Amendment in respect of foreign employment income exemption

Alongside the 2017 Medium Term Budget Policy Statements, National Treasury released the revised version of the Taxation Laws Amendment Bill 27 of 2017 (Bill) on 25 October 2017. The Bill contains those proposals that were accepted by National Treasury and which were communicated to Parliament’s Standing Committee on Finance, during the report-back hearings.

Initially in the draft Taxation Laws Amendment Bill, 2017 (Draft Bill), the proposal was to repeal the exemption on foreign employment income in terms of s10(1)(o)(ii) of the Income Tax Act, No 58 of 1962 (Act). National Treasury (Treasury) thereafter engaged in an extensive consultation process on the proposed amendments with various stakeholders. In terms of the Bill, the Act will be amended to allow the first R1 million of foreign remuneration in respect of a year of assessment to be exempt from tax in South Africa if the person is outside of South Africa for more than 183 days and for a continuous period of longer than 60 days during a 12 month period. In its Draft Response Document dated 14 September 2017, Treasury stated that:

The exemption threshold should reduce the impact of the amendment for lower to middle class South African tax residents who are earning remuneration abroad. The effect of
the exemption will also be that South African tax residents in high income tax countries are unlikely to be required to pay any additional top up payments to SARS.

This was in response to comments that the tax will have a severely negative impact on finances and remittances to South Africa, especially for those on relatively lower incomes and that it would increase the cost of employment of South African tax residents who work abroad. Treasury stated that the introduction of the capped exemption should alleviate the increased taxation costs associated with employing South Africans abroad. One should note that the balance of the remuneration, being the amount in excess of R1 million, will be taxed in South Africa irrespective of the days spent outside of South Africa.

There were also a few other comments raised by stakeholders and addressed by Treasury during the consultation process:

- One of the comments received was that the cost of living in foreign countries is higher than in South Africa, and should be taken into account in the design of the tax. This comment was taken into account by Treasury in introducing the R1 million exemption, but Treasury also stated that the tax system does not usually cater for differences in the cost of living.

- Residency was also a big discussion point with views expressed that the amendment would lead to accelerated formal emigration from South Africa or breaking of residency. In response, Treasury reiterated that the proposal is not related to citizenship and should not lead to South Africans giving up their passports as the application rests solely on tax residency. However, it added that South African tax residents who left the country many years ago are encouraged to formalise their tax residency status.

- Another comment received was that the amendment will result in cash flow problems as the foreign tax credit
(s6quat) can only be claimed on assessment. Treasury rejected this comment as employers are currently able to apply for a hardship directive from SARS, which would effectively take foreign employment taxes into account in determining employees tax (PAYE).

Interestingly, in the Draft Bill released on 19 July 2017, Treasury cited the unequal treatment that had been created between public and private sector employees, as one of the reasons for the initially proposed repeal of s10(1)(o)(ii) (see our Tax and Exchange Control Alert dated 20 July 2017 Foreign employment income is this the end?). However, the revised amendment does not do away with this unequal treatment as the entire s10(1)(o)(ii) will still not apply to public sector employees.

The Bill states that the amendment will come into operation on 1 March 2020 and will apply in respect of years of assessment commencing on or after that date. Treasury has granted taxpayers leniency, as the Draft Bill proposed that the amendment come into effect on 1 March 2019. Treasury stated that this will also allow individuals time to adjust either their contracts or their circumstances and to finalise or formalise their tax residency status.