South Africa Revenue Service (SARS)

and

National Treasury
Overview of International Agreements
Mr Lutando Mvovo
Director: International Tax & Treaties
National Treasury

Ms Oshna Maharaj
Manager: International Development and Treaties
SARS

Mr Thanduxolo Twala
Manager: International Development and Treaties
SARS
Jurisdictional Framework for International Tax

Jurisdictional *nexus* is the threshold that must be met before a country can tax income (pursuant to international law).

The required *nexus or* connection is residence or source.
Jurisdictional Framework for International Tax

**Source system**
- Income taxed in the country where it is derived and is located
- Income earned outside that country is not taxed

**Residence system**
- Residents taxed on their worldwide income
- Sometimes specific exclusions are allowed known residency minus (e.g. foreign income of residents working abroad for more than 6 months)
- Source still relevant for residents because they will get credit for foreign sourced income
- Non-residents are only subject to tax on income derived from a source in a country
Purpose of tax Treaties

- Prevent double taxation of the same income
  - limit the right to tax passive income in the source country
  - residence country must provide credit or exemption

- Create Fiscal Stability
  - changes 5 or 10 years from the date of entry into force
  - termination made by giving 6 months notice to the other treaty partner
  - provides for dispute resolution mechanism (MAP)

- Prevent tax avoidance and evasion
  - exchange of information and
  - assistance in tax collection
Double Taxation

- Same income taxed in the hands of the same person in more than one country (Juridical double taxation)

- This occurs where:
  - Same income is taxed in the hands of the person in source country and country of residence (source/residence double taxation) or
  - Same person treated by both countries as being their own resident and taxed on residence basis by both countries (residence/residence double taxation) or
  - Both countries treaty the income as having a source in their jurisdiction (source/source double taxation)
Source/residence double taxation is addressed by:

- Allocation of exclusive taxing right over income or capital to one country

Or

- Where taxation is permitted in both countries under a treaty, the country of residence required to provide relief for taxes imposed in the source country
A person is regarded as a resident for tax purposes in both countries.

For example, an individual may be regarded by one country as

- its resident because that person ordinarily resides in that country and
- the other country also regards her as its resident because she has spent more than 183 days in that other country.

This double taxation is addressed by the inclusion of tie-breaker clause that deem the person to be a resident of only one of the countries, for treaty purposes.
Double Taxation-Source/Source

- Both countries regard the same income as having a source in their territory under domestic law

- For example
  - One country may regard income from certain services as being sourced in their territory if the activities are performed in that country
  - While another country may treat the same income as sourced in their territory if the services are paid for by a resident of that country

- To address this, the treaty provide explicit rules for determining the source of income for treaty purposes e.g. for interest, dividends, royalties etc.

- They ensure that where a country impose tax on that income in terms of the treaty the other country must provide double tax relief in accordance with Article 23
Interaction between tax treaties and domestic law

The Constitution

- S 231(1)- Signing and negotiation of all international agreements responsibility of the National Executive

- S 231 (2)- Binds the Republic once approved by Parliament (NA and NCOP)

- S 231 (4)- Becomes law in the Republic when it is enacted into law by national legislation
Interaction between tax treaties domestic law

**Income Tax Act**

⇒ Section 108 (2):

- Agreement approved by Parliament
- Published in the government gazette
- Have effect as if enacted in the Income Tax Act
Negotiation of Tax Treaties

- NT and SARS jointly negotiate

**National Treasury**

- driver of tax treaties (initiates treaties/receives requests);
- determine tax treaty policy;
- identify treaties to be negotiated or renegotiated based on policy

**SARS:**

- implementer of tax treaties (e.g. interpretation);
- identify and negotiate exchange of information agreements (TIEA)
Other Role players

- Government
  - DIRCO
  - DTI
  - Foreign Embassies

- Private sector
  - SA multinational companies
  - Representative organisations (SAICA, BASA, ASISA etc.)

