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OFFSHORE TAX PLANNING WORKBOOK

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THINK WORLD CLASS

TAX PLANNING FOR INVESTING OFFSHORE

CONTENTS

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TAX FORMULA

GROSS INCOME (Section 1-“resident”-worldwide, non-resident SA source, special inclusions)

LESS EXEMPT AMOUNTS (sections 10, 10B, 10C and 12T)

INCOME

LESS DEDUCTIONS (Sections 11 etc *but not* 11F or 18A)

LESS ASSESSED LOSS (Sections 20, 20A)

ADD AMOUNTS TO BE INCLUDED IN TAXABLE INCOME

- ALLOWANCES (taxable portion eg Travel allowance)
- TAXABLE CAPITAL GAINS (Net capital gain x 40% inclusion rate - indiv)

LESS

Section 11F (Retirement fund contributions)

Section 18A (Donations to qualifying PBO’s)

TAXABLE INCOME (**excluding qualifying lump sums*)

(multiply by tax rate in tax table)

TAX PAYABLE

Less rebates (section 6 and 6quat)

ADD Tax payable on qualifying lump sums (see lump sums tax tables)

Less medical rebates (sections 6A and 6B)

FINAL TAX PAYABLE

TAX RESIDENCE

The concept of ‘resident’ is fundamental to the worldwide or residence-based system of taxation. A person who qualifies as a ‘resident’ as defined in s 1 is subject to tax in the Republic on worldwide receipts and accruals.

A non-resident, that is, a person who does not qualify as a resident, is subject to tax in the Republic only on receipts and accruals from a source within or deemed to be within the Republic.

In determining the tax liability of “residents” and non-residents the effect of a double tax agreement between the Republic and the relevant foreign country must be borne in mind.

The following persons are defined as being ‘resident’:

- A natural person who is ***ordinarily resident*** in the Republic.
- A natural person who is not at any time during the year of assessment ordinarily resident in the Republic, if such person is physically present in the Republic for certain periods.
- A person other than a natural person that is incorporated, established or formed in the Republic.
- A person other than a natural person that has its place of effective management in the Republic.

Meaning of ‘resident’: natural persons

The term ‘resident’ is defined in s 1, in relation to a natural person, as

‘(a) a person who is

(i) ordinarily resident in the Republic; ***or***

(ii) meets the requirements of the physical presence test’

A natural person qualifies as a resident, therefore, if he is ordinarily resident in the Republic ***or*** if he meets the requirements of the ‘physical presence’ test. <u>These two tests are mutually exclusive.</u>

Expressly not *included* (rather than expressly excluded) as a ‘resident’ is

‘any person who is deemed to be exclusively a resident of another country for purposes of the application of any agreement entered into between the governments of the Republic and that other country for the avoidance of double taxation.’

This effective exclusion applies only if the person is deemed to be *exclusively* a resident of the other country that is a party to the agreement.

Natural persons — Ordinarily resident

In determining whether a natural person is a resident, therefore, the first test is the common law concept of 'ordinarily resident'. The term 'ordinarily resident' has no special or technical meaning and there is also no definition in the Act of the term 'ordinarily resident'. The reason no doubt being that it is not possible to define satisfactorily the qualities that will determine whether or not a person is ordinarily resident in the Republic. But it could be said that the adverb 'ordinarily' in the expression 'ordinarily resident' should be taken as the converse of 'extraordinarily'; not 'casual and uncertain' but in the ordinary course of the person's life.

As a general rule, 'one is ordinarily resident in the country where, in the settled routine of his life he regularly, normally or customarily lives'. Put somewhat differently, a person's ordinary residence will, essentially, be the country that he regards as his home and to which he would naturally and as a matter of course return from his wanderings.

The question whether a person is 'ordinarily resident' in a country is one of fact. Consequently, it is for the courts to decide on the particular facts of each case whether a person is ordinarily resident in the Republic or not.

Interpretation Note 3 (Issue 2)

When assessing whether a natural person is ordinarily resident in the Republic, the following factors will be taken into consideration:

- An intention to be ordinarily resident in the Republic
- The natural person's most fixed and settled place of residence
- The natural person's habitual abode, that is, the place where that person stays most often, and his or her present habits and mode of life
- The place of business and personal interests of the natural person and his or her family
- Employment and economic factors
- The status of the individual in the Republic and in other countries, for example, whether he or she is an immigrant and what the work permit periods and conditions are
- The location of the natural person's personal belongings
- The natural person's nationality
- Family and social relations (for example, schools, places of worship and sports or social clubs)
- Political, cultural or other activities
- That natural person's application for permanent residence or citizenship
- Periods abroad, purpose and nature of visits
- Frequency of and reasons for visits

The above list *is not intended to be exhaustive* and is merely a guideline.

The circumstances of the natural person must be examined as a whole, taking into account the year of assessment concerned and that person's mode of life before and after the period in question. It is not possible to specify over what period the circumstances must be examined. The examination must cover a sufficient period in the context of the specific case for it to be possible to determine whether the natural person is ordinarily resident in the Republic. The conduct of that person over the entire period of examination must receive special attention.

The effect of the above requirements is that a natural person may be resident in the Republic even if that person was not physically present in the Republic during the relevant year of assessment. A physical presence at all times is not a prerequisite to being ordinarily resident in the Republic. The purpose, nature and intention of a natural person’s absence must be established and considered as part of all the facts in determining whether that person is ordinarily resident.

GROSS INCOME

The definition of the term ‘gross income’ in s 1 of the Income Tax Act is central to the whole of the Income Tax Act. Once the residence of a taxpayer has been established, the taxpayer’s gross income must be determined in relation to the year of assessment or period of assessment of the taxpayer. If the taxpayer is a resident, gross income will be determined on a worldwide basis. If the taxpayer is a non-resent then only amounts from a SA source may be included into the taxpayer’s gross income.

As far as is here relevant, gross income will include:

- the total amount, in cash or otherwise,
- received by or accrued to a person
- during such a year or period of assessment,
- excluding receipts or accruals of a capital nature, but including, without limitation of the scope of the definition, certain amounts, whether of a capital nature or not, commonly referred to as the ‘special inclusions’.

ELEMENTS OF DEFINITION

‘the total amount, in cash or otherwise’

‘Gross income’ is the total amount received by or accrued to the taxpayer whether in cash or otherwise. Even without the words ‘whether in cash or otherwise’, the definition of ‘gross income’ would include, by virtue of the term ‘amount’, ‘not only money, but the value of every form of property earned by the taxpayer.

For example, a person who renders services in return for shares instead of cash will have included in his gross income the value of the shares.

The value to be placed upon the asset other than cash received or accruing as income is the amount that could be obtained for it on the open market if it were to be sold under some reasonable method of sale.

‘Received by or accrued to’

The reference in the definition of the term ‘gross income’ in s 1 to the total amount ‘received by or accrued to or in favour of’ a person during a particular year or period of assessment makes it clear that the definition applies both to ‘receipts’ and to ‘accruals’. However an amount which has been taxed as an accrual cannot again be taxed when it is received, and an amount which has been taxed as a receipt cannot again be taxed when it accrues.

It is also clear that, despite the frequent use of the word ‘profits’, it is not profits but (gross) receipts and accruals that are included in gross income. There must be either a receipt or an accrual, and, in the absence of special provisions, when a person neither receives anything nor has anything accrued to him, there can be no amount to be included in his gross income. For example, an unrealized appreciation in the value of his assets or the rental value of the residence he owns and occupies cannot lead to an inclusion in his gross income, since the benefit arising does not constitute a receipt or an accrual.

Generally, the time of accrual of income derived from a foreign source is no different from the time of accrual of income from a source within the Republic.

Meaning of ‘received by’

In *Geldenhuys v CIR* [1] it was held that the words ‘received by or accrued to or in favour of any person’ in the definition of ‘gross income’ in s 1 relate to the taxpayer, and that the words ‘received by’ must mean ‘received by the taxpayer on his own behalf for his own benefit’. Therefore rent received by an attorney on behalf of a client

[1] (14 SATC 419) (1947 (3)SA 256(C))

forms part of the gross income of the client, since the attorney has not received it on his own behalf and for his own benefit.

Meaning of 'Accrued to'

In *Lategan v CIR* [2] it was held that the meaning of the words 'has accrued to' in the definition of the term 'gross income' meant 'to which [any person] has become entitled'. That is, as soon as an amount becomes unconditionally and uncontingently due to a taxpayer, it must be recognized as income. In other words, at the time that a taxpayer obtains a vested right to a future payment, the amount accrues to the taxpayer.

Not in taxpayer's hands or SA

It is often difficult for taxpayers to understand that an amount can be included into "gross income" despite the taxpayer having had no physical receipt of the amount and in certain instances, the amount may not even have been repatriated to SA.

NB Legal and illegal trade: The Act is not concerned with the legality or illegality of a transaction. Receipts and accruals from an unlawful business are taxable if there is a scheme of profit-making involved.

