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No more tax breaks in foreign trusts and companies

PREVIOUSLY, individuals who wished to register companies or form trusts outside of South Africa, could easily do so, and in most instances may have done so on the prudent advice of their financial adviser.

The tax exemptions available to South African residents in receiving foreign dividends or distributions made placing funds in a foreign trust or acquiring shares in a foreign company an attractive investment option.

However, this position has recently changed.

The amendments to the Income Tax Act (the Act) that were published on January 17 this year include changes in the law that relate to South Africans who hold assets in an offshore company or through an offshore trust. These amendments come on the heels of legislative efforts to bring foreign dividends and capital gains received by South African residents within the South African tax net.

The effects of these amendments on the repatriation of dividend and capital distributions into South



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Africa will be far-reaching, especially on those residents who hold such interests offshore with the view to re-channelling the funds at a later stage. South African residents who held shares directly in a foreign company were exempt from tax on their foreign dividends under “the participation exemption” provisions in section 10B(2)(a) and paragraph 64B of the Act which were enacted to make South Africa more appealing, from an international tax perspective.

Similarly, residents who were beneficiaries of foreign trusts were exempt from tax, in certain circumstances, in terms of section 7(8) and paragraph 72 and 80.

According to the amended

provisions, all distributions from a foreign trust to a South African resident made after March 1 this year will now be taxed. This amendment is similar to the earlier amendment of section 9D of the Act, which sought to close the “loophole” where a South African resident holding shares in a controlled foreign company (CFC) through a foreign interposed trust was also exempt from any tax implications that would have been applicable had he held those shares directly. Offshore trusts have long been viewed by the SA Revenue Service (Sars) as vehicles which assisted individuals to avoid tax.

The participation exemptions will now also be disregarded. What this means is that even if a foreign dividend or gain from the disposal of shares in a foreign company would have been exempt under the participation exemption, that foreign dividend or gain will now be taxed in the hands of the South African resident, where applicable.

Persons who will mostly be affected by these amendments will be those who have set-up offshore trusts but did

not intend to keep the funds offshore indefinitely.

Repatriating these funds could trigger significant tax implications in the hands of the resident. And since “following the money” and leaving the country is not an option for most South Africans, especially those more senior in years, it would always be prudent to revisit trusted advisers to assist with the arrangement of your offshore financial affairs.

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