

## Investing in South Africa

- No. 176 -

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The South African government's policy is to encourage the country's economic development and stimulate foreign investment. The Department of Trade and Industry provides over ninety incentives, loans and rebates, including investment support, small business development, empowerment finance and export assistance. One example of government support of foreign investment includes "Business Partners Limited" (BPL) which is an unlisted public company that provides support for customised and integrated investment, mentorship and property management services for small to medium enterprises in South Africa.

When looking at South Africa as a place of investment, other points worth consideration are the strategic positioning, economic growth and infrastructure.

The country is well positioned creating easy access to another 14 countries, belonging to SACU (Southern African Customs Union), with a total population of 180 million. It also serves as transshipment point between Central & South America as well as Australia, New Zealand and Far East Asia.

The country's economic growth pattern has clearly followed the political pattern and has in recent years moved away from an inward looking economy towards an internationally competitive economy. These changes have opened South Africa's domestic economy to international competition, and there has been a significant reduction in tariff barriers as well as a market related and competitive exchange rate. There are no restrictions on the type or extent of investments available to foreigners nor is government approval required. There is a strengthening of competition and development of industrial cluster support programs available. Exchange control on non-residents has been largely abolished and there has been a substantial reduction of controls on residents. A proactive strategy to attract foreign strategic equity partners

into the process of restructuring state assets and infrastructure has been developed as well as the introduction of a greater and more flexible labour market. Finally, investment incentives to enhance international competitiveness, technology transfer and foreign direct investment are available.

South Africa has a modern and sophisticated infrastructure, which includes the following facilities: rail, road and transportation services, postal and telecommunications. It also includes one of the fastest growing cellular telephone industries in the world. Most major international airlines serve South Africa and the country has a nationwide network of both state owned and private airports.

In general, subject to some exchange control restrictions and applicable laws, investments by non-resident persons (natural & juristic) are not restricted or regulated. Investment can be made directly into newly formed or existing companies in South Africa or through the establishment of a business entity.

Almost all business activities are available to foreign investors. Only in limited cases are there restrictions. One such restriction being a limitation of 15% of foreign equity holdings in newly established banks.

### The Economy

Until about 1950, the economy was largely dependant on its mineral and agricultural products - South Africa being the leading world gold producers and ranking as the 5th largest extractor of diamonds and other precious stones. Currently, gold accounts for 25% of annual export. After World War Two, manufacturing began to play a more important role than before and in the early 90's contributed to 25% of the Gross Domestic Product (GDP). The capital needed for the manufacturing was raised on both a local (the government playing an important role) and a foreign level.

Today, cities like Johannesburg, Cape Town, Durban and Port Elizabeth are major manufacturing centres. During this time, the white population took advantage of the political & economical situation and created a high standard of living for themselves, similar to that of Western Europe, whereas the black population was unfortunately subjected to poverty, lack of education and skills. During "apartheid" in the 80's, the economy was severely hindered when sanctions were imposed. Since the 1990's, in what has been informally termed as "the New South Africa" the economy has been struggling to recover, but has made some significant progress due to the great effort put into reducing poverty and implementing reforms.

At present, South Africa is generally regarded as being an emerging or developing market in the middle-income bracket. It is also seen as the gateway to Africa. The majority of imports into Southern Africa are manufactured or transported via South Africa. It has a well-developed financial, legal, communications, energy and transport system and stock exchange, which is rated amongst the 15 largest in the world. The country has been experiencing a positive growth rate since 1993, the end of the apartheid era. Last year, the GDP grew by 3%. In the annual budget speech given this year, Mr Manuel, the minister of finance, said that the economy is "poised to grow a further 3,3% during 2003, rising to 4% in 2005". Moody's Investors Service, international rating evaluators also announced that it had changed South Africa's Baa2 country ceilings for foreign currency debt and bank deposits from the previously "stable" to "positive".

Apart from the slowing down of the international economy, the country still faces some daunting challenges regarding the high unemployment rate, poverty, HIV/AIDS, crime and the lack of empowerment amongst the disadvantaged groups.

There are again two sides to this coin: on the one side there are the hurdles mentioned above which have to be overcome, and on the other side the potential is great and already South Africa is offering investors from abroad a wide variety of opportunities to invest.

### **Trade Agreements**

"The EU is South Africa's most important economic trade partner". The government is committed to increasing the global competitiveness of

South Africa by negotiating and forming strong economic trade relations with other countries, one being the SA-EU Trade Development Co-operation Agreement signed in 2000. The General Trade Agreement allows for MFN (Most Favoured Nation) tariff treatment, removing 90% of all trade barriers over the next 10 years. This is in line with the global minimum standard for international trade relations that have been established by the WTO (World Trade Organisation) of which South Africa is an active member. Trade surplus between EU & RSA in 1999 was R6 billion and rose to R30 billion at the end of 2001.

### **Exchange Control**

#### *Non-residents*

Generally, there aren't any controls or restrictions on the inward or outward flow of funds applicable to non-residents where they are the sole beneficial owners of such transfers.

Loans to or by non-residents are however subject to the approval of the exchange control authorities. There are also various tax possibilities relating to this point.

