 came into effect the new value of liabilities definition (without the phasing in) results in an amount of R150. After applying the phasing in rules the value of liabilities is R144 = (R150 – (0.5x 12)).

In respect of the fourth year of assessment after the Insurance Act, 2016 came into effect the new value of liabilities (without the phasing in) results in an amount of R165. After applying the phasing in rules the value of liabilities is R161 = (R165 – (0.333 x 12)).

In respect of the fifth year of assessment after the Insurance Act, 2016 came into effect the new value of liabilities (without the phasing in) results in an amount of R180. After applying the phasing in rules the value of liabilities is R178 = (R180 – (0.167 x 12)).

In respect of the sixth year of assessment after the Insurance Act, 2016 came into effect the new value of liabilities results in an amount of R200. The negative liabilities have been fully phased in and no further adjustment applies.

Effective date

The amendments in relation to adjustment to the definition of “value of liabilities” are deemed to have come into operation on 1 January 2016 and apply in respect of years of assessment commencing after that date.

Other amendments in relation to the tax treatment of long term insurers due to the introduction of SAM will come into operation on the date on which the Insurance Act, 2016, comes into operation and apply in respect of years of assessment ending on or after that date.

CONTROLLED FOREIGN COMPANIES RULES

[Applicable provision: Section 9D of the Act]

Background

Controlled Foreign Companies

The South African tax system has controlled foreign company (CFC) rules that are antiavoidance rules generally aimed at preventing South African residents from shifting tainted forms of taxable income offshore by investing through CFCs. The CFC rules make provision for the net income of a CFC to be attributed and included in the income of South African shareholders.

Section 9D of the Act defines a CFC as any foreign company where more than 50 per cent of the total participation rights in that foreign company are directly or indirectly held, or more than 50 per cent of the voting rights in that foreign company are directly or indirectly exercisable, by one or more persons that are residents other than persons that are headquarter companies.

Section 1 of the Act defines a foreign company as any company which is not a resident. In turn, the definition of a company in section 1 of the Act includes portfolios of foreign collective investment schemes in securities.

The amount of income which is included in the net income of a CFC is subject to various exemptions such as the foreign business establishment, high-tax and related party exemptions.

These exemptions seek to strike a balance between protecting the tax base and the need for South African multinational entities to be competitive.

Collective Investment Schemes

Paragraph (e)(ii) of the definition of a company in section 1(1) of the Act includes any portfolio of a foreign collective investment scheme that is comparable to a portfolio of a collective investment scheme in participation bonds and in securities in pursuance of any arrangement in terms of which members of the public are invited or permitted to contribute or hold participatory interest in that portfolio through shares, units or any other form of participatory interest.

A collective investment scheme is an investment vehicle used by investment managers to pool investors' funds to enable them to access investments which they might not otherwise be able to access in their individual capacities. In South Africa, collective investments schemes are generally established as vesting trusts, with investors in such schemes being the beneficiaries of the trust. The assets of a collective investment scheme portfolio are held by the trustees on behalf of the holders of participatory interests. The taxation of these vesting trusts holders of and participatory interests is regulated by section 25BA. These collective investment schemes are regulated by the Collective Investment Schemes Control Act. No 45 of 2002.

Reasons for change

When funds are invested in a collective investment scheme in participation bonds or in securities portfolio, an investor acquires a portion of the participatory interests in the total collective investment scheme in participation bonds or securities portfolio. In turn, investors get to share the risks and benefits of their investment in a collective investment scheme in securities or in participation bonds in proportion to the participatory interests in that scheme.

At issue is the application of the CFC rules in cases where the South African collective investment scheme in securities or in participation bonds invested in a global fund, which is a foreign fund. Concerns have been raised that as South African collective investment schemes in securities or in participation bonds invested in a global fund, South African collective investment schemes in securities or in participation bonds should be considered to be the direct holders of the participation rights in that global fund. On the other hand, there is an argument that as South African collective investment schemes in securities or in participation bonds are established as vesting trusts, the units in the global fund are beneficially owned by the investors in the South African collective investment schemes in securities or in participation bonds in proportion to their effective interests in such global fund.

In addition, there is uncertainty as to whether the global fund is comparable to a portfolio of collective investment scheme in securities or in participation bonds as envisaged in the abovementioned paragraph (e) (ii) of the definition of "company" of section 1(1) of the Act.

More specifically, the uncertainty arises in the determination of whether:

- The global fund can be regarded as a CFC;
- A South African collective investment scheme or investors in a South African collective investment scheme in securities or in participation bonds should be treated as holders of the participation rights in that global fund;
- A South African collective investment scheme in securities or in participation bonds or investors in a South African collective investment scheme in securities or in participation bonds should be considered to directly or indirectly to exercise voting rights in that global fund.

Amendment

In order to eliminate the uncertainty and potential double taxation described above, the following is amended:

- South African collective investment schemes in participation bonds or in securities investing in a global fund should be excluded from applying the CFC rules (section 9D) to investments made in that global fund;
- A South African collective investment schemes in participation bonds or in securities are established as vesting trusts, the conduit principle should apply when South African collective investment schemes in participation bonds or in securities invest in a global fund and that tax should ultimately arise in the hands of investors in the South African collective investment schemes in participation bonds or in securities in proportion to their effective interests in such global fund.

Effective date

The amendments will come into operation on 1 March 2017 and apply in respect of any foreign tax year commencing on or after that date.

HIGH TAX EXEMPTION IN RESPECT OF CONTROLLED FOREIGN COMPANIES

[Applicable provision: Section 9D(2A) of the Act]

Background

The 2009 tax legislative amendments introduced the CFC high-tax exemption. The purpose of the exemption is to disregard tainted CFC income, if little or no South African tax was at stake after taking into account the South African tax rebates.

The CFC will qualify for the high-tax exemption if it's net income as an aggregate is subject to foreign tax of at least 75 per cent of the amount of normal tax that would have been imposed had that CFC been fully taxed in South Africa.

The high-tax exemption is based on a calculation of a hypothetical amount of the global level foreign taxes imposed by all foreign spheres of government. The global foreign tax is calculated after disregarding foreign tax carryover and carry-back losses as well as group losses.

Reasons for change

Generally, the income tax does not allow foreign tax rebate on notional taxable income. However, in the calculation of the hypothetical amount of foreign taxes some CFCs within a group of companies that are in a loss making position benefit from the high tax exemption. This creates an anomaly because in these circumstances, no foreign tax is actually paid or payable by the CFC.

Example:

Facts:

SA Company, Co A owns all the shares in CFC 1, CFC 2 and CFC3 and CFC 4. All these four CFC's are resident in country Y. CFC 1 generates a loss of $ 100, CFC 2 generates a loss of $ 200, CFC 3 generates income of $ 1500 and CFC 4 generates a loss of $ 5000.

Results in Country Y

Country Y has group taxation provisions and the group of companies gets treated as a single entity for tax purposes, which is referred to as a fiscal unity. The result is that the profit of CFC3 will be offset with the losses of the three CFC's resulting in an overall loss of $ 3800. As a result, the fiscal unity does not get to pay any tax in country Y.

Results in South Africa

In terms of SA tax law, the net income of CFC 3 will be translated to a rand amount in order to be imputed into South African resident, Co A's

income. The high tax exemption calculation will then be performed in order to establish as to whether the income is exempt from imputation or not. The actual foreign tax imposed in country Y is at a rate of 25%. The comparison will be as follows:

- Net Income of CFC 3 - $1500 x 15 exchange rate = R22 500
- Tax deemed to be payable in county Y - R22 500 x 25% = R5 625
- SA Tax payable as if the CFC was a SA resident – R22 500 x 28%= 6300
- High tax exemption calculation =R5 625/R6 300 = 89%

Because the 89% is more than the 75% the R22 500 will be exempt from imputation.

The anomaly then arises because CFC 3 did not pay any tax in country Y as a result of the overall group loss. However in performing the high tax exemption, a notional tax of R5 625 is calculated as though the CFC paid tax in its country of resident.

In the absence of the high tax exemption no section 6quat tax rebate would have been granted to the controlled foreign company.

Amendment

In calculating the high tax exemption, the CFC will no longer use foreign group losses. The second part of paragraph 2(ii)(bb) of the proviso to section 9D(2A) dealing with group losses is deleted. However, the CFC will still be able to disregard its own foreign losses in the high tax exemption calculation. The CFC's own foreign losses to be disregarded will be limited to foreign losses arising from foreign tax years ending after that foreign company becomes a CFC.

Effective date

The amendments will come into operation on 1 January 2017.

TAX EXEMPTION OF MULTILATERAL DEVELOPMENT FINANCIAL INSTITUTIONS

[Applicable provisions: New section 10(1)(bC) and sections and 50D of the Act]

Background

After 1994, South Africa became a signatory to a number of agreements with multilateral development financial institutions. In this context, a multilateral development financial institution refers to a financial institution created by a group of countries that provides financing and professional advice for the purpose of development.

These institutions have large memberships including both developed donor countries and developing borrower countries. They finance projects in the form of long-term loans at market rates, very-long-term loans (also known as credits) below market rates, and through grants.

Multilateral development institutions provide financial assistance to developing countries in order to promote economic and social development. They primarily fund large infrastructure and other development projects and provide loans tied to policy reforms by the government.

In particular, the multilateral development financial institutions which South Africa has signed agreements with include the following; the World Bank, the International Monetary Fund, the African Development Bank, the European Investment Bank, the African Export-Import Bank and the New Development Bank (formerly known as the BRICS Development Bank). The agreements with these institutions provide for blanket exemptions from all taxes, including income tax, withholding taxes on interest and dividends, value added tax and capital gains tax.

Further, these institutions are also granted diplomatic immunity status in terms of the Diplomatic Immunities and Privileges Act 37, 2001 which gives the Minister of International Relations and Cooperation the power to, inter alia, grant immunities and privileges to any organization recognised by the Minister of the International Relations and Cooperation.

Reasons for change

Currently, section 10(1)(bA) of the Act makes provision for exemption from income tax in respect of all receipts or accruals of any institution or body established by a foreign government to the extent that that body or institution is appointed by that government to perform its functions in terms of an official development assistance agreement that is binding in terms of section 231(3) of the Constitution of the Republic of South Africa, 1996 (the Constitution). In addition, such official development assistance agreement must provide that the receipts and accruals of that institution or body are exempt from normal tax. This exemption is also extended to apply to multinational organisations providing foreign donor funding in terms of the official development assistance agreement that is binding in terms of the Constitution.

There is a disconnect between the current tax exemption provisions of the Act and the articles dealing with the tax treatment of these multilateral development financial institutions in the agreements signed by South Africa with these institutions. While these agreements provide for exemption of these multilateral development financial institutions from all taxes, the Act does not have a specific provision enabling the tax exemption of these multilateral developmental financial institutions.

Section 10(1)(bA) of the Act does not cover these multilateral development financial institutions because the application of the provisions of section 10(1)(bA) of the Act is limited only to institutions or bodies appointed by foreign governments to perform functions of such foreign government in South Africa in terms of an official development assistance agreement or to multinational organisation providing foreign donor funding in South Africa in terms of an official assistance development assistance agreement. On the other hand, the agreements signed by South Africa with these multilateral development financial institutions are not regarded as official development assistance agreements, hence they don't qualify for tax exemption in terms of the current provisions of section 10(1)(bA) of the Act.

The disconnect between the current tax exemption provisions of the Act and the articles dealing with the tax treatment of these multilateral development financial institutions in the agreements signed by South Africa with these institutions also extends to withholding tax on interest, that was introduced on 1 March 2015. According to these agreements, interest paid by South African residents to these multilateral development financial institutions is exempt from withholding tax on interest; however, the Act does not make specific provision for similar exemption in respect of withholding tax on interest.

