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TAX AND EXCHANGE CONTROL ALERT

IN THIS **ISSUE**

MORE EXCHANGE, LESS CONTROL – FURTHER AMENDMENTS MADE TO THE CURRENCY AND EXCHANGES MANUAL FOR AUTHORISED DEALERS

The Currency and Exchanges Manual for Authorised Dealers (Authorised Dealer Manual), was published on 29 July 2016 and came into effect on 1 August 2016. It replaced the Exchange Control Rulings that had been in place up until that point. The Authorised Dealer Manual contains, amongst other things, the permissions and conditions applicable to transactions in foreign exchange that may be undertaken by Authorised Dealers (ADs) and/or on behalf of their clients in terms of Regulation 2(2) of the Exchange Control Regulations (Regulations).

AMNESTY THEN AND NOW

On 15 May 2003, then Minister of Finance, Trevor Manuel, announced the introduction of a joint tax and exchange control amnesty. He punted the amnesty as an opportunity, in the face of the prevailing unfavourable international economic climate, for South Africans (including *inter alia*, deceased estates and trusts) to place their confidence in the South African economy and declare their contravention of the Exchange Control Regulations (Regulations) and certain tax acts. The minister assured South Africans that in applying for amnesty, they would achieve the regularisation of their affairs in respect of foreign-held assets.

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In terms of section B.3(E) of the Authorised Dealer Manual, royalties and fees payable to non-residents in respect of licence agreements involving the local manufacture of goods can only take place if certain criteria have been met.

The Authorised Dealer Manual must be read in conjunction with the Regulations. Following the announcement in the 2017 Budget Speech that certain requirements pertaining to exchange control would be relaxed, the South African Reserve Bank's Financial Surveillance Department (FinSurv) released Exchange Control Circulars Nos. 7 and 8/2017, in terms of which the Authorised Dealers Manual was amended to give effect to these changes. We reported on these amendments in our Tax and Exchange Control Alert of 3 March 2017.

On 20 April 2017, FinSurv released Exchange Control Circular No. 9/2017 (Circular 9/2017), in which it announced further amendments to the Authorised Dealer Manual and other guideline documents. We discuss some of these amendments below.

Foreign bank accounts

In terms of section E.D of the Authorised Dealer Manual, ADs may approve requests by South African companies to open and operate foreign bank accounts, subject to certain conditions set out in section E.D(i). Circular 9/2017 points out that a new paragraph E.D(iv) has now been added to the Authorised Dealers Manual, which states that ADs may, where applicable, approve the extension of the authorities previously granted by FinSurv provided the conditions stipulated in section E.D(i) are strictly adhered to.

Licence agreements involving the local manufacture of goods

In terms of section B.3(E) of the Authorised Dealer Manual, royalties and fees payable to non-residents (related and unrelated parties) in respect of licence agreements involving the local manufacture of goods can only take place if certain criteria have been met. Previously, it was required, *inter alia*, that the Department of Trade and Industry (DTI) had to assess the licence agreement and forward its assessment to FinSurv for final consideration. An AD would then have to be satisfied that the payments fall within the terms of the relative agreement, and where applicable, that it complies with any conditions laid down in the authority granted by DTI and FinSurv. Prior to effecting payments, ADs would also need to view a copy of the approval letter from FinSurv. Following the amendment to the Authorised Dealer Manual, it is now no longer a requirement for FinSurv to approve the agreement. Only DTI needs to approve the agreement.

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From the perspective of businesses, the granting of additional powers to ADs and the reduced need for FinSurv approval under the circumstances referred to above, might be a positive development as it could make it easier to do business locally and abroad.

