Tax Alert

15 September 2009

2009 Taxation Laws Amendment Bills

The Minister of Finance introduced the final Taxation Laws Amendment Bills (No's B-10 and B-11) before Parliament on 1 September 2009. We present herewith a summary of the main amendments proposed in these Amendment Bills.

Administration

Provisional Tax – 2nd Payment

A new two-tier model is introduced. For Tier One taxpayers (taxable income of R1m or less), the "basic amount" safe harbour is reintroduced and no penalty is charged if the estimate is not below the lesser of basic or 90% of the actual taxable income for the year (i.e. identical to the position before the 2008 changes). The penalty remains unchanged at 20%. However, the basic amount will now be automatically increased by 8% per year.

Tier two taxpayers will continue to be subject to the current regime (i.e. the 80%-rule, without the "basic" safe harbour). However, the 20% underestimate penalty will now have to be individually considered on a case-by-case basis by SARS (and manually applied at their discretion), as opposed to being automatic.

Objections: Pay-now-argue-later

As a default rule, the obligation to pay tax will not be suspended pending the outcome of an objection. (This is already the case for appeals). There is also some guidance on factors that SARS must take into account in considering a request for deferral of payment.

Compound interest

The Commissioner is authorised to prescribe that interest (on outstanding tax) will be calculated on a daily basis and compounded monthly. The Commissioner must however first announce the tax types to which (and dates from when) this authority will be invoked.

Environmental incentices

CERs (Certified Emission Reductions)

An exemption is introduced for the disposal of CERs derived from qualifying CDM (Clean Development Mechanism) projects. Only the CER-producers can claim the exemption, not secondary CER-traders.

CERs are expected to be zero-rated for VAT purposes where these are supplied to non-residents.

The exemption expires at the end of 2012 in line with the Kyoto Protocol, although CERs sold after that date will still be exempt if the relevant CDM projects are registered before the deadline.

PRICEWATERHOUSECOOPERS

Energy efficiency

A deduction will be allowed for the notional savings that result from energy efficiency initiatives. This recognises that the benefit of energy efficiency (i.e. cost savings) would otherwise be diminished by the tax on these savings. The allowance is based on a formula, and will expire in 2020.

Companies and dividends

Collective Investment Schemes (CISs)

Investors into CISs will now be taxed on a look-though basis, akin to beneficiaries of a trust. A CIS is to be renamed a PCISS (portfolio of a collective investment scheme in securities) and will no longer be treated as a 'company'. Several other definitional changes also result from these new measures.

However, where income is retained in the PCISS for more than 12 months, the income will be taxed in the PCISS, not the beneficiary. The likely tax rate is 40% (expected to be confirmed in the 2010 Budget Speech).

Dividend Tax ("DT")

Several amendments are being made to the initial version of the rules that was legislated in the 2008 Amendments.

Dividends from non-resident companies that are listed in SA will also be potentially subject to DT if the dividend is paid to a SA-resident.

The differing treatments of certificated and uncertificated shares is dispensed with, although the differing treatments of listed and unlisted shares are confirmed and streamlined. Exempt shareholders will have to certify their exemption status in advance of every dividend declaration (as opposed to once every three years).

The treatment of specie dividends is clarified. DT will be based on the market value of the assets distributed, and valuation-date rules have also been added.

Although dividends received by insurers remain exempt from DT, internal allocations by an insurer to its "individual policyholder fund" will be subject to DT.

Deemed dividends – Value Extraction Tax ("VET")

As opposed to including "deemed dividends" into the DT rules, a separate tax regime will be established –effectively to mirror DT. Perhaps the most critical difference from DT is that VET is a tax on the company, i.e. essentially similar to the current STC.

The list of "value extraction" events bear some resemblance to the current deemed dividend rules in s64C, most notably including loans.

New "dividend" definition

In addition to the exclusion for CTC (contributed tax capital), the definition now also specifically excludes capitalisation issues, share buy-backs by listed companies (but only if undertaken through the JSE), and redemptions of units by foreign unit trusts.

Dividend-stripping

In the context of the disposal of shares, pre-sale dividends received may be treated as income or as additional CGT proceeds. These anti-avoidance rules target scenarios where, in the 18 months before the share transfer, the incoming purchaser funds the payment of dividends (by the company) to the outgoing seller.

Capital expenditure

Conversion of Tele-communications Licences

Roll-over relief from CGT and recoupment taxation is allowed where an existing (restricted) licence is converted to the new-style (comprehensive) licence. The older licences were technology-specific (e.g. permitting only cellular but not fixed-line operations), whereas the new system promotes competitiveness by allowing comprehensive licences.

Cables, pipelines and trans-mission lines – right of use

Depreciation write-offs will now be permitted not only for the cost the actual assets, but also for the right to use such assets. This follows the development of high capacity submarine telecommunication cables on the coasts of Africa, and the increasing use of "indefeasible rights of use", as an alternative to actual ownership. This allowance applies to railway lines, cables, transmission lines and pipelines.

Improvements on state-owned land

Leasehold improvements undertaken on property owned by the Government may now be written off where the right-of-use is

at least 20 years. Since the State is tax-exempt, this amendment represents an exception to the general rule that the tenant is prohibited from taking the allowance if the property-owner is not taxed on the improvements.

