2022 Budget Review Highlights

Reform to grow

Major Tax Announcements

Tax revenue

As predicted, tax revenues are expected to be well above the projections at R1.55 trillion (largely attributable to elevated commodity prices). There will be no significant tax increases and neither the general fuel levy nor the Road Accident Fund levy will be increased. This is welcomed and will support the economic recovery.

Kyle Mandy, Head of Tax Policy, PwC

Tax collections in the mining industry

The R1.55 trillion projection is R62 billion higher than the estimates from four months ago, and R182 billion higher than the estimates from last year's budget. This has come mainly from the mining sector due to higher commodity prices.

The expected increase in the collection of mineral and petroleum royalties in respect of 2021/2022 is further evidence of the improved profitability of mining companies. In the 2021 Budget Review estimates, the budget estimate for mineral and petroleum royalties was R15 937 million, whereas the revised budget estimate in the 2021/2022 Budget Review amounts to R27 979 million. It is also worth noting that the revised budget estimate for 2021/2022 is a 96.6% increase from the mineral and petroleum royalties revenue outcome of 2020/2021.

Laetitia Le Roux, Energy, Utilities and Resources Tax Partner

Personal Income Tax

The Minister of Finance announced in the Budget Review that there would be an inflation adjustment to the individual tax brackets and rebates.

The net result is that, with effect from 1 March 2023, the maximum rate of 45% applies to taxable income more than R1,731,600 (up from R1,656,600) while the lowest rate of 18% applies to taxable income up to R226,000 (up from R216,200) with similar adjustments to the brackets in between. There will also be an approximate 4.5% increase in the primary, secondary, and tertiary rebates. The tax-free threshold has now increased from R87,300 to R91,250 for taxpayers under 65 years of age.

It was expected that the medical tax credit available to taxpayers, who are members of medical aid schemes, would be adjusted. They have been increased from R332 to R347 per month for each of the first two dependents and from R224 to R234 per month for every subsequent dependent.

In an attempt to assist in addressing youth unemployment, National Treasury has announced an increase in the maximum employment tax incentive that can be claimed for qualifying employees from R1,000 to R1,500 for the first 12-month period and from a maximum of R500 to R750 for the second 12-month period with effect from 1 March 2022.

National Treasury has confirmed that it will continue to look into changes to the taxing of retirement fund lump sums when a taxpayer ceases to be a tax resident. However, this will require the re-negotiation of several double tax agreements which they intend to commence within the coming year. National Treasury will also continue to look into instituting a two-pot system for the preservation of retirement benefits. It is disappointing to note that no mention was made about adjustments for expenses incurred by employees working from home.

It was also announced that, with effect from 2023, provisional taxpayers with business interests who have personal assets over R50 million will be required to make more detailed disclosure in their tax returns of certain of their personal assets and liabilities. These will need to be disclosed to SARS at market value rather than at cost.

Barry Knoetze, Associate Director

Corporate Tax (Business general)

Restructuring of corporate income tax and reduction in the corporate income tax rate

As announced in the 2020 Budget Review, the government intends to restructure the corporate income tax system. In this regard, the headline tax rate for companies will be reduced to 27%, effective for tax years ending on or after 31 March 2023. The reduction in tax rate is aimed at making South Africa a more competitive investment destination to support economic growth.

To ensure that the rate reduction does not reduce tax revenue, it will be accompanied by other tax base-broadening measures, which will also become effective from the same date. The base-broadening measures include limitations on the utilization of assessed losses and interest expense deductions. More specifically, it is proposed that companies (excluding certain smaller companies) with assessed losses will only be entitled to set off a maximum of 80% of their assessed tax losses against their taxable income in a specific year. This proposal should not necessarily result in additional tax but would impact the timing of tax payments by companies with assessed losses. Additionally, the existing rules on the limitation of interest deductions are proposed to be broadened to be better aligned with the OECD / G20 recommendations on base erosion and profit shifting to ensure tax revenue neutrality with the above restructure of the corporate income tax system.

Proposals for clarification and refining of 2021 amendments to Contributed Tax Capital ("CTC")

As part of the 2021 legislative process, an amendment was proposed to the CTC definition to combat certain anti-avoidance concerns. Given the potential impact of this amendment on legitimate restructuring transactions, its effective date has been postponed to 2023 and will be further assessed as part of the 2022 legislative cycle. Hopefully, the potential issues will be addressed by this further review.

