



Retrenchment payouts

The worldwide economic recession has hit South Africa and with it comes the inevitable and unwanted consequence of job losses as employers are forced to retrench employees. Retrenched employees will find themselves on the receiving end of a retrenchment package (a lump sum) which will increase their taxable incomes, and it is important that employees ensure they benefit from the taxation relief available, albeit of little consolation.

Exemption

An exemption of R30 000 is granted to the employee if the lump sum is received by an employee whose services are terminated owing to his/her employer having ceased to carry on, or intending to cease to carry on trade, or the employee having become redundant in consequence of his/her employer effecting a general retrenchment in personnel. It is important to note that the employee must be retrenched; a voluntary resignation, although tempting to avoid the stigma of retrenchment, will not ensure an employee access to the tax relief.

This "retrenchment" exemption is, however, available only if the person concerned was not at any time a director of the employer company and did not at any time hold more than

5% of its issued share capital or members' interest.

The R30 000 exemption is an exemption per taxpayer per lifetime. Therefore previous benefits that enjoyed such exemption must be deducted from current retrenchment benefits.

In order that the retrenchment lump sum be correctly treated by SARS, it is important that the employer ensure that the lump sum is correctly disclosed and coded on the employee's IRP5 tax certificate using the "3901 – Gratuities" code. In the case of a retrenchment, such a gratuity would normally include any severance pay forming part of the retrenchment package and, accumulated leave pay is often included as part of the gratuity in order to take advantage of the preferential tax treatment.

Rating concession

A further concession exists for that portion of a retrenchment lump sum that is not exempt from taxation. This concession is that all of, or at least a portion of, the award will qualify for the "rating concession" as set out in section 5(10) of the Income Tax Act. The qualifying amount will then be taxed at the taxpayer's lower "average rate" of tax (but not a rate lower than 18%), as opposed to his normal "marginal rate" of tax.

SARS tax directive

The relief set out above is not automatic and the employer must timeously seek a directive from SARS. The directive will set out the exact amount of employee's tax to be withheld by the employer from the final payment made to the employee.

Bernard Sacks

Public Benefit Organisations and the raising of funds

Secondary trade

Initially, Public Benefit Organisations (PBOs) were only permitted to carry out limited trading activities within the permissible rules, being that the trading activities were done on a cost recovery basis or on an occasional basis using voluntary labour. If the limited threshold of trading were exceeded, a PBO would lose its exempt status.

This was found to be impractical, as PBOs need to be self-sustaining to survive.

From 1 April 2006, however, a system of partial taxation was implemented allowing PBOs to carry on trading activities outside the permissible rules without losing their exempt status.

The extent of the exemption from income tax for income arising from the “secondary” trading activities is limited to the greater of 5% of the gross receipts of the organisation or R150 000. The receipts and accruals from the PBOs’ permissible trade activities will remain exempt for normal tax purposes. It is important that PBOs’ accounting records clearly distinguish between the two distinct income streams.

The amendment is not a license for the PBO to carry on a separate profitable set of trading activities. The PBOs’ secondary trading activities must support the aims and objectives of the PBO. It is still required that the PBO carry

on its activities for the benefit of the public at large in a non-profit manner with a philanthropic intent and must not be aimed at promoting the economic or self interest of any officer or employee of the organisation.

Tax deductible donations and BEE scorecard

For most donors, donations to a PBO will ensure them a tax deduction limited to 10% of the donor’s taxable income, and these donations will not attract donations tax or CGT.

A PBO with a turnover of less than R5 million is

automatically accorded a level 4 status for BEE purposes, which means that other enterprises that procure goods or services from the PBO will have the procurement recognised for their own BEE scorecard purposes.

PBOs with a turnover of between R5 million and

R35 million that carry on an approved socio-economic development programme (SED), which includes healthcare and HIV programmes, will ensure BEE scorecard points for contributors to the PBO.

The extent to which SED contributions will be recognised for the purposes of the contributor’s scorecard will depend upon the extent to which the contributions favour black people. The full value of a contribution may be recognised if at least 75% of the value of the contribution directly benefits black people. If not, the value of the contribution will be recognised to the extent that it directly benefits black people.

“The PBO’s secondary trading activities must support the aims and objectives of the PBO.”