'excluding receipts or accruals of a capital nature'

There is no definition in the Act of receipts and accruals 'of a capital nature'.

- Amounts received by a taxpayer for allowing the use of an asset to some other person, for example, interest, rental, royalties, all partake of the nature of income (revenue) and fall within the definition of gross income. As long as the amount is received for the right of use of an asset without any change in ownership of the asset, it is usually in the nature of income.
- Amounts received for services rendered clearly partake of the nature of income.
- Fortuitous accessions to capital, such as lump-sum legacies and gifts, and isolated lottery, betting or sweepstake wins, are of a capital nature and fall outside the definition of gross income.
- The proceeds derived from the sale of ordinary income-producing investments or from the sale of assets by a person who does not trade in such assets, for example, a private dwelling, rental property and shares are of a capital nature. On the other hand, if the taxpayer makes it their business to buy and sell the same assets, the proceeds derived from the sale would be of an income nature.

Capital vs Revenue

What is a receipt of a capital nature in the hands of one taxpayer may therefore be of an income nature in the hands of another. How do the courts ascertain whether a particular receipt or accrual is 'of a capital nature'?

Capital amount

Generally speaking, amounts of a capital nature are excluded from "gross income" (subject to the special inclusions). This does not mean that the amount is free from tax, but rather that the consequences of capital gains tax (CGT) must be considered. The effective rates of are

- Natural person: 7.2%-18%
- Company: 22.4%
- Trust: 36%

[2] (2 SATC 16) (1926 CPD 2013)

Revenue amount

An amount that is revenue in nature, will be included in “gross income”. Qualifying expenses may be deducted and the resulting taxable amount taxed at the rates relevant for the particular taxpayer:

- Natural person: 18-45%
- Company: 28%
- Trust: 45%

The differing tax treatment of capital vs revenue amounts makes it clear why this issue has resulted in decades of dispute between taxpayers and SARS and a multitude of court decisions.

Onus of proof

The first point to note is that in terms of s 102 of the Tax Administration Act the burden of proof that an amount is of a capital or revenue nature rests upon the taxpayer.

No “one size fits all”

Secondly, the inquiry whether an amount is of an income or a capital nature is a question of law, which has to be decided upon the facts of each case.

Intention — the golden rule

The most important ‘test’ employed by the courts in deciding whether the proceeds arising upon the disposal of an asset are in the nature of income or capital is the test of ‘intention’: with what intention did the taxpayer:

- acquire,
- hold and
- dispose of the asset?

It is well settled law that the test of intention is subjective and its application involves a consideration of all the circumstances surrounding the acquisition of and method of dealing with an asset.

Scheme of profit making-revenue

The proceeds will be in the nature of income if the asset was acquired and held for the purpose of resale at a profit in a scheme for profit-making (the asset is then regarded as trading stock).

Investment intention-capital

The proceeds will be in the nature of capital and not included in gross income, if the asset was acquired and held not for the purpose of resale at a profit but, for example, in order to produce an income in the form of rent, interest or dividends.

The taxpayer’s intention may change between the acquisition and disposal of the asset, with the consequence that the character of the asset, as income or capital, also changes.

It follows that the taxpayer’s intention must be investigated not only at the time he acquired the asset, but during the whole period over which he held the asset and at the time he disposes of the asset.[3]

[3] *Capstone 556 (Pty) Ltd v Commissioner for the South African Revenue Service* 2014(6) SA 195 (WCC)

The taxpayer's own evidence about his intention and his credibility will be considered by a court but, because of subjectivity, self-interest, the uncertainties of recollection and the possibility of mere reconstruction, it will test that evidence against the surrounding facts and circumstances in order to establish his true intention.
One must consider:

- the *ipse dixit* (say so) of the taxpayer as to his intent and purpose
- objective review of all the relevant facts and circumstances
- the course of conduct of the taxpayer in relation to the transactions in issue,
- the nature of the taxpayer's business or occupation and
- the frequency or otherwise of the taxpayer's past involvement or participation in similar transactions.

Change of intention

An original intention to use an asset as an investment may be changed to one to use it in the carrying out of a scheme of profit-making. Conversely, an original intention to acquire an asset for the purpose of resale at a profit may be changed into one to hold it as an investment.
If the original intention of buying land is not to buy it in order to sell again but to work it, and subsequently the owner changes his intention, decides to become a land-dealer and, in pursuance of that intention, cuts up the land into plots and merges them into the general profit-making scheme of buying and selling land, any proceeds derived from the sale of the land would be of an income nature, since the owner has changed his intention from one of investment to a profit-making scheme. Conversely, if the land was originally acquired for resale at a profit, that is, to carry out a scheme of profit-making, and subsequently the owner changes his intention and decides to use the land for the erection of buildings in which he will run a factory, any proceeds derived from a subsequent sale of the land would be of a capital nature since the owner has changed his intention from one of a profit-making scheme to one of investment, so that the proceeds have resulted from the realization of an investment.
In deciding whether a taxpayer has changed his original intention in regard to a particular asset and has gone over to the business of selling that asset for profit, the courts will consider the history and activities of the taxpayer.
A change of intention requires something more than the mere decision to dispose of a capital asset, notwithstanding the fact that there may be protracted negotiations or hard bargaining in order to obtain the maximum price on a realization.

CAPITAL GAINS TAX

The provisions to determine a capital gain or capital loss are contained in the Eighth Schedule to the Income Tax Act.

Assets disposed of by a person, on or after 1 October 2001 (referred to as the valuation date), are subject to CGT, irrespective of whether those assets were acquired by that person before or after valuation date. But, only the capital gain or capital loss relating to the period subsequent to valuation date is subject to CGT.

Residents are subject to CGT on their world-wide assets. But non-residents are subject to CGT on only immovable property (including an interest or right in it) situated in the Republic and the assets of a permanent establishment situated in the Republic.

TAXABLE CAPITAL GAINS AND ASSESSED CAPITAL LOSSES

A person's capital gain or loss is determined, for each asset disposed, during the year of assessment as follows:

Proceeds	xx xxx
Less: base cost	x xxx
Capital gain or loss	xx xxx

A capital gain may be excluded, deferred, disregarded or attributed to another person. Special rules apply to capital losses. Capital losses may be offset against capital gains. Yet, capital losses may not be offset against other normal income. They must be carried forward to the subsequent year of assessment to be set off against future capital gains.

To calculate a taxable capital gain:

1. First, the sum of the all capital gains and losses for each asset (determined separately) disposed of during the year of assessment is determined.
2. Then the resulting total is reduced by an annual exclusion (R40 000) for a taxpayer who is a natural person or special trust, resulting in the aggregate capital gain or loss for the year of assessment.
3. An assessed capital loss brought forward from the previous year of assessment is then deducted from the aggregate capital gain or loss, resulting in a net capital gain or capital loss.
4. The net capital gain is then multiplied by an inclusion rate to determine the amount to be included in the taxpayer's taxable income.
5. A net capital loss is carried forward to the next year of assessment. It becomes an assessed capital loss.

The inclusion rate for a natural person or special trust is 40% and for a company or trust it is 80%

Example (natural person 2023 YOA)

Capital gains

Shares

Proceeds on disposal	2 300 000	
Less base cost	1 700 000	600 000

Block of flats

Proceeds on disposal	4 500 000	
Less base cost	4 600 000	-100 000
Sum of gains and losses		500 000
Less annual exclusion		40 000
Aggregate capital gain		460 000
Less assessed capital loss brought forward (assumed)		84 000
Net capital gain		376 000
		× 40%
Inclusion in taxable income – 40% of net capital gain		150 400

MAIN ELEMENTS OF CGT

Residence

Residents pay CGT on their worldwide assets

Non-residents only pay CGT on
- Immovable property in republic
- Interest in immovable property
- (see s35A)

The four building blocks of CGT are:

- An asset
- A disposal
- Proceeds
- Base Cost

A capital gain or a capital loss is made when proceeds or deemed proceeds arise on the disposal of an asset. A disposal is therefore the event that causes a potential liability for capital gains tax (CGT). It is therefore essential to identify when a disposal has occurred.

A disposal is any event, act, forbearance or operation of law which results in the creation, variation, transfer or extinction of an asset. Para 11 specifically includes as disposals a donation of an asset and the exchange (swap) of one asset for another.

Certain events are deemed to be disposals regardless of the nature of the event:

- Cessation of tax residence
- Death
- Amendment of the inclusion rate

TAXATION OF FOREIGN INCOME AND SET-OFF OF FOREIGN LOSSES

Due to the residence basis of taxation SA residents are taxed on foreign sourced income. A Double tax Treaty will in many instances alter this general principle and therefore must always be considered.

Foreign investments

The SA Reserve bank's exchange control provisions currently permit SA resident natural persons to transfer a maximum of R11 million out of SA for investment purposes each year, subject to certain provisions and tax clearances from SARS. Special provisions apply to companies.