Lay-bys

The government proposes to review the debtor's allowance rules to limit the adverse effect of the current legislation on lay-by arrangements.

Angus du Preez, Partner

Corporate Tax (Business incentives)

Tax treatment of mining operations – Interaction between the application of the assessed loss restriction rules and capital expenditure regime for mining operations.

The introduction of the new assessed loss restriction rules and the interaction thereof with the current capital expenditure regime applicable to mining operations in terms of section 36 of the Income Tax Act results in an anomaly, i.e., circular reasoning, in determining taxable income and the limitation thereon.

Government proposes that the legislation be clarified to ensure that the assessed loss restriction in terms of section 20 of the Income Tax Act is calculated before taking into account the capital expenditure deduction for mining operations in terms of section 36 of the Income Tax Act.

There is, however, no mention made as to how the limitations will need to be applied in terms of the ring-fencing principles contained in section 36 of the Income Tax Act, i.e., should the limitation be applied per mine (ring-fence) or at a taxpayer level.

Once the proposed tax law amendments are available for comment, careful consideration will have to be given to all the different ring-fencing permutations that may be applicable.

Laetitia Le Roux, Energy, Utilities and Resources Tax Partner

Tax treatment of mining operations – Interaction between the application of the interest limitation rules and capital expenditure regime for mining operations

In strengthening the rules dealing with the limitation of interest deductions on debts owed to persons not subject to tax, certain changes were made in section 23M of the Income Tax Act. The question arose as to how these amendments will interact with the current capital expenditure regime applicable to mining operations in terms of section 36 of the Income Tax Act. The poignant question is, does section 23M apply in respect of the interest expense of non-producing mining operations where the interest is deemed to form part of the capital expenditure of such mining operations?

Government proposes clarifying the legislation so that the interest limitation rules in section 23M will not be applied to the interest expense of non-producing mining operations that forms part of capital expenditure of such mining operations in terms of section 36 of the Income Tax Act.

Laetitia Le Roux, Energy, Utilities and Resources Tax Partner

Tax treatment of an asset acquired as government grant in kind

It is proposed that the tax treatment of assets acquired in the form of certain government grants be aligned with assets acquired from funding received through cash grants listed in the Eleventh Schedule i.e., the tax allowance will be limited by the amount of the grant received. There may however be a window of opportunity for assets received through grants not listed in the Eleventh Schedule.

Tapie Marlie, Audit of Tax and Incentives, Tax Partner

Research and development tax incentive to be extended

Although an extension of the research and development allowances for qualifying expenditure incurred until 31 December 2023 is welcomed, a longer extension period was envisaged to further encourage innovation and technological developments. A further extension will hopefully be granted following the workshops with National Treasury.

Tapie Marlie, Audit of Tax and Incentives, Tax Partner

Energy-efficiency-savings tax incentive to be extended

As part of the transitional support measures afforded as part of the carbon tax implementation, the energy-efficiency-savings tax incentive in section 12L will be extended from January 2023 to 31 December 2025.

Expiry of corporate tax incentives

Various other incentives that reach their sunset dates on 28 February 2022 (and 31 December 2021) will not be reviewed. These include Section 12DA (rolling stock), Section 12F (airport and port assets), Section 12O (films), Section 13sept (sale of low-cost residential units through an interest-free loan). The reluctance to extend the section 12(O) film allowance together with the recent tightening of cash grants on local and foreign films is bound to have a big impact on the local film industry.

A glaring omission is the further incentivization of renewable energy to help alleviate the energy crisis that the country is facing.

Tapie Marlie, Audit of Tax and Incentives, Tax Partner

Corporate Tax (Financial Services)

Impact of IFRS17 insurance contracts on the taxation of insurers

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

From a tax perspective, both life insurers (as catered for in section 29A of the Act) and non-life insurers (as catered for in section 28 of the Act) will be impacted.

For life insurers, the current tax legislation requires that the life insurer pay tax at the end of each year of assessment on underwriting profits which generally equate to the amounts by which the market value of assets exceed the value of liabilities in each of the policyholder and risk funds. The value of liabilities is calculated as the insurance contract liabilities under IFRS 4 but subject to specific adjustments catered for under section 29A of the Act. Non-life insurers will be equally impacted as the current tax basis allows non-life insurers to deduct IFRS insurance contract liabilities relating to premiums and claims.

IFRS 17 will significantly impact the measurement of insurance contract liabilities which will correspondingly impact the taxable profits of life and non-life insurers. In this regard, National Treasury must engage with the life and non-life insurers, as well as the representative industry bodies, to carefully assess the tax impact this will have on the insurance industry.

