Doing business in South Africa

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LEGAL SYSTEM

1. What is the legal system (civil law, common law or a mixture of both)?

The legal system in South Africa is based on:

- Common law (founded on Roman-Dutch law).
- Statute.
- The Constitution.
- Case law.
- Customary law.

FOREIGN INVESTMENT

2. Are there any restrictions on foreign investment (including authorisations required by central or local government)?

Foreign investment is actively encouraged in all sectors of the economy and there are, generally, few restrictions on investment. There are certain ownership and control restrictions, and specific authorisations can be required in regulated sectors such as:

- Broadcasting.
- Telecommunications.
- Banking.
- Insurance.
- Defence.

3. Are there any exchange control or currency regulations?

The South African Reserve Bank imposes exchange controls on South African residents. Currency must not be transferred by a South African resident into, or out of, South Africa, except in accordance with the terms of the Exchange Control Regulations 1961. However, the South African government remains committed to the gradual relaxation of exchange controls.

4. What grants or incentives are available to investors? Are any of these aimed specifically at foreign investors?

Manufacturing and export incentives exist for investment within certain areas of South Africa. These apply equally to foreign and local investors.

BUSINESS VEHICLES

5. What is the most common form of business vehicle used by foreign companies to conduct business in your jurisdiction?

In relation to this vehicle, please state:

- **Registration formalities (including timing).**
- **Minimum (and maximum) share capital.**

- **Whether shares can be issued for non-cash consideration, such as assets or services (and any formalities).**
- **Any restrictions on the rights that can attach to shares.**
- **Any restrictions on foreign shareholders.**
- **Management structure and any restrictions on foreign managers.**
- **Directors' liability.**
- **Parent company liability.**
- **Reporting requirements (including filing of accounts) and cost of compliance.**

Foreign companies conduct business in South Africa either through a branch or a subsidiary. To operate through a branch, the foreign company must submit certain information and its memorandum and articles of association (constitutional documents) to the Companies Office within 21 days of establishing a place of business in South Africa. The most common form of corporate vehicle to be established by a foreign company in South Africa is the private limited liability company.

- **Registration formalities.** A company must register its name and constitutional documents with the Registrar of Companies at the Companies Office. Registration of a new company takes between seven and 14 days from submission of the relevant documents. It is also possible to buy an off-the-shelf company.

- **Share capital.** A private company must have a share capital, but there is no minimum or maximum amount.

- **Non-cash consideration.** Private companies can issue shares for non-cash consideration (including assets and services rendered). A formal valuation process is not required.

- **Rights attaching to shares.** There are no restrictions on the rights that can attach to shares, provided that these are specified in the company's constitutional documents.

- **Foreign shareholders.** There are no restrictions on foreign shareholders unless the company is foreign-controlled and in a certain regulated industry (*see Question 2*). A private company cannot have more than 50 shareholders.

- **Management structure.** Private companies are managed by a board of directors consisting of at least one director. The articles of association usually allow directors to delegate their powers to a managing director or other executive managers.

- **Directors' liability.** A director is personally liable, under common law, for company acts if he cannot show that he has acted honestly and with the knowledge, skill and experience which can reasonably be expected of him. Statutory personal liability can arise for fraud or trading when the director knows, or ought to know, that the company cannot avoid insolvent liquidation. Criminal liability can apply for breaches of health and safety and environmental laws.

- **Parent company liability.** A parent company is not generally liable for the debts of its subsidiaries unless it has given a guarantee, indemnity or surety.

- **Reporting requirements.** A company must provide the Companies Office with up to date information on the following:

  - constitutional documents;
  - registered office;
  - directors' details;
  - secretary details (if appointed);
  - auditor details;
  - any allotment, redemption or reduction of capital;
  - accounting reference date;
  - special resolutions;
  - company name.

Any changes to this information must be submitted and updated periodically by submitting an annual return. Annual financial statements do not need to be filed by a private company.

