

EXECUTIVE BRIEF - FOREIGN EXCHANGE CONTROLS IN SOUTH AFRICA

February 2009

I am often asked for advice on how South African residents can either, get some of their savings offshore, or how they can invest in more stable currencies. There are a few routes that can be followed, depending on the amount required offshore, and on the lengths you are prepared to go to in order to protect your savings and investments.

Basic premise for investing offshore

I am not necessarily a Rand "Bear", that is, by writing this article I am not suggesting that the Rand is a one way street downwards and everyone should invest offshore. I do however subscribe to free market principles and believe that every person should be entitled to invest their money anywhere they want, and that they should make this decision, not the Government. A good investment policy is to diversify one's portfolio, and this includes diversifying one's currency base. This brief is to provide some guidance to those South Africans who may want to invest offshore.

Basics of Exchange Control regulations

Foreign exchange controls are various forms of controls imposed by a government on the purchase/sale of foreign currencies by residents or on the purchase/sale of local currency by non-residents.

Common foreign exchange controls include:

- Banning the use of foreign currency within the country
- Banning locals from possessing foreign currency
- Restricting currency exchange to government-approved exchangers
- Fixed exchange rates
- Restrictions on the amount of currency that may be imported or exported

Countries with foreign exchange controls are also known as "Article 14 countries," after the provision in the International Monetary Fund agreement allowing exchange controls for transitional economies. Such controls used to be common in most countries, particularly poorer ones, until the 1990s when free trade and globalization started a trend towards economic liberalization. Today, countries which still impose exchange controls are the exception rather than the rule.

Current countries with foreign exchange controls (list very incomplete)

Argentina ; Bahamas ; Brazil ; China ; Cuba ; Egypt ; India ; Libya ; Malaysia ; Pakistan ; South Africa ; Venezuela.

(Information above provided by Wikipedia)

In South Africa these regulations prohibit South African Residents from owning any foreign exchange, or foreign assets, with some exceptions which we look at below. An important note is the reference to "Residents", not South African Citizens or passport holders. Residents are

persons residing in South Africa, and to some extent, those no longer residing in South Africa but who have not formally emigrated. Whilst the position regarding South African living abroad, many who have not immigrated is clearly impractical, it is useful to bear this in mind when considering one's actions with regard to foreign exchange and foreign assets.

Note also that "Residence" in terms of tax law is not the same and refers to, generally, where one would call "home". There are numerous time related guides set down in the Income Tax Act, as well as substantial case law on the topic. One should seek professional advice, such as ours, on this when the issue arises.

Options available to exporting capital

The common exceptions and options allowed under the exchange control regulations are as follows:

1. Annual travel allowance

- a. In 2008 the SA Government announced an annual allowance of R500,000 for individuals for travel, gifts and all foreign transactions. This was an attempt to cut down on red tape and give individuals more access to foreign exchange they intended to spend overseas. It is important to note that this was not extended to investment overseas, the intention being that the allowance was either spent, or returned to SA for conversion back into Rands.

2. Foreign investments with South African Investment houses

- a. Many investment houses provide options to invest in foreign currencies either through asset swap mechanisms, or foreign investment allocations allowed by exchange control regulations for insurance companies and the like. Obviously these investment options carry the costs of the investment house, and there are limits which tend to get used up quite quickly. However they provide a very attractive route to hedging exchange rate risk. Why not contact our financial advisor in South Africa for more information on this option. Their contact details are:

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3. Foreign Investment Allowance

- a. Individual residents of South Africa are permitted to invest up to R2 million offshore, once they have obtained clearance that their tax affairs are up to date. The implication of the tax clearance is that the South African Revenue Services want to be in a position to know that the funds going offshore have been in the past, and will be in the future, dealt with correctly in terms of South African tax. Notwithstanding that, the tax clearance is a relatively simple process, and our offices in Johannesburg would be happy to help with this. Their contact details are:

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- b. Once the funds have been invested offshore, there is nothing to stop the funds growing beyond the R2 million level. Remember that any income accruing on the investment should be declared and taxed, if applicable, in South Africa, if you are still a resident for SA tax purposes.

4. Foreign Direct Investment

- a. Businesses in South Africa are permitted to invest offshore with permission. Up to R50 million, this permission can be obtained from a bank, above this amount the permission of the South African Reserve Bank is required. The general principle is that the investment must be to the general benefit of South Africa. It should be noted that "benefit" does not necessarily include a profit on the investment and foreign dividends. Interested parties should contact us or the foreign exchange division of your bank for more advice.

5. Emigration

- a. A resident of South Africa, who formally emigrates, is entitled to take all their assets offshore after payment of a 10% levy to the State and after obtaining permission. A resident cannot "emigrate", take their assets offshore and pay the 10% levy, and then simply return to South Africa as a way of getting assets offshore. However, this remains a solid alternative for amounts greater than R2 million and interested parties should contact us for more advice.
- b. Emigration is also a trigger for Capital Gains Tax, so residents should be aware that any unrealised gains in assets they hold may be subject to CGT. Interested parties should contact us for more advice.

Our advice

I always recommend that anyone wanting to avail themselves of access to foreign exchange work from top to bottom of the above list. The initial items have little or no costs, while the later options come with tax and levy implications as well as consulting fees. The area is a complex one and should not be tackled lightly. However there are options available and we encourage all serious investors to consider their options.

Our company has offices in Johannesburg, where they have a full range of services that can help with all of the above. Our Charlotte, North Carolina office has hands on experience in dealing for the banks on foreign exchange and is in a position to facilitate foreign payments and manage investments offshore.