

INTERPRETATION NOTE 115 (Issue 2)

DATE: 30 June 2023

ACT : INCOME TAX ACT 58 OF 1962
SECTION : SECTIONS 50A to 50H
SUBJECT : WITHHOLDING TAX ON INTEREST

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Preamble

In this Note unless the context indicates otherwise –

- “**Companies Act**” means the Companies Act 71 of 2008;
- “**Financial Markets Act**” means the Financial Markets Act 19 of 2012;
- “**JSE**” means the exchange operated by JSE Ltd which facilitates trade in securities under the style of “Johannesburg Stock Exchange” and is licensed as an exchange under the Financial Markets Act;
- “**Schedule**” means a Schedule to the Act;
- “**section**” means a section of the Act;
- “**TA Act**” means the Tax Administration Act 28 of 2011;

- “**tax treaty**” means an agreement for the avoidance of double taxation entered into between South Africa and another country;¹
- “**the Act**” means the Income Tax Act 58 of 1962; and
- any other word or expression bears the meaning ascribed to it in the Act.

All interpretation notes referred to in this Note are available on the SARS website at www.sars.gov.za. Unless indicated otherwise, the latest issues of these documents should be consulted.

1. Purpose

This Note deals with the interpretation and application of sections 50A to 50H relating to withholding tax on interest.

The information in this Note is based on the income tax and tax administration legislation (as amended) as at the time of publishing and includes the following:

- The Taxation Laws Amendment Act 20 of 2022 which was promulgated on 5 January 2023 (as per *Government Gazette* 47826).
- The Tax Administration Laws Amendment Act 16 of 2022 which was promulgated on 5 January 2023 (as per *Government Gazette* 47827).
- The Rates and Monetary Amounts and Amendment of Revenue Laws Act 19 of 2022 which was promulgated on 5 January 2022 (as per *Government Gazette* 47825).

2. Background

South African residents sometimes engage in cross-border transactions either for a trade or a non-trade purpose. Some of these transactions are entered into for the purpose of raising foreign debt capital. The debt capital often incurs an interest charge with the result that repayments comprise both a return of the borrowed capital and the interest incurred. The interest incurred may result in a deduction for the resident taxpayer (if legislative requirements are met) while the corresponding interest income may be exempt from tax for the recipient by virtue of section 10(1)(h). This situation results in the erosion of the domestic tax base. In order to address this loss of income to the *fiscus*, a withholding tax on interest paid to or for the benefit of a foreign person was introduced under sections 50A to 50H with effect from 1 March 2015.

The Explanatory Memorandum on the Taxation Laws Amendment Bill, 2010 explains the rationale for introducing withholding tax on interest as follows:

“[T]he current blanket interest exemption does not achieve a fair balance between the attraction of foreign debt capital and the need to protect the tax base against potential erosion. The exemption is also not in line with global practice.

Most developed and emerging economies currently exempt cross-border interest relating to mobile portfolio debt (and possibly incidental trade finance). Other forms of cross-border debt remain fully taxable (and subject to a flat rate form of withholding).

¹ 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.

More generous forms of exemption typically exist only through tax treaties where both countries believe that the cross border interest will remain subject to a relatively high level of global tax. Hence the current blanket exemption employed via domestic South African tax legislation appears to be overly generous from a competitive point of view.”

A prerequisite for the imposition of withholding tax on interest is that the interest must be from a South African source. The withholding tax on interest is a final tax currently levied at a rate of 15%, which may be reduced by the application of a tax treaty or limited to nil in specified circumstances for interest paid by oil and gas companies. In addition to a legislative amendment to the rate of withholding tax on interest, the Minister may announce a new rate of withholding tax on interest in the national annual budget which will be effective from the date mentioned as the effective date in the Minister’s announcement. The new rate will apply for a period of 12 months from the effective date as announced by the Minister pending the passing of legislation by Parliament giving effect to that announcement within that period.²

Interest payments fulfilling the requirements of section 50D or section 12Q(4) will be exempt from withholding tax on interest.

It is not a requirement that the interest must be incurred for a trade purpose or that it must be deductible by the payer before it may be subject to withholding tax on interest.

3. The law

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

4. Interpretation and application of the law

4.1 Definitions

4.1.1 “Bank”

The term “bank” for the purpose of withholding tax on interest means a bank or branch of a bank as defined in the Banks Act³, a mutual bank as defined in the Mutual Banks Act⁴ or a co-operative bank as defined in the Co-operative Banks Act.⁵

Section 1 of the Banks Act defines the terms “bank”, “branch” and “branch of a bank” as follows:

“**[B]ank**” means a public company registered as a bank in terms of this Act;

“**[B]ranch**” means an institution that is not a public company as contemplated in section 11(1), but by means of which a foreign institution conducts the business of a bank in the Republic under an authorization referred to in section 18A;

“**[B]ranch of a bank**” means an institution by means of which a bank conducts the business of a bank outside the Republic;

² Section 50B.

³ Act 94 of 1990.

⁴ Act 124 of 1993.

⁵ Act 40 of 2007.

Section 1 of the Mutual Banks Act defines a mutual bank as follows:

<p>“[M]utual bank” means a juristic person —</p> <p>(a) the members of which —</p> <p style="padding-left: 40px;">(i) qualify as such by virtue of their being shareholders in that juristic person; and</p> <p style="padding-left: 40px;">(ii) are entitled to participate in the exercise of control in a general meeting of that juristic person; and</p> <p>(b) that is registered as a mutual bank in terms of this Act;</p>

Section 1 of the Co-operative Banks Act defines a co-operative bank as follows:

<p>“[C]o-operative bank” means a cooperative or a co-operative financial institution registered as a co-operative bank in terms of this Act whose members—</p> <p>(a) are employed by a common employer or who are employed within the same business district; or</p> <p>(b) have common membership in an association or organisation, including a religious, social, co-operative, labour or educational group; or</p> <p>(c) reside within the same defined community or geographical area.</p>
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The definition of “bank” is relevant for the purposes of section 50D(1)(a)(i)(bb), which, amongst others, exempts from withholding tax on interest any interest paid by a “bank” as defined in section 50A(1) to any foreign person. Thus, interest paid by a local bank to a foreign person will be exempt from withholding tax on interest. Likewise, interest paid by a branch of a foreign bank operating in South Africa to a foreign person will be exempt from withholding tax on interest.

Subsidiary of a bank

The exemption relating to interest paid by the local branch of a foreign bank does not apply to a subsidiary of a bank, which is itself not a bank, because subsidiaries are defined differently from branches and the exemption is restricted to a bank or a branch of a bank as defined above. Section 1 of the Banks Act defines “subsidiary” to mean a subsidiary provided for in section 3 of the Companies Act. Section 3 of the Companies Act deals with subsidiary relationships.

4.1.2 “Foreign person”

Section 50A(1) defines a foreign person as “any person that is not a resident”. The term “resident” is defined in section 1(1) and contains separate requirements for natural and juristic persons. The term “person” includes a natural person, a deceased estate, an insolvent estate, a trust and a company but excludes a foreign partnership.⁶

⁶ The full meaning of “person” has to be deduced from its ordinary dictionary meaning and from the inclusionary definitions of the term in section 1(1) and the Interpretation Act 33 of 1957.

A natural person is considered to be resident in South Africa when such person is –

- ordinarily resident⁷ in South Africa; or
- not at any time during the relevant year of assessment ordinarily resident in South Africa, if that person was physically present⁸ in South Africa –
 - for a period or periods exceeding 91 days in aggregate during the relevant year of assessment, as well as for a period or periods exceeding 91 days in aggregate during each of the five years of assessment preceding such year of assessment; and
 - for a period or periods exceeding 915 days in aggregate during those five preceding years of assessment; and
- a tax treaty does not deem that person to be exclusively a resident of another country for purposes of the application of any tax treaty.

A juristic person is considered to be resident in South Africa, when it is –

- incorporated, established or formed in South Africa; or
- has its place of effective management⁹ in South Africa; and
- a tax treaty does not deem that person to be exclusively a resident of another country for purposes of the application of any tax treaty.

4.1.3 “Interest”

With effect from 1 March 2016, and applicable to interest paid or due and payable on or after that date, section 50A(1) defines “interest” to mean interest as contemplated in paragraph (a) or (b) of the definition of “interest” in section 24J(1) (see below and **Annexure**) but does not include interest that is deemed to be a dividend *in specie* under section 8F(2) or 8FA(2) (see **10.3**).¹⁰

Paragraph (a) and (b) of the definition of interest in section 24J(1) make reference to –

- the gross amount of any interest or similar finance charges, discount or premium payable or receivable in terms of or in respect of a financial arrangement; and
- an amount (or portion thereof) payable by a borrower to a lender under a lending arrangement, representing compensation for any amount to which the lender would have been entitled were it not for the lending arrangement.

It is not a requirement of the definition that the amount be calculated on a fixed or variable rate of interest, or that it be payable or receivable as a lump sum or in equal instalments during the term of the financial or lending arrangement.

⁷ See Interpretation Note 3 “Resident: Definition in Relation to a Natural Person – Ordinarily Resident”.

⁸ See Interpretation Note 4 “Resident: Definition in Relation to a Natural Person – Physical Presence Test”.

⁹ See Interpretation Note 6 “Resident: Place of Effective Management (Companies)”.

¹⁰ The specific exclusion in the definition applies to amounts paid on or after 1 January 2022. Prior to that date whether the amount was interest for the recipient depended on the wording of section 8F(2) and 8FA(2) at the time the interest accrued.

For the definition of “interest” in section 50A(1) to apply, there needs to be a lender and a borrower in relation to a financial or lending arrangement. A lender (the “holder” as defined in section 24J) is a person to whom interest accrues. A borrower (the “issuer” as defined in section 24J) is the person that incurs any interest on the financial or lending arrangement.

4.2 Levy of withholding tax on interest [sections 50B]

In order for an amount of interest to be subject to withholding tax on interest –

- there must be an amount;
- the amount must constitute interest (see **4.1.3**);
- which is paid by any person (see **4.3**);
- to or for the benefit of any foreign person (see **4.4**);
- to the extent that the amount is regarded as having been received or accrued from a source within South Africa under section 9(2)(b) (see **4.5**); and
- interest must have been paid or become due and payable on or after 1 March 2015¹¹ (see **4.3**).

These requirements and the computation of the amounts of withholding tax on interest are considered further below.

Withholding tax on interest is a final tax currently levied at a rate of 15%¹² of the amount meeting the requirements listed above. The rate of 15% may be altered by legislative amendment or the Minister may announce a new rate of withholding tax on interest in the national annual budget which is effective from the date included in the Minister’s announcement. In the latter case, the new rate will apply for a period of 12 months from the effective date as announced by the Minister pending the passing of legislation by Parliament giving effect to that announcement within that period.¹³

When a person withholds an amount of withholding tax on interest as contemplated in section 50E(1) (see **6.2**), that person is, for the purposes of withholding tax on interest, deemed to have paid the amount so withheld to or for the benefit of a foreign person. Withholding tax on interest is therefore levied on and withheld from the gross amount of the interest.¹⁴

¹¹ Part IVB of the Act came into operation on 1 March 2015 and applies in respect of interest that is paid or that becomes due and payable on or after that date – see section 98(2) of the Taxation Laws Amendment Act, 31 of 2013 and section 125 of the Taxation Laws Amendment Act, 43 of 2014.

¹² Subject to any reduction required by an applicable tax treaty or, if applicable, limited to nil for specified expenditure incurred by oil and gas companies.

¹³ Section 50B.

¹⁴ Section 50B(4).

Example 1 – Resident that withholds withholding tax on interest deemed to have paid that amount to the foreign person

Facts:

X, an individual who is a resident of Country C, advanced money on loan account to Company Y, a South African resident. The loan agreement entered into by X and Company Y stipulated that X was entitled to interest at 6% a year on the amount advanced of R300 000. The interest for one year became due and payable on 31 January 2023. Country C does not have a tax treaty with South Africa. X has not spent more than 183 days in South Africa in any 12 month period.

Company Y withheld withholding tax on interest of R2 700 $[(R300\ 000 \times 6\%) \times 15\%]$ from the interest payable to X under section 50E(1) and paid the net amount of the interest of R15 300 $[(R300\ 000 \times 6\%) - R2\ 700]$ to X.

Result:

Under section 50B(4) Company Y is deemed to have paid the withholding tax on interest withheld of R2 700 to X. Withholding tax on interest at the rate of 15% was withheld from the gross amount of the interest.

The total amount of interest that Company Y may deduct under section 24J if all the requirements of that section are met is R18 000 $(R300\ 000 \times 6\%)$.

X has gross income of R18 000, since under section 9(2)(b) the source of the interest income is South Africa. The interest income is, however, exempt from normal tax under section 10(1)(h).

Example 2 – Return payable at a rate net of withholding tax

Facts:

X, a resident, borrowed R100 000 from Y, a non-resident. The loan agreement required Y to receive a return of 10% after taking any withholding tax into account. There is no tax treaty in place between the country in which Y is resident and South Africa.

No exemptions from withholding tax on interest apply.

Result:

Y must receive R10 000 $(R100\ 000 \times 10\%)$ after withholding tax on interest which must be levied at 15%.

If the amount net of withholding tax on interest to be paid to Y is R10 000, the gross amount of the interest (x) is calculated as follows:

$$\begin{aligned} x - 0,15x &= R10\ 000 \\ 0,85x &= R10\ 000 \\ x &= R10\ 000 / 0,85 \\ x &= R11\ 764,71 \end{aligned}$$

The withholding tax on interest is calculated as follows:

	R
Gross interest	11 764,71
Withholding tax on interest R11 764,71 × 15%	<u>1 764,71</u>
Net amount payable to Y = R11 764,71 – R1 764,71 =	<u>10 000,00</u>

As noted in **2**, it is not a requirement that the interest must be incurred for a trade purpose or that it must be deductible before such interest is subject to withholding tax. If the requirements listed above are met, section 50B(1) will apply irrespective of the purpose of the debt and interest.

See **6.1** for “Liability for withholding tax on interest” and **6.2** for “Liability to withhold the tax”.

4.3 Paid by any person

Section 50B(2) provides that for the purposes of withholding tax on interest, interest is deemed to be paid on the earlier of –

- the date on which it is paid; or
- the date on which it becomes due and payable.

Part IVB of the Act came into operation on 1 March 2015 and applies in respect of interest that is paid or that becomes due and payable on or after that date.¹⁵ However, because section 50B(2) deems interest to have been paid on the earlier of the date of payment and the date on which it becomes due and payable, it means that Part IVB will apply only if the interest is both paid and due and payable on or after 1 March 2015.

4.3.1 Paid

An amount can be paid in a variety of ways, including in cash, in kind, in the form of set-off or by agreeing that the amount may be retained as a loan.¹⁶ There is generally little difficulty in determining the date of payment when expenditure is paid in cash, which in practice is often the case with interest payments. However, the date of payment can be more difficult to establish when payment is in a form other than cash and in these instances the importance of the facts of the particular case should not be lost sight of. ITC 1688¹⁷ sets out some useful principles for determining the date of payment when payment is in the form of set-off, cheque¹⁸ or by way of a loan.

In that case the appellant company declared two dividends to the sole holder of its shares on 2 March 1992 and 5 March 1993, respectively. Payment of these dividends was not made in cash or by cheque. Rather, the resolutions declaring the dividends provided that payment of the dividends would be effected by crediting the holder’s loan account. Journal entries were duly effected giving credit to the holder of the shares,

¹⁵ Section 98(2) of the Taxation Laws Amendment Act, 31 of 2013 and section 125 of the Taxation Laws Amendment Act, 43 of 2014.

