DISSERTATION (FTX5032W)

A COMPARATIVE ANALYSIS OF THE FOREIGN TAX CREDIT SYSTEM OF SOUTH AFRICA, WITH SPECIFIC REFERENCE TO CORPORATE TAXPAYERS AND TECHNICAL SERVICE FEES

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Douglas Allanson
Cape Town, February 2021

ABSTRACT

The growth in the worldwide services economy combined with an expansion by South African multinational enterprises into the African market has often resulted in increased instances of double taxation for South African corporate taxpayers, as a result of the fact that the majority of the jurisdictions in Africa apply a withholding tax on technical service income paid to non-residents.

The ability to claim relief for the juridical double taxation suffered as a result of the withholding tax applied is governed in South African tax legislation by section 6*quat* of the Act.

This paper analyses section 6*quat* of the Act with particular reference to the relief available and unavailable to taxpayers for foreign taxes paid in relation to withholding taxes on technical service fee income, in treaty and non-treaty scenarios. The issue of continued double taxation, despite the relief mechanisms of section 6*quat*, resulting from source issues and the provision of services remotely from South Africa or differing interpretation on the application of Double Taxation Agreements by South Africa and the foreign jurisdictions for example, are also reviewed.

South Africa's relief mechanisms are then compared to the relief mechanisms of 5 other jurisdictions (peer nations who export services) to determine if any of these jurisdictions have more advanced ideas for the reduction of juridical double taxation in the context of technical service fees.

It is determined in the final analysis that South African taxpayers are not alone with regard to the problem of unrelieved double taxation despite the best efforts of local legislation to provide some form of relief. None of the jurisdictions reviewed have mechanisms in place that provide full relief whilst also protecting the tax base.

A number of recommendations are given for ways that South Africa could possibly improve the situation and reduce instances of juridical double taxation. The most obvious being a wide treaty network, with up-to-date treaties, with as many jurisdictions as possible, with a technical services article.

ABBREVIATIONS AND ACRONYMS

ATAF	African Tax Administration Forum
BEPS	Base Erosion and Profit Shifting
DTA	Double Taxation Agreement
DTR	Double Tax Relief
EU	European Union
FTC	Foreign Tax Credit
GBL	Global Business License
GDP	Gross Domestic Product
HMRC	HM Revenue and Customs
ICT	Information and Communications Technology
IRC	Internal Revenue Code
MNE	Multinational Enterprise
MAP	Mutual Agreement Procedures
MRA	Mauritius Revenue Authority
MTC	Model Tax Convention
OECD	Organisation for Economic Co-operation and Development
PE	Permanent Establishment
SARS	South African Revenue Services
STC	Secondary Tax on Companies
TAA	Tax Administration Act
TIOPA	Taxation (International and Other Provisions)
UK	United Kingdom
UN	United Nations
USA	United States of America
USD	United States Dollar
WTO	World Trade Organisation

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CHAPTER 1: INTRODUCTION AND BACKGROUND

1.1 Background

In a globalised business environment, companies not only trade within their own jurisdiction but will generally also engage in cross-border trade with customers and suppliers in foreign jurisdictions. Where a company is resident in a country which has adopted a worldwide basis of taxation, the income derived from sales to local and foreign parties would be included in the taxable income of that company.[1]

A company that provides services (whether of a technical, managerial, consulting or professional nature) as part of its portfolio, will often be subject to withholding taxes on the payment of fees derived from the provision of those services to customers in foreign jurisdictions. This is especially true when provided to customers in developing economies, such as those within the African continent, as these jurisdictions engage in efforts to protect and expand their tax bases. A comparative table of withholding taxes in Africa is presented in the attached Annexure 1.[2]

Since 2001, South Africa has adopted the worldwide basis of taxation. Thus, a corporate taxpayer, resident in South Africa, is subject to tax on their worldwide taxable income, which is derived from a source within, or deemed to be within, South Africa as well as from a source outside of South Africa.

A South African company trading in the services industry, cross-border, will inevitably encounter situations where tax is withheld on payments by the foreign customer, in terms of their domestic tax legislation, to the company for services provided.

Tax may be withheld by the foreign customer on payment of the service income to the South African supplier, as the foreign jurisdiction may deem the service income to have been derived from a source within their jurisdiction, as a result of the consumption of the services and benefit being received in that jurisdiction or as a result of payment being

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[1] Although some source basis countries may specifically include certain foreign income items into the tax net in a hybrid form of source and residence basis of taxation.

[2] Refer to Annexure 1: *Withholding Taxes on Technical Service Fees in Africa*.

derived from that country. Foreign sourced income may sometimes be taxed by both the country of source as well as the country of residence, being South Africa, leading to juridical double taxation.[3]

Relief from double taxation can be granted bilaterally, by means of a Double Taxation Agreement ("DTA"), or unilaterally by means of the domestic legislation of the country concerned.

The relief so granted can be by means of a credit, a deduction, an exemption or a combination of these relief methods. Most countries provide unilateral relief by means of a mixture of these methods.

In South Africa, relief is generally granted by means of the credit and deduction methods, together with a number of exemptions which are granted on various foreign sourced income items received by, or accrued to, residents.[4]

The credit method is governed, in South African domestic legislation, by the provisions of section 6*quat* of the Income Tax Act No. 58 of 1962 ("the Act").

The unilateral relief in the form of a foreign tax credit ("FTC"), is only available in South Africa where the source of the service fee income is deemed to be from a source outside of South Africa and, where that foreign tax paid, is proved to have been paid or payable to a foreign government.

In a number of treaties which South Africa has entered into, even bilateral relief in the form of an FTC may be subject to the provisions of the FTC rules in terms of section 6*quat* of the Act.[5]

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[3] South African Revenue Service, *Interpretation Note 18 (Issue 3), Sections 6quat, 6quin and 64N: Rebates and Deduction for Foreign Taxes on Income,* at par. 2 pg. 4, 26 June 2015, [hereinafter SARS IN18 Issue 3].
[4] Ibid at par. 2 pg. 5.
[5] Ibid at par. 4.9 pg. 64-77.

Foreign taxes which do not qualify for relief in the form of a credit, can be deducted, as an expense, from the taxable income of the resident, subject to provisos, in terms of section 6*quat*(1C) of the Act.

South Africa's interpretation of source in terms of FTCs is laid out in SARS Interpretation Note 18.[6] This interpretation of source can create problems of unresolved double taxation, in both treaty and non-treaty scenarios.

Where services are provided to a foreign customer, virtually or digitally from South Africa, the foreign jurisdiction may consider the source of the income to be that foreign country, as that is where the service is consumed, the benefit is received and where the payment is being sourced from.

South Africa, however, may deem the source of that income to be South Africa where the service was not physically provided in the foreign jurisdiction. Where South Africa deems the source of the income to be from within South Africa, no relief in the form of an FTC would be granted, in terms of section 6*quat* of the Act, as this is deemed to be domestic income. Partial relief in the form of a deduction for the foreign tax paid, may however be allowed. This same item of income is then taxed in the foreign jurisdiction and South Africa.

In treaty scenarios, the problem can usually be resolved if the treaty between South Africa and the other contracting state contains a specific technical fees article which deems the source and therefore taxing rights. The source of the service income generally being seen to be that of the recipient of the services, if a deemed source rule is included in the article.

Article 23 of the treaty (using the OECD Model Tax Convention ("MTC") for 2017 as proxy[7]) will then impose an obligation on South Africa to provide relief, subject to certain provisos, in the form of a tax credit, effectively overriding the provisions of section 6*quat* of the Act, which would otherwise have denied such credit. In certain cases,

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[6] SARS IN18 Issue 3.

[7] OECD (2017), *Model Tax Convention on Income and on Capital: Condensed Version 2017*, OECD Publishing. http://dx.doi.org/10.1787/mtc_cond-2017-en, [hereinafter OECD MTC 2017].

however, the article is structured in such a way as to impose the South African domestic legislation on the double taxation elimination process, which could result in the denial of tax treaty relief.[8]

The problems of unresolved double taxation that could arise where treaties are in place, occur where those treaties either have a technical service fee article that does not have a deemed source rule or where the treaties do not have a technical service fee article or technical service fee clause in any other articles. In these instances, the interpretation of technical service fees and source, as well as the applicability of other treaty articles, such as the Business Profits or Royalties articles, are paramount to determining taxing rights and the relief to be granted.

In addition to the above there is the problem, in treaty scenarios, where jurisdictions do not abide by the reduced withholding rates in terms of the treaty, or applicability of other treaty articles, and withhold tax in terms of their domestic rates. This may often be the result of foreign customers being unaware of the treaty implications and simply withholding based on domestic rates, or of suppliers being unaware of administrative procedures which need to be followed in order for a reduced rate to apply.

If South Africa grants a credit, it will only be in terms of the amount allowed by the treaty. The difficulty in obtaining refunds, for excess or incorrect taxes withheld, from African jurisdictions especially, compounds this problem. The poor statistics of South African taxpayers making use of Mutual Agreement Procedures ("MAP") also alludes to difficulties in resolving conflicts such as this through MAP.[9]

In non-treaty, and certain treaty, scenarios, where services are provided cross-border but virtually from South Africa, South Africa's interpretation of source will effectively deny the taxpayer relief, as the credit will likely not be granted, resulting in unresolved double taxation for which only minimal relief (a deduction) is granted in terms of section 6*quat*(1C) of the Act. Again, the South Africa supplier's options are often limited as obtaining refunds of tax withheld from foreign tax jurisdictions, especially in Africa, are

[8] SARS IN18 Issue 3 at par. 4.9 pg. 64-77.
[9] Organisation for Economic Co-Operation and Development (OECD), *Mutual Agreement Procedure statistics per jurisdiction for 2018*, South Africa, http://www.oecd.org/tax/dispute/2018-map-statistics-south-africa.pdf.

often difficult and not practical for the South African taxpayer in terms of a cost vs. benefit analysis.

This dissertation aims to analyse the problems of unresolved juridical double taxation, in treaty and non-treaty scenarios, for South African corporate taxpayers, with regard to taxes withheld on technical service fees, resulting from the South African interpretation of source. It will review the FTC mechanisms created to provide relief in terms of the Act as well as the interaction of these mechanisms with treaties, where applicable. Interpretation Notes as well as various commentary thereto will also be reviewed. This will also include the withdrawal of section 6*quin* of the Act.

The insights gained from the analysis of the MTC's and the practical application of the relief provided by the other countries analysed in the comparison, may assist in providing recommendations for the reduction of instances of unresolved double taxation in South Africa in respect of technical service fees.

1.2 Research questions

In terms of the introduction above, the dissertation aims to provide answers to the following:

1.2.1 Is the SARS interpretation of source, in the context of technical service fees, outdated when considered against the growth of the digital economy and the provision of virtual services?

1.2.2 Is South Africa alone, amongst its service exporting peers, with regards to its interpretation of source in the context of technical service fees?

1.2.2.1 Can any guidance be obtained from these peers with regard to their treatment of unresolved double taxation and technical service fees in both treaty and non-treaty scenarios?

1.2.3 Would a technical service fee article or clause in South Africa's treaties assist in resolving instances of juridical double taxation?

1.2.4 Would the reintroduction of a provision similar to the withdrawn section 6*quin* of the Act, assist in providing relief against foreign tax incurred by taxpayers on technical service fees, when presented with unresolved double taxation in

a non-treaty scenario? Can this be done whilst also limiting any negative impact on the tax base?

1.3 Research method

The research methodologies to be applied in this dissertation, are derived largely from the doctrinal research method and specifically include the descriptive and comparative legal research methods.

The research will begin with an analysis of the FTC system in South Africa in terms of domestic legislation, as well as the SARS interpretation thereof, with specific reference to technical service fees.

This will entail a review of relevant information which includes South African and international literature and commentaries, relevant case law, the MTC's of the OECD, UN and ATAF (as well as their commentaries), relevant DTAs and various opinions by South African and foreign commentators.

A comparative analysis will also be performed on the FTC systems imposed by other foreign jurisdictions in the context of technical service fees. This will include a brief overview of the relevant jurisdiction's source rules.

The impact of the relatively limited utilisation by taxpayers of the remedies provided by MAP within Africa on this form of double taxation, as well as the perceived poor outcomes when MAP is used, will also be briefly examined.

1.4 Limitation of scope

The scope of the dissertation will be limited to corporate taxpayers only.

The focus will be on technical service fees earned from, and withholding tax withheld by, African jurisdictions. The scope will further be limited to those technical service fees which are not rendered physically in the foreign jurisdiction i.e. provided remotely or virtually from the corporate taxpayers' resident country.

The comparative analysis will focus on countries which export services into Africa namely the United States of America ("USA"), the United Kingdom ("UK"), Mauritius, India and Sweden.[10]

1.5 Structure of the dissertation

The dissertation will consist of 6 chapters, with Chapter 1 being the Introduction.

Chapter 2 will review the domestic legislation of South Africa with regard to its FTC system. The chapter will also review the SARS interpretation of the legislation governing this system and its views on source. The chapter will also review the reasons behind the withdrawal in South Africa of section 6*quin* of the Act.

Chapter 3 will focus on the scenarios of juridical double taxation still resulting after the application of section 6*quat* in South Africa.

Chapter 4 will review the decision not to implement sections 51A to 51H of the Act in relation to a South African withholding tax on technical service fees. It will also review the MTC's of the OECD, UN and ATAF, and their commentaries with regard to technical service fees. An analysis will also be done on which models have a technical service fee article. A review of the relevant models and commentaries relating to the "Elimination of Double Taxation", "Business Profits" and "Other Income" articles will be included. The chapter will also include commentary on the digital economy and the import/export of technical service fees. The chapter will also review the DTAs that South Africa has in place and which of them have technical service fee articles and "subject to domestic legislation" clauses.

Chapter 5 will focus on the jurisdictions selected for comparative analysis. The chapter will be split per jurisdiction and will include a basic analysis of each jurisdiction's unilateral relief measures with specific reference to technical service fees and whether instances of unresolved double taxation arise in treaty and non-treaty scenarios. The methods these jurisdictions use to combat these issues will also be analysed.

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[10] These countries are being analysed as they are large exporters of services into Africa as a result of the global technology companies that are resident within their jurisdictions.

The treaty network of these jurisdictions, relating to Africa, will also be examined and those DTAs with technical service fee articles will be noted.

Chapter 6 will summarise the dissertation and provide conclusions and recommendations based on the analysis performed.

CHAPTER 2: UNILATERAL RELIEF AND THE FOREIGN TAX CREDIT SYSTEM OF SOUTH AFRICA

2.1 Relief from double taxation

Amounts derived by a resident of South Africa, or any other country, from a foreign source may at times be taxed in the country of source as well as the country of residence, resulting in juridical double taxation.[11]

Juridical double taxation refers to the situation where a taxpayer is taxed twice with respect to the same item of income or capital. In an international context, this form of double taxation occurs where two or more jurisdictions tax the same taxpayer on the same income or capital.[12] It occurs as a result of overlapping taxing rights and conflicts of the qualification of the income by the domestic rules applied by the relevant jurisdictions.

Relief from double taxation resulting from the imposition of tax by a source country and a residence country on the same amount of income, is generally granted by the country of residence of the taxpayer concerned. Countries can provide relief unilaterally, through provisions in their domestic law, or bilaterally through DTAs entered into between two contracting states.[13]

Tax treaties generally also include provisions which aim to avoid income being taxed twice in the hands of the same taxpayer by both contracting states. Treaty relief is often in the form of an exemption or credit.[14]

2.2 Section 6*quat*: history and purpose

The primary legislation governing South Africa's system of unilateral relief through an FTC or deduction mechanism, is section 6*quat* of the Act.

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[11] SARS IN18 Issue 3.

[12] Saw, R '*How Double Taxation Arises – The Role of Domestic Tax Systems*' in O Ostaszewska & B Obuoforibo (eds) *Roy Rohatgi on International Taxation Volume 1: Principles*, at par. 2.2.2. at pg. 21, IBFD, 2018.

[13] SARS IN18 Issue 3 at par. 2 at pg. 4, 26 June 2015.

[14] Vlasceanu, R '*Double Taxation Relief*' in O Ostaszewska & B Obuoforibo (eds) *Roy Rohatgi on International Taxation Volume 1: Principles*, at par. 3.1. at pg. 25, IBFD, 2018.

The basis of section 6*quat* of the Act, in its current form,[15] was inserted into the Act in 1987.[16] South Africa at the time taxed income in terms of the source basis of taxation. As a result, this version of the rebate provision was relatively simple and straightforward, as it generally only applied to foreign taxes incurred on dividend income.

Significant amendments were made to section 6*quat* in 1997 as a result of the introduction in that year of sections 9C (Circumstances in which proceeds from disposal of shares are deemed to be capital) and 9D (Net income of controlled foreign companies) of the Act.[17] These new sections, at the time, taxed South African residents on their worldwide passive income.[18] Further amendments in this regard, were made in 2000 as a result of the insertion of section 9E, which dealt with the taxation of foreign dividends.[19]

The introduction of the worldwide, or residence, basis of taxation to South Africa in 2000 resulted in substantial changes to the content of section 6*quat* of the Act.[20] Changes to section 6*quat* were not treated as an amendment but rather as a substitution of the entire section.

Up until the changes of the Revenue Laws Amendment Act No. 59 of 2000, section 6*quat* largely dealt with foreign taxes suffered on investment, dividend and other passive income, which was received or accrued from a source within, or deemed to be within, the Republic.

