University of the Witwatersrand, Johannesburg

A research report submitted to the Faculty of Commerce, Law and Management in partial fulfilment of the requirements for the degree of Master of Commerce specialising in the field of Taxation

A critical evaluation and comparative study on section 10(1)(*o*)(ii) foreign employment exemption

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Declaration

I declare that this research report is my own unaided work. It is submitted in partial fulfilment of the requirements for the degree of Master of Commerce (specialising in Taxation) at the University of the Witwatersrand, Johannesburg. It has not been submitted for any other degree or examination at any other university.

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Abstract

In 2001, South Africa changed to a residence-based system of taxation to align with international best practice and to limit the opportunities for tax arbitrage (Manuel, 2000, 36.). Section 10(1)(*o*)(ii) of the Income Tax Act 58 of 1962 (the Act) was amended to exempt foreign employment income of a resident if the resident was outside his or her country of residence for a period exceeding 183 days (National Treasury, 2000, 5). National Treasury cautioned against this exemption and in the *Explanatory Memorandum on the Revenue Laws Amendment Bill, 2000* it was stated,

> The effect of the relief measure will be monitored to determine whether certain categories of employees abuse it to earn foreign employment income without foreign taxation.

The main purpose of the exemption was to prevent double taxation from occurring, considering the limited number of double taxation agreements concluded between South Africa and other countries at the time (Mzizi, 2017, 10). The exemption created an opportunity for double non-taxation where the source country imposes little or no tax on employment income and no tax was applied in South Africa (Legwaila, 2019). Consequently, in the *Budget Review 2017*, National Treasury sought to amend the provisions of s 10(1)(*o*)(ii) as it was seen to be 'excessively generous'. At first, National Treasury proposed to repeal the exemption, however after much consultation and public comments received, National Treasury introduced a capped exemption limited to R1 million in line with the principle of fairness and progressivity (National Treasury, 2017b, 7). Subsequently, in the *2020 Budget Review*, the exemption threshold was revised upwards to R1.25 million per year from 1 March 2020 to encourage all South Africans working abroad to maintain their ties to South Africa.

In this report, the researcher investigates the qualifying requirements and implications of s 10(1)(*o*)(ii) on South African resident expatriates, their employers (local and foreign) and the South African Revenue Service (SARS).

Key words: *South African resident expatriate, local employer, foreign employer, double taxation agreement (DTA), foreign employment income, foreign employment income exemption, double taxation relief measures, Income Tax Act, s 10(1)(o)(ii), s 6quat, breaking tax residency*

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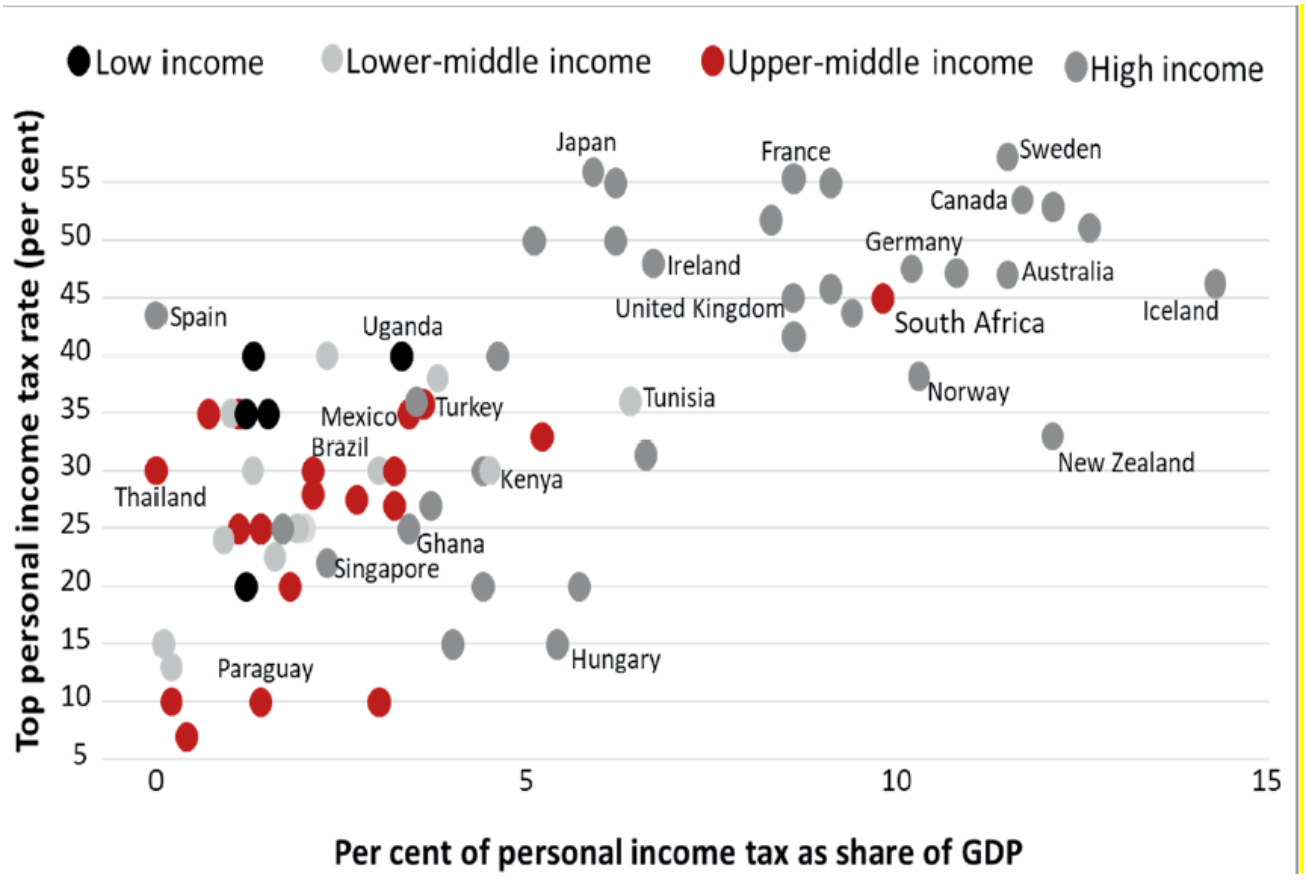
Chapter 1: Introduction

1.1 Protecting the individual tax base

In the 2021 Budget, delivered by Tito Titus Mboweni, Minister of Finance, on 24 February 2021, it was announced that the budget deficit has been revised to 14% of GDP in 2020/21 and that the country will achieve a primary surplus on the main budget in 2024/25. This is the highest budget deficit recorded by South Africa and between the 2020 budget and the 2021 budget, the consolidated budget deficit for 2020/2021 doubled. (National Treasury, 2021, 1, 34.)

South Africa has a progressive income tax system (National Treasury, 2021, 45) with marginal rates ranging from 18%-45% and has one of the highest top personal income tax rates, as shown in the graph below.



Source: Budget 2021, Budget Review, page 46

Figure 1: Per cent of personal income tax as a share of GDP

Over the past few years, personal income taxes have been revised upwards to raise more revenue to finance the annual budget. The most recent increase is the introduction of a new top rate of 45% in 2017. Personal income tax (PIT) accounts for about 38-39% of gross tax revenue and is therefore

an important source of revenue to protect. (National Treasury, 2021, v.) Protecting the individual tax base is of critical importance and this would be the reason for National Treasury to design tax policies and legislation to protect this tax base as well as to close tax loopholes (avoid circumstances of double non-taxation) and to limit opportunities for tax avoidance (Grange, da Silva, Madden, Gouws, Duffy, van Wyk and de Villiers, 2017, 2).

1.2 Tax policy - Residence-based system of taxation and amendment to s 10(1)(*o*)(ii)

Prior to 2001, South Africa applied a source-based system of taxation (National Treasury, 2000, 2). This meant all income which, therefore, 'originate[d]' in South Africa or which was 'deemed to be from a source' within South Africa was taxable in terms of the Income Tax Act 58 of 1962 (the Act) and the residence of the taxpayer was irrelevant (National Treasury, 2000, 2). The source-based system of taxation was replaced by the residence-based tax system which came into effect from the years of assessment beginning 01 January 2001 (National Treasury, 2000, 2). The tax system was changed to align with international best practice and limit the opportunities for tax arbitrage (Manuel, 2000, 19).

Residence-based taxation means that South African residents are taxed on their world-wide income, regardless of the source of that income and whether they were physically present in South Africa or not. Non-residents continue to be taxed in South Africa on income from a source within South Africa. (National Treasury, 2000, 3-4.)

The residence-based system of taxation adopted by South Africa is based on a 'residence minus' system, in line with international practice, which means residents are taxed on their world-wide income subject to certain categories of income arising from activities undertaken outside South Africa being exempt from South African tax (SARS, 2003, 1). Section 10(1)(*o*)(ii) was amended to align with international best practice to exempt foreign employment income of a resident if the resident was outside his or her country of residence for a period exceeding 183 days (National Treasury, 2000, 5).

Section 10(1)(*o*)(ii) of the Income Tax Act (prior to amendment by Act No. 74 of 2002) stated:

> 10. Exemptions. – (1) There shall be exempt from normal tax-…
> (*o*) any remuneration derived by any person-
> (i) …
> (ii) in respect of services rendered outside the Republic by such person for or on behalf of any employer, if such person was outside the Republic—
> (*aa*) for a period or periods exceeding 183 full days in aggregate during any 12 months period commencing or ending during a year of assessment; and

> (*bb*) for a continuous period exceeding 60 full days during that period of 12 months,
> and such services were rendered during such period or periods: Provided that the provisions of this subparagraph shall not apply in respect of any remuneration derived in respect of holding of any office or from services rendered for or on behalf of any employer, as contemplated in s 9(1)(e)[1].

The exemption did not apply in respect of remuneration derived from services rendered outside South Africa for any employer 'in the national or provincial spheres of government or any public entity if 80% or more of the expenses of such entity is defrayed from funds voted by Parliament[1]'(National Treasury, 2000, 5) .

1.3 Abuse of s 10(1)(*o*)(ii) and unequal treatment of South African resident taxpayers

The effect of s 10(1)(*o*)(ii) was to exempt foreign employment income received by or accrued to a South African resident from tax in South Africa subject to certain qualifying criteria, being:

- certain types of remuneration;
- in respect of employment; and
- in respect of services rendered;
- outside the Republic;
- during specified qualifying periods;
- and not subject to an exclusion.

The exemption was introduced to prevent double taxation between South Africa and the source country, given that South Africa had concluded a limited number of Double Tax Agreements (DTAs) at the time (Mzizi, 2017, 10). National Treasury, 2000a at 5 stated that:

> The effect of this relief measure will be monitored to determine whether certain categories of employees abuse it to earn foreign employment income without foreign taxation.

The exemption created an opportunity for double non-taxation where the source country imposes little or no tax on employment income and no tax was applied in South Africa (Legwaila, 2019). The exemption has also created the unequal treatment of foreign employment income between private and public sector employees (Mzizi, 2017, 10). In terms of proviso (B) of s 10(1)(*o*)(ii), public sector employees do not qualify for the foreign employment income exemption.

[1] Section 9(1)(e) referred at the time to employers in the national or provincial spheres of government or any public entity if 80% or more of the expenses of such entity is defrayed from funds voted by Parliament.

1.4 Repeal or amendment of s 10(1)(*o*)(ii)

Subject to certain conditions, if a South African resident works in a foreign country for more than 183 days a year, the foreign employment income earned was exempt from tax (National Treasury, 2017a, 138). Therefore, if a South African resident earned foreign employment income on which there was no (or very little) foreign tax payable in the source country, and the resident was outside the country for more than 183 days, that foreign employment income of the resident would benefit from double non-taxation. However, it was proposed that the foreign employment income exemption be adjusted as it was 'excessively generous' (National Treasury, 2017a, 138). To counter the double non-taxation of foreign employment income, National Treasury proposed that the foreign employment income exemption 'be adjusted' to exempt the foreign employment income if it was subject to tax in the foreign country (National Treasury, 2017a, 138).

In terms of the proposal in the Draft Taxation Laws Amendment Bill, 2017 (Draft Amendment Bill 2017), the entire exemption in terms s 10(1)(*o*)(ii) was to be repealed as opposed to merely being adjusted. As a result, all South African residents would be subject to tax on foreign employment income in respect of services performed outside of South Africa but relief in terms of double taxation may be sought in terms of DTAs or s6*quat* of the Act. (Mzizi, 2017, 10.)

The Standing Committee on Public Finance (SCOF) held public hearings on the Draft Amendment Bill 2017 and the Draft Tax Administration Laws Amendment Bill on 29 August 2017. In the meeting summary it was noted that: (Finance Standing Committee, 2017, 1-9)

> A repeal of the foreign employment exemption would result in a significant increase in compliance burden for taxpayers and administrative burden for the South African Revenue Service (SARS). Unintended consequences would include the financial implications for expatriates, emigration, capital flight and the competitiveness of South African business [PricewaterhouseCoopers submission]
>
> SARS' foreign tax mechanism was onerous. Even if one did everything correctly, taxpayers struggle two years to get their credit back. That meant a South African working overseas could be liable for paying 75% tax in South Africa and in the country where he or she is working, and then wait a considerable time for the tax credit [South African Institute of Tax Professionals submission]
>
> The standardisation of the resident basis of taxation and efforts to eliminate double non-taxation was welcome. However the current exemption was a pragmatic solution to an administratively complex alignment [South African Institute of Chartered Accountants submission]
>
> Such a significant change in policy should only be proceeded with once the full economic impact of it was properly considered and weighed against the policy reasons on the upside of this change. It

> requested for consideration on whether the proposal should be no more comprehensively weighed against international best practice as it was out of sync with the norm, and would place South Africa at a disadvantage [Tax Consulting South Africa submission]
>
> …proposing the repeal of Article 10, had resulted in predominant sense of doom and gloom for South African expatriates. A lack of clear definition of whom and how individuals would be affected by the repeal had generated confusion and fear resulting in anger and decisions being made which will not augur well for South Africa's future [South African Expatriates Tax Petition Group submission]

In response to the public comments on the proposed repeal of s 10(1)(*o*)(ii), National Treasury stated:

> The repeal on [sic] foreign employment income tax exemption was not an abnormal provision, and was applied in countries as New Zealand and the UK. It was not its intention to scare people into surrendering their passports.

After extensive consultations by National Treasury and SARS with various stakeholders, public comments and responses on the proposed repeal of s 10(1)(*o*)(ii), National Treasury issued a Draft Response Document dated 14 September 2017, that contains responses to the most pertinent issues raised by the public. The main public comments have been succinctly summarised as follows:

- 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;
- the cost of living in foreign countries is higher than in South Africa, and should be taken into account in the design of tax;
- the amendment would lead to accelerated formal emigration from South Africa or breaking South African tax residency; and
- the amendment will result in cash flow problems as the foreign tax credit (section 6*quat* of the Act) can only be claimed on assessment. (Mzizi and Botha, 2017, 4-5.)

In the *Explanatory Memorandum on the Taxation Laws Amendment Bill, 2017*, National Treasury stated that:

> It is required of policy makers to continuously ensure that the tax system espouses the principle of fairness and progressivity. Therefore, considerable attention should be given to the principle of equity which ensures that taxpayers in an equal position should be taxed in an equal manner as they have the same ability to bear the tax burden (horizontal equity), and that taxpayers with better circumstances should bear a larger part of the tax burden as a proportion of their income (vertical equity). (National Treasury, 2017b, 6-8.)

And in-line with the principle of fairness and progressivity, National Treasury further stated that:

> For this reason, it is proposed that foreign employment income earned by a resident should no longer be fully exempt as is currently provided. Tax residents who spend more than 183 days outside of South Africa rendering employment services will now only be exempted up to the first R1 million of their employment income earned abroad. (National Treasury, 2017b, 8.)

The capped exemption was introduced by National Treasury after an extensive consultation process with all stakeholders and was effective from 1 March 2020. Mzizi and Botha stated that:

> 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. (Mzizi and Botha, 2017, 4)

In the *2020 Budget Review* (p. 46), the exemption threshold was revised upwards to R1.25 million per year from 1 March 2020. National Treasury stated that the amendment was applied:

> … to encourage all South Africans working abroad to maintain their ties to the country (National Treasury, 2020, 46).

1.5 Statement of the problem

Section 10(1)(*o*)(ii) provides for an exemption for foreign employment income received for services rendered outside South Africa. An amendment to s 10(1)(*o*)(ii) of the Act was promulgated and came into effect on 1 March 2020. From 1 March 2020, if the requirements of s10(1)(*o*)(ii) are met, the exemption is limited to R1.25 million. Any remuneration received in excess of R1.25 million will be subject to income tax in South Africa, irrespective of whether tax is paid in another country (SARS, 2020a, 2). The amendment does not put an end to the unequal treatment of taxpayers as s 10(1)(*o*)(ii) still specifically excludes public sector employees under para (bb) proviso (B) of s 10(1)(o)(ii) (Mzizi and Botha, 2017, 5).

The question that arises is this: what are the qualifying requirements and implications of s 10 (1)(*o*)(ii) on South African resident expatriates, their employers (local and foreign) and the South African Revenue Service (SARS)?

This research report defines for the purposes of this report, what is meant by a South African resident expatriate and their employer (local and foreign) and then the report establishes who is eligible to claim the s 10(1)(*o*)(ii) foreign employment income exemption. The requirements to qualify for s 10(1)(*o*)(ii) are analysed and all related definitions in the Act are discussed. The researcher

investigates the implications of s 10(1)(*o*)(ii) on a South African resident expatriate's South African taxable income calculation if the foreign employment income was earned in three foreign countries, namely: the United Kingdom, Dubai, and India. The three foreign countries were selected, based on economic country conditions, that is, a developed country or a developing country and then based on whether the foreign country levies personal income tax or not. The double tax relief measures in terms of South African domestic law and any tax treaties between South Africa and the foreign country are also discussed.

The researcher investigates and describes the process for claiming the s 10(1)(*o*)(ii) exemption on an individual's income tax return from the perspective of the South African resident expatriate and the implications thereof on SARS. This includes a discussion on the responsibility of an employer (local and foreign) with respect to the employer's employees' tax obligations and the documentation required by SARS to support the South African resident expatriate's income tax return.

1.5.1 The sub-problems

Who are South African resident expatriates and their employers (local and foreign)?

What are the requirements to qualify for the s 10(1)(*o*)(ii) exemption on foreign employment income limited to R1.25 million?

What are the implications of s 10 (1)(*o*)(ii) on South African resident expatriates in relation to the following matters?

- How does a South African resident expatriate's taxable income calculation compare if the South African resident earned foreign employment income that qualifies for the s 10(1)(*o*)(ii) relief in three foreign countries considering double tax relief measures in terms of South African domestic law and any tax treaties between South Africa and the foreign country?

- What relief measures are available to a South African resident expatriate when a double tax situation arises in respect of the portion of foreign employment income earned above the R1.25 million limitation?

- What is the administrative and compliance process for a South African resident expatriate to claim the s 10(1)(*o*)(ii) exemption on their income tax return (pay-as-you-earn (PAYE) and provisional taxpayers)? What disclosures are required to be made by a South African resident expatriate to SARS and what additional documentation is required to be submitted to SARS to support a taxpayer's income tax return with a s 10(1)(*o*)(ii) exemption?

- What are the implications of s 10(1)(*o*)(ii) on the local and foreign employers of South African resident expatriates?

- What are the implications of s 10(1)(*o*)(ii) on SARS?

1.6 Research Methodology

The research is of a qualitative and interpretive nature. The sources which are analysed include the South African Income Tax Act 58 of 1962, the Explanatory Memorandum on the Taxation Laws Amendments Bill, 2017, the Taxation Laws Amendment Act, 2017, SARS Interpretation Notes, SARS Frequently Asked Questions (Foreign Employment Income Exemption), Double Taxation Agreements (DTAs) with selected foreign countries, case law, journal articles and various publications. The analysis of these sources assist with addressing the research problem and sub-problems contained within the report.

