SC Finance 28/11/17

2017 TAXATION LAWS AMENDMENT BILL & TAX ADMINISTRATION LAWS AMENDMENT BILL

Select Committee on Finance

Presenters: National Treasury and SARS | 28 November 2017

national treasury
Department:
National Treasury
REPUBLIC OF SOUTH AFRICA

Consultation process

- The 2017 Draft Taxation Laws Amendment Bill (TLAB) and 2017 Draft Tax Administration Laws Amendment Bill (TALAB) were published for public comment on 19 July 2017.
- National Treasury and SARS received written comments from 1420 organisations and individuals by the deadline of 18 August 2017.
- National Treasury and SARS briefed the Standing Committee on Finance (SCoF) on the draft bills on 15 August 2017.
- Oral presentations by taxpayers and tax advisors on the draft bills were made at hearings by the SCoF on 29 August 2017.
- Workshops with stakeholders to discuss their comments on the 2017 Draft TLAB & TALAB were held on 4 and 5 September 2017.
- On 14 September 2017, National Treasury and SARS presented to the SCoF a draft response document containing a summary of draft responses to public comments received on the draft bills.
- On 10 October 2017, National Treasury and SARS gave an update to the SCoF on the steps taken in addressing the key issues raised during the consultation process on the 2017 Draft TLAB and TALAB.
- The 2017 TLAB & TALAB were introduced by the Minister in National Assembly on 25 October 2017.
- The SCoF voted on the 2017 TLAB & TALAB on 8 November 2017.
- The 2017 TLAB & TALAB were debated in National Assembly on 21 November 2017.
- Today, 28 November 2017, National Treasury and SARS are briefing the Select Committee on Finance on the key issues in the TLAB & TALAB.

TLAB: Contents

- The TLAB contains more complex and technical amendments announced by the Minister in the Budget.
- The key issues contained in the TLAB include the following:
  - Limitation of foreign employment income exemption
  - Tax relief for Bargaining Councils regarding tax non-compliance
  - Addressing the circumvention of anti-avoidance rules dealing with share buy backs and dividend stripping
  - Tax implications of debt relief:
    - Debt relief for benefit of mining companies
    - Debt relief for dormant group companies
    - Tax treatment of conversion of debt into equity
  - Tax treatment of banks and certain other financial institutions due to changes in the financial reporting standard from IAS 39 to IFRS 9
  - Extending the application of CFC rules to foreign companies held via foreign trusts and foundations

Limitation of foreign employment income exemption

- The 2017 TLAB contains an amendment aimed at limiting the current exemption applicable to foreign employment income earned by South African tax residents.

- With effect from 1 March 2020, South African tax residents who spend more than 183 days outside of South Africa rendering employment services will now only be exempted up to the first R1 million of their employment income earned abroad.

- The R1 million exemption will provide relief for lower to middle income South Africans working abroad.

- Any foreign employment income earned that exceeds R1 million will be taxed in South Africa.

Tax relief for Bargaining Councils regarding tax non-compliance

- Bargaining Councils receive moneys from employers of the members of Bargaining Councils (without deducting PAYE) as contributions for certain benefits such as holiday and sick leave and pay it to their members at an appropriate time.
- It has come to Government's attention that some Bargaining Councils have not deducted PAYE from the above-mentioned contributions paid to their members, and/or have not been paying income tax in respect of the growth/returns generated from their financial investments.
- The non-compliance potentially extends back a number of decades. Given that some of these Bargaining Councils would be at risk of closure or would suffer severe financial distress if high penalties and interest are imposed for non-compliance, and given the unique circumstances of this case, specific set of provisions is required to address the situation.
- The 2017 TLAB makes provision for the introduction of a specific relief for Bargaining Councils that have been non-compliant with tax legislation.
- Non-compliant Bargaining Councils will be required to pay a levy of :
  - 10% of the total PAYE that should have been deducted from all payments made to their members between 1 March 2012 and 28 February 2017, and
  - 10% of the total untaxed investment income between 1 March 2012 and 28 February 2017.
- The relief will apply in respect of the 5 year period starting from 1 March 2012 to 28 February 2017.
- Non-compliant Bargaining Councils must submit a return and pay a levy to SARS on or before 1 September 2018.
- The tax relief does not apply if the levy is not paid in time.

Addressing the circumvention of anti-avoidance rules dealing with share buy backs and dividend stripping

- The 2017 TLAB contains tax avoidance measures aimed at curbing the use of share buy backs schemes and dividend stripping by companies.
- These anti-avoidance measures will be limited to apply to dividends that are considered excessive (known as extraordinary dividends) as compared to normally acceptable dividends, received by a company within 18 months preceding the disposal of shares in another company.
- In addition, it is proposed that these rules should apply to transactions that were not finalised before 19 July 2017 as well as to any future transactions. Transactions whose terms were finally agreed to by parties on or before 19 July 2017 will not be subject to these rules.

Tax implications of debt relief

Debt relief for mining companies

- The Income Tax Act contains various rules dealing with the tax implications of debt relief. However, these rules do not apply to mining companies, due to the fact that mining companies have a special tax regime. In order to address this disparity, the 2017 TLAB contains specific rules to align the tax treatment of debt relief for mining companies with companies in other sectors.

Debt relief for dormant companies

- Also, the 2017 TLAB contains provisions aimed at limiting the current rules dealing with intra-group debt relief to apply only to dormant group companies.

