

Protocol Amending the Agreement with the Government of the Republic of South Africa for the Avoidance of Double Taxation

Background

- 4.1 The proposed treaty action is to bring into force the Protocol Amending the Agreement between the Government of Australia and the Government of South Africa for the Avoidance of Double Taxation and the Prevention of Fiscal Evasion with Respect to Taxes on Income of 1999¹ (the Protocol).
- 4.2 The Protocol will amend the existing Agreement between Australia and South Africa for the Avoidance of Double Taxation and the Prevention of Fiscal Evasion with Respect to Taxes on Income [1999] ATS 34 (the Agreement), signed on 1 July 1999.²
- 4.3 South Africa is Australia's largest market in Africa, our 21st largest trading partner and our 16th most significant merchandise export market.³

1 Full Title: Protocol Amending the Agreement between the Government of Australia and the Government of the Republic of South Africa for the Avoidance of the Double Taxation and the Prevention of Fiscal Evasion with respect to Taxes on Income of Income of 1999, done at Pretoria on 31 March 2008.

2 NIA, para. 1.

3 DFAT Brief on South Africa: In 2007 two-way merchandise trade was valued at \$3.88 billion. Two-way investment flows between Australia and South Africa have expanded since the end of Apartheid. South Africa dominates African investment in Australia. At the end of 2006 (latest figures), investment from South Africa amounted to \$1.1 billion. Although Australian investment in South Africa's mining sector is steadily increasing. Apart from the mining sector, agriculture, infrastructure and services are other sectors attracting Australian investment.

Obligations

4.4 The key obligations under the Protocol are:

- Articles 1 to 13 of the Protocol make minor alterations to the type of property which Parties may tax and the rate imposable.⁴

4.5 In addition new provisions to the agreement as outlined in the NIA include:

- Article 9 inserts a new Article 23A into the Agreement on non-discrimination (Article 9, i), requiring each Party, in levying taxes, to treat nationals of the other Party no less favourably than it treats its own nationals in similar circumstances. The article contains several express exceptions; for example, discriminatory taxation laws are permitted to prevent tax evasion and to provide tax deductions for expenditure on research and development. The Parties may also agree on further exemptions through an Exchange of Notes.
- Article 10 amends Article 25 of the Agreement extending obligations for the exchange of information (Article 10) between the two Parties, including a specific obligation to gather and provide information upon request. Consistent with the current Article 25 in the Agreement, the Protocol imposes a correlative obligation on the Party receiving any such information to treat it in the same manner as information obtained under its domestic laws. It allows either Party to decline to provide requested information on limited grounds, including where to do so would be contrary to law or public policy.
- Article 11, inserts Article 25A into the Agreement which contains a new provision that obliges each Party to take certain action in its own territory to assist the collection of taxes owed to the other Party.⁵

Reasons for Australia to take treaty action

4.6 According to the NIA the key objectives of the Protocol are to: (i) meet Australia's most favoured nation (MFN) obligations with South Africa under the existing Agreement; (ii) promote closer economic cooperation between Australia and South Africa; and (iii) upgrade the framework

4 NIA, para. 14.

5 NIA, para. 17.

through which the tax administrations of Australia and South Africa can prevent international fiscal evasion. The protocol...

is expected to reduce barriers to bilateral trade and investment, as lowered withholding tax rates on interest and royalties is expected to reduce costs for Australian businesses. I can provide the committee members with more details of any of these if they like. We therefore recommend that members of the committee support the treaty action as proposed.⁶

4.7 The Department of the Treasury stated that the entry into force in 2003 of the Convention between the Government of Australia and the Government of the United Kingdom of Great Britain and Northern Ireland for the Avoidance of Double Taxation and the prevention of Fiscal Evasion with respect to Taxes on Income and on Capital Gains:

... triggered a total of eight clauses in other treaties, and we were aware of that when we entered into it.⁷

4.8 The Agreement requires Australia to enter into negotiations with South Africa with a view to establishing rules to protect nationals and businesses of one country from tax discrimination in the other country. Australia's MFN obligations will be met when the Protocol enters into force.⁸

4.9 The Protocol aligns withholding tax (WHT) rates on dividends, interest and royalties and capital gains tax treatment more closely with broad practice among Organisation for Economic Co-operation and Development (OECD) members and improves integrity measures within the Agreement. In particular, by extending the scope of information exchange provisions and introducing provisions for cross-border collection of tax debts.⁹

4.10 The Protocol is expected to reduce barriers to bilateral trade and investment caused by overlapping taxing jurisdictions. Reduced WHT rates on interest and royalty payments will make it cheaper for Australian businesses to obtain business loans and intellectual property from South Africa.¹⁰

4.11 The existing Agreement provides for a dividend WHT rate of zero for non-portfolio inter-corporate dividends that are paid out of profits that

