TAX UPDATE

For period: 1 January 2015 to 31 March 2015

Prepared by: Johan Kotze

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JK TAX SPECIALISTS

1. INTRODUCTION

The purpose of this update is to summarise developments that occurred during the first quarter of 2015 specifically in relation to Income Tax and VAT. Johan Kotze has compiled this summary and at the time of drafting this summary was Bowman Gilfillan's Head of Tax Dispute Resolution.

The aim of this summary is for clients, colleagues and friends alike to be exposed to the latest developments and to consider areas that may be applicable to their circumstances. The reader is invited to contact Johan Kotze to discuss their specific concerns and, for that matter, any other tax concerns.

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Interpretation notes, rulings and guides are all important aspects of the developments that took place, as they give taxpayers an insight into SARS' application of specific provisions. It is however important to note that these publications are not law, but may bind SARS. Taxpayers should nonetheless consider these publications carefully to determine whether, and how, they are actually applicable to their own circumstances.

Enjoy reading on!

2. NATIONAL BUDGET

2.1 Evolution of tax policy

Tax policy reforms aim to raise revenue in a manner that is fair and efficient, while maintaining social solidarity and supporting long-term economic growth and job creation. An equitable and progressive tax system imposes a similar tax burden on individuals at similar income levels, with a higher proportion of tax paid by those who have higher incomes. An efficient tax system will not unduly influence the economic decisions of taxpayers or make compliance overly burdensome.

The three main sources of tax revenue are personal income tax, corporate income tax and VAT. Tax policy reforms since 1994 have broadened the tax base, increasing the portion of total income that is taxable. Government introduced capital gains tax and broadened the inclusion of fringe-benefits 'in kind' as part of taxable income. Alongside this broadening of the tax base, government has consistently provided tax relief to individuals, offsetting the impact of inflation (i.e. fiscal drag).

Efficiency improvements at the South African Revenue Service (SARS) and expansion of the pay-as-you-earn system (where employers pay tax on behalf of employees) have also enhanced the ability of the state to collect revenues, allowing for net tax relief in previous budgets.

The headline corporate income tax rate was reduced from 40% in 1994 down to 28% in 2008. Yet corporate income tax increased substantially as a share of taxable income until the recession of 2009, supported by strong corporate profitability and high commodity prices. This trend reversed with the onset of the global financial crisis, with negative nominal growth rates of -18% and -1% in 2009/10 and 2010/11 respectively. Corporate income tax revenues have recovered but remained volatile in response to shifting commodity prices and labour unrest, with nominal growth rates fluctuating between 5% and 14% between 2011/12 and 2013/14. In general, revenues from this instrument are more volatile than VAT and personal income tax.

Government has provided significant tax relief and incentives to business, including depreciation allowances that seek to support investment. Tax expenditures, or revenue foregone, to support social or industrial policy objectives is estimated at R120 billion, or 15% of gross tax revenue.

The VAT rate has remained unchanged at 14%. While South Africa's corporate and personal income tax rates are comparable to many Organisation for Economic Cooperation and Development (OECD) countries, its VAT rate remains comparatively low. Since VAT is directed at consumption, it is regarded as more efficient than other taxes, with a less damaging impact on long-term economic growth. Other indirect taxes, such as fuel taxes, were increased more or less in line with inflation.

Between 1998 and 2002, the top personal income tax rate was decreased from 45% to 40%. Between 2005 and 2014, the tax-free threshold (below which individuals do not pay personal income tax) for taxpayers below 65 years old increased by an average of 8.1% per year, from R35 000 to R70 700. The net result is that the effective personal income tax rate has remained below its 1999/2000 peak of 20.6%.

The need for additional revenues to close the structural deficit requires increases in some tax rates. There is little room, however, to broaden the tax base since this approach has largely been exhausted.

2.2 Davis Tax Committee recommendations

The Davis Tax Committee, established in 2013, is advising government on future refinements to the tax system. The committee has noted that compared with rates in other countries, there appears to be some scope to increase taxes on capital income, marginal personal income tax rates and indirect taxes such as fuel levies and VAT. The committee's interim report on small and medium-sized enterprises was released for comment in 2014, and its recommendations on changes to the turnover tax regime for micro businesses are included in these tax proposals. The committee has also published a report on base erosion and profit shifting.

The National Treasury expects reports on the overall tax system, VAT, estate duty, wealth and mining taxes, to be published soon. These reports will inform policy considerations in the 2016 Budget.

2.3 Tax proposals

The 2015 Budget tax proposals aim to increase tax revenues, limit the erosion of the corporate tax base, increase incentives for small businesses and promote a greener economy. The main tax proposals include:

- Increasing marginal personal income tax rates by one percentage point for all taxpayers earning more than R181 900, and adjusting tax brackets and rebates to account for fiscal drag
- Taking further steps to combat base erosion and profit shifting
- Providing for a more generous turnover tax regime for small businesses
- Changing transfer duty rates and brackets.

2.4 Personal income tax

To raise additional tax revenues while enhancing the progressive character of the tax system, government proposes to increase the marginal personal income tax rates by one percentage point for all income tax brackets except the lowest, which will remain at 18%. This also requires a one percentage point increase in the tax rate for trusts.

To provide relief for inflation-related earnings increases (fiscal drag), all income tax brackets and rebates will be increased by 4.2%. The tax-free threshold for individual taxpayers below 65 years will increase from R70 700 to R73 650.

The rates of tax for the 2014/15 tax year and those proposed for 2015/16 are set out below.

2015 year of assessment		**2016 year of assessment**	
Taxable Income	**Rates of tax**	**Taxable Income**	**Rates of tax**
R0 – R174 550	18% of each R1	R0 – R181 900	18% of each R1
R174 551 – R272 700	R31 419 + 25% of the amount above R174 550	R181 901 – R284 100	R32 742 + 26% of the amount above R181 900
R272 701 – R377 450	R55 957 + 30% of the amount above R272 700	R284 101 – R393 200	R59 314 + 31% of the amount above R284 100
R377 451 – R528 000	R87 382 + 35% of the amount above R377 450	R393 201 – R550 100	R93 135 + 36% of the amount above R393 200
R528 001 – R673 100	R140 074 + 38% of the amount above R528 000	R550 101 – R701 300	R149 619 + 39% of the amount above R550 100
R673 101 and above	R195 212 + 40% of the amount above R673 100	R701 301	R208 587 + 41% of the amount above R701 300
Rebates		**Rebates**	
Primary	R12 726	Primary	R13 257
Secondary	R7 110	Secondary	R7 407
Third rebate	R2 367	Third rebate	R2 466
Tax threshold		**Tax threshold**	

Below age 65 Age 65 and over Age 75 and over	R70 700 R110 200 R123 350	Below age 65 Age 65 and over Age 75 and over	R73 650 R114 800 R128 500

2.5 Medical tax credits

Monthly medical scheme contribution tax credits will, from 1 March 2015, be increased from R257 to R270 per month for the first two beneficiaries and from R172 to R181 per month for each additional beneficiary.

2.6 Turnover tax regime for micro businesses

The turnover tax regime was introduced to limit the compliance burden on micro businesses with annual turnover of up to R1 million. These rules eliminate the need for a great deal of paperwork and compliance expenses.

The Davis Tax Committee recommended that this incentive be made more generous to improve the participation of small businesses in the economy and the tax system. Government proposes to adjust the rates and thresholds to make the turnover tax more attractive, as shown below:

2015 year of assessment		**2016 year of assessment**	
Taxable Income	**Rates of tax**	**Taxable Income**	**Rates of tax**
R0 – R150 000	0% of taxable turnover	R0 – R335 000	0% of taxable turnover
R150 001 – R300 000	1% of the amount above R150 000	R335 501 – R500 000	1% of the amount above R335 000
R300 001 – R500	R1 500 + 2% of	R500 001 – R750	R1 650 + 2% of

000	the amount above R300 000	000	the amount above R500 000
R500 001 – R750 000	R5 500 + 4% of the amount above R500 000	R750 001 – R 1 000 000	R6 650 + 3% of the amount above R750 000
R750 001 – R1 000 000	R15 500 + 6% of the amount above R750 000		

2.7 Base erosion and profit shifting

Many countries face the problem of businesses exploiting gaps in international tax rules to artificially shift profits and avoid paying tax. These avoidance measures, practiced widely by multinational firms, substantially reduce their contributions to national tax bases. In recent years, government has taken measures to limit artificial reductions of taxable income through cross-border interest payments.

Building on these steps, government will propose amendments to improve transfer-pricing documentation and reporting, and change the rules for controlled foreign companies and the digital economy. These proposals are in line with matters examined in a recent OECD report, 'Addressing Base Erosion and Profit Shifting', which examined the practice. A December 2014 report by the Davis Tax Committee on the same subject highlighted these concerns in the South African context. Tax returns will place a greater focus on indicators of potential base erosion and profit shifting.

2.8 Transfer duties

Average house prices have recovered slowly over the past two years following a post-2009 decline. The rates and brackets for transfer duties on the sale of property on or after 1 March 2015 will be adjusted to provide relief to middle-income households. The new rates will eliminate transfer duty on all property acquired below R750 000, decrease effective transfer duty liability for properties acquired up to about R2.3 million and increase liability for properties above this amount.

2015 year of assessment		**2016 year of assessment**	
Property value	**Rates of tax**	**Property value**	**Rates of tax**
R0 – R600 000	0% of property value	R0 – R750 000	0% of property value
R600 001 – R1 000 000	3% of the property value above R600 000	R750 001 – R1 250 000	3% of the property value above R750 000
R1 000 001 – R1 500 000	R12 000 + 5% of the property value above R1 000 000	R1 250 001 – R1 750 000	R15 000 + 6% of the property value above R1 250 000
R1 500 001 +	R37 000 + 8% of the property value above R1 500 000	R1 750 001 – R2 250 000	R45 000 + 8% of the property value above R1 750 000
		R2 250 001 +	R85 000 + 11% of property value above R2 250 000

2.9 Medical tax credits as part of PAYE: over 65 years

Employees over 65 are experiencing a decrease in their take-home pay as a result of the move to medical tax credits, although they may claim back some of these amounts on assessment after the end of the tax year. To alleviate this burden, it is proposed that medical tax credits related to medical scheme contributions be taken into account for both PAYE and provisional tax purposes.