Chapter 2: Explanation of the meaning of South African resident expatriates and their employers (local and foreign)

2.1 South African tax system

Prior to 2001, South Africa applied a source-based system of taxation which meant that income was taxed in the country in which it originated, irrespective of whether it was earned by a resident or a non-resident. In the 2000 Budget Speech, the then Minister of Finance, Trevor Manuel, proposed that the tax system be changed to a residence-based system of taxation. (Manuel, 2000, 19.) As a consequence of the change to a residence-based system of taxation, the definition of gross income was amended and most of the references to 'income from a source in the Republic' were deleted (National Treasury, 2000, 3). The amendment to the definition of gross income in s 1 has the effect of taxing residents on their worldwide income (subject to certain exclusions and exemptions), regardless of the source of that income and taxing non-residents on income from a source within or deemed to be within South Africa.

2.2 Resident definition

The definition of a 'resident' in s 1 refers to a natural person as being a resident for tax purposes in South Africa either by being ordinarily resident or by physical presence. These concepts are elaborated in the subsequent sections. Physical presence only applies to natural persons who are not ordinarily resident, however if such a person leaves South Africa for a continuous period of at least 330 days, the person is deemed to be no longer resident from the first day of the 330-day period (s 1 the definition of a 'resident' proviso (B) to para (a)). If a person is a resident in terms of being ordinarily resident, then such person ceases to be a resident from the day on which the person leaves South Africa to settle in another country (proviso to the definition of a 'resident' in s 1(1)). Refer to section 4.2.4 for a discussion on change in tax residency status.

The definition of a resident in s 1(1) specifically excludes 'any person who is deemed to be exclusively a resident of another country for purposes of the application' of a double tax agreement (DTA) between that country and South Africa, even if the person is ordinarily resident or physically present in South Africa.

2.2.1 Ordinarily resident

Ordinarily resident is not defined in the Act, however South African courts have established principles in determining the country in which a natural person is ordinarily resident (SARS, 2018a, 2). Two court cases are usually cited whenever the question of residence or ordinarily resident is raised: *Cohen v CIR,* 1946 AD 174, 13 SATC 362 and *CIR v Kuttel*, 1992 (3) SA 242 (A), 54 SATC 298.

In the case of *Cohen v CIR* at 362, the following facts were applicable:

- the taxpayer, a South African resident, was requested by his company to work in the United States of America (USA)
- the taxpayer and his family lived in New York for 20 months and during this time neither the taxpayer nor his family returned to South Africa.

The court had to decide whether an individual who had been physically outside of South Africa for an entire year of assessment could be 'ordinarily resident' in South Africa (*Cohen v CIR*, 362).

In *Cohen v CIR*, Schreiner JA stated at 362 the following regarding residence or ordinary residence:

> …it seems to me that the question whether he [the taxpayer] was in that year an individual not ordinarily resident in the Union is essentially a question of degree to which no single, certain, answer could be given; the answer depends on the weight to be given to the various factors set out in the stated case.

In ruling the taxpayer was ordinarily resident in South Africa at the time, the court established three principles:

- A person's ordinary residence would be the country to which he would naturally and as a matter of course return from his wanderings and unlike other countries in which a person may live, a person's ordinary residence is the person's usual or principal residence, or the person's real home.
- Ordinary residence was not determined solely by the facts applicable to a particular year of assessment but may extend to the person's mode of life before or after the year of assessment under consideration.
- A person can be ordinarily resident in a country in a year of assessment even if that person was physically absent from that country for the entire year. (Cohen v CIR, 371-372.)

In the case of *CIR v Kuttel*, the taxpayer emigrated to the United States of America (USA) where he took up residence and was granted a permanent residence permit. The taxpayer visited South Africa and other countries but had lived and worked in the USA. The taxpayer returned to South Africa to pursue his business interests and to participate in yachting activities and stayed in his home in Cape Town which he retained as a hedge against a drop in the exchange rate. During the period under review, from September 1983 to November 1985, the taxpayer spent on average just over one third of the time in South Africa. As such, the Revenue Service taxed him as a resident. In *CIR v Kuttel*, the meaning of the words ordinarily resident were of concern. In *CIR v Kuttel,* Goldstone JA commented at 298 that, in his opinion, and agreeing with Schreiner JA's view in *Cohen v CIR*, the

meaning of ordinarily resident is narrower than resident and that an individual may have more than one residence at any one time. Goldstone JA adopted the interpretation of Schreiner JA's meaning of the words ordinarily resident, and Goldstone JA held at 298 that:

> a person is 'ordinarily resident' where he has his usual or principal residence, i.e., what may be described as his real home.

The fact that the taxpayer kept his house in Cape Town and returned to the country several times during the period under review did not change the fact that his principal residence and his real home was in the USA (CIR v Kuttel, 298-299).

In *Interpretation Note 3 (Issue 2) Resident: Definition in relation to a natural person – Ordinarily resident,* SARS has provided a list of factors which will be taken into consideration when assessing whether a natural person is ordinarily resident in South Africa. The following are a few examples that have been taken from the interpretation note:

- An intention to be ordinarily resident in the Republic
- The natural person's most fixed and settled place of residence
- The natural person's habitual abode, that is, the place where that person stays most often, and his or her present habits and mode of life
- The place of business and personal interests of the natural person and his or her family
- Employment and economic factors
- The status of the individual in the Republic and in other countries, for example, whether he or she is an immigrant and what the work permit periods and conditions are
- The location of the natural person's personal belongings
- …
- Family and social relations (for example, schools, places of worship and sports or social clubs)
- …
- …
- Periods abroad, purpose and nature of visits
- … (SARS, 2018a, 5.)

In conclusion, the facts, and circumstances of an individual need to be established and considered when determining whether an individual is ordinarily resident in South Africa and the principle of physical presence is not a prerequisite to be ordinarily resident in South Africa (SARS, 2018a, 6).

An individual who becomes ordinarily resident in South Africa will become a resident for tax purposes as from the date he/she became ordinarily resident in South Africa (SARS, 2018a, 7).

2.2.2 Physical presence

A person who is not at any time during the relevant year of assessment 'ordinarily resident' will be 'resident' if that person is physically present in South Africa for a prescribed amount of time, that is, if he meets the requirements of the physical presence test (definition of a 'resident' in s 1(1)).

The physical presence test in the definition of a resident in s 1(1) states that a person will fall within the definition of a resident if such a person was:

- not at any time during the relevant year of assessment ordinarily resident in South Africa; and
- physically present in South Africa
    - for a period or periods exceeding 91 days in aggregate during the relevant year of assessment under consideration;
    - for a period or periods exceeding 91 days in aggregate during each of the five years of assessment preceding such year of assessment under consideration; and
    - for a period or periods exceeding 915 days in aggregate during those five preceding years of assessment.

In terms of the above, a person can-

> only become a resident for tax purposes in the year after a period of five consecutive years of assessment during which the person is physically present in the Republic for a qualifying period or periods (SARS, 2018b, 4).

Therefore, a person who meets the requirements of the physical presence test is a resident from the first day of the year of assessment during which all the requirements of the test are met (SARS, 2018b, 5).

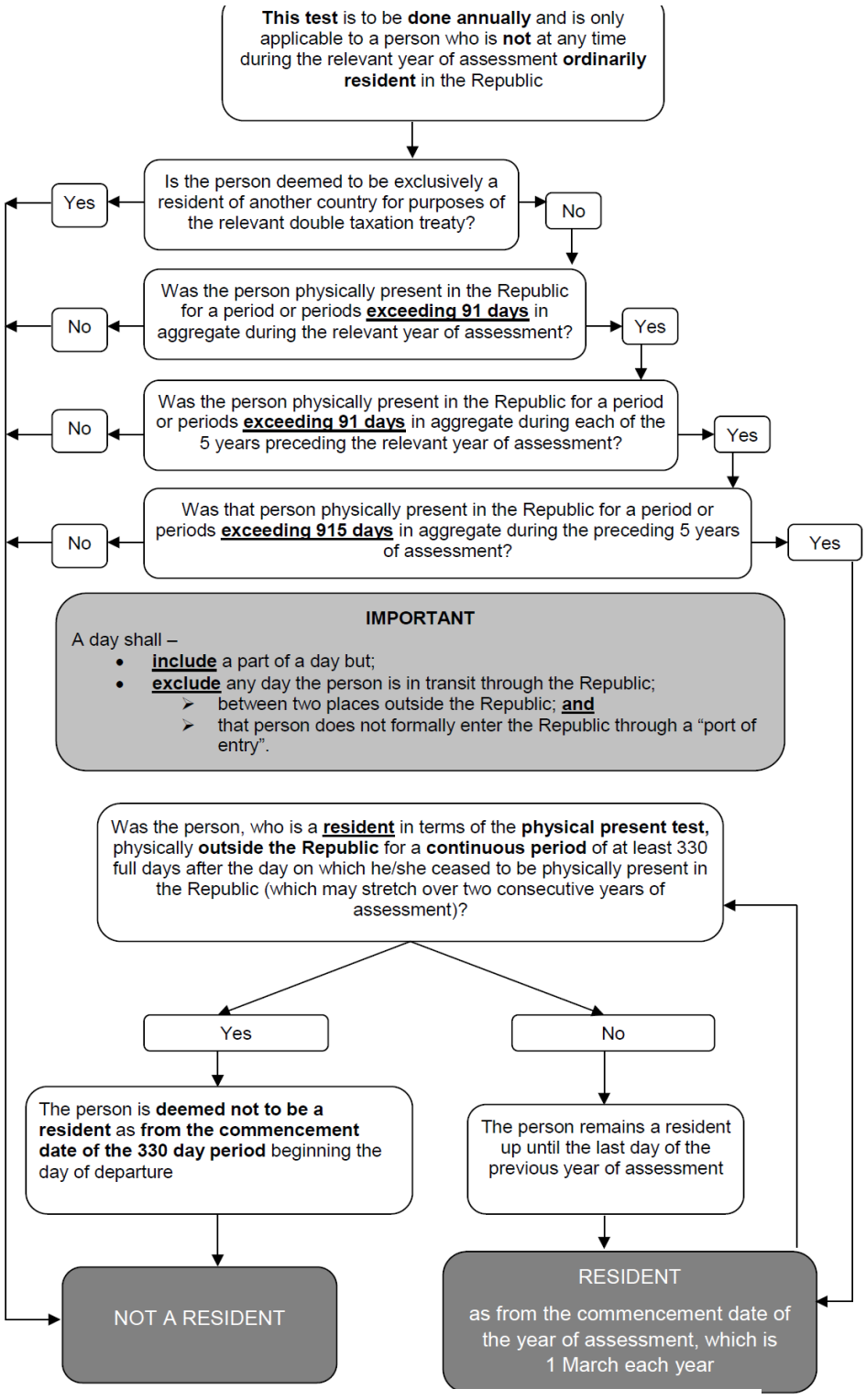
When determining the number of days in South Africa under proviso (A) to the definition of a resident 'a day shall include a part of a day'. A day begins at 00.00 and ends at 24.00 and therefore the days of arrival in and departure from South Africa are included in the count of the number of days (SARS, 2018b, 2).

An individual who is a resident by means of the physical presence test ceases to be a resident when the individual is physically outside South Africa for a continuous period of at least 330 full days (proviso (B) to the definition of a resident). That individual will no longer be a resident from the day the individual ceased to be physically present in South Africa, that is from the day following the day on which the individual left South Africa. The continuous period of 330 full days will almost certainly extend over two years of assessment as the physical presence test requires that an individual be

present in South Africa for ‘more than 91 days’ during that year to qualify as a resident. (SARS, 2018b, 6.)

The requirements for the physical presence test can be summarised in the diagram below:

Physical presence test diagram



Source: SARS (2018b:10)

Figure 2: Physical presence test diagram

2.2.3 Deemed to be exclusively tax resident in another country for purposes of the application of a DTA

The definition of a resident in s 1(1) specifically excludes 'any person who is exclusively deemed to be a resident of another country for purposes of the application' of a DTA between that country and South Africa, even if the person is ordinarily resident or physically present in South Africa. If there is a conflict between the definition of a resident in s 1(1) and a more specific definition of a resident in a DTA, the maxim *generalia specialibus non derogant*[2] applies and the more specific definition in the DTA takes precedence. (SARS, 2018b, 7-8.)

For the purposes of clarity, a DTA is an agreement between two Contracting States to eliminate, or at least minimise, double taxation by allocating taxing rights between the Contracting States. A DTA provides for a means of settling on a uniform basis the most common problems that arise in the field of international juridical taxation (OECD, 2017). Refer to section 4.2.2 for a general discussion on DTAs.

Where a person is treated as tax resident in two countries because of each country's domestic laws and those countries have a signed DTA, that person's tax residence status is determined with reference to the tie-breaker clauses, usually Article 4(2) in most DTAs (SARS, 2018b, 8). Dual tax residency may occur because of two reasons: domestic laws of countries may define resident for tax purposes in different ways and tax years may overlap (TTT Group, n.d.). According to Gouws in the University of the Witwatersrand Masters Lecture for ACCN 7022A International Tax on 19 June 2019, 'the tie-breaker clauses found in DTAs are based on fact and circumstances and a step-by-step approach is taken to determine the country of residence.'

- An individual is deemed to be resident of the state in which they have a permanent home;
- If the individual has a permanent home in both contracting states, the individual will be deemed to be a resident of the country in which their personal and economic relations are closer (centre of vital interests);
- If the state in which their centre of vital interests is closer cannot be determined and the individual has a permanent home available in both countries or in neither country, the individual will be a resident of the country in which the individual is considered to have an habitual abode. Habitual abode is considered to be the country in which the individual spends most of their time;
- Where an individual has a habitual abode in both countries, the tax residency will be determined according to their nationality;

[2] Latin **maxim** of interpretation: the provisions of a general statute must yield to those of a special one. Also known as the rule of implied exception. Source: http://www.duhaime.org/LegalDictionary/G/GeneraliaSpecialibusNonDerogant.aspx#:~:text=Latin%20maxim%20of%20interpretation%3A%20the,the%20rule%20of%20implied%20exception.

- If the individual is a national of both or neither of the contracting states, dual residency cannot be solved using the tie-breaker clauses and consequently the tax authorities of both contracting states have to mutually decide which of the two states should be allowed to tax the individual as the country of residence. (Gouws, 2019, 5.)

The 'tie breaker' clauses contained in the Article on Residence in DTA's are only referred to when there is a conflict of the definition of a resident between two contracting states in terms of their domestic laws (OECD, 2017, 106).

2.3 The meaning of a South African resident expatriate

An individual is tax resident in South Africa either by way of ordinarily resident or by way of physical presence. However, in terms of the definition of a resident in s 1(1), an individual who is deemed to be exclusively a resident of another country for purposes of a DTA is excluded from being tax resident in South Africa.

There is no definition of an expatriate in the Act, therefore the word is used in this report in its general sense. The Merriam-Webster online dictionary defines an expatriate as a person who lives in a foreign country. Often, an expatriate may live in a foreign country temporarily and for work reasons and the term 'expatriate' usually refers to: professionals or skilled workers taking positions outside their home country, either independently or sent abroad by their employers (Nash, 2017).

Section 10(1)(*o*)(ii) is being used by two groups:

> Group A: a South Africa tax resident that directly takes a job opportunity abroad with an employer in a foreign country who does not have a South African presence.
>
> Group B: a South African tax resident that is either an original South African tax resident or an international assignee that has become South African tax resident due to physical presence or due to becoming ordinarily resident. Group B are formally employed by a South African or international employer and are sent outside South Africa on assignment in countries where their employer group operates. (Grange et al., 2017)

2.4 Local and foreign employers

The exemption under s 10(1)(*o*)(ii) only applies to remuneration in respect of services rendered outside of South Africa by an employee for or on behalf of 'any employer'. The term 'employer' is defined in the Act in para(1) of the Fourth Schedule as:

> any person (excluding any person not acting as a principal, but including any person acting in a fiduciary capacity or in his capacity as a trustee in an insolvent estate, an executor or administrator of a benefit fund, pension fund, provident fund, retirement annuity fund or any other fund) who pays or is liable to pay to any

> person any amount by way of remuneration, and any person responsible for the payment of any amount by way of remuneration to any person under the provisions of any law or out of public funds (including the funds of any provincial council or any administration or undertaking of the State) or out of funds voted by Parliament or a provincial council.

The specific wording in the exemption refers to 'any employer' which means that services rendered to resident (local employer) or non-resident employers (foreign employer) could qualify for exemption (SARS, 2021c, 3). A local employer and/or a foreign employer who has a representative employer in South Africa is liable to deduct and withhold employees' tax from an employee's remuneration (para 2(1) of the Fourth Schedule). A foreign employer with no representative employer in South Africa has no employees' tax withholding obligation. The obligation to withhold employees' tax is determined by who is liable to pay the remuneration, therefore if a South African employer acts as a representative employer of a foreign employer in South Africa, the South African employer will be required to withhold employees' tax on behalf of the foreign employer. (SARS, 2020a, 12.) Employees' tax is deducted (or withheld) from an employee's remuneration each month and is paid over to SARS. The employees' tax that has been deducted is used to reduce the employee's normal tax payable and is calculated according to an employee's remuneration using the applicable rates of tax for individuals. (SARS, 2021e, 18.)

A South African resident expatriate who is employed by a foreign employer with no representative employer in South Africa is required to register as a provisional taxpayer to settle their South African tax liability (definition of 'provisional taxpayer' in para 1(1) of the Fourth Schedule). Provisional taxpayers are required to make at least two provisional tax payments during the year of assessment. The first payment shall be made within six months from the commencement of the year of assessment (for natural persons, this is 1 March) and the second payment shall not be made later than the last day of the year of assessment (for natural persons this is 28/29 February of the following year) (para 21(1)). A third additional payment may be made by provisional taxpayers to avoid or reduce paying interest in terms of s 89*quat* in respect of their tax liability for a particular year of assessment (para 23A). For natural persons who are provisional taxpayers, this payment should be made within seven months after the end of the year of assessment (s 89*quat*(1)). Provisional tax payments are based on the taxpayer's estimate of his/her taxable income for the year of assessment in question and he/she is required to complete an IRP6 return which is requested and submitted via E-filing (para 19(1)(a)).

In practice, it is often difficult to determine who is the employer of a South African resident expatriate who is assigned by a local employer to render services in a foreign country for or on behalf of the local employer's affiliate or business partner in the foreign country. The issue is further complicated if the local employer's affiliate or business partner charges the local employer for the costs of the

employee's salary and benefits. For the purposes of this report, it is assumed that the determination of who is the employer of a South African resident expatriate, either the local employer or the local employer's affiliate or business partner in the foreign country, has been correctly made.

The wording of s 10(1)(*o*)(ii) precludes independent contractors and self-employed persons from claiming the exemption as these persons do not render services for or on behalf of an employer, that is, an employment relationship does not exist (SARS, 2021c, 3). An employment relationship exists if there is a causal link between the services rendered or to be rendered and the receipt or accrual of remuneration and whether there is the required relationship between an 'employee' and an 'employer' (De Koker and Williams, 2021, 709). The term 'employee' is not defined in the main body of the Act, however s 1(1) of the Fourth schedule defines an 'employee' as:

(a) any person (other than a company) who receives any remuneration or to whom remuneration accrues;
(b) any person who receives any remuneration or to whom any remuneration accrues by reason of any services rendered by such person to or on behalf of a labour broker;
(c) any labour broker;
(d) any person or class or category of person whom the Minister of Finance by notice in the Gazette declared to be an employee for the purposes of this definition;
(e) any personal services provider definition of an employee is and hence it is given its ordinary meaning.