6 Mr Rawstron, *Transcript of evidence*, 16 July 2008, p. 22.

7 Ms Redman, *Transcript of evidence*, 16 July 2008, p. 23.

8 NIA, para. 6.

9 NIA, para. 4.

10 NIA, para. 7.

have borne the normal rate of company tax and a rate of 15 per cent for all other dividends.¹¹ Significantly, the secondary tax on companies (STC), as a tax borne by resident South African companies, has not been subject to treaty limitations.¹²

- 4.12 The South African Government announced in its 2007/08 Budget that the STC will be phased out and replaced by a dividend tax on shareholders, which will be subject to treaty limitations. This is subject to the renegotiation of several tax treaties, including its tax treaty with Australia. To facilitate South Africa's domestic law changes the Protocol provides for dividend WHT at a rate of 5 per cent for non-portfolio inter-corporate dividends and 15 per cent for all other dividends, consistent with the OECD Model Tax Convention.¹³
- 4.13 South Africa's proposed domestic law changes, combined with limitations on dividend WHT in the new Protocol, should benefit Australian investors. According to the NIA, in the case of non-portfolio inter-corporate dividends, Australian shareholder companies should benefit from a reduction in total South African tax on the corporate profit since the South African dividend WHT is limited to 5 per cent under the Protocol. In the case of all other dividends, the overall South African tax rate would be the same, however, Australian investors would benefit from being able to claim a foreign tax credit in Australia for the dividend WHT. This will reduce their overall tax burden.¹⁴
- 4.14 The Protocol enhances the existing framework of the Agreement by updating the exchange of information rules to match the 2005 OECD standard and inserting assistance in collection provisions to help in the recovery of tax debts from those Australian taxpayers who move to South Africa.¹⁵ On being questioned about whether there were any problems with the implementation of the agreement, the Department of the Treasury stated:

No. The revised protocol has updated our exchange of information arrangements and in that regard it provides a wider range of taxes that allows us to exchange information. It also requires that bank

11 These existing rates reflect the fact that South Africa currently levies no dividend WHT. Instead, South African corporate profits are subject to tax in two parts: a primary company tax; and an additional secondary tax on companies (STC) (currently 12.5 per cent, reducing to 10 per cent from 1 October 2007). The STC is imposed on the company for net dividends distributed (that is, dividends distributed less dividends earned).

12 NIA, para. 9.

13 NIA, para. 10.

14 NIA, para. 11.

15 NIA, para.9.

secrecy is not a blocker to providing information. The new protocol also contains an assistance in collection provision that allows Australia to collect tax debts on behalf of South Africa and vice-versa.¹⁶

Entry into force and withdrawal

- 4.15 As the Protocol affects Commonwealth income tax legislation, enabling legislation must be enacted by the Commonwealth to give the proposed Protocol the force of law in Australia. There is no change to the existing roles of the Commonwealth, or the States and Territories, in tax matters as a consequence of implementing the Convention.¹⁷
- 4.16 The Protocol itself does not contain an express provision dealing with withdrawal or denunciation as it merely amends the more comprehensive Agreement. Article 28 of the Agreement provides for termination by either Party on or before 30 June in any calendar year beginning after the expiration of 5 years from the date of its entry into force.¹⁸

Costs

- 4.17 Australian revenue would be reduced to the extent that Australian WHT is decreased and additional foreign tax credits in respect of South African dividend withholding tax (when introduced) exceed the reductions in foreign tax credits for South African withholding tax on interest and royalties. However, the cost to revenue arising from the Protocol is expected to be negligible. The closer alignment with international treaty practice would generally be expected to reduce compliance costs.¹⁹

16 Mr Jacobs, *Transcript of Evidence*, 16 June 2008, p. 23.

17 NIA, para. 18.

18 NIA, para. 25

19 NIA, paras. 19-21.

Consultation

- 4.18 Comments were sought from the business community regarding the issues that might be raised during negotiations with South Africa through the Tax Treaties Advisory Panel. The panel includes: Business Council of Australia; CPA Australia; Corporate Tax Association; Institute of Chartered Accountants; International Fiscal Association; Investment and Financial Services Association; Law Council of Australia; Minerals Council of Australia; and Taxation Institute of Australia. The State and Territory Governments were consulted via the Standing Committee on Treaties.²⁰

Conclusion and recommendations

- 4.19 In the light of the information provided to the Committee, the Committee considers that the Protocol will be in Australia's national interest and supports binding treaty action being taken.

Recommendation 7

The Committee supports the Protocol Amending the Agreement between the Government of Australia and the Government of South Africa for the Avoidance of Double Taxation and the Prevention of Fiscal Evasion with Respect to Taxes on Income of 1999 (the Protocol) and recommends that binding treaty action be taken.

Kelvin Thomson MP
Chair
2 September 2008

²⁰ NIA, Consultation, Attachment A, paras 1-2.