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Tax Developments on one page

Tax proposals 2018: Wealth planning and investments

The draft Taxation Laws Amendment Bill, published on 16 July 2018, includes a number of proposals that may impact wealth planning and investment instruments. In particular, the proposed changes affect the tax consequences of offshore trust structures. Amendments are also proposed to the venture capital company regime. The proposals are open for comment and may still change before they are enacted.

The South African National Treasury released the draft Taxation Laws Amendment Bill (draft TLAB) for comment on 16 July 2018. This article provides a brief overview of some of the significant proposals made in the draft TLAB that are likely to affect wealth planning and investment instruments.

Offshore trust structures

For a number of years, the National Treasury have noted in the annual budget review that they intend to expand the controlled foreign company (CFC) rules to also apply to foreign companies held via offshore trusts. During the previous legislative cycle, they proposed amendments in this regard; however, these changes were not implemented due to practical concerns around its application.

The draft TLAB again include proposals to address the National Treasury's concerns arising from these offshore trust structures. The proposed amendments target dividends that accrue to resident taxpayers through foreign trusts, where those dividends arose from foreign companies in which the foreign trust (and its connected persons) holds more than 50% of the shares.

Foreign dividends are generally subject to the so-called participation exemption if the recipient holds at least 10% of the equity shares of the foreign company paying the dividends. The essence of the proposals is that if the foreign dividends targeted by the amendments flow to a resident through a foreign trust, the benefit of the participation exemption will no longer be available and that the dividends be subject to tax when it accrue to the resident beneficiary. The proposals will also similarly affect the application of the attribution rules where the participation exemption would currently result in no attribution of dividend income being required to a person who made the donation, settlement or disposition as a result of which the dividends accrue to the foreign trust.

Deemed donations in respect of loans to trusts

The draft TLAB contains a proposal to clarify and limit the scope of the deemed donation rules in section 7C to loans advanced to companies of which the shares are held by trusts. This amendment is welcomed as the current scope of the provision is arguably wider than intended.

Investments in venture capital companies

There has been a significant increase in the uptake of the venture capital company (VCC) incentive, as contained in section 12J, over the past two to three years. The National Treasury indicated in the explanatory memorandum that accompanied the draft TLAB that it has identified abuse of this incentive. The draft TLAB include a number of proposed amendments that would appear to primarily be aimed at curbing this abuse. In short, the proposals are:

- A VCC may only issue one class of share. This would imply that all investors would be required to subscribe for the same type of shares in the VCC.
- A qualifying company that is funded by an investment made by the VCC may only issue one class of share. This would imply that there can be no distinction between the shares held by the owner/manager of the company and the VCC as passive investor.

It is submitted that the effect of these changes could be far-reaching and are likely to impact existing VCC structures.

Concluding thoughts

The developments mentioned in this article are only proposals. Persons potentially affected by it should keep a keen eye on these proposals as they develop into amendments towards the end of the year. *(August 2018)*

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