South Africa: Budget Speech Highlights 2023

In brief

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In this issue

In depth

A. Corporate Tax

Expansion of the renewable energy tax incentive

In an effort to encourage the installation of energy generation capacity by the private sector, Treasury has temporarily expanded the renewable energy tax incentive. The incentive will no longer be subject to generation thresholds or deductions over a three year period.

Businesses will now able to deduct 125% of the cost of renewable energy installations brought into use for the first time between 1 March 2023 and 28 February 2025.

Deductibility of expenditure to earn interest

Practice note 31 of 1994 sets out the South African Revenue Service's ("**SARS**") practice of allowing the deduction of expenditure incurred to earn interest income. For example, finance charges incurred on money borrowed in order to loan out at a profit, regardless of whether the taxpayer's trade was the lending of money.

In 2022, SARS and Treasury indicated the intention to withdraw Practice Note 31, to be effective for years of assessment starting on or after 31 March 2023, as a result of abuse.

The Budget indicates that government will consider legislative measures to allow the deduction in legitimate cases.

Interest deductibility limitations

To ensure the reduction of the corporate tax rate is effected in a revenue neutral way, Treasury has introduced measures to broaden the tax base. One of these measures was refining the application of the rule that limits the amount of deductible interest expenditure where the interest income will not be subject to South African tax and the creditor is in a controlling relationship with the debtor.

Treasury has identified the following further clarifications:

- Introduction of a definition of "creditor"

- Restrict adjusted taxable income inclusions to balance of assessed loss arising in the previous year of assessment
- Extension of the institutional lending exemption to include both foreign banks and local banks
- Aligning the operation of the "controlling relationship" definition and group of companies test as triggers to the application of the rule.

Third-party backed shares

The Income Tax Act 58 of 1962 ("Act") contains anti-avoidance provisions aimed at preventing tax evasion using certain types of equity instrument structures defined as Third-Party Backed Shares. The rules apply to deem any dividend paid in respect of such a Third-Party Backed Share to be income in the hands of the shareholder.

An exemption to this anti-avoidance rule applies where the subscription proceeds are utilized to purchase shares in an operating company. However, the anti-avoidance rules are not re-triggered where the shares in the operating company are disposed of by the issuer of the Third-Party Backed Shares.

The Budget includes a proposal to apply the anti-avoidance rules where the shares in the operating company are no longer held by the issuer of the Third-Party Backed Shares.

Contributed tax capital - foreign companies

Where a foreign company becomes tax resident in South Africa, the contributed tax capital of such newly resident company is deemed to be the market value of the shares in that company.

Treasury has identified avoidance schemes where, for example, a foreign holding company would hold a South African company through a foreign intermediary holding company. The intermediary holding company would then become tax resident in South Africa, resulting in its contributed tax capital being deemed equal to the market value of the shares in the intermediary holding company (essentially equal to the value of the underlying South African company). The South African company would then declare exempt dividends to the newly South African resident intermediary holding company. A tax free capital distribution would then be made out of contributed tax capital established in the newly South African company.

Treasury has proposed modifying the definition of contributed tax capital to restrict these and similar practices and to cater for the conversion of amounts of contributed tax capital denominated in foreign currency into Rand.

Corporate roll over relief

Interaction between debt concession or compromise rules and corporate roll over relief rules

A dormant company exemption exists in the debt concession or compromise rules dealing with expenditure on revenue assets and capital assets. This exemption applies to prevent the debt benefit resulting in a reversal of the tax benefit that arose from the expenditure of the borrowed amount.

However, under the first proviso to the dormant company exemption, the exemption does not apply where the asset, acquired with the borrowed amount, is subsequently disposed of under a roll over relief transaction.

Treasury has indicated that clarity is needed on whether the proviso is triggered where the disposal of the asset is subsequent to the debt benefit arising or whether it is also triggered where the disposal of the asset precedes the debt benefit arising.

Clarification of the interaction between the deemed base cost and asset for share rules

Amendments were introduced in 2021 to clarify that the deemed base cost rules apply to asset for share transactions. Treasury is seeking to clarify whether capital allowances may be determined against the base cost of an asset acquired in exchange for the issue of shares.

