



2014/2015 Budget Proposals - Tax Overview

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Last year we noted that, from a tax perspective, the number of proposed changes to the various fiscal Acts (mainly the Income Tax Act and VAT Act) were considerably fewer than in prior years.

INTRODUCTION

This year there are even fewer proposed amendments and they are less wide-ranging. This was not unexpected given that this is an election year, Parliament sitting for a shorter time in the year than usual; the Davis Tax Review Committee is yet to report and it would not be wise to make significant changes before receiving and considering the report; and, it must be said, Treasury has lost a considerable amount of skills in the tax area during this past year, which will obviously impact on their ability to consider and draft the changes.

Contrary to widespread speculation there were no increases in direct taxation, but rather there was some tax relief for individuals, to eliminate the effects of inflation.

A number of the proposed amendments which were announced are of a highly technical nature. We have thus attempted to limit ourselves to matters which are likely to be of more general and widespread interest.

INDIVIDUALS

Investing offshore through local policies

Investors take out policies with local long-term insurance companies which then re-insure with foreign reinsurers, which link the policy gains to underlying foreign investments. Currently reinsurance premiums and claims are disregarded in determining the insurance company's tax liability. It is proposed that the net returns be taxed, with the result that the return to the policyholder will obviously reduce.

Sickness and disability policies

Last year an amendment was introduced, to apply with effect from this year, that premiums will no longer be deductible and claims will no longer be taxable. It is proposed to clarify the legislation to prevent certain structured products from falling outside the ambit of the legislation, so as to ensure that premiums on all personal insurance policies will not be allowed as a deduction, and that the proceeds will all be tax-free.

Tax preferred savings accounts

The possibility of this savings incentive was raised in 2012, the proposal being that the maximum annual contribution would be R30 000, with a lifetime contribution limit of R500 000 (to be increased in line with inflation). The account will allow investments in bank deposits, collective investment schemes, exchange-traded funds and retail savings bonds. These proposals will now be proceeded with.

Fringe benefits

The major change proposed is that employer-provided residential accommodation will be valued on a different basis – currently it is valued by means of a formula applied to the employee's remuneration. As a first step, the focus of the change will be on rented and shared accommodation, as opposed to employer-owned accommodation. As regards rental accommodation, the value of use will be the cost to the employer; while as regards shared accommodation, it is proposed that a form of apportionment be considered.

BUSINESSES

Interest limitation rules

Last year interest limitation rules were introduced in relation both to debt borrowed from connected persons who were not taxable, and in relation to debt arising from reorganisation and acquisition transactions.

It is proposed to ease the rules relating to interest limitations on reorganisation and acquisition transactions. The changes proposed include:

- ▶ taking into account the previous year's EBITDA (for tax purposes);
- ▶ allowing an adjustment when the repo rate exceeds 8% and not, as it currently is, 10%; and
- ▶ ignoring assessed losses brought forward, which would otherwise reduce the tax EBITDA, and hence the amount of interest allowable.

Third-party backed shares

Extensive amendments were made in 2012, and small amendments in 2013, to section 8EA of the Income Tax Act which section, very shortly, removes the tax exemption on dividends from (mainly) redeemable preference shares if performance under the shares has been guaranteed by a third party. The major exception to this rule was where the preference shares were used directly or indirectly to fund an investment in an operating company (as defined).

It is proposed to extend the exception to where the investment is in an exploration company, which would not otherwise meet the requirements of being an operating company. Failure to extend this exception affects especially BEE parties investing in an exploration company.

Concessions will also be made in relation to certain limited pledges of the shares, and in respect of refinancing transactions.

Debt reduction rules

Revised rules were introduced in 2012 to reduce the tax effect of debtors being relieved of having to pay their creditors in full, particularly motivated by cases where the debtor companies faced financial hardship.

It is proposed that tax relief measures be considered for companies undergoing business rescue in terms of the Companies Act, and other forms of debt compromise.

Keyman policy

It is possible to elect that premiums under keyman policies be deductible, with the proceeds being taxable, or to allow the default position where the premiums are not deductible and the proceeds are not taxable.

Where the deductibility election is made, it is intended to tighten up the rules so that deductibility will be allowed only where the employer is insured against loss due to the death, disablement or severe illness of an employee or director, and not in other circumstances, such as to provide funds for the repayment of a loan.

Public Private Partnerships

Consideration will be given to allowing relief on depreciation to be claimed on improvements erected on land owned by the State, to improve the financial viability of the projects (there is already such an allowance contained in section 12N of the Income Tax Act, so presumably this allowance is to be enhanced in some manner).

