TAX UPDATE

For period: 1 July 2016 to 30 September 2016

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1. INTRODUCTION

The purpose of this update is to summarise developments that occurred during the third quarter of 2016, specifically in relation to Income Tax and VAT. Johan Kotze, who is a Tax Executive at Shepstone & Wylie Attorneys, has compiled this summary.

The aim of this summary is for clients, colleagues and friends alike to be exposed to the latest developments and to consider areas that may be applicable to their circumstances. The reader is invited to contact Johan Kotze to discuss their specific concerns and, for that matter, any other tax concerns.

The reader is recommended to scroll through the explanatory memoranda and if any aspect is applicable to your circumstances to consider it together with the actual amended legislation.

The cases are always interesting to read and should help you to plan you affairs. The writer was involve in the New Adventure case, which is due to go to the SCA in the fourth quarter of 2016.

Interpretation notes, rulings and guides are all important aspects of the developments that took place, as they give taxpayers an insight into SARS' application of specific provisions. It is however important to note that these publications are not law, but may bind SARS. Taxpayers should nonetheless consider these publications carefully to determine whether, and how, they are actually applicable to their own circumstances.

Enjoy reading on!

I am glad I learned in school about parallelograms instead of how to do tax. It's really come in handy this parallelogram season. (sic.)

2. MEDIA STATEMENT: 2016 BUDGET TAX BILLS

National Treasury and SARS published the last two bills to give effect to the tax proposals announced by the Minister in the 2016 Budget. One of the bills also contains amendments not announced in the Budget, which deal with improving the effectiveness of the Office of the Tax Ombud.

The two bills published are:

- the 2016 Draft Taxation Laws Amendment Bill (TLAB) and
- the 2016 Draft Taxation Laws Amendment Bill (TALAB).

These bills give effect to most of the tax proposals announced in the 2016 Budget Speech and the 2016 Budget Review. Other legislative amendments to give effect to the 2016 Budget tax proposals have already been published, namely the 2016 Draft Rates and Monetary Amounts and Amendment of Revenue Laws Bill, Rates and Monetary Amounts and Amendment of Revenue Laws (Administration) Bill the now enacted Revenue Laws Amendment Act No 2 of 2016.

The 2016 Draft TLAB deals with the more substantive changes to the tax laws, excluding the rates and monetary thresholds and Special VDP, which are dealt with in the earlier tax bill already published for comment. The 2016 Draft TALAB deals with changes to the administrative provisions of tax legislation. The draft tax amendments are split into two bills due to Constitutional requirements, namely a money bill (section 77 of the Constitution) dealing with charging provisions and an ordinary bill (section 75 of the Constitution) dealing with issues relating to tax administration.

The 2016 draft TLAB gives effect to the following key proposals announced in the 2016 Budget Review:

- Introducing measures to prevent tax avoidance through the use of trusts
- Refinement of the taxation of retirement savings
- Addressing the circumvention of rules dealing with employee share incentive schemes
- Refinement of the anti-avoidance rules dealing with cross border hybrid

debt instruments rules

- Extending the renewable energy incentive to include supporting infrastructure used in producing renewable energy
- Repeal of the withholding tax on services regime
- Revision of a previous VAT amendment relating to notional input tax on goods containing gold

The 2016 Draft TALAB gives effect to the following key proposals:

- Enhancing the independence and effectiveness of the office of Tax Ombud
- Extension of objection and condonation periods
- Commercial member to assist presiding officer in tax court
- Clarification of pending audit or investigation for purposes of the voluntary disclosure relief
- Confirmation that an audit unrelated to the default being disclosed will not disqualify an applicant for full voluntary disclosure relief
- Imposition of understatement penalty in General anti-avoidance rule (GAAR) matters

The current bills do not deal with the youth employment tax incentive (ETI) and the learnership tax incentive, which are currently being reviewed through a separate but parallel process. The two incentives will cease to continue if no further amendments are enacted this year – further amendments will be incorporated in the revised draft to be published in September 2016 should the reviews warrant the continuation or amendment of these incentives in one form or another.

3. EXPLANATORY MEMORANDUM ON TAXATION

LAWS AMENDMENT BILL, 2016 – SELECTED TOPICS

3.1. Retirement fund contribution deduction against passive income

[Applicable provision: Section 11(k) of the Income Tax Act No.58 of 1962 ('the Act')]

Background

From 1 March 2016 the tax treatment of contributions to retirement funds was amended to be harmonized across all retirement funds. Previously, deductions to retirement annuity funds were only allowed to be set off against 'non-retirement funding income' (which included passive income such as interest or royalties, but excluded taxable capital gains), while deductions to pension funds could only be set off against 'retirement funding income' (which represented income from employment and did not include passive income).

Reasons for change

The harmonisation of the tax treatment of contributions in section 11(k) allowed for a deduction against income from 'carrying on a trade', which unintendedly excluded passive income. This resulted in members of retirement annuity funds who were using the deduction against passive income to no longer able to deduct their contributions against the passive income.

Proposal

In order to correct this anomaly and to allow retirement annuity members to continue to receive a deduction and fully align the treatment between all retirement fund members, it is proposed that deductions for contributions to all retirement funds should be allowed to be set off against passive income. For the purpose of the section 11(k) deductions, the passive income does not include taxable capital gains.

<u>Example 1</u>

Facts:

Mr Thrift receives remuneration of R75 000 for part-time work over the course of the 2016/17 year of assessment. He also receives R10 000 in interest from a money market account and sells unit trusts to receive a capital gain of R750 000. The value of the taxable capital gain is R300 000. Before the end of the year he contributes R100 000 to his retirement annuity fund.

The maximum allowable deduction for the contribution to the retirement annuity fund is limited to either 27.5% of the greater of taxable income or remuneration, or R350 000. Mr Thrift's taxable income of R385 000 in this case is higher than his remuneration and his maximum allowable deduction is thus R105 875.

Result:

The R100 000 retirement annuity fund contribution is below the maximum allowable deduction and may be deducted against income from 'carrying on a trade' and passive income (but excluding taxable capital gains). Mr Thrift can deduct R85 000 (remuneration and interest income). The R15 000 in contributions that was not deductible can be carried over to be deducted in a subsequent year of assessment or will be tax free on receipt of the retirement benefit when Mr Thrift retires.

<u>Effective date</u>

The proposed amendments are deemed to have come into effect from 1 March 2016.

3.2. Rollover of excess retirement fund contributions before 1 March 2016

[Applicable provision: Section 11(k) of the Act]

Background

Before 1 March 2016 retirement annuity contributions that were above the allowable deductible amounts were allowed to be rolled over to the following year to potentially be deducted in that year. Pension fund contributions that were above the limit were not allowed to be rolled over to the following year, but upon retirement these amounts could be taken tax free.

Reasons for change

The 2016 changes to the legislation relating to the harmonisation of the tax treatment of contributions to retirement funds applies to contributions made after 1 March 2016, and any contributions above the limit to any retirement fund can be rolled over to the following year.

However, these legislative changes do not cater for any excess contributions made before 1 March 2016 and previous contributions above the limit to retirement annuity funds can no longer be rolled over. Contributions above the limits to both retirement annuity funds and pension funds made before 1 March 2016 would then not be afforded the rollover treatment and could only be received tax free at retirement.

Proposal

To continue with the current rollover treatment for retirement annuity funds and align the treatment for excess contributions to pension funds it is proposed that excess contributions to both of these funds before 1 March 2016 should be allowed to be rolled over and deducted in the following tax year. Excess provident fund contributions would not be allowed to be rolled over since there was no requirement for provident funds to purchase an annuity before 1 March 2016.

Effective date

The proposed amendments are deemed to have come into effect from 1 March 2016.

3.3. *Clarifying source rules of retirement annuity funds*

[Applicable provisions: Sections 9(2)(i) and 9(3) of the Act]

Background

Sections 9(2)(i) and 9(3) of the Act deems the portion of the lump sum and annuity payments from a pension fund and provident fund to be from a source outside South Africa, if the amounts received are in respect of services rendered outside South Africa.

Reasons for change

There is a view within the industry that the exclusion from South Africa source rule referred to in sections 9(2)(i) and 9(3) of the Act also includes payments made from retirement annuities. However, contributions to retirement annuities are not linked to employment and should not be associated with any type of services rendered, whether they are within South Africa or outside of South Africa.

Proposal

It is proposed that changes should be made in section 9(2)(i) of the Act to remove the ambiguity and clarify that the exclusion from South Africa source rule in section 9(2)(i) does not apply to lump sum, or annuities received from retirement annuity funds.

It is also proposed that section 9(3) of the Act be repealed as it creates ambiguity.

Effective date

The proposed amendments will come into effect on the date of promulgation of the Taxation Laws Amendment Act, 2016.

3.4. *Using the correct definition of income for the formula to determine the fringe benefit for defined benefit contributions*

and eliminating a potential loophole

[Applicable provision: Paragraph 12D of the Seventh Schedule of the Act]

Background

The new paragraph 12D of the Seventh Schedule (dealing with the valuation of contributions made by employers to certain retirement funds) inserted a formula to calculate the taxable fringe benefit for contributions to a retirement fund that has a defined benefit component. The provisions of paragraph 12D of the Seventh Schedule stated the formula would cover contributions by the employer to the retirement fund.

Reasons for change

The formula in paragraph 12D of the Seventh Schedule to the Act assumes that the value 'A' represents the income that the retirement fund uses to calculate the required level of contributions given the expected liabilities of the fund. However, the wording of the provision currently refers to 'remuneration' which is a different income figure. Remuneration may also differ for two individuals depending on the level of travel allowance, leading to a situation where two identical members of the same defined benefit fund would have a different fringe benefit value for the employer contribution.

This wording also refers only to employer contributions and is silent on contributions made on behalf of the employer by the fund. These types of contributions may be interpreted to be exempt from the formula, creating a potential loophole.

Proposal

It is proposed that changes be made in paragraph 12D of the Seventh Schedule to adjust the definition of income to determine the value 'A' in the formula and to include contributions made by the fund on behalf of the employer.

Effective date

The proposed amendment in respect of the adjustment of the definition of income to determine the value 'A' in the formula will apply in respect of contributions made after 1 March 2017.

The proposed amendments in respect of inclusion of contributions made by the fund on behalf of the employer will be deemed to apply in respect of contributions made after 1 March 2016.

3.5. Increase on thresholds for exemption of employer provided bursaries

Background

Currently, the Act makes provision for tax exemption for all 'bona fide' bursaries or scholarships granted by employers to employees or relatives of qualifying employees, subject to certain monetary limits and other requirements.

If a bursary or scholarship is awarded to a relative of the employee, the exemption will apply only if the employee's remuneration does not exceed R250 000 during the year of assessment. In addition, the amount of the bursary or scholarship will only be exempted up to a limit of R10 000 for studies from Grade R to 12 including qualifications in NQF levels 1 to 4 and R30 000 for qualifications in NQF levels 5 to 10.

Reasons for change

The monetary limits associated with bursaries and scholarships granted to relatives were last revised in 2013. In order to support skills development and to encourage the private sector (employers) in the provision of education and training, Government intends to increase the monetary limits for bursaries and scholarships granted to the relatives of qualifying employees.

Proposal

It is proposed that the monetary limits be increased for bursaries and scholarships granted by employers to employees or relatives of qualifying employees:

- The monetary limit in respect of remuneration for qualifying employees will be increased from R250 000 to R400 000.
- The monetary limits in respect of exempt bursary or scholarship will be increased from R10 000 to R15 000 and from R30 000 to R40 000 respectively.

Effective date

The proposed amendments are deemed to have come into effect from 1 March 2016 and will be applicable in respect of years of assessment commencing on or after that date.

3.6. *Introducing measures to prevent estate duty and donations tax avoidance through transfer of assets to a trust using interest fee loans*

[Applicable provisions: New sections 7C and 56 of the Act]

Background

When transferring assets to a trust, a person currently has the following options. Each of these options gives rise to different tax outcomes.

- In the first instance, a person may donate the assets and trigger donations tax at 20% of the fair market value of the assets in the hands of the person.
- Secondly, a person may sell the assets to the trust on loan account at an arm's length interest charge. If interest on the loan is market related, the seller will be fully taxed on the interest portion of the loan repayments.
- Lastly a person may sell the assets to the trust on loan account at an interest charge that is below arm's length or charge no interest on the loan.

Reasons for change

At issue is the avoidance of estate duty and donations tax when a person sells assets to a trust and the sale of those assets is financed by way of an interest free loan or a loan with interest below market rates. Donations tax will not be triggered on the asset when the asset is sold at market value to a trust in this manner because there is no gratuitous disposal as required for donations tax purposes.

Coupled with the above, in some instances the seller reduces the loan capital which is supposed to be paid back to him/her by donating amounts to the trust to be set off against the loan to the trust using the current provisions of section 56(2)*(b)* which provides for the R100 000 annual exemption from donations tax. This further avoids estate duty through the tax-free reduction of the asset base of the seller achieved by such annual donation to the trust.

Due to the fact that the loan is an interest free loan or a loan with interest below market rates, no interest is paid to the seller or interest paid is less than market rates, the seller will not be liable for income tax on the interest that is forgone or will not be liable for income tax on the interest that is below market rates. This results in a further reduction of the tax base.

<u>Proposal</u>

In order to limit taxpayers' ability to transfer wealth without being subject to tax, it is proposed that rules focusing on interest free loans or loans with interest below market rates that are made directly or indirectly by a natural person, or by a company that is a connected person in relation to that person to a trust, be introduced.

According to these rules, it is proposed that an amount equal to the difference between interest that would arise as determined with reference the official rate of interest (as determined in terms of the Seventh Schedule to the Act) and the applicable actual rate of the loan below market rates made to a trust and will be regarded as an amount of income accrued or received by the seller. Such amount imputed as income in the hands of the seller will not qualify for the section 10(1)(*i*) exemption in respect of interest.

Further, with regard to interest free loans, as there is no actual payment of interest by the trust to the seller, no deduction may be claimed by the trust. On the other hand, with regard to loans with interest rates below market value, only the amount of interest below market rates that is actually paid by the trust to the seller can be claimed as a deduction if the requirements of the general deduction formula are met.

In addition, any reduction of the interest free loans or to loans with interest below market rates to which these rules apply will not qualify for the section 56(2)*(b)* R100,000 annual exemption of donations tax.

Furthermore, the amount of normal tax attributable to the income which is included in the income received or accrued to the seller may be recoverable by the seller from the trust as the trust benefits from the low or no interest charge. If the seller does not recover this amount of tax from the trust within a period of three years after the end of the year of assessment in which the income was included in the income of the seller, the tax attributable to that income will be treated as a donation by the seller to the trust on the date on which the three year period ends, and thus attracting donations tax.

<u>Effective date</u>

The proposed amendments will come into effect on 1 March 2017 and applies in respect of years of assessment ending after that date.

3.7. Addressing the circumvention of rules dealing with employee based share incentive schemes

[Applicable provisions: Section 8C, new section 8CA and section 10(1)(k) of the Act]

<u>Background</u>

Amounts in cash or in kind that are received or accrue in respect or by virtue of services or employment are treated, as a point of departure, as ordinary revenue. Section 8C (dealing with taxation of directors and employees on vesting of equity instruments) forms part of a set of anti-avoidance measures aimed at preventing the characterisation of an amount that relates to services or employment as a capital gain or as an exempt amount subject only to dividends tax. For example, dividends that are received or that accrue in respect of services or by virtue of employment or the holding of an office are treated as ordinary revenue.

Section 8C governs schemes that are based on equity shares. A restricted equity instrument represents an interest in the equity shares underlying the scheme that is held either directly or through a derivative mechanism. The retention or acquisition, by a scheme beneficiary, of the benefits flowing from the scheme, e.g. dividends, is subject to suspensive or resolutive terms or conditions. These benefits are dependent, in essence, on continued employment or the rendering of services for a specified period. The distributions derived from a restricted equity instrument and the growth in value of the underlying shares until the date the restrictions fall away constitute, in effect, benefits that arise in respect of services and form part of the reward for services rendered. Dividends in respect of a restricted equity instrument will be exempt only if that instrument complies with specific requirements.

Taxation under section 8C is as a general rule triggered when the restrictions in respect of the interest in the underlying equity shares fall away, i.e. when the employee can, in broad terms, freely dispose of or deal with those shares on the same basis as any shareholder who is not an employee, or is entitled to an amount equal to their value. The amount subject to section 8C is determined with reference to the value of those shares at that time, thus treating the growth in value of that payment in kind as revenue.

Reasons for change

Section 8C is based on the implicit assumption that the full value of the equity shares underlying a restricted equity instrument will vest in the employee when the restrictions fall away. The value derived from the underlying shares may, however, be liquidated in full or in part by means of distributions that are effected before these restrictions fall away, e.g. distributions resulting from the disposal or redemption of the underlying shares or resulting from a return of capital in respect of the underlying shares. Distributions qualifying as a return of capital or a foreign return of capital in respect of the underlying equity shares are treated as revenue. The current inclusion does not extend, however, to a return of capital by way of a distribution of an equity instrument. Distributions in the form of dividends may also impact negatively on the value of the underlying shares.

The policy intent underlying the inclusion, in the income of a holder of a restricted equity instrument, of a return or foreign return of capital was expressed as follows in the Explanatory Memorandum on the Taxation Laws Amendment Bill, 2010: 'Capital distribution will generally trigger ordinary revenue in recognition of this partial cash-out. However, if the capital distribution consists of another restricted equity instrument, the capital distribution will be treated as a non-event.' The current exclusion of a return or foreign return of capital does not reflect this policy clearly. A return of capital in the form equity shares that are not restricted will erode the value of the equity shares from which the value of a restricted equity instrument is derived.

