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Let's talk

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

Gavin Duffy
Johannesburg
+27 (0) 11 797 4271
gavin.duffy@pwc.com

James Whitaker
Cape Town
+27 (0) 21 529 2638
james.whitaker@pwc.com

Jade Hansen
Cape Town
+27 (0) 21 529 2605
jade.hansen@pwc.com

Rushika Valodia
Johannesburg
+27 (0) 21 529 2194
rushika.valodia@pwc.com

Exchange Control: Recent developments

In brief

During 2020, the National Treasury announced that South Africa's Exchange Control regime would be replaced by a new Capital Flow Management system. This transition is intended to reduce 'red tape' in the case of legitimate financial flows and to introduce more robust measures to detect, deter and disrupt illegitimate cross-border financial flows. Since the announcement, the South African Reserve Bank ('SARB') has issued a number of Circulars that effect changes to the existing Exchange Control Regulations applicable to emigration and loop structures. In this Alert, we explore some of the changes brought about by these Circulars.

In detail

Phasing out of 'emigration'

As per Exchange Control Circular No. 5/2021, as from 1 March 2021, the term 'emigration' as recognised by SARB is being phased out. From this date, all new emigration applications will be processed by the South African Revenue Service ('SARS') and involve a confirmation of cessation of tax residence.

In Exchange Control Circular No. 6/2021, SARB explains that individuals seeking to emigrate only need to submit a request for an emigration Tax Compliance Status ('TCS') pin from SARS. Since 1 March 2021, the completion and submission of the MP336(b) form has no longer been a requirement. Along with the changes to the emigration application process, we have seen SARS place a greater emphasis on the tax compliance of the applicant as well as entities connected to the applicant.

According to Circular No. 6/2021, applications to transfer offshore amounts above the single discretionary allowance threshold of R1 million require the TCS pin. Transfers offshore by an individual of an amount within the single discretionary allowance only require a formal declaration to SARS of cessation of residence or a declaration in the submission of the ITR12 return.

However, should the net asset value of the amount involved in the emigration application exceed R10 million, the application will be subject to additional requirements (including the verification of the source of the funds and risk assessments relating to anti-money laundering and countering terror financing).

As per the Circular, the current process of controlling or blocking an emigrant's remaining assets in a special 'blocked funds account' will fall away, and all transfers from these accounts will be handled as normal fund transfers in line with any other foreign capital allowance transfer.

Withdrawal of retirement benefits through the emigration process

As per Exchange Control Circular No. 6/2021, as from 1 March 2021, emigrants may withdraw their applicable retirement benefits provided that they have been non-residents for South African tax purposes for an uninterrupted period of three years and an applicable tax directive has been issued to the relevant fund by SARS (the emigrant will be required to provide the TCS pin to the Authorised Dealer (i.e. their South African bank), as well as documentation from the fund showing the final amount to be paid out to the emigrant).

As per Exchange Control Circular No. 11/2021, Authorised Dealers may allow the transfer of monthly pension and/or annuity payments subject to the provision, at least once a year, of a TCS of good standing.

Singular use of the single discretionary allowance

Exchange Control Circular No. 8/2021, dated 21 May 2021, effects a number of changes to the Currency and Exchanges Manual for Authorised Dealers. One of these changes is that an individual may, in the year that they cease to be a tax resident, make use of the R1 million travel allowance, and that the travel allowance may not be used in subsequent years.

Income due to non-residents and private individuals who have ceased to be South African tax residents

Authorised Dealers may allow the transfer of salaries and/or fees payable to *bona fide* non-residents and private individuals who have ceased to be residents of South Africa for tax purposes, provided that the individual is unrelated to the payor and the services are rendered abroad.

Regarding the transfer of other amounts such as dividends and profits (other than pensions and/or retirement annuities, excluding lump sum payments) such amounts may not be transferred to South African residents temporarily abroad and may only be transferred on provision of an annual TCS of good standing (for amounts up to R10 million) or in terms of a Foreign Investment Allowance application (for amounts exceeding R10 million).

Loop structures

Generally, the formation of a loop structure involves the export of funds from South Africa by a South African resident (whether in terms of Exchange Control rules or otherwise) and the establishment of an offshore entity (such as a company or trust) in which the South African resident holds an interest. The 'loop' arises where the offshore entity then reinvests into the Common Monetary Area ('CMA') through, for example, the acquisition (directly or indirectly) of shares in a company resident in the CMA, or the provision of a loan to such a company.

Prior to the issue of Exchange Control Circular No. 1/2021, South African resident individuals, companies and private equity funds were, whether alone or together with any other South African resident(s), only permitted to hold up to a 40% interest in the non-resident entity.

Circular No. 1/2021 has broadly removed this 40% limit on holdings, provided that the investment is reported to an Authorised Dealer and an annual report on the investment is provided to the Authorised Dealer. It is important to note that existing unauthorised loop structures must still be reported and regularised with SARB.

Takeaways

Most of the most recent changes effected to the Exchange Control regime are mostly directed at individuals and aimed at alleviating the administrative burdens relating to cross-border transactions.

Importantly, these changes have brought a renewed focus on the tax compliance of South African individuals who are emigrating. In particular, the changes enable SARS to conduct in-depth tax audits of individuals upon their departure from South Africa. It is therefore more important than ever to ensure that your tax affairs are in order before you permanently leave South Africa.