The implementation of the worldwide basis of taxation extended the income tax base of residents of South Africa to include income from all sources, within or outside of the Republic, subject to certain provisos and exclusions. The revised version of section 6*quat*

[15] Prior to the current section 6*quat* which relates to the rebate in respect of foreign taxes on income, it was previously inserted in terms of section 9 of Income Tax Act No. 89 of 1969 as a rebate provision in respect of diamond profits tax. This version of section 6*quat* was subsequently repealed in terms of section 5 of Income Tax Act No. 94 of 1983.
[16] Inserted in terms of section 5 of Income Tax Act No. 85 of 1987.
[17] Amended in terms of section 5 of Income Tax Act No. 28 of 1997.
[18] Department of National Treasury, *Explanatory Memorandum on the Revenue Laws Amendment Bill, 2000,* at pg. 2, Government of the Republic of South Africa [hereinafter 2000 Explanatory Memo].
[19] Amended in terms of section 15 of Taxation Laws Amendment Act No. 30 of 2000.
[20] Amended in terms of section 4 of Revenue Laws Amendment Act No. 59 of 2000.

therefore, provided for a rebate on foreign taxes paid on all foreign sourced income included in the gross income of the South African resident, subject to certain provisos.

Onshore mixing of FTCs was also allowed in the amendment and the carry forward period for excess FTCs was extended from three to seven years, subject to provisos. The ability to utilise excess FTCs against Secondary Tax on Companies ("STC"), however, fell away.[21]

The amendment of section 6*quat*(1)(a), which dealt with source, effectively resulted in no credit being claimable, through subsection (i), if the foreign income was from or deemed to be from a source within the Republic.[22]

Two further sets of amendments were processed in 2001,[23] largely relating to the introduction of Capital Gains Tax in South Africa.

In 2002, a number of substantial amendments were introduced.[24] National Treasury noted these amendments were as a result of technical corrections which were required to further refine the legislation after the implementation of the worldwide basis of taxation.[25]

One of these technical corrections related to the question of whether an item of income arose in South Africa or in a foreign jurisdiction. It was reiterated, that only foreign source income, or income from a source outside of the Republic, is eligible for a section 6*quat* rebate.[26] The ability to claim a rebate on foreign taxes paid on certain income items (related to mineral rights, mining and government service) deemed to be from a source within the Republic was abolished with the deletion of section 6*quat*(1)(a)(ii). The remainder of the explanation for the section 6*quat* amendment dealt with the introduction of source rules into the Capital Gains Tax provisions of the Act.[27]

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[21] 2000 Explanatory Memo, at pg. 10.
[22] Ibid. at pg. 13.
[23] Section 8 of Taxation Laws Amendment Act No. 5 of 2001 and section 20 of Second Revenue Laws Amendment Act No. 60 of 2001.
[24] Amendments in terms of section 9 of Revenue Laws Amendment Act No. 74 of 2002.
[25] Department of National Treasury, *Explanatory Memorandum on the Revenue Laws Amendment Bill, 2002*, at pg. 9, Government of the Republic of South Africa [hereinafter 2002 Explanatory Memo].
[26] 2002 Explanatory Memo, at pg. 11.
[27] 2002 Explanatory Memo at pg. 16.

Around this time, SARS released the first issue of Interpretation Note 18 which dealt with section 6*quat* under the subject, Rebate for Foreign Taxes: Natural Persons. This Interpretation note was relatively simplified, only dealt with natural persons and did not make any detailed reference to the applied interpretation of source or deemed source.[28]

In 2007, the title of section 6*quat* was amended to read "Rebate or deduction in respect of foreign taxes on income". Subsection (1C) of section 6*quat* was inserted which provided taxpayers with the opportunity to treat the foreign tax paid, on income which was deemed to be from a source within the Republic in terms of section 6*quat*(1)(a), as a deduction in the determination of the taxable income of the taxpayer.[29]

The Explanatory Memorandum of 2007 again reaffirmed the South African position, that the foreign tax rebate cannot be claimed on foreign tax incurred on income which has been deemed to be from a source within South Africa. The specific example of services performed in South Africa is provided, with the memorandum further stating that foreign countries were incorrectly applying source jurisdiction rules in this regard.[30]

In 2009, SARS released issue 2 of Interpretation Note 18. This issue reflected the change in title and focus of section 6*quat* and no longer focused purely on individual taxpayers. Issue 2 now also contained substantially more detail than issue 1, with regards to source, the application of section 6*quat* and the interaction of the provisions of section 6*quat* with South Africa's DTAs in force.[31]

Amendments to section 6*quat* in 2011 were relatively minor and dealt with timing issues as well as the impact on section 6*quat* of the introduction of the new section 6*quin* (see 2.3 below).[32] The Explanatory Memorandum issued by National Treasury for these 2011 amendments however, contained detailed commentary on the issue of the source of

[28] South African Revenue Service, Interpretation Note 18 (Issue 1), *Section 6quat: Rebate for Foreign Taxes: Natural Persons*, 31 March 2003[hereinafter SARS IN18 Issue 1].
[29] Amendment in terms of section 7 of Revenue Laws Amendment Act No. 35 of 2007.
[30] Department of National Treasury, *Explanatory Memorandum on the Revenue Laws Amendment Bill, 2007*, at pg. 56, Government of the Republic of South Africa [hereinafter 2007 Explanatory Memo].
[31] South African Revenue Service, Interpretation Note 18 (Issue 2), *Section 6quat: Rebate or Deduction for Foreign Taxes on Income*, 31 March 2009[hereinafter SARS IN18 Issue 2].
[32] Amendment in terms of section 11 of Taxation Laws Amendment Act No. 24 of 2011.

income and the need for unified source rules and a unified approach to issues of source throughout the Act.[33]

It was the view of National Treasury that the current rules of source throughout the Act were varied, which together with differing interpretations and applications of the common law principles, gave rise to uncertainty.[34] The goal therefore for the 2011 amendments, as noted in the Explanatory Memorandum, was to align the rules and application thereof, whilst also providing clarity on governments' position.

Amendments to the source rules for dividends, interest and royalties were aligned with the source rules found under OECD model tax treaty principles, whereby the residence of the payor of the income items was considered as a determinant of source. These amendments resulted in the doctrine of originating cause as the main determinant for source no longer applying to these income items, as well as to gains from the disposal of an asset.[35]

Items of income that have a service element however, would continue to use the doctrine of originating cause as the main determinant for source.[36] In this regard, SARS would continue to rely on the South African common law principles and specifically on the outcomes of the *CIR v Lever Brothers & Unilever* case.[37]

The common law principles focus largely on where services are rendered to a foreign client, to be consumed outside of the Republic, but the services are physically provided from South Africa. The source of that fee income is deemed to be from within South Africa (Refer to 2.4 below for a further discussion on source).

In 2015, section 6*quat* of the Act was amended to accommodate the withdrawal of section 6*quin* of the Act with an amended form of relief.[38] The amendments were focused

[33] Department of National Treasury*, Explanatory Memorandum on the Taxation Laws Amendment Bill, 2011*, at par. 4.2 on pg. 95, Government of the Republic of South Africa [hereinafter 2011 Explanatory Memo].
[34] Ibid, at par 4.2 on pg. 96.
[35] Ibid, at par 4.2 on pg. 100.
[36] Ibid, at par 4.2 on pg. 100.
[37] South Africa, *Commissioner for Inland Revenue v Lever Brothers & Unilever Ltd* 1946 AD 441 14 SATC 1, 30 March 1946.
[38] Amendment in terms of section 6 of Taxation Laws Amendment Act No. 25 of 2015.

on the deduction clauses of the provision, in terms of section 6*quat*(1C). This allowed taxpayers to deduct, subject to various provisos, as an expense in the determination of taxable income, the withholding tax incurred on foreign service fee income deemed to be from a source within South Africa. The amendment also provided for mechanisms where the withholding tax suffered was subsequently refunded by the relevant foreign government.[39]

The most recent amendments, in 2017[40] and 2018[41], were of a relatively minor character, with no proposed amendments highlighted in the Draft Taxation Laws Amendment Bill of 2019.[42]

2.3 Section 6*quin*: history and purpose

In providing a more uniform interpretation of source with the amendments of 2011 to the Act, National Treasury did take note of the impact the common law doctrine of source would have on income from services provided to foreigners, specifically where that income was subject to withholding tax on payment.[43] This was found to be a particular issue with services exported into Africa, with African jurisdictions withholding tax on service fee payments, often incorrectly (where treaties are in place). The double taxation suffered as a result, would be afforded partial relief through the deduction method, as no credits would be allowed where the source of the income was deemed to be from South Africa. This was seen to potentially have a negative impact on South Africa's desire to become a regional financial centre.[44]

In order to combat this and the potential for corporates moving regional operations away from South Africa to more preferential jurisdictions, the National Treasury introduced section 6*quin* of the Act as a rebate in respect of foreign taxes on income from a source within the Republic.[45] This limited tax credit would be available solely to foreign taxes imposed on services rendered in South Africa.

[39] Department of National Treasury, *Explanatory Memorandum on the Taxation Laws Amendment Bill, 2015*, at par. 5.2 on pg. 51, Government of the Republic of South Africa [hereinafter 2015 Explanatory Memo].
[40] Amendment in terms of section 4 of Taxation Laws Amendment Act No. 17 of 2017.
[41] Amendment in terms of section 7 of Taxation Laws Amendment Act No. 23 of 2018.
[42] Draft Income Tax Amendment Bill of 2019, 30 July 2019.
[43] 2011 Explanatory Memorandum, at par 4.3 on pg. 100.
[44] Ibid, at par 4.3 on pg. 100.
[45] Inserted in terms of section 12 of the Taxation Laws Amendment Act No. 24 of 2011.

Clarification amendments to section 6*quin* of the Act were processed in 2012.[46] In 2015, the special foreign tax rebate in terms of section 6*quin* of the Act was withdrawn prior to implementation date.[47]

The section was withdrawn as National Treasury were of the view that its implementation encouraged South Africa's treaty partners to disobey the relevant provisions within the tax treaties, whilst also resulting in the indirect subsidisation of these countries by South Africa.[48]

2.4 Source

2.4.1 Definition of source

Whilst the Act contains specific source rules which relate to specific types of income, the concept of "source" is, in itself, not defined in the Act.[49]

Despite most states having their own basic source rules in their domestic law and despite the patterns which emerge with regard to the global understanding of source rules for particular items of income, there is no global standard or set of rules for source by which states must abide.[50] There is no universal definition or understanding of the meaning of "source".[51]

As a result of this, the problem can arise of juridical double taxation from a source-source conflict. A source-source conflict is where two (or more) jurisdictions treat the taxable income or capital of a taxpayer as having been sourced in each of their own respective states. Without any relief, the taxpayer is subjected to tax to the fullest extent of each state's laws.[52]

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[46] Amended in terms of section 4 of the Taxation Laws Amendment Act No. 22 of 2012.
[47] Amendment in terms of section 7 of Taxation Laws Amendment Act No. 25 of 2015.
[48] 2015 Explanatory Memorandum, at par. 5.2 on pg. 51.
[49] SARS IN18 Issue 3, par. 4.2.1. at pg. 12.
[50] Saw, R '*How Double Taxation Arises – The Role of Domestic Tax Systems*' in O Ostaszewska & B Obuoforibo (eds) *Roy Rohatgi on International Taxation Volume 1: Principles*, par. 2.1.3. at pg. 19, IBFD, 2018.
[51] SARS IN18 Issue 3, par. 4.2.1. at pg. 12.
[52] Saw, R '*How Double Taxation Arises – The Role of Domestic Tax Systems*' in O Ostaszewska & B Obuoforibo (eds) *Roy Rohatgi on International Taxation Volume 1: Principles*, par. 2.2.2.1. at pg. 22, IBFD, 2018.

In South Africa, where source is not covered by specific provisions in the Act, the source of an item of income is determined and interpreted under the common law principles as formulated by the South African courts.[53]

The generally accepted definition of source in terms of South African law, and to which SARS abides, was laid down by Watermeyer CJ in *CIR v Lever Brothers & Unilever Ltd* where it was stated that:

> "*the source of receipts, received as income, is not the quarter whence they come, but the originating cause of their being received as income and that this originating cause is the work which the taxpayer does to earn them, the quid pro quo which he gives in return for which he receives them"*.[54]

In terms of this judgement, where the source of particular amounts of income is an issue, the source is not derived from where payment of the fees is made but rather from what caused those fees to arise in the first instance and where that action is located. It is therefore necessary to perform a two-part analysis. First to establish the "originating cause" of the income and secondly to establish where that originating cause is located.[55]

2.4.2 SARS Interpretation of source

SARS issues Interpretation Notes from time to time on relevant topics. The Interpretation Notes are intended to provide guidance to various stakeholders on the interpretation and application of the provisions of the legislation administered by the SARS Commissioner.[56] In terms of South African law, Interpretation Notes are not binding on the courts or the taxpayer but could set out a "practise generally prevailing" in terms of the Tax Administration Act, which has significant legal impact on taxpayers.[57]

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[53] SARS IN18 Issue 3, par. 4.2.1. at pg. 13.
[54] *Commissioner for Inland Revenue v Lever Brothers & Unilever Ltd* 1946 AD 441 14 SATC 1 at 449-450.
[55] Williams, RC (ed), *Income Tax in South Africa Case and Materials* (1995), at pg. 17.
[56] South African Revenue Service, Interpretation Notes available at https://www.sars.gov.za/Legal/Interpretation-Rulings/Interpretation-Notes/Pages/default.aspx accessed on 4 September 2019.
[57] Strauss, B, Cliffe Dekker Hofmeyr, Tax & Exchange Control Alert 4 May 2018, "*Status of Interpretation Notes*" available at https://www.cliffedekkerhofmeyr.com/en/news/publications/2018/Tax/tax-alert-4-may-status-of-sars-interpretation-notes-.html accessed on 4 September 2019.

A "practise generally prevailing" is, in terms of s5(1) of the Tax Administration Act No. 28 of 2011 ("the TAA"), a practise set out in an official publication regarding the application or interpretation of a tax Act.

An "official publication" is defined in s1 of the TAA as a binding general ruling, interpretation note, practise note or public notice issued by a senior SARS official or the Commissioner.

As noted in 2.4.1. above, SARS will in most instances place reliance on the South African common law view of source being determined by the originating cause of the income. This view was confirmed in issues 2[58] and 3[59] of SARS Interpretation Note 18.[60]

In terms of SARS Interpretation Note 18, SARS adheres to the view that the source of income is not defined as "the quarter from whence it comes" but rather is defined in terms of "originating cause".[61]

Thus, in terms of this interpretation, technical services which are rendered virtually to a foreign customer in a foreign jurisdiction, whilst the service provider is physically present in South Africa, will be deemed to have its true source in South Africa.

2.5 Application of section 6*quat*

In order to qualify for any rebate under section 6*quat*, the taxpayer will need to meet certain income qualification requirements in terms of section 6*quat*(1). In terms of this, the taxable income of the resident taxpayer must include any one of a number of options in terms of this section.

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[58] SARS IN18 Issue 2.
[59] SARS IN18 Issue 3.
[60] This view is also upheld in the draft version of issue 4 of Interpretation Note 18.
[61] SARS IN18 Issue 3, par. 4.2.1. (b) at pg. 14.

For the purposes of this paper however, the focus is on section 6*quat*(1)(a) which states that the taxable income, as noted above, must include "*any income received by or accrued to such resident from any source outside the Republic*".

Once this income requirement is met, the foreign tax incurred on this income must meet four further requirements in terms of section 6*quat*(1A) in order to qualify for a rebate in terms of the Act.[62] The requirements for the rebate mechanism are as follows:

2.5.1 The tax must be payable on income

The foreign tax will only be accepted as a tax on income if the basis of taxation in the foreign tax jurisdiction is substantially similar to the provisions of the Act. Thus, the taxing system of the foreign jurisdiction should be compared with that of South Africa.[63] The foreign tax incurred must be a tax on income within the South African concept thereof.[64]

The foreign tax paid must also be a final tax. Withholding taxes which constitute an advance payment on an ultimate foreign tax liability will not qualify as a tax on income, however the ultimate final tax paid will.[65]

2.5.2 The tax must be proved to be payable to any sphere of foreign government

A tax will be "proved to be payable" if the resident taxpayer has an unconditional legal liability to pay the tax and the resident has either paid the tax or will have to pay the tax in future. This should be read together with the requirement for there to be no right of recovery for the foreign taxes paid.[66]

For the foreign tax paid to be "proved to be payable", the tax is also required to be have been levied legitimately in accordance with the foreign jurisdictions tax

[62] Section 6*quat*(1A) states "For the purposes of subsection (1), the rebate shall be an amount equal to the sum of any 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) by-(a) such resident in respect of – (i) any income contemplated in subsection (1)(a)".
[63] SARS IN18 Issue 3, par. 4.3.1. at pg. 20.
[64] Ibid, par. 4.3.1. at pg. 20.
[65] Ibid, par. 4.3.1. at pg. 21.
[66] Ibid, par. 4.3.2. at pg. 24.

laws, as well as with the relevant provisions of the DTA, where applicable. The foreign tax paid must not be in dispute and must be finally determined.

If the tax has been levied incorrectly, in SARS' view, even if it is paid and has not been challenged by the taxpayer, it will not be regarded as having been levied legitimately and cannot be proven to be payable or of not having any right of recovery.[67] In such an instance the rebate in terms of section 6*quat* will generally not apply to the amount of foreign tax which SARS deems to have been levied incorrectly or illegitimately, but can be challenged by the taxpayer.

In the instance where the provisions of the DTA have not been correctly applied and the foreign jurisdiction has withheld the incorrect amount of tax, such as withholding the domestic rate instead of the reduced rate per the DTA, the rebate is limited to the tax which may be levied in terms of the DTA. The excess withholding taxes in this regard will not qualify for a deduction under section 6*quat*(1C) or section 11(a).

The resident taxpayer will need to seek a refund of the excess withholding tax from the relevant foreign jurisdiction. Excess withholding taxes are seen to include instances where taxes have been withheld on technical service fee income and no technical service fee article exists in the DTA. SARS would be of the view that the Business Profits article applies and therefore South Africa, where the income is not earned through a PE, would have sole taxing rights. Thus, the entire amount of withholding tax is seen to be "excess".[68]

Lastly, the foreign tax must be payable to any sphere of government of a foreign country which includes taxes at a national, provincial, state, local or municipal level.[69]

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[67] SARS IN18 Issue 3, par. 4.3.2. at pg. 25. Despite this, it must be noted that there is no case law to support this view and, further, Interpretation Notes are not law and can be challenged in the courts.
[68] Ibid, Examples 12 and 13, at pg. 25.
[69] Ibid, par. 4.3.2. at pg. 27.