2.10 Bus rapid transit payments to affected taxi operators

In 2010, government introduced the bus rapid transit system, which resulted in the compensation of affected taxi operators for the loss of potential earnings. It is proposed that the tax treatment of such payments to affected taxi operators be reviewed.

2.11 Employee share schemes

The interrelationships in the application of section 8C of the Income Tax Act, including the taxation of directors and employees on vesting of equity instruments; the attribution of capital gains to beneficiaries; the income tax exemption of dividends; and the employees' tax provision related to the return of capital, will be reviewed to remove anomalies.

2.12 Income and disposal to and from deceased estates

Section 25 of the Income Tax Act provides that no income or disposal is triggered in the deceased's hands upon death, but that income may be recognised in the hands of the deceased estate, heir or legatee. Paragraph 40 of Schedule 8, however, recognises capital gains and losses upon death. To address the anomalies created when the two regimes interact, the provisions will be examined and amendments may be proposed.

2.13 Withdrawal from retirement annuity funds by non-residents

Non-residents who move to South Africa for a fixed term of employment often contribute to a retirement annuity fund to continue saving for retirement in a tax-efficient manner. The current definition of 'retirement annuity fund' does not allow these individuals to withdraw the amounts they have saved over this fixed term if they return to their home countries. In contrast, if South Africans emigrate, they are allowed to withdraw their retirement annuity interest. The mismatch in treatment will be reviewed.

2.14 Harmonisation of the treatment of retirement funds

The taxation of contributions and the rules on compulsory annuitisation for pension funds, provident funds and retirement annuity funds will change from 1 March 2016. The level of deductible contributions will be limited to 27.5% of the greater of taxable income or remuneration per year. An additional amendment will be investigated to correct an omission in 2013 that inadvertently excludes some retirement funds that enjoy the benefit of higher deductions without being subject to the uniform annuitisation rules.

2.15 A maximum age for the preservation of retirement assets

From 1 March 2015, a retirement fund member may defer the drawing of their retirement income until after their retirement date (if the retirement fund allows). This will provide greater flexibility for retirement fund members and encourage the preservation of retirement assets. However, to limit tax planning opportunities, it is proposed that a maximum age at which withdrawals must be taken be introduced. This is in line with other countries that have similar retirement funding arrangements.

2.16 Estate duty and retirement funds

Amendments in 2008 removed the upper age limit at which an individual was required to purchase an annuity if they had an interest in a retirement annuity fund, and excluded retirement fund benefits from the dutiable estate when a member passed away. These two amendments have made it possible for some individuals to avoid estate duty by transferring their assets into a retirement annuity fund before their death. In the deceased's tax calculation, lump sums paid to the estate are subject to the lump sum retirement taxable. However, lump sums equal to amounts above the allowable deduction (non-deductible contributions) are not subject to the lump sum tax table or estate duty.

To eliminate the potential to avoid estate duty, government proposes that an amount equal to the non-deductible contributions to retirement funds be included in the dutiable estate when a retirement fund member passes away.

2.17 Corporate reorganisation rules

Township developer allowance: Section 45 of the Income Tax Act makes provision for allowances on capital assets to be transferred. However, the definition of a capital asset in section 41 excludes trading stock. The township developer allowance covers assets that qualify as trading stock, so it cannot be transferred in terms of this section. Government proposes to amend the wording of the section to include the allowance.

Asset for share transaction: The current anti-avoidance measure in section 42(5) of the Income Tax Act is creating anomalies and needs to be clarified.

Cross-border intra-group transactions: In 2012, section 45(3A) of the Income Tax Act was amended to clarify that the section also applies to cross-border intra-group transactions. However, subparagraph (c) of this section was inadvertently not amended, which creates anomalies. It is proposed that this subparagraph be amended to clarify that the provisions of this section refer to the same group of companies as defined in section 1 of the act.

2.18 Distribution and issue of shares for no consideration

The current wording in section 40C of the Income Tax Act creates anomalies when a company distributes shares internally. It is proposed that changes be made to clarify that the section's provisions only apply to the issue of shares, not their distribution.

2.19 Amounts from disposal of shares

Government will consider the provisions of section 9C of the Income Tax Act to address the problem of return of capital after a taxpayer has held a share for a period of three years, as well as the meaning of the term 'disposal' for the purpose of this section.

2.20 Cancellation of contracts

If a contract is cancelled, it is expected that the parties will be restored to the status quo before the transaction. However, it is argued that the cancellation of contracts results in the rebasing of the asset's base cost, leading to zero capital gain or capital loss. This is prevalent between connected persons. It is proposed that this potential anomaly be removed.

2.21 Third-party-backed shares

In 2014, changes were made in the Income Tax Act regarding the refinancing of third-party-backed shares for qualifying transactions and limited pledges. Further refinements are needed to clarify the requirements or meaning of 'qualifying purpose' to further the provisions' objectives.

2.22 Sharia-compliant financing arrangements

In 2010, government enacted legislation that recognises certain forms of Islamic finance as equivalent to traditional finance entailing interest. In 2014, changes were made in the Income Tax Act to include public entities in the Islamic finance arrangements and to extend the definition of sukuk to include other entities. To create a more enabling environment for Islamic finance, it is proposed that the murabaha and sukuk financing arrangements be extended to listed entities and that section 8A of the Securities Transfer Tax Act (2007) be amended to cater for murabaha transactions.

2.23 REITS

In 2012, a special tax dispensation for listed REITS was introduced in the Income Tax Act. The provisions of section 25BB will be refined to remove anomalies.

2.24 Unlisted property-owning companies

Unlisted property-owning companies marketed to the general public or held by institutional investors do not qualify for the same special tax dispensation as listed real estate investment trusts. Government proposes that unlisted property-owning companies should qualify for the same tax treatment if they become regulated. A regulatory framework for unlisted property-owning companies will be developed.

2.25 Hedge funds

Government proposes that hedge funds be declared as collective investment schemes, subjecting them to similar rules as other collective investment schemes in terms of the Collective Investment Schemes Control Act (2002). Tax amendments will be considered to minimise any inadvertent tax consequences that may arise from the restructuring of regulated hedge funds.

2.26 Securities lending arrangements

The transfer of collateral in a securities lending arrangement provides the lender with confidence that they will not lose the underlying value of the securities lent, which increases liquidity in this market.

However, the transfer of collateral currently results in securities transfer tax and capital gains tax. The taxation consequences of the collateral transfer may negatively affect liquidity and South Africa's attractiveness as an investment destination.

Government proposes to review the tax treatment of the transfer in beneficial ownership of collateral to reduce any negative effects on acceptable business practices and limit the use of collateral in possible tax avoidance arrangements. In addition, the current tax treatment of securities lending arrangements will be reviewed to account for corporate actions during the term of such arrangements.

2.27 Introduction of the SAM basis of regulating long-term insurers

In 2016, the Financial Services Board intends to implement Solvency Assessment and Management (SAM), a risk-based supervisory regime for long- and short-term insurers. The SAM basis of valuing policyholder liabilities is not in line with the current tax treatment. To take account of SAM, government proposes a new valuation method for the policyholder liabilities of long-term insurers. The new approach will be based on an adjusted International Financial Reporting Standards method of valuation.

2.28 Industrial policy projects

The industrial policy project tax incentive supports the National Industrial Policy Framework's objectives to diversify South Africa's industrial output, develop the knowledge-based economy and create higher levels of employment. To allow for more projects to be included, it is proposed that the window period for the incentive be extended from 31 December 2015 to 31 December 2017.

2.29 Depreciation deductions for hydropower generation

Investments in renewable energy to generate electricity are incentivised through accelerated depreciation deductions. However, a capacity limit of 30 megawatts is in place for hydropower generation because of concerns about possible environmental impact.

This limit may be overly restrictive because installed capacity alone may not be the best indication of a project's environmental impact. Consideration will be given to including hydropower generators of more than 30 megawatts if other environmental concerns are addressed. A broader incentive could increase electricity supply and support the transition to a low-carbon economy.

2.30 Urban development zone incentive

Current legislation allows municipalities with a population of more than 2 million people to demarcate two areas as urban development zones (UDZs). With the amalgamation of various municipalities, the need for the demarcation of more than one UDZ has become apparent. Consideration will be given to allowing for the demarcation of two or more UDZs per municipality, within an overall limit of the area of the UDZs.

2.31 Research and development incentive

The research and development (R&D) tax incentive was introduced to boost R&D as a percentage of gross domestic product, and to encourage knowledge transfer and skills development. For expenditure to qualify for the tax incentive in terms of the Income Tax Act, the taxpayer must submit an application for approval to the adjudication committee. However, the backlog in the approval process is creating difficulties, especially for smaller businesses, which have to wait months for approval. Measures will be considered to ensure that taxpayers are not disadvantaged by undue delays by the adjudication committee. The issue of third-party funding for R&D activities will also be considered.

2.32 Government grants

Government will review the tax treatment of government grants to remove unintended anomalies arising before and after the introduction of section 12P of the Income Tax Act, as well as the regulatory mechanism relating to these grants. Government aims to address anomalies related to grants that were not previously listed, the claiming of deductions on tax-exempt grants, and grant relationships with public-private partnerships.

2.33 Indefeasible right of use of transmitting electronic communications outside South African territorial waters

In 2009, government introduced a deduction for premiums or consideration paid for the 'right of use' of transmission lines or cables used to transmit electronic communications outside South African territorial waters, where the term of the right of use is 20 years or more. Due to the change in business models and international best practices, it is necessary to review the term set as a condition of this deduction.