Amendment

In order to take into account the spirit of these multilateral development financial institution agreements and in order to eliminate any potential confusion regarding the tax exemption status of these multilateral development financial institutions, the following is amended:

- The current income tax exemption applicable to institutions or bodies appointed by foreign government to perform functions in South Africa in terms of an official development assistance agreement or to multinational organisations providing foreign donor funding in South Africa in terms of an official assistance development assistance agreement, be extended to apply only to the following multilateral development financial institutions that South Africa has signed agreements with, namely, the World Bank, the International Monetary Fund, the African Development Bank, the European Investment Bank, the African Export-Import Bank and the New Development Bank.
- Since the main aim of these multilateral development financial institutions is to provide finance to specified projects in terms of the agreement signed with South Africa, interest paid by South African residents to the multilateral development financial institutions in terms of the agreement should be exempt from withholding tax on interest. The withholding tax on interest exemption will only apply to the following multilateral developmental financial institutions that South Africa has signed agreements with, namely, the World Bank, the International Monetary Fund, the African Development Bank, the European Investment Bank, the African Export- Import Bank and the New Development Bank.

Effective date

With regard to the amendment in respect of income tax exemption on receipts or accruals of the listed multilateral development financial institutions that South Africa has signed agreements with, the amendment will come into operation on the date of promulgation of the Taxation Laws Amendment Act, 2016.

On the other hand, with regard the amendment in respect of withholding tax on interest exemption in respect of interest paid by South African residents to the listed multilateral development financial institutions that South Africa has signed agreements with, the amendment is deemed to have come into operation on 1 March 2015 and applies in respect of interest that is paid or becomes due and payable on or after that date.

BAD DEBT DEDUCTION RULE ON EXCHANGE DIFFERENCES

[Applicable provision: Insertion of new section 24I(4) of the Act]

Background

Section 24I was first introduced in the Act in 1993 to deal comprehensively with all aspects of foreign exchange gains and losses in relation to debts due to or by the taxpayer, as well as forward exchange contracts and foreign currency option contracts. The purpose of this section is to achieve simplicity, fairness, economic reality, and a realignment of the tax rules with International Financial Reporting Standards.

Section 24I requires that a gain or loss on a foreign exchange transaction be included in or deducted from the income of a taxpayer carrying on a trade within the Republic, if that exchange difference arose from a transaction entered into by that taxpayer in the course of that trade. In

essence, the section taxes all gains and losses, whether realised or unrealised relating to any foreign exchange transactions entered into by the taxpayer over the period of the transaction. An exchange difference is determined only in respect of an "exchange item" as defined in section 24I(1).

Reasons for change

Currently, exchange differences arising on a foreign currency denominated loan by a South African taxpayer, who is not a money-lender to another person are taken into account in the determination of a taxable income as either an inclusion of deduction.

However, where that loan becomes bad, a taxpayer is not allowed to claim a deduction in terms of section 11(a) of the Act in relation to the exchange gains that were included in the income.

The loss reflects a loss of fixed capital rather than floating capital. Further, a taxpayer is not allowed to claim a deduction under section 11(i) of the Act because the amount of the debt, being the foreign currency denominated amount, was not included in income. Consequently, the current tax provisions do not give a taxpayer any relief in relation to irrecoverable amounts on which it has been subjected to tax.

The following examples illustrates this current situation as well as the results of the new section 24I(4).

Example 1:

Facts

Company A, a South African resident, sold R100 stock on credit to Company B, a USA resident on 1 January 2015.

Company A has a 31 December year end. The exchange rates on the respective dates were as follows:

- 1 January 2015: R1=$14
- 31 December 2015: R1=$16
- 31 December 2016: R1=$12

The debt was written off as bad debt on 31 December 2016.

Results: Company A

First year of assessment: 31 December 2015

1 January 2015: Gross Income (100*14) R1 400

31 December 2015: Foreign exchange gain [(14-16)*100)] R200

Second year of assessment: 31 December 2016

Foreign exchange loss [(16-12)*100)] (400)

Deduction under section 11(i) (12*100) (1 200)

In determining Company A's taxable income; the debt fell within the ambit of section 11(i) and the net inclusion in taxable income for both years of assessment of R nil (R1400+R200-R400-R1200) reflects the correct outcome. In this example, there was no anomaly created because the debt was included in income, and as a result, foreign exchange gains and losses arising as a result of that debt are deducted in terms of section 11(i).

Example 2

Facts

Company A, a South African resident advanced a loan of R100 to Company B, a USA resident on 1 January 2015. The loan is of a capital nature from Company A's perspective. At the end of the second year of assessment it was clear Company B would not be able to repay the loan and Company A wrote the loan off as bad on 31 December 2016. The rates at the respective dates were as follows:

- 1 January 2015: R1=$14
- 31 December 2015: R1=$16
- 31 December 2016: R1=$12

Results: Company A

Current section 24I provisions

First year of assessment: 31 December 2015

1 January 2015: No entry in gross income as the loan is of a capital nature for company A

Foreign exchange gain included in income under section 24I(3)(a)

[R100 x (14-16)] = R200

Second year of assessment: 31 December 2016

Foreign exchange loss deducted from income under section 24I(3)(a) [R100 x (16-12)] = R400

In this example, Section 11(i) is not applicable as the loan was never included in Company A's income. Company A will not be able to deduct the previous foreign exchange gains included in income of R200. Company A will furthermore, not be able to include in its income the foreign exchange losses deducted from income of R400.

The new amendments to section 24I seek to address this anomaly, and as a result, in applying the new provisions of section 24I(4), the implications to Company A will be as follows:

New Section 24I(4) provisions

Deduction of previous foreign exchange gains included in income under section 24I(4)(a) = R200

Inclusion in income of previous foreign exchange losses deducted from income under section 24I(4)(b) = R400.

Example 3

Facts

Company A, a South African resident advanced a loan of R100 to Company B, a USA resident on 1 January 2015. The loan is of a capital nature from Company A's perspective. Company B repaid R40 of the debt on 31 December 2015. At the end of the second year of assessment it was clear Company B would not be able to repay the balance of the loan of R60. Company A wrote the balance of R60 off as bad on 31 December 2016. The exchange rates at the respective dates were as follows:

- 1 January 2015: R1=$14
- 31 December 2015: R1=$16
- 31 December 2016: R1=$12

Results: Company A

First year of assessment: 31 December 2015

Foreign exchange gain included in income under section 24I(3)(a) on realisation of part of the debt [R40 x (14-16)] = R80

Foreign exchange gain included in income under section 24I(3)(a) on translation of the balance of the debt of R60 [R60 x (14-16)] = R120

Second year of assessment: 31 December 2016

Foreign exchange loss deducted from income under section 24I(3)(a) [R60 x (16-12)] = R240

Deduction of previous foreign exchange gains included in income under section 24I(4)(a) = R120

Inclusion in income of previous foreign exchange losses deducted from income under section 24I(4)(b) = R240*

Section 24I(4) is only applicable to the extent that the debt has become bad and therefore under the new section 24(4)(a) and (b) the deduction from income of current and previous exchange gains included income and the inclusion in income of current and previous exchange losses deducted from income is calculated with reference to the balance of the debt of R60 which went bad.

Exchange differences which arose under section 24I on the portion of the debt which has been realised are not relevant under section 24I(4).

Section 11(i) will not be applicable as the loan was never included in Company A's income.

Amendment

In order to provide relief in relation to exchange differences that are included in or deducted from income the provisions of section 24I of the Act is extended to apply to any exchange difference in respect of a debt that has been included in or deducted from income during the year of assessment, provided that the debt has gone bad.

Effective date

The amendments will come into operation on 1 January 2017 and apply in respect of years of assessment ending after that date.

INTEREST WITHHOLDING TAX WHERE INTEREST IS IRRECOVERABLE

[Applicable provision: Part IVB of Chapter II of the Act: Section 50G of the Act]

Background

On 1 March 2015, a withholding tax on interest was introduced. The withholding tax on interest applies in respect of interest paid by a South African resident to or for the benefit of any foreign person to the extent that the interest is from a South African source. The final withholding tax is levied at a tax rate of 15 per cent of the amount of the interest paid to a foreign person.

However, the withholding tax is subject to some exemptions.

The withholding tax on interest rules have deeming provisions and deems interest to be paid on the earlier of the date on which the interest is actually paid or becomes due and payable.

Reasons for change

In circumstances where interest withholding tax is paid on interest that becomes due and payable, but the interest subsequently becomes irrecoverable, there is no mechanism for SARS to refund the interest withholding tax already paid. For example, if a foreign person provides unsecured interest-bearing loan to a South African resident, withholding tax on interest is paid monthly on interest that accrues to that foreign person monthly if that interest becomes due and payable monthly. The interest is for the purposes of determining the tax liability therefore deemed to have been paid.

If either the foreign person or the withholding agent pays the tax in respect of the interest that is deemed to have been paid for tax purposes, there is currently no mechanism available for the person that paid the tax to obtain relief for the tax paid on interest that becomes irrecoverable at a later stage. This contrasts with the approach in respect of income tax where, if the foreign person had been a taxpayer in South Africa, that foreign person would have paid income tax on accrued interest. However, the foreign person would have been able to claim a deduction in terms of section 11(i) of the Act in respect of any irrecoverable interest.

Amendment

To provide relief in cases where interest withholding tax is paid on interest that becomes due and payable, but is not actually paid, the tax will be refunded to the person that paid it if that interest becomes irrecoverable.

Effective date

The amendment is deemed to have come into operation on 1 March 2015.

REPEAL OF THE WITHHOLDING TAX ON SERVICES FEES REGIME

[Applicable provisions: Part IVC of Chapter II and Sections 51A to 51H of the Act]

Background

In the 2013 Budget Speech, the Minister announced and introduced a withholding tax on crossborder services. This withholding tax is a final tax in respect of fees payable by a resident to a non-resident for technical, management and consulting services rendered by that non-resident to a resident. The main aim of the introduction of this withholding tax was to identify and collect revenue from non-resident taxpayers who provide technical, management or consulting services and earned fee income from a South African source. It was also aimed at preventing the potential for the erosion of the South African tax base.

The tax rate for the withholding tax on services is 15 per cent of the gross amount of fees paid to a non-resident (subject to tax treaty relief). The

liability to withhold the tax is with the payor of the service fees to or for the benefit of the non-resident taxpayer.

Reasons for change

In June 2015, SARS issued a draft public notice listing a reportable arrangement in terms of section 35(2) of the Tax Administration Act No. 28 of 2011 for public comment. This dealt with arrangements in terms of which certain service fees are paid by a resident to a non-resident. On 3 February 2016, SARS issued in Notice 140 of the Government Gazette no 39650 a revised list of reportable arrangements. According to this Notice an arrangement for the rendering of consultancy, construction, engineering, installation, logistical, managerial, supervisory, technical or training services to a South African resident or a non-resident having a permanent establishment in South Africa, in terms of which arrangement a non-resident was, is, or is anticipated to be physically present in South Africa in connection with or for purposes of rendering the services and the expenditure incurred or to be incurred in respect of the services exceeds or is anticipated to exceed R10 million, is a reportable arrangement in terms of the Tax Administration Act provided that it does not qualify as 'remuneration' for employees' tax purposes.

If the reportable arrangement regime were to be applied concurrently with the withholding tax on services regime, it would have resulted in additional administrative functions for SARS and a compliance burden for taxpayers. The two regimes are virtually aimed at achieving the same goal (i.e. identifying and collecting revenue from non-resident taxpayers who provide technical, management or consulting services).

Further, concerns have been raised that the application of withholding tax on services regime will give rise to uncertainty on the application of domestic tax law and limited revenue due to limited taxing rights under tax treaties.

Amendment

In view of the above the withholding tax on services was repealed from the Act. Therefore, payment of certain service fees by South African residents to non-residents will now be dealt with under the provisions of Reportable Arrangements in the Tax Administration Act.

Effective date

The amendment will come into operation on 1 January 2017.