The foreign investments may be divided into four broad categories:

- Deposits in foreign financial institutions producing foreign interest
- Fixed property producing foreign rental (see Foreign trade below)
- Shares producing foreign dividends
- Collective investment schemes/funds (CIS)

Foreign interest

There is no exemption from normal tax in respect of foreign interest.

Section 6quat provides a special rebate for foreign taxes payable, deductible from South African normal tax payable by a resident whose taxable income includes foreign interest. The rebate is limited to the amount of South African tax payable on that income.

Foreign trade (eg rental)

A SA resident carrying on trade as a sole proprietor outside SA will be liable for tax in the same way as if the trade were carried on in SA. The foreign trade income is converted in SA rands in terms of section 25D.

Should the income from the foreign trade not be capable of being remitted to SA (due to the laws of the country in which the foreign trade income was produced), section 9A ensures that the amount of foreign trade income will not be taxed in SA until it is remitted.

If the foreign trade results in an assessed loss, the foreign loss may be set off against other foreign trade income but not against any income form the carrying on of a trade in SA.

Taxation of dividends paid by foreign companies

Foreign dividends may be received from direct holding of shares in a foreign company by a taxpayer or through investing in a local CIS through which foreign dividends are earned.

A foreign CIS is regarded as a "foreign company" for the purposes of the income tax Act.

As a general rule, foreign dividends are included in the recipient's *gross income* and any portion of the amount that is not exempt will be taxed at the marginal/tax rates relevant to the specific recipient (that is, 28 percent for companies, up to 45 percent for individuals and 45 percent for Trusts).

Partial exemption section 10B(3)

The partial exemption formula rates are (wef 1 March 2017):

- the 25/45 exemption for natural persons and trusts and
- the 8/28 exemption for companies
- the 10/30 exemption where the person is an insurer in respect of its individual policyholder fund

Total exemption section 10B(2)

Foreign dividends are now subject to four total exemptions, the most relevant participation exemption is listed below:

- *10B(2)(a):* Under this exemption, foreign dividends will be exempt if received by or accrued to a person who holds at least ***10 percent*** of the equity shares and voting rights in the company declaring the foreign dividend.

Expenses to produce foreign dividends disallowed

In terms of section 23(q) the deduction of any expenses incurred to produce foreign dividends is disallowed. As a result, no deductions will be allowed for expenses incurred in relation to the acquisition of the foreign shares.

Section 25D

A natural person and a non-trading trust may elect that all amounts received by, or accrued to and all expenses incurred by that person (or non-trading trust) may be translated into rands by applying:

- The spot rate on the date the amount was received or accrued or the expense was incurred or;
- The average exchange rate for the relevant year of assessment

PARAGRAPH 32: Base cost of identical assets

Identical assets are:

- If any one of the assets sold would realise the same amount AND
- Assets can't be individually distinguished apart from identifying numbers they may bear

In respect of base cost a taxpayer must adopt:

1. Specific identification: using reference/identifying numbers or date of acquisition and cost, **OR**
2. FIFO: the oldest asset sold first, or
3. Weighted average

At present the weighted average method cannot be used for crypto assets. Weighted average is used for local and foreign listed shares and local and foreign CIS's.

PARAGRAPH 43: *Assets bought and sold in the same foreign currency*

Calculate the foreign gain or loss and translate into SA rands at:

- the average exchange rate for the year of assessment in which asset disposed of or;
- the spot rate at the date of disposal

Assets bought and sold in different currencies

Convert the base cost to rands:

- Spot rate on the date the expense of the base cost was incurred or;
- Average exchange rate for the year of assessment in the year that the expense of the base cost was incurred

Convert the proceeds to rands

- Spot rate on the date of disposal or;
- Average exchange rate for the year of assessment of the disposal

SECTION 9H: CEASING TO BE RESIDENT

Section 9H provides for a single charge when a person ceases to be a resident.

When a natural person ceases to be a resident, that person is deemed to have disposed of all their assets at market value on the day before that person ceases to be a resident and reacquired all those assets at an expenditure equal to that same market value on the day that person ceases to be a resident. This could trigger either a capital or a revenue gain. Subsection 9H(7) stipulates that the market value of such assets reacquired will be in the same currency in which the assets were originally acquired.

SA immovable property

In terms of section 9H(4), certain assets are excluded from this deemed disposal, the most relevant being immovable property situated in the Republic.

Year of assessment

In terms of section 9H, when a taxpayer ceases to be tax resident, their year of assessment is deemed to have ended on the date immediately before the day on which the taxpayer ceased to be resident. The next succeeding year of assessment will be deemed to start on the day the taxpayer ceases to be resident.

OFFSHORE TRUSTS

Tax residence of company or trust

For a person other than a natural person, a resident is an entity that is incorporated, established or formed in the Republic or which has its place of effective management in the Republic.

This means that to be a non-resident, the entity must not be

- incorporated,
- established or formed, or
- have its place of effective management in the Republic.

All three of these requirements must be performed outside the Republic.

Normal Tax Provisions

Section 25B(1) and (2)

The combined application of the provisions of section 7 and section 25B ensure that the receipts and accruals of a trust are going to be included in the gross income (or income) of any one, or more, of

- its 'creator', to the extent that the provisions of section 7 apply,
- its beneficiaries, if the provisions of section 25B(1) or (2) apply, or
- itself, again if the provisions of section 25B(1) apply.

In terms of section 25B(3) the deductions and allowances that the trust is entitled to, are then granted to its 'creator', its beneficiaries, or itself, on exactly the same basis as its receipts and accruals have been allocated.

If the 'creator' of the trust is a resident, and if the receipts and accruals of the trust accrue or are deemed to accrue to him in terms of section 7, then despite these receipts and accruals being from a non-South African source, they will be included in his income. Being a resident his world-wide receipts and accruals are included in his gross income (or income).

If a beneficiary of the trust is a resident, and if the receipts and accruals of the trust accrue or are deemed to accrue to him in terms of section 25B(1) or (2), then despite these receipts and accruals being from a non-South African source, they will be included in his income. Being a resident his world-wide receipts and accruals are included in his gross income (or income).

As indicated above, if the receipts and accruals of the offshore trust are deemed to be its own receipts and accruals in terms of section 25B(1), then because they are deemed to accrue to a non-resident, and because they are from a non-South African source, they will not be included in its gross income. For a non-resident to include an amount in his gross income it must be from a Republic true or deemed source.

The provisions of section 25B(1) provide that when any amount is received by or accrues to or in favour of any person in his capacity as the trustee of a trust fund, it is deemed to be an amount that has accrued to an ascertained beneficiary with a vested right to it, to the extent that it has been derived for his (the beneficiary's) immediate or future benefit.

In terms of section 25B(2), when a beneficiary has acquired a vested right to any amount referred to in section 25B(1) in consequence of the exercise by the trustee of a discretion vested in him in terms of the trust deed, agreement or will, this amount is for the purposes of section 25B(1) deemed to have been derived for his (the beneficiary's) benefit.

To the extent that any amount received by or accrued to or in favour of the trustee has not been derived for the immediate or future benefit of an ascertained beneficiary with a vested right to it – in other words, the beneficiary has only a contingent right to it – it will be deemed to be an amount that accrues to the trust (section 25B(1)). The trustee will be liable for the tax on this amount in a representative capacity.

Section 25B(1) is made subject to the provisions of section 7. This provision deems the income derived by a trustee in consequence of a 'donation, settlement or other [similar] disposition' to be the income of the donor. It should be noted that the provisions of section 7 are unlikely to apply to a testamentary trust as in most instances a donation, settlement or other similar disposition would not have taken place.

From the above discussion, it follows that the receipts and accruals of an offshore trust will not be taxed in South Africa provided that

- they are not deemed to accrue to a resident 'creator' in terms of the provisions of section 7, and
- no resident beneficiary has a vested right to them (section 25B(1)), or has acquired a vested right to them in terms of section 25B(2) because the trustees of a discretionary trust have now exercised their discretion and have agreed to award an amount to the beneficiary.

It would not be difficult for the 'creator' to ensure that the provisions of section 25B(1) or (2) do not apply to a resident beneficiary. The trust deed must make it clear that a resident beneficiary does not have a vested right to the receipts and accruals of the trust. And then the provisions of section 25B(2) can easily be avoided by ensuring that the trustees do not exercise their discretion and award an amount to a resident beneficiary.

How the 'creator' avoids the provisions of section 7 applying to him is not at all clear. It is likely that the receipts and accruals of the offshore trust are not going to vest in a beneficiary. And it is also likely they are not going to be awarded to a beneficiary. They are simply going to be retained in the trust for the benefit of some future beneficiary. It would therefore seem that this is the precise situation that will bring the provisions of section 7(5) into operation.