#### *Foreign-owned businesses*

There are some local borrowing restrictions in place for business entities that are 75% or more owned or controlled by non-residents. Local borrowings include overdrafts; instalment sales, financial leasing, mortgage bonds, shareholder's loans etc. The capacity to borrow is limited to a percentage of the "total effective capital" of the company. Effective capital is the net worth of the company, including shareholder's loans, which are regarded as investment funds.

The local borrowing restrictions are generally strictly applied, however the exchange controls tend to adapt more flexible approaches to businesses that are established in decentralised areas or have substantial import substitution or export potential.

### **Commencing Business in South Africa**

Starting a business or making an investment in South Africa isn't very complicated. There are no permits required for foreigners (apart from business and work permits) or locals to begin a busi-

ness. Normally, however, a range of administrative procedures has to be complied with.

If you are thinking about starting a business in South Africa, you'll need to consider which vehicle is best suited to your circumstances. Some of the factors necessary to consider include taxation, liability, control, size, legal personality etc.

The main forms of business entities include companies (public, private, or external branch); close corporations; partnerships; trusts and sole proprietors.

### *The Public Company*

A public company must end with the words "Limited". Such a company has limited liability. It may also be listed on the Johannesburg Stock Exchange (JSE), although this is not a requirement. Listed companies are subject to rules and regulations as set out by the JSE and Securities Exchange South Africa. In terms of the Companies Act of 1973, it must have at least seven shareholders (unless it is a wholly-owned subsidiary of another company) and two directors. The directors need not have a shareholding in the company or be resident in South Africa, however a South African resident must be appointed as a public officer, one being a South African citizen, to handle the Income Tax matters arising. The board of directors is responsible for daily management of the company. The shareholders exercise their rights and powers in general meetings and they may be either natural or juristic persons or bodies and all or any of the company's shares may be held by non-residents.

### *The Private Company*

A private company must end with the words "(Proprietary) Limited". This sort of company also has limited liability. The articles of association forms part of the company's constitution and must, in terms of the Companies Act provide for: a) the restriction of transfer of shares; limitation of its shareholdership to fifty persons and prohibit offers for subscription of any shares to the public. There must be a minimum of one shareholder and one director, although one person can fulfil both of these functions.

### *External Company and Branches*

A foreign company may choose to operate through a branch in South Africa instead of through a subsidiary. An external company is one which has been incorporated outside South Africa and has established a place of business in South Africa. The definition of an external company has been extended to include a foreign company which has acquired immovable property in South Africa. Such a company must register with the Registrar of Companies in terms of the Companies Act of 1973 and is required to appoint a South African resident who is authorised to accept notices served on the company. It must also establish a registered office and appoint a registered auditor. After registration, the company will be treated under South African law as an incorporated company.

Foreign investors usually make use of either the private company or the external branch.

Foreign individuals occasionally use the close corporation, but its use is limited because the exchange control regulations are applied more strictly to these entities.

All South African companies are governed by the Companies Act of 1973, which was originally based on English company law. From the date of incorporation of a company, it has a separate legal existence and the shareholders enjoy limited liability. Both natural and juristic persons can hold shares in a company. The Act prescribes the procedures to be followed to form a private or public company. The Companies Act is administered by the Registrar of Companies, whose offices are centralised and situated in Pretoria.

### *Close Corporations*

A Close Corporation indicates its status by the letters "CC" at the end of its name. The Close Corporations Act governs all South African close corporations and has in more recent years become a popular form of business entity due to the fact that it has fewer requirements and formalities, but are however subject to stricter exchange controls.

There are no formal procedures relating to the formation of partnerships and sole proprietorships. However, in a partnership, the membership is limited to twenty persons, except for partnerships of

certain recognised professions, including accountants and attorneys.

The trustees of a trading trust must be authorised to act as trustees by the Master of the High Court.

### Social and Business Customs

There is a significant variety in social customs and one should bear this in mind when doing cross-cultural business investing. Generally speaking, in the major urban centres, all the sectors of the population conform to familiar international social and business customs, but one will occasionally encounter a different approach. On the whole, however, visitors and foreign investors shouldn't experience more difficulty in adjusting themselves to the South African customs than they would have in any European country. Business customs are Western-orientated, and haggling, bargaining and bartering are unknown in formal commerce.

### Taxation

South Africa's taxation system is a mixture of direct and indirect taxation. Direct taxes are imposed on natural and juristic persons and these include Income Tax, Capital Gains Tax, Secondary Tax (STC), Donations Tax and Estate Duty.

Indirect taxes are levied on transactions rather than persons and these include Value-Added tax (VAT), Customs and Excise tax and Stamp Duties. South Africa is party to a number of double taxation agreements with various countries. These agreements provide relief in respect of withholding taxes on royalties and know-how.

The provisions of a double taxation agreement would need to be considered in determining the tax liability of a foreign company.

### The Currency

The unit of currency is the Rand (ZAR) and consists of 100 cents. The South African Reserve Bank administers the regulations regarding ZAR.

The declining price of gold on the world markets, amongst other things, has caused the value of the Rand against the Euro to be volatile.

However the decreased value of the Rand is an advantage for foreign investors who are able to get more "value for money" and it also promotes the countries export activities. However, a steady

increase in the Rand will also create stability and a more favourable perception by foreign investors.

15. Januar 2003

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