Miscellaneous transfers – Refunds

Prior to the amendment of the Authorised Dealer Manual, section B.14(J) of the Authorised Dealer Manual provided that ADs could only approve the payment of refunds, where it involved the following:

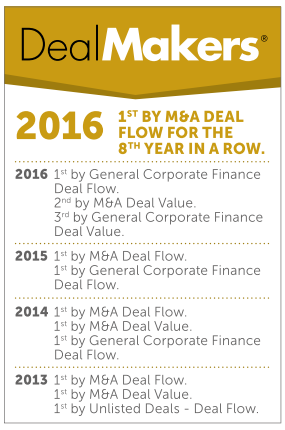
- payment by the South African Revenue Service (SARS) to non-residents;
- where a pension payment has been received from outside the Common Monetary Area (South Africa, Namibia, Lesotho and Swaziland) after the demise of a resident beneficiary; and
- where the refund was in respect of orders, tour reservations, registration fees, erroneous payments and overpayments by non-residents.

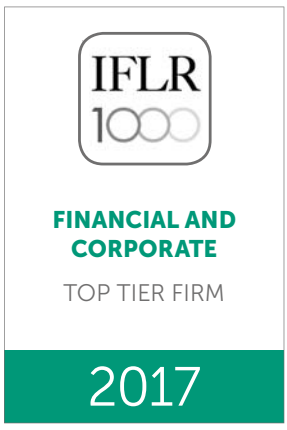
Paragraph B.14(J)(iv) has now been added and states that ADs may also approve the payment of refunds not exceeding a total value of R100,000 per calendar year due to non-residents involving related parties. However, the AD must be satisfied that the relevant transaction complies with the transfer pricing guidelines and that suitable documentary evidence is viewed in this regard.

Comment

From the perspective of businesses, the granting of additional powers to ADs and the reduced need for FinSurv approval under the circumstances referred to above, might be a positive development as it could make it easier to do business locally and abroad.

Louis Botha





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AMNESTY THEN AND NOW

The promulgation of the Financial Intelligence Centre Act, No 38 of 2001 (FICA) had increased the risk of holding illegal foreign assets.

On 15 May 2003, then Minister of Finance, Trevor Manuel, announced the introduction of a joint tax and exchange control amnesty. He punted the amnesty as an opportunity, in the face of the prevailing unfavourable international economic climate, for South Africans (including *inter alia*, deceased estates and trusts) to place their confidence in the South African economy and declare their contravention of the Exchange Control Regulations (Regulations) and certain tax acts. The minister assured South Africans that in applying for amnesty, they would achieve the regularisation of their affairs in respect of foreign-held assets.

In the run-up to the 2003 amnesty, many South Africans holding funds illegally outside South Africa had been reluctant to repatriate such funds or even disclose their existence for tax or other purposes for fear of criminal prosecution in terms of the Regulations.

He observed that the time was ripe for the proposed amnesty, given the prevailing desire of many South Africans to repatriate their foreign held assets voluntarily and regularise their affairs due to greater international co-operation in tax compliance efforts and enhanced surveillance of international capital flows. In addition, the promulgation of the Financial Intelligence Centre Act, No 38 of 2001 (FICA) had increased the risk of holding illegal foreign assets. Internationally, the legal and economic environment had also become less favourable for illegally held foreign assets. Since 1994, South Africa had expanded its tax treaty network, thereby facilitating improved international information exchange. The global community had become increasingly intolerant of tax haven jurisdictions and had reinforced measures to combat illegal money laundering. Finally, the then prevailing state of the global economy indicated that the growth prospects of foreign earnings were comparatively less attractive than the earning potential from domestic investments.

In the run-up to the 2003 amnesty, many South Africans holding funds illegally outside South Africa had been reluctant to repatriate such funds or even disclose their existence for tax or other purposes for fear of criminal prosecution in terms of the Regulations. In addition, they were concerned about the considerable tax penalties, which would have been inevitable had the South African Revenue Service (SARS) found out about the illegally-held foreign funds. In terms of FICA, SARS had been granted the power to impose income tax on a calculated amount of the value of assets or funds owned offshore which had not been declared or accounted for in any tax return submitted for the 2003 and subsequent tax years.