Section 7(5)

Section 7(5) provides that if any person (a 'creator') has made any donation, settlement or other similar disposition that is subject to a stipulation or condition, whether made or imposed by him or anybody else, to the effect that a beneficiary will not receive the income or some portion of it until the happening of some event, whether fixed or contingent, so much of any income as would, but for this stipulation or condition, in consequence of the donation, settlement or other similar disposition be received by or accrue to or in favour of the beneficiary, must, until the happening of that event or his death (the 'creator's' death), whichever takes place first, be deemed to be his (the 'creator's') income.

Included in section 7(5) is the term 'any donation, settlement or other [similar] disposition'. This term is not defined in the Act but the following principles have been laid down:

- The term 'any donation, settlement or other [similar] disposition' as used in section 7 excludes any disposal of property made for due consideration.
- The word 'disposition' means any disposal of property made wholly or to an appreciable extent gratuitously out of the liberality or generosity of the disposer.
- When there is a settlement or other disposition for some consideration but there is also an appreciable element of gratuitousness, the resulting income may be apportioned between these two elements. If no apportionment is possible, or if the taxpayer fails to produce evidence to justify an apportionment, the

whole of the income must be regarded as having been derived by the beneficiary by reason of a gratuitous disposition.[4]

In addition the court has held that the word 'disposition' as used in section 7 is *ejusdem generis* with the word 'donation' and 'settlement' in the provision and does not include a transaction made for full value.[5]

Trollip JA who delivered the judgment in *Ovenstone v SIR* said the following on what is meant by the word 'disposition' when it is used in section 7:[6]

> 'Hence, the words "donation, settlement or other disposition" all have this feature in common: they each connote the disposal of property to another otherwise than for due consideration, i.e. otherwise than commercially or in the course of business. "Donation" and "settlement" have this further feature in common: the disposal of property is made gratuitously or (occasionally in the case of a "settlement") gratuitously to an appreciable extent. Since "disposition", the general word that rounds off the critical phrase, was not intended to have its wide, unrestricted meaning, I think that this is an appropriate situation in that to circumscribe its scope by extending that common element of gratuitousness to it too by the *ejusdem generis* or *noscitur a sociis* rule. The critical phrase should, in other words, be read as "any donation, settlement or other similar disposition".
>
> 'So construed, "disposition" means any disposal of property made wholly or to an appreciable extent gratuitously out of the liberality or generosity of the disposer.'

As this expression covers any disposal of property made wholly gratuitously out of liberality or generosity it must cover all situations when a transaction contains an element of gift.

It would therefore seem that the only way that the 'creator' could stop the provisions of section 7(5) from applying is to ensure that there has not been a donation, settlement or other 'similar' disposition. As the 'creator' has set up the offshore trust, it seems inevitable that an element of a gift would exist.

Section 7(8)

The provisions of section 7(8)(*a*) apply when

- there has been a donation, settlement or other similar disposition (other than a donation, settlement or other similar disposition to an entity that is not a resident and is similar to a public benefit organisation contemplated in section 30);
- the donation, settlement or other similar disposition was made by a 'resident', as defined;
- in consequence of which an amount is received by or accrued to a person who is not a resident (other than a controlled foreign company in relation to the resident).

When these requirements are met, the resident must include in his income so much of the amount of any income as is attributable to the donation, settlement or other similar disposition.

Section 7(9) deems a donation to arise in certain circumstances for the purposes of section 7. It provides that when an asset has been disposed of for a consideration that is less than its market value, the amount by which its market value exceeds the consideration will for the purposes of section 7 be deemed to be a donation. What this means in the context of section 7(8), is that a donation will be deemed to arise when an asset is disposed of by a resident to a non-resident for less than its market value.

Section 7(8) does not deem the amount to be received by or accrued to the resident donor, to be the income of that donor. The section merely requires that the amount be included in the income of the resident donor. This

4 *Ovenstone v SIR* 1980 (2) SA 721 (A), 42 SATC 55.
5 *Joss v SIR* 1980 (1) SA 674 (T), 41 SATC 206.
6 At SATC 55.

means that for tax purposes the amount still accrues to the non-resident to whom it goes, and as such, if the amount is income from a South African source, the non-resident will also be subject to tax on that amount. This is regarded as an economic double tax from which there is no relief.

Paragraph (*b*) was introduced as an amendment in 2005, to allow the resident donor deductions in respect of the amount that is deemed to be included in the income of the resident donor due to provisions of section 7(8)(*a)*.

Section 7(8)(*b*) provides as follows:

- Any amount incurred by the person contemplated in section 7(8)
- in relation to the amount received or accrued to that person
- must be deemed to have been incurred by the resident in whose income the amount is included.

Therefore where the amount is included in the income of the resident donor in terms of section 7(8)(*a*), section 7(8)(*b*) deems the amount to be incurred by the resident donor. The normal deduction rules must then be applied to claim a deduction.

SECTION 25B(2A)

If the receipts and accruals of an offshore trust are not caused by a donation, settlement or other similar disposition then the provisions of section 7 will not apply. Then provided the receipts and accruals are not from a South African source and provided no resident beneficiary has a vested right to them, they may escape Republic taxation.

The word ‘may’ is used because if the provisions of section 25B(2A) then apply, a resident beneficiary is going to be taxed in the Republic on the receipts and accruals (or some form of them).

The provisions of section 25B(2A) apply when a resident acquires a vested right to any amount representing capital of a non-resident trust if

- this capital arose (directly or indirectly) from any receipts or accruals of the trust that would have constituted income had the trust been a resident, during any previous year of assessment in which the resident had only a contingent right to that amount, and
- that amount was not previously subject to tax in the Republic.

When a resident acquires a vested right to an amount of capital, then in terms of section 25B(2A), the amount is included in the income of the resident in the year of assessment in which the resident acquires this vested right.

Para 80(3) Eighth Schedule

Para 80(3) Eighth Schedule ensures the same tax consequence in respect of any capital gains arising in the non-resident trust, when the contingent beneficiary obtains a vested right to the relevant capital gain. Para 80(3) will cause the relevant capital gain be taken into account where determining the aggregate capital gain or aggregate capital loss of the resident beneficiary in the year of assessment that the resident beneficiary obtains a vested right to the capital gain.

International Retirement Annuity Trust

An international retirement annuity trust is a vehicle that is set up in certain offshore jurisdictions for example Guernsey, Malta or Gibraltar. These retirement trusts are generally unapproved retirement annuity trust schemes and may be regarded more as a retirement savings plan than a retirement fund as recognized in terms of the South African retirement fund legislation. Most retirement trusts are based on a master trust deed and each plan has its own member issued Letter of Wishes. The Letter of Wishes provides direction to the Trustee as to how the member would have wished to distribute any remaining assets held in the retirement trust. The distribution of the remaining assets in the retirement trust is at the discretion of the Trustee.

Any contributions to a retirement annuity trust will not be deductible in terms of section 11F of the Income Tax Act and the provisions of the Second Schedule which apply to lump sum payments from retirement funds, do not apply.

An international retirement annuity trust will be regarded as a non-resident trust as long as the place of effective management remains outside South Africa.

ITR12 DISCLOSURE

Was any income distributed to you / vested in you as a beneficiary of a trust, or deemed to have accrued in terms of s7 ? Y ◯ N ◯

Indicate the number of trust(s) applicable? Number of trusts

Trust Income – Income distributed to you / vested in you as a beneficiary of a trust or deemed to have accrued in terms of s7 ^

Trust Details ^

Trust Name

Trust Registration Number | Trust Tax Reference Number

Details of **Local Income** ^

R Local Remuneration	Source Code	R Distributions from Real Estate Investment Trust/s (REIT)	4238	R Local Business and Trading Income (excluding Rental Income from letting of fixed property(ies) and income from Farming Operations)	Source Code

Details of **Local Income**

R Local Annuities	Source Code	R Local Capital Gain / Loss	Source Code	R Income from Local Farming Operations (IT48)	Source Code
R Local Interest	4201	R Local Rental Income from the letting of fixed property(ies)	4210	R Deemed Annuity	3611
R SARS Interest	4237	R Dividends deemed to be income in terms of s8E and s8EA	4292	R Other Local Income	Source Code

Details of **Foreign Income** ^

R Foreign Interest	4218	R Foreign Capital Gain / Loss	Source Code	R Imputed Net Income from Controlled Foreign Companies (CFC)	4276
R Foreign Tax Credits on Foreign Interest	4113	R Foreign Tax Credits i.r.o. Capital Gain / Loss	4114	R Foreign Tax Credit on Imputed Net Income from Controlled Foreign Companies (CFC)	4122
R Foreign Dividends	4216	R Foreign Farming	0192	R Other Foreign Income	4220
R Foreign Tax Credits on Foreign Dividends	4112	R Foreign Tax Credits on Foreign Farming Income	4119	R Foreign Tax Credits on other Foreign Income	4110

AUTOMATIC EXCHANGE OF FINANCIAL ACCOUNT INFORMATION

EXCHANGE OF INFORMATION CONVENTIONS / AGREEMENTS

South Africa is a member of the Global Forum on Transparency and Exchange of Information for Tax Purposes. It has been confirmed that South Africa has undertaken to exchange information automatically in relation to new accounts and pre-existing individual high value accounts by the end of September 2017.

