

## Dividends a new form of Taxation

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{pp}Tax is one of the most compelling legislative tools, thus dividends being tax exempt have given equities a decided advantage for investment purposes. But, from October 2007 this all changed for Capital Gains Tax (CGT) purposes said Denis Lloyd, Executive Chairman of Walkers Attorneys.

This introduces further complexity and, of course, the additional costs of obtaining share valuations for shareholders, apart from the upfront CGT payment and the dividend tax that is about to be introduced to replace STC.

As announced in the Budget all distributions by a company will be treated as dividends for STC purposes unless it can be shown that the distribution represents a return of actual capital originally invested ( including the share premium reserve) when the shares were issued. While STC has been reduced to 10% the tax will be changed to a dividend tax payable by the taxpayer but withheld by the company effecting the distribution.

When this all happens, later this year presumably, all STC credits will lapse. A cascading tax relief will, however, result in the dividend tax only being payable when the distribution is paid out to a natural person.

For avoidance purposes, dividends paid to closely held (pty) companies - being passive investment companies used to leverage income at the lower company tax rate than that which would have applied to an individual - will also be subject to a 10% tax rate.

Exactly how the dividend paying company is to determine the status of the eventual recipient will be a &lsquo;taxing&rsquo; exercise in itself. Taxpayers might hope that they will be able to deduct interest on money borrowed to buy shares because dividends will constitute taxable income, but SARS clearly has different ideas having announced that &ldquo;dividend tax will &hellip;not form part of shareholder income&rdquo;.

Time will tell whether this comes about. In the meantime companies should ensure that all STC credits are used up. Individuals may also begin to think twice before investing in equities.

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