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CAPITAL GAINS TAX

The seller of the property will have to give consideration to the matter of payment of Capital Gains Tax. Prior to the 1st October 2001 there were certain profits which foreigners and South African citizens and residents could make without being required to pay any form of tax in the RSA. These profits were termed "capital gains" and arose from profits made on the sale of assets [including property] where the seller concerned had not acquired the property with the view to speculating on the potential resale of the property for profit. Since the 1st October 2001 however the situation changed and the laws of the RSA thereafter stipulated that tax will be payable on such previously exempted profit which tax is known as Capital Gains Tax. The tax applies to the property of all South African citizens and permanent residents wheresoever such property may exist [i.e. here or abroad] and furthermore to property owned by foreigners [i.e. non citizens / residents] which property is situate within the RSA.

The law which created the Capital Gains Tax provided for certain exclusions from the tax [i.e. allowed for capital gains which would otherwise be taxed to be tax free], the most important of which, for purposes of this commentary relates to property which constitute the taxpayers primary residence. As long as the taxpayer is a human being [not a corporate entity such as a close corporation, company or trust] the first R2 million capital gain [profit] made by that taxpayer on the sale of the property is exempt from the tax.

The gain made by a taxpayer is determined by the difference between the "base cost" of the property and the selling price. "Base cost" however includes more than just the original purchase price of the property. One is also allowed to include in base cost the original costs of taking transfer of the property, the costs of selling the property [i.e. agent's commission] and the costs incurred in <u>improving</u> the property over the years. The taxpayer is not however permitted to include any interest paid on a mortgage bond, repairs and maintenance to the property, insurance premiums and rates and taxes.

The Capital Gains Tax is triggered in most instances by the sale of the property [i.e. the date of conclusive sale and not transfer]. The property is however deemed to have been sold [even though not really sold at all] in certain circumstances which include a resident ceasing to be a resident [i.e. deciding to emigrate from South Africa] and the death of a taxpayer, unless in the latter case the property is left to the surviving spouse of the taxpayer in which case the death of the taxpayer is for Capital Gains Tax purposes ignored.

As the Capital Gains Tax is not intended to affect gains made before the 1st October 2001, all taxpayers were offered an opportunity to have all properties owned by them as of that date valued for purposes of calculating future capital gains based on that valuation as the deemed purchase price of the property. The law does provide for other ways of dealing with such properties but the generally accepted opinion is that taxpayers would have been well advised to have adopted this "valuation" method. Valuations should have been effected within a limited period from the 1st October 2001 failing which this more preferable method would not be available. The time period has since elapsed and tax payers who did not obtain a valuation will be obliged to adopt one of the other two valuation models.

As at date of this article and as a <u>rule of thumb</u> the effective tax payable in terms of the Capital Gains Tax by human beings amounts to approximately 13.3% of the gain, by companies and close corporations about 18.6% of the gain by trusts about 26.7% of the gain.

<u>Withholding of Capital Gains Tax:</u>

For South African residents the Capital Gains Tax is payable at the end of the tax year in which the gain occurred. Insofar as non-residents are concerned and as from the 1st September 2007 the South African Revenue Service changed the law to cope with the fact that non-residents were getting away with selling properties in South Africa without paying the Capital Gains Tax which might have been payable.

The effect of the amendments is the following:

Whenever the seller is a non-resident (the definition of "resident" is fairly complex) and the purchase price is more than two million rand both the estate agent and the conveyancer involved with the transaction are obliged in law to inform the buyer in writing of the fact that the seller is a non-resident.

Failure on the part of the estate agent and/or the conveyancer to inform the buyer could result in the forfeit to SARS of the commission/fee earned from the transaction.

Once the buyer is informed the buyer is obliged to withhold a certain percentage of the purchase price at the time of transfer and to pay it to SARS within 14 days from date of transfer for the account of the seller. The percentage applicable is 5% if the seller is a natural person, 7.5% if the seller is a company or close corporation and 10% if the seller is a trust.

It is envisaged that the seller will then approach SARS with a proper calculation of the actual Capital Gains Tax payable (if any) by the seller and receive a refund of the excess received by SARS. The seller can approach SARS for a special ruling on the withholding tax earlier if he wishes.

Non-resident sellers should go and register with SARS and obtain an income tax reference number as soon as they decide to sell their property. This does not mean that they will have to pay tax on their foreign income. It simply provides a reference number for purposes of enabling SARS to process the withheld amount.

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