The exclusion should apply only in respect of an equity instrument that qualifies as a restricted equity instrument subject to section 8C, i.e. if the gain or loss in respect of that instrument will be treated as being of a revenue nature. Other receipts or accruals in respect of a restricted equity instrument that are not treated as dividends and that are not taken into account in determining the gain or loss in respect of the restricted equity instrument may also erode the value of the underlying shares and result in a leakage of the gains that should be treated as income in terms of section 8C. The current requirements regarding dividends in respect of restricted equity instruments that are exempt from normal tax do not deal adequately with dividends consisting of or derived from:

- the proceeds from the disposal or redemption of:
  - the underlying equity shares; or
  - shares from which those equity shares derive their value; or
- the liquidation of a company from which those equity shares derive their value.

The treatment, as an exempt dividend, of an amount that reduces or liquidates the gain subject to section 8C converts, in effect, an amount that should be taxed at marginal rates to an amount that is taxed at a lower rate. This conflicts with the policy objective underlying section 8C (i.e. that there should be parity of treatment of amounts in cash and in kind).

<u>Proposal</u>

The dispensation regarding restricted equity instruments should be aligned more clearly with the policy intent regarding amounts that should be subject to revenue treatment in terms of section 8C. Based on the above, the following is proposed:

- It is proposed that the current inclusion, in the income of a holder of a restricted equity instrument, in respect of a return or foreign return of capital be extended to any amount received or accrued if that amount is not:
  - a return of capital or foreign return of capital by way of a distribution of a restricted equity instrument; or
  - subject to the provisions of the Act with respect to a dividend in respect of that restricted equity instrument; or
  - taken into account in terms of section 8C in determining the gain or loss in respect of that restricted equity instrument.

Example 1

Facts:

Mr Eager, an executive director of Last Hope Ltd, holds a restricted equity instrument in the Last Hope Employee Share Trust that will remain restricted for a period of 5 years after that instrument was awarded to Mr Eager. It entitles him to dividends derived from 10 000 of the equity shares in Real Hope (Pty) Ltd that are held by the trust while the restrictions governing that equity instrument apply and the transfer of those shares once those restrictions fall away. Real Hope (Pty) Ltd is a subsidiary of Last Hope Ltd.

Real Hope buys back 90% of the shares held in it by the trust at R200 per share 4 years after the award of that restricted equity instrument. The trust distributes an amount of R1 800 000 to Mr Eager as a dividend in respect of his restricted equity instrument.

Result:

The dividend of R1 800 000 will not be exempt as it consists of the consideration paid by Real Hope in respect of the share buy-back. This result will apply irrespective of whether the consideration in respect of the share buy-back consists of cash or an asset in kind.

- It is proposed that a dividend in respect of a restricted equity instrument scheme be treated as ordinary revenue. As a result, carve out measures which qualified certain dividends in relation to restricted equity instruments as exempt from normal taxation will fall away. This implies that paragraph *(dd)* of the proviso to section 10(1)*(k)*(i) will be deleted. Further changes will be made to paragraph *(ii)* of the proviso to section 10(1)*(k)*(i) to clarify that dividends will only be exempt after the restriction falls away and the equity instrument vests in the employee in terms of section 8C or when a marketable security is held by an employee in terms of section 8A.

Example 2

Facts:

Ms Sharp, an executive director of Tower Projects, holds a restricted equity instrument in the Tower Group Employee Share Trust that will remain restricted for a period of 5 years after that instrument was awarded to her. It entitles her to dividends derived from 10 000 of the equity shares in Mini Tower that are held by the trust while the restrictions governing that equity instrument apply and the transfer of those shares once those restrictions fall away. Mini Tower holds 100% of the class B equity shares in Tower Software while Tower Projects holds all the class A equity shares in Tower Software.

Tower Software redeems 80% of the class B equity shares at R200 per share 4 years after the award of that restricted equity instrument. Mini Tower distributes this amount as a dividend to the trust. The trust distributes an amount of R1 600 000 to Ms Sharp as a dividend in respect of her restricted equity instrument scheme.

Result:

The dividend of R1 600 000 will not be exempt as it is derived from the consideration in respect of the redemption of the class B equity shares.

- Due to the fact that employee share schemes are aimed at encouraging employees to remain in employment and providing an incentive to employees to align their interests with that of the company, any value flowing to an employee (whether through dividends or shares that vest) can be seen as remuneration in the hands of the employee. This reflects that regardless of whether an employee receives payment for employment in cash or another form, the resulting tax treatment is the same. Based on the above, it is proposed that more certainty be provided on how the employer should treat the contributions in respect of restricted equity instruments. The following is proposed:
    - The historic cost actually incurred and paid by the employer to provide its employees with restricted equity instruments scheme will be regarded as being in the production of income and will qualify for a deduction in terms of the new section 8CA.
    - This deduction will be spread over the period during which

the restriction in respect of the equity instrument applies. The new section 8CA will cater for this.

- In instances where an employee leaves the employee share scheme, the current recoupment provisions in section 8(4)(a) will apply.

Effective date

The proposed amendments will come into effect on 1 March 2017 and applies in respect of any amount received or accrued on or after that date.

3.8. Disallowing the exemption for a lump sum, pension or annuity from a retirement fund that is located within South Africa

[Applicable provision: Section 10(1)(gC)(ii) of the Act]

Background

When the residence based system was introduced in 2001, section 10(1)(gC) was included in the Act to exempt the receipt of foreign pensions arising from employment outside of South Africa. The provisions of section 10(1)(gC) allows a South African tax resident who is employed outside of South Africa to receive those retirement benefits (that they earned while outside the country) free from tax.

Reasons for change

There is uncertainty regarding the interpretation of the current provisions of section 10(1)(gC). The consequence is that South African tax residents who work outside of South Africa can receive a tax deduction on contributions made to the South Africa retirement fund (local retirement fund). The deduction can either be made in the same tax year if they have other forms of taxable income or worked partially within that year or the amounts can be rolled over to be deducted in a future year of assessment. However, upon receipt of the retirement benefits the amount that accrued while the South

African tax resident was employed outside South Africa will be free from tax.

Proposal

To ensure a fair tax treatment of retirement benefits received by South African residents, it is proposed that the exemption provided in section 10(1)(gC)(ii) only applies to retirement benefits from foreign retirement funds, i.e. retirement funds other than a pension fund, pension preservation fund, provident fund, provident preservation fund or retirement annuity fund as defined in section 1 of the Act (where members are eligible for deductible contributions).

Effective date

The proposed amendments will come into effect on 1 March 2017 and applies in respect of years of assessment commencing on or after that date.

3.9. Inclusion of emigration for exchange control purposes in respect of withdrawals from retirement funds

[Applicable provision: Definition of 'retirement annuity fund' in section 1 of the Act]

Background

In 2015, changes were made in the Act to allow individuals to withdraw a lump sum from the retirement annuity fund when they cease to be tax resident or when they leave South Africa at the end of their work visa.

Reasons for change

The 2015 Draft Taxation Laws Amendment Bill (2015 Draft TLAB), which was released for public comments on 22 July 2016 made provision for the following criteria to be met in order for individuals to be able to withdraw a lump sum from their retirement annuity fund:

- when the individual emigrated from South Africa and that emigration is recognised by the South African Reserve Bank for purposes of exchange control, or
- when the individual ceases to be a tax resident; or
- when the individual leaves South Africa at the expiry of the work visa contemplated in the Immigration Act, 2002 and
- is not regarded as a resident by the South African Reserve Bank for purposes of exchange control

Based on the public comments received on the 2015 Draft TLAB, changes were made in the 2015 TLAB to limit the criteria to be met in order for the individuals to be able to withdraw a lump sum from their retirement annuity fund to only the following:

- when the individual ceases to be tax resident; or
- when the individual leaves South Africa at the expiry of the work visa contemplated in the Immigration Act, 2002.

It has come to Government attention that exclusion of the requirement that an individual must emigrate from South Africa and that emigration must be recognised by the South African Reserve Bank for purposes of exchange control creates a loophole for South African nationals or tax residents to be able to make an early withdrawal from their retirement annuity funds, without formally emigrating. This was not the original policy intention.

<u>Proposal</u>

In order to align the current provisions of the Act allowing individuals to withdraw a lump sum from their retirement annuity fund to the underlying policy objectives, the following is proposed:

- The definition of the 'retirement annuity fund' in section 1(b)(x)(dd) should be amended to include the requirement that an individual must emigrate from South Africa and that emigration must be recognised by the South African Reserve Bank for purposes of exchange control as one of the criterion to be met in order for individuals to be able to withdraw a lump sum from their retirement annuity fund.

Effective date

The proposed amendments are deemed to have come into effect on 1 March 2016 and applies in respect of years of assessment commencing on or after that date.

3.10. Cross-border hybrid debt instruments

[Applicable provisions: Sections 8F and 8FA of the Act]

Background

In 2013, changes were made in the Income Tax Act to introduce specific anti-avoidance rules in section 8F and section 8FA dealing with hybrid debt instrument and hybrid interest. These anti-avoidance rules reclassify interest as dividends *in specie* under a two-fold regime. In the first instance, the anti-avoidance rules focus on the equity-like features that relate to the debt instrument itself. The second set of rules focuses on the nature of the yield (i.e. the interest labelled return).

The rules focusing on the debt instrument seek to identify the equity features of the debt instrument. By so doing the rules focus on the convertibility of the debt instrument into shares, the repayment of the debt or interest on the debt instrument conditioned upon the solvency of the issuer and the reasonableness of the period the debt will remain outstanding. The rules focusing on the nature of the yield require that the yield must be determined with reference to a rate of interest, and that the rate of interest must not be dependent on the profits of the issuer for that yield to qualify as interest instead of some other equity-like return (i.e. hybrid-interest).

These anti-avoidance rules are aimed at preventing the artificial generation of interest deductions by an issuer if the debt instrument qualifies as a hybrid debt instrument because of its equity features, or if the yield is determined not to constitute *bona fide* interest. In addition, the issuer is furthermore liable for dividends tax at a rate of 15%.

Reasons for change

The 2013 Draft Taxation Laws Amendment Bill (2013 Draft TLAB) which was released for public comments on 4 July 2013 made provision for these specific anti-avoidance rules to only apply to debt that was issued by South African tax resident companies. Based on the public comments received on the 2013 Draft TLAB, changes were made in the 2013 TLAB to extend the application of these rules to debt issued by both resident and non-resident companies.

It has come to Government's attention that the application of the current re-classification feature of the anti-hybrid debt instrument and anti-hybrid interest rules creates opportunities for tax arbitrage. Transactions involving non-resident issuers of debt instruments are intentionally made to include equity features in their debt instruments as a mechanism of taking advantage of the re-classification feature of these anti-avoidance rules.

Under these schemes, the parties (e.g. a non-resident issuer and a resident holder) intentionally make the debt instrument or the interest subject to the anti-hybrid debt instrument and anti-hybrid interest rules. The re-classification of interest as dividends in specie under these anti-avoidance rules will not, in these circumstances, deny the non-resident issuer an interest deduction. This is because the non-resident issuer would not be subject to the South African anti-hybrid debt rules. However, the re-classification will be beneficial for the resident holder as that holder will be deemed to have received a dividend in specie that is exempt from normal tax in respect of which the non-resident issuer is only subject to a dividends withholding tax of 15% (subject to various exemptions and treaty benefits).

This creates a mismatch in the tax treatment applicable to the interest paid by the non-resident issuer as the non-resident issuer benefits from a full tax deduction of the interest it incurs in its country of residence, but only pays tax at a preferential tax rate of 15% (or potentially no tax at all) as a result of the operation of the re-classification in the South African tax legislation and treaty benefits.

Proposal

In order to curb this mismatch and discourage non-resident issuers from structuring their loans to specifically contain the equity features that trigger the re-classification of their interest payments for South African tax purposes, it is proposed that both sets of anti-avoidance rules should be limited to instances under which the intended denial of the interest deduction will be applicable.

As a result, it is proposed that the anti-avoidance rules should only apply to the following:

- in instances where the issuer is a resident company,
- in instances where the issuer is a non-resident company, the rules should only apply in respect of a debt instrument that is solely attributable to a permanent establishment in South Africa or a controlled foreign company whose profits are attributed to a South African resident.

Effective date

These amendments are deemed to have come into effect on 24 February 2016 and are applicable in respect of amounts incurred on or after that date.

3.11. Hybrid debt instruments subject to subordination agreements

[Applicable provision: Section 8F of the Act]

Background

Section 8F of the Act makes provision for the specific anti-avoidance rules aimed at reclassifying any amount of interest in respect of a debt instrument or interest incurred as a dividend *in specie* declared and paid by the issuer if that debt instrument or the interest contain equity-like or dividend like features. This re-classification of the interest denies the issuer an interest deduction and the issuer also becomes liable for dividend withholding tax at a rate of 15% in respect of such dividend *in specie*.

For purposes of section 8F, the anti-avoidance rules take into account not only the equity features of the instrument itself, but the side agreements or subordination agreements that were entered into in respect of the debt instrument. In particular, these anti-avoidance rules will be triggered by any arrangement where the obligation to repay any amount owing in respect of the debt instrument (i.e. the corpus or interest) will be disregarded if that obligation is conditional upon the solvency of the debtor (i.e. the market value of the issuer's assets being less than its liabilities).

In such an instance, these anti-avoidance rules do not only look to the imbedded features of the instrument itself, but any other side agreement or subordination agreement that gives rise to an arrangement that makes the issuer's obligation to make a payment in respect of the debt instrument conditional upon the solvency of that issuer.

<u>Reasons for change</u>

In the current economic climate, it is not uncommon for companies to find themselves going through periods of varying levels of financial distress. These periods of financial distress may be short-term or may be fairly sustained. As a result, many companies revert to entering into subordinate agreements aimed at subordinating their shareholder loans in favour of third party borrowings. Furthermore, it has come to Government's attention that oftentimes the trigger for these subordination agreements is that when a company is undergoing audit, auditors of the company will in certain circumstances require that shareholder loans should be subordinated to ensure that the annual financial statements do not need to be qualified as it may be questionable whether the company is a going concern given its financial position.

Typically a subordination agreement provides that the company will not make any payments in respect of a debt until such time as the assets of the company fairly valued exceed the liabilities of the company. This conditionality of the repayments and/or interest payments upon the solvency of the company is more aligned to the payment considerations directors of companies are faced with in paying out dividends and is a trigger for the re-classification under the anti-hybrid debt rules.

The re-classification of the interest as a result of the subordination agreement, gives rise to added pressures for the company. In the first instance the company will be treated as having paid a dividend *in specie* in respect of any interest payments it may make on the subordinated loan (which interest payments are not always suspended under the subordination agreement). Secondly, the denial of an interest deduction in respect of the paid or unpaid but incurred interest charges may place the company in a tax paying position in its period of business difficulty.

Proposal

It is proposed that the re-classification feature of the anti-avoidance rules should not apply in the instances where an issuer that owes an amount to a company that forms part of the same group of companies as the issuer and payments in respect of that amount owing are suspended due to the financial difficulties of the issuer. For purposes of this concession, the liquidity and solvency tests envisaged under the Companies Act will be the benchmark for the levels of financial distress aimed at assisting. This is in line with audit practices, as auditors would require an issuer that is technically insolvent and/or illiquid to subordinate its shareholder loans in favour of third party creditors.

This concession for group debt that is subordinated in favour of third party creditors will result in the company continuing to claim its interest deduction of the debt. In addition, as there will be no re-classification of the interest as dividends *in specie*, the company will not suffer the added burden of a dividends withholding tax.

Effective date

These amendments will come into effect on 1 January 2017 and are applicable in respect of amounts incurred on or after that date.

3.12. Extending the small business corporation regime to personal liability companies

[Applicable provision: Section 12E of the Act]

Background

In 2001, a special dispensation for qualifying business corporations was introduced. In order to qualify for the special dispensation, the entity had to meet the definition of a 'small business corporation' as defined in the Act. The Act required that an entity qualifying as a small business corporation had to either be a close corporation or a company registered as a private company in terms of the then applicable Companies Act, 1973 (Act No. 61 of 1973). Furthermore, the scope of the definition of small business corporation was intentionally limited to curb the disguise of passive income and remuneration as business earnings. Such a disguise would otherwise have allowed persons rendering professional services to take advantage of the concessionary tax rates that apply to small business corporations instead of taxing the disguised passive income and remuneration at the normal company tax rate.

The limitation measure provides that an entity that has more than 20% of its revenue receipts and accruals and capital gains being made up of passive income and income earned by the entity for rendering certain professional services which are performed by a person who holds an interest in the entity (i.e. personal services) could not qualify as a small business corporation. In 2005 the abovementioned measure in respect of personal services was relaxed. As a result entities that rendered personal services could qualify as small business corporations provided that they employ at least three full-time employees who do not have an interest in the entity and are not connected persons (i.e. relatives) in relation to those that have an interest in the entity.

Reasons for change

In 2009, the new Companies Act, 2008 (Act No. 71 of 2008) was promulgated and is administered by the Department of Trade and Industry. Many provisions of the Income Tax Act depended or referred to company law principles and definitions contained in the old Companies Act, 1973 (Act No. 61 of 1973). Over the past years subsequent technical corrections have been made in the Income Tax Act due to the commencement of the 2008 Companies Act in 2011.