IFRS 17 also introduces new terminologies dealing with the classification and measurement of revenue and expenses which are not currently catered for in the Act. Therefore, tax amendments may also be required to ensure that the new terminologies are incorporated into the Act.

Stephen Boakye, Associate Director, Financial Services Tax & Jos Smit, Partner, Financial Services Tax

Tax treatment of amounts received by or accrued to portfolios of collective investment schemes (CIS)

In 2018, National Treasury proposed amendments to the tax legislation to clarify and provide certainty on the tax treatment for trading profits of a collective investment scheme (CIS). National Treasury raised concerns regarding the level of trading by some CIS portfolios and suggested that profits from certain transactions be treated as income (or revenue in nature) rather than capital. Industry bodies then engaged with National Treasury on the impact the proposal could have on the CIS industry, as well as the savings culture, following which National Treasury withdrew the proposed amendments.

The government has now proposed that a further discussion document dealing with the tax treatment of amounts received by or accrued to a CIS be published for public comments before the enactment of any amendment. In this regard, we welcome the National Treasury's approach of prior engagement with industry.

Stephen Boakye, Associate Director, Financial Services Tax & Jos Smit, Partner, Financial Services Tax

Updating the definitions and terms relating to the Insurance Act in the determination of net income of controlled foreign companies

In broad terms, where a resident shareholder has an interest in the participation rights of a controlled foreign company (CFC), an amount of the CFC's net income is required to be imputed into the taxable income of the shareholder (subject to certain exclusions).

One of the exclusions relates to the participation rights which can be directly attributable to a linked policy or directly attributed to a policy where the amount of the policy benefit is not guaranteed by the insurer but rather determined entirely by reference to the value of particular underlying assets. The new Insurance Act came into effect on 1 July 2018 and changed, among others, the definition of a linked policy. It is proposed that this exclusion be amended to refer to the appropriate provisions of the Insurance Act.

Stephen Boakye, Associate Director, Financial Services Tax & Jos Smit, Partner, Financial Services Tax

International Tax

Similar to the previous year, no major reforms have been announced. The amendments seem to target the controlled foreign company (CFC) rules contained in section 9D.

The CFC rules have now been extended to deem a CFC to be a resident for the purposes of section 10(1)(l). This closes a loophole that was used to prevent royalties from being imputed in terms of the so-called 'diversionary rules'.

Further amendments have been proposed to account for a situation where amounts from hybrid equity instruments are deemed to be income and whether the inter-CFC exemption would still apply in such a situation. The key concern is to remove inequitable treatment for both the payor and payee, which does not give rise to the tax neutral treatment that the inter-CFC exemption was designed to achieve.

Lastly, the exclusion from the foreign dividend definition for the redemption of a participatory interest in a foreign portfolio of collective investment scheme will be widened to also include the sale of a participatory interest in a foreign collective investment scheme's portfolio.

Raagesh Singh, Associate Director, International Tax Services

Base erosion, profit shifting and digital services taxation

South Africa is a member of the Steering Group of the OECD/G20 Inclusive Framework tasked with finding consensus-based solutions to tax challenges associated with digitalisation of the economy. In October 2021, the Inclusive Framework agreed on a two-pillar solution and will work on an implementation framework to take effect by 2023.

Following developments worldwide and corresponding measures being taken by the Inclusive Framework countries, the budget announces legislative amendments to implement these rules in South Africa, once the framework has been finalised and translated into a local context.

Archi Ramana, Associate Director, Transfer Pricing

Mining and Oil & Gas

Upstream petroleum tax regime

A review of the tax regime for the upstream petroleum industry, published at the end of 2021, proposed replacing the variable royalty rate with a flat-rate royalty of 5 per cent. National Treasury indicated that public comments have been received, including some expressing concerns about this approach. A workshop will be held to engage on the various issues so that a proposal can be included in the 2022 Taxation Laws Amendment Bill.

Laetitia Le Roux, Energy, Utilities and Resources Tax Partner

Exchange Control (Capital Flow Management Framework)

The new capital flow management system ("CFM system") was introduced in the 2020 Budget Review, with the objective to allow all foreign-currency transactions, except for a specific risk-based list of capital flow measures. The Minister stated that this change will increase transparency, reduce burdensome and unnecessary administrative approvals and promote certainty.

