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Global Tax Alert

South Africa's Minister of Finance delivers 2020 Budget Review

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On 26 February 2020, South Africa's Minister of Finance, Tito Mboweni, delivered his 2020 Budget Review (the Budget).

This Alert summarizes the key highlights from the Budget.

Corporate tax

To promote economic growth, the South African Government intends to restructure the corporate income tax system over the medium term by broadening the tax base and reducing the corporate income tax rate.

Broadening the corporate tax base will include:

- A systematic review of tax incentives to repeal inefficient incentives.
- Strengthening existing interest limitations rules[1] which will limit the net interest deduction to 30% of tax EBITDA,[2] irrespective of connected person status. National Treasury has released a discussion document for public comment by 17 April 2020.
- Restricting the offset of prior assessed tax losses carried forward to 80% of taxable income.[3]

The corporate income tax rate therefore will remain unchanged at 28% but rate reductions will be implemented in a revenue-neutral manner.

Building a better working world

Other notable corporate tax proposals include:

- Clarification of the tax treatment of doubtful debt for non-bank taxpayers with security; and taxpayers operating a leasing business. The doubtful debt tax treatment of impairments under IFRS9 for banks will also be reviewed.
- Double tax anomalies that may result from the interaction of anti-avoidance de-grouping rules and rules for the transfer of assets and assumption of related debt will also be addressed.
- The interplay between the specific base cost rules on asset acquisitions in exchange for debt issued and the general anti-avoidance rules dealing with disposals between connected persons will be addressed to avoid unintended consequences.
- Anti-avoidance measures in relation to the transfer of collateral in securities lending arrangements will be broadened.
- The participation exemption related to the disposal of shares in a company that ceased to be a resident and dividends arising from previous tax-deductible expenses will be disallowed.
- The application of transfer pricing rules in the context of a transaction between a controlled foreign company and a nonresident connected person (where there is no tax benefit for the controlled foreign company but lower imputation for a South African tax resident) will be confirmed.
- The potential for a resident to eliminate dividends tax/capital gains tax through a controlled foreign company loop structure will be eliminated.
- The export of dual listed securities, due to exchange control liberalization, will be treated as a deemed disposal that triggers income tax or capital gains tax.
- A refund will be available for Withholding Tax on Royalties should the royalty that became due and payable become irrecoverable.
- A nonresident shareholder and an unbundling company will be precluded from tax-free unbundling share distributions where 20% or more of the shares in the unbundled company will be held by nonresidents and irrespective of whether there is a connected person relationship between such nonresidents.
- Preference shares and non-equity shares will not qualify for inclusion in the real estate investment trust (REIT) tax dispensation as this was not intended. The definition of share will therefore be amended to exclude such shares.
- The foreign company dividend participation exemption will no longer be available to REITs given the tax deduction available to REITs on onward distribution of such dividends to REIT shareholders. The dividend exemption and dividend deduction mismatch in a REIT's hands will therefore be removed.
- The following will be addressed during the 2020 legislative cycle:
  - Taxation of unlisted REITs
  - Tax treatment of amounts received by portfolios of collective investment schemes
- National Treasury will review the mining capital expenditure regime to address concerns about whether both a mining right holder and a contract miner should benefit from accelerated capital allowances.
- Removal of the discretion of the Finance Minister on the use of ring fenced per mine capital expenditure.
- Consideration of the tax implications of a bank deposit insurance scheme (funded by bank contributions) to protect depositors in the case of bank failure.
- Review of interactions between different rules relating to the taxation of benefits received by short term insurance policyholders and the tax treatment of related expenses.

Personal taxes

Personal income tax brackets and rebates to be increased by above inflation rates, effective from 1 March 2020.

Other notable personal income tax proposals include:

- Increase of the foreign remuneration exemption threshold to R1.25 million from 1 March 2020.
- Phasing out of the "financial emigration" concept for exchange control to emphasize that tax residency is not necessarily broken in such a way.
- From 1 March 2020 employees will be precluded from structuring portions of their ordinary remuneration packages as tax-exempt bursaries granted to their dependents.
- Introduction of measures to prevent circumvention of trust related anti-avoidance rules, through subscription for preference shares in a company owned by a trust that is a connected person in relation to the subscriber.

Value-Added Tax (VAT)

The VAT rate remains unchanged at 15%.

Other notable VAT proposals include:

- The definition of telecommunication services in the regulations relating to VAT on electronic services will be revised given an incorrect reference that gives rise to unintended consequences.
- VAT rollover relief will apply in respect of assets disposed of under corporate rules despite income tax relief not being applicable to such assets.
- Clarification of the application of VAT value of supply rules in the context of irrecoverable debts.
- Assessment of the impact and role of historic section 72 VAT rulings to ascertain whether these should be discontinued or extended under the new provisions of section 72.

Other indirect taxes

Key indirect tax proposals include:

- Increase in the carbon tax rate by 5.6% for the 2020 calendar year
- Increase in fuel levies by 25 cents
- Inflationary increase of sin taxes (4.4% - 7.5%)
- Intention to tax electronic cigarettes from 2021
- Introduction of excise duty on heated tobacco products
- Significant increase in plastic bag levy and potential inclusion of single-use plastics
- Export taxes on scrap metal
- Vehicle emission tax to increase in line with global standards and shift to fuel-efficient cars
- Government to prepare an environmental fiscal reform review paper
- The *Customs and Excise Act* will be amended to allow tariff determinations to be published to contribute to consistency and transparency in the classification of goods

Tax administration

Key tax administration proposals include:

- Extension of South African Revenue Service's (SARS) powers to withhold refunds to include outstanding returns in respect of other employment-related taxes.
- Empowering SARS to issue a further estimated assessment should a taxpayer fail on more than once occasion to respond to a request for relevant material. This will prevent an objection and appeal until the material has been provided.
- Reducing the tax compliance burden for individuals and firms through simplification of tax legislation and through the creation of a more standardized system.
- Modernizing the Pay As You Earn legislative and administrative framework to ease compliance for employers and also eliminate tax return obligations for salaried employees.

Exchange control

Other exchange control developments include:

- Introduction over the next 12 months of a new capital flow management system to increase transparency, reduce burdensome and unnecessary administrative approvals, and promote certainty.
- Foreign-currency transactions will generally be allowed. Certain risk-based capital flow measures will remain.

Endnotes

1. Effective years of assessment commencing or of after 1 January 2021.
2. Earnings before interest, taxes, depreciation and amortization.
3. Effective years of assessment commencing or of after 1 January 2021.

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