The Exchange of Information Conventions/Agreements/Standards are divided into these categories:

- USA FATCA Intergovernmental Agreement
- Multilateral Mutual Administrative Assistance (MAA) Conventions / Agreements
- Bilateral Tax Information Exchange Agreements (TIEAs)
- Standard for Automatic Exchange of Financial Account Information in Tax Matters (CRS)

The **USA FATCA Intergovernmental Agreement** is an agreement between the governments (tax administrations) of the United States of America and the Republic of South Africa to exchange information automatically under the provisions of the double taxation agreement between these countries.

The **Standard for Automatic Exchange of Financial Account Information in Tax Matters** (also referred to as the Common Reporting Standard or CRS) is the Global Model for automatic exchange of information under the Multilateral Competent Authority Convention to which South Africa is a signatory.

The **CRS** is a standardised automatic exchange model, which builds on the FATCA Inter Governmental Agreement to maximise efficiency and minimise costs, except that the ambit is now extended to all foreign held accounts and not only those of US citizens. South Africa is also one of the early adopters of the CRS and is committed to commence exchange of information automatically on a wider front from 2017, together with over 90 other jurisdictions.

THE COMMON REPORTING STANDARD

The Common Reporting Standard means that the holding of funds off-shore that have not been declared to SARS will no longer be an option for SA residents. The principle of bank-secrecy is being terminated as a result of measures being taken to prevent offshore tax-evasion.

Common Reporting Standard (CRS)

The Standard for Automatic Exchange of Financial Account Information in Tax Matters (also referred to as the Common Reporting Standard or CRS) is the Global Model for automatic exchange of information under the Multilateral Competent Authority Convention to which South Africa is a signatory.

The CRS is a ‘universal code’ of reporting aimed at incorporating as many jurisdictions possible on a mutually beneficial basis. Jurisdictions will each disclose information to each other. For example, if SA, France and the UK are all signatories to the CRS, the UK would have to report to SA or France on any accounts held by SA or French tax residents with financial institutions situated in the UK and vice-versa.

Early adopters

The CRS was initially adopted by over 40 jurisdictions, known as the “Early Adopters”. The Early Adopters group will start reporting in terms of the CRS in September 2017. SA is included in this group. Other jurisdictions which form part of this group include Luxembourg, Liechtenstein, Malta, Cyprus, the UK, the UK’s Crown Dependencies of Isle of Man, Guernsey and Jersey, the UK Overseas Territories, France, Germany, Greece, India, Ireland, Italy, the Netherlands, Norway, Portugal, Spain, Sweden.

The rest of the signatory states will start reporting in 2018. This second-phase group includes Switzerland, UAE, Mauritius, Hong Kong, Singapore, Macao, Monaco, Antigua and Barbuda, the Bahamas, as well as Australia, New Zealand and Canada.

Reportable information

Reportable information will be required to be exchanged with other countries under the agreement is as follows:

- the name, address, tax identification number and date and place of birth in the case of an individual
- the account number
- the name and identifying number of the reporting financial institution
- the account balance or value as of the end of the relevant calendar year or other appropriate reporting period
- ·the total amount paid or credited to the account holder with respect to the account during the calendar year or other period as the case may be

The CRS defines the information that is required to be shared, the financial institutions required to report, the types of people that are subject to information exchange and defines the procedures that financial institutions must follow.

The scope of ‘reportable accounts’ information extends beyond offshore bank or investment accounts and includes information relating to beneficiaries and settlors of offshore trusts.

Establishing a trust in a state which is not party to the CRS is also no guarantee of escape, since any account held by such trust with a bank situated in a CRS-signatory state, for example, will require the trustees to disclose the identity of the trust’s beneficiaries, settlors and protectors to the bank, which in turn will disclose the information under the CRS.

Unlike settlors, however, discretionary beneficiaries who have no further interest in the trust do not automatically fall into the reporting net. They would only be caught if a distribution was made to them within the relevant reporting calendar year.

Implications for SA residents

The implementation of the CRS will have many implications for SA tax residents.

- Focuses mostly on SA tax resident individuals holding investments and having accounts with a “financial institution” in a foreign signatory country
- SARS is likely to discover any undeclared offshore funds, which could result in criminal prosecution and understatement penalties of up to 200% in terms of the Tax Administration Act.
- SARS will gain access to an excessive amount of information relating to SA residents’ offshore transactions and structures. Residents with such structures must ensure they are tax and excon compliant.
- SARS in terms of Vision 2024 will have the IT capacity using artificial intelligence, “super computers” and specifically trained staff to process and utilise the information to address non-compliance.

LOANS TO TRUSTS- DEEMED DONATION

Insertion of section 7C in Act 58 of 1962

7C. Loan or credit advanced to a trust by a connected person.—(1) This section applies in respect of any loan, advance or credit that—

(a) a natural person; or

(b) at the instance of that person, a company in relation to which that person is a connected person in terms of paragraph (*d*) (iv) of the definition of connected person,

directly or indirectly provides to—

(i) a trust in relation to which—

(*aa*) that person or company; or

(*bb*) any person that is a connected person in relation to the person or company referred to in item (*aa*),

is a connected person; or

(ii) a company if at least 20 per cent of—

(*aa*) the equity shares in that company are held, directly or indirectly; or

(*bb*) the voting rights in that company can be exercised,

by the trust referred to in subparagraph (i) whether alone or together with any person who is a beneficiary of that trust or the spouse of a beneficiary of that trust or any person related to that beneficiary or that spouse within the second degree of consanguinity [*Sub-s. (1) amended by s. 5 (1) (a) of Act No. 17 of 2017 deemed to have come into operation on 19 July, 2017 and applicable in respect of any amount owed by a trust or a company in respect of a loan, advance or credit provided to that trust or that company before, on or after that date*.]

(1A) If a person acquires a claim to an amount owing by a trust or a company in respect of a loan, advance or credit referred to in subsection (1), that person must for purposes of this section be treated as having provided a loan, advance or credit to that trust or company—

(a) on the date on which that person acquired that claim; or

(b) if that person was not a connected person on that date in relation to—

(i) that trust; or

(ii) the person who provided that loan, advance or credit to that trust or company,

on the date on which that person became a connected person in relation to that trust or person, that is equal to the amount of the claim so acquired.

[*Sub-s. (1A) inserted by s. 5 (1) (b) of Act No. 17 of 2017 deemed to have come into operation on 19 July, 2017 and applicable in respect of any amount owed by a trust or a company in respect of a loan, advance or credit provided to that trust or that company before, on or after that date*.]

(1B) Where—

(a) a natural person; or

(b) at the instance of a natural person, a company that is a connected person in relation to that natural person in terms of paragraph (d)(iv) of the definition of 'connected person',

subscribes for a preference share in a company in which 20 per cent or more of the equity shares are held (whether directly or indirectly) or the voting rights can be exercised by a trust that is a connected person in relation to that natural person or to that company, whether alone or together with any person who is a beneficiary of that trust—

(i) consideration received by or accrued to that company for the issue of that preference share shall be deemed to be a loan for the purposes of subsection (3); and

(ii) any dividend or foreign dividend accrued in respect of that preference share shall be deemed to be interest in respect of the loan contemplated in paragraph (i).

(TLAA 2020 WEF 1 January 2021, applicable to any dividend of foreign dividend accruing during any year of assessment commencing on or after that date)

(2) No deduction, loss, allowance or capital loss may be claimed in respect of—

(a) a disposal, including by way of a reduction or waiver; or

(b) the failure, wholly or partly, of a claim for the payment,

of any amount owing in respect of a loan, advance or credit referred to in subsection (1).

(3) If a trust or company incurs—

(a) no interest in respect of a loan, advance or credit referred to in subsection (1) , (1A) or (1B)

(b) interest at a rate lower than the official rate of interest,

an amount equal to the difference between the amount incurred by that trust or company during a year of assessment as interest in respect of that loan, advance or credit and the amount that would have been incurred by that trust or company at the official rate of interest must, for purposes of Part V of Chapter II, be treated as a donation made to that trust by the person referred to in subsection (1) (*a*), (1A) or (1B) on the last day of that year of assessment of that trust.

(4) If a loan, advance or credit was provided by a company to a trust or another company at the instance of more than one person that is a connected person in relation to that company as referred to in paragraph (*b*) of subsection (1), each of those persons must be treated as having donated, to that trust or company, the part of that amount that bears to that amount the same ratio as the equity shares or voting rights in that company that were held by that person during that year of assessment bears to the equity shares or voting rights in that company held in aggregate by those persons during that year of assessment.