Long-term insurance companies

Apart from the change referred to above in relation to foreign reinsurance, it is proposed that where a long-term insurer issues a risk policy (which is very little different to the types of policies issued by short-term insurance companies) the profits should be taxed in a similar way to a short-term insurance company, ie at 28%, rather than in one of the policyholder funds where the effective tax rate can be considerably lower.

It is also proposed to review the fairness of the taxation of the individual policyholder fund, where a tax rate of 30% applies, irrespective of the level of income of policyholders.

Venture Capital Companies (VCC)

The purpose of a VCC is to encourage investments into small and medium enterprises, and the major incentive is that an investment into a VCC is tax-deductible. Despite this, the VCC has not proved popular.

It is therefore proposed to enhance its attractiveness by:

- ▶ removing the recoupment provision when the investment in the VCC is disposed of, if the shares have been held for a minimum period of time;
- ▶ allowing transferability of tax benefits on disposal of the shares;
- ▶ increasing the amounts by which the VCC can invest in underlying investee companies;
- ▶ exempting the VCC from CGT; and
- ▶ expanding the permitted business forms for a VCC (eg, presumably to include trusts, limited partnerships, and the like).

Small and Medium Enterprises (SMEs)

A number of proposals have been made to encourage the establishment of SMEs by enhancing the tax system. These include:

- ▶ simplifying certain aspects of the turnover tax regime for micro businesses;
- ▶ replacing the reduced tax rate regime for small business corporations with an annual refundable tax compliance rebate (this being a recommendation of the Davis Tax Review Committee); and
- ▶ making grants received by SMEs tax-exempt, regardless of the source of the funds (presumably this means the exemption will no longer be limited to Government grants).

Public Benefit Organisations (PBOs)

Currently PBOs to which donations are made that qualify for an income tax deduction under section 18A of the Income Tax Act, must distribute up to 75% of their receipts within a year following the year-end of receipt. It is proposed to relax this requirement to improve sustainability.

Taxpayer reference number

The Minister announced that in the next fiscal year the SARS will implement a single registration of taxpayers and traders for the main taxes. The Tax Administration Act already contains the regulatory and statutory framework for such a single taxpayer reference number.

INTERNATIONAL

Transfer pricing rules

Currently when there is a transfer pricing adjustment arising from a transaction between a South African resident and a connected person who is a foreign resident, a notional loan is deemed to come into existence, and, in effect, notional interest thereon is deemed to accrue in subsequent years, which is also taxable, until the loan is "repaid" – presumably by a payment to the South African resident to compensate it for the under- or over-charge, as the case may be.

It is now recognised that this is cumbersome and it is proposed to substitute this so-called secondary adjustment with a different type of secondary adjustment, namely, treating it either as a dividend or a capital contribution, as the circumstances may determine (it will be recalled that under the previous transfer pricing rules, the secondary adjustment was deemed to be a dividend subject to STC).

Controlled foreign companies (CFCs)

Currently the profits of a CFC will not be taxed in the South African shareholder's hands where the CFC either has a qualifying foreign business establishment, or it is resident in a country where the tax that it pays there is equal at least to 75% of the tax it would have paid had it been a South African- resident company (the latter colloquially being referred to as the high-tax exemption).

Unfortunately the high tax exemption is somewhat problematical, because it was designed to alleviate the need to make CFC calculations, but it is still necessary to make the calculation in order to determine that it is no longer necessary to make the calculation!

To ease the compliance burden it is proposed that where a South African resident company owns a number of CFCs, an option be provided to deem the net income of the CFC to be nil if either the high-tax exemption or the foreign business establishment test, when applied to the aggregate taxable amounts, is met.

Cross-border retirement saving

Currently, expatriates coming to work in South Africa, who continue to contribute to foreign

retirement funds, are only able to claim the deduction if the foreign fund is approved by the SARS (which is very rare in practice). A similar problem faces South African residents who work abroad. It is proposed to reconsider the cross-border pension issues over the next two years.

INDIRECT TAXES

Carbon tax

The implementation of the controversial carbon tax is to be postponed to 2016 to align the design of the carbon tax and the proposed desired emission-reduction outcomes.

VAT

There are two significant proposals:

- ▶ Notional input tax is allowed as a deduction to a registered vendor that acquires second-hand goods from a non-vendor. This concession is to be removed in the case of second-hand goods made from precious metals.
- ▶ Technically, a zero-rated sale of a business as a going concern is only possible where the purchaser is a registered VAT vendor. The SARS has dealt with this administratively whereby it allows zero-rating provided the application for registration is made before the agreement is concluded, in which case the registration is backdated to date of application, thereby ensuring that the parties qualify. The legislation will be amended to remove the uncertainty regarding whether a person must be a vendor before the acquisition of the going concern.

