

ASAP

Legal and Technical Update

2020 Budget: Exchange control and emigration matters

In the recent Budget, mention was made that the concept of emigration as we know it would disappear. This has resulted in a lot of questions and fear that government will prevent South African residents from emigrating in an attempt to retain the right to tax all their income in South Africa (SA).

This document attempts to confirm what was stated in the Budget, how it is interpreted and the possible impact it may have. In addition it will focus on document released by the SA Reserve Bank which will most likely provide some much need context.

Introduction

It is important to note that this process resulting in this Budget's comments started many years ago. Since 1995 SA has started relaxing its exchange control regulations, making it easier to invest abroad whilst introducing cross-border reporting systems.

In 2017 the Finance Minister said that the current capital flow management system (exchange control system) would be reviewed and benchmarked against other countries' systems.

In the 2019 interim Budget the Finance Minister said that changes will be introduced.

2020 Budget

As a result of the Budget, it is known that exchange control regulations will change in the next year, emigration as a process will cease to exist in its current format and as a result access to retirement funds due to emigration will be impacted on as well as the emigration factor when determining tax residency.

The relevant extract contained in Annexure E to the Budget Speech reads as follows:

“Tax and exchange control treatment of individuals

Following reforms to the income tax treatment of South African tax residents who receive remuneration outside the country, government proposes to remove the exchange control treatment for individuals, while strengthening the tax treatment. The intention is to allow individuals who work abroad **more flexibility**, provided **funds are legitimately sourced and the individual is in good standing with the South African Revenue Service**. Individuals who **transfer more than R10 million** offshore will be subjected to a more **stringent verification process**. Such transfers will **also trigger a risk management test** that will **include certification of tax status and the source of funds, and assurance that the individual complies with anti-**

money laundering and countering terror financing requirements prescribed in the Financial Intelligence Centre Act (2001). This will be phased in by 1 March 2021. Under the new system, natural person emigrants and natural person residents will be treated identically.

Additional restrictions on emigrants – such as the restrictions on emigrants being allowed to invest, and the requirement to only operate blocked accounts, have bank accounts and borrow in South Africa – have been repealed. The concept of emigration as recognised by the Reserve Bank will be phased out, to be replaced by a verification process based on the requirements above. Tax residency for individuals will continue to be determined by the ordinarily resident and physically present tests as set out in the Income Tax Act (1962). Under existing international standards, South Africa participates in the automatic sharing of information between tax authorities on individuals' financial accounts and investments. These Cooperative practices will remain in place to ensure that South African tax residents who have offshore income and investments pay the appropriate level of tax."

In addition to the above extract, the SARB also published a notice on the new Cash Flow Management System. It is as a result of the benchmarking exercise that was embarked on in 2017 to review our process with other similar countries.

The new system will allow all cross-border transactions, except for those that are subject to the capital flow management measures or those that pose a high risk iro illegitimate cross-border financial flows.

Therefore, red tape will be reduced for normal international transactions and measures will be in place to detect, deter and disrupt illegitimate flows.

The main features of the new system will include:

- Move away from exchange controls and towards a cash management system to regulate cross-border flows;
- Modern, transparent and risk-based approval process;
- Stronger measures to fight illegitimate cross-border flows and tax evasion;
- Enhance cross border reporting;
- Closer working relationship between SARB, FIC, SARS and other relevant bodies.

The results

The system will be more inviting to international investors as it will pose less red tape.

It will result in SA residents and emigrants from SA being treated similarly when engaging in cross-border transactions. Therefore the process for both will be identical and the limits imposed will be universal.

Prudential limits will remain for corporate investors, but will be reviewed regularly. SA trusts will still be prohibited from investing directly abroad.

For natural persons the limits will be as follows:

- The single discretionary allowance will remain at R1 million to be reviewed regularly;

- If a person wants to take more than R1 million but less than R10 million abroad, they can do so without prior authorization, however, tax clearance will still be required.
- If more than R10 million is transferred abroad, a more stringent process will be followed which includes a risk management process.

Conclusion

From the system being introduced it is clear that the playing fields are equal for a SA resident and emigrant and that both will be able to move funds abroad within the same framework, with their tax status being the biggest determining factor.

This will then give rise to the review of the emigration process. No additional information is available at the moment, but it is assumed a process similar to the management system above will be followed. And that the transfer of funds abroad will be one of the factors to consider when determining if someone is a SA tax resident or not.

If the person is no longer a SA tax resident, there will be a deemed disposal of all assets, excluding immovable property, which may result in capital gains tax, as is currently the case. However, the process to formally be seen as a SA non-resident from the SARS point of view is not clear at this stage.

How this verification process will impact the accessibility of funds in a retirement annuity or preservation fund is not clear. At the moment, if a person has formally emigrated (or where a visa has expired) that person can access their RA or preservation fund as a pre-retirement withdrawal (full access taxed as a withdrawal). To see how the management system above will be used to allow access to these funds in future, is a matter of waiting and seeing.

We will keep you up to date as this develops.

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