TAX FLASH

BUDGET EDITION 2025

Content

We are proud to share our first *Tax Flash – Budget Edition*, in which WTS Renmere's experts share their views regarding tax and exchange control proposals announced in the 2025 Budget Speech of the National Treasury (RSA). We cover a wide array of topics, to illustrate the extent of our service offering.

1 Individual Income Tax

1.1 Personal income tax rates: More bracket creep and no relief for low-income earners

On 19 February 2025, the tabling of the Minister of Finance's (Minister) budget was postponed for the first time. When the budget was ultimately tabled on 12 March 2025 (Budget), it was announced that there would be no changes to the personal income tax brackets to account for the effect of inflation, for the 2025/2026 tax year (ending on 28 February 2026). This is sometimes referred to as bracket creep and the practical effect is that any increase in a person's income would now be taxed at a higher rate.

This is an unfortunate announcement, especially for lower income earners. In the budget documents that would have been tabled on 19 February 2025, which came to light after National Treasury lifted the embargo on budget documents issued and allowed reporting thereon, there was a different proposal. There, it was proposed that the bottom two personal income tax brackets and rebates be adjusted to fully compensate for inflation with the remaining brackets only being partially adjusted for inflation.

When income tax brackets are not adjusted for inflation, even a modest raise in salary could push an individual into a higher tax bracket, resulting in a greater proportion of their income being taxed at a higher rate. In some cases, this could offset the financial benefit of the salary increase, leaving the taxpayer with less disposable income than they initially expected. Consequently, individuals may want to carefully evaluate whether the extra income after tax will significantly improve their financial situation, or if the additional tax burden outweighs the potential benefits. It may also be wise to explore other factors such as potential tax-saving strategies or deductions that could mitigate the impact of higher taxes.

By way of illustration, if a taxpayer earned R15,000 in the 2025 year of assessment, the taxpayer's total tax payable for the year after only considering the primary rebate should equal c. R15,165 which results in an effective tax rate of c.8.43%. If both the personal income tax brackets and the taxpayer's salary are adjusted for inflation (for illustrative purposes, say 6%), in the 2026 year of assessment (i.e. the taxpayer now earns R15,900 pre-tax), the total tax payable for the year by the taxpayer would have been R16,075, also resulting in an effective tax rate of c.8.43%. However, since the personal income tax brackets are not adjusted for inflation, as proposed in the Budget, the total tax payable for the year by the taxpayer (based on an adjusted salary of R15,900) would be c.R17,109, which results in an effective tax rate of c.8.97%.

Danielle Annandale, Louis Botha & Dean van den Berg

1.2 Fenced in: Proposed expansion of the ring-fencing of assessed losses

Broadly speaking, an assessed loss arises when a taxpayer's 'taxable income' for a given year of assessment is negative.

Natural persons (and other taxpayers that are not companies) are permitted in terms of section 20(1)(a) of the Income Tax Act, 58 of 1962 (ITA) to set off against their 'taxable income' in a given year of assessment *"any balance of assessed loss incurred by that person in any previous year* *which has been carried forward from the preceding year of assessment".* This is subject to section 20A, which contains rules limiting the set-off of assessed losses realised in respect of different trades. For example, an individual could earn income from employment and from renting immovable property, which are seen as two separate trades.

The intention behind section 20A of the ITA is to ring-fence assessed losses arising from so-called 'suspect trades' carried on by natural persons. There are listed 'suspect trades', such as trading in crypto assets or where the taxpayer incurred losses in the relevant trade for at least three of the past five years. The effect of ring-fencing an assessed loss arising from a specific trade is that in future years, the assessed loss can only be deducted against income from that specific trade (and not against income from other trades). Currently, section 20A only applies where the maximum marginal tax rate applies to the taxpayer. In other words, his total taxable income exceeds R1.817 million. Even if a person has multiple trades, some of which may be suspect trades, section 20A would not apply if the taxable income requirement is not met.