Refining provisions applicable to the unbundling transactions

In 2020 and 2021, amendments were made to the unbundling transaction provisions to curb avoidance practices where shares were unbundled to persons outside of the South African tax net, by ensuring only qualifying persons benefited from the roll over relief and pro-rated the operation of the anti-avoidance rule to ensure a more equitable outcome.

It has been proposed that further amendments be introduced to ensure an equitable outcome regarding tax paid by the unbundling company, by allowing this tax to be apportioned between the shares in the unbundling company and unbundled company and to cater for the situation where the unbundling company is not in a taxable position, meaning the effect of the anti-avoidance rule is absorbed by the unbundling company.

B. International Tax

Pillar two

In 2022, an announcement was made that legislative amendments would be proposed to implement the two pillar solution to the taxation of the digital economy. To date, significant progress has been made by the OECD on pillar two, which deals with the imposition of a minimum effective global tax rate.

Treasury has indicated that in 2023 a position paper will be released outlining government's proposed policy on pillar two and legislative proposals will be made that will be effected in the 2024 legislative cycle.

Foreign dividends

South African listed shares

An exemption from income tax exists for dividends received in respect of South African listed shares. Treasury has identified that schemes are being set up where South Africans invest in a non-resident company which is listed on a South African exchange, with this company then investing in interest bearing debt securities in South Africa. The result being that the South African tax base is eroded, as the interest deduction is not matched by a taxable foreign dividend.

Treasury has therefore proposed to amend the round trip financing anti-avoidance rule for foreign dividends, to be triggered where the foreign dividend is directly or indirectly funded with amounts that were deductible in South Africa.

Participation exemption anti-avoidance rule

Foreign dividends may be exempt, unless any amount of the foreign dividend is directly or indirectly derived from an amount which is deductible in South Africa. Where this rule applies, the foreign dividend will be taxed at a maximum rate of 20%, despite the deduction being applied to reduce an amount that is taxed at 27%.

Treasury proposes to align the treatment to prevent the base erosion that would occur in such a situation.

Controlled foreign companies

Foreign business establishment exception

The foreign business establishment exception applies where a controlled foreign company has an operation in another country which meets certain substance requirements. Treasury has identified schemes where controlled foreign companies retain sufficient substance in-country to satisfy the exception, but outsources important functions that the controlled foreign company earns incomes from. Amendments will be proposed to prevent the application of the exception where such outsourcing takes place.

Controlled foreign company return of capital participation exemption

A participation exemption applies to the sale of shares in a foreign company, where such shares were held for at least 18 months. This participation exemption similarly applies to foreign returns of capital by controlled foreign companies. However, it is not subject to the 18 month holding requirement. Treasury has proposed aligning the holding requirements for both aspects of the participation exemption.

Taxation of non-resident beneficiaries of South African trusts

Currently the Income Tax Act provides that capital gains realised by South African trusts, where a non-resident beneficiary has a vested right to such capital gain, is taxed in hands of the trust. The income tax provision that attributes income received by or accrued to resident trusts, however, allows for the flow through of such income to the non-resident beneficiary that is not subject to SARS' jurisdiction.

It is proposed to limit the flow through of income to non-resident beneficiaries for tax purposes and instead tax the resident trust on such amounts.

Participation exemption on disposal of foreign company shares

A participation exemption to capital gains tax applies where a South African tax resident disposes of shares in a foreign company. The policy intention underlying this participation exemption is to encourage the repatriation of the proceeds of such disposal to South Africa.

Treasury has proposed to restrict the participation exemption's application to instances where there is a substantial change in the shareholding of the foreign company and restrict its application where the disposal is to another group company.

C. Value Added Tax

VAT treatment of short-term insurance industry supplies

The earlier changes to section 72 of the VAT Act, which afford SARS discretionary powers over VAT decisions, affect all SARS decisions made before 21 July 2019. This includes the decisions in Binding General Ruling 14 which deals with the VAT treatment of specific supplies, such as the supply of insurance and related intermediary services, hull and associated liability insurance, indemnity and third party payments, among others, in the short-term insurance industry. The VAT Act will be amended to clarify the VAT treatment of these specific supplies.

