

# STANDING COMMITTEE ON FINANCE PUBLIC HEARINGS



## DRAFT TAX BILLS 2017

29 AUGUST 2017

Presented by:  
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2016

# DRAFT BILL OVERVIEW

## DISCUSSION POINTS TODAY

NT consultation and other important matters

Foreign income exemption

Bargaining council amnesty

Share buy backs and dividend stripping

Extension of CFC rules to Trusts

Relief on dormant group company debt waivers



01

# Important matters to discuss with NT

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## OTHER IMPORTANT MATTERS TO BE DISCUSSED WITH NT

- It is noted that on most points raised in our submission there has been no consultation by NT prior to the submission of the Draft Bill to SCoF as the workshops are only scheduled for 4-5 September 2017.
- We look forward to especially discussing a number of anomalies as outlined in our detailed submission, in particular relating to the following:
  - The proposed extension of section 7C and interaction of this section with Transfer Pricing and the NCA
  - Sections 19A and 19B recoupable interest and debt
  - Section 44 assumption of contingent liabilities
  - The policy in respect of retrospective and retroactive legislation.





02

# Foreign employment income exemption

Addressing cross border arbitrage fairly

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# FOREIGN INCOME EXEMPTION

## POLICY RATIONALE

- **Reducing compliance cost**
  - Implemented due to tax policy change: Residency base taxation
  - Transition would require previous exempt foreign source income to be taxed in SA
  - SA may in many instances not have ultimate taxing rights due to DTAs
  - Costly tax administration to provide credit system

# FOREIGN INCOME EXEMPTION NOT A CONCERN AND PROPOSAL

- **Addressing double non-taxation**
  - Repeal provision
  - No other proposals
- **Arbitrage with public sector**
  - Repeal private sector exemption

# FOREIGN INCOME EXEMPTION

## ANOMOLIES TO BE ADDRESSED

- **Financial hardship**
  - Tax to be paid in two or more countries with employee to carry cash flow until refunded. Currently on tax paid in foreign country.
- **Complex administration**
  - DTA and section 6quat to be applied for **each** country separately. Country no added administration.
- **Administration challenges**
  - SARS has strict proof of withholding requirements and many countries do not have formal withholding tax certificates.
- **Foreign workers face tax deduction arbitrage**
  - If all income taxable in SA, foreign employees should be allowed foreign social security and retirement contribution deduction, as their SA employed counterparts





# FOREIGN INCOME EXEMPTION RECOMMENDATION

- **Full repeal to be reconsidered**
  - Provision should be amended to address double non-taxation
- **Tax cash flow provisions**
  - Where an exemption is not considered, liability for taxes should be deferred till assessment to prevent employees having to carry cash flow.
- **Administration**
  - The administrative process from the current corporate tax proof requirements e.g. employer to just prove and declare foreign tax payment as is practice in SA.



03

## Bargaining council amnesty

Addressing non-compliance

SAICA SOUTHERN REGION STAFF



# BARGAINING COUNCIL AMNESTY

## POLICY RATIONALE

- Fiscus will forgo income in certain instances if it is in the greater economic good

# BARGAINING COUNCIL AMNESTY

## NT CONCERN AND PROPOSAL

- **NT concern**
  - Council tax non-compliance created large financial exposure
  - Threatens financial viability of councils due to penalty and interest exposure
- **Proposal**
  - Charge a fixed levy on 10% of investment income and employees tax unpaid between 1 March 2012 and 28 February 2017

# BARGAINING COUNCIL AMNESTY CONCERNS

- **NT policy rationale**

- The rationale to provide amnesty to specific taxpayers rather than for specific transgressions is arbitrary
- The rationale to relieve **both** employees and councils of their obligations and councils is unclear. The policy to provide tax amnesty to a very select group of employees rather than to a type of transgression cannot be supported and can lead to abuse
- There is currently relief offered for transgressions in the form of the VDP and para 5(2)-5(5)
- No indication as to the extent of non-compliance before 1 March 2012 and whether that will threaten financial viability?
- The scope of the relief is unclear. EM refers to end of the year payments i.e. bonuses as well, but legislation excludes this?