Di Secombe

Take heed before deregistering

As of 1 March 2009, the compulsory VAT registration threshold was increased from R300 000 to R1 million; that is, vendors with taxable supplies under R1 million per annum may deregister for VAT. Qualifying vendors that choose to deregister are no longer obligated to account for VAT or submit VAT returns, reducing the relevant administrative costs and the maintenance and upkeep drudgery of VAT records.

However, while the benefits may be enticing, qualifying vendors should be aware of the disadvantages of deregistration. The VAT Act specifically accommodates deregistration from VAT and dictates the consequences – when a vendor deregisters from VAT, the vendor will have to account for output VAT on the lower of market value or cost of all assets held by the business at the time of deregistration. Vendors deregistering were afforded six

months to settle the output VAT arising, provided that the application for deregistration was made prior to 30 June 2009.

Once deregistered, the non-vendor business will not be entitled to claim any input VAT in relation to previously qualifying stock, assets or services acquired. There is also the possibility of non-vendor status affecting the procurement of work or sales, ie. potential clients who themselves are registered vendors typically prefer dealing with fellow registered vendors. In most circumstances, a registered vendor may only claim an input tax credit where they have acquired goods or services from another registered VAT vendor and where VAT was levied on the sale.

VAT vendors who no longer meet the compulsory VAT registration requirements should take prudent cognizance of the benefits and the disadvantages of deregistering from VAT, as the disadvantages may very well outweigh the benefits. Do not rush into deregistration full steam ahead without shrewd deliberation.

Anne Bardopoulos

Second chance to dispose of domestic residence

The distribution of assets by a company in liquidation (read to include winding-up or deregistration) to a natural person generally constitutes a disposal for Capital Gains Tax (CGT) purposes at both the company and shareholder levels and constitutes a dividend for Secondary Tax on Companies (STC) purposes.

Prior to 2001, many natural persons utilised companies to hold a domestic residence. A limited window period provided the opportunity to transfer the residence out of a company free from CGT, STC and transfer duty consequences. This window period has long since expired.

A proposed amendment will provide tax relief for a two-year window period so that companies holding only a residence used exclusively for domestic purposes (by the individual shareholder or spouse) can liquidate free of CGT, STC and transfer duty.

The distribution of the domestic residence on liquidation should be viewed as a CGT rollover event whereby all CGT gains and losses will be deferred until the natural person subsequently disposes of the residence.

The proposed provision will apply to all distributions occurring on or after 1 January 2010 but before 31 December 2011.

Di Seccombe

Foreign income and withholding taxes

With the progression of international business relations, many South African (SA) companies are rendering services to companies and governments in other African countries. For example, like many of its African counterparts, Mozambique levies a 20% withholding tax on amounts paid to foreign service providers. These payments would include amounts paid to SA companies for the utilisation of their equipment and the rendering of services.

What tax relief is available to SA companies for these taxes withheld?

In order for the SA companies to obtain some tax relief for the taxes withheld, the determination of the “source” of the amounts paid to them for foreign services rendered is important. There is no definition of the word “source” in the Income Tax Act (the Act). The source of an amount has been defined to first be the originating cause of the amount and secondly the location of the originating cause.

In the case of the example above, the originating cause of the amounts paid to them by Mozambique is the services that the companies render to Mozambique. Where these services are rendered in Mozambique, the source of these amounts paid to the SA companies is Mozambique.

To prevent double taxation of the SA companies, that are taxed on a worldwide basis in terms of section 6quat of the Act, any foreign taxes that are payable on foreign-sourced amounts that have been included in the SA company’s taxable income are set off against the normal SA tax payable by the SA company on those amounts.

The application of the foreign tax rebate results in the foreign sourced amount only being subject to normal tax in SA when the foreign tax rate is less than the SA normal tax rate.

Entitlement to a foreign tax credit under section 6quat arises for a SA company in the year of assessment in which the foreign sourced amount is included in the SA company’s taxable income. It is unnecessary for the foreign tax liability to be incurred in the same tax year that the foreign amount is included in the SA taxpayer’s taxable income.

In order for a section 6quat rebate to be claimed, despite the fact that the foreign tax liability might not yet have been paid, the SA taxpayer must be certain that an absolute and unconditional legal liability to pay the taxes exists.

The tax withheld is regarded as being paid directly by the SA company for the purposes of determining the section 6quat rebate. Payment is considered to have been made at the time the amount of tax was withheld. The foreign taxes must be translated into Rand on the last day of the company’s year of assessment by applying the average exchange rate (published by SARS) for that year.

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