To supplement the definition of an employee above, the Merriam-Webster online dictionary defines an 'employee' as someone who is employed by another, usually for wages or salary, and in a position below executive level.

The main purpose of this chapter was to clarify the meaning of a South Africa resident expatriate and his/her local and/or foreign employer as these words are fundamental in the application of s 10(1)(*o*)(ii) foreign employment income exemption.

Chapter 3: Explanation of the requirements for the s 10(1)(*o*)(ii) exemption

The previous chapter explained when a natural person is considered to be tax resident in South Africa and in this chapter, the requirements of s 10(1)(*o*)(ii) are discussed.

3.1 Section 10(1)(*o*)(ii) exemption effective 1 March 2020

With effect from 1 March 2020, foreign employment income earned by a South African tax resident is no longer fully exempt as the exemption under s 10(1)(*o*)(ii) is limited to R1.25 million (National Treasury, 2020, 46). Any foreign employment income earned in excess of the R1.25 million exemption limit is subject to income tax in South Africa. It should be noted that all the requirements to qualify for the s 10(1)(*o*)(ii) exemption remained the same after the amendment. Interpretation Note no. 16, issue 4 (28 June 2021), provides a comprehensive interpretation of the requirements to qualify for the exemption under s 10(1)(*o*)(ii).

3.2 Requirements of s 10(1)(*o*)(ii)

The requirements to qualify for the s 10(1)(*o*)(ii) exemption are set out below:

- the taxpayer must earn certain types of remuneration;
- the remuneration earned by the taxpayer must be for employment services rendered by way of employment outside of South Africa;
- the services rendered outside of South Africa by the taxpayer must be during qualifying periods. (SARS, 2021c, 2.)

The exemption is not available to a South African resident expatriate if any of the exclusions in proviso(B) apply.

South Africa applies a residence-based system of taxation which means that residents are taxed on their worldwide income subject to certain exemptions and exclusions and non-residents are taxed on income from a source within or deemed to be within South Africa. Refer to chapter 2.2 for a discussion on the definition of a resident in terms of s 1(1) of the Act. In order to qualify for the s 10(1)(*o*)(ii) exemption, a taxpayer must be a tax resident of South Africa because the starting point for a resident's taxable income calculation is gross income (worldwide income) and thereafter exemptions or exclusions may apply.

3.2.1 The taxpayer must earn certain types of remuneration

Remuneration that qualifies for exemption is any salary, taxable benefit (as determined in terms of the Seventh Schedule), leave pay, wage, overtime pay, bonus, gratuity, commission, fee, emolument or allowance in terms of s 8 and any gain made from the disposal of equity shares acquired in terms

of broad-based employee share plans (s 8B) or equity instruments vesting in terms of s 8C earned in respect of services rendered outside of South Africa for or on behalf of any employer (s 10(1)(*o*)(ii)). It should be noted that the exemption does not apply to payments for the termination, loss, cancellation or variation of employment as these payments do not relate to services rendered (De Koker and Brincker, 2018, 570).

3.2.2 The remuneration earned by the taxpayer must be for employment services rendered by way of employment outside of South Africa

The wording 'in respect of services rendered…for or on behalf of any employer' implies that an employment relationship exists which is governed by a contract of employment and excludes self-employed persons and independent contractors (SARS, 2021c, 3). Generally, an employee is someone who renders services to an employer for a salary or wage subject to the control and direction of the employer (De Koker and Williams, 2021, 709). The term 'any employer' in s 10(1)(*o*)(ii) means services rendered to resident and non-resident employers (SARS, 2021c, 3). Refer to chapter 2.4 for a discussion on local and foreign employers.

The exemption only applies to remuneration for services rendered 'outside the Republic'. The 'Republic' is defined in s 1(1) and means:

> the Republic of South Africa and, when used in a geographical sense, includes the territorial sea thereof as well as any area outside the territorial sea which has been or may be designated, under international law and the laws of South Africa, as areas within which South Africa may exercise sovereign rights or jurisdiction with regard to the exploration or exploitation of natural resources.

It should be noted that the definition of the Republic includes the landmass of South Africa and its territorial waters which is a belt of sea adjacent to the landmass not exceeding 12 nautical miles (22,2 km) beyond the coastline of the country (s 4 of the Maritime Zones Act 15 of 1994).

In the instance where remuneration is earned in respect of services rendered inside and outside of South Africa an apportionment needs to be made so that only the portion of remuneration that relates to foreign services rendered is exempt in terms of s 10(1)(*o*)(ii) (SARS, 2021c, 3). The Interpretation Note no. 16, issue 4, p. 9 (28 June 2021) stipulates what SARS will accept as the correct method to calculate the exempt portion of remuneration as this differs from the calculation used for the 183-day and 60 continuous day tests.

3.2.3 The services rendered outside South Africa by the taxpayer must be during qualifying periods

A qualifying period of employment outside South Africa must be for more than 183 full days during any period of 12 months and must include a continuous period of absence of more than 60 full days during that period of 12 months (s 10(1)(*o*)(ii)(aa) and (bb)). The following shall apply when calculating the 183-day and 60 continuous days:

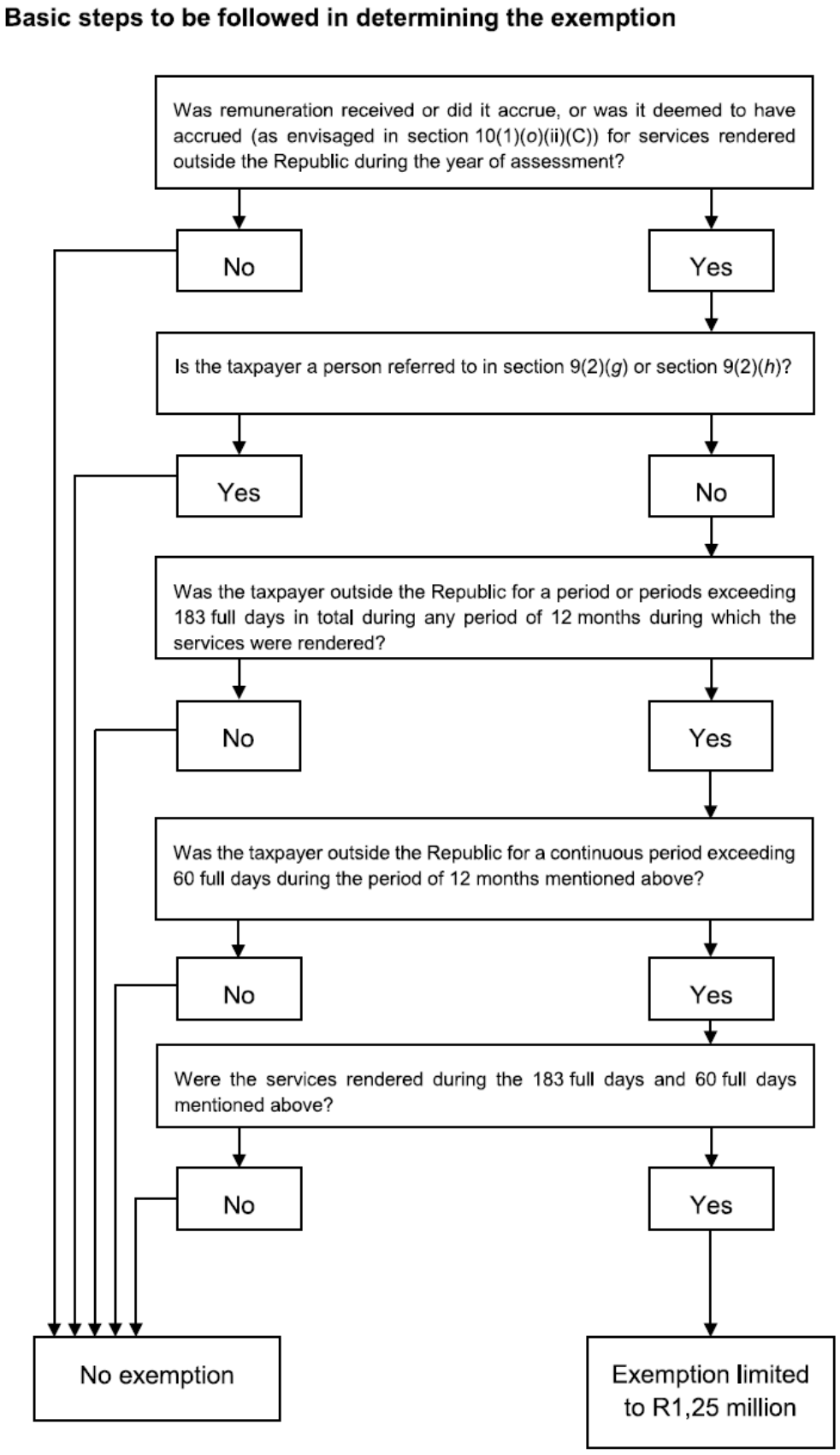
- a 'full day' means 24 hours from 00h00-24h00 and to exceed 183-days and 60-days means any amount of time over these days, for example, an hour or a minute;
- number of days in the calculation includes weekends, public holidays, vacation leave, sick leave and rest periods (if in terms of a contract of employment) as long as these days are spent outside of South Africa. Days spent outside of South Africa not in employment do not qualify for the s 10(1)(*o*)(ii) exemption;
- 'during any period of 12 months' means any period of 12 consecutive months and does not need to be a financial year, year of assessment or a calendar year. In practical terms, the requirement is to look forward and backward for a period of 12 months from any point in the tax year to determine whether the 183-day test is met. It should be noted that the 60 continuous days must fall into the same 12-month period used for the 183 day test. (SARS, 2021c, 4-7.)

3.2.4 Exclusions

The exemption specifically excludes any remuneration derived in respect of the holding of a public office contemplated in s 9(2)(*g*)[3]; or received by or accrued from services rendered to or work or labour performed outside the Republic for or on behalf of any employer contemplated in s 9(2)(*h*)[4] (proviso (B) to s 10(1)(*o*)(ii)).

SARS has prepared a flow diagram to assist a South African taxpayer to determine if he/she can claim the s 10(1)(*o*)(ii) exemption. The flow diagram has been included for summary purposes only.

[3] Section 9(2)(g) refers to a public office holder who has been appointed or is deemed to have been appointed in terms of an Act of Parliament.
[4] Section 9(2)(h) refers to employees of any employer in the national, provincial or local sphere of government of the Republic, certain constitutional institutions, national and provincial public entities listed in Schedule 2 and 3 of the Public Finance Management Act 1 of 1999 and municipal entities as defined in s 1 of the Local Government: Municipal Systems Act 32 of 2000.



Source: SARS (2021c:19)

Figure 3: Basic steps to be followed in determining the exemption

In summary, a South African resident expatriate can claim the s 10(1)(*o*)(ii) exemption if he/she satisfies all the qualifying requirements, as discussed in this chapter, which are specific and detailed. The amendment to s 10(1)(*o*)(ii) which was effective 1 March 2020 introduced a cap of R1 million, however, the cap was subsequently increased to R1.25 million but all the qualifying requirements remained the same. Consequently, a South African resident expatriate may be subject to juridical double taxation on his/her foreign employment income above R1.25 million. The various methods of relief for double taxation are discussed in Chapter 4.

Chapter 4: South African personal income tax system and double taxation relief measures

4.1 Personal income tax for South African resident expatriates

South African resident expatriates are subject to income tax on their worldwide receipts and accruals and capital gains and as such, South African resident expatriates are potentially liable for income tax and/or liable to submit an annual income tax return and hence these individuals are required to register as taxpayers with SARS and submit an annual income tax return to SARS (SARS, 2021e, 4). The South African year of assessment for natural persons covers 12 months commencing 1 March of a specific year and ends on the last day of February the following year (SARS, 2021e, 5).

A comprehensive framework is followed to determine a taxpayer's taxable income (as defined in s1(1) of the Act) and normal tax payable for any year of assessment. The framework is presented in the table below:

The framework for calculating taxable income and normal tax payable:

Table 1: Framework for calculating taxable income and normal tax payable

Description	**Rand amount**
Gross income (as defined in s 1(1))	Rxxx
Less: Exempt income (ss 10, 10A-10C and certain sections in s 12)	(xxx)
Income (as defined in s 1(1))	xxx
Less: Deductions and allowances (ss 11–19, ss 21–24P, excluding s 11F and s 18A)	(xxx)
Less: Assessed loss (ss 20-20B)	(xxx)
	xxx
Add: Other amounts included in taxable income (for example s 8(1)(a))	xxx
	xxx
Add: Taxable capital gain (s 26A)	xxx
	xxx
Less: Deductions in terms of s 11F	(xxx)
Less: Deductions in terms of s 18A	(xxx)
Taxable income (as defined in s 1(1))	xxx
Normal tax (determined in accordance with the Rates of Tax for Individuals as published by SARS	xxx
Less: Rebates and tax credits (s 6(2), s 6*quat*)	(xxx)
Normal tax payable	Rxxx

Source: Silke South African Income Tax, Chapter 2: 2.5.3

4.2 Double tax relief measures available to South African resident expatriates

Double tax arises when the same person (taxpayer) is taxed twice on the same income by more than one country and is referred to as 'juridical double taxation' (SARS, 2020b, 4). Juridical double taxation is succinctly summarised by De Koker and Brincker at 11 as follows:

> Juridical double taxation is usually the result of two or more fiscal jurisdictions claiming taxing rights in respect of the same subject-matter for the same period, and arises where comparable taxes are imposed by two or more fiscal jurisdictions, which have the same tax bases and incidence, that is to say, they impose tax on the same taxpayer in respect of the same income over the same period of time. (De Koker and Brincker, 2018, 11.)

Juridical double taxation happens in three situations, namely:

1. in residence/source conflicts, that is, the residence country taxes an individual based on the individual's tax residence irrespective of the origin of the income and the source country taxes the income based on the source of that income being located within the source country
2. in residence/residence conflicts, the residence country and source country view an individual as being a tax resident of each country and as a result the individual will be taxed in both countries on his/her same (worldwide) income
3. in source/source conflicts, two countries view the same income as having been earned from a source located in each country (De Koker and Brincker, 2018, 651-652.)

Since the introduction of the residence-based system of taxation in 2001, South African tax residents are taxed on their worldwide receipts and accruals and capital gains (the definition of 'gross income' in s 1(1)). Foreign sourced income derived by a resident may be taxed in the country of source and by South Africa (country of residence) which results in double taxation (SARS, 2020a, 6). In the instance where the source country has the right to tax, relief from double taxation is usually granted by the residence country (SARS, 2020b, 4).

The following double taxation relief mechanisms may be available to South African tax residents to avoid being double taxed on their foreign employment income:

- s 10(1)(*o*)(ii) exemption, limited to R 1.25 million
- DTAs, if in force and applicable
- Foreign tax credits in terms of s 6*quat*
- Change in tax residency status

4.2.1 Section 10(1)(o)(ii) exemption

Section 10(1)(*o*)(ii) applies to the first R1.25 million of foreign-sourced income, subject to the requirements for the exemption being met. Refer to Chapter 3 for an explanation of the requirements for s 10(1)(*o*)(ii). If a South African resident expatriate earned more than R1.25 million of foreign sourced employment income, then he/she may still be exposed to double taxation on that income. Hence the South African resident expatriate will need to look at additional options for relief of double taxation.

4.2.2 DTAs

The provisions of any DTA entered into between South Africa and a foreign country become relevant to a taxpayer's circumstances if that taxpayer is subject to international juridical double taxation, for example if a taxpayer is earning income in South Africa and a foreign country or if the taxpayer is tax resident in South Africa and only has foreign sourced income.

There are, in principle, three model conventions which countries use to negotiate and draft treaties they enter into, namely:

- the 1997 Model Double Taxation Convention on Income and Capital, published by the Organisation for Economic Co-operation and Development (OECD); and
- the 1980 United Nations Model Double Taxation Convention between Developed and Developing Countries; and
- the United States Model Income Tax Convention.

Although South Africa is not a member of the OECD, it has adopted the OECD model in many of its DTAs and hence this research report focuses on the OECD Model Tax Convention on Income and Capital. The OCED Model Tax Convention has detailed commentary to illustrate and explain the interpretation and application of the various provisions, however the commentary does not form part of any DTA. It should be noted that no country has enacted the OECD model into their domestic law and as such, the commentary cannot be binding upon the courts of contracting states. (De Koker and Brincker, 2018, 345-347.)

In the introduction to the OECD Model Tax Convention on Income and Capital, paragraph 19 states:

> For the purposes of eliminating double taxation, the Convention establishes two categories of rules. First, Articles 6 to 21 determine, with regard to different classes of income, the respective rights to tax of the State of source or situs and of the State of residence and Article 22 does the same with regard to capital. In the case of a number of items of income and capital, an exclusive right to tax is conferred on one of the Contracting States. The other Contracting State is thereby prevented from taxing those items and double taxation is

avoided. As a rule, the exclusive right to tax is conferred on the State of residence. In the case of other items of income and capital, the right to tax is not an exclusive one.

Second, insofar as these provisions confer on the State of source or situs a full or limited right to tax, the State of residence must allow relief so as to avoid double taxation; this is the purpose of Articles 23A and 23B. The Convention leaves it to the Contracting States to choose between two methods of relief, i.e. the exemption and the credit method. (OECD, 2017, 15-16.)

Paragraph 21 further states:

The following are classes of income…that may be taxed without any limitation in the State of source or situs:

remuneration in respect of an employment in the private sector, exercised in that State, unless the employee is present therein for a period not exceeding 183 days in any twelve month period commencing or ending in the fiscal year concerned and certain conditions are met. (OECD, 2017, 16.)

In terms of the above, the country of source is only given taxing rights in respect of income from employment if the employment is actually exercised in the country of source (OECD, 2017, 305). In this instance, the country of residence has the obligation to eliminate double taxation. Two methods of relief are available, namely: the exemption method and the credit method. (OECD, 2017, 17.)

Under the exemption method, income that is taxable in the country of source is exempted from tax in the country of residence (OECD, 2017, 17).

Under the credit method, income that is taxable in the country of source is also subject to tax in the country of residence, however the country of residence allows a deduction from its own tax for the taxes paid in the source country on that income limited to its own tax applicable to that income. The following formula is used to calculate the limit: South African normal tax payable on (B) x Taxable income derived from all foreign sources (A)/ Taxable income derived from all sources (B) (SARS, 2020b, 65).

The majority of the DTAs concluded by South Africa provide for the relief of double taxation under the credit method and the wording of the relevant article in the DTA, namely the elimination of double taxation, will determine how the credit method of relief must be applied (SARS, 2020b, 66). The article on the elimination of double taxation can either provide relief from double taxation under the credit method:

- without any reference to the provisions of domestic law relating to the granting of a credit for foreign taxes[5]; or

[5] Ignoring the provisions of s 6*quat*

- subject to the provisions of the law of South Africa regarding the deduction of foreign taxes from normal tax payable in South Africa[6]. (SARS, 2020b, 65-66.)

A DTA is required to be approved by Parliament before it is published in the Government Gazette and once published, s 108(2) enables the DTA to be incorporated into South African domestic law (enacted in the Income Tax Act) (du Plessis, 2015). Section 108(2) states:

> As soon as may be after the approval by Parliament of any such agreement, as contemplated in s 231 of the Constitution, the arrangements thereby made shall be notified by publication in the *Gazette* and the arrangements so notified shall thereupon have effect as if enacted in this Act.

Section 231(3) of the Constitution of the Republic of South Africa, 1996 states:

> An international agreement of a technical, administrative or executive nature, or an agreement which does not require either ratification or accession, entered into by the national executive, binds the Republic without approval by the National Assembly and the National Council of Provinces, but must be tabled in the Assembly and the Council within a reasonable time.