The Budget states that government is of the view that the current application of section 20A enables taxpayers below the maximum marginal rate threshold to exploit the tax system by continuously offsetting losses from certain trades against other sources of income. In its view, this creates a loophole that leads to substantial revenue losses for the fiscus, as taxpayers receive full refunds of their employees' tax when those losses are allowed. As such, it is proposed that the threshold at which ring-fencing rules apply is to be reviewed and amended.

Individual taxpayers who conduct multiple trades but have escaped the application of section 20A solely by virtue of not falling into the maximum marginal tax rate bracket have to take note of this development. Depending on how government proposes to address this apparent loophole, the assessed losses incurred by such individuals from certain trades may become ring-fenced upon the amendment of section 20A.

Dewald Pieterse

2 Corporate Income Tax

2.1 Renewable energy incentive: Government backtracks?

In a media statement issued by Eskom on 31 January 2025, it was announced that following more than ten months of uninterrupted power supply due to the success of Eskom's 'Generation Recovery Plan', loadshedding would again be implemented. Since then, the country has experienced different stages of intermittent loadshedding.

Installed capacity of renewable energy generation resources under the Department of Mineral Resources' Renewable Energy Independent Power Producer Procurement Programme (REIPPPP) still only makes up a comparatively small proportion of the total generation capacity in South Africa. However, the Budget indicates that the overarching Independent Power Producer Procurement Programme has resulted in agreements for more than 8 588 megawatts (MW) of new generation capacity, totalling more than R280 billion in investment. To date, 6,331 MW are in operation and 2,257 MW of projects are still under construction and expected to become operational in 2025/26.

Key to the growing investment by the private sector in renewable energy production assets has been the favourable tax allowances afforded in terms of sections 12B of the ITA. Section 12B provides a write-off of capital expenditure incurred on machinery, plant, implement, utensil or article owned and brought into use for the first time by a taxpayer in generation of electricity through wind, photovoltaic solar energy, concentrated solar energy, hydropower (up to 30 megawatt) and certain biomass. The write-off period is generally three years (50/30/20), but this is reduced to one year for photovoltaic solar energy assets not generating more than 1 megawatt. Section 12B however restricts the ability of lessors to claim capital allowances in respect of qualifying assets unless the lease meets certain criteria (e.g. it exceeds five years and the lessee carries on a trade).

In response to the country's electricity crisis, section 12BA was introduced in 2023 to increase the capital allowance on qualifying assets used in the generation of electricity through renewable assets to 125% of expenditure incurred. The increased capital allowance only applied to qualifying assets brought into use for the first time by a taxpayer for purposes of carrying on a trade on or after 1 March 2023 and before 1 March 2025. Once the requirement was met, the 125% allowance was claimable in that year. Section 12BA did not impose a limit on generation capacity of the assets in question, nor did it contain the same restrictions as section 12B for lessors of qualifying assets. Section 12BA also resulted in substantial private investment in renewable energy generation.

In last year's budget (2024 Budget) it was announced that consideration would be given to the generation thresholds and leasing restrictions of section 12B, specifically the differentiation between photovoltaic solar energy assets, and that any resultant amendments would apply from 1 March 2025 when section 12BA ceased to apply. This created the expectation that the accelerated one-year write-off period catered for in section 12B would be extended to all photovoltaic solar energy assets irrespective of their generation capacity.

The Budget states that after careful consideration it is proposed that the generation capacity thresholds and leasing restrictions in section 12B will remain unchanged. Eskom's improved performance during 2024 may well have played a role in this decision by government, notwithstanding the recent setbacks experienced. Given the significant capital investment required to construct renewable energy generation assets, the capital allowances afforded to qualifying taxpayers and the timing thereof can have a significant impact on the commercial viability of and the cost of electricity generated by such projects. Government's decision not to remove the restrictions in section 12B to lend further fiscal support may well cause investors to rethink the viability of their planned investments or have an effect on the cost of electricity purchased by Eskom from independent power producers.

