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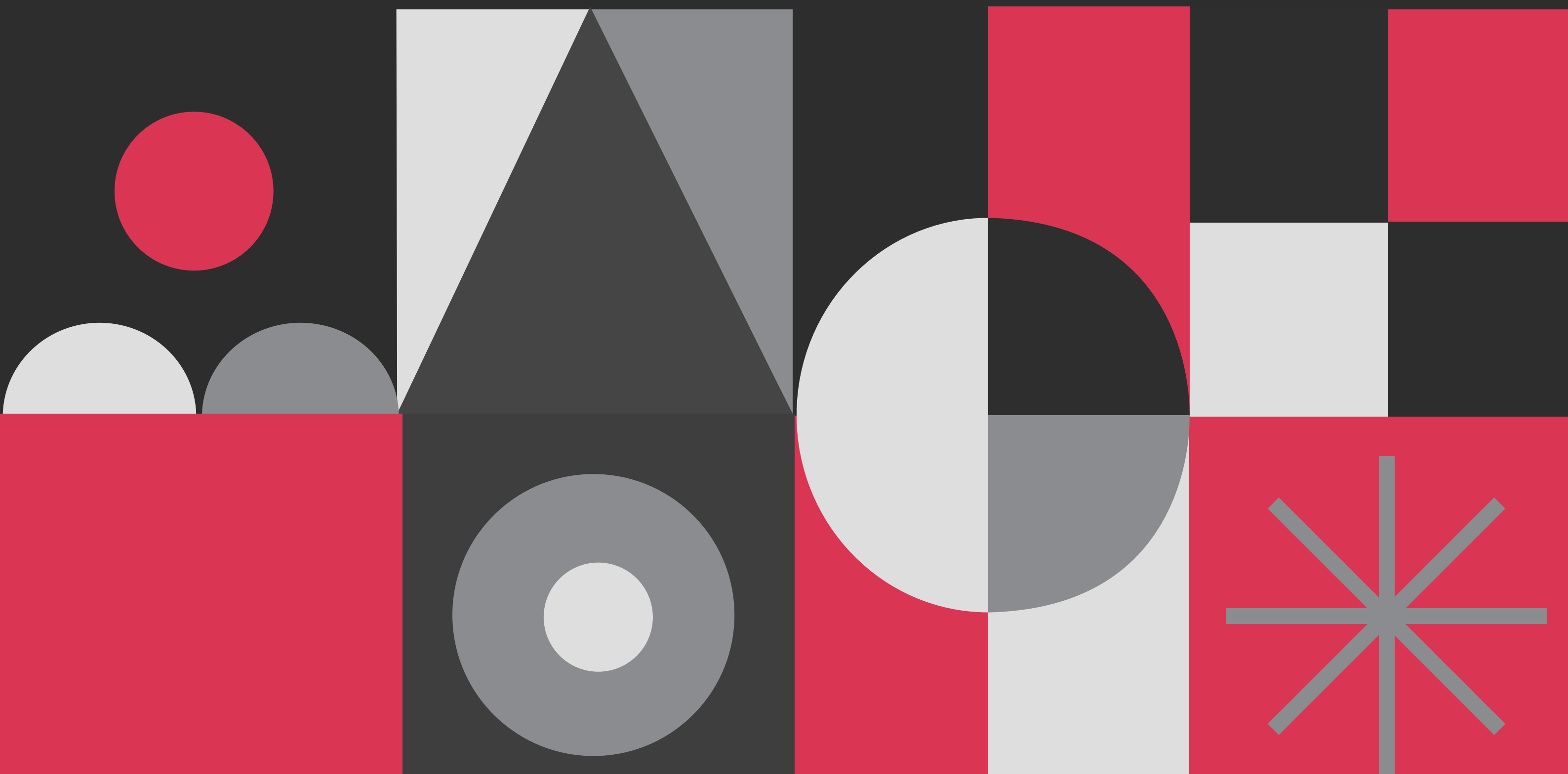
2023 Budget Review Highlights

Adapt for change



Major Tax Announcements

Tax revenue

Tax revenues for 2022/23 are expected to be R94 billion higher than was estimated at the time of 2022 Budget and some R10 billion higher than the estimate in the October mini budget. The primary contributor to this is corporate income tax, but personal income tax and customs duties have also performed better than expected than at the times of the previous budgets. VAT is, however, estimated to be lower than previously estimated, illustrating the pressure that the consumer is under.

