

**INTERPRETATION NOTE 18 (Issue 5)**

DATE: 9 December 2022

**ACT : INCOME TAX ACT 58 OF 1962**  
**SECTION : SECTION 6quat**  
**SUBJECT : REBATE AND DEDUCTION FOR FOREIGN TAXES ON INCOME**

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### **Preamble**

In this Note unless the context indicates otherwise –

- **“CFC”** means a “controlled foreign company” as defined in section 1(1);
- **“foreign source”** means a source<sup>1</sup> outside South Africa;
- **“foreign-source amount”** means an amount derived from a foreign source;
- **“normal tax”** means “normal tax” as defined in section 1(1), namely, income tax referred to in section 5(1);<sup>2</sup>
- **“OECD”** means the Organisation for Economic Co-operation and Development;
- **“qualifying foreign taxes”** means foreign taxes qualifying for a rebate or deduction;
- **“Schedule”** means a Schedule to the Act;
- **“section”** means a section of the Act;
- **“South Africa”** and **“the Republic”** are treated as having the same meaning;
- **“South African-source amount”** means an amount derived from a source<sup>3</sup> in South Africa;
- **“TA Act”** means the Tax Administration Act 28 of 2011;
- **“the Act”** means the Income Tax Act 58 of 1962;

<sup>1</sup> See 5.2.3 for the principles applicable to the determination of the source of an amount.

<sup>2</sup> Income tax referred to in section 5(1) is levied on taxable income received by or accrued to or in favour of a person.

<sup>3</sup> See 5.2.3 for the principles applicable to the determination of the source of an amount.

- “**tax treaty**” means an agreement (including a convention) for the avoidance of double taxation entered into between South Africa and another country;<sup>4</sup> and
- any other word or expression bears the meaning ascribed to it in the Act.

All guides, interpretation notes and rulings referred to in this Note are available on the SARS website at [www.sars.gov.za](http://www.sars.gov.za). Unless indicated otherwise, the latest issue of these documents should be consulted.

## 1. Purpose

This Note explains the scope, interpretation and application of section 64N which provides for a rebate or deduction for foreign taxes on income.<sup>5</sup>

Section 64N, which provides for a rebate for foreign taxes on dividends against dividends tax payable, is not dealt with in this Note. The *Comprehensive Guide to Dividends Tax* contains details in this regard.

This Note reflects the income tax and tax administration legislation (as amended) at the time of publication and includes the following:

- The Taxation Laws Amendment Act 20 of 2021 which was promulgated on 19 January 2022 (as per *Government Gazette* 45787).
- The Tax Administration Laws Amendment Act 21 of 2021 which was promulgated on 19 January 2022 (as per *Government Gazette* 45786).
- The Rates and Monetary Amounts and Amendment of Revenue Laws Act 19 of 2021 which was promulgated on 19 January 2022 (as per *Government Gazette* 45788).

## 2. Background

Residents are subject to income tax on their worldwide taxable income regardless of the source of the income. Foreign-source amounts derived by a resident may under specific circumstances be taxed by the country of source and by South Africa, resulting in international juridical double taxation. International juridical double taxation refers to the imposition of similar taxes by two or more sovereign countries on the same item of income (including capital gains) of the same person.

Relief from double taxation resulting from the imposition of tax by a residence country and a source country on the same amount is normally granted by the residence country. Thus, the source country’s right to tax generally has priority over the residence country’s right to tax. In many instances, countries provide for relief from international

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<sup>4</sup> South Africa deposited its instrument of ratification in respect of the Multilateral Convention to Implement Tax Treaty Related Measures to Prevent Base Erosion and Profit Shifting (BEPS MLI) with the OECD on 30 September 2022. The MLI will enter into force for South Africa on 1 January 2023. Beginning in January 2023, SARS will publish non-binding synthesised texts that summarise the impact of the BEPS MLI on individual tax treaties. Taxpayers will need to consider whether and, if so, how the MLI modifies an applicable tax treaty.

<sup>5</sup> Section 64N provided for a rebate for foreign taxes paid on South African-source service income included in South African taxable income. Section 64N(1) to (4) were deleted with effect from years of assessment commencing on or after 1 January 2016. For details of the section see Issue 3 of this Note which is available on the website under “Legal Counsel ⇒ Legal Counsel Archive ⇒ Interpretation Notes”. Section 64N(5) deals with the treatment of refunds or discharges in respect of amounts previously claimed as a rebate under section 64N.

juridical double taxation under a tax treaty, although many countries (including South Africa) also provide unilateral tax relief in their domestic law.

South Africa provides relief from double taxation to its residents in its domestic law mainly by rebate methods<sup>6</sup> or by a deduction<sup>7</sup> for foreign taxes payable on income that is subject to South African normal tax. The rebate and deduction methods are supplemented by certain exemptions for foreign-source amounts received by or accrued to residents.

### 3. The law

The relevant sections of the Act are quoted in **Annexure C**.

### 4. Introduction to section 6quat(1) and (1C)

#### *The rebate methods of relief for foreign taxes*

The following rebate methods are currently employed in South Africa:

- Section 6quat(1) which is the principal method used to provide relief for foreign taxes proved to be payable on income derived from a foreign source which is included in a resident's taxable income. Foreign taxes proved to be payable on income derived from a foreign source do not qualify for a deduction under section 6quat(1C)(a). Section 6quat(1) provides for the deduction of foreign taxes against normal tax payable.

Section 64N which provides for relief for foreign taxes paid on foreign dividends paid by a foreign company on listed shares.<sup>8</sup> Section 64N provides for a deduction of foreign taxes against dividends tax levied under section 64E(1).

#### *The deduction method of relief for foreign taxes*

Under section 6quat(1C)(a) a resident may claim certain foreign taxes that are not contemplated in section 6quat(1) as a deduction in determining taxable income derived from carrying on any trade, that is, essentially, foreign taxes paid or proved to be payable on South African-source amounts and foreign taxes paid, but not proved to be payable, on income derived from a foreign source.

Depending on the nature and detail of the amounts, one or more of the methods of relief provided for in section 6quat(1), section 6quat(1C)(a) and section 64N may apply to a person in respect of different amounts received by or accrued to or paid to that person during a particular year of assessment.

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<sup>6</sup> Sections 6quat(1) and 64N(1).

<sup>7</sup> Section 6quat(1C)(a).

<sup>8</sup> See the *Comprehensive Guide to Dividends Tax* for details on dividends tax and section 64N.

**Example 1 – Methods of relief for certain foreign taxes paid or proved to be payable**

*Facts:*

The following income is received by a resident during a year of assessment:

Nature of income	Foreign taxes paid or proved to be payable without any right of recovery R
(A) Trading income derived from Country A (the income constitutes a foreign-source amount).	15 000
(B) Fees received for managerial services rendered in South Africa to a person resident in Country B (the income constitutes a South African-source amount).	20 000
(C) Royalty income received from a person resident in Country C (the income constitutes a South African-source amount).	30 000
(D) Cash foreign dividends received from a foreign company on shares listed on an exchange <sup>9</sup> (the income constitutes a foreign-source amount).	20 000

No tax treaties are in place for any of these scenarios.

*Result:*

In respect of the foreign taxes, the resident is potentially entitled in the year of assessment under –

- (A), to a rebate under section 6quat(1) if the foreign taxes were proved to be payable, or to a deduction under section 6quat(1C)(a) if the foreign taxes were paid but not proved to be payable;
- (B), to a deduction under section 6quat(1C)(a);
- (C), to a deduction under section 6quat(1C)(a); and
- (D), to a rebate for dividends tax purposes under section 64N (Note).

**Note:**

The foreign dividend is exempt from normal tax under section 10B(2)(d).

*Exemption for certain foreign-source amounts*

The rebate methods under section 6quat(1) and section 64N and the deduction method under section 6quat(1C)(a) are complimented with exemptions or the disregarding of certain types of foreign-source income and capital gains received by or accrued to a resident, for example:

- Exemption for foreign dividends when a person (whether alone or together with any other company forming part of the same group of companies as that

<sup>9</sup> As defined in section 1 of the Financial Markets Act 19 of 2012 and licensed under section 9 of that Act.

person) holds at least 10% of the total equity shares and voting rights in a foreign company declaring a foreign dividend [section 10B(2)(a)].

- Exemption for foreign dividends which relate to amounts previously included in the income of a resident under section 9D<sup>10</sup> [section 10B(2)(c)].
- Partial exemption for foreign dividends received or accrued which are not otherwise exempt under section 10B(2). The exempt portion is calculated according to a formula in section 10B(3). For example, in respect of a natural person the exempt portion equals the amount of the foreign dividend multiplied by the ratio of 25 / 45.<sup>11</sup>
- Exemption for remuneration received by or accrued to an employee for services rendered outside South Africa if that employee was outside South Africa for a period exceeding 183 full days in aggregate during a 12-month period or for a period or periods exceeding 117 full days in aggregate during any period of 12 months in respect of any year of assessment ending on or after 29 February 2020 but on or before 28 February 2021 and for a continuous period exceeding 60 full days during that period [section 10(1)(o)(ii)].<sup>12</sup> With effect from years of assessment commencing on or after 1 March 2020, a maximum of R1,25 million can qualify for the exemption under section 10(1)(o)(ii) provided the relevant requirements are met.
- Exemption for certain pensions received by or accrued to a resident from a source outside South Africa for past services rendered outside South Africa [section 10(1)(gC)(ii)].
- The disregarding of any capital gain or capital loss on the disposal of equity shares in foreign companies if certain requirements are met [paragraph 64B of the Eighth Schedule].

#### *Order of deducting rebates from the amount of normal tax payable*

A person's normal tax liability is determined by deducting rebates from normal tax according to the sequence of the sections in the Act:

#### *A natural person*

	R
Normal tax payable	XXX
Less: Primary, secondary and tertiary rebates – section 6	(XXX)
Less: Medical scheme fees tax credit – section 6A	(XXX)
Less: Additional medical expenses tax credit – section 6B	(XXX)
Less: Rebate for foreign taxes – section 6quat(1)	(XXX)
Normal tax payable	<u>XXX</u>

#### *Any person other than a natural person*

Normal tax payable	XXX
Less: Rebate for foreign taxes – section 6quat(1)	(XXX)
Normal tax payable	<u>XXX</u>

<sup>10</sup> Section 9D deals with the attribution of net income of CFCs in certain circumstances.

<sup>11</sup> The ratio of 25 / 45 applies to years of assessment of a natural person commencing on or after 1 March 2017. See Interpretation Note 93 "The Taxation of Foreign Dividends" for the ratios applicable to persons other than natural persons.

<sup>12</sup> See Interpretation Note 16 "Exemption from Income Tax: Foreign Employment Income" for more information on section 10(1)(o)(ii).

The sum of the rebates under sections 6, 6A, 6B and 6quat(1) could potentially exceed the amount of normal tax payable.<sup>13</sup> To the extent that the sum of those rebates exceeds the normal tax payable, any excess is forfeited and is not refundable – see **Examples 1** [part 2.4 (b) and (c)], **5** [parts (d), (e) and (f)] and **6** [parts (f) and (g)] in **Annexure B**. The excess may also not be carried forward to the immediately succeeding year of assessment for purposes of determining the normal tax payable in that year. This outcome can be contrasted with the situation in which the amount of the qualifying foreign taxes exceeds the amount of the rebate determined under section 6quat(1A). Paragraph (ii) of the proviso to section 6quat(1B)(a) provides that certain excess foreign taxes proved to be payable may be carried forward to the immediately succeeding year of assessment to potentially qualify for set-off under paragraph (ii) of the proviso to section 6quat(1B)(a) in that year (see **5.8**).

*A comparison of the rebate method under section 6quat(1) and the deduction method under section 6quat(1C)(a)*

Foreign taxes taken into account as a tax rebate reduce a resident's liability for normal tax. However, if taken into account as a deduction from income, the foreign taxes merely reduce a resident's taxable income. In most situations, it will benefit a person if the foreign taxes qualify for a rebate rather than a deduction.

**Example 2 – Comparison of tax payable under the deduction and rebate methods**

*Facts:*

A resident company received income of R100 on which foreign taxes of 25% (R25) are proved to be payable.

*Result:*

The results obtained by applying the rebate method under section 6quat(1) or the deduction method under section 6quat(1C)(a) are as follows:

	Deduction Method	Rebate Method
	R	R
Taxable income from a South African source	100	0
Taxable income from a foreign source	0	100
Less: Foreign taxes qualifying for a deduction	(25)	<u>(0)</u>
Taxable income after deduction of foreign taxes	<u>75</u>	<u>100</u>
Normal tax (28%) <sup>14</sup>	21,00	28,00
Less: Rebate under section 6quat(1)	<u>(0)</u>	<u>(25,00)</u>
Normal tax payable	<u>21,00</u>	<u>3,00</u>
Total tax (normal tax and foreign tax)	<u>46,00</u>	<u>28,00</u>

<sup>13</sup> The possibility arises as a result of, for example, the rebates under sections 6, 6A and 6B which are available to natural persons.

<sup>14</sup> The normal tax rate for companies is 27% with effect from years of assessment ending on or after 31 March 2023.



### *Grossing-up of foreign-source amounts*

The gross amount of foreign source income, and not the amount which is net of the foreign tax liability incurred on that amount, must be included in a person's gross income.

The foreign taxes would incorrectly be taken into account twice, first, as a deduction and, secondly, as a foreign tax rebate if the net foreign-source amount were to be included in gross income.

## **5. Rebate for foreign taxes on income [section 6quat(1), (1A), (1B), (2), (3) and (5)]**

### **5.1 Introduction to the rebate for foreign taxes on income**

Section 6quat(1) is South Africa's primary mechanism for avoiding double taxation. "Rebate" means "a deduction from an amount to be paid" and, more specifically, under section 6quat refers to a deduction of foreign taxes from normal tax otherwise payable. South Africa grants this relief unilaterally through domestic legislation and bilaterally through most of its tax treaties.

Section 6quat provides detailed rules for determining the rebate. These rules cover, amongst others, the following:

- The deduction of a rebate from normal tax payable by a resident in respect of specified receipts and accruals of income and capital gains, included in the resident's taxable income (see 5.2).
- The determination of the amount of the rebate for certain foreign taxes on income proved to be payable by specified persons [section 6quat(1A)] (see 5.3 and 5.4).
- The requirements for foreign taxes to be regarded as qualifying foreign taxes (see 5.3).
- Limitations on the amount of the rebate [section 6quat(1B)] (see 5.5, 5.6 and 5.7).
- The carry-forward of the excess amount of foreign taxes to the immediately succeeding year of assessment [section 6quat(1B)] (see 5.8).
- The interaction with the relief provided for in tax treaties [section 6quat(2)] (see 5.9.2).
- The translation of foreign tax to rand [section 6quat(4)] (see 7).
- The issuing of additional or reduced assessments within a period of six years from the date of the original assessment to give effect to the correct calculation of the amount of the rebate [section 6quat(5)] (see 5.10).

A resident does not qualify for a rebate under section 6quat(1) for foreign tax proved to be payable to a foreign country on a South African-source amount.

**Example 3 – Application of section 6quat(1)***Facts:*

A resident company received foreign-source income of R100 000. No expenses were incurred in production of the foreign-source income. No other income was received by the company. In the country of source the income was subject to foreign tax at a rate of 10% which resulted in a tax liability of R10 000 (R100 000 × 10%).

*Result:*

The amount of R100 000 is included in the company's gross income and taxable income. Normal tax payable amounts to R28 000,00 (R100 000 × 28%<sup>15</sup> normal tax rate). The foreign tax of R10 000,00 is allowed as a rebate under section 6quat(1).

The rebate reduces the normal tax payable on the foreign-source income to R18 000,00 (R28 000,00 – R10 000,00).

See **Example 36** for an example of a foreign tax rate exceeding the normal tax rate.

Under section 6quat(1) foreign taxes proved to be payable can be set off only against normal tax payable and cannot be set off against other domestic taxes, for example, turnover tax on micro businesses levied under section 48A.

**5.2 Foreign-source amounts included in taxable income [section 6quat(1)]****5.2.1 Types of foreign-source amounts included in a resident's taxable income**

Under section 6quat(1) a rebate for foreign taxes on income as calculated under section 6quat must be deducted from normal tax if any of the foreign-source<sup>16</sup> amounts listed in (a) to (f) below, are included in a resident's taxable income.<sup>17</sup>

See **5.2.2** for details on the definition of "taxable income".

*(a) Any income received by or accrued to a resident from a foreign source [section 6quat(1)(a)]*

"Income" means "income" as defined in section 1(1), namely, the amount remaining of the gross income of any person for any year or period of assessment after deducting therefrom any amounts exempt from normal tax under Part I of Chapter II. The exclusion of exempt amounts from income means that foreign taxes which are attributable to exempt income will generally not qualify for a rebate under section 6quat(1). For example, foreign taxes attributable to an amount exempt under section 10(1)(o)(ii) will not qualify for a rebate under section 6quat(1) (see **Example 7** in **Annexure B**). There is, however, an exception to this rule in relation to foreign dividends in that for the purposes of section 6quat(1A) when determining the amount of the rebate, the amount of income included in taxable income is determined as if the partial exemption under section 10B(3) did not apply (see **5.5.2** and **Annexure B** for examples).<sup>18</sup> This means that the amount of foreign taxes relating to the portion of the foreign dividend which is exempt under section 10B(3) will potentially qualify for a

<sup>15</sup> The normal tax rate for companies is 27% with effect from years of assessment ending on or after 31 March 2023.

<sup>16</sup> See **5.2.3**.

<sup>17</sup> Unless the relief provided for in a tax treaty is chosen – see **5.9.3**.

<sup>18</sup> Paragraph (ii) of the proviso to section 6quat(1A).

rebate under section 6quat(1) subject to the limitation under section 6quat(1B) (see 5.5.2).

*(b) Any portion of the net income of a CFC as contemplated in section 9D which is attributed to a resident under section 9D(2) [section 6quat(1)(b)]*

Generally speaking,<sup>19</sup> under section 9D(2) a portion of the net income of a CFC is included in the income of a resident<sup>20</sup> that, directly or indirectly, together with a connected person, holds at least 10% of the participation rights and can exercise at least 10% of the voting rights in the CFC. This is commonly referred to as attribution of income. Special rules apply in the case of the participation rights of a resident in a foreign company which is a CFC as a result of its financial results being included in that resident company's<sup>21</sup> consolidated financial results. In calculating the net income of a CFC under section 9D(2A) for purposes of attributing it to a resident, the CFC is regarded as a taxpayer and a resident for certain sections, amongst others, the definition of "gross income" in section 1(1).

*(c) Any taxable capital gain as contemplated in section 26A, from a foreign source [section 6quat(1)(e)]*

Under section 26A a person's taxable capital gain as determined under the Eighth Schedule must be included in a resident's taxable income. A taxable capital gain equals the percentage specified in paragraph 10 of the Eighth Schedule multiplied by the person's net capital gain. See 5.6 for detail on the inclusion of a foreign-source taxable gain in taxable income.

*(d) Any amount contemplated in section 6quat(1)(a) or (b) which is received by or accrued to another person but which is deemed to have been received by or accrued to a resident under section 7 [section 6quat(1)(f)(i)]*

Income received by or accrued to a person from a source outside South Africa or income attributed from a CFC to that person can be deemed to have been received by or accrued to another person, being a resident, under section 7. Section 7(2) to (8) are dealt with below.

### *Section 7(2)*

Any income received by or accrued to a person married in or out of community of property<sup>22</sup> (the recipient) is deemed to be income accrued to the person's spouse (the donor) if –

- the income was derived in consequence of a donation, settlement or other disposition made by the donor on or after 20 March 1991 or of a transaction, operation or scheme entered into or carried out by the donor on or after 20 March 1991, and the sole or main purpose was the reduction, postponement or avoidance of the donor's liability for any tax, levy or duty which, but for the donation, settlement, other disposition, transaction, operation or scheme, would have become payable by the donor under the Act or any other Act administered by the Commissioner; or

<sup>19</sup> See, for example, the exclusion in paragraph (B) of the proviso to section 9D(2).

<sup>20</sup> Other than a headquarter company.

<sup>21</sup> Other than a headquarter company.

<sup>22</sup> See section 7(2A) for detail regarding how income derived from carrying on a trade, income from the letting of fixed property and income derived otherwise than from carrying on a trade are dealt with in relation to spouses married in community of property.

- income was received by or accrued to the recipient –
  - from a trade carried on by the recipient in partnership or association with the donor or which is in any way connected with a trade carried on by the donor; or
  - from the donor or a partnership of which the donor was at the time of such receipt or accrual a member or a private company of which the donor was at such time the sole or main holder of shares or one of the principal holder of shares,

and such income represents the whole or any portion of the total income so received by or accrued to the recipient which exceeds the amount of income to which the recipient would reasonably be entitled having regard to the nature of the relevant trade, the extent of the recipient's participation therein, the services rendered by the recipient or any other relevant factor.

#### *Section 7(3)*

Income is deemed to have been received by the parent of a minor child or stepchild, if by reason of any donation, settlement or other disposition made by that parent it has been –

- received by or accrued to or in favour of that child;
- expended for the maintenance, education or benefit of that child; or
- accumulated for that child's benefit.

#### *Section 7(4)*

Any income received by or accrued to or in favour of a minor child or stepchild of a person, by reason of a donation, settlement or other disposition made by another person, shall be deemed to be the income of the parent of that child, if the parent or parent's spouse made a donation, settlement or other disposition or gave some other consideration in favour directly or indirectly of the said other person or the other person's family.

#### *Section 7(5)*

Section 7(5) applies if a person has made a donation, settlement or other disposition which is subject to a stipulation or condition, whether made or imposed by that person or anybody else, to the effect that the beneficiaries or some of them shall not receive the income or some portion of the income thereunder until the happening of some fixed or contingent event. The effect is that so much of any income as would, but for the stipulation or condition, in consequence of the donation, settlement or other disposition be received by or accrue to or in favour of the beneficiaries, shall, until the earlier of happening of that event or the death of that person be deemed to be the income of that person.

#### *Section 7(6)*

Section 7(6) applies if a deed of donation, settlement or other disposition contains a stipulation that the right to receive income thereby conferred may, under powers retained by the person by whom the right is conferred, be revoked or conferred upon another person. The effect is that so much of any income as in consequence of the donation, settlement or other disposition is received by or accrues to or in favour of the

person on whom that right is conferred, shall be deemed to be the income of the person by whom it is conferred, so long as that person retains those powers.

#### *Section 7(7)*

Section 7(7) applies if by reason of a donation, settlement or other disposition made by a person (the donor) –

- the donor's right to receive or have paid for the donor's benefit an amount of passive income referred to in that sub-section, is ceded or otherwise made over to any other person or to a third party for that other person's benefit in such manner that the donor remains the owner of or retains an interest in the property referred to or if the property or interest is transferred, delivered or made over to the other person or to a third party for the other person's benefit, in such manner that the donor is or will at a fixed or determinable time be entitled to regain ownership of or the interest in the property; or
- the donor's right to receive or have paid to the donor or for the donor's benefit any income which is or may become due by another person acting in a fiduciary capacity is ceded or otherwise made over to any other person or to a third party for that other person's benefit in such manner that the donor is or will at a determinable time be entitled to regain the said right,

and means any such passive income as is received by or accrues to or for the benefit of the other person and which would otherwise, but for the donation, settlement or other disposition, have been received by or have accrued to or for the benefit of the donor, shall be deemed to have been received by or to have accrued to the donor.

#### *Section 7(8)(a)*

Section 7(8)(a) applies if by reason of or in consequence of a donation, settlement or other disposition (other than to a non-resident which is similar to a public benefit organisation contemplated in section 30) made by a resident, an amount is received by or accrued to a non-resident (other than a CFC in relation to the resident), which would have constituted income had that person been a resident. The effect is that the amount attributable to that donation, settlement or other disposition, shall be included in the resident's income.<sup>23</sup>

*(e) A capital gain from a source outside South Africa which is received by or accrued to another person but which is attributed to a resident under paragraph 68, 69, 70, 71, 72 or 80 of the Eighth Schedule [section 6quat(1)(f)(ii)]*

Capital gains are attributed to a resident as indicated in the relevant paragraphs of the Eighth Schedule below.

#### *Paragraph 68*

A person's capital gain which can be attributed to circumstances which are similar to those referred to in section 7(2) as detailed in (d) above, must be disregarded in the person's hands and taken into account when determining the aggregate capital gain or aggregate capital loss of the person's spouse.

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<sup>23</sup> See Interpretation Note 114 "Interaction between Section 25B(1) and Section 7(8) in case of Conflict, Inconsistency or Incompatibility".

*Paragraph 69*

A minor child's capital gain which can be attributed to circumstances which are similar to those referred to in section 7(3) or (4) as detailed in (d) above, must be disregarded in the child's hands and taken into account when determining the aggregate capital gain or aggregate capital loss of the child's parent.

*Paragraph 70*

A person's capital gain which can be attributed to circumstances which are similar to those referred to in section 7(5) as detailed in (d) above, must be disregarded in the person's hands and taken into account when determining the aggregate capital gain or aggregate capital loss of the person who made the donation, settlement or other disposition.

*Paragraph 71*

A beneficiary's capital gain which can be attributed to circumstances which are similar to those referred to in section 7(6) as detailed in (d) above, must be disregarded in the person's hands and taken into account when determining the aggregate capital gain or aggregate capital loss of the person retaining the power of revocation.

*Paragraph 72*

A person's capital gain which can be attributed to circumstances which are similar to those referred to in section 7(8)(a) as detailed in (d) above, must be disregarded in the person's hands and taken into account when determining the aggregate capital gain or aggregate capital loss of the resident.

*Paragraph 80*

A capital gain of a trust must under specified circumstances be disregarded in the trust and taken into account for the purpose of calculating the aggregate capital gain or aggregate capital loss of a resident beneficiary.

*(f) Any amount contemplated in section 6quat(1)(a), (b) or (e) which forms part of the capital of a non-resident trust and which is included in income of a resident under section 25B(2A) or taken into account in determining the aggregate capital gain or aggregate capital loss of that resident under paragraph 80(3) of the Eighth Schedule [section 6quat(1)(f)(iii)]*

*Section 25B(2A)*

A resident that acquired a vested right to specified amounts representing capital of a non-resident trust during a year of assessment must include that amount in income in that year. The specified amounts are amounts of capital of the trust which arose from receipts or accruals that would have constituted income of the trust if it had been a resident during any previous year of assessment in which the resident had a contingent right to that amount and which was not previously subject to tax in South Africa.

*Paragraph 80(3) of the Eighth Schedule*

This paragraph is similar to section 25B(2A) because it provides that when a resident acquires a vested right to specified amounts representing the capital of a non-resident trust those amounts must be taken into account in calculating the resident's aggregate capital gain or aggregate capital loss in that year. The specified amounts are any capital gains on assets contemplated in paragraph 2(1)(b) of the Eighth Schedule if

such gains were not subject to tax in South Africa at the time they arose (for example, because of the application of a tax treaty) and any amount which would have constituted a capital gain had the trust been a resident (namely, capital gains on assets other than assets referred to in paragraph 2(1)(b) of the Eighth Schedule), provided the resident had a contingent right to the capital in the year the gain arose.

## 5.2.2 Definition of “taxable income”

As indicated in 5.2.1 a rebate for foreign taxes on income as calculated under section 6quat(1A) must be deducted from normal tax if any of the foreign-source amounts listed in 5.2.1 are included in a resident’s taxable income.

“Taxable income” is defined in section 1(1) to mean the aggregate of –

- “(a) the amount remaining after deducting from the income of any person all the amounts allowed under Part I of Chapter II to be deducted from or set off against such income; and
- (b) all amounts to be included or deemed to be included in the taxable income of any person in terms of this Act;”

It is evident from this definition that taxable income can be a positive or negative figure. Paragraph (a) of the definition of “taxable income” would become negative when the amounts allowed under Part I of Chapter II exceed the income of a person. Furthermore, Part I of Chapter II includes section 20 which deals with assessed losses.<sup>24</sup>

Even if a person has an assessed loss it does not mean that the foreign-source income has not been included in taxable income. It may have been included in taxable income in which case, assuming all the other requirements are met, the foreign tax would potentially qualify for a rebate although not in that particular year. The reason is that section 6quat(1B)(a) provides that the rebate shall not exceed an amount which bears to the total normal tax payable the same ratio as total foreign taxable income bears to total taxable income (see 5.5). If taxable income for a year of assessment is a negative figure, normal tax for that year is nil and the amount of the rebate in that year of assessment is also nil. However, it will be possible for a person to carry forward the balance of excess qualifying foreign taxes determined under paragraph (ii) of the proviso to section 6quat(1B)(a) to the immediately succeeding year of assessment to potentially qualify for a rebate in that year. Not all excess qualifying foreign taxes may be carried forward under paragraph (ii) of the proviso to section 6quat(1B)(a) (see 5.8).

### Example 4 – Set-off of local trading losses against foreign trading profits

#### *Facts:*

Company A, a resident, received foreign-source income from Country S of R100 000. Country S allowed deductions of R40 000 and levied tax at the rate of 10% on the taxable profit of R60 000, namely, R6 000,00 (R60 000 × 10%). The income is also taxable in South Africa at a rate of 28%<sup>25</sup> with deductions of only R30 000 allowable under the Act.

<sup>24</sup> “Assessed loss” means, for purposes of section 20, any amount by which the deductions admissible under section 11 exceeded the income in respect of which they are so admissible.

<sup>25</sup> The normal tax rate for companies is 27% with effect from years of assessment ending on or after 31 March 2023.

Company A also conducted other operations in South Africa and received income of R250 000 and incurred expenses of R350 000 in this regard.

*Result:*

*Calculation of taxable income / assessed loss*

**Foreign trade**

	R	R
Gross income	100 000	
Less: Deductions	<u>(30 000)</u>	
Profit from foreign trade		70 000

**South African trade**

Gross income	250 000	
Less: Deductions	<u>(350 000)</u>	
Loss from South African trade		<u>(100 000)</u>
Assessed loss for current year		<u>(30 000)</u>

Foreign taxable income of R70 000 is included in taxable income of (R30 000). The foreign tax of R6 000,00 potentially qualifies for a rebate under section 6quat(1). It is, however, not allowed as a rebate in the current year of assessment because of the limitation in section 6quat(1B)(a). The excess of R6 000,00 is carried forward to the immediately succeeding year of assessment under paragraph (ii) of the proviso to section 6quat(1B)(a).

**Example 5 – Effect of foreign trading losses on the determination of a rebate under section 6quat(1)**

*Facts:*

Company A, a resident, conducts its primary trading operations in South Africa. It also has a branch in Country N.

*Year 1*

Company A received trading income of R100 000 from a South African source. Its branch in Country N incurred a loss of R300 000.

*Year 2*

Company A received trading income of R100 000 from a South African source. Its branch in Country N derived taxable income of R400 000. Foreign tax is levied in Country N at the rate of 5%.

*Result:*

**Year 1**

**Tax position in Country N**

The branch has an assessed loss of R300 000 which is carried forward to year 2 under that country's domestic tax legislation.



**Tax position in South Africa**

The foreign assessed loss of R300 000 is ring-fenced under paragraph (b) of the proviso to section 20(1) and is carried forward to year 2. The local trade income of R100 000 is subject to normal tax at the rate of 28%.<sup>26</sup>

**Year 2****Tax position in Country N**

	R	R
Taxable income		400 000
Less: Assessed loss brought forward from year 1		<u>(300 000)</u>
Taxable income		<u>100 000</u>
Tax levied at 5%		<u>5 000,00</u>

**Tax position in South Africa****Taxable income from a foreign source**

Taxable income for year 2	400 000	
Less: Assessed loss brought forward from year 1 (Note)	<u>(300 000)</u>	100 000

**Taxable income from a South African source**

Trade income from a South African source		<u>100 000</u>
Taxable income (all sources)		<u>200 000</u>
Normal tax payable at 28% <sup>27</sup>		56 000,00

**Rebate limitation under section 6quat(1B)(a)**

Taxable income derived from all foreign sources (A) × Normal tax payable on (B)

Taxable income derived from all sources (B)

R100 000 / R200 000 × R56 000,00

= R28 000,00

The full amount of foreign tax of R5 000,00 qualifies for the rebate under section 6quat(1) in year 2.

**Note:**

With effect from years of assessment ending on or after 31 March 2023, the amount of the assessed loss to be set off is the higher of R1 million or R400 000 (R500 000 × 80%), limited to the amount of the assessed loss brought forward of R300 000.<sup>28</sup>

<sup>26</sup> The normal tax rate for companies is 27% with effect from years of assessment ending on or after 31 March 2023.

<sup>27</sup> The normal tax rate for companies is 27% with effect from years of assessment ending on or after 31 March 2023.

<sup>28</sup> Section 18 of the Taxation Laws Amendment Act 20 of 2021 read with section 9 of the Draft Rates and Monetary Amounts and Amendment of Revenue Laws Bill, 2022.

### Example 6 – Set-off of foreign trading losses against foreign trading profits

#### Facts:

Company A, a resident, conducts operations in Country S which gives rise to income of R20 million, deductible expenses of R10 million and foreign tax of R4 million. The corporate tax rate in Country S is 40%.

Company A also conducts operations in Country T which gives rise to income of R10 million and deductible expenses of R14 million. No foreign tax is payable in Country T as a result of the loss of R4 million.

Company A's operations in South Africa give rise to income of R15 million and deductible expenses of R10 million.

#### Result:

#### South African taxable income / assessed loss

##### Foreign operations

	R	R
Taxable income in Country S (R20 million – R10 million)	10 000 000	
Assessed loss in Country T (R10 million – R14 million)	<u>(4 000 000)</u>	
Taxable income from foreign operations		6 000 000

##### South African operations

(R15 million – R10 million)		<u>5 000 000</u>
Total taxable income		<u>11 000 000</u>
Normal tax payable at 28% <sup>29</sup>		3 080 000,00

#### Limitation of the rebate under section 6quat(1B)(a)

Taxable income derived from all foreign sources (A) × Normal tax payable on (B)

Taxable income derived from all sources (B)

$$= R6\,000\,000 / R11\,000\,000 \times R3\,080\,000,00$$

$$= R1\,680\,000,00$$

The rebate under section 6quat(1) is limited to R1 680 000,00. Paragraph (ii) of the proviso to section 6quat(1B)(a) provides that the excess of R2 320 000 (R4 000 000,00 – R1 680 000,00) may be carried forward to the immediately succeeding year of assessment to rank for a rebate in that year.

The effective combined foreign tax rate on foreign taxable income of R6 million is 66,7% (foreign tax of R4 000 000 / foreign taxable income of R6 000 000 × 100%).

The effective combined foreign tax rate is significantly higher than Country S's tax rate of 40%, because paragraph (b) of the proviso to section 20(1) does not prohibit the set-off of foreign trading losses against foreign trading profits, meaning that taxable income derived from all foreign sources is R6 million and not R10 million.

<sup>29</sup> The normal tax rate for companies is 27% with effect from years of assessment ending on or after 31 March 2023.