In brief, the joint amnesty dealt equitably with past transgressions and provided for improved future disclosure of foreign assets and income. It also permitted the repatriation to South Africa or retention of such assets offshore. In order to take advantage of the joint amnesty, for which

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The benefits of applying for relief under the amnesty were indubitable.

applications had to be submitted within the 1 May - 31 October 2003 window period, the following principles were applicable:

- Applicants could apply for the exchange control and/or the tax amnesty provided such applicants were not subject to an exchange control or tax investigation at the time.
- Exchange control amnesty had to be sought through an authorised dealer of the South African Reserve Bank (SARB).
- Income tax amnesty was to be applied for through SARS.

In the event of a successful application, the following liabilities arose:

- From an exchange control perspective, to the extent that foreign assets were repatriated to South Africa, a once off exchange control levy of 5% would be due on the market value of the foreign assets. Alternatively, if the applicant elected to retain the foreign assets offshore, a once off exchange control levy of 10% would be due on the market value of the foreign assets. In both instances, the levies would only be payable to the extent that the value of the foreign assets exceeded the then overseas investment allowance limits of R750,000 per natural person, less any amount of the allowance previously utilised.
- Applicants filing for income tax amnesty were required to pay all taxes due on foreign income earned during the year of assessment ending 28 February 2003. No income tax was levied on foreign income earned prior to 28 February 2002, provided the tax amnesty relief was applied for in the prescribed manner and timeframe. Foreign income had to be disclosed in all post-2003 tax returns.

The benefits of applying for relief under the amnesty were indubitable and included:

- From an exchange control perspective, the release of successful applicants from all civil penalties and criminal liabilities arising from the illegal movement of funds offshore in contravention of the Regulations on or before 28 February 2002.
- From a tax perspective, the release of successful applicants from all income taxes, interest, civil penalties and criminal penalties arising from the failure to disclose gross income or capital gains from foreign sources if such income and/or capital gain arose on or before 28 February 2002.
- No relief was granted for transgressions pertaining to employees' tax and/or withholding tax on royalties.

Suffice it to state that the timing of the amnesty was impeccable.

Fourteen years on, with the global introduction of the Organisation for Economic Co-operation and Development's (OECD's) initiative, the Common Reporting Standards (CRS), South Africa has seen fit to introduce the Special Voluntary Disclosure Programme (SVDP) for exchange control and/or tax transgressions, operative from 1 October 2016 to 31 August 2017. We have covered the terms of the SVDP application process, both from a tax and exchange control perspective, the imposition of levies and/or taxes and the relief to be afforded

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The 2003 amnesty was lauded as a resounding success, attracting in the range of 43,000 applications, with some prominent South Africans going public with their amnesty disclosures in a cloying show of national pride and enthusiasm.

to successful applicants, in previous Tax and Exchange Control Alert publications. Accordingly, we shall not repeat them here. The permanent tax VDP remains available during the SVDP window period and we are able to assist clients in determining on how best to proceed with the regularisation of their offshore assets and income from a tax and exchange control perspective, should they wish to do so.

So on the face of it, the amnesty then and now, appear fundamentally similar, with minor inconsequential differences; except that the unutilised portion of any applicant's offshore capital investment allowance may not be set off against the market value of foreign assets in respect of which relief is sought. The 2003 amnesty was lauded as a resounding success, attracting in the range of 43,000 applications, with some prominent South Africans going public with their amnesty disclosures in a cloying show of national pride and enthusiasm.

At the time of the previous amnesty, Minister Manuel was well on his way to establishing a global reputation as an effective finance minister. Pravin Gordhan, the then Commissioner for SARS, was effectively shifting the culture towards professionalism and integrity and collected tax from the rich to meet the needs of the poor, with impressive efficiency. With Gordhan at the helm of SARS, tax collection increased beyond expectation due to improved enforceability. Furthermore, thousands of new taxpayers were registered, improved collection procedures garnered millions in outstanding returns and rigorous corporate tax collection methodology resulted in a substantial growth in revenue.