The better than expected revenue collections over the October estimate is expected to partially carry through to the medium term, although it is expected that the contributions from the mining sector will decline.

Kyle Mandy, Head of Tax Technical and Policy, Tax Partner

Personal Income Tax

The Minister of Finance announced in the Budget that there would be an inflation-adjustment to the individual tax brackets and a long overdue change to the retirement tax tables. There will also be relief to households that install solar panels and no increase in fuel levies.

The rooftop solar incentive for individuals will be in the form of a rebate to the value of 25% of the cost of any new or unused solar PV panels up to a maximum of R15,000 per individual. There will be certain qualification criteria that will need to be met to qualify and the rebate will be limited to solar PV panels installed at a private residence and not for inverters or batteries.

The personal income tax brackets will be adjusted by 4.9% with the result that, with effect from 1 March 2023, the maximum rate of 45% applies to taxable income in excess of R1,817,001 (up from R1,731,600), while the lowest rate of 18% applies to taxable income up to R237,100 (up from R226,000) with similar adjustments to the brackets in between. There will also be an approximately 4.9% increase in the primary, secondary and tertiary rebates. The tax-free threshold has now increased from R91,250 to R95,750 for taxpayers under 65 years of age.

The medical tax credit available to taxpayers who are members of medical aid schemes has been increased nominally from R347 to R364 per month for each of the first 2 dependents and from R234 to R246 per month for every subsequent dependent.

The amount which can potentially be paid tax-free upon retirement from a retirement fund or as a severance benefit from an employer has been increased from R500,000 to R550,000 and the level at which the maximum rate of 36% is applicable has increased from R1,050,000 to R1,155,000, with similar adjustments to the two levels in between. For retirement fund withdrawal benefits, the maximum potential tax-free limit has increased from R25,000 to R27,500 and the maximum rate of 36% now applies to amounts in excess of R1,089,000, up from the previous level of R990,000, with similar adjustments in between.

The two pot retirement system announced last year now has a targeted implementation date of 1 March 2024 for the first phase, although it is acknowledged that further work is required in this regard.

Reform to the pay-as-you-earn (PAYE) and personal tax administration previously announced will continue with the aim that, over time, the need for employer PAYE annual reconciliations will fall away and discussions with employers and representative organisations are ongoing.

Where taxpayers cease to be tax resident during a year of assessment, it is proposed that the tax-free investment contribution limit as well as the annual limit on the deduction of retirement fund contributions will be apportioned, in the same way that the capital gains tax exclusion and interest exemption were previously limited.

Increases have also been announced in respect of tax-free subsistence allowances that can be paid to employees spending time away from their usual residences for work purposes for incidental costs, or meals and incidental costs (R152 to R161 and R493 to R522 respectively). The tax-free travel reimbursement rate that can be paid to employees for business travel under certain circumstances is up from R4,18/km to R4,64/km.

Barry Knoetze, Tax Associate Director

Corporate Tax (Business general)

Review of Practice Notes to be withdrawn

The South African Revenue Service (SARS) recently issued a notice of its intention to withdraw the Practice Notes relating to *Interest paid on moneys borrowed* and *Deduction of fees paid to accountants, bookkeepers and tax consultants for the completion of income tax returns*. After considering public comments received, Government will consider the impact of the proposed withdrawal and the introduction of legislation to accommodate legitimate transactions impacted by this withdrawal. The proposed withdrawal will accordingly be deferred and aligned with the introduction of the new legislation.

Clarifying anti-avoidance rules dealing with third-party backed shares

In terms of the current rules, the anti-avoidance provisions relating to third-party backed shares (which essentially deem dividends on debt-like equity instruments to be taxable) do not apply where the funding is used to acquire equity shares in an operating company. This exclusion from the anti-avoidance rules will be clarified to address the instance where the equity shares in an operating company are no longer held.