It has come to Government's attention that amendments made to the provisions dealing with small business corporations as a result of the 2008 Companies Act did not adequately take into account some of the issues related to small business corporations, for example, under the 2008 Companies Act the definition of a private company expressly excludes a personal liability company. As the definition of a small business corporation in the Act includes a private company, the resultant anomaly is that personal liability companies which typically render personal services are currently automatically excluded from being small business corporations for tax purposes.

Proposal

In order to correct this anomaly created by the exclusion of personal liability companies from the definition of a private company in the 2008 Companies Act, it is proposed that personal liability companies should be expressly included in the definition of a 'small business corporation' contained in the Income Tax Act. However, these personal liability companies would be subject to the requirement to employ at least three full-time employees who do not have an interest in the entity and are not connected persons in relation to those that have an interest in the entity.

Effective date

These amendments will come into effect in respect of years of assessment ending on or after 1 January 2017.

3.13. Asset-for-share transactions for natural persons employed by a company

[Applicable provision: Section 42 of the Act]

Background

Roll-over treatment is granted where a person disposes of an asset to a company that issues shares to that person in exchange for the asset. This roll-over relief is granted in an asset-for-share transaction in the instance that either:

- subsequent to the transaction the person holds a qualifying interest in the company acquiring the asset of that person; or
- the person disposing of the asset to the company is a natural person who is engaged on a full-time basis in the business of that company of rendering a service.

When the roll-over provisions were introduced, the abovementioned qualifying conditions were put in place to ensure that only substantial and long-term transfers of assets in exchange for shares issued by the acquiring company could benefit from roll-over relief. Furthermore, the latter condition in respect of natural person was aimed at professional service firms, which operate in an incorporated form, that wish to incorporate. It was intended that a Shareholder/Director of such professional service firm would not be required to hold a qualifying interest in the company after the asset-for-share transaction.

Reasons for change

Some taxpayers have indicated that the original intention of the qualifying condition in respect of natural persons that are involved in the business of the company that acquires the assets in an asset-for-share transaction is not clearly reflected. As it currently stands, the wording potentially allows for unintended roll-over relief without requiring the natural person to hold a qualifying interest in the acquiring company. This results in the qualifying condition going much further than the original policy intention to provide roll-over relief to a group of professionals setting up business under a professional services firm without regard for the qualifying interest requirement.

Proposal

To clarify the conditions under which an asset-for-share transaction between a natural person and a company will qualify for roll-over relief without having regard to the required qualifying interest at the close of that asset-for-share transaction, it is proposed that only asset-for-share transactions involving personal liability companies should qualify. This is because professional service providers to whom the benefit was initially intended for, such as lawyers, doctors or accountants after incorporation operate as personal liability companies.

Effective date

The proposed amendments should be applicable in respect of transactions entered into on or after date of promulgation of the Taxation Laws Amendment Act, 2016.

3.14. Refining the tax implications on outright transfer of collateral provisions

[Applicable provisions: Section 1, 22 and paragraph 11 of the Eighth schedule of the Act and section 1 of the Securities Transfers Act No. 25 of 2007]

Background

In 2015, changes were made in the tax legislation to provide relief in respect of an outright transfer in beneficial ownership of collateral. As a result, there are no capital gains tax and securities transfer tax implications if a listed share is transferred as collateral in a lending arrangement, provided that the identical shares are returned to the borrower by the lender within a limited period of 12th months from the date in which the collateral arrangement was entered into. The 2015 tax dispensation that was introduced in the tax legislation for the outright transfer of collateral is similar to the tax dispensation applicable to securities lending arrangements.

The above-mentioned new tax dispensation for collateral arrangements necessitated the introduction of a concept of 'identical share' in the tax legislation as well as changes to the provisions dealing with amalgamation transactions in section 44 of the Act, to take into account the impact of amalgamation transaction on the ability of a party to a lending arrangement to return a share of the same class in the same company as that share originally transferred in terms of that lending arrangement.

Reasons for change

The tax relief on collateral arrangements has been welcomed by industry and taxpayers but concerns have been raised about certain of the restrictions and potential shortcomings not addressed in the current legislation. These restrictions include the following:

A. 12th Month limitation

The limitation of a collateral arrangement to a period of 12 months or less without the ability to re-post collateral due to the underlying obligation is unduly restrictive and would have the effect that it can only be applied in a context of a short term debt and would severely restrict the ability of banks to benefit from collateral arrangements in terms of meeting the regulatory requirements in so far as it relates to high quality liquid assets.

B. Corporate Actions

The 2015 changes to the definition of 'identical share' in the Act only recognize the impact of specific corporate actions on the ability of parties to collateral arrangements to return an identical share only to the extent of amalgamation transactions as envisaged in section 44 of the Act. These changes do not cater for situations outside of the control of a party to a securities lending/collateral arrangement that could possibly result in an identical share being unable to be returned in terms of securities lending/collateral arrangements. In practice, corporate actions and its impact on the ability to deliver an identical share in relation to collateral arrangement can be separated into two categories where a corporate action can either:

- impact the listed status of the share through the following actions (list not exhaustive nor definitive):
    - suspension/termination or withdrawal of share listing on a recognized exchange;
    - winding up/insolvency of issuer of shares; or
    - unbundling transactions; or
- result in additional or different shares being returned through the following actions (list not exhaustive nor definitive):
    - rights offers;
    - scrip dividends;
    - capitalization issues; or
    - unbundling transactions.

These categories or actions could potentially impact the securities lending/collateral arrangement definition post implementation of the securities lending/collateral arrangement, by no fault of the parties to the securities lending/collateral arrangement, which would result in the application of both capital gains tax and securities transfer tax to such securities lending/ collateral arrangement. 22

C. Listed shares

The special tax dispensation for the outright transfer of collateral only applies to the instruments listed in paragraph (a) of 'security' as defined in the Securities Transfer Tax Act that is listed on an exchange. This limits the exemption on collateral arrangements to listed shares only to be transferred as collateral. As a result, if bonds and other instruments not listed in paragraph (a) of the definition of security are transferred as collateral, they will not qualify for this special tax dispensation.

Proposal

A. Extending the 12th Month limitation to a 24th month limitation

Government is still concerned that the 2015 changes made in the tax legislation to provide relief in respect of an outright transfer in beneficial ownership of collateral moves away from common law principles in regard to a change of beneficial ownership. As a result, the 12 month limitation in respect of collateral arrangement was introduced to assist in limiting tax avoidance scenarios where either the sale of shares are disguised as collateral transactions or transactions where the collateral is used against rolling debt positions that are designed to keep a collateral position open for extended periods of time or even indefinitely.

Due to the fact that collateral arrangements supports financial stability objectives because of the role they play in mitigating credit risk, it is proposed that the legislation be amended to extend the allowable period within which the identical shares are returned to the borrower by the lender from the date on which the collateral arrangement was entered into from 12 to 24 months.

B. Broadening the definition of 'identical share' to cater for other specified corporate actions

It is proposed that the legislation, as it relates to an ‘identical share’ for purposes of a collateral arrangement, be broadened to cater for corporate actions in relation to situations outside of the control of a party to a securities lending/collateral arrangement that could possibly result in an identical share being unable to be returned in terms of that securities lending/collateral arrangement. The legislation should only recognize corporate actions announced and released, post finalisation of the securities lending/collateral agreement, by a Stock Exchange News Service (SENS) announcement if it specifically relates to the allowable security/collateral within that securities lending/collateral arrangement.

As an additional measure, no party to the securities lending/collateral arrangement in question that is subject to a corporate action should be able to directly or indirectly control or influence the outcome of such corporate action as published by the Johannesburg Stock Exchange.

C. Including listed government bonds as allowable instrument on collateral arrangements

Government is concerned that the extension of collateral arrangements to other instruments, for example bonds, has little merit due to the fact that bonds are not subject to securities transfer tax and will only be subject to capital gains tax if and when bonds are traded in the secondary market at a capital gain. The value of bonds generally only increases when the market has low inflation or disinflationary expectations, which would see increased demand for fixed instruments such as bonds. The vast majority of bonds in South Africa are held until maturity, meaning that there will be no gains or losses at maturity, regardless of market conditions.

That said, Government recognises that the use of government bonds as collateral is embedded in the financial markets industry and affects all its participants and transactions. Based on the above, it is proposed the provisions of collateral arrangements be extended to include listed government bonds. As a result, listed government bonds that are transferred as collateral, will qualify for the above-mentioned special tax dispensation.

Effective Date

The following effective dates are proposed:

- Extending the 12th month limitation to a 24 month limitation on collateral arrangements
- Including listed Government Bonds as allowable instrument on collateral arrangements
    - The proposed amendments will apply in respect of any collateral arrangement entered into on or after 1 January 2017.
- Broadening the definition of 'identical share' to cater for other corporate actions in relation to situations outside of the control of a party to a securities lending or collateral arrangement

- The proposed amendments will apply in respect of any securities lending or collateral arrangement entered into on or after 1 January 2017.

3.15. Refinement of third-party backed shares: pre-2012 legitimate transactions

[Applicable provision: Section 8EA of the Act]

Background

Third-party backed share anti-avoidance rules were introduced by Government during 2012 to deal with identifiable concerns regarding preference shares with dividend yields backed by third parties. These anti-avoidance rules deem dividend yields of third-party backed shares to be treated as ordinary revenue unless the funds derived from the issue of the third-party backed shares are used for a qualifying purpose.

The policy rationale for these rules (with its subsequent amendments) seeks to introduce anti-avoidance rules applicable to share instruments (typically preference shares) loaded with debt like features. The legislation targets share issues where the dividends in respect of those shares are guaranteed by unrelated third parties. These third party guarantees effectively meant that the holder of the share had no direct or indirect meaningful stake in the risks associated with the issuer.

For purposes of these specific anti-avoidance rules, section 8EA of the Act defines third-party backed shares as preference shares in respect of which an enforcement right or obligation exists for the benefit of the holder of the preference shares. In turn, an enforcement right or obligation, in relation to any share, means any obligation or right, of any person, other than the issuer of the share to acquire the share from the holder of the share or make any payment in respect of a guarantee, indemnity or similar arrangement.

Reasons for change

Over the past 2 years, changes have been made in the third-party backed share anti-avoidance rules to address adverse tax consequences affecting legitimate business transactions with no intention of anti-avoidance. Concerns have been raised that certain provisions in these rules still impede certain historic arrangements and transactions that were entered into before the introduction of these anti-avoidance rules in the Act in 2012.

These historic arrangements and transactions were often entered into with excessive guarantees and obligations being bolted on by lenders as standard practice effectively trapping parties to these transactions and arrangements within the ambit of the targeted anti-avoidance, post introduction of the legislation.

Taxpayers who entered into the historic arrangements and transactions could restructure them so as to remove the excessive guarantees and obligations but at issue is the fact that in absence of any commercial reasons for restructuring other than to avoid the provisions of section 8EA of the Act, such restructuring could attract the application of the general anti-avoidance rules.

Proposal

In order to provide relief in respect of those transactions entered into before 2012, it is proposed that the:

- legislation be amended to allow any parties that entered into any arrangement or transaction finalised (all terms and conditions precedent of the arrangement or transaction being met) before 01 April 2012, (earliest effective date of the third-party backed share anti-avoidance rules) that fall foul of the provisions of section 8EA be allowed to cancel any enforcement obligation or right;
- cancellation of any enforcement obligation or right be made within a proposed window period. The period will start from the date of

introduction of the TLAB 2016 and will end on 31 December 2017.

- relief be prospective and no refund of tax will be given by SARS to taxpayers already affected by the provisions of section 8EA of the Act.

Effective Date

The proposed amendments will apply in respect of any dividend or foreign dividend received or accrued during years of assessment commencing on or after 01 January 2017.

3.16. Addressing circumvention of anti-avidance rules dealing with third party back shares

[Applicable provisions: Sections 8E and section 8EA of the Act]

Background

During 2012 the tax legislation was amended by seeking to strengthen anti-avoidance measures on instruments with debt-like features. These anti-avoidance rules came in two forms. Firstly, the legislation targeted share issues where the dividends in respect of those shares were guaranteed by unrelated third parties. These third party guarantees effectively meant that the holder of the share had no direct or indirect meaningful stake in the risks associated with the issuer. Secondly, the legislation targeted share issues where the dividends in respect of those shares were fully secured by financial instruments (i.e. the secured financial instrument served as the basis for the dividend yield as opposed to a mix of assets associated with the issuing company as a whole).

Reasons for Change

Several schemes have been identified where investors structure transactions to circumvent the hybrid equity anti-avoidance rules. These schemes include, for example, the formation of trust holding mechanisms whereby investors acquire participation rights in trusts and the underlying investments of those trusts are preference shares. The formation of a trust effectively breaks the anti-avoidance link by interposing a trust between the investor and the tainted preference share to avoid activating any one of the anti-avoidance measures. The preference shares merely operate as a conduit for underlying debt instruments with the holder looking solely to the debt as collateral.

Proposal

In order to curb the circumvention of these specific anti-avoidance measures, it is proposed that amendments be made in the definitions of ‘hybrid equity instrument’ in section 8E as well as 'preference share' in section 8EA to include any right or interest where the value of that right or interest is directly or indirectly determined by the underlying share that is either an equity share or a share other than an equity share. Provided that the value or any return on that share is accordingly based or determined with reference to a specified rate of interest or time value of money.

Effective Date

The proposed amendments will come into effect on or after 1 January 2017 and applies in respect of years of assessment ending on or after that date.

3.17. Tax treatment of REITs – Qualifying distribution rule

[Applicable provision: Section 25BB(1) of the Act, definition of 'rental income']

Background

As from 1 April 2013, a special tax dispensation for a listed company that is a Real Estate Investment Trust ('REIT') or a company that is a subsidiary of a REIT ('controlled company') that is a resident was introduced in section 25BB of the Income Tax Act (the Act). Under this special tax regime, a REIT or a controlled company that is a resident is entitled to deduct from its income the amount of any 'qualifying distribution' incurred during that year of assessment by that REIT or controlled company that is a resident. 'Qualifying distribution' is defined in section 25BB of the Act to include any dividend declared or interest incurred in respect of a debenture forming part of a property linked unit by a REIT or a controlled company, during a year of assessment, if more than 75% of the gross income received by or accrued to such REIT or controlled company consists of rental income.

Based on this specific tax dispensation of a REIT or controlled company, a REIT or controlled company is not entitled to claim specific allowances in respect of immovable property in terms of sections 11(g), 13, 13*bis*, 13*ter*, 13*quat*, 13*quin*, or 13*sex* of the Act.

Reasons for change

At issue is the fact that a REIT or controlled company may have claimed the above-mentioned specific allowances in respect of immovable property before it become a REIT or controlled company. On disposal of such immovable property the general recoupment provisions of section 8(4) of the Act will apply to a REIT or controlled company in so far as that entity claimed the above-mentioned allowances in respect of immovable property. In terms of paragraph (n) of the definition of gross income in section 1 of the Act, the REIT or controlled company will therefore have to include the amount of recoupments in respect of allowances previously claimed in its gross income in the year of disposal. The inclusion of the amount of recoupment in the gross income of the REIT or controlled company could affect the 75% rental income analysis for purposes of the qualifying distribution rule.

Example:

Facts: The REIT or controlled company disposes of property A, on which it had previously claimed commercial building allowances of R30 million during the 2016 financial year. The REIT or controlled company earns rental income of R70 million during the 2016 financial year.

Results: Based on current legislation

Gross income = R70 million + R30 million = R100 million

Rental income = R70 million

Qualifying distribution threshold = Rental income/Gross income =

R70million/ R100million = 70%

The net effect is that a REIT or controlled company that is a resident will not qualify for the qualifying distribution deduction (75%).

Proposals

In order to assist those REITs or controlled companies that may have claimed the above-mentioned specific allowances in respect of immovable property before they obtained the status of a REIT or controlled company, it is proposed that the amount of recoupments in respect of allowances previously claimed be included in the 'rental income' definition of section 25BB and form part of the 75% rental income analysis for purposes of the qualifying distribution rule.

The proposed changes will only apply to those REITS or controlled companies that may have claimed the above-mentioned specific allowances in respect of immovable property before qualifying as a REIT or controlled company.

Effective date

The proposed amendments are deemed to have come into effect on 1 January 2016 and applies in respect of years of assessment ending on or after that date.

3.18. Interaction between REITs and section 9C

[Applicable provisions: Sections 9C and 25BB of the Act]

Background

In 2007, section 9C was introduced in the Act which currently makes provision for amounts in respect of equity shares that are held for a period of at least three continuous years to be deemed to be of a capital nature.

Section 9C(5) provides that when the equity share, held for at least 3 years, is disposed of there must be included in the taxpayer's income any expenditure or losses allowed as a deduction in terms of section 11 in any previous year of assessment: Provided that this subsection does not apply in respect of any expenditure or loss to the extent that the amount was recouped in terms of section 8(4)(a) or section 19.

Dividends received from a resident REIT or controlled company, as defined in section 25BB(1), are not exempt from tax in terms of paragraph *(aa)* of the proviso to section 10(1)(k)(i) but expenditure incurred to produce these taxable dividends and allowed as a deduction may be recouped on disposal of the equity shares in the REIT or controlled company.

Reasons for change

The current provisions of section 9C are inappropriate for equity shares in REITs and controlled companies that are residents. Dividends received from a REIT or a controlled company (as defined in section 25BB(1) that is a resident), form part of taxable income but allowable expenditure incurred to produce these taxable dividends that is recouped under section 9C(5) is then effectively not deductible. It is therefore proposed that a proviso be added to section 9C that subsection (5) does not apply to shares in a REIT or controlled company, as defined in section 25BB, that is a resident. 28

Proposal

In order to remove this anomaly, it is proposed that amendments be made in section 9C(5) to clarify that this section does not apply to shares in REITs or controlled companies.