Oil and Gas

The requirements for oil and gas companies are relaxed to allow for companies with mixed trades to qualify for incentives. Although the 10th Schedule benefits will continue to apply only to income from oil or gas production, the company as a whole will not be disqualified purely because it also earns other income (e.g. trading in oil or leasing).

Venture Capital Companies

The rules for VCCs have been revised. The restrictive approval requirements have been relaxed slightly, and the approval is now automatically presumed from the start (pending possible withdrawal after review) –as opposed to being withheld for 3 years pending possible future approval.

Employment

Travel Allowances

The ability to use deemed business km will be withdrawn from 2010, so that only actual business km supported by a logbook can be used. (The deemed cost tables will be retained.) Also, the PAYE inclusion rate for fixed travel allowances will be increased to 80% (from 60%).

Medical Expenditure

For the sake of administrative simplicity, the link between employer-contributions to medical aids and the employee's own medical deductions, will be revamped. There should be no net tax-cost effect. From 2010, employer-contributions will be taxed in full (as fringe benefits) but the corresponding deduction-rules will be amended accordingly –i.e. the extra deductions will cancel out the extra fringe benefit inclusion.

Post-retirement medical scheme contributions

Employers will be allowed to deduct the full lump sum payments made to cover future medical scheme contributions of retired employees. (This does not relate to current employees.) The payment may be made directly to the former employee, or for the acquisition of an insurance product that will cover the medical aid obligations.

RAF deductions

Retirement annuity fund contributions that are made by an employer, but taxed as a fringe benefit in the hands of the employee, will represent a deductible contribution for the employee.

Retirement Funds

Since retirement fund lump sums are subject to separate tax tables, they will now be excluded from the average tax rate benefit in the so-called "rating formula". The tables are also streamlined to reflect the pre-retirement exemption (R22,500) and post-retirement exemption (R300,000).

Retrenchment lump sums will benefit from the preferential retirement treatment, notwithstanding that they are technically pre-retirement withdrawals.

The treatment of the splitting of fund benefits upon divorce is further clarified.

The taxation of minor beneficiary benefits is restructured. Instead of exempting the initial lump sum payout and then taxing the subsequent pay-outs (to the minor beneficiaries), the initial lump sum will be taxed and the subsequent pay-outs will be fully exempt.

Learnership Allowances

The learnership allowance provisions are restructured to simplify and enhance the deductions for learnership allowances and to remove the recoupment provisions.

International

CFC Exemption Rulings

In the context of CFCs (controlled foreign companies), certain of the "rulings" provisions are deleted and replaced with 'outright' exemptions, i.e. taxpayers no longer need to first obtain SARS rulings before applying the exemption. These are the so-called:

'same-country-group' ruling –where the CFC uses the facilities of another group company in a foreign country; and

'high-taxed-income' ruling –where the CFC suffers a significant level of tax outside SA.

The specifics of the new rules are slightly different to the original rulings provisions, and are made retrospective so that most "pending" rulings are also covered.

Foreign SA-listed dividends

When the new DT regime comes into effect, dividends from foreign companies that are also listed in SA will be subject to differing tax treatments, depending on whether the shares are acquired on the SA stock exchange or offshore.

For shares listed on the SA stock exchange the dividends will be subject to DT but exempt from Normal Tax, whereas for shares acquired elsewhere the dividends will be exempt from DT but fully subject to Normal Tax.

Foreign 'loop' structures

'Loop' structures refer to positions where a SA investor holds an interest in a foreign entity, which in turn earns income from a SA-source (or dividends from a SA company). When the new DT regime comes into effect, the SA element of such foreign dividends will no longer be exempt from Normal Tax.

Other changes

Mining stock-piles and Trading stock

For mining operations, the meaning of trading stock is widened to include any items that are obtained through mining, even if they still require further processing (extraction, separation, etc.) before any saleable item is achieved. This would include, for example, ore stock-piles. However, the taxable inclusion is dependant on accounting rules, in that it can only apply to items that are treated as inventory under GAAP, and the accounting value also represents the minimum tax value.

CGT on Primary Residences

The primary residence exclusion is extended to automatically exempt disposals where the proceeds are less than R2million –subject to certain restrictions. The R1.5m exclusion will continue to operate for homes that are sold for more than R2m.

Homes that are currently owned in companies or trusts (where the occupants are in fact the shareholders or beneficiaries) may now be transferred tax-free to the shareholders or beneficiaries. This exemption covers CGT, as well as Transfer Duty and STC, and is subject to certain conditions (e.g. periods of residence). Transfers must be effected before the end of December 2011.

Recreational clubs

The full-exemption status of previously exempt clubs is extended to 30-Sep-10 (instead of 31-Mar-09), so the new partial-taxation regime is deferred until 1-Oct-10.

Whereas existing clubs were required to apply (for partial exempt status) by 31-Mar-09, the rules have been relaxed to allow for late applications and retrospective approval –as long as they were in any event complying with the requirements.

Estate Duty Abatement

The unused balance of a deceased person's 'abatement' (R3.5m) may be transferred to the surviving spouse –so upon the death of the second-dying spouse the abatement could be as high as R7m. However, the estate duty return of the first-dying spouse must have been retained by the surviving spouse.

VAT on Re-organisations

VAT relief in respect of the so-called corporate roll-over rules will only be available where a 'going concern' is transferred.

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