Budget Summary:
A New Era in Tax

KPMG South Africa's 2023/24 Budget Summary

Finance Minister, Mr Enoch Godongwana, delivered the National Budget address on Wednesday, 22 February 2023

Key highlights

The 2023 Budget Speech has been delivered by the Minister of Finance.

Noted below are the key proposals of the Budget Speech of potential relevance

Tax policy objectives

- The government intends to avoid tax increases while the economy is recovering from recent shocks. Further, the 2023 Budget utilises the tax system to help address particular market failures, such as a lack of research and development **(R&D)** or inadequate electricity generation capacity.

Individuals and employment tax

- The personal income tax brackets, primary, secondary and tertiary rebates have been adjusted for inflation. The tax-free threshold increases to R95 750 per year, and medical tax credits will be adjusted to a limited extent.
- The tax bracket for transfer duties, retirement fund lump sum benefits and retirement fund lump sum withdrawal benefits will be adjusted upwards by 10%. No transfer duty payable on property sales up to R1.1 million and no personal income tax on retirement fund lump sum benefits up to R550 000 or withdrawal benefits up to R27 500. The tax rates will remain unchanged.
- A discussion document will be released this year to outline workplace practices and policies, changes in the current environment and how different workplaces are affected by home office and travel allowance policies. This will be a multi-year review.
- The intention of the two-pot retirement system is to enable pre-retirement access to a portion of one's retirement assets, while preserving the remainder for retirement. Phase 1 of the two-pot retirement system takes effect on 1 March 2024. Permissible withdrawals from funds accrued before 1 March 2024 will be taxed according to the lump sum tables. Withdrawals from the "savings pot" before retirement will be taxed at marginal rates. On retirement, any remaining amounts in the savings pot will be taxed according to the retirement lump sum table.
- To address an anomaly that arose in 2022 legislative changes, it is proposed that members of pension or provident funds who have reached the normal retirement age but have not yet opted to retire must be able transfer between funds tax-free.
- Currently, non-resident employers who have employees rendering services in South Africa may not be liable to deduct or withhold employees' tax from the remuneration paid to those employees as a result of them not having a representative employer in South Africa for employees' tax purposes. However, there is still a requirement for the non-resident employer to register with SARS as an employer and to pay the required skills development levies and unemployment insurance contributions. To ensure consistency, it is proposed that the various provisions of legislation be aligned.
- The Fourth Schedule to the Income Tax Act allows employees to request a variation in employees' tax withholding taking into account foreign taxes paid. Currently, this application excludes remuneration arising from share options and similar schemes with the result that employees will only be entitled to claim a foreign tax credit when they complete their annual tax returns. It is proposed that remuneration arising from share options and similar schemes are now included.
- Where a taxpayer disagrees with an auto-assessment received by SARS, it is proposed that the period for the submission of the fully completed annual return by the taxpayer be aligned with the annual tax return submission due date for non-provisional taxpayers.

- The PAYE and personal income tax administration reform announced in the 2022 Budget will continue over the medium term with a view to reduce the administrative burden for employers, payroll administrator and SARS. SARS is in consultation with employers and representative organisations, to provide employer and employee data on a monthly basis in a fully automated approach. It is expected that over time, the need for employer PAYE annual reconciliations will fall away and the reform will be extended to third-party data providers.

Trusts and deceased estates

- The anti-avoidance rules for low-interest or interest-free loans to trusts are to be amended. Rules exist to curb tax-free transfer of wealth to trusts using low-interest or interest-free loans, advances or credit. These rules deem any interest foregone in respect of such loans to a trust to be a donation subject to a donations tax. Exclusions exist when the loan is used to purchase a primary residence for the person advancing it to the trust, company or spouse of such person. However, the rules do not fully encompass what constitutes a primary residence or provide clarity on how foreign currency should be converted. National Treasury proposed to address these issues.
- National Treasury is concerned about the discrepancy between the rules of normal tax treatment of income attributed to beneficiaries of trusts (section 25B) and the rules of tax treatment of capital gains in relation to beneficiaries (paragraph 80). Paragraph 80 does not allow capital gains to be attributed to non-residents (which results in the trust being liable for the tax). Section 25B makes no such distinction. Changes are proposed to align the two provisions and reduce the collection risk for SARS.