RESEARCH PROJECTS

A number of tax policy research projects are on Treasury's agenda over the next two fiscal years, including:

- ▶ A study of effective tax rates for companies in different sectors, including a review of the effectiveness of some tax incentives;
- ▶ the removal of the zero-rating provision of housing subsidies, and to make them standard-rated (but at the same time to increase the value of the grant); and
- ▶ a review of how educational services and public transport are treated for VAT purposes (currently they are both exempt, which means that no VAT is charged, and no input tax can be claimed, by the supplier).

EXCHANGE CONTROLS

Last year a tax and exchange control concession was introduced to allow a listed group of companies to designate, and register with the Reserve Bank, one subsidiary to conduct international treasury operations. This subsidiary is essentially free of exchange controls and the listed holding company is entitled to transfer to it, without exchange control approval, up to R750 million per annum (and more with approval).

The Minister announced that, as further steps to simplify trade with Africa, this regime will be extended to unlisted companies, and the limits for listed companies will be increased (though no amounts were mentioned in his speech).

TAX RATES AND THRESHOLDS

Individuals

Relief will be granted by adjustments to the personal income tax table as follows:

Personal income tax rate and bracket adjustments

2014/15		2013/14	
TAXABLE INCOME (R)	RATES OF TAX	TAXABLE INCOME (R)	RATES OF TAX
0 – 174 550	18% of each R1	0 – 165 600	18% of each R1
174 551 – 272 700	R31 419 + 25% of the amount above R174 550	165 601 – 258 750	R29 808 + 25% of the amount above R165 600
272 701 – 377 450	R55 957 + 30% of the amount above R272 700	258 751 – 358 110	R53 096 + 30% of the amount above R258 750
377 451 – 528 000	R87 382 + 35% of the amount above R377 450	358 111 – 500 940	R82 904 + 35% of the amount above R358 110
528 001 – 673 100	R140 074 + 38% of the amount above R528 000	500 941 – 638 600	R132 894 + 38% of the amount above R500 940
673 101 +	R195 212 + 40% of the amount above R673 100	638 601 +	R185 205 + 40% of the amount above R638 600

	2014/15	2013/14
REBATES	R	R
Primary	12 726	12 080
Secondary	7 110	6 750
Tertiary	2 367	2 250
TAX THRESHOLD		
Below age 65	70 700	67 111
Age 65 and over	110 200	104 611
Age 75 and over	123 350	117 111

Retirement fund lump sum withdrawal benefits

2014/15		2013/14	
TAXABLE INCOME (R)	RATES OF TAX	TAXABLE INCOME (R)	RATES OF TAX
0 – 25 000	0% of taxable income	0 – 22 500	0% of taxable income
25 001 – 660 000	18% of taxable income above R25 000	22 501 – 660 000	18% of taxable income above R22 500
660 001 – 990 000	R114 300 + 27% of taxable income above R660 000	600 001 – 900 000	R103 950 + 27% of taxable income above R600 000
990 001 +	R203 400 + 36% of taxable income above R990 000	900 001 +	R184 950 + 36% of taxable income above R900 000

Retirement fund lump sum benefits or severance benefits

2014/15		2013/14	
TAXABLE INCOME (R)	RATES OF TAX	TAXABLE INCOME (R)	RATES OF TAX
0 – 500 000	0% of taxable income	0 – 315 000	0% of taxable income
500 001 – 700 000	18% of taxable income above R500 000	315 001 – 630 000	18% of taxable income above R315 000
700 001 – 1 050 000	R36 000 + 27% of taxable income above R700 000	630 001 – 945 000	R56 700 + 27% of taxable income above R630 000
1 050 001 +	R130 500 + 36% of taxable income above R1 050 000	945 001 +	R141 750 + 36% of taxable income above R945 000

The relief, insofar as it applies to individuals younger than 65 years, is illustrated in the following comparative table:

TAXABLE INCOME	2014/15 RATES	2013/14 RATES	TAX REDUCTION	% REDUCTION
R	R	R	R	R
75 000	774	1 420	- 646	- 45.5%
80 000	1 674	2 320	- 646	- 27.8%
85 000	2 574	3 220	-646	- 20.1%
90 000	3 474	4 120	-646	- 15.7%
100 000	5 274	5 920	-646	- 10.9%
120 000	8 874	9 520	-646	- 6.8%
150 000	14 274	14 920	-646	- 4.3%
200 000	25 056	26 328	- 1 273	- 4.8%
250 000	37 556	38 828	- 1 273	- 3.3%
300 000	51 421	53 391	- 1 970	- 3.7%
400 000	82 549	85 486	- 2 937	- 3.4%
500 000	117 549	120 486	- 2 937	- 2.4%
750 000	213 246	217 685	- 4 439	- 2.0%
1 000 000	313 246	317 685	- 4 439	- 1.4%