2.5.3 There must be no right of recovery

As noted above, there must be no right of recovery by the resident taxpayer with regards to the foreign taxes paid or payable. The phrase "right of recovery by any person" is interpreted very broadly and is not limited merely to refunds but any form of relief against a foreign tax liability.[70] In terms of SARS interpretation, this can include a refund, credit, rebate, remission, deduction or any other form of economic benefit to which a person becomes entitled to in consequence of the payment of the relevant tax.[71]

The existence of the right of recovery is the important factor, thus even if this right is not utilised, the right of recovery still exists and the rebate in terms of section 6*quat* will not be allowed.[72]

It is unclear whether access to MAP is considered to be a right of recovery available to the resident taxpayer. MAP is specifically excluded as a "right of recovery" in section 6*quat*(1C)(a)[73] but a similar exclusion is not noted in section 6*quat*(1A).[74]

2.5.4 The foreign income must be included in the resident's taxable income

Section 6*quat*(1A)(i)(a) states that the requirements of section 6*quat*(1A) are in respect of income contemplated in terms of section 6*quat*(1)(a) as noted above.

The last requirement is therefore that the income, on which foreign taxes have been incurred, must be included in the taxable income of the resident taxpayer

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[70] SARS IN18 Issue 3, par. 4.3.3. at pg. 29.
[71] Economic benefits can include Goods; Services; Fees or other payments; Rights to use, acquire or extract resources or other property; and discharge of contractual obligations.
[72] SARS IN18 Issue 3, par. 4.3.3. at pg. 29.
[73] Section 6quat(1C)(a) states "For the purpose of determining the taxable income derived by any resident from carrying on any trade, there may at the election of the resident be allowed as a deduction from the income of such resident so derived the sum of any taxes on income (other than taxes contemplated in subsection (1A)) paid or proved to be payable by that resident to any sphere of government of any country other than the Republic, without any right of recovery by any person other than in terms of a mutual agreement procedure in terms of an international tax agreement or 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".
[74] It is unclear whether SARS takes the view that a MAP procedure could be seen to also be a "right of recovery" in terms of section 6*quat*(1C)(a). This is not noted in the Interpretation Note 18.

in terms of the section 1 of the Act definition of taxable income, in order to qualify for the rebate in terms of section 6*quat*.[75]

Section 6*quat*(1B) then provides the detail on the calculation of the rebate and the limitations applicable thereto.

2.6 Limitations in terms of section 6*quat*(1B)

Section 6*quat*(1B)[76] provides detail of the general and certain specific limitations that are applied to the tax credit relief afforded by section 6*quat*(1).

In simple terms, the general limitation results in the tax credit available as a result of foreign tax paid being capped at the amount of South African tax payable, or the foreign tax paid if less. The South African resident taxpayer can therefore not obtain a credit for taxes paid which are in excess of the tax that would be normally payable in South Africa. The limit is thus designed to prevent a refund of normal tax where the foreign tax paid or payable exceeds the attributable South African tax payable on the foreign source income.[77]

The limit is determined by means of a formula as expressed by section 6*quat*(1B)(a) and can be recorded as follows:[78]

$$\text{Tax credit limit} = \frac{\text{Taxable income derived from } \textbf{all foreign sources} \text{ (A)}}{\text{Taxable income derived from } \textbf{all sources} \text{ (B)}} \text{ X Normal tax payable on (B)}$$

[75] SARS IN18 Issue 3, par. 4.3.4. at pg. 30. A foreign amount may be included in gross income but then excluded under an exemption which leaves no foreign amount included in taxable income.

[76] Section 6*quat*(1B) *Notwithstanding the provisions of subsection (1A) – (a) the rebate or rebates of any tax proved to be payable as contemplated in subsection (1A), shall not in aggregate exceed an amount which bears to the total normal tax payable the same ratio as the total taxable income attributable to the income, proportional, amount, taxable capital gain or amount, as the case may be, which is included as contemplated in subsection (1), bears to the total taxable income.*

[77] Hattingh, J (2019), *Chapter 36: Elimination and avoidance of international double taxation,* At par. 36.26. pg. 76, In De Koker, A P and Brincker, E (eds.) Silke on International Tax, LexisNexis.

[78] SARS IN18 Issue 3, par. 4.5. at pg. 3. A foreign amount may be included in gross income but then excluded under an exemption which leaves no foreign amount included in taxable income.

Taxable income is assumed to take on its defined meaning and as a result the profit for each item of foreign source income attributable to the resident taxpayer must be determined.[79]

This is done by deducting any allowable expenses which can be directly attributed to the foreign source income as well as deducting a portion, based on a fair and reasonable apportionment, of the total general expenses which are not directly attributable to income sourced from within or outside South Africa.[80]

The limitation ensures that the rebate is only available where foreign income has been included in the taxable income of the South African resident in a particular year. Thus, if there is no foreign income in a particular year, despite foreign tax being paid, the rebate will not be available.[81]

It is apparent from the calculation of the limitation that where there is no South African normal tax payable, such as in a case of a tax loss or an assessed loss brought forward, the rebate would also not be available.

The limitation formula also effectively pools all the foreign income and foreign taxes together for double taxation relief purposes. All the foreign income and foreign taxes for a particular year are calculated together, there is therefore no "per country" limitation.[82]

"Unused" credits are treated as excess credits in terms of section 6*quat*(1B)(a)(iB)(ii) and are "rolled over" to the immediately succeeding year, where it will potentially qualify as a foreign tax available for rebate. The excess credits can be "rolled over" for a period not exceeding 7 years determined from the date the excess credit was first carried forward.

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[79] Hattingh, J (2019), *Chapter 36: Elimination and avoidance of international double taxation,* At par. 36.26. pg. 76, In De Koker, A P and Brincker, E (eds.) Silke on International Tax, LexisNexis.
[80] SARS IN18 Issue 3, par. 4.5. at pg. 37. A foreign amount may be included in gross income but then excluded under an exemption which leaves no foreign amount included in taxable income.
[81] Ibid, par. 4.5. at pg. 36. A foreign amount may be included in gross income but then excluded under an exemption which leaves no foreign amount included in taxable income.
[82] Olivier, L and Honiball, M (2011), *International tax: a South African perspective*, 5th edition, at Chapter 17: Unilateral and Tax Treaty Relief at par. 2.2.2. pg. 453, Siber Ink.

The next chapter will touch on specific scenarios of double taxation that can arise and the interaction with the relief measures provided by section 6*quat*.

CHAPTER 3: JURIDICAL DOUBLE TAXATION, ON TECHNICAL SERVICE FEES, AS A RESULT OF (OR DESPITE OF) SECTION 6*quat*

Where technical services are provided physically, via virtual or digital means, from South Africa to a customer in a foreign jurisdiction, this can lead to double taxation for the resident taxpayer, under treaty as well as non-treaty scenarios, as a result of the provisions of section 6*quat*, as noted above, and interpretation of source.

3.1 Treaty scenarios and interaction with section 6*quat*

12 out of 79 of the DTAs that South Africa has in force currently contain a technical service fee article, whilst 2 out of the 79 DTAs (Saudi Arabia[83] and Netherlands[84]) contain a clause specifying that technical service fees must be dealt with in terms of the Business Profits article. The 12 treaties with specific technical service fee articles all contain a deemed source rule within the technical service fee article.

Juridical double taxation can arise in South Africa, under the following circumstances:

3.1.1 Tax withheld on foreign source income, is not in accordance with the treaty

In terms of the domestic legislation of the foreign state, Country A, withholding tax on payments for technical service fees to non-residents may be set at 15 per cent for example. In terms of the DTA between Country A and South Africa however, the technical service fee article reduces this to 10 per cent.

Assuming that the income met the source requirements of section 6*quat* or that the article contained a deemed source rule, the rebate available to the South African resident taxpayer would be limited in terms of section 6*quat*(1A).

[83] *Convention between the Government of The Republic of South Africa and the Government of the Kingdom of Saudi Arabia for the Avoidance of Double Taxation and the Prevention of Tax Evasion with respect to Taxes on Income and on Capital* (1 May 2008), Art. 7(9), SARS, https://www.sars.gov.za/AllDocs/LegalDoclib/Agreements/LAPD-IntA-DTA-2012-68%20-%20DTA%20Saudi%20Arabia%20GG%2031796.pdf [hereinafter RSA-SA Income and Capital Tax Treaty].

[84] *Protocol amending the Convention between the Republic of South Africa and the Kingdom of the Netherlands for the Avoidance of Double Taxation and the Prevention of Fiscal Evasion with respect to Taxes on Income and on Capital, with Protocol* (28 December 2008), V Ad Art. 7, SARS, https://www.sars.gov.za/AllDocs/LegalDoclib/Agreements/LAPD-IntA-DTA-2012-58%20-%20DTA%20Netherlands%20GG%2031797.pdf [hereinafter RSA-NL Income and Capital Tax Treaty].

Where tax is withheld at 15 per cent, despite the existence of a DTA, only the tax withheld up to the 10 per cent of the gross technical service fee payment, in terms of the treaty, can be proved to be payable or paid. The additional 5 per cent is not payable, in terms of section 6*quat* of the Act, in accordance with the treaty. Further to this, the additional 5 per cent is subject to a right of recovery by the taxpayer from the relevant tax authorities of Country A. Therefore the 5 per cent cannot be included in the possible rebate available to the taxpayer.

The resident taxpayer is expected to now approach the tax authorities of Country A for a refund of the excess withholding tax charged. Failing which, the taxpayer can initiate MAP in terms of the treaty.

Double taxation arises in this scenario as a result of the following:

- The taxpayer is unsuccessful in obtaining a refund of the excess withholding tax from the tax authorities of Country A; or
- The taxpayer is unsuccessful in obtaining relief through MAP

In many instances, after weighing up the costs involved, with either MAP or engaging with the relevant tax authority, versus the benefits of the refund and MAP approaches, the taxpayer will probably not pursue the matter. Unfortunately, relief in the form of an expense deduction for the excess withholding tax is also not available either in terms of section 6*quat*(1C), or section 11(a).[85]

The excess withholding tax cannot be deducted in terms of section 6*quat*(1C) as the provision only applies to foreign taxes levied against <u>South African source income</u>, whereas in this scenario the income is foreign sourced.

It is SARS' view that foreign taxes are not deductible in terms of section 11(a), read together with section 23(g), as they deem the expense to not have been incurred in the production of income. SARS relies on the principles laid out in

[85] SARS IN18 Issue 3, par. 4.3.2. at pg. 25.

the case of *Port Elizabeth Electric Tramway Company Ltd v CIR*.[86] Further to this, is the SARS view that taxes which are levied on a gross basis, like a final withholding tax, are incurred *on* income and not *in the production of* income. [87]

A final withholding tax refers to taxes withheld on certain income types, such as interest or dividends, which is not creditable against the Income Tax liability of the taxpayer. Withholding taxes on technical service fee income are generally not considered, by SARS, to be a final withholding tax.[88]

However, SARS further goes on to state that foreign taxes which are a charge against profits may qualify for a deduction in terms of section 11(a) read with section 23(g), with "charge against profits" being defined as "a tax which is incurred irrespective of whether the taxpayer is in a taxable profit, taxable loss or break-even position".[89] A withholding tax on fee income applies to the payment of the fee and not the profit, loss or otherwise of the particular transaction or contract from which the fee payment arose.

Thus, despite the SARS view that withholding taxes levied on a gross basis cannot be claimed as a deduction, it appears possible that withholding taxes on service fee income might, depending on the circumstances, be allowed as a deduction. In general terms, it can be argued that if the imposition of the particular foreign tax is recurring expenditure closely associated with the general foreign income producing trade operation of a South African tax resident, it may well be allowed as a deduction.[90]

The additional 5 per cent of withholding tax suffered, in this scenario, is therefore a double tax which is unrelieved in full, despite the provisions of the treaty and section 6*quat*.

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[86] *Port Elizabeth Electric Tramway Co Ltd v CIR* 1936 CPD 241, 8 SATC 13
[87] SARS IN 18 Issue 3, par. 4.5.2. at pg. 43.
[88] Ibid, par. 4.3.1. at pg. 20-21.
[89] Ibid, par. 4.5.2. at pg. 43.
[90] Hattingh, J (2019), *Chapter 36: Elimination and avoidance of international double taxation,* At par. 36.32. pg. 83, In De Koker, A P and Brincker, E (eds.) Silke on International Tax, LexisNexis.

3.1.2 No deemed source rule and South Africa deems source to arise within the Republic

Country A has entered into a DTA with South Africa and the technical service fee article contained within that DTA does not contain a specific deemed source rule. In this instance there is no overriding provision in terms of source and the rules in terms of section 6*quat* apply.

The South African resident taxpayer has provided technical services from South Africa to the foreign customer in Country A. In terms of the domestic legislation of Country A, tax must be withheld on all payments of technical service fees to non-residents. In terms of the relevant article of the treaty, both Country A and South Africa have a right to tax. Country A therefore legitimately withholds a reduced withholding tax amount of 10 per cent (as compared to 15 per cent per Country A's domestic legislation), in terms of their legislation and the treaty.

As the South African taxpayer was not physically present in Country A whilst the services were delivered, the source of the income would be deemed to arise in South Africa.

Without the deemed source override in the DTA, the taxpayer will not be able to obtain a rebate in terms of section 6*quat*(1) as the income is not from a source outside of the Republic. The taxpayer will however be able to obtain a deduction in terms of section 6*quat*(1C). The deduction in terms of section 6*quat*(1C) is limited to foreign taxes levied on South African source income derived from trade operations.[91]

It is not a full rebate as the taxpayer effectively only receives a maximum 28 per cent benefit on the 10 per cent withholding tax which was incurred. Thus, double taxation is incurred on the amount of the withholding tax not relieved by the section 6*quat*(1C) deduction.

[91] SARS IN18 Issue 3, par. 5. at pg. 77.

3.1.3 No technical service fee article

Where a treaty does not contain a specific technical service fee article, it is incumbent on the relevant parties to determine if any of the other articles within the treaty apply to the technical service fee income in question.

Generally, this would result in a review of the relevant provisions of Article 7 dealing with Business Profits, Article 12 Royalties,[92] Article 14 Independent Personal Services[93] and Article 21 dealing with Other Income in terms of the OECD MTC to determine which should apply.[94]

South Africa's approach appears to be that if a DTA does not have a technical service fee article, then the provisions of the Business Profits article must apply.[95] Therefore, from a SARS perspective, if tax is withheld by Country A, and the DTA between Country A and South Africa is silent with regards to technical service fees, SARS will not see the tax withheld to be legitimate. In SARS' view the Business Profits article would apply which would, unless the fees are provided via a permanent establishment, give South Africa the sole taxing rights to the technical service fee income. As a result, the foreign tax is not seen to have been "proved to be payable", even though it has been paid. Thus, the tax would not qualify for a rebate in terms of section 6*quat*(1). A deduction in terms of section 6*quat*(1C) would also not apply where the income is foreign sourced. The taxpayer is expected to approach the authorities of Country A for a refund or to initiate MAP procedures.

South Africa generally applies the OECD Model with regards to its DTAs. However, consideration is also paid to the UN (which includes a technical service fee Article in its MTC) and ATAF MTCs, thus the relevant aspects of these will also be reviewed.

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[92] UN (2018), *United Nations Model Double Taxation Convention between Developed and Developing Countries 2017 Update*, Commentary on Article 12A, at par. 4 Pg. 120, Department of Economic and Social Affairs. IBFD version.[hereinafter UN MTC 2017 IBFD].

[93] Article 14 was deleted from the OECD MTC (2000) and subsumed into Articles 5 and 7. The UN MTC (2017) however still retains a version of Article 14. Versions of Article 14 may appear in older South African treaties.

[94] OECD MTC 2017.

[95] SARS IN18 Issue 3, Example 42 at pg. 79.

In order for the Business Profits article to apply, the rendering of technical services would have to meet the definition of a business or enterprise in terms of Article 3 of the OECD MTC.[96]

Article 3(c) of the OECD MTC defines the term “enterprise” as “the carrying on of any business”. Article 3(h) then defines the term “business” as “including the performance of professional services and of other activities of an independent character.[97] Some of the treaties in South Africa’s network specifically include a definition of “business” similar to that referred to in Article 3(h).[98] As the definition of “business” is inclusive, the term has its ordinary meaning as well as that of professional and other independent services. “Business” is undefined in the model treaties, thus the meaning it has under the domestic law of the treaty parties must be applied.[99]

Business is not a defined term in the Act.[100] The ordinary meaning, in terms of the dictionary, defines business as “work relating to the production, buying, and selling of goods or services.”[101] In terms of the Commentary to Article 7 of the OECD MTC however, it should be understood that the term “profits”, when used in the Article and elsewhere in the MTC, has a broad meaning which includes all income derived in carrying on an enterprise.[102]

The OECD MTC commentary to Article 3 states that the term “enterprise” applies to the carrying on of any business. Since the term “business” is expressly defined to include the performance of professional services and of other activities of an independent character, this clarifies that the performance of professional services or other activities of an independent character must be

[96] OECD MTC 2017, at Art. 3(1)(c) pg. M-10.
[97] Ibid, at Art. 3(1) pg. M-10.
[98] Refer paragraph 4.4.
[99] Arnold, B J *Article 5: Permanent Establishment – Global Tax Treaty Commentaries*, at 1.1.1.2, Global Tax Treaty Commentaries IBFD (accessed23 January 2020).
[100] South Africa, Section 1, Income Tax Act No. 58 of 1962.
[101] Definition of ‘business’, Collins English Dictionary, https://www.collinsdictionary.com/dictionary/english/business.
[102] OECD MTC 2017*,* Commentary on Article 7, at par. 71 pg. C(7)-28.

considered to constitute an enterprise, regardless of the meaning of that term under domestic law.[103]

Lang held the view that domestic law is only considered for interpretation purposes when nothing more can be derived from the treaty itself.[104] He went on to say that the fact that "business" and "enterprise" were not adequately defined in the MTC, should not lead to the automatic conclusion that domestic law and terminology would apply in order to interpret the concepts. The system should instead take the systematic, ideological and historical factors of the MTC/DTA into account. This would, according to Lang, lead to the result that Article 7 applies to income from activities that are not services or where there is significant capital expenditure. This was the view however before Article 14 was deleted.[105]

With the deletion of Article 14, Lang held the view that all income formerly covered under Article 14 of the OECD MTC should now be assigned to Article 7 of the OECD MTC.[106]

The broad scope of the concept of "business profits" and its interaction with other articles is illustrated by its application to two categories of profits that were previously dealt with in other articles, referring to Article 14, of the OECD MTC, and are still dealt with in these other articles in the UN MTC. The effect of the deletion of Article 14 was to move the profits into article 7 of the OECD Model, as explained in the Commentary on Article 7 of the OECD MTC. [107]

The provision of technical services for a fee should therefore fall within the definition of business. The US Technical Explanation to the DTA between

[103] OECD MTC 2017, Commentary on Article 3, at par. 4 pg. C(3)-2.
[104] Lang, M *Introduction to the Law of Double Taxation Conventions* 2ed (2013), at par.74 pg. 45.
[105] Ibid, at par. 75 pg. 45-46.
[106] Ibid, at par. 242 pg. 92.
[107] Sasseville, J & Vann, R *Article 7: Business Profits – Global Tax Treaty Commentaries*, at 6.1.1.1., Global Tax Treaty Commentaries IBFD (accessed 23 January 2020).

