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Interest Withholding Tax Effective From 1 March 2015

Posted on December 8, 2014 by c2m

The Taxation Laws Amendment Bill confirms the introduction of Interest Withholding Tax (IWT) at a rate of 15% effective from 1 March 2015. This is applicable to interest that is paid or that becomes due and payable to non-residents on or after that date. 

It is often difficult for tax authorities to collect income tax on the earnings derived by residents of other countries from business carried out in the source country. To enable the collection of taxes from non-residents in South Africa, SARS impose various withholding taxes. Normally a resident taxpayer is appointed as the non-resident's agent, and is obligated to withhold a certain percentage of tax from payments made to the non-resident and must pay it over to the tax authorities. If the resident agent does not comply with this duty or if he/she withholds an incorrect amount of tax, personal liability can be imposed on the resident agent.

- From 1 March 2015, interest will be taxable in South Africa at the withholding tax rate of 15%. Certain Double Tax Agreements will reduce the rate, some reducing the rate to 0%
- Dividends Withholding Tax (WHT) is levied on dividends declared at a rate of 15%. The dividend tax will generally be withheld by the company paying the dividend or a paying intermediary, and the net dividend will be paid to the shareholder.
- South African branches of foreign companies are taxed at a rate of 28%. No dividend withholding tax is imposed on the remittance of branch profits.

- There is a withholding tax of 15% on royalties paid offshore as from 1 January 2015 (previously 12%). This may be reduced per various Double Taxation Agreements, and in certain cases the rate is 0%.
- In the past, interest paid to foreign lenders was not taxable unless they had a permanent establishment in South Africa. This is not a prerequisite as from 1 January 2015.
- Withholding tax on service fees will be introduced from 1 January 2016, at the rate of 15%. This applies to non-residents providing services within South African. The withholding tax on services may also be reduced per various Double Taxation Agreements, and in certain cases the rate is 0%.

Note that the definition of “interest” extends beyond common law interest as it includes any discount or premium in respect of a financial arrangement as well as compensation payable by a borrower to a lender in terms of any lending arrangement. In addition, the provisions of section 24J of the Act deem repurchase agreements and resale agreements to be interest bearing. Qualifying repurchase and resale agreements are effectively treated as loans and the differential between the sale price and resale price of the underlying asset therefore constitutes interest.

The scope of the IWT provisions could extend wider than anticipated, for example to payments made in respect of financial arrangements entered into at a discount or a premium rate, lending arrangements, as well as repurchase and resale agreements.

Interest paid by a non-resident borrower to a non-resident lender may be subject to the IWT where the non-resident borrower has utilised or applied in South Africa, the funding obtained from the non-resident lender. This will result in a withholding obligation being placed on a non-resident. The impact of transactions such as these entered into between non-resident counterparties may not have been considered from a South African withholding tax perspective. Failure to comply with the IWT provisions could lead to an IWT liability and, inter alia, the imposition of penalties and interest on unpaid taxes.

The impact of the above will likely result in non-residents having to register as South African taxpayers in order to submit IWT returns. This may increase the tax compliance burden on non-residents. For example, a non-resident may be required to register as a taxpayer in order to submit an IWT return in instances where the non-resident in question is not required to make payment of any IWT.

Comments adapted from articles published online by Grant Thornton on 9 July 2014 and Michael Reifarh (ENSafrica) on 25 September 2014.