MANAGING INBOUND AND OUTBOUND PAYROLLS - from a tax perspective

SAPA CONFERENCE

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SOME STATISTICS

18.2 million registered taxpayers as at 1 March 2015

6.6 million are expected to file returns

PIT = 353.9 bn (35.6% of revenue collected)

OPENING THOUGHTS

Evolution in the tax landscape

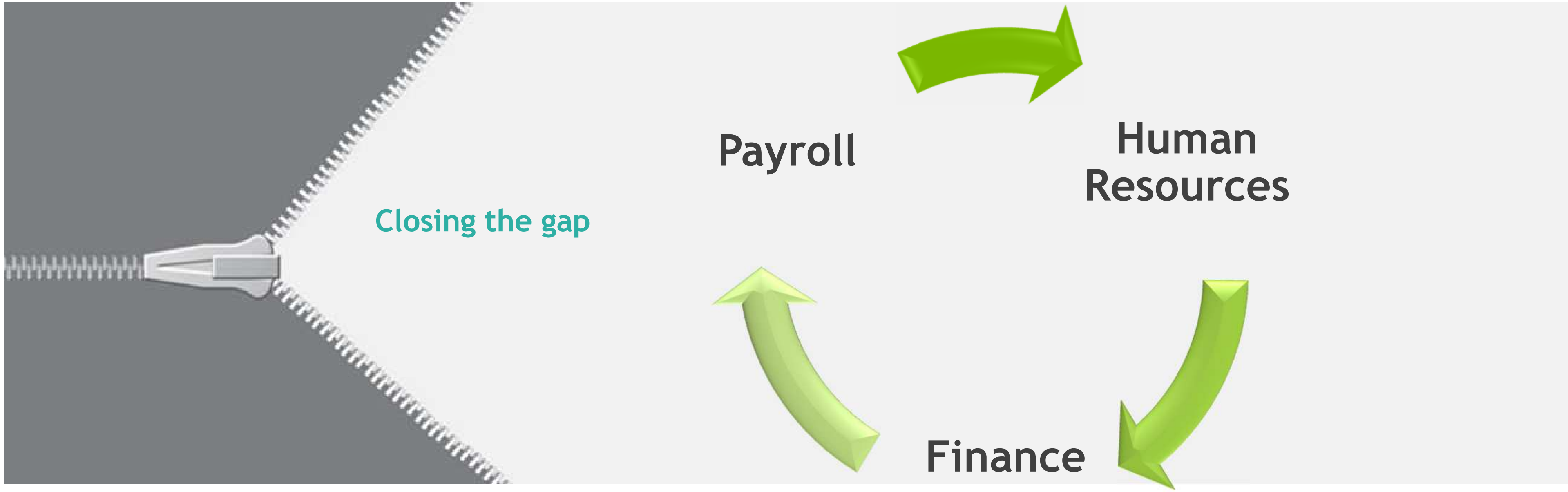
Is there a shift in focus?

Increased regulatory compliance

- **Liability on employer** to ensure accurate information is processed
- **Tax Compliance Status System** - introduced April 2016 - 'real time' status and non-compliance flagged
- **Automatic Exchange of Information** together with Common Reporting Standards (CRS) - 'nowhere to hide'
- **Opportunities are limited** to fly under the radar without being detected.
- **PIT revenue collections** have increased - Administrative non-compliance penalties for non-submission of returns;
- **Tax Administration Act** (TAA) - reduced propensity to engage in unethical behavior - tax practitioners are regulated.
- **Data analytics** - increased use to 'mine data' assists with interrogation process.