2.34 Revision of manufacturing assets deduction

Section 12C of the Income Tax Act makes provision for an accelerated depreciation deduction for manufacturing assets, provided that the assets are directly used by the taxpayer for the purposes of his or her trade. Due to changes in the business models of some manufacturing activities, government will review the conditions of the granting of this allowance without undermining the current limitation provisions in section 23D of the Income Tax Act.

2.35 Film incentives

Government will refine film incentives in section 12O of the Income Tax Act to remove anomalies arising as a result of the interaction of its provisions with other provisions in the Income Tax Act.

2.36 Special economic zones: definition of qualifying company

In order for a company to qualify for the 15% special economic zone income tax benefit, at least 90% of its income must be derived from conducting business or providing services within approved special economic zones. However, there is a risk that profits may be artificially shifted from fully taxable connected persons to the qualifying company. Government therefore proposes that a company be disqualified from the tax benefit if more than 20% of its expenditure or gross income arises from transactions with connected persons.

2.37 Withdrawal of special foreign tax credits for service fees sourced in South Africa

In 2011, government introduced a special foreign tax credit for withholding taxes imposed on South African residents by foreign countries for services rendered in South Africa for clients who were residents in those countries. However, taxes imposed in these circumstances were not in accordance with the provisions of tax treaties between South Africa and these countries. The concession aims to alleviate the compliance burden on South African taxpayers to apply for a refund of the tax that was incorrectly imposed. While the introduction of relief was well intended, it has resulted in a significant compliance burden to both taxpayers and SARS. Some taxpayers are also exploiting this relief. As a result, it is proposed that the special foreign tax credits for services be withdrawn.

2.38 Capital gains tax implications on cross-issue of shares

In 2013, government amended the Income Tax Act to counter base erosion and profit shifting. If a South African resident company issues shares as a consideration for an acquisition of shares in a foreign company, it will result in a capital gain for the resident company. Although the concerns that led to the changes in tax legislation are understood, these changes may affect legitimate commercial transactions, curtailing the growth and expansion of South African multinationals. Government will consider relaxing the provision's requirements, without losing sight of the initial policy intent, which is to counter untaxed corporate migration out of South Africa.

2.39 Controlled foreign company rules

Before 2011, the controlled foreign company (CFC) legislation had diversionary rules to prevent the shifting of income offshore through the sale of goods by a CFC to a connected resident. In 2011, these rules were removed because transfer pricing rules could be applied as an alternative. However, CFC rules have proven less effective in immediately addressing profit shifting by South African resident companies. Although transfer pricing rules can be applied in these circumstances, the CFC diversionary rules are more effective in taxing profits from these transactions. It is proposed that diversionary rules applicable to the sale of goods by a CFC to a connected resident be reinstated. In addition, consideration will be given to allowing CFCs held by interposed trusts to be subject to tax in South Africa.

2.40 Sale of immovable property by non-residents

Withholding on disposal of immovable property by non-residents: Section 35A of the Income Tax Act states that a purchaser does not need to withhold tax from a deposit 'until the agreement for that disposal has been entered into'. It is proposed that the wording should be amended to clarify the timing of the withholding.

Definition of immovable property: To remove any anomalies, it is proposed that the definition of immovable property in paragraph 2(2) of schedule 8 be aligned with the definition in the Organisation for Economic Cooperation and Development's model tax treaty, specifically the definition related to the right to work mineral deposits.

2.41 Withholding tax on interest

Definition of interest: It is proposed that interest for withholding tax purposes be defined. This will ensure that there is no confusion with other definitions related to interest in the Income Tax Act.

Alignment of section 50B(1) with section 9(2)(b) of the Income Tax Act: The provisions of these sections should be aligned to provide for exemption for interest paid to a non-resident for debt owed by another non-resident, unless the other non-resident was present in South Africa for a period exceeding 183 days or the debt claim is effectively connected to a permanent establishment in South Africa.

2.42 Withholding tax on services

It is proposed that the section be reviewed to clarify definitions and remove any anomalies.

2.43 VAT - Educational services

Educational services are currently exempt from VAT, but there are uncertainties around the exact definition of 'educational services' and the VAT treatment of certain expenditures, such as accommodation and the provision of meals. The Davis Tax Committee is reviewing the VAT implications for educational institutions, and its conclusions will guide potential changes.

2.44 VAT - Thresholds for payment basis

To help with cash flow, some vendors with annual taxable supplies below R2.5 million are allowed to account for VAT on a payment basis rather than an accrual basis. These vendors must be natural persons or unincorporated bodies of which all members are natural persons. The Davis Tax Committee is reviewing this provision. There may be scope to increase the threshold and/or broaden the application to include incorporated businesses under this regime. However, the abuses previously experienced when businesses on the accrual basis transact with businesses on the payment basis will have to be addressed.

2.45 VAT on SABC TV licences

The South African Broadcasting Corporation Limited (SABC) is a Public Finance Management Act (1999) Schedule 2 Public Entity. Under the Broadcasting Act (1999), anyone who possesses or uses a television set or any device capable of receiving a broadcast television signal must pay an annual television licence fee. The SABC issues notices of renewal two months before the TV licence expires.

Under VAT rules, the SABC should account for output tax on the earlier of an issued invoice or payment received. However, the SABC is experiencing a high level of licence non-payment. This is compounded by the VAT requirement to account for output tax on an invoice basis for revenue it might not be able to collect. Government proposes that the SABC be allowed to account for VAT on a payment basis on its entire operations, including that of its subsidiaries.

2.46 VAT - Regulation prescribing foreign electronic services

To address base erosion and profit shifting, several legislative amendments were made to the VAT Act, including the introduction of a framework for VAT on foreign electronic services. The regulations prescribing electronic services will be updated to include software and other electronic services and to remove some uncertainties.

2.47 VAT - Adjusted cost

To remove unintended anomalies, it is proposed that the definition of 'adjusted cost' in section 1 of the VAT Act be amended to deem VAT at the standard rate to be included where the acquisition was subject to VAT at the zero-rate.

2.48 Commercial accommodation

The definition of 'commercial accommodation' in section 1 of the VAT Act states that an establishment is a commercial accommodation if it regularly or systematically supplies the listed supplies and where the total annual receipts from such supplies exceed (or are expected to exceed) R60 000 in a period of 12 months. It is proposed that the registration and threshold requirements of a commercial accommodation be reviewed to limit potential abuse.

2.49 VAT - Fixed property

The supply of a share by a share block company that confers the right to or an interest in the use of immovable property is subject to VAT at the standard rate in terms of section 7(1)(a) of the VAT Act because it is specifically included in the definition of fixed property in section 1 of the act. Similar rights or interests in the use of immovable property supplied by a cooperative, however, do not fall within the ambit of the definition of 'fixed property'. To address this anomaly, it is proposed that the definition of 'fixed property' in section 1 be amended to include a right or interest in the use of immovable property supplied by cooperatives or other entities entering into similar arrangements.

2.50 VAT - Resident of the republic

It is proposed that the definition of 'resident of the republic' in section 1 of the VAT Act be clarified to remove anomalies.

2.51 VAT - Deemed supply: corporate reorganisation rules

To qualify for corporate relief in terms of section 8(25) of the VAT Act, a vendor must comply with the requirements of the provisions of section 42, 44, 45 or 47 of the Income Tax Act. These provisions only apply to groups of companies that are incorporated, and do not apply to unincorporated entities such as joint ventures and partnerships. The VAT Act, however, recognises unincorporated persons as vendors. It is proposed that the VAT Act be amended to remove the unintended anomalies and allow for reorganisation relief for all vendors.

2.52 VAT - Time of supply: connected persons (undetermined amounts)

It is proposed that sections 9(2) and 10(4) of the VAT Act be amended to clarify the time and value of supplies between connected persons where the value of the supply cannot be determined until a future date.

2.53 VAT - Zero-rating: goods delivered by a cartage contractor

The supply of movable goods in terms of a sale or instalment sale agreement to a customs-controlled enterprise or an industrial development zone operator is subject to zero-rated VAT, provided that the goods are delivered by a registered cartage contractor whose 'main activity' is transporting goods. In terms of SARS Interpretation Note 30 (issue 3), the term 'cartage contractor' is defined as a person whose 'activities include' the transportation of goods. This has a wider scope than the VAT Act's current requirement. It is proposed that the term cartage contractor in section 11(1)(m)(ii) of the VAT Act be broadened to align it with the term's definition in Interpretation Note 30 (issue 3).

2.54 VAT - Zero-rating of services: loop transactions

Section 11(1)(q) of the VAT Act provides for the zero-rating of goods supplied to a non-resident recipient that are delivered to the recipient's customer in South Africa. Section 11(2)(l)(ii)(bb) of the VAT Act, however, allows for the zero-rating of services supplied to a non-resident recipient if the services are in relation to goods situated in South Africa and form part of the recipient's supply of goods to a vendor in the country. The VAT Act does not provide a comparable zero-rating provision for services supplied to a non-resident recipient but that are actually provided to the recipient's customer in South Africa where such services do not form part of the supply referred to in section 11(2)(l)(ii)(bb) of the VAT Act. It is proposed that a comparable provision be included in the VAT Act to cater for such loop transactions where the supply is of services only and they do not relate to any goods situated in South Africa.

2.55 VAT - Zero-rating of services: vocational training

In terms of section 11(2)(r) of the VAT Act, the words 'for an employer who is not a resident' implies that for zero-rating to apply, a contractual relationship must exist between the person supplying the vocational services and the employer. It does not cater for situations where the employees' training is subcontracted by a non-resident supplier to a third-party vendor in South Africa. It is proposed that the section be amended to refer to vocational training provided 'for the benefit' of a non-resident employer.

