Exemption of foreign pensions received by South African residents

Over the past few years there has been uncertainty surrounding the circumstances of South African residents receiving pension payments for services rendered or partly rendered outside South Africa. The South African Revenue Service (SARS) has previously taken the view that if the fund was located in South Africa, then the source was deemed to be in South Africa and therefore rendered the total amount of the pension payment as being taxable in South Africa, irrespective of the fact that the pension may have related partly to services that were rendered outside the country.

Binding General Ruling No 25 (Ruling), issued by SARS on 14 November 2014, provides clarity on the interpretation and application of the words “from a source outside the Republic” contained in s10(1)(gC) of Income Tax Act, No 58 of 1962 (Act). It is now indicated that the reference to ‘source’ in the Act refers to the originating cause which gave rise to the pension income. In terms of the Ruling, a formula will be used to determine the portion of the pension that will be exempt.

Section 10(1)(gC) of the Act does not refer to the source rule contained in s9(2)(i) of the Act. Section 10(1)(gC) of the Act exempts from the payment of income tax any pension received by or accrued to any resident from a source outside South Africa as consideration for past employment outside South Africa.

Section 9(2)(i) of the Act in turn provides that an amount is deemed to have been received by or accrued to a person from a source within South Africa if that amount constitutes a pension or annuity and the services in respect of which that amount is so received or accrued were rendered within South
Africa. However, if the amount is received or accrued in respect of services which were rendered partly within and partly outside South Africa, only a relevant portion will be from a source within South Africa.

In the Explanatory Memorandum on the Taxation Laws Amendment Bill 2011, pursuant to which s9(2)(i) was introduced, it was indicated that the source of pension payments will be based on the source of the underlying services giving rise to those payments.

Section 9(2)(i) of the Act specifically provides for when a pension payment is deemed to be sourced in South Africa and when not and the section provides for an apportionment of the pension concerned in respect of services that were rendered partly within and partly outside South Africa.

The ruling applies from the date of issue (14 November 2014) and will apply until it is withdrawn or the relevant legislation is amended.

Accordingly, recipients of pension benefits should ensure that the correct formula is applied in determining which portion of the pension benefit received may be exempt on the basis of services having been rendered outside South Africa.

However it appears that the Ruling did not deal with the receipt of lump sum payments.