*“Transactions” between a resident’s head office in South Africa and its foreign permanent establishment”*

A resident’s South African presence (for example, a head office) may “transact” with its foreign permanent establishment (for example, a branch in Country A) and for accounting purposes charge a fee including a mark-up on those “transactions”. However, from a South African tax perspective when calculating taxable income and attributing profits to the South African presence and the foreign permanent establishment, transactions within one legal entity are not recognised.<sup>30</sup> Therefore, in this example, the fee payable by the foreign branch to the head office is not recognised in the resident’s hands (that is, there is no gross income) and the foreign branch may be allocated only a relevant portion of the external costs excluding any internal mark-up.

Assuming the services are rendered in the foreign country, it means that if, for example, the foreign government levies a foreign withholding tax on the payments by the foreign branch to the head office, the South African resident will not qualify for a rebate under section 6quat(1). The reason is that the accounting fee “charged” by the head office is not recognised for tax purposes and there is no foreign-source income which is included in the resident’s taxable income. This treatment applies irrespective of whether the withholding tax was levied on the cost portion of the “fee” or the full “fee” including the mark-up and irrespective of whether the withholding tax was permitted under a tax treaty.<sup>31</sup>

### 5.2.3 Meaning of “source” for purposes of section 6quat

“Source” is a crucial concept in a residence-based tax system like South Africa’s in –

- determining taxes to be levied on income from a South African source received by or accrued to non-residents; and
- allowing a rebate for foreign taxes on foreign-source amounts included in a resident’s taxable income.

Although the Act contains specific source rules for certain types of income in section 9, “source” is not defined in the Act. There is also no universal definition or understanding of the meaning of “source”.

The determination of whether an amount is received or accrued from a South African source (alternatively referred to as a source within South Africa) or a foreign source (alternatively referred to as a source outside South Africa) is important for purposes of section 6quat, since the rebate is allowed only for foreign taxes proved to be payable on foreign-source amounts.

In determining the source of an amount, the following must be considered:

- Domestic tax legislation, namely, section 9.
- Common law as formulated by South African courts.

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<sup>30</sup> Certain exceptions may apply to interest in the case of financial enterprises. See OECD *Model Tax Convention on Income and on Capital: Condensed version* (2017) OECD Publishing for detail.

<sup>31</sup> South Africa has reserved the right to use the version of article 7 of the OECD Model Tax Convention on Income and on Capital, and the relevant commentary, immediately prior to the July 2010 update. See OECD *Model Tax Convention on Income and on Capital: Condensed version* (2017) OECD Publishing at page 625.

- The application of the articles of relevant tax treaties.

A tax treaty may override the position which would otherwise be reached under section 9 or common law. See **Example 7**.

This approach is relevant for purposes of determining the source of gross income,<sup>32</sup> calculating the rebate under section 6quat(1) and determining the deduction of foreign taxes under section 6quat(1C)(a).

In applying this approach, if the source of an amount is South Africa, it will be treated as South African source for South African tax purposes irrespective of whether it is treated as being foreign source under a foreign jurisdiction's legislation.

#### **(a) Domestic tax legislation (section 9)**

Section 9 contains provisions to determine whether the amount of certain types of income and capital gains is received or accrued from a source within or outside South Africa. Section 9 overrides the common law position [see **5.2.3(b)**] in cases of conflict. However, the articles of a tax treaty [see **5.2.3(c)**] override section 9 and the common law in cases of conflict.

The source rules contained in section 9 do not cover all types of income, for example, income received or accrued from professional services.

The source of items of income which are not specifically covered by the Act will be determined under common law principles as formulated by the South African courts and, if applicable, tax treaties.

#### **(b) Common law as formulated by South African courts**

The particular items of income received by or accrued to a taxpayer and the facts and circumstances applicable to these items of income need to be considered when applying common law principles to determine the source of the income. In *Liquidator, Rhodesia Metals Ltd v COT, Southern Rhodesia* Stratford CJ quoted with approval that –<sup>33</sup>

“[s]ource means, not a legal concept, but something which a practical man would regard as a real source of income’, ‘the ascertainment of the actual source is a practical hard matter of fact.’ (see *Ingram’s work*, p.66.)”

The purpose of this Note is not to provide an in-depth source analysis of particular items of income. The source of income has generally been defined by the courts in terms of a two-level analysis, firstly, the identification of the originating cause of the income (as opposed to the quarter from which it was received) and, secondly, the location of that originating cause.<sup>34</sup> The courts have also noted that the originating cause may occur in different places and may even occur in different countries.<sup>35</sup>

<sup>32</sup> As defined in section 1(1).

<sup>33</sup> 1938 AD 282, 9 SATC 363 at 379.

<sup>34</sup> *CIR v Lever Brothers & Unilever Ltd* 1946 AD 441, 14 SATC 1 at 8 and *Overseas Trust Corporation Ltd v CIR* 1926 AD 444, 2 SATC 71 at 76.

<sup>35</sup> *CIR v Lever Brothers & Unilever Ltd* 1946 AD 441, 14 SATC 1 at 10. See also Interpretation Note 73 “Tax Implications of Rental Income from Tank Containers” for details on the meaning of “source”.

For example, a resident company manufactures teapots, which are sold internationally. One factory is located in South Africa and the other factory in Country B. South Africa does not have a tax treaty with Country B. Based on the specific facts and circumstances of the case, the originating cause of the income is the manufacturing activity which is conducted in two different countries. The source of the income arising from the sale of the teapots would therefore need to be apportioned between South Africa and Country B using an appropriate method.

The same approach applies for purposes of determining the source of gross income for non-residents,<sup>36</sup> calculating the rebate for foreign taxes for residents under section 6quat(1) and determining the deduction of foreign taxes under section 6quat(1C)(a). The South African jurisprudence in relation to determining source for purposes of gross income therefore remains valid for determining source for purposes of section 6quat.

Some tax commentators have suggested that the word “source” should be interpreted differently for the purposes of section 6quat than from the way in which it is interpreted in relation to the definition of “gross income”.<sup>37</sup> They argue that in the context of section 6quat “source” should be given the less-restrictive meaning of “the quarter from which it comes” rather than the meaning of “originating cause”. The purpose of this Note is not to provide an in-depth analysis of the meaning of source or to discuss alternative views on source. Nevertheless, SARS has considered this view, but does not accept it.

### (c) Deeming source rules in tax treaties which override actual source rules

Section 108(1) and (2) stipulate as follows:

**“108. Prevention of or relief from double taxation.**—(1) The National Executive may enter into an agreement with the government of any other country, whereby arrangements are made with such government with a view to the prevention, mitigation or discontinuance of the levying, under the laws of the Republic and of such other country, of tax in respect of the same income, profits or gains, or tax imposed in respect of the same donation, or to the rendering of reciprocal assistance in the administration of and the collection of taxes under the said laws of the Republic and of such other country.

(2) As soon as may be after the approval by Parliament of any such agreement, as contemplated in section 231 of the Constitution, the arrangements thereby made shall be notified by publication in the *Gazette* and the arrangements so notified shall thereupon have effect as if enacted in this Act.”

In *C: SARS v Tradehold Ltd* Boruchowitz AJA stated the following:<sup>38</sup>

“[16] Once brought into operation a double tax agreement has the effect of law. Its legal effect was described by Corbett JA in *Secretary for Inland Revenue v Downing* 1975 (4) SA 518 (A) at 523A (37 SATC 249 at 255):

‘[A]s long as the convention is in operation, its provisions, so far as they relate to immunity, exemption or relief in respect of income tax in the Republic, have effect as if enacted in Act 58 of 1962 (see s 108(2)).’

<sup>36</sup> Definition of “gross income” in section 1(1).

<sup>37</sup> As defined in section 1(1).

<sup>38</sup> 2013 (4) SA 184 (SCA), 74 SATC 263 at 269.

[17] Double tax agreements effectively allocate taxing rights between the contracting states where broadly similar taxes are involved in both countries. They achieve the objective of s 108, generally, by stating in which contracting state taxes of a particular kind may be levied or that such taxes shall be taxable only in a particular contracting state or, in some cases, by stating that a particular contracting state may not impose the tax in specified circumstances. A double tax agreement thus modifies the domestic law and will apply in preference to the domestic law to the extent that there is any conflict.”

A tax treaty between South Africa and a foreign country may contain “deemed source” rules for determining the source of certain items of income and capital gains, in which case the outcome from applying these rules is applied for purposes of the Act as a whole.

Therefore, if the outcome of the application of the deemed source rules in a tax treaty<sup>39</sup> is that the source of a particular amount is different to the position reached when applying section 9 and common law principles, the deemed tax treaty source rules apply for purposes of, amongst others, gross income and section 6quat.

It could mean that South Africa loses its right to tax a non-resident on actual South African-source income or that South Africa needs to grant a resident a rebate under section 6quat(1) on actual South African-source income. However, this is an acceptable consequence of tax treaties.

#### **Example 7 – Deeming source rule for interest under a tax treaty**

##### *Facts:*

A resident company received interest income as a result of money lent to a Namibian resident. The funds were used by the Namibian resident in South Africa.

##### *Result:*

Under section 9(2)(b)(ii) interest income is derived from a source in South Africa when it is received in respect of the use or application in South Africa by any person of funds or credit obtained under any form of interest-bearing arrangement. However, under article 11(5) of the tax treaty entered into between South Africa and Namibia, the interest income is deemed to be derived from a source in Namibia, since the payer is a person resident in Namibia. Article 11(5) reads as follows:

“5. Interest shall be deemed to arise in a Contracting State when the payer is that State itself, a political subdivision, a local authority or a resident of that State....”

Even though the funds are used by the Namibian resident in South Africa, the source of the interest is Namibia, since article 11(5) of the tax treaty overrides the source rule under section 9(2)(b)(ii).

<sup>39</sup> Taking into account any agreement reached in an applicable mutual agreement procedure.

While the tax treaty treats the interest income received by the resident company as being derived from a source in Namibia, and therefore permits Namibia to impose tax on such interest income under paragraph 2 of article 11 of the tax treaty, South Africa still has the right to tax the interest income in the resident company under paragraph 1 of article 11 of the tax treaty. However, under article 23 of the tax treaty, South Africa<sup>40</sup> will need to provide a rebate for the tax, if any, suffered in Namibia. South Africa will exercise its right to tax the income by including the interest in the resident company's gross income and taxable income and may potentially grant a rebate for Namibian tax on the interest income under section 6quat(1).

### **Example 8 – No deeming source rule for interest under a tax treaty**

*Facts:*

A resident company received interest income as a result of money lent to a person resident in Country Z. The funds were used in South Africa. Country Z taxed the resident company on the interest.

The tax treaty entered into between South Africa and Country Z does not provide for a deemed source rule for interest income in favour of Country Z.

*Result:*

Under section 9(2)(b)(ii) interest income is received from a source in South Africa when it is received in respect of the use or application in South Africa by any person of funds or credit obtained under any form of interest-bearing arrangement.

South Africa will not grant a rebate under section 6quat(1) for the taxes levied by Country Z on the interest income because the interest income is derived from a source in South Africa.

### **Example 9 – Source – Interaction between common law and a tax treaty**

*Facts:*

A resident company manufactures teapots in South Africa which are sold in stores operated by the resident company in South Africa and Country X.

Based on the specific facts and circumstances of the case, the originating cause of the income is the manufacturing activity which is conducted in South Africa.

The business profit article in the tax treaty entered into between South Africa and Country X provides that –

“the profits of an enterprise of a Contracting State shall be taxable only in that State unless the enterprise *carries on business* in the other Contracting State *through a permanent establishment* situated in that other State. If the enterprise carries on business in that manner, the profits of the enterprise may be taxed in the other State but only so much of them as is attributable to that permanent establishment”.

(Emphasis added.)

<sup>40</sup> As the country of residence.

The store operated by the resident company in Country X constitutes a permanent establishment as defined in the tax treaty. Under the tax treaty, both South Africa and Country X have a right to tax the income.

*Result:*

Section 9(2) does not contain a specific source rule for income derived from the manufacture of goods. However, under common law, based on the originating cause being in South Africa, the income is determined to be from a source in South Africa. The common law position is, however, overridden by the tax treaty when the business profit article of the tax treaty gives Country X a right to tax the profits attributable to the permanent establishment in Country X. The income underlying the attributable profits will effectively be treated as being from a foreign source. This means that the resident will potentially qualify for relief under section 6quat(1) for the taxes proved to be payable on such income in Country X.

#### 5.2.4 The source of income from services

“Services” is not defined in the Act. Consideration should therefore be given to its ordinary grammatical meaning taking into account the context in which it appears and the purpose to which it is directed.

The *Merriam-Webster Dictionary*<sup>41</sup> defines the word “service” as –

- “1 a: the occupation or function of serving // in active *service*
- b: employment as a servant // entered his *service*
- 2 a: the work performed by one that serves // good *service*
- ....
- 4 : the act of serving: such as
- ...
- b: useful labor that does not produce a tangible commodity — usually used in plural // charge for professional *services*”.

“Services” may include, amongst other things, independent professional services such as scientific, literary, artistic, educational or teaching activities as well as the activities of physicians, lawyers, engineers, architects, dentists and accountants.

#### **Example 10 – Distinction between services and goods**

*Facts:*

X is employed by Company A which manufactures washing machines.

Company A sells the washing machines to local and international customers and also provides a repair service to domestic clients.

*Result:*

X renders employment services to Company A which renders repair services to its customers. The repair services are distinguishable from the goods which Company A provides to its customers.

<sup>41</sup> [www.merriam-webster.com/dictionary/service](http://www.merriam-webster.com/dictionary/service) [Accessed 9 December 2022].



**(a) General approach in determining the source of service income**

Determining the source of service income can be complex, particularly since the type of service and the fact that it may be rendered in multiple locations may impact on the determination of the location(s) of source. Despite the possible complexities, the approach to be followed is the same as that stated in **5.2.3**.

Section 9(2) has source rules for certain types of service income. In applying section 9(2) the nature of the particular service rendered must be considered.

In the absence of section 9(2) applying it will be necessary to apply common law principles. Consequently, the concept of “originating cause” remains valid for purposes of determining the true source of income derived from services rendered. In *COT (SR) v Shein*<sup>42</sup> the court held that “*prima facie*, the test of the source of a payment for services rendered is the place where those services are rendered”. The Court also expressed the view that if certain services in a particular country were subsidiary and incidental it would not be practical to suggest that a portion of the income was sourced in that country.

In addition, consideration must be given to whether any deemed tax treaty source rules apply. For example, a number of South Africa’s tax treaties have a deemed source rule for income derived from independent professional services.

**Example 11 – Tax treaty providing for a deemed-source rule for service income**

*Facts:*

A resident company provides technical consulting services to a company resident in Eswatini<sup>43</sup> under an agreement negotiated and concluded in South Africa. The services are rendered in South Africa. The company in Eswatini does not have a presence in South Africa and *vice versa* for the resident company.

Under Eswatini’s domestic tax law a withholding tax of 15% is imposed on fees derived from independent professional services remitted to South Africa. The tax treaty between South Africa and Eswatini reduces the rate of the withholding tax to 10%.

*Result:*

The true source of the fees is where the services are rendered, namely, South Africa.

However, article 13(5) of the tax treaty between South Africa and Eswatini, which deals with technical fees, provides as follows:

“Technical fees shall be deemed to arise in a Contracting State when the payer is a resident of that State...”

Article 13(5) overrides the true source for the service fees and deems the fees to be from a source in Eswatini for purposes of the Act and the tax treaty. As a result, article 13(2) gives Eswatini a right to tax the income subject to the limitation that the tax charged may not exceed 10% of the gross amount of the fees.

<sup>42</sup> 1958 (3) SA 14 (FC), 22 SATC 12 at 15.

<sup>43</sup> Eswatini was previously called Swaziland.

South Africa also has a right to tax the income in the resident company<sup>44</sup> but article 22 imposes an obligation on South Africa to provide relief for the tax suffered in Eswatini. This obligation is met by South Africa potentially providing a rebate under section 6quat(1). To qualify for the rebate all the requirements of section 6quat must be met. For example, although Eswatini imposed the withholding tax at the domestic rate of 15%, the 5% withholding tax above the permitted rate of 10% will not meet the “proved to be payable” requirement (see 5.3.2) and will not qualify for the rebate. The 5% withholding tax paid above the permitted 10% may potentially qualify for a deduction under section 6quat(1C)(a) if all the requirements of that section are met.

**Note:**

In the absence of article 13(5), the amount would be from a South African source irrespective of whether Eswatini’s domestic tax law treated the amount as being sourced in South Africa or Eswatini.

**(b) Dominant originating cause versus subsidiary causes**

In considering the facts and circumstances of a particular item of service income, it must be determined whether the service itself is the dominant originating cause or whether the service is incidental to and part of another activity which is the dominant originating cause. The principle of determining the dominant originating cause when there is more than one originating cause is not unique to service income.

**Example 12 – Subsidiary and separate originating cause**

*Facts:*

A, a resident, manufactures factory equipment in South Africa which is sold to customers based in and outside South Africa. As part of the sale of the equipment, A provides on-site assistance with the installation of the equipment. Most of A’s clients are located in South Africa.

During the year of assessment, A sold equipment to C in Zimbabwe and sent a technician to Zimbabwe to assist with the installation. A does not have a permanent establishment in Zimbabwe.

In addition to the manufacture and sale of the equipment, A concludes contracts with some clients to provide on-site monthly maintenance services.

A has concluded a maintenance contract with three South African clients and with C.

*Result:*

**Manufacture, sale and installation**

The manufacturing of the equipment, and not the installation thereof, is the dominant originating cause of the income received by or accrued to A in respect of the manufacture and sale of the equipment. The source of the income is South Africa.

The installation services are not the dominant originating cause and are merely an incidental part of the composite supply and installation of the equipment.

<sup>44</sup> Article 13(1) of the tax treaty between South Africa and Eswatini.

**Maintenance contracts**

The monthly service contract is separate from the manufacture and sale of the equipment. The true source of the income will be where the services are rendered (see **5.2.4(c)** for the apportionment of service income between locations).

**(c) Apportionment of service income between different locations**

In the absence of section 9 or an article in a tax treaty providing otherwise, the location of the source of the income is where the service is physically rendered if the originating cause of income is the rendering of the service. The service may be rendered in more than one location, in which case an apportionment of the source of the income will be required (assuming the locations are in different countries).

For example, a single invoice may be issued for services carried out partly in South Africa and partly outside South Africa. In these situations it is necessary to consider what services were conducted in which location and to apply an appropriate basis to apportion the source of the income to its appropriate location. This apportionment will, for example, impact on whether a resident is entitled to relief from double taxation under section 6quat(1) or (1C)(a).

The appropriate basis of apportionment will depend on the facts and circumstances of the particular case. For example, if the *same* service is rendered in two countries and the same hourly rate is charged, time (for example, hours) may be an appropriate basis of apportionment. However, if a different rate is charged, a pure time basis would be inappropriate. Also, if the nature of the service rendered in the two locations is different, that would need to be taken into account in the apportionment of the income.

**5.3 Requirements for foreign taxes to be regarded as qualifying foreign taxes [section 6quat(1A) and (3)]**

Foreign taxes must meet the requirements set out in **5.3.1** to **5.3.4** to potentially qualify for a rebate under section 6quat(1). In addition, if the foreign taxes relate to a capital gain or to attributed income of a CFC, the total amount of foreign taxes which potentially qualifies for a rebate is limited under paragraphs (iA) and (iB) of the proviso to section 6quat(1B)(a). These limits, as well as the general limitation, are considered in **5.5**, **5.6** and **5.7**.

**5.3.1 The taxes must be payable on income [section 6quat(1A)]**

In determining whether a particular foreign tax qualifies as a tax on income, the basic scheme of application of the foreign tax must be compared with that of the Act. The foreign tax will be accepted as a tax on income only if the basis of taxation is substantially similar to that under the Act.

To a certain extent it is immaterial that the detail of a foreign tax law differs from South Africa's domestic tax law. The important consideration is whether the basis of taxation is substantially similar. For example, a foreign tax law may include certain items of income or may allow certain exclusions or deductions not included or allowed under South African domestic tax law, yet, it could still be considered a tax on income.

In contrast, the mere fact that a foreign tax is regarded as a tax on income by the country levying the tax or that the same term is used is insufficient. The precise nature of the foreign tax and the meaning of particular terms must be determined and considered. The foreign tax liability must be a tax on income within the South African concept of such a tax. SARS levies the following taxes on income:<sup>45</sup>

- Normal tax on taxable income, which includes a taxable capital gain (section 5)
- Withholding tax on royalties, a final tax [section 49B(1)]
- Withholding tax on interest, a final tax [section 50B(1)]
- Tax on foreign entertainers and sportspersons, a final tax [section 47B(1)]
- Turnover tax on micro businesses (section 48A)
- Dividends tax [section 64E(1)]

Any foreign taxes which are substantively similar in nature to the aforementioned taxes will be considered a tax on income. Withholding taxes which constitute an advance payment on an ultimate foreign tax liability do not qualify as a foreign tax on income, however, the underlying ultimate foreign tax liability itself may qualify as a tax on income. Foreign taxes similar to employees' tax, provisional tax and withholding tax levied on payments made to non-resident sellers of immovable property in South Africa under section 35A would therefore not qualify as a tax on income. (See "Advance payments" in **5.3.2.**)

#### *Taxes covered in a tax treaty*

Taxes covered in a tax treaty between South Africa and another country will generally qualify as a tax on income. An exception, for example, is the French wealth tax covered in article 2(3)(a)(iv) of the tax treaty between South Africa and France. It does not qualify as a tax on income because it is levied on unrealised increases in the market value of a person's assets which is not a basis that is similar to South Africa's capital gains tax legislation (which is a tax on income). If a resident is subject to a wealth tax in France, the resident will not be entitled to a rebate for foreign taxes under section 6quat(1) for that tax.

#### *Taxes levied on gross receipts*

Taxes levied on a gross receipt basis are similar to taxes levied on a turnover basis. "Gross receipts" generally have a wider meaning than "turnover" and includes gross sales and capital gains. "Turnover" would generally include only gross sales. Both the gross receipt basis and the turnover basis are concerned with taxing receipts, often at a fixed percentage, and it is irrelevant whether the recipient makes a net profit or loss.

Although South Africa primarily taxes persons on a taxable income basis, certain persons are taxed on a turnover basis when qualifying as, and electing to register as, a micro business. As noted, turnover tax on a micro business is a tax on income which means taxes levied by foreign tax jurisdictions on gross receipts or turnover will also constitute a tax on income provided the basis is similar.

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<sup>45</sup> See Binding General Ruling 9 "Taxes on Income and Substantially Similar Taxes for Purposes of South Africa's Tax Treaties".

The amount subject to tax on a gross receipt or turnover basis will not be equal to the amount subject to tax on a net profit basis but this does not mean that the full amount of the foreign tax will not potentially qualify for a rebate. For example, if Country X taxes an amount on a gross receipt or turnover basis and South Africa taxes it as part of taxable income, the amount subject to tax in Country X will be more than the amount subject to tax in South Africa. The amount of foreign tax could be greater than or less than the amount of South African tax depending on the rate at which it is levied. The amount of foreign tax will qualify for a rebate under section 6quat(1) assuming it meets all the requirements of section 6quat and will be subject to limitation under section 6quat(1B)(a) (see 5.5).

### **Example 13 – Limiting foreign taxes levied on gross receipts**

#### *Facts:*

Company Z, a resident, received income for independent professional services rendered in Country A. The presence of Company Z in Country A did not create a permanent establishment for Company Z in that country.

In year 1 Company Z received gross income of R100 000 and incurred operating expenses of R80 000 for services rendered in Country A. Country A levied tax on independent professional services at a rate of 10% on gross receipts. The tax payable in Country A was R10 000,00 (R100 000 × 10%) for year 1.

Company Z had other taxable income of R50 000 sourced in South Africa. Normal tax payable in South Africa was R19 600,00 [(R100 000 – R80 000 + R50 000) × 28%<sup>46</sup>].

#### *Result:*

From a South African tax perspective the foreign tax of R10 000,00 potentially qualifies for a rebate under section 6quat(1) but is subject to limitation under section 6quat(1B)(a):

$$\begin{aligned} & \frac{\text{Taxable income derived from all foreign sources (A)}}{\text{Taxable income derived from all sources (B)}} \times \text{Normal tax payable on (B)} \\ &= \text{R20 000} / \text{R70 000} \times \text{R19 600,00} \\ &= \text{R5 600,00} \end{aligned}$$

The amount of the rebate under section 6quat(1) in year 1 is limited to R5 600,00. The excess of R4 400,00 (R10 000,00 – R5 600,00) may be carried forward to year 2 under paragraph (ii) of the proviso to section 6quat(1B)(a) to potentially qualify for a rebate in that year.

<sup>46</sup> The normal tax rate for companies is 27% with effect from years of assessment ending on or after 31 March 2023.

*Liability for interest, additional foreign taxes, fines and penalties*

A liability for interest, additional foreign taxes, fines, penalties or any other similar obligation imposed under the tax laws of a foreign country is not regarded as a tax on income and does not qualify for a rebate under section 6quat(1).

The aforementioned expenses, except possibly for interest depending on the facts, are generally not deductible under section 11(a) read with section 23(g), since all the requirements for deduction are unlikely to be met. See **8.** for the reasons why taxes on income do not qualify for a deduction under section 11(a) read with section 23(g).

In addition, section 23(o)(ii) prohibits the deduction of certain fines and penalties.

*Foreign taxes not constituting taxes on income*

Examples of taxes which are not considered to be a tax on income include the following:

- Annual wealth taxes
- Business licence and other trade taxes
- Capital taxes<sup>47</sup>
- Capital transfer taxes
- Commodity or consumption taxes
- Company duties
- Customs and excise duties
- Diamond export levies
- Environmental taxes such as a greenhouse gas tax, carbon tax or international oil pollution compensation fund contributions levy
- Estate and inheritance taxes
- Franking credits<sup>48</sup>
- Gift or donation taxes
- Import and export duties
- Mineral export levies
- Net worth taxes
- Property or real estate taxes
- Purchase tax, similar taxes and employers' contributions collected for the financing of a social insurance scheme
- Registration duties
- Resource royalties

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<sup>47</sup> Capital taxes include, for example, taxes levied at irregular and infrequent intervals on the values of the assets or net worth owned by institutional units or on the values of assets transferred between institutional units as a result of legacies, gifts *inter vivos* or other transfers.

<sup>48</sup> For example, in Australia dividends paid to shareholders by Australian resident companies are taxed under a system known as imputation. The tax paid by the company is allocated to shareholders by franking credits attached to the dividends they receive..

- Sales tax
- Skills development levies and unemployment insurance fund contributions
- Stamp duties or security transfer taxes
- Transfer duties
- Value-added tax

**Example 14 – Foreign tax on interest-bearing bonds not qualifying as a tax on income**

*Facts:*

A resident invests in interest-bearing bonds issued in Country A. Country A levies a tax on bonds issued in that country which is payable by the issuers of the bonds but recoverable from the bondholders. The tax is imposed at a rate based on the taxable value of the bonds.

*Result:*

The tax is levied on the issue of the interest-bearing bonds and is not linked in any way to the income earned by the issuer or holder. The tax is not regarded as a tax on income for South African tax purposes.

*Consideration for the right to extract any mineral or natural oil [section 6quat(3)]*

Some countries “charge” persons for the right to extract minerals and oil. In addition to income taxes, two common methods of “charging” are the payment of royalties on the minerals and natural oil extracted, and production sharing.

“Taxes on income” as defined in section 6quat(3) specifically excludes any compulsory payment to a foreign government which constitutes consideration for the right to extract any mineral or natural oil. For example, royalty payments made in cash or in kind are excluded from taxes on income.

The terms of a particular production-sharing agreement must be considered. Generally, production-sharing agreements stipulate the percentage of resources to which the government and the contractor are entitled. The right to and ownership of the specified resources is established upfront and as such even when the resources are transferred to the government or sold on their behalf there is no payment *per se* by the contractor to the government which requires consideration. The agreement will also stipulate which costs the different parties will incur and may stipulate that the contractor will be responsible for all third-party costs. The contractor is often responsible for providing the capital, services and technical knowledge. If a production-sharing agreement is structured in such a way that a contractor is required to make a payment to a government in return for extracting the related resources and to settle that payment through product, the payment will not be considered to be a payment of a tax on income<sup>49</sup> and will not qualify for a rebate under section 6quat(1).

<sup>49</sup> Definition of “taxes on income” in section 6quat(3).

### **5.3.2 The taxes must be proved to be payable to any sphere of government of any country other than South Africa in respect of an existing foreign tax liability [section 6quat(1A)]**

#### *Proved to be payable*

A tax will be “proved to be payable” if a person has an unconditional legal liability to pay the tax in future or the person had an unconditional legal liability and paid the tax. An unconditional legal liability to pay foreign tax arises only once all the events that determine the amount of the foreign tax and the person’s liability have taken place.

Although the word “payable” includes situations in which actual payment of the tax has not yet have taken place, if an amount remains outstanding for an extended period, it may call into question whether there is indeed an unconditional obligation to pay the amount.

Given that section 6quat(1A) requires the foreign tax to be “proved to be payable” by a person **and** that no person has “any right of recovery” of the tax (see **5.3.3**), an unconditional legal liability in the context of section 6quat means the foreign tax must have been levied legitimately under the foreign jurisdiction’s tax law and tax treaty (if applicable) to potentially qualify for a rebate under section 6quat(1). If the foreign tax has not been levied legitimately under the domestic law of the foreign jurisdiction or has been levied contrary to the provisions of a tax treaty (if applicable), the foreign tax would not be “proved to be payable” and a person might, depending on the foreign laws and procedures, have a “right of recovery”. Such foreign tax would not qualify for a rebate under section 6quat(1). See **6.** for the requirements which must be met to qualify for a deduction under section 6quat(1C)(a).

A practical example includes the situation in which a foreign country levies a withholding tax at the rate specified in its domestic tax legislation and does not limit the withholding tax levied to the lower rate specified in an applicable tax treaty. The amount of foreign tax potentially qualifying for a rebate under section 6quat(1) is limited to the tax which may be levied under the applicable tax treaty. The person could possibly claim a refund of the excess withholding tax from the foreign tax authorities. The excess withholding taxes do not qualify for a deduction under section 6quat(1C)(a) (if the person had a right of recovery), section 11(a) or any other section.

Should a person exercise a right to contest a foreign tax liability by lodging an objection or taking a matter to alternative dispute resolution or to court, the disputed amount of the foreign tax liability will not be allowed as a rebate under section 6quat(1) while the tax is under dispute and not yet finally determined. The amount of the foreign tax liability under dispute will be taken into account for purposes of determining that rebate under section 6quat(1) only when the dispute is resolved. The dispute will be regarded as being resolved when, taking into account all the facts, all reasonable legal remedies relating to the tax liability have been exhausted or a decision in the matter is no longer open to such remedies, subject to what is said in the paragraph below. A person may be called upon to provide evidence to support a claim that all reasonable legal remedies have been exhausted or extinguished. SARS will not allow a rebate on the disputed amount even if a person has paid the amount pending resolution of the dispute.



There could be cases in which a person decides not to commence or continue with a dispute process, or a decision is no longer open to dispute, but the foreign government's treatment is clearly incorrect. The relevant tax in these cases is not considered to be "proved to be payable". For example, if a foreign government, in contravention of a tax treaty with South Africa, incorrectly withholds foreign tax from payments to residents, the foreign tax will not be considered to be "proved to be payable" even though the dispute process was commenced but not completed. If such foreign taxes were paid, they may, subject to meeting the necessary requirements, qualify for a deduction under section 6quat(1C)(a).

**Example 15 – Foreign country imposing withholding tax at its domestic rate of tax instead of the lower rate specified in the tax treaty**

*Facts:*

South Africa has concluded a tax treaty with Country X under which the latter may levy a withholding tax of 10% on the gross amount of interest being remitted from Country X. However, Country X levied tax at the rate of 25% on interest income remitted to a resident of South Africa, who did not carry on a trade.

The source of the interest is in Country X.

*Result:*

The resident has an unconditional legal obligation to pay tax at the rate of 10%, even though 25% was withheld. The resident may claim a rebate to the extent of 10% as specified in the tax treaty under section 6quat(1). The remaining foreign tax of 15% may not be claimed as a rebate under section 6quat(1). It may also not be claimed as a deduction under section 6quat(1C)(a), since the receipt of interest income does not constitute the carrying on of a trade.

**Example 16 – Foreign withholding taxes levied on services rendered in a foreign country – No technical services article in the tax treaty**

*Facts:*

A, a resident, renders services to Company B in Country D. A does not have a permanent establishment in Country D. Company B withholds and remits 10% withholding tax to Country D's tax authorities. The income is from a foreign source.

South Africa has a tax treaty with Country D. The tax treaty does not contain a technical services article. This means that irrespective of Country D's domestic law, the tax treaty gives South Africa the sole taxing right and does not permit Country D to charge any tax on the service fees paid by Company B to A.

*Result:*

The foreign withholding tax does not qualify for a rebate under section 6quat(1) because Country D did not have a taxing right under the tax treaty. The foreign tax is not "proved to be payable" even though it was paid. If A does not have a right of recovery (excluding a right of recovery under a mutual agreement procedure under the tax treaty or any entitlement to carry back losses to a previous year of assessment), the foreign taxes potentially qualify for a deduction under section 6quat(1C)(a).

**Example 17 – Withholding taxes levied on services rendered in a foreign country – Technical services article in the tax treaty**

*Facts:*

C, a resident, renders services to Company D in Country E. C does not have a permanent establishment in Country E. Company D withholds and remits 10% withholding tax to the tax authorities of Country E. The income is sourced in Country E.

South Africa has a tax treaty with Country E which contains a technical services article permitting Country E to tax the amount at a maximum rate of 10%.

*Result:*

The foreign withholding tax qualifies as taxes “proved to be payable” under section 6quat(1A), since it was withheld in accordance with the tax treaty. The foreign tax will qualify for a rebate under section 6quat(1) if the other requirements of the section are met.

*Tax-sparing arrangements*

Foreign taxes which are waived or rebated by a foreign government, for example, in tax-sparing arrangements,<sup>50</sup> do not qualify for a rebate under section 6quat(1) because the amount of tax waived or rebated represents an amount of tax which is not payable to a foreign government. This position may, however, be altered by the provisions of a tax treaty. For example, article 22(2) of the tax treaty with Botswana provides that in certain circumstances “Botswana tax paid” is deemed to include the amount of tax which would have been paid in Botswana but for the tax sparing arrangement.

*Payable to any sphere of government of a foreign country*

The taxes must be payable to any sphere of government of a foreign country, for example, the national, state, provincial, local or municipal sphere. A foreign levy is a tax if it requires a compulsory payment pursuant to the authority of a foreign country to levy taxes. Taxes on income imposed at a supra-national level, for example, tax imposed by the European Union on pensions paid to its former employees, do not qualify for a rebate under section 6quat(1) because it is not a tax levied by a sphere of government of a foreign country.

*Advance payments*

Many countries impose some form of advance payment for a tax liability which is finally determined and becomes unconditional only at a future date. The specific terms of these advance payments vary but are generally based upon the taxpayer’s tax liability for the preceding year of assessment or an estimate of its liability for the current year of assessment. An advance payment of an income tax liability imposed by a foreign tax jurisdiction, which is similar to South Africa’s employees’ tax or provisional tax, is made on an estimated tax liability rather than on an unconditional final tax liability. Advance payments of tax are not taxes which are proved to be payable to a foreign government and are merely advance payments of taxes which may ultimately be proved to be payable to a foreign government.