2.56 VAT - National housing programme

In terms of section 11(2)(s) and section 8(23) of the VAT Act, a person is deemed to have supplied services to a public authority or municipality to the extent of any payment made to or on behalf of that vendor in terms of the national housing programme contemplated in the Housing Act (1997), which is approved by the Minister of Finance after consultation with the Minister of Human Settlements. These services may be zero-rated. There has been confusion among taxpayers and municipalities regarding the scope of the services that qualify for zero-rating. It is proposed that the provisions of the sections dealing with this issue be reviewed to remove anomalies.

2.57 Transfer Duty Act

The definitions of ‘date of acquisition’ and ‘property’ in the Transfer Duty Act (1949) need to be reviewed to align the terms with other legislative provisions.

2.58 Tax administration

Self-assessment system for income tax: Amendments to the Income Tax Act are proposed to provide for the move to an income tax self-assessment system.

Appeal and dispute resolution procedures for customs and excise: Uniform appeal and dispute resolution procedures for taxes administered by SARS are proposed by aligning the procedures under the Customs Control Act (2014), the Customs Duty Act (2013) and the Customs and Excise Act (1964) with dispute resolution procedures under the Tax Administration Act (2011).

3. NOTICES & REGULATIONS

3.1 Public notice listing arrangements for purposes section 35(2) and 36(4) of the Tax Administration Act

1. General

In this notice, unless the context indicates otherwise, any word or expression to which a meaning has been assigned in the Income Tax Act, 1962, or the Tax Administration Act, 2011, has the meaning so assigned.

2. Reportable arrangements

The following arrangements have been identified to be reportable arrangements:

2.1 Any arrangement that would have qualified as –

(a) a 'hybrid equity instrument' in terms of section 8E of the Income Tax Act, 1962, if the prescribed period in that section had been 10 years; or

(b) a 'hybrid debt instrument' in terms of section 8F of the Income Tax Act, 1962, if the prescribed period in that section had been 10 years, but does not include any instrument listed on an exchange regulated in terms of the Financial Markets Act, 2012;

2.2 Any arrangement in terms of which –

(a) a company buys back shares on or after the date of publication of this notice from one or more shareholders for an aggregate amount exceeding R10 million; and

(b) that company issued or is required to issue any shares within 12 months of entering into that arrangement or of the date of any buy-back in terms of that arrangement;

2.3 Any arrangements in terms of which –

(a) a person that is a resident makes any contribution or payment on or after the date of publication of this notice to a trust that is not a resident and has or acquired a beneficial interest in that trust; and

(b) the amount of all contributions or payments, whether made before or after the date of publication of this notice, or the value of that interest exceeds or is reasonably expected to exceed R10 million, excluding any contributions or payments made to or beneficial interest acquired in any –

(i) portfolio compromised in any investment scheme contemplated in paragraph (e)(ii) of the definition of 'company' in section 1(1) of the Income Tax Act, 1962; or

(ii) foreign investment entity as defined in section 1(1) of the Income Tax Act, 1962;

2.4 Any arrangement in terms of which one or more person acquire the controlling interest in a company on or after the date of publication of this notice, including by means of acquiring shares, voting rights or a combination of both, that –

(a) (i) has carried forward or reasonably expects to carry forward a balance of assessed loss exceeding R50 million from the year of assessment immediately preceding the year of assessment in which the controlling interest is acquired; or

(ii) has reasonably expects to have an assessed loss exceeding R50 million in respect of the year of assessment during which the controlling interest is acquired, or

(b) directly or indirectly holds a controlling interest in a company referred to in paragraph (a); and

2.5 Any arrangement between a person that is a resident and a person that qualifies as an insurer in terms of any law of any country other than the Republic (hereinafter referred to as the foreign insurer) in terms of which –

(a) an aggregate amount that exceeds or is reasonably expected to exceed R5 million has been paid or becomes payable by the resident to the foreign insurer; and

(b) any amount payable on or after the date of publication of this notice, in cash or otherwise, to any beneficiary in terms of that arrangement is to be determined mainly by reference to the value of particular assets or categories of assets that are held by or on behalf of the foreign insurer or by another person for purposes of that arrangement.

3. Excluded arrangements under section 36(4) of the Tax Administration Act, 2011

Any arrangement referred to in section 35(1) of the Tax Administration Act, 2011, is an excluded arrangement if the aggregate tax benefit which is or may be derived from that arrangement by all participants to that arrangement does not exceed R5 million.

4. INTERPRETATION NOTES

4.1 VAT – The supply of goods and services by professional hunters and taxidermists to non-residents – No. 81

This Note explains the VAT treatment of various supplies made to foreign hunters, which includes hunting services, taxidermy services, the supply of a trophy and the subsequent export of the trophy.

The various goods and services generally supplied to foreign hunters are:

- Accommodation

  A foreign hunter will usually be provided with accommodation by the hunting outfitter as part of the overall hunting safari package.

- Hunting services

  Hunting services may include game viewing, tracking game, assistance with the hunt and other related services but exclude raw preparation and taxidermy services.

- Trophy fee and raw trophy

Once the foreign hunter has hunted the animal, the foreign hunter becomes the owner of the raw trophy and is required to pay a trophy fee, irrespective of whether the animal (or any part of the animal) is retained by the hunter. Hunting outfitters may also require hunters to pay trophy fees for wounded animals.

- Dip and pack services

  These services are performed as the initial treatment of the raw trophy and include all work which may be required to ensure that the trophy does not decay.

- Taxidermy services

  Taxidermists supply both goods (for example, the mounting forms) and services to the foreign hunter at an all-inclusive price.

- Other services consumed in the Republic

  These services may form part of the hunting safari package or may be supplied separately by other vendors and include services such as transportation, car rental, medical assistance and so forth.

Accommodation, hunting services and other goods or services supplied or rendered while the foreign hunter is present in South Africa are subject to VAT at the standard rate, unless the supply is exempt under section 12. The supply of the trophy by the hunting outfitter to the foreign hunter qualifies for zero-rating if the trophy is subsequently exported to the foreign hunter. The supply of dip and pack and taxidermy services qualifies for zero-rating if the trophy is exported to the foreign hunter. The zero-rating of the abovementioned supplies are subject to the relevant supplier retaining supporting documentary evidence as is acceptable to the Commissioner.

4.2 Income Tax – Trading stock: Assets not used as trading stock – No. 11(3)

In this Note unless the context indicates otherwise:

- 'paragraph (jA)' means paragraph (jA) of the definition of 'gross income' in section 1(1), and
- 'paragraph (jA) asset' means an asset contemplated in paragraph (jA).

This Note provides guidance on the application and interpretation of paragraph (jA) and its interaction with other provisions of the Act.

Taxpayers sometimes manufacture capital assets for use in their businesses which are similar to the trading stock which they manufacture for resale. The treatment of the amount received or accrued on disposal of such manufactured capital assets was the subject of a dispute between SARS and the taxpayer in C: SARS v Volkswagen of South Africa (Pty) Ltd. The taxpayer in that case manufactured motor vehicles for sale to the public but also manufactured vehicles for its own use which it used for some time and then sold. SARS argued that the proceeds on disposal of the latter vehicles were of a revenue nature. However, the court disagreed, holding that the amount derived from the disposal of these vehicles was of a capital nature.

As a result of the decision in the Volkswagen case paragraph (jA) was inserted into the definition of 'gross income' in section 1(1). The effect of this deemed inclusion in gross income means that despite the amounts derived from the disposal of such assets being of a capital nature, they are deemed to be gross income and the assets remain trading stock until disposed of.

Any amount received by or accrued to a taxpayer from the disposal of a paragraph (jA) asset used as a capital asset on or after 12 December 2001 must be included in the taxpayer's gross income. This inclusion in gross income means that a paragraph (jA) asset constitutes trading stock as defined in section 1(1) and section 22 will therefore apply.

In order to avoid double taxation, amounts included in paragraph (jA) are specifically excluded from inclusion in income under section 8(4)(a) and 22(8)(b)(iv).

The deductibility of costs associated with paragraph (jA) assets will be considered under section 11(a) read with section 23(g). No capital allowances can therefore be claimed for these assets

4.3 Income Tax – Additional deduction for learnership allowance – No. 20(5)

In this Note unless the context indicates otherwise:

- ‘annual allowance’ means a deduction granted under section 12H(2) during any year of assessment in which a learner is a party to a registered learnership agreement,
- ‘completion allowance’ means a deduction granted under section 12H(3) and (4) in a year of assessment in which a learner successfully completes a learnership,
- ‘SETA’ means a sector education and training authority established under the Skills Development Act and
- ‘Skills Development Act’ means the Skills Development Act No. 97 of 1998.

This Note provides clarity on the interpretation and application of section 12H which provides deductions for registered learnership agreements.

The amendments to section 12H by the Taxation Laws Amendment Act No. 43 of 2014 have been taken into account in this Note and are effective from 20 January 2015 and applicable to all learnership agreements entered into on or after that date.

Section 12H provides additional deductions to employers for qualifying learnership agreements. These additional deductions are intended as an incentive for employers to train employees in a regulated environment in order to encourage skills development and job creation. Training contracts that qualify for these deductions are learnership agreements and apprenticeships registered with a SETA. These additional deductions consist of an annual allowance and a completion allowance.

Section 12H provides an annual allowance and a completion allowance to employers that are a party to a qualifying learnership agreement with an employee. The annual allowance of R30 000 is subject to a pro rata reduction when the number of full months in a year of assessment is less than 12. The completion allowance is limited to R30 000 when the learnership is for a period of less than 24 full months. For longer agreements the completion allowance is R30 000 multiplied by the number of consecutive 12-month periods covered by the agreement. The allowances are increased to R50 000 for learnerships entered into with employees having a disability.