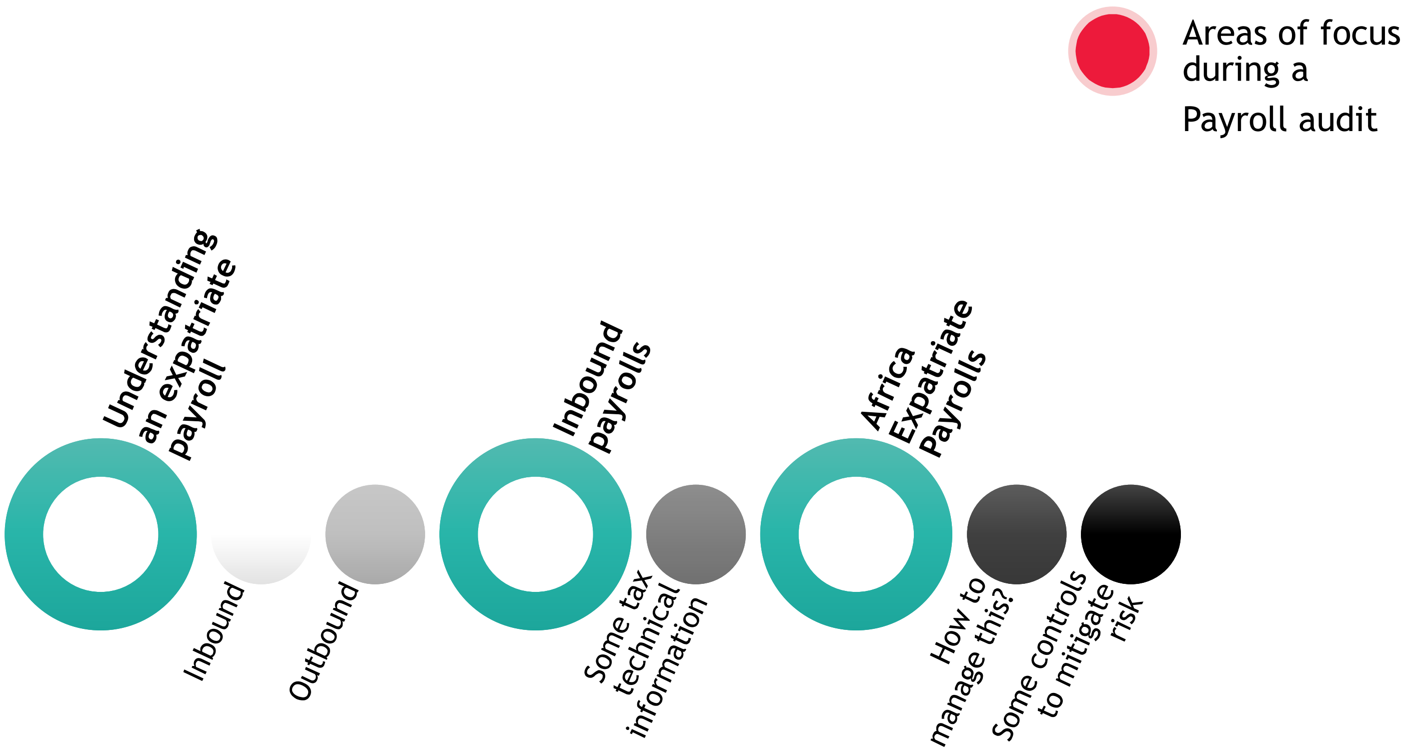
Precursor to the discussion

- Significant challenge is communication (business case demands)
- Payroll, Finance and Human Resources should be a combined effort to streamline the payroll service offering
- Results in unclear / inconsistent treatment of inbound/outbound employees
- Ripple effect – impact on encouraging mobility among assignees
- Compliance risk – home & host locations



The payroll process

What will be covered?



What is Payroll Tax?

Employees' tax perspective – 'tax collection mechanism' where a liability for normal tax exists

Fourth Schedule to the Income Tax Act – Amounts to be deducted or withheld by employers in respect of the liability for normal tax

Employer (resident) or representative employer (if the employer is not a resident)

Employee

Payment of remuneration or the liability to pay remuneration

INBOUND PAYROLL …
Some initial questions

What is an inbound payroll?

Why does the individual need to pay tax in SA when the full salary is paid and processed offshore?

The individual has not worked in SA for more than 183 days

What is regarded as taxable elements of pay and what should be reported?