INCOME TAX: BUSINESSES (INCENTIVES)

CLARIFYING THE TAX TREATMENT OF GOVERNMENT GRANTS

[Applicable provision: Paragraph (lC) of the definition of "gross income" in section 1 of the Act]

Background

A uniform regime for the taxation of government grants was introduced under section 12P of the Act in 2012. Under this uniform regime, government grants can only be exempt if they form part of the comprehensive legislative list set out in the Eleventh Schedule or they are specifically identified by the Minister of Finance by notice in the Government Gazette as a mechanism to cater for grants originating in the middle of a legislative cycle for which there will be a delay in listing them in the Eleventh Schedule. These two mechanisms were introduced to ensure that the key determinations to be observed when seeking to exempt any government grant are properly considered. The intention is that these mechanisms would ensure that only genuine grants and not some forms of disguised consideration or transfer paid for or in exchange for goods and services required by Government would be exempt and that the financial and tax implications were borne in mind when deciding to grant an exemption.

Reasons for change

Under the current dispensation, a government grant that is neither listed in the Eleventh Schedule nor identified by the Minister in the Government Gazette may still avoid being taxed.

This arises as a result of the grant falling outside the definition of "gross income" because that grant is meant to subsidise the procurement or acquisition of capital assets and is thus capital in nature.

Proposal

It is proposed that the legislation should be clarified and aligned in accordance with normal tax practices applicable to taxable receipts. Firstly, the amount must be included in the "gross income" of the recipient. Any exclusion from tax should be made on the basis of a special exemption granted in terms of section 12P read together with the Eleventh Schedule to the Act.

The proposed inclusion in "gross income" for all government grants will be included under a new paragraph (lC) of the definition of "gross income".

Effective date

The amendments will apply to all grants received or accrued on or after the date of promulgation of the Taxation Laws Amendment Act, 2016.

NATIONAL HOUSING FINANCE CORPORATION

[Applicable provisions: Sections 10(1)(t) and section 30(3)(b) of the Act]

Background

The Department of Human Settlements is currently consolidating all its Human Settlement Development Finance Institutions, namely, the National Housing Finance Corporation (NHFC), National Urban Reconstruction and Housing Agency (NURCHA) and the Rural Housing Loan Fund (RHLF) under one entity, namely, the NHFC, which is wholly owned by Government.

Currently, NURCHA and RLHF qualify as Public Benefit Organisations (PBOs) in terms of the Act and are exempt from normal income tax. On the other hand, NHFC is a taxable entity.

Reason for Change

The existing different tax treatment of Human Settlement Development Finance Institutions creates difficulties, more especially during consolidation. Before consolidation, the activities were performed by two entities (NURCHA and RHLF), which are tax exempt. After consolidation, the same activities will be performed by one entity (NHFC), which is not exempt from tax.

In turn, the consolidation of functions into one entity requires the transfer of assets and liabilities from the aforementioned two tax exempt entities to this single taxable entity, which triggers a tax charge. Given that these activities qualify as public benefit activities and were tax exempt before consolidation, consolidation should not deter public benefit activities that qualify for tax exemption.

Amendment

The Human Settlement Development Finance plays a key role in improving the delivery of adequate housing to the needy. It is proposed that the receipts and accruals of NHFC should be exempt from tax in terms of section 10(1)(t) of the Act.

In order to allow for tax neutral transfer of assets and liabilities from NURCHA and RHLF to NHFC, a further amendment is made to section 30(3)(b) of the Act.

Effective Date

The amendments are deemed to have come into operation on 1 April 2016 and apply in respect of receipts and accruals on or after that date.

RESEARCH AND DEVELOPMENT (R&D) INCENTIVE PRESCRIPTION RULES

[Applicable provisions: Section 11D of the Income Tax Act 58 of 1962 and section 93 of the Tax Administration Act 28 of 2011]

Background

The income tax system contains an incentive for research and development to promote R&D related job opportunities and economic growth in South Africa. The tax incentive is in the form of a 150 per cent deduction for non-capital R&D expenditure. Taxpayers seeking to benefit from this allowance are required to obtain pre-approval from the Minister of Science and Technology, who in turn decides whether to provide such approval based on the findings of a committee set up for this purpose. Management and administration of the pre-approval committee is essentially done by the Department of Science and Technology (DST), although the committee comprises people sourced from the DST, National Treasury and SARS.

Since inception of the R&D pre-approval system in 2012, the pre-approval adjudication committee has experienced teething, administration and capacity problems. These setbacks have led to delays and substantial backlogs in the processing of applications. The backlogs have resulted in calls by taxpayers and tax practitioners for a task team to be appointed to make recommendations on how the R&D tax incentive could be improved. The Minister of Science and Technology responded to these calls and appointed such a task team, consisting of expert representatives from academia, government and the private sector. The task team has completed its mandate and has provided the Minister of Science and Technology with its findings.

Reason for change

Amongst the issues raised by the task team was that delays in processing approvals could cause assessments to prescribe before an application is adjudicated upon. This situation is exacerbated because SARS has made it clear that submission of income tax and provisional tax returns should not be delayed pending pre-approval by the R&D committee. Further, taxpayers have been advised that when submitting such returns, they should not assume a successful preapproval as wrongfully doing so could result in them being subject to the imposition of interest and penalties.

Example:

Facts:

Company X has a 30 June year end. On 1 November 2012, Company X submitted a proposed research and development project to DST for preapproval. On 1 August 2013 Company X submitted its return to SARS for assessment and was duly assessed on that day (company has until 30 June 2014 to submit its return). In submitting its return the taxpayer claimed certain R&D expenditure to the value of R1, 000,000 (incurred between November 2012 and 30 June 2013). On 10 August 2016, the DST approved the pre-approval application of 1 November 2012.

Results:

At the time of submitting the tax return, the taxpayer did not claim an additional R500,000, which it anticipated it would be entitled to once its R&D project was approved by the Minister of Science and Technology. Given the approval date by DST on 10 August 2016, which is more than three years after the date of assessment, the taxpayer wanted to re-open its 2013 tax return to include a claim for an additional allowance of R500,000. Since the authority to revise an assessment prescribes three years after a tax return has been assessed, the taxpayer has lost the benefit of the R&D allowance. In this case the taxpayer's return would have already been prescribed by 1 August 2016 before receiving the decision from DST.

Amendment

An amendment was made to section 11D to allow for a re-opening of assessments in the circumstances outlined above.

Effective date

The amendment is deemed to have come into operation on 1 October 2012 and applies in respect of expenditure incurred in respect of research and development on or after that date, but before 1 October 2022.

INDUSTRY POLICY PROJECTS

[Applicable provision: Section 12I of the Act]

Background

Section 12I of the Act allows taxpayers an additional investment and training allowance in respect of industrial policy projects provided that the projects meet certain criteria prescribed by way of regulation. The additional investment allowance ranges from 35 per cent to 100 per cent of the cost of any new and unused manufacturing assets used for the project, depending on whether the project has qualifying status or preferred status, and whether the project is located in an industrial development zone (or designated special economic zone).

The additional investment allowance also has specific legislative requirements that requires the asset:

- To be owned by the company claiming the additional allowance;
- To be used for the furtherance of the industrial policy project carried on by that company;
- To have been acquired and contracted for on or after the date of approval of the relevant project as an industrial policy project; and
- Was brought into use within four years from the date of approval of the relevant project as an industrial policy project.

Reasons for change

Status change of project

The current provisions of section 12I(12) only envisages the withdrawal of project approval when the company fails to comply with any requirements as set on approval. It, however, does not account for the situation where the project was initially approved on preferred status, but the project status subsequently changes and becomes a qualifying status project by the end of the compliance period.

For example, the project may have scored 7 out of 8 points upon project approval and qualified as a preferred status project, but by the end of the compliance period, the project only scores 6 out of 8 points and is regarded as a qualifying status project. In this example, the approved project may not be disqualified as it still meets the minimum requirements for an approved industrial policy project, i.e. qualifying status project. Nonetheless, if it does not meet the scoring criteria for a preferred status project by the end of the compliance period, it should not be allowed to claim the preferred status allowance of either 55 per cent or 100 per cent of the cost of any new and used manufacturing assets, depending on whether the project is located within a special economic zone or not.

The risk to the fiscus is that the project which was approved as a preferred status but changes to a qualifying status before the end of a compliance period could be claiming a larger allowance value than it is allowed to claim, thereby reducing revenue collection over that period. This is a gap in the current legislation which needs to be addressed, because there is a risk that this may happen more frequently as many more projects near the end of the compliance period.

Extending period to bring assets into use

Given the estimates used at the approval stage and the nature of these large-scale manufacturing projects, start-up delays are a distinct possibility. In this regard the legislation does allow the Minister of Trade and Industry the discretion to extend the period within which assets are required to be brought into use, after taking into account the recommendations of the adjudication committee. Current legislation contains a technical oversight in that the relevant discretionary enabling legislation does not extend to certain other provisions in the section. There is no policy rationale for the Minister's discretion in this regard to not extend to all the relevant provisions.

Amendment

Status change of project

Section 12I is amended to enable SARS to recoup the difference in allowance claimed in respect of a project which was approved as a preferred status but changes to a qualifying status by the end of the compliance period. If a project was initially approved on preferred status and claimed

allowances on that basis, but by the end of the compliance period the project only reaches qualifying status, the Commissioner must substitute the preferred approval with that of a qualifying approval. To recognise the impact that the change in status could possibly have on historic provisional tax return the excess value claimed should be recouped from the taxpayer in the year of assessment that the Commissioner, after taking into account the recommendations of the adjudication committee, makes the decision to substitute the statuses and not the year that the Minister identifies as the year of assessment that the change effectively occurred.

Extending period to bring asset into use

The discretion contemplated in section 12I(19)(a) should be extended to also include a reference to subparagraph (7)(c) of the same section.

Effective date

The amendments come into operation on the date of promulgation of the Taxation Laws Amendment Act, 2016.

EXTENSION OF THE LEARNERSHIP TAX INCENTIVE

[Applicable provision: sections 12H of the Act]

Background

The Learnership Tax Incentive was introduced to encourage skills development and job creation, by providing an additional tax deduction for formal, SETA-registered training programmes.

Reasons for change

The review of the programme indicated that the incentive delivers on its objectives where it is accessible to employers and training programmes are relevant to needs of employers. Claims are not evenly spread across sectors. Sectors with high uptake are sectors where SETAs are perceived to administer training programmes effectively.

In its current form, the incentive will only be available for learnership registered before 1 October 2016. An extension will require legislative amendment.

The current design targets all skills levels equally. The economic situation and skills development priorities have shifted since, and government support should target workers that are most vulnerable to unemployment due to a lack of relevant qualifications.

Amendment

The amendment provides for the continuation of the programme until a sunset date of 31 March 2022.

The values of the claims are adjusted to target the incentive to crucial training, in line with DHET policies. While all registered learnerships will still qualify for the incentive, our proposed targeting prioritises learners without basic to intermediate qualifications by providing a higher value of claims. The prior qualifications of the learner entering the learnership agreement will determine the value of the claim.

Table 1: New Learnership Tax Incentive claim values:

Type of person	Qualification	Proposed	Current
Person without disability	NQF 1 - 6	R 40 000	R 30 000
	NQF 7 - 10	R 20 000	R 30 000
Person with disability	NQF 1 - 6	R 60 000	R 50 000
	NQF 7 - 10	R 50 000	R 50 000

To augment the future evidence base for policy evaluation, National Treasury and the SARS are discussing the most appropriate mechanism to collect more information on claims and learners. The intention is to make reporting compulsory for claimants of the learnership tax incentive.

Effective date

The amendments are deemed to have come into operation on 1 October 2016 and apply in respect of learnership agreements entered into on or after that date.

VENTURE CAPITAL REGIME FOR START-UP VENTURE CAPITAL COMPANIES

[Applicable provision: Section 12J of the Act]

Background

To encourage equity funders to invest in small businesses, the venture capital company (VCC) regime was introduced in 2008. Taxpayers investing in a VCC generate an upfront deduction for the investment (whereas most equity investments are non-deductible) with a recoupment upon withdrawal if the investment is not held for a minimum of five years.

The VCC has several sets of requirements including investor-level requirements for the allowable deduction in the hands of the investor. Included in the investor-level requirements is a connected person test provision (connected persons do not qualify for the VCC tax deduction) that ensures that a taxpayer cannot obtain a deduction merely by recycling funds among closely connected parties (as opposed to obtaining a new independent investment).