There was slow progress on the development and implementation of the CFM system during 2020 and in Budget 2021, it was confirmed that National Treasury and the Reserve Bank will continue to develop the legislative framework for the CFM system with the expectation that the system should be substantially completed during the year.

During the course of 2021, we did not see much activity in this regard but a number of proposals have now been announced for the year ahead in keeping with the gradual relaxation of exchange controls which is proceeding further. These include:

Individuals

- The export of dual-listed domestic securities to a recognised foreign share exchange is permitted and limited to the exchange control allowance amounts.
- Resident individuals may receive and retain gifts from non-residents and may use their single discretionary allowance to participate in online foreign-exchange trading activities but may not use credit or debit cards to do so.
- Residents may in the future lend or dispose of authorised foreign assets held offshore to other South African residents, subject to local tax disclosure and compliance.
- South African residents may transfer, for foreign investment purposes, authorised capital of more than R10 million per year through offshore trusts, subject to the current tax application and reporting requirements.
- Authorised dealers may, on a once- of basis, remit abroad the remaining cash balances (of up to R100 000 in total) of people who have ceased to be residents for tax purposes, without reference to SARS.

Companies and Institutional investors

- After a lengthy process, it has been decided that all debt securities referencing foreign assets listed on a South African stock exchange remain classified as foreign.
- The offshore limit for all insurance, retirement, and savings funds is harmonised at 45% inclusive of the 10% African allowance. The previous maximum limits were set at 30% or 40% for different investors.
- Institutional investors may open foreign-currency accounts with authorised dealers for funding and to accept foreign-currency deposits from disinvestment proceeds of foreign assets, pending the reinvestment of the funds offshore.
- The foreign direct investment limit for companies investing funds offshore will increase from R1 billion to R5 billion.
- Excess income or profits of offshore branches and offices of South African firms may be retained offshore, subject to annual reporting.
- Authorised dealers may process transfers from the parent company to the domestic treasury management companies up to a maximum of R5 billion (an increase from R3 billion) per calendar year for listed entities; and up to R3 billion (an increase from R2 billion) per calendar year for unlisted entities. Funds transferred under this dispensation may be used for new investments, expansions as well as other transactions of a capital nature.

In addition, crypto asset transactions will be considered going forward.

Michael Butler, International Tax Partner

Value-Added Tax

As was widely expected, the government did not announce an increase in the VAT rate, although the Minister has stated that the tax rate will need to increase in the future. The proposed amendments affecting VAT are largely technical in nature.

Reviewing section 72 arrangements and decisions

In 2019, changes were made to section 72 of the VAT Act to limit the Commissioner's discretion to make arrangements or decisions to overcome difficulties, anomalies, or incongruities regarding the application of the Act. These limitations affected the arrangements or decisions made by SARS on or before 21 July 2019.

During the past two years, SARS and National Treasury reviewed the impact of those arrangements or decisions. As a consequence, certain changes to the VAT Act were implemented. These changes were, however, not sufficient to address all of the valid difficulties, anomalies or incongruities.

In light of this, National Treasury has proposed that further changes be made to the VAT Act. However, this proposal is vague and does not specify the areas that will be addressed. This creates uncertainty for taxpayers as there were many proposals of this nature made by the public.

Updating the regulations prescribing electronic services

With effect from 1 April 2019, the regulations prescribing electronic services were amended to broaden the scope of electronic services that are subject to South African VAT, in line with the OECD Action 1 Report.

The regulations will be reviewed to cater for further developments in this area.

Once-off supply of electronic services

An exception to registering as a VAT vendor in South Africa is where a once-off supply exceeding R1 million is made by a resident supplier. It is proposed this exception be extended to non-resident suppliers who make a once-off supply of electronic services to a recipient in South Africa.

This will prevent unnecessary VAT registrations, limit costs and the administrative burden for both non-resident suppliers and SARS.

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Customs and excise

While surprisingly the government did not increase the Road Accident Fund levy or the fuel levy, largely due to concerns around the affordability of petrol and diesel as prices now exceed R20/l, it is notable that the government does propose above-inflation increases in alcohol and tobacco excise duties.

Customs

As there are currently no provisions in the Customs and Excise Act enabling the SARS to issue advance rulings. It is proposed that an enabling framework for advance rulings be enacted.

As there is no prescribed period in the Customs and Excise Act within which an entry for loose or breakbulk cargo imported by rail, air, or sea should be made, the government proposes making rules for the entry time of any category of goods, which may include break-bulk cargo imported by sea, air or rail.

