

# How the law change affects SA tax residents working abroad

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The changes made to income tax regulation from 1 March 2020, regarding the exemption provided to South African tax residents working outside the country has a big impact on employees and their South African employers.



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Prior to that date, foreign employment income earned by a South African tax resident was exempt from tax in South Africa provided:

- the employment was exercised outside the country,
- the person spent more than 183 days out of the country in a 12-month period,
- of which in excess of 60 full days needed to be continuously.

After that date, the exemption still applies, but only covering foreign related remuneration up to R1.25m per year of assessment. In other words, if a South African tax resident earns R2m employment income while working outside the country in a year of assessment, R750,000 will be subject to normal tax in South Africa (i.e. R2m less the R1.25m exemption). This can have significant implications for the employer where paid, or part paid, from South Africa.

## Employer considerations

For the employer, the first consideration is whether they have an obligation to withhold PAYE on remuneration paid to an employee working outside the country. A South African resident employer has an obligation to withhold PAYE if they pay or become liable to pay remuneration to any employee.

Careful consideration needs to be taken to determine whether the employer is liable to withhold PAYE or not. If the employer is under no obligation to withhold PAYE for an employee who is working outside of South Africa, then no action need be taken by the employer (although the employee would need to ensure that the correct tax is paid to the South African Revenue Service (Sars)). This may also be the case if the employee has broken South African tax residency; non-tax residents are only subject to tax in South Africa on South African sourced income (non-incidental employment income earned whilst working abroad is not considered South African sourced).

Whether an individual has broken South African tax residency is always fact dependent and each person's circumstances need to be considered on a case by case basis. To the extent that the South African employer is not withholding based on a non-resident employee position, then it is recommended that proof on such a position is retained in the event of a Sars PAYE audit.

## **Employer obligation**

If it has been established that the employer has an obligation to withhold PAYE and its outbound employees are South African tax resident, the employer must ensure that PAYE is withheld on all amounts earned by the employee over R1.25m. The tracking of such amounts can be complex where there is foreign denominated payments or benefits provided by the host entity. There is also a general obligation on the employer to withhold PAYE on amounts under R1.25m, but the employer may decide not to do so if they are certain that the employees will comply with the section 10(1)(o)(ii) exemption. They will, however, bear the risk of payment of the tax if the employees do not comply with section 10(1)(o)(ii).

## **Foreign tax credits**

The next issue to be considered are foreign tax credits. A foreign tax credit is a credit given in South Africa for taxes paid in a foreign country on foreign sourced income. For example, if a South African resident individual works in the UK and pays tax in the UK, they will be given a credit in South Africa for taxes paid in the UK. How this works practically is as follows: when an individual files his or her tax return in South Africa, they will declare all foreign employment income earned. This will be subject to tax on amounts over R1.25m; Sars will then reduce the South African tax liability by the foreign taxes paid (subject to certain restrictions).

If the employer has withheld PAYE on behalf of the employee and the employee receives a refund from Sars upon filing of his or her tax return (as a result of the foreign tax credit and subsequent over payment of PAYE), this refund would be due back to the employer if the employee is tax equalised. It is also possible for the South African employer to apply for an IRP3(q) directive to reduce PAYE remittances to account for estimated foreign tax credits – this however can be administratively complex.

Considering the variables that are present in these types of cases, it is prudent that your company carefully considers how they are dealing with the changes to the law to ensure that the PAYE implications are being dealt with correctly and penalty and interest exposures avoided.

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