

Synopsis

Tax today

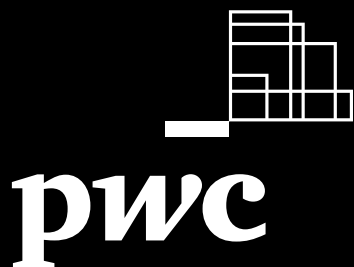
July 2019

A monthly journal, published by PwC South Africa, that gives informed commentary on current developments in the tax arena, both locally and internationally.

Through analysis of and comment on new laws and judicial decisions of interest, Synopsis helps executives to identify developments and trends in tax law and revenue practice that may affect their business.

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Proposed amendments to the CFC rules

On 21 July 2019, National Treasury published the Draft Taxation Laws Amendment Bill ('DTLAB') for public comment. This DTLAB contains a number of proposed tax amendments, including proposed amendments to our 'controlled foreign company' ('CFC') rules.

The proposed amendments to the CFC rules come as no surprise, as these were already announced by the Finance Minister during his Budget Speech delivered on 20 February 2019. They seek to reduce the high tax exemption ('HTE') threshold and to strengthen the anti-diversionary rules.



Background

The SA Income Tax Act ('ITA') contains anti-avoidance rules which are specifically designed to prevent income from being shifted from SA to foreign companies which are controlled by SA residents. These rules are commonly referred to as controlled foreign company CFC rules and are found in section 9D of the ITA.

A CFC is defined as either any foreign company in which more than 50% of the participation rights (or voting rights) are directly or indirectly held (or exercisable) by SA residents, or a foreign company whose financial results are reflected in the consolidated financial statements of any SA-resident company. The DTLAB includes a proposed amendment to clarify that the latter part of the definition does not apply to a headquarter company.

Section 9D provides for the net income of the CFC to be included in the SA resident's income in proportion to that resident's participation rights (or voting rights) in that CFC, subject to a number of exemptions.

Proposed amendment to the HTE threshold

Currently, the net income of a CFC is deemed to be nil where *inter alia* the aggregate amount of foreign tax on income

payable by that CFC to any foreign revenue authority is at least 75% of that CFC's notional SA tax (i.e., the so-called high tax exemption).

The mere application of the HTE implies that the SA tax which would have been due on the foreign business profits of a CFC would either have been very little or nil. It is for this reason that the HTE is intended to ease the compliance burden for SA multinationals by exempting the foreign business profits of its CFCs and therefore eliminating the need for the SA multinationals to claim tax credits in SA in respect of the foreign taxes levied on those foreign business profits.

Given the global trend towards lower corporate tax rates, it is proposed that the HTE exemption threshold be reduced from 75% to 67.5%. This means that the high tax exemption will now apply where the CFC's effective foreign tax on income is 18.9% (or higher) assuming that this income is calculated similarly to the notional SA income.

This decision by National Treasury to amend the HTE threshold also suggests that SA's CIT rate can be expected to remain unchanged at 28% in the immediate future, which is consistent with the recommendations of the Davis Tax Committee.

Proposed amendment to the anti-diversionary rules

With SA's relatively high CIT rate, National Treasury is likely to remain concerned that taxpayers may be engaging in schemes devised to divert income from SA to low tax jurisdictions, particularly through the sale of goods and services.

National Treasury has been clear that its preferred mechanism of countering these schemes is through anti-diversionary rules.

As a general matter, the anti-diversionary rules are relevant to CFCs which seek to rely on the foreign business establishment ('FBE') exemption.

Briefly, the FBE exemption has the effect of excluding from net income all the CFC's receipts and accruals attributable solely to its FBE. However, this is on condition that such receipts and accruals do not fall within the categories of potentially diversionary income described in section 9D(9A).

Currently, there are three sets of anti-diversionary rules in relation to actual goods and services, namely, CFC inbound sales, CFC outbound sales and CFC inbound services.

The proposed amendments, which are aimed at all three sets of these rules, are intended to address National Treasury's latest concern, which is multi-layered structures aimed at circumventing the current anti-diversionary rules. These structures typically entail the imposition of additional CFC(s) in the supply chain

such that the link between the SA-resident connected person and the independent non-resident supplier or customer is broken, resulting in the non-application of the anti-diversionary rules.