Corporate income tax

- After consideration of public comments, the proposed withdrawal of Practice Note 31 (Interest paid on moneys borrowed) and Practice Note 37 (Deduction of fees paid to accountants, bookkeepers and tax consultants for the completion of income tax returns) will be delayed as government considers possible changes to the legislation to accommodate legitimate transactions affected by such withdrawal.
- In relation to debt-like equity instruments, government proposes that the anti-avoidance rules relating to third-party backed shares be clarified, particularly the deeming of dividends as income when shares in an operating company are no longer held by the person who initially acquired them.
- The following technical amendments are proposed to be made to the corporate reorganisation rules:
  - Clarifying the interaction between the debt reduction rules and the disposal of assets exclusion rule for dormant group companies.
  - In relation to asset for share transactions, clarifying the legislation on whether allowances in respect of an acquired asset may be determined according to the deemed base cost.
  - Refining the rules applicable to unbundling transactions.

Financial sector

- Government announced in 2020 that a deposit insurance scheme would be established in order to protect depositors and promote a more stable financial system. In 2022, Parliament passed related legislation and it is now proposed that law be amended in order to address the tax implications of a deposit insurance scheme.
- In order to ensure alignment, it is proposed that the provisions related to Shariah-compliant financing arrangements be extended across all tax acts.
- Application of IFRS 17 to cell captive owners:
  - International Financial Reporting Standards 17 (IFRS 17) became effective for periods commencing on or after 1 January 2023, in respect of all insurance contracts. In 2022, changes were made to sections 28 and 29A of the Income Tax Act in order to accommodate the impact that this standard would have on both short and long-term insurers. Certain third-party cell captive arrangements are treated as reinsurance arrangements for IFRS purposes, resulting in the recognition of reinsurance assets and reinsurance liabilities. These arrangements are not seen as commercial reinsurance arrangements and consequently, for income tax purposes, these amounts should be disregarded in determining the taxable income of the cell captive.

  - Cell captive arrangements effected in terms of preference share arrangements can be accounted for either as Insurance contract liabilities (IFRS 17) or investment contract liabilities (IFRS 9). Accounting for the preference shares under either standard results in those liabilities being included in the definition of "adjusted IFRS value" in section 29A of the Income Tax Act. This may result in double-counting of liabilities if a separate liability for profits due to the cell owner is also included in the "value of liabilities" definition (also in section 29A of the Income Tax Act.) Consequently, it is proposed that the definition of "value of liabilities" in section 29A of the Income Tax Act be amended to exclude any other liabilities, related to a cell owner.

