

## GROWING THE TAX TREATY NETWORK

By MICHAEL HONIBALL

SA is having a massive rethink on its double tax treaties (DTAs). Not only due to their importance in international tax planning but also because their absence can actually be a disincentive to new foreign investment. No company or individual wants to be taxed twice on the same income. Clear evidence of this is the upsurge in new US investment since the conclusion last December of the new US/SA tax treaty.

At the time of the 1994 election, SA had double taxation agreements with just 24 countries. The US treaty had been terminated by the US in 1987 – a victim of the US Comprehensive Anti-Apartheid Act. The treaty with Canada was also terminated. Four of these agreements were with former TBVC states, which were not recognised internationally and should therefore technically be excluded from this list.

Many of these treaties were of limited scope, in that they did not cover all types of taxes and withholding taxes. For example, there was a single agreement of limited scope with the former British territories of Grenada, Mauritius, Seychelles and Sierra Leone which did not even cover withholding tax on dividends.

The process of negotiating or renegotiating new DTAs also revealed various anomalies. As far as SA was aware, there was a single agreement between both Tanzania and Uganda which was later discovered to have been unilaterally terminated. In 1995, for instance, when SA Revenue Services international department negotiators called the Ugandan authorities to indicate that SA wanted to renegotiate the treaty, the Ugandans pointed out that it had already been terminated on independence in the Sixties. The same thing with Tanzania. The Revenue only found out in 1997 that it had also terminated the treaty at the same time as Uganda.

At the time, the SA tax authorities were still honouring the Uganda/Tanzania treaty and would have granted relief to any Ugandan or Tanzanian resident. SA's international tax advisors would also have believed that the treaty was still in place and



would have structured investments accordingly. Advocate Meyerowitz, for example – in his book *Meyerowitz On Income Tax: Double Taxation Agreements* (August 1997) – still includes this treaty as a valid SA double tax treaty.

In effect, therefore, SA had only 15 internationally recognised tax treaties, many of which were not favourable towards SA – in that they allowed the relevant foreign country to levy relatively high withholding tax or they did not cover a particular type of tax.

Today SA has tax treaties with 37 countries and tax treaties with a further 22 are either awaiting ratification, signature or being negotiated. Once finalised, SA will have one of the widest treaty networks – 59 – in the world.

Most of the new tax treaties are favourable towards SA because SA levies no withholding taxes (except on royalties), which most other countries do. While the rapid expansion of South Africa's treaty network is welcome, there is concern that too many treaties are being too rapidly concluded, resulting in South Africa entering into treaties which are not always beneficial for South Africa as they could be with a bit more negotiation.

None of SA's tax treaties has antitreaty shopping provisions (anti-abuse provisions preventing the use of the treaty for back-to-back transactions between countries to take advantage of particular benefits within the treaty); the notable exception is the new US treaty. This, coupled with our source-based system, no capital gains tax and the fact that dividends are tax exempt (and the absence of a withholding tax on dividends) makes SA an attractive holding company jurisdiction – particularly for sub-Saharan Africa investments. Promoting SA as such has the potential to boost real investment, not only in SA but in the entire region.

For this reason any introduction of a capital gains tax in this year's Budget is likely to have a negative impact on the role which SA could play as a regional holding company jurisdiction. ●

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