Addressing the abuse relating to contributed tax capital

Contributed tax capital is the consideration received by a company in exchange for the issue of shares. A distribution by a company which constitutes a reduction of its contributed tax capital is essentially classified as a capital distribution (and not a dividend) for tax purposes and hence is not subject to dividends tax.

Government has identified a structure which abuses the current contributed tax capital rules, whereby a South African company held by a foreign holding company via another foreign intermediary could make distributions to the ultimate foreign holding company without incurring dividends tax. This is generally achieved by migrating the tax residence of the foreign intermediary to South Africa, which allows for the creation of a contributed tax capital balance equal to the value of the shares of that foreign intermediary before its migration. To address this abuse, Government proposes that amendments be made to the tax legislation relating to contributed tax capital.

Debt reduction rules for dormant companies disposing of assets in terms of corporate reorganisation transactions

In terms of the debt reduction rules, adverse tax implications may arise for a debtor where there is a concession or compromise in respect of a debt. These debt reduction rules however generally do not apply to dormant group companies, but there are exceptions. One such exception is in relation to debt which funds an asset that is disposed of by a dormant group company in terms of the corporate reorganisation provisions. Government proposes clarifying the application of the rules regarding this exception.

Acquisition of assets in exchange for shares

Where a company issues shares in exchange for the acquisition of an asset, it is deemed to acquire a base cost in the asset equal to the market value of the shares issued plus any capital gain that may be triggered by the anti-value-shifting rules. The deemed base cost rule was recently extended to corporate reorganisation transactions and Government now proposes clarifying the legislation as to whether allowances may be determined with reference to the deemed base cost.

Unbundling transactions

In 2020, changes were made to unbundling transaction rules to curb tax avoidance where unbundling transactions are used to distribute shares of unbundled companies to tax-exempt persons or non-resident investors. Distributions of unbundled companies to disqualified persons holding more than five percent of the equity shares in the unbundling company are therefore subject to tax and, as a result, such tax paid can be added to the base cost of the shares unbundled. Government proposes revisiting these rules and whether it is appropriate to increase the base cost in such instances.

Interest limitation rules

As part of the package of reducing the headline corporate tax rate in a revenue-neutral manner, one of the measures to broaden the tax base included strengthening the rules dealing with the limitation of interest deductions for debts owed to certain persons not subject to tax. It has come to Government's attention that these measures require further clarification in the following areas:

- Treatment of assessed losses in determining the interest limitation
- Treatment of exchange gains and losses
- Application of the rules where withholding tax is payable on the interest
- Exemption from the rules where the creditor provides the loan with funds granted to it by a lending institution, which is proposed to also include South African lending institutions
- A 'controlling relationship' requirement and definition for the rules to apply

Angus du Preez, Tax Partner

Corporate Tax (Business incentives)

Accelerated and increased section 12B capital allowance

To promote renewable energy and encourage private investment in the renewable energy industry, Government proposes an increased capital allowance in terms of section 12B for qualifying investments brought into use for the first time between 1 March 2023 and 28 February 2025. Taxpayers will enjoy an increased allowance of 125% of the cost of qualifying investments in the year the asset is first brought into use. There will be no limitation of the maximum allowance claimed.

Extending and refining the Research and Development (R&D) tax incentive

The R&D incentive as it currently stands has a sunset date of 1 January 2024. After public consultation, Government proposes to extend the R&D incentive for 10 years from 1 January 2024. A six-month grace period will be allowed for projects to commence before the application is submitted.

The definition of R&D will be simplified but the incentive will only be allowed if the activities are aimed at resolving a scientific or technological uncertainty. The R&D must be novel, uncertain, systematic and transferable and/or reproducible.

Furthermore, internal business processes that were previously excluded will now be allowed. R&D would therefore qualify for the incentive irrespective of whether it is intended for sale or use.

