Friends Provident International

Sharing our experience

Your guide to taxation in South Africa

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Policyholder's guide to taxation in South Africa

Friends Provident International (FPI) provides life insurance, savings and investment products for expatriate clients in Asia, the Middle East and other selected markets. With over 35 years' experience in the offshore financial services market we have developed an award-winning range of solutions that is flexible enough to suit most of your financial planning requirements.

While tax planning should be an important part of your overall financial planning process, it is not the only issue to consider. It is not enough for an investment to be tax efficient; it should be a good investment. Plans to secure your financial wellbeing and to provide protection for your family and other dependents must be flexible enough to meet your lifestyle and ever-changing needs, wherever you choose to live and work.

This document is a guide. We do not give taxation and/or legal advice - so please ensure you always speak with your financial adviser before making any investment decisions.

The tax rates in this document are for the year of assessment ending 28 February 2018. Please note that these tax rates and provisions are subject to change in the future. While every care has been taken to ensure the accuracy of the information, we can accept no responsibility for any actions taken or not taken based on the content of this document. Friends Provident International does not condone tax evasion. The company's products and services may not be used to evade taxes.

Paying tax in South Africa

The South African tax year for individuals runs from 1 March to≈the end of February.

The extent of your liability to tax in South Africa depends on your residency status. The income tax system changed in 2001 from a source-based system to a residence basis of taxation, with the effect that South African tax residents are generally liable to income tax on their worldwide income. Non-residents remain liable to tax in South Africa on income from a source within (or deemed to be within) the country.

There are two ways you can be considered resident in South Africa for tax purposes:

- Ordinarily resident in South Africa; or
- Complying with all the requirements of the physical presence test

Ordinarily resident in South Africa

Ordinarily resident is not defined in legislation. The South African Revenue Service (SARS) issued Interpretation Note No 3, which was published on 4 February 2002, to explain how the courts determine the rules for being considered ordinarily resident.

The concept of ordinarily resident means the country to which you would - as a matter of course - return after living abroad. It can therefore be called your usual or principal residence and, compared to other countries, would be described as your real home.

It is not necessary to be present in South Africa during a year of assessment to be considered ordinarily resident, and this can have an impact on expatriates as we will see later in this guide.

If you become ordinarily resident, it will be from a specific date in the tax year, in effect splitting the year. For example if you became ordinarily resident on 1 November 2017, all income received from sources outside South Africa before that date would be excluded from your income for the year ending 28 February 2018. All income received after 1 November will be taxable in South Africa.

Physical presence test

SARS' Income Tax Interpretation Note No 4 (issue 4) published on 12 March 2014 defines how you will become resident as a result of meeting the physical presence test.

The physical presence test is only applicable if you are not ordinarily resident, and determines residence in a particular tax year, based on the number of days spent in South Africa during that year and the five previous tax years.

You will be resident in a tax year if present as follows:

(i) for a period or periods exceeding 91 days in aggregate during the year of assessment under consideration;

(ii) for a period or periods exceeding 91 days in aggregate during each of the five years of assessment preceding the year of assessment under consideration; and

(iii) for a period or periods exceeding 915 days in aggregate during the five preceding years of assessment

If all three of the above tests are passed you will become resident for the year under consideration from the beginning of that year – 1 March.

A day is counted if you are present for any amount of time during that day unless you're in transit and don't legally enter the country. For example arrival in the country at 2330hrs still counts as one day. If you arrived at 1900hrs on 1 November and left on 4 November at 0600hrs, while you will have been in the country for two days and 11 hours in total, this amounts to a day count of four for the physical presence test. The days of arrival and departure are both counted.

The South African tax system

The South African system of taxation is administered by SARS and taxes collected under the Income Tax Act 1962 include tax on income (including taxable capital gains), and donations. These taxes are payable by ordinarily resident individuals and those who pass the physical presence test.

In addition, estate duty is payable on the estates of deceased persons:

- who were ordinarily resident in South Africa at the date of death; or
- who were not ordinarily resident, but owned assets in South Africa at the date of death in accordance with the Estate Duty Act 1955.

Income Tax

Both resident and non-resident persons are subject to normal (income) tax on the taxpayer's taxable income, at progressive tax rates, determined for each year of assessment. The tax, which is determined in accordance with the table below, is then reduced by certain rebates.