¹⁶ See the commentary on ITC 1688 (1999) 62 SATC 478 (N) below. Although that case relates to whether a dividend was “paid” for purposes of secondary tax on companies (since repealed), the principles regarding payment apply when considering when interest will be considered “paid” for purposes of withholding tax on interest.

¹⁷ (1999) 62 SATC 478 (N).

¹⁸ With effect from 1 January 2021 cheques are no longer an acceptable form of payment or bill of exchange in South Africa.

but the holder's loan account was credited only on 31 July 1993. At issue was whether the dividends were subject to STC which came into operation on 17 March 1993. The relevant legislation provided that dividends declared before 17 March 1993 that were paid on or after that date, were deemed to be declared on 17 March 1993, thus making them potentially subject to STC. The crisp issue was whether the dividends were paid before 17 March 1993.

In delivering his judgment Galgut J stated the following about the nature of payments generally:¹⁹

"The determination of the date upon which a payment is made is of course a question of fact. When payment of a dividend is made in cash there can of course be no difficulty in determining the date of such payment. The same applies to a payment by cheque, even if the cheque is post-dated or dishonoured, because payment will be effected when the proceeds of the cheque are received by or on behalf of the payee.

Payment can of course be made other than in cash or by cheque. There are a number of possibilities. To take but one, it might happen for example that a shareholder owes his company money, and that the company thereafter becomes indebted to the shareholder by the declaration of a dividend. In such a case the company may elect to effect a set-off, provided of course all of the other requisites for a set-off are present. One such requisite is that both debts must be fully due. In such a case the shareholder would have no choice because, as was said in *Lester Investments (Pty) Ltd v Narshi* 1951 (2) SA 464 (C) at 472B-C, set-off operates *ipso jure*,²⁰ and it is effective from the date upon which the parties became mutually indebted to each other. It would therefore operate without the shareholder's consent, and what is more it would operate immediately upon the declaration of the dividend. If the debt owing by the shareholder is recorded in a loan account with the company, then the set-off will be recorded by crediting the taxpayer's loan account in the amount concerned.

It is important to emphasise, however, that such crediting is no more than a recording of a pre-existing fact, so that the operation of the set-off will not depend upon the crediting of the loan account.

As distinct from the operation of a set-off, or from the tender of cash or (subject to certain qualifications which are not relevant for present purposes) a cheque, all other forms of payment can only discharge a debt if the creditor agrees thereto. One such agreement is where the creditor agrees, as in the present case, to lend the money concerned to the debtor, where he agrees in other words that the debtor may retain the money as a loan. In such an event, as in the case of a set-off, both the payment of the dividend and the advancing of the loan in each instance take place automatically, and as such they are effected *pari passu* with the conclusion of the agreement. As such, and this must be emphasised, payment is in each case effected on the date upon which the agreement is concluded. It would of course be otherwise were the resolution whereby the dividend is declared to contain a term showing that the dividend is to be paid at some date thereafter, or were the agreement of loan to contain a term showing that the loan would similarly be delayed. In the absence of such an indication, in the absence in other words of anything to show that the parties intended otherwise, it would be fair to conclude that both the payment of the dividend and the reciprocal advancing of the loan occurred, and were intended to occur, then and there."

In summary, the court held that payments in a form other than cash, cheque²¹ or set-off can discharge a debt only with the creditors consent. Based on the facts of the case the court found that this took place when the respective resolutions were passed and

¹⁹ At 481.

²⁰ By operation of law.

²¹ Subject to certain qualifications not relevant to the decision.

not when the physical crediting of the loan account took place and accordingly found in favour of the appellant.

In concluding the court stated the following:²²

“I should emphasise finally that nothing I have said should be understood to mean that where declared dividends are left on loan in a company, it will be presumed or will necessarily mean that payment takes place at the time the dividend is declared. At the risk of repeating myself I stress that the date of payment is a question of fact, and that as such the date must be determined on the particular facts of each case.”

The judge’s concluding comments highlight that the outcome of ITC 1688 may have been different had the resolution contained a term indicating that payment would be made at a later date. This case emphasised the importance of the facts of the particular case in determining when an amount is considered to be paid and highlighted that the crediting of a loan account will not always necessarily constitute payment.

Similarly, interest may have accrued to a recipient and be payable as opposed to paid. Payment by way of agreeing to retain the amount as a loan must be distinguished from an accrual. The former means the amount will have been paid and therefore withholding tax will be triggered, while a mere accrual which is not a payment will not trigger withholding tax on interest. The *Explanatory Memorandum on the Taxation Laws Amendment Bill, 2012*²³ in explaining the rationalisation of withholding taxes on payments to foreign persons and the changes to withholding tax on interest stated the following:

“[A] mere accrual will no longer be the basis for withholding. In line with the new Dividends Tax, the trigger date for withholding will now be the date that a sum is paid or becomes due and payable.”

Example 3 – Determination of when interest is considered “paid” for purposes of withholding tax on interest

Facts:

P, a resident of Country K, advanced funds on loan account to Company F, a South African resident, on 1 January 2022. Company F’s year of assessment ends on 31 December 2022. According to the loan agreement entered into by P and Company F, P is entitled to interest of 9% a year on the outstanding loan balance of R600 000. Under the loan agreement interest which accrues between 1 January and 31 December each year is due and payable 4 months after the calendar year end. Therefore, the interest which accrued for the year ending 31 December 2022 was due and payable on 30 April 2023. However, Company F decided to pay the interest on 31 March 2023.

There is no tax treaty between Country K and South Africa.

²² At 482.

²³ This section of the *Explanatory Memorandum* related, amongst others, to the insertion of a new Part IA of the Act dealing with withholding tax on interest. Although this insertion was repealed before it became effective, many of the comments in the *Explanatory Memorandum* remain relevant because the same wording was used in a number of the subsections when introducing the replacement Part IVB into the Act. In particular, the wording of the now repealed section 37J(2) in the Taxation Laws Amendment Act, 22 of 2012 is exactly the same as section 50B(2).

Result:

Section 50B(1)(a) requires withholding tax on interest to be levied on interest paid to or for the benefit of a foreign person. Interest is deemed to be paid for the purpose of withholding tax on interest on the earlier of the date on which it is actually paid or becomes due and payable. Accordingly, withholding tax must be levied and withheld from the payment of interest made on 31 March 2023, since the actual date of payment is earlier than the date on which interest is due and payable.

The accrual of the interest under the contract and under section 24J during the 2021 year of assessment does not comprise payment based on the facts of this case and therefore does not trigger withholding tax during or at the end of the 2021 year of assessment.

Example 4 – Interest accrued converted to a loan*Facts:*

K, a resident of Country M, provided a short-term loan to Company V on 1 July 2022. Company V's year of assessment ends on 31 December 2022. According to the loan agreement entered into by K and Company V, K is entitled to interest of 10% a year on the outstanding loan balance of R500 000. Under the loan agreement interest accrues monthly and is due and payable 2 months after the end of Company V's year of assessment. Therefore, the interest which accrued for the year ending 31 December 2022 was due and payable on 28 February 2023. However, on 31 January 2023, K and Company V agree that Company V would retain the money underlying the interest accrual for 1 July 2022 to 31 December 2022 as a loan and converted it to an additional loan (additional to the initial R500 000 loan) on that date.

There is no tax treaty between Country M and South Africa.

Result:

Section 50B(1)(a) requires withholding tax on interest to be levied on interest paid to or for the benefit of a foreign person. Interest is deemed to be paid for the purpose of withholding tax on interest on the earlier of the date on which it is actually paid or becomes due and payable. The interest for the 6 months was due and payable on 28 February 2023, however, the conversion of the interest accrual to a loan on 31 January 2023 constituted payment. As withholding tax must be withheld on the earlier of the date when the interest is paid or becomes due and payable Company V must withhold the withholding tax at the rate of 15% on 31 January 2023 when the interest accrual for the period 1 July 2022 to 31 December 2022 was converted to a loan. The withholding tax withheld must be paid to SARS on or before 28 February 2023.

Note:

- 1) If instead of converting the interest accrual to a loan account, Company V converted it to share capital and issued K with shares in the Company, the answer would be the same. The conversion to share capital constitutes payment in kind and therefore triggers withholding tax on interest.

2) For completeness, although not related to withholding tax on interest, it noted the Company V would need to consider if there are debt reduction consequences on the conversion of the interest accrual under section 19 and paragraph 12A of the Eight Schedule.

4.3.2 Due and Payable

The words “due” and “payable” are not defined in either section 50A or the Act. These words were considered in various judgments. In *CIR v Janke*²⁴ Stratford J quoted²⁵ the judgment of Searle J in *Stafford v Registrar of Deeds*:²⁶

“It is clear that the word ‘payable’ is sometimes construed as meaning ‘payable at a future time’ or ‘in respect of which there is a liability to pay’. It is also true that it is sometimes used to mean ‘payable immediately’ or ‘actually due and presently demandable’.”

In *Singh v C: SARS*, Olivier JA stated the following:²⁷

“The word ‘payable’ can have at least two different meanings, viz ‘. . . (a) that which is due or must be paid, or (b) that which may be paid or may have to be paid . . . The sense of (a) is a present liability – due and payable – . . . (b) . . . a future or contingent liability’.”

Accordingly, an amount may be due under a contract (*dies cedit*) but not payable (*dies venit*). An amount will be payable only when the time for payment arrives. For an amount to be “due and payable” the amount must not only be owed but the recipient must have the right to claim payment of it.²⁸

Example 5 – Determination of when interest is considered due and payable for purposes of withholding tax on interest

Facts:

P, a resident of Country K, advanced R600 000 on loan account to Company F, a South African resident. According to the loan agreement entered into by P and Company F, P is entitled to interest of 9% a year on the cumulative balance which includes the loan and original capitalised interest. Interest is determined on a monthly basis and capitalised against the loan account. The interest for the period is payable only on 30 April 2023. There is no tax treaty between the country in which P resides and South Africa.

Result:

Section 50B(1)(a) requires withholding tax on interest to be levied on interest paid to or for the benefit of a foreign person. Interest is deemed to be paid for the purpose of withholding tax on interest on the earlier of the date on which it is actually paid or becomes due and payable.

²⁴ 1930 AD 474, 4 SATC 269.

²⁵ 1930 AD 474, 4 SATC 269 at 276.

²⁶ 1913 CPD 329.

²⁷ 2003 (4) SA 520 (SCA), 65 SATC 203 at 216.

²⁸ L Mitchell “Cash Consideration Only” (2005) 19 *Tax Planning* 84.

The interest due to P is capitalised against its loan account on a monthly basis. In this example the capitalisation of the interest on a monthly basis does not constitute payment for purposes of withholding tax on interest, since such amount is only due but not payable on a monthly basis. P and Company F have not agreed that Company F can retain the money underlying the accrued interest on loan account, it is simply not yet payable by Company F. Withholding tax on interest will be levied only when the interest becomes due and payable, that is, on 30 April 2023, unless it is paid earlier.

Note:

It is important to consider the meaning of “capitalise” in the context in which it is used when assessing whether the interest has been paid. In this example capitalise is simply used to indicate that interest is calculated on a compound basis and that interest is included in the cumulative balance on which interest is calculated. Although the interest has accrued it is not yet payable in terms of the loan agreement and the parties have not amended the agreement and agreed that the money underlying it may be retained by the Company F on loan account. “Capitalise” can, however, have a different meaning and indicate that payment has occurred. For example, it may be used to describe a situation in which the parties agreed that the amount underlying an interest accrual may be retained on loan account (instead of being settled on a previously agreed date) or it can be used to indicate another form of payment in kind such as through the issue of share capital – see Example 4.

Example 6 – Interest due and payable which is paid before 1 March 2015

Facts:

X, a resident of Country C, advanced money on loan account to Company Y, a South African resident. The loan agreement entered into by X and Company Y stipulated that X was entitled to interest at 6% a year on the amount advanced of R300 000. The interest became due and payable on 31 January 2015 and was paid on 12 February 2015. Country C does not have a tax treaty with South Africa.

Result:

The interest which accrued to X became due and payable on 31 January 2015 and is therefore deemed to have been paid on that date. The interest is not subject to withholding tax on interest, since it was paid before withholding tax on interest came into effect on 1 March 2015.

Example 7 – Interest due and payable before 1 March 2015 but paid after that date

Facts:

R, a resident of Country Z, advanced money on loan account to Company C, a South African resident. The loan agreement entered into by R and Company C stipulated that R was entitled to interest at the rate of 10% a year on the amount advanced of R400 000. The interest became due and payable on 25 February 2015 but was actually paid on 12 March 2015 after completion of the necessary administrative processes. Country Z does not have a tax treaty with South Africa.

Result:

The interest received by R became due and payable on 25 February 2015. Section 50B(2) deems interest to have been paid on the earlier of the date on which it is actually paid or becomes due and payable. Since the interest is deemed under section 50B(2) to have been paid before the implementation of withholding tax on interest on 1 March 2015, it is not subject to withholding tax on interest.

Example 8 – Interest due and payable for a quarter which includes a period before the effective date of withholding tax on interest

Facts:

Z, a resident of Country Z, advanced money on loan account to Company X, a South African resident. The loan agreement entered into by Z and Company X stipulated that Z was entitled to interest calculated at the rate of 9% a year on the amount advanced of R450 000. Interest was due and payable at the end of each quarter, with the first quarter comprising the months of February, March and April. Therefore, the interest for February, March and April became due and payable on 30 April 2015. As a result of cash-flow difficulties, Company X made payment of the interest only on 12 June 2015. Country Z does not have a tax treaty with South Africa.

Result:

Interest is deemed to have been paid on the earlier of the date on which it is paid or becomes due and payable. On 30 April 2015, Z acquired a personal right to demand payment of the interest. The interest was therefore deemed under section 50B(2) to have been paid on this date.

The next step is to determine the quantum of the interest that is subject to withholding tax on interest. Since the interest is payable only at the end of each quarter, Z will be entitled to the total interest for the first quarter only on 30 April 2015. This means that the interest for February is subject to withholding tax, since it became due and payable after the commencement of withholding tax legislation on 1 March 2015. The total interest payment is therefore subject to withholding tax on interest at 15%.

Example 9 – Interest becomes irrecoverable after the amount became due and payable

Facts:

V, a resident of Country V, provided a loan of R100 000 to S, a South African resident, on 1 August 2021. The loan was repayable in three annual instalments and incurs interest at 12% a year. The first repayment (inclusive of interest and capital) was due and payable on 31 July 2022. S had been experiencing financial difficulties and, after discussions with V during August 2022, the latter agreed to waive the interest due and payable. The capital amount of the debt remained due and payable.

There is no tax treaty between South Africa and Country V.

Result:

Section 50B(2) deems interest to have been paid to a foreign person for purposes of withholding tax on interest on the earlier of the date on which it is paid or becomes due and payable. S was required to withhold tax at the rate of 15% on the amount of interest that became due and payable to V on 31 July 2022 and to pay that amount to SARS by 31 August 2022 (see 7). The subsequent waiving of the interest by V in August 2022 does not affect V's liability to pay withholding tax on interest, since the debt was waived after the interest became due and payable and was deemed to be paid for purposes of withholding tax on interest. Section 50G(2) makes provision for a refund of withholding tax on interest that has been paid when the interest becomes irrecoverable (See 8.). S would be entitled to claim a refund under section 50G(2).