South Africa and the USA specifically states that the income earned by an enterprise from the furnishing of services is business profits.[108]

In terms of paragraph 4 of Article 7 of the OECD MTC, Article 7 applies to business profits which do not belong to categories of income covered by other Articles, with specified forms of income, and, in addition, to income which under paragraph 4 of Articles 10 and 11, paragraph 3 of Article 12 and paragraph 2 of Article 21, falls within Article 7.[109]

In the UN MTC, the interaction between Article 7 and Article 12A is such that, where both articles are present in a treaty, if income is derived from Technical Fees but are accrued through a permanent establishment, Article 7 would take precedence.[110] It could surely be interpreted therefore, that where a treaty does not contain an Article 12A, that the provisions of Article 7 would apply to the income derived from the providing of technical services.

Where a technical service fees article does not exist conflict can occur where states deem technical service fees to fall within the ambit of Article 12[111] or Article 21 instead of Article 7. Refer to section 4.8 for further discussion on the interaction between these articles.

Some states are of the opinion that if a tax treaty does not specifically deal with Technical Fees, by means of the inclusion of a specific Article or provision, payments that are Technical Fees under their domestic law would fall under article 21 of the OECD MTC, other income, and be taxable in the source state

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[108] Department of the Treasury (1998), *Technical Explanation of The Convention Between The United States of America and The Republic of South Africa for The Avoidance Of Double Taxation and The Prevention of Fiscal Evasion with Respect to Taxes on Income and Capital Gains*, Article 7(1).
[109] OECD MTC 2017*,* Commentary on Article 7, at par. 74 pg. C(7)-28.
[110] UN (2018), *United Nations Model Double Taxation Convention between Developed and Developing Countries 2017 Update*, Commentary on Article 12A, at par. 93 Pg. 354 and par. 104 pg. 357, Department of Economic and Social Affairs.
[111] Certain treaties contain wording in their Article 12 which specifically includes the provision of technical assistance, which may result in the provision of technical services being deemed to fall within the reach of Article 12. In addition, certain jurisdictions are of the view that even without specific "technical assistance" wording, the provision of technical service fees could be seen to be the provision of know-how. Refer UN MTC 2017 IBFD, Commentary on Article 12A, at par. 4 Pg. 120.

under article 21(3) of the UN MTC.[112] Sasseville and Vann however state, in their commentary on Article 7, that the domestic rules applicable to a certain activity is not sufficient, in itself, to conclude that an activity does not constitute a business for treaty purposes.[113]

Article 21 of the OECD MTC is a residual clause which is meant to deal with items of income not dealt with under Articles 6 to 20.[114]

3.1.4 "Subject to" clause in Elimination of Double Taxation article

In addition to the above, there is another treaty scenario that can impact the ability of the South African taxpayer to claim an FTC on tax withheld on payments of technical service fees.

Of the 79 DTAs which South Africa currently has in force with other foreign jurisdictions, 40 of these treaties contain specific wording in the "Elimination of Double Taxation" article which can impact the ability of a South African taxpayer to claim FTCs (Annexure 2).[115] These treaties contain a reference, which is not based on OECD model wording, that makes relief "subject to" the provisions applicable in terms of domestic tax legislation.[116]

Wording of this nature would result in the source of income restrictions found in South African domestic law, specifically section 6*quat*, applying to these treaties.[117] However, where a specific technical service fees article is included in the DTA and this article contains a "deemed source" rule, this rule would override the source rules contained within section 6*quat*.[118] This deemed source

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[112] Sasseville, J & Vann, R *Article 7: Business Profits – Global Tax Treaty Commentaries*, at 5.1.2.3.2., Global Tax Treaty Commentaries IBFD (accessed 23 January 2020).
[113] Ibid, at 5.1.2.3.2.
[114] Schoueri, L *Article 21: Other Income – Global Tax Treaty Commentaries*, at 1.1.1.1., Global Tax Treaty Commentaries IBFD (accessed 21 January 2020).
[115] Refer to Annexure 2: *South Africa's treaty network in relation to Technical Service Fees & Elimination of Double Taxation.*
[116] Hattingh J, *Volume 96b Subject 2: Key practical issues to eliminate double taxation of business income*, South Africa at pg. 582, Cahiers de Droit Fiscal International, International Fiscal Association (2011).
[117] Ibid.
[118] SARS IN18 Issue 3, par. 4.2.1. (c). at pg. 14.

override would also apply to treaties that include the "subject to" clause as noted above. This view has been confirmed by SARS.[119]

Of the 40 treaties that contain this wording, 10 have specific technical service fee articles or wording. All 10 contain deemed source rules.

Neither the OECD[120], UN[121] or ATAF[122] MTCs contain wording to this effect in their elimination of double taxation articles i.e. "subject to" domestic legislation. The commentaries touch on the possibility of this wording being used but do not provide detail or opinions.

3.1.5 Non-treaty scenarios and interaction with section 6*quat*

The foreign tax incurred has been withheld by a foreign jurisdiction with which South Africa does not have a DTA in place. The foreign jurisdiction has deemed the source to arise from where payment is made and the service is consumed i.e. the foreign jurisdiction, whilst South Africa has deemed the source to originate from South Africa.

Where the income is deemed to be from a South African source, the only relief available to the taxpayer would be a deduction in terms of section 6*quat*(1C).

Where the income is deemed to be from a foreign source, a rebate would be allowed if the provisions of section 6*quat*(1A) are met.

3.1.6 Assessed tax losses and section 6*quat*

As noted above, in 2.6, where tax has been withheld by a foreign jurisdiction on the foreign source income of a South African resident taxpayer and that South

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[119] SARS IN18 Issue 3, Example 8 at pg. 17-18.
[120] OECD MTC 2017*,* Commentary on Articles 23A and 23B, at par. 60 pg. C(23)-29.
[121] UN (2018), *United Nations Model Double Taxation Convention between Developed and Developing Countries 2017 Update*, Commentary on Article 23, at par. 60 Pg. 511, Department of Economic and Social Affairs.
[122] ATAF (2016), *Commentary on the articles: THE ATAF MODEL TAX AGREEMENT for the avoidance of double taxation and the prevention of fiscal evasion with respect to taxes on income MTC*, Commentary on Article 23 Elimination of Double Taxation, at pg. 46, ATAF Publications.

African resident taxpayer is in an overall or assessed tax loss position, the relief available is limited.

The unutilised excess credit is carried forward to the following year of assessment up to a maximum roll-over period of 7 years. However, the provisions of section 6*quat* as well as the relevant SARS Interpretation Notes are silent on what becomes of the excess credit once the 7-year roll-over period has elapsed. It is assumed that these expired excess credits would be allowed as deductions in the year in which they expire but section 6*quat* only appears to allow a deduction under section 6*quat*(1C). It is therefore apparent that the legislators hold the view that these should be forfeited, as a deduction under section 6*quat*(1C) can only be claimed if the requirements of section 6*quat*(1) have not been met, resulting in unresolved double taxation.[123]

This is especially troubling in light of SARS view that these tax expenses cannot be claimed in terms of the General Deduction formula and section 11(a) as read with section 23(g).

In most treaty scenarios, issues of double taxation can generally be resolved through application of the elimination method clauses or the administrative clauses of the relevant DTA. Unresolved double taxation can arise, however, where there is no DTA in place, or where the DTA contains a clause, in the general relief provision, that the relief is "subject to" the domestic tax law of the Contracting States.

As we have seen, double taxation can also arise where deduction of foreign taxes paid is disallowed in terms of the General Deduction formula. The aim of a general tax deduction is surely to provide some form of ultimate relief for unresolved actual international double taxation. In the ordinary course, no issue of tax avoidance or evasion would arise when such a tax deduction may be granted because of the presence of actual double taxation.[124]

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[123] Hattingh, J (2019), *Chapter 36: Elimination and avoidance of international double taxation,* At par. 36.32. pg. 83, In De Koker, A P and Brincker, E (eds.) Silke on International Tax, LexisNexis.
[124] Ibid.

The next chapter will examine technical service fees in more detail together with their treatment in terms of the OECD, UN and ATAF MTC's.

CHAPTER 4: TECHNICAL SERVICE FEES IN FURTHER DETAIL AND IN RELATION TO THE MODEL TAX CONVENTIONS, SOUTH AFRICA'S ABANDONED WITHHOLDING TAX AND THE ECONOMIC IMPACT OF THESE SERVICES.

4.1 Definition of technical service fees in the Model Tax Conventions

Technical service fees or the term "fees for technical services" is defined, in a treaty context by the MTCs of the UN[125] and ATAF[126], as:

"*Any payment in consideration for any service of a managerial, technical or consultancy nature, unless the payment is made: (a) to an employee of the person making the payment; (b) for teaching in an educational institution or for teaching by an educational institution; or (c) by an individual for services for the personal use of the individual.*"

Whilst the OECD MTC[127] does not contain a specific article dealing with the taxation of technical service fees, the matter is discussed at various points in the Commentaries to the Model. The Commentary on Article 12 provides examples of fees for the provision of services which include "*payments for pure technical assistance*" and

"*Payments for advice provided electronically, for electronic communications with technicians or for accessing, through computer networks, a trouble-shooting database such as a database that provides users of software with non-confidential information in response to frequently asked questions or common problems that arise frequently.*"[128]

SARS defined "service fees" in, now repealed, section 51A of the Act as:

"*Any amount that is received or accrues in respect of technical services, managerial services and consultancy services but does not include services incidental to the imparting of or the undertaking to impart any scientific, technical, industrial or commercial knowledge or*

[125] UN (2017), *United Nations Model Tax Convention between Developed and Developing Countries 2017 Update*, Department for Economic and Social Affairs, Article 12A par 3 at pg. 24.
[126] ATAF (2016), *ATAF Model Tax Agreement for the avoidance of double taxation and the prevention of fiscal evasion with respect to taxes on income*, African Tax Administration Forum, Article 13 par. 3 at pg. 9.
[127] OECD MTC 2017.
[128] Ibid, Commentary on Article 12, par. 11.4. at C(12)-11.

information, or the rendering of or the undertaking to render any assistance or service in connection with the application or utilisation of such knowledge or information."

4.2 Technical service fees and the Model Tax Conventions

The approach towards the treatment of technical service fees in MTCs appears to largely revolve around whether the MTC is intended for developed or developing countries.

The two most widespread MTCs are those provided by the OECD and the UN. The OECD model is generally targeted at developed countries whilst the UN model is targeted at developing countries.[129]

Interestingly though, withholding taxes on technical service fees is not a product solely of developing countries. Out of the 42 EU and OECD member states selected for comparison purposes (refer Annexure 3)[130], 25 have a form of withholding tax on technical service fees paid to non-residents. Of these 42 OECD and EU member states, 36 have DTAs in place with South Africa but only 1 refers specifically to technical service fees.[131] This may simply be a result of the fact that South Africa does not have a withholding tax on technical service fees.

Whilst the OECD model does not deal with payments of technical service fees by means of a specific Article, it is referred to in various points within the Commentaries. Commentary to Article 12 states that distinction must be made between payments for know-how versus payments for the provision of technical services. Know how may be dealt with under Article 12 whilst the provision of technical services would generally be dealt with under Article 7.[132]

In the Commentary to Article 12A of the UN model it is stated that the Article was added to provide clarity and certainty on a topic that had, in the past, raised a number of classification issues. It is also stated that the Article was included to try and mitigate any

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[129] So much so in fact that the title of the 2017 model is the *United Nations Model Tax Convention between Developed and Developing Countries.*
[130] Refer Annexure 3: *Withholding Taxes on Technical Service Fees in OECD and EU Member States.*
[131] RSA-NL Income and Capital Tax Treaty.
[132] OECD MTC 2017, Commentary on Article 12, at par. 11 pg. C(12)-9 to 12.

possible BEPS impacts resulting from excessive service fee payments, especially with regard to intragroup services.[133]

Intragroup services are seen to provide opportunities to multinational enterprises to shift profits from high-tax jurisdictions to low or lower tax jurisdictions.

4.3 Withholding tax on technical service fees in South Africa: Reasons for implementation and subsequent repeal of sections 51A to 51H

Taxation Laws Amendment Act of 2013, inserted Part IVC into Chapter II of the Act, and specifically sections 51A to 51H which dealt with a withholding tax on technical service fees.[134]

The insertion of these provisions was done with the intention of bringing South Africa in line with other developing countries and providing a method of tax base protection where payment of managerial fees could pose base erosion risk. Per National Treasury's explanation, payments of fees of this type, together with interest and royalties amounted to billions per annum, most of which was shifted to low-tax jurisdictions. Thus, a withholding tax similar to that applied to interest and royalties was enacted.[135]

Base Erosion and Profit Shifting ("BEPS") refers to tax planning strategies, by Multinational Enterprises ("MNE"), that exploit gaps and mismatches in tax rules to artificially shift profits to low or no-tax locations where there is little or no economic activity or to erode tax bases through deductible payments such as interest, royalties or management fees. Although some of the schemes used are illegal, the majority are not. This undermines the fairness and integrity of tax systems because MNEs that operate across borders can use BEPS to gain a competitive advantage over enterprises that operate at a domestic level. Moreover, when taxpayers see MNEs legally avoiding income tax, it undermines voluntary compliance by all taxpayers.[136]

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[133] UN MTC 2017 IBFD, Commentary on Article 12A, at par. 7-8 Pg. 121.

[134] Inserted in terms of section 99 of Taxation Laws Amendment Act no. 31 of 2013.

[135] Department of National Treasury, *Explanatory Memorandum on the Revenue Laws Amendment Bill, 2013*, at pg. 75, Government of the Republic of South Africa [hereinafter 2013 Explanatory Memo].

[136] OECD, *What is BEPS?*, http://www.oecd.org/tax/beps/about/ (accessed 15 March 2020).

BEPS is of major significance for developing countries due to their heavy reliance on corporate income tax, particularly from MNEs.[137]

In addition to the above base erosion protection intentions, the withholding tax was to be a final withholding tax that would be used to identify and collect revenue from non-resident taxpayers who provided certain services within a South African source that fell outside of the normal tax. More specifically, all payments for services to a foreign resident from a South African source would be subject to this withholding tax if those services were of a technical, managerial or consultative nature.[138]

Exemptions for service fees earned via permanent establishments would have only been allowed, in terms of the Explanatory Memorandum, if proof was provided to the payor of the fees of the SARS registration of the permanent establishment of the non-resident. This would ensure that permanent establishments were part of the tax base, and subject to Corporate Income Tax, before any exemption was granted.[139]

The withholding tax on technical service fees as outlined in section 51A to 51H of the Act was repealed in 2016, before the withholding tax even became effective.[140]

National Treasury stated that the reason for the repeal was that revisions were made to the list of arrangements which constitute a reportable arrangement in terms of section 35(2) of the Tax Administration Act No. 28 of 2011 ("the TAA"). [141]

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[137] OECD, *What is BEPS?*, http://www.oecd.org/tax/beps/about/ (accessed 15 March 2020).
[138] 2013 Explanatory Memo at pg. 76.
[139] Ibid, at pg. 77.
[140] Repealed in terms of section 60 of Taxation Laws Amendment Act no. 15 of 2016.
[141] Department of National Treasury, *Explanatory Memorandum on the Revenue Laws Amendment Bill 17B of 2016*, 2016, at pg. 74, Government of the Republic of South Africa [hereinafter 2016 Explanatory Memo].
In terms of the revised list a reportable arrangement now included "an arrangement for the rendering of consultancy, construction, engineering, installation, logistical, managerial, supervisory, technical or training services to a South African resident or a non-resident having a permanent establishment in South Africa, in terms of which arrangement a non-resident was, is, or is anticipated to be physically present in South Africa in connection with or for purposes of rendering the services and the expenditure incurred or to be incurred in respect of the services exceeds or is anticipated to exceed R10 million, is a reportable arrangement in terms of the Tax Administration Act provided that it does not qualify as 'remuneration' for employees' tax purposes.".