# BARGAINING COUNCIL AMNESTY

## RECOMMENDATIONS

- The relief for employees should be separated from the obligation of the Council
- If employees are to be provided amnesty, affected employees should be applying for relief separately from Councils
- The problem should be addressed in its totality. Therefore amnesty should be provided to Councils for all historical liabilities and not just a levy on quantified for liability for last 5 years. SARS is not empowered by law to compromise debt outside the current legislative framework and cannot ignore older obligations



04

# Share buy backs and dividend stripping

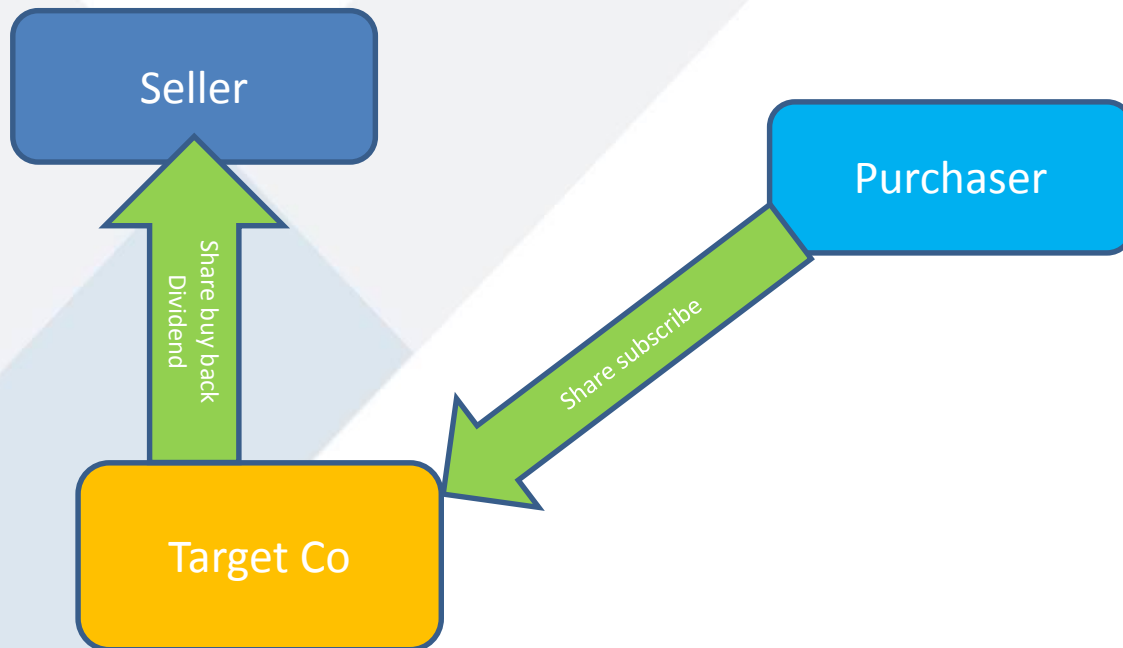
Section 22B and para 43A

SAICA STAFF: NONCEBA XINTI  
Personal Assistant: Members in Business

# SHARE BUY BACKS

## CONCERN SHARE BUY BACKS – EXAMPLE 1

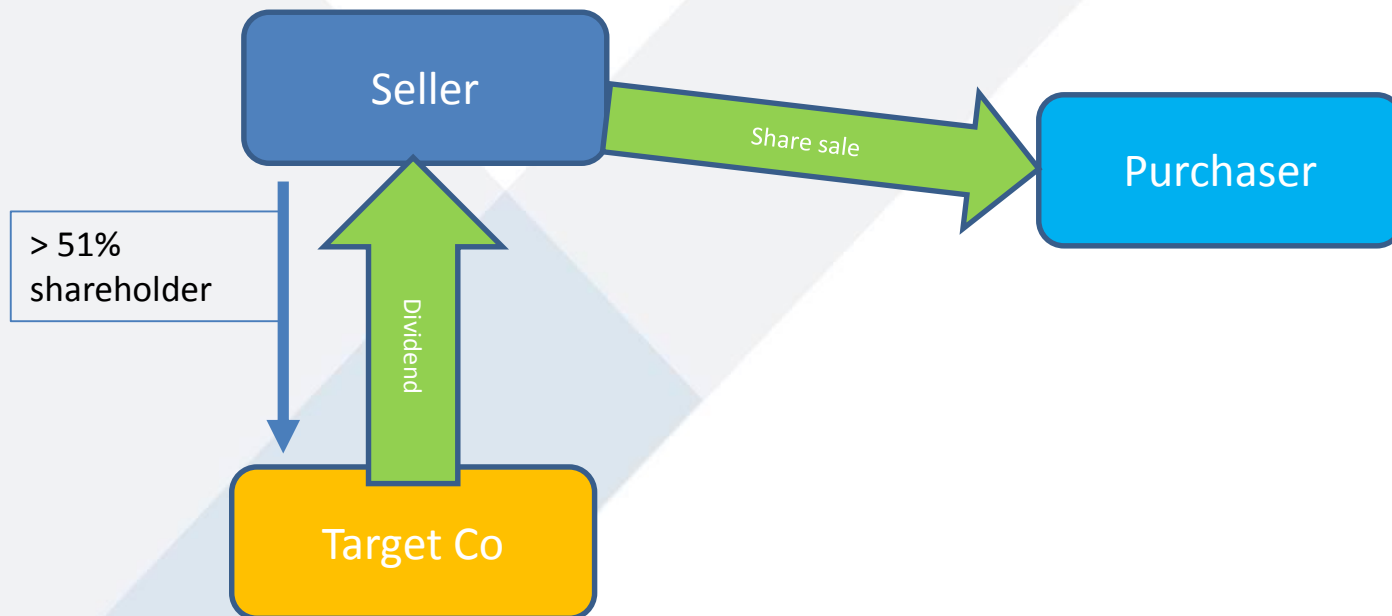
Seller owns 100% of Target Co and wants to sell Target Co for R100 to purchaser. Has a base cost of R60 with potential CGT of R9. Purchaser subscribes for shares for R100, the shares of the Seller are bought back and in the process Seller receives exempt share buy back dividend of R100.



# SHARE BUY BACKS

## CONCERN DIVIDEND STRIPPING – EXAMPLE 2

Seller, a >51% shareholder wants to sell Target Co for R100 to purchaser. Has a base cost of R60 with potential CGT of R9. Target Co has money reserves of R40. Seller agrees with Purchaser to sell Co exclusive of money reserves for R60.





# SHARE BUY BACKS

## NT PROPOSAL

- Extend current dividend stripping rules to address both concerns and make it more principle-based
- This includes:
  - Inclusion of a timing rule of 18 months without a causal link between the dividend and the sale
  - Reduce ownership requirement to 20% where no person holds majority
- Remove connection to loan or other funding from purchaser as presently required
- Apply retrospectively to 19 July 2017 to disposals on or after this date