Concerns have been raised that at the initial stages of finding investors for a VCC, it may transpire that only a limited number of investors are able to provide seed funding. This could mean that these initial investors hold more than 20 per cent shares in the VCC, which could potentially put them in breach of the investor level requirements of the VCC. Due to the timing issues typical of start-ups like new VCC's, initial anchor investors risk not meeting the investor level requirements. As a result, VCC's have indicated that several potential large investors have opted out of the VCC initiative, making it less likely that smaller investors will come on board as well.

Reasons for change

The current VCC regime makes provision for investors to obtain a tax deduction in respect of any expenditure incurred in acquiring shares in a VCC, subject to various limitations. At issue is the limitation imposed by the connected person test. The connected person test defines any person holding 20 per cent or more of shares in a company at the end of any year of assessment as connected. This connected person test provides that no deduction will be granted to taxpayers who acquire shares in a VCC, where immediately after the acquisition the taxpayer is a connected person in relation to the VCC. Currently, the Act makes provision for the connected person test to be performed at the end of every year of assessment of the VCC.

In an already challenging economic environment, it is believed that the additional risks associated with the application of the connected person test will prevent many VCC's from raising capital.

Amendment

Timing of the connected person test:

The connected person test must first be performed 36 months after the first shares are issued by the VCC and where after it is performed at the end of every year of assessment.

By only performing the first connected person test after 36 months from first shares being issued, it should enable the VCC's to find additional start-up/angel investors, and give them more flexibility in terms of when they issue the shares in the start-up phase of the VCC.

Anti-avoidance:

To address the concerns raised with regard to potential abuse regarding the proposed timing of the connected person test, the following amendments were made:

Initial connected person test

Should any taxpayer who is an investor in a VCC be a connected person in relation to that VCC, with effect from the day after the 36 months from the date of the first issue of shares expired and after due notice to the VCC by the Commissioner:

- The Commissioner must withdraw the approval of that company as a VCC, if corrective steps acceptable to the Commissioner are not taken by the company within a period stated in the notice; and
- The VCC must include an amount equal to the expenditure incurred (which qualified for a deduction) for the issue of those shares held in that venture capital company in the income of that VCC during the year of assessment in which approval is withdrawn.

Subsequent connected person test

Should any taxpayer who is an investor in a VCC or any person that incurs expenditure to acquire any share in a VCC be a connected person in

relation to that VCC, during any year of assessment after the 36 months from the date of the first issue of shares expired and after due notice to the VCC by the Commissioner:

- The Commissioner must withdraw the approval of that company as a VCC, if corrective steps acceptable to the Commissioner are not taken by the company within a period stated in the notice; and
- The VCC must include an amount equal to the expenditure incurred (which qualified for a deduction) for the issue of those shares held in that venture capital company in the income of that VCC during the year of assessment in which the approval is withdrawn.

Effective date

The amendments will come into operation on 1 January 2017.

SMALL BUSINESS CORPORATIONS LOCATED IN SPECIAL ECONOMIC ZONES

[Applicable provision: Section 12R of the Act]

Background

In 2013, the Department of Trade and Industry (DTI) together with the National Treasury proposed the introduction of special economic zones (SEZs) regime. The SEZ regime was intended to replace the Industrial Development Zones (IDZs) regime with the aim to further promote investment, growth and job creation in the South African manufacturing sector and the development of selected key zones. The SEZ regime (which will apply to the current IDZs and any newly designated zones approved by the Minister) differs from the IDZ regime in that it expands on the value-added tax and customs duty relief that are applicable within customs controlled areas in the IDZs. This expansion under the SEZ regime includes normal income tax incentives that will encourage higher levels of investments into the designated zones.

Reasons for change

For normal tax purposes, companies that qualify for the incentives under the SEZ regime will be taxed at a more favourable rate of 15 per cent and are also eligible for an accelerated capital allowance on buildings built within a designated SEZ. However, the current provisions of the Act that provide for these incentives do not provide clarity on the tax rates applicable in the instance that the qualifying company is a small business corporation as defined in section 12E of the Act.

At issue is that the current provisions of the SEZ incentives provide only for a flat tax rate of 15 per cent while section 5(2) and the annual Rates and Monetary Amounts and Amendment of Revenue Laws Acts provide for concessionary tax rates which follow a graduated marginal structure (0 per cent, 7 per cent, 21 per cent and 28 per cent). In instances that the small business corporation would have been taxed at an effective rate that is lower than 15 per cent, the flat rate of 15 per cent would not be advantageous. In addition, it is currently not clear in the legislation which rate should apply in the instance that the small business corporation would have been taxable at an effective rate that is higher than 15 per cent (for example 21 per cent or 28 per cent).

Amendment

A small business corporations located within an SEZ should be able to benefit from the lower effective tax rate that they would otherwise qualify for under the graduated marginal structure and should, furthermore, also be able to benefit from the flat rate of 15 per cent in the instance that their effective tax rate would have exceeded the flat rate of 15 per cent. As such, a small business corporation will be subject to tax at the flat rate of 15 per cent or the effective rate determined in terms of the graduated marginal structure, whichever is the lower.

It should be noted that there is no policy change regarding qualifying companies that are currently excluded from benefiting from the preferential tax rates as a result of their activities.

Effective date

These amendments are deemed to have come into operation on the date on which the Special Economic Zones Act, 2014 (No. 16 of 2014) came into operation. The rates applicable are reflected in the 2016 Rates and Monetary Amounts and Revenue Laws Amendment Act.

SUPPORTING INFRASTRUCTURE USED IN PRODUCING RENEWABLE ENERGY

[Applicable provision: Section 12U of the Act]

Background

South Africa as a party to the United Nations Framework Convention on Climate Change (UNFCCC) aims to reduce greenhouse gas (GHG) emissions and to incentivise investments in low carbon, clean energy. Renewable energy is prioritized by government as a viable alternative to the current carbon–intensive economy. Since 2005 targeted incentives for renewable energy have been introduced through the provisions of the Act.

Reasons for change

Currently, large scale renewable energy projects are not adequately catered for under the existing accelerated depreciation regime due to the capital-intensive nature of supporting infrastructure whose tax treatment would need to be specifically targeted. Capital expenditures that indirectly support renewable electricity production, such as the construction of fences and roads, do not qualify for deductions under the Act. According to industry, this is one of the limitations that influence the viability of most large-scale renewable energy projects.

Amendment

The provisions of the Act is broadened to include the supporting capital infrastructure in the form of capital expenditure actually incurred on roads and security fences for large scale renewable energy projects as follows:

Renewable energy projects qualifying for deductions:

Only large scale renewable energy projects that generate electricity exceeding 5MW will qualify. Current evidence suggests that renewable energy projects within the band of 5 – 50MW are barely economically viable and as such this proposed incentive will assist in increasing the financial viability. The proposed amendment further took into account that the majority of renewable energy projects approved under the auspices of the Renewable Energy Independent Power Producers Procurement Programme of the Department of Energy currently exceed 5MW.

Timing of proposed deduction:

Should the renewable energy production supporting capital infrastructure expense be incurred pre-commencement of trade, then similar to section 11A of the Act which provides for certain pre-trade expenditure to be allowed as a deduction, the capital expense will have to be:

- Actually incurred prior to the commencement of and in preparation of carrying on that trade; and
- Not have been allowed as a deduction in that year or any previous year of assessment.

Roll over:

The envisaged allowable supporting infrastructure capital expenditure that exceeds the taxable income to the specific trade of the production of renewable energy in any year of assessment can be rolled-over as an allowable capital expenditure during the next succeeding year of assessment against income specific to the trade of the production of renewable energy.

Effective date

The amendments are deemed to have come into effect on 1 April 2016 and apply in respect of years of assessment commencing on or after that date.

URBAN DEVELOPMENT ZONES (USZ)

[Applicable provision: Section 13quat of the Act]

Background

The urban development zone tax incentive was designed to encourage property investment in central business districts i.e. areas with high population carrying capacity and developed infrastructure for transport. The principal objective of the incentive is to address dereliction and dilapidation, and promote urban renewal by stimulating investment in the construction and renovation of commercial and low cost residential buildings. The incentive is in the form of an accelerated depreciation allowance under section 13quat of the Act. The incentive is aimed at promoting investment in 16 designated inner cities, 15 of which now have demarcated UDZs within its boundaries. The incentive was initially available from January 2004 until March 2014, where after a review of its effectiveness it was extended to March 2020.

In 2015, changes were made in the Act to allow municipalities with a population of 1 million demarcate an additional UDZ area. Furthermore, where the municipality's population is below 1 million, the Minister of Finance (MoF) may approve the demarcation of an additional UDZ having regard to the provisions set out under section 13quat(6) and (7) of the Act.

Reason for change

Municipalities outside of the 16 designated UDZs areas have approached the Minister to broaden the scope of the UDZ incentive to cover additional municipalities, as they seek to integrate the incentive into existing urban renewal plans. Section 13quat of the Act only caters for the 16 municipalities (Annexure A) and makes no provision for municipalities not listed under subsection 13quat(6)(a) to be eligible for the incentive.

Given the continued state of under-development and dilapidation in their inner cities, there is demand from municipalities to expand the scope of the incentive and allow municipalities to apply to the Minister to be considered for the UDZ tax incentive. Where this inner city dilapidation continues, it discourages new investment and increases disinvestment in property.

There may thus be a case to expand the scope of the incentive as it is seen to stimulate investment in the construction and renovation of commercial and low-cost residential buildings in the inner city.

Amendment

Additional Municipalities

Section 13quat of the Act is amended to provide a framework for the Minister to consider applications from municipalities currently not allowed to designate a UDZ area. The Minister's assessment criteria will be based on the current legislative requirements as contained in section 13quat(6) and (7), as well as the additional criteria contained in Annexure B below.

The application process will apply to all municipalities that are not listed under subsection 13quat(6)(a) – i.e. all municipalities not currently part of the original 16 that were eligible since the inception of the UDZ incentive. Such municipalities may apply directly to the Minister for a UDZ area to be demarcated If the municipality's application is successful and the Minister issues the notice in the Government Gazette, the municipality will be added to the list of qualifying municipalities through a legislative amendment under subsection 13quat(6)(a).

Additional Criteria

The inclusion of the additional criteria contemplated in Annexure B is aimed at providing an assessment framework to consider when broadening access to the incentive, through prioritising urban renewal and development in a manner that counters spatial fragmentation. Essentially Annexure B prescribes several criteria items of differing significance, dependent on each application's facts and circumstances, which have to be applied in context of each application.

A broader target market for the incentive could potentially increase the associated fiscal cost, however, the additional criteria essentially focuses on high-performing municipalities that have significant growth potential. The demarcation of the UDZ should not put an additional strain on municipal finances, but contribute positively towards an increase in the generation of own revenues from the municipality.

The municipality must support its application with evidence that it meets all the requirements of subsections 13quat (6) and (7).

The additional criteria proposed in Annexure B should be issued as a separate document through the means of a regulation to guide both the Minister and municipalities when considering approving/applying (for) a UDZ area. These represent some of the factors that the Minister will use in assessing whether to allow the demarcation of a UDZ in that municipality.

The additional criteria contained in Annexure B will also be used to assist the Minister in assessing applications for additional UDZs from municipalities that have a population of less than 1 million [s13quat (7)(bA)].

Effective date

The amendments will come into operation on the date of promulgation of the Taxation Laws Amendment Act, 2016.

MINING COMPANIES SPENDING ON INFRASTRUCTURE FOR THE BENEFIT OF MINING COMMUNITIES

[Applicable provision: Section 36 of the Act]

Background

The Mineral and Petroleum Resources Development Act, 2002, (Act No 28 of 2002) (MPRDA) has multiple purposes – one of which is to transform mining and production industries in South Africa. To ensure effective transformation, the MPRDA makes it compulsory for mining companies to submit a Social and Labour Plan (SLP). SLPs are entered into between the community, the mining company and the Department

of Mineral Resources (DMR). One of the requirements is to assist with the development of mining communities, which typically involves a company agreeing to build infrastructure – ranging from roads and drainage systems to crèches, schools, clinics, housing, and recreational buildings – to benefit workers and communities surrounding the mine.