To illustrate this point, take for example a SA-resident company that imports raw materials for processing. If the goods are initially procured by a CFC and then on-sold to the resident, they are currently hit by the existing anti-diversionary rule which denies exemption for the supply of goods by a CFC to a SA-resident connected person. If, however, a multi-layer arrangement exists, in which CFC1 procures and sells to CFC2 which, in turn, sells to the SA resident, only CFC2's profits would be caught. The margin retained by CFC1 would not be subject to the existing anti-diversionary rules because it sold the goods to another CFC (not to an SA-resident connected person). However, CFC2's sales to CFC1 would arguably be caught if the rules are extended to include goods sold 'indirectly' (by CFC2) to the SA-resident connected person.

In an effort to strengthen the anti-diversionary rules to deal with such multi-layered structures, it is proposed that the current anti-diversionary rules be extended to include both direct and indirect transactions between:

- a. an SA-resident connected person and a CFC for the export of goods from SA;
- b. a CFC and an SA-resident connected person for the import of goods; and
- c. a CFC and an SA-resident connected person for rendering of services (by that CFC to the SA-resident).

The takeaway

Some commentators argue that this proposal is in direct (or indirect) response to the recent *SASOL* case (see November-December Synopsis issue) where the taxpayer had a multi-layered procurement structure. SARS attempted to include the net income of a CFC that appeared to be indirectly selling to an SA-resident connected person, but the Supreme Court of Appeal found in favour of the taxpayer. It is noteworthy that the *SASOL* case centred on SA's general anti-avoidance rules – and thus was critically dependent on the taxpayer's motive – whereas the new amendment proposal does not include any motive test. Equally important is that the extended reach of these rules does not suggest any grandfathering for pre-existing structures.

The public has until 23 August 2019 to submit its comments and recommendations on the DTLAB to National Treasury.

Subject to the outcome of the public consultations, the proposed amendments will come into effect and apply in respect of the years of assessment ending on 1 January 2020.



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The Tax Director series: Article 7

Change is happening – as responsible taxpayers, organisations need to level up to be fit for the future.

Transform* tax through automation (Part 1)

‘Digital’ is not just about the technologies. It’s about new ways of solving problems, creating unique experiences and accelerating business performance.

Digital trust

The business trust equation has a new variable: digital trust. Governing boards are called upon to update the organisation’s processes, and to rethink its role as an enabler of change. Digital technology eases the access to information. Information that’s accurate, timely and secure strengthens how much internal and external stakeholders trust the business. A serious commitment to data governance makes board members true guardians of data. It’s clear that ‘digital’ is having a

dramatic impact on all businesses today. The trend is only going to accelerate as companies look for efficiencies and different channels to reach the tech-enabled generation.¹

In this connected era, tax needs to consider innovative ways to become a digital leader in collecting and processing financial data. It needs to move away from manual manipulation and reconciliation to more forward-thinking analytics and real-time decision-making by finding innovative ways to collect and analyse data.

¹ PwC, Five reasons the management board needs a digital mindset (2019)

Core processes and routine activities can have a significant and lasting impact on the tax function. As tax laws and accounting standards continue to evolve, tax is challenged to look closely at how data and related documents are received, processed, and ultimately retained, while continuing to add value through strategic decision-making, planning, forecasting, increased efficiency, improved processes, risk management and transparent reporting.

While companies largely understand the importance of creating strategies around technology and pursuing related initiatives aimed at increased automation, better-integrated data and more analytic capabilities, most have yet to make appropriate investments in these areas. These investments play an integral role in transforming tax into a strategic business partner within the organisation and often lead to a reduction in the cost of delivery and sustained bottom-line improvements, while simultaneously reducing tax risk to the organisation. As such, tax leadership should engage with company leadership and commit to the next steps in the evolution of its tax function.

Scrutiny over tax positions taken will only increase. Are you comfortable that data related to your business’s position

on tax, tax numbers, key performance indicators, and economic contributions to the governments, per jurisdiction, is not just accessible, but reliable and understandable?