Effective date

The proposed amendments will come into effect in respect of years of assessment ending on or after 1 January 2017.

3.19. Urban development zones (UDZ) – Allowing additional municipalities to apply for the UDX tax incentive

[Applicable provision: Section 13*quat* of the Act]

Background

The urban development zone tax incentive was designed to encourage property investment in central business districts i.e. areas with high population carrying capacity and developed infrastructure for transport. The principal objective of the incentive is to address dereliction and dilapidation, and promote urban renewal by stimulating investment in the construction and renovation of commercial and low cost residential buildings. The incentive is in the form of an accelerated depreciation allowance under section 13*quat* of the Act. The incentive is aimed at promoting investment in 16 designated inner cities, 15 of which now have demarcated UDZs within its boundaries. The incentive was initially available from 2013 until March 2014, where after a review of its effectiveness it was extended to March 2020.

In 2015, changes were made in the Act to allow municipalities with a population of 1 million demarcate an additional UDZ area. Furthermore, where the municipality's population is below 1 million, the Minister of Finance (MoF) may approve the demarcation of an additional UDZ having regard to the provisions set out under section 13*quat* (6) and (7) of the Act.

<u>Reason for change</u>

Municipalities outside of the 16 designated UDZs areas have approached the Minister to broaden the scope of the UDZ incentive to cover additional municipalities, as they seek to integrate the incentive into existing urban renewal plans. Section 13*quat* of the Act only caters for the 16 municipalities (Annexure A) and makes no provision for municipalities not listed under subsection 13*quat*(6)(a) to be eligible for the incentive.

Given the continued state of underdevelopment and dilapidation in their inner cities, there is demand from municipalities to expand the scope of the incentive and allow municipalities to apply to the Minister to be considered for the UDZ tax incentive. Where this inner city dilapidation continues, it discourages new investment and increases disinvestment in property. There may thus be a case to expand the scope of the incentive as it is seen to stimulate investment in the construction and renovation of commercial and low-cost residential buildings in the inner city.

<u>Proposal</u>

A. Additional Municipalities

It is proposed that section 13quat of the Act be amended to provide a framework for the Minister to consider applications from municipalities currently not allowed to designate a UDZ area. The Minister's assessment criteria will be based on the current legislative requirements as contained in section 13*quat*(6) and (7), as well as the additional criteria contained in Annexure B below.

The application process will apply to all municipalities that are not listed under subsection 13*quat* (6)(a) – i.e. all municipalities not currently part of the original 16 that were eligible since the inception of the UDZ incentive. Such municipalities may apply directly to the Minister for a UDZ area to be demarcated

If the municipality's application is successful and the Minister issues the notice in the government *gazette*, the municipality will be added to the list of qualifying municipalities through a legislative amendment under subsection 13*quat* (6)(a).

B. Additional Criteria

The inclusion of the additional criteria contemplated in Annexure B is aimed at providing an assessment framework to consider when broadening access to the incentive, through prioritising urban renewal and development in a manner that counters spatial fragmentation. Essentially Annexure B prescribes several criteria items of differing significance, dependent on each application's facts and circumstances, which have to be applied in context of each application.

A broader target market for the incentive could potentially increase the associated fiscal cost, however, the additional criteria essentially focuses on high-performing municipalities that have significant growth potential. The demarcation of the UDZ should not put an additional strain on municipal finances, but contribute positively towards an increase in the generation of own revenues from the municipality.

The municipality must support its application with evidence that it meets all the requirements of subsections 13*quat* (6) and (7).

The additional criteria proposed in Annexure B should be issued as a separate document through the means of a regulation to guide both the Minister and municipalities when considering approving/applying (for) a UDZ area. These represent some of the factors that the Minister will use in assessing whether to allow the demarcation of a UDZ in that municipality.

The additional criteria contained in Annexure B will also be used to assist the Minister in assessing applications for additional UDZs from municipalities that have a population of less than 1 million [s13quat(7)(bA)]. 36

Effective date

The proposed amendments will come into effect on the date of promulgation of the Taxation Laws Amendment Act, 2016.

Annexure A

Municipalities Eligible for UDZ incentive: 1 Buffalo City 2 Cape Town 3 Ekurhuleni 4 Emalahleni 5 Emfuleni 6 eThekwini Metro 7 Mahikeng 8 Johannesburg Metro 9 Mangaung 10 Matjhabeng 11 Mbombela 12 Msunduzi 13 Nelson Mandela Metro 14 Polokwane 15 Sol Plaatje 16 Tshwane Metro

Annexure B

SUGGESTED CRITERIA FOR NEW APPLICATIONS AND ADDITIONAL URBAN DEVELOPMENT ZONES

Category	**Item**	**Motivation**	**Measurement**
Urban renewal	Proposed area should contain derelict and dilapidated buildings that require rejuvenation	Relates to the original purpose of the UDZ, i.e. to rejuvenate the inner cities.	Number of derelict buildings in need of upgrading.

Spatial Targeting	Proposed area should be located within/close to a spatially targeted node identified within the municipal spatial framework (SDF) and have proven locational potential.	This criteria acts as a counter against urban sprawl and ensures that densification and focused, integrated interventions are addressed. It also ensures that the basic requirements for economic development are in place.	The following key elements need to be considered in evaluating the proposed UDZ: A transport interchange in close proximity to the area; Convergence of people; The area should be linked to primary and/or at least secondary transport routes. A conglomeration of mixed use activities and facilities should be present within the area.
Economic growth	Economic growth prospects and performance of the municipality as a whole	The overall economic output of the municipality needs to demonstrate positive growth over the last 2 years. Proven market	Gross value added (GVA) to be more than the national average, but a minimum of 1.5% over the previous 2 years.

		performance should be evident.	
Municipal commitment	Proven fiscal measures and plans towards improvements in the area. Municipality should demonstrate current ability to generate own revenue.	Own revenue should be >=50% of total municipality income	Own revenue : total municipal income = 0.5: 1
Annual submission of progress reports on historically approved UDZ's	Municipality must have submitted reports annually as required in section 13*quat* (9).	The reports will provide information regarding the current progress of the UDZ and whether an extension of the area is justified.	

3.20. Accelerated capital allowance in respect of supporting infrastructure used in producing renewable energy

[Applicable provision: Section 12U of the Act]

Background

South Africa as a party to the United Nations Framework Convention on Climate Change (UNFCCC) aims to reduce greenhouse gas (GHG) emissions and to incentivise investments in low carbon, clean energy. Renewable energy is prioritized by government as a viable alternative to the current carbon–intensive economy. Since 2005 targeted incentives for renewable energy have been introduced through the provisions of the Act, 58 of 1962.

Reasons for change

Currently, large scale renewable energy projects are not adequately catered for under the existing accelerated depreciation regime due to the capital intensive nature of supporting infrastructure whose tax treatment would need to be specifically targeted. Capital expenditures that indirectly support renewable electricity production, such as the construction of fences and roads, do not qualify for deductions under the Act. According to industry, this is one of the limitations that influence the viability of most large-scale renewable energy projects.

Proposal

It is therefore proposed that the provisions of the Act be broadened to include the supporting capital infrastructure in the form of capital expenditure actually incurred on roads and security fences for large scale renewable energy projects as follows:

A. Renewable energy projects qualifying for deductions:

It is proposed that only large scale renewable energy projects that generate electricity exceeding 5MW will qualify. Current evidence suggests that renewable energy projects within the band of 5 – 50MW are barely economically viable and as such this proposed incentive will assist in increasing the financial viability. The proposed amendment further took into account that all renewable energy projects approved under the auspices of the Renewable Energy Independent Power Producers Procurement Programme of the Department of Energy currently exceed 5MW.

B. Timing of proposed deduction:

Should the renewable energy production supporting capital infrastructure expense be incurred pre-commencement of trade, then similar to section 11A of the Act which provides for certain pre-trade expenditure to be allowed as a deduction, the capital expense will have to be:

- actually incurred prior to the commencement of and in preparation of carrying on that trade; and
- not have been allowed as a deduction in that year or any previous year of assessment.

C. Ring fencing and roll over:

As an anti-avoidance measure and with specific reference to the fact that the supporting infrastructure expense is of a capital nature, it is proposed that any supporting infrastructure capital expenditure that exceeds the income in any year of assessment be ring fenced to the specific trade of the production of renewable energy.

It is further proposed that the envisaged allowable supporting infrastructure capital expenditure that exceeds the taxable income to the specific trade of the production of renewable energy in any year of assessment be rolled-over as an allowable capital expenditure during the next succeeding year of assessment against income specific to the trade of the production of renewable energy.

<u>Effective date</u>

The proposed amendments will only apply to large-scale renewable energy projects embarked during any year of assessment commencing on or after 1 April 2016.

3.21. Tax exemption of National Housing Finance Corporation

[Applicable provisions: Sections 10(1)(t) and section 30(3)(b) of the Act]

<u>Background</u>

The Department of Human Settlements is currently consolidating all its Human Settlement Development Finance Institutions, namely, the National Housing Finance Corporation (NHFC), National Urban Reconstruction and Housing Agency (NURCHA) and the Rural Housing Loan Fund (RHLF) under one entity, namely, the NHFC, which is wholly owned by

Government. Currently, NURCHA and RLHF qualify as Public Benefit Organisations (PBOs) in terms of the Income Tax Act and are exempt from normal income tax. On the other hand, NHFC is a taxable entity.

Reason for Change

The existing different tax treatment of Human Settlement Development Finance Institutions creates difficulties, more especially during consolidation. Before consolidation, the activities were performed by two entities (NURCHA and RHLF), which are tax exempt. After consolidation, the same activities will be performed by one entity (NHFC), which is not exempt from tax.

In turn, the consolidation of functions into one entity requires the transfer of assets and liabilities from the aforementioned two tax exempt entities to this single taxable entity, which triggers a tax charge. Given that these activities qualify as public benefit activities and were tax exempt before consolidation, consolidation should not deter public benefit activities that qualify for tax exemption.

Proposal

The Human Settlement Development Finance plays a key role in improving the delivery of adequate housing to the needy. It is proposed that the receipts and accruals of NHFC should be exempt from tax in terms of section 10(1)(t) of the Act.

In order to allow for tax neutral transfer of assets and liabilities from NURCHA and RHLF to NHFC, it is proposed that a further amendment be made to section 30(3)(b) of the Income Tax Act.

Effective Date

The proposed amendments will be deemed to have come into effect on 1 April 2016 and will be applicable in respect of years of assessment commencing on or after that date.

3.22. *Tax treatment of land donated under land-reform initiatives*

[Applicable provisions: Section 56 of the Act, addition of a new provision in paragraph 64A of the Eighth Schedule to the Act]

Background

The Act makes provision for tax relief in respect of land donated under certain land reform programmes. For example, land granted in terms of the Land Reform Programme as contemplated in the White Paper on South African Land Policy, 1997, is exempt from donations tax. In addition, awards or compensations in terms of Restitution of Land Rights Act, 1994 are exempt from capital gains tax.

Reasons for change

The above-mentioned tax relief was introduced in the Income Tax Act in 1994 and 2002 respectively. Subsequent to this, Government has since introduced other land reform initiatives as stipulated in Chapter 6 of the National Development Plan (NDP). As the existing tax relief in the Income Tax Act was introduced prior to the publishing of the NDP, the relief does not extend to land reform initiatives aligned to Chapter 6 of the NDP.

Proposal

In order to provide relief to other land reform initiatives as stipulated in Chapter 6 of the NDP, it is proposed that:

- Exemption from donations tax in section 56 of the Act be extended to include land reform initiatives under Chapter 6 of the NDP.
- Exemption from capital gains tax in paragraph 64A of the Eighth Schedule to the Income Tax Act be extended to include awards in terms of land reform initiatives under Chapter 6 of the NDP.
- Introduction of new paragraph 64D of the Eighth Schedule to the Act to cater for exemption from capital gains tax in respect of land donated in terms of the land reform initiatives under Chapter 6 of the NDP.

Effective date

The following effective dates are proposed:

- Extending the exemption from donations tax in section 56 of the Income Tax Act to include the land reform initiatives under Chapter 6 of the NDP.
    - The proposed amendment is deemed to have come into operation on 1 March 2016 and applies in respect of donations received or accrued on or after that date.
- Extending the exemption from capital gains tax in paragraph 64A of the Eighth Schedule to include awards in terms of land reform initiatives under Chapter 6 of the NDP
- Introducing a new exemption in terms of paragraph 64D of the Eighth Schedule to cater for exemption in respect of land donated in terms of land reform initiatives under Chapter 6 of the NDP.
    - The proposed amendment is deemed to have come into operation on 1 March 2016 and applies in respect of years of assessment ending on or after that date.

The proposed amendments are deemed to have come into effect from 1 March 2016 and will be applicable in respect of years of assessment commencing on or after that date.

3.23. Clarifying the tax treatment of Government grants

[Applicable provision: Paragraph *(l)* of the 'gross income' definition in section 1 of the Act]

Background

A uniform regime for the taxation of government grants was introduced under section 12P of the Act in 2012. Under this uniform regime, government grants can only be exempt if:

(1) they form part of the comprehensive legislative list set out in the

Eleventh Schedule or

(2) they are specifically identified by the Minister of Finance by notice in the *Gazette* as a mechanism to cater for grants originating in the middle of a legislative cycle for which there will be a delay in listing them in the Eleventh Schedule.

These two mechanisms were introduced to ensure that the key determinations to be observed when seeking to exempt any government grant are properly considered. The intention is that these mechanisms would ensure that only genuine grants and not some forms of disguised consideration or transfer paid for or in exchange for goods and services required by Government would be exempt and that the financial and tax implications were borne in mind when deciding to grant an exemption.

Reasons for change

Under the current dispensation, a government grant that is neither listed in the Eleventh Schedule nor identified by the Minister in the *Gazette* may still avoid being taxed. This arises as a result of the grant falling outside the definition of gross income because that grant is meant to subsidise the procurement or acquisition of capital assets and is thus capital in nature.

Proposal

It is proposed that the legislation should be clarified and aligned in accordance with normal tax practices applicable to taxable receipts. Firstly, the amount must be included in the gross income of the recipient. Any exclusion from tax should be made on the basis of a special exemption granted in terms of section 12P read together with the Eleventh Schedule. The proposed inclusion in gross income for all government grants will be included under paragraph (l) of the definition of 'gross income'.

Effective date

These amendments will apply to all grants received or accrued on or after 1 January 2017.

3.24. Provision for exception to the research and development (R&D) incentive prescription rules

[Applicable provisions: Section 11D of the Income Tax Actand section 93 of the Tax Administration Act 28 of 2011]

Background

The income tax system contains an incentive for research and development to promote R&D related job opportunities and economic growth in South Africa. The tax incentive is in the form of a 150% deduction for non-capital R&D expenditure. Taxpayers seeking to benefit from this allowance are required to obtain pre-approval from the Minister of Science and Technology, who in turn decides whether to provide such approval based on the findings of a committee set up for this purpose. Management and administration of the pre-approval committee is essentially done by the Department of Science and Technology (DST), although the committee comprises people sourced from the DST, National Treasury and SARS.

Since inception of the R&D pre-approval system in 2012, the pre-approval adjudication committee has experienced teething, administration and capacity problems. These setbacks have led to delays and substantial backlogs in the processing of applications. The backlogs have resulted in calls by taxpayers and tax practitioners for a task team to be appointed to make recommendations on how the R&D tax incentive could be improved. The Minister of Science and Technology responded to these calls and appointed such a task team, consisting of expert representatives from academia, government and the private sector. The task team has completed its mandate and has provided the Minister of Science & Technology with its findings.

Reason for change

Amongst the issues raised by the task team was that delays in processing approvals could cause assessments to prescribe before an application is adjudicated upon. This situation is exacerbated because SARS has made it clear that submission of income tax and provisional tax returns should not be delayed pending pre-approval by the R&D committee. Further, taxpayers have been advised that when submitting such returns they should not assume a successful pre-approval as wrongfully doing so could result in them being subject to the imposition of interest and penalties.

Example:

Facts:

Company X has a 30 June year end. On 1 November 2012, Company X submitted a proposed research and development project to DST for pre-approval. On 1 August 2013 Company X submitted its return to SARS for assessment and was duly assessed on that day (company has until 30 June 2014 to submit its return). In submitting its return the taxpayer claimed certain R&D expenditure to the value of R1, 000,000 (incurred between November 2012 and 30 June 2013). On 10 August 2016 the DST approved the pre-approval application of 1 November 2012.

Results:

At the time of submitting the tax return, the taxpayer did not claim an additional R500,000, which it anticipated it would be entitled to once its R&D project was approved by the Minister of Science and Technology. Given the approval date by DST on 10 August 2016, which is more than three years after the date of assessment, the taxpayer wanted to reopen its 2013 tax return to include a claim for an additional allowance of R500, 000. Since the authority to revise an assessment prescribes three years after a tax return has been assessed, the taxpayer has lost the benefit of the R&D allowance. In this case the taxpayer's return would have already been prescribed by 1 August 2016 before receiving the decision from DST.

<u>Proposal</u>

An amendment should be made to section 11D to allow for a reopening of assessments in the circumstances outlined above.

<u>Effective date</u>

The proposed amendments should be made effective in respect of assessments raised after the date of promulgation of section 11D of the Taxation Laws Amendment Act, 2016.