Eugene du Plessis

2.2 Asset-for-share transactions: Changes proposed for listed shares and collective investment schemes

In the context of transaction structuring, asset-for-share transactions, as contemplated in section 42 of the ITA, are one of the most common tools used. Broadly, section 42 of the ITA provides for tax roll-over relief, if certain requirements are met. The benefit of this provision is that in the context of disposing of capital assets for example, any capital gain arising from the disposal of the asset in question will be rolled over until a later stage, if certain requirements are met. One of the requirements is that where the asset holder is a South African resident, the person must dispose of the asset to a South African resident company, which must issue equity shares to the person in exchange for the asset received by the company. It is required that the proceeds of the asset disposed of must exceed its base cost. Further, there is also a so-called qualifying interest requirement, which differs depending on whether the company issuing equity shares has its shares listed on a recognized exchange or if it is merely a private company.

The Budget proposes amending the rules for these transactions in the context of listed shares, to align with the original policy intent. It appears the intention is to limit the rollover relief so that it only applies to shareholders holding less than 20% of the equity shares in the target company before the transaction. There is also a proposal to amend the provisions to prevent unintended tax avoidance in the context of transfers of shares to collective investment schemes.

Louis Botha & Jané Visagie

3 International Tax

3.1 Controlled foreign companies: Proposals to amend the high tax exemption

The 'controlled foreign company' (CFC) provisions are found in section 9D of the ITA. These rules effectively operate as a type of anti-avoidance regime by taxing South African resident shareholders in non-resident companies, in terms of the principle of attribution.

A foreign company is regarded as a CFC of a South African tax resident shareholder, *inter alia*, where South African tax resident shareholders collectively (i) hold more than 50%, directly or indirectly, of the CFC's participation rights; or (ii) can exercise more than 50%, directly or indirectly, of the CFC's voting rights. A foreign company will also be regarded as a CFC when its financial results are reflected in the consolidated financial statements of any company that is a resident, other than a headquarter company, as required under IFRS 10.

One of the aims of section 9D is also to tax passive income earned offshore by South African tax resident shareholders, where such income has not already been subjected to a sufficiently high tax rate in the foreign jurisdiction.

These specific tax rules, when applicable, may result in attribution of all or a portion of the CFC's 'net income' (essentially its foreign taxable profit/income) to its RSA tax resident shareholders on an accrual basis, as opposed to when funds are actually repatriated in future by the CFC (e.g. via dividends) – this attribution is typically done on a proportional basis with reference to the RSA tax resident shareholder's respective participation rights in the CFC (subject to certain exclusions).

Certain provisos to the determination of 'net income' in subsection 9D(2A) deem a CFC's net income to be nil in certain circumstances, potentially resulting in no effective attribution under the CFC rules for any South African tax resident shareholders. One of these provisos is the 'comparable tax exemption' (also known as the 'high-tax exemption'). Essentially, where a CFC's taxes payable on income in the foreign jurisdiction is equal to at least 67.5% of the amount of normal tax that would have been payable if the CFC's taxable income were subject to tax in South Africa at the domestic corporate tax rate of 27%, the CFC's net income is deemed to be nil. Simply stated, where the CFC is subject to a minimum effective tax rate of at least 18.23% in the foreign jurisdiction, the high-tax exemption should apply – this will however require an actual tax calculation to be performed under the CFC rules (i.e. computed as if the foreign company was subject to tax in South Africa).

The Budget states that Treasury is concerned that the comparable tax exemption does not consider tax systems of countries that allow a refund to certain shareholders of a foreign company for taxes paid by the company declaring the dividend. It is proposed that a tax refund to a shareholder in such circumstances should also be taken into account in applying the 'comparable tax exemption.' Arguably, such a refund to the shareholder would lower the effective tax rate of the foreign company when assessing application of the 'comparable tax exemption' and the minimum 18.23% threshold effective tax rate. One must bear in mind that this threshold tax rate is also affected by any fluctuations in South Africa's domestic corporate tax rate.

To the extent that the above merely amounts to a refund of sorts by a foreign country's tax authority in respect of dividend withholding tax otherwise levied on the shareholders, one would hope that this does not affect the amount of income tax calculated in respect of a CFC's net income. This is because the withholding tax is arguably a separate tax not levied on the income of the CFC, but on a subsequent distribution of after-tax profits. It remains to be seen how Treasury intends to treat such situations.

