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Global NewsFlash

South Africa - Proposed repeal of foreign employment income tax exemption

In this issue:

Overview

Current position

Impact of Proposal

Deloitte's view

Contacts

Overview

In terms of the **Draft Taxation Laws Amendment Bill**, dated 19 July 2017, National Treasury proposed that section 10(1)(o)(ii) of the **Income Tax Act**, No. 58 of 1962 be repealed effective 1 March 2019.

The main reason given for this proposal is to curb situations of double non-taxation – being situations in which an individual's employment income is not subject to tax in either South Africa (SA) or in the foreign country where the services are rendered.

Subsequently, extensive representations have been made to National Treasury by interested parties outlining their concerns regarding the impact of a repeal of section 10(1)(o)(ii).

During a meeting of Parliament's Standing Committee for Finance held on 15 September 2017, National Treasury suggested certain changes to their original proposal, namely:

- Section 10(1)(o)(ii) will no longer be repealed in totality;
- But, the first ZAR1 million of foreign remuneration will remain exempt from tax in SA if the individual meets the requirements of section 10(1)(o)(ii) in relation to that remuneration; and
- The effective date of this change will be extended to 01 March 2020.

Current position - section 10(1)(o)(ii)

SA tax residents are taxable on their worldwide income. However, remuneration earned for services rendered outside SA is exempt from SA tax if an employee spent more than 183 full days (including a continuous period of more than 60 full days) outside SA in any 12-month period during which those services were rendered outside SA.

In the event that a resident employee does not meet the requirements of the exemption, they remain taxable in SA on their worldwide remuneration, but, in terms of section 6*quat* of the Income Tax Act, a rebate (foreign tax credit) in respect of foreign taxes paid on income may be offset against the tax payable in SA (with certain restrictions).

The impact of the proposal

If the proposed changes are implemented, where a SA resident individual earns remuneration of more than ZAR1 million as a result of services performed outside SA, the portion of the foreign remuneration above ZAR1 million will be included in the person's SA taxable income and taxed at the applicable

personal income tax rate even if they comply with the requirements of section 10(1)(o)(ii).

This may lead to an increased SA tax liability for that individual, to the extent that they have not paid tax on that remuneration in that foreign jurisdiction.

In addition, where the employee is subject to employees' tax (PAYE) withholding on their remuneration both in SA (due to the impact of the amendment) and in the country where the services are rendered, there may be excessive withholding leading to cash-flow constraints. If so, a hardship directive would need to be obtained from SARS to request relief from SA PAYE to the extent that a rebate in respect of the foreign taxes paid on that remuneration is available.

From an employer perspective, the proposed change may increase costs where the employees are tax-equalized, (i.e. where tax is borne by the employer) as many employers relied on the exemption to cushion the equalization costs.

In addition, the Skills Development Levy and Unemployment Insurance Fund contributions will be due on the remuneration, which may have previously been exempt from taxation in SA.

Back to top

Deloitte's view

The proposed changes may increase the cost of assignments and may impact the profitability of certain projects. Additional analysis would be required to ensure that the investment return on assignments remain within business imperatives.

Currently, delays are experienced for SARS to process and allow foreign tax credits. It is hoped that National Treasury's view that the tax credit system as administered by SARS will not be overwhelmed by the increased number of persons, who may need to claim foreign tax credits, will be proven correct in practice.

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