The sequence in which a taxpayer's taxable income is determined is, in essence, summarised as follows:

X		**ZAR**
	Gross income	XXX
Less:	Exempt income	(XX)
	Income	XXX
Less:	General deductions and allowances	(XXX)
Less:	Assessed loss brought forward if applicable	(XX)
Less:	Pension fund contributions	(X)
Less:	Retirement annuity fund contributions	(X)
Add:	Taxable portion of capital gains and allowances	XX
Less:	Qualifying donations	(X)
	TAXABLE INCOME (ASSESSED LOSS)	XXX

This shows that the starting point in the determination of taxable income is gross income.

Gross income, in relation to any year of assessment, is defined as:

- in the case of any tax resident, the total amount, in cash or otherwise, received or accrued to or in favour of such resident; or
- in the case of any person other than a tax resident, the total amount, in cash or otherwise, received or accrued to or in favour of such person from a source within or deemed to be within South Africa, excluding receipts and accruals of a capital nature. The definition then goes on to list certain specific inclusions.

In practice, gross income arises at the earlier of:

- the date of receipt; or
- the date of accrual.

Accrual takes place when the right to receive an amount has become absolute, i.e. when the taxpayer becomes unconditionally entitled to receive it, even though payment may only be due in the future.

Income tax is payable if your taxable income is in excess of the thresholds shown in the following table.

Age	Threshold (ZAR)
Below age 65	75,750
Age 65 to below age 75	117,300
Age 75 and over	131,150

The amount of income tax payable is based on your taxable income, which is derived from your gross income by deducting any exemptions and qualifying deductions. Using the table below the normal tax payable is determined, from which can be deducted the following tax rebates.

Rebates	Amount (ZAR)
Primary rebate (claimable by all individuals under age 65)	13,635
Plus: Secondary rebate (for all individuals aged 65 and older)	7,479
Plus: Tertiary rebate (for all individuals aged 75 and older)	2,493

The income tax rates for the year of assessment ending 28 February 2018 are as follows.

Taxable income (ZAR)	Tax rates
0 – 189,880	18% of taxable income
189,881 – 296,540	ZAR34,178 plus 26% of the amount above ZAR189,880
296,541 – 410,460	ZAR61,910 plus 31% of the amount above ZAR296,540
410,461 – 555,600	ZAR97,225 plus 36% of the amount above ZAR410,460
555,601 – 708,310	ZAR149,475 plus 39% of the amount above ZAR555,600
708,311 – 1,500,000	ZAR209,032 plus 41% of the amount above ZAR708,310
1,500,000 and above	ZAR533,625 plus 45% of the amount above ZAR1,500,000

The following example assumes you are under age 65. Further deductions not used in the example include contributions to pension funds and retirement annuities. As an employee, any tax previously paid under the Pay-As-You-Earn employees' tax system, will be deducted from the tax liability shown below.

Salary	ZAR180,000
Overtime	ZAR17,000
Bonus	ZAR15,000
Interest from South African bank deposit	ZAR24,000
Rental income	ZAR17,000
Gross income	**ZAR253,000**
Less interest exemption	(ZAR23,800)
Taxable income	**ZAR229,200**
Normal tax payable	ZAR44,401
Less primary rebate	(ZAR13,635)
Tax liability	**ZAR30,766**

Withholding taxes

The Income Tax Act also imposes withholding taxes in respect of interest, royalties and dividends.

Withholding tax on interest

Any amount of interest which is received by or accrued to a person that is not a resident, will be exempt from normal tax, unless:

- that person is an individual (i.e. 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 received by or accrues to that person; or
- the debt, from which the interest arises, is effectively connected to a permanent establishment (PE) of that non-resident recipient in South Africa.

Such exempt (from normal tax) interest may, however, be subject to the withholding tax on interest (the WTI). The WTI is a final tax and levied at a rate of 15% of the amount of any interest that is paid 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 South Africa in terms of the domestic source rules. An amount of interest is received by or accrued to a person from a source within South Africa if:

- it is paid by a resident of South Africa, unless the amount paid is attributable to a PE of the resident which is situated outside of South Africa; or
- it is received or accrues in respect of the utilisation or application of funds/credit in South Africa.