Is the local entity required to report the earnings?

INBOUND PAYROLL …
A precursor to the discussion

INBOUND – refers to an individual who is sent to SA either:

- on a **short-term business trip (STBT)**; or
- on **secondment** (loaned from one entity to another).

The individual is in most cases, likely to be regarded as non-resident for taxation purposes in SA.

How to determine whether he/she is liable to tax in SA?

A resident is generally only liable to tax in the country in which he/she is regarded as a tax resident. In some cases, the individual may also be liable to tax in the country where the services are being rendered. This could potentially give rise to double taxation.

Consult the dependent personal services article of the Double Taxation Agreement between SA and the home country

INBOUND PAYROLL …

A precursor to the discussion

3 requirements contained in the Dependent Personal Services Article of most DTAs

If the STBT/assignee:

(a) Spends less than 183 days in a rolling 12 month period/in a calendar year/fiscal year in SA;

(b) Is not paid by or on behalf of an employer who is a resident of SA (this includes no recharge of salary costs to a SA entity); and

(c) the salary cost is not borne by a permanent establishment the home country employer has in SA.

If all 3 requirements are met above, then DTA relief will apply and the income derived for services rendered in SA will not be subject to normal tax.

INBOUND PAYROLL …

A precursor to the discussion

The EMPLOYER as envisaged in (b) may refer to the legal employer and economic employer - to prevent abuse in terms of the international hiring out of labour. SA is not a member of the Organisation for Economic Cooperation and Development (“OECD”) but subscribes to its guidelines.

Facts and circumstances of each case must be reviewed to determine who the ‘economic employer’ is. Some of the considerations include:

- who benefits from the services rendered?
- who bears the risk of the results produced by the assignee?
- is the individual integrated into the business activities of the local entity?

DTA relief applies = No normal tax liability / No PAYE deduction / If below tax threshold no need to submit a personal income tax return

DTA relief does not apply = Normal tax liability/ If employer paying remuneration is resident - register for PAYE

INBOUND PAYROLL

Non-resident taxpayer

Literature derived from the following sources:

- Income Tax Act No. 58 of 1962
- Case law
- Interpretation Notes (issued by SARS)
- Advanced Tax Rulings

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INBOUND PAYROLL …

Resident vs Non-resident taxpayer

Generally, an individual must be subject to tax because he or she is **resident** or **domiciled** in at least one country.

The domestic tax laws of a each country will determine whether an individual is a resident.

Definition of "gross income" in section one of the Income Tax Act includes the word "resident" which is defined as being a natural person who is:

- **Ordinarily resident** in South Africa or
- **Physically present** in South Africa for a specified period of time (Physical Presence)

- In other words 2 tests apply to determine whether a person is a resident of South Africa, i.e. the ordinarily resident test and the physical presence residence test

INBOUND PAYROLL …

Resident vs Non-resident taxpayer

The term **"Ordinarily Resident"** is not defined in the Income Tax Act and therefore case law is used to ascribe a meaning. A person who regards South Africa as the place to which he would naturally and as a matter of course return to from his 'wanderings' is regarded as ordinarily resident for tax purposes

- Although the test to determine OR is subjective, a host of objective factors are used to determine whether a person is to be regarded as OR.
- **NB:** Private Binding Ruling issued by SARS indicated the mere purchase of an investment property in SA is not sufficient to regard a person as OR to the extent he is on **secondment** to SA and will be repatriating upon termination of his/her secondment.

Dual residence

In certain instances, an individual may be regarded as a tax resident of both, the home country and the country in which he or she renders a service.

