Dear Sir/Madam

We refer to the call for proposals on the above-mentioned. Enclosed is the SAICA National Tax Committee’s submission.

INCOME TAX – INDIVIDUALS, EMPLOYMENT AND SAVINGS

INCOME TAX – DOMESTIC BUSINESS

1. Sections 24I(10) and 24I(10A)

Legal nature
Section 24I(10) prohibits the deduction or inclusion of exchange differences in respect of exchange items between certain connected persons.
Factual description
The new proviso to section 24I(10) reads:

“Provided further that any exchange item...that is held and not realised before the last
day of the last year of assessment of a person...ending before the year of assessment of
that person commencing on or after 1 January 2014 shall be deemed to have been
realised on that last day”.

Thus, for example, if a company has a December year end, and an exchange item (long term
loan) arose on 1 January 2012 and is still outstanding on 1 January 2014, according to
section 24I(10) the exchange item will be deemed to have been realised on
31 December 2013. At this point the exchange difference from 1 January 2012 to
31 December 2013 will, in terms of this section, need to be brought to account.

We then turn to section 24I(10A). This section requires that, subject to subsection (7A) and
paragraph (b), exchange differences arising on certain types of exchange items arising
between connected persons or groups of companies may not be included in, or deducted from,
the taxpayer’s income. The section comes into operation on 1 January 2013 and applies in
respect of years of assessment commencing on or after that date. Thus, for the year of
assessment ending 31 December 2013 (in our example above), this section (10A) also
requires that the exchange differences on the specified types of exchange items in the section
must not be brought to account.

However, sub-paragraph (b) reads:

“Where paragraph (a) was applied during any year of assessment to any exchange
difference in respect of an exchange item and... (ii)... (bb) that exchange item is
realised, an amount in respect of that exchange item must be included in or deducted
from the income of that person ....in the year of assessment during which that exchange
item is realised.....’

Since, in our example, section 24I(10) will deem the exchange item to have been realised on
31 December 2013, the exchange differences in respect of the long term loan will have to be
recognised on that date regardless of whether they arose before 1 January 2013. Only the
recognition for inclusion or deduction of those exchange differences which arise going
forward from 1 January 2014 will then be delayed until actual realisation in terms of the section (10A).

**Nature of business impacted**
The effect of the sections read together, and their effective dates, means that all exchange differences up to the 31 December 2013 (per our example) will be treated as realised and therefore recognised. Based our understanding, this is not the intention.

**Proposal**
To solve the problem it is suggested that section 24I(10) be made subject to Section 24I(10A).

2. **Section 31**

**Legal nature**
Section 31 requires that international transactions to be based on arm’s length principle. In the Explanatory Memorandum to the Bill (2010) that introduced the section in its current format the following was stated, on page 79:

> “SARS will amplify its interpretation of the rules in this context by way of Interpretation Note or other published guidance”.

**Factual description**
The effective date of the section was made 1 October 2012 and therefore already applies now. The guidance has not been provided.

**Nature of taxpayers impacted**
The lack of guidance impacts on all taxpayers engaged in international transactions with connected persons.

**Proposal**
It is suggested that the guidance be made available as a general binding ruling or that section 31 is amended to clarify issues requiring interpretation.

3. **The Fourth Schedule**

3.1 **Employees’ tax certificates**
Legal nature
Paragraph 13(12) refers to a “mechanized accounting system” and the consent of SARS to use that.

Factual description
The employees’ tax certificates are now done through the efiling and if this is not used a mechanised system will not meet the specifications.

Proposal
The provision should be repealed.

3.2 Provisional tax - Paragraph 18 of the Fourth Schedule to the Income Tax Act

Legal nature
This paragraph provides for an exemption from the payment of provisional taxes for individuals under certain circumstances. It differentiates between taxpayer on the basis of age and then provides the exemption in basically the same circumstances.

Factual description
It is submitted that there is justification for the exemption on the basis that the amounts involved would not justify the submission of provisional tax and the current wording does not really achieve that. There is no reason why the exemption should be limited to specific source of taxable income. The R120 000 used for persons over the age of 65 has also not been adjusted to take account of the increase in the tax threshold – for instance for a person over the age of 75, the threshold is already close to this amount.