(5) Subsections (2) and (3) do not apply in respect of any amount owing by a trust or company during a year of assessment in respect of a loan, advance or credit referred to in subsection (1) if—

(a) that trust or company is a public benefit organisation approved by the Commissioner in terms of section 30 (3) or a small business funding entity approved by the Commissioner in terms of section 30C;

(b) that loan, advance or credit was provided to that trust by a person by reason of or in return for a vested interest held by that person in the receipts and accruals and assets of that trust and—

(i) the beneficiaries of that trust hold, in aggregate, a vested interest in all the receipts and accruals and assets of that trust;

(ii) no beneficiary of that trust can, in terms of the trust deed governing that trust, hold or acquire an interest in that trust other than a vested interest in the receipts and accruals and assets of that trust;

(iii) the vested interest of each beneficiary of that trust is determined solely with reference and in proportion to the assets, services or funding contributed by that beneficiary to that trust; and

(iv) none of the vested interests held by the beneficiaries of that trust is subject to a discretionary power conferred on any person in terms of which that interest can be varied or revoked;

(c) that trust is a special trust as defined in paragraph (*a*) of the definition of a special trust;

(d) that trust or company used that loan, advance or credit wholly or partly for purposes of funding the acquisition of an asset and—

(i) the person referred to in subsection (1) (*a*) or the spouse of that person used that asset as a primary residence as contemplated in paragraph (*b*) of the definition of ―primary residence‖ in paragraph 44 of the Eighth Schedule throughout the period during that year of assessment during which that trust or company held that asset; and

(ii) the amount owed relates to the part of that loan, advance or credit that funded the acquisition of that asset;

(e) that loan, advance or credit constitutes an affected transaction as defined in section 31 (1) that is subject to the provisions of that section;

(f) that loan, advance or credit was provided to that trust or company in terms of an arrangement that would have qualified as a sharia compliant financing arrangement as contemplated in section 24JA, had that trust or company been a bank as defined in that section;

(g) Loan advance or credit subject to section 64E(4)

(h) ………………………………………….

OFFICIAL RATE OF INTEREST

The "official rate" is now defined in section 1 of the Income Tax Act is specifically linked to the repurchase rate (repo rate). The official rate is adjusted at the beginning of the month following the month during which the Reserve Bank changes the repurchase rate.

- ***Debt in Rands:***

  Rate of interest equal to the SA Repo rate plus 100 basis points

  - 1 Aug 2017-31 March 2018: **7.75%**
  - 1 April 2018-30 November 2018: **7.5%**
  - 1 December 2018-31 July 2019: **7.75%**
  - 1 August 2019 – 31 January 2020 **7.5%**
  - 1 February 2020 -31 March 2020 **7.25%**
  - 1 April 2020 – 30 April 2020 **6.25%**
  - 1 May 2020 – 31 May 2020 **5.25%**
  - 1 June 2020 – 31 July 2020 **4.75%**
  - 1 August 2020 – 30 November 2021 **4.5%**
  - 1 December 2021 – 31 January 2022 **4.75%**
  - 1 February 2022 – 31 March 2022 **5%**
  - 1 April 2022 –until there is a change in the repo rate **5.25%**

- ***Debt in foreign currency***

  Rate of interest that is the equivalent of the SA repo rate applicable in that currency plus 100 basis points

***Example* deemed donation 2021 YOA**

Assume a resident natural person made an interest free loan to a Trust of R5 million. The natural person is a connected person to the trust. Assume the natural person made no other donations during the 2021 YOA.

Deemed donation at 28 February 2021:

5000 000 x 7.25% x 1/12 = 30 208

5000 000 x 6.25% x 1/12 = 26 041

5000 000 x 5.25% x 1/12 = 21 875

5000 000 x 4.75% x 2/12 = 39 583

5000 000 x 4.5% x 7/12 = 131 250

Total	248 957
(Less (s56(2)(b))	100 000)
Total deemed donation	**148 957**

Donations tax payable by 31 March 2021

DONATIONS TAX

All sections referred to in this chapter are from the Income Tax Act (the Act).

Non residents

Non-residents are not liable for donations tax even in respect of the donation of assets situated in South Africa, bearing in mind that such assets would attract estate duty.

Donations tax

Donations tax is levied in terms of Part V of the Income Tax Act. Section 54 subjects to donations tax donations made by any "resident". Donations tax is levied at a flat rate of 20% until the cumulative donations made exceed R30 million. After this point, donations will attract a 25% tax rate.

Deemed donations

Section 58 provides that donations for this purpose include property disposed of for what, in the opinion of the Commissioner, is an inadequate consideration, to the extent of that inadequacy.

Meaning of "donation"

A donation is defined as:

"Any gratuitous disposal of property including any gratuitous waiver or renunciation of a right" (section 55(1)).

Property in the definition of "donation" means "any right in or to property movable or immovable, corporeal or incorporeal, wheresoever situated".

The common law definition of a donation requires the following essential characteristics:

- A contract between donor and donee;
- a promise by the donor to give something to the donee, or such a gift;
- as the motive of the donor is that of pure liberality, no consideration from the donee can be involved;
- the donation impoverishes the donor's estate and enriches that of the donee.

Property disposed of for any inadequate consideration

Section 58 reads as follows:

"Where any property has been disposed of for a consideration which, in the opinion of the Commissioner, is not an adequate consideration that property shall for the purposes of this Part be deemed to have been disposed of under a donation: Provided that in the determination of the value of such property a reduction shall be made of an amount equal to the value of the said consideration."

Effective date of a donation

A donation is deemed to take effect on the date on which the legal formalities for a valid donation are complied with (section 55(3)).

Exemptions from donations tax

Certain categories of donations are exempt from donations tax:

- Donations to or for the benefit of the spouse of the donor under a duly registered antenuptial contract or post-nuptial contract or under a notarial contract entered into as contemplated in section 21 of the Matrimonial Property Act, 1984 (Act 88 of 1984) (section 56(1)(*a*));

- donations to or for the benefit of the spouse of the donor who is not separated from him under a judicial order or notarial deed of separation (section 56(1)(*b*));
- donations made as a *donatio mortis causa*, that is, in contemplation of death (section 56(1)(*c*));
- donations in terms of which the donee will not obtain any benefit thereunder until the death of the donor (section 56(1)(*d*))
- donations cancelled within six months of taking effect (section 56(1)(*e*);
- where the property donated consists of any right in property situated outside the Republic (what may loosely be called "foreign property") and it was acquired by the donor:

– before the donor became a resident of the Republic for the first time; or

– by inheritance from a person who at the date of his death was not ordinarily resident in the Republic, or by a donation if at the date of the donation the donor was a person (other than a company) not ordinarily resident in South Africa (section 56(1)(*g*)(ii)); or

– out of funds derived by him from the disposal of any property referred to in the above two sub-paragraphs or, if the donor disposed of such last-mentioned property and replaced it with other properties (all situated outside the Republic and acquired by the donor out of funds derived from the disposal of any of the said properties), out of funds derived by him from the disposal of, or revenue from, any of those properties (section 56(1)(*g*)(iii));

- donations *by or to* certain essentially non-profit making institutions which are themselves exempt from income tax (section 56(1)(*h*));
- property which is a voluntary award for services rendered and is required to be included in the recipient's gross income or the gain in respect of which must be included in the income of the donee in terms of sections 8A, 8B or 8C (section 56(1)(*k*)); or
- property which is disposed of under or in pursuance of any trust (section 56(1)(*l*)). This means that distributions by a trust, whether of income or capital, are free of donations tax; or
- donations of the right of the use or occupation of land used for farming purposes to a child of the donor, provided that this right is not a fiduciary, usufructuary or like interest (section 56(1)(*m*)); or
- donations by any company recognised as a public company for tax purposes (section 56(1)(*n*)); or
- donations of immovable property made in terms of an approved land reform programme project (section 56(1) (*o*));
- property disposed of to any other company that is a resident and is a member of the same group of companies as the company making that donation (section 56(1)(*r*)).

In addition, the following are exempt from donations tax:

- *Bona fide* payments towards the maintenance of any person, to the extent to which the Commissioner considers these to be reasonable (section 56(2)(*c*)). Maintenance paid to a dependent via a trust is an exempt donation;
- casual gifts such as wedding, birthday or Christmas gifts which do not exceed R10 000 in any given year of assessment, where the donor is not a natural person. For periods of assessment of less than a year, this amount is reduced on a *pro rata* basis (section 56(2)(*a*)); and
- donations made by a natural person up to a maximum of R100 000 in respect of each year of assessment. It should be noted that this R100 000 per annum threshold is available to each spouse. Accordingly, a married couple may freely dispose of property worth up to R200 000 per annum without being subject to donations tax (section 56(2)(b).

Where the donated property formed part of the joint estate, each spouse is deemed to have made half the donation. Where the donated property is excluded from the joint estate, the donation is deemed to have been made solely by the donor spouse (section 57A).

Interest-free loans section 7C

Interest-free and low-interest loans, which are very common in estate plans must be carefully examined in order to determine if a deemed donation is triggered in terms of section 7C.