The status of DTAs in relation to the Act is a contentious issue and there are divergent views as to whether a DTA should override the provisions of the domestic law. Accordingly, Brinker and De Koker are of the view that the following approaches are potentially applicable:

(1) the DTA will override the domestic law in case of a conflict;
(2) in the case of conflict between the provisions of a DTA and the provisions of the Act, the conflict should be resolved by reconciling the conflicting provisions and applying the ordinary principles of statutory interpretation;
(3) to the extent that domestic law is specifically worded, it should take precedence. (De Koker and Brincker, 2018, 325.)

DTAs apply in respect of taxes covered by the relevant DTA and to persons who are residents of one or both of the Contracting States (OECD, 2017, 15). The term ‘resident’ is covered in Article 4 across all three DTAs referred to in this report, namely: the DTA between South Africa and India, the DTA between South Africa and the United Kingdom (UK) and the DTA between South Africa and the United Arab Emirates (UAE). The wording in Article 4(1) of all the three DTAs is aligned with the OECD Model Tax Convention and hence a ‘resident’ is any person who is liable for tax in one of the Contracting States by reason of domicile, residence, place of effective management or any other similar criterion (Article 4(1) of the OECD Model Tax Convention). If a person is resident in both

[6] The credit method of relief is subject to s 6*quat*

Contracting States in terms of the domestic law in each State, then the 'tie breaker' clauses in Article 4(2) are used to determine the person's residence. Refer to section 2.2.3 for a discussion on the 'tie breaker' clauses.

For the purposes of the illustrative comparative analysis in sections 5.2 and 5.3, the South African resident expatriate is tax resident in:

- South Africa and India; and
- South Africa and the UK.

According to Articles 4(2)(a) of the DTA between South Africa and India and the DTA between South Africa and the UK, the South African resident expatriate is deemed to be resident in South Africa as he has a permanent home in South Africa.

In Dubai, there is no personal tax and there is no domestic legislative definition of personal tax residence (PwC, 2021b). Based on the fact there is no personal income tax in Dubai, the South African resident expatriate residing in Dubai is only tax resident in South Africa.

4.2.3 Foreign tax credits

A South African resident who is subject to (juridical) double taxation on foreign sourced income is entitled to claim unilateral double taxation relief by way of domestic tax law (s 6*quat*). This section is used by South African residents when there is no DTA between South Africa and a foreign country or when the relief provided under s 6*quat* results in a more favourable tax position for the resident than if the DTA was used (SARS, 2020b, 66). The rebate shall be claimed on assessment when the South African resident expatriate submits his/her income tax return (Grange et al., 2017, 10).

Section 6*quat* provides for two methods of relief in the form of a rebate/credit (s 6*quat*(1)) or deduction (s 6(1C)(a)). The s 6*quat*(1) rebate is a deduction of foreign taxes payable by a resident (i.e. for the purpose of this research report, a natural person) in respect of income from foreign sources against normal tax payable and s 6*quat*(1C) is a deduction of foreign taxes payable on income derived from a source within South Africa in the calculation of the resident's taxable income (SARS, 2020b, 5). For the purpose of this research report the focus is on the tax relief provided in s 6*quat*(1) in relation to foreign employment income.

Section 6*quat*(1) states:

> Subject to subsection (2), where the taxable income of any resident during a year of assessment includes—

(*a*) any income received by or accrued to such resident from any source outside the Republic; or
(*b*) any proportional amount contemplated in section 9D; or
(*c*) …
(*d*) …
(*e*) any taxable capital gain contemplated in section 26A, from a source outside the Republic; or
(*f*) any amount—
(i) contemplated in paragraph (*a*) or (*b*) which is received by or accrued to any other person and which is deemed to have been received by or accrued to such resident in terms of section 7;
(ii) of capital gain of any other person from a source outside the Republic and which is attributed to that resident in terms of paragraph 68, 69, 70, 71, 72 or 80 of the Eighth Schedule; or
(iii) contemplated in paragraphs (*a*), (*b*) or (*e*) which represents capital of a trust, and which is included in the income of that resident in terms of section 25B(2A) or taken into account in determining the aggregate capital gain or aggregate capital loss of that resident in terms of paragraph 80(3) of the Eighth Schedule,

in determining the normal tax payable in respect of that taxable income there must be deducted a rebate determined in accordance with this section.

For the purposes of s 6*quat*(1)(a) the following definitions are relevant:

- 'resident' is defined in s 1(1);
- 'income' is defined in s 1(1), that is, gross income after deducting any amounts exempt from normal tax under Part I of Chapter II. Therefore, foreign taxes which are paid on exempt income will not qualify for a rebate under s 6*quat*(1);
- 'taxable income' is defined in s 1(1) and it is the aggregate of the following amounts:
  (a) the amount remaining after deducting from the income of any person all the amounts allowed under Part I of Chapter II to be deducted from or set off against such income; and
  (b) all amounts to be included or deemed to be included in the taxable income of any person in terms of the Act.

  Taxable income can be either a positive or negative amount. It is interesting to note that, a person with an assessed loss can potentially qualify for a rebate in terms of s 6*quat*(1) although not in that particular year. For example, if a person's taxable income is negative for a year of assessment the normal tax for that year is nil and consequently no rebate can be claimed in that year of assessment. However, paragraph (ii) of the proviso to s 6*quat*(1B)(*a*) provides for the carry-forward of excess qualifying foreign taxes to the immediately succeeding year of assessment. (SARS, 2020b, 14-15.)

- 'source' is not defined in the Act, however in the Interpretation Note 18 p.18, SARS recommends that the following should be considered when determining the source of an amount:
  - Domestic tax law in terms of s 9. The s 9 provisions-

> determine whether the amount of certain types of income and capital gains is received or accrued from a source within or outside South Africa.

Section 9 falls outside the scope of this research report as the foreign employment income exemption is only applicable to remuneration received by or accrued to an employee for services rendered outside South Africa by that employee for or on behalf an employer.

- Common law established by South African courts. The source of income has generally been defined by the courts as follows:
  - In *CIR v Lever Brothers & Unilever Ltd*, 1946 AD 441 (page 12 of 14 SATC 1), the source of income is 'the originating cause' of the income; and
  - In *Overseas Trust Corporation Ltd v CIR*, 1926 AD 444 (page 76 of 2 SATC 71), the source of income is the 'location' of that originating cause.
- The application of the articles of relevant DTAs. A DTA between South Africa and a foreign country may contain 'deemed source' rules for determining the source of certain types of income and capital gains and, in this instance, the DTA takes precedence. (SARS, 2020b, 18-20.) For example, in Article 14 of the DTA between South Africa and India, income derived by an individual from performing independent personal services will be subject to tax in his/her state of residence. However, the income may be taxed in the source state if the individual who is a resident of the other Contracting State stays in the source state for 183 days or more in any twelve-month period.

The amount of the rebate is calculated in accordance with s 6*quat*(1A) which states:

> (1A) For the purposes of subsection (1), the rebate shall be an amount equal to the sum of foreign taxes on income proved to be payable to any sphere of government of any country other than the Republic, without any right of recovery by any person (other than a right of recovery in terms of any entitlement to carry back losses arising during any year of assessment to any year of assessment prior to such year of assessment) …

In terms of the wording in s 6*quat*(1A), the foreign tax on income is required to be subject to a form of taxation similar to South Africa's domestic tax law, that is, the basis of taxation in the foreign country must be substantially similar to that under the Act. (SARS, 2020b, 26.)

The amount of foreign taxes which qualify for the rebate under s 6*quat*(1) in a particular year of assessment is the lesser of:-

- The sum of qualifying foreign taxes (s 6*quat*(1A)(*a*)(i)); or
- The amount as calculated by way of the limitation formula (s 6*quat*(1B)(a)). (SARS, 2020b, 38)

Qualifying foreign taxes are limited to foreign taxes in respect of foreign income included in a resident's taxable income and are calculated using the following formula:

> Remuneration for foreign services included in taxable income x foreign tax
> Total remuneration for foreign services
> (SARS, 2020b, 114)

The limitation is calculated as follows:

> Taxable income derived from all foreign sources (A)/ x Normal tax payable on (B)
> Taxable income derived from all sources (B)
> (SARS, 2020b, 38)

SARS defines 'Taxable income derived from all foreign sources' in Interpretation Note 18 (Issue 4) at 38 as follows:

> …all amounts of foreign source income which were included in the resident's total taxable income regardless of the rate of foreign tax (if any) to which those amounts are subject.

For example, if a South African resident expatriate earned foreign employment income and claimed a s 10(1)(*o*)(ii) exemption then only the amount of remuneration above the limitation (R1.25 million) is included in taxable income. 'Taxable income' and 'normal tax' (South African income tax) are determined according to the Act. (SARS, 2020b, 38.)

The taxable income attributable to the included income (i.e., the total taxable income from *all* (emphasis added) foreign sources) must be aggregated as must the normal tax payable on this income for the purpose of calculating the rebate. Therefore, it is evident that the rebate is calculated on a 'pooled basis' which means that the foreign tax need not link to a specific amount of income. (SARS, 2020b, 38-39.)

The limitation formula above is calculated in terms of the 'ordinary tax credit' method which avoids a refund of normal tax where the foreign qualifying taxes exceed the applicable South African normal tax on the foreign income included in the taxable income (De Koker and Brincker, 2018, 780).

The excess of foreign taxes which were not allowed in the current year of assessment as a s 6*quat*(1) rebate, may be carried forward to the next year of assessment to be set off against future South African normal tax payable on taxable income derived from foreign sources (paragraph (ii)(aa) and (bb) of the proviso to s 6*quat*(1B)(a)) and the excess amount shall not be carried forward for more than seven years (s 6*quat*(1B)(a)(iii)).

It is important to note that s 6*quat*(2) provides that where a resident has been granted relief under a DTA, the resident is not entitled to claim the rebate under s 6*quat*(1) and the deduction under s 6*quat*(1C) 'in addition' to the DTA relief. However, the rebate under s 6*quat*(1) and the deduction under s 6*quat*(1C) may be granted 'in substitution' for the relief in terms of the DTA (s 6*quat*(2)). In the instance where a resident does not elect which form of relief to apply, SARS in practice applies s 6*quat* (SARS, 2020b, 66).

Section 6*quat*(4) addresses the translation of foreign taxes into Rands and prescribes that any foreign taxes payable or proved to be payable on foreign sourced income shall be translated to Rands on the last day of that year of assessment by applying the average exchange rate for that year of assessment.

A South African resident expatriate may claim the s 6*quat* rebate on his/her annual income tax return (ITR12) or alternatively, if the South African resident is employed by a South African employer who has a responsibility to withhold PAYE, the employer may, under paragraph 10 of the Fourth Schedule of the Act, apply for a tax directive to take into account the potential foreign tax credit to determine the employee's PAYE liability on a monthly basis. The application for a tax directive can only be made if the employer has an obligation to withhold PAYE, therefore a foreign employer may not apply for this tax directive as the foreign employer has no PAYE withholding obligation. It is important to note in the instance where the employer has received a directive from SARS to take into account the potential foreign tax credit on a monthly basis when calculating the South African resident expatriate's employees' tax, the South African resident expatriate may only claim the s 6*quat* rebate on assessment when submitting his/her ITR12. (SARS, 2020a, 6, 12.) The alternative, being the application for a tax directive, may assist in reducing the negative cash flow impact placed on the South African resident expatriate.

When a South African resident expatriate is evaluating the potential application of s 6*quat,* the benefits and limitations of the section must be considered.

Benefits of applying s 6*quat* for relief of double taxation: -

- In the instance where the qualifying foreign taxes paid/payable are greater than the foreign tax credit allowed to be claimed, the excess foreign taxes may be carried forward but for a maximum of seven years (s 6*quat*(1B)(a)).
- If a taxpayer is in an assessed loss position, SARS may allow the foreign taxes paid to potentially qualify for a rebate in the immediately succeeding year of assessment (paragraph (ii)(aa) and (bb) of the proviso to s 6*quat*(1B)(a)).

- The rebate calculated under s 6*quat*(1) is on a 'pooled basis', that is, the total taxable income from all foreign sources must be aggregated across all foreign sourced income despite the country, as must the normal tax payable on this income for the purpose of calculating the rebate (SARS, 2020b, 38-39).

Limitations of applying s 6*quat* for relief of double taxation: -

- The s 6*quat* rebate only applies to qualifying foreign taxes on income. The nature of the foreign tax must be determined to ensure it is a tax on income substantially similar to South African taxes on income, for example but not limited to: normal tax on taxable income, withholding taxes on royalties (s 49B(1)) and withholding tax on interest (s 50B(1)). (SARS, 2020b, 26.)
- Foreign countries may impose taxes on employed individuals which do not qualify as income taxes (e.g., social security) and as a result, no foreign tax credit will be available in respect of these taxes, although these amounts have been paid by a South African resident expatriate (Grange et al., 2017, 10).
- A South African resident expatriate can only claim the actual s 6*quat* rebate when their ITR12 is submitted to SARS for assessment. This creates a cash flow problem for South African resident expatriates who are employed by local or foreign employers. If a South African resident expatriate is employed by a local employer, he/she may be liable for tax monthly in South Africa and the foreign country, however the local employer may apply for a directive from SARS to take into account the potential foreign tax credit to determine the South African resident expatriate's PAYE liability on a monthly basis (para 10 of the Fourth Schedule). If a South African resident is employed by a foreign employer, he/she may be liable for at least two provisional tax payments in South Africa and monthly tax in the foreign country (para 21(1) of the Fourth Schedule).
- The South African resident expatriate has to prove entitlement to a rebate under s 6*quat*(1) or a deduction under s 6*quat*(1C). Interpretation Note 18 (Issue 4) provides details of information that is generally required by SARS to prove the foreign tax has been paid in the foreign country (this may include employee's tax or tax paid on assessment). The requirement for information places a considerable administrative and compliance burden on the South African resident expatriate. (SARS, 2020b, 85-86.)
- Different countries have different years of assessment, and the challenge arises in being able to prove to SARS the tax has been paid in the foreign country as the proof of tax paid might not always be available for the South African year of assessment in which the income tax return is being submitted. For example, the UK tax year runs from 6 April to 5 April the following year, therefore, any rebate for foreign tax claimed in South Africa would be claimed in respect of the period April to February of the UK tax year. The tax paid in respect of March can only be claimed in the following year of assessment. (Grange et al., 2017, 38.)

- A further challenge arises where a South African resident expatriate earned foreign employment income in a country where payroll is the final tax and there is no assessment process. For example, in Nigeria, Nigerian tax is paid on remuneration as employee's tax withholding on a monthly basis and the only proof of tax paid is a stamped Excel spreadsheet presented at a bank in Nigeria with all the employees' names. (Grange et al., 2017, 38.)

4.2.4 Change in tax residency status

In terms of South African domestic tax law, a natural person is a resident for tax purposes either by being ordinarily resident or by physical presence (s1(1)). With effect from 1 March 2020, foreign employment income earned by a South African resident expatriate is no longer fully exempt as the exemption under s 10(1)(*o*)(ii) is limited to R1.25 million (National Treasury, 2020, 46). Consequently, South African resident expatriates earning foreign employment income in countries with little or no income tax are greatly impacted as they incur South African income tax on foreign employment income earned above the R1.25 million exemption limit. As such, these expatriates may decide to change their tax residency status and become non-resident for tax purposes in South Africa which results in them being taxed only on their South African sourced income. A South African resident expatriate who is ordinarily resident in South Africa can change his/her tax residency status in one of two ways:

- By leaving South Africa with no intention of returning to South Africa and settling permanently in another country (with or without formal emigration); or
- By becoming resident in the foreign country in which he/she works and by applying the tie-breaker clauses contained in the residence article of the applicable DTA. (Hughes and Crocker, 2018)

A South African resident expatriate who is resident by virtue of the physical presence test can change his/her residency status by being physically outside the country for at least 330 continuous days (s 1(1)).

Accordingly, when a South African resident expatriate breaks their tax residency status, a deemed disposal for capital gains tax purposes takes place and he/she is deemed to have disposed of their worldwide assets, excluding immovable property situated in South Africa, at market value the day before ceasing their tax residency (s 9H). This event could potentially give rise to a capital gain that may result in a tax liability to SARS (Hughes and Crocker, 2018). The reality of breaking tax residency is that many South Africans cannot afford to settle the 'exit charge', being the cash liability to SARS (Grange et al., 2017, 30).

A South African resident expatriate who has ceased to be tax resident in South Africa must declare their change in residency status to SARS as residency status impacts the basis on which a person is

subject to tax in South Africa and how a person's returns are assessed going forward. This can be done in two ways: (1) complete a Registration, Amendments and Verification Form (RAV01) on e-Filing or (2) capture the date the taxpayer ceased to be resident on the ITR12 tax return. (SARS, 2021a)

A South African resident expatriate may be subject to juridical double taxation on his/her foreign employment income even after the application of s 10(1)(*o*)(ii) and in this respect he/she may want to apply the provisions of a DTA or s 6*quat* for the relief of double taxation. In situations where a South African resident expatriate earns foreign employment income in a low or no tax jurisdiction, he/she may consider changing their tax residency status to avoid paying South African income tax.

Chapter 5: Implications of s 10(1)(*o*)(ii) on South African resident expatriates

This chapter presents a comparative analysis of taxable income calculations and normal tax liability for a South African resident expatriate earning foreign employment income in India, the UK and Dubai that qualifies for the s 10(1)(*o*)(ii) exemption. Each country identified has a DTA in force with South Africa. The analysis includes the impact of any other double taxation relief measures available to South African resident expatriates who after the s 10(1)(*o*)(ii) exemption are still subject to double taxation. Relief from double taxation is granted unilaterally in terms of South African domestic tax law (s 6*quat* - foreign tax rebate) and bilaterally in terms of the application of a DTA. The following three DTAs are discussed in this report:

- Agreement between the Government of the Republic of South Africa and the Government of the Republic of India for the avoidance of double taxation and the prevention of fiscal evasion with respect to taxes on income
- Convention between the Government of the Republic of South Africa and the Government of the United Kingdom of Great Britain and Northern Ireland for the avoidance of double taxation and the prevention of fiscal evasion with respect to taxes on income and on capital gains
- Agreement between the Government of the Republic of South Africa and the Government of the United Arab Emirates for the avoidance of double taxation and the prevention of fiscal evasion with respect to taxes on income

Three examples using different foreign employment income levels are used to illustrate the impact of s 10(1)(*o*)(ii) exemption on a South African resident expatriate's taxable income calculation and normal tax liability. Each example considers a South African resident expatriate who earns foreign employment income, that qualifies for the s10(1)(*o*)(ii) exemption, in India, the UK and Dubai:

- Example 1 assumes that the South African resident expatriate earns foreign employment income in the foreign country of R1 million (below the s 10(1)(*o*)(ii) exemption limit of R1.25 million)
- Example 2 assumes that the South African resident expatriate earns foreign employment income in the foreign country of R1.5 million (above the s 10(1)(*o*)(ii) exemption limit of R1.25 million)
- Example 3 assumes that the South African resident expatriate earns foreign employment income in the foreign country of R5 million

Consideration is given to any double taxation and the alternative options available to a South African resident expatriate to eliminate double taxation and this is illustrated by way of scenarios:

- Scenario 1 calculates the South African resident expatriate's taxable income and normal tax liability without applying any relief measures for double taxation across examples 1, 2 and 3 for India, the UK and Dubai
- Scenario 2 calculates the South African resident expatriate's taxable income and normal tax liability after the application of the relevant DTA for the elimination of double taxation across examples 1, 2 and 3 for India, the UK and Dubai
- Scenario 3 calculates the South African resident expatriate's taxable income and normal tax liability after the application s 6*quat* for the relief of double taxation across examples 1, 2 and 3 for India, the UK and Dubai

5.1 Comparative analysis - facts to be considered

For the purpose of scenarios 1, 2 and 3, the following facts are applicable:

- the tax year under consideration is 2020/2021 tax year;
- the taxpayer is a South African tax resident by way of ordinary residence, under the age of 65 and has a permanent home in South Africa;
- the taxpayer, a South African resident expatriate, meets all the requirements of s 10(1)(*o*)(ii) and s 6*quat* unless stated otherwise;
- the taxpayer, a South African resident expatriate, did not receive any other income or incur any tax-deductible expenses during the 2020/2021 year of assessment;
- the South African tax payable amount used in the calculation for the elimination of double taxation is after the primary rebate (2021: R14 958) under s 6(2) ((SARS, 2020b, 68);
- the SARS average exchange rates for the 2021 year of assessment is used to convert the foreign employment income earned in India, the UK and Dubai for examples 1,2 and 3.
- the taxpayer renders employment services in:
    (1) India for an Indian employer and the taxpayer is present in India for more than 183 days. In terms of the domestic tax law in India, the taxpayer is considered tax resident in India because of being physically present in India for a period of 182 days or more in the tax year (PwC, 2021a).
    (2) the UK, for a UK employer and the taxpayer is present in the UK for more than 183 days. In terms of domestic tax law in the UK, the taxpayer is considered tax resident in the UK (based on the Automatic UK Residence Test as the taxpayer spends more than 183 days in the UK in the relevant tax year) (PwC, 2021c).
    (3) Dubai for a Dubai employer and the taxpayer is present in Dubai for more than 183 days. In Dubai, there is no domestic legislative definition of personal tax residence (PwC, 2021b) and hence the issue about dual residence is not applicable.