4.4 Meaning of “to or for the benefit of any foreign person”

The phrase “to or for the benefit of any foreign person” requires withholding tax on interest to be levied on interest paid to a foreign person beneficially entitled to it and interest paid to another person for the benefit of a foreign person. As a result, the interest need not be paid directly to the foreign person but can also be paid to, for example, the foreign person's nominee, representative or agent.

The withholding obligation (see 6.2) is placed on the payer of the interest, and not the person that receives it for their own benefit or, generally, that receives it on behalf of another.

The terms and conditions as contractually agreed between the payer and payee are one of the factors which are important in determining when and to whom the interest is payable.

If interest is paid to a trust there are a number of factors to consider in determining whether the payment is to or for the benefit of a foreign person, for example, whether the trust itself is resident in South Africa or a foreign person, the type of trust, whether the beneficiaries are resident in South Africa or elsewhere and whether the income is vested in beneficiaries.

For example, in the case of a vesting trust which confers a vested right to interest on a beneficiary, the payer must assess if that beneficiary is a foreign person and, if so, then the interest will be to or for the benefit of a foreign person (see Examples 10 and 11).

Example 10 – Interest paid to a vesting trust*Facts:*

ZB Trust, a South African registered and resident trust, has one beneficiary, D. D, a resident in Foreign Country NY, has a vested right to the trust's capital and income. ZB Trust provided a loan of R100 000 to S, a South African resident, on 1 August 2021. The loan was repayable in three annual instalments and incurs interest at 12% a year. The first repayment (inclusive of interest and capital) was due and payable and was paid on 31 July 2022.

There is no tax treaty between South Africa and Foreign Country NY.

Result:

Section 50B(1)(a) requires withholding tax on interest to be levied on interest paid to or for the benefit of a foreign person. Interest is deemed to be paid for the purpose of withholding tax on interest on the earlier of the date on which it is actually paid or becomes due and payable.

Under section 25B(1) if any amount, is received by or accrues to a trust and a beneficiary has a vested right to that amount during that year of assessment, such amount is deemed to accrue to that beneficiary and not that trust. Given that D has a vested right to the interest, ZB Trust is merely acting as a conduit and receiving the interest on behalf of D, who is a foreign person. Accordingly, S, as the person making the payment of interest, must withhold withholding tax on interest at 15% on the payment of interest on 31 July 2022 under section 50E(1) and pay it over to SARS under section 50F(2) by 31 August 2022.

Example 11 – Interest paid to a vesting trust*Facts:*

ZB Trust, a South African registered and resident trust, has two beneficiaries, A and D. A is resident in South Africa, D is resident in Foreign Country NY. A and D each have a vested right to 50% of the trust's capital and income. ZB Trust provided a loan of R100 000 to S, a South African resident, on 1 August 2021. The loan was repayable in three annual instalments and incurs interest at 12% a year. The first repayment (inclusive of interest and capital) was due and payable and was paid on 31 July 2022.

There is no tax treaty between South Africa and Foreign Country NY.

Result:

Section 50B(1)(a) requires withholding tax on interest to be levied on interest paid to or for the benefit of a foreign person. Interest is deemed to be paid for the purpose of withholding tax on interest on the earlier of the date on which it is actually paid or becomes due and payable.

Under section 25B(1) if any amount, is received by or accrues to a trust and a beneficiary has a vested right to that amount during that year of assessment, such amount is deemed to accrue to that beneficiary and not that trust. Given that A and D have a vested right to the interest, ZB Trust is merely acting as a conduit and receiving the interest on behalf of A and D. Accordingly, S, as the person making the payment of interest, must under section 50E(1), where applicable, withhold withholding tax on interest from the payment of interest made on 31 July 2022 and pay it over to SARS under section 50F(2) by 31 August 2022. S is only required to withhold withholding tax on interest at 15% on 50% of the interest which vests in D, a foreign person. No withholding is required on the 50% which vests in A because A is not a foreign person.

The position with discretionary trusts can practically be complicated as a result of the interaction between the withholding tax provisions and section 25B. This arises because sometimes when the payer pays the interest, or it becomes due and payable, it appears as if it is for the benefit of the trust. However, depending on whether and when the trustees exercise their discretion, this can change such that section 25B deems the amount to have accrued to the beneficiary and therefore it is for the beneficiary's benefit and not the trust.

For example, a resident discretionary trust receives interest during the year of assessment. After receiving the interest but before the end of the trust's year of assessment, the trustees exercise their discretion to vest the interest in the beneficiary. Section 25B(1), read with section 25B(2), deems the amount to have accrued to the beneficiary and not the trust. Accordingly, it is the identity of beneficiary that must be considered when assessing whether the interest is "to or for the benefit of a foreign person". The complexity arises because section 25B can deem the amount to have accrued to the beneficiary after it was actually paid to the trust and whilst the trust in this example is a resident, the beneficiary in which the interest was vested may not be a resident.

If the trustees in the above example exercised their discretion to vest the interest in a beneficiary after the end of the trust's year of assessment, the interest is deemed to accrue to the trust [section 25B(1)]. Accordingly, it is the identity of the trust that must be considered when assessing whether the interest is "to or for the benefit of any foreign person".

In the context of discretionary trusts and vesting, an important point is that the trigger for withholding tax on interest remains "paid", being the earlier of paid and due and payable. The time of payment may be different to the time at which vesting takes place. For example, payment may take place in a year of assessment after the year of assessment in which the trustees exercise their discretion and vest the interest in a beneficiary. Payment could also be triggered before vesting occurs – see Example 12.

Example 12 – Interest paid to a resident discretionary trust

Facts:

ZB Trust, a South African registered and resident trust, is a discretionary trust with two discretionary beneficiaries, D and C. D is resident in Foreign Country NY and has not visited South Africa in the last 2 years. C is resident in South Africa.

ZB Trust provided a 6-month loan of R100 000 to S, a South African resident, on 28 February 2022. The loan and interest at 12% were payable on 31 August 2022. S repaid the loan and the interest to ZB Trust on 31 August 2022 as required.

The trustees met on 28 February 2023 and vested the interest income in D. ZB Trust's year of assessment ends on the last day of February each year.

There is no tax treaty between South Africa and Foreign Country NY.

Result:

Section 50B(1)(a) requires withholding tax on interest to be levied on interest paid to or for the benefit of a foreign person. In these circumstances, at the date of making the payment of interest, S made the payment to a resident, ZB Trust, and was not aware that the interest might ultimately be vested in D and as a result of the application of section 25B(2) be deemed to have been derived by D. Accordingly, S does not have a withholding responsibility under section 50E(1) at the date of payment.

As a result of the exercise of the trustees' discretion to vest the interest in D on 28 February 2023, which is in the same year of assessment in which the interest was received by ZB Trust, section 25B(2) deems the interest to have been derived by D. Since the interest is deemed to have accrued to a foreign person (D) and it was paid by S to the trust on 31 August 2022, ZB Trust is regarded as the withholding agent that is responsible for withholding the withholding tax on interest at 15% and paying it over to SARS by the end of the calendar month after the month in which vesting took place. In this example, since S has paid the interest to the trust, the interest has been paid for purposes of withholding tax on interest (earlier payment and being due and payable) and the date of vesting is the date on which the trust must withhold withholding tax on interest. Although the South African-sourced interest is included in D's gross income, it is exempt from normal tax under section 10(1)(h).

Note:

- 1) If the interest had accrued to the trust but had not been paid by S, nor become due and payable, by the date the trustees exercised their discretion and vested the interest in D, the interest would not be "paid" for purposes of withholding tax on interest. The trust's obligation to withhold withholding tax on interest would then not be triggered on vesting, but would be triggered only when S paid the interest or it became due and payable.
- 2) Since the withholding agent is responsible for withholding any withholding tax on interest that may be applicable, ZB Trust must assess whether any exemptions or reduced rates of withholding tax are available. For example, if S was a bank, the payment of the interest would not be subject to withholding tax on interest as section 50D(1)(a)(i)(bb) provides an exemption for interest paid to any foreign person by any bank.
- 3) If the trustees had exercised their discretion and vested the interest in D after the end of ZB Trust's year of assessment in which the interest was received by or accrued to the trust, the trust would have been deemed to have derived the interest [section 25B(1)] and not D. No withholding obligation would have arisen, since S would have paid the interest to a resident. ZB Trust would, however, have been required to include the interest in its gross income.

The same principles considered above for a resident discretionary trust apply to a foreign resident discretionary trust.

4.5 Amounts must be received or accrued from a source within South Africa

A prerequisite for the levying of withholding tax on interest is that the interest paid to or for the benefit of a foreign person must have been received or accrued from a source within South Africa. The rules for determining the source of interest are contained in section 9(2)(b). Section 9(2)(b) provides that an amount which constitutes interest as defined in section 24J is received by or accrues to a person from a source within South Africa if –

- it 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 South Africa; or
- is received or accrues in respect of the utilisation or application in South Africa by any person of any funds or credit obtained in terms of any form of interest-bearing arrangement.

The source rules are based on where the debtor is resident or whether the funds advanced are productively employed in South Africa. The word “credit” is not defined for purposes of the Act and its ordinary meaning must therefore be considered. *Dictionary.com*²⁹ defines “credit” as follows:

“8b an agreement to entrust a buyer with goods or services without immediate payment, based on confidence in the buyer’s ability and intention to pay:.....”

For example, it is common commercial practice for suppliers to extend credit to customers in order to facilitate the sale of their goods and services. The extension of credit is normally subject to the condition that interest is charged on a debtor’s balance outstanding beyond a specified number of days. In such instance the interest charge encourages prompt payment and is incidental to the main business of the supplier. Nevertheless, such interest, when received by or accruing to a foreign person, as a result of credit being used or applied by the debtor in South Africa, irrespective of where the debtor is resident, is held to be from a South African source and potentially subject to withholding tax on interest if the other requirements of the section are met.

Example 13 – Determining the source of interest

Facts:

Z Ltd is a foreign-registered company and does not trade in South Africa. The company has recently invented a new home appliance and to gain market share the company offered extended credit terms to retailers of the product. A condition of the extended credit terms was that interest was due and payable by the retailer on any outstanding balance older than 4 months. A South African-resident company, X Pty Ltd, retailed the products in South Africa and incurred interest of R25 000 on its outstanding balance due to Z Ltd.

²⁹ <https://www.dictionary.com/browse/credit> [Accessed 26 June 2023].

Result:

The interest received by or accrued to Z Ltd is attributable to interest incurred by X Pty Ltd, a resident. Accordingly, the requirements of section 9(2)(b)(i) are met.

The requirements of section 9(2)(b)(ii) are also met because the interest payable by X Pty Ltd to Z Ltd is as a result of credit utilised in South Africa.

Although both section 9(2)(b)(i) and (ii) apply in this instance, the interest would have been from a South African source even if only one of these provisions had applied.

5. Exemptions from withholding tax on interest [section 50D]

Section 50D provides for exemptions from withholding tax on interest which are set out below. In addition, section 12Q(4) provides for an exemption from withholding tax on interest in respect of debt used for specified purposes in relation to South African ships used in international shipping – see **10.4**.

(a) Payer of the interest³⁰

Interest paid to a foreign person is exempt from withholding tax on interest if paid by –

- the government of South Africa in the national, provincial or local sphere;
- any bank,³¹ the South African Reserve Bank, the Development Bank of Southern Africa,³² or the Industrial Development Corporation³³ (see also **5.3**);
- a headquarter company in respect of the granting of financial assistance as defined in section 31(1) to which section 31 does not apply as a result of the exclusion contained in section 31(5)(a) (see **5.1**);
- a person in respect of any listed debt (see **5.2**);
- a person when the amount is payable as contemplated in section 21(6) of the Financial Markets Act and the foreign person is a client as defined in section 1 of that Act (see **5.4**);
- a person in respect of a debt owed by another foreign person (see **5.8**) unless –
 - the other foreign person is a natural person who was physically present in South Africa for a period exceeding 183 days in aggregate during the twelve-month period preceding the date on which the interest is paid (see **5.8**); or
 - the debt claim in respect of which that interest is paid is effectively connected with a permanent establishment of that other foreign person in South Africa if that other foreign person is registered as a taxpayer under Chapter 3 of the TA Act (see **5.8**);
- a person to the African Development Bank established on 10 September 1964;

³⁰ Section 50D(1).

³¹ See **4.1.1**.

³² Development Bank of Southern Africa Limited, incorporated under the Development Bank of Southern Africa Act 13 of 1997.

³³ Industrial Development Corporation of Southern Africa Limited, incorporated under the Industrial Development Corporation Act 22 of 1940.

- a person to the World Bank established on 27 December 1945 including the International Bank for Reconstruction and Development and International Development Association;
- a person to the International Monetary Fund established on 27 December 1945;
- a person to the African Import and Export Bank established on 8 May 1993;
- a person to the European Investment Bank established on 1 January 1958 under the Treaty of Rome; or
- a person to the New Development Bank established on 15 July 2014.

However, under section 50D(2) interest paid by a bank as a result of “back-to-back” loans will not qualify for exemption from withholding tax on interest (see **5.3**).

(b) Physical presence of a natural person

Also exempt from withholding tax on interest is a foreign natural person who was physically present in South Africa for more than 183 days in aggregate during the twelve-month period preceding the date on which the amount is paid (see **5.5**).³⁴ Such a person will be subject to normal tax on the interest, since the normal tax exemption will be rendered inapplicable by section 10(1)(h)(i).

(c) Permanent establishment

A foreign person will be exempt from withholding tax on interest if the debt claim for which the interest is paid is effectively connected with a permanent establishment of that foreign person in South Africa and that person is registered as a taxpayer under Chapter 3 of the TA Act.³⁵ Such a person will be subject to normal tax on the interest, since the normal tax exemption will be rendered inapplicable by section 10(1)(h)(ii). See **5.6**.

(d) Interest attributed to a resident under section 7(8)

An amount of interest is exempt from the withholding tax on interest if it is included in the income of a resident as a result of it being attributable to a donation, settlement or other disposition made by a resident as contemplated in section 7(8)(a). See **5.8**.

5.1 Headquarter companies, section 31 and section 50D

The objective in creating a headquarter tax regime is to promote South Africa as a regional financial centre, that is, as a holding company jurisdiction.³⁶ A company that meets the requirements set out in section 9I may elect to be a headquarter company for a year of assessment. Included in the incentives available to headquarter companies³⁷ is the exemption from withholding tax under section 50D(1)(a)(i)(cc) on interest paid to any foreign person arising on specified transactions. This exemption is limited to transactions constituting financial assistance which are excluded from the transfer-pricing provisions in section 31 under section 31(5)(a).

³⁴ Section 50D(3)(a).

³⁵ Section 50D(3)(b).

³⁶ *Explanatory Memorandum on the Taxation Laws Amendment Bill, 2012*.

³⁷ See Interpretation Note 87 “Headquarter Companies”.

Section 31 deals with the transfer pricing of specified international transactions. Financial assistance is defined in section 31(1) as including any debt, security or guarantee.

Section 31(5)(a) provides that section 31 does not apply to the extent that –

- there is a transaction, operation, scheme, agreement or understanding (“a transaction”) between a headquarter company and a foreign person;
- the transaction is in respect of the granting of financial assistance by the foreign person to the headquarter company;
- the headquarter company directly applies that financial assistance as financial assistance to any foreign company (“the borrowing company”); and
- the headquarter company directly or indirectly (whether alone or together with any other company forming part of the same group of companies as that headquarter company) holds at least 10% of the equity shares and voting rights in that borrowing company.