# SHARE BUY BACKS

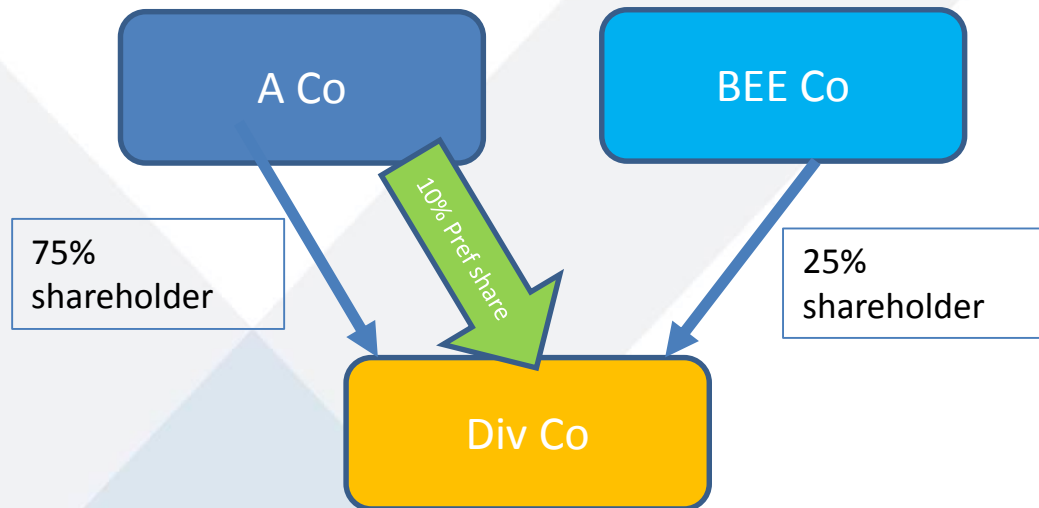
## CONCERNS AND RECOMMENDATIONS

- Anti avoidance will apply to any dividend declared within 18 months irrespective of a causal link between the dividend and the sale. Dividend must still be linked to sale as an additional requirement.
- Time based rule (i.e.18 month rule) as proposed will apply retrospectively to sales concluded before 19 July 2017 but that were subject to suspensive conditions, irrespective of causal link to sale. Should apply only to dividends declared on or after 19 July 2017.
- Qualifying interest : Say A holds a 30% interest in the company, B holds 30% and C holds the remaining 40%. If A and B are 'connected persons' then in effect C only holds a minority stake and could be outvoted by connected persons A and B. C's holding of 40% should therefore not be regarded as a 'qualifying interest'.

# SHARE BUY BACKS

## CONCERNS AND RECOMMENDATIONS

20% rule will apply to non-equity shares as well which are not part of the relevant anti avoidance concerns. The provision should only apply to **equity shares**



For example, Company A holds 75% of the equity shares in Company B. The balance of the equity shares are held by a BEECo. In order to fund Company B, Company A subscribed for redeemable preference shares carrying a right to dividends at a fixed rate. The effect of the provisions is that any dividends received by Company A in respect of the preference shares within 18 months of their **redemption** or as part of the redemption will be included in proceeds and will be subject to CGT

05

# Extension of CFC rules to Trusts

Sections 9D and 25BC

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Credit Control Supervisor: Finance

# EXTENSION OF CFC RULES TO TRUSTS

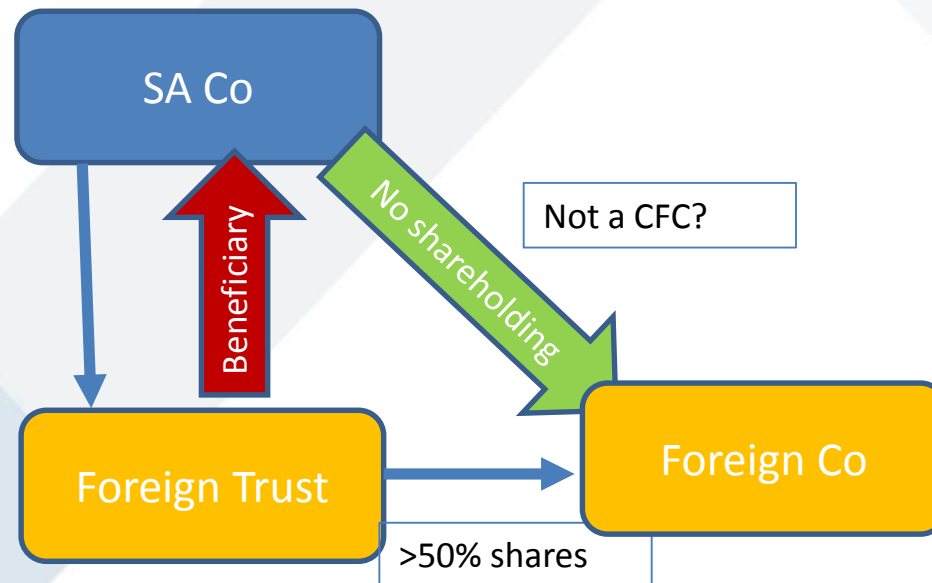
## POLICY RATIONALE

- CFC imputation is an anti-avoidance measure to ensure that mainly passive income that should be taxed in SA for SA residents is not diverted to a non-resident company
- Where an actual business is conducted, no imputation should be done and that foreign country alone should exercise taxing rights
- Non-resident trusts that hold shares in CFCs do not give rise to CFC imputation

# EXTENSION OF CFC RULES TO TRUSTS

## NOT A CONCERN

The interposition of a foreign trust breaks SA resident holding requirement for the participation rights.