Cross border tax

- A legislative framework is to be introduced in order to empower SARS to conclude bilateral advance pricing agreements. This is aimed at creating certainty and clarity relating to transfer pricing matters.
- During the 2023 legislative cycle a draft position paper on the implementation of OECD Pillar Two, which proposes an effective global minimum corporate tax of at least 15% for large MNEs, is to be published for public comment with the aim of inclusion in the 2024 Taxation Laws Amendment Bill. Pillar One, which focuses on the allocation of taxing rights in the digital economy, is still awaiting agreement.
- Amendments are to be made to the contributed tax capital (CTC) rules as pertains to companies that change their tax residency to South Africa, so as to prevent the avoidance of capital gains tax and dividends tax as well as to clarify the conversion of CTC, denominated in another currency, to ZAR.
- Foreign dividends received or accrued from shares listed on a South African exchange is generally exempted from normal (income) tax. To combat certain avoidance schemes, it is proposed that the round-tripping anti-avoidance rule for foreign dividend be expanded to include foreign dividends arising from shares listed on the South African stock exchange, where the foreign dividends are funded by amounts deductible in South Africa.
- A partial exemption applies that limits the effective normal rate at which the receipt of foreign dividends are taxed to 20% To address an overlap between the rules it is proposed that, where the anti-avoidance rule for foreign dividends funded from South African tax deductible amounts applies, this partial exemption will not be available.
- It is proposed that in order for a Controlled Foreign Company **(CFC)** to qualify as a foreign business establishment, all important functions for which the CFC is compensated by its clients should be performed by the CFC, or by another group company that is tax resident in the same country as the CFC.
- The participation exemption for the sale of shares in foreign companies is to be refined.
- It is proposed that the participation exemption relating to the sale of shares in foreign companies, be limited so as not to apply to the proceeds from shares sold to non-resident companies in the same group as the disposing company, or where the shareholders of the acquiring company are substantially the same as the shareholders of any company in the disposing company's group.
- To ensure consistency between the participation exemption available in respect of the sale of shares in foreign companies, it is proposed that the requirements of the participation exemption available in respect of foreign returns of capital from a CFC is to be expanded so as to include a minimum holding requirement of 18 months for the shares in the CFC.
- The interest limitation rules contained in section 23M of the Income Tax Act are to be further refined and clarified.

Incentives

- A "rooftop solar incentive" is to be introduced in term of which individuals receive a tax rebate equal to 25% of the cost of acquiring new and unused solar PV panels, limited to R15 000, if installed at a private residence during 1 March 2023 - 29 February 2024, and a certificate of compliance for installation is issued.
- The 150% R&D Tax Incentive Deduction is to be extended until 31 December 2033 and the definition of R&D refined to simplify understanding and administration. The internal business processes exclusion will be removed and a 6-month pre-approval grace period is to be introduced.
- The urban development zone tax incentive, which allows for an accelerated allowance in respect of buildings in designated areas, will be extended to 31 March 2025 to enable the conclusion of the public consultation part of the incentive policy review.

- To stimulate faster private investment to ease South Africa's energy crisis, the current renewable energy tax incentive available to companies will be expanded temporarily. Businesses will be eligible for a 125% deduction of the costs for renewable energy projects brought into use in the period 1 March 2023 and 28 February 2025, with no threshold on generation capacity.
- Further legislative amendments are to be considered in order to clarify the timeframes of the compliance requirements for industrial policy projects.
- The minimum Mineral Petroleum and Resources Royalty rate for Oil and Gas companies will increase from 0.5% to 2%, with the maximum remaining at 5%.

Public Benefit organisations (PBOs)

- Certain entities, such as recreational clubs, associations and PBOs, are required to have three unconnected "persons" who accept fiduciary responsibility, due to the non-profit status of the entity. In order to provide clarity on the term "person", it is proposed that legislation be amended to make it clear that this refers to natural person, rather than a juristic person.
- It is proposed that SARS be explicitly empowered to disclose all entities that may issue receipts for tax-deductible donations, and that have a section 18A approval.

Value-Added Tax (VAT)

- The VAT administrative framework to be reviewed with the purpose of simplification and modernisation.
- VAT treatment of supplies in the short term (non-life) insurance industry to be clarified in the VAT Act as a result of amendments made to section 72 and the impact on Binding General Ruling No.14.
- VAT treatment of prepaid vouchers supplied in the telecommunications industry to be used for services provided by a third party to be clarified.
- Clarification of various definitions, transitional measures and responsibilities of the recipient of valuable metals in the Regulations on the domestic reverse charge to be provided.
- Amendments have been proposed to address difficulties with obtaining documentary evidence substantiating the zero rating of VAT in respect of gold exports.
- Definitions and legislation relating to temporary letting of residential property to be amended to address anomalies identified.