EMPLOYEES

6. What are the main laws regulating employment relationships?

Employment in South Africa is regulated by statute, common law and contract. Legislation, such as the Basic Conditions of Employment Act 1997 (BCEA), provides minimum protection for employees, which cannot be contracted out of. These protections include the right not to be unfairly dismissed or subjected to an unfair labour practice. Legislation, such as the Labour Relations Act 1995 (LRA), also regulates collective bargaining.

A contract of employment is subject to the BCEA and the LRA. Parties can agree different terms provided these are not less favourable than the BCEA terms. Collective agreements, ministerial decrees and regulations often vary the application of the BCEA.

The Employment Equity Act 1998 prohibits unfair discrimination in any employment policy or practice on grounds such as race, gender, sex, age and religion and regulates the implementation of affirmative action (that is, positively seeking employees from specific demographic groups).

In general, South African employment law applies to all employees working in South Africa. In certain circumstances, it may also apply to South African employees working abroad.

7. Is a written contract of employment required? What, if any, other terms are likely to govern the employment relationship?

Written employment contracts are usually not mandatory, but are recommended for certainty and to avoid disputes. However, certain employment contracts must be in writing, such as those relating to merchant seamen and apprentices. In addition, the BCEA requires that certain details of employment must be set out in writing, such as:

- The name and address of the employer.
- A description of the work performed.
- Working hours.
- Employment commencement date.
- Details of remuneration.

8. Are employees entitled to management representation and/or to be consulted in relation to corporate transactions (such as redundancies and disposals)?

Employees are not legally entitled to management representation.

The extent of consultation with employees in relation to corporate transactions depends on the nature of the transaction. For example, where redundancies are contemplated, employees must be consulted. The employer must consider the views of employees, or their representatives, in good faith. However, where a business is transferred as a going concern, no consultation obligation exists, but information sharing with employees is recommended.

9. What statutory rules govern the termination of individual employment contracts?

Dismissal

Employees have the right not to be unfairly dismissed. Any dismissal must be both substantively and procedurally fair.

There are three grounds for dismissal:

- Misconduct of the employee.
- Incapacity of the employee (that is, poor work performance or ill health).
- The operational requirements of the employer.

On dismissal, an employee is entitled to:

- Accrued holiday pay.
- Payment in lieu of notice (*see below, Notice*), unless summarily dismissed in which case no notice payment is required.
- Severance pay of a minimum of one week's salary for every completed year of service with the em-

ployer, if the dismissal is a result of operational requirements.

- Any other amounts that the employee is entitled to under the employment contract.

Notice

Notice periods are normally regulated in the employment contract. However, the BCEA provides for the following minimum notice periods:

- One week, if the employee has been employed for less than six months.
- Two weeks, if the employee has been employed for more than six months but less than one year.
- Four weeks, if the employee has been employed for more than one year.

10. Are redundancies/mass layoffs regulated? If so, please give details.

Redundancies, whether individual or collective, must be both substantively and procedurally fair. Substantive fairness requires that the redundancies are required for operational reasons such as structural, technological or economic changes.

Procedural requirements include a consultation process with the potentially affected employees or their representatives. An employer must provide the potentially affected employees, or their representatives, with all the relevant information in writing.

Section 189A of the LRA regulates mass redundancies and additional consultation requirements apply in these circumstances.

11. In relation to employees, what constitutes tax residency in your jurisdiction?

South African tax residents are liable for income tax in South Africa on their worldwide income. A person is a South African tax resident once he has resided in South Africa for four years, provided that he has been present both:

- For more than 91 days in each of those years.
- More than 549 days over the first three years.

If the South African resident is also taxed in another country on income earned from employment there, relief is likely to be available under a double tax treaty or may be given unilaterally by the South African Revenue Service (SARS).

12. What income tax or social security contributions must the following pay:

- **Tax resident employees?**
- **Non-tax resident employees?**
- **Employers, in relation to their employees?**

Tax resident employees

Employees in South Africa are subject to income tax on all remuneration, including bonuses and benefits in kind. Employers must withhold tax known as pay as you earn (PAYE), from employees' salaries and pay it directly to the SARS.

