CAPITAL GAINS TAX

PAPER PREPARED

FOR SACAFMA

by G.Wolhuter

September 2001

CAPITAL GAINS TAX

There is an old mediterranean saying

ñGet caught in the grip of an octopus and you will soon find out how many tentacles and suckers it hasò

AN OVERVIEW OF CGT

Å Announced by Minister in budget speech
23 February 2000

Å Initial implementation date - 1April 2001

Å SARS issued guide with basics

Å General public given 1 month to comment-
over 300 submissions received

Å Following submissions - changes made

Å First draft bill published for comment
on 12 December 2000

AN OVERVIEW OF CGT(cont.)

Å A further 150 submissions received

Å Introduction of CGT postponed to Oct 2001

Å Second draft bill released 2 March 2001

Å Taxation Laws Amendment Bill tabled - Subsequently passed

Å Schedule 8 covers CGT

HOW IS CGT TRIGGERED?

Å Asset disposed of- proceeds not subject to I/Tax

Å Determine difference between proceeds and base costs

Å Resulting gain aggregated with other capital gains

Å After deducting assessed capital loss

- ï Assessed capital loss carried forward
- ï Nett capital gain multiplied by inclusion rate

Å Taxable gain included in taxable income

- ï taxed at marginal rate

CGT TAX TABLE

Type of taxpayer	Inclusion rate %	Statutory rate %	Effective rate %
Individuals	25	0-42	0-10,5
Retirement funds	N/a	25	N/a
Trusts			
• Unit	N/a	30	N/a
• Special	25	0-42	0-10,5
• Other	50	32-42	16-21
Life Assurers	0-50	0-30	0-15
Companies	50	30	15

WHEN IS CGT PAYABLE?

Å Payable after assessment of tax return

Å Provisional taxpayers -

ï pay with 3rd payment

ï to avoid interest

WHAT IS EXCLUDED?

- Primary residence
  - Natural person or special trust - R1m excluded
- Gains on personal motor vehicles
- Gains on personal effects & jewellery
- Lump sum benefits
- Winnings from lotteries, casinoôs, horse racing
- Compensation for injury, illness & defamation

WHAT IS EXCLUDED?(cont.)

Å Gains on exchanging forreign currency for rands

Å Sale of assets of small business - R500000

Å Unit trusts investing in companies with
immovable property - investor subject to CGT

Å R10000 excluded per annum

WHAT IS INCLUDED?

Shares, unit trusts & private investments

Land

Property not used as primary residence

Aircraft exceeding 450 kg

Boats exceeding 10m in length

Gold & platinum coins

Mineral rights

Assets not specifically excluded

Gains above subject to CGT but losses disregarded

DEFINITIONS

- CGT taxpayer- resident taxed on worldwide assets
- Non residents - subject to CGT on disposal of
  - Immovable property(80% in S.A.)
  - Assets through which trade carried on in S.A
- Assets - defined as property(excl. currency but incl. Gold & platinum coins)

DEFINITIONS(cont.)

Å Disposals include

- ï Scrapping , loss or damage of an asset
- ï Distribution of asset to shareholder
- ï Granting, renewal, extension or exercise of options

Å Disposals exclude

- ï Transfer of asset as security for a debt
- ï Issue of shares or debentures
- ï Distribution of trust asset to beneficiary

DEFINITIONS(cont.)

Å Proceeds

ï Basic rule - actual or deemed amount derived by a person as consequence of the disposal

ï In case of donation - market value at date of donation

DEFINITIONS(cont.)

Å Base cost

ï Allowable expentiture in determining base cost

Å Cost incurred on acquisition

Å Valuation expenditure

Å Expenditure related to acquisition or disposal

Å Expenditure in defending legal title

Å Improvements

Å Valuation date value of options

Å Holding expenditure on assets used for business

Å VAT not allowed as input tax credit

DEFINITIONS(cont.)

Å Base cost

ï Cost excluded from base cost

Å Expenditure claimed for income tax

Å Expenditure recovered from another person

Å Expenditure not paid when asset is disposed of

Å Holding expenditure on primary residence

Å Inflation

DEFINITIONS(cont.)