Based on the facts presented in (1), (2) and (3) above, the South African resident expatriate is tax resident in South Africa, India, and the UK and hence the 'tie breaker' clauses in Article 4(2) of the relevant DTAs between South Africa and India and South Africa and the UK must be applied to determine in which country the individual is exclusively tax resident. In terms of the 'tie breaker' clauses in Article 4(2) that have been discussed in section 2.2.3, the South African resident expatriate is deemed to be exclusively tax resident in South Africa as his permanent home is in South Africa (Article 4(2)(a)).

- In terms of the relevant DTAs in this report, the following Articles are applicable:
  (1) Article 1 Persons Covered – this Article is standard across all three DTAs and provides that a DTA is applicable to persons (Article 3 of the relevant DTAs defines a person as an individual, company and any other body of persons that is treated as an entity for tax purposes) who are residents of one or both Contracting States.
  (2) Article 2 Taxes covered:
    - the DTA between South Africa and India covers Indian income tax (including any surcharge thereon) and South African income tax and secondary tax on companies (Article 2(1)(a))
    - the DTA between South Africa and the UK covers taxes on income and capital gains imposed on behalf of the relevant tax authorities (Article 2(1) and (2)) and in the case of the UK, the taxes include income tax, corporation tax and capital gains tax (Article 2(3)(b))
    - the DTA between South Africa and Dubai covers taxes on income imposed on behalf of the relevant tax authorities (Article 2(1) and (2)) and in the case of Dubai, the taxes include income tax and corporation tax (Article 2(3)(a))
  (3) Article 15[7] or Article 14[8] which deals with income from employment. The contents of this Article are similar across the relevant DTAs and hence, for simplicity purposes, only Article 15 of the DTA between South Africa and India is discussed.
  Article 15(1) of the DTA between South Africa and India refers to Dependent Personal Services and states:

> Subject to the provisions of article 16,18 and 19, salaries, wages and other similar remuneration derived by a resident of a Contracting State in respect of an employment shall be taxable only in that State unless the employment is exercised in the other Contracting State. If the employment is so exercised, such remuneration as is derived therefrom may be taxed in that other State.

[7] Refers to Dependent Personal Services in the DTA between South Africa and India
[8] Refers to Income from Employment in the DTAs between South Africa and the UK and South Africa and Dubai

The foreign employment income earned by the South African resident expatriate was not earned as a director (Article 16), as a pension (Article 18) or in respect of government service (Article 19). As such, Article 15(1) applies.

OECD states the following applies when interpreting Article 15(1), (this is not an exhaustive list):

- …the general rule as to the taxation of income from employment (other than pensions), namely, that such income is taxable in the State where the employment is actually exercised.
- Employment is exercised in the place where the employee is physically present when performing the activities for which the employment income is paid.
- …'salaries, wages and other similar remuneration' include benefits in kind received in respect of an employment (e.g. stock-options, the use of residence or automobile, health or life insurance coverage and club memberships). (OECD, 2017, 305.)

As discussed earlier in this chapter, the South African resident expatriate renders employment services in India, the UK and Dubai and therefore, the foreign employment income is taxable in those countries (source states). However, the taxing right of the source state may be limited by Article 15(2), which states:

> Notwithstanding the provisions of paragraph 1, remuneration derived by a resident of a Contracting State in respect of an employment exercised in the other Contracting State shall be taxable only in the first-mentioned State if:
>
> a. the recipient is present in the other State for a period or periods not exceeding in the aggregate 183 days in any twelve-month period commencing or ending in the fiscal year concerned; and
> b. the remuneration is paid on or on behalf of an employer who is not resident of the other State; and
> c. the remuneration is not borne by a permanent business establishment or a fixed base which the employer has in the other State.

It should be noted that the three conditions contained in Article 15(2) must all be satisfied for the remuneration to not be subject to tax in the source state to qualify for exemption. Based on the facts presented above, the foreign employment income earned by the South African resident expatriate while working in India, the UK and Dubai is subject to tax in the source state.

The South African resident expatriate's employer in India or the UK is required to withhold the relevant tax from the employment income paid to the employee (PwC,

2021a, PwC, 2021c). There is no requirement of this nature in Dubai because there is no personal income tax. Consequently, the South African resident expatriate is liable for income tax in both South Africa (based on the residence basis of taxation) and the foreign country (being India and the UK) which results in the foreign employment income being subject to double taxation.

The analysis of scenarios 1,2 and 3 for each country is presented in sections 5.2, 5.3 and 5.4. The countries are discussed in the following order: India, the UK and Dubai. Each country section begins with an overview of the country's individual tax system and the taxable income calculations and normal tax liability calculations for examples 1,2 and 3 follow in a table. Section 5.5 consolidates all the separate countries' tables and concluding comments are presented.

5.2 Foreign employment income earned in India

5.2.1 Overview of the individual tax system in India

The Indian tax year runs from 1 April to 31 March and individuals are required to file their tax returns by 31 July immediately following the end of the relevant tax year. Individuals are liable to pay taxes in India based on residential status in the relevant tax year. (PwC, 2021a) An individual can be classified as being:

- Resident and ordinarily resident – subject to tax in India on their worldwide income;
- Resident but not ordinarily resident – subject to tax in India on income sourced in India or from a business controlled in or a profession set up in India; and
- Non-resident in India – subject to tax in India on income sourced in India. (PwC, 2021a)

An individual is resident in the tax year if he/she is:

- physically present in India for a period of 182 days or more in the tax year; or
- physically present in India for a period of 60 days or more during the relevant tax year and 365 days or more in aggregate in four preceding tax years. (PwC, 2021a)

If neither of the above two conditions are met, the individual is non-resident in the current tax year (PwC, 2021a).

A resident individual is treated as being resident but not ordinarily resident if the following conditions apply:

- the individual has been non-resident in nine out of ten tax years preceding the current tax year; or
- the individual's physical presence in India is less than 729 days during the seven tax years preceding the current tax year. (PwC, 2021a)

On the basis of the facts in section 5.1, the South African resident expatriate renders employment services in India and is present in the country for more than 183 days. Based on the definition of a resident in terms of Indian domestic law, the South African resident expatriate is resident in India. Therefore, the South African resident expatriate is resident in both South Africa and India. In terms of the 'tie breaker' clauses in Article 4(2) of the DTA between South Africa and India, which have been discussed in section 2.2.3, the South African resident expatriate is deemed to be exclusively tax resident in South Africa as his permanent home is in South Africa (Article 4(2)(a)). As such, the South African resident expatriate is viewed as being non-resident in India and is therefore subject to tax in India on income sourced in India.

India taxes individuals, irrespective of residential status, at marginal tax rates. The tax table for the Indian 2020/2021 tax year is as follows:

Table 2: Tax table for Indian 2020/2021 tax year

Taxable income[9]			
From (INR)	**To (INR)**	**Basic tax (INR)**	**% on excess**
0	250 000	0	0%
250 001	500 000	0	5% over INR 250 000
500 001	1 000 000	12 500	20% over INR 500 000
Above 1 000 000	-	112 500	30% over INR1 000 000

Source: PwC Worldwide Tax Summaries: Territory India (https://taxsummaries.pwc.com/india/individual/taxes-on-personal-income)

A new optional tax regime came into effect on 1 April 2020 for individuals and offers lower tax rates spread across six income levels, however this new tax regime does not allow for any exemptions or deductions when calculating an individual's taxable income (PwC, 2021a). For the purpose of this research the optional tax regime is ignored.

Salaried employees in India are paid net of a withholding tax which is calculated based on an employee's gross salary adjusted for perquisites (defined as any casual emolument or benefit attached to an office or position in addition to salary or wages[10]), exemptions and allowances (Iyer, 2018). In the case where the amount of tax withheld at source is less than the actual tax liability, an individual is liable to pay advance/self-assessment tax (KPMG, 2021).

[9] The official currency of India is the Indian Rupee (INR)
[10] The India Income Tax Act, 1961 s 17(2)

5.2.2 Illustrative analysis

The foreign employment income earned in example 1, 2 and 3 is converted to Indian Rupees using the SARS average exchange rate for the year of assessment ending 28 February 2021 of R0.2217 (SARS, 2021d) and is equivalent to:

Table 3: Examples converted to Indian rupees

All amounts rounded to nearest whole number	**Rand salary**	**Exchange rate**	**INR salary (converted)**
Example 1	R 1 000 000	R 0.2217	INR 4 510 600
Example 2	R1 500 000	R 0.2217	INR 6 765 900
Example 3	R5 000 000	R 0.2217	INR 22 553 000

Using the tax calculator provided on the Indian Income Tax Department website[11], the Indian income tax liability on foreign employment income earned in India for example 1, 2 and 3 is:

Table 4: Indian tax comparison for examples

All amounts rounded to nearest whole number	**INR salary (converted)**	**INR tax[12]**	**Exchange rate**	**Rand tax (converted)**
Example 1	INR 4 510 600	INR 1 165 680	R 0.2217	R258 431
Example 2	INR 6 765 900	INR 2 026 497	R 0.2217	R449 274
Example 3	INR 22 553 000	INR 8 223 000	R 0.2217	R1 823 039

Using the information contained in the tables above, the South African taxable income and normal tax liability is calculated for scenario 1, 2 and 3.

[11] Source: Indian Income Tax Department: https://www.incometaxindia.gov.in/pages/tools/tax-calculator.aspx

[12] INR tax excludes the Health and Education cess which is defined as an additional levy by the government with the aim of addressing the education and healthcare needs of rural families in India Sharma, A. K. 2020. *Why do you have to pay health and education cess?* [Online]. Available: https://www.livemint.com/money/personal-finance/why-do-you-have-to-pay-health-and-education-cess-11579710581856.html [Accessed 11 January 2022].

Table 5: South African taxable income and normal tax liability for examples

Scenario 1 – South African taxable income calculation and normal tax liability For remuneration earned in India (all amounts have been rounded to the nearest rand)	**Example 1 Salary of R1 million**	**Example 2 Salary of R1.5 million**	**Example 3 Salary of R5 million**
	Rands (R)	**Rands (R)**	**Rands (R)**
Gross income			
Foreign employment income sourced in India	1 000 000	1 500 000	5 000 000
Less: exempt income s 10(1)(*o*)(ii) exemption limited to R1 250 000	(1 000 000)	(1 250 000)	(1 250 000)
Income	0	250 000	3 750 000
Taxable Income	**0**	**250 000**	**3 750 000**
Normal tax liability	0	48 528[13]	1 537 179[14]
Less: Primary rebate – s 6(2)	-	(14 958)	(14 958)
South African tax liability (before double tax relief)	**0**	**33 570**	**1 522 221**

Analysis of scenario 1 – South African taxable income and normal tax liability before double tax relief

In example 1, the South African resident expatriate is not liable for any South African tax because the foreign employment income earned in India was below the s 10(1)(*o*)(ii) exemption limit of R1.25 million. As such there is no instance of double tax and hence there was no requirement to consider the DTA between South Africa and India and s 6*quat.* However, in example 2 and 3 the South African resident is liable for South African tax on the portion of foreign employment income above the exemption limit of R1.25 million and consequently the South African resident expatriate is taxed twice on a portion of the foreign employment income earned in India. For example 2 and 3, the South African resident expatriate has two options for the elimination of double taxation, namely, the application of the DTA between South Africa and India or s 6*quat* (SARS, 2020b, 66).

Scenarios 2 and 3 examine the relief of double taxation by application of the DTA between South Africa and India and application of s 6*quat* respectively.

[13] = [R37 062 + (R250 000 taxable income – R205 900 per tax table) x 26%]
[14] = [R559 464 + (R3 750 000 taxable income – R1 577 300 per tax table) x 45%]

Analysis of scenario 2 – South African taxable income and normal tax liability after the elimination of double tax by way of DTA

In examples 2 and 3, the South African tax liability before any double tax relief is R33 570 and R1 522 221 respectively and the South African resident expatriate is subject to double taxation on the foreign employment income above the s 10(1)(*o*)(ii) exemption limit.

In terms of s 6*quat*(2), a taxpayer resident in South Africa may elect to apply the tax treaty credit method of relief instead of the s 6*quat* rebate method of relief and if so decides, none of the provisions of s 6*quat* will apply (for example, the taxpayer is not allowed to carry forward any excess foreign taxes under paragraph (ii) of the proviso to s 6*quat*(1B)(a)) (SARS, 2020b, 66). In scenario 2, the South African resident expatriate elects under s 6*quat*(2) to use the DTA relief for the elimination of double taxation.

Article 22 of the DTA between South Africa and India refers to the Elimination of Double taxation and states:

> Double taxation shall be eliminated as follows:
>
> a. …
> b. In South Africa, Indian tax paid by residents of South Africa in respect of income taxable in India, in accordance with the provisions of the Agreement, shall be deducted from the taxes due according to South African fiscal law. Such deduction shall not, however, exceed an amount which bears to the total South African tax payable the same ratio as the income concerned bears to the total income.

According to Article 22(b) of the DTA between South Africa and India, the South Africa resident expatriate is entitled to claim double taxation relief for the 2020/2021 tax year, but the relief is limited to the South African tax payable in the same ratio as the foreign taxable income bears to the total taxable income (the maximum deduction). The maximum deduction is limited to: the total South African tax payable x Taxable income concerned[15]/ Total taxable income and is calculated on a 'per country' basis (SARS, 2020b, 67-68).

[15] Taxable income concerned refers to taxable income in respect of the income which is taxed in South Africa and is also taxed, in accordance with the provisions of the tax treaty in the other country (SARS, 2020b, 67-69)

Most of the South African DTAs provide for the elimination of double taxation under the 'ordinary credit' method (SARS, 2020b, 66) and Article 22(b) is an example of this credit principle. As stated by De Koker and Brincker (2018):

> …the ordinary credit method of limitation is designed to prevent a refund of normal tax in cases where the foreign qualifying taxes exceed the attributable South African normal tax on the foreign income in respect of which the foreign tax was suffered. (De Koker and Brincker, 2018, 780)

Therefore, the elimination of double tax is the lesser of the maximum deduction under the DTA in terms of Article 22(b) (Calculation (a)) and the proportional share of foreign tax paid on the amount included in taxable income (Calculation (b)).

Table 6: Scenario 2

Scenario 2 - South African taxable income calculation and normal tax liability after the application of the DTA between South Africa and India **For remuneration earned in India** (all amounts have been rounded to the nearest Rand)	**Example 2** **Salary of** **R1.5 million**	**Example 3** **Salary of** **R5 million**
	Rands (R)	**Rands (R)**
Taxable income	250 000	3 750 000
South African tax liability (before double tax relief)	33 570	1 522 221
Application of the DTA between South Africa and India – Article 22(b) Elimination of double taxation The elimination of double tax is the lesser of calculation (a) and (b): Calculation (a)[16,17] The South African tax payable on the income included in taxable income - (Taxable) Income concerned x South African tax payable Total (taxable) income Calculation (b)[18,19] The proportional share of foreign tax paid on the amount included in taxable income	(33 570) 33 570 74 879	(1 367 279) 1 522 221 1 367 279
South African tax liability based on the application of the DTA	**0**	**154 942**

[16] Example 2 = R250 000 (R1 500 000- R1 250 000)/ R250 000 x R33 570 = R 33 570
[17] Example 3 = R3 750 000 (R5 000 000- R1 250 000)/ R3 750 000 x R1 522 221 = R 1 522 221
[18] Example 2 = (R250 000/R1 500 000) x R449 274 = R 74 879
[19] Example 3 = (R3 750 000/R5 000 000) x R1 823 029 = R 1 823 029 = R 1 367 279

In example 2, there is no South African tax payable after the application of Article 22(b) and the excess foreign tax, being R41 309 (R74 879 – R33 570), 'is forfeited, since it is not refundable and may not be carried forward to the immediately succeeding year of assessment' (SARS, 2020b, 69).

In example 3, the maximum deduction under the DTA is R 1 522 221, however this amount exceeds the foreign tax paid on the foreign employment income included in taxable income of R 1 367 279 and hence the deduction is the lesser of the two amounts. Therefore, the South African resident expatriate is liable for South African tax of R154 942 after the application of Article 22(b).

Analysis of scenario 3 – South African taxable income and normal tax liability after the application of s 6quat(1) for the elimination of double tax

In example 2 and 3, the South African tax liability before any double tax relief is R33 570 and R1 522 221 respectively, and the South African resident expatriate is subject to double taxation on the foreign employment income above the s 10(1)(*o*)(ii) exemption limit.

In terms of s 6*quat*(2), the South African resident expatriate elects the relief of double tax provided for under s 6*quat*(1). The amount of foreign taxes that qualify for a rebate under s 6*quat*(1) are limited to foreign taxes in respect of foreign income included in a resident's taxable income. Foreign taxes in respect of the exempt foreign income of R1.25 million do not qualify for the rebate under s 6*quat*(1) and are not carried forward to subsequent years of assessment. (SARS, 2020b, 36.)

The amount of foreign taxes that qualify for a rebate under s 6*quat*(1A) is calculated as follows:

$$\frac{\text{Remuneration for foreign services included in taxable income}}{\text{Total remuneration for foreign services}} \times \text{foreign tax}$$

(SARS, 2020b, 114)

The s 6*quat* rebate is limited to the South African tax payable on the foreign employment income included in taxable income and is calculated in terms of s 6*quat*(1B)(a) as follows:

$$\frac{\text{Taxable income derived from foreign sources}}{\text{Total taxable income derived from all sources}} \times \text{South African tax payable}$$

(SARS, 2020b, 114)

Table 7: Scenario 3

Scenario 3 - South African taxable income calculation and normal tax liability after the application of s 6*quat* For remuneration earned in India (all amounts have been rounded to the nearest Rand)	**Example 2 Salary of R1.5 million**	**Example 3 Salary of R5 million**
	Rands (R)	**Rands (R)**
Taxable income	250 000	3 750 000
South African tax liability (before double tax relief)	33 570	1 522 221
Application of s 6*quat*(1) to eliminate double taxation The amount of foreign taxes that qualify for a rebate under s 6*quat*(1A) is calculated as follows[20,21]: Remuneration for foreign services included in taxable income x foreign tax Total remuneration for foreign services Limitation of the rebate under s 6*quat*(1B)(a) is calculated as follows[22,23]: Taxable income derived from foreign sources x South African tax payable Total taxable income derived from all sources	(33 570) 74 879 33 570	(1 367 279) 1 367 279 1 522 221
South African tax liability based on the s 6*quat* rebate	**0**	**154 942**

In example 2, there is no South African tax payable after the application s 6*quat*. The amount of foreign taxes that qualify for a rebate under s 6*quat*(1A) is R74 879 exceeds the rebate under s 6*quat*(1B)(a) of R33 570. Under paragraph (ii)(aa) of the proviso to s 6*quat*(1B)(a), the balance of foreign tax of R41 309 (R74 879 – R33 570) is carried forward to the 2022 year of assessment and will potentially qualify as a foreign tax for set-off against South African normal tax payable on taxable income derived from foreign sources.