A tax technology strategy enables alignment with the organisation’s business objectives, tax strategy, and enterprise technology investments and should focus on five dimensions of data:

- Breath of information;
- Depth of information;
- Integration of data;
- Tax management practices; and
- Quality of data.

PwC’s five key automation success factors:

1. Understanding the business process and pain points
2. Putting people and culture at the heart of the strategy
3. Ensuring sustainability through robust governance
4. Evolving the technology ecosystem to meet goals
5. Measuring business returns beyond financial return on investment (ROI)

Achieving success by going smart, fast, and small

In part one of ‘Transform* tax through automation’ we discussed how small automation² (that is in addition to ‘big enterprise automation’) can help tax become a better strategic partner within the wider organisation.

Why should your company invest in small automation now?

Small automation allows organisations to respond to the demand for quality data and technology-enabled processes, but in a more measured and controlled manner. Looking at processes within the tax function, it achieves this via fast implementation of flexible and adaptable technologies not easily accomplished by enterprise systems. The critical benefit here is that tax functions, with relatively small consulting budgets, time restrictions, and limited IT support, can generate targeted quick ‘wins’ that in series can transform the function and bring to scale the automation discussion for larger enterprise-wide consumption and buy-in.

Successful deployment of new self-service tools can support a more flexible and directional technology roadmap to move towards a strategic, long-term vision for the tax function. We have seen tax functions methodically deploy these new tools to automate processes end-to-end in a matter of weeks. A governance model is established to manage the automation programme from implementation to

scale-out, and adoption then continues to manage maintenance.

While other emerging technologies, such as advanced machine learning and natural language processing, are being applied to tax functions in expanded-use cases, there are three types of self-service automation solutions driving small automation in tax today:

- Extract, transform, and load (ETL) – used to integrate, manipulate and perform simple to very complex transformation of data from disparate sources;
- Robotics – coded software to perform rule-based processes which mimic the interactions of users; and
- Analytics and data visualisation (e.g., dynamic/interactive dashboard displays).

These tools require minimal technology to develop code (i.e., low or no code) and allow for flexibility and autonomy for the end tax users to maintain. The functionality provided by these tools in combination allows for end-to-end automation of many disparate tax processes. Understanding the integration of these tools and how they connect various tax processes is key to success.

There is more than one bottom line for small automation

When developing the business case for change, and subsequently measuring success, stakeholders will undoubtedly want to have a clearly articulated value proposition for investing in automation.

Stakeholders need to know that automation drives benefits that resonate with larger enterprise-wide goals. As you consider your own small automation journey and scaling the impact beyond the tax function, what is top of mind for the C-suite should be built into the proposition for automation now. You should also consider all angles when developing the value proposition beyond obvious financial metrics to include benefits which address critical aspects of operating in today’s dynamic global business environment. Consider important benefits such as improved quality, better-managed risk, and a higher level of employee engagement and retention, that have a trickledown effect on the financial metrics of the organisation.

Initial deployment of small automation

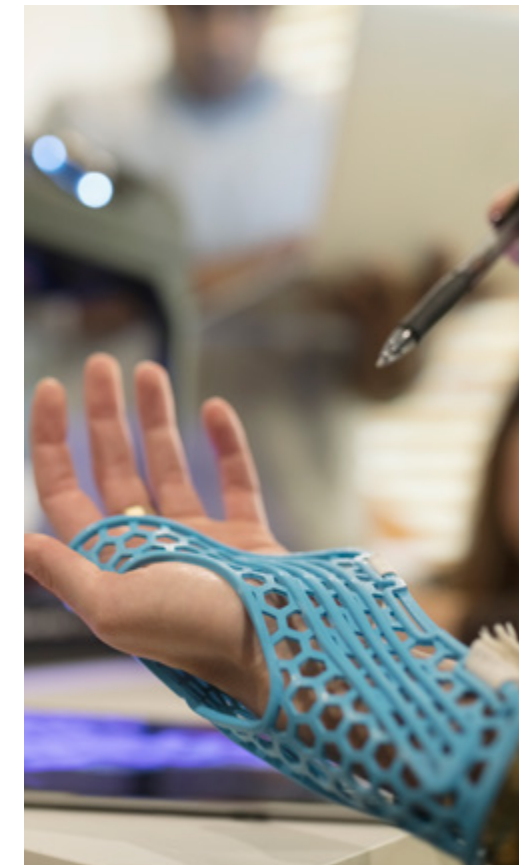
Upon introduction of small automation, teams will be trained on the use of the automation tools. Teams gain hands-on experience with the application and identify ways to automate their day-to-day tasks. Initial use cases are implemented, and quick wins are achieved with select stakeholder participants, and often leverage external support to augment internal capabilities.

