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Aligning the tax and accounting treatment of dividend income for covered persons

Summary

- Section 24JB of the Income Tax Act currently excludes dividends and foreign dividends from fair value adjustments included in taxable income for covered persons.
- A proposed amendment narrows this exclusion: dividends received on equity investments used as hedging instruments, measured at fair value through profit or loss (“FVPL”) under IFRS 9, will now be taxable.
- The amendment is intended to align the tax treatment of these dividends with IFRS accounting and eliminate mismatches where dividend earning instruments hedge liabilities with tax-deductible payments.
- The amendment is proposed to apply for years of assessment commencing on or after 1 January 2026.

Legislative amendment

The exclusions in section 24JB(2)(b) are to be amended to bring dividends and foreign dividends back into the net of section 24JB, by excluding a dividend:

*“… **other than** a dividend or foreign dividend in respect of a hedging instrument that is measured at fair value in profit or loss in terms of IFRS 9.”*

Background

Section 24JB was enacted to align the taxation of financial instruments for covered persons with their financial reporting under IFRS. Covered persons must generally include fair value changes and other amounts recognised under IFRS in respect of these financial instruments in their taxable income or loss.

IFRS 9 provides that dividends from equity instruments designated at FVPL or formally recognised under hedge accounting are typically recognised in profit or loss. **However, section 24JB has until now excluded all dividends and foreign dividends. If excluded, these dividends would potentially be exempt from income tax in terms of sections 10(1)(k) and 10B.**

Government has identified that certain covered persons invest in shares and receive exempt dividends to hedge financial liabilities (such as equity-linked notes) where payments are deductible for tax purposes, leading to tax mismatches.

Proposal

To address the mismatch, the exclusion for dividends in section 24JB will be narrowed. Dividends (and foreign dividends) on hedging instruments measured at fair value in profit or loss under IFRS 9 will be included in taxable income for covered persons.

The tax treatment follows financial reporting outcomes under IFRS 9 and IAS 12, aligning the inclusion of dividend income as part of a covered person's income with the tax deductibility of payments on the hedged liabilities.

Effective date

The proposed amendment will come into operation on 1 January 2026 and will apply to years of assessment commencing on or after that date.

Our view

The proposed amendment will have a significant impact on stockbrokers and other covered persons who use equity instruments as hedging instruments for equity-linked liabilities. It removes the blanket exclusion for dividends under section 24JB and may increase taxable income, increasing effective tax rates across the industry.

The exemption of dividend income in sections 10(1)(k) and 10B aims to promote investment, prevent double taxation and create neutrality in financing choices. **The proposed amendment to section 24JB effectively removes dividend exemptions for everyone.** Any structured investment, apart from vanilla direct investment in shares, may result in dividends being taxable in the hands of the ultimate investor as well as the stockbroker or financier.

Has the potential negative investor sentiment been considered?

Interestingly, the proposed amendment in section 24JB would apply irrespective of whether hedged items (i.e. equity-linked liabilities and any related payments) are tax deductible.

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