National Treasury were of the view that the above reportable arrangement, together with a withholding tax on services would be an administrative burden on both the taxpayer and SARS, thus the withholding tax was repealed.[142]

4.4 Technical service fees and South Africa's treaty network

South Africa currently has 79 DTA's worldwide which are in force. Of those 79 treaties, only 12 have specific articles relating to technical service fees, whilst 2 have specific technical service fee clauses in the Business Profits article.[143]

The DTA Protocol with the Netherlands contains a clause which deems that technical service fees are to be treated as business profits and that Article 7 must accordingly be applied.[144] The DTA with Saudi Arabia also states that technical service fees are to be treated as Business Profits and that Article 7 must be applied.[145]

22 of the DTAs currently in force include the following wording in the "General Definitions" article *"the term "business" includes the performance of professional services and of other activities of an independent character."* 10 of these DTAs are with African jurisdictions. Of these 10 African DTAs, 4 of them already have a technical service fee article. By including the performance of professional services in the definition of business, support is provided in the application of the Business Profits article where a technical service fees article is not recorded in the DTA.

Of the 79 DTA's that South Africa currently has in force, 58 of these are with jurisdictions which have some form of technical service fee withholding tax in their domestic legislation. 23 of these DTA's are with African jurisdictions and all 23 of those African jurisdictions have a withholding tax for technical service fees in their domestic legislation. However, only 9 of the South African DTA's with African jurisdictions have specific technical service fee articles. 7 of these DTAs contain a "subject to" clause in the Elimination of Double Taxation article. Commentary on the impact of a "subject to" clause was noted in paragraph 3.1.4. above.

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[142] 2016 Explanatory Memo at pg. 74.
[143] Refer Annexure 2: *South Africa's treaty network in relation to Technical Service Fees & Elimination of Double Taxation*.
[144] Ad Art. 7, RSA-NL Income and Capital Tax Treaty.
[145] Art. 7(9), RSA-SA Income and Capital Tax Treaty.

Of the 54 countries in Africa, only Libya and South Africa do not charge a withholding tax on technical service fees. Information relating to Somalia is not available.

Increased business and investment into Africa by South African companies (as well as companies from other jurisdictions) therefore leads to increased opportunities for juridical double taxation as a result of tax withheld on technical service fee income.

4.5 Technical service fees and its impact on the economy

The UN states that in 2018 international trade in services accounted for 7 per cent of global Gross Domestic Product ("GDP"). In 2018, in a large number of economies of Europe, Central America, the Caribbean and South-Eastern Asia, internationally sold services (exported services) accounted for more than 10 per cent of GDP. Several smaller European economies, such as Luxembourg, Malta or Ireland, and some island economies, such as Aruba, Antigua and Barbuda or the Seychelles, relied to a particularly great extent on services exports. By contrast, in large parts of South America, Western and Central Africa as well as Western and Eastern Asia, the export of services amounted to less than 3 per cent of their respective GDP. Africa as a whole recorded significant growth of 11.9 per cent in the import of services, combined with much slower growth in the export of services.[146]

The United States of America ranked as the world's top services exporter in 2018, with services exports totalling USD828 billion, which represented 14 per cent of global services exports. The USA was followed at some distance, by three European countries (the UK, Germany and France) that jointly captured 17 per cent of the world market. China, the leading exporter among developing economies, ranked fifth.[147]

The top five exporting developing economies were all Asian economies, comprising China, India, Singapore, Hong Kong and the Republic of Korea. They held a combined world market share of almost 15 per cent, the same as all other developing economies

[146] United Nations, *2019 e-Handbook of Statistics: International Trade in Services*, United Nations Conference for Trade and Development, https://stats.unctad.org/handbook/Services/Total.html#figure1.
[147] Ibid.

combined.[148] Reasons for this could be related to the fact that a large number of developing nations are predominantly importers of services rather than exporters.

South Africa falls within the top 5 countries in Africa for the import of services as well as the export of services.[149] Total value of services imported by South Africa for 2018 amounted to approximately USD16.5 billion, whilst services exported by South Africa for 2018 amounted to approximately USD15.9 billion.[150]

The World Trade Organisation ("WTO") have stated that over the last 20 years the international trade in services has become the most dynamic segment of world trade, growing more quickly than trade in goods. Developing countries and transition economies have played an increasingly important role in this area, increasing their share in exports of world services from a quarter to one-third over this period.[151]

The increasing status of services in world trade, and especially in Africa, provides context for the desire of African jurisdictions to include this trade item within their tax bases and capture as much tax revenue as possible through mechanisms such as withholding taxes on imported services such as technical service fees paid to non-residents or the establishment of permanent establishments through the provision of services in a jurisdiction – a services PE.

The broad definition of technical service fees includes a wide variety of possible income items which, by their very nature, can be performed physically at a customer's site, remotely from the supplier's site or by a combination of these. In the digital economy with the prevalence of Information and Communications Technology ("ICT"), a large proportion of those services no longer require physical presence in a country or at a customer's site in order for the service to be performed.

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[148] United Nations, *2019 e-Handbook of Statistics: International Trade in Services*, United Nations Conference for Trade and Development, https://stats.unctad.org/handbook/Services/Total.html#figure1.
[149] Ibid.
[150] World Integrated Trade Solution, South Africa trade statistics, https://wits.worldbank.org/CountryProfile/en/ZAF.
[151] World Trade Organisation, *Trade in Services: The most dynamic segment of international trade*, WTO publications, https://www.wto.org/english/thewto_e/20y_e/services_brochure2015_e.pdf.

4.6 Services provided remotely

Recent technological advancements have made it easier to supply services across borders which in turn opens up new opportunities for service providers and the economies in which they are resident. The World Trade Organisation states that, in value-added terms, the trade in services accounts for 50 per cent of world trade. The policy treatment by jurisdictions of the trade in services therefore can have direct impact on foreign direct investment.[152]

The provision of services remotely instead of physically in the jurisdiction of the customer in theory places less demands on the infrastructure of the customer jurisdiction and therefore less demands on the tax revenue of that jurisdiction. This can however be countered with the argument that government spending is still required on the infrastructure necessary to ensure a stable and efficient digital connection with the outside world.

Some countries, such as Mauritius, will only levy a withholding tax, on services paid to non-residents, where the services are physically rendered in Mauritius.[153]

Most developing nations will however aim to have as wide a tax base as possible to maximise the generation of tax revenues.

4.7 Reasons for the introduction of withholding taxes on technical services fees in domestic legislation

Prior to the 2017 amendments of the UN MTC a large proportion of African jurisdictions had introduced a withholding tax on technical service fees in their domestic legislation in an effort to protect their tax bases and increase tax revenues. Specifically, with regard to management and similar fees levied by MNEs against their in-country subsidiaries. Concerns were noted that MNEs could easily shift profits from one jurisdiction to another by means of the invoicing of large fees which would reduce the taxable income of the local entity and "shift" the profits to another jurisdiction and thereby negatively impact the tax base of the jurisdiction paying the intragroup fee.

[152] World Trade Organization, Services trade, https://www.wto.org/english/tratop_e/serv_e/serv_e.htm.
[153] Section 111B(h), The Income Tax Act 1995, Mauritius, Mauritius Revenue Authority, http://mra.mu/download/ITAConsolidated.pdf.

In addition to the risks posed by intragroup services charges, concern was also noted regarding the ability for entities resident in one jurisdiction to be substantially involved in another jurisdiction's economy, through the provision of cross border services, without a permanent establishment or fixed base in that jurisdiction and without any substantial physical presence in that jurisdiction.[154]

Advancements in the digital economy and the means of communication and information technology, also resulted in the ability of an enterprise of one jurisdiction being able to provide substantial services to customers in the other jurisdiction and therefore maintain a significant economic presence in that jurisdiction without having any fixed place of business in that jurisdiction and without being physically present in that jurisdiction for any substantial period.[155]

Introducing mechanisms in domestic legislation to withhold tax on technical service fees paid to non-residents was seen as a method to help minimise lost tax revenues and improve domestic anti-avoidance measures.

Withholding taxes of this nature were also seen to simplify the administration and compliance costs for both the tax authority and the non-resident service provider. This administrative and compliance burden however is shifted somewhat to the resident customer.[156]

By charging withholding tax, a tax authority is reasonably assured of collecting at least as much tax as would have been charged if corporate income tax were levied on the net profits from providing the technical services in question. Thus, the need to enforce furnishing of tax returns by non-residents and deal with them is also dispensed with. Furthermore, the withholding tax charged may be sufficient to ensure that the tax paid, is at least as much as would be collected through corporate income tax, if the arm's length principle was applied by the tax authority, so that the MNE is unable to achieve

[154] UN MTC 2017 IBFD, Commentary on Article 12A, at par. 2 Pg. 120.
[155] Ibid.
[156] Miller, A (2015), *Taxing Cross-Border Services: Current Worldwide Practices and the Need for Change*, at Ch. 9 par. 9.3.3. pg. 15, Books IBFD (accessed 16 April 2019), https://research-ibfd-org.ezproxy.uct.ac.za/#/doc?url=/document/itts_chaphead.

low-cost profit shifting. Thus, through the mechanism of withholding tax, a tax authority is relieved of the need to have a staff complement trained to a high standard.[157]

Withholding taxes, especially in relation to technical service fees, do however come with their own problems such as issues of source and characterisation, both in terms of domestic legislation and to a larger degree treaty interpretation.

Definitions for technical service fees in domestic legislations are generally quite broad and can create confusion when trying to distinguish between fees of similar nature such as a fee for technical services and a fee for information concerning commercial, scientific or industrial experience which could lead to the fee being deemed to be a royalty. This is usually mitigated by ensuring that the withholding tax applicable to both technical services and royalties are the same.

If the source principle forms the basis of the right to tax, a clear nexus between the service provider and the taxing jurisdiction is expected to be established. Two main principles of source are noted namely the economic allegiance principle and the base erosion principle. The economic allegiance principle has an expectation that the non-resident would make some use of the facilities provided by the taxing jurisdiction and have some sort of physical presence in that jurisdiction. Economic allegiance would apply to the "place of performance" method of source determination.[158]

The base erosion principle applies to jurisdictions where the right to tax the non-resident is claimed based on where the services provided are either utilised in their territory or paid for by their residents.[159]

The majority of developing nations apply the base erosion principle and deem source, in terms of withholding taxes on technical service fees, to arise where the services are

[157] Miller, A (2015), *Taxing Cross-Border Services: Current Worldwide Practices and the Need for Change*, at Ch. 9 par. 9.3.3. pg. 15, Books IBFD (accessed 16 April 2019), https://research-ibfd-org.ezproxy.uct.ac.za/#/doc?url=/document/itts_chaphead.
[158] Ibid. at Ch. 5 par. 5.6.2. pg. 6.
[159] Ibid.

utilised and/or paid for. Developed nations largely take the economic allegiance approach or a combination of this with other tests of source.[160]

4.8 Interaction between Article 7, Article 12 and Article 21

Prior to the introduction of Article 12A in the UN MTC, there was much uncertainty with regards to the treaty treatment of technical service fees. This uncertainty was undesirable for both taxpayers and tax authorities and also resulted in difficult disputes which cost taxpayers and tax authorities in terms of time, financial cost and skill.[161]

Until the addition of Article 12A income from services derived by an enterprise of a Contracting State was taxable exclusively, in terms of Article 7, by the State in which the enterprise was resident, unless the enterprise carried on business through a permanent establishment in the other State (the source State) or provided professional or independent personal services through a fixed base in the source State.[162]

This concept however is not universally applied. Debate has arisen in certain states as to whether Article 7 of the OECD MTC applies to profits from activities such as the provision of services of a technical or managerial nature, that are subject to a special treatment under domestic law in the form of a specific withholding tax.[163]

Some states, largely developing nations, have concluded that if a tax treaty does not specifically deal with technical fees, e.g. by including them in Article 12, on royalties, or in a specific Article on technical fees along the lines of Article 12A of the UN MTC (2017), payments that are technical fees under their domestic law would fall under Article 21, other income, and be taxable in the source state under article 21(3) of the UN MTC. [164] This of course only applies to treaties modelled on the UN MTC with the OECD MTC not containing paragraph 3 within its wording of Article 21.[165]

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[160] Miller, A (2015), *Taxing Cross-Border Services: Current Worldwide Practices and the Need for Change*, at Ch. 5 par. 5.6.2. pg. 7, Books IBFD (accessed 16 April 2019), https://research-ibfd-org.ezproxy.uct.ac.za/#/doc?url=/document/itts_chaphead.

[161] UN MTC 2017 IBFD, Commentary on Article 12A, at par. 6 Pg. 121.

[162] Ibid, Commentary on Article 12A, at par. 2 Pg. 120.

[163] Sasseville, J & Vann, R *Article 7: Business Profits – Global Tax Treaty Commentaries*, at 5.1.2.3.2 at pg. 84, Global Tax Treaty Commentaries IBFD (accessed 23 January 2020).

[164] Ibid.

[165] OECD MTC 2017.

The fact that special domestic tax rules apply to a certain activity, such as technical or managerial fees, is not sufficient, in itself, to conclude that this activity does not constitute a business for treaty purposes. If, however, the domestic tax law clearly provides that a certain activity does not constitute the carrying on of a business, it could be argued, that the activity is not deemed to be a business for treaty purposes, in terms of Article 3(2) of the OECD MTC. This can be countered by specifically including the provision of professional services in the definition of "business" under Article 3.[166]

Article 21(3) states that items of income of a resident of a contracting state "arising" in the other contracting state may be taxed in the latter, if its domestic legislation so provides. No definition of "arising" is noted however.[167] The prevalence of certain jurisdictions claiming taxing rights through the application of Article 21(3), in terms of the UN model, can be attributed to efforts to combat base erosion. Some states though, will take a very narrow view of the term "business profits" and treat withholding tax on technical service payments as not being covered under Article 7, as this Article deals with profits. However, it can be argued that the inclusion of paragraph 3 in Article 21 can actually create more opportunities for classification conflicts such as this and therefore result in more double taxation.[168]

> Arnold stated in commentary that Article 21(3) of the UN Model is a problematic provision with regard to the taxation of technical service fees as it allows jurisdictions to apply Article 21(3) rather than Article 7 or 14 by characterizing income under their domestic law as something other than income from business or independent personal services. Under Article 21(3), the source of income is determined by reference to domestic law. In addition, Article 21(3) does not provide any threshold for source country taxation, and does not impose any limits on source country taxation. It was

[166] Sasseville, J & R. Vann, R *Article 7: Business Profits – Global Tax Treaty Commentaries*, at 5.1.2.3.2 at pg. 84, Global Tax Treaty Commentaries IBFD (accessed 23 January 2020).
[167] Schoueri, L *Article 21: Other Income – Global Tax Treaty Commentaries*, at 1.1.1.2.2. at pg. 3, Global Tax Treaty Commentaries IBFD (accessed 21 January 2020).
[168] Sasseville, J & Vann, R *Article 7: Business Profits – Global Tax Treaty Commentaries*, at 5.1.2.3.2 at pg. 84, Global Tax Treaty Commentaries IBFD (accessed 23 January 2020).

Arnolds view that Article 21(3) should be repealed or amended to mitigate the problems caused.[169]

The UN in its commentary to the model readily acknowledges this but merely recommends the application of Article 23A or Article 23B where appropriate.[170]

4.9 BEPS concerns and its impact on the creation of Article 12A in the UN MTC

In terms of the commentary to the UN MTC, the foundational thinking behind the introduction of a separate article which dealt with technical service fees was based largely around concerns of BEPS risk in developing economies. The article was also intended to address uncertainty surrounding the treatment of technical service fees (resulting from an inconsistent interpretation of the definition of royalties or the variety of domestic and treaty policies in this regard). Issues of nexus were also noted due to the fact that, with modern technology and the Internet, it is possible to conduct substantial business activities in a state remotely.[171]

The BEPS risks arising from cross-border transactions were of serious concerns for both developed and developing countries. However, the problem was found to be of greater significance from the perspective of developing countries, because they are generally disproportionately importers of technical services and often lack the administrative capacity to control or limit such BEPS risks through the implementation of anti-avoidance rules in their domestic law and tax treaties.[172]

Prior to the introduction of Article 12A, the inability of countries to tax fees for technical services provided by non-resident service providers may have given non-resident service providers, in certain circumstances, a tax advantage over domestic service providers. Fees for technical services provided by domestic service providers are subject to domestic tax at the ordinary rate applicable to business profits. However, non-resident service providers would not have been subject to any domestic tax if they

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[169] Arnold, B J *The Taxation of Income from Services under Tax Treaties: Cleaning Up the Mess – Expanded Version*, 65 Bull. Intl. Taxn. 2 (2010), par. 2.3.12. at pg. 19, Journals IBFD (accessed 10 April 2019).
[170] UN MTC 2017 IBFD, Commentary on Article 21, at par. 5 Pg. 170.
[171] Jimenez, A M *Article 12: Royalties (OECD and UN Models) and Article 12A: Technical Services (UN Model (2017)) – Global Tax Treaty Commentaries*, at 5.1.8.3.2.1. at pg. 157, Global Tax Treaty Commentaries IBFD (accessed 23 January 2020).
[172] UN MTC 2017 IBFD, Commentary on Article 12A, at par. 10 Pg. 121.

did not have a permanent establishment or fixed base in that country. Article 12A therefore also assists developing countries in levelling the playing fields somewhat.[173]

As with other withholding taxes which are implemented on a gross basis there is also the risk of the non-resident service provider grossing up their fees in order to ensure their margins are not negatively impacted. This could result in the resident entity bearing the brunt of this with higher costs and the jurisdiction of the resident entity still facing some BEPS risks. The non-resident entity who chooses this path however puts itself at risk of over-pricing which may not be desirable, especially in a competitive market.[174]

The effectiveness of Article 12A however is completely dependent on how quickly and how widely it is rolled out in the treaty networks of developed and developing countries.

4.10 Services PE

Another element brought about by the UN MTC is the specific addition of a "services" permanent establishment to Article 5.[175] In terms of this, the provision of services in a country for a period of time exceeding the set threshold may deem the supplier of those services to have a permanent establishment in that country. The standard threshold of 183 days within a 12-month period.

The following chapter will analyse the treatment of technical service fees and the definition of source in a number of countries.