3.25. Addressing possible administrative and technical changes in respect of industry policy for section 12I

[Applicable provision: Section 12I of the Act]

<u>Background</u>

Section 12I of the Act allows taxpayers an additional investment and training allowance in respect of industrial policy projects provided that the projects meet certain criteria prescribed by way of regulation. The additional investment allowance ranges from 35% to 100% of the cost of any new and unused manufacturing assets used for the project, depending on whether the project has qualifying status or preferred status, and whether the project is located in an industrial development zone (or designated special economic zone).

The additional investment allowance also has specific legislative requirements that requires the asset:

- to be owned by the company claiming the additional allowance;
- to be used for the furtherance of the industrial policy project carried on by that company;
- to have been acquired and contracted for on or after the date of approval of the relevant project as an industrial policy project; and
- was brought into use within four years from the date of approval of the relevant project as an industrial policy project.

<u>Reasons for change</u>

A. Status change of project

The current provisions of section 12I(12) only envisages the withdrawal of project approval when the company fails to comply with any requirements as set on approval.

It, however, does not account for the situation where the project was initially approved on preferred status, but the project status subsequently changes and becomes a qualifying status project by the end of the compliance period.

For example, the project may have scored 7 out of 8 points upon project approval and qualified as a preferred status project, but by the end of the compliance period, the project only scores 6 out of 8 points and is regarded as a qualifying status project. In this example, the approved project may not be disqualified as it still meets the minimum requirements for an approved industrial policy project, i.e. qualifying status project. Nonetheless, if it does not meet the scoring criteria for a preferred status project by the end of the compliance period, it should not be allowed to claim the preferred status allowance of either 55% or 100% of the cost of any new and used manufacturing assets, depending on whether the project is located within a special economic zone or not.

The risk to the fiscus is that the project which was approved as a preferred status but changes to a qualifying status before the end of a compliance period could be claiming a larger allowance value than it is allowed to claim, thereby reducing revenue collection over that period. This is a gap in the current legislation which needs to be addressed, because there is a risk that this may happen more frequently as many more projects near the end of the compliance period.

B. Extending period to bring assets into use

Given the estimates used at the approval stage and the nature of these large-scale manufacturing projects, start-up delays are a distinct possibility. In this regard the legislation does allow the Minister of Trade and Industry the discretion to extend the period within which assets are required to be brought into use, after taking into account the recommendations of the adjudication committee.

Current legislation contains a technical oversight in that the relevant discretionary enabling legislation does not extend to certain other provisions in the section. There is no policy rational for the Minister's discretion in this regard to not extend to all the relevant provisions.

Proposal

A. *Status change of project*

It is proposed that section 12I be amended to enable SARS to recoup the difference in allowance claimed in respect of a project which was approved as a preferred status but changes to a qualifying status by the end of the compliance period. If a project was initially approved on preferred status and claimed allowances on that basis, but by the end of the compliance period the project only reaches qualifying status, the excess value claimed should be recouped from the taxpayer.

B. *Extending period to bring asset into use*

The discretion contemplated in section 12I(19)(a) should be extended to also include a reference to subparagraph (7)(c) of the same section.

Effective date

The proposed amendments will come into effect on the date of promulgation of the Taxation Laws Amendment Act, 2016.

3.26. Providing tax relief for mining companies spending on infrastructure for the benefit of mining communities

[Applicable provision: Section 36 of the Act]

Background

The Mineral and Petroleum Resources Development Act, 2002, (Act No 28 of 2002) (MPRDA) has multiple purposes – one of which is to transform mining and production industries in South Africa. To ensure effective transformation, the MPRDA makes it compulsory for mining companies to submit a Social and Labour Plan (SLP). SLPs are entered into between the community, the mining company and the Department of Mineral Resources

(DMR). One of the requirements is to assist with the development of mining communities, which typically involves a company agreeing to build infrastructure – ranging from roads and drainage systems to crèches, schools, clinics, housing, and recreational buildings – to benefit workers and communities surrounding the mine.

Reasons for change

Currently, section 36(11) of the Act enables mining companies to deduct certain capital expenditure in lieu of other sections in the Act. Mining companies can only deduct such capital expenditure if it relates directly to its employees, not the wider community. If, for example, a mining company builds a clinic purely to serve its employees, the mining company will be entitled to deduct the related capital expenses in equal amounts over a ten year period. If the clinic was built to serve the wider community instead, the mining company is unable in terms of the current provisions of the Act to deduct any of the capital expenditure incurred.

In particular, section 36(11)(e) of the Act makes provision for mining companies to deduct capital expenditure incurred pursuant to the MPRDA, but excluding capital expenditure incurred by mining companies in respect of infrastructure or environmental rehabilitation.

Proposal

To recognise the SLP requirements (of the MPRDA) for mining companies to meaningfully contribute toward community development, and because it has become practically and administratively difficult for mining companies or SARS to differentiate between whether employees or people from the wider mining community are using developmental infrastructure (for example a clinic), the following is proposed:

- To extend the current relief provided to mining companies (for capital expenditure incurred in respect of infrastructure for the benefit of employees) to capital expenditure incurred by mining companies on infrastructure in terms of the SLP requirements of the MPRDA, for the benefit of the people living in mining communities (other than employees).

- To be eligible for the capital expenditure deduction, the infrastructure erected or developed by the mining company should reflect what was agreed to between the mining company and the DMR in terms of SLP requirements of the MPRDA.
- The DMR will improve effective monitoring and oversight of such plans and the Tax Administration Act allows SARS to request the SLP and associated annual reports.
- That current ten year period for deductions applicable to mining companies in respect of capital expenditure incurred on infrastructure for the benefit of employees be applicable in respect of capital infrastructure expenditure incurred by mining companies in terms of the SLP requirements of the MPRDA. The primary rationale for using the same time period for deductions is simplicity as it is often the case that a clinic or road will be used by both employees and the wider community. Having different write-off periods will create unnecessary complexity in determining the use ratio of employees and community members.

<u>Effective date</u>

The proposed amendments will be effective for years of assessments commencing on or after 1 April 2017.

3.27. Tax exemption of public benefit organizations providing industry based education and training activities

[Applicable provision: Part I of the Ninth Schedule to the Act]

Background

The Act contains provisions in sections 10(1)*(cN)* and 30, and the Ninth Schedule that provide exemption for public benefit organisations if they meet certain requirements as set out in the Act, including the carrying on of public benefit activities. Paragraph *(a)* of the definition of public benefit activities refers to activities listed in Part 1 of the Ninth Schedule. In turn, paragraph 4 of Part I of the Ninth Schedule lists qualifying education and development public benefit activities. Tax exemption is not automatic and public benefit organisation must still apply to SARS in order to obtain the tax exemption status.

Reasons for change

It has come to Government's attention that certain industries establish special associations to promote the common interest of members in that particular industry or profession. These associations also provide training to employees of that particular industry as well as implementing industry based standards. The associations also develop certification schemes for employees working in that specific industry in line with best international practice. The main source of funding is derived from training courses and other related income which is analogous to tuition fees received by a University. Industry based associations such as these are directed by the requirements of the industry and are linked for accreditation to the Quality Council for Trades and Occupations (QCTO).

Although the principal object of these associations is to carry on educational and training activities for the benefits and needs of the public, these associations do not qualify for tax exemption as they do not meet the requirements set out in sections 10(1)*(c*N*)* and 30, and paragraph 4 (dealing with exemption of education and development) in Part 1 of the Ninth Schedule.

Proposal

In order to encourage the industry to provide education and development, which play a key role in increasing not only more skilled individuals in the workplace but also to the poor and needy persons who seek cost effective/affordable quality industry based education and training, it is proposed that amendments be made in the Act to extend the list of public benefit activities qualifying public benefit organisations for tax exemption to education and training activities to benefit industry based training organisations.

It is therefore proposed that:

- receipts and accruals of industry based public benefit associations providing education and training programmes and courses for the development of persons or employees in that particular industry be exempt from normal taxation by including the activities performed by them under 'Education and Development' in paragraph 4 of Part I of the Ninth Schedule to the Act provided that those qualifications are compatible with the type of qualifications in the Quality Council for Trades and Occupations.
- Receipts and accruals of industry based public benefit associations administering examination and providing certification programmes for the benefit of that particular industry be exempt from normal taxation by including the activities performed by them under 'Education and Development' in paragraph 4 of Part I of the Ninth Schedule to the Act, provided that that association is accredited to conduct those activities by the South African National Accreditation System (SANAS), South Africa's member of the International Accreditation Forum.

Effective date

The proposed amendments will come into operation on the date of promulgation of the Taxation Laws Amendment Act of 2016.

3.28. Repeal of withholding tax on services fees regime

Background

In the 2013 Budget Speech, the Minister announced and introduced a withholding tax on cross-border services. This withholding tax is a final tax in respect of fees payable by a resident to a non-resident for technical, management and consulting services rendered by that non-resident to a resident. The main aim of the introduction of this withholding tax was to identify and collect revenue from non-resident taxpayers who provide technical, management or consulting services and earned fee income from a South African source. It was also aimed at preventing the potential for the erosion of the South African tax base.

The tax rate for the withholding tax on services is 15% of the gross amount of fees paid to a non-resident (subject to tax treaty relief). The liability to withhold the tax is with the payor of the service fees to or for the benefit of the non-resident taxpayer.

Reasons for change

In June 2015, SARS issued a draft public notice listing a reportable arrangement in terms of section 35(2) of the Tax Administration Act, 2011 for public comment. This dealt with arrangements in terms of which certain service fees are paid by a resident to a non-resident. On 3 February 2016, SARS issued in Notice 140 of the Government Gazette no 39650 a revised list of reportable arrangements. According to this Notice an arrangement for the rendering of consultancy, construction, engineering, installation, logistical, managerial, supervisory, technical or training services to a South African resident or a non-resident having a permanent establishment in South Africa, in terms of which arrangement a non-resident was, is, or is anticipated to be physically present in South Africa in connection with or for purposes of rendering the services and the expenditure incurred or to be incurred in respect of the services exceeds or is anticipated to exceed R10 million, is a reportable arrangement in terms of the Tax Administration Act provided that it does not qualify as ‘remuneration’ for employees’ tax purposes.

If the reportable arrangement regime were to be applied concurrently with the withholding tax on services regime, it would have resulted in additional administrative functions for SARS and a compliance burden for taxpayers. The two regimes are virtually aimed at achieving the same goal (i.e. identifying and collecting revenue from non-resident taxpayers who provide technical, management or consulting services)

Further, concerns have been raised that the application of withholding tax on services regime will give rise to uncertainty on the application of domestic tax law and limited revenue due to limited taxing rights under tax treaties.

<u>Proposal</u>

In view of the above, it is proposed that the withholding tax on services be repealed from the Act. Therefore, payment of certain service fees by South African residents to non-residents will now be dealt with under the provisions of Reportable Arrangements in the Tax Administration Act.

<u>Effective date</u>

The proposed amendments will be effective to all service fees that are paid or that become due and payable on or after 1 January 2017.

3.29. Exemption of collective investment schemes in securities from controlled foreign companies rules

[Applicable provision: Section 9D of the Act]

<u>Background</u>

A. Controlled Foreign Companies

The South African tax system has controlled foreign company (CFC) rules that are anti-avoidance rules generally aimed at preventing South African residents from shifting tainted forms of taxable income offshore by investing through CFCs. The CFC rules make provision for the net income of a CFC to be attributed and included in the income of South African shareholders.

Section 9D of the Act defines a CFC as any foreign company where more than 50% of the total participation rights in that foreign company are directly or indirectly held, or more than 50% of the voting rights in that foreign company are directly or indirectly exercisable, by one or more persons that are residents other than persons that are headquarter companies. Section 1 of the Act defines a foreign company as any company which is not a resident. In turn, the definition of a company in section 1 of the Act includes portfolios of foreign collective investment schemes in securities.

The amount of income which is included in the net income of a CFC is subject to various exemptions such as the foreign business establishment, high-tax and related party exemptions. These exemptions seek to strike a balance between protecting the tax base and the need for South African multinational entities to be competitive.

B. Collective Investment Schemes and Securities

Paragraph (e)(ii) of the definition of a company in section 1(1) of the Act includes any portfolio of a foreign collective investment scheme that is comparable to a portfolio of a collective investment scheme in participation bonds or a portfolio of a collective investment scheme in pursuance of any arrangement in terms of which members of the public are invited or permitted to contribute or hold participatory interest in that portfolio through shares, units or any other form of participatory interest.

A collective investment scheme is an investment vehicle used by investment managers to pool investors' funds to enable them to access investments which they might not otherwise be able to access in their individual capacities. In South Africa, collective investments schemes are generally established as vesting trusts, with investors in such schemes being the beneficiaries of the trust. The assets of a collective investment scheme portfolio are held by the trustees on behalf of the holders of participatory interests. The taxation of these vesting trusts holders of and participatory interests is regulated by section 25BA. These collective investment schemes are regulated by the Collective Investment Schemes Control Act. No 45 of 2002.

<u>Reasons for change</u>

When funds are invested in a collective investment scheme in securities portfolio, an investor acquires a portion of the participatory interests in the total collective investment scheme in securities portfolio. In turn, investors get to share the risks and benefits of their investment in a collective investment scheme in securities in proportion to the participatory interests in that scheme.

At issue is the application of the CFC rules in cases where the South African collective investment scheme in securities invests in a global fund, which is a foreign fund. Concerns have been raised that as South African collective investment schemes in securities invest in a global fund, South African collective investment schemes in securities should be considered to be the direct holders of the participation rights in that global fund. On the other hand, there is an argument that as South African collective investment schemes in securities are established as vesting trusts, the units in the global fund are beneficially owned by the investors in the South African collective investment schemes in securities in proportion to their effective interests in such global fund.

In addition, there is uncertainty as to whether the global fund is comparable to a portfolio of collective investment scheme in securities as envisaged in the above-mentioned paragraph (e) (ii) of the definition of a company of section 1(1) of the Act.

More specifically, the uncertainty arises in the determination of whether:

- the global fund can be regarded as a CFC;
- a South African collective investment scheme or investors in a South African collective investment scheme in securities should be treated as holders of the participation rights in that global fund;
- as South African collective investment scheme in securities or investors in a South African collective investment scheme in securities should be considered to directly or indirectly exercise voting rights in that global fund.

Proposal

In order to eliminate the uncertainty and potential double taxation described above, it is proposed that:

- South African collective investment schemes in securities investing in a global fund should be excluded from applying the CFC rules (section 9D) to investments made in that global fund;
- a South African collective investment schemes in securities are established as vesting trusts, the conduit principle should apply when South African collective investment schemes in securities invest in a global fund and that tax should ultimately arise in the hands of investors in the South African collective investment schemes in securities in proportion to their effective interests in such global fund.

Effective date

The proposed amendments will apply in respect of years of assessment commencing on or after 1 January 2017.

3.30. Extending the bad debt deduction rule to exchange differences arising on foreign currency denominated loan

[Applicable provision: Section 11(i) of the Act]

Background

Section 11(i) of the Act permits a deduction of the amount of any debt due to the taxpayer to the extent that such debt has become bad during the year of assessment. However, In order to get the deduction under section 11(i) of the Act, the amount of the debt in question must have been included in that taxpayer's income either in the current year or previous year of assessment. The determination as to whether a debt is bad must be made at the time that the debt is claimed as bad.

Reasons for change

Currently, exchange differences arising on a foreign currency denominated loan by a South African taxpayer, who is not a money-lender to another person are taken into account in the determination of a taxable income as either an inclusion of deduction.

However, where that loan becomes bad, a taxpayer is not allowed to claim a deduction in terms of section 11(a) of the Act in relation to the exchange gains that were included in the income. The loss reflects a loss of fixed capital rather than floating capital. Further, a taxpayer is not allowed to claim a deduction under section 11(i) of the Act because the amount of the debt, being the foreign currency denominated amount, was not included in income. Consequently, the current tax provisions do not give a taxpayer any relief in relation to irrecoverable amounts on which it has been subjected to tax.

Proposal

In order to provide relief in relation to exchange differences that are included in taxable income, it is proposed that the provisions of section 11(i) of the Act be extended to apply to any exchange difference in respect of a debt that has been included in income during the year of assessment.

Effective date

The proposed amendments will apply in respect of the years of assessment ending on 1 January 2017

3.31. Interest withholding tax where interest is written off

[Applicable provisions: Part IVB of Chapter II of the Act: Sections 50G of the Act]

Background

On 1 March 2015 a new withholding tax on interest was introduced. The withholding tax on interest applies in respect of interest paid by a South African resident to or for the benefit of any foreign person to the extent that the interest is from a South African source. The withholding tax is levied at a final withholding tax rate of 15% of the amount of the interest paid to a foreign person. However, the withholding tax is subject to some exemptions.

The withholding tax on interest rules have deeming provisions and deems interest to be paid on the earlier of the date on which the interest is paid or becomes due and payable.

<u>Reasons for change</u>

In circumstances where interest withholding tax is paid on interest that becomes due and payable, but the interest is subsequently written-off as irrecoverable, there is no mechanism for SARS to refund the interest withholding tax already paid. For example, if a foreign person provides unsecured interest-bearing loan to a South African resident, withholding tax on interest is paid on interest that accrues to that foreign person monthly on the basis that the interest becomes due and payable monthly. The interest is for the purposes of determining the withholding tax on interest liability therefore deemed to have been paid.