Reasons for change

Currently, section 36(11) of the Act enables mining companies to deduct certain capital expenditure in lieu of other sections in the Act. Mining companies can only deduct such capital expenditure if it relates directly to its employees, not the wider community. If, for example, a mining company builds a clinic purely to serve its employees, the mining company will be entitled to deduct the related capital expenses in equal amounts over a ten-year period. If the clinic was built to serve the wider community instead, the mining company is unable in terms of the current provisions of the Act to deduct any of the capital expenditure incurred.

In particular, section 36(11)(e) of the Act makes provision for mining companies to deduct capital expenditure incurred pursuant to the MPRDA, but excluding capital expenditure incurred by mining companies in respect of infrastructure or environmental rehabilitation.

Amendment

To recognise the SLP requirements (of the MPRDA) for mining companies to meaningfully contribute toward community development, the following is amended:

- To extend the current relief provided to mining companies (for capital expenditure incurred in respect of infrastructure for the benefit of employees) to capital expenditure incurred by mining companies on infrastructure in terms of the SLP requirements of the MPRDA, for the benefit of the people living in mining communities (other than employees). The intent is not to widen this treatment to all expenditure in respect of an SLP (e.g. teachers' salaries), but rather to cater for eligible infrastructure.
- To be eligible for the capital expenditure deduction, the infrastructure erected or developed by the mining company should reflect what was agreed to between the mining company and the DMR in terms of SLP requirements of the MPRDA.
- The DMR will improve effective monitoring and oversight of such plans and the Tax Administration Act, 2011 (No. 28 of 2011) allow SARS to request the SLP and associated annual reports.
- That current ten year period for deductions applicable to mining companies in respect of capital expenditure incurred on infrastructure for the benefit of employees be applicable in respect of capital infrastructure expenditure incurred by mining companies in terms of the SLP requirements of the MPRDA. It is recognised that this may not render a benefit for mining companies nearing the end of their useful lives as the deduction is likely to add to assessed losses, which the company derives no value from. However, policy choices involve a balancing act between policy objectives and affordability for the fiscus.

Effective date

The amendments will come into operation on 1 April 2017 and apply in respect of expenditure incurred during years of assessment commencing on or after that date.

LAND DONATED UNDER LAND-REFORM INITIATIVES

[Applicable provisions: Section 56 of the Act, paragraph 64A of the Eighth Schedule and an addition of new paragraph 64D of the Eighth Schedule to the Act]

Background

The Act makes provision for tax relief in respect of land donated under certain land reform programmes. For example, land granted in terms of the Land Reform Programme as contemplated in the White Paper on South African Land Policy, 1997 is exempt from donations tax. In addition, awards or compensations in terms of Restitution of Land Rights Act, 1994 are exempt from capital gains tax.

Reasons for change

The above-mentioned tax relief was introduced in the Act in 1994 and 2002 respectively. Subsequent to this, Government has since introduced other land reform initiatives as stipulated in Chapter 6 of the National Development Plan (NDP). As the existing tax relief in the Act was introduced prior to the publishing of the NDP, the relief does not extend to land reform initiatives aligned to Chapter 6 of the NDP.

Amendment

In order to provide relief to other land reform initiatives as stipulated in Chapter 6 of the NDP, the following is amended:

- Exemption from donations tax in section 56 of the Act be extended to include land reform initiatives under Chapter 6 of the NDP.
- Exemption from capital gains tax in paragraph 64A of the Eighth Schedule to the Act be extended to include awards in terms of land reform initiatives under Chapter 6 of the NDP.
- Introduction of new paragraph 64D of the Eighth Schedule to the Act to cater for exemption from capital gains tax in respect of land donated in terms of the land reform initiatives under Chapter 6 of the NDP.

Effective date

Extending the exemption from donations tax in section 56 of the Act to include the land reform initiatives under Chapter 6 of the NDP.

- The amendment is deemed to have come into operation on 1 March 2016 and applies in respect of any donation made on or after that date.

Extending the exemption from capital gains tax in paragraph 64A of the Eighth Schedule to include awards in terms of land reform initiatives under Chapter 6 of the NDP

- The amendment is deemed to have come into operation on 29 February 2016 and applies in respect of years of assessment ending on or after that date.

Introducing a new exemption in terms of paragraph 64D of the Eighth Schedule to cater for exemption in respect of land donated in terms of land reform initiatives under Chapter 6 of the NDP.

- The amendment is deemed to have come into operation on 29 February 2016 and applies in respect of years of assessment ending on or after that date.

PUBLIC BENEFIT ORGANISATIONS PROVIDING INDUSTRY BASED EDUCATION AND TRAINING ACTIVITIES

[Applicable provision: Part I of the Ninth Schedule to the Act]

Background

The Act contains provisions in sections 10(1)(cN) and 30, and the Ninth Schedule that provide exemption for public benefit organisations if they meet certain requirements as set out in the Act, including the carrying on of public benefit activities. Paragraph (a) of the definition of public benefit activities refers to activities listed in Part 1 of the Ninth Schedule. In turn, paragraph 4 of Part I of the Ninth Schedule lists qualifying education and development public benefit activities.

Tax exemption is not automatic and public benefit organisation must still apply to SARS in order to obtain the tax exemption status.

Reasons for change

It has come to Government's attention that certain industries establish special associations to promote the common interest of members in that particular industry or profession. These associations also provide training to employees of that particular industry as well as implementing industry based standards. The associations also develop certification schemes for employees working in that specific industry in line with best international practice. The main source of funding is derived from training courses and other related income which is analogous to tuition fees received by a University. Industry based associations such as these are directed by the requirements of the industry and are linked for accreditation to the Quality Council for Trades and Occupations (QCTO).

Although the principal objective of these associations is to carry on educational and training activities for the benefits and needs of the public, these associations do not qualify for tax exemption as they do not meet the requirements set out in sections 10(1)(cN) and 30, and paragraph 4 (dealing with exemption of education and development) in Part 1 of the Ninth Schedule.

Amendment

Amendments were made in the Act to extend the list of public benefit activities to qualifying public benefit organisations, in order to exempt education and training activities to benefit industry based training organisations. This is to encourage the industry to provide education and development, which play a key role in increasing not only more skilled individuals in the workplace but also to the poor and needy persons who

seek cost effective/affordable quality industry based education and training.

The following amendments were made:

- Receipts and accruals of industry based public benefit associations providing education and training programmes and courses for the development of persons or employees in that particular industry be exempt from normal taxation by including the activities performed by them under "Education and Development" in paragraph 4 of Part I of the Ninth Schedule to the Act provided that those qualifications are compatible with the type of qualifications in the Quality Council for Trades and Occupations.
- Receipts and accruals of industry based public benefit associations administering examination and providing certification programmes for the benefit of that particular industry be exempt from normal taxation by including the activities performed by them under "Education and Development" in paragraph 4 of Part I of the Ninth Schedule to the Act, provided that that association is accredited to conduct those activities by the South African National Accreditation System (SANAS), South Africa's member of the International Accreditation Forum.

Effective date

The amendments will come into operation on the date of promulgation of the Taxation Laws Amendment Act of 2016.

EXTENSION OF THE EMPLOYMENT TAX INCENTIVE

[Applicable provisions: sections 1, 4, 7, 9, 10 and 12 of the Employment Tax Incentive Act No. 26 of 2013]

Background

The Employment Tax Incentive (ETI) was introduced in January 2014 to promote employment, particularly of young workers. A programme of this nature is new to the South African policy landscape. The initial three-year period of the programme was intended to evaluate the viability of the programme, and to indicate initial economic effects.

Reasons for change

During the legislative process to introduce the ETI, National Treasury committed to review the programme before its sunset, i.e. after three years. From the review process, we are now able to indicate significant positive effects on growth rates of youth employment in claiming firms albeit modest in size. Significant, wide-spread negative effects did not materialise.

In its current form, the incentive can only be claimed by employers up to 31 December 2016. In order to extend the programme, the process of legislative amendment is required.

Government has seen a higher-than-expected take up, which means that the programme exceeded initial cost estimates. We have also started to gather an evidence base to indicate for which employers the incentive makes the biggest impact – namely in smaller firms. While this does not suggest that there are no effects in larger firms, we can attempt to target the incentive better in order to eliminate some portion of windfall benefits for activities that would have taken place in absence of the incentive.

Amendment

To extend the ETI programme beyond 31 December 2016, we propose the following refinements to its application:

- Extending the incentive: Allow claims beyond the current sunset of 31 December 2016, namely until 28 February 2019. The extension to the end of February is proposed in order to coincide with the end of the tax year. During this period, further data and evidence on the performance of the programme can shed light on impacts of the programme.
- Limit back-dated claims: Monthly claims can only be made up to the date of each 6- monthly reconciliation. After that no further claims for that reconciliation period can be allowed. Now, any excess becomes available as a refund.
- Clarifying the number of hours worked in the definition of "monthly remuneration".
- Clarifying the applicable hours in the grossing up / grossing down calculation.
- Administrative issues.

Effective date

The amendments will come into operation on 1 March 2017. A separate effective date for extension of the ETI is deemed to have come into

effect from 1 October 2016.

VALUE – ADDED TAX

REGISTRATION OF AN ENTERPRISE SUPPLYING COMMERCIAL ACCOMMODATION

[Section 1 of the definition of an enterprise of the Value-Added Tax Act No. 89 of 1991]

Background

Where a person carries on or intends carrying on an enterprise or activity supplying commercial accommodation, and the total value of taxable supplies in the preceding period of 12-months or which it can reasonably be expected that that person will make in a period of 12-months, will not exceed R60 000 shall be deemed not to be the carrying on of that enterprise.

Amendment

The threshold increased to R120 000.

NOTIONAL INPUT TAX ON GOODS CONTAINING GOLD

[Applicable provisions: Section 1(1) of the Value-Added Tax Act of 1991 (VAT Act) – proviso (ii) of the definition of "second-hand goods"]

Background

In 2014, changes were made in the VAT Act to amend the definition of "second-hand goods" to specifically exclude "gold" and "goods containing gold" from the definition and thereby denying the notional input tax credit on these goods. The policy rationale for the 2014 amendments was to curb fraudulent notional input tax deductions on the acquisition of gold and gold jewellery. The amendment was not intended to have a negative impact on legitimate transactions within the second-hand goods industry.

Reasons for change

Concerns have been raised that the 2014 amendments have led to unintended consequences whereby the notional input tax credit on all goods containing gold is denied to vendors that are dealers in second-hand goods. The denial applies where those goods which were acquired are sold either exactly as they were acquired or with minor modifications to make them suitable for resale in essentially the same state, irrespective of whether the gold content is substantial or negligible.

At issue is, for example, when a second-hand dealer purchases a computer from a non-vendor, based on the 2014 amendments, the notional input tax credit is denied because some of the components in the computer contain an element of gold. Another example is when a second-hand dealer purchases an expensive watch from a non-vendor, the notional input tax credit is denied because the watch contains a certain amount of gold. There is an argument that the value of the gold content on the above-mentioned items, i.e. computer and watch, are insignificant compared to the intrinsic value of the items itself. The values of the computer and watch are based on the mechanism, the design and the make which are the main intentions for trading with these items, and not the presence of a small fraction of gold in these items.

Amendment

To address the above-mentioned unintended consequences the 2014 amendments have been revised. Paragraph (ii) of the definition of "second-hand goods" in section 1(1) of the VAT Act is amended to allow the deduction of the notional input tax credit on goods containing gold, if the goods are sold in the same or substantially the same state as when those goods were acquired.

Effective date

The amendments will come into operation on 1 April 2017.

ALLOWING MUNICIPAL ENTITIES TO ACCOUNT FOR VAT ON THE PAYMENT BASIS WHERE THE SUPPLY IS R 100 000 OR MORE

[Applicable provision: Section 15(2A) of the VAT Act]

Background

The VAT Act makes provision for certain persons, including public authorities and municipalities to register and pay VAT on a payments basis.