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[173] UN MTC 2017 IBFD, Commentary on Article 12A, at par. 11 Pg. 121.
[174] Ibid, at par. 14 Pg. 122.
[175] The OECD model on the other hand refers to a deemed "services" permanent establishment in the commentary to Article 5.

CHAPTER 5: TREATMENT OF TECHNICAL SERVICE FEES AND SOURCE BY OTHER COUNTRIES

This chapter will perform an analysis on a selected number of jurisdictions with regards to each country's treatment of technical service fees and source as well as the unilateral relief mechanisms available, in comparison to South Africa. Treaty networks, with regard to African jurisdictions, will also be reviewed. Any unique methodologies that are observed as part of the review that may be beneficial to South Africa's system will be noted.

5.1 United States of America

The USA was selected due to the size of its economy and the large volume of services exported to Africa. Despite this, the USA only has four DTAs currently in force with African countries (Egypt, Morocco, South Africa and Tunisia).

Its FTC rules, along with other provisions of its tax code, are generally perceived to be highly complex and administratively burdensome.[176]

The determination of the source of income is largely governed by sections 861 to 863 and section 865 of the Internal Revenue Code of the USA ("IRC").[177]

These provisions cover rules relating to certain specific income items such as interest, dividends, compensation for services, rents and royalties, gains from sales of property and social security benefits. In terms of these provisions, business income is generally deemed to be sourced where the services are actually performed.[178] The place of contracting and the time and place of payment are irrelevant in the determination of source in this regard.[179]

The USA relieves international double taxation by granting an FTC. The credit is granted under US domestic law, in terms of sections 901 to 909 of the IRC, and does not require the application of a DTA, although where treaties are in place these will

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[176] Suringa, D *Volume 96b Subject 2: Key practical issues to eliminate double taxation of business income*, United States at pg. 690, Cahiers de Droit Fiscal International, International Fiscal Association (2011).
[177] United States of America, Internal Revenue Code of 1986, Title 26 of the United States Code.
[178] Bischel, J E & Levin, L D *Volume 97a Subject 1: Enterprise services*, United States at pg. 721, Cahiers de Droit Fiscal International, International Fiscal Association (2012).
[179] U.S. Department of the Treasury, Internal Revenue Service (2017), *Sourcing of Income*, FTC/C/10_02-05, LB&I Concept Unit Knowledge Base – International.

generally obligate the USA to grant an FTC in any event, consistent with the normal rules and limitations applicable in the USA.[180]

In terms of the FTC rules, the credit is only available as a credit against USA tax on foreign source income. Thus, as services physically provided in the USA to a customer in an African jurisdiction will be deemed to be USA source income, the tax withheld on the payment from the African jurisdiction will not be eligible for a credit.

In order for an FTC to be allowed the foreign tax must be compulsory, which includes being reasonably owed in terms of foreign law and being levied in accordance with a reasonable interpretation of foreign legislation or the relevant clauses of a DTA.[181]

In treaty terms, FTCs are limited to the reduced rates noted in the relevant treaty. Taxpayers are expected to approach the authorities of the foreign jurisdiction for refund of the excess tax paid. Where a US treaty does not include a specific technical service fee article, this income is to be dealt with in terms of the Business Profits article which could result in the USA deeming a 0 per cent tax rate to apply to a specific service fee transaction, whilst the foreign jurisdiction may apply their domestic rate. This tax incurred by the USA taxpayer would not be allowable as a credit.

If, however, the USA taxpayer can prove that all reasonable efforts to obtain a refund of such excess tax from the foreign jurisdictions or competent authorities have been made, it may be possible for that foreign tax paid to be allowable as a credit.[182]

There are many administrative hurdles associated with providing the necessary evidence required though. The burden of proof, will rest with the taxpayer.

Where the amount of excess foreign tax paid is disallowed as an FTC and proof cannot be provided of exhausting all avenues of remedy it does not appear that the excess amount can be claimed as a deduction from taxable income.

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[180] Rienstra, J G *United States - Corporate Taxation*, Country Tax Guides IBFD (accessed 24 Jul. 2019), par. 7.2.6.1.1. at pg. 123, https://research-ibfd-org.ezproxy.uct.ac.za/#/doc?url=/linkresolver/static/cta_us.
[181] U.S. Department of the Treasury, Internal Revenue Service (2017), *Exhaustion of Administrative Remedies*, FTC/P/10_01_02-01, LB&I Concept Unit Knowledge Base – International.
[182] Ibid.

USA taxpayers must make an annual declaration as to whether a claim for foreign taxes paid will be in the form of a deduction from taxable income or in the form of an FTC against their tax liability. The method chosen applies to all foreign taxes paid and claimable in that particular year of assessment. Mixing of credit and deduction methods is not allowed unless specific exemptions apply.[183]

An interesting aspect to the FTC rules provided by the US IRC, is that FTCs are disallowed in full for foreign taxes paid to jurisdictions with which the USA has sanctioned diplomatically or with which diplomatic ties have been severed or which the USA does not recognise.[184]

Excess qualifying FTCs can be carried over for a period of ten years and carried back to the previous year of assessment.

The definition of source and application of FTC rules in the USA, appear to largely be consistent with the treatment and application in South Africa.

5.2 India

India is a developing nation but also a significant exporter of services. India also has well defined and firm views on source.

Source rules in India are generally governed by section 5, which deals with source rules, and section 9, which deals with deemed source rules, of the India Income Tax Act.[185]

In terms of section 5, income, from whatever source, that arises or accrues in India or is deemed to arise or accrue in India will have its source in India.[186] The expressions

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[183] U.S. Department of the Treasury, Internal Revenue Service (2017), *Creditability of Foreign Tax Credit Claimed*, FTC/C/10_01-05, LB&I Concept Unit Knowledge Base – International.

[184] Rienstra, J G *United States - Corporate Taxation*, Country Tax Guides IBFD (accessed 24 Jul. 2019), par. 7.2.6.1.9.1. at pg. 134, https://research-ibfd-org.ezproxy.uct.ac.za/#/doc?url=/linkresolver/static/cta_us.

[185] India, *Income Tax Act, 1961 [43 of 1961] as amended by Finance Act, 2020 and Taxation and Other Laws (Relaxation of Certain Provisions) Ordinance, 2020*, https://www.incometaxindia.gov.in/pages/acts/income-tax-act.aspx.

[186] India, Section 5, *Income Tax Act, 1961 [43 of 1961] as amended by Finance Act, 2020 and Taxation and Other Laws (Relaxation of Certain Provisions) Ordinance, 2020*, https://www.incometaxindia.gov.in/pages/acts/income-tax-act.aspx.

"accrues in India" and "arise in India" are used in the India Income Tax Act and the relevant literature interchangeably and thus can be seen to mean the same thing. The concepts of receipt and accrual are not expanded on in the India Income Tax Act, but these concepts are well developed in a wide spectrum of Indian case law spanning many decades.[187]

The central principle of the source rules in India is that of "territorial nexus". Thus, if income generating activities are performed in India, the income is regarded as (actually) arising in India and therefore, taxable in India.[188]

In addition to the source rules as laid out in section 5, deemed source rules are provided in terms of section 9 of the India Income Tax Act.[189] This provision describes various situations, in which income is deemed to arise in India even if it does not actually arise in India. Interestingly income arising directly or indirectly through or from any *business connection* in India may be deemed to be from a source within India.[190]

Although "business connection" is not defined in the India Income Tax Act, explanations within section 9 provide some guidance. There is also significant volumes of case law and judicial interpretation of the concept. In basic terms the guidance around establishing a "business connection" appear to be similar to that for establishing whether a permanent establishment exists or not. In other words, is there significant economic presence, with an element of continuity, that creates a real connection with India.[191]

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[187] Mehta, A *Source rules in India*, Asia-Pacific Tax Bulletin, 2014 (Volume 20) No. 6, 26 November 2014, at par. 3 at pg. 4, IBFD, https://www.ibfd.org/sites/ibfd.org/files/content/pdf/aptb_2014_06_in_2.pdf.
[188] Ibid, at par. 2 at pg. 1.
[189] India, Section 9(1), *Income Tax Act, 1961 [43 of 1961] as amended by Finance Act, 2020 and Taxation and Other Laws (Relaxation of Certain Provisions) Ordinance, 2020*,
https://www.incometaxindia.gov.in/pages/acts/income-tax-act.aspx
The following incomes shall be deemed to accrue or arise in India :—
(i) all income accruing or arising, whether directly or indirectly, through or from any business connection in India, or through or from any property in India, or through or from any asset or source of income in India, or through the transfer of a capital asset situate in India.
[190] Mehta, A *Source rules in India*, Asia-Pacific Tax Bulletin, 2014 (Volume 20) No. 6, 26 November 2014, at par. 3 at pg. 4, IBFD, https://www.ibfd.org/sites/ibfd.org/files/content/pdf/aptb_2014_06_in_2.pdf.
[191] All Answers Ltd. November 2018. *Business Connection and Income Tax Act*. [online]. Available from: https://www.lawteacher.net/free-law-essays/commercial-law/business-connection-and-income-tax-act-commercial-law-essay.php?vref=1 [Accessed 10 August 2020].

In an effort to provide further guidance, section 9A of the India Income Tax Act deals with the activities which are specifically not deemed to create a business connection with India.

Relief from foreign taxation is provided in two ways, namely unilateral relief, governed by section 91 of the India Income Tax Act, and bilateral relief, governed by section 90 of the India Income Tax Act.

Unilateral relief is provided by means of the ordinary credit method, in the form of an FTC, in respect of income derived from a country with which India does not have a DTA. This aspect is interpreted strictly, hence even if a country has a limited agreement in place with India, unilateral relief, in terms of section 91, will be denied in respect of income from that country. The FTC is applicable to foreign income tax on income which accrues or arises outside India and is not deemed to accrue or arise in India. The credit allowed against Indian income tax is given at the Indian or foreign rate of tax, whichever is lower.[192]

The FTC is calculated separately for each source of income arising from each country. India does not provide for the rollover of excess credits, thus any FTCs not claimable in a particular year of assessment are lost.[193] Furthermore, these lost credits cannot be claimed as a business expense in terms of section 37 of the India Income Tax Act.[194]

Where an agreement relating to double taxation relief is in place, the relief will be granted in terms of the DTA. However, where the provisions of the India Income Tax Act are more favourable to a taxpayer than the provisions under the tax treaty, the provisions of the India Income Tax Act will apply.[195] Where foreign tax has been paid which exceeds the amount of tax payable in accordance with the provisions of the DTA,

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[192] Shah, S *India - Corporate Taxation*, Country Tax Guides IBFD (accessed 8 Jan. 2020), par. 7.2.6.1. at pg. 140, https://research-ibfd-org.ezproxy.uct.ac.za/#/doc?url=/document/cta_in_chaphead.
[193] Ibid, par. 7.2.6.1. at pg. 141.
[194] Ibid, par. 7.2.6.1. at pg. 142.
[195] Shah, S *India - Corporate Taxation*, Country Tax Guides IBFD (accessed 8 Jan. 2020), par. 7.4.1.2. at pg. 154, https://research-ibfd-org.ezproxy.uct.ac.za/#/doc?url=/document/cta_in_chaphead.

this excess tax paid will be disregarded.[196] This excess amount would also not be claimable as a business expense in terms of section 37.

The definition and interpretation of source in terms of Indian tax legislation and case law appears to have a much wider scope than South Africa. This, together with provisions of the India Income Tax Act relating to unilateral and bilateral double taxation relief, which are largely similar to that of South Africa, can create similar opportunities for unrelieved double taxation. This is especially true when the fact that excess credits are disregarded in full is taken into consideration.

5.3 Mauritius

Mauritius was selected due to this jurisdiction's efforts to position itself as a hub for MNEs to expand into Africa. Prior to the Finance Act of 2018,[197] Mauritian companies who were in possession of a Category 1 Global Business License ("GBL") were eligible to apply the higher of actual FTCs or a deemed 80 per cent FTC against all types of foreign source income. This resulted in an effective tax rate of 3 per cent, which together with no foreign exchange controls, made Mauritius a very attractive investment destination. However, the GBL rules also resulted in Mauritius gaining tax haven status, which limited this attractiveness to business, in the modern BEPS era.

A vast array of domestic tax and finance legislation amendments have been processed in the last couple of years, specifically with regard to improvements in tax good governance and policies, which resulted in Mauritius being removed from the EU[198] and OECD[199] black/grey list of tax haven countries. This, it can be argued, together with an expanding tax treaty network has made Mauritius more attractive as an

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[196] India, *Rule-128 Foreign Tax Credit*, Income Tax, 1961 [43 of 1961] as amended by Finance Act, 2020 and Taxation and Other Laws (Relaxation of Certain Provisions) Ordinance, 2020, https://www.incometaxindia.gov.in/Rules/Income-Tax%20Rules/rule128.htm.

[197] Legal Supplement to the Government Gazette of Mauritius No. 71 of 9 August 2018, *The Finance (Miscellaneous Provisions) Act 2018, Act No. 11 of 2018.*

[198] European Commission, *Evolution of the EU list of tax havens*, 8 November 2019, https://ec.europa.eu/taxation_customs/sites/taxation/files/eu_list_update_08_11_2019_en.pdf.

[199] OECD (2017), *Global Forum on Transparency and Exchange of Information for Tax Purposes: Mauritius 2017 (Second Round): Peer Review Report on the Exchange of Information on Request*, Global Forum on Transparency and Exchange of Information for Tax Purposes, OECD Publishing, Paris, https://doi.org/10.1787/9789264280304-en.

investment destination and the country can now be seen to be a more direct competitor to South Africa for entities seeking a base from which to expand into the continent.

Part of the amendments implemented focused on revised GBL rules and included the abolishment of the deemed FTC, much stricter substance and "place of effective management" rules and the implementation of an 80 per cent deemed exemption which applies only to specific income types, such as foreign source interest and foreign source dividends.[200]

The unilateral relief mechanism provided by section 77 of the Income Tax Act of Mauritius, is that of an ordinary FTC scheme that now applies equally to standard companies as well as those holding GBL designation. The taxpayer may elect to claim the credit on aggregate foreign-source income or on a source-by-source basis. For the credit to be allowed, the foreign tax must be a tax on income and must be of a similar character to Mauritian tax.[201]

Excess credits are not refunded and the balance of excess credits cannot be carried forward to a subsequent year.[202]

Foreign source income is defined in the Mauritius Income Tax Act as "income which is not derived from Mauritius".[203] Section 74 of the Mauritius Income Tax Act specifically states which items of income are deemed to be derived from Mauritius. Further guidance with regards to the treatment of FTCs are provided by means of specific Income Tax Regulations ("Foreign Tax Credit Regulations) which deal with FTCs.[204]

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[200] Hamzaoui, R *Mauritius - Corporate Taxation*, par. 1.3.2. at pg. 8, Country Tax Guides IBFD (accessed 8 Jan. 2020), https://research-ibfd-org.ezproxy.uct.ac.za/#/doc?url=/document/gtha_mu_chaphead.
[201] Ibid, par. 6.1.4. at pg. 20.
[202] Ibid.
[203] Mauritius, Section 2 of The Income Tax Act 1995 (Consolidated up to June 2020), http://mra.mu/download/ITAConsolidated.pdf.
[204] Mauritius, *The Income Tax (Foreign Tax Credit) Regulations 1996 GN 80 of 1996 - 20 July 1996*, Regulations made by the Minister under sections 77 and 161 of the Income Tax Act 1995, http://mra.mu/download/Regulations_foreignTaxCredit_GN_55_2011.pdf.

The relevant sections of the Mauritius Income Tax, the Foreign Tax Credit Regulations and the Statement of Practise on Foreign Tax Credits[205] issued by the Mauritius Revenue Authority ("MRA") interact with each other in regard to the treatment of FTCs. Further to this, taxpayers can approach the MRA for Income Tax rulings, and in this regard a number have been issued relating to FTCs.

Section 77 of the Mauritius Income Tax Act states that:

> "*where a taxpayer derives income which is subject to foreign tax, the amount of foreign tax so paid shall be allowed as a credit against income tax payable in Mauritius in respect of that income.*"

Despite this seeming to apply to all income which was subject to foreign tax, the Regulations and Statement of Practise clarify that the credit will only be granted against foreign source income.

A review of the Income Tax rulings issued also confirms that the MRA takes the view that where fees are derived from services provided in Mauritius, these fees will be seen to be derived from Mauritius i.e., not foreign source.[206]

Thus, whilst it may appear that the legislation governing the application of FTCs in Mauritius is more straightforward than in South Africa, the concepts relating to source are largely the same. Admittedly however there does appear to be less of the complexity noted in the South African system. The benefit of a lower Corporate Income Tax rate must also be weighed up against the fact that Mauritius does not have a roll-over mechanism for excess credits.

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[205] Mauritius, *Statement of Practise (SP2/09): Claim for Foreign Tax Credit*, https://www.mra.mu/download/SP_FTaxCredit.pdf.
[206] Mauritius, Income Tax Rulings, Mauritius Revenue Authority, https://www.mra.mu/index.php/media1/rulings/income-tax-rulings.

5.4 United Kingdom

The UK is a significant trading partner with many countries in Africa. The UK also has an extensive treaty network and has a large number of DTAs in force with African jurisdictions. The UK is also a large exporter of services into Africa.

Foreign tax relief in the UK is largely governed by the provisions of the Taxation (International and Other Provisions) Act 2010 ("TIOPA"). The UK provides relief, depending on the source and type of income, by either the credit method or the exemption method. In certain cases, deduction of foreign taxes paid is also allowed.[207] However, despite a deduction method being available, it is not possible to claim relief for the same amount of foreign tax by both a credit and a deduction.[208]

Income from the provision of services would fall within the credit relief method.