- But core arbiter of tax policy (in consultation with Cabinet and President) is the Minister of Finance
CONSIDERATIONS FOR TAX TREATY

- **Treaty country identification (New Treaties):**
  - Investment flows (inbound and outbound);
  - Main corporate players making cross border investments in either country;
  - Political relations, in some cases;
  - Trade flows (mere indication of economic activity)
  - Gateway to Africa’s strategy;
  - Potential economic and political advantages against risk of compromising the domestic tax base;
\(\text{Treaty Renegotiation:}\)

- Modernisation (e.g. global trends);
- Competitiveness with other treaty partners;
- Taxpayer identification of shortcomings;
- Change in domestic law;
- Closure of tax avoidance
TAX TREATY BENCHMARK

ˌ Country tax profile:

- Tax system [basis of tax, domestic tax rates, domestic and treaty withholding tax rates]
- Special tax vehicles and instruments [effective tax rates, tax on interest, dividends, royalties, capital gains etc.]
- Treaty network and variations [common trends + common treaty partners]
- Interrelationship between the tax systems of two countries [whether distort economic activity].
- Potential tax avoidance [e.g. transfer pricing] and treaty shopping
South Africa has largest tax treaty network than any other country in Africa;

South Africa has concluded over 73 tax treaties:
- 21 with African countries;
- 29 European countries;
- 13 with Asian and Pacific countries;
- 4 with North and South America and
- 5 with Middle East.
Main tax treaty focus is on expanding and improving SA’s tax treaty network in Africa

The breakdown of SA’s treaty network in Africa is as follows:

- 12 with SADC countries;
- 3 with North African countries;
- 3 with East African countries; and
- 3 with West African countries

Tax treaties with Lesotho, Malawi, Mauritius, Zambia and Zimbabwe have been renegotiated with the view to modernise them

Tax treaties with Gabon, Kenya, Sudan ratified in SA

Tax treaties with Cameroon, Senegal under negotiation
Base Erosion and Profit Shifting
International Tax Developments - Rules are Changing

- OECD published the BEPS Action Plan in July 2013
- Endorsed by G20 Heads of State in September 2013
- 15 Actions Plan and 10 Focus groups

  - Digital economy (1)
  - Hybrid Mismatches (2)
  - CFCs (3)
  - Interest Deductions (4)
  - Harmful Tax Practices (5)
  - Preventing Tax Treaty Abuse (6)
  - Avoidance of PE Status (7)
  - TP Aspects of Intangibles (8)
  - TP Risk Transactions (10)
  - Methodologies & data Analysis (11)
  - Disclosure Rules (12)
  - TP Documentation (13)
  - Dispute Resolution (14)
  - Multilateral Instrument (15)
International Tax Developments-What is BEPS?

- Tax planning strategies that exploit loopholes and mismatches in tax rules to make profits disappear for tax purposes by:
  - Shifting profits to low or no tax jurisdictions (tax havens)
  - Locations where there is little or no real activity resulting in little or no overall corporate tax being paid
- Taking advantage of a combination of features of home and host countries tax systems
- Ensuring that income is not taxed anywhere (double non-taxation);
- Creating offshore entities (in tax havens) and routing income through them to escape taxation
- Excessive interest deductions
- Deliberately creating dual residence to take advantage of tax treaty
Treaty abuse is one of the most important sources of BEPS

**Action 6 required to work in three different areas:**

- Develop model treaty provisions and recommendations regarding the design of domestic rules to prevent the granting of treaty benefits in inappropriate circumstances

- Clarify that tax treaties are not intended to be used to generate double non-taxation

- Identify the tax policy considerations that countries should consider before deciding to enter into a tax treaty with another country
Preventing Tax Treaty Abuse (6)

Some of the propose changes to the existing text:

- **Treaty Shopping**
  - Combined LOB and MPT test? (objective vs subjective test)
  - Dividend transfer transaction
  - Transaction that cummvent Art 13(4)
  - Tie-breaker rule – MA by CAs (current OECD alternative approach)
  - Anti-abuse rule for PEs situated in 3rd States
  - Tax treaties not intended for double non-taxation- changes to the Preamble (Art 31 (2) of the Vienna Convention)
Legal Framework

- Customs and Excise Act No. 91 of 1964 as amended which provides: Section 49 Agreements in respect of rates of duty lower than general rates of duty and other agreements providing for matters requiring customs administration.—

- (1) (a) Whenever any international agreement which binds the Republic as contemplated in section 231 of the Constitution of the Republic of South Africa, 1996, is an agreement—

- (ii) concerning customs co-operation, including for the exchange of information and the rendering of mutual and technical assistance in respect of customs co-operation;
Legal Framework

- (v) which provides for any other matter which either expressly or by implication requires to be administered by customs legislation;
- such agreement or any protocol or other part or provision thereof is enacted into law as part of this Act when published by notice in the Gazette.
Value-Added Tax Act No. 89 of 1991 as amended which provides:

Section 75. Tax Agreements -(1) The National Executive may enter into an agreement with the government of any other country whereby arrangements are made with that government with a view to—