In example 3, the s 6*quat* rebate calculated under s 6*quat*(1A) of R1 522 221 exceeds the amount of foreign taxes that qualify for a rebate under s 6*quat*(1A) of R1 367 279. The reason is the effective tax rate in South Africa (based on the foreign employment exemption of R1.25 million and the marginal tax rates) is higher than the same in India. The s 6*quat* rebate is R 1367 279 which results in the South African expatriate being liable for South African tax of R154 942.

[20] Example 2 = R250 000 (R1 500 000-R1 250 000)/1 500 000 x R449 274 = R74 879

[21] Example 3 = R3 750 000 (R5 000 000-R1 250 000)/5 000 000 x R1 823 039 = R1 367 279

[22] Example 2 = R250 000 (R1 500 000-R1 250 000)/250 000 x R33 570 = R33 570

[23] Example 3 = R3 750 000 (R5 000 000- R1 250 000)/ R3 750 000 x R1 522 221= R1 522 221

Conclusion:
In terms of scenario 2 and 3 for example 2, the South African resident expatriate will have a Rnil tax liability for the current year, however he/she will be financially better off selecting the double tax relief provided for under s 6*quat* rather than the DTA relief because the excess foreign taxes can be carried forward to the following year of assessment.

In terms of scenario 2 and 3, for example 3, the South African resident expatriate will be in the same tax position if either double tax relief method was chosen as the South African tax payable in scenario 2 and 3 is R154 942. In the instance of the South African resident expatriate earning foreign sourced employment income in more than one country, SARS states:

> …it would not be to the taxpayer's advantage to elect that the tax treaty method of relief apply, since the amount determined under section 6quat is potentially further limited under a per country limitation calculation as required under the tax treaty. (SARS, 2020b, 70)

The South African resident expatriate should evaluate the administrative and compliance advantages and disadvantages of each method before deciding which relief method should be pursued. The nature of this evaluation is beyond the scope of this report.

5.3 Foreign employment income earned in the UK

5.3.1 Overview of the individual tax system in the UK

The UK tax year runs from 6 April to 5 April the following year and individuals are required to file their tax returns by 31 January (online) or 31 October (if a paper return is filed) following the end of the tax year. Individuals are liable to pay taxes in the UK, based on residential status in the UK. A resident who is domiciled in the UK is taxed on their worldwide income and capital gains; a non-resident is taxed on UK sourced income and capital gains in respect of UK property. (PwC, 2021c) Effective 6 April 2017, a resident who is not domiciled (and not deemed domiciled) in the UK, can elect for the remittance basis of taxation. The election allows the resident to be taxed on their non-UK investment income and capital gains only if these amounts are remitted to the UK (PwC, 2021c). The remittance basis of taxation is beyond the scope of this report.

An individual's residence status is determined with reference to the Statutory Residence Test which is made up of the following (PwC, 2021c):

- Automatic overseas test;
- Automatic UK tests; and
- A sufficient ties test.

An individual will be non-UK resident if one of the three automatic overseas tests apply.

Automatic overseas tests (excludes the automatic overseas tests when an individual dies during the relevant tax year) as stated by PwC:

- If the individual was UK resident in one or more of the three prior tax years and the individual spent less than 16 days in the UK in the year in question.
- If the individual was not UK resident in any of the three prior tax years and the individual spent less than 46 days in the UK in the year in question.
- If the individual works full-time overseas in the year in question, they spend less than 31 days working in the UK, and they spend less than 91 days in the UK; where a UK workday is a day on which an individual works more than 3 hours in the UK. (PwC, 2021c)

Automatic UK residence tests:

If an individual has not met any of the Automatic overseas tests, then he/she must consider the Automatic UK residence tests. An individual will be UK resident for the relevant tax year if he/she meet at least one of the three automatic UK residence tests.

(1) The individual spends at least 183 days in the UK in the tax year.

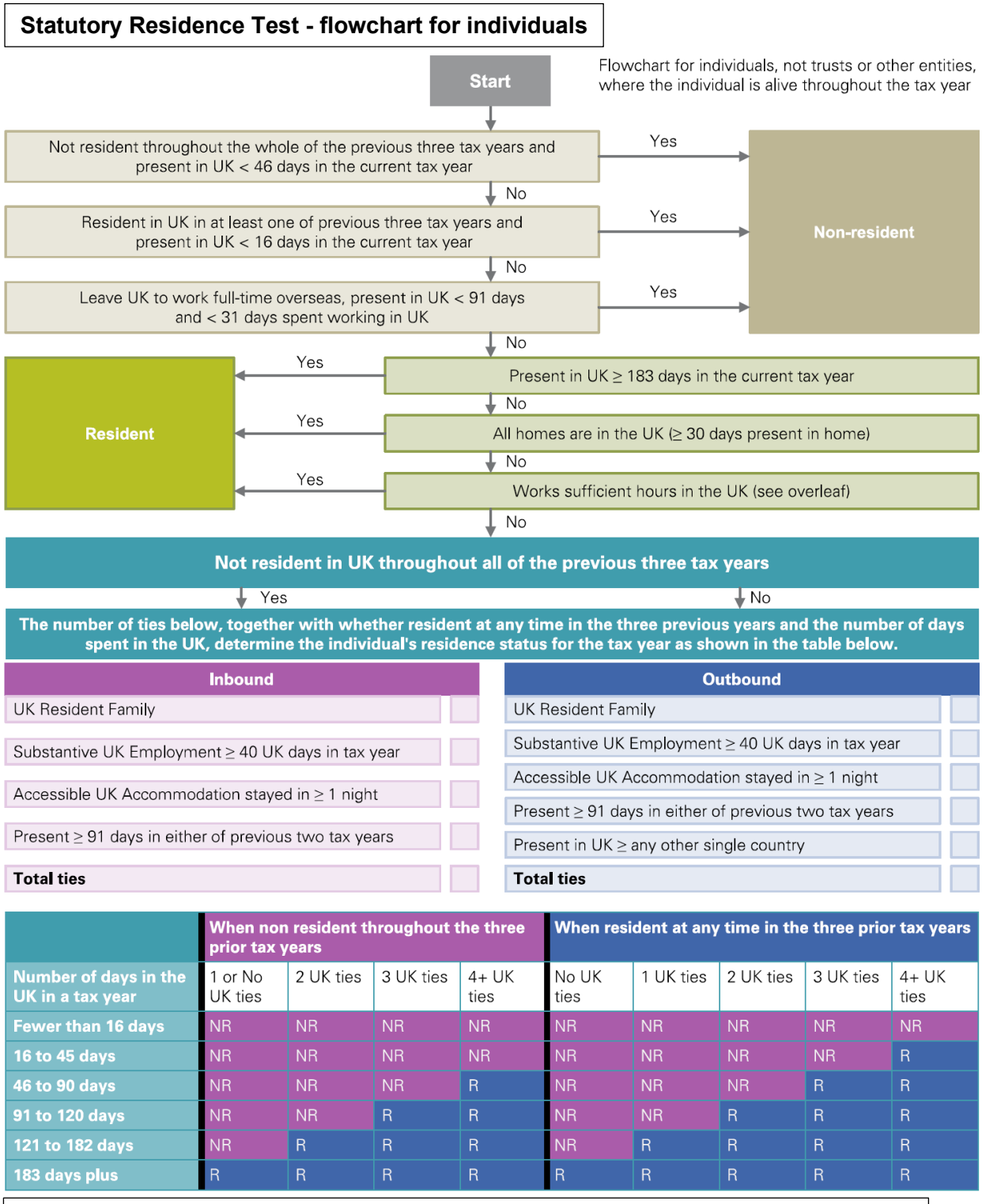
(2) The individual has a home in the UK which is available for at least 91 consecutive days and the home is actually used by the individual for at least 30 days in the tax year.

(3) The individual works full-time in the UK for a period of 365 days, part of which falls in the tax year (full-time work is considered on average 35 hours or more per week). (PwC, 2021c)

If there is no conclusive result about the individual's residence from applying the automatic overseas tests and the automatic UK residence tests, then the 'sufficient ties test' is used to determine the individual's residence status. PwC explains that:

> The ties are effectively connections with the United Kingdom involving family, accommodation, work, 90-days spent in the United Kingdom in previous tax years, or if the United Kingdom is the country in which an individual spends most of their time.
>
> …The more days an individual spends in the United Kingdom, the fewer United Kingdom ties are needed for them to pass the sufficient ties test and be UK resident. (PwC, 2021c)

The following is a flowchart, published by KPMG in the UK, to summarise how the Statutory Residence Test determines residence in the UK.



	When non resident throughout the three prior tax years				When resident at any time in the three prior tax years				
Number of days in the UK in a tax year	1 or No UK ties	2 UK ties	3 UK ties	4+ UK ties	No UK ties	1 UK ties	2 UK ties	3 UK ties	4+ UK ties
Fewer than 16 days	NR	NR	NR	NR	NR	NR	NR	NR	NR
16 to 45 days	NR	NR	NR	NR	NR	NR	NR	NR	R
46 to 90 days	NR	NR	NR	R	NR	NR	NR	R	R
91 to 120 days	NR	NR	R	R	NR	NR	R	R	R
121 to 182 days	NR	R	R	R	NR	R	R	R	R
183 days plus	R	R	R	R	R	R	R	R	R

Source: KPMG website United Kingdom – Taxation of International executives, https://assets.kpmg/content/dam/kpmg/pdf/2016/01/statutory-residence-test-flowchart.pdf

Figure 4: Statutory residence test

Based on the facts presented in section 5.1, the South African resident expatriate renders employment services in the UK and is present in the country for more than 183 days. Based on the 'Automatic UK Resident test' above, the South African resident expatriate is resident in the UK. The

South African resident expatriate is resident in the UK based on the 'Automatic UK Resident test' and is also resident in South Africa due to being 'ordinarily resident'. In terms of the 'tie breaker' clauses in Article 4(2) of the DTA between South Africa and the UK, which have been discussed in section 2.2.3, the South African resident expatriate is deemed to be exclusively tax resident in South Africa as his permanent home is in South Africa (Article 4(2)(a)). As such, the South African resident expatriate is viewed as being non-resident in the UK and is therefore subject to tax on UK sourced income and capital gains in respect of UK property in the UK.

UK income tax is charged at progressive rates of tax and residents and non-residents are taxed at the same rate.

The tax tables for the UK 2020/2021 tax year are as follows[24]:

Table 8: Tax tables for UK 2020/2021 tax year

Taxable income			
From (GBP)	**To (GBP)**	**Basic tax (GBP)**	**% on excess**
0	37 700	0	20% (basic rate)
37 701	150 000	7 540	40% (higher rate)
150 001	Over 150 000	52 460	45% (additional rate)

Source: PwC Worldwide Tax Summaries: Territory UK (https://taxsummaries.pwc.com/unitedkingdom/individual/taxes-on-personal-income)

Employers in the UK are required to withhold employees' tax from earnings (which generally include salaries, bonuses and commissions) made to employees under the pay-as-you-earn (PAYE) system. Similar to the employees' tax system in South Africa, UK employers are required to report details of earnings and deductions to Her Majesty's Revenue and Customs (HMRC) electronically on or before the time of payment of earnings to the employee. (PwC, 2021c)

5.3.2 Illustrative analysis

The foreign employment income earned in example 1, 2 and 3 is converted to British Pounds using the SARS average exchange rate for the year of assessment ending 28 February 2021 of R21.3264 (SARS, 2021d) and is equivalent to:

Table 9: Examples in British pounds

All amounts rounded to nearest whole number	**Rand salary**	**Exchange rate**	**GBP salary (converted)**
Example 1	R 1 000 000	R 21.3264	GBP 46 890

[24] The official currency of the UK is British Pounds/Pounds Sterling (GBP)

Example 2	R1 500 000	R 21.3264	GBP 70 335
Example 3	R5 000 000	R 21.3264	GBP 234 451

Using the tax calculator provided on the Government of the UK website[25], the UK income tax liability on foreign employment income earned in the UK in example 1, 2 and 3 is:

Table 10: UK tax table for examples

All amounts rounded to nearest whole number	**GBP salary (converted)**	**GBP tax***	**Exchange rate**	**Rand tax (converted)**
Example 1	GBP 46 890	GBP 6 862	R 21.3264	R 146 342
Example 2	GBP 70 335	GBP 15 562	R 21.3264	R 331 881
Example 3	GBP 234 451	GBP 85 431	R 21.3264	R 1 821 936

* Income tax excluding National Insurance

Using the information contained in the tables above, the South African taxable income and normal tax liability is calculated for scenario 1, 2 and 3.

Table 11: Scenarios 1, 2 and 3

Scenario 1 - South African taxable income calculation and normal tax liability **For remuneration earned in the UK** (all amounts have been rounded to the nearest Rand)	**Example 1** **Salary of R1 million**	**Example 2** **Salary of R1.5 million**	**Example 3** **Salary of R5 million**
	Rands (R)	**Rands (R)**	**Rands (R)**
Gross income			
Foreign employment income sourced in the UK	1 000 000	1 500 000	5 000 000
Less: exempt income s 10(1)(*o*)(ii) exemption limited to R1.25 million	(1 000 000)	(1 250 000)	(1 250 000)
Income	0	250 000	3 750 000
Taxable Income	**0**	**250 000**	**3 750 000**
Normal tax liability		48 528[26]	1 537 179[27]
Less: Primary rebate – s 6(2)	-	(14 958)	(14 958)
South African tax liability (before the relief of double tax)	**0**	**33 570**	**1 522 221**

Analysis of scenario 1 – South African taxable income and normal tax liability before double tax relief
In example 1, the South African resident expatriate is not liable for any South African tax because the foreign employment income earned in the UK was below the s 10(1)(*o*)(ii) exemption limit of R1.25 million. As such, there is no instance of double tax and hence there was no requirement to consider

[25] Source: Government of the UK website: https://www.tax.service.gov.uk/estimate-paye-take-home-pay/your-pay
[26] Example 2 – [R37 062 + (R250 000 taxable income – R205 900 per tax table) x 26%]
[27] Example 3 -[R559 464 + (R3 750 000 taxable income – R1 577 300 per tax table) x 45%]

the DTA between South Africa and the UK and s 6*quat.* However, in example 2 and 3, the South African resident is liable for South African tax on the portion of foreign employment income above the exemption limit of R1.25 million and consequently, the South African resident expatriate is taxed twice on a portion of the foreign employment income earned in the UK. For example 2 and 3, the South African resident expatriate has two options for the elimination of double taxation, namely, the application of the DTA between South Africa and the UK or s 6*quat* (SARS, 2020b, 66).

Scenarios 2 and 3 examine the relief of double taxation by application of the DTA between South Africa and the UK and by application of s 6*quat* respectively.

Analysis of scenario 2 – South African taxable income and normal tax liability after the elimination of double tax by way of DTA

In examples 2 and 3 of scenario 1, the South African tax liability before any double tax relief is R33 570 and R1 522 221 respectively and the South African resident expatriate is subject to double taxation on the foreign employment income above the s 10(1)(*o*)(ii) exemption limit.

In terms of s 6*quat*(2), a taxpayer resident in South Africa may elect to apply the tax treaty credit method of relief instead of the s 6*quat* rebate method of relief and if so, decides none of the provisions of s 6*quat* will apply (for example, the taxpayer is not allowed to carry forward any excess foreign taxes under paragraph (ii) of the proviso to s 6*quat*(1B)(a)). In scenario 2, the South African resident expatriate elects under s 6*quat*(2) to use the DTA relief for the elimination of double taxation.

Article 21 of the DTA between South Africa and the UK refers to the Elimination of Double taxation and states:

> (1) Subject to the provision of the law in South Africa regarding the deduction from tax payable in South Africa of tax payable in any country other than South Africa, United Kingdom tax paid by residents of South Africa in respect of income taxable in the United Kingdom, in accordance with the provisions of this convention, shall be deducted from taxes due according to South Africa fiscal law. Such deduction shall not, however, exceed an amount which bears to the total South African tax payable the same ratio as the income concerned bears to the total income.
> (2) …
> (3) …

The words ‘subject to’ in Article 21(1) indicates that the credit for foreign tax paid must be determined under s 6*quat* which deals with the deduction of foreign taxes from South African tax payable (SARS, 2020b, 69). An additional limitation on the relief granted in terms of s 6*quat* is imposed in Article 21(1) and states:

> Such deduction shall not, however, exceed an amount which bears to the total South African tax payable the same ratio as the income concerned bears to the total income.

The limitation in Article 21(1) is colloquially referred to as the 'the maximum deduction' and is calculated in the same manner as Article 22(b) of the DTA between South Africa and India. That is, the maximum deduction is limited to: the total South African tax payable x Taxable income concerned[28]/ Total taxable income (Article 21(1)) and is calculated on a 'per country' basis (SARS, 2020b, 67-68).

The amount of foreign taxes that qualify for a rebate under s 6*quat*(1) are limited to foreign taxes in respect of foreign income included in a resident's taxable income (s 6*quat*(1A)). Foreign taxes in respect of the exempt foreign income of R1.25 million do not qualify for the rebate under s 6*quat*(1) and are not carried forward to subsequent years of assessment.

The amount of foreign taxes that qualify for a rebate under s 6*quat*(1A) is calculated as follows:

> Remuneration for foreign services included in taxable income x foreign tax
> Total remuneration for foreign services
> (SARS, 2020b, 114)

The s 6*quat* rebate is limited to the South African tax payable on the foreign employment income included in taxable income and is calculated in terms of s 6*quat*(1B)(a) as follows:

> Taxable income derived from foreign sources x South African tax payable
> Total taxable income derived from all sources
> (SARS, 2020b, 114)

Article 21(1) is 'subject to' s 6*quat* and hence the elimination of double tax is calculated in accordance with the provisions contained in s 6*quat*. In examples 2 and 3, the amount of foreign taxes that qualify for a rebate under s 6*quat*(1A) is R55 314[27] and R1 366 452[28] respectively. Under s 6*quat*(1A)(a)(i) foreign taxes that qualify for a rebate under s 6*quat*(1) are limited to foreign taxes in respect of foreign income included in a resident's taxable income. Foreign taxes in respect of the exempt foreign income of R1.25 million do not qualify for the rebate under s 6*quat*(1) and are not carried forward to subsequent years of assessment. (SARS, 2020b, 115.)

[28] Taxable income concerned refers to taxable income in respect of the income which is taxed in South Africa and is also taxed, in accordance with the provisions of the tax treaty in the other country (SARS, 2020b, 67-69)

The s 6*quat* rebate for examples 2 and 3 is calculated in terms of s 6*quat*(1B)(a) and is R 33 570 and R1 522 221 respectively. See the scenario 2 calculations set out below. These amounts are also equivalent to the maximum deduction in terms of Article 21(1). Consequently, relief of double taxation in terms of the DTA in examples 2 and 3 is R33 570 and R1 366 452 respectively. However, for example 2, R33 570 of the qualifying withholding tax of R55 314 is deductible from normal tax payable. What is important to note is that Article 21(1) is 'subject to the provisions of the law in South Africa [s 6*quat*]' and consequently the balance of R21 744 (R55 314 – R33 570) is carried forward to the 2022 year of assessment and may qualify as a foreign tax for set-off against South African normal tax payable on taxable income derived from foreign sources (para (ii)(aa) of the proviso to s 6*quat*(1B)(a)).