Scaling of small automation

More teams become on-boarded to the automation tools as initial success stories are recognised. Internal capabilities develop and automation deployment starts to become more efficient. Applications are shared in server/cloud for scaling and coordination.

Establishment of centre of excellence (COE)

A governance model is formalised and managed by cross-functional COE. The COE defines process intake methodology and workflow priority, documentation protocols, and supports planning and deployment of automation projects. Internal capabilities allow companies to execute with limited external support. The COE continues to explore and innovate with new emerging technologies.



² Automation for tax – You can have your cake and eat it too! PwC (2018)

Measuring the elusive 'ROI' question

It is also important to note that ROI for automation will change as you progress on your automation journey. It likely will not be the same at implementation as it will be at scaling, as advances in automation begin to take hold in your organisation. Related variables will adjust.

- Time and cost associated with training employees will decrease as initial users develop necessary skills.
- Costs to execute small automation projects decrease as internal capabilities expand, streamlined implementation methodologies and best practices are refined, and synergies across projects are developed.
- Risks with implementation will decrease as you develop best practices and a vetted governance structure to rely on for future implementation/scaling.
- Quality of work will increase.
- Strategic decision-making will be better supported, as the time to manipulate data will decrease.
- Up-skilling naturally will increase, as employees will be able to dedicate more time to more strategic tasks (over routine reporting tasks).

For more information view our Tax Function of the Future series [here](#).

We value your input

Our way of working is to take the time to understand your business, your tax function and the issues and challenges you are facing, specifically around tax technology, so that we can use our local and global knowledge to help you introduce and deliver appropriate tax technology strategies that work specifically for you.

To this end, we have designed a survey to gain insight into your specific needs so that we can work with you to chart a course to creating a tax function that is fit for the future.



Click on the link to access the survey.

The survey takes approximately ten minutes to complete and your responses will be held in the strictest confidence. Any data published will be presented in aggregate.



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SARS Watch

SARS Watch 26 June 2019 – 25 July 2019

Legislation		
22 July 2019	Manual on the Promotion of Access to Information Act, 2000	Notice No. 997 published in Government Gazette No. 42584 with an effective date of 19 July 2019.
21 July 2019	Draft Tax Administration Laws Amendment Bill, 2019 and related memorandum	Comments are due to SARS and National Treasury by Friday, 23 August 2019.
21 July 2019	Draft Taxation Laws Amendment Bill, and related memorandum	Comments are due to SARS and National Treasury by Friday, 23 August 2019.
17 July 2019	Draft tariff amendment notice – Note 8 of Schedule No. 5	Comments must be submitted to SARS by Friday, 16 August 2019.
12 July 2019	Amendment to Part 1 of Schedule No. 2, by the substitution of Anti-Dumping items 215.11/8201.10.10/01.08; 215.11/8201.30.03/01.08; 215.11/8201.30.90/01.08 and 215.11/8201.90.20/01.08 to review the rate of Anti-Dumping duty on garden spades and shovels, rakes and picks originating in or imported from the People's Republic of China (PRC): Final Determination – ITAC Report 602	Notice R. 986 published in Government Gazette No. 42577 with an implementation date of 12 July 2019.
12 July 2019	Amendment to Part 1 of Schedule No. 1, by the substitution and insertion of various items under Chapter 73 to increase the rate of customs duty on certain tubes, pipes and hollow profiles, seamless, of iron (excluding cast iron) or steel – ITAC Report 601	Notice R. 985 published in Government Gazette No. 42577 with an implementation date of 12 July 2019.
12 July 2019	Amendment to Part 1 of Schedule No. 1, by the substitution of tariff subheading 8511.30.30 in order to reduce the rate of customs duty on distributors and ignition coils identifiable for use solely or principally with motor vehicles, engines – ITAC Report 568	Notice R. 984 published in Government Gazette No. 42577 with an implementation date of 12 July 2019.
8 July 2019	Draft rules under section 49 – trade agreements	Comments must be submitted to SARS by Monday, 22 July 2019.
8 July 2019	Draft rule under section 38 – SACU UCR Botswana	Comments must be submitted to SARS by Monday, 22 July 2019.
28 June 2019	Notice in terms of section 25 of the Tax Administration Act for submission of 2019 income tax returns	Notice 342 published in Government Gazette No. 42525 with an implementation date of 28 June 2019.
Case law		
In accordance to date of judgment		
17 July 2019	Wingate-Pearse v Commissioner for the South African Revenue Service (29208/15) [2019] ZAGPJHC 218 (17 July 2019)	A review application in which the judgment was in SARS's favour.
12 June 2019	TCIT 14287	Whether the appellant is liable for tax in terms of section 64 of the Income Tax Act.