In order for multinationals operating in South Africa to remain commercially competitive, one would hope that Treasury carefully considers this proposed change to the CFC regime. This is to avoid any undue burden on South African tax resident shareholders in relation to their foreign subsidiaries and the income earned from such operations.

Jaco du Toit & Neethling van Heerden

3.2 Trust taxation turmoil: Further changes proposed to the taxation of trusts and trust beneficiaries

One of the most fundamental principles of the taxation of the trust concept is the so-called conduit pipe principle. This common-law phenomenon arguably enables the unmatched flexibility and versatility of the trust structure and distinguishes the way trusts function from other entity types. In essence, it enables income earned by a trust to flow through to the trust beneficiaries, pursuant to vesting of such income by the trust. However, the absolute nature of the flow-through principle was recently restricted with the 2023 amendment of section 25B of the ITA. Continuing this trend, Treasury has yet again proposed certain amendments, this time focusing on the interaction between section 7 and section 25B.

Section 25B of the ITA can be described as a deeming provision. It aims to regulate and determine which income, or part thereof, derived by a trust is taxable in the hands of which party. However, it is important to be cognisant that section 25B functions subject to section 7 of the ITA. Thus, Section 25B comes into operation only to the extent that section 7 does not already apply.

In 2023 section 25B was amended to align it with paragraph 80 of the Eighth Schedule to the ITA by limiting the flow through (conduit-pipe) principle only to resident beneficiaries. This limitation meant that any distribution to a non-resident beneficiary will no longer be taxed in the hands of the beneficiary, but rather in the hands of the trust. As a result, the tax rate applicable to the same amount vested in resident and non-resident beneficiaries now differs substantially. By virtue of this amendment, all income, including rental income and interest, vested in a non-resident beneficiary are taxed at the rate of 45% in the hands of the trust, whereas the marginal income tax tables will apply if the amount is vested in a resident beneficiary. The rate of 45% only applies to the portion of the resident beneficiary's taxable income above the marginal threshold.

The policy rationale for the 2023 amendment read as follows: *"The flow through of amounts by South African trusts to non-residents places SARS in a difficult position to collect income tax from those beneficiaries as they may not be taxed on foreign sourced amounts. Tax recovery actions may be difficult and in the case of non-resident trusts that are beneficiaries, SARS may not have information on the persons in whom the foreign trusts vest the income."*

In pursuance of the objective to further clamp down on the use of trusts for tax avoidance, the taxation of trusts and beneficiaries are once again in the spotlight. The Budget proposes that the interaction between section 7 and section 25B be reviewed, since the current rules may give rise to unintended consequences where non-resident beneficiaries are involved.

While the exact mischief Treasury intends to prevent remains to be seen, there may be a concern that where in certain circumstances a non-resident transfers assets to a South African trust, the application of section 7 before section 25B does not achieve the desired policy intent.

The ongoing scrutiny and proposed amendments to the taxation of trusts and their beneficiaries reflect a significant effort by Treasury to plug the perceived loopholes that have allowed for tax avoidance via trusts. It will be crucial for taxpayers and their advisors to stay informed and adapt to the changing landscape, ensuring compliance while navigating the complex realm of trust taxation.

Dr Hendri Herbst

4 Value-Added Tax

4.1 The VAT rate increases to 15.5% on 1 May 2025: What now?

The Minister announced an increase in the value-added tax (VAT) rate of 0.50% on 12 March 2025, taking effect on 1 May 2025, while a further 0.50% increase was proposed, effective 1 May 2026.

Registered VAT vendors now have a month and a half to comply with the amendment to ensure that –

- output tax is levied at the increased rate of 15.5% where applicable, and
- when claiming input tax, the correct rate is applied.

These changes require time and effort to implement, leaving VAT vendors little time to consider the effect that the increase may have on supplies made. Following the 2018 VAT increase from 14% to 15%, we learned that VAT vendors did not always consider all the scenarios relevant to the rate increase, therefore only realising the risks of non-compliance after the fact.