However, such amounts are nonetheless exempt from the WTI in the following instances:

- if it is paid by the South African Government;
- if it is paid by a South African bank, the South African Reserve Bank, the Industrial Development Corporation, or the Development Bank of Southern Africa;
- if it is paid by a South African headquarter company (provided that relevant requirements have been meet);
- if it is paid in respect of any debt that is listed on the Johannesburg Stock Exchange, or a similar exchange in a country other than South Africa, which has been recognised by the Minister of Finance by notice in the Gazette; or
- if it is payable by a regulated person to any foreign client in respect of securities services.

Further, an amount of interest that accrues to a non-resident person, and does not qualify for the normal tax exemption, as discussed above, will be exempted from the WTI.

Where an amount of interest is so exempt from the WTI (but subject to normal tax), or subject to the WTI at a reduced rate by virtue of the application of a relevant agreement for the avoidance of double taxation (DTA), the payer of the interest is not required to withhold WTI at the standard rate of 15%, provided that the beneficial owner of the interest submit to the payer a declaration and written undertaking by a date determined by the payer, or if no date is so determined, by the date of payment, to the following effect:

- a declaration, in the prescribed form, that the interest is either:
  - exempted from WTI for the reasons listed above, or
  - subject to a reduced rate of tax by virtue of the application of the relevant DTA; and
- a written undertaking to inform the payer in writing, should the circumstances affecting the application of the relevant DTA change.

Withholding tax on royalties

South Africa imposes a withholding tax on royalties (the WTR), calculated at the rate of 15% of the amount of any royalty 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 by or accrued to that foreign person from a source within South Africa.

Royalties, as defined for the purposes of the provisions pertaining to the WTR, are regarded as being from a source in South Africa where:

- the royalty is incurred by a South African resident, unless the incurral of the royalty is attributable to a PE of that resident which is situated outside of South Africa;
- the royalty is received or accrued in respect of the use, or right of use, or permission to use, any intellectual property in South Africa;

- the royalty is attributable to an amount incurred by a person that is a resident of South Africa and is received or accrued in respect of the imparting of (or the undertaking to impart) any scientific, technical, industrial or commercial knowledge or information, or the rendering of (or the undertaking to render) any assistance or service in connection with the application or utilisation of such knowledge or information, unless the amount so incurred is attributable to PE of that resident which is situated outside of South Africa; and
- the royalty is received or accrues in respect of the imparting of (or the undertaking to impart) any scientific, technical, industrial or commercial knowledge or information for use in South Africa, or the rendering of (or the undertaking to render) any assistance or service in connection with the application or utilisation of such knowledge or information.

A royalty is exempt from the WTR (but subject to normal tax), if:

- the foreign recipient is an individual (i.e. a natural person) who is physically present in South Africa for a period exceeding 183 days in aggregate during the 12 month period preceding the date on which the royalty is paid; or
- the property in respect of which the royalty is paid is effectively connected with a PE of that foreign person in South Africa, and provided that foreign person is registered as a taxpayer in South Africa.

Any person making payment of any amount of royalties to or for the benefit of a foreign person must withhold WTR at a rate of 15% unless, by:

- a date determined by the person making the payment; or
- if no date is so determined, by the date of payment,

the foreign recipient submits to the person making the payment a declaration that the royalty is:

- exempt from the WTR; or
- is subject to a reduced rate of tax as a result of the application of a relevant DTA.

Withholding tax on dividends

Dividends declared by companies that are resident in South Africa are generally exempt from normal (income) tax. However, such exempt dividends (from normal tax) are usually subject to dividends tax where the beneficial owner of the dividend is non-resident or an individual, regardless of where such individual may be tax resident.

Dividends tax is levied at a rate of 20% of the amount of any dividend paid by the company. The dividends tax is a final tax. The company paying the dividends must withhold dividends tax at a rate of 20% unless, by:

- a date determined by the company; or
- if no date is so determined, by the date of payment,

the beneficial owner of the dividend submits to the company:

- a declaration, in the prescribed form, that the dividend is either:
  - exempted from the dividends tax, or
  - subject to a reduced rate of tax by virtue of the application of the relevant DTA; and
- a written undertaking to inform the company in writing, should the circumstances affecting the exemption or the application of the relevant DTA change.