It has come to our attention that based on the nature of the debt and the profile of the lenders, a high level of default on interest payments is experienced, with the result that a large portion of the accrued interest is written-off monthly as irrecoverable. Due to the application of the deeming provisions that deem interest to be paid on the earlier of the date on which the interest is paid or becomes due and payable, interest withholding tax is suffered on interest that has not been paid and will never be paid without there being any mechanism available to the foreign person to obtain relief for the withholding tax suffered. This is in contrast to the more equitable approach in respect of income tax where, if the foreign person had been a taxpayer in South Africa, that foreign person would have paid income tax on accrued interest. However, the foreign person would have been able to claim a deduction in terms of section 11(i) of the Act in respect of any irrecoverable interest.

Proposal

In order to provide relief in cases where interest withholding tax is paid on interest that becomes due and payable, but interest is subsequently written-off as irrecoverable, it is proposed that interest that is subject to withholding tax on interest monthly will be interest that accrues to the foreign person in a particular month excluding any interest which becomes irrecoverable in the same month, to the extent that the interest withholding tax was paid in respect of such irrecoverable interest.

Effective date

The proposed amendment will be effective for years of assessment commencing on or after 1 March 2015.

3.32. Adjusting the calculation for high tax exemption in respect of controlled foreign companies

[Applicable provisions: Section 9D(2A) of the Act]

Background

The 2009 tax legislative amendments introduced the CFC high-tax exemption. The purpose of the exemption is to disregard tainted CFC income, if little or no South African tax was at stake after taking into account the South African tax rebates.

The CFC will qualify for the high-tax exemption if it's net income as an aggregate is subject to foreign tax of at least 75% of the amount of normal tax that would have been imposed had that CFC been fully taxed in South

Africa.

The high-tax exemption is based on a calculation of a hypothetical amount of the global level foreign taxes imposed by all foreign spheres of government. The global foreign tax is calculated after disregarding foreign tax carryover and carry-back losses as well as group losses.

Reasons for change

Generally, the income tax does not allow foreign tax rebate on notional taxable income. However, in the calculation of the hypothetical amount of foreign taxes some CFCs within a group of companies that are in a loss making position benefit from the high tax exemption. This creates an anomaly because in these circumstances, no foreign tax is actually paid or payable by the CFC.

Example:

Facts

SA Company, Co A owns all the shares in CFC 1, CFC 2 and CFC3 and CFC 4. All these four CFC's are resident in country Y. CFC 1 generates a loss of $ 100, CFC 2 generates a loss of $ 200, CFC 3 generates income of $ 1500 and CFC 4 generates a loss of $ 5000.

Result in Country Y

Country Y has group taxation provisions and the group of companies gets treated as a single entity for tax purposes, which is referred to as a fiscal unity. The result is that the profit of CFC3 will be offset with the losses of the three CFC's resulting in an overall loss of $ 3800. As a result, the fiscal unity does not get to pay any tax in country Y.

Result in South Africa

In terms of SA tax law, the net income of CFC 3 will be translated to a rand amount in order to be imputed into South African resident, Co A's income. The high tax exemption calculation will then be performed in order to establish as to whether the income is exempt from imputation or not. The actual foreign tax imposed in country Y is at a rate of 25%.

The comparison will be as follows:

Net Income of CFC 3 - $1500 x 15 exchange rate = R22 500

Tax deemed to be payable in county Y - R22 500 x 25% = R5 625

SA Tax payable as if the CFC was a SA resident – R22 500 x 28%= 6300

High tax exemption calculation =R5 625/R6 300 = 89%

Because the 89% is more than the 75% the R22 500 will be exempt from imputation.

The anomaly then arises because CFC 3 did not pay any tax in country Y as a result of the overall group loss. However in performing the high tax exemption, a notional tax of R5 625 is calculated as though the CFC paid tax in its country of resident.

In the absence of the high tax exemption no section 6quat tax rebate would have been granted to the controlled foreign company.

Proposal

In view of the above, it is proposed that the adjustment for foreign group losses be withdrawn in the determination of foreign tax for high tax exemption purposes.

Effective date

The proposed amendments will come into effect on 1 January 2017

3.33. Tax exemption of multilateral development financial institution

[Applicable provisions: New section 10(1)(*bC*) and sections 50A and 50D of the Act]

Background

After 1994, South Africa became a signatory to a number of agreements with multilateral development financial institutions. In this context, a multilateral development financial institution refers to a financial institution created by a group of countries that provides financing and professional advice for the purpose of development.

These institutions have large memberships including both developed donor countries and developing borrower countries. They finance projects in the form of long-term loans at market rates, very-long-term loans (also known as credits) below market rates, and through grants.

Multilateral development institutions provide financial assistance to developing countries in order to promote economic and social development. They primarily fund large infrastructure and other development projects and provide loans tied to policy reforms by the government.

In particular, the multilateral development financial institutions which South Africa has signed agreements with include the following; the World Bank, the International Monetary Fund, the African Development Bank, the European Investment Bank, the African Export-Import Bank and the New Development Bank (formerly known as the BRICS Development Bank). The agreements with these institutions provide for blanket exemptions from all taxes, including income tax, withholding taxes on interest and dividends, value added tax and capital gains tax.

Further, these institutions are also granted diplomatic immunity status in terms of the Diplomatic Immunities and Privileges Act 37, 2001 which gives the Minister of International Relations and Cooperation the power to, *inter alia*, grant immunities and privileges to any organisation recognised by the Minister of the International Relations and Cooperation

<u>Reasons for change</u>

Currently, section 10(1)(*bA*) of the Act makes provision for exemption from income tax in respect of all receipts or accruals of any institution or body established by a foreign government to the extent that that body or institution is appointed by that government to perform its functions in terms of an official development assistance agreement that is binding in terms of section 231(3) of the Constitution of South Africa of South Africa, 1996 (the Constitution). In addition, such official development assistance agreement must provide that the receipts and accruals of that institution or body are exempt from normal tax. This exemption is also extended to apply to multinational organisations providing foreign donor funding in terms of the official development assistance agreement that is binding in terms of the Constitution.

There is a disconnect between the current tax exemption provisions of the Act and the articles dealing with the tax treatment of these multilateral development financial institutions in the agreements signed by South Africa with these institutions. While these agreements provide for exemption of these multilateral development financial institutions from all taxes, the Act does not have a specific provision enabling the tax exemption of these multilateral developmental financial institutions.

Section 10(1)(*bA*) of the Act does not cover these multilateral development financial institutions because the application of the provisions of section 10(1)(*bA*) of the Act is limited only to institutions or bodies appointed by foreign governments to perform functions of such foreign government in South Africa in terms of an official development assistance agreement or to multinational organisation providing foreign donor funding in South Africa in terms of an official assistance development assistance agreement. On the other hand, the agreements signed by South Africa with these multilateral development financial institutions are not regarded as official development assistance agreements, hence they don't qualify for tax exemption in terms of the current provisions of section 10(1)(*bA*) of the Act.

The disconnect between the current tax exemption provisions of the Act and the articles dealing with the tax treatment of these multilateral development financial institutions in the agreements signed by South Africa with these institutions also extends to withholding tax on interest, that was introduced on 1 March 2015. According to these agreements, interest paid by South African residents to these multilateral development financial institutions is exempt from withholding tax on interest; however, the Act does not make specific provision for similar exemption in respect of withholding tax on interest.

Proposal

In order to take into account the spirit of these multilateral development financial institution agreements and in order to eliminate any potential confusion regarding the tax exemption status of these multilateral development financial institutions, the following is proposed:

- The current income tax exemption applicable to institutions or bodies appointed by foreign government to perform functions in South Africa in terms of an official development assistance agreement or to multinational organisations providing foreign donor funding in South Africa in terms of an official assistance development assistance agreement, be extended to apply only to the following multilateral development financial institutions that South Africa has signed agreements with, namely, the World Bank, the International Monetary Fund, the African Development Bank, the European Investment Bank, the African Export-Import Bank and the New Development Bank.
- In view of the fact that the main aim of these multilateral development financial institutions is to provide finance to specified projects in terms of the agreement signed with South Africa, it is proposed that interest paid by South African residents to the multilateral development financial institutions in terms of the agreement should be exempt from withholding tax on interest. The withholding tax on interest exemption will only apply to the following multilateral developmental financial institutions that South Africa has signed agreements with, namely, the World Bank, the International Monetary Fund, the African Development Bank, the European Investment Bank, the African Export-Import Bank and the New Development Bank.

Effective date

With regard to the proposed amendment in respect of income tax exemption on receipts or accruals of the listed multilateral development financial institutions that South Africa has signed agreements with, it is proposed that the amendment will come into effect on the date of promulgation of the Taxation Laws Amendment Act, 2016.

On the other hand, with regard the proposed amendment in respect of withholding tax on interest exemption in respect of interest paid by South African residents to the listed multilateral development financial institutions that South Africa has signed agreements with, it is proposed that the amendment is deemed to have come into operation on 1 March 2015 and applies in respect of income and/or interest that is paid or becomes due and payable on or after that date.

3.34. Clarifying the non-application of the re-organisation rules to deferred exchange gains and losses

[Applicable provisions: Sections 24I(10A) and 41(2) of the Act]

Background

For income tax purposes, gains and losses in respect of exchange items in foreign currency (i.e. a unit of currency, debt, forward exchange contracts and foreign currency option contracts) are governed by special rules. These rules annually account for the unrealised gains and losses in respect of exchange items in the income of the taxpayer. However, specific rules exist for the tax treatment of exchange differences arising from exchange items entered into between related parties. Exchange differences in respect of related-company exchange items are not taken into account in the income of the taxpayer on an annual basis. These exchange differences are deferred until the exchange item is realised (i.e. settled).

Since 2001, the Act has catered for the tax-free transfer of assets through the corporate reorganisation rules. The objective of these rules is to facilitate transactions between companies in the same economic unit by ensuring that the transactions inherent in any restructuring occur on a tax neutral basis. This is achieved mainly by allowing for rollover of the gains and losses that typically arise upon the disposal of assets (i.e. normal tax and capital gains tax). In variably, the potential gains and losses from the disposal of assets are not triggered because the provisions seek to put the transferee in the same shoes as the transferor by deeming them to be one and the same person.

Reasons for change

The specific rules dealing with exchange differences between related parties envisage that any deferred exchange gains or losses will be recognised in the income of a taxpayer when the exchange item to which they relate is realised. However, it has come to Government's attention that when an exchange item is realised through its transfer using the reorganisation rules, the intended trigger for the recognition of the deferred exchange differences may not be achieved when applying the provisions of the reorganisation rules, which deem the transferor and the transferee to be one and the same person.

It was never intended that the exchange differences between related parties should be deferred through the use of the reorganisation rules. This treatment would be in line with that of accrued or incurred interest in respect of debt instruments that are transferred to a transferee under the reorganisation rules. The accrued and incurred amounts of interest are never rolled-over to the transferee. Similar consequences were intended for exchange differences, irrespective of whether they arise in respect of exchange items between related parties or not.

Proposal

It is proposed that the current rules governing deferred exchange gains and losses in respect of exchange items between related parties should not be transferred to transferee companies as a result of the application of the roll-over provisions. This will result in the deferred exchange gains and losses being included in or deducted from the income of the transferor of any exchange item to which they relate on the date that the reorganisation transaction is entered into and the exchange items are realised from the perspective of the transferor.

Effective date

The proposed amendments will come into effect on 1 January 2017 and applies in respect of transactions under Part III of Chapter II of the Act concluded on or after that date.

3.35. VAT – Revision of the 2014 amendment relating to notional input tax on goods containing gold

[Applicable provisions: Section 1(1) of the Value-Added Tax Act of 1991 (VAT Act) – proviso (ii) of the definition of 'second-hand goods']

Background

In 2014, changes were made in the VAT Act to amend the definition of '*second-hand goods'* to specifically exclude 'gold' and 'goods containing gold' from the definition and thereby denying the notional input tax credit on these goods. The policy rationale for the 2014 amendments was to curb fraudulent notional input tax deductions on the acquisition of gold and gold jewellery. The amendment was not intended to have a negative impact on legitimate transactions within the second-hand goods industry.

Reasons for change

Concerns have been raised that the 2014 amendments have led to unintended consequences whereby the notional input tax credit on all goods containing gold is denied to vendors that are dealers in second-hand goods. The denial applies where those goods which were acquired are sold either exactly as they were acquired or with minor modifications to make them suitable for resale in essentially the same state, irrespective of whether the gold content is substantial or negligible.

At issue is, for example, when a second-hand dealer purchases a computer from a non-vendor, based on the 2014 amendments, the notional input tax credit is denied because some of the components in the computer contain an element of gold. Another example is when a second-hand dealer purchases an expensive watch from a non-vendor, the notional input tax credit is denied because the watch contains a certain amount of gold. There is an argument that the value of the gold content on the above-mentioned items, i.e. computer and watch, are insignificant compared to the intrinsic value of the items itself. The values of the computer and watch are to a large extent based on the mechanism, the design and the make which are the main intentions for trading with these items, and not the presence of a small fraction of gold in these items.

<u>Proposal</u>

In order to address the above-mentioned unintended consequences, it is proposed that the 2014 amendments be revised. In this regard it is proposed that, paragraph (ii) of the definition of 'second-hand goods' in section 1(1) of the VAT Act be amended to allow the deduction of the notional input tax credit on goods containing gold, provided that the goods are sold in the same or substantially the same state as when those goods were acquired.

<u>Effective date</u>

The proposed amendments will come into effect from 1 April 2017.

3.36. VAT – Allowing municipal entities to account for VAT on the payment basis where the supply is R100 000

[Applicable provision: Section 15(2A) of the VAT Act]

<u>Background</u>

The VAT Act makes provision for certain persons, including public authorities and municipalities to register and pay VAT on a payments basis. The provisions of the VAT Act require those vendors who are registered on the payments basis to account for VAT on the invoice basis in respect of any supply where the consideration is R100 000 or more. However, only public authorities and municipalities are allowed to deviate from this rule and account for VAT on the payments basis on supplies where the consideration is R100 000 or more.

Reasons for change

Municipal entities (envisaged in section 15(2)(a)(iv) of the VAT Act render services similar to municipalities and are regulated under the Municipal Systems Act and the Municipal Finance Management Act. Therefore, there is no policy rationale not to extend the same dispensation, currently available to public authorities and municipalities, to municipal entities.

Proposal

It is therefore proposed that section 15(2A) of the VAT Act be amended to allow municipal entities, referred to in section 15(2)(a)(iv) of the VAT Act, to account for VAT on the payment basis in respect of any supply where the consideration is R100 000 or more.

Effective date

The proposed amendments will come into effect from 1 April 2017.

3.37. VAT exemption in respect of inported goods that are lost, destroyed or damaged through natural disasters

[Applicable provision: Schedule 1 of the VAT Act]

Background

In terms of Schedule 4 of the Customs and Excise Act, a taxpayer is exempt from paying customs duty and fuel levy (if applicable) on the importation of goods if those goods are subsequently lost, destroyed or damaged through natural disasters or under such circumstances as SARS deems exceptional.

This relief is applicable to circumstances where the customs duty amount and the fuel levy (if applicable) is not less than R2500 on any single occasion while such goods are in any customs and excise warehouse, in any appointed transit shed, under the control of SARS, being removed with deferment of payment of duty, under rebate of duty from a place in South Africa to any other place in terms of the provisions of the Customs and Excise Act or being stored in any rebate storeroom (subject to certain provisos, including that the goods did not enter into home consumption).

<u>Reasons for change</u>

At issue is the fact that the VAT Act does not have an exemption similar to Schedule 4 of the Customs and Excise Act, in respect of goods that are imported, if those goods, after importation and before being entered for home consumption, are lost, destroyed or damaged through natural disasters or under such circumstances as SARS deems exceptional. This creates uncertainty in the interpretation and application of both the provisions of the Customs and Excise and the VAT Acts.

<u>Proposal</u>

In order to remove the ambiguity and provide certainty, it is proposed that Schedule 1 of the VAT Act be aligned to Schedule 4 of the Customs and Excise Act by introducing an exemption from the tax imposed in terms of section 7(1)(b) of the VAT Act, where those goods are lost, destroyed or damaged through natural disasters or under such circumstances as SARS deems exceptional, as contemplated in the Customs And Excise Act, provided that such goods have not yet been entered for home consumption.

<u>Effective date</u>

The proposed amendments will come into effect from 1 April 2017.

4. MEMORANDUM ON THE OBJECT OF THE TAXATION ADMINISTRATION LAWS AMENDMENT BILL, 2016

The Bill proposes to amend amongst other the Income Tax Act, the VAT Act and the Tax Administration Act.

4.1. Income Tax Act - FSB's approval to disclose income tax status

SARS' function to approve a pension fund, pension preservation fund, provident fund, provident preservation fund or retirement annuity fund or the amendments to the rules of these funds were delegated to the Executive Officer of the Financial Services Board ('FSB'), with effect from 1 April 2012, under section 3(5). Accordingly, with effect from 1 April 2012, these funds had to submit all rules and amendments directly to the FSB to be considered for income tax approval.

The FSB publishes a list of all the funds that are registered with the FSB on their website. However, section 70(3)(*b*) of the Tax Administration Act, 2011, only provides that required information, such as the income tax approval status of a pension fund, pension preservation fund, provident fund, provident preservation fund and retirement annuity fund, may be provided to the FSB in order for the FSB to carry out their duties and functions in respect of the regulation and supervision of the Pension Funds Act, 1956, under section 3*(a)* of the Financial Services Board Act, 1990. This section does not give the FSB permission to disclose the information provided by SARS to any third party.