The personal income tax year runs from 1 March to 28 or 29 February. Tax rates range from:

- 18%, for employees whose income in a tax year does not exceed ZAR100,000 (about US$14,063).
- 40%, for employees whose income in a tax year exceeds ZAR400,000 (about US$56,252).

Employees must also contribute 1% of their monthly gross salary (up to a maximum of ZAR109.66 (about US$15)) to the Unemployment Insurance Fund (UIF). The UIF insures employees against loss of earnings due to, among other things, termination of employment, illness and maternity leave.

Non-tax resident employees

Subject to the provisions of any relevant double tax treaty, employees of foreign companies who are seconded to South Africa are taxed on income which is derived from a South African source.

If an employee seconded to South Africa is treated as South African tax resident (*see Question 11*), he is liable for South African income tax on worldwide income, although an exemption or credit may be available under tie-breaker rules in a relevant tax treaty.

Employers

A Skills Development Levy of 1% of gross pay must be paid by employers. All employers must also register with the UIF and are required to contribute 1% of gross pay per month (up to a maximum of ZAR109.66 for each employee to the UIF).

13. Do foreign employees require work permits and/or residency permits? If so, how long does it take to obtain them and how much do they cost?

Various categories of work permits are required, depending on the type of employment and terms of the employment contract. A work permit generally takes about one month to process and costs approximately ZAR1,520 (about US$214).

TAX

14. In relation to business entities, what constitutes tax residency in your jurisdiction?

Companies incorporated or managed in South Africa are subject to South African income tax on their worldwide income and capital gains tax on their worldwide capital gains.

15. What proportion of a tax resident business entity's income is taxed and what are the main taxes that potentially apply (including rates)?

Income tax

All companies are liable to pay income tax (subject to any relevant double tax treaties). The income tax rate is 29%. Secondary tax is also payable at the rate of 12.5% on all dividends declared by a South African company.

Capital gains tax

Companies must also pay capital gains tax, the effective rate for which is 14.5%.

Value added tax (VAT)

South Africa levies VAT at the rate of 14% on the supply of all goods and services by registered vendors at each stage within the distribution chain. Some supplies are zero rated (such as exported goods, going concern businesses and basic food stuffs) or exempt (such as financial services).

Stamp duty

Tax is payable on transfers of property and certain other documents (such as lease agreements) executed in South Africa. The standard rate for the sale of shares or other marketable securities is 0.25%.

16. How are the activities of non-tax resident business entities taxed?

Non-resident companies are taxed on income derived from South African sources and on capital gains made on the disposal of assets situated in South Africa or assets of their permanent establishments in South Africa, unless a relevant double tax treaty applies.

17. Please explain how each of the following is taxed:

- **Dividends paid to foreign corporate shareholders.**
- **Dividends received from foreign companies.**
- **Interest paid to foreign corporate shareholders.**
- **Intellectual property (IP) royalties paid to foreign corporate shareholders.**

- **Dividends paid.** Foreign corporate shareholders are not taxed in South Africa on dividends they receive. The local company declaring the dividends however, must pay a tax known as secondary tax on companies (STC) at a rate of 12.5% on the total amount declared and paid as a dividend.

- **Dividends received.** South African residents are taxed on dividends received from foreign companies. However, dividends received by a South African resident, or a controlled foreign company, holding more than 20% in the foreign company's total equity share capital, are exempt from tax.

- **Interest paid.** There is no tax on interest paid to foreign corporate shareholders.

- **IP royalties paid.** Royalties payable to a non-resident shareholder from a South African source are subject to withholding tax of 12% (subject to any applicable double tax treaty).

18. Are there any thin capitalisation rules (restrictions on loans from foreign affiliates)? If so, please give details.

If a South African company is considered by the SARS to be thinly capitalised, the deductibility of interest may be challenged under South Africa's transfer pricing regime (*see Question 20*). In general, the SARS does not apply the thin capitalisation provisions where the debt-to-equity ratio of the local entity does not exceed 3:1.