INBOUND PAYROLL …

Resident vs Non-resident taxpayer

- In these circumstances, where an individual is resident of both contracting states, the **tie-breaker rules** (contained in most Double Taxation Agreements), need to be applied in order to tie break the individual to one particular state.
- In terms of the tie breaker rules:
- an individual is deemed to be a resident of the State where he has a **permanent home** available to him. [Note a rented property is also regarded as a permanent home] Where a taxpayer lets the property, such property may no longer be regarded as 'available'.
- if the individual has property in both contracting states, he will be deemed to be a resident of the country in which his **personal and economic relations** are closer and significant (**centre of vital interests**).
- if state of vital interests cannot be determined and if he does not have a permanent home available in the home and host countries, he shall be a resident of the country in which he is considered to have a **habitual abode.**

INBOUND PAYROLL …
Resident vs Non-resident taxpayer

- where an individual has a habitual abode in both countries, he shall be considered to be a resident of the country in which he is regarded as a **national.**
- if he is not considered a national of either state, the competent authorities will consider the position.

INBOUND PAYROLL …
Resident vs Non-resident taxpayer

- **Physical presence resident**
- An individual who arrives to work in South Africa may trigger residence in his sixth year of being physically present in South Africa if he is present as follows:
  - > 91 days in the current year of assessment; and
  - > 91 days in the 5 preceding years of assessment; and
  - > 915 days in aggregate in the preceding 5 years of assessment.
- A further requirement – the individual must also not be regarded as **exclusively a tax resident** in another jurisdiction. The definition of "Resident" in the ITA excludes a person who remains **exclusively resident in another country** for purposes of the application of the DTA between South Africa and that other country.

INBOUND PAYROLL …
Resident vs Non-resident taxpayer

Current Year

Preceding 5 fiscal years

2016	2015	2014	2013	2012	2011
> 91 days	> 91 days	> 91 days	> 91 days	> 91 days	> 91 days

AND

> 915 days in aggregate

WHY IS IT IMPORTANT TO DETERMINE WHO IS A RESIDENT and NON RESIDENT

Residents

Liable to tax on worldwide income and capital gains (subject to certain exclusions)

No apportionment for workdays outside SA

Non-residents

Liable to tax on South African sourced income only

Apportionment of salary based on workdays spent outside SA … non-SA sourced income

Common terminology
Inbound payrolls

Laissez Faire

Expatriate is responsible for his/her own taxes in the home and host countries

Tax Protection

The employer will pay any tax liability which is higher than that of the home country

Tax Equalisation

Employee receives the same net salary and pays the same amount of tax as if he had continued to work in the home country.

COMMON TERMINOLOGY
Inbound payrolls

Shadow payroll

What?

Continues to be paid by the home country employer but has a tax obligation in the host country.

A shadow payroll is then used to capture information for quantifying the employees' tax withholding obligation. Not a 'live' payroll given that no payments are processed.

Why?

- Used to determine the employees' tax or personal tax liability for the expatriate in South Africa
- Makes compliance easier
- Reduces reputational risk and encourages mobility – employees not left to their own devices

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TYPICAL ELEMENTS OF PAY & SOURCE CODES

Inbound payrolls

Salary (3601/3602) or (3651/3652)	Bonus (3605) or (3655)	Cost of Living Allowance (3713) or (3763)
Hardship Allowance (3713) or (3763)	Travel allowance – for home flights (3713) or (3763)	Use of Motor Vehicle (3802)
	Payment of Employee Debt – Gross-up (3808)	

Note:

3651 = taxable income for foreign services
3652 = non-taxable income for foreign services rendered

An exemption for foreign services will only be considered where the appropriate foreign source code is used.