VAT treatment of pre-paid vouchers in the telecommunications industry to be clarified

Following the decision in a recent Supreme Court of Appeal judgment not to issue a declaratory order in relation to the VAT treatment of prepaid vouchers in the mobile telecommunications industry, it is no surprise to see a proposal for the VAT Act to be amended to provide clarity in this regard. The current proposal, however, seems to be limited to providing clarity in instances where prepaid vouchers are used for services provided by third parties, the mobile telecommunication company is acting as an agent and/or the third-party services are exempt or not considered taxable for VAT purposes.

Meaning of "adjusted cost" for purposes of the temporary letting of residential property to be clarified

Under section 18D of the VAT Act, which was introduced with effect from 1 April 2022 to clarify the VAT treatment of the temporary letting of residential property, a residential property developer who temporarily lets out properties developed for sale is deemed to be making a taxable supply of that property at the value determined in section 10(29), being the adjusted cost of the construction, extension or improvement of that property. It is unclear whether the term "adjusted cost" also includes the cost of the land and it is proposed that section 10(29) be amended to clarify this.

Rule dealing with output tax declared on temporary letting of residential property to be clarified

A property developer is deemed to be making a taxable supply for VAT purposes when it temporarily lets residential property developed for purposes of sale and therefore liable to pay output tax. When the developer subsequently sells that property, it should be able to recover the output tax. Section 18D(5), read with section 16(3)(o), makes provision for an input tax deduction, while at the same time creating an anomaly in section 18D(5)(c) which refers to an adjustment under section 18(1). The anomaly would be clarified through the deletion of section 18D(5)(c) from the VAT Act.

Rules dealing with documentary requirements for gold exports to be addressed

In addition to refining and smelting gold or ore received from its customers (or depositors), refineries also act as agents for the sale and export of gold on depositors' behalf. During the refining or smelting process, the gold from various depositors are combined to make up the volume required for sale or export and consequently the gold loses its original identity, making it difficult for depositors to obtain the relevant documents required to support the application of the zero rate on a transaction-by-transaction basis. The VAT Act will be amended to address this.

Rules dealing with documentary requirements for gold exports to be dealt with

The Domestic Reverse Charge Regulations were introduced in July 2022 as a mechanism to curb the use of the VAT system to obtain undue VAT refunds. VAT registered vendors had a transitional period of one month to comply with the requirements of the regulations in August 2022, however, the regulations require clarification in certain areas, including the definitions of the terms "residue" and "valuable metal", the alignment of the definition of valuable metal with that in the Precious Metals Act, 2005, as well as with respect to certain exclusions from the definition of valuable metal. It is further proposed that a 'de minimis' rule be introduced to the definition of valuable metal and that the transitional measures and responsibilities of the recipient of valuable metal be clarified. There are also proposals to clarify the responsibilities of the recipient of "valuable metal", since the current regulations require a recipient to issue a statement to the supplier of the "valuable metal" detailing, amongst other things, the percentage of gold content within the valuable metal. This requirement has proved problematic, as recipients are not always equipped with specialized instruments to measure the gold content. The regulations will be amended to transfer this responsibility to the supplier.

D. Carbon Tax

Carbon tax rates

Effective 1 January 2023, the carbon tax rate increased from ZAR 144 to ZAR 159 per tonne of carbon dioxide equivalent. The carbon fuel levy for 2023/24 will increase by 1c to 10c/l for petrol and 11c/l for diesel from 5 April 2023. The carbon tax cost recovery quantum for the liquid fuels refinery sector increased from 0.63c/l to 0.66c/l.

Baker McKenzie.

Proposed extension of the utilisation period in the Carbon Offsets Regulations

It is proposed that the utilisation period in the Carbon Offsets Regulations be extended to align with the extension of the first phase of the carbon tax until up to 31 December 2025. This amendment is effective from 1 January 2023.

Fuel emission factors in Carbon Tax Act

A new schedule 1 to the Carbon Tax Act (2019) is to be inserted providing for updated carbon dioxide emission factors for domestic (tier 2) in order to align the act with the amended methodological guidelines for qualifying greenhouse gas emissions. This amendment is effective from 1 January 2023.