5. DRAFT INTERPRETATION NOTES

5.1 Whether certain quarrying operations constitute mining operations

This Note provides guidance on whether the extraction of the following deposits from the earth constitute 'mining operations' and 'mining' for income tax purposes:

- Clay
- Granite
- Gravel
- Limestone

- Rock
- Sand
- Slate
- Stone

Any explanations and examples used in this Note must be read in the context of the above composites only. Whilst it is acknowledged that certain mining processes in general may involve other processes (for example, manufacture) in order to win or recover minerals from the soil, the discussion in this Note is limited to the above composites and does not apply to the winning or recovering of any mineral or substance not mentioned.

The South African mining industry has historically received favourable tax concessions, especially in relation to its capital expenditure on mining assets which qualifies for an immediate redemption against income derived from mining operations under section 15(a) read with section 36. Under section 36(7E) the taxable income derived from mining operations is ring-fenced from taxable income derived from other trades.

The concession for persons carrying on mining operations was made in view of the high risk and considerable expenditure incurred in the early stages of the mining enterprise. In order to encourage the profitable exploitation of mineral resources it is vital that the initial capital expense be recovered as and when the enterprise starts generating profits. The rationale behind the capital redemption allowance available for miners is to encourage the winning (recovery) of minerals through a method or process of mining.

A strict interpretation of the relevant legislation is followed in order to ensure that only persons who are actually conducting mining operations are entitled to claim the capital redemption allowance available for miners.

This approach to interpretation was supported by the court in Western Platinum Ltd v C: SARS in which Conradie JA stated the following:

‘*[1] The fiscus favours miners and farmers. Miners are permitted to deduct certain categories of capital expenditure from income derived from mining operations. Farmers are permitted to deduct certain defined items of capital expenditure from income derived from farming operations. These are class privileges. In determining their extent, one adopts a strict construction of the empowering legislation. That is the golden rule laid down in Ernst v Commissioner for Inland Revenue 1954 (1) SA 318 (A) at 323C-E and approved in Commissioner for Inland Revenue v D & N Promotions (Pty) Ltd 1995 (2) SA 296 (A) at 305A-B.*’

A restrictive approach to interpretation must accordingly be applied when determining whether a quarrying operation constitutes a mining operation and hence entitles the operator to claim the favourable capital redemption allowances available to miners under section 15(a) read with section 36 in respect of such operations.

In addition, a distinction must be drawn between mining operations and a process of manufacture. This distinction has to be made in order to establish whether capital expenditure on mining assets used to extract minerals from the earth qualifies for the capital redemption allowance available to miners (see section 15(a) read with section 36) or alternatively the allowances available for persons carrying on a process of manufacture (see section 12C and 12E).

The terms ‘mining operations’ and ‘mining’ must be interpreted to mean those operations conducted by a person to win minerals from the earth for their inherent mineralogical qualities. Such operations include various activities but do not include operations to the extent that their purpose is to obtain materials from the earth for their physical properties for agriculture, building, road making, landscaping, construction or similar purposes.

Activities undertaken in respect of materials extracted for their physical attributes constitute manufacturing processes and not mining operations. The capital equipment used in both the initial extraction operation and subsequent process of manufacture qualifies for the allowance under section 12C or 12E.

5.2 Rules for the translation of amounts measured in foreign currencies other than exchange differences governed by section 24I

In this Note unless the context indicates otherwise:

- ‘authorised dealer’ means an institution authorised by the Minister of Finance to act as an authorised dealer in foreign exchange for the purposes of the Exchange Control Regulations administered by the Financial Surveillance Department of the Reserve Bank;
- ‘average exchange rate’ means average exchange rate as discussed in the Note;
- ‘buy rate’ means the rate at which an authorised dealer will buy foreign currency;
- ‘CMA’ means Common Monetary Area comprising Lesotho, Namibia, Swaziland and South Africa;
- ‘CMA currency’ means the currency of any member of the CMA and includes the Lesotho Loti, the Namibian dollar, the Swaziland lilangeni and the rand;
- ‘CFC’ means ‘controlled foreign company’ as defined in section 9D(1);
- ‘domestic PE’ means a PE located in South Africa;
- ‘DTMC’ means ‘domestic treasury management company’ as defined in section 1(1);
- ‘foreign currency’ means any currency other than the rand;
- ‘foreign currency amount’ means any amount denominated in a foreign currency that is received by or accrues to a person, or

expenditure or loss denominated in a foreign currency incurred by a person, during a year of assessment, including any amounts of a capital nature;

- 'foreign PE' means a PE located outside South Africa;
- 'functional currency' means functional currency as discussed in the Note;
- 'HQC' means 'headquarter company' as defined in section 1(1);
- 'IAS 21' means International Accounting Standard 21 'The Effects of Changes in Foreign Exchange Rates';
- 'ISC' means 'international shipping company' as defined in section 12Q;
- 'non-trading trust' means any trust that is not engaged in trade;
- 'PE' means 'permanent establishment' as defined in section 1(1);
- 'recognise' and 'recognition', in relation to a foreign currency amount, refers to the receipt or accrual of any amounts denominated in a foreign currency or to the incurral of any expenditure or loss in a foreign currency, as the case may be;
- 'sell rate' means the rate at which an authorised dealer will sell foreign currency;
- 'spot rate' means spot rate as discussed in the Note, and
- 'translate' refers to the restatement of a foreign currency amount in rand.

This Note provides guidance on the application of the foreign currency translation rules contained in the Act, except for those in:

- section 24I; and
- the Eighth Schedule to the Act which are dealt with in the Draft Comprehensive Guide to Capital Gains Tax (Issue 5).

Residents are subject to normal tax on their worldwide taxable income, that is, taxable income derived from sources within and outside South Africa. A person that is not a resident is only subject to normal tax on taxable income derived from a source within South Africa.

In determining taxable income, foreign currency amounts must be translated to an equivalent amount in rand using either a spot rate or an average exchange rate. The Act generally prescribes which rate must be used depending upon the nature of the underlying transaction and the type of taxpayer involved.

This Note discusses the translation rules in sections 6quat(4) and (4A), 6quin(4), 9A, 9D(6), 25D, 35A(5), 47J, 49H, 50H, 51H and 64N. Depending on the circumstances, the determination of a person's normal tax liability may require the application of more than one of these provisions. For example, a natural person may use the spot rate to translate foreign currency amounts includable in taxable income for a year of assessment in accordance with section 25D(1). In addition, assuming some of the foreign currency amounts were from a foreign source and the natural person qualified for a foreign tax rebate on the foreign tax paid on that income, the natural person would apply the average exchange rate to translate the amount of foreign tax to rand under section 6quat.

In general, subject to the specific provisions governing foreign tax rebates, dividends tax rebates, blocked foreign funds, hyperinflationary currencies, exchange items and capital gains and losses:

- the spot rate must be used by:
    - any natural person and non-trading trust, unless that person or trust elects to use the average exchange rate in a year of assessment in accordance with section 25D(3);
    - any person to translate any foreign currency amount which has been deducted or withheld from amounts payable to a non-resident in accordance with section 35A (sales of immovable property), section 47J (amounts paid to entertainers or

sportspersons), section 49H (royalties), section 50F (withholding tax on interest, effective in 2015) or section 51F (withholding tax on services, effective in 2016);

- any foreign PE, CFC, HQC, DTMC or ISC to translate amounts recognised by it in foreign currencies other than its functional currency to its functional currency;
- any domestic PE; and
- any foreign PE with a functional currency in a CMA currency to translate other foreign currencies to rand, unless the person is an individual or non-trading trust which has elected to use an average exchange rate; and

- the average exchange rate must be used by:
  - any natural person or trust that elects to use it in a year of assessment in accordance with section 25D(3); and
  - any foreign PE, CFC, HQC, DTMC or ISC to translate its taxable income in its functional currency to rand.

Depending on whether the person has or is a foreign PE, CFC, HQC, DTMC or ISC, amounts in rand must either be left as is or be translated to the foreign PE, CFC, HQC, DTMC or ISC's functional currency at spot before being translated back to rand at an average exchange rate.

5.3 Headquarter companies

This Note provides guidance and clarity on the interpretation and application of section 9I which deals with headquarter companies. Section 9I was initially inserted into the Act effective for years of assessment commencing on or after 1 January 2011.

The Note also briefly discusses the provisions of the Act that provide special tax relief for headquarter companies, as well as the specific anti-avoidance rules that are designed to prevent misuse or abuse of those provisions.

The Note does not discuss all of the sections which are applicable to headquarter companies. For example, the Note does not discuss 'gross income' as defined in section 1(1) or section 11(a) which, although these sections do not specifically refer to headquarter companies, are applicable to headquarter companies.

The South African government wishes to promote South Africa as a gateway for investments into Africa. The Explanatory Memorandum on the Taxation Laws Amendment Bill, 2010[1] stated:

> '*South Africa is the economic powerhouse of Africa. South Africa's location, sizable economy, political stability and overall strength in financial services make South Africa an ideal location for the establishment of regional holding companies by foreign multinationals. Furthermore, South Africa's network of tax treaties provides ready access to other countries in the region. South Africa is therefore a natural holding company gateway into the region.*
>
> *However, in order to serve as an ideal holding company jurisdiction, three sets of South African tax rules were identified as significant barriers: (i) the CFC rules, (ii) the charge on outgoing dividends, and (iii) the thin capitalisation rules.*'

As part of the initiative to promote South Africa as a location for headquarter companies, the government amended certain provisions of the Act in order to create a more favourable tax dispensation for parties using South Africa as a gateway for investment into Africa.

A headquarter company is subject to tax in the same way as any other resident company, however it is entitled to certain relief from income tax, CGT and dividends tax which is not available to resident companies that are not headquarter companies. As a consequence of the special relief granted to headquarter companies they are also subject to special anti-avoidance rules.

In addition to the headquarter companies themselves, a foreign person receiving interest or royalties from a headquarter company will, under specified circumstances, be exempt from withholding tax on interest and royalties respectively.