The type of transaction envisaged under section 31(5)(a) is essentially one in which the headquarter company acts as a conduit in obtaining financial assistance from a foreign lender and on-provides it to a foreign company in which it holds the required percentage of equity shares and voting rights.

The exclusion from the transfer-pricing provisions, and therefore the exemption from withholding tax on interest, applies only to the extent the financial assistance directly meets the criteria listed above.

Example 14 – Application of the exemption under section 50D(1)(a)(i)(cc)

Facts:

The year of assessment of MN (Pty) Ltd (MN) ends on the last day of February.

During the 2023 year of assessment MN met the requirements in section 9I and elected to be a headquarter company. MN’s sole investment comprised a 25% interest in ZAM (Pty) Ltd (ZAM), a company incorporated and trading in Country Z. On 1 March 2022 MN obtained a loan from a private foreign financier of R20 million which bore interest at 9% a year. The loan was obtained for a dual purpose. The main purpose was to on-lend R18 million to ZAM while the secondary purpose was to fund its own operating expenditure with the remaining R2 million. MN incurred interest of R1,8 million on the loan which was paid on 28 February 2023.

The foreign financier is not listed as a person that is exempt from the withholding tax under section 50D(1)(d).

Result:

Under section 31(5)(a), R18 million of the loan will not be subject to the transfer pricing provisions of section 31 because that amount of financial assistance from a foreign person was directly applied by MN, a headquarter company, in extending a loan to a foreign company in which MN holds at least 10% of the equity shares and voting rights.

In addition, the interest paid in respect of the R18 million which falls within the ambit of section 31(5)(a) qualifies for an exemption from withholding tax on interest under section 50D(1)(a)(i)(cc). Withholding tax on interest is calculated as follows:

	R
Interest paid on 28 February 2023	1 800 000
Less: Interest relating to loan to ZAM (R1,8 million × R18 million / R20 million)	<u>(1 620 000)</u>
Interest subject to withholding tax on interest	<u>180 000</u>

Withholding tax on interest = R180 000 × 15% = R27 000

The exemption under section 50D(1)(a)(i)(cc) is unavailable for the interest incurred on the loan which was not on-lent to ZAM.

5.2 Interest paid to a foreign person in respect of a listed debt

Section 50D(1)(a)(ii) exempts from withholding tax on interest any amount of interest paid to any foreign person in respect of any listed debt. The term “listed debt” is defined in section 50A(1) as –

“any debt that is listed on a recognised exchange as defined in paragraph 1 of the Eighth Schedule”.

Paragraph 1 of the Eighth Schedule defines a “recognised exchange” as –

- (a) an exchange licensed under the Financial Markets Act; or
- (b)
- (c) an exchange in a country other than the Republic which is similar to an exchange contemplated in paragraph (a) and which has been recognised by the Minister for purposes of this Schedule by notice in the *Gazette*”.

The company issuing the debt need not be listed, but the debt itself must be listed in order to qualify for the exemption under section 50D(1)(a)(ii).

Example 15 – Investment in listed debt

Facts:

MZ, a South African-resident company not listed on any exchanges in South Africa, required additional funding, but did not wish to dilute its share capital by issuing shares. On 6 June 2022, MZ issued debentures bearing interest at 10% a year through a listing of the debentures on the JSE. ZP, a foreign company, acquired a parcel of the listed debentures on 10 August 2022. A year after purchasing the debentures, ZP received interest of R80 000 from MZ.

Result:

The debt on which the interest is paid is debt listed on the JSE, being an exchange licensed under the Financial Markets Act. Since the interest paid to ZP relates to a listed debt instrument, it is exempt from withholding tax on interest under section 50D(1)(a)(ii). The listing requirement does not extend to the equity shares of the payer but only its debt. There is therefore no obligation on MZ to withhold tax on the interest paid to ZP.

Example 16 – Investment in debentures*Facts:*

After 1 March 2022 LT Co, a South African-resident company listed on the JSE, issued debentures of R200 000 bearing interest at 12% a year, payable annually. The debentures were not listed on any recognised exchange. E, a foreign person, purchased the LT Co debentures. In terms of the debt arrangement, interest of R24 000 is due and payable a year from the date of issue. There is no tax treaty between South Africa and the country in which E is resident.

Result:

LT Co is a listed company but the debentures issued by it are not listed on any recognised exchange. The debentures therefore do not constitute “listed debt” as defined in section 50A(1). The exemption in section 50D(1)(a)(ii) applies only if the debt is listed. The exemption is not concerned with whether the company issuing the debentures is listed.

The interest due and payable to E by LT Co of R24 000 will therefore be subject to withholding tax on interest at 15%.

5.3 Exclusion from the exemption of interest paid by a bank on “back-to-back” loans [section 50D(2)]

As a general matter, South African-source interest paid by a bank to a foreign person is exempt from withholding tax on interest.³⁸ However, this exemption does not apply when the foreign person advances an amount to a bank in the course of any arrangement, transaction, operation or scheme to which the foreign person and any other person are parties and in terms of which the bank advances any amount to that other person on the strength of that advance by the foreign person to the bank. In other words, the loan advanced by the bank to the other person is dependent on the amount advanced by the foreign person to the bank. It is not a requirement that the foreign person, the bank or the recipient of the loan be connected persons³⁹ in relation to each other; the only requirement is that the amount advanced by the foreign person and the amount advanced by the bank are interdependent. The effect of the exclusion is that the gross interest paid by the bank to the foreign person is subject to withholding tax on interest.

Example 17 – Limitation of the exemption under section 50D(1)(a)(i)(bb) as contained in section 50D(2)*Facts:*

P, a foreign person, advanced \$250 000, the equivalent of R3 million, to B Bank, a South African resident. P earned interest of 4% a year on the amount advanced. Based on the advance received from P, B Bank was obliged to advance a loan of R3,2 million to S at an interest rate of 6% a year. There is no tax treaty between South Africa and the country in which P resides. S paid interest at 6% to B Bank, and B Bank paid interest at 4% to P at the end of the year when it was due and payable.

³⁸ Section 50D(1)(a)(i)(bb).

³⁹ See Interpretation Note 67 “Connected Persons”.

Result:

P's withholding tax on the interest liability is calculated as follows:

	R
Interest paid to P (R3 million × 4%)	120 000
Withholding tax on interest (R120 000 × 15%)	18 000

Section 50B(1)(a) requires withholding tax on interest to be levied on interest paid to or for the benefit of a foreign person. Accordingly, withholding tax must be levied and withheld from the payment of interest by B Bank to P at the end of the year. The interest paid to P is not exempt from withholding tax on interest because the loan to S was advanced by B Bank on the strength of the loan made by P to B Bank and section 50D(2) therefore applies. The effect of section 50D(2) is to nullify the exemption from withholding tax on interest under section 50D(1)(a) that would otherwise have applied to interest payments by a bank.

5.4 Interest payable under section 21(6) of the Financial Markets Act

Investment or trading in securities is governed by the Financial Markets Act. The objective of this Act is to ensure that the financial markets are fair, efficient and transparent by requiring that services be provided in a fair, efficient and transparent manner.⁴⁰ In this regard rules and regulations are prescribed to protect regulated persons, clients and investors when providing and receiving securities services.⁴¹ Section 21 of the Financial Markets Act deals with the segregation of funds and requires that every authorised user⁴² must open and maintain a trust account at a bank designated for client funds or may use such an account opened and maintained by an exchange. The funds held in a trust account are considered to be "trust property", that is, they belong to identifiable specific persons and not the authorised user. Section 21(6) of the Financial Markets Act provides that any interest accruing on the funds held in the trust account is payable to the owner of the funds. Any interest accruing to a foreign person by virtue of being the part-owner of funds held in the trust account will be exempt from withholding tax on interest under section 50D(1)(b).

5.5 The 183-day rule for determining whether a foreign person is exempt from withholding tax on interest

Section 50D(3)(a) provides that a foreign person who is a natural person is exempt from withholding tax on interest if that foreign person was physically present in South Africa for a period exceeding 183 days in aggregate during the twelve-month period preceding the date on which the interest is paid.

This exemption applies because the foreign person would potentially be subject to normal tax as a result of falling outside the exemption in section 10(1)(h). Under section 10(1)(h)(i) the exemption from normal tax does not apply to a natural person

⁴⁰ Section 2 of the Financial Markets Act.

⁴¹ The term "securities services" is defined in section 1 of the Financial Markets Act as the buying and selling of securities for own account or on behalf of another person as a business, as part of a business or incidental to conducting a business; the use of the trading system or infrastructure of an exchange to buy or sell listed securities; the furnishing of advice to any person; the custody and administration of securities by a participant or nominee; the management of securities and funds by an authorised user; clearing services or settlement services.

⁴² The term "authorised user" is defined in section 1 of the Financial Markets Act as a person authorised by a licenced exchange to perform one or more securities services under the exchange rules, and includes an external authorised user, where appropriate.

who was physically present in South Africa for a period exceeding 183 days in aggregate during the twelve-month period preceding the date on which the interest was received by or accrued to that person.

Meaning of “day”

In considering whether a foreign person has been physically present in South Africa for a period exceeding 183 days, the meaning of “day” needs to be considered. The word “day” is not defined in the Act and must therefore be given its ordinary dictionary meaning. A “day” is defined in *Dictionary.com*⁴³ as follows:

“3a ... a division of time equal to 24 hours and representing the average length of the period during which the earth makes one rotation on its axis.”

“3c ... a division of time equal to 24 hours but reckoned from one midnight to the next.”

Since a day consists of a continuous 24-hour period commencing at midnight, it excludes a part of a 24-hour period. The day of arrival and departure of a person are not considered when calculating the aggregate number of days because they will not comprise a continuous 24-hour period.

Determination of the 12-month period

Under section 1 of the Interpretation Act 33 of 1957 “month” means a calendar month. In this regard, Van der Westhuizen J stated the following in *Ex parte Minister of Social Development & others*:⁴⁴

“This Court has as yet not considered the computation of time or time periods. The general common-law rule is that, in the calculation of time the civilian method is applicable, unless a period of days is prescribed by law or contracting parties intended another method to be used.

According to the civil computation method, a period of time expressed in months expires at the end of the day preceding the corresponding calendar day in the subsequent month. It is settled law that the commencement of a period of time in curial calculation is governed by the ordinary civilian method where any unit of time other than days is used.

It follows, therefore, that 18 months from the date of judgment on 6 September 2004 ended at midnight on 5 March 2006.”

Twelve-month period preceding the date on which the interest is paid

Under section 50B(2) interest is deemed to be paid on the earlier of the date on which the interest is paid or becomes due and payable.

The 12-month period concerned therefore ends on the day before the earlier of the date on which the interest is paid or becomes due and payable. For example, if interest is due and payable on 1 January of year 2, the period of 12 months will run from 1 January of year 1 to 31 December of year 1.

⁴³ <https://www.dictionary.com/browse/day> [Accessed 26 June 2023].

⁴⁴ *Ex parte Minister of Social Development & others* 2006 (4) SA 309 (CC) at 316.

Therefore, should the foreign person be physically present in South Africa for more than 183 days during this 12-month period, the exemption from withholding tax on interest will apply. At the same time, the interest will become subject to normal tax because the exemption from normal tax in section 10(1)(h) will be rendered inapplicable because of the similar 183-day exception in section 10(1)(h)(i).

Example 18 – Calculation of the 12-month period

Facts:

P, a foreign individual, lent a sum of money to Company X, a resident. The interest is payable every six months on 1 July and 1 January. P regularly visits family in South Africa and has during the last 19 months been physically present in South Africa for the following periods:

June 2021	0 days
July 2021	0 days
August 2021	0 days
September 2021	0 days
October 2021	0 days
November 2021	28 days
December 2021	31 days
January 2022	31 days
February 2022	28 days
March 2022	0 days
April 2022	0 days
May 2022	0 days
June 2022	0 days
July 2022	0 days
August 2022	20 days
September 2022	30 days
October 2022	31 days
November 2022	30 days
December 2022	20 days

Result.

The 12-month period preceding the date on which the interest was paid must be determined for each period for which interest is due and payable.

Interest due and payable 1 July 2022

The 12-month period preceding the date on which the interest was paid on 1 July 2022 for the 1 January 2022 to 30 June 2022 interest, started on 1 July 2021 and ended on 30 June 2022. During this period P was physically present in South Africa for 118 days (28 + 31 + 31 + 28). Since P was physically present in South Africa for not more than 183 days, the exemption under section 50D(3)(a) will not apply, resulting in the interest payment being subject to withholding tax on interest.

Interest due and payable 1 January 2023

The 12-month period preceding the date on which the interest was paid on 1 January 2023 for the 1 July 2022 to 31 December 2022 interest, started on 1 January 2022 and ended on 31 December 2022. During this period P was physically present in South Africa for 190 days (31 + 28 + 20 + 30 + 31 + 30 + 20). Since P was physically present in South Africa for more than 183 days, the interest paid on 1 January 2023 is exempt from withholding tax on interest under section 50D(3)(a).

5.6 Interest paid on a debt claim which relates to a permanent establishment

A permanent establishment is defined in section 1(1) with reference to a permanent establishment as defined from time to time in Article 5 of the Model Tax Convention on Income and on Capital of the Organisation for Economic Co-operation and Development (Model Tax Convention).⁴⁵ Article 5(1) defines a “permanent establishment” as -⁴⁶

“a fixed place of business through which the business of the enterprise is wholly or partly carried on”.

A place of business must pass the location and duration tests before it can be considered a fixed place of business. The location test requires that the place of business exist in a specific geographical spot and the duration test necessitates that the place of business be at the specific geographical spot with a certain degree of permanence.

Article 5 includes as examples of permanent establishments –

- a place of management;
- a branch;
- an office;
- a factory;
- a workshop, and
- a mine, an oil or gas well, a quarry or any other place of extraction of natural resources.

⁴⁵ See the definition of the term in section 1(1) for special rules which apply when determining whether a qualifying investor in relation to a partnership, trust or foreign partnership has a permanent establishment in the Republic.

⁴⁶ Model Tax Convention – 21 November 2017.

See Article 5(1) – 5(8) of the Model Tax Convention for the complete definition of a permanent establishment as defined from time to time in Article 5.

Section 50D(3)(b) exempts a foreign person from withholding tax on interest if the debt claim in respect of the interest is effectively connected with that foreign person's permanent establishment (as defined) in South Africa and that foreign person is registered as a taxpayer under Chapter 3 of the TA Act.

Interest received by or accrued to a foreign person from a source within South Africa on a debt which is effectively connected to that foreign person's permanent establishment in South Africa is potentially subject to normal tax in the hands of that foreign person because the exemption in section 10(1)(h) is rendered inapplicable by the exclusion in section 10(1)(h)(ii). The latter exclusion applies when "the debt from which the interest arises is effectively connected to a permanent establishment of that person in the Republic". The interest received by the foreign person through a permanent establishment is thus taxed under the normal tax provisions and not the withholding tax on interest provisions.

