South African
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Dear Ms Mpotulo and Ms Collins

RE: CALL FOR COMMENT: DRAFT TAXATION LAWS AMENDMENT BILL, 2013

Thank you for the opportunity to contribute commentary on the draft Taxation Laws Amendment Bill, 2013.

Set out below, is the consolidated commentary on the **international tax issues only** developed from both an internal review of the provisions as well as from consultations with members, stakeholders and industry. The commentary reflects the collective view of members, stakeholders and industry role players consulted.

1 CURRENCY RULES FOR DOMESTIC TREASURY MANAGEMENT COMPANIES (s1, 24I, 25D, para 43(7) of 8th Schedule)

Problem statement:
It is uncertain why an individual can invest its money off shore with no currency gains being incurred but the treatment for a company is made so complex. The Minister in his budget speech stated that the purpose of the introduction of domestic treasury management company ('DTMC') was to bring the treasury company to South Africa and for it not to be treated as a South African Reserve Bank ('SARB') resident. However, the SARB Circular appears to state that the company must be a treasury company but also a holding company, but specifically a Headquarter company ('HQC'). The linkage to the HQC regime makes the application of these amendments complex and not very practically as it is our understanding that the audience for the HQC regime was foreign parented groups whereas the DTMC regime's audience is South African parented groups.

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Proposed solution / recommendation:
The SARB circular should be amended to so as to remove the link between a treasury company and a holding company that is a HQC as a HQC regime has not relevance for South African parented group. The complexity of the legislation should also be addressed.

2 REFINEMENT OF PARTICIPATION EXEMPTION IN RESPECT OF FOREIGN DIVIDENDS DERIVED FROM NON-EQUITY SHARES (s10(B)(2))

Problem statement:
The proposal to restrict the participation and same country exemptions to dividends derived from equity shares only is considered too broad. Although this amendment is presumed to be targeting tax avoidance schemes using preference shares (once the 10% equity limit was reached), it is also inadvertently adversely affecting legitimate commercial arrangements. These proposed changes could result in, for instance, foreign share schemes becoming more attractive than local share schemes. This clearly cannot be the intention behind this legislation.

Proposed solution / recommendation:
These provisions should be linked back to the section 8C, 8E, 8F and 8FA and not merely to any share that is not an equity share.

3 CONTROLLED FOREIGN COMPANY AND THE WORKING CAPITAL EXEMPTION (s9D(9A)(a)(iii)(cc))

Problem statement:
Although the intention behind the proposed amendment makes sense, it appears that the test to determine the five percent has been made tighter across the board, that is, the denominator used to calculate the five percent excludes not only the amounts derived from the activities of a treasury operation or a captive insurer but also "amounts in respect of which paragraphs (c) to (fB) of subsection 9 apply.

Proposed solution / recommendation:
The inclusion of the items under paragraphs (c) to (fB) of subsection 9 in the denominator should be removed.

OTHER RELEVANT POINTS REGARDING CONTROLLED FOREIGN COMPANY EXEMPTIONS

Problem statement:
The exemptions to section 9D appear to have an inequitable effect on South African outbound multinationals if compared to foreign branches of inbound multinationals for whom no changes over the last few years have been enacted. An example of the detrimental effect of these exemptions on South African outbound multinationals is as follows:

If the high tax rate exemption for controlled foreign companies ('CFC') is used (second proviso to s9D(2A)) by a South African multinational company wishing to establish a treasury function in, say the United Kingdom, the exemption would not be applicable because the tax rate in the UK is going to drop to 20%, (which would not be at least 75% of the net normal tax payable in South Africa). As the UK is one of the countries for which it has been indicated renegotiations with the DTAs is not going to take place and is a bone fide country within which to business, it seems strange that this would not be, from a tax perspective, a suitable country in which to set up a South African outbound multinational's treasury operation.

Proposed solution / recommendation:
It is proposed that the 75% of the South African tax rate referred to in the second proviso to s9D(2A) be lowered to 70% to provide South African outbound multinationals with the opportunity to conduct their affairs in countries that would make commercial sense. We are, however, not suggesting that a designated country exemption be re-introduced.

