Anti-avoidance rules for Trusts: compliance obligations

6 February 2018

In brief

As advised in previous Tax Alerts, section 7C of the Income Tax Act, 1962 (Act No. 58 of 1962) ("the Act"), came into effect on 1 March 2017. Generally, the section applies in respect of any interest-free or low-interest loan provided to a trust by a person that is a related party (e.g. a founder or a beneficiary) in relation to the trust. The effect of the application of section 7C is that, effectively, the interest that is foregone by the person providing the loan to the trust is deemed to be a donation to the trust, which donation will attract donations tax.

The year of assessment ending on 28 February 2018 will generally be the first year of assessment in respect of which section 7C will deem donations to have been made. This Tax Alert serves to remind taxpayers of any compliance obligations that they might have in respect of this year of assessment.

In detail

In terms of section 7C, if a natural person lends money to a trust in the form of a loan, advance or credit and the trust incurs interest at a rate lower than the official rate of interest or incurs no interest at all, this will, for purposes of donations tax, result in a donation. The amount of the donation will be the difference between the amount of interest incurred in respect of the loan and the amount of interest that would have been incurred at the official rate of interest. Donations tax is levied at 20% of the value of the property donated.

This can be illustrated as follows:

The founder of a trust lends R1 000 000 to the trust on 1 March 2017 and charges no interest on the loan amount. The official rate of interest is 8%.

(1 000 000 x 8%) – (1 000 000 x 0%) = R80 000, which is treated as a donation for purposes of donations tax and taxed at the donations tax rate of 20%.

The calculation of the amount to be treated as a donation must be done annually as at the end of the year of assessment of the person that advanced the loan (for natural persons, this is generally the last day of February every year).

Relief is available in the form of the donations tax exemption (the first R100 000 of donations made every year is exempt from donations tax).

It is possible that the South African Revenue Service ("SARS") will issue new ITR12T returns that provide for section 7C. However, this has neither been confirmed nor communicated by SARS.

Donations tax must be paid by the end of the month following the month during which the donation takes effect. This means that, where section 7C applies to treat an amount as having been donated, the donations tax incurred as a result must generally be paid by the end of March.

As regards, compliance steps that must be taken once the donation is deemed to have been made on the last day of February, an IT144 (Declaration by Donor/Donee) must be completed and submitted at a SARS branch, together with proof of payment. Payments may be made *via* SARS' eFiling platform.

It must be noted that extensions are not

automatically granted, and a taxpayer must make a request for an extension, which SARS will assess on a case-by-case basis.

Takeaway

This year, any donations tax arising as a result of the application of section 7C must be paid by 31 March 2018. It is unlikely that SARS will grant any extension for payment. Consequently, taxpayers should start preparing for their section 7C donations tax declarations now.

Where you believe that there could be complexities in accounting for donations tax payable as a result of the application of section 7C, it is advisable to approach SARS and request an extension before the 28 February 2018 in order to avoid possible penalties.

It must also be ensured that, for accounting purposes, such loans are correctly disclosed in the annual financial statements.

Let's talk

For a deeper discussion of how this issue might affect your business, please contact:

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