19. Are there any controlled foreign company rules? If so, please give details.

South Africa's controlled foreign company rules impute the profits of foreign affiliates to South African resident companies that hold participation rights in the foreign company, subject to certain exclusions. Participation rights include the right to participate, directly or indirectly, in the share capital, share premium, current or accumulated profits or reserves of that foreign company, whether or not of a capital nature. The net income of the foreign controlled company is imputed to the South African resident company in proportion to its participation rights.

20. Are there any transfer pricing rules? If so, please give details.

Transactions between South African companies and foreign affiliates must be done at arm's length. If they are not, the SARS can adjust the agreed price and charge tax on the basis of the adjustment. These rules apply where the South African company either:

- Has overall control of the foreign company.

- Holds at least 20% of the company's share capital and no shareholder has the majority of voting rights in the foreign company.

The Organisation for Economic Co-operation and Development guidelines apply in determining whether a transaction is made at arm's length.

21. How are imports and exports taxed?

Goods imported into, or exported from, South Africa are liable for VAT and customs duty, subject to the availability of rebates and refunds.

Direct exports (where the South African seller supplies the goods) are subject to VAT at a zero rate and indirect exports (where, for example, a client of the South African seller arranges for the delivery of the goods to the client's customer in the country to which the goods are exported) are subject to VAT at 14%.

If goods are imported from one of the countries falling within the Common Customs Area (Namibia, Botswana, Lesotho and Swaziland), they are exempt from customs duty but not VAT.

22. Is there a wide network of double tax treaties? If so, please give details.

South Africa has double tax treaties with about 57 countries, including the US.

COMPETITION

23. Are restrictive agreements and practices regulated by competition law in your jurisdiction? If so, please give brief details.

Competition law in South Africa prohibits restrictive vertical practices, restrictive horizontal practices and the abuse of a dominant position. Certain types of substantial anti-competitive conduct are prohibited outright, such as price-fixing, dividing markets and collusive tendering. Other anti-competitive conduct is subject to a rule of reason analysis where, for the conduct to be prohibited, it must substantially prevent or lessen competition and not be justifiable on the basis of technology, efficiency or another pro-competitive gain that outweighs the anti-competitive conduct.

INTELLECTUAL PROPERTY

24. Please outline the main intellectual property rights that are capable of protection in your jurisdiction. In each case, please state:

- **Nature of right.**
- **How protected.**
- **How enforced.**
- **Length of protection.**

Patents

- **Nature of right.** For an invention to be patentable, it must:
  - be new;
  - involve an inventive step;
  - be capable of industrial application;
  - not be specifically excluded from protection as a patent.

  A patent holder has the right to exclude others from making, using, disposing or importing the invention so that the right holder enjoys all the benefits relating to the invention.

- **How protected.** A patent must be registered with the South African Registrar of Patents to be protected.

- **How enforced.** Patent disputes are dealt with by the Commissioner of Patents or the High Court. The following reliefs are available for infringement (*The Patents Act 1978*):
  - interdicts;
  - the delivery of the infringing product;
  - damages.

- **Length of protection.** Protection lasts for 20 years from the date of application, provided that annual renewal fees are paid. A patent cannot be renewed.

Trade marks

- **Nature of right.** Trade marks must be capable of distinguishing the goods or services of one undertaking from those of other undertakings. The right holder is entitled to prevent unauthorised use of an identical or substantially similar mark used in the same type of industry as that in which the trade mark has been registered.

- **How protected.** Trade marks can be registered with the South African Registrar of Trade Marks. Unregistered marks can be protected under the common law of passing off.

- **How enforced.** Where there has been an infringement, the High Court can (*Trade Marks Act 1993*):
  - grant interdicts;
  - order the removal of the infringing mark or the surrender of the products containing the mark;
  - award damages.

- **Length of protection.** Trade marks are registered for ten years but can, on application, be renewed for an unlimited number of additional ten-year periods.