The provisions of the VAT Act require those vendors who are registered on the payments basis to account for VAT on the invoice basis in respect of any supply where the consideration is R100 000 or more. However, only public authorities and municipalities are allowed to deviate from this rule and account for VAT on the payments basis on supplies where the consideration is R100 000 or more.

Reasons for change

Municipal entities (envisaged in section 15(2)(a)(iv)) of the VAT Act render services similar to municipalities and are regulated under the Municipal Systems Act and the Municipal Finance Management Act. Therefore, there is no policy rationale not to extend the same dispensation, currently available to public authorities and municipalities, to municipal entities.

Amendment

Section 15(2A) of the VAT Act is amended to allow municipal entities, referred to in section 15(2)(a)(iv) of the VAT Act, to account for VAT on the payment basis in respect of any supply where the consideration is R100 000 or more.

Effective date

The amendments will come into operation on 1 April 2017.'

VAT EXEMPTION IN RESPECT OF IMPORTED GOODS THAT ARE LOST, DESTROYED OR DAMAGED THROUGH NATURAL DISASTERS

[Applicable provision: Schedule 1 of the VAT Act]

Background

In terms of Schedule 4 of the Customs and Excise Act 91 of 1964, a taxpayer is exempt from paying customs duty and fuel levy (if applicable) on the importation of goods if those goods are subsequently lost, destroyed or damaged through natural disasters or under such circumstances as the Commissioner deems exceptional.

This relief is applicable to circumstances where the customs duty amount and the fuel levy (if applicable) is not less than R2500 on any single occasion while such goods are in any customs and excise warehouse, in any appointed transit shed, under the control of the Commissioner, being removed with deferment of payment of duty, under rebate of duty from a place in the Republic to any other place in terms of the provisions of the Customs and Excise Act or being stored in any rebate storeroom (subject to certain provisos, including that the goods did not enter into home consumption).

Reasons for change

At issue is the fact that the VAT Act does not have an exemption similar to Schedule 4 of the Customs and Excise Act, in respect of goods that are imported, if those goods, after importation and before being entered for home consumption, are lost, destroyed or damaged through natural disasters or under such circumstances as the Commissioner deems exceptional. This creates uncertainty in the interpretation and application of both the provisions of the Customs and Excise and the VAT Acts.

Amendment

To remove the ambiguity and provide certainty, Schedule 1 of the VAT Act is aligned to Schedule 4 of the Customs and Excise Act by introducing an exemption from the tax imposed in terms of section 7(1)(b) of the VAT Act, where those goods are lost, destroyed or damaged through natural disasters or under such circumstances as the Commissioner deems exceptional, as contemplated in the Customs and Excise Act, provided that such goods have not yet been entered for home consumption.

Effective date

The amendments will come into operation on 1 April 2017.

TAX ADMINISTRATION LAWS AMENDMENT ACT

AMENDMENT TO THE DEFINITION OF A PROVISIONAL TAXPAYER

[Paragraph 1 of the Fourth Schedule]

Background

Paragraphs (a) and (b): If foreign employers in South Africa do not deduct PAYE, local employees should pay provisional tax in terms of the Fourth Schedule.

In terms of paragraph (c) of the definition of a provisional taxpayer, a person can become a provisional taxpayer upon notification by the Commissioner. A method for doing so would be for SARS to send letters to the various employers informing them that all local recruits employed by them are regarded as provisional taxpayers. However, notification of the local recruits employed by foreign employers is cumbersome and administratively onerous for SARS. In many cases SARS may not even have some of the personal information of the local recruits on record. This will require SARS to obtain all the necessary information from the employers and thereafter inform the employees that they are provisional taxpayers.

Amendment

The amendment aims to avoid this administratively onerous task by providing that any person who derives, by way of income, remuneration from an employer that is not registered in terms of the Fourth Schedule, be included in the definition of provisional taxpayer.

AMENDMENT TO THE DEFINITION OF REMUNERATION

[Paragraph 1 of the Fourth Schedule]

Background

Certain dividends received from restricted equity instruments do not qualify for an income tax exemption and are taxable on assessment of the directors and employees.

Amendment

The amendment specifically includes these taxable dividends in the definition of ''remuneration'' for PAYE in paragraph 1 of the Fourth Schedule.

PAYMENT OF EMPLOYEES' TAX ON DIRECTOR REMUNERATION

[Paragraph 11C of the Fourth Schedule & Section 7B]

Background

Since March 2002 private companies and close corporations have had to withhold employees tax from amounts paid to directors.

Because directors of private companies and members of close corporations are often not paid on a regular basis it was necessary to incorporate a provision which would deem income to be received on a regular basis. This provision was contained in paragraph 11C of the Fourth Schedule which provides a mechanism for calculating a deemed monthly remuneration.

Amendment

The amendment repeals the provision for the payment of employees' tax (PAYE) by directors of private companies. The provisions of section 7B would apply to the variable remuneration received by the director in that it is deemed to accrue to the director on the date on which it is paid to the director. This is also the date on which the amount of the remuneration becomes claimable as expenditure by the private company.

LATE SUBMISSION OF SECOND ESTIMATE FOR PROVISIONAL TAX

[Paragraph 20 &19(6) of the Fourth Schedule]

Background

If an estimate for the second provisional tax period is not submitted before the due date of the subsequent provisional tax payment, the provisional taxpayer is deemed to have submitted an estimate of nil taxable income, thereby triggering a penalty under paragraph 20.

Amendment

The window period for submission of provisional tax estimates will be closed four months after the end of the relevant year of assessment. Furthermore, this deeming provision relates to the submission of an estimate and is therefore moved from paragraph 20 to subparagraph (6) of paragraph 19.

PENALTY FOR THE UNDERPAYMENT OF PROVISIONAL TAX

[Paragraph 20 of the Fourth Schedule]

Background

The penalty for underpaying provisional tax is based on a percentage of normal tax payable after taking into account rebates and tax already paid. Certain once-off amounts, such as retirement lump-sum and severance-benefit payments, are excluded from the calculation of the penalty because they are taxed separately in terms of special tables and the tax owed is withheld before payment is made. Taxpayers are required to pay provisional tax on the other amounts listed in paragraph (d) of the definition of gross income in section 1, because these other amounts are not taxed under the lump-sum tax tables. However, because these amounts are excluded from the penalty calculation, taxpayers are not penalised if they fail to pay the required provisional tax.

Amendment

To correct this the penalty calculation's exclusion of the amounts in paragraph (d) not taxed in terms of the special tables, is removed. Furthermore, the relief granted by the Commissioner for failure to submit an estimate not due to an intent to evade or postpone the payment of provisional tax only applies to the non- submission of a provisional tax estimate by the end of the four-month period specified in paragraph 19(6) of the Fourth Schedule.

DOCUMENTATION REQUIREMENTS FOR INPUT TAX PURPOSES

[Section 16.2(g) of the Value-Added Tax Act No. 89 of 1991]

Background

The Value-Added Tax Act places a statutory obligation on vendors to issue documents in a defined form and manner. These requirements are attuned to commercial and accounting practice and ensure a seamless audit trail. Recipient vendors are occasionally issued with defective documents or are unable to obtain documents from supplying vendors, resulting in an inability to make input tax deductions.

Amendment

With effect from 1 April 2015, section 25 of the Tax Administration Laws Amendment Act, 2015, introduced section 16(2)(g) in the Value-Added Tax Act to provide relief to recipient vendors in these situations. The current amendment provides clarity about the considerations that the Commissioner will consider for accepting alternative documentary proof. It is important to note that vendors can only access this relief as a last resort. Vendors must still be able to demonstrate that a sincere effort has been put into obtaining the proper documents and maintain proof of those efforts. Furthermore, vendors would have to make an application for a ruling no later than 2 months prior to expiry of the five-year prescription period and only when that ruling is issued, may the amount be deducted as input tax at that later stage. Lastly, invoking this provision will not allow vendors to backdate the claim to a past tax period that has already been closed.

REFUND OF VAT

[Section 44 of the Value-Added Tax Act No. 89 of 1991]

Background

A vendor is required to submit VAT returns in accordance with its allocated tax period. Where the total amount of input tax for a tax period exceeds the total amount of output tax for that tax period, the vendor will submit a VAT return for that tax period, requesting SARS to pay a refund to that vendor. This is commonly referred to as a refund of VAT arising from a VAT return.

Amendment

The time limit within which a vendor or any other person must request a refund of VAT arising from a VAT return for SARS to properly pay that refund is clarified. Accordingly, for a refund arising from a VAT return, the VAT return must be submitted within five years from the due date of that VAT return.

If the return is submitted later than this, the excess will not be treated as a refund, but as a payment to the national Revenue Fund.

TAX OMBUD

[Tax Administration Act, 2011: section 14, 15, 16 and 20]

Background

The mandate of the Tax Ombud is to review and address any complaint by a taxpayer regarding a service matter, or a procedural or administrative matter arising from the application of the provisions of a tax Act by SARS.

Amendment

The amendment aims to enhance the independence of the Tax Ombud by extending his or her tenure. The term of the Tax Ombud is extended from 3 years to 5 years.

An amendment to section 15(1) aims to enhance the independence of the Tax Ombud in respect of the appointment of the staff of the Office of the Tax Ombud. The Tax Ombud can now employee staff without doing it in consultation with the Commissioner.

An amendment to section 15(4) is passed so that the expenditure connected with the functions of the office of the Tax Ombud is paid in accordance with a budget for the office approved by the Minister. The amendment furthermore provides that the Tax Ombud must appoint the staff of his or her office which staff must be employed in terms of the South African Revenue Service Act, 1997 (SARS Act). The reference to the SARS Act is essential if the Tax Ombud's staff are to enjoy the same conditions of service as SARS staff.

An amendment to section 16(1) aims to extend the mandate of the Tax Ombud to include the investigation and review, at the request of the Minister or at the initiative of the Tax Ombud with the approval of the Minister, of any systemic and emerging issue related to a service matter, the application of the provisions of the Tax Administration Act, or procedural or administrative provisions of a tax Act, as defined in the Tax Administration Act.

An amendment to section 20(2) aims to enhance the effectiveness of the Tax Ombud's recommendations. If SARS or the taxpayer does not accept them, reasons must be provided within a period of 30 days. This will ensure that the Tax Ombud is able to review the reasonableness of the reasons to inform future action.

LODGING OF OBJECTION

[Tax Administration Act, 2011: section 104]

Background

The current period for lodging an objection is 30 business days from the date of assessment. This has been shown to be too short in practice, particularly in complex matters, resulting in a large number of applications for condonation. If a taxpayer is aggrieved by an assessment, or a decision made by a SARS official, he may object.

Prior to lodging an objection, the taxpayer can write to SARS within 30 business days after the date of the assessment and request written reasons for the assessment. SARS has 30 days to notify the taxpayer where he already provided a reason or if not, SARS has 60 days to do so. The taxpayer has 30 days from the later of the day of assessment, or the date the written reasons are given to object. Condonation for a late objection not based on exceptional circumstances may be extended by SARS for a period up to 21 days.

Amendment

Section 104(5) is amended to allow for a longer period for lodging an objection which will be effected in the dispute resolution rules issued under section 103 of the Act. A condonation of a late objection not based on exceptional circumstances may now be extended by SARS for a period up to 30 days, but if there are exceptional circumstances this period may be further extended by SARS. The maximum period within which a late objection may be extended remains three years.

UNDERSTATEMENT PENALTY

[Tax Administration Act, 2011: section 221]

Background

The understatement penalty is a percentage in accordance with the table set out below, applied to the shortfall of the tax. An "understatement" is a default in rendering a return, an omission from a return, an incorrect statement in a return, or if no return is required the failure to pay the correct amount of tax. A "substantial understatement" is a case where the prejudice to the fiscus exceeds the greater of 5% of the amount of tax properly chargeable or refundable for the relevant period, or R 1 000 000.

Amendment

Amendments were made to the understatement penalty regime to enhance clarity with regard to whether and the extent to which understatement penalties are imposable in GAAR matters pursuant to recent contentions in this regard, are proposed. Under the additional tax penalty regime, the predecessor to the understatement penalty regime, case law supported the imposition of such penalties in GAAR matters. The amendments will clarify that this prevails in respect of understatement penalties, which is also in line with international law.