<sup>50</sup> Tax-sparing arrangements are often used to incentivise foreign investment in a country and may involve a residence country giving a tax credit not only for foreign taxes paid to the source country but also on tax spared or waived in that country.

Notwithstanding that an advance payment of a foreign income tax liability, which is similar to South Africa's employees' tax or provisional tax, is not considered to be a tax which is proved to be payable to a foreign government for purposes of section 6quat(1) and 6quat(1C)(a), it does not mean that to the extent the income is also subject to tax in South Africa that the Commissioner cannot take it into account in considering an application for a directive under paragraph 10 of the Fourth Schedule. Under paragraph 10 of the Fourth Schedule, if the circumstances warrant it the Commissioner may approve a variation to the basis used in calculating the amount of employees' tax to be deducted on a monthly basis.

The final foreign tax liability, which may arise months after the advance payments have been made, is the amount which will be regarded as being "proved to be payable" for purposes of section 6quat(1) and the deduction under section 6quat(1C)(a). Part of the final foreign tax liability may have been paid as advance payments and part of it may still be payable in the future. In contrast, the excess of advance payments above the final foreign tax liability is generally refunded and does not qualify for a rebate under section 6quat(1) or the deduction under section 6quat(1C)(a). SARS recognises that cash-flow timing mismatches will occur if a foreign tax year ends after the South African year of assessment. As a result, SARS may regard the advance or provisional tax payments as being "proved to be payable" for purposes of the rebate under section 6quat(1) and the deduction under section 6quat(1C)(a) *to the extent that* a resident taxpayer can satisfy SARS that such payments correspond to and do not exceed the final foreign tax liability.

An understanding of the relevant foreign tax is necessary in determining whether a foreign tax payment is an advance payment which is similar to South Africa's employees' tax or provisional tax. For example, in some self-assessment countries, a provisional payment is in substance a final payment which is based on actual taxable income for the particular year of assessment, not an estimate, and is not an interim partial payment made during the year which is subject to change based on the final amount submitted by the taxpayer. Such payment may be referred to as a provisional payment because it may be amended if the taxpayer is reviewed or audited and the calculation which the taxpayer submitted is amended. In this situation, and subject to obtaining a detailed understanding of the relevant foreign tax, SARS may treat the payment as a final tax payment and not a provisional tax payment.

See 7.4 regarding the treatment of foreign provisional tax payments when calculating South African provisional tax payments.

#### **Example 18 – Advance payments – Foreign-source royalty income**

*Facts:*

Resident Company R received royalty income from a source in Country S. Country S levies a withholding tax on royalty payments made by its residents to non-residents at a rate of 15%. The withholding tax levied on royalty payments made to non-residents is not a final withholding tax. A final tax determination is made on an annual basis based on taxable income which is subject to a corporate tax rate of 20%.

*Result:*

The tax withheld does not represent taxes "proved to be payable" and does not qualify for a rebate under section 6quat(1).

### **Example 19 – Advance payments – Foreign-source service income**

*Facts:*

A natural person resident in South Africa took up employment in Country Z.

The resident's remuneration is subject to a payroll withholding tax in Country Z. The payroll withholding tax is similar to South Africa's employees' tax system and represents an advance payment of the resident's tax liability in Country Z. The resident's tax liability in Country Z is determined on an assessment basis.

South Africa does not have a tax treaty with Country Z.

*Result:*

The payroll withholding taxes levied on the service income sourced in Country Z do not constitute foreign taxes which are proved to be payable, which will potentially qualify for a rebate under section 6quat(1), without a right of recovery. The final foreign tax proved to be payable is only determined upon assessment. Therefore these withholding taxes do not qualify for a rebate under section 6quat(1).

Notwithstanding that the payroll withholding taxes do not qualify for a rebate under section 6quat(1), depending on the circumstances there may be grounds for the employer to apply under paragraph 10 of the Fourth Schedule for the payroll withholding taxes to be taken into account to the extent that income is also subject to employees' tax when calculating the amount of employees' tax which must be deducted and paid over to SARS on a monthly basis.

### **5.3.3 The taxes on income must be proved to be payable without any right of recovery by any person [section 6quat(1A)]**

A resident is entitled to claim a rebate under section 6quat(1) for a foreign tax on income only to the extent that the amount of the foreign tax is proved to be payable to a sphere of government of a foreign country *without a right of recovery by any person (other than a right of recovery under any entitlement to carry back losses arising during any year of assessment to any year of assessment before such year of assessment)*.

"Right of recovery by any person" is interpreted very broadly and includes any form of relief against a foreign tax liability. For example, a refund, credit, rebate, remission, or deduction, is considered to be a right of recovery. Any other form of economic benefit to which a person becomes entitled to in consequence of the payment of the relevant tax is also considered to be a "right of recovery by any person".

Examples of economic benefits include the following:

- Goods received
- Services rendered
- Fees or other payments
- Rights to use, acquire or extract any resources or other property
- Discharge of contractual obligations

- Linked subsidies<sup>51</sup>

The “right of recovery” may be by the taxpayer or any other person and includes situations in which a holder of shares in a company receives a refund for the tax paid by the company. The amount which the company could potentially claim as a rebate under section 6quat(1) would be reduced by the amount of the refund received by the holder of the shares.

If a person is entitled to but chooses not to seek a refund, the amount not refunded will still not qualify for a rebate under section 6quat(1) because a right of recovery for the amount existed. The existence of a right of recovery and not the enforcement of that right is the relevant factor. A resident claiming a rebate under section 6quat(1) must disclose relevant information to SARS when any person, including the resident, becomes entitled to a right of recovery in respect of a foreign tax liability incurred by that resident.

**Example 20 – Right of recovery of foreign tax by means of a government subsidy**

*Facts:*

Two resident retail companies formed a joint venture to distribute and sell products owned by the government of Country A in Country A. In Country A the joint venture is regarded as a taxable entity. The joint venture sold the products at inflated prices which resulted in an increase in its liability for tax. The government of Country A in turn gave the joint venture a subsidy as a form of economic incentive to compensate for the extra taxes paid owing to the inflated sale prices. The income received for the distribution and selling of the products was from a foreign source.

In South Africa each company wanted to claim a rebate under section 6quat(1) based on its proportionate share of the total amount of foreign taxes paid by the joint venture without taking into account the amount of the government subsidy received.

*Result:*

The treatment applied by the two resident companies is incorrect and must be corrected. In determining the amount of the rebate under section 6quat(1A) to be allowed under section 6quat(1), the foreign tax liability must be reduced by the amount of the government subsidy. The amount of the government subsidy must be apportioned between the companies based on each company’s interest in the joint venture.

<sup>51</sup> K Vogel *Double Taxation Conventions* 3 ed (1997) Kluwer Law International Ltd London United Kingdom in paragraph 154 at page 1223 - Klaus Vogel's<sup>51</sup> remarks provide further insight on the nature of this item, namely, “[i]f any of the tax collected is returned to the taxpayer in the form of a (non-repayable) subsidy – as it is in certain cases under Brazilian law – the allowable credit is restricted to the amount of tax remaining after the deduction of the subsidy...”.

### **5.3.4 The taxes must be proved to be payable in respect of amounts included in a resident's taxable income [section 6quat(1A) and paragraph (ii) of the proviso to section 6quat(1A)]**

The foreign taxes must be "proved to be payable" in respect of specified foreign-source amounts which are included in a resident's taxable income. The specified foreign-source amounts are considered in **5.2**.

#### *Foreign taxes payable in respect of exempt foreign dividends*

Foreign taxes which are payable in respect of exempt income will generally not qualify for a rebate under section 6quat(1), since, as noted above, the foreign taxes must be "proved to be payable" in respect of amounts included in a resident's taxable income. For example, foreign taxes attributable to an amount exempt under section 10(1)(o)(ii) will not qualify for a rebate under section 6quat(1). However, the full amount of foreign taxes payable in respect of the exempt portion of foreign dividends under section 10B(3) will potentially qualify for a rebate under section 6quat(1).<sup>52</sup> While the full amount of the exempt foreign dividends must be included under paragraph (ii) of the proviso to section 6quat(1A) in the resident's taxable income for the purpose of determining the amount of foreign taxes which potentially qualify for the rebate under section 6quat(1), those foreign taxes will still be subject to the limitation determined under section 6quat(1B)(a) (see **5.5.2**).

## **5.4 Persons by whom foreign taxes on income must be proved to be payable [section 6quat(1A) and paragraph (i) of the proviso to section 6quat(1A)]**

### **5.4.1 General introduction**

Generally, the person potentially entitled to claim a rebate under section 6quat(1) is a resident that is liable to pay foreign tax on a foreign-source amount included in the resident's taxable income.

However, in the circumstances mentioned in section 6quat(1A)(b) and (f) and paragraph (i) of the proviso to section 6quat(1A), a resident may take an amount of foreign tax into account notwithstanding that another person was liable for the amount of foreign tax. For example, in calculating the rebate under section 6quat(1) a resident must take into account an amount of foreign tax which that resident's spouse was liable for, provided the related foreign-source amount is deemed to have accrued to the resident under section 7(2).<sup>53</sup> The resident's spouse is not allowed to claim a rebate for the foreign taxes proved to be payable under these circumstances, since the foreign-source amount is not included in the spouse's taxable income.

In the context of withholding taxes, although the payer of an amount (for example, a royalty) is required to withhold and remit an amount of tax to the relevant foreign government, the tax itself is generally levied on the amount which is received by or accrues to the payee and the payee is the person who is liable to pay the foreign tax, not the payer. In these circumstances the payee is the person that would potentially qualify for a rebate under section 6quat(1). The specific wording of the legislation must be considered to determine if the payer or payee is liable for the tax.

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<sup>52</sup> Paragraph (ii) of the proviso to section 6quat(1A).

<sup>53</sup> Section 6quat(1A)(f).

#### 5.4.2 Foreign taxes must be proved to be payable by specified persons [section 6quat(1A)]

The qualifying foreign taxes on income taken into account in calculating the rebate under section 6quat(1) must be proved to be payable by any of the following persons:

- A resident in respect of –
  - any income received by or accrued to that person from a foreign source [section 6quat(1A)(a)(i)]; or
  - any amount of taxable capital gain contemplated in section 26A derived from a foreign source [section 6quat(1A)(a)(iii)].
- A CFC in respect of the proportional amount of the CFC's net income which is attributed to a resident under section 9D(2), subject to section 72A(3)<sup>54</sup> [section 6quat(1A)(b)].
- A person in respect of the amounts of income received or accrued from a foreign source or any proportional amount of a CFC's net income which is to be included in another resident's income under section 9D(2), if the amount is deemed to have been received by or accrued to a resident under section 7 [section 6quat(1A)(f)].
- A person in respect of any amount of capital gain from a source outside the Republic which is attributed to a resident under paragraph 68, 69, 70, 71, 72 or 80 of the Eighth Schedule [section 6quat(1A)(f)].
- A non-resident trust in respect of the following amounts which represent the capital of that trust and which is included in a resident's income under section 25B(2A) or taken into account in determining that resident's aggregate capital gain or aggregate capital loss under paragraph 80(3) of the Eighth Schedule:
  - Any income received or accrued from a foreign source.
  - The proportional amount of a CFC's net income which is attributed to a resident under section 9D(2).
  - Any amount of a taxable capital gain contemplated in section 26A derived from a foreign source [section 6quat(1A)(f)].

In addition, when the resident is either a member of a partnership or a beneficiary of a trust and the partnership or trust is liable for tax as a separate entity in a foreign country, a proportional amount of tax payable by that entity is deemed to be payable by that resident member or beneficiary for purposes of section 6quat(1A). The proportional amount must be determined with reference to the resident's interest in the partnership or trust in relation to the total interest held in the partnership or trust [paragraph (i) of the proviso to section 6quat(1A)].<sup>55</sup>

<sup>54</sup> See 5.7.1 for a consideration of section 72A.

<sup>55</sup> See Binding Private Ruling 222 "Foreign Partnership – Rebate in respect of Foreign Taxes on Income".

As noted above, foreign tax may be “proved to be payable” by a person other than a resident in whose taxable income certain amounts are included, for example:

- A resident’s spouse when the underlying income is deemed to have accrued to that resident under section 7(2).
- A trust when the underlying income is deemed to have been received by a resident parent of a minor child under section 7(3) or (4).
- A trust or the beneficiary of a trust when any of paragraphs 68 to 72 or 80 of the Eighth Schedule attributes a capital gain to that resident.
- A discretionary trust when section 25B(2A) applies to include an amount in that resident’s income.
- A partnership which is treated as a separate entity for tax purposes in another country on an amount included in that resident partner’s taxable income.
- A CFC on a proportional amount included in that resident’s taxable income under section 9D(2).

**Example 21 – Foreign taxes proved to be payable by a resident discretionary trust with resident and non-resident beneficiaries**

*Facts:*

Resident discretionary Trust A derived local and foreign sourced income. It has resident and non-resident beneficiaries. The trust disposed of fixed property located in a foreign country which resulted in a capital gain. The trust was liable for foreign taxes on the capital gain in the foreign country. The capital gain was vested in the resident and non-resident beneficiaries during the same year of assessment in which the property was disposed of.

Paragraphs 68 – 71 of the Eighth Schedule do not apply.

*Result:*

Under paragraph 80(2) of the Eighth Schedule the portion of the capital gain vested in resident beneficiaries is disregarded in the trust and taken into account as a capital gain in the calculation of the relevant resident beneficiary’s aggregate capital gain or aggregate capital loss. A proportional amount of the foreign tax payable by the trust on the capital gain which is attributable to the relevant resident beneficiary’s interest in the capital gain will be deemed to be payable by the resident beneficiary under paragraph (i) of the proviso to section 6quat(1A) and the resident beneficiary will potentially qualify for a rebate under section 6quat(1) if the requirements of the section are met.

The portion of the capital gain vested in non-resident beneficiaries remains a capital gain for the trust, since paragraph 80(2) does not allow capital gains to be attributed to non-resident beneficiaries. The portion of the foreign tax payable by the trust on the portion of the capital gain retained in the trust is regarded as payable by the trust and the trust will potentially qualify for a rebate under section 6quat(1) if the requirements of the section are met.



## 5.5 Limitation of the amount of the rebate [section 6quat(1B)(a)]

The amount of foreign taxes which qualify for the rebate under section 6quat(1) in a particular year of assessment is the lesser of –

- the sum of the qualifying foreign taxes;<sup>56</sup> or
- the amount calculated under the limitation as set out below.

The limitation is calculated as follows:<sup>57</sup>

Taxable income derived from all foreign sources (A) × Normal tax payable on (B)  
Taxable income derived from all sources (B)

“Taxable income derived from all foreign sources” includes all amounts of foreign-source income which were included in the resident’s total taxable income regardless of the rate of foreign tax (if any) to which those amounts are subject. The taxable income of both the numerator and the denominator is determined according to the Act. “Taxable income from all foreign sources” is limited to “Taxable income derived from all sources” – See Example 26.

Normal tax is South African income tax calculated under the Act on taxable income. It is determined before the deduction of any rebates contemplated in sections 6, 6A, 6B and 6quat(1).

The purpose of the limitation in section 6quat(1B)(a) is to ensure that the rebate granted for foreign taxes proved to be payable relates only to the foreign income included in a resident’s taxable income. If no foreign income is included in a resident’s taxable income, no rebate will be available even if the foreign tax is proved to be payable by the resident. The purpose of the rebate under section 6quat(1) is to provide relief to residents for the foreign taxes proved to be payable to the extent that the foreign-source amount has also been taxed in South Africa. The purpose is not to subsidise the tax base of foreign jurisdictions by providing relief for all foreign taxation.

The application of the limitation under section 6quat(1B)(a) results in normal tax being reduced only by foreign taxes payable on foreign-source amounts. The limitation does not reduce normal tax payable on South African-source amounts.

The limitation is an “overall” limitation in the sense that all the foreign-source amounts derived from different foreign sources are added together without being subdivided further between the different foreign countries from which the amounts were derived. This is in contrast to the “per country” limitation or the “per income item” limitation adopted in some countries.

Effectively the “overall” limitation divides a resident’s taxable income into two separate components, namely, taxable income derived from –

- a South African source; and
- a foreign source.

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<sup>56</sup> The sum of qualifying foreign taxes is potentially limited in relation to situations dealing with capital gains (see 5.6) and attributed income of CFCs (see 5.7).

<sup>57</sup> Section 6quat(1B)(a).

Under an overall limitation system, all qualifying foreign taxes are aggregated and the rebate is limited (capped) at the lesser of the aggregate of the foreign taxes proved to be payable and the proportion of normal tax payable on the resident's foreign taxable income.

Before applying the limitation under section 6quat(1B)(a), one must first determine –

- income from a South African source; and
- income from a foreign source (see 5.2.3).

Secondly, a taxable income computation must be performed under South African tax principles and requirements to determine the taxable income resulting from –

- the income derived from South African sources; and
- the income derived from foreign sources.

In determining the taxable income derived from a foreign source, the following principles must be applied:

- Any expenditure incurred which is directly attributable to income derived from a foreign source must be deducted from such income (assuming it meets the requirements for deductibility under the relevant section and irrespective of whether such expenditure is incurred in or outside South Africa).
- A portion of any general expenses incurred which are not directly attributable to income derived either from a South African source or a foreign source, for example, head office expenses, must be apportioned between taxable income<sup>58</sup> derived from South African sources and foreign sources.
- If apportionment is required it must be based on any method which gives a fair and reasonable result appropriate to the circumstances of the particular case (for example, turnover, gross profit or value of fixed assets).<sup>59</sup>

**Example 22 – Expenses incurred in South Africa attributable to foreign-source income**

*Facts:*

Resident Company A incurred expenditure in obtaining advice from a South African legal adviser on the operations of a foreign branch located in Country B.

*Result:*

Although the expenditure was incurred in South Africa, it relates directly to Company A's foreign operations and must be deducted from the foreign branch's income when calculating taxable income derived from foreign sources.

<sup>58</sup> Assuming it meets the requirements for a deduction.

<sup>59</sup> This approach is endorsed in *International Tax Primer* 2 ed (2002) Kluwer Law International The Hague The Netherlands at page 48 by Brian Arnold advocating two methods for allocating expenses, namely, tracing and apportionment.

**Example 23 – Foreign expenses attributable to South African-source income***Facts:*

Resident Company A incurred expenditure in obtaining advice from a solicitor based in London for a deal it concluded for the sale of various products manufactured in South Africa to a person resident in London. This expenditure meets the requirements of section 11(a). Company A has a branch in London which manufactures a different line of products to those manufactured in South Africa.

*Result:*

The expense relates directly to the sale of products manufactured by Company A in South Africa. The expense may not be deducted from income received or accrued from the branch in London when calculating taxable income arising from a foreign source.

The expense must be deducted from South African-source income when calculating Company A's taxable income from all sources.

The Act requires taxable income to be calculated separately for each trade carried on by a person.<sup>60</sup> Consequently, any expense attributable to a particular trade must be deducted in determining that trade's taxable income and may not be deducted in determining the taxable income derived from another trade carried on by a person. Taxable income from a taxpayer's various trades is aggregated except that assessed losses (current or prior year) from carrying on a trade outside South Africa may not be set off against any amount derived from a South African source.<sup>61</sup> The trades (local and foreign) of a resident that trades in and outside South Africa are regarded as two separate trades for purposes of the Act. This treatment will apply even if the operations conducted inside South Africa and outside South Africa are identical in nature, for example, a retail operator with retail shops in South Africa and outside South Africa.

**Example 24 – Application of section 6quat(1B)(a) – Allocation of expenses relating to foreign-source income***Facts:*

Resident Company A received the following income in a year of assessment:

	R
Taxable income from a South African source	1 000
Taxable income from a foreign source attributable to a foreign permanent establishment	100

The above-mentioned amounts do not include the borrowing of R100 by the foreign branch from a financial institution in South Africa at 10% interest and the investment of that R100 in a bank deposit in the foreign country where the branch is located. The deposit earned interest at 11%.

<sup>60</sup> See, for example, the preamble to section 11 which provides that for the purposes of calculating the taxable income from carrying on any trade, specified deductions are permitted, and section 20(1)(b) which refers to the set-off of an assessed loss from one trade against the income from another. See also *C v COT* 1966 (3) SA 6 (RAD) 28 SATC 127.

<sup>61</sup> Paragraph (b) of the proviso to section 20(1).

The corporate tax rate is 40% in the foreign country and 28%<sup>62</sup> in South Africa.

*Result:*

The interest incurred by the foreign branch of R10 relates to the earning of foreign-source interest of R11 and must therefore be claimed as a deduction in the calculation of the foreign-source taxable income.

	Taxable income (foreign source)	Taxable income (all sources)
	R	R
Taxable income before interest	100	1 100
Interest income	11	11
Interest expense	(10)	(10)
Taxable income	<u>101</u>	<u>1 101</u>

**Tax payable**

Foreign tax (R101 × 40%)	40,40
South African normal tax (R1 101 × 28% <sup>63</sup> )	308,28

**Limitation of the rebate under section 6quat(1B)(a)**

$\frac{\text{Taxable income derived from all foreign sources (A)}}{\text{Taxable income derived from all sources (B)}} \times \text{Normal tax payable on B}$

= R101 / R1 101 × R308,28

= R28,28

The amount of foreign taxes proved to be payable is R40,40. However, the amount qualifying for a rebate under section 6quat(1) is limited to R28,28. The excess of R12,12 (R40,40 – R28,28) may be carried forward to the immediately succeeding year of assessment in which it will be deemed to be foreign tax paid in that year on foreign-source income.

<sup>62</sup> The normal tax rate for companies is 27% with effect from years of assessment ending on or after 31 March 2023.

<sup>63</sup> The normal tax rate for companies is 27% with effect from years of assessment ending on or after 31 March 2023.

**Example 25 – Determination of the rebate under section 6quat(1) – No limitation under section 6quat(1B)(a)**

*Facts:*

Resident Company A conducts its trading operations in South Africa. It also has a branch in Country L.

The following results are applicable to the year of assessment:

	South Africa	Country L	Total
	R	R	R
Turnover	8 000	2 000	10 000
Less: Direct expenses	(2 000)	(800)	(2 800)
Less: Indirect expenses			<u>(600)</u>
Taxable income (all sources)			<u>6 600</u>
Foreign taxes proved to be payable			108,00
South African normal tax (R6 600 × 28% <sup>64</sup> )			1 848,00

*Result:*

**Calculation of taxable income derived from Country L**

Turnover	2 000
Less: Direct expenses	(800)
Less: Indirect expenses	<u>(120)*</u>
Taxable income	<u>1 080</u>

\* Indirect expenses apportioned to branch in Country L based on turnover

$$= (R2\,000 / R10\,000) \times R600$$

$$= R120$$

**Limitation of the rebate under section 6quat(1B)(a)**

Taxable income derived from all foreign sources (A) × Normal tax payable on B

Taxable income derived from all sources (B)

$$= (R1\,080 / R6\,600) \times R1\,848,00$$

$$= R302,40$$

The amount of foreign taxes proved to be payable is R108,00. Therefore the full amount of R108,00 qualifies for a rebate under section 6quat(1).

<sup>64</sup> The normal tax rate for companies is 27% with effect from years of assessment ending on or after 31 March 2023.

**Example 26 – Determination of rebate – No limitation under section 6quat(1B)(a)***Facts:*

Resident Company A conducts its trading operations in South Africa. It also has a branch in Country L.

The following results are applicable to the year of assessment:

	South Africa	Country L	Total
	R	R	R
Turnover	10 000	4 000	14 000
Less: Direct expenses	(12 000)	(500)	(12 500)
Taxable income (all sources)	(2 000)	3 500	1 500
Foreign taxes proved to be payable			700,00
South African normal tax (R1 500 × 28% <sup>65</sup> )			420,00

*Result:***Limitation of the rebate under section 6quat(1B)(a)**

$$\frac{\text{Taxable income derived from all foreign sources (A)}}{\text{Taxable income derived from all sources (B)}} \times \text{Normal tax payable on B}$$

$$= (\text{R3 500 limited to R1 500} / \text{R1 500}) \times \text{R420,00}$$

$$= \text{R420,00}$$

The amount of foreign taxes proved to be payable is R700,00. However, the amount qualifying for a rebate under section 6quat(1) is limited to R420,00. The excess of R280,00 (R700,00 – R420,00) may be carried forward to the immediately succeeding year of assessment in which it will be deemed to be foreign tax paid in that year on foreign-source income.

**Example 27 – Determination of rebate – Application of the limitation under section 6quat(1B)(a)***Facts:*

Resident Company A conducted share-dealing activities through a branch operated by a dependent agent<sup>66</sup> in Country M. The branch bought shares in a foreign company resident in Country M for R10 000. The branch received a gross payment of R1 000 from which withholding tax of R150,00 was deducted. The payment was made from the foreign company's income reserves. Under Country M's tax laws the amount distributed is treated as a payment of interest and not as a payment of a dividend.

The shares were held by Company A as trading stock. During the same year of assessment the foreign branch sold the shares for R9 500. The sale of the shares did not result in a tax liability in Country M.

<sup>65</sup> The normal tax rate for companies is 27% with effect from years of assessment ending on or after 31 March 2023.

<sup>66</sup> A dependent agent may create a permanent establishment, unlike an independent agent.

Expenses of R300 were incurred on these transactions. No other transactions or activities were concluded by Company A.

*Result:*

The amount received by Company A does not constitute a foreign dividend<sup>67</sup> for South African tax purposes because the foreign payment is not treated as a dividend for income tax purposes under the tax laws of the country where the company paying the foreign amount is resident. The receipt of R1 000 constitutes a revenue receipt, since the shares were held as trading stock and the payment was from the foreign company's income reserves (that is, it was not a capital distribution).

**Calculation of taxable income**

	R
Sale of shares	9 500
Revenue receipt	<u>1 000</u>
	10 500
Less: Acquisition cost	(10 000)
Less: Other expenses	<u>(300)</u>
Taxable income – foreign source	200
Taxable income – South African source	<u>0</u>
Taxable income (all sources)	<u>200</u>
Normal tax payable (R200 × 28% <sup>68</sup> )	56,00
Foreign withholding taxes	150,00

**Limitation of the rebate under section 6quat(1B)(a)**

Taxable income derived from all foreign sources (A) × Normal tax payable on B

Taxable income derived from all sources (B)

$$= R200 / R200 \times R56,00$$

$$= R56,00$$

The rebate is limited to R56,00 under section 6quat(1B)(a). The excess of R94,00 (R150,00 – R56,00) may be carried forward to the immediately succeeding year of assessment during which it will be deemed to be foreign tax paid in that year on foreign-source income.

<sup>67</sup> As defined in section 1(1).

<sup>68</sup> The normal tax rate for companies is 27% with effect from years of assessment ending on or after 31 March 2023.

### 5.5.1 Deductions for contributions to retirement funds and donations [paragraph (i) of the proviso to section 6quat(1B)(a)]

*Years of assessment commencing on or after 1 March 2018*<sup>69</sup>

In determining the amount of the taxable income that is attributable to the income, proportional amount, taxable capital gain or amount referred to in section 6quat(1)<sup>70</sup> –

- any allowable deductions under sections 11F and 18A must be deemed to have been incurred proportionately in respect of taxable income derived from sources within and outside the Republic;
- the deduction under section 11F must be allocated in relation to the taxable income from sources within and outside the Republic before taking into account any deduction under that section, section 6quat(1C)(a) and section 18A; and
- the deduction under section 18A must be allocated in relation to taxable income from sources within and outside the Republic before taking into account any deduction under that section and section 6quat(1C)(a).

The following sequence must be followed to calculate the deductions under sections 11F and 18A:

	R
Gross income from all sources	XXX
Less: Exempt income – section 10(1)	(XXX)
Income	XXX
Less: Deductible expenditure	(XXX)
Taxable capital gain from all sources	XXX
Taxable income before contributions to retirement funds and donations to certain organisations	XXX
Less: Contributions to retirement funds – section 11F*	(XXX)
Donations to certain organisations – section 18A**	(XXX)
Taxable income from all sources	XXX

\* When calculating the deduction for contributions to retirement funds under section 11F on or after 1 March 2016, the taxable capital gain must be included in the amount on which the 27,5% allowable deduction is calculated under section 11F(2)(b)(ii). This treatment must be contrasted with the calculation under section 11F(2)(c) which specifically requires any taxable capital gain to be excluded from taxable income for purposes of that calculation.

\*\* The deduction under section 18A is generally based on taxable income. Taxable capital gains form part of taxable income as determined before the deduction under section 18A is calculated. Thus, taxable capital gains must generally be taken into account in determining the deduction under section 18A.

See the examples in **Annexure B**.

<sup>69</sup> See earlier issues of this Note for the deductions for retirement annuity fund contributions and donations in earlier years.

<sup>70</sup> That is, taxable income from a foreign source as referred to in section 6quat(1) – see 5.5.



### 5.5.2 Foreign taxes payable on exempt foreign dividends [paragraph (ii) of the proviso to section 6quat(1A) and section 6quat(1B)(a)]

As noted in 5.2 and 5.3, foreign taxes proved to be payable in respect of exempt income will generally not qualify for a rebate under section 6quat(1). Paragraph (ii) of the proviso to section 6quat(1A) contains an exception to this rule by providing that when determining the foreign taxes that potentially qualify for the rebate, the amount included in the resident's taxable income must be determined without regard to the partial exemption in section 10B(3). The amount of foreign taxes relating to the exempt portion of foreign dividends under section 10B(3) will therefore potentially qualify for a rebate.

This exception under paragraph (ii) of the proviso to section 6quat(1A) does not extend to the limitation determined under section 6quat(1B)(a). Paragraph (ii) of the proviso to section 6quat(1A) states "for the purposes of this subsection", namely, section 6quat(1A). The application of paragraph (ii) of the proviso is therefore limited to section 6quat(1A) and does not extend to the other provisions of section 6quat. "Taxable income" and "normal tax payable" in section 6quat(1B)(a) have their ordinary meaning under the Act. In calculating taxable income and normal tax for purposes of section 6quat(1B)(a) the portion of foreign dividends which are exempt under section 10B(3) is therefore excluded.

To the extent that the amount of qualifying foreign taxes payable, including the foreign taxes payable on the exempt portion of foreign dividends, exceed the amount of the rebate [after applying paragraphs (i), (iA) and (iB) of the proviso to section 6quat(1B)(a)], the excess may be carried forward to the immediately succeeding year of assessment and will potentially qualify for a rebate in that year (see 5.5 to 5.8).

#### **Example 28 – Foreign taxes qualifying for a rebate under section 6quat(1)**

##### *Facts:*

Resident Company X received income from local and foreign sources.

The income from foreign sources and the foreign tax (see below) have already been translated to rand.

##### **Foreign-source income**

###### (1) Foreign dividends

Company X holds 5% of the equity shares in Company Y, a foreign company. On 20 February year 1 Company Y declared a dividend of R1 405 920 (amount before withholding tax). A dividend of R70 296 (R1 405 920 × 5%) accrued to Company X on 20 February year 1. Withholding tax of R7 851,12 was deducted from the gross amount of the dividend.

###### (2) Loss incurred by a foreign branch

Company X's foreign branch incurred a loss for the year of R30 000.

##### **South African-source income**

During the year of assessment ending on 28 February year 1 Company X received consulting fees of R1 million and interest income of R100 000. No expenses were incurred in the production of the consulting fees and interest income.

<i>Result:</i>	
<b>1 Tax calculation</b>	
<b>1.1 Taxable income from foreign sources</b>	
	R
Foreign dividends included in gross income (Note 1)	70 296
Less: Exemption under section 10B(3) [R70 296 × 8 / 28]	(20 085)
Less: Loss incurred by foreign branch (Note 1)	<u>(30 000)</u>
Taxable income from foreign sources	<u>20 211</u>
<b>1.2 Taxable income from South African sources</b>	
Consulting fees	1 000 000
Interest	<u>100 000</u>
Taxable income from South African sources	<u>1 100 000</u>
<b>1.3 Total taxable income from all sources</b>	
Taxable income from foreign sources	20 211
Taxable income from South African sources	<u>1 100 000</u>
Total taxable income from all sources	<u>1 120 211</u>
<b>1.4 Normal tax calculation</b>	
<b>(a) Calculation of normal tax payable before rebates</b>	
	R
Normal tax payable (R1 120 211 × 28% <sup>71</sup> )	313 659,08
<b>(b) Calculation of the rebate under section 6quat(1)</b>	
Amount of foreign taxes proved to be payable (Notes 2 and 3)	7 851,00
<i>Limitation of the rebate under section 6quat(1B)(a)</i>	
<u>Taxable income derived from all foreign sources (A)</u> × Normal tax payable on B	
Total taxable income derived from all sources (B)	
<u>R20 211</u> × R313 659,08	
R1 120 211	
= R5 659,08	
Therefore, the amount of the rebate is R5 659,08 (Note 4).	
<b>(c) Calculation of normal tax payable after the rebate under section 6quat(1)</b>	
	R
Normal tax payable before rebates	313 659,08
Less: Rebate under section 6quat(1)	<u>(5 659,08)</u>
Normal tax payable	<u>308 000,00</u>

<sup>71</sup> The normal tax rate for companies is 27% with effect from years of assessment ending on or after 31 March 2023.

**Notes:**

- (1) The spot rate was applied under section 25D(1) to translate amounts received or accrued and expenditure incurred to rand.
- (2) The average exchange rate was applied under section 6quat(4) to translate the foreign taxes to rand (see 7.1). The amount of R7 851,12 was rounded off to R7 851,00 under section 6quat(4A) (see 7.2).
- (3) Under paragraph (ii) of the proviso to section 6quat(1A) the amount of foreign taxes attributable to the exempt portion of foreign dividends under section 10B(3) is included in the foreign taxes which qualify for the rebate under section 6quat(1).
- (4) R5 659,08 of the qualifying withholding tax of R7 851,00 is deductible from normal tax payable. The balance of R2 191,92 (R7 851,00 – R5 659,08) is carried forward to the next year of assessment to be used in determining the rebate under section 6quat(1) for that year.

See **Examples 1 to 5** in **Annexure B** which illustrate the tax treatment of foreign taxes on exempt foreign dividends received by or accrued to natural persons.

## **5.6 Application of section 6quat to capital gains [paragraph (iB) of the proviso to section 6quat(1B)(a)]**

### **5.6.1 General capital gains tax principles**

As noted in 5.2, foreign taxes on foreign capital gains potentially qualify for a rebate under section 6quat(1). The amount of the rebate is equal to the amount of any foreign taxes proved to be payable on the taxable capital gain<sup>72</sup> reduced as required by the three-step limitation process under section 6quat(1), (1A) and (1B)(a) (see 5.6.4).