However, all was not rosy for South Africa. A loss of confidence prevailed due to regional instability, particularly in Zimbabwe. In South Africa, there were grave concerns about a number of issues, including the levels of unemployment, HIV/AIDS and crime. The South African rand in the first half of 2002 (reaching ZAR9,74 to the US dollar) but came under increased pressure thereafter. Consequently, CPIX, which had averaged 6,8% in the fourth quarter of 2001, spiked at 12,5% in September 2002, and ultimately averaged 9,6% for 2002. The Monetary Policy Committee increased the repurchase rate of the SARB four times between January and September 2002 (by 1% on each occasion) resulting in a rate of 13,5% by September 2002. Real South African GDP growth for 2003 was 2,9% - inadequate to its economic needs and incapable of achieving meaningful inroads in unemployment.

Fast forward to the present day and the economic outlook is bleak. South Africa's economy grew by a paltry 0,3% in 2016 - the weakest pace of growth in seven years. The economy has been consistently falling behind growth targets, which is having serious implications for business and consumer confidence. In February, then Finance Minister Gordhan presented his 2017 Budget Speech, in which he projected a moderate improvement in economic growth to 1,1% for 2017. He also confirmed that, as at 22 February 2017, SARS had received disclosures under the SVDP of R3,8 billion in foreign assets, with an anticipated revenue yield of approximately R600 million.

Shortly after Gordhan was removed from his position as Minister of Finance, South Africa's foreign debt was downgraded

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AMNESTY THEN AND NOW

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Shortly after Gordhan was removed from his position as Minister of Finance, South Africa's foreign debt was downgraded to junk status by Standard & Poor's (S&P) and Fitch Ratings agency.

to junk status by Standard & Poor's (S&P) and Fitch Ratings agency. In practical terms, downgrades mean that the ratings agencies believe that South Africa will struggle to repay its foreign currency denominated debt. South Africa could be discarded by some extensively used global bond indexes, and the international funds which track those indexes or which are prohibited from holding sub-investment grade securities, will be forced to sell. Shares of South African banks, retailers and listed properties will come under significant pressure, as will bonds. Several domestic and foreign investment funds that invest pensions or savings into debt, are prohibited from investing in junk status jurisdictions for fear of losing the money. Investment of such funds into South Africa will therefore be curtailed or cauterised altogether. As people sell rands to buy other currencies, the rand will likely depreciate even further. A weaker rand means petrol prices will inevitably rise. With petrol price increases, food prices too will rise. In short, junk status means that South Africa will have to pay much more to borrow money, the increased cost of which will cascade down to the man on the street.

What does this mean for the potential efficacy of the current SVDP as a revenue-generating mechanism? It is evident that, in anticipation of the automatic exchange of information between international tax authorities, which is to begin in September 2017, and the aftershock of the Panama Papers, affected South Africans may well feel obliged to make use of the SVDP to regularise their undisclosed foreign assets. Having stated as much, it appears that there are very few South Africans publicly declaring their intention to make use of the SVDP out of a sense of national obligation. Rather, there is hushed anxiety about increased inter-jurisdictional information sharing and international transparency; fear of the potential abuse and/or unauthorised disclosure by Competent Authorities of the information that will shortly be at their disposal; and a resurgence in enquiries about foreign citizenship and/or residence.

Only time will tell whether the SVDP will be as successful as the 2003 amnesty or not.

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BBBEE STATUS: LEVEL THREE CONTRIBUTOR
Cliffe Dekker Hofmeyr is very pleased to have achieved a Level 3 BBBEE verification under the new BBBEE Codes of Good Practice. Our BBBEE verification is one of several components of our transformation strategy and we continue to seek ways of improving it in a meaningful manner.

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