Urban Development Zone (UDZ) incentive extended

As a result of the policy review process of the Urban Development Zone incentive likely not being finalised by 31 March 2023, the incentive is extended for two years to 31 March 2025 to allow for the review process to be concluded.

Solar-related loans — Energy Bounce Back Scheme

In order to incentivise renewable energy, rooftop solar, and address energy-related constraints experienced by small and medium enterprises, Government will guarantee solar-related loans for small and medium enterprises on a 20 percent first-loss basis.

The Energy Bounce Back Scheme will be launched in April 2023.

Tapie Marlie, Audit of Tax and Tax Incentives Partner

Corporate Tax (Financial Services)

Refining the provisions dealing with the impact of International Financial Reporting Standard 17 insurance contracts on the taxation of insurers

The International Financial Reporting Standard (IFRS) 17 relating to insurance contracts replaced IFRS 4 with effect for reporting periods starting on or after 1 January 2023. The new standard requires a new approach to the measurement, reporting, and disclosure of the profitability of insurance contracts.

Changes were made to the tax treatment of short-term and long-term insurers in sections 28 and 29A, respectively, to accommodate the implementation of IFRS 17 with the most notable change being the determination of insurance contract liabilities deductible for income tax purposes.

Under IFRS 17, amounts recoverable from a cell owner under certain third-party cell captive arrangements are treated as reinsurance arrangements even though these arrangements may not qualify as commercial reinsurance. In addition, liabilities payable to the cell owner by the insurer in respect of profits due to the cell owner may be included in the value of liabilities that are deductible for income tax purposes under section 29A.

It is proposed that reinsurance contracts relating to a cell owner be disregarded. In addition, the definition of the value of liabilities in section 29A will be amended to exclude any other liabilities relating to a cell owner.

Due to the complexity of insurance tax, further technical corrections relating to the practical implementation of the new IFRS 17 tax regime may be required in 2023.

Reviewing the Sharia-compliant financing arrangements

It is proposed that legislation dealing with Sharia-compliant financing arrangements be extended across all the tax acts to ensure alignment with the already existing legislation.

Stephen Boakye, Financial Services Tax Associate Director

Jos Smit, Financial Services Tax Partner

International Tax

Foreign dividends sourced from tax-deductible payments

At present, the outright exemption for certain categories of foreign dividends is denied if those foreign dividends are directly or indirectly sourced from tax-deductible payments (typically interest). It is now proposed that:

- those targeted foreign dividends will also be denied the partial exemption that currently results in an effective tax rate of 20% — so those dividends will now end up being taxed at the full normal tax rates; and
- this anti-avoidance regime (including, presumably, the additional proposal above) will be extended to foreign dividends from so-called dual-listed companies, i.e., where tax-deductible payments are round-tripped through foreign companies whose shares are also traded on the JSE.

Controlled foreign companies (CFCs) — outsourced functions

It is proposed that the 'foreign business establishment' (FBE) definition be amended to disqualify certain outsourcing arrangements. That is, it will be 'clarified' that, to qualify as an FBE, all important functions for which a CFC is compensated must be performed by the CFC or by another qualifying CFC (subject to certain requirements).

Capital gains tax (CGT) participation exemption

The CGT exemption for returns of capital from foreign companies will now also be subject to the 18-month minimum holding period that is required for the CGT exemption in respect of the outright disposal of foreign shares.

A further anti-avoidance measure will also be introduced to deny the exemption where the seller and non-resident purchaser are ultimately controlled by the same shareholders.

Foreign beneficiaries of trusts

Whereas SA-source trust income attributable to non-SA beneficiaries is currently taxable in the hands of those beneficiaries, SA capital gains (attributable to those non-resident beneficiaries) are taxed in the trust itself. It is proposed to align the taxation of income with that of capital gains, i.e., to charge and collect the tax from the trust, rather than from the non-resident beneficiary.

Global minimum corporate tax

National Treasury will publish (during 2023) a draft position paper to implement the OECD's 'Pillar Two' proposals, i.e. a global minimum corporate tax of 15%. The draft paper will inform legislation to be included in the 2024 tax amendments — which presumably means that SA could implement Pillar Two from 2025.