The following capital gains tax principles are particularly relevant when calculating a rebate to be allowed under section 6quat(1) for foreign taxes proved to be payable on foreign capital gains:

- A person's taxable capital gain for a year of assessment is equal to the relevant inclusion rate multiplied by the person's net capital gain for the year.<sup>73</sup>
- A person's "net capital gain" for a year of assessment is, amongst other things, the positive amount remaining after deducting any assessed capital loss brought forward from the previous year of assessment from the aggregate capital gain for the year.<sup>74</sup>
- A person's aggregate capital gain or loss (as appropriate) for a year of assessment is equal to the sum of the capital gains for the year plus the other capital gains required to be taken into account less the sum of the capital losses for the year less or plus<sup>75</sup> the annual exclusion<sup>76</sup> (for a natural person or special trust).<sup>77</sup>

<sup>72</sup> Section 6quat(1A)(a)(iii).

<sup>73</sup> Paragraph 10 of the Eighth Schedule.

<sup>74</sup> Paragraph 8 of the Eighth Schedule.

<sup>75</sup> The annual exclusion reduces both gains and losses.

<sup>76</sup> The annual exclusion is limited to the sum of capital gains and capital losses in a year of assessment.

<sup>77</sup> Paragraphs 6 and 7 of the Eighth Schedule.

### 5.6.2 Inclusion of a foreign-source taxable capital gain in taxable income

A resident may choose the order in which capital gains are reduced by any capital losses and the order in which an assessed capital loss brought forward from the previous year of assessment is applied against capital gains. In determining the aggregate capital gain, a person may in the first instance allocate capital losses against those capital gains on which no foreign tax liability was incurred. Any excess capital losses must then be applied against those capital gains derived from a foreign source that were subject to foreign tax. Also, in determining the net capital gain, the resident may in the first instance allocate carried forward assessed capital losses against those capital gains on which no foreign tax liability was incurred.

This allocation is relevant when determining if the resident qualifies for a rebate under section 6quat(1) and when calculating the general limitation (see 5.5), since it impacts on the calculation of total foreign taxable income (that is, analysing what portion of the net capital gain is foreign and included in taxable income from all foreign sources). Foreign taxes on a foreign capital gain will not qualify for a rebate to the extent any capital losses for the year of assessment, or an assessed capital loss for the previous year of assessment, is set off against the foreign capital gain under consideration, since to that extent there would be no net capital gain and therefore no taxable capital gain as required under section 6quat(1)(e).<sup>78</sup>

### 5.6.3 Source of a capital gain

Section 9(2)(j) and (k) and section 9(4)(d) provide the source rules for capital gains and capital losses.

Section 9(2)(j) provides that the source of any capital gain or capital loss resulting from the disposal of immovable property or any interest or right of whatever nature to or in immovable property contemplated in paragraph 2 of the Eighth Schedule, is in South Africa if the property is situated in South Africa.

Section 9(2)(k) provides that any capital gain or capital loss resulting from the disposal of an asset [other than an asset contemplated in section 9(2)(j)] is derived from a South African source when the asset is disposed of –

- by a resident and –
  - the asset is not effectively connected with a permanent establishment of the person situated outside South Africa; and
  - the proceeds from the disposal are not subject to any taxes on income which are payable to a foreign jurisdiction; or
- by a non-resident and that asset is effectively connected with a permanent establishment of that person which is situated in South Africa.

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<sup>78</sup> See Binding Private Ruling 382 “Rebate in respect of Foreign Taxes”.

Conversely, a capital gain or capital loss will be derived from a foreign source under section 9(4)(d) if the asset is –

- immovable property or any right or interest in immovable property situated outside South Africa; or
- disposed of by a resident; and
  - the asset is effectively connected with a foreign permanent establishment of that person situated outside South Africa; and / or
  - the proceeds on disposal are subject to a foreign tax on income; or
- disposed of by a non-resident and the asset is not effectively connected with a permanent establishment of that person which is situated in South Africa.

In addition to section 9(2) and (4), any deeming source rules in a tax treaty which override the actual source rules must be considered [see **5.2.3(c)**].

#### **Example 29 – Source of a capital gain**

##### *Facts:*

Resident Company A acquired shares in a foreign company which is a resident of Country S. Company A subsequently disposed of the shares at a capital gain. Under Country S's domestic tax laws the proceeds derived by a person who is not a resident of Country S from the sale of shares in a company resident in that country are subject to capital gains tax in that country.

The sale of the shares is not effectively connected with a permanent establishment of Company A in Country S.

##### *Result:*

The capital gain from the disposal of the shares in the foreign company is from a foreign source because the proceeds are subject to foreign tax and are not effectively connected with a foreign permanent establishment [section 9(4)(d)]. Resident Company A will therefore be entitled to a rebate under section 6quat(1).

#### **5.6.4 The three-step limitation process [section 6quat(1), (1A) and (1B)(a)]**

The portion of foreign taxes qualifying for a rebate under section 6quat(1) on a foreign taxable capital gain is determined under a three-step limitation process:

- Step 1 – The comparative inclusion limitation [section 6quat(1) and (1A)].
- Step 2 – Foreign tax limitation on specified foreign taxable capital gains [paragraph (iB) of the proviso to section 6quat(1B)(a)].
- Step 3 – The overall normal tax on taxable income limitation [section 6quat(1B)(a)].

*Step 1 – The comparative inclusion limitation [section 6quat(1) and (1A)]*

In South Africa capital gains are taxed more favourably than ordinary income resulting in less than 100% of capital gains ultimately being included in taxable income.

For example, only a certain percentage of a taxpayer's net capital gain is included in taxable income. The percentage included depends on the nature of the person and varies between 0% and 80%.<sup>79</sup> The relevant percentages are as follows:

- A natural person or special trust 40%.<sup>80</sup>
- The individual policyholder fund of an insurer 40%.<sup>81</sup>
- The untaxed policyholder fund of an insurer 0%.<sup>82</sup>
- The company policyholder fund and risk policy fund of an insurer 80%.<sup>83</sup>
- In any other case, 80%.<sup>84</sup>

Other examples illustrating the favourable tax treatment of certain capital gains include the following exclusions, amongst others, provided for in the Eighth Schedule:

- The annual exclusion which is deducted from the sum of a natural person or special trust's capital gains and capital losses for the year.<sup>85</sup>
- The primary residence exclusion for a natural person or special trust.<sup>86</sup>
- Exclusion for small business assets of a natural person.<sup>87</sup>
- Exclusion for personal-use assets of a natural person or special trust.<sup>88</sup>

The full amount of foreign tax proved to be payable on a foreign capital gain will not qualify for a rebate under section 6quat(1) if less than 100% of the capital gain is included in taxable income.<sup>89</sup> Only so much of the foreign tax as is attributable to the portion of the capital gain which is included in taxable income will potentially qualify for the rebate. This is referred to as the *comparative inclusion limitation* and involves a comparison between the portion of the capital gain subjected to foreign tax and the portion subject to South African normal tax, that is:

$$\frac{\text{Amount of foreign taxable capital gain included in taxable income}}{\text{Amount of foreign taxable capital gain subject to foreign taxes}} \times \text{Foreign tax payable}$$

"Amount of foreign taxable capital gain included in taxable income" is limited to "Amount of foreign taxable capital gain subject to foreign taxes".

<sup>79</sup> Paragraph 10 of the Eighth Schedule.

<sup>80</sup> With effect from years of assessment commencing on or after 1 March 2016.

<sup>81</sup> With effect from 29 February 2016 on deemed disposals made by virtue of section 29B and 1 March 2016 on other disposals.

<sup>82</sup> With effect from 1 January 2016.

<sup>83</sup> With effect from 29 February 2016 on deemed disposals made by virtue of section 29B and 1 March 2016 on other disposals.

<sup>84</sup> With effect from years of assessment commencing on or after 1 March 2016.

<sup>85</sup> Paragraph 5 of the Eighth Schedule.

<sup>86</sup> Paragraph 45 of the Eighth Schedule.

<sup>87</sup> Paragraph 57(2) of the Eighth Schedule.

<sup>88</sup> Paragraph 53 of the Eighth Schedule.

<sup>89</sup> In contrast, when 100% of the capital gain is included in taxable income but less than 100% of the gain is subject to foreign tax, a gross-up of the foreign tax is not allowed.

No rebate will be allowed for amounts or portions thereof which are not subject to normal tax in South Africa. The taxes disqualified under this step are forfeited and do not qualify to be carried forward to succeeding years of assessment. In addition, the disqualified taxes do not qualify for a deduction under section 6quat(1C)(a) or any other section.

Therefore, if, for example, a foreign country taxes 100% of a capital gain of a natural person resident in South Africa while South Africa taxes only 40% of that gain, only 40% (40% of the foreign taxable capital gain included in taxable income / 100% of the foreign taxable capital gain subject to foreign taxes  $\times$  100% foreign tax) of the foreign taxes on the capital gain will potentially qualify for a rebate under section 6quat(1) (that is, before the limitation in steps 2 and 3).

**Example 30 – Determination of the portion of foreign tax proved to be payable which relates to a foreign taxable capital gain**

*Facts:*

Resident A, a natural person, disposed of a fixed property (which was not the resident's primary residence) located in Country A for R1 040 000 during the year of assessment. The property was acquired for no consideration.

Country A regarded the proceeds as income of a revenue nature and the full amount was subject to tax at a rate of 30%.

*Result:*

The foreign tax liability amounted to R312 000,00 (R1 040 000  $\times$  30%).

In South Africa the taxable capital gain is determined as follows:

	R
Capital gain (proceeds of R1 040 000 – base cost of RNil)	1 040 000
Less: Annual exclusion	<u>(40 000)</u>
Net capital gain	<u>1 000 000</u>
Inclusion rate	40%
Taxable capital gain	400 000

Only R120 000 (R400 000 / R1 040 000  $\times$  R312 000,00) of the foreign tax liability will potentially qualify for a rebate. The remaining R192 000,00 (R312 000,00 – R120 000,00) will not be taken into account because it does not relate to an amount subject to normal tax in South Africa. The excess amount of R192 000,00 is forfeited and may not be carried forward and taken into account in the immediately succeeding year of assessment.

*Step 2 – Foreign tax limitation on specified foreign taxable capital gains [paragraph (iB) of the proviso to section 6quat(1B)(a)]*

The amount of foreign tax which potentially qualifies for a rebate under section 6quat(1) is further limited if a resident derives a foreign-source capital gain<sup>90</sup> on the disposal of an asset which is not attributable to a permanent establishment of that resident outside South Africa. In these circumstances the amount of any foreign taxes proved to be payable on the taxable capital gain which potentially qualifies for a rebate under section 6quat(1) is limited to the amount of normal tax attributable to the taxable capital gain [paragraph (iB) of the proviso to section 6quat(1B)(a)].

This limitation is calculated as follows:

$$\frac{\text{Amount of the foreign-source taxable capital gain which is not attributable to a permanent establishment of the resident outside South Africa included in taxable income (A)}}{\text{Total taxable income from all sources (B)}} \times \text{Normal tax payable on (B)}$$

A limitation calculation is performed for each foreign capital gain when more than one foreign capital gain is subject to paragraph (iB) of the proviso to section 6quat(1B)(a). No provision is made for the aggregation of foreign capital gains in applying paragraph (iB) of the proviso.

Any excess foreign tax determined under step 2 is forfeited and does not qualify for a deduction under section 6quat(1C)(a) or any other section. In addition, any excess foreign tax may not be carried forward to the immediately succeeding year of assessment to potentially qualify for a rebate in that year under paragraph (ii) of the proviso to section 6quat(1B)(a) (see **Example 31**).

*Step 3 – The overall normal tax on taxable income limitation [section 6quat(1B)(a)]*

Once the limitations in steps 1 and 2 have been applied, the remaining foreign taxes are added to the other qualifying foreign taxes proved to be payable on the amounts contemplated in section 6quat(1)(a) to (f). The final step in the limitation process is performed under section 6quat(1B)(a) (see **5.5**).

**Example 31 – Limitation of foreign taxes proved to be payable – Asset not attributable to a foreign permanent establishment**

*Facts:*

Resident Company A holds 5% of the shares in Foreign Company B, a resident of Country T. The shares were acquired 5 years ago for R100 000. Company A has no presence in Country T. Company A disposed of the shares for R1 million. Country T subjected the gain realised on the sale of the shares to withholding tax at a rate of 30%.

Other income and foreign tax proved to be payable:

**Income**

	R
Income from a South African source	300 000
Interest income sourced in Country T	200 000

<sup>90</sup> See section 9(4)(d).



<b>Foreign Taxes</b>		R
Withholding tax levied on the interest income sourced in Country T		20 000,00
Withholding tax levied on the foreign capital gain (R1 000 000 – R100 000) × 30%		270 000,00
<i>Result:</i>		
<b>(a) Foreign taxable capital gain on disposal of the shares</b>		
The foreign taxable capital gain is determined as follows:		
Capital gain (proceeds of R1 000 000 – base cost of R100 000)		900 000
Inclusion rate		80%
Taxable capital gain		720 000
<b>(b) Normal tax payable</b>		
Taxable income sourced in South Africa		300 000
Interest income sourced in Country T		200 000
Taxable capital gain sourced in Country T		<u>720 000</u>
Taxable income		<u>1 220 000</u>
Normal tax (R1 220 000 × 28% <sup>91</sup> )		341 600,00
<b>(c) Application of the three-step limitation in section 6quat for a foreign taxable gain not attributable to a foreign permanent establishment of a resident</b>		
<b>Step 1 – The comparative inclusion limitation [section 6quat(1) and (1A)]</b>		
<u>Amount of foreign taxable capital gain included in taxable income</u> × Foreign tax		
Amount of foreign capital gain subject to foreign taxes		
= R720 000 / R900 000 × R270 000,00		
= R216 000,00		
Foreign taxes of R216 000,00 potentially qualify for a rebate under section 6quat(1) before applying steps 2 and 3. The remaining R54 000,00 (R270 000,00 – R216 000,00) or (R270 000,00 × 20%) does not qualify for the rebate because it relates to the portion of the capital gain of R180 000 (R900 000 – R720 000) which is not subject to tax in South Africa. This amount is forfeited and may not be carried forward to the immediately succeeding year of assessment.		

<sup>91</sup> The normal tax rate for companies is 27% with effect from years of assessment ending on or after 31 March 2023.

**Step 2 – Foreign tax limitation on specified foreign taxable capital gains [paragraph (iB) of the proviso to section 6quat(1B)(a)]**

The amount of any foreign taxes proved to be payable on the taxable capital gain potentially qualifying for a rebate under section 6quat(1), is limited to the amount of normal tax attributable to the taxable capital gain:

$$\frac{\text{Amount of the foreign-source taxable capital gain which is not attributable to a permanent establishment of the resident outside South Africa included in taxable income (A)}}{\text{Total taxable income from all sources (B)}} \times \text{Normal tax payable on (B)}$$

$$= R720\,000 / R1\,220\,000 \times R341\,600,00$$

$$= R201\,600,00$$

Only R201 600,00 of the qualifying foreign taxes of R216 000,00 potentially qualifies for the rebate. The balance of R14 400,00 is forfeited.

**Step 3 – The overall normal tax on taxable income limitation [section 6quat(1B)(a)]**

The remaining qualifying foreign taxes calculated in Step 2 are added to the other qualifying foreign taxes proved to be payable on the amounts contemplated in section 6quat(1)(a) to (f). The final step is the overall limitation under section 6quat(1B)(a).

**Sum of qualifying foreign taxes**

	R
Withholding tax on foreign-source interest income	20 000,00
Withholding tax on foreign-source capital gain	<u>201 600,00</u>
Total	<u>221 600,00</u>

$$\frac{\text{Taxable income derived from all foreign sources (A)} \times \text{Normal tax payable on (B)}}{\text{Taxable income derived from all sources (B)}}$$

$$= (R200\,000 + R720\,000) / R1\,220\,000 \times R341\,600,00$$

$$= R920\,000 / R1\,220\,000 \times 341\,600,00$$

$$= R257\,600,00$$

Thus the full amount of R221 600,00 qualifies for the rebate under section 6quat(1).

**5.7 Application of section 6quat to the attributed income of a controlled foreign company**

**5.7.1 General provisions applying to controlled foreign companies (section 9D(2), (2A), (9)(b) and (9A)(a)(i)(aa) and section 72A)**

As noted in 5.2, any portion of the net income of a CFC as contemplated in section 9D which is attributed to a resident potentially qualifies for a rebate under section 6quat(1). The amount of the rebate is calculated under the three-step limitation process explained in 5.7.2.

Section 9D(2) includes in the income of a resident the “proportional amount” of the “net income” of a CFC. “Proportional amount” refers to the resident’s effective interest in the “net income” of the CFC. “Net income” is defined in section 9D(2A) and in simplified terms is the CFC’s taxable income determined as if it were a resident.

The deemed inclusion in income does not apply to a resident holding less than 10% of the participation rights and that may not exercise at least 10% of the voting rights in a CFC.

Paragraph (i) of the further proviso to section 9D(2A) provides that the net income of a CFC for a foreign tax year will be deemed to be nil when –

- the aggregate amount of tax payable by the CFC to all spheres of government of any country other than the Republic for the foreign tax year of the CFC is at least 67,5% of the amount of normal tax which would have been payable on any taxable income of the CFC had the CFC been a resident for the foreign tax year; or
- all the receipts and accruals of the CFC are attributable to a foreign business establishment which is not required to be taken into account under section 9D.

Section 9D(9)(b) excludes from “net income” any amount attributable to a “foreign business establishment”. Section 9D(9A)(a) contains a number of exceptions to this exclusion; in other words, section 9D(9A)(a) determines certain instances when an amount attributable to a foreign business establishment must be included in “net income”.

Under section 72A(1) a resident who directly or indirectly, together with any connected person, holds at least 10% of the participation rights in a CFC (otherwise than indirectly through a resident company) must on an annual basis submit a return in the form prescribed by the Commissioner. In addition section 72A(2) requires that such a resident must have available for submission to the Commissioner when so requested, a copy of the financial statements of the CFC for the relevant tax year of the CFC. These must be translated into English, or one of South Africa’s official languages, if so requested by a senior SARS official.<sup>92</sup>

Failure to comply with section 72A(2) will result in section 6*quat* not applying to any tax proved to be payable to a foreign government on an amount included in the income of a person under section 9D(2) in relation to the CFC, unless reasonable grounds exist either for the failure which is outside the control of the person or for the person to believe that section 72A(2) did not apply.<sup>93</sup>

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<sup>92</sup> Section 33 of the TA Act.

<sup>93</sup> Section 72A(3)(b)(ii).

**Example 32 – Application of section 6quat(1) to foreign taxes paid by a CFC in more than one country**

*Facts:*

Resident Company A holds 100% of the shares in CFC B, a resident of Country B. CFC B received dividends of R100 000 from Company C, a resident of Country C. Company C is not a CFC. CFC B did not earn any other income.

Company C withheld tax of R10 000,00 from the dividend paid to CFC B.

Country B levied tax of R15 000,00 on the dividend received by CFC B and allowed a credit of R4 000,00 for the withholding tax paid to Country C.

Country B and Country C's tax treatment of the dividend is appropriate under the tax treaty between these two countries and the domestic tax laws of each country.

*Result:*

**Proportional amount attributed to Company A under section 9D(2)**

The dividend of R100 000 received by CFC B from Company C constitutes a foreign dividend and is included in CFC B's net income under section 9D(2A).

The foreign dividend is partially exempt under section 10B(3). The exempt portion of the foreign dividend is calculated as follows:

$$\begin{aligned} & R100\,000 \times 8 / 28^{94} \\ & = R28\,571 \end{aligned}$$

The taxable portion of the foreign dividend is R71 429 (R100 000 – R28 571). This amount represents the net income of CFC B and is attributed to Company A under section 9D(2).

**Amount of foreign taxes which potentially qualify for a rebate under section 6quat(1)**

Paragraph (ii) of the proviso to section 6quat(1A) provides that, for the purposes of section 6quat(1A), the amount included in a resident's taxable income must be determined without regard to section 10B(3). The foreign tax relating to the gross amount of the dividend (R100 000) therefore potentially qualifies for a rebate under section 6quat(1).

<sup>94</sup> This ratio applies with effect from years of assessment commencing on or after 1 March 2017.

**Sum of qualifying foreign taxes****Country B**

	R
Tax on income levied	15 000,00
Less: Rebate for foreign taxes	(4 000,00)

**Country C**

Withholding tax paid	<u>10 000,00</u>
Total foreign taxes proved to be payable	<u>21 000,00</u>

Foreign taxes potentially qualifying for a rebate under section 6quat(1) is R21 000,00. The limitation formula in section 6quat(1B) will apply to the foreign taxes of R21 000,00.

**Example 33 – Application of section 6quat(1) to foreign taxes proved to be payable by an intermediate CFC which relate to the net income of a lower tier CFC resident in another foreign country**

*Facts:*

Resident Company A holds 100% of the shares in CFC B, a resident of Country B. CFC B holds 100% of the shares in CFC C, a resident of Country C.

CFC C received passive income of R100 000. CFC C does not have a business establishment in Country C. CFC C is subject to tax in Country C on the passive income of R100 000. The foreign tax amounts to R10 000. CFC C distributes the after-tax income of R90 000 as a dividend to CFC B.

Country C does not levy any withholding tax on the dividend distributed by CFC C to CFC B.

Country B has CFC rules similar to those of South Africa. The application of the CFC rules results in the attributed income which is included in CFC B's taxable income (R100 000) being subject to tax in Country B at a rate of 30% which represents a tax liability of R30 000,00. The foreign dividend received from CFC C is exempt from tax in Country B. Country B does not grant CFC B any foreign tax credits.

*Result:*

Under South Africa's CFC rules each CFC in a chain of CFCs is considered separately.

**CFC C**

Section 6quat(1A) provides that the foreign taxes proved to be payable to a sphere of a foreign government by any CFC *in respect of* the proportional amount attributed to the resident may qualify for a rebate.

CFC C's passive income of R100 000 is attributed to and included in Company A's income under section 9D(2). Company A therefore potentially qualifies for a rebate under section 6quat(1) for the foreign tax paid by CFC C of R10 000,00.

Company A also potentially qualifies for a rebate for the foreign tax paid by CFC B of R30 000,00 because the foreign taxes are paid by a CFC and it relates to the same income. The passive income which was attributed to CFC B under Country B's tax rules and on which the foreign tax is payable by CFC B is the same income as that which was attributed to Company A under section 9D(2).

### **CFC B**

The dividend of R90 000 received by CFC B from CFC C constitutes a foreign dividend for purposes of calculating CFC B's net income under section 9D(2A). However, the full amount qualifies for the participation exemption under section 10B(2)(a). Thus the net income of CFC B which is attributable to Company A under section 9D(2) is RNil.

If the dividend had been included in net income for South African attribution purposes, the foreign taxes paid by CFC B in Country B would not qualify for a rebate under section 6quat(1), since the tax was paid on attributed notional income under Country B's CFC rules and not on actual income (the dividend).

### **5.7.2 The three-step limitation process in determining the rebate for foreign taxes proved to be payable by a controlled foreign company [section 6quat(1B)(a) and paragraph (iA)(bb) of the proviso to section 6quat(1B)(a)]**

The amount of foreign taxes which qualify for a rebate under section 6quat(1) on the proportional amount of a CFC's net income which is attributed to a resident is determined under a three-step limitation process:

- Step 1: Determine the amount of foreign tax proved to be payable by the CFC which is attributable to the proportional amount of net income included in the resident's income.
- Step 2: Limit the proportional amount of foreign tax determined in step 1 to the relevant amount of South African normal tax [paragraph (iA)(bb) of the proviso to section 6quat(1B)(a)].
- Step 3: Apply the overall limitation under section 6quat(1B)(a) taking steps 1 and 2 into account.

*Step 1: Determine the amount of foreign tax proved to be payable by the CFC which is attributable to the proportional amount of net income included in the resident's income.*

In assessing whether foreign tax is proved to be payable from a CFC's perspective, the applicable foreign domestic tax law and any tax treaties which are applicable to the CFC and the other foreign country must be considered. The tax treaty between South Africa and foreign jurisdictions will not be relevant in these circumstances.

The amount of foreign taxes proved to be payable by a CFC must be adjusted to –

- reflect only the resident taxpayer's effective interest in the CFC (that is, the same interest applied in determining the proportional amount of net income requiring attribution); and
- limit the amount of foreign tax potentially qualifying for the rebate when foreign taxable income is greater than net income determined under section 9D(2A).<sup>95</sup>

<sup>95</sup> A gross-up is inapplicable when the foreign taxable income is less than net income calculated under section 9D(2A).

If this is the case, the amount of foreign taxes must be limited to the amount that the net income [as determined under South African tax law, namely, section 9D(2A)] bears to the foreign taxable income (as determined under foreign tax law).

If a resident, for example, holds 75% of the participation rights in a CFC, 75% of the foreign tax is potentially available for the rebate under section 6quat(1). The qualifying foreign taxes will be further limited to a ratio of 1 / 3 if the amount of the net income is R1 million and foreign taxable income (in rand) is R3 million. The difference of R2 million is not included in net income under section 9D(2) and the foreign tax thereon does not qualify for a rebate under section 6quat(1) (see **Examples 34 and 35**).

*Step 2 – Limit the proportional amount of foreign tax determined in step 1 to the relevant amount of South African normal tax [paragraph (iA)(bb) of the proviso to section 6quat(1B)(a)]*

To the extent that the proportional amount of net income, and the proportional amount of foreign taxes, include an amount which is attributable to a CFC's foreign business establishment and which does not qualify for exclusion from attribution under section 9D(9A)(a) or 9D(9)(b), the amount of foreign taxes which potentially qualify for a rebate is limited under step 2. Broadly speaking, this includes amounts attributable to a foreign business establishment which are not determined on an arm's length basis or which are specifically required to be taken into account as a result of the application of section 9D(9A)(a)(i) – (vii). These amounts are referred to in this paragraph of the Note as "tainted income".

The amount of foreign taxes, as calculated under step 1, *relating to* the tainted income is further limited to the amount of normal tax attributable to the inclusion of the tainted income in the resident's income under section 9D(2). This limitation is calculated as follows:

Proportionate share of tainted income of CFC × Amount determined under Step 1  
Proportionate share of net income of CFC

*Limited to:*

Proportionate share of tainted income of CFC × Normal tax  
Total South African taxable income

Any excess is forfeited and may not be carried forward to the immediately succeeding year of assessment.<sup>96</sup> The excess also does not qualify for a deduction under section 6quat(1C)(a) or any other section. In a number of circumstances the limitation will be applicable and must be calculated but will not have an impact because the normal tax on the comparable amount will be greater than the foreign tax on that amount. This arises because, amongst other reasons, section 9D excludes high taxed jurisdictions from attribution. See paragraph (i) of the proviso to section 9D(2A) under which the net income of a CFC is deemed to be nil when its foreign taxes are at least 67,5% of the amount of normal tax which would have been payable had attribution been required.

<sup>96</sup> Paragraph (ii) of the proviso to section 6quat(1B)(a).

*Step 3: Apply the overall limitation under section 6quat(1B)(a) taking steps 1 and 2 into account*

The amount of foreign taxes which qualify for the rebate under section 6quat(1) in a particular year of assessment is the lesser of –

- the sum of the qualifying foreign taxes after applying steps 1 and 2; or
- the amount calculated under the limitation as set out below.

The limitation formula is calculated as follows:

$\frac{\text{Taxable income derived from all foreign sources (A)}}{\text{Taxable income derived from all sources (B)}} \times \text{Normal tax payable on (B)}$

See **5.5** for details on the limitation under section 6quat(1B)(a).

**Example 34 – Limitation of foreign taxes on an amount attributable from a CFC which is not excluded from attribution under section 9D**

*Facts:*

Resident A holds 75% of the participation rights in CFC B. CFC B's net income of R500 000 includes interest of R150 000 attributable to CFC B's foreign business establishment which did not qualify for the foreign business establishment exclusion and was required to be taken into account as a result of section 9D(9A)(a)(iii)(cc). CFC B's taxable income under the tax laws of its country of residence amounted to R490 000 and the foreign tax liability thereon was R100 000,00.

Resident A's taxable income was R1 million (which included 75% of CFC B's net income of R500 000, namely R375 000). Normal tax payable by Resident A was R280 000,00.

*Result:*

**CFC B**

**Step 1: Foreign taxes attributable to the proportional amount of net income included in Resident A's taxable income**

$[\text{Foreign taxes} \times (\text{net income under section 9D(2A)} / \text{taxable income under foreign tax law})^*] \times \text{participation interest}$

$= [\text{R}100\,000,00 \times (n/a^*)] \times 75\%$

$= \text{R}75\,000,00$

\* not applicable, since CFC B's taxable income under foreign tax law of R490 000 is less than its net income under section 9D(2A) of R500 000.



**Step 2:**

The limitation in paragraph (iA)(bb) of the proviso to section 6quat(1B)(a) applies because interest of R150 000 received by CFC B is attributable to a foreign business establishment and included in net income under section 9D(9A)(a)(iii)(cc).

**(a) Calculation of foreign taxes attributable to non-tainted income**

$\frac{\text{Proportionate share of non-tainted income of CFC B}}{\text{Proportionate share of net income of CFC B}} \times \text{Amount determined under step 1}$

$$= \left[ \frac{((R500\,000 - R150\,000) \times 75\%)}{(R500\,000 \times 75\%)} \right] \times R75\,000,00$$

$$= R262\,500 / R375\,000 \times R75\,000,00$$

$$= R52\,500,00$$

**(b) Calculation of foreign taxes attributable to tainted income**

$\frac{\text{Proportionate share of tainted income of CFC B}}{\text{Proportionate share of net income of CFC B}} \times \text{Amount determined under step 1}$

**Limited to:**

$\frac{\text{Proportionate share of tainted income of CFC B}}{\text{Total South African taxable income}} \times \text{Normal tax}$

$$= \left[ \frac{(R150\,000 \times 75\%)}{(R500\,000 \times 75\%)} \right] \times R75\,000,00 \text{ limited to } \left[ \frac{(R150\,000 \times 75\%)}{R1\,000\,000} \right] \times R280\,000,00$$

$$= R22\,500,00 \text{ limited to } R31\,500,00$$

The limitation has no effect, since the limitation amount is greater than the applicable amount.

**Total foreign taxes subject to limitation under section 6quat(1B)(a) in step 3**

= Foreign taxes attributable to non-tainted income and foreign taxes attributable to tainted income

$$= R52\,500,00 + R22\,500,00$$

$$= R75\,000,00$$

**Step 3: Applying the overall limitation under section 6quat(1B)(a) taking steps 1 and 2 into account**

The remaining qualifying foreign taxes proved to be payable by CFC B are added to any other qualifying foreign taxes proved to be payable on the amounts contemplated in section 6quat(1)(a) to (f). The final step in the limitation process is performed, namely, the overall limitation under section 6quat(1B)(a) (see 5.5).

$\frac{\text{Taxable income derived from all foreign sources (A)}}{\text{Taxable income derived from all sources (B)}} \times \text{Normal tax payable on (B)}$

$$= (R500\,000 \text{ net income} \times 75\% \text{ participation interest}) / R1\,000\,000 \times R280\,000,00$$

$$= R105\,000,00$$

Therefore, the amount of foreign taxes to be allowed under section 6quat(1) is R75 000,00 (see steps 1 and 2).

**Example 35 – Limitations of foreign taxes on an amount attributable to a CFC (but not its foreign business establishment) which is not excluded from attribution under section 9D**

*Facts:*

Resident A holds 60% of the participation and voting rights in CFC B which does not have a foreign business establishment. The net income of CFC B is R100 000, consisting of interest income.

Resident A has other foreign-source taxable income of R50 000. Foreign taxes on this income proved to be payable are R15 000,00.

Resident A does not earn any South African-source income.

Resident A's total taxable income is R110 000 [(Net income of CFC B of R100 000 × 60%) + other income of R50 000] and normal tax payable is R30 800,00 (R110 000 × 28%<sup>97</sup>).

In its country of residence, CFC B's equivalent taxable income amounts to R120 000 which results in a tax liability of R12 000,00 in that country.

*Result:*

**CFC B**

**Step 1: Foreign taxes attributable to the proportional amount of net income included in Resident A's taxable income**

[Foreign taxes × (net income of CFC B under section 9D(2A) / taxable income of CFC B under foreign tax law)\*] × participation interest

$$= [R12\ 000,00 \times (R100\ 000 / R120\ 000)] \times 60\%$$

$$= R6\ 000,00$$

\* This element of the step 1 limitation is applied because CFC B's taxable income under foreign tax law of R120 000 is greater than its net income under section 9D(2A) of R100 000.

**Step 2:**

Step 2 does not apply, since the foreign taxes and related net income are not attributable to a foreign business establishment.

**Sum of total foreign taxes potentially qualifying for a rebate under section 6quat(1)**

= R6 000,00 in relation to CFC B (taking steps 1 and 2 into account) + R15 000,00 relating to the other foreign-source taxable income

$$= R21\ 000,00$$

<sup>97</sup> The normal tax rate for companies is 27% with effect from years of assessment ending on or after 31 March 2023.

**Step 3: Calculation of the limitation of the rebate under section 6quat(1B)(a)**

$\frac{\text{Taxable income derived from all foreign sources (A)}}{\text{Taxable income derived from all sources (B)}} \times \text{Normal tax payable on (B)}$

= R110 000 / R110 000 × R30 800,00

= R30 800,00

Therefore, the amount of foreign taxes allowed as a rebate under section 6quat(1) is R21 000,00.

See **Annexure A** for an example applying the three-step limitation with regards to foreign branch operations, foreign dividend income and income attributed from a CFC.

### 5.8 The carry-forward of a balance of excess foreign taxes [paragraphs (ii) and (iii) of the proviso to section 6quat(1B)(a)]

To the extent that the amount of qualifying foreign taxes proved to be payable exceeds the amount of the rebate determined under section 6quat(1A) and (1B) (see **5.5**, **5.6** and **5.7**), the excess amount is carried forward to the immediately succeeding year of assessment. The amount so carried forward will potentially qualify as a foreign tax available for set-off against the normal tax payable on taxable income derived from foreign sources in the immediately succeeding year of assessment [paragraph (ii) of the proviso to section 6quat(1B)(a)].

Any balance of excess foreign taxes may not be carried forward for more than seven years, calculated from the year of assessment in which the balance was carried forward for the first time [paragraph (iii) of the proviso to section 6quat(1B)(a)].

The excess amount of foreign taxes does not relate to any taxes overpaid to SARS, but relates solely to taxes paid to foreign tax jurisdictions. SARS may not refund any portion of the excess to the relevant taxpayer or transfer it to another taxpayer such as a company in the same group of companies.

Section 6quat does not provide for the carry-back of a balance of excess foreign taxes to previous years of assessment.

The amount of the rebate determined under section 6quat(1A) and (1B) relating to the taxable foreign income derived during a year of assessment must be applied against the normal tax payable in that year. Thereafter, any balance of excess foreign taxes brought forward from the preceding year may be set off against the remaining balance of normal tax payable on taxable income derived from foreign sources [paragraph (ii)(bb) of the proviso to section 6quat(1B)(a)].

The balance of excess foreign taxes determined under paragraph (ii) of the proviso to section 6quat(1B)(a) may not be applied against normal tax payable on taxable income derived from South African sources (see **Example 3** in Annexure B).