Rulings		
18 July 2019	BPR 323: Debt reduction by means of set-off	This ruling determines the tax consequences for the applicant of a proposed settlement of a shareholder's debt and the subsequent issue of ordinary shares.
16 July 2019	BPR 322: Equity linked note	This ruling determines the nature of an amount received or which accrues as a redemption amount of an equity linked note (ELN), as well as the nature of the amount paid to acquire the ELN. It further determines that the ELN is not an instrument as defined in section 24J(1).
2 July 2019	BPR 321: Surplus retirement fund assets	This ruling determines the tax consequences of transferring surplus retirement fund assets between funds and allocating assets from employer surplus accounts to the retirement accounts of members as provided for by the Pension Funds Act 24 of 1956.
2 July 2019	BCR 068: Surplus retirement fund assets	This ruling determines the tax consequences of transferring surplus retirement fund assets between funds and allocating assets from employer surplus accounts to the retirement accounts of members as provided for by the Pension Funds Act 24 of 1956.
Guides		
5 July 2019	Frequently asked questions: Supplies of electronic services (Issue 3)	The guide has been compiled based on questions that vendors and the public are likely to have about the implications of the Updated Regulations and the amendments.
28 June 2019	Comprehensive Guide to the Income Tax Return for Individuals	The purpose of this guide is to provide guidance for the completion of the ITR12 return and to briefly explain the various sections of the Income Tax Act No. 58 of 1962 that will be applied during the assessment process.
28 June 2019	Guide to the Individual Income Tax Return for Deceased and Insolvent Estates	The purpose of this guide is to provide assistance to complete an income tax return for individuals where there is income received or accrued to a deceased or insolvent estate.
28 June 2019	How to submit your Individual Income Tax Return via eFiling	The purpose of this guide is to assist in filing an income tax return for individuals when using the eFiling system.
28 June 2019	Guide to the SARS eFiling Application	The purpose of this guide is to assist taxpayers navigating the SARS MobiApp.
Other publications		
23 July 2019	OECD: Latest results on preferential regimes and new results on no or only nominal tax jurisdictions	The review covers not only preferential tax regimes, but the results of the review of the substantial activities factor for no or only nominal jurisdictions.
28 June 2019	OECD: Secretary-general tax report to the G20 leaders	The report contains activities and developments that have taken place since the last tax report issued in December 2018. Part I reports on the activities and achievements in the OECD's international tax agenda. Part II reports on the activities and achievements of the Global Forum on Transparency and Exchange of Information for Tax Purposes.
28 June 2019	Tax Alert: 2019 Filing Season	The alert discusses the requirements announced by SARS to file income tax returns and the various filing periods based on the SARS system used.
27 June 2019	OECD: Model Mandatory Disclosure Rules on Common Reporting Standard Avoidance Arrangements and Opaque Offshore Structures	In order to support the operational and technical side of the Model Mandatory Disclosure Rules ('MDR') exchanges, the OECD has developed the MDR XML Schema and User Guide to support MDR exchanges, which will facilitate the structured collection and exchange of information on Common Reporting Standard Avoidance Arrangements and Opaque Offshore Structures.



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(19-24243)