

GMS Flash Alert



2019-083 | April 26, 2019

South Africa - Foreign Remuneration Exemption: What Will Changes Mean?

The legislative cap to the foreign remuneration exemption, which goes into effect next year, is likely to impact many South Africans working temporarily abroad.

The change to the legislation means that the remuneration earned for foreign services will no longer be completely exempt from South African income tax. From 1 March 2020, only the first ZAR 1 million of remuneration relating to foreign services will be exempt from South African tax, assuming that the taxpayer meets all of the requirements for the exemption to apply.

On 6 March 2019, a workshop was jointly hosted by National Treasury (NT) and the South African Revenue Service (SARS) with various stakeholders, to address practical concerns arising as a result of the legislative amendment¹ It was confirmed that the legislation will not be amended any further, and the implementation date will not move beyond 1 March 2020. However SARS confirmed its willingness to work with taxpayers to ensure a smooth implementation.

This newsletter considers some of the likely consequences of the change and practical considerations.

WHY THIS MATTERS

The exemption cap could result in increased tax costs for employers and assignees. When appropriate, adjustments to gross-up packages and withholding taxes need to be considered. Furthermore, employers need to be aware of the challenges facing employees because foreign tax credits are not currently accounted for in South African payroll systems.

In certain circumstances, employees could experience a cash-flow issue, which could be disruptive and upsetting for them.

Background

Currently, the foreign remuneration exemption contained in section 10(1)(o)(ii) of the Income Tax Act No 58 of 1962 ("ITA") states that foreign remuneration earned by a South African resident taxpayer will not be subject to South African income tax if the taxpayer has spent more than 183 days rendering services outside of South Africa in a rolling twelve-month period, of which more than 60 days were consecutive.

South Africa's Taxation Laws Amendment Act, No. 17 of 2017 (18 December 2017), contained an amendment capping the private-sector foreign employment income tax exemption to ZAR 1 million for foreign-earned remuneration as of 1 March 2020. (For prior coverage, see GMS [Flash Alert 2018-020](#) (26 January 2018).)

Employee Tax

South African employers who pay remuneration for foreign services through a local South African payroll may cease to withhold South African employees' tax on qualifying foreign remuneration. If the employee fails to meet the requirements of section 10(1)(o)(ii), however, the employer becomes liable for the withholding of employees' tax owed to SARS, and the employer is liable for penalties and interest that result.

When a South African ("SA") resident earns foreign-sourced income and pays foreign tax on that income, it is also taxable in South Africa, and the SA resident may claim foreign tax credits ("FTCs") against the SA tax due on that income, subject to certain limitations.

Currently the ITA does not specifically allow for FTCs to be applied through the payroll to reduce an employee's tax liability to SARS. The result is that if an employee either does not qualify for the exemption, or earns more than the ZAR 1 million amount of foreign income after 1 March 2020, and pays tax in the foreign country, a cash flow problem occurs. The employee will pay tax in both countries on foreign income or on the portion greater than the ZAR 1 million exemption.

KPMG NOTE

This potential for double tax is an unintended consequence that will need to be resolved before the legislation becomes effective.

Two options for addressing the problem are amending the legislation to allow for the FTC offset, or obtaining a specific ruling from the Commissioner to allow for the offset for each employee concerned. Although potentially administratively burdensome for taxpayers, employers and SARS, the ruling option is currently the only solution available.

Foreign Tax Credits (FTCs)

A resident taxpayer is required to report all local and foreign income (remuneration, interest, dividends, and rental, etc.) on the taxpayer's provisional and annual tax returns and would be entitled to claim FTCs to reduce the South African tax liability. Additional South African taxes will be due if the FTCs are insufficient to cover the South African tax liability on the worldwide income.

KPMG NOTE

The ITA provides that FTCs may be claimed to the extent that the foreign taxes are “paid or proved to be payable.” Taxpayers often find it difficult to obtain proof of taxes to be paid, and it is unclear what would constitute sufficient proof of payment or proof of liability, if taxes have not yet been paid.

Globally, individual taxes are paid through differing mechanisms. Some countries have self-assessment tax return systems, in which no assessments are issued. Others have monthly taxes payable by employers on behalf of their employees. And others have payroll withholding, which is not a final tax, and does not reflect an assessment of the taxes paid or payable. Thus proving the payment of foreign taxes is difficult for employees, and even more difficult on a “real time” monthly basis, to enable offset through SA payroll.

This problem of claiming FTCs already exists on a smaller scale for those employees who do not qualify for the exemption and who are taxable in the country in which they work, but has not created much concern. Given the likely impact of the change to the legislation, it is essential to answer the question of what would constitute sufficient proof for the offset of FTCs before it becomes effective. Time is, however, running short for this.

Given the cash-flow difficulties that could be experienced by employees working abroad and paid from South Africa, there is a likelihood that South African residents may seek alternative solutions, such as “breaking South African tax residence,” resulting in being taxed only on South African-sourced income. This would present challenges, however, and is not always possible for foreign employees on temporary assignments abroad.