The excess amount determined for more than one year of assessment must be recorded separately and applied on a first-in-first-out basis against normal tax payable in future years of assessment.

**Example 36 – Foreign tax rate exceeds the normal tax rate***Facts:*

Resident Company A received income of R100 000 from a source in Country S. No other income was received by or accrued to Company A from either a local or foreign source.

The income was subject to tax at a rate of 30% in Country S and 28%<sup>98</sup> in South Africa.

*Result:*

	R
Taxable income	100 000
Normal tax (R100 000 × 28%)	28 000,00
Less: Rebate under section 6quat(1) (Note)	<u>(28 000,00)</u>
Normal tax payable	<u>0</u>

**Note:****Qualifying foreign taxes**

$$= R100\,000 \times 30\%$$

$$= R30\,000,00$$

**Limitation of the rebate under section 6quat(1B)(a)**

$\frac{\text{Taxable income derived from all foreign sources (A)}}{\text{Taxable income derived from all sources (B)}} \times \text{Normal tax payable on (B)}$

$\frac{R100\,000}{R100\,000} \times R28\,000,00$

$$= R100\,000 / R100\,000 \times R28\,000,00$$

$$= R28\,000,00$$

The rebate for the current year is R28 000,00. The excess of R2 000,00 (R30 000,00 – R28 000,00) is carried forward to the immediately succeeding year of assessment.

**Example 37 – Utilisation of excess foreign taxes carried forward from a previous year***Facts:*

Resident Company A conducts trading operations in South Africa as well as in Country C. In year 1 Company A had an assessed loss from its South African operations which exceeded the taxable income earned from its operations in Country C.

As a result, excess foreign taxes of R400 000,00 were carried forward under paragraph (ii) of the proviso to section 6quat(1B)(a) to year 2 to qualify for a rebate.

In year 2 Company A had taxable income from the operations conducted in Country C of R1 500 000. The government of Country C granted special tax incentives in year 2 and as a result no tax was payable in Country C.

<sup>98</sup> The normal tax rate for companies is 27% with effect from years of assessment ending on or after 31 March 2023.

Company A's operations in South Africa in year 2 gave rise to income of R15 million and deductible expenses of R10 million. The corporate tax rate was 28%.

*Result:*

### **Year 2**

#### **South African taxable income**

	R
Foreign operations – Country C	1 500 000
South African operations (R15 000 000 – R10 000 000)	<u>5 000 000</u>
Total taxable income for year 2	<u>6 500 000</u>
Normal tax payable at 28%	1 820 000,00
Less: Rebate under section 6quat(1)*	<u>(420 000,00)</u>
Normal tax payable	<u>1 400 000,00</u>

#### **\* Limitation of the rebate under section 6quat(1B)(a)**

Taxable income derived from all foreign sources (A) × Normal tax payable on (B)

Taxable income derived from all sources (B)

= R1 500 000 / R6 500 000 × R1 820 000,00

= R420 000,00

No foreign taxes were proved to be payable in year 2. However, there was taxable income from foreign sources in year 2 and as a result the excess foreign taxes from year 1 can potentially be used in year 2. The maximum amount of rebate in year 2 is R420 000,00 which means that the full amount of the excess foreign taxes of R400 000,00 carried forward from year 1 can be used in year 2.

## **5.9 Interaction between credit methods of relief under a tax treaty and relief under section 6quat(1)**

### **5.9.1 Tax treaty methods for providing relief from double taxation**

This paragraph of the Note considers the article in tax treaties which deals with the elimination of double taxation not otherwise already eliminated by a country's domestic tax law or by the distributive tax rules in the tax treaty. For example, a tax treaty may grant a particular country the sole taxing right which means that there is no double taxation which needs to be addressed by the article in the tax treaty specifically dealing with the elimination of double taxation. Tax treaties employ two principles to address double taxation, namely, the exemption principle and the credit principle.

Under the credit principle, the resident state calculates the resident's tax liability under its domestic law taking into account the applicable provisions of the tax treaty and allows a deduction from its own tax for the taxes paid in the other country. Two methods for applying the credit principle are –

- the “full credit” method under which the resident state allows a deduction from local tax of the total tax paid in the other country on income which is also taxed in the resident state; and

- the “ordinary credit” method under which the amount of the deduction from local tax permitted by the resident state for the tax paid in the other country on income which is also taxed in the resident state is limited to its own tax applicable to that income.

The majority of the tax treaties concluded by South Africa provide for the elimination of double taxation under the ordinary credit method while a few of the older treaties provide for the exemption method of relief in the article dealing with the elimination of double tax.<sup>99</sup> None of South Africa’s tax treaties provide for the “full credit” method of relief.

Depending on the particular tax treaty, in some circumstances when the foreign tax which would otherwise be payable has been reduced in accordance with laws designed to promote economic development, the amount of the reduction is considered to be a tax paid for purposes of calculating the credit relief available under section 6quat(1) and the tax treaty. See, for example, article 22(2) of the tax treaty between South Africa and Botswana.

### **5.9.2 Choice between the tax treaty credit method and rebate method under section 6quat(1)**

Section 6quat(2) provides a resident with a choice between the relief provided for in the tax treaty (if applicable) and the relief provided for under section 6quat(1) or (1C) as appropriate. A resident is not entitled to claim both forms of relief. A resident may also not elect tax treaty relief and at the same time seek to apply the more favourable elements of section 6quat such as the carry-forward of excess taxes.

The choice of relief, namely, section 6quat(1)<sup>100</sup> or tax treaty relief, can be exercised annually per taxable income per country. The resident is not bound by a choice made in a previous year of assessment. A resident may elect different methods of relief when more than one treaty applies during a particular year of assessment. SARS will apply section 6quat(1) if the resident does not elect which form of relief must be applied.

### **5.9.3 Tax treaty credit method – Effect of wording of relevant articles**

The wording of the relevant article in the tax treaty will determine how the tax treaty credit method must be applied in a specific case. Tax treaty articles can be divided into –

- those providing relief from double taxation under the credit method without any reference to the provisions of domestic law relating to the granting of a credit for foreign taxes (namely, section 6quat), and
- those which are “subject to” the provisions of the law of South Africa regarding the deduction of foreign taxes from normal tax payable in South Africa (namely, section 6quat).

<sup>99</sup> For example, the tax treaties with Germany and Zambia.

<sup>100</sup> For the rest of 5.9 and its subparagraphs assume the income is from a foreign source and that section 6quat(1C)(a) does not apply.

#### 5.9.4 The tax treaty credit method – Articles not “subject to” section 6quat

Some tax treaties providing for the credit method of relief are not phrased to be “subject to” domestic law relating to the granting of a credit for foreign taxes (namely, section 6quat). In these circumstances a resident may elect to apply the tax treaty credit method of relief instead of the section 6quat rebate method of relief (assume the income is foreign-source). This election is sanctioned under section 6quat(2).

The election is made in its entirety, meaning that if a resident elects the relief provided under the tax treaty, none of the provisions of section 6quat (including the additional relief measures) apply. A person electing to use a tax treaty credit method will, for example, not be entitled to carry forward any excess foreign taxes under paragraph (ii) of the proviso to section 6quat(1B)(a).

An example of a tax treaty which is not “subject to” section 6quat is the tax treaty between South Africa and Australia.<sup>101</sup> The relevant part of article 23 of the tax treaty, which deals with the elimination of double taxation, reads as follows:

“3. In the case of South Africa, *Australian tax paid* by a resident of South Africa in respect of income taxable in Australia *in accordance with the Agreement*, shall be deducted from *the taxes due according to South African fiscal law*. *The deduction shall not, however, exceed an amount which bears to the total South African tax payable the same ratio as the income concerned bears to the total income.*”

(Emphasis added.)

Section 6quat therefore does not apply when calculating the relief provided under the tax treaty. Regard must be had to the particular tax treaty, or, if applicable, a separate agreement with the particular country to determine the tax treaty relief. Having regard to the tax treaty with Australia, the following points are, for example, relevant in calculating the tax treaty relief:

- Australian tax paid refers to the tax paid in Australia as calculated under Australian domestic law and the tax treaty.
- “In respect of income taxable in Australia” – practically the source of the income will often be Australian, however, this wording does not limit the source of the income to Australia, the income could be sourced in Australia, South Africa or even a third country. The important requirement is that the income must be taxable in Australia.
- “In accordance with the Agreement” means that a credit is available only for the foreign tax paid on items of income correctly taxed under the tax treaty.
- Taxes due according to South African fiscal law refers to the tax payable in South Africa as calculated under the Act and the tax treaty. This requires the calculation of taxable income under the Act (namely, South African tax law).

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<sup>101</sup> The wording of the specific treaty must be considered, since it can vary from treaty to treaty and differences in wording can impact on the interpretation of the articles of the treaty.

- The deduction from South African normal tax is limited. The limitation is calculated on a “per country” basis rather than on a “per income item” or an “overall” basis. The maximum deduction is limited to:<sup>102</sup>

$$\text{Total South African tax payable} \times \frac{\text{(Taxable) Income concerned}^{103}}{\text{Total (taxable) income}}$$

- “Income” is interpreted to mean taxable income (see **5.9.7** – “Meaning of ‘income’ in the article dealing with the elimination of double tax in tax treaties”).
- “Total South African tax payable” is, and can only be, calculated under the Act (namely, South African tax law) taking into account the provisions of the applicable tax treaty. This determination requires, amongst other aspects, the calculation of taxable income under the Act. Total South African tax is normal tax before the rebate under section 6*quat*(1) but, for natural persons, after the primary, secondary and tertiary rebates under section 6(2) and the medical tax credits under sections 6A and 6B.
- “Taxable income concerned” refers to taxable income in respect of the income which is taxed in South Africa and is also taxed, in accordance with the provisions of the tax treaty, in the other country (namely, Australia in this example).
- In calculating the *pro rata* portion of the South African tax which is attributable to the income taxed in both countries, both the taxable income concerned and total taxable income must be calculated in accordance with the Act. Taxable income as determined under the tax laws of the other contracting state is irrelevant.
- The calculation of taxable income in accordance with the Act requires an allocation of the appropriate expenses to the income concerned.
- Notwithstanding the formula, the maximum deduction, across all countries applicable to a particular taxpayer, is limited to the total South African tax payable in the particular tax year and any excess foreign tax is forfeited.

### Example 38 – Maximum deduction under treaty relief

#### Facts:

Resident Company A conducts its trading operations in South Africa, Country A and Country B. Company A’s taxable income from foreign sources and loss incurred in South Africa were as follows:

	R
Loss – South African operations	(100 000)
Taxable income – Country A	200 000
Taxable income – Country B	<u>300 000</u>
	<u>400 000</u>

Company A paid tax of R58 000,00 in Country A and R75 000,00 in Country B.

<sup>102</sup> Words in brackets are added for clarification.

<sup>103</sup> See bullet points below for further detail.



The tax treaty between South Africa and Country A and the tax treaty between South Africa and Country B are not subject to section 6quat. Company A elected under section 6quat(2) to use the treaty relief for the elimination of double taxation, rather than the section 6quat method of relief.

*Result:*

**Normal tax payable = South African normal tax less tax treaty credit**

$$= (R400\,000 \times 28\%^{104}) - R112\,000,00 \text{ (see calculation 1)}$$

$$= R112\,000,00 - R112\,000,00$$

$$= RNil$$

### **Calculation 1**

**The maximum foreign tax credit = maximum Country A foreign tax credit (calculation 2) + maximum Country B foreign tax credit (calculation 3)**

$$= R56\,000,00 + R75\,000,00$$

$$= R131\,000,00$$

The maximum foreign tax credit in respect of all countries is, however, limited to the total normal tax payable in the particular year of assessment, namely, R112 000,00. The excess of R19 000,00 (maximum foreign tax credit of R131 000,00 – South African normal tax of R112 000,00) is forfeited, since it is not refundable and may not be carried forward to the immediately succeeding year of assessment.

### **Calculation 2**

**Calculation of the maximum foreign tax credit in respect of Country A tax paid under the tax treaty on a country-by-country basis**

Foreign tax paid in Country A = R58 000,00

**Maximum treaty credit**

$$= \text{Total South African tax payable} \times \frac{\text{(Taxable) Income concerned (Country A)}}{\text{Total (taxable) income}}$$

$$= R112\,000,00 \times R200\,000 / R400\,000$$

$$= R56\,000,00$$

### **Calculation 3**

**Calculation of the maximum foreign tax credit in respect of Country B tax paid under the tax treaty on a country-by-country basis**

Foreign tax paid in Country B = R75 000,00

<sup>104</sup> The normal tax rate for companies is 27% with effect from years of assessment ending on or after 31 March 2023.

**Maximum treaty credit**

$$= \text{Total South African tax payable} \times \frac{\text{(Taxable) Income concerned (Country B)}}{\text{Total (taxable) income}}$$

$$= R112\,000,00 \times R300\,000 / R400\,000$$

$$= R84\,000,00$$

Therefore, the full amount of foreign tax paid in Country B of R75 000,00 potentially qualifies as a credit.

**5.9.5 The tax treaty credit method – Articles “subject to” section 6quat**

In providing for the credit method of relief, some tax treaties stipulate that the credit must be determined –

*“subject to the provisions of the law of South Africa regarding the deduction from tax payable in South Africa of tax payable in any country other than South Africa”.*

(Emphasis added.)

The words “subject to” indicate that the credit must be determined under the section of the Act dealing with the deduction of foreign taxes from tax payable, namely, section 6quat. In the case of foreign-source income, the whole of section 6quat applies and not merely certain elements of it.

Some tax treaties could impose additional limitations on the relief granted, namely, limitations in addition to the requirements of section 6quat. A number of the tax treaties which include the “subject to” wording also include the same wording as above in relation to tax treaties without the “subject to” wording. This means that the article also contains the following additional limitation:

*“Such deduction (the deduction calculated in terms of section 6quat) shall not, however, exceed an amount which bears to the total South African tax payable the same ratio as the income concerned bears to the total income.”*

(Emphasis added.)

In these instances it would not be to the taxpayer’s advantage to elect that the tax treaty method of relief apply, since the amount determined under section 6quat is potentially further limited under a per country limitation calculation as required under the tax treaty. An article of this nature therefore has the effect that section 6quat(1) is often practically the only method available for determining a foreign tax rebate for foreign-source income under a tax treaty which contains a “subject to” provision.

An example of a tax treaty that is “subject to” section 6quat is article 22 of the tax treaty between South Africa and Turkey<sup>105</sup> which deals with the elimination of double taxation and provides that double taxation shall be eliminated as follows:

*“In South Africa, subject to the provisions of the law of South Africa regarding the deduction from tax payable in South Africa of tax payable in any country other than South Africa (which shall not affect the general principle hereof), Turkish tax paid by residents of South Africa in respect of income which, in accordance with the provisions of this Agreement, may be taxed in Turkey shall be deducted from the taxes due according to South African tax law. Such deduction shall not, however,*

<sup>105</sup> The wording of the specific treaty must be considered, since it can vary from treaty to treaty and differences in wording can impact on the interpretation of the articles of the treaty.

exceed an amount which bears to the total South African tax payable the same ratio as the income concerned bears to the total income;”

(Emphasis added.)

Assuming the amount which is subject to double tax is foreign-source, the following is relevant in interpreting the tax treaty relief provided under article 22(a) of the tax treaty:

- The taxpayer has a choice between the relief provided under section 6quat(1) and the relief provided under the tax treaty between South Africa and Turkey.
- Assuming the taxpayer elects the tax treaty relief, the “subject to the provisions of the law of South Africa” indicates that section 6quat must be applied when calculating the relief provided by the tax treaty.

Support for the principle that a resident country’s domestic tax law must be applied when the treaty relief is subject to domestic law can be found in the technical explanation document released by the Treasury Department of the United States of America on the tax treaty between the United States of America and South Africa which explains the meaning of “in accordance with the provisions and subject to the limitations of the law of the United States”.<sup>106</sup>

- The wording “in respect of income which ... may be taxed in Turkey” does not limit the source of the income to a foreign source (Turkey or a third country). However, in the context of section 6quat(1) the income must be foreign-source.
- Turkish tax paid refers to the tax paid in Turkey as calculated under Turkish domestic law and the provisions of the tax treaty.
- “In accordance with the provisions of this Agreement” means that a credit is available only for the foreign tax paid on items of income correctly taxed under the tax treaty.
- Taxes due according to South African tax law refers to the tax payable in South Africa as calculated under the Act and the tax treaty. This determination requires, amongst other things, the calculation of taxable income under the Act (namely, South African tax law).
- Having calculated the deduction from South African normal tax under section 6quat, there is an additional tax treaty limitation to consider. The tax treaty limitation is the same as the limitation mentioned in 5.9.4 and is calculated on a “per country” basis rather than on a “per income item” or an “overall” basis. The maximum deduction is therefore limited to:

$$\text{Total South African tax payable} \times \frac{\text{(Taxable) Income concerned}^{107}}{\text{Total (taxable) income}}$$

- “Income” is interpreted to mean “taxable income” (see 5.9.7 – “Meaning of “income” in the article dealing with the elimination of double tax in tax treaties”).

<sup>106</sup> Department of Treasury Technical Explanation of the Convention between the United States of America and the Republic of South Africa for the Avoidance of Double Taxation and the Prevention of Fiscal Evasion with respect to Taxes on Income and Capital Gains, Article 23, available from [www.irs.gov/pub/irs-trty/safitech.pdf](http://www.irs.gov/pub/irs-trty/safitech.pdf) [Accessed 9 December 2022].

<sup>107</sup> See bullet points below for further detail.

- “Total South African tax payable” is and can only be calculated under the Act (namely, South African tax law) taking into account the applicable tax treaty. This requires, amongst other things, the calculation of taxable income under the Act. Total South African tax is normal tax before the rebate under section 6*quat*(1) but, for natural persons, after the primary, secondary and tertiary rebates under section 6(2) and the medical tax credits under section 6A and 6B.
- “Taxable income concerned” refers to taxable income in respect of the income which is taxed in South Africa and is also taxed, in accordance with the tax treaty, in the other country (namely, Turkey in this example).
- In calculating the *pro rata* portion of the South African tax which is attributable to the income taxed in both countries, both the taxable income concerned and total taxable income must be calculated in accordance with the Act. Taxable income as determined under the tax laws of the other contracting state is irrelevant.
- The calculation of taxable income in accordance with the Act requires an allocation of the appropriate expenses to the income concerned.
- Notwithstanding the formula, the maximum deduction, across all countries applicable to a particular taxpayer, is limited to the total South African tax payable in the particular year of assessment and any excess foreign tax is forfeited.

#### 5.9.6 Application of the tax treaty credit method and section 6*quat* rebate method in the same year of assessment

A resident deriving foreign-source amounts from both –

- a foreign country with which South Africa has concluded a tax treaty providing for a credit method of relief which is effectively subject to section 6*quat*, and
- a foreign country with which South Africa has concluded a tax treaty providing for a credit method of relief which is not subject to section 6*quat*,

within the same year of assessment that elects to follow the tax treaty credit method of relief in respect of the tax treaty not subject to section 6*quat*, must perform two separate credit limitation calculations for the year.

#### **Example 39 – Determination of rebate under section 6*quat*(1) and a tax treaty credit within the same year of assessment**

*Facts:*

Resident Company A conducts its trading operations in South Africa. It also has branches in Country L and Country M. South Africa has a tax treaty with each of these countries. The tax treaty with Country L provides for the credit method of relief and is expressly subject to section 6*quat* while the tax treaty with Country M provides for the credit method of relief without any express reference to section 6*quat*. Company A elects the tax treaty credit method of relief on income derived from Country M.

Taxable income and taxes paid are as follows:

Description	South Africa R	Country L R	Country M R	Total R
Taxable income	100 000	20 000	30 000	150 000
Foreign taxes proved to be payable		9 000,00	12 000,00	21 000,00
Normal tax payable at 28% <sup>108</sup>				42 000,00

*Result:*

**(a) Calculation of the rebate under section 6quat(1) – Country L**

$$\begin{aligned} & R20\,000 / R150\,000 \times R42\,000,00 \\ & = R5\,600,00 \end{aligned}$$

Under paragraph (ii) of the proviso to section 6quat(1B)(a) the balance of R3 400,00 (R9 000,00 – R5 600,00) may be carried forward to the immediately succeeding year of assessment.

**(b) Calculation of the tax treaty credit – Country M**

$$\begin{aligned} & R30\,000 / R150\,000 \times R42\,000,00 \\ & = R8\,400,00 \end{aligned}$$

The balance of R3 600,00 (R12 000,00 – R8 400,00) is forfeited and may not be carried forward to future years, since the tax treaty does not provide for the carry-forward of excess foreign taxes.

**(c) Calculation of normal tax payable**

Normal tax payable	R 42 000,00
Less: Rebate under section 6quat(1)	(5 600,00)
Less: Tax treaty credit rebate	<u>(8 400,00)</u>
Normal tax payable	<u>28 000,00</u>

### 5.9.7 Meaning of “income” in the article of a tax treaty dealing with the elimination of double taxation

The word “income”, as used in the article of a tax treaty dealing with the elimination of double taxation when determining the limitation on the amount of the rebate available under the tax treaty, must be interpreted to mean “net income” or “taxable income”. It does not mean “income” as defined in section 1(1).

<sup>108</sup> The normal tax rate for companies is 27% with effect from years of assessment ending on or after 31 March 2023.

This interpretation is in alignment with the OECD commentary on the maximum credit which provides that –<sup>109</sup>

“... the deduction which the State of residence (R) is to allow is restricted to that part of the income tax which is appropriate to the income derived from the State S, or E (so-called ‘maximum deduction’). Such maximum deduction may be computed ... by apportioning the total tax on total income according to the ratio between the income for which the credit is to be given and the total income... .

The maximum deduction is normally computed as the tax on net income, i.e. on the income from State E (or S) less allowable deductions (specified or proportional) connected with such income.”

South Africa levies income tax on taxable income and not on “income” as defined in section 1(1) (namely, the end result of gross income less exempt income). A ratio which is based on taxable income of the income concerned (namely, the foreign-source taxable income) to total taxable income achieves the objective of restricting the credit to that part of the tax which is attributable to the foreign-source taxable income. Since South Africa does not impose tax on “income” as defined in section 1(1), basing the apportionment on income or gross income is inappropriate.

#### **5.9.8 Payment of foreign tax under the tax treaty credit method**

Under the tax treaty credit method, foreign taxes must be paid before the relief can be granted. In contrast, section 6quat merely provides that the foreign taxes must be proved to be *payable*. SARS will not limit the application of the credit relief provided for in the tax treaty to foreign taxes actually paid, but will include an amount which is proved to be payable even if it has not yet been paid.

#### **5.10 Recalculation of the rebate under section 6quat(1) [section 6quat(5)]**

The entitlement to a rebate under section 6quat(1) arises in the year of assessment in which a foreign-source amount (on which foreign taxes are payable) is included in a resident’s taxable income. This fact is apparent from the wording of section 6quat(1) which provides that when the taxable income of a resident includes the types of foreign-source income specified in the section, the rebate calculated under section 6quat(1) must be deducted from the normal tax payable on that taxable income.

The foreign taxes may, however, be incurred in an earlier year of assessment, the same year of assessment or in a subsequent year of assessment to the year in which the foreign-source amount is included in the resident’s taxable income. The entitlement to the rebate does not arise in the year of assessment in which the foreign taxes are payable but arises when the foreign-source income is included in taxable income.

Foreign taxes which become payable in an earlier or the same year of assessment can and must be taken into account in the calculation of the rebate under section 6quat(1). It may happen that a foreign tax liability becomes payable only, or is increased or reduced, in a year of assessment subsequent to the year in which the foreign tax rebate has been allowed and subsequently proved to be inaccurate.

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<sup>109</sup> OECD *Model Tax Convention on Income and on Capital: Condensed Version* (2017) OECD Publishing at page 398 in paragraphs 62 and 63.

Section 6quat(5) provides that notwithstanding sections 99(1)<sup>110</sup> or 100 of the TA Act, an additional or reduced assessment may be made within six years *from* the date of the original assessment under which the taxpayer was entitled to the rebate under section 6quat(1) to give effect to an increased or reduced foreign tax credit in respect of that year.

Section 6quat(5) can also be applied to correct an overstatement or understatement error in the calculation of the amount of the rebate under section 6quat(1A) even if all the facts were known at the time of issue of the original assessment.

The onus rests with the taxpayer to immediately notify SARS in writing when that taxpayer claimed a rebate or deduction (or could have claimed a rebate or deduction) for purposes of section 6quat in a previous year of assessment and it is subsequently established that the actual amount of foreign tax payable exceeds or is less than that previously taken into account. The taxpayer must also provide SARS with sufficient information to be able to correct the relevant assessment assuming the timing requirements under section 6quat(5) are met.

SARS is not bound by the six-year limit if it is satisfied that the amount of tax proved to be payable was incorrectly reflected due to fraud, misrepresentation or non-disclosure of material facts.<sup>111</sup>

**Example 40 – Foreign taxes paid in a year subsequent to the years in which the related income accrued**

*Facts:*

Resident A received remuneration for management services from a foreign source under a three-year management contract. For South African tax purposes the income accrues as and when the services are rendered over the period of the contract even though payment takes place only at the end of the contract (namely, at the end of year 3). A final withholding tax is levied by the source country as and when payment is made (namely, in year 3).

The contract income is included in Resident A's taxable income in each of the three years on an accrual basis while the related foreign tax liability arises and is proved to be payable only in year 3.

*Result:*

The foreign tax paid in year 3 must be allocated to each of the three years in which the management fees accrued. Revised assessments must be issued for years 1 and 2, taking section 6quat(5) into account.

<sup>110</sup> Refers to a three-year prescription period.

<sup>111</sup> The exceptions to the prescription periods under section 99(2) of the TA Act also apply to the period prescribed under section 6quat(5).

**Example 41 – Refund of foreign taxes in a year of assessment, subsequent to the year in which the income accrued**

*Facts:*

Resident Company A had a capital gain on disposal of rental property in Country R. The capital gain was taxed in Country R in year 1 and payment of foreign tax was made to the tax authorities of Country R at the end of year 1. For South African tax purposes the amount was taxed in year 1. The date of issue of the original assessment for year 1 was 1 February of year 2.

During year 6 Company A discovered that it had incurred some additional expenses in connection with the disposal of the rental property which it had neglected to claim when submitting its tax return in Country R in year 1. Company A submitted a request for a reduced assessment in Country R. Country R's tax authorities approved the request in year 6 and reduced the tax liability of year 1. This resulted in a refund of foreign tax on 31 December of year 7.

*Result:*

The reduction in foreign taxes has the effect that the rebate originally allowed in year 1 must be reduced. This will result in a corresponding increase in the South African normal tax payable.

The Commissioner must issue an additional assessment to rectify the matter within six years from the date of the assessment in which the rebate was originally allowed.

The six-year period ends six years from 1 February of year 2, namely, on 31 January of year 8. Company A must inform SARS timeously that its foreign tax liability has been reduced. SARS must revise the relevant assessment on or before 31 January of year 8.

Failure by the taxpayer to disclose that the amount of the foreign tax liability was reduced will be regarded as non-disclosure of a material fact. Consequently, SARS will not be bound by the six-year period limitation in section 6quat(5) and may revise the relevant assessment at any time.

**Example 42 – Taxes payable in foreign jurisdiction determined in a year subsequent to the year in which the related foreign-source amount is taxed in South Africa**

*Facts:*

Resident Company A holds 100% of the participation and voting rights in CFC B. A portion of the income of CFC B did not qualify for any of the exemptions in section 9D(9) and an amount equal to the "net income" of CFC B was included in Company A's income. CFC B was subject to tax on the income in the foreign jurisdiction where it carries on its operations. Company A is entitled to claim a rebate under section 6quat(1).



However, because of the timing of the submission of the returns and payment of the taxes in the country of residence of CFC B, it was not possible to determine the amount of the foreign taxes proved to be payable when Company A submitted its tax return in South Africa.

*Result:*

Company A's assessment which included CFC B's net income may be reopened within six years under section 6quat(5) to allow a rebate for the foreign taxes proved to be payable.

## 6. The deduction of foreign taxes on income from a South African source [section 6quat(1C) and (1D)]

Section 6quat(1C)(a) provides for the deduction of foreign taxes from the income of a resident taxpayer in specified circumstances when determining the taxable income derived from carrying on any trade. If the taxpayer meets all the requirements of section 6quat(1C)(a), the taxpayer may elect to claim the deduction under the section but is not compelled to claim it.

The application of section 6quat(1C)(a) is limited to foreign taxes on income other than taxes contemplated in section 6quat(1A). Section 6quat(1A) determines the amount of the rebate for purposes of section 6quat(1) and in so doing contemplates any taxes on income proved to be payable to any sphere of government of a foreign country, without a right of recovery (other than a right of recovery to carry back losses to a prior year of assessment), on income and capital gains from a foreign source which are included in section 6quat(1). If any of these elements are not met, the foreign tax on income is not contemplated in section 6quat(1A) and potentially qualifies for a deduction under section 6quat(1C)(a) provided the requirements of that section are met. This means that the deduction under section 6quat(1C)(a) will be allowed in respect of –

- foreign taxes paid or proved to be payable by a resident on income from a South African-source; and
- foreign taxes paid but not proved to be payable by a resident on income from a foreign source,

without any right of recovery by any person [other than the two rights of recovery specified in section 6quat(1C)(a)], provided all the requirements of section 6quat(1C) and (1D) are met.

For example, a foreign tax validly paid to Country A's revenue authority in terms of Country A's local tax law and the relevant tax treaty, without a right of recovery, on services rendered in Country A is contemplated in section 6quat(1A) and therefore cannot qualify for a deduction under section 6quat(1C)(a). By contrast, a foreign tax incorrectly levied and paid to Country A's revenue authority in terms of Country A's local tax law and the relevant tax treaty on services rendered in Country A is not contemplated in section 6quat(1A) and therefore potentially qualifies for a deduction under section 6quat(1C)(a) if no person has a right of recovery (excluding the two rights specified in the section, broadly, a right to carry back losses or a right under a mutual agreement procedure). A further example of foreign tax not contemplated in section 6quat(1A) includes a foreign tax paid to Country A's revenue authority on services rendered in South Africa in contravention of the relevant tax treaty, since it is not a foreign tax on income from a foreign source included in section 6quat(1), it is not

proved to payable and there may also be a right of recovery. As the foreign tax is not contemplated in section 6quat(1A), it may qualify for a deduction under section 6quat(1C)(a) if the requirements of that section are met.

The following requirements must be met for section 6quat(1C)(a) to apply:

- The resident must be carrying on a trade.<sup>112</sup>
- The taxes must be a tax on income other than taxes contemplated in section 6quat(1A) (see above).
- The taxes must be paid<sup>113</sup> or proved to be payable by the resident to any sphere of government of any country other than South Africa, without any right of recovery by any person other than under a mutual agreement procedure under an international tax agreement<sup>114</sup> or a right of recovery under any entitlement to carry back losses arising during any year of assessment to any previous year of assessment.<sup>115</sup> The “without a right of recovery” requirement applies to taxes paid and taxes proved to be payable.

The following should be noted in applying section 6quat(1C) and (1D):

- A resident may not choose between the rebate method of relief under section 6quat(1) and the deduction method of relief under section 6quat(1C)(a). The deduction method potentially applies only to taxes which are not contemplated in section 6quat(1A) (see above).
- Excess foreign taxes calculated under section 6quat(1B)(a) (see 5.5) do not qualify for a deduction under section 6quat(1C)(a).
- The foreign taxes are deductible only from taxable income derived from the carrying on of any trade. No deduction is permissible against passive income.
- The deduction under section 6quat(1C)(a) is subject to section 23 which denies a deduction in specified circumstances notwithstanding that the expenditure may have met the requirements for deduction under any other section. Sections 23(f) and 23(g) respectively deny a deduction if the expense was incurred in respect of an amount which does not constitute income or to the extent the expense was not laid out for purposes of trade.
- The fact that the foreign taxes must be paid or proved to be payable, without any right of recovery by any person other than in terms of a mutual agreement procedure or an entitlement to carry back losses, generally means that the foreign tax jurisdiction must have a legal right under its tax laws and, if applicable, a relevant tax treaty or agreement to tax a particular item of income, since, although it depends on the laws of the particular country concerned, in the absence of such legal right existing the person will often have a right of recovery. A deduction will not be allowed when the resident, or another person, has a right of recovery (see 5.3.3) other than in terms of a mutual agreement procedure under an international agreement or an entitlement to carry back

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<sup>112</sup> See Interpretation Note 33 “Assessed Losses: Companies: The ‘Trade’ and ‘Income from Trade’ Requirements” for the meaning of “trade” and “carrying on of a trade”.

<sup>113</sup> The word “paid” was inserted in section 6quat(1C)(a) with effect from years of assessment commencing on or after 1 January 2016.

<sup>114</sup> With effect from years of assessment commencing on or after 1 January 2016.

<sup>115</sup> A resident may, for example, make an election in a foreign country for carry-back relief which means that a current year’s unabsorbed trade loss will be deducted against assessable income of the immediately preceding year of assessment.

losses. For example, a resident may have a right to dispute the incorrectly levied foreign tax under foreign law or a right to a rebate in respect of the foreign tax. Only the two specified rights of recovery are not taken into account when assessing whether the foreign tax is paid or proved to be payable, without a right of recovery.

- The foreign taxes are deductible only in the earlier of the year of assessment in which they are paid or proved to be payable, assuming the other requirements of the section are met such as there being no right of recovery [excluding the ones specifically referred to in section 6quat(1C)(a)]. Foreign taxes may not be deducted in an earlier or subsequent year of assessment. A foreign tax that is paid or proved to be payable in year 2 may potentially qualify for a deduction only in year 2 notwithstanding that the income to which it relates may have been partly included in taxable income in year 1 and partly in year 2.
- Section 6quat(1D) determines that the amount of foreign taxes which may be deducted under section 6quat(1C)(a) is limited to the taxable income [before taking into account any deduction under section 6quat(1C)(a)] attributable to income which is subject to tax as contemplated in that subsection. The deduction under section 6quat(1C)(a) may therefore not create or increase an assessed loss attributable to that income. For example, service income from a South African source is subject to foreign tax in Country X of R150,00. Taxable income from that service income is R100. The taxpayer incurred a loss from other sources of R500. Section 6quat(1D) limits the deduction under section 6quat(1C)(a) to R100 taxable income from the service income from a South African source. The taxpayer's assessed loss of R500 from other sources may be carried forward to subsequent years of assessment and is not impacted by the application of section 6quat(1D) (see **Examples 5 and 6** in **Annexure B** for the application of section 6quat(1D) in relation to a natural person).
- In determining the amount of the taxable income attributable to the income subject to foreign taxes contemplated in section 6quat(1C)(a), with effect from years of assessment commencing on or after 1 March 2018,<sup>116</sup> –
  - any allowable deductions under sections 11F and 18A must be deemed to have been incurred proportionately in respect of attributable and non-attributable taxable income;
  - the deduction under section 11F must be allocated in relation to the taxable income from attributable and non-attributable taxable income before taking into account any deduction under that section and sections 6quat(1C)(a) and 18A; and
  - the deduction under section 18A must be allocated in relation to attributable and non-attributable taxable income before taking into account any deduction under that section and section 6quat(1C)(a) [section 6quat(1D)]. See **Example 6** in **Annexure B**.