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IRP5 disclosure
INBOUND

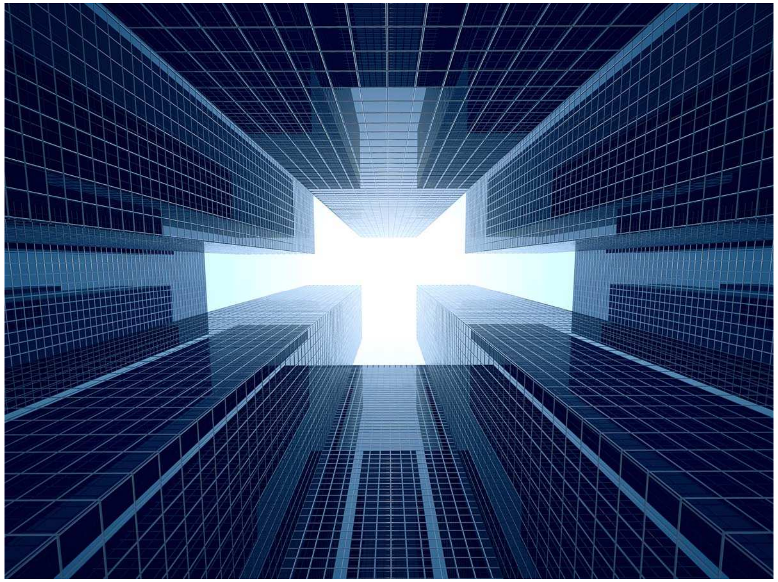
Apportionment for workdays outside SA – to be done on IRP5 certificate.

Calculation includes:

- Workdays outside SA
- Total workdays in a calendar month
- Total workdays in SA / Total workdays in a calendar month X salary

SARS issued an alert in April 2015 that apportionment of workdays /other changes to financial information, must be corrected on the IRP5 certificate as opposed to claiming the apportionment on the annual income tax return.

!!! SARS requires a revised IRP5 and not submitting the revised certificate protracts the dispute resolution process



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Outbound Payrolls
Remains tax resident but renders services abroad

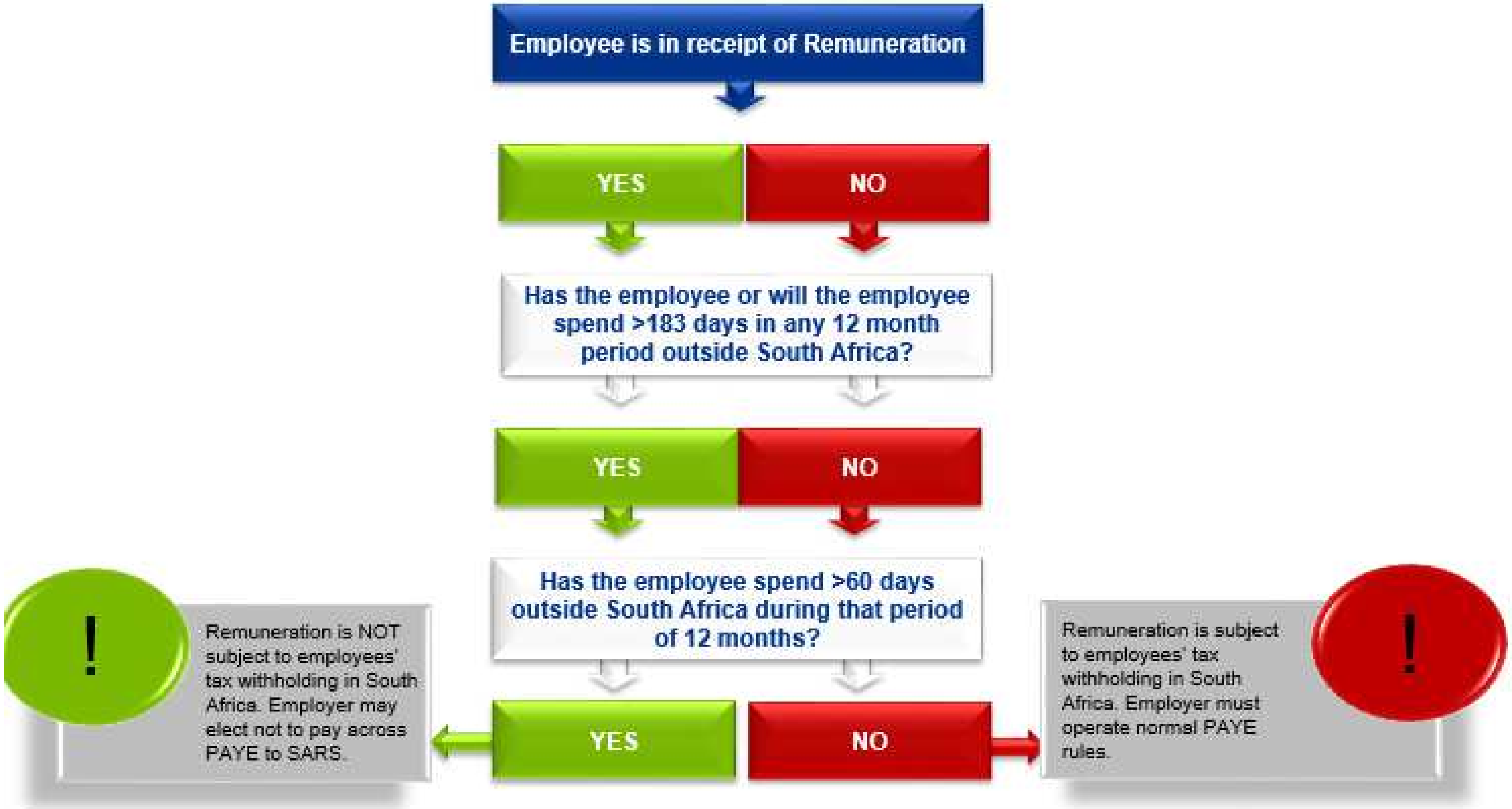
Section 10(1)(*o*)(ii)