Breaking South African Tax Residence

There may be some confusion over the difference between “breaking tax residence” and the term “financial emigration.” The latter involves changing status from permanent resident or resident living temporarily abroad to non-resident in South Africa – it is not a tax term and is in fact not necessary for breaking tax residence in South Africa.

Tax residence can be broken by a South African citizen, who is ordinarily resident in South Africa, in two ways:

- By leaving South Africa and deciding not to return – settling permanently outside of South Africa, with or without formal emigration (breaking ordinary tax residence); or
- By becoming resident in the foreign country in which the taxpayer works, and by applying the “tie breaker” clauses contained in the Residence article of the applicable Double Tax Agreement (DTA) concluded between South Africa and the other tax jurisdiction (breaking residence through the application of a DTA).

From the above, it is clear that a taxpayer can no longer simply “decide” not to be a tax resident in South Africa and expect that SARS will accept this decision. A decision must be supported by facts and circumstances, should SARS query the residence status.

On breaking residence, it is important to note that a South African taxpayer will be deemed to have disposed of all worldwide assets, excluding South African immovable property, at market value on the day before breaking residence, as an “exit charge.” The total gain calculated, less ZAR 40,000, will result in the net gain for inclusion in taxable income. Forty percent of this gain must then be included in income and taxed at the taxpayer’s marginal rate.

KPMG NOTE

If a South African-resident taxpayer holds assets which have grown significantly in value since acquisition, and have not been disposed of, this could be a very costly exercise, without having liquidated these assets in order to cover the cost of the tax due.

Next Steps and Things to Consider

The area relating to the application of FTCs needs urgent legislative clarification to enable proper implementation by taxpayers, employers, tax practitioners and SARS alike. SARS assessors and auditors need to be trained and equipped to deal with the likely increase in the application of FTCs through payrolls (assuming rulings can be obtained from the Commissioner) and through annual tax returns.

Tax-resident individuals employed abroad should critically evaluate their South African tax residence position, to determine whether they should remain tax resident in South Africa. They need to fully evaluate their global tax position to understand what will be required of them from 1 March 2020, and what the likely cost implications will be if they remain South African tax residents. Each individual's circumstances need to be addressed on a case-by-case basis.

Advice should be sought well in advance of March 2020, to foster adequate advance planning and careful consideration of all the possible consequences.

FOOTNOTE:

1 The March 6 National Treasury workshop was widely covered in the news, including in *Businessstech* (see, "Treasury is going ahead with South Africa's expat tax – and experts say it could be devastating," 7 March 2019, by clicking [here](#)) and the *SA Financial Markets Journal* (see, H. Dudley, "Looming 'expat tax' is ultimately fair," by clicking [here](#)). *Please note these are third-party (non-governmental, non-KPMG) websites. Provision of these links does not represent an endorsement of the websites by KPMG.*

* * * * *

ZAR 1 = EUR 0.062
ZAR 1 = USD 0.069
ZAR 1 = INR 4.87
ZAR 1 = GBP 0.054

Contact us

For additional information or assistance, please contact your local GMS or People Services professional or one of the following professionals with the KPMG International member firm in South Africa:



Carolyn Chambers
Head of Global Mobility Services &
Employment Tax Advisory
KPMG SA
Tel. + 27 (0)83 440 5564
carolyn.chambers@kpmg.co.za



Melissa Duffy
Director, Global Mobility Services &
Employment Tax Advisory
KPMG SA
Tel. + 27 (0)82 448 1989
melissa.duffy@kpmg.co.za

The information contained in this newsletter was submitted by the KPMG International member firm in South Africa.

© 2019 KPMG Services Proprietary Limited, a South African company and a member firm of the KPMG network of independent member firms affiliated with KPMG International Cooperative ('KPMG International'), a Swiss entity. All rights reserved.

www.kpmg.com

kpmg.com/socialmedia



© 2019 KPMG LLP, a Delaware limited liability partnership and the U.S. member firm of the KPMG network of independent member firms affiliated with KPMG International Cooperative ("KPMG International"), a Swiss entity. All rights reserved. Printed in the U.S.A. NDPPS 530159

The KPMG name and logo are registered trademarks or trademarks of KPMG International.

The KPMG logo and name are trademarks of KPMG International. KPMG International is a Swiss cooperative that serves as a coordinating entity for a network of independent member firms. KPMG International provides no audit or other client services. Such services are provided solely by member firms in their respective geographic areas. KPMG International and its member firms are legally distinct and separate entities. They are not and nothing contained herein shall be construed to place these entities in the relationship of parents, subsidiaries, agents, partners, or joint venturers. No member firm has any authority (actual, apparent, implied or otherwise) to obligate or bind KPMG International or any member firm in any manner whatsoever. The information contained in herein is of a general nature and is not intended to address the circumstances of any particular individual or entity. Although we endeavor to provide accurate and timely information, there can be no guarantee that such information is accurate as of the date it is received or that it will continue to be accurate in the future. No one should act on such information without appropriate professional advice after a thorough examination of the particular situation.

Flash Alert is a GMS publication of KPMG LLP's Washington National Tax practice. To view this publication or recent prior issues online, please click [here](#). To learn more about our GMS practice, please visit us on the Internet: click [here](#) or go to <http://www.kpmg.com>.