In addition, to provide clarity as to what would be the appropriate penalty in GAAR matters, it is proposed that a new behavioural category is inserted in the understatement penalty table below.

1. Standard case
2. If obstructive or if it is a 'repeat case'
3. Voluntary disclosure after notification of audit
4. Voluntary disclosure before notification of audit

Behaviour	1	2	3	4
Substantial understatement	10%	20%	5%	0%
Reasonable care not taken in completing return	25%	50%	15%	0%
No reasonable grounds for tax position taken	50%	75%	25%	0%
Impermissible avoidance arrangement	75%	100%	35%	0%
Gross negligence	100%	125%	50%	5%
Intentional tax evasion	150%	200%	75%	10%

VOLUNTARY DISCLOSURE PROGRAMME

[Tax Administration Act, 2011: section 226]

Background

A person may apply for voluntary disclosure relief unless that person is aware of a pending audit or investigation into the affairs of the person seeking relief, or an audit or investigation has commenced but has not yet been concluded and the default does not relate to what is being audited or investigated.

Amendment

The proposed amendments aim to clarify the application of the section. It furthermore inserts a requirement that a person seeking voluntary disclosure relief must be given notice of the commencement of an audit or criminal investigation into the affairs of the person as opposed to the requirement that the person has become aware of a pending audit or criminal investigation or that the audit or criminal investigation has commenced.

OTHER IMPORTANT AMENDMENTS

SPECIAL VOLUNTARY DISCLOSURE PROGRAMME

Background

On 24 February 2016, the Minister of Finance in his Budget Speech announced the introduction of a Special Voluntary Disclosure Programme to provide a further opportunity for non-compliant taxpayers who still have undisclosed assets abroad to voluntarily disclose their offshore assets and income. With the new global standard for automatic exchange of financial account information in tax between tax authorities commonly known as the Common Reporting Standard (CRS) requiring governments to obtain detailed account information from their financial institutions and exchange that information automatically with other jurisdictions on an annual basis from September 2017, time for taxpayers who still have undisclosed assets abroad.

Reasons for change

The CRS provides for annual automatic exchange between governments of financial account information, including balances, interest, dividends, and sales proceeds from financial assets, reported to governments by financial institutions and covering accounts held by individuals and entities including trusts and foundations. The CRS is intended to assist governments in reducing the possibility for tax evasion by providing for the exchange of non-resident information with the tax authorities in the taxpayer's country of residence. It is also aimed at enabling governments to discover formerly undetected tax evasion and to recover tax revenue lost to non-compliant taxpayers, and further strengthen international efforts to increase transparency, cooperation, and accountability among Multinational Entities and tax administrations.

In order to encourage compliance, government saw the need to give non-compliant taxpayers the last opportunity to come forward and disclose their offshore activities. This will be open for individuals and companies in order to assist them to regularise their tax affairs before September 2017.

Amendment

In order to encourage compliance and assist non-compliant taxpayers to regularise their affairs it is proposed that a Special Voluntary Disclosure Programme (SVDP) is introduced as follows:

Window period of Special Voluntary Disclosure Programme

Applications for relief under the SVDP will apply for a limited window period of eleven months starting on 1 October 2016 and closing on 31 August 2017.

Application process under the SVDP

The application process for the existing Voluntary Disclosure Programme will be extended to the SVDP.

Persons that may apply for the SVDP

Individuals and companies may apply for the SVDP on the same basis as for the existing Voluntary Disclosure Programme contemplated in Part B of Chapter 16 of the Tax Administration Act, 2011. That is to say, an initial "no-name approach" may be made; applications may be made in a representative capacity, etc.

Individuals and companies who did not impute the net income of the controlled foreign company as defined in section 9D(2) of the Income Tax Act may also apply for the SVDP on the same basis as for the existing Voluntary Disclosure Programme.

Trusts will not qualify to apply for the SVDP.

Settlors, donors, deceased estates and beneficiaries of foreign discretionary trusts may, however, participate in the SVDP if they elect to have the trust's offshore assets and income deemed to be held by them for tax purposes.

Persons may not apply for the SVDP if they are aware of a pending audit or investigation in respect of foreign assets or foreign taxes or an audit or investigation in respect of foreign assets or foreign taxes has commenced. However, if the scope of an audit or investigation is in respect of other assets (other than foreign assets of foreign taxes, for example in respect of PAYE), persons may still qualify to apply for relief under the SVDP.

Amounts in respect of which SARS obtained information under the terms of any international exchange of information procedure will not be eligible for the SVDP.

Relief granted under the SVDP

40 per cent of the highest value of the aggregate of all assets situated outside South Africa between 1 March 2010 and 28 February 2015 that were derived from undeclared income will be included in taxable income and subject to tax in South Africa.

The undeclared income that originally gave rise to the assets above, will be exempted from income tax, donations tax and estate duty in the past. However, future income will be fully taxed and assets declared will remain liable for donations tax and estate duty in the future, should the applicant donate these assets or pass away while holding them.

The value referred to above is the market value determined in the relevant foreign currency and translated to the South African Rand at the spot rate at the end of each year of assessment.

For the purpose of determining any capital gains or losses, the asset referred to above that was held and not disposed of on the last day of the year ending on or before 28 February 2015, must be deemed to have been acquired on that day at a cost equal to market value. However, such cost will be limited to the proceeds on the disposal of that asset less any expenditure allowable under paragraph 20 of the eight schedule to Income Tax Act.

Taxes and levies such as Value Added Tax, Skills Development Levy and Unemployment Insurance Fund Contributions are excluded from the SVDP.

Where taxpayers do not have any assets situated abroad post 1 March 2010 but might still want to apply for the SVDP because they are concerned that they might be identified through one of the global leaks, such taxpayers may also apply for the SVDP. Where the value in this regard cannot be determined, the Commissioner may agree to accept a reasonable estimate of that value.

Example:

Jane Roe and John Doe did not declare 10% of the income from their jointly operated long distance transport business from 1990 to 2001. Using a British Virgin Islands trust and a Panamanian company, they invested the proceeds in a similar business in South America. Unfortunately, they did not fully understand the local market conditions, so the business went bankrupt in 2003 and they lost their entire investment. They have felt no pressing need to come forward up to now, since they no longer have illicit assets offshore.

With the leak of the Panama Papers they fear that SARS will unravel the structure they put together and detect their tax evasion. The provision above allows them to make use of the SVDP by determining (or if this is impossible, estimating) the highest value of their illicit offshore assets from 1990 to 2001. Assuming this value to be R14 million in total or R7 million each, this amount will be deemed to be the value for SVDP purposes. As a result, 40% or R4.2million will be included in each of their taxable incomes and taxed at their marginal rate.

Waiver of penalties under the SVDP

No understatement penalties will be levied where an application under the SVDP is successful.

Exemption from criminal prosecution under the SVDP.

As is currently the case in the existing Voluntary Disclosure Programme, SARS will not pursue criminal prosecution for a tax offence where an application under the SVDP is successful.

Reporting

The Minister of Finance will report to the National Assembly on the outcome of the SVDP for both Tax and Exchange control purposes.

Effective date

The proposed SVDP will be deemed to have come into effect on 1 October 2016 and will apply for a limited window period of eleven months commencing on 1 October 2016 and ending on 31 August 2017.

EXCHANGE CONTROL SPECIAL VOLUNTARY DISCLOSURE PROGRAMME

South African residents (individuals. sole proprietorships, partnerships, deceased estates, insolvent estates, South African trusts. close corporations and companies) and former South African residents will be a allowed to disclose foreign assets held in contravention of the Regulations as at 2016-02-29.

Applications and the relevant supporting documents must be submitted to the SVDP unit via the South African Revenue Service (SARS) eFiling system or at any of the SARS branches countrywide. Separate electronic application forms for the tax and exchange control administrative relief has been created.

Any party involved in a matter currently under investigation by FinSurv may not apply for administrative relief.

Application

Applications may be made in a personal or representative capacity. Persons applying in a representative capacity must ensure that the necessary proof of authority to act in such capacity is furnished together with the SVDP application.

FinSurv may grant administrative relief to a South Africa resident in terms of Regulation 24, provided that:

- The unauthorised foreign assets for which administrative relief is sought was held by the applicant on or before 2016-02-29;
- Applications are made within the SVDP period;
- The declaration made by the applicant is made voluntarily;
- The applicant makes a full disclosure of all unauthorised foreign assets (of whatever nature, excluding bearer instruments) in which the applicant stipulates the source of all unauthorised foreign assets and includes details of the manner in which such assets were transferred and retained abroad; and
- The applicant furnishes all documentation and information as stipulated in the SVDP application form, which information and documentation includes, but is not limited to:
  - The market value at 2016-02-29 of the unauthorised foreign asset in the foreign currency of the country in which such asset is situated;
  - A description of the identifying characteristics and location of such foreign asset,
  - A valuation certificate by a valuator of the country where the unauthorised foreign asset is located, or a valuation by a sphere of government of the country where such asset is located, or an original or certified statement of account indicating the balance or market value, or any other form of proof of value of that foreign asset as the Treasury may on good cause shown allow to be submitted; and
  - A sworn affidavit or solemn declaration of the contravention.

Levy to be paid

In order to be granted administrative relief as outlined above, applicants will have to pay a levy based on the market value of such assets as at 2016-02-29, subject to the following conditions.

- A levy of 5 per cent is payable on the value of the unauthorised foreign assets or the sale proceeds thereof if such assets are repatriated to the Republic of South Africa (South Africa). The 5 per cent levy must be paid from foreign-sourced funds;
- A levy of 10 per cent is payable on the value of the unauthorised foreign assets if such assets are retained abroad. The 10 per cent levy must be paid from foreign-sourced funds;
- A levy of 12 per cent is payable on the value of the unauthorised foreign assets, in circumstances where the 10 per cent levy is not paid from foreign-sourced funds;
- Applicants will not be allowed to deduct any exchange control allowance or any remaining portion thereof from any leviable amount
- The applicable levy may not be reduced by any fees or commissions;
- The applicable levy must be paid by the applicant within three months from the date of receipt of notification from FinSurv;
- In cases where the 5 or 10 per cent levy is payable, such levy must be repatriated to South Africa to an account held at a local Authorised Dealer and must be converted in South Africa at the ruling spot exchange rate; and
- The Rand proceeds of the foreign currency introduced in terms of paragraphs (a) and (b) above and the Rand value described in (c) above must be paid by an Authorised Dealer, into an account held at the Corporation for Public Deposits, established in terms of section 2 of the Corporation for Public Deposits Act, 1984 (Act No. 46 of 1984).

Where the unauthorised foreign assets declared are denominated in multiple foreign currencies, applicants are permitted to convert those foreign currency amounts to United States Dollar for purposes of the levy using the rate of exchange as at 2016-02-29.

Foreign assets held in contravention of the Regulations

The sale, cession or assignment by residents of intellectual property, owned or developed by South African residents, without having obtained FinSurv approval. In this regard, full disclosure of the sale or assignment will be required including the identity of the parties involved and royalties paid by residents pursuant to any disposal.

Foreign liabilities incurred by residents to acquire foreign assets with recourse to South Africa without having obtained FinSurv approval. In

this regard, full disclosure of the underlying transaction relating to the liability will be required, including details of the liability itself and the parties involved.

The acquisition of a direct or indirect interest in a foreign asset (including foreign cash balances) as a result of the retention of funds abroad which should have been repatriated to South Africa or by having remitted funds abroad without having obtained FinSurv approval. Such transactions include, but are not limited to, the acquisition of foreign securities (including unauthorised share swaps), the retention abroad of export proceeds, unauthorised spending on credit cards resulting in foreign assets and inheritances from South African deceased estates with unauthorised foreign assets. In this regard, full disclosure of the transaction, including any underlying transactions will be required and details of all the parties involved therein are to be provided.

Re-investment of foreign assets or the proceeds thereof into South Africa (loop structures/ 74/26 structures).