It is recommended that section 69(8) of the Tax Administration Act be amended to specifically allow the FSB to disclose the income tax approval status of a pension fund, pension preservation fund, provident fund, provident preservation fund and retirement annuity fund to a third party. The proposed amendment will allow the FSB to similarly also publish the details of funds approved for income tax purposes on their website.

4.2. Income Tax Act – relieve from filing exempt dividends tax return

Investors receiving dividends from tax-free investments are required to submit an exempt dividends tax return to SARS following the receipt of every dividend payment. The proposed amendment aims to relieve investors from this obligation.

4.3. Income Tax Act – Provisional tax registration of local employees employed by foreing employers

If foreign employers in South Africa do not deduct PAYE, local employees have to pay provisional tax in terms of the Fourth Schedule . Currently there is no provision in the Fourth Schedule which compels the local recruits who earn remuneration to register as provisional taxpayers.

In terms of paragraph *(c)* of the definition of a provisional taxpayer, a person can become a provisional taxpayer upon notification by SARS. A method of ensuring that SARS registers these employees as provisional taxpayers is if SARS was to send letters to the various employers informing them that all local recruits employed by them are regarded as provisional taxpayers. However, notification of the local recruits employed by foreign employers is cumbersome and administratively onerous for SARS. In many cases SARS may not even have some of the personal information of the local recruits on record. This will require SARS to obtain all the necessary information from the employers and thereafter inform the employees that they are provisional taxpayers.

The proposed amendment aims to avoid this administratively onerous task by providing for SARS to notify such persons by public notice that they are provisional taxpayers.

4.4. *Income Tax Act – Inclusion of taxable dividends in 'remuneration'*

Certain dividends received from restricted equity instruments do not qualify for an income tax exemption and are taxable on assessment of the directors and employees. The proposed amendment aims to specifically include these taxable dividends in the definition of 'remuneration' for PAYE in paragraph 1 of the Fourth Schedule.

4.5. *Income Tax Act – Tables to take account of section 6quat rebates*

Paragraph (a): The proposed amendment aims to update the text by removing an obsolete reference. It also clarifies the fact that the deduction tables prescribed by SARS in terms of this paragraph cannot take into account all the rebates claimable by taxpayers, specifically foreign tax credits claimable by employees under section 6*quat*. The proposed provision instead states clearly that the prescribed manner in which these tables are applied should take account of all rebates afforded to taxpayers, including those under section 6*quat*.

4.6. *Income Tax Act – Repeal of directors of private companies' employees' tax provisions*

The proposed amendment repeals the provision for payment of employees' tax (PAYE) by directors of private companies. The provisions of section 7B would apply to the variable remuneration received by the director in that it is deemed to accrue to the director on the date on which it is paid to the director. This is also the date on which the amount of the remuneration becomes claimable as expenditure by the private company.

4.7. Income Tax Act – Nil second provisional tax returns

If an estimate for the second provisional tax period is not submitted before the due date of the subsequent provisional tax payment, the provisional taxpayer is deemed to have submitted an estimate of nil, thereby triggering a penalty under paragraph 20. It is proposed that the window period for submission be closed four months after the end of the relevant year of assessment. Furthermore this deeming provision relates to the submission of an estimate and is therefore moved from paragraph 20 to subparagraph (6) of paragraph 19.

4.8. Income Tax Act – Underpayment provisional tax penalty exclusions remove

The penalty for underpaying provisional tax is based on a percentage of normal tax payable after taking into account rebates and tax already paid. Certain once-off amounts, such as retirement lump-sum and severance-benefit payments, are excluded from the calculation of the penalty because they are taxed separately in terms of special tables and the tax owed is withheld before payment is made. Taxpayers are required to pay provisional tax on the other amounts listed in paragraph *(d)* of the definition of gross income in section 1, because these other amounts are not taxed under the lump-sum tax tables. However, because these amounts are excluded from the penalty calculation, taxpayers are not penalised if they fail to pay the required provisional tax. To correct this, it is proposed that the penalty calculation's exclusion of the amounts in paragraph *(d)* not taxed in terms of the special tables, be removed.

The wording of subparagraph (1) and the rest of paragraph 20 is adjusted to provide greater clarity.

4.9. Value-Added Tax Act – defective input tax documents

The Value-Added Tax Act places a statutory obligation on vendors to issue documents in a defined form and manner. These requirements are attuned to commercial and accounting practice and ensure a seamless audit trail. Recipient vendors are occasionally issued with defective documents or are unable to obtain documents from supplying vendors, resulting in an inability to make input tax deductions.

With effect from 1 April 2015, section 25 of the Tax Administration Laws Amendment Act, 2015, introduced section 16(2)*(g)* in the Value-Added Tax Act to provide relief to recipient vendors in these situations. The current amendment provides clarity with regard to the considerations that SARS will take into account for accepting alternative documentary proof. It is important to note that vendors can only access this relief as a last resort. Vendors must still be able to demonstrate that a sincere effort has been put into obtaining the proper documents and maintain proof of those efforts. Furthermore, vendors would have to make an application for a ruling and only if and when that ruling is issued, may the amount be deducted as input tax at that later stage. Lastly, invoking this provision will not allow vendors to backdate the claim to a past tax period that has already been closed.

4.10. Value-Added Tax Act – Input tax deduction in tax period of time of supply and refund claim within five years

A person may deduct an amount from output tax attributable to a later tax period, provided this later period falls within five years from the date of certain events, for example, the date a tax invoice should have been issued. It is proposed that an input tax deduction be limited in certain instances to the tax period in which the time of supply occurred. In addition, it is proposed that the time limit for the payment of refunds be clarified in that a claim for the refund must be received by SARS within five years after the date upon which the payment of the amount claimed to be refundable was made.

4.11. Tax Administration Act – Legal practitioners' independence

The proposed amendment aims to address uncertainty that has arisen in this regard in practice. A legal practitioner briefed to present SARS in legal matters, in particular advocates, must advise and assist SARS with the required degree of independence and does not, in doing so, carry out the provisions of a tax Act under the control, direction or supervision of SARS.

4.12. Tax Administration Act – Legal costs recovered to SARS

Legal costs recovered by the state attorney on behalf of SARS are paid directly to SARS, not to the National Revenue Fund. The proposed amendment provides that all legal costs recovered by the state attorney on behalf of SARS must be paid to the National Revenue Fund.

4.13. Tax Administration Act – Enhance independence of Tax Ombud

The proposed amendment aims to enhance the independence of the Tax Ombud by extending his or her tenure.

4.14. Tax Administration Act – Tax Ombud's budget to be approved by Minister

The proposed amendment aims to enhance the independence of the Tax Ombud in respect of the appointment of the staff of the Office of the Tax Ombud. In addition, an amendment is proposed that although the expenditure connected with the functions of the office of the Tax Ombud is paid out of the funds of SARS, it is subject to a budget for the office approved by the Minister.

4.15. Tax Administration Act – Extention of mandate of Tax Ombud

The proposed amendment aims to extend the mandate of the Tax Ombud to include the investigation and review, at the request of the Minister, of any systemic issue related to a service matter; the application of the provisions of the Tax

Administration Act; or procedural or administrative provisions of a tax Act, as defined in the aforesaid Act.

4.16. Tax Administration Act – Enhance effectiveness of Tax Ombud

The proposed amendment aims to enhance the effectiveness of the Tax Ombud's recommendations. If SARS or the taxpayer does not accept them, reasons must be provided. This will ensure that the Tax Ombud is able to review the reasonableness of the reasons to inform future action.

4.17. Tax Administration Act – Clarify 'record' of assessment

The proposed amendment aims to clarify that the 'record' of an assessment includes the return and the supporting documents thereof where provided to SARS for purposes of a verification or audit. It would be nonsensical to only destroy the assessment and not the supporting documents which generally constitute the more voluminous part of the 'record' of an assessment. The period of 5 years is extended to 7 years to align it with section 99(3), and additional grounds where a further period may be required are added.

4.18. Tax Administration Act – Clarity to exceptional circumstances

The general principle is that finality of a dispute must be achieved, i.e. the resolution of a dispute in respect of the issues in dispute and the relevant tax period must be final. If not, the right to object and appeal will become nugatory. The amendment clarifies that only in exceptional circumstances should SARS be allowed to 'reopen' the tax period, audit and issue an additional assessment *after prescription*. Prior to the expiry of the periods listed in section 99(1), where the factors listed in section 99(2) are absent, SARS may still issue an additional assessment to comply with its statutory duties to ensure payment of the correct amount of tax in respect of the tax period that was under dispute within the normal expiry period for that tax period.

4.19. Tax Administration Act – Extension of objection periods

The current period for lodging an objection is 30 business days from the date of assessment. This has been shown to be too short in practice, particularly in complex matters, resulting in a large number of applications for condonation. A longer period for lodging an objection will be proposed which will be effected in the dispute resolution rules issued under section 103 of the Act. It is proposed that condonation of a late objection not based on exceptional circumstances may be extended by SARS for a period up to 30 days, but if there are exceptional circumstances this period may be further extended by SARS. The maximum period within which a late objection may be extended remains three years.

4.20. Tax Administration Act – Tax Court's commercial members

Currently section 118 provides that if a tax appeal relates to the business of mining, the commercial member must be a registered engineer with experience in that field, or a sworn appraiser if it involves the valuation of assets. Because other matters of a technical nature may also require a commercial member with expertise in the relevant field, it is proposed that an amendment be considered to include a more generic provision for this purpose. The proposed amendment gives effect to this proposal.

4.21. Tax Administration Act – Understatement penalty for GAAR

Amendments to the understatement penalty regime to enhance clarity with regard to whether and the extent to which understatement penalties are imposable in

GAAR matters pursuant to recent contentions in this regard, are proposed. Under the additional tax penalty regime, the predecessor to the understatement penalty regime, case law supported the imposition of such penalties in GAAR matters. The amendments will clarify that this prevails in respect of understatement penalties, which is also in line with international law. In addition, to provide clarity as to what would be the appropriate penalty in GAAR matters, it is proposed that a new behavioural category is inserted in the understatement penalty table.

4.22. Tax Administration Act – VDP in the case of pending audit or investigation

A person who is aware of a pending audit or investigation may not apply for voluntary disclosure relief. The proposed amendment aims to clarify what is meant by a pending audit or investigation.

5. CASE LAW

5.1. C:SARS v Kluh Investments (Pty) Ltd

The Thesen Group of companies owned property in Knysna on which they conducted forestry, timber-growing and a plywood manufacturing business.

During May 2001, Steinhoff Southern Cape (Pty) Ltd ('Steinhoff') concluded written agreements with Thesen Company (Pty) Ltd and Thesen Properties (Pty) Ltd (collectively referred to as 'Thesen') in terms of which the former or its nominee, as purchaser, agreed to acquire for the total purchase price of R45 million, all of the assets and the business as a going concern of the latter, including the land and the plantation with which this case was concerned.

However, the board of Steinhoff's ultimate holding company blocked the acquisition of the land and plantation, because it was at that time their policy not to acquire fixed property in South Africa. As a result, as it was put in the evidence, Steinhoff had to then 'find somebody to own the land.' In the event, agreement was reached that Steinhoff would purchase Thesen's machinery and equipment, including the latter's sawmill for R15 786 881, and the Respondent, Kluh Investments (Pty) Ltd ('Kluh'), a special purpose subsidiary of a Swiss company, Fihag Finanz und Handels AG ('Fihag'), would acquire the remaining assets for R29,5 million.

Thesen agreed to the cancellation of the May 2001 agreements and, although an oral agreement had been reached between the parties by June 2001, substitute agreements were only executed during October of that year. On 29 June 2001, Kluh took possession of the plantation and the land.

In terms of the written agreement executed on 3 October 2001, the purchase price of R29,5 million was apportioned as follows: R11 596 121 to the plantation; R12 528 459 to the land; and the balance to other assets.

Kluh retained the land and plantation but onsold the other assets, including an erf, the plywood business and certain trademarks to third parties.

By the beginning of 2003, prompted in part by escalating timber prices and the scarcity of plantation resources, Steinhoff had a change of heart and it arrived at the conclusion that it would be desirable to acquire the plantation and land that Kluh had purchased from Thesen during 2001.

In the result, on 21 February 2003, Steinhoff and KLuh concluded a written agreement of sale but certain disputes had arisen between the parties flowing from that agreement and those were resolved by way of a settlement agreement concluded on 29 July 2004. In terms of that settlement agreement, which had a new effective date of 1 June 2004, the 'final purchase price' of the combined assets was agreed at R159,7 million, of which R144,7 million was in respect of 'the plantation.'

SARS had assessed Kluh to tax on the basis that the proceeds of that sale formed part of its gross income by virtue of section 26(1) of the Income Tax Act read with par. 14(1) of the First Schedule thereto.

The Cape Tax Court (see *ITC 1869* (2013) 75 SATC 329) *per* Davis J had agreed with SARS and had accordingly dismissed Kluh's appeal to it and ordered that 'the initial assessment be amended by the addition of an amount of R12 million by virtue of section 129(*b*) of the Tax Administration Act.'

The court *a quo*, being the full court of the then Western Cape Division of the High

Court, Cape Town, (see *Kluh Investments (Pty) Ltd* v *C: SARS* 77 SATC 23) *per* Rogers J, Traverso DJP and Allie J concurring, in overturning the decision of the Tax Court, held that the proceeds of the sale were not gross income in terms of section 26(1) of the Act.

SARS then appealed to the Supreme Court of Appeal with its leave.

Section 26(1) of the Income Tax Actprovided at the relevant time:

'26. *Determination of taxable income derived from farming*.

(1) The taxable income of any person carrying on pastoral, agricultural or other farming operations shall, in so far as it is derived from such operations, be determined in accordance with the provisions of this Act but subject to the provisions of the First Schedule.'

Paragraph 14(1) of the First Schedule to the Act provided at the relevant time:

'14(1) Any amount received by or accrued to a farmer in respect of the disposal of any plantation shall, whether such plantation is disposed of separately or with the land on which it is growing, be deemed not to be a receipt or accrual of a capital nature and shall form part of such farmer's gross income.'

The primary issue in this appeal was whether Kluh was 'carrying on farming operations' as contemplated by section 26(1) of the Income Tax Act.

The evidence had revealed that Steinhoff had initially purchased the plantation itself, with the intention of carrying on its own farming operations thereon but was not permitted to proceed with this agreement because the board of its ultimate holding company prevented it from owning the land, due to the Group's then policy not to own land in South Africa. Steinhoff thus acquired from Thesen, independently of the Respondent, all the equipment and the personnel required to carry on farming operations on the plantation. When Thesen disposed of the plantation Kluh in 2001, it was already a mature plantation in rotation.

The plantation, which had been well managed by Thesen, had reached the stage where it could annually yield a steady and sufficient number of mature trees for commercial felling, with younger trees taking their place year by year.

Steinhoff, which owned the equipment necessary for conducting the plantation operations and had employed the employees who worked on the plantation, was entitled to harvest the timber for its own account.

Kluh had owned no equipment and had no employees and all operational income and expenditure were earned and incurred by Steinhoff and reflected in its accounts.

Hence, Kluh's financial records and financial statements for the period between the acquisition and the disposal of the plantation reflected no operational income and expenditure.

The oral arrangement between Kluh and Steinhoff was for an indefinite duration and, due to the Steinhoff group policy in 2001 not to own land in South Africa, it was expected to endure for a lengthy period although either party could obviously have terminated the arrangement on reasonable notice.

On termination of the arrangement, the plantation would comprise trees of the same volume and quality as at the commencement and this meant that Steinhoff, in conducting the plantation operations, had to keep the plantation in rotation and perform such other pruning, thinning and maintenance as would ensure that, upon termination, it could restore the plantation as in its June 2001 state.

Steinhoff was required to manage the plantation using best practice so that, what was described as, Forest Stewardship Council certification could be obtained, thereby ensuring that the timber would qualify for export to Europe.

Steinhoff, which was responsible for fire protection, had insured the plantation against fire in the light of its obligation to restore the plantation to Kluh at the end of the arrangement.

Judge Ponnan held the following:

(i) That the primary issue in this appeal was whether Kluh was ‘carrying on farming operations’ as contemplated by section 26(1) of the Income Tax Act. Both the Tax Court and the full court approached the enquiry on the basis that the ‘critical’ or ‘important’ facts for the purposes of answering the question whether Kluh was carrying on farming operations were common cause, but on those common cause facts they had reached starkly contradictory conclusions.

(ii) That the term ‘farming operations’ in section 26(1) of the Act shall, insofar as the taxable income of any person is derived from such operations, be determined in accordance with the provisions of the Act, but subject to the provisions of the First Schedule thereto and the First Schedule is concerned with the ‘Computation of Taxable Income from Pastoral, Agricultural or other Farming Operations’ and it deals in detail with how taxable income derived from farming operations is to be computed.

(iii) That there was no definition of ‘farming operations’ in the Income Tax Act and whether or not a person's economic activity constituted farming operations was essentially a question of fact. The full court thus correctly held that ‘the questions whether a person is carrying on farming operations and whether particular income has been derived from farming operations are questions of fact.’

(iv) That the approach of the full court conduces to confusion. As Innes CJ put it in *CIR* v *George Forest Timber Co Ltd* 1924 AD 516: ‘It is dangerous in income tax cases to depart from the actual facts; the true course is to take the facts as they stand and apply the provisions of the statute.’