Tax implications of debt relief

Conversions of debt into equity

- The 2017 TLAB contains definitive rules dealing with the tax treatment of conversions of debt into equity.
- In order to avoid unintended consequences and based on public comments received, the original proposals (sections 19A and 19B) contained in the draft bill that was published for public comment were removed. Changes were made in current provisions in section 19 of the Act to reflect the comments received.
- In addition, an anti-avoidance measure dealing with the trigger of a debt benefit whenever there is a change in any term or condition of the loan was introduced. This is aimed at closing a loophole whereby connected parties may be able to defer the recognition of any debt benefit indefinitely by repeatedly extending the duration of subordination agreements.
- SAIT strongly opposes the introduction of this anti-avoidance measure.
- In order to address SAIT's concerns, in view of the fact that the commencement date of this proposal is 1 January 2018, any unintended consequences as a result of the practical application of this provision, based on facts and circumstances, will be dealt with in the following Budget cycle.

Tax treatment of banks and certain other financial institutions due to changes in financial reporting standard

- The 2017 TLAB contains amendments dealing with the tax treatment of banks and certain other financial institutions due to changes in the financial reporting standards from IAS 39 to IFRS 9.
- To avoid a negative impact on the banking sector due to the fact that banks that are registered under the Banks Act are treated differently from other financial service providers, in that they are highly regulated by the South African Reserve Bank and subject to stringent capital requirements, the 2017 TLAB proposes definitive rules dealing with the tax treatment of impairment allowances for banks as follows:
  - 85% of an amount classified as being in default (including retail exposure) in terms of Regulation 67 issued under the Banks Act and administered by the South African Reserve Bank;
  - 40% of IFRS 9 loss allowance relating to impairment based on annual financial statements as is equal to the difference between the amount of the loss allowance relating to impairment that is measured at an amount equal to the lifetime expected credit losses and the amount that is classified as being in default; and
  - 25% of IFRS 9 loss allowance relating to impairment based on annual financial statements excluding the loss allowances under the 405 and 85% categories.

Extending the application of CFC rules to foreign companies held via foreign trusts and foundations

- In line with the G20/OECD base erosion and profit shifting (BEPS) Action 3 report dealing with *"Designing Effective Controlled Foreign Companies Rules (CFC)"*, the 2017 TLAB contains anti-avoidance measures aimed at extending the application of CFC rules to foreign companies held via foreign trusts or foundations and whose financial results are reflected in the consolidated financial statements (as contemplated in IFRS 10) of a South African resident company.
- In order to avoid unintended consequences and based on public comments received, proposed CFC rules under section 9D were adjusted. However, the other proposal relating to section 25BC contained in the draft bill was removed.
- It is proposed that measures to address the loophole to have been addressed in the removed section 25BC be dealt with in the following Budget cycle.

TALAB: Contents

- The TALAB contains the administrative tax amendments announced by the Minister in the Budget.
- The key issues contained in the TALAB include the following:
  - Fourth Schedule to the Income Tax Act: Spread of cap on deductible retirement fund contributions for PAYE purposes
  - Tax Administration Act: Fraudulent refunds – hold on a refund in a taxpayer's account by bank
  - Customs Control Act: Rules and applications prior to Act coming into operation

Fourth Schedule to the ITA: Spread of cap on deductible retirement fund contributions for PAYE purposes

- The 2017 TALAB clarifies the application of the annual monetary cap on contributions to retirement funds for PAYE purposes by proposing that the R350 000 be spread over a tax year.

- Initially a simple spread of R29,166.67 per month was considered but, after consultation with payroll software industry, this was revised to a cumulative basis for the portion of the year of assessment that the employee receives remuneration from the relevant employer.

- Example: If an employee is employed by an employer for 7 months during the 2018/19 tax year a cumulative deduction limitation of R204 167 (R29 166.67 X 7) will apply in the 7th month.

Tax Administration Act: Fraudulent refunds – hold on a refund in a taxpayer's account by bank

- The 2017 TALAB contains an amendment to improve the effectiveness of combatting refund fraud and respond to representations by members of the financial sector.
- It is proposed that a bank not be required to notify SARS of suspected refund fraud and then place a hold on the refund amount on SARS' instruction but instead enables the bank to notify SARS and automatically place a 2 business day hold on the refund if the bank reasonably suspects that the payment of a refund into the taxpayer's account is related to a tax offence.
- The *modus operandi* in respect of refund fraud generally involves transfer of the refund amount as fast as possible to other accounts or cash withdrawals – an automatic hold will ensure that the funds are secured as soon as the transaction is detected.
- Banks generally have sophisticated systems to detect and analyse suspicious transactions, the hold in issue is limited to 2 business days and the amount of the suspicious refund – not the whole account.
- The 2 business day hold may be lifted if either SARS or a High Court directs otherwise, so a taxpayer who believes the hold is inappropriate or faces prejudice may approach either to make their case.

Customs Control Act: Rules and decisions prior to Act coming into operation

- The 2017 TALAB contains an amendment that permits the publications of rules and taking of decisions, such as the appointment of customs officers and delegation of powers and duties, under the new Customs Duty Act and Customs Control Act before the Acts come into operation.
- This approach is intended to facilitate the transition to the new Acts and is only a more specific version of a similar provision in the Interpretation Act.
- The rules and decisions will only be effective when the new Acts come into operation.

THANK YOU