(b) the refunding of value-added tax or any similar tax, or any portion of such value-added tax or similar tax, levied under the laws of the Republic and such other country in respect of the supply of goods or services in the Republic or such other country, as the case may be, where such goods or services are imported into such other country or the Republic, as the case may be;
Legal Framework

- (c) regulating or co-ordinating any matter with regard to the levying and collection, under the laws of the Republic and such other country, of value-added tax or any similar tax; or
- (d) the rendering of reciprocal assistance in the administration of and the collection of value-added tax or any similar tax under the laws of the Republic and such other country, or in respect of the execution of the arrangements provided for in any agreement entered into in terms of this section.
(2) As soon as may be possible after the approval by Parliament of any such agreement, as contemplated in section 231 of the Constitution, the arrangements thereby made shall be notified by publication in the Gazette and thereupon the arrangements so notified shall have effect as if enacted by this Act.
Overview of functions undertaken by International Development and Treaties
Interpretation element of the responsibilities also entails assisting with resolution of cross border tax disputes through Mutual Agreement Procedure (“MAP”), a process which is facilitated by designated competent authorities of treaty partners.
Double Taxation Agreements/Conventions (DTA/DTC)
A submission is made to the Minister of Finance to obtain approval from the Minister of Finance to negotiate the DTA.

Once approval has been obtained negotiation of the DTA is placed on a treaty work programme before negotiations can commence.

South Africa has a DTA Model which is a combination of the OECD (Organisation for Economic Co-operation and Development) Model Tax Convention and the UN (United Nations) Model Tax Convention.
Double Taxation Agreements

- The other country will provide their DTA Model.

- After the exchange of Models, the following will be studied and considered: the other countries Model, the basics of the other countries tax system, other treaties the other country has in force and signed and the reservations made by the other country in the OECD Models Tax Convention.

- The two DTA Models are merged and negotiations are conducted on the differences between the two Models.
Double Taxation Agreements

- Negotiations usually take two rounds to finalise and are hosted by each country.

- Once negotiations have been finalised and consensus has been reached with regard to the English text, the English text is initialled.

- The constitutional and legal requirements will commence.
Double Taxation Agreements

- In South Africa legal opinions must be obtained from the State Law Adviser’s of the Departments of Justice and Constitutional Development and International Relations and Co-operation.

- The State Law Adviser from the Department of Justice and Constitutional Development will scrutinise the Agreement and check for consistency with the domestic law.

- The State Law Adviser from the Department of International Relations and Co-operation will scrutinise the Agreement and check for consistency with International Law.
Double Taxation Agreements

- The legal advisors may suggest changes to the draft Agreement.

- A preliminary hearing is presented to the National Assembly Standing Committee on Finance in order to deal with any issues arising.

- The foreign language text is requested from the other country and forwarded to our National Language Service for certification.
Double Taxation Agreements

- A submission is prepared and forwarded to the Minister of Finance to obtain approval to sign the Agreement.

- President’s Minute is obtained from the Presidency (equivalent to the Instrument of Full Powers document). This gives authority to a Minister to sign the Agreement on behalf of the Government of South Africa.

- Once the Agreement is signed hearings for final ratification are presented before the Standing Committee on Finance and the Select Committee on Finance.
Once the Minutes of Proceedings from the two houses of Parliament are obtained, these Minutes of Proceedings and a Note Verbale are sent through the diplomatic channel advising our counterparts in the other country that the legal and constitutional process required to bring the Agreement into force in South Africa have been completed.

The other country will notify South Africa through the diplomatic channel once they have completed their legal and constitutional requirements to bring the Agreement into force.
Double Taxation Agreements

- On receipt of the later notification through the diplomatic channel the Agreement will enter into force in terms of the entry into force Article.

- In South Africa there is a legal requirement that the DTA must be published in our Government Gazette and the DTA becomes part of the Income Tax Act No. 58 of 1962, as amended.

- When the DTA enters into force a copy of the published DTA is placed on our website http://www.sars.gov.za/Legal/International-Treaties-Agreements/DTA-Protocols/Pages/default.aspx.
Overview of Double Taxation Agreements

Article 1: Persons covered
- Agreement applies to persons who are residents of one or both of the contracting states.