In order to claim Double Tax Relief ("DTR") in terms of UK tax legislation, the taxpayer must first be able to show that they have taken all reasonable steps, either under the foreign domestic legislation or in terms of the applicable DTA, to minimise the foreign tax payable.[209] HM Revenue and Customs ("HMRC") will not accept a claim for DTR unless these steps have been taken.[210]

When DTR can be claimed, credit relief is only granted on a source-by-source, item-by-item basis.[211]

FTC relief is also only available against foreign-source income and is limited, in terms of a formula, to the relevant amount of UK Corporate Income Tax payable.

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[207] Bennet, J *United Kingdom - Corporate Taxation*, par. 7.2.6. at pg. 68, Country Tax Guides IBFD (accessed 24 Jul. 2019), https://research-ibfd-org.ezproxy.uct.ac.za/#/doc?url=/document/cta_uk_chaphead.

[208] Bramsdon, J *Tax Factsheet | Double Tax Relief*, Saffrey Champness (Feb 2020), https://www.saffery.com/news-and-events/publications/double-tax-relief-february-2020.

[209] Kayser, M & Richards, G *Volume 96b Subject 2: Key practical issues to eliminate double taxation of business income*, United Kingdom at pg. 676, Cahiers de Droit Fiscal International, International Fiscal Association (2011).

[210] Bramsdon, J *Tax Factsheet | Double Tax Relief*, Saffrey Champness (Feb 2020), https://www.saffery.com/news-and-events/publications/double-tax-relief-february-2020.

[211] Bennet, J *United Kingdom - Corporate Taxation*, par. 7.2.6. at pg. 68, Country Tax Guides IBFD (accessed 24 Jul. 2019), https://research-ibfd-org.ezproxy.uct.ac.za/#/doc?url=/document/cta_uk_chaphead.

Excess qualifying credits can be carried forward for an unlimited period of time and may also be carried back for a period of 3 years.[212]

The UK does not have general rules in place for the determination of the source of an item of income. In terms of relevant case law and practise prevailing, the source is deemed to be the place of performance.[213]

The main criterion used by the HMRC in determining source is to determine where the operation took place from which the profits, in substance, arise. Thus, in relation to services the relevant factor would be the place where the services are actually performed.[214]

In the scenario where services are provided from the UK, to a customer in a foreign jurisdiction, that income will be seen to be UK source income and will not qualify for FTC relief.

Section 9 of TOPIA specifically states that unilateral relief is only available to foreign taxes paid on income arising from that foreign territory.[215]

The determination of source and application of FTC relief in the UK is largely consistent with the methodologies applied by South Africa.

5.5 Sweden

Whilst Sweden may not be thought of as a large exporter of services to Africa, it's application of unilateral relief in terms of its domestic tax legislation, which is considered to be quite generous, has some interesting aspects. Sweden was chosen due to its unique position with regards to unilateral tax relief and its FTC mechanism.

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[212] Bennet, J *United Kingdom - Corporate Taxation*, par. 7.2.6.1. at pg. 69, Country Tax Guides IBFD (accessed 24 Jul. 2019), https://research-ibfd-org.ezproxy.uct.ac.za/#/doc?url=/document/cta_uk_chaphead.
[213] Miller, A *Volume 97a Subject 1: Enterprise services*, United Kingdom at pg. 706, Cahiers de Droit Fiscal International, International Fiscal Association (2012).
[214] Ibid at pg. 706-707.
[215] United Kingdom, Taxation (International and Other Provisions) Act 2010, Part 2, Section 9, *Rule 1: the unilateral entitlement to credit for non-UK tax*, https://www.legislation.gov.uk/ukpga/2010/8/part/2.

Sweden has an extensive DTA network which includes a relatively large amount of treaties with various African jurisdictions.

In terms of the DTAs that Sweden currently has in force, only a few older treaties elect the exemption method of relief with the remaining majority electing the credit method of relief.

FTCs are governed, in terms of domestic legislation, by the Foreign Tax Credit Law.[216] Where treaties are in force these provisions are read together with the provisions of the relevant treaty.

Sweden imposes the following general conditions for an FTC to be allowable. These are:

- It must be the taxpayer that has earned the income;
- which has been assessed according to the Swedish Income Tax Act i.e. included in the taxpayer's taxable income;
- the taxpayer has been taxed on this income in a foreign state; and
- the income in question is considered to arise in that foreign state as a result of the application of that foreign state's domestic tax legislation.[217]

Based on the above it is evident that the Swedish unilateral tax relief mechanism has a unique approach to determining the source of income. The mechanism itself does not contain any source rules as such with the main precondition being that the other state considers the income to arise from its own territory.[218]

The requirement for the determination of the source of income generally only arises when questions of dual residence arise. The source of income is therefore determined on the basis of the foreign states tax legislation. By doing so, discrepancies between the states are avoided to a large extent.[219]

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[216] Sweden, Lag om avräkning av utländsk skatt("AvrL"), Foreign Tax Credit Law.
[217] Berglund, M & Bexelius, F *Volume 96b Subject 2: Key practical issues to eliminate double taxation of business income*, Sweden at pg. 629, Cahiers de Droit Fiscal International, International Fiscal Association (2011).
[218] Ibid.
[219] Ibid.

This methodology is also aligned with the Swedish treaty policy.

Sweden obviously applies limitations to the FTC claimable and this is determined by means of a formula and is also limited to the rate of Swedish Corporate Income Tax payable, which is currently set at 22 per cent.

Sweden also allows for both the deduction and credit methods, simultaneously. In terms of this, foreign taxes paid (subject to certain provisos) are deemed to be deductible expenses in the determination of a taxpayer's taxable income. Where foreign taxes paid are also eligible for an FTC, the allowable credit is reduced by the Swedish tax saved as a result of the deduction allowance.[220] Any excess FTCs remaining, can be carried forward for a period of 5 years.

The Swedish system is certainly interesting but its applicability in a South African context is questionable. Sweden has a relatively low Corporate Income Tax rate which helps with the limitation of the allowable credit. The application of this method in a high tax environment would likely lead to abuse and tax base erosion for the state of residence.

The following chapter will summarise the findings of this basic analysis of the South African FTC system. Where applicable, recommendations for possible improvements to the system will be noted and any useful methodologies utilised by other countries will be included. Concluding remarks will then be noted.

[220] Van Der Zeijden, F *Sweden - Corporate Taxation*, par. 7.2.6.1. at pg. 37, Country Tax Guides IBFD (accessed 8 Jan. 2020), https://research-ibfd-org.ezproxy.uct.ac.za/#/doc?url=/linkresolver/static/cta_se.

CHAPTER 6: RECOMMENDATIONS AND CONCLUSION

At the outset of this paper, the South African legislation and practise surrounding determination of source and the provision of tax relief, in the form of FTCs, was judged negatively.

A review of the unilateral relief mechanisms, specifically in the form of FTCs, of several countries were reviewed, with 5 being included for analysis in this paper, and it was noted that, to a large extent, the South African application of FTCs and determination of source is consistent with that of foreign jurisdictions.

This doesn't mean however that the system is correct. It does mean that our FTC system in South Africa and the systems present in many foreign jurisdictions have not progressed and improved over time and are not well suited to the increasing trade in services and the service economy.

Together with this is the need for the tax policies of capital importing countries and capital exporting countries as well as the tax policies of the OECD and UN to aim for better alignment. This is not an easy task as the needs and requirements, from a tax perspective, of developed nations differs from that of developing nations, especially within the realm of technical service fees and determination of source.

In the South African context, any amendments that are implemented must ensure competitiveness but also minimise any risk of unnecessarily reducing the tax base.[221]

6.1 Treaty network and treaty wording

The most obvious method to improve the treatment and application of FTCs and their perceived fairness is to increase the network of countries with which South Africa has not yet negotiated and entered into DTAs with. The assumption being that an extensive DTA network should reduce opportunities for double taxation and provide some level of certainty for taxpayers and investors alike. The wording of the treaties

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[221] Davis Tax Committee, *Executive Summary of the second interim report on Base Erosion and Profit Shifting (BEPS): OECD BEPS Project from a South African perspective: Policy perspectives and recommendations for South Africa* (2016), at 7.7.10., (accessed 7 September 2020), https://www.taxcom.org.za/docs/New_Folder3/1%20BEPS%20Final%20Report%20-%20Executive%20Summary.pdf.

must provide clarity and reduce opportunities for confusion, both from the perspective of the taxpayer and the tax authority.

In conjunction with this, is the renegotiation of all of the treaties that are currently in place that are outdated and not in accordance with the modern format of the OECD or UN models.[222]

Renegotiation can be in the form of Protocols, where the current treaty is in the modern OECD or UN format or a completely new treaty where the current treaty is out of date.

All new treaties should include the following:

- A technical service fee article, which will go hand in hand with the introduction in South Africa of a withholding tax on service fee payments to non-residents (see below); or
- Including a technical service fee provision in either the Royalties article or the Business Profits article in a similar way to what was negotiated in the South African treaties with the Netherlands and Saudi Arabia;
- Where a technical service fee article or provision cannot be included, for whatever reason, then the treaty needs to include a definition of "business" in the definitions article of the treaty. This definition of "business" must include the provision of professional services;
- Concerns surrounding BEPS could be combatted by including to the effect that a reduced rate of withholding tax will not apply to service fee transactions between connected parties which are not at arm's length.

Clarity of wording and inclusion of specific articles or provisions will also aid in reducing double taxation on service fee income, and other conflicts, arising as a result of the application of Article 21(3).

[222] Several of South Africa's double tax treaties were entered into force in the fifties and sixties and are outdated

6.2 South African withholding tax on services

South Africa, despite its earlier intentions, did not implement a withholding tax on technical service fee payments made to non-residents. Instead, National Treasury felt that this was dealt with sufficiently by the provisions of the Reportable Arrangement rules. These rules however only apply to transactions in excess of R10 million.

Whilst the Reportable Arrangement mechanism has its benefits, it may be of better effect if it worked hand-in-hand with a withholding tax on service fee income. Thus, below the threshold of R10 million, the service fee income is subject only to a withholding tax whilst over that threshold, the Reportable Arrangement rules apply in addition to a withholding tax.

By implementing a withholding tax on services, which as can be noted in Annexure 1 is implemented by a large number of our trading peers, the tax base in increased and our negotiating position for amending current tax treaties to include articles or provisions relating to technical service fees is improved.

Having a withholding tax on services may also provide some leeway for the tax authorities to improve some of the reliefs provided by the FTC rules.

6.3 Services PE

All new treaties that are negotiated by South Africa must include a Services PE clause in line with the recommendations of the Davis Tax Committee as well as the latest OECD and UN MTCs.[223]

In order to assist with negotiation of treaties, in line with the recommendation noted in 6.1, South Africa could possibly also adopt a reduced services PE threshold of 120 days. This may not be beneficial to South African taxpayers but may encourage our partners to be more amenable to other suggestions South Africa notes in treaty negotiations.

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[223] Davis Tax Committee, *Davis Tax Committee Note on territorial taxation: Will a move from a worldwide to a territorial system ensure the efficiency of South Africa's tax system?* (2016), at par (c), (accessed 7 September 2020), https://www.taxcom.org.za/docs/20180412%20DTC%20Note%20on%20Territorial%20Taxation.pdf.

6.4 Concessions for unilateral relief in non-treaty scenarios

Unilateral relief in non-treaty scenarios encounters complications where the income is deemed to be from a source within South Africa. South Africa exports a large number of services into Africa, and a large number of these services are provided remotely.

A provision, similar to that of the repealed section 6*quin* could be considered with stricter caveats.

- Taxpayer would be required to separate its declaration of FTCs between treaty countries and non-treaty countries;
- A deemed FTC of 5 per cent or 10 per cent (based on the service fee income earned from the non-treaty countries) could be applied or the taxpayer could elect the actual allowable FTCs available on the actual foreign source service fee income. The taxpayer would have to elect this on an annual basis and this would apply to all non-treaty countries for the relevant year of assessment.
- If the deemed credit is elected, excess credits would not be eligible for roll-over.

6.5 Improved usage and access to MAP

African jurisdictions have very low take-up, in comparison to our peers in other parts of the world, of the relief mechanisms provided by the DTAs such as MAP and arbitration.

If South Africa intends to market itself as the destination of choice for Multinationals to expand into Africa, it needs to improve its collaboration with its African peers in the sphere of taxation and resolution of double taxation issues.

As ever though, MAP and other treaty remedies are only available where treaties are actually in place and in force and are thus limited by the treaty network.

6.6 Other amendments to the foreign tax credit rules

A relaxation of source rules with regards to FTC available on service fee income could be considered if implemented together with the following concessions:

- Reduction of the FTC roll-over period from 7 years to 5 or less;
- Introducing a source-by-source, item-by-item or per country FTC limitation

A large number of these recommendations come together with administrative burdens. However, with the increasing amount of trade in services on the African continent this is an issue which will have to be dealt with sooner rather than later.

The simplest solution is an increased treaty network, with detailed treaties but this is not necessarily a realistic solution, when politics and the treaty negotiation timelines are considered. The best way forward may then be for some combination of all of the above recommendations to be implemented. The appetite for amendments such as this may, even if countered with an introduction of a withholding tax on services, be minimal especially when considering the environment of already reduced tax collections and tough economic conditions.

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Revenue Laws Amendment Act 32 of 2004

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Jurisdiction	DTA with South Africa	Technical Service Fee Article in Treaty	Technical Service Fee WHT in domestic law of jurisdiction	Domestic rate of WHT on Technical Service Fees (to non-residents)	Rate of WHT on Technical Service Fees per DTA	Comment
Algeria	Yes	No	Yes	24,00% 20,00%	N/A	Reduced rate of WHT applies to management fee payments to non-residents
Angola	No	N/A	Yes	6,50%	No DTA	
Benin	No	N/A	Yes	12,00%	No DTA	
Botswana	Yes	Yes	Yes	15,00%	10,00%	
Burkina Faso	No	N/A	Yes	20,00%	No DTA	
Burundi	No	N/A	Yes	15,00%	No DTA	
Cameroon	Yes	Yes	Yes	15,00%	10,00%	
Cape Verde	No	N/A	Yes	20,00%	No DTA	
Central African Republic (CAR)	No	N/A	Yes	15,00%	No DTA	
Chad	No	N/A	Yes	25,00% 20,00%	No DTA	Reduced rate of WHT applies to management fee payments to non-residents
Comoros	No	N/A	Yes	10,00%	No DTA	
Congo, Democratic Republic of the	Yes	No	Yes	14,00%	N/A	
Congo, Republic of the	No	N/A	Yes	20,00% 5,75%	No DTA	Reduced rate of WHT if derived from contracts related to "Zone of Unitization"
Cote d'Ivoire	No	N/A	Yes	20,00%	No DTA	
Djibouti	No	N/A	Yes	15,00% 0,00%	No DTA	Reduced rate of WHT applies if payments to non-residents are made by entities: established in Djibouti "Free Zones"; or exempt in terms of Djibouti Investment Code
Egypt	Yes	No	Yes	20,00%	N/A	
Equatorial Guinea	No	N/A	Yes	20,00%	No DTA	
Eritrea	No	N/A	Yes	10,00%	No DTA	
Eswatini (formerly Swaziland)	Yes	Yes	Yes	15,00%	10,00%	
Ethiopia	Yes	No	Yes	15,00%	N/A	
Gabon	No	N/A	Yes	20,00%	No DTA	
Gambia	No	N/A	Yes	15,00% 10,00%	No DTA	Reducedrate of WHT applies for services rendered by contractors during exploration/appraisal stages of petroleum operations
Ghana	Yes	Yes	Yes	20,00%	10,00%	
Guinea	No	N/A	Yes	15,00%	No DTA	
Guinea-Bissau	No	N/A	Yes	10,00%	No DTA	The WHT is not a final tax
Kenya	Yes	No	Yes	20,00% 5,00%	N/A	Reduced rate of WHT applies if paid by a "special economic zone" enterprise, developer or operator
Lesotho	Yes	Yes	Yes	10,00%	7.5%	
Liberia	No	N/A	Yes	15,00%	No DTA	
Libya	No	N/A	No	0,00%	No DTA	
Madagascar	No	N/A	Yes	10,00%	No DTA	
Malawi	Yes	No	Yes	15,00% 10,00%	N/A	Reduced rate of WHT applies to mining projects
Mali	No	N/A	Yes	15,00%	No DTA	
Mauritania	No	N/A	Yes	15,00% 25,00%	No DTA	Lower rate is on gross basis if service provider is operating in Mauritania for less than 6 months. Otherwise the increased rate, at the net basis, will apply
Mauritius	Yes	No	Yes	10,00%	N/A	
Morocco	No	N/A	Yes	10,00%	No DTA	
Mozambique	Yes	No	Yes	20,00% 10,00%	N/A	Reduced rate of WHT applies to fees paid by telecommunication and international transport companies, certain electrical power-related activities and fishing boat leasing
Namibia	Yes	No	Yes	10,00%	N/A	
Niger	No	N/A	Yes	16,00%	No DTA	
Nigeria	Yes	No	Yes	10,00%	N/A	
Rwanda	Yes	Yes	Yes	15,00%	10,00%	
Sao Tome and Principe	No	N/A	Yes	20,00%	No DTA	
Senegal	No	N/A	Yes	20,00%	No DTA	
Seychelles	Yes	No	Yes	15,00%	N/A	
Sierra Leone	Yes	No	Yes	15,00%	N/A	
Somalia	No	N/A	No Data	No Data	No DTA	
South Sudan	No	N/A	Yes	15,00%	No DTA	
Sudan	No	N/A	Yes	7,00%	No DTA	
Tanzania	Yes	No	Yes	15,00%	N/A	
Togo	No	N/A	Yes	20,00%	No DTA	
Tunisia	Yes	Yes	Yes	15,00% 25,00%	12,00%	Increased rate of WHT applies if the recipient is resident in a jurisdiction applying a preferential tax regime
Uganda	Yes	Yes	Yes	15,00%	10,00%	

Jurisdiction	DTA with South Africa	Technical Service Fee Article in Treaty	Technical Service Fee WHT in domestic law of jurisdiction	Domestic rate of WHT on Technical Service Fees (to non-residents)	Rate of WHT on Technical Service Fees per DTA	Comment
Zambia	Yes	No	Yes	20,00%	N/A	
Zimbabwe	Yes	Yes	Yes	15,00%	5,00%	