Time of supply vs date of goods provided/date of services performed

It is important that VAT vendors understand the difference between when goods are provided or when services are performed, since the provision date or performance date my differ from the supply date as per the Value Added Tax Act, 89 of 1991 (VAT Act). The following questions should therefore be considered, amongst others:

- Were goods provided before the date of the increase?
- Were goods provided in terms of a rental agreement, or agreement that provides for payments in instalments or periodically?
- Were goods provided or services performed directly in the construction, repair, improvement, erection, manufacture, assembly or alternation of goods where the consideration for the goods or services become due and payable in instalments or periodically in relation to the progressive nature of the work?
- Were services performed during the period beginning before, and ending before, on or after or after 1 May 2025?

If the answer to any of the questions is "yes", the time of supply rules in section 9 if the VAT Act should be applied to these transactions. The time of supply rules determine when VAT must be accounted for, not the performance or provision date, meaning, if the rate applied by the vendor was the lower rate of 15% based on a performance or provision date, the time of supply rule may determine that the increased rate of 15.5% should apply.

Fixed property & lay-by agreements

VAT vendors supplying fixed property, or goods under lay-by agreements should take additional care when applying a rate during the transition period. Vendors would be well advised that the underlying agreements to these supplies are reviewed in detail to determine whether VAT should be applied at 15% or 15.5%.

Rate manipulation

The VAT Act provides for specific rules in anticipation of vendors trying to manipulate the rate increase. If the time of supply rule for goods or services in section 9 deem the date of the supply to be between 12 March 2025 (announcement date) and 1 May 2025 (increase date), but the actual provision of the goods or performance of the service only follows after the increase date, the increased rate may be applicable. This is even if an invoice for the lower rate was issued between 12 March 2025 and 1 May 2025. Vendors should therefore consider outstanding customer invoices issued before 1 May 2025 and by applying section 67A(2) of the VAT Act to the facts of these invoice conclude why the increased rate of 15.5% should not apply.

Recommendation

Since it is proposed that the VAT rate will increase again on 1 April 2026, VAT vendors would be well-advised to ensure that they have a clear understanding of the impact a rate increase has on their business. It would thus be prudent that any decisions now made by VAT vendors to apply a specific rate to certain supplies are well documented, to ensure the same principles are applied, should the 2026 increase ensue.

Tom Combrink

5 Carbon Tax

5.1 Phase 2 no more? Budget proposals regarding the carbon tax signal an unexpected change

After Treasury published the discussion paper on phase 2 of the carbon tax in November last year for public comment, we indicated in a previous Tax Flash that we expected phase 2 to come into effect on 1 January 2026 as intended. This is because the start of phase 2 had been delayed more than once, partly due to economic challenges faced by South Africa, including those as a result of the Covid-19 pandemic and concomitant lockdown.

However, it appears that after the public consultation process and a Treasury workshop that took place in January 2025 to consider the public submissions made on the discussion paper, Treasury has had a change of heart. The changes now proposed to the Carbon Tax Act, 15 of 2019 (Carbon Tax Act), are not far-reaching.

The key proposals contained in the Budget regarding the carbon tax are as follows:

- The carbon offset allowance is proposed to increase by only 5 percentage points from 1 January 2026, that is, to 10% for fugitive and process emissions and to 15% for combustion emissions. Although the Budget states that future allowance increases may be considered in response to changes in the carbon market and associated standards, the discussion paper proposed that these percentages be set at 20% and 25% respectively for phase 2.
- Significantly, it is proposed that the basic tax-free allowance be maintained until 31 December 2030 as opposed to decreasing it gradually from 2026 as was proposed in the discussion paper. The reason given in the Budget relates to concerns around availability of low-carbon technologies, energy costs, competition, load-shedding and logistical challenges, consultations will take place for it to reduce only from 1 January 2031.
- The 30% trade intensity threshold used to determine the trade exposure allowance will remain the same and will not increase to 50%, given concerns raised around competitiveness. The threshold will be retained to allow a longer transitional period for hard-to-abate sectors.
- Extension of the commitment to electricity price neutrality, although the electricity generation levy will be removed from 1 January 2026 and the carbon tax will be applied to emissions from electricity. The carbon tax on electricity generation will be revenue neutral.
- Introduction of a greenhouse gas emission intensity benchmark from 1 January 2026, which will allow companies to qualify for a performance allowance if they outperform the approved sector intensity benchmark.