L**iability for and payment of donations tax**

The tax is payable by the donor. However, if the donor fails to pay within the stipulated time period, both the donor and the donee become jointly and severally liable for the tax (section 59).

Where any property is disposed of under a donation by any body corporate at the instance of any person, the person at whose instance the donation is made, is deemed to have made the donation (section 57(1)). Thus the latter is liable for the tax. However, the deemed donor in such circumstances may recover the tax from the body corporate. Property is deemed to be disposed of at the instance of a person if, having regard to the circumstances under which the body corporate made the donation, the Commissioner is of the opinion:

- That it was not made in the ordinary course of the normal income earning operations of that body corporate; and
- that the selection of the donee who benefited by the donation was made at the instance of that person (section 57(2)).

Donations tax is payable by the end of the month, following the month during which the donation took effect (section 60(1)). Payment of the tax must be accompanied by an IT144 return (section 60(4)).

Donations to a trust

Donations to a trust by a resident are subject to the donations tax provisions applicable to donations by a resident generally. It is not possible to argue that a donation to a trustee is not a donation because the trustee does not benefit from the donation.

SECTION 9HB. TRANSFER OF ASSET BETWEEN SPOUSES.—

(1)(*a*) A person (hereinafter referred to as "the transferor") must disregard any capital gain or capital loss determined in respect of the disposal of an asset to his or her spouse (hereinafter referred to as "the transferee").

(b) The transferee must be treated as having—

(i) acquired the asset on the same date that such asset was acquired by the transferor;

(ii) incurred an amount of expenditure equal to the expenditure contemplated in paragraph 20 of the Eighth Schedule that was incurred by that transferor in respectof that asset;

(iii) incurred that expenditure on the same date and in the same currency that it was incurred by the transferor;

(iv) used that asset in the same manner that it was used by the transferor; and

(v) received an amount equal to any amount received by or accrued to that transferor in respect of that asset that would have constituted proceeds on disposal of that asset had that transferor disposed of it to a person other than the transferee.

(2) For the purposes of subsection (1)—

(a) a person whose spouse dies must be treated as having disposed of an asset to that spouse immediately before the date of death of that spouse, if ownership of that asset is acquired by the deceased estate of that spouse in settlement of a claim arising undersection 3 of the Matrimonial Property Act, 1984 (Act No. 88 of 1984); or

(b) a person must be treated as having disposed of an asset to his or her spouse, if that asset is transferred to that spouse in consequence of a divorce order or, in the case of a union contemplated in paragraph (*b*) or (*c*) of the definition of "spouse" in section 1, an agreement of division of assets which has been made an order of court.

(3) A person who disposes of an asset consisting of trading stock, livestock or produce contemplated in the First Schedule to his or her spouse, must be treated as having disposed of that asset for an amount received or accrued that is equal to the amount that was allowed as a deduction inrespect of that asset for purposes of determining that person's taxable income, before the inclusion of any taxable capital gain.

(4) Where a person acquires an asset consisting of trading stock, livestock or produce contemplated in the First Schedule from his or her spouse, that person and his or her spouse must, for purposes of determining any taxable income derived by that person, be deemed to be one and the same person with respect to the date of acquisition of that asset by that person and the amount and date of incurral by that spouse of any cost or expenditure incurred in respect of that asset as contemplated in section 11(*a*) or 22(1) or (2).

(5) ***This section must not apply in respect of the disposal of an asset by a person to his or her spouse who is not a resident, unless the asset disposed of is an asset contemplated in section 9J or inparagraph 2(1)(b) of the Eighth Schedule.***

SECTION 9HA DISPOSAL TO AND FROM DECEASED ESTATE

APPLICABLE TO PERSONS DYING ON OR AFTER 1 MARCH 2016

Disposal by a deceased person: Section 9HA(1)

In terms of section 9HA(1), a person who dies on or after 1 March 2016 is deemed to have disposed of his or her assets at the date of the persons death for an amount received or accrued equal to the market value of the assets at that date (market value as per para 31 in the Eighth schedule).

In terms of section 9H(3) if any asset which is deemed to have been so disposed of is transferred directly to an heir or legatee of the deceased, that heir or legatee (*other than a resident surviving spouse*) is deemed to have acquired the asset for an amount of expenditure equal to the market value of the asset at the date of death of the deceased.

Exclusions from deemed disposal

The following assets are *not deemed* to have been disposed of:

- A long term insurance policy of the deceased if any capital gain or loss that would have been determined in respect of a disposal that resulted in proceeds of that policy being received by or accruing to the deceased would have been disregarded in terms of para 55 (see Annexure B) of the Eighth Schedule, and
- An interest of the deceased in a pension, pension preservation, provident, provident preservation or retirement annuity fund (in or outside the Republic), if any capital gain or loss that would have been determined in respect of a disposal of that interest that resulted in a lump sum benefit being received by or accruing to the deceased would have been disregarded in terms of para 54 (see Annexure B) of the Eighth Schedule.

Recoupment of allowances previously claimed

The effect of the deemed disposal provisions of section 9HA(1) is that recoupments may be included in the gross income of the deceased person in terms of section 8(4)(a) should the deceased be the owner of depreciable assets at date of death of the deceased on which tax allowances were claimed.

Section 9HA(2) Assets bequeathed to resident surviving spouse

In terms of this section, a deceased is deemed to have disposed of assets to a **resident** surviving spouse if those assets are acquired by the surviving spouse in terms of the will of the deceased, the laws of intestate succession, re-distribution agreement between heirs and legatees of that person in the course of winding up the deceased estate or a re-distribution agreement in terms of section 3 of the Matrimonial Property Act (1984).

Section 9HA(2)(b)

The deemed disposal of an asset to a resident surviving spouse will be for an amount received or accrued (to the deceased) that is equal to, in the case of:

- Trading stock, or livestock or produce as contemplated in the First Schedule, the amount that was allowed as a deduction in respect of that asset for the purposes of determining that persons taxable income, before the inclusion of ant taxable gain, for the year of assessment ending on or after the date of that person's death; or
- Any other asset, the base cost of the asset as determined in terms of para 20 of the Eighth Schedule.

As a result there will be no recoupment in the hands of the deceased in respect of trading stock or other business assets (on which capital allowances were claimed) transferred to a surviving spouse, while the capital gain or loss in respect of an asset is rolled over to the surviving spouse, resulting in a capital gain for the deceased of NIL.

Summary

- Asset transferred to heir or legatee (not *resident* surviving spouse), deceased treated as having disposed of asset at market value: If the market value of the asset at date of death of deceased was R300 000, and the base cost R100 000, a capital gain of R200 000 (proceeds of R300 000 less base cost of R100 000) would have to be taken into account in the deceased person's last assessment.
- Same asset as above transferred to a resident surviving spouse, deceased treated as having disposed of asset at an amount equal to the base cost of the asset: Proceeds from the disposal will be R100 000 less the base cost of the asset R100 000, and the capital gain will be NIL

(DRAFT IN NOTES SARS on sections 9HA and 9HB)

The deceased person will also be entitled to

- An exclusion of R300 000 in the year of death
- The personal use asset exclusion
- The primary residence exclusion, and
- Potential small business asset relief in terms of para 57

ENDOWMENTS

Even though the proceeds of an Endowment policy are seen to be tax free there is still tax payable during the duration of the investment term and potentially on withdrawal of amounts in the Fund.

All proceeds from Endowment policies are paid out to the investor net of tax due to the fact tax is raised in the fund and not in the hands of the investor.

Fact that tax is raised in the Fund and therefore paid indirectly by investor eases all tax administration on the investor when amounts paid out or withdrawn from the Fund

SA Endowments

Endowments are taxed in terms of the Five Fund Approach as set out in Section 29A of the Income Tax Act of 1962. The Five Fund Approach refers to the separate pools at which individuals, companies, corporate entities and non-taxable entities, are taxed.

- Income Tax – The Income Tax applicable to Endowments is withheld at source, which means that the insurance or investment company administrating the investment will pay tax on the investors' behalf.

Individuals and trusts with natural persons as beneficiaries will be taxed at a fixed rate of 30%.

- Capital Gains Tax – The Capital Gains Tax payable is also done so at source (paid by the Insurance or Investment company on behalf of the investors). Individuals and Trusts with natural persons as beneficiaries will have an effective Capital Gains Tax rate of 12%

Endowments tend to be more beneficial investment solutions for investors with higher tax rates.

Capital gains tax

Paragraph 55(1)(a)(i) of the Eighth Schedule provides that any capital gain or loss on disposal of a long-term policy must be disregarded by its original beneficial owner or one of its original beneficial owners. The type of policy envisaged is one that gives rise to the receipt or accrual of an amount in the hands of the original beneficial owner or owners upon its disposal. The exclusion applies to a long-term policy as defined in the Long-term Insurance Act 52 of 1998, *issued by a South African insurer.*

Second hand policy

If the policy had been issued to someone else and was purchased by the taxpayer - a so-called second hand policy - the gain on its disposal, including by way of maturity or surrender, would be subject to CGT.