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<sup>116</sup> See earlier issues of this Note for the determination of the amount of taxable income attributable to the income subject to foreign taxes contemplated in section 6quat(1C)(a), relating to earlier years of assessment.

- Any excess foreign taxes under section 6quat(1C)(a) are forfeited and will not qualify for a deduction in that year under any other section [section 23B(3)]. Excess foreign taxes may also not be carried forward to succeeding years of assessment.
- Section 6quat(1C)(b) provides that when, during any year of assessment, any amount was deducted under section 6quat(1C)(a) from the income of a resident and, in any year of assessment subsequent to that year of assessment, the person receives a refund for the amount so deducted or is discharged from any liability in respect of that amount, so much of the amount received or so much of the amount of that discharge as does not exceed the amount of the deduction, must be included in income in that subsequent year of assessment.

**Example 43 – Deduction for foreign taxes under section 6quat(1C)(a) – A right of recovery exists under a tax treaty**

*Facts:*

Resident A provides managerial and technical support services to a client situated in Foreign Country B. All the work is performed in South Africa. Resident A does not have a permanent establishment in Foreign Country B. Despite the work being done in South Africa, Foreign Country B levies a withholding tax on fees paid for managerial and technical support services. Acting under its domestic law, Foreign Country B withheld the tax from the amount remitted to the resident.

A tax treaty has been entered into between South Africa and Foreign Country B. The tax treaty between South Africa and Foreign Country B does not specifically deal with income derived from rendering managerial and technical support services. Article 7, which deals with business profits, must be applied. The article provides that the profits of an enterprise of a contracting state shall be taxable only in that state unless the enterprise carries on business in the other contracting state through a permanent establishment situated therein. The tax treaty also makes provision for a mutual agreement procedure for the recovery of taxes between the contracting states.

Under Foreign Country B's domestic laws, the tax treaty prevails over domestic tax laws. Also under Foreign Country B's domestic laws, Resident A has a right to appeal and apply for a refund if tax is incorrectly levied under domestic laws and the tax treaty. Resident A elects not to appeal the incorrect levying of tax in Foreign Country B.

*Result:*

Under South Africa's source rules (see **5.2.3**) the actual source of income derived from the rendering of managerial and technical support services is located in the country where the work is done. In this instance the work is done in South Africa and the income is therefore from a South African source. Despite the fact that Foreign Country B's tax laws may support its right to tax the income, article 7 in effect confers an exclusive taxing right on South Africa. Resident A has a right of recovery under Foreign Country B's domestic laws which must be exercised by approaching the tax authorities of Foreign Country B.

The withholding tax paid to Foreign Country B is not a tax on income contemplated in section 6quat(1A), since it not a foreign tax on income from a foreign source included in section 6quat(1), it is not proved to payable as it is in contravention of the relevant tax treaty and there is a right of recovery. The withholding tax does not qualify for a rebate under section 6quat(1). However, the withholding tax may qualify for a deduction under section 6quat(1C)(a) if the requirements of that section and section 6quat(1D) are met.

One of the requirements in section 6quat(1C)(a) for both taxes paid (applicable in this example) or proved to be payable (not applicable in this example) is that there must be no right of recovery (other than the carry back of losses or in terms of a specified mutual agreement procedure). Resident A has a right of recovery and will therefore not qualify for a deduction under section 6quat(1C)(a). The decision by Resident A not to enforce the right of recovery does not mean that Resident A does not have a right of recovery. If the facts of the case were such that Resident A did not have a right of recovery in Foreign Country B, the withholding tax paid in that country would, subject to section 6quat(1D), qualify for a deduction under section 6quat(1C)(a).

**7. The translation of foreign taxes to rand and the treatment of foreign provisional tax payments (section 6quat(4) and (4A) and section 66(13A) and paragraph 21(1)(a)(ii) and (b)(ii) and paragraph 23 of the Fourth Schedule)**

**7.1 The translation of foreign taxes to rand [section 6quat(4)]**

A resident's liability for normal tax is determined in rand. For purposes of this determination any amount in foreign currency and related underlying foreign tax (which may qualify either for a rebate or a deduction) must be translated to rand.

Any foreign taxes proved to be payable as contemplated in section 6quat(1A) or any foreign taxes paid or proved to be payable as contemplated in section 6quat(1C) in respect of any amount included in a resident's taxable income in any year of assessment must be translated to rand on the last day of the year of assessment in which that amount is required to be included in a person's taxable income by applying the average exchange rate for the year of assessment.<sup>117</sup> The average exchange rate which must be used in translating the foreign tax liability is the average exchange rate for the year of assessment in which the amount received or accrued is included in the taxpayer's taxable income.

"Average exchange rate" is defined in section 1(1) in relation to a year of assessment and means the average determined by using the closing spot rates at the end of daily or monthly intervals during that year of assessment which must be consistently applied within that year of assessment. A person may choose between daily or monthly intervals each year. This choice must, however, be applied consistently in determining the average exchange rates for all foreign currency amounts recognised within that year. For example, a person may not use daily intervals to determine the average exchange rate for amounts received in euro and monthly intervals to determine the average exchange rate for amounts received in Canadian dollars. "Spot rate" is defined in section 1(1) and means the appropriate quoted exchange rate at a specific time by any authorised dealer in foreign exchange for the delivery of currency.

<sup>117</sup> Section 6quat(4).

Average exchange rates for a range of foreign currencies are available on the SARS website. These exchange rates may be used to translate foreign taxes to rand. Average exchange rates may also be –

- obtained from any authorised dealer in foreign exchange; or
- compiled using spot rates obtained from any authorised dealer.

#### **Example 44 – Translation of foreign taxes to rand**

*Facts:*

During year 1 a resident received interest denominated in euro from Country A on a monthly basis. The interest is subject to a withholding tax in Country A.

*Result:*

The foreign taxes expressed in euro must be translated to rand by applying the average exchange rate between the rand and the euro for year 1.

Multiple foreign tax liabilities denominated in different currencies must each be translated separately to rand using the applicable average exchange rate.

Fluctuations in exchange rates may cause a difference between –

- the rand equivalent of the amount of the foreign tax liability determined on the date that the liability is incurred; and
- the rand equivalent of the amount (or amounts) of the foreign tax paid, determined on the date (or dates) of payment of the foreign tax liability.

Any such difference has no bearing on the determination of the rand equivalent value of the taxpayer's foreign tax liability for purposes of section 6quat. Section 6quat(4) requires the foreign tax to be translated at the average exchange rate which applies in the year of assessment in which the amount in foreign currency is required to be included in the taxpayer's taxable income.

Section 24I governs the tax treatment of exchange differences. The spot rate on the date the foreign tax liability is incurred is the ruling exchange rate on transaction date for purposes of section 24I. A foreign exchange gain or loss must be determined on the foreign tax liability on translation and realisation date. There will be a difference between the spot rate on transaction date and the average exchange rate applied under section 6quat(4). This difference is not taken into account for tax purposes.

See also Interpretation Note 63 "Rules for the Translation of Amounts Measured in Foreign Currencies other than Exchange Differences Governed by Section 24I and the Eighth Schedule" and Interpretation Note 101 "Section 24I – Gains or losses on Foreign Exchange Transactions".

#### **Example 45 – Translation of foreign taxes to rand at the average exchange rate**

*Facts:*

Resident A received income of €100 from a foreign source in Country B in year 1 and became liable for income tax in Country B in that year of assessment. The tax was payable only in year 2. The average exchange rate for year 1 was €1: R14,0000 while the spot rate when the foreign taxes were paid was €1: R12,0000.

*Result:*

The foreign taxes are translated to rand for the purposes of section 6quat(1) by applying the average exchange rate of €1: R14,0000, being the average exchange rate in year 1 in which the resident was obliged to include the income earned in Country B in taxable income (year 1). The difference of R2 between the average exchange rate and the spot rate on the date of payment (14,0000 – 12,0000) is ignored in determining the amount of the foreign tax liability for purposes of the rebate under section 6quat.

The resultant movement in the exchange rate between the date the foreign tax liability was incurred, the last day of the year of assessment and the date on which the foreign tax liability is settled must be determined under section 24I and does not impact on the determination of the rebate under section 6quat(1).

## 7.2 Rounding off of foreign tax translated to rand, to the nearest R1 [section 6quat(4A)]

An amount translated under section 6quat(4) (see 7.1) must be rounded off to the nearest rand if it includes a number of cents which is less than one rand. By convention, amounts of less than 50 cents are rounded down, while amounts of 50 cents or more are rounded up. Thus R100,50 would be rounded up to R101 but R100,49 would be rounded down to R100.

## 7.3 A foreign tax year which does not match a South African year of assessment [section 66(13A)]

Section 66(13A) provides for the situation in which a person (other than a company) cannot conveniently return income for a year of assessment. In such event, the Commissioner may grant permission to draw accounts to a different agreed date. The agreed date may fall before or after the end of the year of assessment. There is no need to apportion the corresponding foreign tax liability between more than one South African year of assessment when the Commissioner grants permission for business income derived by a person (other than a company) from a foreign source to be returned over a period other than a year of assessment. See Interpretation Note 19 “Year of Assessment: Accounts Accepted to a Date other than the Last Day of February” for the practical application of section 66(13A).

### **Example 46 – Determination of the rebate under section 6quat(1) when a person’s foreign tax year does not match the year of assessment**

*Facts:*

Resident Individual A received business income from Country B during the calendar year ending 31 December year 1. The foreign tax year of an individual in Country B ends on 31 December. Under section 66(13A) SARS granted permission for Individual A to return the business income for the calendar year ending 31 December year 1 in the return of income for year 2 (namely, in the year of assessment ending 28 February year 2).

*Result:*

The foreign tax liability for the calendar year ending 31 December year 1 must be taken into account in Individual A's year of assessment ending February year 2 in determining the rebate under section 6quat(1). The tax liability must be translated to rand at the average exchange rate for the year of assessment ending February year 2.

In the absence of SARS' approval under section 66(13A), Individual A would have included the business income from Country B for the period 1 March year 1 to 31 December year 1 and 1 January year 2 to 28 February year 2 in the year of assessment ending 28 February year 2. In considering the rebate under section 6quat(1), the appropriate portion of the foreign tax liability for the years ending 31 December year 1 and 31 December year 2 would be taken into account assuming it satisfied all the requirements of section 6quat.

#### **7.4 Foreign provisional tax payments (paragraphs 21(1)(a)(ii) and (b)(ii) and paragraph 23 of the Fourth Schedule)**

In determining the amount of provisional tax payable for South African income tax purposes, a provisional taxpayer may take into account any tax proved to be payable to the government of any other country on foreign-source income provided it will qualify as a rebate under section 6quat(1). In practice SARS may allow provisional taxpayers to take foreign provisional tax payments (or similar advance payments) legally due and payable into account when determining their local provisional tax payments to the extent that the taxpayer is able to satisfy SARS that those payments will be or are the same or similar to the final tax liability in that country. Each case will be considered on its own merits.

To the extent section 6quat(1C)(a) applies, provisional taxpayers may take into account any tax paid or proved to be payable to the government of any other country when estimating taxable income for provisional tax purposes.

See 9. for documentary proof required by SARS for foreign taxes.

#### **8. Deductibility of foreign taxes against income in determining taxable income (sections 11(a), 23(d), 23(g) and 23B)**

Under section 23(d) any tax imposed under the Act may not be deducted in determining taxable income. The fact that a deduction of foreign taxes on income is not specifically denied under section 23(d) does not mean that foreign taxes automatically qualify for a deduction. To qualify for a deduction the foreign taxes must meet the requirements for deductibility under an appropriate section.

Section 11(a) read with section 23(g) is relevant in determining whether a foreign tax meets the requirements for deductibility and is therefore deductible in calculating taxable income. Section 6quat(1C)(a) also provides for a deduction of foreign taxes in limited circumstances (see 6.).

Section 11(a) provides a deduction for expenditure and losses, which are not of a capital nature, actually incurred in the production of the income. In context, the requirement which is of particular relevance is whether the foreign tax has been incurred in the production of income.



A tax, domestic or foreign, on profits is not an expense which has been incurred in the production of income but is instead an appropriation of profits already earned. In *Port Elizabeth Electric Tramway Company Ltd v CIR*, which is supportive of the principle, Watermeyer AJP held that –<sup>118</sup>

“[t]here is certainly one type of expenditure which must be excluded, and that is expenditure payable out of income after it has been earned. An example is a tax upon profits. In a sense such expenditure might be said to be attendant upon business operations, but there is a real distinction between “charge against profits and an appropriation of profits after they have been earned.” See *Van Ryn Deep Ltd v Commissioner for Inland Revenue* (1922, W.L.D. 22).”

In *Van Ryn Deep Ltd v CIR* the court held<sup>119</sup> that provincial tax, which had been imposed upon the profits after the profits had been earned, could in no way be said to have been an expense incurred in earning the profits or connected in any way with the production of the profits. The provincial tax was consequently not deductible for income tax purposes. The court held that what was done either voluntarily or involuntarily with the profits after it is earned does not affect the income tax.

Some tax commentators are of the opinion that foreign taxes on income claimed as a rebate under section 6quat(1) also qualify for a deduction under section 11(a). They appear to base their opinion on the fact that the rebate is a *deduction against normal tax payable* while a deduction under section 11(a) constitutes a *deduction against income* for purposes of determining taxable income. Consequently, their argument is that there is no double deduction as prohibited under section 23B. It is, however, unnecessary to consider whether section 23B prohibits any double deductions or prohibits double deductions only for the purposes of determining taxable income because there is no deduction for foreign taxes paid under section 11(a).

Similarly, taxes on income which are levied on a gross receipts basis, for example, a final withholding tax, are incurred *on* income and not *in* the production of income and therefore do not qualify for a deduction under section 11(a).

Taxes which are a charge against profits,<sup>120</sup> may, depending on the facts, be incurred in the production of income and qualify for a deduction under section 11(a) read with section 23(g) provided all the requirements of those sections are met. For example, Resident Company A carries on trading operations outside South Africa. Company A receives taxable sales income and incurs foreign customs duties. The customs duties are a charge against profits and not an appropriation of profits already earned. These duties are expenditure incurred in the production of income and will qualify for a deduction under section 11(a) read with section 23(g) if all the requirements of those sections are met.

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<sup>118</sup> (1936) CPD 241, 8 SATC 13 at 18.

<sup>119</sup> (1922) WLD 22, 33 SATC 101 at 105.

<sup>120</sup> A tax is a charge on profits if it is incurred irrespective of whether the taxpayer is in a taxable profit, taxable loss or break-even position.

**Example 47 – Deductibility of foreign taxes***Facts:*

Municipality A in Country Z levies two types of taxes, namely a tax on profits and municipal rates and taxes based on the value of properties owned.

*Result:*

The tax on profits is an appropriation of profits already earned and, depending on the facts, will potentially qualify for a rebate under section 6quat(1). A tax on profits is not considered to be incurred in the production of income and will not qualify for a deduction under section 11(a).

In contrast, the municipal rates and taxes are a charge against profits and not a tax on profits. Accordingly, although a charge of this nature will not qualify for a rebate under section 6quat(1), it may, depending on the facts, be incurred in the production of income and qualify for a deduction under section 11(a). For example, if the property is a rental property a deduction may be claimed under section 11(a) for the municipal rates and taxes if all the requirements of the section are met.

**9. Documentary proof required by SARS for foreign taxes**

Any foreign-source amount received by or accrued to a resident must be declared in the person's income tax return.

A person bears the onus to prove an entitlement to a rebate under section 6quat(1) or a deduction under section 6quat(1C)(a). A person must keep adequate records of amounts of income as well as foreign taxes proved to be payable or paid.

The requirements detailed in 9.1 – 9.5 reflect the information which is generally required, however SARS is not limited to the items mentioned and may request additional information and supporting documentation in a particular case.

Each case will be considered having regard to the facts of the particular case. Cases in which a taxpayer is unable to meet the requirements detailed in this Note will be handled on a case-by-case basis taking into consideration the facts of the particular case, the reasons why the taxpayer is unable to meet the requirements as detailed in this Note and the alternative sources of evidence provided by the taxpayer.

**9.1 Basic information required by SARS for foreign taxes**

SARS may request a resident to submit a statement containing the following information:

- The foreign tax year during which the relevant income was received by or accrued to the person.
- The precise name of the tax and the foreign country in which it was levied.
- The name of the law under which the tax was imposed.
- Whether the tax was levied by the national government, a state or local authority and the name of such authority.

## **9.2 Additional information required when the foreign tax has been withheld at source**

A person must on request provide certified copies of –

- a certificate of tax withheld, issued by the person withholding the tax; or
- a copy of a receipt issued by the relevant revenue authority as evidence of payment to the revenue authority of the amount of tax withheld.

## **9.3 Additional information required when the foreign tax was not withheld at source and the foreign tax jurisdiction operates a system of self-assessment of income tax**

A person must on request provide –

- certified copies of the relevant parts of the foreign income tax return containing the calculation of taxable income and taxes due, schedule of provisional tax payments and signature of the resident;
- certified copies of calculations of foreign provisional tax payable;
- documentary proof that a foreign tax liability was incurred, for example, a letter from the relevant foreign tax authority or a receipt for taxes paid; and
- a certificate from the resident's auditor stating that the amount is payable.

## **9.4 Additional information required when the foreign tax was not withheld at source and the foreign tax jurisdiction operates a system of assessment similar to South Africa**

On request a person must provide certified copies of –

- the relevant notice of assessment;
- the relevant parts of the foreign income tax return showing the calculation of the taxable income and taxes due, schedule of provisional tax payments and signature of the resident;
- calculations of any provisional taxes payable; and
- a copy of a statement of account issued by the relevant revenue authority requesting payment.

SARS may request further information such as –

- documentary proof that a foreign tax liability has been incurred, for example, a letter from the relevant foreign tax authority or a receipt for taxes paid; and
- a certificate from the resident's auditor stating that the amount is payable.

## 9.5 Translation of information worded in a foreign language

SARS may require a person to have any documentary evidence worded in a foreign language translated to English by a sworn translator.<sup>121</sup> A certificate prepared by the translator officially stating that the translation is a true rendition of the original may also be requested.

## 10. Conclusion

Section 6*quat*(1) provides for a rebate of foreign taxes on income to be deducted from normal tax payable by a resident. The amount of the rebate is determined under section 6*quat*(1A).

A resident is entitled to claim such a rebate only to the extent that the amount of the foreign tax is proved to be payable to a sphere of government of a foreign country without a right of recovery by any person, other than a right of recovery under any entitlement to carry back losses arising during any year of assessment to any year of assessment before such year of assessment.

A resident will not qualify for a rebate under section 6*quat*(1) for foreign tax proved to be payable to a foreign country on a South African-source amount.

To the extent that the amount of qualifying foreign taxes proved to be payable exceeds the amount of the rebate determined under section 6*quat*(1A) and (1B), the excess amount is carried forward to the immediately succeeding year of assessment. The amount so carried forward will potentially qualify for set-off against the normal tax payable on taxable income derived from foreign sources in the immediately succeeding year of assessment [paragraph (ii) of the proviso to section 6*quat*(1B)(a)].

Any balance of excess foreign taxes may not be carried forward for more than seven years, calculated from the year of assessment in which the balance was carried forward for the first time [paragraph (iii) of the proviso to section 6*quat*(1B)(a)].

Section 6*quat*(1C)(a) provides for the deduction of foreign taxes from the income of a resident taxpayer (as opposed to the claiming of a tax rebate). Its application is limited to foreign taxes other than taxes contemplated in section 6*quat*(1A). Section 6*quat*(1A) contemplates any taxes on income proved to be payable to any sphere of government of a foreign country, without a right of recovery (other than a right of recovery to carry back losses to a prior year of assessment, on income and capital gains from a foreign source which are included in section 6*quat*(1)). If one of these elements are not met, the foreign tax on income is not contemplated in section 6*quat*(1A) and potentially qualifies for a deduction under section 6*quat*(1C)(a) provided the requirements of that section are met.

Taxes must, for purposes of section 6*quat*(1C)(a), be paid or proved to be payable by the resident to any sphere of government of any country other than South Africa, without any right of recovery by any person other than under a mutual agreement procedure in terms of an international agreement or a right of recovery under any entitlement to carry back losses arising during any year of assessment to any previous year of assessment.

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<sup>121</sup> Under section 33(1) of the TA Act a senior SARS official may by notice require a person to produce a translation of information, which is not in one of the official languages of South Africa, in one of the official languages determined by the official within a reasonable period.

Section 6quat(1C)(b) provides that when, during any year of assessment, any amount was deducted under section 6quat(1C)(a) and the person receives a refund for the amount so deducted or is discharged from any liability for that amount in any subsequent year of assessment, so much of the amount received or so much of the amount of that discharge as does not exceed the amount of the deduction, must be included in the person's income in that subsequent year.

Any foreign taxes proved to be payable for purposes of section 6quat(1) or any foreign taxes paid or proved to be payable for purposes of section 6quat(1C) in respect of any amount which is included in taxable income in any year of assessment must be translated to rand on the last day of that year of assessment in which the amount is required to be included in a person's taxable income by applying the average exchange rate for the year of assessment. The average exchange rate which must be used in translating the foreign tax liability is the average exchange rate for the year of assessment in which the amount received or accrued is included in the taxpayer's taxable income.

Section 6quat(5) provides that notwithstanding sections 99(1) or 100 of the TA Act, an additional or reduced assessment may be made within six years *from* the date of the original assessment under which the taxpayer was entitled to the rebate under section 6quat(1) to give effect to an increased or reduced foreign tax credit for the year.

#### **SOUTH AFRICAN REVENUE SERVICE**

Date of 1st issue : 31 March 2003  
Date of 2nd issue : 31 March 2009  
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## Annexure A – Comprehensive Example – Three-step limitation under section 6quat

### Example – Foreign branch operations, foreign dividend income and income attributed from a CFC – Three-step limitation under section 6quat

#### Facts:

Resident Company D derived income and incurred expenses as follows during the year of assessment:

	SA Operations R	Foreign branch R	Foreign dividends R
Income	350 000	120 000	
Deductible expenses	(150 000)	(40 000)	
Foreign dividends (Note 1)			52 500
Foreign tax proved to be payable		20 000,00	3 500,00

Company D held shares in foreign companies which all constituted CFC's (Notes 2 to 4):

	CFC A	CFC B	CFC C
% Participation rights held by Company D	60%	15%	75%
Net income under section 9D(2A)	100 000	100 000	100 000
Taxable income of CFC in foreign country	120 000	125 000	100 000
Foreign tax proved to be payable by CFC	12 000,00	12 500,00	8 000,00

#### Notes:

- (1) The foreign dividend was paid by a foreign company which is not a CFC in relation to Company D. Company D held 5% of the equity shares in the foreign company.
- (2) CFC A did not have a foreign business establishment in the foreign country. CFC A's net income under section 9D(2A) consisted of interest income.
- (3) CFC B had a foreign business establishment in the foreign country. Although Company D held only 15% of the participation rights in the company, other residents held 60% of the participation rights which means the company is a CFC. CFC B's net income under section 9D(2A) [which constituted interest income in excess of the *de minimis* exclusion in section 9D(9A)(a)(iii)(cc)] for the year amounted to R100 000.
- (4) CFC C had a foreign business establishment in the foreign country. CFC C's net income under section 9D(2A) was made up as follows:
  - Interest income of R20 000 which was not attributable to CFC C's foreign business establishment.
  - "Diversionary" service income as contemplated in section 9D(9A)(a)(ii) attributable to CFC C's foreign business establishment which are not excluded from imputation under section 9D(2) under either section 9D(9A)(a) or section 9D(9)(b) of R80 000.

*Result:*

**Determination of Company D's taxable income and normal tax payable**

	R
South African-source taxable income (R350 000 – R150 000)	200 000
Profits of the foreign branch (R120 000 – R40 000)	80 000
Foreign dividend (Note A)	37 500
Attributed income from CFC A (R100 000 × 60%) (Note B)	60 000
Attributed income from CFC B (R100 000 × 15%) (Note B)	15 000
Attributed income from CFC C (R100 000 × 75%) (Note B)	<u>75 000</u>
Taxable income	<u>467 500</u>
Normal tax (R467 500 × 28% <sup>122</sup> )	130 900,00
Less: Rebate under section 6quat(1) (see calculations below)	<u>(37 000,00)</u>
Normal tax payable	<u>93 900,00</u>

**Notes:**

(A) The foreign dividend is partially exempt under section 10B(3). The taxable portion of the foreign dividend is calculated as follows:

$$R52\,500 - R15\,000 \text{ (Exempt portion is } R52\,500 \times 8 / 28) ^{123} = R37\,500$$

(B) Attributed income = net income × participation interest

**Calculation of the rebate of R37 000,00 to be allowed under section 6quat(1)**

**Determination of the amounts of foreign taxes potentially qualifying for a rebate under section 6quat(1), before applying the limitation under section 6quat(1B)(a) (see 1 – 5 below)**

**1. Foreign tax proved to be payable on foreign dividends**

The full amount of withholding tax of R3 500,00 potentially qualifies for a rebate under section 6quat(1) [paragraph (ii) of the proviso to section 6quat(1A)].

**2. Foreign tax proved to be payable on income derived from the foreign branch**

The full amount of R20 000,00 potentially qualifies for the rebate under section 6quat(1).

**3. Foreign tax proved to be payable on income attributed from CFC A**

**Step 1: Determination of foreign taxes attributable to the proportional amount of CFC A's net income included in Company D's income**

[Foreign taxes × (CFC A's net income determined under section 9D(2A) / CFC A's taxable income determined under foreign tax law)\*] × participation interest

$$[R12\,000,00 \times (R100\,000 / R120\,000)] \times 60\%$$

$$= R6\,000,00$$

\* = only applicable if taxable income under foreign tax principles is greater than net income under South African tax principles

<sup>122</sup> The normal tax rate for companies is 27% with effect from years of assessment ending on or after 31 March 2023.

<sup>123</sup> This ratio applies to companies with effect from years of assessment commencing on or after 1 March 2017.

**Step 2: Limitation under paragraph (iA)(bb) of the proviso to section 6quat(1B)(a)**

Paragraph (iA)(bb) of the proviso to section 6quat(1B)(a) does not apply, since CFC A does not have a foreign business establishment in the relevant foreign country.

The amount of foreign taxes proved to be payable by CFC A which potentially qualifies for the rebate under section 6quat(1) is therefore R6 000,00.

**4. Foreign tax proved to be payable on income attributed from CFC B****Step 1: Determination of foreign taxes attributable to the proportional amount of CFC B's net income included in Company D's income**

[Foreign taxes × (CFC B's net income determined under section 9D(2A) / CFC B's taxable income determined under foreign tax law)\*] × participation interest

[R12 500,00 × (R100 000 / R125 000)] × 15%

= R1 500,00

\* Only applicable if taxable income under foreign tax principles is greater than net income under South African tax principles

**Step 2: Limitation under paragraph (iA)(bb) of the proviso to section 6quat(1B)(a)**

The limitation under paragraph (iA)(bb) of the proviso to section 6quat(1B)(a) applies, since CFC B's net income includes an amount attributable to a foreign business establishment which is not excluded from attribution under section 9D(9A)(a) or section 9D(9)(b). As a result, the foreign tax will be limited to the normal tax attributable to the proportional amount of CFC B's net income included in Company D's income:

Proportional amount of CFC B's net income of R15 000 (R100 000 × 15%) / Company D's taxable income of R467 500 × normal tax payable of R130 900,00 = R4 200,00.

The amount of foreign taxes proved to be payable by CFC B potentially qualifying for a rebate under section 6quat(1) is R1 500,00, since this amount is less than the amount of the limitation determined under paragraph (iA)(bb) of the proviso to section 6quat(1B)(a).

**5. Foreign tax proved to be payable on income attributed from CFC C****Step 1: Determination of foreign taxes attributable to the proportional amount of CFC C's net income included in Company D's income**

[Foreign taxes × (CFC C's net income determined under section 9D(2A) / CFC C's taxable income determined under foreign tax law)\*] × participation interest

[R8 000,00 × (R100 000 / R100 000)] × 75%

= R6 000,00

\* Only applicable if taxable income under foreign tax principles is greater than net income under South African tax principles



**Step 2: Limitation under paragraph (iA)(bb) of the proviso to section 6quat(1B)(a)**

The limitation does not apply to the passive income not attributable to CFC C's foreign business establishment. The limitation applies only to the service income attributable to a CFC's foreign business establishment.

**Determination of foreign tax not subject to limitation under paragraph (iA)(bb) of the proviso to section 6quat(1B)(a)**

Attributable foreign taxes × (CFC C's passive income × participation interest) / (CFC C's total net income × participation interest)

$$R6\,000,00 \times (R20\,000 \times 75\%) / (R100\,000 \times 75\%)$$

$$= R6\,000,00 \times (R15\,000 / R75\,000)$$

$$= R1\,200,00$$

**Determination of foreign tax subject to limitation under paragraph (iA)(bb) of the proviso to section 6quat(1B)(a)**

Attributable foreign taxes × (CFC C's service income × participation interest) / (CFC C's total net income × participation interest)

$$R6\,000,00 \times (R80\,000 \times 75\%) / (R100\,000 \times 75\%)$$

$$= R6\,000,00 \times (R60\,000 / R75\,000)$$

$$= R4\,800,00$$

The foreign tax of R4 800,00 attributable to the service income will be limited to the amount of normal tax attributable to that amount, namely, R16 800,00, calculated as follows:

Proportional amount of CFC C's service income / Company D's taxable income × Normal tax payable by Company D

$$R60\,000 / R467\,500 \times R130\,900,00$$

$$= R16\,800,00$$

Thus, the full amount of foreign taxes of R4 800, 00 attributable to the service income qualifies for a rebate because this amount is less than the limitation of R16 800,00 determined under paragraph (iA)(bb) of the proviso to section 6quat(1B)(a).

The total amount of foreign taxes proved to be payable by CFC C potentially qualifying for a rebate under section 6quat(1) is R6 000,00 (R1 200,00 + R4 800,00).

**Summary of foreign taxes potentially qualifying for the rebate under section 6quat(1) (see 1 to 5 above)**

Foreign tax relating to –

	R
Foreign dividends	3 500,00
Net income of foreign branch	20 000,00
Net income of CFC A attributed to Company D	6 000,00
Net income of CFC B attributed to Company D	1 500,00
Net income of CFC C attributed to Company D	<u>6 000,00</u>
Total	<u>37 000,00</u>

**Final step (Step 3) in determining the overall limitation under section 6quat(1B)(a)**

Taxable income derived from all foreign sources (A) × Normal tax payable on (B)

Taxable income derived from all sources (B)

(R80 000 + R37 500 + R60 000 + 15 000 + R75 000) × R130 900,00

R467 500

= R267 500 × R130 900,00

R467 500

= R74 900,00

Since the total amount of foreign taxes qualifying for a rebate of R37 000,00 is less than the amount of the limitation determined under section 6quat(1B)(a) of R74 900,00, the full amount of R37 000,00 is allowed as a rebate under section 6quat(1).

## Annexure B – Additional examples relating to natural persons

### Example 1 – Persons married in community of property receiving foreign dividends

#### Facts:

A and B are married in community of property. They are residents and under the age of 65.

B holds 5% of the equity shares in Foreign Company C which are part of their joint estate. On 20 February 2022 Company C paid a dividend of \$5 400 to B. Withholding tax of \$600 was withheld from the gross amount of the dividend of \$6 000. A and B elected to translate the foreign dividend to rand by using the average exchange rate under section 25D(3). Assume that the average exchange rate for the 2022 year of assessment was \$1: R10,0000. B incurred interest of R1 000 in respect of the dividend received.

B received remuneration of R100 000 for the 2022 year of assessment from which employees' tax of R2 291,00 was deducted.

A and B received interest of R62 000 on a joint investment in South Africa.

#### Result:

#### Appropriation of foreign dividends and withholding taxes for purposes of section 7(2A)(b) and (2B)

	Total (100%) R	A (50%) R	B (50%) R
Foreign dividends (\$6 000 × R10,0000) <sup>124</sup>	60 000	30 000	30 000
Withholding tax (\$600 × R10,0000) <sup>125</sup>	6 000,00	3 000,00	3 000,00

#### 1. Calculation of normal tax payable by B

##### 1.1 Taxable income derived from foreign dividends (foreign source)

	R
Foreign dividends included in gross income	30 000
Less: Exemption under section 10B(3) (R30 000 × 25 / 45)	<u>(16 667)</u>
Taxable foreign dividends	<u>13 333</u>

#### Note:

Under section 23(q) B's portion of the interest incurred is not deductible.

##### 1.2 Taxable income derived from a South African source

	R	R
Remuneration		100 000
Interest received (R62 000 / 2)	31 000	
Less: Interest exemption under section 10(1)(i)	<u>(23 800)</u>	<u>7 200</u>
Taxable income derived from a South African source		<u>107 200</u>

<sup>124</sup> Application of the average exchange rate under section 25D(3).

<sup>125</sup> Application of the average exchange rate under section 6quat(4).

**1.3 Total taxable income derived from all sources**

	R
Taxable income derived from foreign sources	13 333
Taxable income derived from South African sources	<u>107 200</u>
Total taxable income	<u>120 533</u>

**1.4 Calculation of normal tax payable****(a) Calculation of normal tax payable before rebates**

Normal tax payable (R120 533 × 18%)	21 695,94
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**(b) Calculation of the rebate under section 6quat(1)**

Amount of foreign taxes potentially qualifying for the rebate is R3 000,00.

**Calculation of the limitation under section 6quat(1B)(a)**

Taxable income derived from all foreign sources (A) × Normal tax payable on (B)  
Taxable income derived from all sources (B)

$$\frac{R13\,333 \times R21\,695,94}{R120\,533} = R2\,399,94$$

**Notes:**

- (1) Under paragraph (ii) of the proviso to section 6quat(1A) the amount of foreign taxes attributable to the foreign dividends exempt under section 10B(3) of R16 667, potentially qualifies for the rebate under section 6quat(1).
- (2) R2 399,94 is allowed as a rebate under section 6quat(1). The balance of R600,06 (R3 000,00 – R2 399,94) may be carried forward to the 2023 year of assessment and be available for set-off under paragraph (ii) of the proviso to section 6quat(1B)(a) for that year.

**(c) Calculation of normal tax payable after taking into account rebates**

	R
Normal tax payable before rebates	21 695,94
Less: Primary rebate	<u>(15 714,00)</u>
	5 981,94
Less: Rebate under section 6quat(1)	<u>(2 399,94)</u>
Less: Employees' tax	<u>(2 291,00)</u>
Normal tax payable	<u>1 291,00</u>

**2. Calculation of normal tax payable by A****2.1 Taxable income derived from foreign dividends (foreign source)**

Foreign dividends included in gross income	30 000
Less: Exemption under section 10B(3) (R30 000 × 25 / 45)	<u>(16 667)</u>
Taxable income from foreign dividends	<u>13 333</u>

**Note:**

Under section 23(q) A's portion of the interest incurred is not deductible.