TAX FREE PORTION OF INTEREST

	2014/15	2013/14
	R	R
Interest - under 65	23 800	23 800
- over 65	34 500	34 500

TRAVEL ALLOWANCE

VALUE OF VEHICLE INCLUDING VAT (R)	FIXED COST (R p.a.)	FUEL COSTS (c/km)	MAINTENANCE COST (c/km)
0 – 80 000	25 946	92.3	27.6
80 001 – 160 000	46 203	103.1	34.6
160 001 – 240 000	66 530	112.0	38.1
240 001 – 320 000	84 351	120.5	41.6
320 001 – 400 000	102 233	128.9	48.8
400 001 – 480 000	120 997	147.9	57.3
480 001 – 560 000	139 760	152.9	71.3
Exceeding 560 000	139 760	152.9	71.3

MONTHLY MEDICAL TAX CREDIT

Description	2014/15	2013/14
	R	R
Medical scheme fees tax credit, in respect of benefits to the taxpayer	257	242
Medical scheme fees tax credit, in respect of benefits to the taxpayer and one dependent	514	484
Medical scheme fees tax credit, in respect of benefits to each additional dependant	172	162

CORPORATE INCOME TAX RATES

Income tax – Companies

For the financial years ending on any date between 1 April and the following 31 March, the following rates of tax will apply:

	2014/15	2013/14
TYPE	RATE OF TAX (%)	
Companies (other than gold mining companies and long term insurers)	28	28
Personal service providers	28	28
Foreign resident companies earning income from a South African source	28	28
Dividends Tax	15	15

Tax regime for small business corporations

2014/15		2013/14	
TAXABLE INCOME	RATE	TAXABLE INCOME	RATE
0 – R70 700	0%	Below R67 111	0%
R70 701 – R365 000	7%	R67 112 to R365 000	7%
R365 001 – R550 000	21%	R365 001 to R550 000	21%
550 001 +	28%	R550 001 +	28%

CAPITAL GAINS TAX

Effective capital gains tax rates

TYPE	2014/15	2013/14
For individuals and special trusts	13.3%	13.3%
Companies	18.6%	18.6%
Trusts	26.6%	26.6%

Capital gains exemptions

DESCRIPTION	THRESHOLDS 2014/15	THRESHOLDS 2013/14
	R	R
Annual exclusion for individuals and special trusts	30 000	30 000
Exclusion on death	300 000	300 000
Exclusion in respect of disposal of primary residence (based on amount of capital gain or loss on disposal)	2 million	2 million
Maximum market value of all assets allowed within definition of small business on disposal when person over 55	10 million	10 million
Exclusion amount on disposal of small business when person over 55	1.8 million	1.8 million

TRANSFER DUTY

The transfer duty table, which applies to all types of purchasers, is as follows:

VALUE OF PROPERTY (R)	RATE
0 – 600 000	0%
600 001 – 1 000 000	3% of the value above R600 000
1 000 001 – 1 500 000	R12 000 + 5% of the value above R1 000 000
1 500 001 +	R37 000 + 8% of the value exceeding R1 500 000

About Werksmans Tax practice

Our Tax practice is able to respond swiftly and efficiently on local and international tax matters. Team members have extensive experience in consulting to the commercial sector and are able to provide integrated advice and assistance on a wide range of tax issues.

Services range from consulting on the tax aspects of clients' commercial dealings to interacting on their behalf with the tax authorities and, where necessary, dealing with objections and disputes.

Special areas of expertise include the tax aspects of commercial activities such as mergers and acquisitions, private equity and black economic empowerment transactions, and corporate re-organisations.

Team members are also skilled in handling settlement negotiations, appeals in the Tax

Court and High Court, and alternative dispute resolution processes.

In terms of international tax services, the team has a well-established track record in inward and outward investment matters and offshore structuring, taking into account the exchange control implications thereof.

Services include dealing with:

- ▶ Domestic tax: income tax, withholding tax, capital gains tax, employees' tax, value-added tax and securities transfer tax
- ▶ International tax: inward and outward investment
- ▶ Exchange control advice
- ▶ Estate planning

- ▶ Tax rules relating to financial services and products: encompassing insurance, private equity, securitisations, hedge funds, structured and project finance, debt and derivative instruments
- ▶ Tax structuring of transactions: including black economic empowerment transactions, mergers and acquisitions, unbundlings, reconstructions, management buyouts, distributions, funding, securities issues and buy-backs
- ▶ Tax litigation and dispute resolution: from liaison with tax authorities and regulators on settlement negotiations, alternative dispute resolution, objections and Tax Court appeals.

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With a formidable track record in mergers and acquisitions, banking and finance, and commercial litigation and dispute resolution, Werksmans is distinguished by the people, clients and work that it attracts and retains.

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