Tax Update

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Tax · IFRS

A glance at the tax law amendment bills for 2013

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The Taxation Laws Amendment Bill (Bill 39 of 2013) (hereafter referred to as the Bill) was released by the National Treasury on 24 October 2013. The Bill contains the amendments to the Income Tax Act, Value Added Tax Act and other tax legislation such as the Transfer Duty Act. It includes a number of long awaited amendments, some favourable to taxpayers and, as it could be expected, some amendments that taxpayers will not necessarily be looking forward to. The Bill must still be finally approved by the President before it will become the Taxation Laws Amendment Act. There may therefore strictly speaking still be changes to it, but these have traditionally only been minor amendments.

This newsletter aims to provide a high level overview of some of the amendments that I am of the view are likely to have the greatest effect on taxpayers and practitioners going forward.

Anti-hybrid debt instrument re-characterisation rules (ss 8F and 8FA)

The existing rules dealing with debt instruments that have certain characteristics of equity instruments have proven to be ineffective, mainly due to the fact that the conversion rights in question must be exercisable within 3 months from the date of issue.

Sections 8F and 8FA introduce a more comprehensive reclassification regime with effect from 1 April 2014. Debt instruments may be classified as hybrid debt instrument, or as bearing hybrid interest, based on criteria linked to repayment terms, conversion rights and the manner in which interest is determined. These sections will deem the interest incurred in respect of such instruments to be dividends *in specie*, which could be subject to dividends tax and are not deductible in the hands of the payer. The good news is that the classification now also applies to the recipient of the interest, who can qualify for the dividend exemption in section 10(1)*(k)*(i).

Shareholder loans should be closely examined to determine the effect of this amendment. It must however be noted that the impact could be wider than shareholder loans.

Limitation of interest deduction arising in respect of certain connected person loans (s 23M)

Over the past year I have had many queries from companies, including smaller companies, concerned about the effect of the new withholding tax on interest (which has been postponed to only become effective in 2015). Many of these concerns related to the effect that the withholding tax may have on the interest rate on these loans. In many cases, the provisions of the double tax agreements that South Africa have concluded with other governments result in the withholding tax rate being reduced, in some cases even to nil.

The provisions of section 23M (which become effective from 1 January 2015) are likely to have a bigger effect on companies making use of foreign connected person debt than the withholding tax. In brief, this provision limits the amount of interest that a borrower can deduct in respect of debt owing to a connected person in whose hands the interest is not subject to tax in South Africa.[1]

Similar limitations would apply under section 23N if funds are borrowed to fund an acquisition transaction (as contemplated in section 24O) or an acquisition of an asset in terms of section 45 or 47. This limitation replaces the pre-approval system in section 23K.

Streamlining of VAT registrations

The long awaited streamlining of the VAT registration process is included in the Bill and is set to come into effect on 1 April 2014.

Compulsory registration will now be required if the value of taxable supplies for a 12 month period has exceeded the R1 million threshold or if the value of taxable supplies in terms of a contractual obligation in writing (as opposed to being based on reasonable grounds as is currently the case), will exceed this threshold in the next 12 months.

Voluntary registration will be allowed if a person has carried on an enterprise and the value of taxable supplies for the preceding 12 months has exceeded R50 000. Persons may also be able to voluntarily register as VAT vendors if they carry on certain

[1] The interest may be exempt from income tax in terms of section 10(1)(h).

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enterprises approved by regulation where the value of taxable supplies are likely to exceed R50 000 in the next 12 months or where the nature of the activity is such that taxable supplies are likely to only be made after a period of time (for example, mining).

Periods following voluntary registration during which no refund for input tax could be claimed, as was proposed in the draft bill in July, was not incorporated into the Bill.

Structuring of remuneration packages

A number of provisions contained in the Bill may have an impact on the structuring of remuneration packages, in particular those of high income earning persons.

Firstly, the Bill makes provision for the alignment of all contributions to retirement funds to be treated in a similar manner. This should result in the tax benefits no longer playing a role in the decision as to the vehicle to be used by a person to accumulate his/her retirement savings. In brief, from 1 March 2015, any contribution to a retirement savings fund by an employer would be treated as a fringe benefit in the hands of the employee. The employee will however be entitled to a deduction in respect of his/her own contributions as well as employer contributions. This deduction is subject to a limit of (a) 27,5% of remuneration or taxable income or (b) R350 000 per annum, whichever is the lower of the two amounts. High income earning persons whose contributions may exceed the R350 000 threshold or who in the past received significant portions of their remuneration packages in the form of non-taxable employer contributions to retirement savings funds are likely to be affected.

Secondly, the battle against remuneration packaged in the form of exempt dividend income continues. Section 10(1)*(k)*(i) will be amended by the insertion of para *(ii),* which explicitly states that any dividend received by a person in respect of services rendered or to be rendered or in respect of or by virtue of employment or the holding of any office will not be exempt from normal tax (i.e. it will be subject to the same tax treatment as other remuneration). It is submitted that the wording of this new exclusion from the dividend exemption still requires an analysis of the causal connection between the receipt of the dividend income and the services or employment. Fortunately, unlike to proposal in the draft Bill, an exception exists for dividends received in respect of restricted equity instruments (see section 8C). Dividends received in respect of shares held by the person (employee) will also fall outside the scope of this exclusion.

Amendments proposed in July that are not included in the Bill

A number of proposed amendments that were much anticipated by taxpayers did not realise. One such amendment is the proposed opening of section 12N to voluntary leasehold improvements under leases with parties other than government entities. It appears as if the scope of section 12N remains limited to lease agreements with the state or certain exempt institutions fulfilling government functions, even though the section now makes provision for allowances in respect of voluntary improvements to property owned by such entities.

Concluding thoughts

Apart from the few aspects mentioned above, the amendments included in the Bill are of a very technical nature and even those amendments with a narrow scope may have a significant impact on entities that it applies to. It would therefore be wise to familiarise yourself with these amendments as soon as possible (especially given the nearby transition dates of many of these amendments) in order to identify the impact thereof on your company or your clients.