CRYPTO ASSETS

SARS'S STANCE ON THE TAX TREATMENT OF CRYPTOCURRENCIES

PRETORIA, 06 April 2018 - The South African Revenue Service (SARS) will continue to apply normal income tax rules to cryptocurrencies and will expect affected taxpayers to declare cryptocurrency gains or losses as part of their taxable income.

The onus is on taxpayers to declare all cryptocurrency-related taxable income in the tax year in which it is received or accrued. Failure to do so could result in interest and penalties.

Taxpayers who are uncertain about specific transactions involving cryptocurrencies may seek guidance from SARS through channels such as Binding Private Rulings (depending on the nature of the transaction).

Increased attentiveness and speculation regarding the future of cryptocurrencies has prompted calls for SARS to provide direction as to how cryptocurrencies should be treated for tax purposes. However, as indicated in this media statement, there is an existing tax framework that can guide SARS and affected taxpayers on the tax implications of cryptocurrencies, making a separate Interpretation Note unnecessary for now.

Cryptocurrency (typified by Bitcoin) is an internet-based digital currency that exists almost wholly in the virtual realm. A growing number of proponents support its use as an alternative currency that can pay for goods and services much like conventional currencies.

In South Africa, the word "currency" is not defined in the Income Tax Act (the Act). Cryptocurrencies are neither official South African tender nor widely used and accepted in South Africa as a medium of payment or exchange. As such, cryptocurrencies are not regarded by SARS as a currency for income tax purposes or Capital Gains Tax (CGT). Instead, cryptocurrencies are regarded by SARS as assets of an intangible nature.

Capital asset or trading stock

Whilst not constituting cash, cryptocurrencies can be valued to ascertain an amount received or accrued as envisaged in the definition of "gross income" in the Act. Following normal income tax rules, income received or accrued from cryptocurrency transactions can be taxed on revenue account under "gross income". Alternatively such gains may be regarded as capital in nature, as spelt out in the Eighth Schedule to the Act for taxation under the CGT paradigm.

Determination of whether an accrual or receipt is revenue or capital in nature is tested under existing jurisprudence (of which there is no shortage).

Taxpayers are also entitled to claim expenses associated with cryptocurrency accruals or receipts, provided such expenditure is incurred in the production of the taxpayer's income and for purposes of trade. Base cost adjustments can also be made if falling within the CGT paradigm.

Gains or losses in relation to cryptocurrencies can broadly be categorised with reference to three types of scenarios, each of which potentially gives rise to distinct tax consequences:

(i) A cryptocurrency can be acquired through so called "mining". Mining is conducted by the verification of transactions in a computer-generated public ledger, achieved through the solving of complex computer algorithms. By verifying these transactions the "miner" is rewarded with ownership of new coins which become part of the networked ledger.

This gives rise to an immediate accrual or receipt on successful mining of the cryptocurrency. This means that until the newly acquired cryptocurrency is sold or exchanged for cash, it is held as trading stock which can subsequently be realized through either a normal cash transaction (as described in (ii) or a barter transaction as described in (iii) below.

(ii) Investors can exchange local currency for a cryptocurrency (or vice versa) by using cryptocurrency exchanges, which are essentially markets for cryptocurrencies, or through private transactions.

(iii) Goods or services can be exchanged for cryptocurrencies. This transaction is regarded as a barter transaction. Therefore the normal barter transaction rules apply.

Value-Added Tax (VAT)

With effect from 1 April 2019, the “acquisition, collection…buying..selling” of any cryptocurrency was included in the definition of a ‘financial service’ in section 2 of the VAT Act and as such will be regarded as an exempt supply for VAT purposes, meaning output VAT will not be levied on the relevant transactions and no input VAT can be claimed.

Capital Gain / Loss
(Excluding amounts received / accrued as a beneficiary of a trust(s), or deemed to have accrued in terms of s7) ^

Did you dispose of any local assets attracting capital gain or loss (including Cryptocurrency)? Y ◯ N ◯

How many disposals (shares to be combined as one disposal) took place? [Number of disposals]

Did you dispose of any foreign assets attracting capital gain or loss (including Cryptocurrency)? Y ◯ N ◯

How many disposals (shares to be combined as one disposal) took place? [Number of disposals]

Local Business, Trade and Professional Income
(Excluding amounts received / accrued as a beneficiary of a trust(s), or deemed to have accrued in terms of s7) ^

Did you derive income from local business, trade or profession other than rental income from the letting of fixed property(ies)? Y ◯ N ◯

How many separate trading activities did you carry on? [Number of partnerships]

ESTATE DUTY

Estate duty is levied in terms of the Estate Duty Act[7] (the Act), whilst donations tax is charged in terms of the Income Tax Act. Unless indicated to the contrary, all section references in this chapter of the notes are to sections of the Estate Duty Act

The purpose of estate duty is to tax the transfer of wealth from the deceased estate to the beneficiaries.

Outline of estate duty liability

Estate duty is levied and collected by the Commissioner in respect of the estate of every person who died on or after 1 April 1955.

Tax residence

Deceased <u>not ordinarily resident</u>

Sections 3(2)(*c*) to (*h*) of the Act specifically exclude from the definition of "property" certain assets where the deceased was not ordinarily resident in the Republic at the date of death. The net effect of the exclusions is that a non-resident is essentially only liable for estate duty on South African assets.

Deceased <u>ordinarily resident</u>

If the deceased was ordinarily resident in the republic at the date of their death, the value of all their property wherever situated, is to be considered for inclusion as property of their estate

Rate

- The duty is levied at a flat rate of 20% of the dutiable estate until 28 February 2018.
- From 1 March 2018, 20% on the dutiable estate as does not exceed R30 million and 25% of the dutiable estate as exceeds R30 million.

The dutiable amount

The dutiable amount of an estate is calculated in the following manner:

The ***sum*** of (gross value of the estate):

– All property of the deceased as at the date of his death (section 3(2)); **and**

– All deemed property of the deceased as at the date of his death (section 3(3));

Less:

The deductions allowable in terms of the Act (section 4) – to arrive at the **net value** of the estate;

Less:

An abatement of R3,5 million (section 4A) – to arrive at the **dutiable amount** of the estate.

Reduction of estate duty

After the calculation of the estate duty there is a possibility of a reduction of the estate duty by:

- transfer duty (section 16)
- foreign death duties
- a successive deaths rebate (first schedule).

[7] Act 45 of 1955

PROPERTY FOR ESTATE DUTY PURPOSES

The estate consists of both the property (as defined) of the deceased as at the date of death, and property deemed to be theirs at that date (section 3(1)).

PROPERTY (SECTION 3(2))

Property is defined in the Act as
"*any right in or to property, movable or immovable, corporeal or incorporeal*" (section 3(2)).

The definition of property is very wide, and would include actual property owned by the deceased at their date of death, movable or immovable, tangible or intangible, as well as any right in or to such property, for example:

- Fixed property
- Shares/unit trusts
- Fixed deposits and other cash investments
- Goodwill, copyright, patents

Property would also include a credit loan account in favour of the deceased. So if, for example, the deceased sold assets on loan account to a family trust, the amount of the loan account still outstanding at the date of death would be property in the deceased's estate.

To be "property" the property must have belonged to the deceased or have vested in the deceased at the date of death. The fact that an amount becomes an asset in the deceased's estate after death does not make it "property" in the estate, eg rent, interest, dividends which accrue after death.

Income earned by the deceased prior to the date of death will form part of the property of the estate, for example interest earned on an interest bearing investment up to the date of death will be included in the balance of the account as property in the estate. Income earned after the date of death will not be included as property of the estate.

TAX TABLE

Taxable income (R)	2021/22 Rates of tax	Taxable income (R)	2022/23 Rates of tax
R0 - R216 200	18% of each R1	R0 - R226 000	18% of each R1
R216 201 - R337 800	R38 916 + 26% of the amountabove R216 200	R226 001 - R353 100	R40 680 + 26% of the amountabove R226 000
R337 801 - R467 500	R70 532 + 31% of the amountabove R337 800	R353 101 - R488 700	R73 726 + 31% of the amountabove R353 100
R467 501 - R613 600	R110 739 + 36% of the amountabove R467 500	R488 701 - R641 400	R115 762 + 36% of the amountabove R488 700
R613 601 - R782 200	R163 335 + 39% of the amountabove R613 600	R641 401 - R817 600	R170 734 + 39% of the amountabove R641 400
R782 201 - R1 656 600	R229 089 + 41% of the amountabove R782 200	R817 601 - R1 731 600	R239 452 + 41% of the amountabove R817 600
R1 656 601 and above	R587 593 + 45% of the amountabove R1 656 600	R1 731 601 and above	R614 192 + 45% of the amountabove R1 731 600

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