4 EXEMPTION FOR INTERNTIONAL SHIPPING TRANSPORT ENTITIES (s9D, s10(1)(o)(i), 12C, 12Q)

Problem statement:
Although we are fully supportive of this initiative, it is uncertain how widely these provisions will apply due to the requirement that the ship must be a 'South African ship' as defined.

Proposed solution / recommendation:
It is hoped that sufficient research has been done to justify this requirement and we propose that the effectiveness of these provisions be regularly monitored.

5 UNIFORM CROSS-BORDER WITHHOLDING REGIME TO PREVENT BASE EROSION (s37J-37O, s49A-49G, 50, 51) (Clauses 103, 105)

5.1 Meaning of 'interest' to which the withholding tax on interest should be applied

Problem statement:
Although section 49B refers to interest received or accrued from a source within the Republic in terms of section 9(2)(b), no specific definition of 'interest' is provided in this section thus making it unclear if it is interest as defined in section 24J or if it is the common law definition of interest.

Proposed solution / recommendation:
A definition of 'interest' should be inserted into section 49A.

5.2 Basis of determining the payment of the withholding tax on interest

Problem statement
With the economy of South Africa being in a distress situation and businesses having in some instances to capitalise the interest due on loans from non-residents, the basis on which the withholding tax on interest is calculated appears iniquitous.

In terms of the legislation the withholding taxes on interest should be calculated based on an amount that is paid to any foreign person to the extent that the amount has been regarded as having been received or accrued from a source within the Republic. Interest is deemed to be paid on the earlier of the date on which payment is made or when it becomes due and payable.

Thus unless a person can change the terms of their agreement, the interest will not be deductible under section 23O and the withholding tax on interest will be triggered. There is no interest cash flow from which to withhold the tax. Thus not only is the person denied an interest deduction under section 23O but it is also required to pay over a withholding tax from funds that have not been remitted.

Although the withholding tax on interest has been discussed above, the problems apply equally to the withholding tax on royalties and services.

Proposed solution / recommendation:
The withholding tax regimes should be based on the cash payment basis, that is, based on "receipts" rather than on "due and payable" which is accrual based. This makes commercial sense as currently (in the above mentioned situations) there are no funds from which to pay the withholding tax.

Proposed solution / recommendation:
The withholding tax regimes should be based on the cash payment basis, that is, based on "receipts' rather than accruals as the Courts have clearly dealt with the term 'receipt' as opposed to 'paid'. This makes commercial sense as currently (in the above mentioned situations) there are no funds from which to pay the withholding tax.

5.3 Exemptions

Problem statement:
It appears that the exemption provided for in section 37K(1)(a)(ii) [the purchase of goods into the Republic] and section 37K(1)(c) [interest accrued to a foreign person in terms of section 25BA(a)] have been removed. Reasons for this are unclear.

Proposed solution / recommendation:
Reasons why these exemptions have been removed should be provided in the explanatory memorandum or the section should be adjusted accordingly.

5.4 Effective date of withholding tax on interest

Problem statement:
The withholding tax on interest became effective on 1 July 2013 according to legislation already promulgated. However, the current draft legislation retrospectively removes this withholding tax obligation and postpones it till 1 January 2015.

It is iniquitous and unconstitutional that the effective date of the interest withholding tax in the draft legislation can backdated the current legislation and that it also backdates it to a period before the proposed amendments are being discussed. Uncertainty thus prevails with regard to whether withholding tax on interest should actually be withheld from 1 July 2013 till 1 January 2015. Furthermore, uncertainty of the effective dates also has an impact on the calculation of provisional tax payable by a company. Another concern is the forms that would be required to be completed in respect of this withholding appear not to have been released as yet.

Proposed solution / recommendation:
The Commissioner must issue an official statement immediately as to when the withholding tax on interest becomes effective. Should the effective date be 1 July 2013, the necessary forms should be available for the

5.5 Meaning of 'service fees'

Problem statement:
Although section 51A(1) defines 'service fees' as amounts received or accrued in respect of technical services, managerial services and consultancy services, the draft explanatory memorandum states that "Less technical services (such as hair stylists, real estate commissions and the like) should not be viewed as falling within the withholding paradigm". It is unclear whether amounts received in respect of a less technical activity, such as administrative services, would fall within the scope of this provision – in particular administrative services that are not of a technical but rather of a routine nature.