Fugitive emission factors formula adjustment

The formula in section 4(2) of the Carbon Tax Act, which is used to calculate total greenhouse gas emissions, has been changed to only multiply certain emission factors by 1000 to convert to tonnes.

E. Customs and Excise

Excise duties

Excise duties on alcohol and tobacco will be increased by 4.9% in line with inflation. The rate for sparkling wine is limited to 3.2 times that of natural unfortified wine.

Extension of diesel fuel refund levy

In 2000, government implemented the diesel refund system to provide full or partial relief for the general fuel levy and the RAF levy to primary sectors. Currently, the refund system is in place for the farming, forestry, fishing and mining sectors. With effect from 1 April 2023, a similar refund on the RAF levy for diesel used in the manufacturing process (such as for generators) will be extended to manufacturers of foodstuffs in order to limit the impact of power cuts on food prices. Refund payments will be processed once the system is developed and will be in force for two years, until 31 March 2025.

F. Other Indirect Taxes

Fuel levies

No increases have been made to the general fuel levy on petrol and diesel and the RAF levy also remains unchanged.

Health promotion levy or sugar tax

From 1 April 2022, the health promotion levy for beverages containing more than 4g of sugar content per 100ml was increased from 2.21c/g to 2.31c/g. Based on the challenges experienced by stakeholders in the sugar industry, there will be no increase in the health promotion levy in 2023/24 and 2024/25 in order to boost the sugar industry and enable stakeholders to restructure. Government intends to publish a discussion paper on the health promotion levy in order to extend this levy to pure fruit juices and lower the 4g sugar content threshold.

G. Tax Proposals Affecting Individuals

Clarifying anti-avoidance rules for low-interest or interest-free loans to trust

Section 7C of the Income Tax Act aims to curb the tax-free transfer of wealth to trusts and companies using low-interest or interest-free loans, advances, or credit. Under these rules, any interest foregone on these loans, advances, or credit is deemed to be a donation subject to donations tax. This deemed donation is calculated as the amount by which the official rate of interest exceeds any amount incurred in that regard. There are certain exclusions, such as if the loan, advance, or credit is used to purchase a primary residence for the person advancing the loan, advance, or credit to the trust, company, or the spouse of such a person.

The proposed amendments are aimed at providing clarity on how and when the amount should be converted into South African rands where the loan, advance, or credit is denominated in foreign currency.

Two-pot retirement system

The first phase of the legislative amendments to the retirement system will take effect on 1 March 2024, which will allow pre-retirement access to a portion of retirement savings while preserving the remainder. Retirement fund contributions will remain deductible up to the lower of ZAR350 000 per year or 27.5 percent of taxable income per year. Permissible withdrawals from funds accrued before 1 March 2024 will be taxed according to the lump sum tables, while withdrawals from the "savings pot" before retirement will be taxed at marginal rates. Upon retirement, amounts remaining in the saving pot will be taxed according to the retirement lump sum table.

Aspects to be clarified in the forthcoming draft legislation include a proposal to provide for withdrawals of seed capital, and legislative mechanisms to include defined benefit funds and legacy retirement annuity funds that are currently excluded from the two pot system. It is further proposed that the second phase of implementation include a review of whether withdrawals should be allowed from the retirement pot if one is retrenched and has no alternative source of income.

H. Tax Administration

Aligning tax registration requirements for non-resident employers

Non-resident employers are not required to have a representative employer in South Africa for purposes of employees' tax. As a result, there is no mechanism to enforce liability to withhold or deduct tax from the remuneration they pay to their employees who render services in South Africa. Notwithstanding, non-resident employers are required to register with SARS as employers where they pay remuneration to employees who are South African tax residents. Similarly, in such circumstances non-resident employers are liable to contribute towards the unemployment insurance fund and skills development levy in respect of such remuneration. It is proposed that the relevant provisions be aligned to ensure consistency in the registration obligations of both resident and non-resident employers.