A company that meets the requirements and elects to be a headquarter company under section 9I for a specific year of assessment will be entitled to the relief outlined in this Note.

A headquarter company potentially qualifies for the following relief:

- Exclusion from the CFC legislation under section 9D(2).
- Exemption from normal tax on foreign dividends received by or accrued under section 10B(2)(a) and 10B(3).
- Relaxation of the transfer pricing rules under section 31(5), but accompanied by ring-fencing of interest incurred under section 20C(2) and ring-fencing of royalties incurred under section 20C(2A).
- Relaxation of the income tax and CGT treatment of foreign exchange transactions under section 24I(3), 25D(4) and (7) and paragraph 43(1A).
- Disregarding of the capital gain or capital loss on the disposal of equity shares in a foreign company under paragraph 64B(2) and disregarding of the capital gain on a foreign return of capital received from a foreign company under paragraph 64B(4).
- A possible rebate for foreign taxes under section 6quat(1A), a deduction for foreign taxes under section 6quat(1C), or a rebate for foreign taxes under section 6quin(1).
- Exemption for a foreign person from withholding tax on interest under section 50D(1)(a)(i)(cc) on the interest paid by a headquarter company on so much of the financial assistance to which section 31 did not apply as a result of the application of section 31(5)(a).
- Exemption for a foreign person from withholding tax on royalties under section 49D(c) on the granting of the use, right of use or

permission to use intellectual property to which section 31 does not apply as a result of the application of section 31(5)(c).

- Exclusion from dividends tax legislation under section 64E(1).

Although a headquarter company qualifies for certain tax relief, anti-avoidance provisions have been introduced to protect the South African tax base:

- A company that becomes a headquarter company is subject to CGT on the deemed disposal of some of its assets under section 9H(3)(b)(i), and to dividends tax on a dividend in specie deemed to have been declared and paid by that company under section 9H(3)(c)(iii) for purposes of section 64EA(b). The deemed disposal and deemed dividend are deemed to have taken place on the day before becoming a headquarter company.
- A headquarter company does not qualify for the relief provided for under the corporate restructuring rules in sections 41 to 47.

Section 9I came into operation with effect from the commencement of years of assessment of a headquarter company commencing on or after 1 January 2011.

6. BINDING PRIVATE RULINGS

6.1 BPR 186 – Asset-for-share transaction between a resident private company and a collective investment scheme in securities

This ruling deals with the tax treatment of the conversion of an existing portfolio of assets into participatory interests in a collective investment scheme in securities (CIS) under section 42 of the Act and the immediate disposal of the participatory interests.

In this ruling references to sections are to sections of the relevant Acts applicable as at 20 November 2014 and unless the context indicates otherwise, any word or expression in this ruling bears the meaning ascribed to it in the relevant Act.

This is a ruling on the interpretation and application of the provisions of:

- sections 24J, 41 and 42 of the Act; and
- sections 1 and 8 of the STT Act.

Parties to the proposed transaction

The Applicant: A private company incorporated in and a resident of South Africa

Existing CIS: An existing collective investment scheme in securities that is a trust registered in and a resident of South Africa

Description of the proposed transaction

The Applicant intends to transfer its existing asset portfolio to a CIS, under section 42 of the Act, in return for the issue of participatory interests in the CIS and immediately dispose of the participatory interests in the CIS to a third party under a separate agreement. The asset portfolio comprises shares, bonds, and shares in REITs as defined in section 1(1) of the Act.

Ruling

The ruling made in connection with the proposed transaction is as follows:

- Section 42 of the Act will be applicable to assets transferred by the Applicant to a CIS in return for the issue of participatory interests in the CIS.
- Section 42 will not be applicable to assets transferred where the market value of these assets is less than their base cost or the expenditure actually incurred.
- Under section 42 the Applicant will acquire the participatory interests in the CIS at the base cost of the assets so transferred to the CIS and the CIS will be deemed to have acquired those assets at their original

base cost or the expenditure actually incurred for purposes of paragraph 20 of the Eighth Schedule to the Act.

- In respect of the transfer of bonds to the CIS:
    - The proceeds upon disposal of the bonds will be deemed to be equal to the their original base cost or the expenditure actually incurred.
    - The CIS will be deemed to have acquired the bonds at their original base cost or the expenditure incurred.
    - The base cost or the expenditure incurred will be equal to the adjusted initial amount at the beginning of the accrual period in which the transfer takes place plus accrual amounts for the current accrual period ending on the date of transfer and other payments made by the holder during the period less any payments received by the holder during the period.
    - The Applicant will be liable for normal tax on interest that accrued in respect of the bonds under section 24J of the Act, up to the date of the transfer.
    - The transfer price for purposes of the treatment of the transfer of the bonds will be deemed to be equal to the base cost or the expenditure incurred.
    - The transfer price for purposes of the treatment of the bonds in the hands of the CIS under section 24J of the Act, subsequent to the proposed transaction, will be deemed to be equal to the base cost or the expenditure incurred.
- Notwithstanding the short period that would have lapsed, the subsequent transfer of the participatory interest in the CIS to the third party will not change the character of the holding of the assets by the Applicant on the basis of it being held on capital account.
- The Applicant will be subject to capital gains tax on transfer of the participatory interest in the CIS to the third party on the difference

between the base cost of the participatory interests and the market value thereof on the date of transfer, on the basis that the Applicant may not utilise any assessed loss or balance of assessed loss to shield any capital gains as a result of the disposal as envisaged in section 42(7) of the Act.

- In relation to STT:
  - The transfer of the bonds is not subject to STT.
  - The transfer of the shares in REITs is exempt from the payment of STT under section 8(1)(t) of the STT Act.
  - The transfer of securities governed by section 42 of the Act is exempt from the payment of STT under section 8(1)(a)(i) of the STT Act.
  - The transfer of securities whose market value has declined below their base cost will not be subject to the payment of STT under section 8(1)(a)(vi) of the STT Act, provided that a sworn affidavit or solemn declaration is made by the public officer of the Applicant as required by section 8(1)(a)(vi) of the STT Act.

6.2 BPR 187 – Waiver of intra-group loan that funded acquisition of a mining operation

This ruling deals with the waiver of a loan that funded the acquisition of a mining operation as a going concern under an intra-group transaction contemplated in section 45 of the Act.

In this ruling references to sections and paragraphs are to sections of the Act and paragraphs of the Eighth Schedule thereto applicable as at 8 September 2014 and unless the context indicates otherwise, any word or expression in this ruling bears the meaning ascribed to it in the Act.

This is a ruling on the interpretation and application of the provisions of:

- section 1(1), definition of 'gross income';

- section 8(4)(a);
- section 15(a);
- section 19;
- section 36;
- section 45; and
- paragraphs 12A, 38(1) and 56(1).

Parties to the proposed transaction

The Applicant: A company incorporated in and a resident of South Africa

The Co-Applicant: A company incorporated in and a resident of South Africa

Description of the proposed transaction

Following the introduction of the Mineral and Petroleum Resources Development for the South African Mining and Minerals industry as contemplated in section 100(2)(a) of that Act, the Co-Applicant entered into a Broad-Based Black Economic Empowerment (BBBEE) transaction in terms of which the Co-Applicant sold its mining operations to the Applicant on loan account. The parties elected that the provisions of section 45 would apply to the transaction. The shares in the Applicant are held 74% by the Co-Applicant and 26% by a company that is classified as a black owned company under the BBBEE Codes of Good Practice issued under section 9 of the Broad-Based Black Economic Empowerment Act No. 53 of 2003.

The material terms of the sale of business agreement were as follows:

- The 'business' for purposes of the sale agreement was defined as the business of prospecting, mining and beneficiating, marketing and selling of the commodity and all related activities, that was conducted by the Co-Applicant.
- All the sale assets, being the fixed assets comprising mining and non-mining allowance assets, the properties, the debtors book, the sale

contracts, the goodwill and all other assets utilised in relation to the conduct of the business as defined were sold to the Applicant.

- The outstanding balance of the purchase price was to bear interest at the same interest rate as was charged to the Co-Applicant by its financial institution in respect of local borrowings, the nominal annual rate compounded monthly, which interest would be payable by the Applicant to the Co-Applicant monthly and in arrears.

The unredeemed balance of 'capital expenditure' as defined in section 36(11) was nil at the date of transfer of the assets and mining operations. Consequently, no further allowances under section 15(a) were available to be claimed by the Applicant in respect of the assets transferred.

As a result of the global financial crisis and the radical decline in commodity prices in recent years, the Applicant has been negatively impacted in that it has been unable to ensure full payment of the capital and the interest charged on the loan account. To date the Applicant has only been able to service part of the interest and the unpaid interest has been written off as a bad debt by the Co-Applicant.

The Co-Applicant therefore proposes to waive the loan account in order to strengthen the balance sheet of the Applicant.

<u>Ruling</u>

Ruling applicable to the Applicant

The ruling made in connection with the proposed transaction, as applicable to the Applicant, is as follows:

- Paragraph 12A will not be applicable to the waiver of the loan account owing by the Applicant to the Co-Applicant.
- Section 19 will be applicable to the waiver of the loan account, to the extent that the debt was used to acquire non-mining allowance assets in respect of which allowances were claimed by the Applicant under the Act, other than deductions under section 15(a).

- Section 19 will not be applicable to recoup or recover allowances claimed as a deduction by the Co-Applicant for the non-mining allowance assets acquired under section 45.
- In respect of trading stock:
    - Section 19(3) and (4) will be applicable to trading stock still on hand that was acquired under the sale of business agreement.
    - Section 19(5) will be applicable to trading stock acquired that has been sold and in respect of which a deduction or an allowance was granted under the Act.
- Section 19 will not be applicable to the waiver of the loan, to the extent that the debt was used to acquire mining assets, that is, expenditure on assets qualifying as 'capital expenditure' as defined in section 36(11), in respect of which allowances were claimed by the Co-Applicant under section 15(a).
- To the extent that there is no recoupment under section 8(4)(a), the waiver of the loan account will not fall within the ambit of 'gross income' as defined in section 1(1).