Article 2: Taxes Covered in South Africa:
- the normal tax
- the withholding tax on royalties
- the dividends tax
- the withholding tax on interest
- the tax on foreign entertainers and sportspersons
Overview of Double Taxation Agreements

Article 3: General Definitions

- person
- company
- business
- enterprise
- enterprise of a contracting state
- a contracting state
- international traffic
- competent authority
- national
- rule for undefined terms
Overview of Double Taxation Agreements

Article 4: Resident
- based on domestic law
- tie breaker rules for dual residents

Article 5: Permanent Establishment (PE)
- definition of a PE means a fixed place of business through which the business of the enterprise is wholly or partly carried on
- services based on physical presence
- dependent agents with a power to contract may be a PE
- independent agents not a PE
Overview of Double Taxation Agreements

Article 6: Income from Immovable Property

- source country has unlimited right to tax income from immovable property
- also applies to income derived from any form of use of immovable property

Article 7: Business Profits

- taxation of net profits by source country allowed to the extent that attributable to a permanent establishment therein
- limits source state taxation to profits attributable to the PE
- is concerned with transactions between parts of the same legal entity
Overview of Double Taxation Agreements

Article 8: Shipping and Air Transport
- exclusive taxation by the country where the place of effective management or residence is located

Article 9: Associated Enterprises
- is concerned with transactions between separate, but related, entities
- right to adjust transfer prices
- corresponding adjustment by other state
Overview of Double Taxation Agreements

Article 10: Dividends
- taxation by source country limited to a certain percentage (5 – 15%)

Article 11: Interest
- taxation by source country limited to a certain percentage (5 -10%)

Article 12: Royalties
- taxation by source country limited to a certain percentage (5 -10%)
Overview of Double Taxation Agreements

Article 13: Capital Gains
- taxation by source country limited to gains on immovable property, business assets of a permanent establishment and shares of property owning companies

Article 14: Income from Employment
- taxation of employment income by source country is allowed but exemption if employee is present for less than 183 days; the employer is non-resident and no PE in the source country.

Article 15: Directors’ Fees
- taxation by country of residence of company
Overview of Double Taxation Agreements

Article 16: Entertainers and Sportspersons
- taxation by source country is allowed
- look through interposed entities

Article 17: Pensions and Annuities
- Source and residence state taxation is permitted

Article 18: Government Service
- exclusive taxation by country for which the services are rendered (exception for nationals and persons who are already residents of the other state)
Overview of Double Taxation Agreements

Article 19: Students

- payments from outside country of study not taxable in the host state

Article 20: Other Income

- source state taxation allowed

Article 21: Elimination of Double Taxation

- foreign tax credits are determined in accordance with the provisions of the respective domestic tax law
Overview of Double Taxation Agreements

Article 22: Non-discrimination
- prevents tax discrimination on basis of nationality
- article applies to all taxes

Article 23: Mutual Agreement Procedure (MAP)
- DTAs have a MAP Article
- enables taxpayers to request competent authorities of two countries to engage with each other
- with a view to resolving double taxation
- does not compel agreement (endeavor to resolve)
- only deals with tax - not penalties or interest charged (these not subject to relief)
Overview of Double Taxation Agreements

Article 24: Exchange of Information (EOI)

- extends to taxes of every kind and description
- paragraph 2 includes a further alternate OECD provision which allows information received by a Contracting State to be used for other purposes when the competent authority of the supplying State authorises such use and such use is allowed under the laws of both States
- ensures that bank secrecy or the absence of a domestic tax interest can no longer be used to deny a request for exchange of information
- full exchanges are authorised – includes automatic exchanges
Overview of Double Taxation Agreements

Article 25: Assistance in the Collection of Taxes
- the two States are empowered to collect taxes on behalf of each other – assessment must be final

Article 26: Members of Diplomatic Missions and Consular Posts
- Nothing in this Agreement shall affect the fiscal privileges of members of diplomatic missions or consular posts under the general rules of international law or under special agreements
Overview of Double Taxation Agreements

Article 27: Entry into Force
- date of entry into force
- date of effect

Article 28: Termination
- fixed period of operation
- different dates of effect
Overview of Double Taxation Agreements

- Protocol at the end of the DTA is to clarify provisions in the DTA or to amend provisions of the DTA.

- Protocol amending the DTA is an integral part of the international agreement.
Protocols amending the Double Taxation Agreement/Conventions

With certain countries the DTA Article on Dividends was amended in view of the phasing out of the secondary tax on companies and its replacement with a dividends tax.

With certain countries the DTA Article on Exchange of Information (EOI) were amended in view of the global initiative to incorporate a comprehensive exchange of information Article in existing DTA.
Protocols amending the Double Taxation Agreements

- The legal and constitutional process followed for the negotiation of the Protocols follows the process outlined for the DTAs.

Tax Information Exchange Agreements (TIEAs)
Tax Information Exchange Agreements


- The legal and constitutional process followed for the TIEAs follows the process outlined for the DTAs.