Transfer pricing APAs

Proposals to introduce a regime for Advance Pricing Agreements (APAs) have been made in previous announcements. This year's review statement again included a proposal to introduce a legislative framework to empower SARS to conclude bilateral APAs.

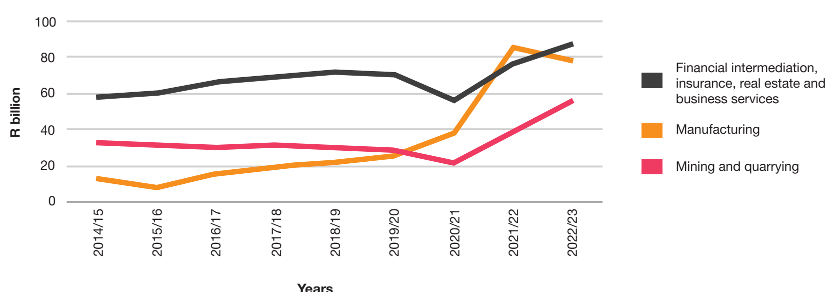
Prof Osman Mollagee, Tax Partner

Mining and Oil & Gas

Revenue collection in the mining industry

The mining industry continued the 2021/2022 trend of its large contribution to the revenue collection due to elevated — although declining — commodity prices. The mining sector accounts for nearly 30 percent of provisional corporate tax collections in 2022/23 — significantly higher than its average share before 2020/21. Although the extended period of elevated prices has led to revenue surpluses over the last two years, National Treasury expects this to be temporary and the current tax revenue outlook assumes that these prices will gradually decline. A continuation of high prices would likely result in future revenue overruns.

Figure 4.2 Provisional corporate income tax collections by sector, 1 Apri – 31 January



Source: 2023 Budget Review, Chapter 4 - Revenue Trends and Tax Proposals

Revenue collection in the mining industry — mineral and petroleum royalties

The expected increase in the collection of mineral and petroleum royalties in respect of 2022/2023 is further evidence of the continued elevated profitability of mining companies. In the 2022 Budget Review estimates, the budget estimate for mineral and petroleum royalties was R18,554m, whereas the revised budget estimate in the 2022/2023 Budget Review amounts to R25,483m. Although the 2022/2023 estimate is lower than the 2021/2022 outcome of R28,456m, it is still a 79.1% increase from the mineral and petroleum royalties revenue outcome of 2020/2021 of R14,228m.

Adjusting the minimum royalty rate for oil and gas companies

Following the consultation process regarding the tax regime of oil and gas companies, Government proposes to retain the variable royalty rate, which is driven by profitability. Using a variable royalty rate recognises that companies face various profit levels depending on the life-cycle of the operations and geological factors (such as operating in deep or shallow waters). In this regard, it is proposed that the minimum royalty rate of 0.5% is increased to 2% to adequately compensate the fiscus for the loss of its finite resources; the maximum rate of 5% will remain unchanged.

Laetitia Le Roux, Energy, Utilities and Resources Tax Partner

Exchange control / financial surveillance

No significant exchange control announcements were made, except that the South African Reserve Bank (SARB) and National Treasury are working together to enhance the monitoring and reporting of crypto asset transactions, to ensure compliance with the exchange control regulations.

VAT

Reviewing the VAT treatment of specific supplies in the short-term insurance industry

In 2013, SARS issued Binding General Ruling 14 (BGR 14) setting out the VAT treatment of specific supplies in the short-term insurance industry. This BGR contained a decision issued under section 72 of the VAT Act relating to excess payments. BGR 14 was subsequently updated in 2018 and 2020.

Due to changes to section 72, and the subsequent withdrawal of the above decision issued under section 72, it is proposed that the VAT Act be amended to clarify the treatment of excess payments.

Clarifying the VAT treatment of prepaid vouchers in the telecommunications industry

The VAT treatment of prepaid airtime vouchers has been the subject of recent case law. Historically, prepaid airtime vouchers have been treated as section 10(19) vouchers, meaning that VAT is accounted for at the time such vouchers are sold, and not at the time of redemption.