Ruling applicable to the Co-Applicant

The ruling made in connection with the proposed transaction, applicable to the Co-Applicant, is as follows:

- The waiver of the loan account will result in a capital loss in the hands of the Co-Applicant, but this loss must be disregarded in accordance with the provisions of paragraph 56(1). To the extent that an amount is included in the income of the Applicant in respect of the debt waiver or an adjustment is made to the carrying value of trading stock under section 19(3), the Co-Applicant may take into account a corresponding amount of the capital loss.

- The waiver of the loan account will not be subject to the provisions of paragraph 38(1).

6.3 BPR 188 – Conversion of a public benefit organisation to a for-profit company

This ruling deals with the conversion of a tax exempt Public Benefit Organisation (PBO) to a for-profit company.

In this ruling references to sections are to sections of the Act applicable as at 4 November 2014 and unless the context indicates otherwise, any word or expression in this ruling bears the meaning ascribed to it in the Act.

This is a ruling on the interpretation and application of the provisions of section 30.

Parties to the proposed transaction

The Applicant: A company, incorporated in a foreign country and limited by guarantee, that is registered in South Africa as an external company under section 23(1)(a) of the Companies Act No. 71 of 2008 and a PBO under section 30.

Description of the proposed transaction

The Applicant is a company incorporated in a foreign country, registered in South Africa as an external company and as a PBO in terms of section 30 that is tax resident in South Africa.

Historically, the Applicant PBO incurred various expenses payable to the Applicant in the foreign country, for instance, royalty payments, management fees and network fees.

The Applicant in the foreign country intends to convert from a tax exempt company to a for-profit company and as a result will convert from a company limited by guarantee to a company limited by shares.

The change in status of the Applicant in the foreign country will result in a change in the status of the Applicant PBO in South Africa under section 10.

The Applicant PBO will accordingly request a notice of withdrawal as a PBO under section 30.

Conditions and assumptions

This binding private ruling is subject to the following additional conditions and assumptions:

- The conversion of the Applicant PBO to a for-profit company will take place during 2014.
- More than 15% of the receipts and accruals of the Applicant PBO within three years preceding the termination of its activities as an approved PBO, must be from a South African source.
- All royalties, management fees, network fees and other fees incurred by the Applicant PBO must constitute bona fide liabilities, as contemplated in section 30(7).

Ruling

The ruling made in connection with the proposed transaction is as follows:

- The provisions of section 30(7) will apply to the proposed transaction.
- To the extent that the Applicant PBO's bona fide liabilities exceed the market value of the assets in question, an amount equal to zero will be included in the Applicant PBO's taxable income.
- No donations tax will be payable by the Applicant PBO.

6.4 BPR 189 – Acquisition of shares subject to suspensive conditions

This ruling deals with the time of acquisition of shares which are acquired under an agreement subject to suspensive conditions.

In this ruling references to sections and paragraphs are to sections of the Act and paragraphs of the Eighth Schedule thereto applicable as at 21 October 2014 and unless the context indicates otherwise, any word or expression in this ruling bears the meaning ascribed to it in the Act.

This is a ruling on the interpretation and application of the provisions of:

- section 1(1), definition of 'connected person';
- section 24J;
- paragraph 13; and
- paragraph 20(1)(a).

Parties to the proposed transaction

The Applicant: Company X, a private company incorporated in and a resident of South Africa

Co-Applicant 1: Trust Y, a resident of South Africa

Co-Applicant 2: Trust Z, a resident of South Africa

Description of the proposed transaction

In the past decade, Co-Applicant 1 and Co-Applicant 2 acquired a number of ordinary shares ('BEE shares') in a listed company (ListCo) via a share subscription agreement, as part of ListCo's Black Economic Empowerment deal (ListCo BEE deal). ListCo's BEE deal is set to expire soon making it possible for the Co-Applicants to dispose of their BEE shares in ListCo.

The Applicant intends to make an offer to acquire some of the BEE shares that the Co-Applicants will hold in ListCo after expiry of the ListCo BEE deal.

As part of the BEE deal close out arrangements ListCo may re-acquire some of the BEE shares under a call option that it holds in relation to the financing arrangements the company has with the Co-Applicants relating to the acquisition of the BEE shares.

Each Co-Applicant further has a call option against ListCo to re-subscribe for ordinary shares in ListCo up to the number of the BEE shares that the Co-Applicant holds in ListCo which are the subject matter of the ListCo call option described above. The Co-Applicants' call options may only be exercised after ListCo's call option has been exercised.

The above call option transactions need to take place before the Co-Applicants can determine the number of ListCo shares available for sale to the Applicant (available ListCo shares).

The Co-Applicants are only entitled to sell the available ListCo shares after the expiry of the ListCo BEE deal, subject to fulfilment of the suspensive conditions as listed in the BEE shares subscription agreement.

The Applicant and the Co-Applicants propose to enter into individual sale agreements. The terms of the agreements will be identical for each Co-Applicant, with the exception of the number of available ListCo shares being committed by each Co-Applicant to be disposed of to the Applicant.

The agreements will be subject to a number of suspensive conditions.

Once all the conditions have been fulfilled, each agreement requires delivery of a trigger notice (as defined in the agreement) by the respective Co-Applicant to the Applicant during the sale period for each tranche of shares being sold to the Applicant. The trigger notice must specify the number of available Listco shares being sold to the Applicant. The Co-Applicants are allowed to sell the committed available ListCo shares in three tranches. If no trigger notice is given for the minimum number of committed shares by a specified date (which date coincides with the end date of the sale period), the Co-Applicant will be deemed to have given a trigger notice as at the specified date for all the available ListCo shares committed under the agreement. The sale period is a period of approximately 3 months commencing after the date the call options have been exercised.

The agreement will specify that ownership, risk and benefit in the available ListCo shares will pass upon delivery of these shares to the purchaser's

Central Securities Depository Participant following delivery of the trigger notice. It is envisaged that payment will first take place and then delivery of the available ListCo shares.

The purchase price per ListCo share under the proposed transaction is subject to a formula which takes into account the 30 day volume weighted average share price (reduced by any distribution paid or payable to the respective Co-Applicant during the sale period) less a specified discount; and the then current average trading price of a ListCo share.

There is no debt funding in the acquisition of the available ListCo shares by the Applicant.

The Applicant is not a beneficiary of the Co-Applicants. Some of the beneficiaries of the Co-Applicants are companies and the Applicant also does not hold any equity shares in any of these companies that are beneficiaries of the Co-Applicants. One of the Applicant's fellow subsidiaries does, however, hold less than 50% of the equity shares in one of the companies that is a beneficiary of Co-Applicant 1.

Ruling

The ruling made in connection with the proposed transaction is as follows:

- The time of disposal by the Co-Applicants and the corresponding time of acquisition by the Applicant of the available ListCo shares is the date the suspensive conditions of the sale agreement are satisfied as contemplated in paragraph 13(1)(a)(i).
- The base cost of the acquired available ListCo shares, as contemplated in paragraph 20(1)(a), is the price payable under each trigger notice.
- The Applicant is not a 'connected person' as defined in section 1(1) in relation to any of the Co-Applicants.
- The provisions of section 24J will not be applicable to the proposed transaction.

6.5 BPR 190 – Notional funding arrangement: The issue and potential repurchase of ordinary shares

This ruling deals with the issue and repurchase of ordinary shares. The proposed arrangement is based on contractual rights and restrictions established separately from any class provisions applicable to those shares in terms of the Applicant company's memorandum of incorporation.

In this ruling references to sections and paragraphs are to sections of the relevant Act and paragraphs of the Eighth Schedule to the Act applicable as at 19 February 2015 and unless the context indicates otherwise, any word or expression in this ruling bears the meaning ascribed to it in the relevant Act.

This is a ruling on the interpretation and application of the provisions of:

- section 24J of the Act;
- paragraphs 11(1)(a) and 35 of the Eighth Schedule to the Act; and
- section 1, definition of 'transfer' of the STT Act.

Parties to the proposed transaction

The Applicant: A company incorporated in and a resident of South Africa

The Co-Applicant: A company incorporated in and a resident of South Africa

Description of the proposed transaction

The Applicant will establish two trusts which will become shareholders in the Co-Applicant for the purpose of the Co-Applicant acquiring ordinary shares in the Applicant.

The two trusts will subscribe for 51% and 49% respectively of the Co-Applicant's issued share capital at nominal value and will then be and remain the sole shareholders of the Co-Applicant.

The Co-Applicant will subscribe at a nominal value for ordinary shares in the Applicant which will, after their issue, constitute 26% of its entire issued share capital.

The ordinary shares to be subscribed for by the Co-Applicant will have exactly the same rights and privileges attached to the rest of the ordinary shares issued by the Applicant. However, it will be contractually agreed (in a subscription and repurchase agreement) between the parties that:

- the Applicant will, on the fifth anniversary of the subscription date (the repurchase date), repurchase a determinable number of ordinary shares held by the Co-Applicant at a nominal amount;
- the Co-Applicant will not be entitled to dispose of the ordinary shares until after the repurchase date;
- the ordinary shares shall be held by the Applicant in safe custody until the repurchase date; and
- the number of ordinary shares to be repurchased by the Applicant will be determined in accordance with a pre-determined notional vendor funding formula which will take into consideration the following:
    - the initial market value of the ordinary shares in the Applicant not subject to the subscription and repurchase agreement;
    - the market value of the ordinary shares in the Applicant not subject to the subscription and repurchase agreement, on the repurchase date;
    - an escalation factor; and
    - the period of time that has elapsed since the subscription date to the repurchase date.

