New tax law stifles foreign work benefits

If it is passed by Parliament, the Draft Taxation Laws Amendment Bill proposal to remove foreign remuneration tax exemption will impact the willingness of South Africans to work abroad.

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South African tax residents working abroad are currently exempt from income tax if they are abroad for at least 61 days and a total of 184 days in a 12-month period.

“If South Africa has a double taxation agreement with the host country and the individual is physically present for 184 days or more in a calendar or tax year, or the salary was recharged to an entity in the host country, or the costs were borne by a permanent establishment in the host location, the income is only subject to tax in the host country,” says Shohana Mohan, committee member of the South African Institute Chartered Accountant (Saica) employees tax and expatriate tax sub-committee.

Benefits and allowances received in-country such as residential accommodation and the use of motor vehicle are currently also exempt from South African tax. This exemption aims to avoid double taxation. The proposed amendment will have the following consequences:

- Employers will need to calculate employees’ tax on salaries processed through a South African payroll or resident employer;
- Employees/employers will be required to pay personal income tax on foreign benefits and allowances (such as assignment related and hardship allowances);
- Employers may need to change their payroll processes to reflect a mirror approach for home and host country payrolls to ensure that all remuneration elements are taxed;
- Employees paid partly through a South African and partly through a foreign payroll (split payrolls) will be required to register for provisional tax;
- Employers’ tax costs will increase if they bear the tax liability of the employee (i.e. a tax equalisation);
- Employers’ compliance costs will increase as a result of registration for and payment of provisional tax and claiming of foreign tax credits, especially if the host countries’ tax year ends differ from that of South Africa; and
- Employees opting to give up their South African tax residency status may trigger capital gains tax on “exit”.

Employers will have to reconsider their international assignment and tax policies. This could include defining, and distinguishing between, durations and natures of the assignment/secondment, including:

- Early career expatriates
- Short-term expatriates
- Medium-term expatriates
- Long-term expatriates
- Localised career expatriates

Revisiting international assignment and tax policies can assist employers to manage tax jurisdiction specific risk. Factors that employers should consider include:

- Nature of the assignment or secondment
- Home and host country tax year ends
- Home and host country marginal tax rates
- The payroll regime, i.e. full payroll in South Africa or a split pay arrangement
- Maximum tax payable in both locations
- Cash flow impact of the tax payable (prior to a foreign tax credit)

With a split payroll, the impact of the provisional tax registration and the total tax payment should be considered.

Example

If an employee gets a medium- to long-term assignement to a host country, and the host country's marginal tax rate is 35%, and 50% of the salary is borne by South Africa and 50% by the host country, the tax payment is likely to be:
45% x 50% of the salary processed in South Africa
45% x 50% of the salary processed in host country
Less: 35% of the tax already paid/payable in host country
The effect is that 10% of 50% of the host country salary will be included for provisional tax purposes in South Africa.
"Employers should review their international assignment and tax policies to limit the effect on business as the impact of these proposals will be far reaching," concluded Mohan.