Remuneration exempt – Domestic law prescribes to the extent **any person** renders services outside South Africa for and on behalf of an Employer for a period or periods exceeding 184 days of which 61 days are continuous during any 12 month period, the remuneration so earned is exempt from South African tax.

The Employer may then elect **not to withhold** employees' tax (PAYE) provided the days' requirements will be met.

The 12 month period relates to *any period* of 12 months and is not limited to a tax year, e.g. Mr X starts his assignment to ABC Limited on 01 May 2014, the 12 month period commences on 01 May 2014 and ends 30 April 2015.

Outbound Payrolls
How does section 10(1)*(o)(ii)* work?



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Focus areas

PAYE Audit

- **POLICY DOCUMENTATION**
- **STANDARD OPERATING PROCEDURES**

Focus area	Suggested controls to mitigate risk
Travel allowances - who qualifies to receive such an allowance and how is the quantum of such allowance calculated?	Adopt a Travel Allowance Policy with clearly defined parameters and qualifying criteria. Desk bound employees should not be allowed to structure a travel allowance.
	Use of a travel allowance calculator (based on specific calculation variables to determine quantum of the allowance)
Travel reimbursements	Payroll software should be configured and mapped to specific codes to ensure the kilometres are tracked to cover reimbursements.
Reimbursement + Travel Allowance	Travel allowance - code (3701) + Reimbursement - code (3702)
Reimbursement > 8 000 kilometres + No Travel Allowance	A reimbursement for business kilometres exceeding 8 000 kilometres per tax year or at a rate exceeding the prescribed rate per kilometre or the employee receives any other form of compensation for travel - **code (3702)**
Reimbursement < 8 00 kilometres + No Travel Allowance	A reimbursement for business kilometres not exceeding 8 000 kilometres per tax year and at a rate which does not exceed the prescribed rate per kilometre. Should only be used if the employee does not receive any other form of compensation for travel and may therefore not be used together with code 3701 and/or 3702.

Focus areas

PAYE Audit…

- **Travel allowance**
- Employees' tax audits are often triggered where the following source codes (relating to travel) are reflected on IRP5 certificates:

- Code 3701 = Travel Allowance
- Code 3702 = Reimbursive Travel (taxable)
- Code 3703 = Reimbursive Travel (non-taxable)