**2.2 Taxable income derived from a South African source**

	R	R
Interest received (R62 000 / 2)	31 000	
Less: Interest exemption under section 10(1)(i)	<u>(23 800)</u>	<u>7 200</u>
Taxable income derived from a South African source		<u>7 200</u>

**2.3 Total taxable income derived from all sources**

Taxable income derived from foreign sources	13 333
Taxable income derived from South African sources	<u>7 200</u>
Total taxable income	<u>20 533</u>

**2.4 Calculation of normal tax payable****(a) Calculation of normal tax payable before rebates**

Normal tax payable (R20 533 × 18%)	3 695,94
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**(b) Calculation of the rebate under section 6quat(1)**

Amount of foreign taxes potentially qualifying for the rebate is R3 000,00.

*Calculation of the limitation under section 6quat(1B)(a)*

Taxable income derived from all foreign sources (A) × Normal tax payable on (B)

Taxable income derived from all sources (B)

R13 333 × R3 695,94

R20 533

= R2 399,94

**Notes:**

- (1) Under paragraph (ii) of the proviso to section 6quat(1A) the amount of foreign taxes attributable to the foreign dividends which are exempt under section 10B(3) of R16 667, potentially qualifies for the rebate under section 6quat(1).
- (2) R2 399,94 may be allowed as a rebate under section 6quat(1) against normal tax payable. The balance of R600,06 (R3 000,00 – R2 399,94) may be carried forward to the 2023 year of assessment and be available for set-off under paragraph (ii) of the proviso to section 6quat(1B)(a) for that year.

**(c) Calculation of normal tax payable after taking into account rebates**

	R
Normal tax payable before rebates	3 695,94
Less: Primary rebate – section 6(2) – R15 714 limited to the amount of normal tax payable	<u>(3 695,94)</u>
	0
Less: Rebate under section 6quat(1) (Note)	<u>(0)</u>
Normal tax payable	<u>0</u>

**Note:**

Since the amount of normal tax payable is RNil after deducting the primary rebate, the amount of the rebate under section 6quat(1) is limited to RNil. The amount of R2 399,94 is forfeited and may not be carried forward to the 2023 year of assessment. This amount also does not qualify for a deduction under section 6quat(1C)(a).

**Example 2 – Natural person receiving foreign dividends and foreign interest***Facts:*

A (the taxpayer), aged 30, is married to B. A and B are residents of South Africa. B is a member of A's medical aid. The following income accrued to or was received by A during the 2022 year of assessment and the following expenses were incurred and taxes paid:

	SA source R	Foreign source R	Total R
Pensionable salary	200 000		200 000
Foreign dividends		56 500	56 500
Interest	121 000	44 000	165 000
Pension fund contributions	16 000		16 000
Retirement annuity fund contributions	15 000		15 000
Medical aid fund contributions	25 000		25 000
Qualifying medical expenses	16 152		16 152
Donations to an approved public benefit organisation*	1 500		1 500
Employees' tax**	6 719,00		6 719,00
Withholding tax on foreign dividends		20 000,00	20 000,00
Withholding tax on foreign interest		8 800,00	8 800,00

\* A obtained a section 18A receipt for the donation.

\*\* Employer deducted pension and retirement annuity fund contributions and the section 6A medical tax credits.

*Result:***(a) Calculation of taxable income**

	SA source R	Foreign source R	Total R
Salary	200 000		200 000
Foreign dividends		56 500	56 500
Interest	<u>121 000</u>	<u>44 000</u>	<u>165 000</u>
Total gross income	321 000	100 500	421 500
<i>Less: Exemptions</i>			
Foreign dividends – section 10B(3) (R56 500 × 25 / 45)		(31 389)	(31 389)
Interest – section 10(1)(j)	(23 800)		(23 800)
Income	297 200	69 111	366 311
<i>Less: Deduction for contributions to retirement funds – section 11F (see below)</i>	(25 151)	(5 849)	(31 000)
Taxable income before the deduction under section 18A	272 049	63 262	335 311
<i>Less: Deduction for donations – section 18A (see below)</i>	(1 217)	(283)	(1 500)
Taxable income	<u>270 832</u>	<u>62 979</u>	<u>333 811</u>

**Calculation of the deduction under section 11F**

The deduction of the contributions to retirement funds is limited to the lesser of:

- (a) R350 000; or
- (b) 27,5% of the higher of –
  - (i) Remuneration of R200 000; or
  - (ii) Taxable income of R366 311 before allowing a deduction for donations
 = R100 736
- (c) Taxable income before inclusion of the taxable capital gain and allowing a deduction for donations = R366 311

The maximum amount to be allowed under section 11F is R100 736. The full amount of R31 000 (R16 000 + R15 000) is therefore allowable under section 11F.

For purposes of determining the limitation under section 6quat(1B)(a) on the rebate under section 6quat(1), the contributions to retirement funds of R31 000 are apportioned between South African-source and foreign-source taxable income under section 6quat(1B)(a)(i)(aa):

South African source:  $R31\ 000 \times R297\ 200 / R366\ 311 = R25\ 151$

Foreign source:  $R31\ 000 \times R69\ 111 / R366\ 311 = R5\ 849$

**Calculation of the deduction under section 18A**

The deduction is limited to 10% of taxable income, therefore R33 531 ( $R335\ 311 \times 10\%$ ).

For purposes of determining the limitation under section 6quat(1B)(a) on the rebate under section 6quat(1), the donations of R1 500 are apportioned between South African-source and foreign-source taxable income under section 6quat(1B)(a)(i)(aa):

South African source:  $R1\ 500 \times R272\ 049 / R335\ 311 = R1\ 217$

Foreign source:  $R1\ 500 \times R63\ 262 / R335\ 311 = R283$

**(b) Calculation of normal tax before rebates**

Normal tax payable: (Rates of tax – 2022 year of assessment)

	R
On R216 200	38 916,00
On R117 611 [(R333 811 taxable income – R216 200 per tax table) × 26%]	<u>30 578,86</u>
Normal tax payable	<u>69 494,86</u>

**(c) Sum of qualifying foreign taxes which relate to total taxable foreign income**

	R
Foreign taxes payable on foreign dividends (Note)	20 000,00
Foreign taxes payable on foreign interest	<u>8 800,00</u>
Foreign taxes paid which relate to total taxable foreign income	<u>28 800,00</u>

**Note:**

Under paragraph (ii) of the proviso to section 6quat(1A) the amount of foreign taxes attributable to the exempt foreign dividends of R31 389 potentially qualifies for the rebate under section 6quat(1).

**(d) Calculation of the rebate under section 6quat(1)****Calculation of the limitation under section 6quat(1B)(a)**

Taxable income derived from all foreign sources (A) × Normal tax payable on (B)  
 Taxable income derived from all sources (B)

R62 979 × R69 494,86

R333 811

= R13 111,36

**Note:**

The amount of the limitation is less than the sum of qualifying foreign taxes of R28 800,00. The rebate under section 6quat(1) for the 2022 year of assessment is limited to R13 111,36 while the excess of R15 688,64 (R28 800,00 – R13 111,36) may be carried forward to the 2023 year of assessment to be used in determining the set-off under paragraph (ii) of the proviso to section 6quat(1B)(a) for that year of assessment.

**(e) Calculation of the rebates under sections 6A and 6B****Medical scheme fees tax credit – Section 6A**

(R664 × 12 months)

= R7 968,00

**Additional medical expenses tax credit – Section 6B****Formula:**

25% of the excess of [{"Medical aid contributions as exceeds "4 × medical scheme fees tax credit") + qualifying medical expenses} as exceeds 7,5% × taxable income]

= 25% of the excess of [{"(R25 000 – "R7 968 × 4") + R16 152} – (taxable income × 7.5%)]

= 25% of the excess of [{"(RNil) + R16 152} – (R333 811 × 7,5%)]

= 25% of the excess of [R16 152 – 25 035,83]

= 25% of the excess of (RNil)

The additional medical expenses tax credit is RNil.

**(f) Calculation of normal tax payable after taking into account the rebates under sections 6(2), 6A, 6B and 6quat(1)**

	R
Normal tax payable before rebates	69 494,86
Less: Primary rebate – section 6(2)	<u>(15 714,00)</u>
	53 780,86
Less: Medical scheme fees tax credit – section 6A	(7 968,00)
Less: Additional medical expenses tax credit – section 6B	(0)
Less: Rebate for foreign taxes – section 6quat(1)	<u>(13 111,36)</u>
	32 701,50
Less: Employees' tax	<u>(6 719,00)</u>
Normal tax payable	<u>25 982,50</u>



**Example 3 – Pensioner receiving foreign dividends and foreign interest***Facts:*

B (the taxpayer), aged 70 and single, is a resident. The following income accrued to or was received by B during the 2022 year of assessment and the following expenses were incurred and taxes paid:

	SA source R	Foreign source R	Total R
Pension	100 000		100 000
Foreign dividends		56 500	56 500
Interest	121 500	44 000	165 500
Qualifying medical expenses	38 000		38 000
Donations to an approved public benefit organisation	5 000*		5 000
Withholding tax on foreign dividends		5 650,00	5 650,00
Withholding tax on foreign interest		2 000,00	2 000,00
Excess foreign taxes brought forward from the 2021 year of assessment – paragraph (ii) of the proviso to section 6quat(1B)(a)			8 500,00

\* B obtained a section 18A receipt for the donation.

*Result:***(a) Calculation of taxable income**

	SA source R	Foreign source R	Total R
Pension	100 000		100 000
Foreign dividends		56 500	56 500
Interest	<u>121 500</u>	<u>44 000</u>	<u>165 500</u>
Total gross income	221 500	100 500	322 000
Less: Exemptions			
Foreign dividends – section 10B(3) (R56 500 × 25 / 45)		<u>(31 389)</u>	(31 389)
Interest – section 10(1)(i)	<u>(34 500)</u>		<u>(34 500)</u>
Income	187 000	69 111	256 111
Less: Deduction for donations			
– section 18A (see below)	<u>(3 651)</u>	<u>(1 349)</u>	<u>(5 000)</u>
Taxable income	<u>183 349</u>	<u>67 762</u>	<u>251 111</u>

**Calculation of the deduction under section 18A****Calculation of the limitation under section 18A(1)**

The deduction is limited to 10% of taxable income, therefore R25 611 (R256 111 × 10%).

For purposes of determining the limitation under section 6quat(1B)(a) on the rebate under section 6quat(1), the deduction is apportioned between South African-source and foreign-source taxable income under section 6quat(1B)(a):

South African source:  $R5\,000 \times R187\,000 / R256\,111 = R3\,651$

Foreign source:  $R5\,000 \times R69\,111 / R256\,111 = R1\,349$

**(b) Calculation of normal tax before rebates**

Normal tax payable: (Rates of tax – 2022 year of assessment)

	R
On R216 200	38 916,00
On R34 911 [(R251 111 taxable income – R216 200 per tax table) × 26%]	<u>9 076,86</u>
Normal tax payable	<u>47 992,86</u>

**(c) Sum of qualifying foreign taxes which relate to total taxable foreign income**

	R
Foreign taxes payable on foreign dividends (Note)	5 650,00
Foreign taxes payable on foreign interest	<u>2 000,00</u>
Foreign taxes paid which relate to total taxable foreign income	<u>7 650,00</u>

**Note:**

Under paragraph (ii) of the proviso to section 6quat(1A) the amount of foreign taxes attributable to the exempt foreign dividends of R31 389 potentially qualifies for the rebate under section 6quat(1).

**(d) Calculation of the rebate under section 6quat(1)****Calculation of the limitation under section 6quat(1B)(a)**

Taxable income derived from all foreign sources (A) × Normal tax payable on (B)

Taxable income derived from all sources (B)

R67 762 × R47 992,86

R251 111

= R12 950,82

**Note:**

The amount of the limitation exceeds the sum of qualifying foreign taxes of R7 650,00. The full amount of R7 650,00 is therefore allowed as a rebate under section 6quat(1) for the 2022 year of assessment.

**(e) Calculation of the rebates under sections 6A and 6B****Medical scheme fees tax credit – Section 6A**

B did not belong to a medical aid fund and therefore does not qualify for the rebate under section 6A.

**Additional medical expenses tax credit – Section 6B****Formula:**

[(33,3% × medical aid contributions as exceeds “3 × medical scheme fees tax credit”) + (33,3% × qualifying medical expenses)]

= (33,3% × RNil) + (33,3% × R38 000)

= R12 654,00

**(f) Calculation of normal tax payable after taking into account the rebates under sections 6(2), 6B and 6quat**

	R
Normal tax before rebates	47 992,86
Less: Primary rebate – section 6(2)(a)	(15 714,00)
Less: Secondary rebate – section 6(2)(b)	<u>(8 613,00)</u>
	23 665,86
Less: Medical scheme fees tax credit – section 6A	(0)
Less: Additional medical expenses tax credit – section 6B	(12 654,00)
Less: Rebate for foreign taxes – section 6quat(1)	<u>(7 650,00)</u>
	3 361,86
Less: Rebate for excess foreign taxes brought forward from the previous year of assessment – paragraph (ii)(bb) of the proviso to section 6quat(1B)(a)*	<u>(3 361,86)</u>
Normal tax payable	<u>0.</u>

\* The portion of the excess foreign taxes brought forward from the 2021 year of assessment which may be utilised in the 2022 year of assessment is calculated as follows:

	R
Amount of the limitation determined under section 6quat(1B)(a)	12 950,82
Less: Rebate for foreign taxes – 2022 – section 6quat(1)	<u>(7 650,00)</u>
Available for utilisation in respect of excess foreign taxes brought forward from previous years of assessment	<u>5 300,82</u>

Limited to normal tax payable of R3 361,86.

**(g) Calculation of excess foreign taxes to be carried forward to the 2023 year of assessment**

	R
Excess foreign taxes brought forward from the 2021 year of assessment – paragraph (ii)(bb) of the proviso to section 6quat(1B)(a)	8 500,00
Less: Amount available for utilisation and utilised in respect of excess foreign taxes brought forward from previous years of assessment (see calculation of normal tax payable above)	<u>(3 361,86)</u>
Excess foreign taxes from the 2021 year of assessment to be carried forward to the 2023 year of assessment	<u>5 138,14</u>

**Example 4 – Natural person receiving foreign dividends and a foreign capital gain***Facts:*

D (the taxpayer), aged 26, is married to E. D and E are residents. E is a member of D's medical aid.

The following income accrued to or was received by D during the 2022 year of assessment and the following expenses were incurred and taxes paid:

	SA source R	Foreign source* R	Total R
Salary	200 000		200 000
Foreign dividends		60 000	60 000
Capital gain	410 000	360 000	770 000
Medical aid fund contributions	25 000		25 000
Qualifying medical expenses	31 548		31 548
Donations to an approved public benefit organisation	50 000**		50 000
PAYE***	12 310,00		12 310,00
Withholding tax on foreign dividends		4 000,00	4 000,00
Foreign tax on capital gain		72 000,00	72 000,00

\* None of the income from a foreign source is attributable to a permanent establishment of D located outside South Africa.

\*\* D obtained a section 18A receipt for the donation.

\*\*\* The employer deducted the medical tax credits under section 6A.

*Result:***(a) Calculation of taxable income**

	SA source R	Foreign source R	Total R
Salary	200 000		200 000
Foreign dividends		<u>60 000</u>	<u>60 000</u>
Total gross income	200 000	60 000	260 000
<i>Less: Exemptions</i>			
Foreign dividends – section 10B(3) (R60 000 × 25 / 45)		<u>(33 333)</u>	<u>(33 333)</u>
Income	200 000	26 667	226 667
Taxable capital gain (see below)	<u>155 481</u>	<u>136 519</u>	<u>292 000</u>
Taxable income before deduction under section 18A	355 481	163 186	518 667
<i>Less: Deduction for donations</i>			
– section 18A (see below)	<u>(34 269)</u>	<u>(15 731)</u>	<u>(50 000)</u>
Taxable income	<u>321 212</u>	<u>147 455</u>	<u>468 667</u>

**Calculation of taxable capital gain****Sum of capital gains**

South African source of R410 000 + foreign source of R360 000

= R770 000

**Aggregate capital gain and net capital gain**

Sum of capital gains of R770 000 – annual exclusion of R40 000  
 = R730 000

**Taxable capital gain**

Net capital gain of R730 000 × inclusion rate of 40%  
 = R292 000

**South African portion of total taxable capital gain**

$R410\,000 / R770\,000 \times R292\,000$   
 = R155 481

Portion of the taxable capital gain allocated to foreign sources (see (c) below)

$R360\,000 / R770\,000 \times R292\,000$   
 = R136 519

**Calculation of the deduction under section 18A****Calculation of the limitation under section 18A(1)**

The deduction is limited to 10% of taxable income, therefore R51 867 ( $R518\,667 \times 10\%$ ).

For purposes of determining the limitation under section 6quat(1B)(a) on the rebate under section 6quat(1), the amount of R50 000 is apportioned between South African-source and foreign-source taxable income under section 6quat(1B)(a):

South African source:  $R50\,000 \times R355\,481 / R518\,667 = R34\,269$

Foreign source:  $R50\,000 \times R163\,186 / R518\,667 = R15\,731$

**(b) Calculation of normal tax payable before rebates**

Normal tax payable: (Rates of tax – 2022 year of assessment)

	R
On R467 500	110 739,00
On R1 167 [(R468 667 taxable income – R467 500 per tax table) × 36%]	<u>420,12</u>
Normal tax payable	<u>111 159,12</u>

**(c) Calculation of the portion of foreign taxes proved to be payable on the foreign taxable capital gain which potentially qualifies for a rebate under section 6quat(1)****Step 1 – The comparative inclusion limitation (Calculation of the portion of foreign taxes relating to the foreign taxable capital gain included in taxable income)**

Amount of the foreign taxable capital gain included in taxable income × Foreign tax payable

Amount of foreign taxable capital gain subject to foreign taxes

$R136\,519 / R360\,000 \times R72\,000,00$

= R27 303,80

**Step 2 – Foreign tax limitation on specified foreign taxable capital gains – Determination of the limitation under paragraph (iB) of the proviso to section 6quat(1B)(a)**

Paragraph (iB) of the proviso to section 6quat(1B)(a) applies because the capital gain is not attributable to a permanent establishment outside South Africa, therefore the amount calculated in step 1 is limited to:

Amount of foreign taxable capital gain which is not attributable  
to D's PE outside South Africa included in taxable income × Normal tax payable  
Total taxable income derived from all sources

R136 519 / R468 667 × R111 159,12

= R32 379,77

The limitation is greater than the amount calculated in step 1. The amount of R27 303,80 therefore potentially qualifies for a rebate under section 6quat(1).

**Step 3 – The overall normal tax on taxable income limitation [section 6quat(1B)(a)]—see (e) below.**

**(d) Sum of qualifying foreign taxes which relate to total taxable foreign income**

	R
Foreign taxes payable on foreign taxable capital gain (see (c) above)	27 303,80
Foreign taxes payable on foreign dividends (Note)	<u>4 000,00</u>
Foreign taxes paid which relate to total taxable foreign income	<u>31 303,80</u>

**Note:**

Under paragraph (ii) of the proviso to section 6quat(1A) the amount of foreign taxes attributable to the exempt foreign dividends of R33 333 potentially qualifies for the rebate under section 6quat(1).

**(e) Calculation of the rebate under section 6quat(1)**

The foreign taxes of R31 303,80 qualify for a rebate under section 6quat(1) subject to the limitation under section 6quat(1B)(a).

**Calculation of the limitation under section 6quat(1B)(a)**

Taxable income derived from all foreign sources (A) × Normal tax payable on (B)  
Taxable income derived from all sources (B)

R147 455 × R111 159,12

R468 667

= R34 973,59

The full amount of R31 303,80 therefore potentially qualifies for the rebate under section 6quat(1), since this amount is less than the amount determined under section 6quat(1B)(a) of R34 973,59.

**(f) Calculation of the rebates under sections 6A and 6B****Medical scheme fees tax credit – Section 6A**

R664 × 12 months

= R7 968,00

**Additional medical expenses tax credit – Section 6B****Formula:**

25% of the excess of [{"Medical aid contributions as exceeds "4 × medical scheme fees tax credit") + qualifying medical expenses} as exceeds 7,5% × taxable income]

= 25% of the excess of [{"(R25 000 – "R7 968 × 4") + R31 548} – (taxable income × 7.5%)]

= 25% of the excess of [{"(RNil) + R31548} – (R468 667 × 7.5%)]

= 25% of the excess of [R31 548 – 35 150]

= 25% of the excess of RNil

= RNil

**(g) Calculation of normal tax payable after taking into account the rebates under sections 6(2), 6A, 6B and 6quat(1)**

	R
Normal tax before rebates	111 159,12
Less: Primary rebate – section 6(2)	<u>(15 714,00)</u>
	95 445,12
Less: Medical scheme fees tax credit – section 6A	(7 968,00)
Less: Additional medical expenses tax credit – section 6B	(0)
Less: Rebate for foreign taxes – section 6quat(1)	<u>(31 303,80)</u>
	56 173,32
Less: Employees' tax	<u>(12 310,00)</u>
Normal tax payable	<u>43 863,32</u>

**Example 5 – Natural person receiving South African-source and foreign-source consulting fees and foreign dividends**

*Facts:*

X (the taxpayer), aged 33, is married to Z. Both are residents. Z belongs to X's medical aid. During the 2022 year of assessment X derived income from local and foreign sources. None of the income derived by X from a foreign source is attributable to a permanent establishment of X located outside South Africa.

X is a business management consultant who provides consulting services to a company resident in Country A of which 60% is rendered in South Africa while the remaining 40% is rendered in Country A. Under the tax laws of Country A withholding tax is levied at a flat rate of 15% on gross receipts. Country A regards all the income derived under the service contract as being derived from a source in Country A because the payment of the consulting fees is funded from Country A. South Africa regards the source of the income as the place where the services are rendered, namely, 60% is sourced in South Africa and the remaining 40% is sourced in Country A.

South Africa has not entered into a tax treaty with Country A. X elected that the foreign taxes attributable to South African-source service fees be deducted from income derived from service fees under section 6quat(1C)(a). X claimed a rebate under section 6quat(1) for the foreign taxes attributable to the foreign-source service fees.

The following income accrued to or was received by X during the 2022 year of assessment and the following expenses were incurred and taxes paid:

	SA source R	Foreign source R	Total R
Consulting fees (R200 000 × 60% / 40%)	120 000	80 000	200 000
Foreign dividends		60 000	60 000
Expenses incurred in the production of consulting fees (R50 000 × 60% / 40%)	30 000	20 000	50 000
Medical aid fund contributions	34 496		34 496
Qualifying medical expenses	31 548		31 548
Donations to an approved public benefit organisation	20 000*		20 000
Withholding tax on consulting fees		30 000,00	30 000,00
Withholding tax on foreign dividends		4 000,00	4 000,00

\* X obtained a section 18A receipt for the donation.

*Result:*

**(a) Calculation of taxable income**

	SA source R	Foreign source R	Total R
Consulting fees	120 000	80 000	200 000
Foreign dividends		<u>60 000</u>	<u>60 000</u>
Total gross income	120 000	140 000	260 000
Less: Exemptions			
Foreign dividends – section 10B(3) (R60 000 × 25 / 45)		<u>(33 333)</u>	<u>(33 333)</u>
Income	120 000	106 667	226 667



	SA source R	Foreign source R	Total R
Less: Expenses incurred in the production of consulting fees	(30 000)	(20 000)	(50 000)
Taxable income before deductions under sections 6quat(1C)(a) and 18A	90 000	86 667	176 667
Less: Deduction for donations – section 18A (see below)	(9 000)	(8 667)	(17 667)
Taxable income before the deduction under section 6quat(1C)(a)	81 000	78 000	159 000
Less: Deduction under section 6quat(1C)(a) (see below)	(18 000)		(18 000)
Taxable income	<u>63 000</u>	<u>78 000</u>	<u>141 000</u>

### Calculation of the deduction under section 18A

#### Calculation of the limitation under section 18A(1)

The deduction is limited to 10% of taxable income, therefore R17 667 (R176 667 × 10%).

For purposes of determining the limitation under section 6quat(1B)(a) on the rebate under section 6quat(1) and the limitation under section 6quat(1D) on the deduction under section 6quat(1C)(a), the amount of R17 667 is apportioned between South African-source and foreign-source taxable income under section 6quat(1B)(a):

South African source:  $R17\ 667 \times R90\ 000 / R176\ 667 = R9\ 000$

Foreign source:  $R17\ 667 \times R86\ 667 / R176\ 667 = R8\ 667$

#### Calculation of the deduction under section 6quat(1C)(a)

##### Foreign taxes attributable to South African-source income

$R30\ 000,00 \times 60\%$

= R18 000,00

Section 6quat(1D) determines that the amount of foreign taxes which may be deducted under section 6quat(1C)(a) (R18 000,00) is limited to the taxable income [before taking into account any deduction under section 6quat(1C)(a)] attributable to income which is subject to foreign tax as contemplated in section 6quat(1C)(a) (R81 000,00). The amount of the limitation determined under section 6quat(1D) of R81 000 is more than the foreign taxes of R18 000,00. Therefore, the amount of the deduction under section 6quat(1C)(a) is R18 000,00.

If X had provided consulting services in South Africa to other clients which were not subject to foreign tax as contemplated in section 6quat(1C), the taxable income attributable to the consulting fees from those services would not form part of the limitation calculation. The limitation in section 6quat(1D) is equal to the taxable income [before taking into account any deduction under section 6quat(1C)(a)] attributable to income which is subject to foreign tax as contemplated in section 6quat(1C).

#### (b) Calculation of normal tax before rebates

Normal tax payable: (Rates of tax – 2022 year of assessment)

R141 000 @ 18%

R  
25 380,00

**(c) Sum of qualifying foreign taxes which relate to total taxable foreign income**

	R
Foreign taxes payable on consulting fees (R30 000,00 × 40%)	12 000,00
Foreign taxes payable on foreign dividends (Note)	<u>4 000,00</u>
Foreign taxes paid which relate to total taxable foreign income	<u>16 000,00</u>

**Note:**

Under paragraph (ii) of the proviso to section 6quat(1A) the amount of foreign taxes attributable to the exempt foreign dividends of R33 333 potentially qualifies for the rebate under section 6quat(1).

**(d) Calculation of the rebate under section 6quat(1)**

*Calculation of the limitation under section 6quat(1B)(a)*

Taxable income derived from all foreign sources (A) × Normal tax payable on (B)

Taxable income derived from all sources (B)

R78 000 × R25 380,00

R141 000

= R14 040,00

The amount of the limitation is less than the sum of qualifying foreign taxes of R16 000,00. The rebate under section 6quat(1) for the 2022 year of assessment is therefore limited to R14 040,00 while the excess of R1 960,00 (R16 000,00 – R14 040,00) may be carried forward to the 2023 year of assessment to be used in determining the set-off under paragraph (ii) of the proviso to section 6quat(1B)(a) for that year.

**(e) Calculation of the rebates under sections 6A and 6B****Medical scheme fees tax credit – Section 6A**

R664 × 12 months

= R7 968,00

**Additional medical expenses tax credit – Section 6B****Formula:**

25% of the excess of [{"Medical aid contributions as exceeds "4 × medical scheme fees tax credit" + qualifying medical expenses} as exceeds 7,5% × taxable income]

= 25% of the excess of [{"(R34 496 – "R7 968 × 4") + R31 548} – (R141 000 × 7.5%)]

= 25% of the excess of [{"R2 624 + R31 548} – (R141 000 × 7.5%)]

= 25% of the excess of [R34 172 – R10 575]

= 25% of the excess of R23 597

= R5 899,25

**(f) Calculation of normal tax payable after taking into account the rebates under sections 6(2), 6A and 6B**

	R
Normal tax before rebates	25 380,00
Less: Primary rebate – section 6(2)	<u>(15 714,00)</u>
	9 666,00
Less: Medical scheme fees tax credit – section 6A	<u>(7 968,00)</u>
	1 698,00
Less: Additional medical expenses tax credit – section 6B (R5 899,25 limited to normal tax payable before the rebate of R1 698,00)	<u>(1 698,00)</u>
	0
Less: Rebate under section 6quat(1) (R14 040,00 limited to normal tax payable before the rebate of RNil).	<u>(0)</u>
Normal tax payable	<u>0</u>

**Note:**

The foreign taxes of R14 040,00 are forfeited, since normal tax payable before allowing the rebate is RNil. This amount may not be carried forward to the 2023 year of assessment to be used in determining the rebate under section 6quat(1) for that year.

**Example 6 – Natural person receiving SA and foreign-source consulting income and a local capital gain***Facts:*

The taxpayer, aged 30, received the following income during the 2022 year of assessment and incurred the following expenses:

	SA source R	Foreign source R	Total R
Consulting fees	120 000	80 000	200 000
Expenses incurred – consulting fees	(30 000)	(20 000)	(50 000)
Taxable capital gain	50 000		50 000
Retirement fund contributions	(100 000)		(100 000)
Donations to an approved public benefit organisation	(20 000)		(20 000)
Withholding tax on consulting fees	36 000,00	24 000,00	60 000,00

\* The taxpayer obtained a section 18A receipt for the donation.

\*\* The taxpayer did not belong to a medical scheme and did not claim any medical expenses.

The taxpayer elected that the foreign taxes attributable to South African-source consulting fees be deducted from income derived from consulting fees under section 6quat(1C)(a). The taxpayer claimed a rebate under section 6quat(1) for the foreign taxes attributable to the foreign-source consulting fees.

*Result:*

**(a) Calculation of taxable income**

	SA source R	Foreign source R	Total R
Consulting fees	120 000	80 000	200 000
Less: Expenses incurred – consulting fees	<u>(30 000)</u>	<u>(20 000)</u>	<u>(50 000)</u>
Taxable income before taxable capital gain and the deductions under sections 6quat(1C)(a), 11F and 18A	90 000	60 000	150 000
Taxable capital gain	<u>50 000</u>	<u>0</u>	<u>50 000</u>
Taxable income before the deductions under sections 6quat(1C)(a), 11F and 18A	140 000	60 000	200 000
Less: Deduction for contributions to retirement funds – section 11F (see below)	<u>(38 500)</u>	<u>(16 500)</u>	<u>(55 000)</u>
Taxable income after section 11F	101 500	43 500	145 000
Less: Deduction for donations – section 18A (see below)	<u>(10 150)</u>	<u>(4 350)</u>	<u>(14 500)</u>
Taxable income before the deduction under section 6quat(1C)(a)	91 350	39 150	130 500
Less: Deduction under section 6quat(1C)(a) (see below)	<u>(36 000)</u>	<u>(0)</u>	<u>(36 000)</u>
Taxable income	<u>55 350</u>	<u>39 150</u>	<u>94 500</u>

**(b) Calculation of the deduction under section 11F**

The deduction of the contributions to retirement funds (R100 000) is limited to the lesser of:

- (a) R350 000; or
- (b) 27,5% of the higher of –
  - (i) Remuneration of R0; or
  - (ii) R200 000 (Taxable income before allowing the deductions under sections 6quat(1C), 11F and 18A) (Taxable consulting income of R150 000 + taxable capital gain of R50 000)
    - = R55 000; or
- (c) Taxable income before allowing the deductions under sections 6quat(1C), 11F and 18A and before the inclusion of the taxable capital gain = R150 000.

The maximum amount allowed under section 11F in the current year is R55 000. Retirement fund contributions of R45 000 (R100 000 – R55 000) are carried forward to the 2023 year of assessment.

For purposes of determining the limitation under section 6quat(1B)(a) on the rebate under section 6quat(1) and the limitation under section 6quat(1D) on the deduction under section 6quat(1C)(a), the amount of R55 000 is treated as having been incurred proportionately in respect of South African and foreign-source taxable income. R38 500 ( $R55\,000 \times R140\,000 / R200\,000$ ) is treated as having been incurred in respect of South African-source taxable income. R16 500 ( $R55\,000 \times R60\,000 / R200\,000$ ) is treated as having been incurred in respect of foreign-source taxable income.

**(c) Calculation of the deduction under section 18A**

The deduction is limited to 10% of taxable income of R145 000 (Taxable consulting income of R95 000 + taxable capital gain of R50 000) = R14 500. Donations of R5 500 (R20 000 – R14 500) are carried forward to the 2023 year of assessment.

For purposes of determining the limitation under section 6quat(1B)(a) on the rebate under section 6quat(1) and the limitation under section 6quat(1D) on the deduction under section 6quat(1C)(a), this amount is treated as having been incurred proportionately in respect of South African and foreign-source taxable income. R 10 150 ( $R14\,500 \times R101\,500 / R145\,000$ ) is treated as having been incurred in respect of South African taxable income. R4 350 ( $R14\,500 \times R43\,500 / R145\,000$ ) is treated as having been incurred in respect of foreign-source taxable income.

**(d) Calculation of the deduction under section 6quat(1C)(a)**

Under section 6quat(1D), the amount of foreign taxes which may be deducted under section 6quat(1C)(a) is limited to the taxable income [before taking into account any deduction under section 6quat(1C)(a)] attributable to income which is subject to tax as contemplated in that subsection. The relevant taxable income is R58 725 (see below), therefore the full amount of R36 000,00 may be deducted.

Taxable income of R58 725 referred to above is calculated as follows:

	R
Net consulting income from a South African source	90 000
Less: Deduction for contributions to retirement funds – section 11F ( $R38\,500 \times R90\,000 / R140\,000$ )	<u>(24 750)</u>
	65 250
Less: Deduction for donations – section 18A ( $R65\,250 \times 10\%$ )	<u>(6 525)</u>
	<u>58 725</u>

If the taxpayer had provided consulting services in South Africa to other clients which were not subject to foreign tax as contemplated in section 6quat(1C), the taxable income attributable to the consulting fees from *those* services would not form part of the limitation calculation. The limitation in section 6quat(1D) is equal to the taxable income [before taking into account any deduction under section 6quat(1C)(a)] *attributable to income which is subject to foreign tax as contemplated in section 6quat(1C)*.

**(e) Calculation of normal tax before rebates**

Normal tax payable: (Rates of tax – 2022 year of assessment)

	R
R94 500 @ 18%	17 010,00

**(f) Calculation of the rebate under section 6quat(1)****Calculation of the limitation under section 6quat(1B)(a)**

Taxable income derived from all foreign sources (A) × Normal tax payable on (B)

Taxable income derived from all sources (B)

R39 150 × R17 010,00

R94 500

= R7 047,00

The amount of the limitation of R7 047,00 is less than the sum of qualifying foreign taxes of R24 000,00. The rebate under section 6quat(1) for the 2022 year of assessment is therefore limited to R7 047,00 while the excess of R16 953,00 (R24 000,00 – R7 047,00) may be carried forward to the 2023 year of assessment to be used in determining the set-off under paragraph (ii) of the proviso to section 6quat(1B)(a) for that year.