While the Budget does not indicate whether the implementation of phase 2 is again being postponed, if phase 2 indeed starts on 1 January 2026, it appears that there is not a significant departure from the current position.

The major disappointment is around the carbon offset allowance, as the discussion paper proposal, if followed, would potentially have increased investment into projects generating carbon offsets.

Louis Botha

6 Tax Administration

6.1 Clarifying the uncertainty around bona fide inadvertent errors

In the complex world of tax compliance, few terms have generated as much recent debate as *"bona fide inadvertent error."* This is evidenced by the Constitutional Court judgments in both the *Thistle Trust* and *Coronation* cases decided in 2024. It plays a crucial role in determining understatement penalties (USP) applicable where there has been an understatement by a taxpayer in their return. The term lacks a statutory definition, leading to varied interpretations and legal disputes, such as the two Constitutional Court matters. If there is no such error, the USP imposed can vary between 10% up to high as 200%, depending on how a taxpayer's behaviour is classified in terms of the USP table in section 223 of the Tax Administration Act, 28 of 2011 (TAA).

Notably, the Constitutional Court decided in *Thistle Trust* that no USP should be imposed, where the taxpayer argued that the understatement in question occurred because of a *bona fide* inadvertent error. The court ultimately decided in favour of the taxpayer on the USP issue, concluding that no USP should be imposed, even though it held in SARS' favour on the main issue regarding capital gains tax. In *Coronation*, the issue did not arise as the court held in favour of the taxpayer on the main issue pertaining to the application of the CFC provisions in the ITA.

The Budget proposes that the term "*bona fide inadvertent error*" be formally defined in the Tax Administration Act, 28 of 2011. Specifically, the Budget states the following:

"The concept and scope of a 'bona fide inadvertent error' has proven to be contentious. This concept is not explicitly used in similar understatement penalty frameworks, because these do not mix purely factual tests such as 'substantial understatement' with taxpayer behaviours in a single provision. To clarify the scope of 'bona fide inadvertent error', it is proposed that 'bona fide inadvertent error' be explicitly linked with 'substantial understatement'."

Currently, where the understatement arises as a result of behaviour classified as a substantial understatement, a USP of 10% will apply if the matter involves a standard case. In terms of the definition in section 221 of the TAA, a substantial understatement is present where the understatement exceeds the higher of 5% of tax properly chargeable, or R1,000,000.

While the proposal aims to provide clarity and consistency in the application of the phrase *"bona fide inadvertent error"*, it may result in a scenario where the benefit of being able to rely on it to escape a USP is limited. Based on the Budget proposal, it appears that by linking it to "substantial understatement", the intention may be that it only applies where the behaviour is classified as "substantial understatement". If that is indeed the case, it would potentially prejudice taxpayers. One concern is that it may then incentivise SARS to classify the behaviour as something other than "substantial understatement", so that a taxpayer cannot rely on the *"bona fide inadvertent error"* defence to escape the imposition of a USP.

Dr Hendri Herbst

7 Exchange Control

7.1 Good for investment? No major changes on exchange control

When it was announced a few years ago that South Africa's Exchange Control Regulations, 1961 (Regulations) would ultimately be replaced by a capital flows management framework, replacing the negative list system in place, there was great excitement. Although the Regulations have still not been replaced with this framework, there have been several relaxations since then. One of the most significant related to the foreign exposure limits for institutional investors. This changed to allow them to invest offshore up to 45% of the assets invested with them by retail investors.

The Budget notes that in the 2024 Budget, it was indicated that research would be undertaken to investigate the impact of these recent reforms to modernise the foreign-exchange system and in turn promote trade and investment. A draft review by the International Monetary Fund regarding 45% limit recommended that the limit not be reduced. This is something that will be welcomed by the South African investment industry and investors in general, especially in light of the recent developments involving the United States of America and President Trump.

Another interesting announcement pertains to the use of travel allowances where it is now proposed that the unused portion of a travel allowance, in other words, the amount with which the traveller returns, can be deposited into his foreign currency account within 30 days of returning.

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Kind regards,

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