- South African residents (both natural persons and corporate entities) who have, prior to 2016-02-29, entered into a transaction or a series of transactions (Transactions), the purpose, and/or effect of which was to export capital, directly or indirectly from South Africa. These Transactions, invariably entail the formation by (or at the instance of) a resident of an Offshore Structure (Offshore Structure) which, by a re investment into South Africa, acquires shares or some other interest in a South African resident company or a South African asset.
- The most prevalent Transaction(s) utilised in this regard usually result(s) in the so-called '74/26 structure' in terms of which (subject to deviations from case to case which do not alter the impact thereof on the Regulations):
    - The resident, either directly or indirectly, procures a non-resident company or entity in which the resident or a non-resident trust, also procured at the direct or indirect instance of the resident, acquires a substantial or total shareholding;
    - The non-resident company or the non-resident trust would acquire 74 per cent or some lesser substantial shareholding in a resident company in which the resident referred to above (or his/her family) holds the remaining shareholding; and
    - The resident would thereafter dispose of certain carefully selected South African growth assets to the resident company mentioned above, on the basis that the consideration for such disposal would be discharged by means of raising a loan account in the resident company. Alternatively, a loan would be advanced to the resident company by the resident for purposes of acquiring such assets.

Special rules for donors to discretionary trusts

A South African resident who is a donor (or the deceased estate of a donor) in relation to a discretionary trust which is not a resident, may elect that any foreign asset which was held by that discretionary trust on 2016-02-29, be deemed to be held by that resident.

The above applies in respect of a foreign asset of a discretionary trust which:

- Was acquired by that discretionary trust by way of a donation made by a South African resident;
- Has been wholly or partly derived from any unauthorised asset or from any amount not declared by the donor to the Commissioner for SARS as required by the Estate Duty Act, 1955 (Act No. 45 of 1955) or Income Tax Act, 1962 (Act No. 58 of 1962); and
- Has not at the time of that election vested in any beneficiary of that discretionary trust.

Where a South African resident has made an election in relation to a foreign asset that resident is deemed to have held the foreign asset for purposes of this administrative relief, from the date that the discretionary trust acquired that foreign asset until that foreign asset is disposed of by that discretionary trust to any other person, in which case that person shall be deemed to have disposed of that foreign asset for consideration equal to its market value on the date of disposal.

In order to make the election, the resident must submit the founding document (including any amendments, codicils and addendums) of the discretionary trust as at 2016-02-29 together with the application.

A levy equal to 5 or 10 per cent (dependent on whether unauthorised assets are to be repatriated) of the value of the foreign asset(s) disclosed will be payable. The market value, in the foreign currency of the foreign asset, shall be that on 2016-02-29.

Supporting documents

Applications and the following relevant supporting documents must be submitted electronically to the SVDP unit via the South African Revenue Service's (SARS) e-Filing system, alternatively at any SARS branch.

- Full disclosure of all unauthorised foreign assets, the source of these assets and details of the manner in which the assets were transferred and retained abroad;

- A description of the identifying characteristics and location of the unauthorised foreign asset;
- A valuation certificate by a valuator of the country where the unauthorised foreign asset is located, or a valuation by a sphere of government in the country where such asset is located, or an original or certified statement of account indicating the balance or market value, or any other form of proof of the value of that asset as the Treasury may on good cause shown allow to be submitted; and
- A sworn affidavit or solemn declaration of the contravention;
- A copy of an ID, smart card, or passport of an individual, director/member of a legal entity and executors of deceases estates.
- Other documents to proof the existence of the assets.

TAX-FREE INVESTMENTS

[Regulations in terms of section 12t(8) of the income tax act, 1962, on the requirements for tax free investment]

Commencement

These regulations are deemed to have come into operation on 1 October 2016.

The National Treasury published a revised draft of amendments to the Regulations on tax free savings accounts (TFSAs). A postponement of transfers until 1 March 2017 was published in the government gazette (Gazette No: 40308 published 28 September 2016). The updated draft regulations cover revised wording for the treatment of performance fees, a relaxation on the rules of access and adjustments to disclosure and compliance requirements.

Wording on performance fees

The policy intent with regard to the treatment of performance fees has been communicated consistently since the first publication of the draft regulations to tax free savings accounts in November 2014. Performance fees may not be charged in TFSAs nor in any of the underlying funds in which the TFSAs are invested.

The amended wording is intended to make the Regulations clearer by removing any ambiguity in relation to performance fees.

Access to tax free savings accounts

As a principle, TFSAs should be available to investors for any short-term needs, including emergencies, large expenditures and asset purchases. Consequently, the ability of investors to access their savings should not be unduly restricted.

However, the current rules which offer access to amounts within 32 days for products with a fixed term and seven days for those without a fixed term appear to have limited the ability of product providers to offer fixed term deposits. Individuals are thus not able to invest in fixed term deposits with higher interest rates as there are few of these products available.

In balancing the above two interests, National Treasury proposes a relaxation of the rules on accessibility, which would allow product providers discretion to only allow individuals access upon the maturity date of the product.

Product providers can, however, still allow investors to access these funds before maturity, as is the case with regular fixed term deposits. The current rules that limit the exit penalty on early withdrawals will remain to safeguard investors against excessive penalties when withdrawing or transferring before maturity.

Transfers

In addition to the amendments to transfers, National Treasury proposes to make amendments to address some compliance issues and the administration of fees.

National Treasury will engage in an additional round of consultations with industry. The transfer regulations will come into effect on 1 March 2017, allowing a number of months after the release of the final Regulations for product providers to adjust their systems to comply with the new requirements.

Compliance

It is proposed that product providers will be required to notify the Financial Services Board (FSB) within a calendar month before a new product is advertised in the market. The FSB will be able to review the features of the product for compliance with the Regulations and endeavour to respond to the product provider within the calendar month.

However, product providers will not be compelled to await the regulator's response on expiry of the calendar month, but the regulator may make certain queries on the compliance of the products after they have been rolled-out.

The draft amendments and the gazetted postponement (Gazette No: 40308 published 28 September 2016) are published on the National Treasury website at www.treasury.gov.za.

UNEMPLOYMENT INSURANCE AMENDMENT ACT 10 OF 2016

[Unemployment Insurance Amendment Act 10 of 2016]

Purpose:

- To amend the Unemployment Insurance Act, 2001, so as to provide for the extension of the unemployment insurance benefits to learners who are undergoing learnership training and civil servants;
- To adjust the accrual rate of a contributor's entitlement to unemployment insurance benefits;
- To finance employment services;
- To extend a contributor's entitlement to benefits under certain circumstances;
- To provide for the process of application for maternity benefits;
- To repeal some enforcement provisions;
- To empower the Unemployment Insurance Board to provide in its constitution for the functions of regional appeals committees;
- To amend Schedule 2 to the Unemployment Insurance Act, 2001, so as to provide for the adjustment of the Income Replacement Rate; and to provide for matters connected therewith.

Amendments:

Section 3

Purpose of amendment is to extend unemployment insurance benefits to employees who are under contract of employment contemplated in section 18(2) of the Skills Development Act, and employees as defined in Section 1 of the Public Service Act.

Section 5

Purpose of amendment is to make provision for the refinancing of unemployment insurance beneficiaries to facilitate re-entry into the labour market.

Section 7(1)

Purpose of amendment is to provide for the money of the fund, other than the money required to meet the current expenditure of the fund, to be deposited on behalf of the fund with the Public Investment Corporation.

Section 12:

Purpose of amendment is to make provision for the payment of benefits to contributors who lose part of their income due to reduced working times, and to provide for a fixed rate of payment of maternity benefits.

Section 13

Section 13(3) provides that a contributor's entitlement to benefits accrues at a rate of one day's benefit for every completed six days of employment as a contributor, subject to a maximum accrual of 238 days. It has been found that the maximum of 238 days is not line with Schedule 2 of the Act. In order to address this anomaly, section 13 is amended to provide for 365 days instead of 238 days.

Section 13 is further amended by the insertion of a new provision which seeks to allow contributors to claim benefits if they have credits, regardless of whether or not they claimed that four-year cycle.

Section 14

Purpose of amendment is to repeal section 14(a) of the Act.

Section 17

Purpose of amendment is to increase the period of submitting applications for unemployment benefits. Currently applications must be submitted within 6 months and the proposal is to extend the period for submitting unemployment benefits from 6 to 12 months.

Section 20

Purpose of amendment is to provide that a contributor would be entitled to illness benefits if the days of illness are less than 7 days.

Section 24

Purpose of amendment is to provide for a period when a contributor is entitled to maternity benefits in case of miscarriage.

Section 25

Purpose of amendment is to provide for a period when a contributor is entitled to maternity benefits in case of miscarriage.

Section 30

Purpose of amendment is to extend the period in which the dependents may apply for benefits on behalf of the deceased from 6 months to 18 months. Section 30 is further amended by the insertion of a new provision allowing contributors to nominate their beneficiaries in cases of death benefits.

Section 33

Purpose of amendment is to prohibit any agency or person purporting to be acting on behalf of the applicant to charge a fee against the applicant.

COURT CASES IN 2017

HIGH COURT

Delivery	Parties involved	Key words
19 December 2016	Van der Merwe GW NO & Others v Zonnekus Mansion (Pty) Ltd & Others	Business rescue proceedings in terms of section 131(1), read with section 131(4)(a) of the Companies Act No 71 of 2008; company in liquidation; Locus standi of First Applicant; whether company was conducting business ; whether cogent business plan proposed; SARS position as 'affected party'; abuse of process; position of liquidators in interim; interdictory relief in terms of section 131(4)(b) barring trustees of trust or any other "affected party" as defined in section 128(1)(a) from further business rescue applications in respect of the company without the prior written authorisation of the Senior Duty Judge; costs
14 November 2016	Lifman MR v The Business Zone 983 CC & 3 Others	Companies Act; business rescue; liquidation
11 November 2016	Nkhoma DT & 4 Others v Zonnekus Mansion (Pty) Ltd (In Liquidation), CSARS & Standard Bank of SA Ltd	Applications for leave to appeal various orders in an application for business rescue; consideration whether there is a reasonable prospect of another court reversing the orders
25 October 2016	Dale PA v Aeronastic Properties Ltd	Business Rescue; Application for; Company in final liquidation; Section 131 read with 131(4) of Companies Act 71 of 2008; Requirement in terms of section 131(4)(a) as to reasonable prospect of rescue
23 March 2016	Ntsanwisi v Khoza & others	Income tax: Whether SARS can be ordered to repay a tax amount levied and collected based on a directive without the directive being amended or a new directive being issued

TAX COURT

Delivery	Case number	Key words
14 December 2016	IT 13935	Assessed loss; Bad debts, USP; Whether the Appellant was entitled to an assessed loss, bad debts and other expenses to be deducted
13 December 2016	IT 13791 & 13792	Section 11(a); interest income; home loan
12 December 2016	IT 12821	Exception; valid assessment; dividend
7 December 2016	IT 14027	Exception; Amendment to Grounds of Objection
4 November 2016	IT 13772	Section 24C of the Income Tax Act; future expenditure; section 222 of the Tax Administration Act; whether the Appellant was entitled to deduct future expenditure in terms of section 24C of the Income Tax Act; an Understatement Penalty was payable by the Appellant in

		terms of section 222 of the Tax Administration Act
7 September 2016	IT 13164	Assessed losses; tax avoidance; whether section 103(2) of the Income Tax Act was applicable to assessed losses carried forward by the Appellant
5 September 2016	VAT 1247	Invoice; section 22(3) of VAT Act; crediting of loan account; whether section 22(3) of the VAT Act was applicable in respect of an invoice relating to input tax claimed by the Appellant
25 August 2016	IT 13539/13673	Whether amounts received in terms of a productive asset allowance scheme were taxable as "gross income" as being revenue in nature
28 July 2016	VAT 1345	Motor car deduction
13 May 2016	IT 13635	Whether the Appellant was entitled to condonation for the late filing of an objection
26 April 2016	IT 13775	Taxable benefit; paragraph 2(e) of the Seventh Schedule; whether taxable benefits were granted to expatriate employees or not in terms of section 1 and the Seventh Schedule of the Income Tax Act