Subsequent to the repurchase of the determined number of ordinary shares from the Co-Applicant, the remaining shares will be released from safe custody and their share certificates will be delivered to the Co-Applicant.

<u>Ruling</u>

The ruling made in connection with the proposed transaction is as follows:

- Section 24J of the Act will not be applicable to the proposed transaction.
- There will be no 'disposal', as contemplated in paragraph 11 in respect of the remaining ordinary shares held by the Co-Applicant following the repurchase transaction.
- The creation of the repurchase and restriction rights in terms of the subscription and repurchase agreement will not give rise to any capital gain or loss as contemplated in paragraphs 3 and 4 for the Applicant or Co-Applicant.
- The repurchase of a portion of the ordinary shares from the Co-Applicant by the Applicant at a nominal price will not give rise to a capital gain or loss for the Co-Applicant.
- No securities transfer tax will be levied in respect of the remaining ordinary shares held by the Co-Applicant following the repurchase transaction.

7. BINDING GENERAL RULING

7.1 BCR 26 – VAT Treatment of the supply and importation of herbs

For purposes of this ruling 'Item 12' means Item 12 in Part B of Schedule 2 to the VAT Act.

This BCR sets out the VAT treatment applicable to the supply and importation of herbs.

Vegetables that are not cooked or treated except for the purposes of preservation fall within the ambit of Item 12. Although the term 'vegetable' is not defined in the VAT Act, the Agricultural Product Standards Act No. 119 of 1990 (the Agricultural Product Standards Act) which, amongst others, regulates the sale of fresh vegetables is of assistance in determining the meaning that must be attributed to this term for purposes of Item 12.

The term 'fresh vegetables' is defined in section 1 of the regulation1 issued under the Agricultural Product Standards Act, to mean those vegetables and herbs specifically mentioned in the definition as well as 'unspecified vegetables'. The term 'unspecified vegetables' is defined in section 1 of the regulation to mean any other kind of vegetables that are not mentioned under 'fresh vegetables'.

Furthermore, the Customs and Excise Act No. 91 of 1964 (the Customs Act) specifically lists culinary herbs as being a vegetable.

The Customs Act distinguishes between herbs that can be used for culinary purposes and herbs to be used for other medicinal or perfumery purposes. Herbs used for culinary purposes are classified under Chapter 73 whereas herbs imported to be used primarily in perfumery, in pharmacy or for insecticidal, fungicidal or similar purposes are classified under Chapter 12.4 Any herb that may be suitable for human consumption (for example, fresh basil), if imported for purposes other than for culinary purposes is not classified as a vegetable under Chapter 7 of the Schedule to the Customs Act.

In light of the above, the importation of a herb may be subject to a different rate of customs duty depending on the use to which it is put (that is, culinary or other). A herb is, however, for VAT purposes, regarded as a vegetable as contemplated in Item 12 even if the recipient uses it for purposes other than human consumption.

Taking the above into account, vegetables contemplated in Item 12 include herbs.

<u>Ruling</u>

Zero-rated supplies

> The supply of herbs that have not been cooked or treated in any manner except for the purpose of preserving such herbs in their

natural state, is zero-rated under section 11(1)(j) read with Item 12. Section 11(3) requires a vendor to obtain and retain documentary proof substantiating the vendor's entitlement to apply the zero rate.

Fresh and frozen herbs sold in the following forms qualify for zero-rating:

- Cut
- Diced
- Shredded

The zero-rating applies regardless of whether the herbs are sold individually (for example, a packet of curry leaves or a packet of angelica) or mixed

Standard-rated supplies

The supply of herbs in the following instances is specifically excluded from Item 12 and is therefore subject to VAT at the rate of 14% under section 7(1)(a):

- Cut, diced or shredded herbs, to which any other substance has been added (other than for the purpose of preserving such herbs in their natural state).
- Minced or pureed herbs.
- Fresh or frozen herbs that have been treated with an additive for the purpose of adding colour or flavour (for example, glucose, dextrose, sugar or salt).
- Herbs supplied in the course of the furnishing or serving of any meal, refreshment, cooked or prepared food or any drink, so as to be ready for immediate consumption when supplied.

The importation of herbs

The importation of zero-rated herbs is under section 13(3) read with paragraph 7(a) of Schedule 1 to the VAT Act exempt from the VAT levied under section 7(1)(b).

The importation of standard-rated herbs is subject to VAT at the rate.

8. DRAFT BINDING GENERAL RULING

8.1 Value-added tax treatment of the supply and importation of fruit and vegetables

For the purposes of this ruling 'Item' means an Item in Part B of Schedule 2 to the VAT Act.

This BGR:

- sets out the VAT rate applicable to the supply and importation of fruit and vegetables; and
- withdraws BGR (VAT) No. 18 'The Zero-Rating of Various Types of Dates' dated 27 March 2013.

Ruling

Zero-rated supplies

The supply of fruit and vegetables that have not been cooked or treated in any manner except for the purpose of preserving such fruit and vegetables in their natural state, is zero-rated under section 11(1)(j) read with Item 12 (vegetables) and Item 13 (fruit) respectively. Fresh and frozen fruit and vegetables sold in the following forms qualify for zero-rating:

- Cut (including fruit and vegetables cut into specific shapes)
- Diced
- Sliced
- Peeled
- Shredded
- De-pitted

Frozen fruit and vegetables1 that have been blanched in hot water for the purpose of preserving the fruit and vegetables in its natural state qualify for the zero-rating.

Subject to the standard rating hereunder, the zero-rating applies regardless of whether the fruit and vegetables are sold individually (for example, a punned of strawberries or a pocket of potatoes) or mixed (for example, mixed diced carrots and potatoes or mixed chopped strawberries and kiwi fruit).

Standard-rated supplies

The supply of fruit and vegetables in the following instances is specifically excluded from Items 12 and 13 respectively, and is therefore subject to VAT at the rate of 14% under section 7(1)(a):

- Cut, diced, sliced, peeled or shredded fruit or vegetables, to which any other substance has been added (other than for purposes of preserving the fruit or vegetables in its natural state). Examples are:
  - a sachet of spices added to sliced mushrooms;
  - fruit juice added to a mixture of sliced fruit; and
  - salad dressing added to a mixture of salad leaves,

  whether or not it is packaged separately in the same container.
- Minced, crushed or pureed fruit or vegetables.
- Fresh or frozen fruit and vegetables that have been treated with an additive for the purpose of adding colour or flavour (for example, glucose, dextrose, sugar or salt).
- Dehydrated, dried or compressed fruit or vegetables, for example, compressed dates.
- Fruit smoothies, fruit and vegetable juice and any similar products.

- Fruit and vegetables supplied in the course of the furnishing or serving of any meal, refreshment, cooked or prepared food or any drink, so as to be ready for immediate consumption when supplied.

Importation of fruit and vegetables

The importation of zero-rated fruit and vegetables under section 13(3) read with paragraph 7(a) of Schedule 1 to the VAT Act, is exempt from the VAT levied under section 7(1)(b).

The importation of standard-rated fruit and vegetables is subject to VAT at 14% under section 7(1)(b).

8.2 Termination of STC credits: Dividend declared before 1 April 2015 but paid on or after that date

This BGR clarifies that STC credits are not available when a dividend is declared before 1 April 2015 but is paid on or after that date.

The STC credit of a company is applied to reduce the amount of a dividend that is potentially subject to dividends tax. It ensures that profits that were previously subject to secondary tax on companies in a distributing company are not again subject to dividends tax when on-distributed by another company to a holder of shares. Some taxpayers have questioned whether the STC credit of a company can be applied to a dividend declared by a company before 1 April 2015 which is paid on or after that date.

<u>Application of the law</u>

Section 64E(1), which came into operation on 1 April 2012, provides that, subject to paragraph 3 of the Tenth Schedule to the Act, dividends tax must be levied at the rate of 15% of the amount of any dividend paid by any company other than a headquarter company.

Section 64J(1) stipulates that a dividend paid by a company is not subject to dividends tax to the extent that the dividend does not exceed the STC credit of the company and the company has by the date of payment notified the person to whom the dividend is paid of the amount by which the dividend reduces the STC credit of the company.

Both section 64E(1) and section 64J(1) refer to a dividend ‘paid’ by a company.

The STC credit of a company can therefore only be applied against a dividend that is paid by a company.

Section 64E(2) determines when a dividend must be deemed to be paid by a company, for purposes of dividends tax. A dividend declared by a listed company must, to the extent that the dividend does not consist of the distribution of an asset in specie, be deemed to be paid on the date on which the dividend is paid. A dividend declared by a listed company that consists of the distribution of an asset in specie, must be deemed to be paid on the earlier of the date on which the dividend is paid or becomes due and payable. Any dividend declared by a company that is not a listed company must be deemed to be paid on the earlier of the date on which the dividend is paid or becomes due and payable.

Section 64J(5) provides that the STC credit of a company on or after the third anniversary of the effective date is deemed to be nil. The latter date is 1 April 2015.

The STC credit of a company must be applied against any dividend paid by that company before 1 April 2015. A dividend paid by a company on or after 1 April 2015 cannot be reduced by any STC credit, since the STC credit of a company on or after 1 April 2015 is deemed to be nil.

Under section 64J(7) a company that pays a dividend will be liable for any dividends tax that is subsequently not withheld by another person as a result of an inaccurate notification provided by that company.

Ruling

The STC credit of a company must be applied against any dividend paid by that company before 1 April 2015 if the requirements of section 64J(1)(b) are met.

The STC credit of a company cannot be applied against a dividend declared by it before 1 April 2015 which is only paid on or after 1 April 2015.

9. INDEMNITY

Whilst every reasonable care has been taken in the production of this update no responsibility for the consequences of any inaccuracies contained herein or for any action undertaken or refrained from taken as a consequence of this update will be accepted.