As a result of industry changes and the evolution of airtime vouchers, National Treasury is of the view that the VAT Act does not provide absolute clarity in instances where, for example, prepaid vouchers are used for services provided by a third party, the mobile telecommunication company is acting as an agent, and/or third-party-provided services are exempt or non-taxable supplies for VAT purposes. It is proposed that changes be made to the VAT Act to provide clarity with regards to the treatment of airtime vouchers.

VAT treatment of temporary letting of residential property

Section 18D clarifies the VAT treatment of the temporary letting of residential property. The temporary letting of residential property results in a deemed supply. Section 10(29) deems the value of the deemed supply to be equal to the adjusted cost to the vendor.

National Treasury will provide clarity as to whether the definition of 'adjusted cost' includes the costs of land, as well as further technical clarifications to this section.

Regulations imposing a domestic reverse charge on valuable metals

Since 1 April 2015, various amendments relating to 'gold' and 'goods containing gold' were made to the VAT Act. The purpose of these amendments was to curb fraudulent input tax deductions on the acquisition of gold and gold jewellery.

National Treasury issued Regulations effective from 1 July 2022 requiring a domestic reverse charge (DRC) on the supply of valuable metals whereby the purchaser (i.e. recipient) and not the seller is required to declare the VAT charged on the sale of valuable metal to SARS.

National Treasury proposes various technical clarifications and changes to the Regulations in clarifying the following areas:

- The VAT rules dealing with documentary requirements for gold exports
- The definition of 'residue'
- The definition of 'valuable metal', taking into consideration:
  - Exclusions
  - Introducing a de minimis rule
  - Aligning the definition with the Precious Metals Act
- Transitional measures
- The responsibilities of the recipient of valuable metal

General proposal — administration

The Budget documents indicate that SARS intends to review the VAT administrative framework to simplify and modernise the current system. While it is not clear exactly what this review will entail, reference is made to providing clarity and certainty to taxpayers through processes like advance rulings.

Matthew Besanko, Indirect Taxes Leader

Rodney Govender, Indirect Taxes Partner

Customs and Excise

Customs

Save for minor proposals relating to the advance declaration of information required for the purposes of making due entry, SARS' discretion in relation to deferment rules and procedures for provisional payment liquidations, no further proposals were made in relation to the Customs and Excise Act.

Excise

Extension of diesel fuel levy refunds

The diesel refund system provides full or partial relief for the general fuel levy and the Road Accident Fund (RAF) levy to primary sectors and was implemented in 2000. The refund system is currently only applicable to the farming, forestry, fishing and mining sectors. A similar refund on the RAF levy for diesel used in the manufacturing process is proposed to be made available to manufacturers of foodstuff from 1 April 2023 for a period of two years ending 31 March 2025.

Duties on alcoholic beverages and tobacco products

Proposed changes in excise duties vary, with some products having no increase while others increase by an inflationary adjustment of 4.9%, as set out below:

- Fuel levy — no increase
- RAF levy — no increase
- Alcoholic beverages (wine, beer and spirits) — 4.9% increase
- Traditional African beer and beer powder — no increase
- Sparkling wine — 0.7% increase
- Tobacco products — 4.9% increase

An alcohol review paper will be published after the budget, followed by a tobacco review paper later this year, after which consultation on the excise policy for these two products will take place.

Health Promotion Levy

While there will be no increase in the Health Promotion Levy in the 2023/24 and 2024/25 financial years, National Treasury intends publishing a discussion paper for consultation on proposals to extend the levy to pure fruit juices and to lower the current threshold of 4 grams.

Herman Fourie, Tax Associate Director

Environmental taxes

- In line with the amendments brought about by the 2022 Taxation Laws Amendment Act, the carbon tax rate increased from R144 to R159 per tonne of carbon dioxide equivalent, effective from 1 January 2023.
- The future adjustments to the carbon tax rate, as outlined in the 2022 Taxation Laws Amendment Act, will be provided in the Carbon Tax Act, so as to ensure transparency and provide certainty.
- With effect from 5 April 2023, the carbon fuel levy for 2023/2024 will increase by 1c, i.e. to 10c/l for petrol and 11c/l for diesel.
- Effective from 1 January 2023, it is proposed that the carbon tax cost recovery quantum for the liquid fuels refinery sector will increase from 0.63c/l to 0.66c/l.