Code 3701 + 3702 = Correct

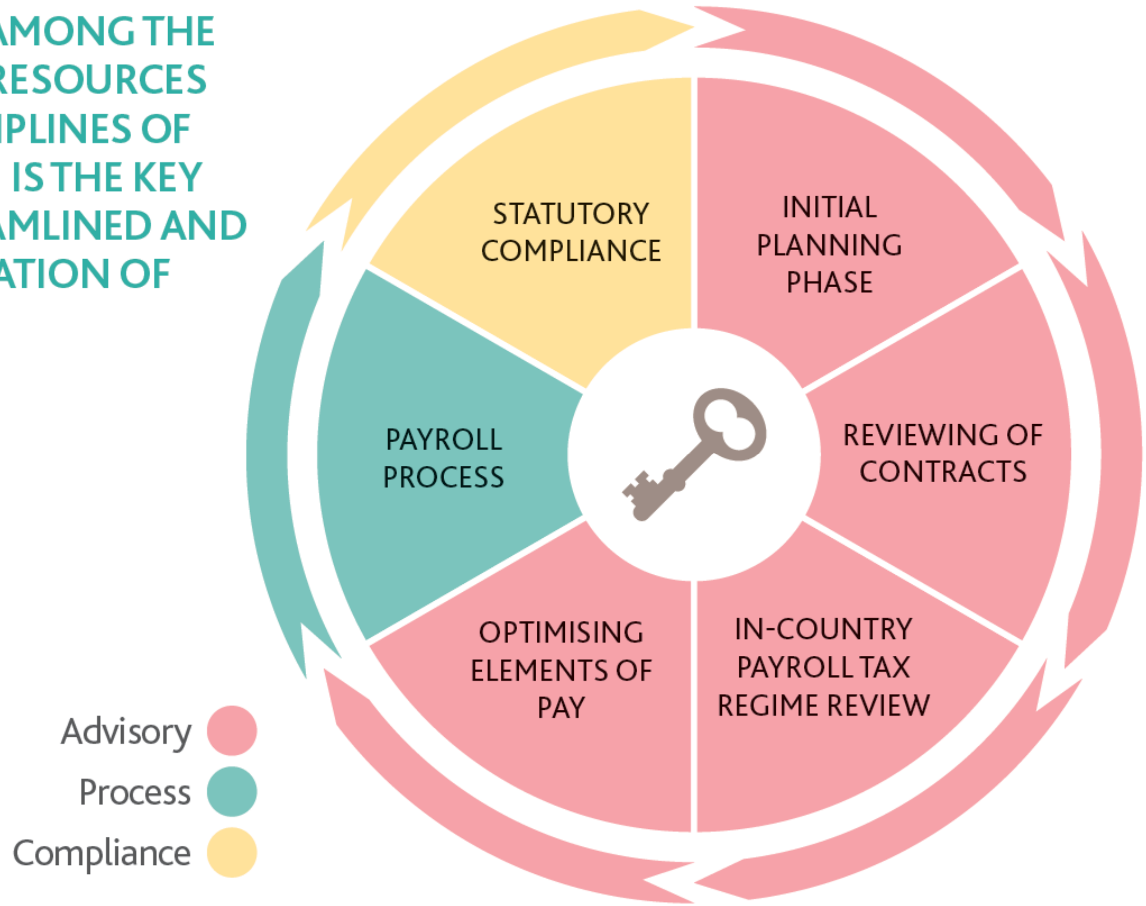
Code 3701 + 3703 = Not correct

Valuation of contributions made by employers to certain retirement funds	Employers to ensure the contribution certificates provided by the respective Fund Administrators reconcile with the payroll records. The corresponding deduction should also be reconciled

AFRICA PAYROLLS

Managing assignments into Africa

CLOSING THE GAP AMONG THE FINANCE, HUMAN RESOURCES AND PAYROLL DISCIPLINES OF AN ORGANISATION IS THE KEY TO ENSURE A STREAMLINED AND EFFECTIVE MOBILISATION OF WORKFORCES.



Managing Africa Payrolls
Some challenges

- Understanding the legislation
- What form part of mandatory contributions?
- Social Security – how is this accounted for? Are there any exemptions?
- Where DTAs are not yet ratified, are employees liable to tax from day one?

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