Example 19 – Interest paid on a debt effectively connected with a foreign person's permanent establishment in South Africa

Facts:

Company K, a multinational conglomerate resident in Country M, opened a branch in South Africa. The branch meets the requirements of a permanent establishment under Article 5 of the OECD Model Tax Convention. All Company K's financing and business operations are carried out through the branch. On 7 April of 2022 Company K, through its branch in South Africa, lent money to X, a resident. Interest on the debt was payable on a quarterly basis at a rate of 9% a year. The first interest payment of R40 000, which was due and payable on 7 July 2022, was paid on 15 July 2022. Company K is also registered as a taxpayer under Chapter 3 of the TA Act and is registered as an external company with the Companies and Intellectual Property Commission (CIPC).⁴⁷

Result:

Since the underlying debt claim is connected with the South African branch of Company K which constitutes a permanent establishment in South Africa and Company K is registered as a taxpayer, the interest due and payable to Company K on the loan advanced to X is exempt from withholding tax on interest under section 50D(3). The interest will, however, be subject to normal tax because it is from a South African source under section 9(2)(b) and the exemption from normal tax under section 10(1)(h) does not apply by virtue of the permanent establishment exclusion in section 10(1)(h)(ii).

⁴⁷ A foreign company cannot register as a taxpayer for income tax purposes without being registered as an external company with CIPC.

5.7 Interest paid to a foreign person in respect of a debt owed by another foreign person

Interest paid by one foreign person in respect of a debt owed to another foreign person is exempt from withholding tax on interest unless the exclusion (see below) applies.⁴⁸ The purpose of this exemption is to prevent withholding tax on interest from being imposed twice when a back-to-back loan is made.

Example 20 – Exemption from withholding tax on interest when interest is paid from one foreign person to another

Facts:

Foreign Company 1 lent R1 million at 8% a year to Foreign Company 2 which in turn on-lent the funds at 10% a year to Resident Individual A who used the money to buy a property in South Africa. Interest of R100 000 became payable to Foreign Company 2 on 30 June 2022. Foreign Company 2 paid Foreign Company 1 interest of R80 000 on the same date. Foreign Company 2 does not have a permanent establishment in South Africa.

Result:

Individual A must deduct withholding tax on interest of R15 000 from the interest paid to Foreign Company 2 (R100 000 × 15%).

The interest paid by Foreign Company 2 is from a South African source under section 9(2)(b)(ii) because the funds provided to Foreign Company 2 were used or applied in South Africa. The requirements for levying withholding tax on interest in section 50B(1) are met. However, the interest paid by Foreign Company 2 to Foreign Company 1 of R80 000 is exempt from withholding tax on interest under section 50D(1)(c) and therefore Foreign Company 2 must not withhold any withholding tax on interest from the payment.

This exemption will not apply when –

- the foreign person paying the interest is a natural person who was physically present in South Africa for a period exceeding 183 days in aggregate during the 12-month period preceding the date on which the interest is paid (see 5.5 for the meaning of “day” and the calculation of the 12-month period); or
- the debt claim giving rise to the payment of interest is effectively connected with a permanent establishment of the payer in South Africa (see 5.6) and the payer is a registered taxpayer under Chapter 3 of the TA Act.

Thus, if Foreign Company 2 in the above example had provided the funds to Individual A through a permanent establishment in South Africa and Foreign Company 2 was registered as a taxpayer in South Africa, Individual A would not have deducted withholding tax on the interest paid to Foreign Company 2 by virtue of the exemption in section 50D(3)(b) (see 5.6). However, Foreign Company 2 would have had to deduct withholding tax on interest from the interest paid to Foreign Company 1 because the debt claim was effectively connected with Foreign Company 2’s permanent establishment in South Africa and therefore the exemption from withholding tax on interest in section 50D(1)(c) would be inapplicable.

⁴⁸ Section 50D(1)(c).

5.8 Interest attributed to a resident under section 7(8)

There must be exempt from withholding tax on interest any amount of interest included in the income of a resident as is attributable to a donation, settlement or other disposition made by a resident as contemplated in section 7(8)(a). The purpose of this exemption is to prevent double taxation. It would apply, for example, when a resident pays interest to a non-resident trust and that interest is attributed to a resident donor under section 7(8). Such attribution could occur as a result of a donation by a resident to the trust or as a result of a loan by a resident to the trust which does not bear interest at an arm's length rate.

Section 7(8)(a) provides that –

“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”.

In *Ovenstone v SIR*⁴⁹ the appellant had lent his four children, two of whom were minors, money in order to enable them to acquire shares in a company without security and bearing interest at the same rate that the bank charged him. Having regard to the appellant's business standing, wealth and relationship with his bank, that rate might well have been a special, low rate. The shares concerned had generated taxable dividend income and the Secretary had included the dividends derived by the two minors in the appellant's income under section 7(3) on the basis that the failure to charge an arm's length rate of interest constituted a donation, settlement or other disposition. Dismissing the appeal, Trollip JA stated the following:⁵⁰

“To sum up: the critical phrase in s 7(3) – ‘any donation, settlement or other disposition’ – excludes any disposal of property that is a wholly commercial or business one, ie made for due consideration; it covers any disposal of property made wholly gratuitously out of liberality or generosity; it also covers any disposal of property made under a settlement or other disposition for some consideration but in which there is an appreciable element of gratuitousness and liberality or generosity.”

The judge noted that when the transaction was partly gratuitous and partly for consideration, an apportionment between the two elements was permissible.⁵¹ Thus, for example, if an interest rate of 6% were charged but an arm's length rate was 10%, the gratuitous element of 4% (10% – 6%) would comprise a “donation, settlement or other disposition” and result in attribution of income to that extent.

Unlike an interest-free or low-interest loan, when the interest income is generated from funds that were donated, the entire amount of such interest will be deemed to be that of the donor under section 7(8) without any limitation.

⁴⁹ 1980 (2) SA 721 (A), 42 SATC 55.

⁵⁰ At SATC 76.

⁵¹ At SATC 76.

Example 21 – Exemption from withholding tax when interest is subject to attribution under section 7(8)

Facts:

On 1 March of the year of assessment under review, B, a resident, lent R1 million to the B Family Trust, a non-resident trust formed and effectively managed in Country G. The loan bore interest at a rate of 2% a year. Had the trust borrowed the money from a commercial bank, it would have paid interest at the rate of 8% a year. The trust immediately on-lent the funds to C, a resident, at a rate of 8% a year. During the year of assessment under review the trust earned interest of R80 000 on the loan to C of which R60 000 was attributed to B under section 7(8) [R1 million × (8% – 2%)].

Result:

Of the interest paid by C to the trust, R60 000 is exempt from withholding tax on interest because that amount was attributed to a resident donor (B) under section 7(8).

Example 22 – Exemption from withholding tax when interest is subject to attribution under section 7(8)

Facts:

On 1 March of the year of assessment under review, B, a resident, donated R1 million to the B Family Trust, a non-resident trust formed and effectively managed in Country G. The trust immediately on-lent the funds to C, a resident, at a rate of 8% a year. During the year of assessment under review the trust earned interest of R80 000 on the loan to C which was attributed to B under section 7(8).

Result:

The interest paid by C to the trust is exempt from withholding tax on interest because it was attributed in full to a resident donor (B) under section 7(8).

6. Liabilities for the payer and recipient of South African-source interest

Broadly speaking, withholding tax on interest must be levied on South African-source interest paid to or for the benefit of a foreign person. The withholding tax on interest system imposes liabilities on both the payer of that interest and the foreign person that receives that interest or for whose benefit that interest is paid. Generally, the payer is required to withhold the tax from the interest payment and to pay it to SARS and the foreign person is liable for the tax unless it has actually been paid over to SARS by someone else. These liabilities are considered further below.

6.1 Liability for withholding tax on interest [section 50C(1)]

Section 50C(1) places the liability for withholding tax on interest on the foreign person to whom or for whose benefit the interest is paid, that is actually paid or becomes due and payable (see 4.3).

If the withholding tax on interest has been withheld as required by the payer (see 6.2) and paid over to SARS as required (see 7 – payment of the tax and the submission of a return are required), it will be regarded as an amount paid in respect of the foreign

person's liability for withholding tax on interest.⁵² The foreign person's liability for withholding tax on interest will not be discharged if withholding tax on interest is withheld by the payer but not paid over to SARS.

6.2 Liability to withhold the tax [section 50E(1)]

Although the liability for withholding tax on interest is on the foreign person to whom or for whose benefit interest is paid (see 6.1), section 50E(1) places the obligation to withhold the tax on the person who makes payment of the interest. For the purposes of the withholding tax on interest, interest is deemed to be paid on the earlier of the date on which the interest is paid or becomes due and payable (see 4.3) and therefore withholding tax on interest must be "withheld" on the earlier of the actual date of payment or when the interest becomes due and payable.

The withholding obligation is thus placed on the person that pays the interest and not on the foreign person who receives it or the person who receives it on behalf of a foreign person. If the beneficial owners are foreign persons, withholding tax on interest will have to be withheld at 15% of the gross amount of the interest (see 4.2) unless an exemption (see 6.3 and 10.4), a lower rate under a tax treaty (see 6.4) or the limitation for specified interest paid by oil and gas companies (see 10.5) applies. The payer of the interest must therefore ascertain the identity of the beneficial recipient of the interest payment in order to be able to comply with the requirements of section 50E. Such an enquiry is particularly important when interest payments are made to trustees or nominees holding investments on behalf of others.

Example 23 – Foreign person having a vested right in the income of a trust

Facts:

K Trust, a resident, made an interest-bearing loan to Z, a resident. The loan was repayable at quarterly intervals over 3 years and bore interest at 10% a year. The first interest payment became due and payable and was paid by Z on 31 August 2022. P, a foreign person and beneficiary of the trust, has a vested right to the income of the trust.

Result:

Subject to the exemptions in section 50E(2) and (3), section 50E(1) requires that any person who makes the payment of interest to or for the benefit of a foreign person must withhold withholding tax on interest. Z is the payer and has an obligation to pay interest to the K Trust. The K Trust is a resident but since it is a vesting trust, any income it receives accrues directly to its beneficiary, P. The interest paid by Z to the K Trust is paid for the benefit of P who is a foreign person. Z therefore has an obligation under section 50E to withhold withholding tax on interest on the interest paid to the K Trust for the benefit of P. K Trust will not have any obligation to withhold any withholding tax on interest under section 50E, since it receives the money on behalf of P and merely on-distributes it in accordance with the trust deed.

⁵² Section 50C(2).

Example 24 – Foreign person acquiring a vested right in the income of a trust*Facts:*

On 1 January 2022 L Trust, a resident discretionary trust, lent R100 000 to Z, a resident, repayable in three years' time. The loan bore interest at 10% a year, payable on 1 January. N, a foreign person, is a beneficiary of L Trust. On 1 January 2023 Z paid R10 000 to L Trust, being the interest due for the period 1 January 2022 to 31 December 2022. On 28 February 2023 the trustees of the L Trust vested the interest income of R10 000 (net of any taxes incurred by the trust) in N. The amount payable to N after taking into account relevant tax consequences (see below) was paid to N on 28 February 2023.

Result:

L Trust included the interest of R1 616.44 ($R100\,000 \times 10\% \times (31+28) / 365$) that accrued to it in respect of January 2022 and February 2022 in its tax return for the year of assessment ended February 2022. The interest of R1 616.44 accrued to the trust under section 25B(1) and 25B(2) because as at the end of L Trust's February 2022 year of assessment it has not been vested in and derived for the immediate or future benefit of an ascertained beneficiary who had a vested right to it.

Subject to the exemptions in section 50E(2) and (3), section 50E(1) requires that any person who makes the payment of interest to or for the benefit of a foreign person must withhold withholding tax on interest. At the time Z paid the interest to the L Trust (1 January 2023) it had not been vested in N and was therefore paid to a resident with the result that Z did not have any obligation to withhold withholding tax on interest.

When the L Trust vested the interest of R10 000 in N on 28 February 2023, interest of R8 383.56 ($R100\,000 \times 10\% \times (31+30+31+30+31+31+30+31+30+31) / 365$) that accrued in respect of March 2022 to December 2022 was deemed under section 25B(1) to accrue to N. Since the interest is deemed to have been derived by a foreign person (N) and payment by Z to the trust was on 1 January 2023, L Trust is regarded as the withholding agent that is responsible for withholding the withholding tax on interest of R8 383.56 at 15% and paying it over to SARS by the end of the calendar month after the month in which vesting took place.

The portion of interest (R1 616.44) which accrued to the L Trust in respect of the 2022 year of assessment and which was vested in N in the 2023 year of assessment is not subject to withholding tax on interest since it represents a distribution of after-tax capital and not interest.

The amount paid to N on 28 February 2023 was R8 015.07 [R10 000 – tax on interest included in L Trust return R727.40 ($R1\,616.44 \times 45\%$) – withholding tax on interest R1 257.53 ($R8\,383.56 \times 15\%$)].

6.3 Release of the obligation to withhold tax on interest [section 50E(2)]

The payer of the interest must not withhold any withholding tax on interest –

- to the extent the interest is exempt from withholding tax on interest under section 50D(1) (see “(a) Payer of interest” and “(d) Interest attributed to a resident under section 7(8)” in **5**); or
- if the foreign person to or for the benefit of which that payment of interest is to be made has, before the interest is paid, submitted to the person making the payment –
 - a declaration in such form as may be prescribed by the Commissioner (see **6.4.1**) that the foreign person is exempt from withholding tax on interest on that payment under section 50D(3) (see “(b) *Physical presence of a natural person*” and “(c) *Permanent establishment*” in **5**) or an applicable tax treaty; and
 - a written undertaking in such form as may be prescribed by the Commissioner (see **6.4.1**) to inform the person making the payment should the circumstances affecting the exemption under section 50D(3) or an applicable treaty change or should the payment of the interest no longer be for the benefit of that foreign person.

The date of payment of the interest is the earlier of the date of payment or the day on which it becomes due and payable (see **4.3**).

With effect from 1 October 2020,⁵³ the declaration and written undertaking referred to above expire and are invalid after a period of five years *from the date of the declaration*, unless the person making the payment is subject to the provisions of –

- the Financial Intelligence Centre Act 38 of 2001;
- the Agreement Between the Government of the Republic of South Africa and the Government of the United States of America to improve International Tax Compliance and to Implement the US Foreign Account Tax Compliance Act; or
- the regulations for purposes of paragraph (a) of the definition of “international tax standard” in section 1 of the TA Act,

with regard to the foreign person to or for the benefit of which the payment is to be made and takes account of these provisions in monitoring the continued validity of the declaration.⁵⁴

If the person making payment does not take account of the above-mentioned provisions in monitoring the continued validity of the declaration, the automatic 5 year expiry will apply. Whether a person making payment’s processes in complying with the above-mentioned provisions take into account the validity of the declaration is something which can be assessed only on a case-by-case basis.

A declaration and written undertaking may expire and be invalid before the automatic expiry after five years from the date of the declaration as referred to above. A declaration and written undertaking will also expire and be invalid as from the date that the foreign person’s circumstances or tax treaty change and the information

⁵³ Section 7(3) of Disaster Management Tax Relief Administration Act 14 of 2020.

⁵⁴ Section 50E(4).

contained in the declaration or written undertaking is no longer accurate. For example, the foreign persons circumstances may change 12 months after giving the declaration such that they are no longer meet the requirements in section 50D(3) for the exemption. In such a case the declaration and undertaking expire and are invalid from the date the circumstances changed and the information in the declaration or written undertaking is inaccurate.