Å Base cost

ï Pre-valuation date assets disposed at a profit base cost can be established by:

Å Market value on valuation day

Å 20% of disposal proceeds

Å Time apportionment

ï Pre-valuation date assets disposed at a loss base cost must be established as follows:

Å If market value not adopted - use time apportionment

Å If market value adopted - base cost is lower of market value or time apportionment cost

DEFINITIONS(cont.)

Å Base cost

Although the taxpayer has a choice of which method to use to determine base cost, the choice depends on the proceeds being higher than the valuation date value plus allowable expenditure on or after that date.

DEFINITIONS(cont.)

- Base cost
  - Market value on valuation date(1 Oct. 2001)
    - Shares listed on JSE - average 24 to 28 Sept
    - Shares listed outside S.A - average price last trading day
    - S.A. Unit Trusts - as for JSE share
  - Time apportionment
    - The apportionment of difference between proceeds and acquisition cost on straight line basis
  - 20% rule
    - Valuation date value is 20% of proceeds(after deducting allowable expenditure after valuation date)

DEFINITIONS(cont.)

- Base cost
  - Rollovers -

    capital gain or loss deferred, disposal disregarded and disposee take over disposer’s base cost

  - Rollover relief is granted for:
    - Involuntary disposals
    - Re-investment in similar assets
    - Disposal between spouses

VALUATIONS

Å Valuations to be done within 2 years

ï i.e not later than 30 September 2003

ï if taxpayer elected to use market value on valuation date

Å Where market value exceed R10m

ï certain other conditions apply

OTHER ISSUES

- Foreign Currency transactions
  - Capital gains and losses dealt with by way of regulations
- Disposal to and from deceased estate
  - Deceased estate liable for Estate Duty & CGT
  - R1m rebate available only for estate duty
  - Capital gain or loss ñrealisedò through death
  - CGT paid by estate - not beneficiaries
  - Annual deduction increased to R50000
  - CGT qualify as deduction in estates above R1m

OTHER ISSUES(cont.)

- Company distribution

  Only company "capital distributions"

  subject to CGT if the distribution:

  - Does not constitute a dividend
  - Constitute a dividend which is exempt from STC

- Trusts and beneficiaries

  - where trust asset is vested in beneficiary
  - who is a resident
  - capital gain disregarded in trust
  - taken into account in determining beneficiary's aggregate capital gain or loss

OTHER ISSUES(cont.)

- Insolvent Estate
  - Disposal of an asset by insolvent estate treated as if it was a disposal of the asset by the insolvent
- Compliance
  - Retention of records
    - Retain records to determine capital gain or loss for 4 years
  - Lump sum benefit on retirement
    - CGT will not affect average rate

PROBLEM AREAS

Problem areas will have to be clarified by a further act of parliament, a practice note from the Receiver or a court decision.

ï Losses carried forward

ÅIt is not clear if the aggregate capital loss will be reduced each year by R10000 if there is no capital gain to set it off against.

PROBLEM AREAS(cont.)

Å Share valuations

ï Taxpayers who are forced to adopt market value in last 5 trading days might loose if shares drop dramatically before 1 October 2001

ï Example:

ï Cost price of shares in 1998 R10 per share

ï Market value 1 October 2001 R5 per share

ï Sells on 1 October 2002 for R7 per share

ï CGT payable R2 per share - actual loss R3 per share

PROBLEM AREAS(cont.)

Å Foreign Currency

ï Will be dealt with by way of regulations

ï What happens when offshore bank account in pounds is moved into a dollar account?

Å Personal motor vehicles used for business purposes

ï Employee receives car allowance

ï Register car in own name

ï Capital gain taxed if used for business purposes

ï When used mainly for business purposes?

CONCLUSION

Å To rephrase the title of Clint Eastwoodôs film

ñEvery which way you looseò

Å One should guard against valuing immovable property too high if you intend to sell the property later. Municipal value which is traditionally lower than market value could then not be used for Estate duty purposes.

Å Refer to www.cgtsa.co.za for question & answer session by SARS