Carbon Offsets Regulations — extension of the utilisation period

- The utilisation period for carbon offsets from projects under taxable activities is proposed to be extended by three years, i.e. from 1 January 2023 to 31 December 2025, in order to align with the extension of the first phase of carbon tax announced in 2022.
- These amendments will be included in the Carbon Offset Regulations effective from 1 January 2023.

Alignment of fuel emission factors with methodological guidelines and regulations

- In order to align the Carbon Tax Act with the changes brought about by amendments to the methodological guidelines for quantifying greenhouse gas emissions, a new table with the Tier 2 emissions factors is proposed to be inserted into Schedule 1 of the Carbon Tax Act.
- The change from a Tier 1 to a Tier 2 methodology is set out under the transitional arrangement provisions within the Technical Guidelines to the National Greenhouse Gas Emission Reporting Regulations.
- The amendments will come into effect from 1 January 2023.

Adjusting the formula for fugitive emission factors

Given the inaccuracies in quantifying fugitive emissions for certain Intergovernmental Panel on Climate Change (IPCC) code activities under Section 4(2) of the Carbon Tax Act, it is proposed that certain technical amendments be made to the fugitive emission formula, so as to rectify the inaccuracies, where necessary.

Asif Joosub, Tax Partner

Jason Daniel, Tax Manager

Tax and Legal services leadership team

James Whitaker

TLS SMA Leader & Private Wealth

james.whitaker@pwc.com

Mbai Rashamuse

TLS SMA Operations and Transformation, Inclusion & Diversity Leader

mbai.rashamuse@pwc.com

Scott Berry

TLS SMA Clients & Markets Leader

scott.berry@pwc.com

Angus du Preez

TLS SMA People Leader

angus.du-preez@pwc.com

Makhosazana Mabaso

Reward

makhosazana.mabaso@pwc.com

Nathan Bokwe

Deals Tax

nathan.bokwe@pwc.com

Lynelle Petersen

Deals Tax

lynelle.petersen@pwc.com

Esmarie Viljoen

Audit of Tax

esmarie.viljoen@pwc.com

Rodney Govender

Value Added Tax

rodney.govender@pwc.com

Matthew Besanko

Value Added Tax and Digital Tax Transformation

m.besanko@pwc.com

Asif Joosub

Customs & International Trade

asif.joosub@pwc.com

Tax and Legal services leadership team

Andreas Horak

Reward

andreas.horak@pwc.com

Osman Mollagee

Co-Lead Transfer Pricing

osman.mollagee@pwc.com

Michael Butler

Co-Lead Transfer Pricing

michael.butler@pwc.com

Ian Olls

Centre of Excellence and PwC Private

ian.olls@pwc.com

Karen Govender

Global Compliance Services

karen.govender@pwc.com

Tapie Marlie

Audit of Tax

tapie.marlie@pwc.com

Laetitia Le Roux

EU&R Consulting and Tax Reporting & Governance

laetitia.le.roux@pwc.com

Frank Mosupa

Deals and Employment Tax

frank.mosupa@pwc.com

Jos Smit

Financial Services Consulting

jos.smit@pwc.com

Kyle Mandy

Tax Technical, Training & Solutions

kyle.mandy@pwc.com

William Eastwood

International Tax Services

william.eastwood@pwc.com

Sibongile Solombela

Corporate Commercial & NewLaw

sibongile.solombela@pwc.com

Elle-Sarah Rossato

Tax Controversy & Dispute Resolution

elle-sarah.rossato@pwc.com

Contact

Kyle Mandy
Tax Policy Leader, PwC
Office: +27 (0) 11 797 4977
Email: kyle.mandy@pwc.com

www.pwc.co.za

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