# EXTENSION OF CFC RULES TO TRUSTS

## NT PROPOSAL

- CFC will now include:
  - Company where an interest is held in a foreign trust or foreign foundation which in turn holds or may exercise >50% of the participation or voting rights ; or
  - Any foreign company that has to be consolidated into the SA company by virtue of IFRS 10
  - New section 25BC to impute income in the case of non-companies that are beneficiaries of a foreign trust or foreign foundation, where the foreign trust holds >50% of the participation or voting rights in a foreign company

# EXTENSION OF CFC RULES TO TRUSTS

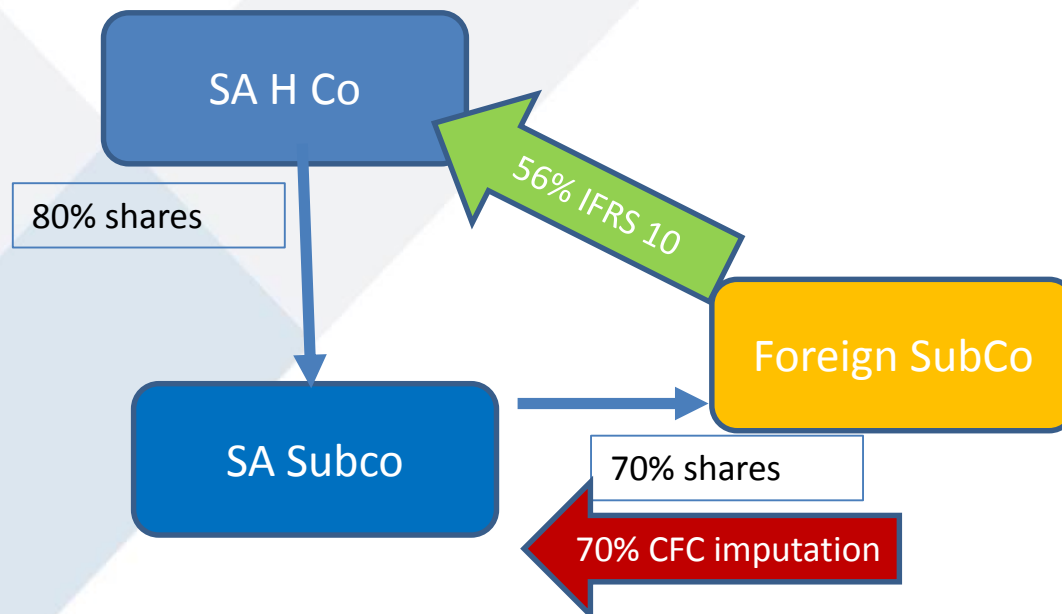
## CONCERNS AND RECOMMENDATIONS (1)

- Current provision section 9D wide enough for vesting trust as covers directly and indirectly. Discretionary trusts will not hold an interest and will have no participation rights in respect of a mere hope (*spes*). Therefore the section 9D proposal will not result in an imputation relating to companies that are discretionary beneficiaries of foreign trusts.
- If discretionary trusts are included and there are multiple beneficiaries, it would be impossible to determine “participation rights” as the right to participation lie at the discretion of the trustees.

# EXTENSION OF CFC RULES TO TRUSTS

## CONCERNS AND RECOMMENDATIONS (2)

Wording of the proposed further proviso to section 9D(2) leads to anomalies and not all accounting concepts are interchangeable with CFC regime. IFRS consolidates at H Co level (56% economic interest) and CFC at SA Subco level (70%). Even greater disparity if foreign trust holds Foreign Subco and there are multiple beneficiaries.