Due to existing uncertainty, amendments will be made to the Customs and Excise Act to clarify the legislative requirements for invoices in respect of import and export goods.

Excise

Fuel levies

No increases in the Road Accident Fund levy, fuel levy, and excise are proposed due to concerns around affordability as the fuel price breaches R20/l for the first time.

The targeted excise tax burden for wine, beer, spirits, and tobacco products will increase as follows:

Alcoholic beverages

The rate of excise duty on traditional African beer remains the same. However, the rate on other alcoholic products will increase between 4.5 and 6.5 percent for 2022 / 2023.

Traditional African beer powder currently attracts a flat excise rate of 34.7c/kg. As there are now also similar products in the market, in the interest of equity, these products will be included in the tax net with an excise equivalent to the powder rate from 1 October 2022.

Tobacco products

The government notes that the consumption of cigars has moved towards more expensive brands, requiring a higher than inflation increase to maintain the tax burden. The increase in excise duty will be between 5.5 and 6.5 percent.

Further, review papers on the alcohol and tobacco industry in relation to the excise duty policy framework will be released shortly for comment.

Health promotion levy (sugar tax)

The health promotion levy for beverages containing more than 4g of sugar content per 100ml will be increased from 2.21c/g to 2.31c/g from 1 April 2022.

Taxation of electronic nicotine and non-nicotine systems

The National Treasury published a discussion paper in December 2021 discussing the potential taxation of electronic nicotine and non-nicotine systems. This activity involving these systems is commonly known as vaping. There are concerns regarding vaping's potential to undermine global tobacco control efforts, and public health in general, considering that these products are not harmless (contrary to popular belief).

Following public consultation, the government proposes to apply a flat excise duty rate of at least R2.90/ml to both nicotine and non-nicotine solutions. The proposal will be included in the 2022 Taxation Laws Amendment Bill for further consultation before being introduced from 1 January 2023.

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Environmental taxes

The government continues to focus on environmental taxes as it aims to achieve its commitments made in terms of the UN Climate Change Conference (Paris Climate Change Agreement). We expect that environmental taxes will increasingly become a more significant contributor to national revenues in the future.

Carbon tax

- The carbon tax rate for the 2022 carbon tax year (i.e. from 1 January 2022) will increase from R134 per tonne of carbon dioxide equivalent to R144 per tonne of carbon dioxide equivalent. This increase is in line with the expected increase as per section 5 of the Carbon Tax Act.
- The carbon fuel levy for 2022 will increase by 1c. This means that consumers will pay a carbon fuel levy of 9c/l for petrol and 10c/l for diesel from 6 April 2022.

Phase 1 of carbon tax

- Phase 1 of the carbon tax will be extended by three years to 31 December 2025. Significant tax-free allowances and revenue-recycling measures (as is currently the case) will continue over this period.
- The anticipated mandatory carbon budgeting system will come into effect on 1 January 2023. National Treasury proposes that a higher carbon tax rate of R640 per tonne of carbon dioxide equivalent will apply to greenhouse gas emissions exceeding the carbon budget.
- Other related proposals include the adjustment of the trade exposure allowance threshold, a three-year extension of the energy efficiency savings tax incentive, and an extension of the electricity price neutrality commitment.
- Changes to section 6(2) of the Carbon Tax Act will be made to clarify the electricity generation levy and renewables deduction for electricity generation.

Climate change response and carbon tax price path

- It is proposed that the carbon tax rate will progressively increase every year by at least approximately R15 to reach approximately R300 per t/CO2e by 2026.
- It is also proposed that the basic tax-free allowances will gradually reduce from the start of Phase 2 (i.e. 1 January 2026), and the carbon offset allowance will increase by 5% to encourage investment in carbon offset projects

Other environmental taxes and levies

An inflationary increase will be applied to the plastic bag levy from 25c/bag to 28c/bag from 1 April 2022 to further discourage consumers from buying plastic bags, and to support reuse and recycling.

The government has also announced that it will investigate an upstream plastic tax and tax on single-use plastics in line with global trends.

With regards to motor vehicle emissions, it has been proposed to increase the vehicle emissions tax rate on passenger cars from R120/gCO2/km to R132/gCO2/km and increase the tax on double cabs from R160/gCO2/km to R176/gCO2/km from 1 April 2022.

Lastly, the incandescent light bulb levy will be increased from R10 to R15 per light bulb from 1 April 2022.

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