Varying employees' tax withholding in respect of remuneration

The Fourth Schedule to Income Tax Act permits employers to request a variation in the withholding of employees' tax in order to account for foreign taxes paid. This variation does not apply to remuneration arising from share options and similar schemes. Treasury has proposed that SARS be empowered to vary the basis for withholding under these circumstances, to ensure an equitable result for employees who benefit from shares incentive schemes.

Aligning with anti-money laundering and combating the financing of terrorism developments

In light of the potential for South Africa to be grey-listed by the Financial Action Task Force, it has been proposed that amendments be made to the tax administration laws to align these with the National Strategy on Anti-Money Laundering, Counter Financing of Terrorism and Counter Financing of Proliferation and the General Laws (Anti-Money Laundering and Combating Terrorism Financing) Amendment Act, 2022.

Summary of Tax Rates

Companies: Financial years commencing on or after 31 March 2023

Type	Rate of Tax
Corporate Tax	27%

Small Business Corporations: Financial years ending on any date between 1 April 2023 and 31 March 2024

Taxable Income (ZAR)	Rates of Tax (ZAR)
1 - 95 750	0% of taxable income
95 751 - 365 000	7% of taxable income above 95 750
365 001 - 550 000	18 848 + 21% of taxable income above 365 000
550 001 and above	57 698 + 27% of taxable income above 550 000

Turnover Tax for Micro Businesses: Financial years ending on any date between 1 March 2023 and 29 February 2024

Taxable Income (ZAR)	Rate of Tax (ZAR)
1 - 335 000	0% of taxable turnover
335 001 - 500 000	1% of taxable turnover above 335 000
500 001 - 750 000	1 650 + 2% of taxable turnover above 500 000
750 001 and above	6 650 + 3% of taxable turnover above 750 000

Value Added Tax (VAT)

Rates

Rate Category	Rate of Tax
Standard rate (most local supplies of goods or services)	15%
Zero rate (direct export and certain specific supplies of goods or services)	0%
Standard rate (non-resident suppliers of electronic services)	15%

Registration Threshold

Registration Requirement	Threshold (ZAR)
Compulsory: taxable supplies exceed in any consecutive 12 months	1 000 000
Voluntary: taxable supplies exceed in any consecutive 12 months	50 000

Individuals and Trusts: Period 1 March 2023 to 29 February 2024

Individuals and special trusts

Taxable Income (ZAR)	Rates of Tax (ZAR)
1 – 237 100	18% of taxable income
237 101 – 370 500	42 678 + 26% of taxable income above 237 100
370 501 – 512 800	77 362 + 31% of taxable income above 370 500
512 801 – 673 000	121 475 + 36% of taxable income above 512 800
673 001 – 857 900	179 147 + 39% of taxable income above 673 000
857 901 – 1 817 000	251 258 + 41% of taxable income above 857 900
1 817 001 and above	644 489 + 45% of taxable income above 1 817 000

Trusts other than special trusts

Type	Rate of Tax
Trusts	45%

Rebates

Type	Amount (ZAR)
Primary	17 235
Secondary (persons 65 and older)	9 444
Tertiary (persons 75 and older)	3 145

Tax Threshold

Age	Threshold (ZAR)
Below age 65	95 750
Age 65 to below 75	148 217
Age 75 and over	165 689

Medical scheme fees tax credit

Persons covered by a medical aid scheme	Tax Rebate (ZAR) per month
For the first two individuals	364
For each additional dependent	246

Transfer Duty: Applicable where sale of property is not subject to VAT

Taxable Income (ZAR)	Rates of Tax (ZAR)
1 – 1 100 000	0%
1 100 001 – 1 512 500	3% of the value above 1 100 000
1 512 501 – 2 117 500	12 375 + 6% of the value above 1 512 500
2 117 501 – 2 722 500	48 675 + 8% of the value above 2 117 500
2 722 501 – 12 100 000	97 075 + 11% of the value above 2 722 500
12 100 001 and above	1 128 600 + 13% of the value above 12 100 000

Estate Duty: Levied on the dutiable value of an estate

Value of Estate (ZAR)	Rate of Tax
1 - 30 000 000	20%
above 30 000 000	25%

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