# EXTENSION OF CFC RULES TO TRUSTS

## CONCERNS AND RECOMMENDATIONS (3)

- There is no clear order of preference for the application of sections 25B, 25BA and 7(8) and they could apply simultaneously in addition to paragraphs 72 and 80 of the Eighth Schedule, leading to double taxation
- Section 25BA taxes as income both capital gains and exempt income received or accrued from a foreign trust, which is overly punitive



06

# Relief on dormant group company debt waiver

Section 19 and para 12A

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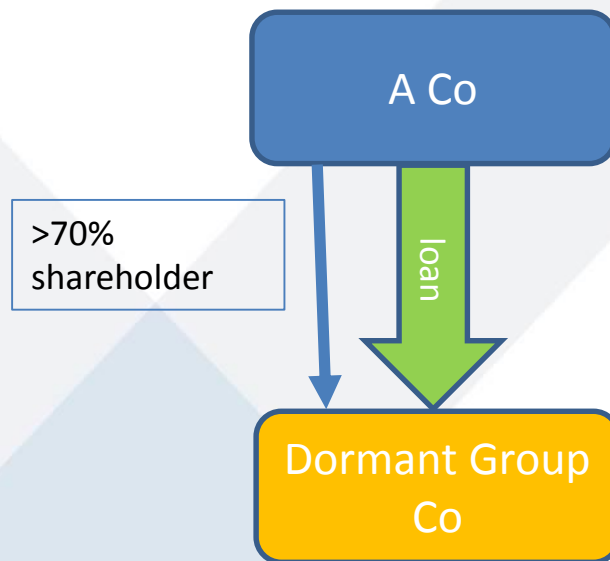
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# RELIEF FOR DORMANT GROUP COMPANY DEBT WAIVERS

## NT RATIONALE – ALIGNING SECTION 19 & PARA 12A

- In principle the alignment of section 19 with para 12A relief is welcomed



- Waiver of the loan in an unpayable loan scenario where revenue recoupments arise, will result in tax in Dormant Co, which could create insolvency

# RELIEF FOR DORMANT GROUP COMPANY DEBT WAIVERS NT PROPOSAL

Refine para 12A(6)(d) by essentially defining **dormant** to be:

- Company has not traded
- No amounts have been received
- No assets have been transferred
- No liability has been incurred or assumed

During the year of waiver and preceding 3 years

- Exclude debt used to finance assets disposed of by the dormant company in terms of the reorganisation rules
- Above relief and requirements to be duplicated in section 19

# RELIEF FOR DORMANT GROUP COMPANY DEBT WAIVERS CONCERN AND RECOMMENDATIONS (1)

## Main request:

- Retain current para 12A(6)(d) and duplicate it in section 19
- Current form is pragmatic and used for other commercial situations other than for dormant companies

# RELIEF FOR DORMANT GROUP COMPANY DEBT WAIVERS CONCERN AND RECOMMENDATIONS (2)

If current relief is not retained then:

- **Time period** of 4 years too long as companies will be forced to retain dormant companies for such period to qualify
- The restriction regarding **asset transferral** to or from the dormant company should be removed. By being dormant companies lose their trade losses for tax
- Dormant companies may have minimal amounts of **income** to fund small expenses like completion of tax returns and CIPC. Should have a de minimus rule instead
- Dormant companies will have small **liabilities** incurred such as CIPC and bank charges. *De minimus* amount recommended

# RELIEF FOR DORMANT GROUP COMPANY DEBT WAIVERS CONCERN AND RECOMMENDATIONS (3)

- Limitation on assets disposed of by the dormant company to fellow group companies does not seem to address any mischief and is overly restrictive
- The Explanatory Memorandum indicated that there would be an exclusion for group debt forgiven. Therefore the exclusion of group debt assumed by the dormant company is puzzling given the lack of any identified mischief



# RELIEF FOR DORMANT GROUP COMPANY DEBT WAIVERS CONCERN AND RECOMMENDATIONS (4)

- The effective date is noted as just 1 January 2018. We recommend that it applies to debt reductions that occur on or after 1 January 2018
- The relief should specifically extend to companies in business rescue as per Budget Review 2017



**THANK YOU**