**(g) Calculation of normal tax payable after taking into account the rebates under sections 6(2) and 6quat(1)**

	R
Normal tax before rebates	17 010,00
Less: Primary rebate – section 6(2)	<u>(15 714,00)</u>
	1 296,00
Less: Rebate under section 6quat(1) (R7 047,00 limited to normal tax payable before the rebate of R1 296,00).	<u>(1 296,00)</u>
Normal tax payable	<u>0</u>

**Note:**

Foreign taxes of R5 751,00 (R7 047,00 – R1 296,00) are forfeited, since the rebate under section 6quat(1) is limited to normal tax payable before allowing the rebate of R1 296,00. The amount of R5 751,00 may not be carried forward to the 2023 year of assessment to be used in determining the rebate under section 6quat(1) for that year.

**Example 7 – Foreign taxes relating to services rendered outside South Africa**

*Facts:*

Individual A, aged 30, rendered services inside and outside South Africa during the 2022 year of assessment. Remuneration for services rendered inside South Africa amounted to R500 000. Remuneration of R1 500 000 was received for services rendered outside South Africa. Individual A qualified for the exemption for services rendered outside South Africa of R1 250 000 under section 10(1)(o)(ii). Foreign taxes of R450 000,00 were withheld from the remuneration of R1 500 000.

*Result:*

**Calculation of the rebate under section 6quat(1)**

**(a) Total taxable income from all sources**

	R
Taxable income from a South African source	500 000
Taxable income from a foreign source (R1 500 000 – R1 250 000)	<u>250 000</u>
Total taxable income	<u>750 000</u>

**(b) Calculation of normal tax payable before rebates**

Normal tax payable: (Rates of tax – 2022 year of assessment)

On R613 600	163 335,00
On R136 400 [(R750 000 taxable income – R613 600 per tax table) × 39%]	<u>53 196,00</u>
Normal tax payable	<u>216 531,00</u>

**(c) Calculation of the amount of foreign taxes qualifying for a rebate under section 6quat(1)**

*Limitation of the amount of foreign taxes under section 6quat(1A)*

Remuneration for foreign services included in taxable income × Foreign tax  
Total remuneration for foreign services

R250 000 (R1 500 000 – R1 250 000) × R450 000,00

R1 500 000

= R75 000,00 (Note 1)

*Limitation of the rebate under section 6quat(1B)(a)*

Taxable income derived from all foreign sources (A) × Normal tax payable on B  
Total taxable income derived from all sources (B)

R250 000 × R216 531,00

R750 000

= R72 177,00

Therefore, the amount of the rebate is R72 177,00 (Note 2).

**(d) Calculation of normal tax payable after taking into account the rebates under sections 6(2) and 6quat(1)**

	R
Normal tax before rebates	216 531,00
Less: Primary rebate – section 6(2)	<u>(15 714,00)</u>
	200 817,00
Less: Rebate under section 6quat(1)	<u>(72 177,00)</u>
Normal tax payable	<u>128 640,00</u>

**Notes:**

- (1) Under section 6quat(1A)(a)(i) foreign taxes qualifying for a rebate under section 6quat(1) are limited to foreign taxes in respect of foreign income included in a resident's taxable income. Foreign taxes in respect of the exempt foreign income of R1 250 000, therefore do not qualify for the rebate under section 6quat(1) and are not carried forward to subsequent years of assessment.
- (2) R72 177,00 of the qualifying withholding tax of R75 000,00 is deductible from normal tax payable. The balance of R2 823,00 (R75 000,00 – R72 177,) is carried forward to the 2023 year of assessment under paragraph (ii)(aa) of the proviso to section 6quat(1B)(a).

## Annexure C – The law

### Section 6quat

**6quat. Rebate or deduction in respect of foreign taxes on income.**—(1) Subject to subsection (2), where the taxable income of any resident during a year of assessment includes—

- (a) any income received by or accrued to such resident from any source outside the Republic; or
- (b) any proportional amount contemplated in section 9D; or
- (c) . . . . .
- (d) . . . . .
- (e) any taxable capital gain contemplated in section 26A, from a source outside the Republic; or
- (f) any amount—
  - (i) contemplated in paragraph (a) or (b) which is received by or accrued to any other person and which is deemed to have been received by or accrued to such resident in terms of section 7;
  - (ii) of capital gain of any other person from a source outside the Republic and which is attributed to that resident in terms of paragraph 68, 69, 70, 71, 72 or 80 of the Eighth Schedule; or
  - (iii) contemplated in paragraphs (a), (b) or (e) which represents capital of a trust, and which is included in the income of that resident in terms of section 25B(2A) or taken into account in determining the aggregate capital gain or aggregate capital loss of that resident in terms of paragraph 80(3) of the Eighth Schedule,

in determining the normal tax payable in respect of that taxable income there must be deducted a rebate determined in accordance with this section.

(1A) For the purposes of subsection (1), the rebate shall be an amount equal to the sum of any taxes on income proved to be payable to any sphere of government of any country other than the Republic, without any right of recovery by any person (other than a right of recovery in terms of any entitlement to carry back losses arising during any year of assessment to any year of assessment prior to such year of assessment) by—

- (a) such resident in respect of—
  - (i) any income contemplated in subsection (1)(a); or
  - (ii) . . . . .
  - (iii) any amount of taxable capital gain as contemplated in subsection (1)(e); or
- (b) any controlled foreign company, in respect of such proportional amount contemplated in subsection (1)(b), subject to section 72A(3); or
- (c) . . . . .
- (d) . . . . .
- (e) . . . . .
- (f) any other person contemplated in subsection (1)(f)(i) or (ii) or any trust contemplated in subsection (1)(f)(iii), in respect of the amount included in the taxable income of that resident as contemplated in subsection (1)(f),

which is so included in that resident's taxable income: Provided that—

- (i) where such resident is a member of any partnership or a beneficiary of any trust and such partnership or trust is liable for tax as a separate entity in such other country, a proportional amount of any tax payable by such entity, which is attributable to the interest of such resident in such partnership or trust, shall be deemed to have been payable by such resident; and
- (ii) for the purposes of this subsection, the amount so included in such resident's taxable income must be determined without regard to section 10B(3).



## (1B) Notwithstanding the provisions of subsection (1A)—

(a) the rebate or rebates of any tax proved to be payable as contemplated in subsection (1A), shall not in aggregate exceed an amount which bears to the total normal tax payable the same ratio as the total taxable income attributable to the income, proportional amount, taxable capital gain or amount, as the case may be, which is included as contemplated in subsection (1), bears to the total taxable income: Provided that—

(i) in determining the amount of the taxable income that is attributable to that income, proportional amount, taxable capital gain or amount—

(aa) any allowable deductions contemplated in sections 11F and 18A must be deemed to have been incurred proportionately in respect of taxable income derived from sources within and outside the Republic;

(bb) the deduction under section 11F must be allocated in relation to the taxable income from sources within and outside the Republic before taking into account any deduction in terms of that section, subsection (1C) and section 18A; and

(cc) the deduction under section 18A must be allocated in relation to taxable income from sources within and outside the Republic before taking into account any deduction in terms of that section and subsection (1C);

(iA) the taxes contemplated in subsection (1A)(b) that are attributable to any proportional amount which—

(aa) . . . . .

(bb) relates to any amount contemplated in section 9D(9A)(a) which is not excluded from the application of section 9D(2) in terms of that section or section 9D(9)(b),

shall in aggregate be limited to the amount of the normal tax which is attributable to those proportional amounts;

(iB) the taxes contemplated in subsection (1A)(a)(iii) which are attributable to any taxable capital gain in respect of an asset which is not attributable to a permanent establishment of the resident outside the Republic, must in aggregate be limited to the amount of normal tax which is attributable to that taxable capital gain;

(ii) where the sum of any such taxes proved to be payable (excluding any taxes contemplated in paragraphs (iA) and (iB) of this proviso) exceeds the rebate as so determined (hereinafter referred to as the excess amount), that excess amount may—

(aa) be carried forward to the immediately succeeding year of assessment and shall be deemed to be a tax on income paid to the government of any other country in that year; and

(bb) be set off against the amount of any normal tax payable by that resident during that year of assessment in respect of any amount derived from any other country which is included in the taxable income of that resident during that year, as contemplated in subsection (1), after any tax payable to the government of any other country in respect of any amount so included during such year of assessment which may be deducted in terms of subsections (1) and (1A), has been deducted from the amount of such normal tax payable in respect of such amount so included; and

(iii) the excess amount shall not be allowed to be carried forward for more than seven years reckoned from the year of assessment when such excess amount was for the first time carried forward;

(b) . . . . .

(c) . . . . .

(d) . . . . .

(e) . . . . .

(1C)(a) For the purpose of determining the taxable income derived by any resident from carrying on any trade, there may at the election of the resident be allowed as a deduction from the income of such resident so derived the sum of any taxes on income (other than taxes contemplated in subsection (1A)) paid or proved to be payable by that resident to any sphere of government of any country other than the Republic, without any right of recovery by any person other than in terms of a mutual agreement procedure in terms of an international tax agreement or a right of recovery in terms of any entitlement to carry back losses arising during any year of assessment to any year of assessment prior to such year of assessment.

(b) Where, during any year of assessment, any amount was deducted in terms of this subsection from the income of a resident and, in any year of assessment subsequent to that year of assessment, that resident receives any amount by way of refund in respect of the amount so deducted or is discharged from any liability in respect of that amount, so much of the amount so received or so much of the amount of that discharge as does not exceed that amount must be included in the income of that resident in respect of that subsequent year of assessment.

(1D) Notwithstanding subsection (1C), the deduction of any tax paid or proved to be payable as contemplated in that subsection shall not in aggregate exceed the total taxable income (before taking into account any such deduction) attributable to income which is subject to taxes as contemplated in that subsection: Provided that in determining the amount of the taxable income that is attributable to that income—

- (a) any allowable deductions contemplated in sections 11F and 18A must be deemed to have been incurred proportionately in respect of attributable and non-attributable taxable income;
- (b) the deduction under section 11F must be allocated in relation to the taxable income from attributable and non-attributable taxable income before taking into account any deduction in terms of that section, subsection (1C) and section 18A; and
- (c) the deduction under section 18A must be allocated in relation to attributable and non-attributable taxable income before taking into account any deduction in terms of that section and subsection (1C).

(2) The rebate under subsection (1) and the deduction under subsection (1C) shall not be granted in addition to any relief to which the resident is entitled under any agreement between the governments of the Republic and the said other country for the prevention of or relief from double taxation, but may be granted in substitution for the relief to which the resident would be so entitled.

(3) For the purposes of this section—

**“controlled company”** . . . . .

**“controlling company”** . . . . .

**“group of companies”** . . . . .

**“qualifying interest”** . . . . .

**“taxes on income”** does not include any compulsory payment to the government of any other country which constitutes a consideration for the right to extract any mineral or natural oil.

(4) For the purpose of this section the amount of any foreign tax proved to be payable as contemplated in subsection (1A) or any amount paid or proved to be payable as contemplated in subsection (1C) in respect of any amount which is included in the taxable income of any resident during any year of assessment, shall be translated to the currency of the Republic on the last day of that year of assessment by applying the average exchange rate for that year of assessment.

(4A) If the amount translated in accordance with subsection (4) includes a number of cents that is less than one rand, that amount must be rounded off to the nearest rand.

(5) Notwithstanding section 99(1) or 100 of the Tax Administration Act, an additional or reduced assessment in respect of a year of assessment to give effect to subsections (1) and (1A) may be made within a period that does not exceed six years from the date of the original assessment in respect of that year.

**Section 7(2) to (8)****7. When income is deemed to have accrued or to have been received.—**

(2) Any income received by or accrued to any person married in or out of community of property (hereinafter referred to as the recipient) shall be deemed for the purposes of this Act to be income accrued to such person's spouse (hereinafter referred to as the donor) if—

- (a) such income was derived by the recipient in consequence of a donation, settlement or other disposition made by the donor on or after 20 March 1991 or of a transaction, operation or scheme entered into or carried out by the donor on or after that date, and the sole or main purpose of such donation, settlement or other disposition or of such transaction, operation or scheme was the reduction, postponement or avoidance of the donor's liability for any tax, levy or duty which, but for such donation, settlement, other disposition, transaction, operation or scheme, would have become payable by the donor under this Act or any other Act administered by the Commissioner; or
- (b) income was received by or accrued to the recipient—
  - (i) from any trade carried on by the recipient in partnership or association with the donor or which is in any way connected with any trade carried on by the donor; or
  - (ii) from the donor or any partnership of which the donor was at the time of such receipt or accrual a member or any private company of which the donor was at such time the sole or main holder of shares or one of the principal holder of shares,
 

and such income represents the whole or any portion of the total income so received by or accrued to the recipient which exceeds the amount of income to which the recipient would reasonably be entitled having regard to the nature of the relevant trade, the extent of the recipient's participation therein, the services rendered by the recipient or any other relevant factor; or
- (c) . . . . .

(2A) In the case of spouses who are married in community of property—

- (a) any income (other than income derived from the letting of fixed property) which has been derived from the carrying on of any trade shall, if such trade is carried on—
  - (i) by only one of the spouses, be deemed to have accrued to that spouse; or
  - (ii) jointly by both spouses, be deemed, subject to the provisions of subsection (2)(b), to have accrued to both spouses in the proportions determined by them in terms of the agreement that regulates their joint trade or, if there is no such agreement, in the proportion to which each spouse would reasonably be entitled having regard to the nature of the relevant trade, the extent of each spouse's participation therein, the services rendered by each spouse or any other relevant factor; and
- (b) any income derived from the letting of fixed property and any income derived otherwise than from the carrying on of any trade shall be deemed to have accrued in equal shares to both spouses: Provided that any such income which does not fall into the joint estate of the spouses shall be deemed to be income accrued to the spouse who is entitled thereto.

(2B) So much of any deduction or allowance which may be made under the provisions of this Act in the determination of the taxable income derived from any income referred to in subsections (2) and (2A) as relates to any portion of such income which is under the provisions of that subsection deemed to be income accrued to a spouse shall be deemed to be a deduction or allowance which may be made in the determination of the taxable income of such spouse.

(2C) For the purposes of subsection (2A)—

- (a) any benefit paid or payable to a spouse in his or her capacity as a member or past member of a pension fund, pension preservation fund, provident fund, provident preservation fund, benefit fund, retirement annuity fund or any other fund of a similar nature shall be deemed to be income derived by such spouse from a trade carried on by him or her;
- (b) any annuity amount (as defined in section 10A) paid or payable to a spouse shall be deemed to be income derived by such spouse from a trade carried on by him; and

(c) where any spouse is the—

- (i) registered holder of a patent as defined in the Patents Act or any design as defined in the Designs Act or any trade mark as defined in the Trade Marks Act; or
- (ii) author of a work on which copyright has been conferred in terms of the Copyright Act or the owner of such a copyright by reason of assignment, testamentary disposition or operation of law; or
- (iii) holder of any other property or right of a similar nature,  
any income derived from the grant of the right of use of such patent, design, trade mark, copyright or other property or right shall be deemed to be income derived by such spouse from a trade carried on by him.

(3) Income shall be deemed to have been received by the parent of any minor child or stepchild, if by reason of any donation, settlement or other disposition made by that parent of that child—

- (a) it has been received by or has accrued to or in favour of that child or has been expended for the maintenance, education or benefit of that child; or
- (b) it has been accumulated for the benefit of that child.

(4) Any income received by or accrued to or in favour of any minor child or stepchild of any person, by reason of any donation, settlement or other disposition made by any other person, shall be deemed to be the income of the parent of that child, if such parent or his or her spouse has made a donation, settlement or other disposition or given some other consideration in favour directly or indirectly of the said other person or his or her family.

(5) If any person has made any donation, settlement or other disposition which is subject to a stipulation or condition, whether made or imposed by such person or anybody else, to the effect that the beneficiaries thereof or some of them shall not receive the income or some portion of the income thereunder until the happening of some event, whether fixed or contingent, so much of any income as would, but for such stipulation or condition, in consequence of the donation, settlement or other disposition be received by or accrue to or in favour of the beneficiaries, shall, until the happening of that event or the death of that person, whichever first takes place, be deemed to be the income of that person.

(6) If any deed of donation, settlement or other disposition contains any stipulation that the right to receive any income thereby conferred may, under powers retained by the person by whom that right is conferred, be revoked or conferred upon another, so much of any income as in consequence of the donation, settlement or other disposition is received by or accrues to or in favour of the person on whom that right is conferred, shall be deemed to be the income of the person by whom it is conferred, so long as he retains those powers.

(7) If by reason of any donation, settlement or other disposition made, whether before or after the commencement of this Act, by any person (hereinafter referred to as the donor)—

- (a) the donor's right to receive or have paid to him or for his benefit any amount by way of rent, dividend, foreign dividend, interest, royalty or similar income in respect of any movable or immovable property (including without limiting the foregoing any lease, company share, marketable security, deposit, loan, copyright, design or trade mark) or in respect of the use of, or the granting of permission to use, such property, is ceded or otherwise made over to any other person or to a third party for that other person's benefit in such manner that the donor remains the owner of or retains an interest in the said property or if the said property or interest is transferred, delivered or made over to the said other person or to a third party for the said other person's benefit, in such manner that the donor is or will at a fixed or determinable time be entitled to regain ownership of or the interest in the said property; or
- (b) the donor's right to receive or have paid to him or for his benefit any income that is or may become due to him by any other person acting in a fiduciary capacity is ceded or otherwise made over to any other person or to a third party for that other person's benefit in such manner that the donor is or will at a determinable time be entitled to regain the said right,

any such rent, dividend, foreign dividend, interest, royalty or income (including any amount which, but for this subsection, would have been exempt from tax in the hands of the said other person) as is received by or accrues to or for the benefit of the said other person on or after 1 July 1983 and which would otherwise, but for the said donation, settlement or other disposition, have been received by or have accrued to or for the benefit of the donor, shall be deemed to have been received by or to have accrued to the donor.

(8)(a) Where by reason of or in consequence of any donation, settlement or other disposition (other than a donation, settlement or other disposition to an entity which is not a resident and which is similar to a public benefit organisation contemplated in section 30) made by any resident, any amount is received by or accrued to any person who is not a resident (other than a controlled foreign company in relation to such resident), which would have constituted income had that person been a resident, there shall be included in the income of that resident so much of that amount as is attributable to that donation, settlement or other disposition.

(aA) In determining, for purposes of paragraph (a), whether an amount received by or that accrued to a person who is not a resident would have constituted income had that person been a resident, the provisions of section 10B(2)(a) must be disregarded in respect of a receipt or accrual consisting of or derived, directly or indirectly, from a foreign dividend—

- (i) paid or payable by a company if—
  - (aa) more than 50 per cent of the total participation rights, as defined in section 9D(1), or of the voting rights in that company are directly or indirectly held or are exercisable, as the case may be, by that person whether alone or together with any one or more persons that are connected persons in relation to that person; and
  - (bb) the resident who made the donation, settlement or other disposition or any person that is a connected person in relation to that resident is a connected person in relation to the person who is not a resident; and
- (ii) to the extent to which that foreign dividend is not derived from an amount that must be included in the income of or that must be attributed as a capital gain to—
  - (aa) the resident who made that donation, settlement or other disposition; or
  - (bb) a resident who is a connected person in relation to the resident referred to in item (aa).

(b) So much of any expenditure, allowance or loss incurred by the person contemplated in paragraph (a) as does not exceed the amount included in the income of the resident in terms of that paragraph and which would be allowable as a deduction under this Act in the determination of the taxable income derived from that amount had that person been a resident, is deemed to be an expenditure, allowance or loss incurred by that resident for purposes of the determination of the taxable income of that resident from that amount.

### **Section 9(2)(b), (j) and (k)**

(2) An amount is received by or accrues to a person from a source within the Republic if that amount—

- (b) constitutes interest as defined in section 24J where that interest—
  - (i) is attributable to an amount incurred by a person that is a resident, unless the interest is attributable to a permanent establishment which is situated outside the Republic; or
  - (ii) is received or accrues in respect of the utilisation or application in the Republic by any person of any funds or credit obtained in terms of any form of interest-bearing arrangement;
- (j) constitutes an amount received or accrued in respect of the disposal of an asset that constitutes immovable property held by that person or any interest or right of whatever nature of that person to or in immovable property contemplated in paragraph 2 of the Eighth Schedule and that property is situated in the Republic;

- (k) constitutes an amount received or accrued in respect of the disposal of an asset other than an asset contemplated in paragraph (j) if—
- (i) that person is a resident and—
    - (aa) that asset is not effectively connected with a permanent establishment of that person which is situated outside the Republic; and
    - (bb) the proceeds from the disposal of that asset are not subject to any taxes on income payable to any sphere of government of any country other than the Republic; or
  - (ii) that person is not a resident and that asset is effectively connected with a permanent establishment of that person which is situated in the Republic; or

#### Section 9(4)(d)

- (4) An amount is received by or accrues to a person from a source outside the Republic if that amount—
- (d) constitutes an amount received or accrued to that person in respect of the disposal of an asset that is not from a source within the Republic in terms of subsection (2)(j) or (k); or

#### Section 9D(2) before proviso's

- (2) There shall be included in the income for the year of assessment of any resident (other than a resident that is a headquarter company) who directly or indirectly holds any participation rights in a controlled foreign company—
- (a) on the last day of the foreign tax year of that controlled foreign company which ends during that year of assessment, an amount equal to—
    - (i) where that foreign company was a controlled foreign company for the entire foreign tax year, the proportional amount of the net income of that controlled foreign company determined for that foreign tax year, which bears to the total net income of that company during that foreign tax year, the same ratio as the percentage of the participation rights of that resident in relation to that company bears to the total participation rights in relation to that company on that last day; or
    - (ii) where that foreign company became a controlled foreign company at any stage during that foreign tax year, at the option of the resident, either—
      - (aa) an amount which bears to the proportional amount determined in accordance with subparagraph (i), the same ratio as the number of days during that foreign tax year that the foreign company was a controlled foreign company bears to the total number of days in that foreign tax year; or
      - (bb) the proportional amount determined in the manner contemplated in subparagraph (i) (as if the day that foreign company commenced to be a controlled foreign company was the first day of its foreign tax year), of the net income of that company for the period commencing on the day that the foreign company commenced to be a controlled foreign company and ending on the last day of that foreign tax year; or
  - (b) immediately before that foreign company ceased to be a controlled foreign company at any stage during that year of assessment before the last day of the foreign tax year of that controlled foreign company, an amount which shall be equal to, at the option of the resident, either—
    - (i) an amount determined in accordance with paragraph (a)(ii)(aa); or
    - (ii) the proportional amount determined in the manner contemplated in paragraph (a)(i) of the net income of that company determined for the period commencing on the first day of that foreign tax year and ending on the day before the company so ceased to be a controlled foreign company:

**Section 9D(2A) before proviso's**

(2A) For the purposes of this section the “**net income**” of a controlled foreign company in respect of a foreign tax year is an amount equal to the taxable income of that company determined in accordance with the provisions of this Act as if that controlled foreign company had been a taxpayer, and as if that company had been a resident for purposes of the definition of “gross income”, sections 7(8), 10(1)(h), 25B and paragraphs 2(1)(a), 24, 70, 71, 72 and 80 of the Eighth Schedule:

**Section 9D(9)(b)**

(9) Subject to subsection (9A), in determining the net income of a controlled foreign company in terms of subsection (2A), there must not be taken into account any amount which—

- (b) is attributable to any foreign business establishment of that controlled foreign company (whether or not as a result of the disposal or deemed disposal of any assets forming part of that foreign business establishment) and, in determining that amount and whether that amount is attributable to a foreign business establishment—
  - (i) that foreign business establishment must be treated as if that foreign business establishment were a distinct and separate enterprise engaged in the same or similar activities under the same or similar conditions and dealing wholly independently with the controlled foreign company of which the foreign business establishment is a foreign business establishment; and
  - (ii) that determination must be made as if the amount arose in the context of a transaction, operation, scheme, agreement or understanding that was entered into on the terms and conditions that would have existed had the parties to that transaction, operation, scheme, agreement or understanding been independent persons dealing at arm's length;

**Section 9D(9A)(a)(i)(aa)**

(9A)(a) Any amount which is attributable to a foreign business establishment of a controlled foreign company as contemplated in subsection (9)(b) must, notwithstanding that subsection, be taken into account in determining the net income of that controlled foreign company if that amount—

- (i) is derived from the sale of goods by that controlled foreign company directly or indirectly to any connected person (in relation to that controlled foreign company) who is a resident, unless—
  - (aa) that controlled foreign company purchased those goods for delivery in the country of residence of that controlled foreign company from any person who is not a connected person in relation to that controlled foreign company;

**Section 11(a)**

**11. General deductions allowed in determination of taxable income.**—For the purpose of determining the taxable income derived by any person from carrying on any trade, there shall be allowed as deductions from the income of such person so derived—

- (a) expenditure and losses actually incurred in the production of the income, provided such expenditure and losses are not of a capital nature;

**Section 23(d) and (g)**

**23. Deductions not allowed in determination of taxable income.**—No deductions shall in any case be made in respect of the following matters, namely—

- (d) any tax imposed under this Act or interest or penalty imposed under any other Act administered by the Commissioner;
- (g) any moneys, claimed as a deduction from income derived from trade, to the extent to which such moneys were not laid out or expended for the purposes of trade;

**Section 72A**

**72A. Return relating to controlled foreign company.**—(1) Every resident who on the last day of the foreign tax year of a controlled foreign company or immediately before a foreign company ceases to be a controlled foreign company directly or indirectly, together with any connected person in relation to that resident, holds at least 10 per cent of the participation rights in any controlled foreign company (otherwise than indirectly through a company which is a resident), must submit to the Commissioner a return.

(2) A resident must have available for submission to the Commissioner when so requested, a copy of the financial statements of the controlled foreign company for the relevant foreign tax year of that controlled foreign company.

(3) Where a person in respect of any year of assessment fails to comply with the provisions of—

- (a) . . . . .
- (b) subsection (2) and no reasonable grounds exist either for that failure which is outside the control of the person or for that person to believe that such person was not subject to that requirement—
  - (i) the proportional amount which must be included in the income of that person in terms of section 9D for that year shall be determined with reference only to the receipts and accruals of the controlled foreign company; and
  - (ii) the provisions of section 6*quat* shall not apply in respect of any tax proved to be payable to the government of any other country with respect to the proportional amount of the net income of that controlled foreign company which is included in the income of that person in terms of section 9D.

**Eighth Schedule – Paragraphs 68 to 72**

**68. Attribution of capital gain to spouse.**—(1) Where a person's capital gain or a capital gain that has vested in or is treated as having vested in that person during the year of assessment in which it arose can be attributed wholly or partly to—

- (a) any donation, settlement or other disposition; or
- (b) any transaction, operation or scheme,

made, entered into or carried out by that person's spouse mainly for purposes of reducing, postponing or avoiding that spouse's liability for any tax, duty or levy which would otherwise have become payable under any Act administered by the Commissioner, so much of the gain as can be so attributed must be disregarded when determining that person's aggregate capital gain or aggregate capital loss and taken into account when determining the aggregate capital gain or aggregate capital loss of that person's spouse.

(2) Where a person's capital gain is derived from—

- (a) any trade carried on by that person in partnership or association with that person's spouse or which is in any way connected with any trade carried on by that spouse; or
- (b) that person's spouse or any partnership or private company at a time when that spouse was a member of that partnership or the sole, main or one of the principal holders of shares in that company,



so much of that gain as exceeds the amount to which that person would reasonably be entitled having regard to the nature of the relevant trade, the extent of that person's participation therein, the services rendered by that person or any other relevant factor, must be disregarded when determining that person's aggregate capital gain or aggregate capital loss and taken into account when determining the aggregate capital gain or aggregate capital loss of that person's spouse.

**69. Attribution of capital gain to parent of minor child.**—Where a minor child's capital gain or a capital gain that has vested in or is treated as having vested in or that has been used for the benefit of that child during the year of assessment in which it arose can be attributed wholly or partly to any donation, settlement or other disposition—

- (a) made by a parent of that child; or
- (b) made by another person in return for any donation, settlement or other disposition or some other consideration made or given by a parent of that child in favour directly or indirectly of that person or his or her family,

so much of that gain as can be so attributed must be disregarded when determining that child's aggregate capital gain or aggregate capital loss and must be taken into account in determining the aggregate capital gain or aggregate capital loss of that parent.

**70. Attribution of capital gain subject to conditional vesting.**—Where—

- (a) a person has made a donation, settlement or other disposition that is subject to a stipulation or condition imposed by that person or anyone else in terms of which a capital gain or a portion of any capital gain attributable to that donation, settlement or other disposition shall not vest in the beneficiaries of that donation, settlement or other disposition or some of those beneficiaries until the happening of some fixed or contingent event;
- (b) a capital gain that is attributable to that donation, settlement or other disposition has arisen during a year of assessment throughout which the person who made that donation, settlement or other disposition has been a resident; and
- (c) that capital gain or a portion thereof has not vested during that year in any beneficiary who is a resident,

that capital gain or that portion thereof must be taken into account in determining the aggregate capital gain or aggregate capital loss of the person who made that donation, settlement or other disposition and disregarded when determining the aggregate capital gain or aggregate capital loss of any other person.

**71. Attribution of capital gain subject to revocable vesting.**—Where—

- (a) a deed of donation, settlement or other disposition confers a right upon a beneficiary thereof who is a resident to receive a capital gain attributable to that donation, settlement or other disposition or any portion of that gain;
- (b) that right may be revoked or conferred upon another by the person who conferred it; and
- (c) a capital gain attributable to that donation, settlement or other disposition or a portion of that gain has in terms of that right vested in that beneficiary during a year of assessment throughout which the person who conferred that right has been a resident and has retained the power to revoke that right,

that capital gain or that portion thereof must be disregarded when determining the aggregate capital gain or aggregate capital loss of that beneficiary and be taken into account when determining the aggregate capital gain or aggregate capital loss of the person retaining the power of revocation.

**72. Attribution of capital gain and other amounts vesting in person that is not a resident—**

(1) This paragraph applies where—

- (a) a resident has made a donation, settlement or other disposition to any person (other than an entity which is not resident and which is similar to a public benefit organisation contemplated in section 30);
- (b) a capital gain (including any amount that would have constituted a capital gain had that person been a resident) attributable to that donation, settlement or other disposition has arisen during a year of assessment; and
- (c) an amount consisting of or derived, directly or indirectly, from—
  - (i) that capital gain; or
  - (ii) the amount that would have constituted a capital gain,
 has during that year vested in or is treated as having vested in any person who is not a resident (other than a controlled foreign company, in relation to that resident).

(2) In determining, for purposes of subparagraph (1), whether an amount would have constituted a capital gain had a person been a resident, the provisions of paragraph 64B(1) and (4) must be disregarded in respect of an amount derived by that person, directly or indirectly, from the disposal of an equity share in a foreign company if—

- (a) more than 50 per cent of the total participation rights, as defined in section 9D(1), or of the voting rights in that company are directly or indirectly held or are exercisable, as the case may be, by that person whether alone or together with any one or more persons that are connected persons in relation to that person; and
- (b) the resident who made the donation, settlement or other disposition or any person that is a connected person in relation to that resident is a connected person in relation to the person who is not a resident; and
- (c) to the extent to which that amount is not included in the income of or attributed as a capital gain to—
  - (i) the resident who made that donation, settlement or other disposition; or
  - (ii) a resident who is a connected person in relation to the resident referred to in subitem (i).

(3) An amount that is equal to so much of the amount described in item (c) of subparagraph (1) that has vested in or is treated as having vested in the person who is not a resident as consists of or is derived, directly or indirectly, from—

- (a) the capital gain must be disregarded when determining the aggregate capital gain or aggregate capital loss of that person; and
- (b) the capital gain or the amount that would have constituted a capital gain must be taken into account as a capital gain when determining the aggregate capital gain or aggregate capital loss of the resident who made the donation, settlement or other disposition described in subparagraph (1).

**Eighth Schedule – Paragraph 80**

**80. Capital gain attributed to beneficiary.**—(1) Subject to paragraphs 68, 69 and 71, where a trust vests an asset in a beneficiary of that trust (other than any person contemplated in paragraph 62(a) to (e) or a person who acquires that asset as an equity instrument as contemplated in section 8C(1)) who is a resident, and determines a capital gain in respect of that disposal or, if that trust is not a resident, would have determined a capital gain in respect of that disposal had it been a resident—

- (a) that capital gain must be disregarded for the purpose of calculating the aggregate capital gain or aggregate capital loss of the trust; and
- (b) that capital gain or the amount that would have been determined as a capital gain must be taken into account as a capital gain for the purpose of calculating the aggregate capital gain or aggregate capital loss of the beneficiary to whom that asset was so disposed of.

(2) Subject to paragraphs 64E, 68, 69 and 71, where a trust determines a capital gain in respect of the disposal of an asset in a year of assessment during which a beneficiary of that trust (other than any person contemplated in paragraph 62(a) to (e)) who is a resident has a vested right or acquires a vested right (including a right created by the exercise of a discretion) to an amount derived from that capital gain but not to the asset disposed of, an amount that is equal to so much of the amount to which that beneficiary of that trust is entitled in terms of that right—

- (a) must be disregarded for the purpose of calculating the aggregate capital gain or aggregate capital loss of the trust; and
- (b) must be taken into account as a capital gain for the purpose of calculating the aggregate capital gain or aggregate capital loss of that beneficiary.

(2A)(a) Subject to paragraphs 64E, 68, 69 and 71, this subparagraph applies where—

- (i) a beneficiary who is a resident (other than any person contemplated in paragraph 62(a) to (e)) derives an amount through vesting during a year of assessment from a trust that is not a resident; and
  - (ii) that amount was derived directly or indirectly from that trust or another trust which is not a resident in respect of the disposal of an asset during the same year of assessment and that amount would have constituted a capital gain had the trust that disposed of the asset been a resident.
- (b) Where item (a) applies, the amount derived by the beneficiary must be taken into account as a capital gain for the purpose of calculating that beneficiary's aggregate capital gain or aggregate capital loss for that year of assessment.

(3) Where during any year of assessment any resident acquires a vested right to any amount representing capital of any trust which is not a resident, and—

- (a) that capital consists of or is derived, directly or indirectly, from an amount—
  - (i) determined as a capital gain of that trust; or
  - (ii) which would have been determined as a capital gain of that trust had that trust been a resident,
 in any previous year of assessment during which that resident had a contingent right to that capital; and
- (b) that capital gain or the amount that would have been determined as a capital gain has not been subject to tax in the Republic in terms of the provisions of this Act,

that amount must be taken into account as a capital gain when determining the aggregate capital gain or aggregate capital loss of that resident in respect of the year of assessment in which that resident acquired that vested right.

(4) In determining, for purposes of subparagraph (1), (2) or (3), whether an amount would have constituted a capital gain had the trust been a resident, the provisions of paragraph 64B(1) and (4) must be disregarded in respect of an amount derived by that trust, directly or indirectly, from the disposal or in respect of an equity share in a foreign company if—

- (a) more than 50 per cent of the total participation rights, as defined in section 9D(1), or of the voting rights in that company are directly or indirectly held or are exercisable, as the case may be, by that trust whether alone or together with any one or more persons that are connected persons in relation to that trust; and
- (b) to the extent to which that amount is not derived from an amount that must be included in the income of or attributed to—
  - (i) the resident to whom an amount is attributed in terms of subparagraph (1), (2) or (3); or
  - (ii) a resident who is a connected person in relation to the resident referred to in subitem (i).