[1] Data obtained from various sources
[2] Country Tables, http://www.healyconsultants.com
[3] Deloitte, Guide to fiscal information, Key economies in Africa 2019, https://www2.deloitte.com/za/en/pages/tax/articles/guide-to-fiscal-information-key-economies-frica-2019.html
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[5] PKF, Africa tax guide 2018-2019, https://pkf.com/media/10038862/pkf-africa-tax-guide-2018-2019_interactive-1.pdf
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South Africa's treaty network in relation to Technical Service Fees & Elimination of Double Taxation **Annexure 2**

Analysis of South Africa's Tax Treaty network with regard to the inclusion of specific articles or provisions for Technical Service Fees

Jurisdiction	Region	Entry into Force	Does the DTA contain a "subject to" clause for South Africa in the "Elimination of Double Taxation" Article?	Inclusion of "services" in definition of business in terms of General Definitions Article of Treaty*	Technical Service Fee Article in Treaty	Does Technical Service Fee Article contain a "deemed source" rule?	Technical Service Fee WHT in domestic law of jurisdiction	Domestic rate of WHT on Technical Service Fees	Rate of WHT on Technical Service Fees per DTA
Algeria	Africa	12 June 2000	No	No	No	N/A	Yes	24%	N/A
Australia	Asia Pacific	21 December 1999	No	No	No	N/A	No	-	N/A
Austria	Europe	6 February 1997	No	No	No	N/A	Yes	20%	N/A
Belarus	Europe	29 December 2003	Yes - Article 22	Yes	No	N/A	Yes	15%	N/A
Belgium	Europe	9 October 1998	No	No	No	N/A	No	-	N/A
Botswana	Africa	20 April 2004	Yes - Article 22	No	Yes - Article 20	Yes - Article 20(5)	Yes	15%	10,00%
Brazil	Americas	24 July 2006	Yes - Article 23	No	No	N/A	Yes	15% (25% if the beneficiary is resident of a low-tax jurisdiction)	N/A
Bulgaria	Europe	27 October 2004	Yes - Article 22	No	No	N/A	Yes	10%	N/A
Cameroon	Africa	13 July 2017	Yes - Article 24	No	Yes - Article 14	Yes - Article 14(5)	Yes	15%	10,00%
Canada	Americas	30 April 1997	No	No	No	N/A	Yes	25%	N/A
Chile	Americas	11 August 2016	Yes - Article 22	Yes	No	N/A	Yes	15% (20% under certain conditions)	N/A
China (People's Republic of China PRC)	Asia Pacific	7 January 2001	No	No	No	N/A	No	-	N/A
Croatia	Europe	7 November 1997	No	No	No	N/A	Yes	15% (20% for non-EU companies under certain conditions)	N/A
Cyprus	Europe	8 December 1998	No	No	No	N/A	Yes	10%	N/A
Czech Republic	Europe	3 December 1997	No	No	No	N/A	Yes	15% 35% (recipient not resident in EU/EEA country; or no treaty or TIEA; or no multilateral agreement for exchange of information)	N/A
Democratic Republic of Congo (DRC)	Africa	18 July 2012	Yes - Article 21	Yes	No	N/A	Yes	14%	N/A
Denmark	Europe	21 December 1995	No	No	No	N/A	No	-	N/A
Egypt	Africa	16 December 1998	No	No	No	N/A	Yes	20%	N/A
Ethiopia	Africa	4 January 2006	Yes - Article 22	Yes	No	N/A	Yes	15%	N/A
Finland	Europe	12 December 1995	No	No	No	N/A	No	-	N/A
France	Europe	1 November 1995	No	No	No	N/A	Yes	31% (75% withholding tax is applied to fees paid to companies located in a non-cooperative jurisdiction)	N/A
Germany	Europe	28 February 1975	No	No	No	N/A	No	-	N/A
Ghana	Africa	23 April 2007	Yes - Article 24	No	Yes - Article 20	Yes - Article 20(5)	Yes	20%	10,00%
Greece	Europe	14 February 2003	No	No	No	N/A	Yes	20%	N/A
Grenada	Americas	5 October 1960	Yes - Article XIII	No	No	N/A	Yes	15%	N/A
Hong Kong	Asia Pacific	20 October 2015	Yes - Article 21	Yes	No	N/A	No	-	N/A
Hungary	Europe	5 May 1996	No	No	No	N/A	No	-	N/A
India	Asia Pacific	28 November 1997	No	No	Yes - Article 12	Yes - Article 12(6)	Yes	10%	10,00%
Indonesia	Asia Pacific	23 November 1998	No	No	No	N/A	Yes	20%	N/A
Iran	Middle East	23 November 1998	No	No	No	N/A	Yes	2.5% to 10%, according to the type of activity and profitability level	N/A
Ireland	Europe	5 December 1997	No	No	No	N/A	No	-	N/A
Israel	Middle East	27 May 1980	Yes - Article 23	No	No	N/A	Yes	20% to 30%	N/A
Italy	Europe	2 March 1999	No	No	No	N/A	No	30% for fees on the use of, or the right to use, industrial, commercial or scientific equipment located in Italy	N/A
Japan	Asia Pacific	5 November 1997	No	No	No	N/A	Yes	20%	N/A
Kenya	Africa	19 June 2015	Yes - Article 23	No	No	N/A	Yes	20% 5% if paid by a special economic zone enterprise, developer or operator	N/A
Korea (Republic of Korea)	Asia Pacific	7 January 1996	No	No	No	N/A	Yes	20%	N/A

Jurisdiction	Region	Entry into Force	Does the DTA contain a "subject to" clause for South Africa in the "Elimination of Double Taxation" Article?	Inclusion of "services" in definition of business in terms of General Definitions Article of Treaty*	Technical Service Fee Article in Treaty	Does Technical Service Fee Article contain a "deemed source" rule?	Technical Service Fee WHT in domestic law of jurisdiction	Domestic rate of WHT on Technical Service Fees	Rate of WHT on Technical Service Fees per DTA
Kuwait	Middle East	25 April 2006	Yes - Article 23	No	No	N/A	No	No 5% retention (until a non-objection letter is obtained from tax authorities) if part of payments are made for contractors and subcontractors	N/A
Lesotho (Renegotiated)	Africa	27 May 2016	Yes - Article 23	Yes	Yes - Article 13	Yes - Article 13(5)	Yes	10%	7,5%
Luxembourg	Europe	8 September 2000	No	No	No	N/A	No	-	N/A
Malawi	Africa	2 September 1971	Yes - Article 12	No	No	N/A	Yes	15% generally 10% for mining projects	N/A
Malaysia	Asia Pacific	17 March 2006	Yes - Article 23	No	Yes - Article 13	Yes - Article 13(4)	Yes	10%	5%
Malta	Europe	12 November 1997	No	No	No	N/A	No	-	N/A
Mauritius (Renegotiated)	Africa	28 May 2015	Yes - Article 22	Yes	No	N/A	Yes	10%	N/A
Mexico	Americas	22 July 2010	Yes - Article 22	Yes	No	N/A	Yes	25% 40% (if paid to entities subject to preferential tax regime; not taxed if services are performed abroad or not used (technical assistance) in Mexico)	N/A
Mozambique	Africa	19 February 2009	Yes - Article 22	Yes	No	N/A	Yes	20% 10% (fees paid by telecommunication and international transport companies, certain electrical power-related activities and fishing boat leasing)	N/A
Namibia	Africa	11 April 1999	No	No	No	N/A	Yes	10%	N/A
Netherlands (Renegotiated)	Europe	28 December 2008	Yes - Article 23	Yes	Ad Article 7 - deemed to fall within Article 7 in terms of Protocol amendment	Yes - Other State unless accrued via Permanent Establishment	No	-	N/A
New Zealand	Asia Pacific	23 July 2004	Yes - Article 21	Yes	No	N/A	Yes	15%	N/A
Nigeria	Africa	5 July 2008	No	No	No	N/A	Yes	10%	N/A
Norway	Europe	12 September 1996	No	No	No	N/A	No	-	N/A
Oman	Middle East	29 December 2003	Yes - Article 21	Yes	No	N/A	Yes	10% (only where paid for R&D)	N/A
Pakistan	Asia Pacific	9 March 1999	No	No	Yes - Article 12	Yes - Article 12(6)	Yes	15%	10,00%
Poland	Europe	5 December 1995	No	No	No	N/A	Yes	20%	N/A
Portugal	Europe	22 October 2008	Yes - Article 23	No	No	N/A	Yes	25%	N/A
Qatar	Middle East	2 December 2015	Yes - Article 21	Yes	No	N/A	Yes	5%	N/A
Romania	Europe	21 October 1995	No	No	No	N/A	Yes	16% 50% if no agreement providing for exchange of information	N/A
Russian Federation	Europe	26 June 2000	No	No	No	N/A	No	-	N/A
Rwanda	Africa	3 August 2010	Yes - Article 22	Yes	Yes - Article 14	Yes - Article 14(5)	Yes	15%	10,00%
Saudi Arabia	Middle East	1 May 2008	Yes - Article 24	No	Article 7(9) furnishing of services specifically included in "Business Profits"	Yes - Other State unless accrued via Permanent Establishment	Yes	5% 15% (services rendered by head office and associated companies)	N/A
Seychelles	Africa	29 July 2002	Yes - Article XIII (Protocol)	Yes (Protocol)	No	N/A	Yes	15%	N/A
Sierra Leone	Africa	05 October 1960	Yes - Article XIII	No	No	N/A	Yes	15%	N/A
Singapore (Renegotiated)	Asia Pacific	16 December 2016	Yes - Article 21	Yes	No	N/A	Yes	17%	N/A
Slovak Republic	Europe	30 June 1999	No	No	No	N/A	Yes	19% 35% for beneficiaries resident in countries not on the white list	N/A
Spain	Europe	28 December 2007	Yes - Article 22	Yes	No	N/A	Yes	24% (19% for EU residents)	N/A
Swaziland (eSwatini)	Africa	8 February 2005	Yes - Article 22	Yes	Yes - Article 13	Yes - Article 13(5)	Yes	15%	10,00%
Sweden	Europe	25 December 1995	No	No	No	N/A	No	-	N/A
Switzerland (Renegotiated)	Europe	27 January 2009	Yes - Article 22	No	No	N/A	No	-	N/A
Taiwan (Republic of China ROC)	Asia Pacific	12 September 1996	No	No	No	N/A	Yes	20% (3% with special approval)	N/A
Tanzania	Africa	15 June 2007	Yes - Article 21	Yes	No	N/A	Yes	15%	N/A

Jurisdiction	Region	Entry into Force	Does the DTA contain a "subject to" clause for South Africa in the "Elimination of Double Taxation" Article?	Inclusion of "services" in definition of business in terms of General Definitions Article of Treaty*	Technical Service Fee Article in Treaty	Does Technical Service Fee Article contain a "deemed source" rule?	Technical Service Fee WHT in domestic law of jurisdiction	Domestic rate of WHT on Technical Service Fees	Rate of WHT on Technical Service Fees per DTA
Thailand	Asia Pacific	27 August 1996	No	No	No	N/A	Yes	3%, 5%, 15%	N/A
Tunisia	Africa	10 December 1999	No	No	Yes - Article 12A	Yes - Article12A(5)	Yes	15% 25% if the recipient is resident in a jurisdiction applying a preferential tax regime	12,00%
Turkey	Middle East	6 December 2006	Yes - Article 22	No	No	N/A	Yes	20% 5% if petroleum related	N/A
Uganda	Africa	9 April 2001	No	No	Yes - Article 13	Yes - Article 13(5)	Yes	15%	10,00%
Ukraine	Europe	29 December 2004	Yes - Article 21	Yes	No	N/A	No	-	N/A
United Arab Emirates	Middle East	23 November 2016	Yes - Article 22	No	No	N/A	No	-	N/A
United Kingdom	Europe	17 December 2002	Yes - Article 21	Yes	No	N/A	No	-	N/A
United States of America	Americas	28 December 1997	No	No	No	N/A	Yes	30%	N/A
Zambia	Africa	31 August 1956	Yes - Article XII	No	No	N/A	Yes	20%	N/A
Zimbabwe (Renegotiated)	Africa	01 December 2016	Yes - Article 22	Yes	Yes - Article 13	Yes - Article 13(5)	Yes	15%	5,00%

* The inclusion of "services" will generally be recorded as: *"the term "business" includes the performance of professional services and of other activities of an independent character"*

Total number of treaties in force	79
Total number of treaties with "subject to" clause in "Elimination of Double Taxation" Article	40
Total number of treating with "Technical Fees" Article	14
Total number of treating with "Technical Fees" Article and "subject to" clause in "Elimination of Double Taxation" Article	12
Total African countries with which SA has DTA	23
Total countries in Africa excl. SA	53

Jurisdiction	DTA with South Africa	Technical Service Fee Article in Treaty	Technical Service Fee WHT in domestic law of jurisdiction	Domestic rate of WHT on Technical Service Fees (to non-residents)	Rate of WHT on Technical Service Fees per DTA	Comment
Australia	Yes	No	No	0,00%	N/A	
Austria	Yes	No	Yes	20,00%	N/A	
Belgium	Yes	No	Yes	33,00%	N/A	Applies only to certain fees paid to non-residents, subject to conditions. 50% exemption may apply reducing rate to an effective 16,50%
Bulgaria	Yes	No	Yes	10,00%	N/A	
Canada	Yes	No	Yes	25,00%	N/A	
Chile	Yes	No	Yes	15,00%	N/A	Increased to 20% if the non-resident country is a preferential tax regime.
Colombia	No	N/A	Yes	20,00%	N/A	Increased to normal corporate tax rate (32% 2020) if non-resident country is a non-cooperative jurisdiction, low-tax jurisdiction or preferential tax regime jurisdiction.
Croatia	Yes	No	Yes	15,00%	N/A	Increased to 20% if the non-resident country is deemed a non-cooperative jurisdiction.
Cyprus	Yes	No	Yes	10,00%	N/A	
Czech Republic	Yes	No	Yes	15,00%	N/A	Increased to 35% if the non-resident country is deemed a tax haven.
Denmark	Yes	No	No	0,00%	N/A	
Estonia	No	N/A	Yes	10,00%	N/A	For services rendered in Estonia. Increased to 20% of non-resident country is deemed a tax haven. If services are not rendered in Estonia, the withholding tax is reduced to 0%.
Finland	Yes	No	No	0,00%	N/A	
France	Yes	No	Yes	28,00%	N/A	Subject to withholding at the normal corporate tax rate 28% (2020).
Germany	Yes	No	No	0,00%	N/A	
Greece	Yes	No	No	0,00%	N/A	If non-resident has operates through a PE in Greece however the WHT applicable to services is 20%
Hungary	Yes	No	No	0,00%	N/A	
Iceland	No	N/A	Yes	20,00%	N/A	
Ireland	Yes	No	No	0,00%	N/A	
Israel	Yes	No	Yes	25,00%	N/A	Reduction or exemption can be sought if services were provided entirely cross-border
Italy	Yes	No	No	0,00%	N/A	Fees paid for the use of industrial, commercial or scientific equipment based in Italy will be subject to a final WHT of 30%
Japan	Yes	No	Yes	20,00%	N/A	
Korea (Rep.)	Yes	No	Yes	20,00%	N/A	
Latvia	No	N/A	Yes	20,00%	N/A	Management & **Consulting** fees
Lithuania	No	N/A	No	0,00%	N/A	
Luxembourg	Yes	No	No	0,00%	N/A	
Malta	Yes	No	No	0,00%	N/A	If not derived from a PE in Malta
Mexico	Yes	No	Yes	25,00%	N/A	
Netherlands	Yes	Ad Article 7 - deemed to fall within Article 7 in terms of Protocol amendment	No	0,00%	0,00% (Business Profits)	
New Zealand	Yes	No	No	0,00%	N/A	
Norway	Yes	No	No	0,00%	N/A	
Poland	Yes	No	Yes	20,00%	N/A	
Portugal	Yes	No	Yes	25,00%	N/A	

Jurisdiction	DTA with South Africa	Technical Service Fee Article in Treaty	Technical Service Fee WHT in domestic law of jurisdiction	Domestic rate of WHT on Technical Service Fees (to non-residents)	Rate of WHT on Technical Service Fees per DTA	Comment
Romania	Yes	No	Yes	16,00%	N/A	
Slovak Republic	Yes	No	Yes	19,00%	N/A	35% if beneficial owner is not on EU White List
Slovenia	No	N/A	Yes	0,00%	N/A	15% if paid to a country where the CIT is below 12.50%. Also only applies to certain specific services.
Spain	Yes	No	Yes	24,00%	N/A	19% if paid to resident of EU or EEA
Sweden	Yes	No	No	0,00%	N/A	
Switzerland	Yes	No	No	0,00%	N/A	
Turkey	Yes	No	Yes	20,00%	N/A	
United Kingdom	Yes	No	No	0,00%	N/A	
United States of America	Yes	No	Yes	30,00%	N/A	Not specifically Service Fees but applies to all US source income of foreign corporations effectively linked with a US trade or business. Can be reduced if treaty in place. Refer US form W-8BEN-E

[1] Data obtained from various sources

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[4] IBFD, Country Key Feature Table Comparison, https://research-ibfd-org.ezproxy.uct.ac.za/#/compare/grid?url=kf_au,kf_at,kf_be,kf_bg,kf_ca,kf_cl,kf_co,kf_hr,kf_cy,kf_cz,kf_dk,kf_ee,kf_fi,kf_fr,kf_de,kf_gr,kf_hu,kf_is,kf_ie,kf_il,kf_it,kf_jp,kf_kr,kf lv,kf lt,kf lu,kf mt,kf mx,kf nl,kf nz,kf no,kf pl,kf pt,kf ro,kf sk,kf si,kf es,kf se,kf ch,kf tr,kf uk,kf us

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