Once a declaration and written undertaking have expired and are therefore invalid, due to the automatic expiry after a period of five years *from the date of the declaration* or a change in circumstances or tax treaty, they will no longer meet the requirements for no withholding tax on interest to be withheld (see above) and the full rate of 15% must be held unless a new and current declaration and written undertaking have been completed and submitted by the foreign person before the interest is paid. For example, if a declaration and written undertaking were submitted by a foreign person on 1 January 2018 and interest is paid to the foreign person on 1 January 2023 without that foreign person having submitted a new declaration and written undertaking before payment, the person making payment must withhold withholding tax on interest at the full rate of 15%.

In summary, if the declaration and written undertaking are not submitted before the interest is paid or if the declaration and undertaking previously submitted have expired and are therefore invalid, withholding tax on interest must be withheld at the full rate of 15%. See **8** for details regarding the availability of a potential refund.

6.4 Reduction of the rate of withholding tax on interest [section 50E(3)]

Section 50E(3) provides for the reduction of the rate at which withholding tax on interest is levied if a tax treaty applies to an interest payment made to or for the benefit of a foreign person. See **10.5** for other specified circumstances in which the rate is limited to nil for interest paid by oil and gas companies.

The application of the reduced tax rate in a tax treaty is not automatic, but is subject to the fulfilment of specified requirements. These requirements relate to the completion and submission, before the interest is paid, by the foreign person to or for the benefit of which the payment of interest is made of –

- a declaration in such form as may be prescribed by the Commissioner (see **6.4.1**) that the interest is subject to a particular reduced rate of tax under an applicable tax treaty; and
- a written undertaking in such form as may be prescribed by the Commissioner to forthwith inform the person making the payment in writing should the circumstances affecting the application of the tax treaty referred to in the preceding bullet point change or should the payment of interest no longer be for the benefit of that foreign person (see **6.4.1**).

The date of payment of the interest is the earlier of the date of payment or the date on which it is due and payable (see **4.3**). The reduced rate applies only if the foreign person submits the duly completed declaration and undertaking before the interest is paid. Without the declaration and undertaking, withholding tax at the full rate of 15% must be withheld and paid over to SARS. Section 50G (see **8**) provides for a refund if the requirements in that section are met.

A tax treaty comes into force only after it has been ratified by both member states. In order for interest to be subject to a particular reduced rate of tax under a tax treaty, any further requirements imposed by a tax treaty on the member states will have to be met.

With effect from 1 October 2020,⁵⁵ the declaration and written undertaking referred to above expire and are invalid after a period of five years from the date of the declaration, unless the person making the payment is subject to the provisions of –

- the Financial Intelligence Centre Act 38 of 2001;
- the Agreement Between the Government of the Republic of South Africa and the Government of the United States of America to improve International Tax Compliance and to Implement the US Foreign Account Tax Compliance Act; or
- the regulations for purposes of paragraph (a) of the definition of “international tax standard” in section 1 of the TA Act,

with regard to the foreign person to or for the benefit of which the payment is to be made and takes account of these provisions in monitoring the continued validity of the declaration.⁵⁶

See the last four paragraphs in 6.3 for commentary on the validity of a declaration and written undertaking which applies equally in the context of a reduction of the withholding rate.

Example 25 – Tax treaty applicable to foreign person

Facts:

T, a resident of Country S, advanced a loan to Company F, a resident. According to the loan agreement entered into by T and Company F, T is entitled to interest at 9% a year on the loan amount of R600 000. The interest became due and payable on 31 August 2022. Article 11(2) of the South Africa – Country S Tax Treaty provides that interest received by a resident of a Contracting State [Country S], from a source within the other Contracting State [South Africa], may be taxed in that other Contracting State [South Africa] but at a rate not exceeding 5% of the interest paid. T duly completed and submitted the declaration and undertaking to Company F before payment of the interest.

Result:

Since T submitted the declaration and undertaking before payment of the interest by Company F, withholding tax on interest must be deducted at the reduced tax rate of 5% under section 50E(3) as follows:

	R
Loan advanced by T	600 000
Interest received (R600 000 × 9%)	54 000
Withholding tax on interest (5% × R54 000)	2 700

⁵⁵ Section 7(3) of Disaster Management Tax Relief Administration Act 14 of 2020.

⁵⁶ Section 50E(4).

6.4.1 Withholding Tax on Interest Declaration form

In order for the payer of interest to or for the benefit of a foreign person not to withhold withholding tax under section 50E(1) or to withhold it at a reduced rate, one of the requirements under section 50E(2)(b) and 50E(3) is that the foreign person must submit the declaration and written undertaking required in those sections in the form prescribed by the Commissioner, which is the Withholding Tax on Interest Declaration form, to the payer before the interest is paid. The date of payment of the interest is the earlier of the date of payment or the date on which it becomes due and payable (see 4.3). The Withholding Tax on Interest Declaration form is available on the SARS website under Types of Tax / Withholding tax on interest.

The following information must be completed on the declaration form:

- The personal details of the payer of the interest.
- The personal details of the foreign person to whom or for who's benefit interest is paid.
- If an exemption is applicable, the reason for the exemption under section 50D(3) or otherwise (for example, the 183-day rule/attributable to a permanent establishment in South Africa/applicable tax treaty/other applicable international agreement).
- If a reduced rate of tax is applicable, the number of the applicable article in the tax treaty between the contracting states and the reduced rate which is the applicable rate of tax under the tax treaty.

For both the declaration in respect of an exemption from tax and the declaration in respect of a reduced rate of tax, the form includes an undertaking that the foreign person will inform the person paying the interest in writing should the circumstances of the person referred to in the declaration change.

A change in circumstances or tax treaty may mean that an exemption or a reduced rate of tax no longer applies. Failure by the foreign person to inform the payer of the change in circumstances could result in an incorrect amount of withholding tax on interest being withheld. The amount not withheld remains payable. Any underpayment may be subject to the imposition of interest and penalties. The declaration must be resubmitted if and when the circumstances of the payee change or if the payment is no longer for the benefit of that foreign person.

In addition, with effect from 1 October 2020, the declaration and written undertaking referred to above expire and are invalid after a period of five years from the date of the declaration. See 6.3 and 6.4 for circumstances in which the five year expiry period does not apply.⁵⁷

In summary, if a declaration and written undertaking have not been submitted before the interest is paid, or if a previously submitted declaration and written undertaking have expired and are therefore invalid, due to the automatic expiry after a period of five years from the date of the declaration or a change in circumstances or tax treaty, withholding tax on interest must be withheld at the full rate of 15%.

⁵⁷ Section 50E(4).

7. Payment of the withholding tax on interest [section 50F]

The foreign person to whom or for whose benefit the interest is paid must pay the withholding tax on interest and submit a return to SARS by the last day of the month following the month in which the interest was paid, paid being the earlier of actually being paid or being due and payable (see 4.3).⁵⁸ Thus, if the interest becomes due and payable on 10 May year 1, the foreign person to whom the interest is due and payable must pay the withholding tax on interest and submit a return to SARS by no later than 30 June year 1. This obligation to make payment and submit a return exists unless the tax has been paid by any other person. For example, if the withholding tax on interest has been withheld by the payer and paid over to SARS, the liability on the foreign person is discharged.

The person that withheld the withholding tax on interest under section 50E is required to submit a return [the Return for Withholding Tax on Interest (form WT002)] and make payment of the amount withheld to SARS by the last day of the month following the month in which the interest payment was made.⁵⁹ Payment occurs on the earlier of the date when the interest was actually paid or became due and payable (see 4.3). Section 50F(3) also requires the person required to withhold withholding tax on interest under section 50E for interest which is due and payable but not actually paid, to submit a return to SARS by the last day of the month following the month in which the interest was due and payable. However, because payment occurs on the earlier of the date of actual payment and when the interest becomes due and payable, it is submitted that the requirement to submit a return is already included in section 50F(2) and that compliance with section 50F(2) will result in compliance with section 50F(3).

In addition to the Return for Withholding Tax on Interest, SARS requires a reconciliation summary of all the withholding tax on interest payments made for the relevant year of assessment.⁶⁰ An IT3(b) certificate (or IT3(s) depending on the circumstances) must be completed and provided to the foreigner and SARS.⁶¹

Section 157(1) of the TA Act holds a withholding agent personally liable for an amount of tax –

- withheld and not paid to SARS; or
- which should have been withheld under a tax Act [such as section 50E(1)], but was not so withheld.

An amount paid or recovered from a withholding agent under section 157(1) is considered to be an amount which is paid on behalf of the relevant taxpayer for that taxpayer's liability under the relevant tax Act.⁶²

⁵⁸ Section 50F(1).

⁵⁹ Section 50F(2).

⁶⁰ See Notice 241 GG 41512 dated 23 March 2018 for detail on the 3rd parties required to make the submission and the information required. The Notice is available on www.sars.gov.za.

⁶¹ <https://www.sars.gov.za/types-of-tax/withholding-tax-on-interest/?swpmtx=c67ab681bc0e329164d3d028ecf2f056&swpmtxnonce=a211a4899b> [Accessed on 26 June 2023].

⁶² Section 157(2) of the TA Act.

Section 160(1) of the TA Act provides that a representative taxpayer, withholding agent or responsible third party that, as such, pays a tax is entitled –

- to recover the amount so paid from the person on whose behalf it is paid; or
- to retain out of money or assets in that person's possession or that may come to that person in that representative capacity, an amount equal to the amount so paid.

Unless otherwise provided for in a tax Act, a taxpayer on whose behalf an amount has been paid to SARS by a withholding agent under a tax Act or by a responsible third party under section 179 of the TA Act, is not entitled to recover from the withholding agent or responsible third party the amount so paid. The person is, however, entitled to recover the amount of an unlawful or erroneous payment from SARS.⁶³

8. Refund of withholding tax on interest [section 50G]

If a foreign person fails to submit the declaration required under section 50E(2)(b) (see 6.3) or section 50E(3) (see 6.4) before the interest is paid, withholding tax on interest must be levied and withheld at the rate of 15% and not at a reduced rate to which the foreign person would have been entitled had the declaration been submitted as required. Section 50G(1) provides an opportunity for such foreign person to have any excess payment of withholding tax on interest above that which would have applied had the declaration been submitted as required, refunded to them by the Commissioner if the outstanding declaration is submitted to the Commissioner within three years after the interest to which the declaration relates was paid. In some instances the three year time frame may be overridden by the agreed terms in a tax treaty.

Section 7(1)(a) of Disaster Management Tax Relief Administration Act 14 of 2020 provides that the period of lock down must not be taken into account when determining if the declaration form was submitted to the Commissioner within three years after the interest to which the declaration relates is paid. The period of lock down is defined in section 1 of that Act as the period between 23H59 on 26 March 2020 until 23H59 on 30 April 2020.

In addition, section 50G(2) provides a mechanism for a refund to the extent withholding tax on interest was paid on interest that became due and payable and then subsequently became irrecoverable. The Commissioner is required to refund withholding tax on interest that was paid on interest that was due and payable and subsequently became irrecoverable to the person who paid the tax.

⁶³ Section 160(2) of the TA Act.

Example 26 – Refund of an overpayment of withholding tax on interest*Facts:*

T, a resident of Country S, lent R600 000 to Company F, a South African resident. The loan agreement entered into by T and Company F stipulated that T is entitled to interest of 9% a year on the loan capital. The interest became due and payable on 31 March 2022. Article 11(2) of the South Africa - Country S Tax Treaty provides that interest received by a resident of a Contracting State (Country S), from a source within the other Contracting State [South Africa], may be taxed in that other Contracting State (South Africa) but at a rate not exceeding 5% of the interest paid.

T did not submit the Withholding Tax on Interest Declaration (WTI Declaration) form declaring that withholding tax on the interest must be withheld at the reduced rate of 5% to Company F before the interest was paid. Company F therefore withheld withholding tax on interest on the interest paid to T at the full rate of 15%. T gave Company F a power of attorney to act on their behalf.

On 15 February 2023 T submitted the WTI Declaration form pertaining to the interest payment on 31 March 2022 to the Commissioner.

Result:

Owing to T's failure to submit the WTI Declaration, the rate of 15% applied at the time of payment.

	R
Amount lent by T	600 000
Interest payable to T (R600 000 × 9%)	54 000
Withholding tax on interest (15% × R54 000)	8 100

Section 50G(1)(c) provides a period of up to three years from the date of payment of the interest in which to submit the WTI Declaration form to the Commissioner. Since Company F submitted the WTI Declaration form on T's behalf within 3 years of the date of payment of the interest, the Commissioner must refund the excess tax paid as calculated below.

The amount to be refunded is calculated by determining the amount of tax that should have been withheld at the reduced rate, and subtracting it from the amount actually withheld by the payer at the time of payment.

	R
Amount lent by T	600 000
Interest payable to T (R600 000 × 9%)	54 000
Withholding tax on interest (5% × R54 000)	2 700

Withholding tax refundable = R5 400 (R8 100 – R2 700)

Section 50G deals only with refunds owing to a declaration under section 50E(2)(b) or (3) not being submitted within the required time period. If withholding tax is incorrectly withheld and paid over to SARS (for example, the reduced rate in the declaration was incorrectly overstated or there was an error in the calculation of the amount) and a declaration form was submitted as required, a refund can potentially be claimed under section 190 of the TA Act if the requirements of that section are met.

9. Currency of payments made to the Commissioner [section 50H]

Interest may be denominated in a currency other than the rand and, if so, the amount withheld under section 50E(1) will also be denominated in a currency other than the rand. This arises because the amount which must be withheld under section 50E(1) is a percentage, currently 15%, of the amount of interest.

Section 50H provides that any amount withheld under section 50E(1) which is denominated in a foreign currency must, for purposes of determining the amount to be paid to the Commissioner, be translated to rand at the spot rate on the date on which the amount was so withheld. Under section 50E(1) the date on which the amount must be withheld is the date the person makes the payment of the amount of interest (see 6.2) and under section 50B(2) that is the earlier of the date the interest is paid or becomes due and payable (see 4.3).

The term “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.⁶⁴

Example 27 – Tax withheld in a foreign currency

Facts:

Q, a foreign person, lent \$1 million on 1 January 2022 to a resident company for a period of 5 years. The dollar-denominated loan bore interest at 5% a year. At the end of the loan, which is 31 December 2026, the initial loan capital of \$1 million is repayable to Q. The interest payments are due and payable on 1 January of each year. The resident company paid the interest to Q after it was due and payable.

The spot rates at the applicable dates are as follows:

Date loan advanced	R11,00
Date interest due and payable (1 January 2023)	R11,50
Date of payment of the tax withheld to the Commissioner (28 February 2023)	R11,60

There is no tax treaty in place between South Africa and the country in which Q is resident. The exemptions under section 50D do not apply.

Result:

Interest due and payable

The interest due and payable to Q on 1 January 2023 is \$50 000 (5% × \$1 million). The interest is calculated on the dollar-denominated amount as agreed with Q.

Withholding tax on interest

The withholding tax on interest leviable on the interest payment is \$7 500 (\$50 000 × 15%).

⁶⁴ For more on the meaning of “spot rate” see 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”.

Payment of withholding tax on interest to the Commissioner

Applying section 50H, the amount which must be paid to the Commissioner in respect of an amount of withholding tax on interest denominated in a currency other than rand, is the amount of withholding tax on interest in foreign currency translated to rand at the spot rate on the date the tax must be withheld. Interest is deemed to be paid on the earlier of the date on which it is paid or becomes due and payable. In the current case the withholding must therefore be “withheld” on the date on which the interest was due and payable. The spot rate applicable at the date of payment to the Commissioner is irrelevant. Withholding tax on interest is therefore translated to the rand equivalent using the spot rate as follows:

$$\$7\,500 \times R11,50 = R86\,250$$

Withholding tax on interest in the amount of R86 250 is payable to the Commissioner.