- The OECD has introduced a Model TIEA on which the South African Model TIEA is based.
Tax Information Exchange Agreements

- South Africa may not wish to enter into a comprehensive DTA with a country, however, in the ongoing exercise to eliminate harmful tax practices by ensuring transparency and exchange of information between jurisdictions, South Africa will pursue the negotiation of a TIEA.

- TIEAs are mainly entered into with jurisdictions that are viewed as financial centres where there is no or minimal possibility of double taxation.

- The TIEA ensures that bank secrecy or the absence of a domestic tax interest can no longer be used to deny a request for exchange of information and allow for the exchange of information on request.
Tax Information Exchange Agreements

- When the TIEA enters into force a copy of the published TIEA is placed on our website http://www.sars.gov.za/Legal/International-Treaties-Agreements/Pages/Exchange-of-Information-Agreements-(Bilateral).aspx.
Multilateral Conventions on Mutual Administrative Assistance in Tax Matters (Multilateral MAA)
Multilateral Conventions on Mutual Administrative Assistance in Tax Matters


- The legal and constitutional process followed to become a Party to the Multilateral Conventions follows the process outlined for the DTAs.

- Multilateral MAAs allow for exchange of information on request, spontaneously or automatically. They also allow for simultaneous examinations and tax examinations abroad – in line with the provisions of a DTA.
South Africa is a Party to the Council of Europe / Organisation for Economic Co-operation and Development (OECD) Multilateral Convention for Mutual Administrative Assistance in Tax Matters.

South Africa is a signatory to the Southern African Development Community (SADC) Agreement on Assistance in Tax Matters and the African Tax Administration Forum (ATAF) Agreement on Assistance in Tax Matters.
Multilateral Conventions on Mutual Administrative Assistance in Tax Matters

Customs Mutual Administrative Assistance Agreements (CMAA)
These are Agreements that fall within the provisions of section 231(3) of the Constitution of the Republic of South Africa Act No. 108 of 1996 read with section 49 of the Customs and Excise Act No. 91 of 1964 and would need to be tabled after signature in both the National Assembly and National Council of Provinces.

These are agreements which have no extra-budgetary, financial or legislative implications.

The legal and constitutional process followed for the negotiation of the Customs agreements follow the process outlined in section 231(3) of the Constitution.
The South African model Customs agreement follows the recommendations of the World Customs Organisation.

Transgression of customs laws have a negative effect on both the economic and social spheres of a country. CMAA’s facilitate greater accuracy in the collection of customs duties, taxes and other charges.

The Agreement covers all aspects of assistance including exchange of information, technical assistance, surveillance, investigations and visits by officials. It also details how information exchanged may be used and the secrecy provisions to be adhered to.
Customs Mutual Administrative Assistance Agreements (CMAA)

- The Agreement is a vital tool in the ongoing exercise of increasing the expertise and efficiency of the customs administration in SARS.

- When the Customs MAA enters into force a copy of the published Customs MAA is placed on our website http://www.sars.gov.za/Legal/International-Treaties-Agreements/Pages/MAAs-on-Customs.aspx.
Value-Added Tax Mutual Administrative Assistance Agreements (VAT MAA)
Value-Added Tax
Mutual Administrative Assistance Agreements

- These are Agreements that fall within the provisions of section 231(2) of the Constitution of the Republic of South Africa Act No. 108 of 1996 read with section 75 of the Value-Added Tax Act No. 89 of 1991 and would need to be formally ratified after signature in both the National Assembly and National Council of Provinces.

- The legal and constitutional process followed for the negotiation of the VAT MAA closely follows the process outlined for the DTAs.
Value-Added Tax

Mutual Administrative Assistance Agreements

- It is the practice in most countries for an indirect tax, known as Value-Added Tax, to be imposed on the supply of certain goods and services. Cross-border transactions have the potential to lead to practices of tax evasion and tax avoidance across the national borders of the Contracting States which in turn will lead to budget losses and are therefore responsible for bringing about distortion of business practices and conditions of unfair competition.

- As the nature of the problem renders national measures inefficient because they do not extend beyond national borders, this Agreement provides for mutual assistance and co-operation for the prevention of fiscal evasion with respect to value-added tax between the States.
Value-Added Tax
Mutual Administrative Assistance Agreements

- These Agreements may also regulate the refund system between the two countries and allow for information exchange.

- When the VAT MAA enters into force a copy of the published VAT MAA is placed on our website http://www.sars.gov.za/Legal/International-Treaties-Agreements/Pages/MAAs-on-Value-Added-Tax.aspx.
Thank you.