The Scenario 2 table below presents the calculation of South African taxable income and normal tax liability after the elimination of double tax by way of DTA. Article 21(1) refers to the elimination of double taxation, which is 'subject to' s 6*quat* and has its own limitation on such deduction (the maximum deduction).

Table 12: Scenario 2

Scenario 2 - South African taxable income calculation and normal tax liability after the application of the DTA between South Africa and the UK **For remuneration earned in the UK** (all amounts have been rounded to the nearest Rand)	**Example 2** **Salary of** **R1.5 million**	**Example 3** **Salary of** **R5 million**
	Rands (R)	**Rands (R)**
Taxable income	250 000	3 750 000
South African tax liability (before the relief of double tax)	33 570	1 522 221
Application of Article 21(1) to eliminate double taxation The amount of foreign taxes that qualify for a rebate under s 6*quat*(1A) is calculated as follows[29,30]:	(33 570)	(1 366 452)
Remuneration for foreign services included in taxable income x foreign tax Total remuneration for foreign services	55 314	1 366 452
Limitation of the rebate under s 6*quat*(1B)(a) and the maximum deduction (Article 21(1)) is calculated as follows[31,32]:		
Taxable income derived from foreign sources x South African tax payable	33 570	1 522 221

[29] Example 2 = R250 000 (R1 500 000-R1 250 000)/1 500 000 x R331 881 = R55 314

[30] Example 3 = = R3 750 000 (R5 000 000-R1 250 000)/5 000 000 x R1 821 936 = R1 366 452

[31] Example 2 = R250 000 (R1 500 000-R1 250 000)/250 000 x R33 570 = R33 570

[32] Example 3 = R3 750 000 (R5 000 000- R1 250 000)/ R3 750 000 x R1 522 221= R1 522 221

Total taxable income derived from all sources		
South African tax liability based on the DTA	**0**	**155 769**

Analysis of scenario 3 – South African taxable income and normal tax liability after the application of s 6quat(1) for the elimination of double tax

Scenario 3 assumes the South African resident expatriate elects the relief provided for under s 6*quat*(1). The processes followed to determine the s 6*quat* rebate is the same as in scenario 2 above and the South African tax liability after the s 6*quat* rebate is Rnil and R 155 769 for example 2 and 3 respectively. In example 2, the amount of foreign taxes that qualify for a rebate under s 6*quat*(1A) (R55 314) exceed the rebate under s 6*quat*(1B)(a) (R33 570). Under paragraph (ii)(aa) of the proviso to s 6*quat*(1B)(a) the balance of R21 744 (R55 314 – R33 570) is carried forward to the 2022 year of assessment and may qualify as a foreign tax for set-off against South African normal tax payable on taxable income derived from foreign sources (para (ii)(aa) of the proviso to s 6*quat*(1B)(a)).

Table 13: Scenario 3

Scenario 3 - South African taxable income calculation and normal tax liability after the application of s 6*quat* For remuneration earned in the UK (all amounts have been rounded to the nearest Rand)	**Example 2 Salary of R1.5 million**	**Example 3 Salary of R5 million**
	Rands (R)	**Rands (R)**
Taxable income	250 000	3 750 000
South African tax liability (before the relief of double tax)	33 570	1 522 221
Application of s 6*quat*(1) to eliminate double taxation The amount of foreign taxes that qualify for a rebate under s 6*quat*(1A) is calculated as follows[33,34]: Remuneration for foreign services included in taxable income x foreign tax Total remuneration for foreign services Limitation of the rebate under s 6*quat*(1B)(a) is calculated as follows[35,36]: Taxable income derived from foreign sources x South African tax payable Total taxable income derived from all sources	(33 570) 55 314 33 570	(1 366 452) 1 366 452 1 522 221
South African tax liability based on s 6*quat* rebate	**0**	**155 769**

[33] Example 2 = R250 000 (R1 500 000-R1 250 000)/1 500 000 x R331 881 = R55 314

[34] Example 3 = = R3 750 000 (R5 000 000-R1 250 000)/5 000 000 x R1 821 936 = R1 366 452

[35] Example 2 = R250 000 (R1 500 000-R1 250 000)/250 000 x R33 570 = R33 570

[36] Example 3 = R3 750 000 (R5 000 000- R1 250 000)/ R3 750 000 x R1 522 221= R1 522 221

Conclusion:

Scenarios 2 and 3 are similar in nature as Article 21(1) of the DTA between South and the UK is 'subject to' s 6*quat*. The South African resident expatriate will be in the same financial position as the same amount of tax is payable in South Africa if she/he elected either form of double tax relief mechanism and under paragraph (ii)(aa) of the proviso to s 6*quat*(1B)(a), any excess foreign tax paid can be carried forward to a succeeding year of assessment and may qualify as a foreign tax for set-off against South African normal tax payable on taxable income derived from foreign sources. In the instance where the South African resident expatriate earned foreign sourced employment income in more than one country, SARS states:

> …it would not be to the taxpayer's [South African resident expatriate's] advantage to elect that the tax treaty [DTA] method of relief apply, since the amount determined under s 6*quat* is potentially further limited under a per country limitation calculation as required under the tax treaty [DTA]. (SARS, 2020b, 67-68)

The South African resident expatriate should evaluate the administrative and compliance advantages and disadvantages of each method before deciding which relief method should be pursued. The nature of this evaluation is beyond the scope of this report.

5.4 Foreign employment income earned in Dubai

5.4.1 Overview of the individual tax system in Dubai, which is part of the UAE

There is currently no personal income tax in Dubai and as such, there is no individual tax registration or reporting obligations and no domestic legislative definition of personal tax residence (PwC, 2021b). As a result, a South African resident expatriate earning foreign employment income in Dubai will not be subject to double taxation on the same income, therefore no double tax relief will be required.

5.4.2 Illustrative analysis

The South African taxable income and normal tax liability is calculated for examples 1, 2 and 3 using the rand denominated foreign employment income amounts and after the s 10(1)(o)(ii) exemption and if applicable, any double taxation relief measures.

Table 14: Scenario 1

Scenario 1 South African taxable income calculation and normal tax liability **For remuneration earned in Dubai** (all amounts have been rounded to the nearest rand)	**Example 1 Salary of R1 million**	**Example 2 Salary of R1.5 million**	**Example 3 Salary of R5 million**
	Rands (R)	**Rands (R)**	**Rands (R)**
Gross income			
Foreign employment income sourced in Dubai	1 000 000	1 500 000	5 000 000
Less: exempt income s 10(1)(*o*)(ii) exemption limited to R1.25 million	(1 000 000)	(1 250 000)	(1 250 000)
Income	0	250 000	3 750 000
Taxable Income	**0**	**250 000**	**3 750 000**
Normal tax payable		48 528[37]	1 537 179[38]
Less: Primary rebate – s 6(2)		(14 958)	(14 958)
Less: DTA relief – not applicable (Note 1)			
Less: s 6*quat* rebate – not applicable (Note 2)			
South African tax payable	**0**	**33 570**	**1 522 221**

Analysis of example 1, 2 and 3

Before the amendment to s 10(1)(*o*)(ii) in 2017 which came into effect on 1 March 2020, the foreign employment income earned in Dubai by a South African resident expatriate would have been exempt from South African income tax, subject to the qualifying criteria of the s 10(1)(*o*)(ii) being met. Consequently, the South African resident expatriate would have been entitled to tax-free foreign employment income earned in Dubai.

Note 1 – reference to the DTA between South Africa and Dubai is made to complete the illustrative analysis.

The DTA between South African and Dubai is applicable to persons who are residents of one or both of the Contracting States in terms of Article 1 Persons Covered (SARS, 2015). For the purposes of examples 1, 2 and 3, the taxpayer is resident in South Africa by way of ordinary residence.

Income from employment is addressed in Article 14 of the DTA between South Africa and Dubai and is similar in nature to the same article in the DTA between South Africa and India. Refer to section 4.2.2 for a discussion on the taxing rights of foreign employment income. In terms of Article 14, the income from Dubai shall only be taxable in South Africa unless the employment services are rendered

[37] Example 2: [R37 062 + (R250 000 taxable income – R205 900 per tax table) x 26%]

[38] Example 3: [R559 464 + (R3 750 000 taxable income – R1 577 300 per tax table) x 45%]

in Dubai, which is the case. It should be noted that in terms of paragraph 2, the income from employment shall be taxable in South Africa if the three conditions prescribed in paragraph 2(a), (b) and (c) are satisfied. Since the taxpayer is present in Dubai for more than 183 days, paragraph 2(a) is not met. Generally, under the provisions of the relevant DTA, if an employee renders services in a foreign country exceeding 183 days, both the country of residence and country of source 'may' tax the income, that is, neither country has an exclusive right to tax the income. However, the country of source is entitled to the first right to tax the income and the country of residence will provide the double tax relief in the form of a foreign tax credit to the extent that double tax arises, subject to limitations. (SARS, 2020a, 6.)

The foreign employment income earned in Dubai by a South African resident expatriate may be taxable in Dubai, however there is no personal income tax in Dubai and hence there is no requirement to consider Article 22 Elimination of Double Taxation in the DTA between South Africa and Dubai.

Note 2 – reference is made to s 6*quat* to complete the illustrative analysis.
The s 6*quat* rebate in respect of foreign taxes on income is only available to taxpayers who received income from a foreign source which has already been taxed in the foreign country (s 6*quat*(1A)). In terms of examples 1, 2 and 3, the foreign employment income earned in Dubai by a South African resident expatriate was not subject to tax in Dubai as the country does not have personal income tax. Therefore, the South African resident expatriate does not qualify for the s 6*quat* rebate.

Conclusion:
The only double tax relief mechanism available to a South African resident expatriate earning foreign employment income in Dubai is s 10(1)(*o*)(ii), if applicable, and the exemption is limited to R1.25 million. Therefore, the maximum foreign employment income earned outside of South Africa subject to double non-taxation is R1.25 million.

5.5 Summary comparative analysis for India, the UK and Dubai

In the previous sections, a thorough analysis was performed on the South African taxable income calculations and normal tax liability of a South African resident expatriate earning foreign employment income in three foreign countries, namely: India, the UK and Dubai. For each country three scenarios were analysed, namely the calculation of a South African resident expatriate's taxable income and normal tax liability across different foreign employment incomes:

- before the relief of double taxation;
- after the application of a DTA for the relief of double taxation;
- after s 6*quat* for the relief of double taxation.

It was assumed for each scenario that the foreign employment income earned in the three countries qualified for the s 10(1)(*o*)(ii) exemption.

Table 15: Summary comparative analysis

Summary results of South African normal tax payable before and after the relief of double taxation			
(All amounts have been rounded to the nearest Rand)	**India**	**The UK**	**Dubai**
Example 1 - Salary of R1 million			
Normal tax payable (before double tax relief)	0	0	0
Example 2 – Salary of R1.5 million			
Normal tax payable – scenario 1 before double tax relief	33 570	33 570	33 570
Normal tax payable – scenario 2 after application of the DTA	0	0	33 570
Normal tax payable – scenario 3 after application of s 6*quat*	0	0	33 570
Example 3 – Salary of R5 million			
Normal tax payable – scenario 1 before double tax relief	1 522 221	1 522 221	1 522 221
Normal tax payable – scenario 2 after application of the DTA	154 942	155 769	1 522 221
Normal tax payable – scenario 3 after application of s 6*quat*	154 942	155 769	1 522 221

Example 1

In example 1, a South African resident expatriate will not be liable for South African tax as he/she qualifies for the s 10(1)(*o*)(ii) exemption because the foreign employment income of R1 million earned in the three foreign countries is below the exemption limit of R1.25 million. Therefore, a South African resident expatriate earning foreign employment income up to R1.25 million should try everything possible to meet the qualifying requirements of s 10(1)(*o*)(ii). The requirements to qualify for the exemption are specific, as discussed in section 3.2, and the taxpayer is required to keep the necessary documentation as proof for SARS that he/she has met all the qualifying requirements for s 10(1)(*o*)(ii).

Example 2

In example 2, a South African resident expatriate will be liable for South African tax before the application of any double taxation relief on foreign employment income earned above the exemption limit of R1.25 million. Two double taxation relief measures are applied in this example, namely: the relevant DTA provisions and s 6*quat*.

For India, the elimination of double taxation by:

- way of DTA is calculated in terms of the ordinary credit method which allows a deduction of foreign tax from South African tax payable calculated on a taxpayer's worldwide income. The

deduction is limited to the proportion of South African tax payable that is attributable to the foreign employment income included in a taxpayer's taxable income and this is termed the 'maximum deduction' (Article 22(b)). After the elimination of double taxation by application of Article 22(b), there is no South African tax payable. However, the excess foreign tax[39] of R41 309 (R74 879 – R33 570) is lost and may not be carried forward to the 2022 year of assessment (SARS, 2020b, 69).

- application of s 6*quat* is calculated in a two-step approach. The first step is to determine the amount of foreign taxes that qualify for a rebate under s 6*quat*(1A) which is R74 879. The next step is to calculate the rebate under s 6*quat*(1B)(a) which is R33 570. In contrast to provisions of Article 22(b), the excess foreign tax of R41 390 (R74 879 – R33 570) can be carried forward to the 2022 year of assessment and may qualify as a foreign tax for set-off against South African normal tax payable on taxable income derived from foreign sources (para (ii)(aa) of the proviso to s 6*quat*(1B)(a)).

The benefit of the application of s 6*quat* as opposed to the application of DTA provisions is that it allows a taxpayer to carry-forward qualifying foreign taxes that were not allowed as a rebate in the current year of assessment to the succeeding year of assessment.

For the UK, the elimination of double taxation by way of DTA is 'subject to' the provisions of s 6*quat,* however Article 21(1) imposes a limitation on the relief in addition to the requirements of s 6*quat* which is colloquially termed the maximum deduction. The limitation is the same as the maximum deduction in the DTA between South Africa and India (Article 22(b)). As with India, the same two-step approach was followed to calculate the s 6*quat* rebate. The foreign taxes that qualify for a rebate of R55 314 (s 6*quat*(1A)) exceed the rebate R33 570 (s 6*quat*(1B)) and therefore the excess foreign tax of R21 744 can be carried forward to the 2022 year of assessment and may qualify as a foreign tax for set-off against South African normal tax payable on taxable income derived from foreign sources (para (ii)(aa) of the proviso to s 6*quat*(1B)(a)).

Conclusion: Where the tax due in India or the UK is higher than the tax due in South Africa on the taxable foreign employment income and where the ordinary credit principle is applied, the South African resident expatriate will not receive a deduction for the entire foreign tax paid. However, if the relief is granted in terms of s 6*quat*, the excess foreign tax can be carried forward to the succeeding year of assessment.

[39] The excess foreign tax = the proportional share of foreign tax paid on the amount included in taxable income (R74 879) above the maximum deduction (R33 570)

A South African resident expatriate is liable for South African tax on foreign employment income earned in Dubai above the exemption limit R1.25 million. There is no personal income tax in Dubai and therefore there is no instance of double taxation.

Example 3

In example 3, a South African resident expatriate is liable for South African tax even after the application of the DTA and s 6*quat,* if applicable. The South African tax payable on foreign employment income earned in India and the UK after the application of either the DTA relief or s 6*quat* is significantly lower compared to the same in Dubai because there is no personal income tax in Dubai. The South African tax payable after the application of the DTA and s 6*quat* for India and the UK of R154 942 and R 155 769 respectively is due to the difference in marginal income tax rates in each country compared to South Africa.

Where the tax due in India or the UK is lower than the tax due in South Africa on the taxable foreign employment income, the South African resident expatriate will always have to pay the same amount of taxes as he/she would have had to pay if he/she were taxed only in South Africa. The results for this conclusion are shown in the table below:

Table 16: Conclusions

When taxes due in India and the UK on foreign employment income that is taxable in South Africa is lower than that in South Africa		
(All amounts have been rounded to the nearest Rand)	**India**	**The UK**
Example 3 – Salary of R5 million		
Foreign tax paid on the taxable foreign employment income	1 367 279	1 366 452
South African tax payable before the relief of double taxation	1 522 221	1 522 221
South African tax payable after the relief of double taxation	154 942	155 769
Total taxes paid In South Africa and the foreign country	1 522 221	1 522 221

It is evident from the comparative analysis, a South African resident expatriate earning foreign employment income in Dubai is severely impacted by the amendment to s 10(1)(*o*)(ii) and the introduction of the exemption limit of R1.25 million. Before the amendment to s 10(10(*o*)(ii) in 2017 which became effective 1 March 2020, foreign employment income earned in Dubai would have been fully exempt from South African tax and there would be no extra income tax imposed on the income as there is no personal income tax in Dubai. In contrast, a South African resident expatriate earning foreign employment income in India and the UK, prior to the s 10(1)(o)(ii) amendment in 2017, would have only been liable for foreign income tax. Based on the summary calculations in example 2 and 3, a South African resident expatriate is marginally affected by the s 10(1)(*o*)(ii) amendment.

Consequently, the introduction of the s 10(1)(*o*)(ii) amendment has achieved National Treasury's purpose to prevent double non-taxation of income (Legwaila, 2019).

Should a South African resident expatriate want to avoid paying any South African tax, he/she can break South African tax residency (cease to be tax resident in South Africa). A change in South African tax residency is based on the manner in which the taxpayer has been resident in South Africa (SARS, 2021a). In this report, the South African resident expatriate is resident in South Africa by way of ordinary residence and therefore the expatriate will no longer be resident in South Africa if he/she changes their country of ordinary residence, however this must be supported by various objective factors (Hughes and Crocker, 2018). There are two ways a South African resident expatriate can cease to be tax resident in South Africa, namely:

(1) by leaving South Africa with no intention of returning to South Africa and settling permanently in another country (with or without formal emigration); or
(2) by becoming resident in the foreign country in which he/she works and by applying the tie-breaker clauses contained in the residence article of the applicable DTA. (Hughes and Crocker, 2018)

The three DTAs discussed in this report each contain a provision for certain South African residents, who meet the requirements specified in the DTA, to be able to break their South Africa tax residency under the DTA (SARS, 2015). The definition of a resident in s 1(1) specifically excludes 'any person who is deemed to be exclusively a resident of another country' by virtue of the application of a DTA. Therefore, that person will be considered non-tax resident in South Africa. When the South African resident expatriate ceases to be resident in South Africa a deemed disposal for capital gains tax purposes takes place. The South African resident expatriate will be deemed to have disposed of his/her worldwide assets, excluding immovable property located in South Africa. (SARS, 2021a) This will trigger a capital gain or loss that may give rise to a tax liability to SARS (Hughes and Crocker, 2018). The reality of breaking tax residency is that many South Africans cannot afford to settle the 'exit charge', being the cash liability to SARS (Grange et al., 2017, 30). Refer to section 4.2.4 Change in tax residency status for a discussion on the implications of ceasing to be tax resident in South Africa.

5.6 The administrative and compliance process to claim a s 10(1)(o)(ii) exemption on an ITR12 including the supporting documentation required by SARS to support the exemption

The focus of this section is on the completion of an individual tax return (ITR12) for a South African resident expatriate with respect to foreign employment income earned outside of South Africa, s 10(1)(*o*)(ii) exemption and other measures for relief of double taxation (e.g., s 6*quat* rebate and relief

in terms of a DTA). For the purpose of this report, the tax year that is considered is the 2021 year of assessment.

A South African resident expatriate who earns foreign employment income outside of South Africa during the year of assessment (ending 28 February 2021) is required to submit an ITR12 for the 2021 year of assessment (SARS, 2021b). The ITR12 can be requested on the Income Tax Work Page via eFiling (an online platform for the submission of South African tax returns and declarations and other related services) that is prepopulated with information available to SARS, such as personal particulars and information received from third parties (e.g., employers).