Capital Gains Tax

The taxation of capital gains (CGT) was introduced with effect from 1 October 2001, and applies to the disposal of capital assets on or after this date. There is no separate capital gains tax, rather this tax forms part of income tax and is contained in the Eighth Schedule of the Income Tax Act 1962. A portion (40% in the case of an individual) of the taxpayer's net capital gain (i.e. total capital gains less capital losses and exclusions) for the year is included in the taxpayer's taxable income, and taxed in terms of the normal tax tables (see above).

Should a net capital loss be realised in any year of assessment, such loss may not be set off against other taxable income and is carried forward to be set off against future capital gains. Capital gains may, however, be set off against normal tax losses.

A taxpayer's capital gain or loss for a year of assessment in respect of the disposal of an asset is defined, in essence, as the difference between the "proceeds" received or accrued in respect of the disposal or deemed disposal of an asset and the "base cost" of that asset. The base cost of an asset is essentially the expenditure incurred on or after 1 October 2001 in respect of the cost of acquisition or creation of that asset. When disposing of assets acquired before 1 October 2001, the market value of the asset on that date may be used as the base cost of the asset (there are other methods of determining base cost for assets held prior to 1 October 2001 as well).

CGT is payable on the disposal of an asset, including deemed disposals on death. It is also payable on a deemed disposal of your assets, should you cease to be a tax resident of South Africa.

Certain exclusions are available to taxpayers which reduce the amount of capital gains arising in the year of assessment and which will be included in taxable income. These include an annual exclusion of ZAR40,000, increasing to ZAR300,000 for gains arising in the year of death, and a primary residence (home) exclusion up to ZAR2 million. The disposal of certain assets, such as "personal-use assets', also fall outside the CGT net.

Residents are subject to South African CGT on the disposal of their worldwide assets. Non-residents are only subject to South African CGT in respect of the disposal of the following assets:

- Immovable property situated in South Africa,
- any right or interest in immovable property situated in South Africa (such as shares in land-rich companies), or
- assets attributable to a PE of that non-resident, which is situated in South Africa.

As an individual you will pay tax on 40% of the arising capital gain at your marginal income tax rate; meaning there is a maximum effective rate of tax on gains of 18% for the year of assessment ending 28 February 2018.

For example, if you pay income tax at the highest marginal rate of 45% and have a capital gain (after exclusions) of ZAR100,000, you will pay 45% tax on ZAR40,000, which equates to ZAR18,000, an effective rate of 18%.

Donations tax

Donations tax is a gift tax payable by South African residents on the value of gratuitous disposals of property or any gratuitous waiver or renunciation of a right. The tax is also payable in respect of disposals made for considerations assessed by SARS to have been inadequate, when compared with the actual value of the property. In this instance the value donated is the difference between the value of the property disposed of and the amount of consideration received.

Donations tax is levied at a flat rate of 20% on the value of the property donated, but there are certain exemptions, including transfers between spouses, and the first donations made to a value of ZAR100,000, in aggregate, by an individual in a tax year.

Therefore if you made a donation of ZAR150,000, tax at 20% on the excess over ZAR100,000, resulting in a charge of ZAR10,000, would be payable by the end of the month following the month during which the donation takes effect (i.e. when all the legal formalities for a valid donation have been complied with).

Donations tax will be something you have to pay in the event you make a gift of your FPI investment, unless you're using the proceeds as a contribution into a scheme that provides benefits on your retirement.

Estate duty

Estate duty is payable on death, in accordance with the Estate Duty Act No.45 of 1955. If you are ordinarily resident in South Africa, your net estate (i.e. the dutiable amount of the estate) is subject to tax at 20% after deducting a basic rebate of ZAR3.5 million. If on the death of the first spouse, the full rebate is not used, the balance remaining can be transferred to the surviving spouse and used to offset estate duty against his/her estate.

Certain reliefs exist which can be used as deductions from the dutiable estate, including transfers to your surviving spouse. Also, certain assets, including property you acquired outside of South Africa before becoming ordinarily resident, can be excluded.

Estate duty is therefore a potential issue for expatriate South Africans because your worldwide estate remains liable to estate duty, if you remain ordinarily resident in South Africa, not just property in South Africa.

Unilateral relief for foreign taxes paid and double taxation agreements

Internationally mobile expatriates may find themselves liable to taxation in their home country on income arising overseas that has already been taxed in the source country. In South Africa, relief from this situation may be provided by way of either unilateral relief given by SARS against taxes already paid, or through a double taxation agreement (DTA) between South Africa and the source country.

