South African Institute of Tax Professionals

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The National Treasury
240 Vermeulen Street
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The South African Revenue Service
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RE: COMMENTS IN RELATION TO THE SECOND BATCH 2016 DRAFT TAXATION LAWS AMENDMENT BILL PROPOSALS

1. Loan or credit advanced to a trust by a connected person

We welcome the revised proposal to use the deemed donation measure rather than the originally proposed deemed interest measure to address the potential estate duty and donations tax avoidance by means of the transfer of assets to a trust using interest free loans.

We have the following comments on the revised proposal:

- The proposed section 7C(3) states that the determined amount must for purposes of Part V of Chapter II (which deals with donations tax) "be treated as a donation made to that trust". A donation is defined in section 55 to mean "any gratuitous disposal of property including any gratuitous waiver

../2

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or renunciation of a right. In terms of section 54, donations tax is "…paid…on the value of any property disposed of…under any donation by a resident…". The donations tax is subject to exemptions contained in section 56 which stipulates the instances where "donations tax shall not be payable in respect of the value of any property which is disposed of under a donation - …" It is not totally clear based on the wording of the proposed section 7C(3) read with these donations tax sections, that an amount that is treated as a donation will be properly regarded as property disposed of for purposes of the donations tax. We recommend that the wording of section 7C(3) be clarified along the lines of the amount determined will "be treated as the value of the property disposed of under a donation".

- We welcome the clarity being provided in the revised proposals that loans which are affected transactions subject to the provisions of section 31 will be excluded from the application of section 7C.

2. Restricted equity instruments for employee share schemes

We appreciate that the public comments were taken into account and that the decision was taken to remove the main proposal, to tax all dividends on restricted equity instruments as remuneration, from the 2016 Taxation Laws Amendment Bill.

We have the following comments on the revised proposal:

- The revised proposal is aimed at putting a stop to tax avoidance through 'dividend stripping'. The proposed mechanism is that the dividend exemption will not be available to any dividend in respect of a restricted equity instrument in the case of a share buy-back or redemption as well as in anticipation or in the course of the winding up, liquidation, deregistration or final termination of a company. We are of the view that these circumstances are too limited to achieve the anti-avoidance

../3

objective as dividend stripping could take place even if these circumstances do not exist. Dividends that are designed to strip the value from the company could be declared in tranches, especially if the company has been set up specifically to facilitate a dividend stripping scheme.

- The employment dividend rules in section 10(1)(k)(i)(jj) and section 10B(6) apply to a restricted equity instrument as defined in section 8C that was "acquired in the circumstances contemplated in section 8C". The phrase "as contemplated in" fails to address the exclusions in section 8C. What if a share was acquired in terms of section 8C(1)(b) and section 8C therefore does not apply to it? Is it still acquired "in the circumstances contemplated in section 8C"?

- The interaction between s 8C(1A) and the new paragraph 80(2A) of the Eighth Schedule has not been addressed. Capital gains accruing to holders of restricted equity instruments (e.g. trust unit holders) will be subject to income tax, and the gain may also be subject to CGT in the trust at 32.8% if the new provisions apply (i.e. if the gain vests "by reason of" a s 8C vesting). We recommend that a specific provision be introduced to prevent double taxation (e.g. paragraph 64C should apply if s 8C(1A) applies to the same amount, so that the trust can disregard the gain).

- It is proposed that section 10B(6) be amended. It appears that there may be an unintended omission in the proposed wording in that the proposed wording of the proviso (jj)(B) to section 10(1)(k)(i) is not included as section 10B(6)(b)(ii). It appears that the phrase “received or accrued in anticipation or in the course of the winding up, liquidation, deregistration or final termination of a company” should be added at the end of section 10B(6).

../4

3. Employment Tax Incentive

We have the following comments on the proposals to amend the Employment Tax Incentive Act:

- It is proposed that the Employment Tax Incentive (ETI) be limited to R20 million per year per employer. This means that an organization which has elected to operate through divisions of one company as opposed to housing such operations in different subsidiary companies may be more adversely affected by the cap. For example, a company which employs qualifying employees who earn between R2,000 and R4,000 per month and which is therefore entitled to a R1,000 incentive per employee, will be able to claim incentives in respect of 1,666 employees (R1,000 incentive x 12 months x 1,666 employees = R19,992,000 incentive claim which is just less than the R20 million annual limit). If such a company employs say 4,000 qualifying employees, which is not a particularly high number in certain service industries, it will not be entitled to claim incentives in respect of 2,334 employees. On the other hand, should the organization be split into 5 subsidiaries of which none employ more than 1,666 qualifying employees, it would be entitled to an incentive of R48 million.

- As we understand the proposal regarding limitations on roll-overs and back-dated claims, from 1 October 2016, monthly claims can only be made up to the date of each 6-monthly reconciliation. After that no further claims for that reconciliation period (March to August, September to February) will be allowed. At that time any excess becomes available as a refund (or can be used as a credit against employees' tax payable).

../5

The link between ETI and remuneration means that when a change to remuneration is reported (after the initial submission of the EMP201), the underlying ETI claim based on that remuneration should also change (the information on the EMP201 should change). Therefore, if the intention is to ensure that an employer only claims the ETI that it reported on during the relevant period, there will be a mismatch between the remuneration on the final IRP5 tax certificates and the ETI claimed and utilised. From an administrative perspective, it is not clear how employers will be able to keep track of the specific amounts.

We request that the reconciliation periods (up to October and May) are included, and that should IRP5 tax certificates be resubmitted to correct remuneration stated in prior periods, that there should be an opportunity for the employer to claim ETI even where ETI was not claimed before (or alternatively reduce the claims).

We welcome the opportunity to comment on these proposals and look forward to future engagements.

Yours sincerely

Jaco la Grange

Chair of the Personal Tax Technical Work Group