SARS South African Revenue Service

BINDING GENERAL RULING (INCOME TAX): NO. 9

DATE: 19 September 2011

SUBJECT : TAXES ON INCOME AND SUBSTANTIALLY SIMILAR TAXES FOR PURPOSES OF SOUTH AFRICA'S TAX TREATIES

Preamble

For the purposes of this ruling –

- **"BGR"** means a binding general ruling issued under section 76P;
- **"section"** means a section of the Act;
- **"STC"** means secondary tax on companies;
- **"tax treaty"** means an agreement for the avoidance of double taxation;
- **"the Act"** means the Income Tax Act No. 58 of 1962; and
- **"treaty relief"** means relief from double taxation.

1. Purpose

This BGR identifies the taxes administered by SARS, which in its opinion constitute taxes on income or substantially similar taxes for purposes of South Africa's tax treaties.

2. Background

A tax treaty generally provides for relief for –

- specified taxes that are in existence at the time the treaty is entered into; and
- any identical or substantially similar taxes that are imposed after the date of signature of the treaty in addition to, or in place of, existing specified taxes.

This ruling reflects SARS's view, based on South Africa's domestic tax laws. A foreign tax jurisdiction may, however, hold a different view based on its own domestic tax laws.

3. Ruling

3.1 Taxes on income

The following taxes (as at publication date of this BGR) are taxes on income and thus qualify for treaty relief under South Africa's tax treaties:

- Normal tax on taxable income, which includes a taxable capital gain [section 5]
- Withholding tax on royalties, a final tax payable by non-residents on income derived from royalties or similar payments [section 35]

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- Withholding tax on foreign entertainers and sportspersons, a final tax [section 47B(2)]
- Turnover tax on micro businesses [section 48A]
- STC [section 64B(2)]

For purposes of the above list, the following taxes represent advance payments of normal tax:

- Employees' tax [Fourth Schedule to the Act]
- Provisional tax [Fourth Schedule to the Act]
- Amounts withheld from payments to non-resident sellers of immovable property in South Africa [section 35A]

The following taxes on income, which will also qualify for treaty relief, are to be introduced in the near future:

- A final withholding tax on dividends, effective 1 April 2012 [section 64E(1)]
- A final withholding tax on interest, effective 1 January 2013 [section 37J(1)]

3.2 Treatment of STC

Corporate taxes on income are imposed at two stages.

Normal tax is imposed at the first stage on an annual basis on corporate profits (or more accurately on "taxable income" as defined in section 1).

At the second stage, STC is imposed on a resident company on the "net amount" as described in section 64B(3) when a dividend is declared by the company. The net amount is the amount by which a dividend declared exceeds the sum of incoming dividends accrued during the "dividend cycle". A dividend cycle begins and ends each time a dividend is declared.

South Africa has reached agreement with all its treaty partners that STC is a creditable corporate tax. The circumstances under which a non-resident will be able to secure a tax credit for STC will depend on the terms of the tax legislation of the non-resident's country of residence.

STC can result in economic double taxation, which involves two persons being subject to tax on the same amount. This would occur, for example, if a non-resident shareholder's country of residence imputed the profits of a South African company to that non-resident under a controlled foreign company system similar to that found in section 9D, or under a full imputation system for taxing foreign dividends,[1] and failed to provide a tax credit for the underlying corporate taxes. By granting a tax credit for the *pro-rata* portion of the underlying corporate income taxes (including STC) the non-resident's country of residence will prevent economic double taxation.

Since STC is not a tax on shareholders, it is not affected by any limitation imposed on the source state under the dividends article of South Africa's tax treaties. In

[1] Under a full imputation system for taxing dividends, the foreign dividend is grossed up to an amount equal to the proportionate share of the underlying pre-tax corporate profits.

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Volkswagen of South Africa (Pty) Ltd v C: SARS[2] a South African-resident wholly owned subsidiary of a German holding company sought to obtain a rate of STC of 7,5% under article 7 of the tax treaty with Germany. The court found that there are substantial differences between STC and a withholding tax, and STC was therefore not substantially similar to a withholding tax. STC is a tax on a company declaring a dividend and not a tax on the recipient shareholders. It is not a tax on dividends as contemplated in the tax treaty and accordingly fell outside the ambit of the article.

3.3 Taxes which are not taxes on income or similar taxes

South African taxes (as at the date of publication of this BGR), which are not taxes on income or similar taxes, and thus do not qualify for treaty relief, include the following:

- Customs and excise duties
- Diamond export levy
- Donations tax[3]
- Estate duty
- Royalty levied on the transfer of a mineral resource extracted from within South Africa
- Securities transfer tax
- Skills development levy
- Transfer duty
- Unemployment insurance contributions
- Value-added tax

The above list is not exhaustive.

4. Period for which this ruling is valid

This BGR applies with effect from the date of publication and will apply for an indefinite period.

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SOUTH AFRICAN REVENUE SERVICE

[2] [2008] JOL 21746 (T), 70 SATC 195.
[3] Under section 54 donations tax is only levied on a donation made by a resident. Consequently, donations tax will never be a creditable tax for treaty purposes.