Registered designs

- **Nature of right.** A registered design is generally used to protect the physical appearance of an article. The design may be aesthetic or functional. An aesthetic design must be new and original. A functional design must be new and not commonplace in the art concerned. Registration of a design grants to the right holder the right to exclude other people from making, importing, using or disposing of any article included in the class in which the design is registered, so that the right holder enjoys all the benefits relating to the design.

- **How protected.** Designs can be registered with the South African Registrar of Patents. Designs for articles which are not intended to be produced in large quantities by industrial process cannot be registered.

- **How enforced.** If a design right is infringed, a right holder can seek (*Designs Act 1993*):
  - an interdict;
  - the surrender of the infringing product;
  - damages;
  - a reasonable royalty.
- **Length of protection.** Registered aesthetic designs are protected for 15 years. Registered functional designs are protected for ten years. The registration of a design cannot be renewed.

Unregistered designs

Unregistered designs are not protected by legislation. However, copyright will exist over the design and protection may be found in terms of copyright law (*see below, Copyright*).

Copyright

- **Nature of right.** The following are eligible for copyright protection, provided that they are original:
  - literary works;
  - musical works;
  - artistic works;
  - cinematography films;
  - sound recordings;
  - broadcasts;
  - programme-carrying signals;
  - computer programs;
  - published editions.

  The right holder is entitled to the exclusive right to reproduce, publish, perform, broadcast or adapt the work in question, depending on the nature of the work being protected by copyright.
- **How protected.** No registration is required as copyright subsists automatically.
- **How enforced.** The owner of copyrighted material can institute an action for (*Copyright Act 1977*):
  - an interdict;
  - damages;
  - delivery of infringing copies;
  - a reasonable royalty.
- **Length of protection.** Protection for literary, musical and artistic works lasts for 50 years from the end of the year in which the creator dies. Protection for all other works lasts for 50 years from the end of the year in which it is first released.

Confidential information

- **Nature of right.** Information is confidential if it was initially communicated in circumstances importing an obligation of confidence. In general, the right holder is entitled to prevent unauthorised disclosure of the confidential information.
- **How protected.** Protection is sought through contractual tortious action for breach of confidence or unlawful competition.
- **How enforced.** An action for damages for unlawful competition must be brought within three years of the infringement becoming known to the claimant.
- **Length of protection.** No length of protection is provided by law.

MARKETING AGREEMENTS

25. Are marketing agreements regulated in your jurisdiction? If so, please give brief details in respect of the following arrangements:

- **Agency.**
- **Distribution.**
- **Franchising.**

- **Agency.** The principles of agency are regulated by common law and contract.
- **Distribution.** There is no specific legislation relating to the appointment of distributors. Distribu-

tion agreements are unlikely to breach competition law unless they contain excessive restrictions such as price fixing (*see Question 23*).

- **Franchising.** There is currently no specific legislation relating to the establishment and operation of franchises. New legislation is likely to be introduced in the near future.

E-COMMERCE

26. Are there any laws regulating e-commerce (such as electronic signatures and distance selling)? If so, please give brief details.

E-commerce is regulated by the Electronic Communications and Transactions Act 2002, which deals with:

- Electronic signatures.
- Cryptography.
- The protection of personal information.
- Domain name administration.
- The liability of service providers.
- Cyber crime.

The Electronic Communications and Transactions Act contains basic consumer protection provisions relating to the sale of goods or services over the internet.

DATA PROTECTION

27. Are there any data protection laws? If so, please give brief details.

The Electronic Communications and Transactions Act 2002 provides limited protection for personal data. Specific data protection legislation is expected in the near future.

PRODUCT LIABILITY

28. Are there any laws regulating product liability and product safety? If so, please give brief details.

There is no specific legislation dealing with product liability. The principles of product liability are regulated by common law and contract. In general, a person can only be held liable for negligence where he should reasonably have foreseen a likelihood of harm. However, strict liability exists for latent defects in products where the latent defect makes the product wholly or partially unfit for its purpose.