10. Other

10.1 Collective investment schemes

A collective investment scheme (CIS) is a type of investment vehicle used by investment managers to pool investor funds to enable them to access investments which they might not otherwise be able to access in their individual capacities. Through a CIS an investor can also achieve a spread of investments in assets such as shares, bonds, deposits, money market instruments and real estate. One of the main characteristics of a CIS is that investors get to share the risks and benefits of their investment in a scheme in proportion to their participatory interests in the scheme.

A CIS operates on behalf of the holders of participatory interests in a portfolio. From the South African perspective, these schemes operate in four categories, namely, a CIS in securities, a CIS in participation bonds, a CIS in property and a CIS in a portfolio declared by the Financial Services Board (incorporating a portfolio of a hedge fund collective investment scheme).

The definition of “person” in section 1(1) includes any trust and any portfolio of a collective investment scheme.

10.1.1 Taxation of a collective investment scheme

Section 25BA contains special rules relating to any portfolio of a CIS,⁶⁵ other than a portfolio of a collective investment scheme in property. These rules detail the manner in which the receipts and accruals, other than those of a capital nature, will be taxed. The tax treatment depends on whether the amount accrued to or, in the case of interest, received by the applicable portfolio is distributed to holders of a participatory interest within or after 12 months of the receipt or accrual by the portfolio.

The general rule is that any amount other than an amount of a capital nature which is distributed within 12 months by the portfolio to a holder of a participatory interest in the portfolio is deemed to have directly accrued to that holder on the date of the distribution. Therefore, if a portfolio distributes a South African-source amount of interest within 12 months to a holder of a participatory interest who is a foreign person, that interest will be subject to withholding tax on interest unless any of the exemptions or a reduced rate of withholding tax under a tax treaty applies. The CIS is the

⁶⁵ See definition in section 1(1).

withholding tax agent and is required to withhold the withholding tax on interest from the payment of interest to or for the benefit of the foreign person.

Amounts not distributed within the time period from either the date of accrual, or, in the case of interest, from the date of receipt, are deemed to have accrued to the portfolio on the last day of the 12-month period commencing on the date of accrual or receipt by the portfolio concerned and to the extent the amount is attributable to a dividend received or accrued it is deemed to be income of the portfolio concerned.⁶⁶ These amounts are therefore taxed in the portfolio in the year of assessment which coincides with the last day of the 12-month period. Therefore, if a holder of a participatory interest who is a foreign person receives a distribution from a portfolio out of after-taxed interest, it would not be subject to withholding tax on interest. The CIS is not liable for withholding tax on interest on the payment of interest by the payer to it, since the CIS is not a foreign person.

Example 28 – Interest distributed by a CIS to a foreign participatory interest holder within 12 months of receipt

Facts:

P, a foreign person, has a participatory interest in a CIS registered in South Africa. The CIS invests in participation bonds which yield a return in the form of South African-source interest. The CIS received interest on 1 June 2022 and made a distribution to participatory interest holders on 15 July 2022. There is no tax treaty in place between the country in which P is resident and South Africa. The interest distribution does not meet any of the requirements for exemption in section 50D.

Result:

Since the distribution of the interest was made by the CIS within 12 months from the date of receipt, it is deemed to have accrued directly to the participatory interest holders. The distribution to P constitutes interest from a source within South Africa. P, being a foreign person and the beneficial owner of interest, is subject to withholding tax on interest at 15%. The rate of 15% applies because there is no treaty between South Africa and the country in which P is resident under which the rate could be reduced.

The CIS must withhold withholding tax on interest from the payment to P.

Example 29 – Interest distributed by a CIS to a foreign participatory interest holder after 12 months of receipt

Facts:

P, a foreign person, has a participatory interest in a CIS registered in South Africa. The CIS invests in participation bonds which yield a return in the form of South African-source interest. The CIS received interest on 1 June 2021 and made a distribution to participatory interest holders on 15 July 2022. There is no tax treaty in place between the country in which P is resident and South Africa. The interest distribution does not meet any of the requirements for exemption in section 50D.

⁶⁶ Section 25BA(1)(b).

*Result:**Income tax consequences for the CIS:*

Section 25BA(1)(b)(i) deems interest not distributed by a CIS to a participatory interest holder within 12 months of receipt by the CIS to have accrued directly to the CIS. A CIS is required to register as a taxpayer and is taxed at the flat rate of tax applicable to a trust. The CIS will accordingly be taxed on the portion of interest that has not been distributed within 12 months from the date of receipt.

The CIS is not a foreign person and is therefore not liable for withholding tax on interest.

Income tax consequences for the foreign person (participatory interest holder):

P, a participatory interest holder, received a distribution out of the interest which was already subject to normal tax in the portfolio. Since this amount had already been taxed in the portfolio, it will constitute a return of portion of the trust capital when received by P and accordingly not be subject to withholding tax on interest.

10.1.2 Foreign collective investment schemes

A foreign collective investment scheme (or its equivalent) may invest in different types of instrument in South Africa. The diversification of the investment portfolio not only mitigates against market risk but provides different streams of income such as interest and dividends. Such a scheme is generally treated as a company for income tax purposes under the definition of “company” in section 1(1).⁶⁷ This assumes the scheme meets the definition of a company and is not a foreign partnership as defined in section 1(1) because foreign partnerships are specifically excluded from the definition of a company. This section of the Note is based on the assumption that the foreign collective scheme is a company as defined, if not the withholding tax on interest consequences may differ to that set out below. The treatment of a foreign collective investment scheme as a company is in contrast to local collective investment schemes which are taxed according to the tax rates applicable to a trust.

Any income that becomes due and payable accrues to the foreign scheme and not to the participatory interest holder. Section 25BA, which deems an amount to accrue directly to the participatory interest holder instead of the portfolio if distributed within 12 months from the date of accrual or, if interest, from the date of receipt (see **10.1.1**), applies only to portfolios of collective investment schemes as defined in section 1(1) and not foreign collective investment schemes. Since the interest is received by or due and payable to the foreign collective investment scheme, being a foreign person, the interest may be subject to withholding tax on interest if none of the exemptions in section 50D or a reduced rate of withholding tax under an applicable tax treaty apply.

Foreign collective investment schemes may wish to solicit investments in their scheme from members of the public in South Africa. Before soliciting investments from the members of the public in South Africa, the foreign investment scheme must obtain approval from the registrar of collective investment schemes.⁶⁸ Although approval from the registrar is required under the Collective Investment Schemes Control Act, this

⁶⁷ Paragraph (e)(ii) of the definition of “company” in section 1(1).

⁶⁸ Section 65 of the Collective Investment Schemes Control Act.

does not mean the foreign collective investment scheme constitutes a portfolio of a collective investment scheme in participation bonds or securities or portfolio of a declared collective investment scheme, as required under section 25BA⁶⁹ in order for that section to apply. This means that the full amount of interest paid to a foreign collective investment scheme will potentially be subject to withholding tax irrespective of the fact that the scheme may have a combination of resident and foreign investors (participatory interest holders).

Example 30 – Foreign collective investment scheme investing in instruments in South Africa

Facts:

A foreign mutual fund, the equivalent of a local CIS, invests in different investment portfolios in South Africa providing a return comprising different income streams. The mutual fund did not solicit business in South Africa and consists exclusively of foreign investors. During the year of assessment under review the mutual fund received South African-source interest of R5 million which it distributed to its participatory interest holders within 12 months of receipt. There is no tax treaty between South Africa and the country in which the foreign mutual fund is resident.

Result:

The interest received by the foreign mutual fund is from a source within South Africa. The foreign mutual fund is a foreign person and, as such, is subject to withholding tax on interest at 15% unless one of the exemptions in section 50D applies or if the rate at which the tax is to be withheld is reduced by the application of a tax treaty. As neither of these exceptions applies, the gross amount of R5 million is subject to withholding tax on interest at 15%.

Importantly, section 25BA(1)(a)(ii), which deems interest to accrue directly to the participatory interest holder if paid within 12 months from the date of receipt by the scheme, does not apply in this instance. Section 25BA applies only to a “portfolio of a collective investment scheme” (other than a portfolio of a collective investment scheme in property)⁷⁰ and the foreign mutual fund is not such a portfolio.

Example 31 – Foreign collective investment scheme soliciting investors from South Africa

Facts:

A foreign mutual fund, the equivalent of a local CIS, invests in different investment portfolios in South Africa providing a return comprising different income streams. The mutual fund solicits business in and outside of South Africa and has both resident and foreign investors. In order to comply with legislative requirements, the mutual fund applied and received approval to solicit investors resident in South Africa.

⁶⁹ Definition of “portfolio of a collective investment scheme” in section 1(1) and section 25BA(1).

⁷⁰ Section 1(1) read with section 25BA(1).

During the year of assessment under review the mutual fund received South African-source interest of R5 million which it distributed to its participatory interest holders within 12 months of receipt. There is no tax treaty between South Africa and the country in which the foreign mutual fund is resident.

Result:

The foreign mutual fund is regarded as a company which is a separate person to its investors for South African income tax purposes. As a foreign person, the foreign mutual fund received R5 million of South African-source interest and is subject to withholding tax on interest at 15% as none of the exemptions in section 50D apply and there is no applicable tax treaty which reduces the rate of withholding tax.

The foreign mutual fund's resident and foreign investors are not subject to withholding tax on interest.

10.2 The interaction between section 31 and Part IVB of the Act

The interest withholding tax provisions in Part IVB of the Act are generally applicable to interest paid, or which becomes due and payable, to or for the benefit of a foreign person on or after 1 March 2015.

Section 31(2), if applicable, requires that taxable income or tax payable of the person in whose hands the tax benefit results or will result must be calculated as if the terms and conditions of the affected transaction had been arm's length. It does not deem the underlying transaction to have been conducted at an adjusted amount for purposes of the Act as a whole and therefore does not alter the amount of interest paid or due and payable to the lender. Accordingly, any "adjustment" to taxable income or tax payable under section 31(2) will not impact on the amount of interest actually paid to the foreign person for purposes of withholding tax on interest under Part IVB of the Act. In addition, section 31(3) is a secondary adjustment which also does not re-characterise or alter the amount of interest paid or due and payable to the lender. For example, in a transaction falling within the ambit of section 31(2), Company A paid Company B, a foreign person, interest of R250 000. An arm's length amount of interest would have been R150 000. Accordingly, when calculating taxable income Company A claimed a deduction for R150 000. In addition, under section 31(3) the difference of R100 000 is deemed to be a dividend *in specie* declared and paid by Company A to Company B and Company A must consider possible dividends tax implications. Company B received interest of R250 000 which is subject to withholding tax on interest. From Company B's perspective there is no impact of the reduced deduction which Company A was permitted under section 31(2) or the deemed dividend under section 31(3) on the amount subject to withholding tax on interest.

10.3 The interaction between section 8F, section 8FA and Part IVB of the Act

Under section 8F(2) any amount that is incurred by a company or accrues to a person⁷¹ in respect of interest on or after the date that the instrument becomes a hybrid debt instrument is –⁷²

- deemed to be a dividend *in specie* in respect of a share that is declared and paid by that company to the person to whom that amount accrued on the last day of the year of assessment of that company during which it was incurred;⁷³
- not deductible;⁷⁴ and
- deemed to be a dividend *in specie* in respect of a share that accrues to that person on the last day of the year of assessment of that company during which it was incurred.⁷⁵

Under section 8FA(2) an amount of interest incurred by a company or accrues to a person⁷⁶ on or after the date that the interest becomes hybrid interest is –⁷⁷

- deemed to be a dividend *in specie* in respect of a share that is declared and paid by that company to the person to whom that amount accrued on the last day of the year of assessment of that company during which it was incurred;⁷⁸
- not deductible;⁷⁹ and
- deemed to be a dividend *in specie* in respect of a share that accrues to that person on the last day of the year of assessment of that company during which it was incurred.⁸⁰

Section 8F(3) and section 8FA(3) provide that section 8F and section 8FA, respectively, do not apply to instruments or interest owed on instruments in specific circumstances.

Sections 8F(2) and 8FA(2) deem the interest accruing on a hybrid debt instrument or interest that constitutes hybrid interest,⁸¹ as appropriate, to be a dividend *in specie* in respect of a share declared and paid by the company incurring the interest, and a dividend *in specie* in respect of a share that accrues to the person to which such interest accrues.

⁷¹ The words ‘or accrues to a person’ apply in respect of amounts incurred or accrued on or after the date of promulgation of the Taxation Laws Amendment Act 20 of 2021, namely 19 January 2022.

⁷² The term ‘hybrid debt instrument’ is defined in section 8F(1).

⁷³ Section 8F(2)(a)

⁷⁴ Section 8F(2)(b)

⁷⁵ Section 8F(2)(c) inserted by section 8(1) of the Taxation Laws Amendment Act 20 of 2021 which was promulgated on 19 January 2022 and are applicable to amounts incurred or accrued on or after this date.

⁷⁶ The words ‘or accrues to a person’ apply in respect of amounts incurred or accrued on or after the date of promulgation of the Taxation Laws Amendment Act 20 of 2021, namely 19 January 2022.

⁷⁷ The term ‘hybrid interest’ is defined in section 8FA(1).

⁷⁸ Section 8FA(2)(a)

⁷⁹ Section 8FA(2)(b)

⁸⁰ Section 8FA(2)(c) inserted by section 9(1) of the Taxation Laws Amendment Act 20 of 2021 which was promulgated on 19 January 2022 and are applicable to amounts incurred or accrued on or after this date.

⁸¹ See definition of “hybrid instrument” in section 8F(1) and 8 FA(1).

The amount of the interest that is deemed to be a dividend *in specie* declared and paid by the company incurring the interest expense may be subject to dividends tax. If applicable, the company incurring the interest expense would be liable for dividends tax because the interest expense is deemed to be a dividend *in specie*.⁸²

The amount of interest that is deemed to be a dividend *in specie* in respect of a share that accrues to a person on the last day of the payer's year of assessment, is included in that person's gross income under paragraph (k) of the definition of 'gross income' in section 1(1). The deemed dividend *in specie* may qualify for exemption under section 10(1)(k)(i). In addition, the amount will not be subject to withholding tax on interest, as the definition of "interest" under section 50A specifically excludes an amount of interest that is deemed to be a dividend *in specie* under section 8F(2) or 8FA(2). Various amendments have been made to sections 8F and 8FA.⁸³ These amendments must be considered in light of the facts of a particular case and taking into account the effective date of the amendments as the treatment may be different to that set out above.

Example 32 – Interest on hybrid debt instrument deemed to be a dividend *in specie*

Facts:

Company A incurred interest of R20 million on an instrument during its year of assessment ending on 31 March 2023. The interest was also due and payable on this date. On 1 April 2022, the instrument was and remained a hybrid debt instrument. The holder of the instrument is X who is a resident of Foreign Country NY.

There is no tax treaty between South Africa and Foreign Country NY. X had no presence in South Africa during the year of assessment.

Result:

Under section 8F(2)(a), interest of R20 million incurred by Company A on the hybrid debt instrument is deemed to be a dividend *in specie* in respect of a share that is declared and paid by Company A to the person to whom the interest accrued, X, on 31 March 2023. Company A is not entitled to a deduction for the amount when calculating taxable income. Company A is liable for dividends tax under section 64EA(b) and is subject to dividends tax at a rate of 20% under section 64E(1). Company A must therefore pay dividends tax of R4 million (R20 million × 20%) to the Commissioner on or before 30 April 2023 [under section 64K(1)(b)].