Nature of taxpayers impacted
It effects all taxpayers who are provisional taxpayers, but do not receive a substantial amount of income from source other than remuneration.

Proposal
It is suggested that all natural person taxpayers should be treated equally in this instance. The following principles should then apply:

- the individual concerned will not be exempt if he or she carries on a business
- the individual will then be exempt from making provisional payments if:
  - the taxable income of that person for the relevant year of assessment will not exceed the tax threshold;
  - the taxable income of that person derived from otherwise than from remuneration does not exceed R20 000.
4. Dividends tax and *en commandite* partnerships

**Legal nature**

Subject to certain exemptions, and the potential application of a particular double tax agreement (DTA), dividends tax is levied at a rate of 15% when a dividend is paid by a South African tax resident company. Further, dividends tax is levied on the beneficial owner of a dividend (i.e. it is levied at the shareholder-level). However, where dividends tax is leviable, it is generally withheld and paid to SARS by the company paying the dividend or by a regulated intermediary on behalf of the beneficial owner of the dividend.

**Factual description**

By reason of certain exemptions, provided the relevant documentation is submitted to the company paying the dividend (Investee Company), dividends tax is essentially only triggered when dividends are paid to individuals, trusts, and persons who are not tax resident in South Africa. For non-residents the relevant double tax treaty may reduce the dividends tax rate. It is, therefore, submitted that the identity, legal persona and country of tax residence of the beneficial owner of the dividend is critical for the investee company in order to determine whether a dividend (or any part thereof) is exempt from dividends tax (or is subject to a reduced tax rate in terms of a particular DTA, if applicable). The legislation caters for this to be made known to the investee company through the provision of a declaration by the beneficial holder to the investee company.

*The limited en commandite partnership*

Legally, investors, as partners in an *en commandite* partnership, are not disclosed to the investee company. In such cases, usually, a general partner (which is disclosed to the investee company) would generally act on behalf of the limited partners to the partnership. Such general partner may also be appointed to distribute returns to the limited partners or reinvest such.

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1. In terms of section 64E(2), a dividend is deemed to be paid on the earlier of the date on which the dividend is paid or becomes payable.
2. As defined in section 64D of the Act
3. A withholding agent interposed between the company paying the dividend and the beneficial owner
4. Section 64G of the Act
5. Section 64G
It is submitted that the current wording of the dividends tax legislation does not provide for the situation where an investee company declares a dividend to the general partner (who may receive such dividend on behalf of the various partners to the *en commandite* partnership- the partners are, however, the beneficial owners of the shares and dividends).

As the general partner is not registered as the beneficial owner of such dividend (and the investee company is not informed of the identity of the beneficial owners of such dividend due to the investment structure in question), the investee company would have no choice but no withhold dividends tax at the full 15% on dividends paid to the general partner, despite the fact that some (or all) of the partners to the *en commandite* partnership may be eligible for exemption from, or qualify for a reduced rate of, dividends tax.

**Nature of the business impacted**
From the above factual description, in terms of current law, it is submitted that partners to *en commandite* partnerships may be prejudiced, either because each partner may be obliged to reveal its identity to the investee company in order to potentially qualify for exemption from, or a reduced rate of, dividends tax. Should this not be feasible (whether through preference or legally), such partner’s return on its investment will be negatively affected as a result of dividends tax suffered, purely because the investment structure is in the form of an *en commandite* partnership (as opposed to a direct investment).

**Proposal**
Based on the above, it is submitted that the dividends tax legislation be updated to allow general partners to be treated similar to regulated intermediaries. Therefore, it is submitted that general partners in *en commandite* partnerships should be allowed to receive dividends from an investee company free of dividends tax. Subsequently, based on the respective partners’ holding percentages and their applicable dividends tax rates, the general partner may then pay the correct amount of dividends tax over to SARS. In this way, the partners’ identities are not disclosed to the investee company (a critical feature of the *en commandite* partnership) whilst the correct return on investment is recognised in the hands of each partner.
Alternatively, the dividends tax legislation could recognise a partnership as a beneficial owner, which is exempt, similar to a company, and set out that the payment of such dividends to partners would then be subject to dividends tax.