Unilateral relief is granted by SARS when a South African resident has paid non-reclaimable tax on the income in the country in which it arises. The tax already paid will be allowed as a credit (subject to certain limitations) towards any South African income tax liability on the same income.

South Africa has 78 DTAs in force that determine which of the two parties to the agreement have the taxing rights over income.

An analysis of the rules in each DTA is beyond the scope of this document and advice should therefore be sought on how a respective DTA will operate if you have income arising overseas.

South Africa currency exchange controls

South Africa operates a system of exchange control whereby the amount of currency you are permitted to expatriate is limited, but those limits have been increasing over the past number of years. The rules are designed to manage the flow of real and financial assets into and out of the country, which protects the foreign currency reserves and helps to maintain a reasonably strong economy.

As a South African resident, over the age of 18 years, in good standing with SARS and wanting to invest overseas, you can apply through your bank for approval to transfer funds subject to the current individual capital investment limit of ZAR10m each calendar year. In addition, there is an annual discretionary allowance of ZAR1m which may be used at the discretion of the resident for any legal purpose abroad.

Policyholder taxation

Taxation of long term insurance policies in South Africa

The purpose of this section is to illustrate how you will be taxed after investing in a FPI lump sum or regular savings plan, and compares this with the position of a similar type of investment issued by a domestic South African life company.

Your tax position as a policyholder in South Africa will depend on whether you have invested in a policy issued by a South African insurance company, or one issued by a foreign overseas insurer, such as FPI in the Isle of Man.

Insurers registered to conduct business in South Africa in accordance with the Long-term Insurance Act, No 52 of 1998, pay 30% tax to SARS on taxable income arising on their individual policyholder funds and investments therefore grow on a 'net roll up' basis.

As an Isle of Man insurance company, FPI does not pay tax on gains and income on our policyholder funds to the Isle of Man Treasury, and so investments accumulate on a 'gross roll up' basis.

Certain underlying investments may be liable to non-reclaimable withholding taxes in the country(ies) in which the investment is held.

If you have invested in a South African company's policy and you are the original beneficial owner of the policy, paragraph 55 of the Eighth Schedule of the Income Tax Act 1962 disregards gains or losses arising when you withdraw money from the policy, or when it matures or you die during its term triggering payment of the death benefit to your beneficiaries.

As foreign insurance companies do not pay tax to SARS on their policyholder funds, you or your estate will pay tax on capital gains at your marginal income tax rate when you withdraw money from the policy, or when it matures or you die during its term triggering payment of the death benefit to your beneficiaries.

An inclusion rate of 40% applies to capital gains which are added to your taxable income in the year of assessment. This means that if you pay the highest marginal income tax rate of 45%, an effective rate of 18% will be payable on gains arising from policies issued by a foreign insurance company.

Policy issued by South African insurance company	
Insurance company	Net roll up. Tax of 30% payable on taxable income.
Policyholder	Original beneficial owner(s) disregards gains and losses.

Policy issued by Isle of Man insurance company	
Insurance company	Gross roll up. No tax on gains and income in the Isle of Man.
Policyholder	Gains are taxable under general rules in accordance with the Eighth Schedule.

For example, if you pay income tax at the highest rate when you surrender your FPI single premium bond, you will pay an effective rate on the resultant gain of 18%, as illustrated below.

Original investment	ZAR500,000
Surrender value	ZAR750,000
Capital gain	ZAR250,000
Annual exclusion	ZAR40,000
Chargeable gain after applying inclusion rate	ZAR84,000
Tax at 45% on the chargeable gain	ZAR37,800 (an effective rate 18% after the annual exclusion)

Death

If you are ordinarily resident in South Africa at the date of your death, you will be treated as having made a disposal for capital gains tax purposes and the value of your FPI policy will be included in your estate when calculating the amount of estate duty payable. These taxes are not specifically deducted from the policy proceeds, but will become a liability of your estate and payable by your appointed representatives.

Should you also be the owner of any domestic South African policies at the time of your death, these will be exempted from capital gains tax, but will be included for estate duty.

This document outlines some of the key things that you should consider before investing in a FPI policy when living outside of South Africa, if there is a likelihood you will return to live there at some stage in the future. It is by no means exhaustive, and should not be relied upon when making a decision on whether or not to invest.

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