Under section 8F(2)(c), interest of R20 million incurred on a hybrid debt instrument is deemed to be a dividend *in specie* in respect of a share that accrued to X. Withholding tax on interest is not applicable on an amount of interest accrued on or after 19 January 2022 that is deemed to be a dividend *in specie* under section 8F(2)(c), as the definition of "interest" under section 50A specifically excludes any amount of interest that is deemed to be a dividend *in specie* under section 8F(2) or 8FA(2). Company A is therefore not required to withhold withholding tax on interest on the amount of R20 million due and payable to X. The dividend would be included in X's gross income but would be exempt under section 10(1)(k)(i).

⁸² See *The Comprehensive Guide to Dividends Tax* for detail.

⁸³ The Taxation Laws Amendment Acts 43 of 2014, 25 of 2015, 15 of 2016, 17 of 2017, 23 of 2018, 34 of 2019, 23 of 2020 and 20 of 2021.

10.4 The interaction between section 12Q and Part IVB of the Act

Section 12Q(4) provides that any amount of interest that is paid to a foreign person (see 4.1.2) by an international shipping company in respect of debt utilised to fund the acquisition, construction or improvements of a South African ship utilised for international shipping is exempt from withholding tax on interest. See section 12Q for the definitions of the terms used in this paragraph.

10.5 The interaction between the Tenth Schedule and Part IVB of the Act

Paragraph 3(2) of the Tenth Schedule provides that notwithstanding Part IVB of Chapter 2 of the Act, the rate of withholding tax on interest as contemplated in that Part may not exceed zero per cent of the amount of any interest that is paid by an oil and gas company, with regard to loans applied to fund expenditure contemplated in paragraph 5(2),⁸⁴ namely capital expenditure relating to exploration and post-exploration in terms of an oil and gas right.

11. Conclusion

In summary:

- Withholding tax on interest became effective on 1 March 2015 and applies to interest paid to or for the benefit of a foreign person from a South African source on or after that date. However, because section 50B(2) deems interest to have been paid on the earlier of the date on which the interest is paid or becomes due and payable, it means that Part IVB of the Act will apply only if the interest is both paid and due and payable on or after 1 March 2015.
- A foreign person is defined in section 50A(1) and means any person that is not a resident.
- Interest is deemed to be paid to a foreign person on the earlier of the date on which the interest is paid or becomes due and payable.
- Withholding tax on interest is levied at the rate of 15% on the gross amount of the interest paid to the foreign person.
- Under section 9(2)(b) interest is from a South African source if –
 - it is payable by a person that is a resident except when it is attributable to a permanent establishment which is situated outside South Africa; or
 - it is received or accrues in respect of the use or application in South Africa by any person of any funds or credit obtained under any form of interest-bearing arrangement.
- It is not a requirement that the interest incurred be deductible by the payer before it may be subject to withholding tax on interest, that is, withholding tax on interest is not subject to a trade requirement.
- While the foreign person is liable for payment of withholding tax on interest, the person who has the obligation to pay the interest also has an obligation under section 50E(1) to withhold withholding tax on interest from that payment.
- The person withholding any withholding tax on interest must submit a return and pay the tax over to SARS by the last day of the month following the month during which the interest was paid.

⁸⁴ See paragraph 5(2) of the Tenth Schedule for detail.

- The foreign person also has an obligation to submit a return and pay the tax over to SARS by the last day of the month following the month during which the interest was paid, unless the tax has been paid by another person.
- Under section 50D an interest payment to a foreign person may be exempt from withholding tax on interest. The exemption may be subject to certain specific requirements being met which are considered in **5**. A payment of interest may also be exempt under an applicable tax treaty or section 12Q(4). Section 50E(2) imposes certain additional requirements for some of the exemptions which must be met before the payer may refrain from withholding the withholding tax on interest (see **6.3**).
- Section 50E(3) provides for withholding tax on interest to be levied at a reduced rate should there be an applicable tax treaty which provides for a reduced rate. The reduced rate at which withholding tax on interest may be levied applies only after the foreign person has submitted the prescribed declaration and undertaking to the payer (see **6.4** and **6.4.1**). Paragraph 3(2) of the Tenth Schedule provides for a rate of 0% in specified circumstances.
- Withholding tax on interest is refundable under specified circumstances under section 50G, including when interest that is due and payable subsequently becomes irrecoverable.
- Any amount of tax withheld under section 50E(1) denominated in a foreign currency must, for purposes of determining the amount to be paid to the Commissioner, be translated to rand at the spot rate on the date on which the amount was so withheld.

Leveraged Legal Products

SOUTH AFRICAN REVENUE SERVICE

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Annexure – The law

Sections 50A to 50H

PART IVB

Withholding tax on interest

50A. Definitions.—(1) In this Part—

“**bank**” means any—

- (a) any bank or branch as defined in section 1 of the Banks Act respectively;
- (b) mutual bank as defined in section 1 of the Mutual Banks Act, 1993 (Act No. 124 of 1993); or
- (c) co-operative bank as defined in section 1 of the Co-operative Banks Act, 2007 (Act No. 40 of 2007);

“**Development Bank of Southern Africa**” means the Development Bank of Southern Africa Limited, incorporated in terms of the Development Bank of Southern Africa Act, 1997 (Act No. 13 of 1997);

“**foreign person**” means any person that is not a resident;

“**Industrial Development Corporation**” means the Industrial Development Corporation of South Africa Limited, registered in terms of the Industrial Development Corporation Act, 1940 (Act No. 22 of 1940);

“**interest**” means interest as contemplated in paragraph (a) or (b) of the definition of “interest” in section 24J(1); but does include an amount of interest that is deemed to be a dividend *in specie* in terms of section 8F(2) or 8FA(2);

“**listed debt**” means any debt that is listed on a recognised exchange as defined in paragraph 1 of the Eighth Schedule.

50B. Levy of withholding tax on interest.—(1) (a) There must be levied for the benefit of the National Revenue Fund a tax, to be known as the withholding tax on interest, calculated—

- (i) at the rate of 15 per cent; or
- (ii) at such rate as the Minister may announce in the national annual budget contemplated in section 27 (1) of the Public Finance Management Act, with effect from a date mentioned in that Announcement,

of the amount of any interest that is paid by any person to or for the benefit of any foreign person to the extent that the amount is regarded as having been received or accrued from a source within the Republic in terms of section 9(2)(b).

(b) If the Minister makes an announcement contemplated in paragraph (a)(ii), that rate comes into effect on the date determined by the Minister in that announcement and continues to apply for a period of 12 months from that date subject to Parliament passing legislation giving effect to that announcement within that period of 12 months.

(2) For the purposes of this Part, interest is deemed to be paid on the earlier of the date on which the interest is paid or becomes due and payable.

(3) The withholding tax on interest is a final tax.

(4) Where a person making payment of any amount of interest to or for the benefit of a foreign person has withheld an amount as contemplated in section 50E(1), that person must, for the purposes of this Part, be deemed to have paid the amount so withheld to that foreign person.

50C. Liability for tax.—(1) A foreign person to which an amount of interest is paid is liable for the withholding tax on interest to the extent that the interest is regarded as having been received by or accrued to that foreign person from a source within the Republic in terms of section 9(2)(b).

(2) Where any amount of withholding tax on interest is—

- (a) withheld as contemplated in section 50E(1); and
- (b) paid as contemplated in section 50F(2),

that amount of withholding tax on interest must be regarded as an amount that is paid in respect of that foreign person's liability under subsection (1).

50D. Exemption from withholding tax on interest.—(1) Subject to subsection (2), there must be exempt from the withholding tax on interest any amount of interest—

- (a) if that amount of interest is paid to any foreign person—
 - (i) by—
 - (aa) the government of the Republic in the national, provincial or local sphere;
 - (bb) any bank, the South African Reserve Bank, the Development Bank of Southern Africa or the Industrial Development Corporation; or
 - (cc) a headquarter company in respect of the granting of financial assistance as defined in section 31(1) to which section 31 does not apply as a result of the exclusion contained in section 31(5)(a); or
 - (ii) in respect of any listed debt;
- (b) payable as contemplated in section 21(6) of the Financial Markets Act to any foreign person that is a client as defined in section 1 of that Act;
- (c) paid to a foreign person in respect of a debt owed by another foreign person unless—
 - (i) the other foreign person is a natural person who was physically present in the Republic for a period exceeding 183 days in aggregate during the twelve month period preceding the date on which the interest is paid; or
 - (ii) the debt claim in respect of which that interest is paid is effectively connected with a permanent establishment of that other foreign person in the Republic if that other foreign person is registered as a taxpayer in terms of Chapter 3 of the Tax Administration Act;
- (d) if that amount of interest is paid to—
 - (i) the African Development Bank established on 10 September 1964;
 - (ii) the World Bank established on 27 December 1945 including the International Bank for Reconstruction and Development and International Development Association;
 - (iii) the International Monetary Fund established on 27 December 1945;
 - (iv) the African Import and Export Bank established on 8 May 1993;
 - (v) the European Investment Bank established on 1 January 1958 under the Treaty of Rome; or
 - (vi) the New Development Bank established on 15 July 2014; or
- (e) included in the income of a resident as is attributable to a donation, settlement or other disposition made by a resident as contemplated in section 7(8)(a).

(2) Interest paid to a foreign person in respect of any amount advanced by the foreign person to a bank is not exempt from the withholding tax on interest if the amount is advanced in the course of any arrangement, transaction, operation or scheme to which the foreign person and any other person are parties and in terms of which the bank advances any amount to that other person on the strength of the amount advanced by the foreign person to the bank.

(3) A foreign person is exempt from the withholding tax on interest if—

- (a) that foreign person is a natural person who was physically present in the Republic for a period exceeding 183 days in aggregate during the twelve-month period preceding the date on which the interest is paid; or
- (b) the debt claim in respect of which that interest is paid is effectively connected with a permanent establishment of that foreign person in the Republic if that foreign person is registered as a taxpayer in terms of Chapter 3 of the Tax Administration Act.

50E. Withholding of withholding tax on interest by payers of interest.—(1) Subject to subsections (2) and (3), any person who makes payment of any amount of interest to or for the benefit of a foreign person must withhold an amount of withholding tax on interest calculated at the rate contemplated in section 50B(1) from that payment.

(2) A person must not withhold any amount from any payment contemplated in subsection (1)—

- (a) to the extent that the interest is exempt from the withholding tax on interest in terms of section 50D(1); or
- (b) if the foreign person to or for the benefit of which that payment is to be made, before the interest is paid, submitted to the person making the payment —
 - (i) a declaration in such form as may be prescribed by the Commissioner that the foreign person is, in terms of section 50D (3) or an agreement for the avoidance of double taxation, exempt from the withholding tax on interest in respect of that payment; and
 - (ii) a written undertaking in such form as may be prescribed by the Commissioner to forthwith inform the person making the payment in writing, should the circumstances affecting the exemption referred to in subparagraph (i) change or should the payment of the interest no longer be for the benefit of that foreign person.

(3) The rate referred to in subsection (1) must, for the purposes of that subsection, be reduced if the foreign person to or for the benefit of which the payment contemplated in that subsection is to be made has, before the interest is paid, submitted to the person making the payment—

- (a) a declaration in such form as may be prescribed by the Commissioner that the interest is subject to that reduced rate of tax as a result of the application of an agreement for the avoidance of double taxation; and
- (b) a written undertaking in such form as may be prescribed by the Commissioner to forthwith inform the person making the payment in writing, should the circumstances affecting the application of the agreement referred to in paragraph (a) change or should the payment of the interest no longer be for the benefit of that foreign person.

(4) A declaration and written undertaking submitted in terms of subsection (2) (b) or (3) are no longer valid after a period of five years from the date of the declaration, unless the person making the payment is subject to the provisions of—

- (a) the Financial Intelligence Centre Act, 2001 (Act No. 38 of 2001);
- (b) the Agreement Between the Government of the Republic of South Africa and the Government of the United States of America to improve International Tax Compliance and to Implement the US Foreign Account Tax Compliance Act; or
- (c) the regulations for purposes of paragraph (a) of the definition of “international tax standard” in section 1 of the Tax Administration Act,

with regard to the foreign person to or for the benefit of which the payment is to be made and takes account of these provisions in monitoring the continued validity of the declaration.

50F. Payment and recovery of tax.—(1) If, in terms of section 50C, a foreign person is liable for any amount of withholding tax on interest in respect of any amount of interest that is paid to or for the benefit of the foreign person, that foreign person must pay that amount of withholding tax and submit a return by the last day of the month following the month during which the interest is paid, unless the tax has been paid by any other person.

(2) Any person that withholds any withholding tax on interest in terms of section 50E must submit a return and pay the tax to the Commissioner by the last day of the month following the month during which the interest is paid.

(3) Any person that pays withholding tax on interest in terms of section 50E in respect of interest due and payable but not actually paid, must submit a return by the last day of the month following the month during which the interest became due and payable.

50G. Refund of withholding tax on interest.—(1) Notwithstanding Chapter 13 of the Tax Administration Act, if—

- (a) an amount is withheld from a payment of an amount of interest as contemplated in section 50E(1);
- (b) a declaration contemplated in section 50E(2)(b) or (3) in respect of that interest is not submitted to the person paying that interest by the date of the payment of that interest; and
- (c) a declaration contemplated in section 50E(2)(b) or (3) is submitted to the Commissioner within three years after the payment of the interest in respect of which the declaration is made,

so much of that amount as would not have been withheld had that declaration been submitted by the date contemplated in the relevant subsection is refundable by the Commissioner to the person to which the interest was paid.

(2) Notwithstanding Chapter 13 of the Tax Administration Act, if—

- (a) an amount of withholding tax on interest is paid as contemplated in section 50E(1) in respect of an amount of interest that became due and payable; and
- (b) the amount of interest subsequently becomes irrecoverable,

so much of that amount as would not have been paid had the interest not become due and payable is refundable by the Commissioner to the person who paid the tax.

50H. Currency of payments made to Commissioner.—If an amount withheld by a person in terms of section 50E(1) is denominated in any currency other than the currency of the Republic, the amount so withheld must, for the purposes of determining the amount to be paid to the Commissioner in terms of section 50F(2), be translated to the currency of the Republic at the spot rate on the date on which the amount was so withheld.

Definition of “recognised exchange” in paragraph 1 of the Eighth Schedule

“recognised exchange” means —

- (a) an exchange licensed under the Financial Markets Act; or
- (b)
- (c) an exchange in a country other than the Republic which is similar to an exchange contemplated in paragraph (a) and which has been recognised by the Minister for purposes of this Schedule by notice in the *Gazette*;

Definition of “interest” in section 24J(1)

“**interest**” includes the —

- (a) gross amount of any interest or similar finance charges, discount or premium payable or receivable in terms of or in respect of a financial arrangement;
- (b) amount (or portion thereof) payable by a borrower to the lender in terms of any lending arrangement as represents compensation for any amount to which the lender would, but for such lending arrangement, have been entitled; and
- (c) [not applicable to the definition of “interest” in section 50A(1) for the purposes of the withholding tax on interest],

irrespective of whether such amount is —

- (i) calculated with reference to a fixed rate of interest or a variable rate of interest; or
- (ii) payable or receivable as a lump sum or in unequal instalments during the term of the financial arrangement;