5. Section 8E and 8EA

Legal nature
Section 8E and 8EA provides 3 exemptions to address the BEE conundrum and thereby protect qualifying holders of at least 20% of a company’s shares.

Factual description
The “at least 20%” requirement is a problem as many BEE transactions were put together through consortium structures where, in many cases, individual stakeholders would hold less than 20% of the shares. Also, where shareholding was acquired in a listed company it could be as low as 2.5%

Nature of the business impacted
All companies involved in BEE consortium structures and the related BEE shareholders.

Proposal
We propose that the 20% requirement be reduced to the 10% limit used in section 42 to address the above concerns.

6. The Tax Administration Act

6.1 Liability of third party appointed to satisfy tax debts

Legal nature
Section 179(1) allows for SARS to require the person (who holds or owes or will hold or owe any money, including a pension, salary, wage or other remuneration, for or to a taxpayer) to pay the money to SARS in satisfaction of the taxpayer’s tax debt.

Factual description
It is the experience of taxpayers that SARS is using this as a way of collecting outstanding amounts for tax and penalties. In many cases the taxpayers were not made aware that they owe the money before the third party is appointed.
Nature of taxpayers impacted
This impacts on all taxpayers, but are particularly relevant to employees.

Proposal
It is proposed that SARS must in the first instance inform the taxpayer concerned before the third party is appointed. This would afford the taxpayer the opportunity to make the payment or arrange for instalments.

This would make sense in the context of section 179(4) as the taxpayer concerned will then not have to engage with the third party to convince that party of its basic living expenses.

6.2 The understatement penalty

Legal nature
Chapter 16 of the Act allows SARS to impose penalties in the event of an understatement by the taxpayer. For this purpose section 223 contains an understatement penalty percentage table and section 222(2) specifically provides that SARS must levy the penalty at the highest applicable understatement penalty percentage. Section 102(2) places the burden of proving whether the facts on which SARS based the imposition of an understatement penalty under Chapter 16 upon SARS.

Factual description
The table uses behaviour as a basis and starts with a “substantial understatement” and in an order of seriousness of the understatement continues to “intentional tax evasion”. The first problem that taxpayers are experiencing is with the second behaviour. If the understatement is not material, but it can be seen that reasonable care was not taken the 50% penalty is applied by SARS. For example, a person accidently captures an amount of a deduction on a return as R1 000 instead of R100. It is SARS is correct to view this as an instance where reasonable care was not taken, but it does not allow for them to consider the intention of the taxpayer.

Nature of taxpayers impacted
This impacts on all taxpayers, and in particular where an assessment is issued by SARS, which differs from the information declared by the taxpayer on the return of income.

Proposal
It is proposed that a definition of “reasonable care” be inserted to provide clarity that this would only apply in instances of negligence, but not gross negligence or where it was intentionally done. The alternative is to change the order of the behaviours by swapping “substantial understatement” with the “reasonable care” one. In other words, the first behaviour on the table should be reasonable care, followed by substantial understatement.
6.3 Tax position and registered tax practitioner

Legal nature
Section 223(3) allows for the remission of an understatement penalty in instances where the taxpayer relied on the opinion of a registered tax practitioner.

Factual description
The wording of section 223(3) appears to limit the application of the principle. The first problem is that it only allows SARS to take this into account where the understatement penalty was levied.

It is unclear if the use of the word “arrangement” in section 223(3)(a) is meant to limit the application of this provision to reportable arrangements.

Nature of taxpayers impacted
This impact on all taxpayers who would want to object to a penalty imposed in terms of the Tax Administration or any Tax Act.

The proposal
The ability to remit a penalty on the basis of a tax opinion by a registered tax practitioner should not be limited to reportable arrangements or otherwise.

In particular, the ability to remit a penalty should also be extended to instances where the third behaviour (no reasonable grounds for ‘tax position’) in the table was used as the basis for the imposition of the penalty.

Yours faithfully

Piet Nel CA(SA)

PROJECT DIRECTOR: TAX

The South African Institute of Chartered Accountants