The first page of an ITR12 (Form Wizard) consists of several questions and based on the answers to these questions, a customised ITR12 is created. There are several sections to an ITR12 and each section has its own requirements and idiosyncrasies. In the employees' tax certificate information section, SARS insists on separate IRP5/IT3(a) certificates where an employee's remuneration consists of local and foreign remuneration. Many payroll systems do not allow for local and foreign source codes for the same employee number and there is little that can be done by way of manual intervention to produce separate certificates. (Foster, June 2013) In addition, the ITR12 does not make provision for the s 6*quat* rebate unless the taxpayer has indicated that he/she has earned foreign income and an amount of foreign income is included in the ITR12 (that is, foreign source codes are used in the IRP5 certificate).

SARS may request the South African resident expatriate to provide proof of income declared and deductions or exemptions claimed on his/her ITR12. Supporting documentation should be retained for a period of five years from the date the return is submitted. The following are examples of the documentation or information that may be required:

- IRP5/IT3(a) Employees' Tax Certificate or similar for remuneration received
- Section 10(1)(*o*)(ii) exemption – proof of qualifying criteria
    - a travel schedule
    - letters of secondment
    - passport
    - employment contract for foreign services (SARS, 2021c, 5)
- s 6*quat* rebate (foreign tax credits) – proof of foreign taxes paid
    - where foreign tax has been withheld at source – a certificate of tax withheld issued by the person withholding the tax, usually the employer
    - where foreign tax has not been withheld at source – an assessment or receipt issued by the relevant tax authority (SARS, 2020b, 86-87.)

As is evident from the above, the completion of an ITR12 for a South African resident expatriate is challenging. It may be necessary for the South African resident expatriate to seek professional tax advice and assistance when it comes to the completion of the ITR12 and the application of double taxation relief mechanisms such as the s 10(1)(*o*)(ii) exemption, s 6*quat* rebate and DTA relief. Typically, the tax returns of South African resident expatriates who are employed locally are managed by their employers' own tax division or outsourced to a tax professional. However, South African resident expatriates who take up direct employment opportunities outside South Africa are usually responsible for their own tax affairs. In both instances, there is a cost for having a tax return prepared which is commensurate with the complexities involved. In addition, South African resident expatriates are confronted with an increased administrative burden with obtaining supporting documentation to satisfy the requirements of s 10(1)(*o*)(ii) and s 6*quat.*

Chapter 6: Implications of s 10(1)(*o*)(ii) on local and foreign employers and SARS

6.1 Local and foreign employers

The specific wording in s 10(1)(*o*)(ii) refers to 'any employer'. This means that services rendered by employees for or on behalf of resident (local employers) or non-resident employers (foreign employers) could qualify for exemption (SARS, 2021c).

6.2 Employees' tax on foreign employment income

With reference to para 2(1) of the Fourth Schedule, a local employer has an obligation to deduct and withhold employees' tax on remuneration to a South African resident expatriate. However, no obligation exists to deduct or withhold employees' tax in the case of a foreign employer with no representative employer in South Africa.

If the local employer is satisfied that the South African resident expatriate meets all the requirements of s 10(1)(*o*)(ii), the local employer may elect not to deduct PAYE on the remuneration paid up to the exemption limit of R1.25 million. However, it should be noted where the exemption was not applicable, the local employer is liable for the PAYE not deducted as well as any penalties and interest. Conversely, if a local employer has deducted and withheld PAYE on behalf of the South African resident expatriate and it later becomes apparent that the remuneration qualifies for the s 10(1)(*o*)(ii) exemption, the local employer may not refund the 'over-deducted' PAYE to the South African resident expatriate. The only remedy in this situation is for the South African resident expatriate to claim a refund on assessment. (SARS, 2020a, 9.)

An employee's tax certificate (IRP5) is issued by the local employer to the South African resident expatriate in terms of para 13(1) of the Fourth Schedule. The local employer has the responsibility to correctly disclose each remuneration item in respect of foreign employment services under the relevant foreign income source code (SARS, 2020a, 11). It should be noted that every source code has a particular tax implication and if the wrong source code is used, this may result in an incorrect assessment from SARS (Musviba, 2020).

In the instance where a South African resident expatriate is in a double taxation position even after applying the s 10(1)(*o*)(ii) exemption, the local employer may apply to SARS for a directive to vary the basis on which PAYE is deducted and withheld (para 10 of the Fourth Schedule), however this may be administratively complex. It is important to note, a directive is issued to the employer which allows the employer to include a potential foreign tax credit on the payroll for PAYE purposes. The employee

is still expected to submit an ITR12 in which the actual s 6*quat* rebate is claimed. (SARS, 2020a, 12.) The s 6*quat* rebate is claimed on assessment when the South African resident expatriate submits his/her ITR12.

6.3 Employees' tax and compliance considerations associated with claiming a s 10(1)(*o*)(ii) exemption

There are many different variables, for example, the many requirements to qualify for the s 10(1)(*o*)(ii) exemption that need to be considered from a tax perspective when a South African resident expatriate is employed by a local employer and earns foreign employment income and it may be prudent for a local employer to engage the services of a tax professional (specialising in International Tax) to advise on a practical approach to deal with PAYE implications and compliance matters in relation to a South African resident expatriate employee.

The South African resident expatriate employed by a foreign employer requires the relevant supporting documentation to substantiate his/her income, exemptions and rebates declared on his/her ITR12. Refer to section 5.6 for a discussion of the relevant supporting documentation.

6.4 The benefit of s 10(1)(*o*)(ii) prior to the amendment effective 1 March 2020 and the compliance consequences of s 10(1)(*o*)(ii) after the amendment

It should be noted that before the amendment to s 10(1)(*o*)(ii) in 2017, which became effective 1 March 2020, foreign employment income earned by a South African tax resident was exempt from South African income tax, subject to certain qualifying criteria. Chambers, Gouws and Rohhamlal summarise the benefits of the exemption (before amendment) for local employers of South African resident expatriates as follows:

- the exemption can be applied upfront in their payroll (cash-flow benefit [to the employee]);
- there is no need to interpret and apply a double tax treaty (DTT) [DTA] to determine potential double taxation;
- there is no need [for an employee] to collect proof of [foreign] income tax paid and claim credits for [foreign] income tax paid;
- they [employers] can send employees to comparatively low-income tax jurisdictions (with concomitantly high import or consumption taxes), without having to consider the effect of a mismatched tax burden. (Chambers, Gouws and Rohhamlal, 2018)

As a consequence of the amendment to s 10(1)(*o*)(ii) to cap the exemption at R1.25 million, local employers who assign employees (i.e., South African resident expatriates) to foreign countries are

faced with an increased cost of employment where they offer tax equalisation[40] or tax protection[41] to their employees and an additional administrative burden (Grange et al., 2017, 36).

Generally, when a South African resident expatriate is assigned to work in a foreign country, he/she is provided with various assignment benefits and/or allowances which are taxed in the foreign country and the tax (including the differential in tax rates should the host country have higher personal tax rates than South Africa) is borne by the employer if the South African resident is tax equalised. The purpose of tax equalisation is to ensure that the employee (a South African resident expatriate) pays approximately the same tax liability as had he/she remained in South Africa. As a result of the amendment to s 10(1)(*o*)(ii), these benefits and/or allowances and the tax equalisation (and gross-up) become taxable in South Africa and consequently, the additional cost is borne by the employer.

The increased tax cost may also include the additional expense incurred by the employers who offer tax filing services to their expatriate employees. (Grange et al., 2017, 11) The overall assignment cost to the employer would increase and this may discourage employers from sending their South African employees on assignments to foreign countries.

A local employer may encounter an additional administrative process for an employee (a South African resident expatriate) as a result of applying to SARS for a directive to vary the basis on which PAYE is deducted and withheld (para 10 of the Fourth Schedule).

6.5 SARS guidance with respect to s 10(1)(*o*)(ii)

SARS issued Interpretation Note 16 (Issue 4) which discusses the interpretation and application of the foreign employment remuneration exemption in s 10(1)(*o*)(ii) as well as SARS has published a document with Frequently asked questions with respect to s 10(1)(*o*)(ii) foreign employment income

[40] 'The objective of tax equalisation is to make sure that assignees do not have a higher or lower income tax liability than if they remained in their home country. Therefore, they receive a net amount of remuneration as if they had remained in their home country (i.e., their packages are recalculated with reference to that tax that they would have paid, had they remained in their home countries-so that all assignment-related benefits are paid tax-free, over and above this net package entitlement). The employer usually bears the responsibility of paying assignee's actual taxes in the home and host countries.' (Source: 'South Africa – Foreign Services Exemption Amended', by KPMG GMS - Chambers C, Gouws B and Rohhamlal, published as a Flash Alert on 26 January 2018, https://home.kpmg/xx/en/home/insights/2018/01/flash-alert-2018-020.html)

[41] 'Under tax protection, the employer generally reimburses an assignee for the excess taxes incurred while on international assignment. The assignee usually bears responsibility for paying all actual taxes in the home and host countries. The annual tax protection calculation compares the 'stay-at-home' or 'hypothetical' tax to the actual worldwide taxes paid by the assignee. The employer reimburses any excess to the assignee. Tax protection policies generally put the burden of filing and paying home and host country taxes on the assignee. Any benefit from the payment of less tax than the stay-at-home position is retained by the assignee.' (Source: 'South Africa – Foreign Services Exemption Amended', by KPMG GMS - Chambers C, Gouws B and Rohhamlal, published as a Flash Alert on 26 January 2018, https://home.kpmg/xx/en/home/insights/2018/01/flash-alert-2018-020.html)

exemption. These documents provide guidelines to taxpayers, tax professionals and SARS when interpreting and applying s 10(1)(*o*)(ii).

The requirements to qualify for the s 10(1)(*o*)(ii) exemption are extensive and the burden of proof lies with the South African resident expatriate claiming the exemption (Grange et al., 2017, 13). SARS may request supporting documentation from the South African resident expatriate to substantiate the s 10(1)(*o*)(ii) exemption claimed on assessment, for example, a travel schedule showing number of days in and out of South Africa, a copy of the South African resident expatriate's passport, an employment contract and an IRP5 (if applicable) (Grange et al., 2017, 13).

6.6 Application of s 10(1)(*o*)(ii) and foreign tax credits on an ITR12

The exemption under s 10(1)(*o*)(ii) is limited to R1.25 million and any excess remuneration above this limit may be subject to double tax. In this situation, a South African resident expatriate may claim foreign tax credits on assessment. An ITR12 does not make provision on the return to claim foreign tax credits unless it is indicated in the return that the South African resident expatriate earned foreign income, despite an IRP5 which contains foreign source codes, and an amount of foreign income is included in the tax return. The workaround to this issue is for the taxpayer to report R1 under the foreign income source code as this will allow the taxpayer to claim the foreign tax credit in the return. If this is not done, the taxpayer will only be able to claim the foreign tax credit on objection. On objection, supporting documentation may be required by SARS and in this instance, proof of taxes paid in the foreign country will need to be submitted. (Grange et al., 2017, 37.)

Foreign tax credit claims may result in refunds to the South African resident expatriate which can take a long time to be paid. Grange et al state the reason for delay in payment is as follows:

> …SARS often insists on auditing refunds and verifying bank details in person… (Grange et al., 2017, 11)

The question that arises is, does SARS have the necessary means and ability to meet and address the additional administrative cost and compliance burdens required by the s 10(1)(*o*)(ii) exemption and the s 6*quat* rebate. This is an area for potential future research, and it would be beneficial to do this on the 2020/2021 tax filing submission, being the first submission after the effective date of the s 10(1)(*o*)(ii) amendment.

Chapter 7: Conclusion

The purpose of this research report was to analyse the application of the qualifying requirements of the foreign employment income exemption under s 10(1)(*o*)(ii) for South African resident expatriates and investigate the implications of the s 10(1)(*o*)(ii) exemption for South African resident expatriates, their local and foreign employers and SARS.

When South Africa changed to a residence-based system of taxation in 2001, s 10(1)(*o*)(ii) was introduced to exempt foreign employment income of a resident if the resident was outside his/her country of residence for a period exceeding 183 days (National Treasury, 2000, 5). An amendment to s 10(1)(*o*)(ii) was enacted in 2017 with an effective date of 1 March 2020 and introduced a cap to the exemption of R1 million as National Treasury sought to limit the instances of double non-taxation of income (National Treasury, 2017b, 7-8). Subsequently, in 2020, the exemption limit was revised upwards to R1.25 million, however, the qualifying requirements of s 10(1)(*o*)(ii) remained the same.

In Chapter 3 the qualifying requirements of s 10(1)(*o*)(ii) were discussed and it became apparent that the requirements of the foreign employment income exemption are technical in nature. Several interpretation notes issued by SARS, case law and South African income tax books were referred to, to fully analyse the application of each requirement. Once a South African resident satisfies the qualifying requirements of s 10(1)(*o*)(ii) exemption, further challenges arise, namely: how to account for the exemption in the payroll if the South African resident expatriate is employed by a South African employer; how to claim the exemption on his/her ITR 12 and what supporting documents need to accompany such a claim; an employer needs to account for the additional tax liability where their employee, the South African resident expatriate, is tax equalised[42]. In addition, the South African resident expatriate or his/her employer may need to engage the services of an international tax consultant to assist with their s 10(1)(*o*)(ii) claim, double tax relief measures and the administrative and compliance processes associated with ‘expat tax’. This is an extra cost for the South African resident expatriate and/or his employer which may not have been necessary before the introduction of the exemption limit. It is clear from the discussion in section 5.6, a substantial administrative and compliance burden is placed on a South African resident expatriate when applying the qualifying requirements of s 10(1)(*o*)(ii) and claiming the exemption on an ITR12.

A South African resident expatriate may, after qualifying for the s 10(1)(*o*)(ii) exemption, still suffer double taxation on the same income. In these circumstances, two methods of relief for double taxation

[42] Refer to section 6.4 for a discussion on tax equalisation and the impact on the employer.

are available, namely: unilateral relief under South African domestic law in terms of s 6*quat* and bilaterally by way of DTAs and these relief methods were analysed in section 4.2.2 and 4.2.3.

The application of s 6*quat* is challenging and requires a South African resident expatriate or their tax professional to have a thorough understanding of the specific provisions. A South African resident expatriate may only claim the s 6*quat* rebate when their own tax return is submitted which presents a cash flow problem. Employees' tax is due and payable monthly in South Africa and the foreign country (if applicable) and foreign tax credits cannot be taken into account when preparing the South African payroll. (Grange et al., 2017, 10.) However, a South African employer may apply for a tax directive to take into account the potential foreign tax credit to determine the employee's tax liability on a monthly basis (paragraph 10 of the Fourth Schedule of the Act). As discussed in section 5.6, further complications develop as a result of a South African resident expatriate's claim for a s 6*quat* rebate on his/her ITR12, namely, providing sufficient proof to SARS of foreign taxes paid may prove to be difficult, different tax years may complicate calculating a s 6*quat* rebate and not all foreign taxes qualify for the s 6*quat* rebate.

If a DTA is in force between South Africa and a foreign country, a South African resident expatriate may use this method for the relief of double taxation. The general rule for foreign employment income is that the source state receives the taxing rights, and the residence state must provide a credit for the foreign tax paid (OECD, 2017, 305). The majority of the DTAs between South Africa and foreign countries provide for the elimination of double taxation under the ordinary credit method which limits the deduction from local tax to the residence state's own tax applicable to the foreign income. The article in a DTA that deals with the elimination of double taxation can be 'subject to' the provisions of domestic law relating to the granting of credit for foreign taxes (i.e., s 6*quat*) or the article can make no reference to the domestic law (SARS, 2020b, 66). If the elimination of double taxation article is not 'subject to', a South African resident expatriate may elect to apply the DTA credit method of relief instead of the s 6*quat* rebate method of relief (s 6*quat*(2)). The disadvantage of applying the DTA credit method is that a South African resident expatriate is not entitled to carry forward any excess foreign taxes under paragraph (ii)(aa) of the proviso to s 6*quat*(1B)(a).

The application of s 6*quat* and a DTA are fairly complex and will most probably require a South African resident expatriate and his/her employer to seek tax advice which comes with an associated cost (Grange et al., 2017, 10). Usually, if a South African resident expatriate is sent to a foreign country on assignment, the local employer will take responsibility for their employee's tax affairs and the associated cost. However, if the South African resident expatriate is employed abroad by a foreign employer, he/she is responsible for their own tax affairs.

In Chapter 5, a detailed comparative analysis was performed on a South African resident expatriate's taxable income calculations and resulting tax payable if the South African resident expatriate earned foreign employment income that qualifies for the s 10(1)(*o*)(ii) exemption in India, the UK and Dubai. Refer to section 5.5 for the summarised results of the detailed comparative analysis.

If the South African resident expatriate earned foreign employment income in excess of the R1.25 million exemption in India and the UK, the foreign employment income would be subject to double taxation and the South African resident expatriate may claim relief for double taxation under s 6*quat* or by way of DTA provisions.

If a South African resident expatriate earned foreign employment income of R1.5 million in India and the UK and applied either double tax relief measure, there would be no South African tax payable, however s 6*quat* may be a preferred method of double tax relief as it allows a taxpayer to carry forward any excess foreign tax to a succeeding year of assessment (para (ii)(aa) of the proviso to s 6*quat*(1B)(a)). Refer to section 5.5 for the South African tax payable calculations for the above conclusion.

However, if a South African resident expatriate earned foreign employment income of R5 million in India and the UK and applied either double tax relief measure, there would be an incremental amount of South African tax payable of R154 942 and R155 769 respectively. Refer to section 5.5 for the calculations supporting the South African tax payable amounts of R154 942 and R155 769. Consequently, in the instance where the tax paid in the foreign country is lower than the tax due in South Africa on the taxable foreign employment income, the South African resident expatriate will potentially have to pay the same amount of taxes as he/she would have had to pay if he/she were taxed only in South Africa. This was the conclusion reached in example 3 in section 5.5.

In Dubai, there is no personal income tax[43] and consequently a South African resident expatriate will only be liable for South African tax payable on foreign employment income over the R1.25 million exemption limit. Before the amendment to s 10(1)(*o*)(ii) in 2017 which took effect on 1 March 2020, foreign employment income earned in a no personal income tax jurisdiction (e.g., Dubai) by a South African resident expatriate would have been exempt in South Africa.

Thus, the amendment of s 10(1)(*o*)(ii) has prevented the double non-taxation of income but it had a significant financial impact on a South African resident expatriate earning foreign employment income in no or low tax jurisdictions. Refer to section 5.4.2 for the basis of this conclusion.

[43] Refer to section 5.3.1 Overview of the individual tax system in Dubai

In determining which double tax relief measure is a preferable option, a South African resident expatriate should consider the benefits and limitations of each tax relief measure. It seems from the analysis performed in Chapter 5 that s 6*quat* is a preferable option as:

(1) it allows the taxpayer to carry forward excess foreign taxes under paragraph (ii)(aa) of the proviso to s 6*quat*(1B)(a);
(2) if a taxpayer earns foreign employment income in more than one country there is no country limitation like that under a DTA;
(3) the taxpayer does not have to go through the complex evaluation to determine if a DTA is applicable and if the DTA applies, then interpret and apply the relevant Articles that refer to residence, income from employment and elimination of double taxation.

The amended exemption came into effect on 1 March 2020 and is effective for the 2021 South African tax year ended 28 February 2021 and subsequent years. It will be useful to do further research, to identify the double tax relief measure that has been applied by the majority of South African resident expatriates and the reasons behind their choice, as well as the resultant impact on SARS. If possible, the research should include reasons for audits, objections, and refunds; practical issues raised by tax practitioners related to claiming double tax relief on an ITR12; the ability of SARS to cope with the additional administration of returns with s 10(1)(*o*)(ii) exemptions and double tax relief claims.

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