Proposed solution / recommendation:
Consideration should be given to amending the definition of service fees so that it refers to specific types of service income rather than general amounts received or accrued in respect of all services. Should this proposal not be accepted, then a list of services that should not be included in this definition should be provided to create certainty for the taxpayer.

5.6 Recognition of DTA relief for the withholding tax on services

Problem statement:
Where South Africa has a DTA with another country, the withholding tax would appear not to apply in the vast majority of situations. Furthermore, the tax will only apply in circumstances in which the service fees are from a South African source. In the majority of situations, the services are rendered outside of South Africa making the tax inapplicable. Even for those countries where South Africa does have a DTA, certain of these countries do not recognize the treaty relief. This forces the South African companies into a difficult situation

Proposed solution / recommendation:
Taking the cost and practical difficulties of administrating this tax, we suggest that this tax be reconsidered or that remedies for the practical difficulties being experienced by taxpayers be taken into consideration.

5.7 Effective date of withholding tax on royalties

Problem statement:
Section 35 is effectively repealed with effect from 1 July 2013 but it is proposed that the royalty withholding tax regime will only come into operation on 1 January 2015. Royalties paid to non-residents between 1 July 2013 and 1 January 2015 will therefore not be subject to any withholding tax and also not qualify for the exemption in section 10(1)(l).

Proposed solution / recommendation:
The repeal of section 35 should be amended to align the repeal of section 35 with the introduction of withholding tax on royalties.

6 TRANSFER PRICING RELIEF FOR EQUITY LOANS (s31)

Problem statement:
In terms of the proposed amendments to section 31, any cross-border loan that does not meet the four requirements laid down in this section would by default be subject to the transfer pricing provisions. In a group context though, section 31(6)(b)(i) provides for an exemption for transfer pricing on interest or intellectual property to a CFC where the shares in the CFC are held "whether alone or together with any other company forming part of the same group of companies as that resident". Thus this exemption applies in a group context but only if the shares are directly held CFCs. This is considered to narrow and should be amended so as to not only apply in these circumstances.

In respect of all other loans (not in a group context) should the four new requirements of section 31 not be met, the loan would be subject to the transfer pricing rules. Should this have been the intention then loans such as those provided to a person's child who has emigrated to the UK or a loan provided to a trust in Jersey would also be affected by these new provisions. Previously the OECD guidelines could be used but the neither section 31 nor the draft Interpretation Note mention the use of these guidelines in such circumstances.

Furthermore, the requirement that the loan must be perpetual or non-redeemable within 30 years is also of concern to us as there are certain loans that are provided as quasi equity loans to subsidiaries for exploration work that will last for well under the 30 year requirement due to the nature of the work at hand.

Proposed solution / recommendation:
The interpretation note on section 31 should address the fact that the OECD guidelines can be used as a point of reference in the circumstances as mentioned above (loans to the broader public and all cross border loans). In the group context, section 31(6)(b)(i) should be amended to cater for the situation where a company does not hold shares directly in a group CFC, but still meets all the other requirements. The repayment period of 30 years is not considered feasible in certain specific circumstances and this period should be reduced or catered for in the interpretation note.

7 SHARE ISSUE IN EXCHANGE FOR FOREIGN SHARES AS A MEANS OF CORPORATE MIGRATION (para 11(2)(b) of 8th Sch)

Problem statement:
The Explanatory Memorandum does not appear to be speak to the proposed legislation. Furthermore, the proposed legislation imposes a tax on a resident where there is no matching economic or capital gain. Ultimately these provisions result in the company having to come up with the tax unless the group relief provisions apply.

Proposed solution / recommendation:
As there is no loss to the fiscus we suggest that the provisions be amended in such a way that the tax is triggered only when the shares are eventually sold.

Please do not hesitate to contact us if you have any queries in this regard.

Yours sincerely,

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