Extending CFC rules to foreign trusts and foundations

By Joon Chong

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On 19 September 2017, Webber Wentzel participated in the National Treasury workshop on the proposed changes in the draft Taxation Laws Amendment Bill, which extends the existing controlled foreign company (CFC) rules to include foreign trusts and foundations, and foreign companies.

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These include entities that are not necessarily subsidiaries of resident companies, but are considered to be "controlled" in terms of International Financial Reporting Standards 10 (IFRS 10).

Reviewing the public participation process

At the start of the workshop, attendees suggested methods that would allow the public participation process on the amendment bills to start earlier. Written submissions are currently only made after the draft bills are circulated (around July), followed by workshops on specific amendments. There is currently no further opportunity to comment on, essentially, the second draft of the bills, as any further amendments made to the (first) draft bills are only publicly available when the final bills are introduced in parliament.

Going forward, we hope that National Treasury would start the workshop process to discuss significant amendments in Annexure C soon after the 2018 Budget is tabled. National Treasury would have the opportunity to discuss the tax policies behind these amendments at these workshops. Attendees would then be invited to make written submissions after the workshops. National Treasury could then already take these written submissions into account when drafting the (first) draft bills circulated around July. There is then a further opportunity to make written submissions and participate in workshops on the draft bills after they are circulated, effectively providing two rounds of written submissions and participation before the final bills are tabled.

Two options

On the proposed amendments to the CFC rules, it appears from the workshop that National Treasury are considering two possible options for these amendments in the final bill for 2017:

- Option 1 involves deleting the extension of the new definition of CFC to foreign trusts and foundations holding more

than 50% of participation or voting rights in a foreign company, and also deleting section 25BC. Section 25BC may be revisited in 2018.
- Option 2 involves retaining the extension to foreign trusts and foundations with clearer references to beneficiaries of the foreign trust. The concept of "foreign foundation" would also be defined. Section 25BC would be amended to deal with potential double taxation of income, foreign tax credits, philanthropic distributions, and exclusions in section 9D. Section 25BC would also be amended to clarify the interaction between this section and section 7, 25B(2A) and the Eighth Schedule.

In both options above, the extension of the new definition of CFC to include any foreign company where the financial results of this company are reflected in the consolidated financial statements of a resident company in terms of IFRS 10, would be retained. The proposed further proviso to section 9D(2) would, however, be amended to include only the financial results of the foreign company to the resident company on a net percentage basis.

Given the additional work required on redrafting section 25BC in option 2, the hope is that National Treasury selects option 1 in the final bill for 2017.

ABOUT THE AUTHOR

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