Customs and Excise Duty proposals

Customs and excise rate increases:

- *Specific excise duties*:
  With effect from 22 February 2023, specific customs and excise duties are increased. Alcoholic beverages increased by 4.9%, (excluding sparkling wine and traditional African beer and beer powder). Sparkling wine increased by 0.7%, while traditional African beer and beer powder remains unchanged). The rate of duty on cigarettes, cigarette tobacco, pipe tobacco and cigars increased by 4.9%.
- *General Fuel Levy & Road Accident Fund Levy:*
  The General Fuel Levy and the Road Accident Fund Levy will remain unchanged.
- *Carbon tax on fuel:*
  With effect from 1 January 2023, the carbon tax rate will increase by to R159 per tonne of carbon dioxide equivalent. The carbon fuel levy for 2023 will increase by 1c to 10c/litre for petrol and 11c/litre for diesel from 5 April 2023. The carbon tax cost recovery quantum for the liquid fuels refinery sector increased to 0.66c/litre from 1 January 2023.

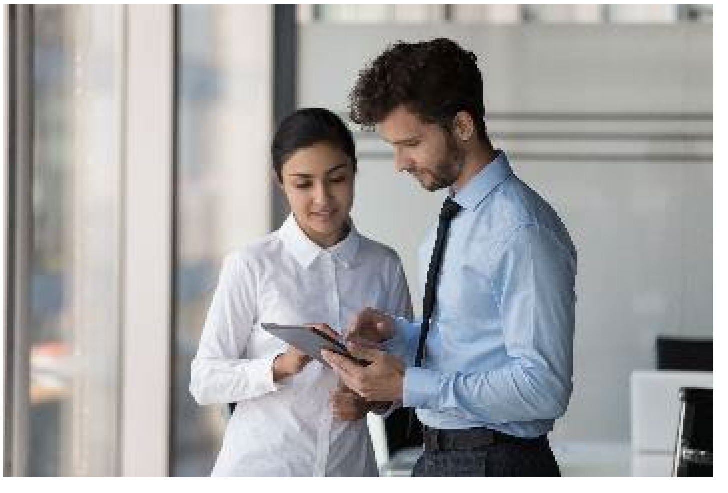
Legislative amendment proposals:

- *Deferment of duties:*
  Government proposes to prescribe conditions under which deferment of duties will be allowed by rules.
- *Single window:*
  Government proposes to introduce a single window to collect advance passenger information and passenger name records through the Department of Home Affairs, for distribution to other government entities such as SARS.
- *Traveller management system:*
  SARS implemented a modern online traveller management system, aimed at strengthening SARS' capability to facilitate legitimate traveller movements, providing travellers with clarity and certainty regarding their obligations, easing compliance, detecting non-compliance and improving enforcement of legislation by SARS and other agencies. It is proposed that the Customs and Excise Act be amended to provide for the declaration of the required information before arrival in or departure from South Africa.

- *Provisional Payments:* Government proposes to amend the customs legislation to provide~~s~~ for the liquidation of provisional payments, including prescription periods that will apply for unclaimed funds.
- *Extension of diesel fuel levy refund:* Refund of RAF levies for diesel used in the manufacturing process (including generators used) will be extended to manufacturers of foodstuffs, effective 1 April 2023 for a limited period ending 31 March 2025.
- *Health promotion levy:* There will be no increase in the health promotion levy in 2023/24 and 2024/25. Government proposes to publish a discussion paper to extend the levy to pure fruit juices and lower the 4-gram threshold.

Carbon tax

- The utilisation period in the Carbon Offsets Regulations is to be extended in order to align with the extension of the first phase of the carbon tax from 1 January 2023 to 31 December 2025.
- The fuel emission factors are to be aligned with the methodological guidelines and regulations (i.e. emission factors to be added in schedule 1 for country-specific tier 2 carbon dioxide reporting).
- The formula for fugitive emission provides for converting the unit of the emission factors for the different greenhouse gases from volume to mass by multiplying by a density factor, followed by multiplying by 1000 to convert to tonnes. It is proposed that the formula be changed to only multiply certain emission factors by 1000.
- With effect from 1 January 2023 the carbon tax rate per tonne of emission increased from R144 to R159.



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