(iv) That on an evaluation of the facts as presented Kluh had derived no income from the actual day-to-day plantation farming operations and had incurred no corresponding day-to-day expenditure. Thus, from the very beginning, Kluh wanted nothing to do with any farming operations. Quite apart from the fact that it had neither the appetite for the risks associated with farming nor the requisite skills, equipment and personnel to undertake farming operations, the whole *raison d’être* of Kluh's involvement was to acquire bare ownership of the land and the plantation, which Steinhoff was prevented from doing. That being so, it was hardly surprising that the full court had answered, what it described as the ‘threshold enquiry’ as follows: ‘. . . the appellant did not even start to conduct plantation operations. From the outset the appellant made the plantation available to Steinhoff so that the latter could conduct plantation operations for its own profit and loss.’ That conclusion, ought, ordinarily at any rate, to have been dispositive of the primary enquiry in the matter.

(vi) That the further branches of SARS' argument must be considered,. SARS contends that:

- The purpose of par. 14(1) of the First Schedule to the Act was to extend tax liability by treating the proceeds of the disposal of a plantation as gross income;
- The mere disposal of a plantation by its owner constituted the conduct of farming operations for purposes of section 26(1), irrespective of the extent to which the owner was involved in the actual conduct of farming operations prior to or separately from such disposal;
- The farming operations were conducted by Steinhoff 'on behalf of Kluh.'

(vii) That par. 14(1) of the First Schedule is a deeming provision which, on its own wording, only applies to a farmer in respect of such farmer's gross income. 'A farmer' in that provision is clearly a short-hand for a person carrying on farming operations as contemplated in section 26(1) of the Act. Carrying on 'farming operations' as contemplated in section 26(1), is clearly the necessary prerequisite that triggers the applicability of the whole of the First Schedule, including the deeming provision in par. 14(1). It must follow that the deeming provision itself cannot be employed to determine whether or not a taxpayer is 'a farmer' or differently put 'a person carrying on farming operations.' Accordingly, the content of the deeming provision in par. 14(1), namely that 'any amount . . . shall . . . be deemed not to be of a capital nature and shall form part of such farmer's gross income', is the consequence of carrying on farming operations, and cannot itself be determinative of whether a person is or is not carrying on farming operations *i.e.* whether a person is 'a farmer' as contemplated in par. 14(1).

(viii) That, in short, the deeming provision in par. 14(1), on its plain wording, only applies to farmers, and logically one cannot use the deeming provision itself to determine who is and who is not a farmer. It must follow that the first contention advanced SARS is fallacious because one cannot use a deeming provision that only applies if Kluh is a farmer to determine whether

Kluh is a farmer.

(ix) That, to say, as SARS does, that the purpose of par. 14(1) is to extend tax liability by including the proceeds of the disposal of a plantation in gross income may well be misleading. The general rule was that section 26(1) and the First Schedule to the Act did not apply unless the taxpayer was carrying on farming operations. SARS suggested that reading section 26(1) and par. 14(1) together, the proceeds of the disposal of a plantation must constitute income derived from farming operations, otherwise they would not be 'captured by section 26(1).' SARS thus asserts that: 'the act of disposing of a plantation in its entirety is itself recognised by the Act as a farming operation. It must follow that in so doing, the owner is at that very moment 'carrying on farming operations', in accordance with section 26(1), irrespective of what else he or she has done in relation to the plantation. However, par. 14(1) only applies where 'farming operations' as contemplated in section 26(1) are carried on. Paragraph 14(1) then deems the proceeds of the disposal of a plantation not to be of a capital nature and requires such proceeds to be included in the farmer's gross income. It does not cause any proceeds to be 'captured by section 26(1)' as contended by the Appellant. Paragraph 14(1) recognises that the disposal of a plantation is not *per se* a farming operation.

(x) That even where the taxpayer is a farmer, par. 14(1) contemplates that the proceeds of the disposal of a plantation are in fact of a capital nature. This is why a farmer's proceeds from the disposal of a plantation are deemed not to be of a capital nature and are required to be included in the farmer's gross income in terms of par. 14(1). Such proceeds are not 'captured by section 26(1)', as suggested by SARS, but simply included in the farmer's gross income in terms of par. 14(1). It may be so that section 26(1) brings the deeming provision in par. 14(1) into operation, but it is wrong to say that the mere disposal of a plantation is therefore recognised as a farming operation. The presence or absence of what is signified by the 'carrying on of farming operations' as contemplated in section 26(1), and by the words 'a farmer' and 'such farmer's' in par. 14(1), must therefore be determined without placing any reliance on the deeming provision in par. 14(1). SARS was constrained to concede that its argument would only be tenable if the court were to substitute the word 'taxpayer' for that of 'farmer' in par. 14(1) and that could not be done.

(xi) That, moreover, par. 14(1), triggered by section 26(1), recognised that the proceeds of the disposal of a plantation were in fact of a capital nature, but only in the case of a farmer. If such proceeds were in fact not of a capital nature there would be no need for the deeming provision and indeed for par. 14(1).

(xii) That even if Steinhoff in some sense had acted on behalf of Kluh, that would not make Kluh a farmer as contemplated in par. 14(1). On the facts, Kluh did not have the right to the yield of the plantation – it had granted this right to Steinhoff for the duration of the agreement. Kluh also did not have the use of the land and the plantation, which right it once again had granted to Steinhoff for the duration of the agreement between them. Kluh did not derive any income from the land and the plantation, the use of which it had granted to Steinhoff to farm for its own benefit, on its own behalf, and for its own account. Thus, the only entity which could be regarded as a 'farmer' as contemplated in par. 14(1) in relation to the plantation owned by Kluh, was Steinhoff.

Appeal, accordingly, dismissed with costs.

5.2. New Adventure Shelf 122 (Pty) Ltd v C:SARS

New Adventure had purchased the immovable property concerned in 1999 for a purchase price of R185 000.

By virtue of the 'valuation date' for capital gains tax ('CGT') purposes having been fixed in terms of the Eighth Schedule to the Income Tax Act as 1 October 2001, the property was a 'pre-valuation date asset' as defined in par. 1 of the Eighth Schedule.

New Adventure, on 20 September 2006, had concluded a written agreement of sale in terms of which the property was sold by it to a third party for the sum of

R17 720 000. Despite an initial contention by New Adventure that the agreement had been subject to certain (unrecorded) suspensive conditions, it was accepted at the hearing that this had not been so and, accordingly, the date of the disposal of the property for the purpose of the determination of New Adventure 's capital gain or capital loss was 20 September 2006 and the date of disposal fell within the Appellant's 2007 year of assessment.

The sale agreement provided for the payment by the purchaser of a deposit in the sum of R1 200 000, which was recorded as having been paid on 30 November 2005. A further payment of R1 million was payable against transfer of the property into the purchaser's name, with the balance of R15 520 000 being payable thereafter in four instalments as specified.

The property was transferred to the purchaser in late 2006 against the registration of a mortgage bond over the property in favour of New Adventure as security for the payment of the outstanding balance of the purchase price. By reason of an advance payment on the balance of the purchase price made during New Adventure's 2007 year of assessment, the purchaser became contractually entitled to a rebate of R840 000.

The disposal of the property was duly accounted for in New Adventure 's return of income for the 2007 tax period.

New Adventure , on 1 August 2008, was issued with an income tax assessment in respect of the 2007 tax year in which the capital gain arising from the disposal of the property was determined as R9 746 875, and the capital gains tax thereon, levied as income tax, was assessed in the sum of R1 413 006, 73.

New Adventure raised no objection to the assessment within the prescribed period and in terms of section 81(5) of the Income Tax Act, which was then still in force, the assessment therefore became ‘final and conclusive.’

New Adventure had failed to pay the assessed tax and payment thereof had still not been made as at the date of the hearing of this application in February 2016.

New Adventure and the purchaser of the property had, on 18 November 2011, during the 2012 tax year, concluded an agreement in terms of which the sale of the property was cancelled because of difficulties being experienced by the purchaser in being able to proceed with the intended development of the property. The cancellation agreement provided that the property would be transferred back into New Adventure 's name and that New Adventure would retain the amount already paid by the purchaser in reduction of the purchase price as pre-estimated damages. The amount thus retained by New Adventure was R4 549 082. The mortgage bond in favour of New Adventure obviously also fell to be cancelled when it resumed registered ownership of the property.

The property was transferred back into New Adventure 's name on 19 April 2012.

New Adventure, on 12 March 2012, notwithstanding that the prescribed period for objection to the assessment had long expired, purported to file a notice of objection to the 2007 assessment of capital gains tax on the sale of the property. The grounds stated by New Adventure for disputing the assessment went as follows 'Sale was cancelled. No capital gains tax was paid. Assessment needs to be withdrawn.'

New Adventure was advised by letter dated 22 May 2012 that the objection could not be entertained as section 79A(2) of the Income Tax Act imposed a three-year time limit from the date of assessment on the exercise of the power conferred on SARS in terms of section 79A(1) and that limit had been exceeded by the time the cancellation agreement was concluded and the purported 'objection' to the assessment was raised.

New Adventure, on 12 February 2014, purported to submit another objection to the assessment which would seem that the second 'objection' was in point of fact an application by New Adventure for SARS to withdraw its 2007 assessment in terms of section 98(1)(*d*) of the Tax Administration Act.

SARS rejected the application on the grounds that section 99(1)(*a*) of the Tax Administration Act prohibited it from issuing an amended assessment more than three years after the date of assessment of an original assessment. It also reiterated that in the absence of a timeous objection, the issued assessment fell to be regarded as final. SARS also contended that in any event none of the conditions prescribed in terms of section 98(1)(*d*)(i) of the Tax Administration Act was applicable on the facts of the case.

On 3 July 2014 the dispute was referred to the Tax Ombud by New Adventure's attorneys and they requested the Tax Ombud to recommend to SARS that it withdraw the assessment and give effect to one or more alternative remedies that would reduce the proceeds in accordance with par. 35(3)(*c*) of the Eighth Schedule, but the Ombud did not have the authority to make any determinative decision.

New Adventure's attorneys then unsuccessfully approached the Legal Delivery Unit of SARS and subsequently the matter was referred for consideration by an 'internal committee' at SARS and by letter dated 28 October 2014 New Adventure's attorneys were advised that the committee had resolved to confirm SARS' position on the non-availability of any remedy in terms of section 98 of the Tax Administration Act.

New Adventure was also advised of SARS' view that par. 35(3)(*c*) of the Eighth Schedule to the Act, upon which New Adventure sought to rely, found no scope for application on the facts. The latter position was reiterated in a further letter from SARS to New Adventure's attorneys dated 26 January 2015. In that letter SARS explained that the downward adjustment in the computation of the proceeds of the disposal of an asset provided in terms of par. 35(3)(*c*) of the Eighth Schedule did 'not allow for an adjustment to be made to a capital gain in the year it arose by an event that occurred in a subsequent year of assessment.'

On 12 February 2015 the Tax Ombud wrote to New Adventure's attorney stating that 'Your matter is now regarded as finalised by this office.'

New Adventure, on 14 April 2015, gave notice, as required in terms of section 11(4) of the Tax Administration Act, of its intention to institute the current proceedings by approaching the High Court for relief, and an application for a review in terms of the Promotion of Administrative Justice Act 3 of 2000 ('PAJA') was commenced on 21 April 2015.

The application for review had been sought in terms of section 6 of the PAJA.

Section 105 of the Tax Administration Act made it clear that a taxpayer may not dispute an assessment except in proceedings in terms of chapter 9 of that Act, i.e. objection or appeal, 'or by application to the High Court for review.'

Pivotal to the effective relief sought by New Adventure was the review and setting aside of the following decisions:

- The assessment for the 2007 tax period;
- SARS' decision to refuse to condone the late filing of the Appellant's objection to the assessment and his decision to disallow the Appellant's objection to the assessment;
- SARS' decision to decline to withdraw the assessment in terms of section 98 of the Tax Administration Act 28 of 2011; and
- SARS' decision to decline to reduce the proceeds of the disposal in terms of par. 35(3)(c) of the Eighth Schedule to the Act.

New Adventure had also applied for an order remitting the matter for reconsideration by SARS as contemplated in section 8(1)(*c*)(i) of the Promotion of Administrative Justice Act.

This matter concerned how a capital gain accrued as a result of the disposal of an asset in a particular year of assessment fell to be treated for capital gains tax purposes when the contract in terms of which the asset was sold is cancelled during a subsequent tax period, with the effect that the taxpayer does not realise the full proceeds of the disposal that had been taken into account in assessing its taxable income in the year that the asset was disposed of.

It was ultimately common cause between the parties that on the facts of the current case the relevant provisions of the Eighth Schedule deem the date of the disposal to have been the date upon which the contract was concluded and that the proceeds are deemed to have accrued to the taxpayer and fall to be accounted for income tax purposes in the year in which the disposal occurs, even if the proceeds actually fall to be received after that year.

New Adventure contended, in essence, that in the circumstances its income tax assessment for the 2007 tax period should be reopened, and that a reassessment of its taxable income in that year of assessment should be undertaken with regard to the amount of the proceeds actually received and retained by it in the context of the cancellation of the contract and New Adventure relied in this regard on what it contended was the effect of the provisions of par. 35(3)(*c*) of the Eighth Schedule to the Act.

SARS rejected the validity of the approach contended for by New Adventure as he was of the view that it would be contrary to basic principle to reopen what had been an admittedly correct and unimpeachable assessment of taxable income for a particular tax period on the basis of an event that occurs in a subsequent tax period.

SARS contended further that the effect of the cancellation of the sale fell to be addressed in the determination of New Adventure's aggregate capital gain or loss in the 2012 tax year after a redetermination, in 2012, of the capital gain or loss from the disposal of the asset in 2007, as provided in terms of par. 25(2)(*b*) and (3) of the Eighth Schedule.

Judge Binns-Ward held the following:

<u>As to the court's jurisdiction to entertain the application for review</u>

(i) That section 7(1) of PAJA prescribes that review proceedings in terms of section 6 of the Act must be brought without unreasonable delay and not later than 180-days after the date on which any proceedings instituted in terms of internal remedies have been concluded; or where no such remedies exist, the date on which the person concerned was informed of the administrative action, became aware of the action and the reasons for it, or might reasonably have been expected to have become aware of the action and the reasons for it. If an application for review under PAJA is brought outside the 180-day period stipulated in section 7(1) a court was only empowered to entertain it if the interest of justice dictates an extension in terms of section 9 of the Act. The bar to the court's ability to entertain a review application brought in terms of PAJA out of time operates as a matter of law and applies irrespective of the failure by a Respondent to rely on it. Section 9 of PAJA allows for the court, on application, to extend the period in terms of section 7(1) if the interests of justice so require and it also permits the parties to extend the period by agreement.

(ii) That New Adventure alleged that the application had been brought within the 180-day limit but the court was not satisfied that that was so. New

Adventure did not identify the basis for its allegation that the 180-day limit had not been surpassed and it was therefore not evident on the papers when it contended that the 180-day period would have commenced in the context of the facts described above. In oral argument New Adventure submitted that the PAJA clock had started ticking only when the Tax Ombud directed the abovementioned letter of 12 February 2015 advising that the matter was regarded as finalised.

(iii) That internal remedies within the meaning of section 7 of PAJA are the defined and identifiable remedies that were available to New Adventure for review when the basis for the complaint about the administrative action in issue, including the administrator's reasons for it, first arose or reasonably should have become known to New Adventure. Assuming in New Adventure's favour, without so finding, that notwithstanding the expiry in 2011 of the three-year limit for the re-opening of its assessment, the 180-day period provided in terms of section 7(1) of PAJA, commenced to run on or about 22 May 2012, it was required to have instituted review proceedings by no later than a date sometime in late November 2012.

(iv) That, confronted with this position, New Adventure applied orally from the bar for the necessary extension of time and that raised the question whether an application in that form and at that stage of the proceedings was permissible. Section 9 does not prescribe any particular form of procedure and applications to the High Court are, however, generally regulated in terms of rule 6. Moreover, the decision whether or not to grant an application for an extension of time in terms of section 9 of PAJA entails the exercise by the court of a broad discretion in the light of all relevant facts.

(iv) That in the circumstances there was not an absolute bar to the court entertaining the application moved orally by New Adventure's counsel. It was not desirable that applications of this nature be brought informally in the manner that happened but if the manner in which the application is brought does not occasion the other litigant(section) involved in the case substantial injustice it would be counterintuitive to the promotion of constitutional values for a court to decline to consider it on its merits on purely procedural grounds.

(v) That however, the apparent reason for the failure to bring the application in proper form would, nevertheless, be one of the considerations to be taken into account in deciding whether the interests of justice would be served by granting it. Moreover, the court did not detect indications of any areas in which SARS might have been substantially prejudiced as a consequence of not having had the opportunity to deal with the application on paper and for all these reasons the court had decided to entertain New Adventure's belated application in terms of section 9 of PAJA.

(vi) That, however, after the hearing and before the court's judgment had been finalised, New Adventure delivered a written application in terms of section 9, together with a set of written submissions in support of it and SARS had indicated that he did not object to the late application and did not intend to oppose it. By virtue of the requirements of ss 7 and 9 of PAJA, it still remained, however, for the court to determine whether it was in the interest of justice to entertain the review.

(vii) That it did not appear that the delay had been prejudicial and no third party rights were affected and SARS had been content to engage internally with New Adventure concerning the merits of its various contentions over a period of several years. The institution of the application occurred reasonably expeditiously after the Tax Ombud's indication that he was closing his file. The issue involved raised important and difficult questions of statutory interpretation concerning capital gains tax and a judicial determination on their import would, in principle, conduce to certainty, which would be in the public interest. In this respect it weighed with the court that SARS' responses to New Adventure's complaints did not provide the sort of guidance that one might have expected had there been a clear understanding of the legislation.

(ix) That it was not SARS' duty to proactively advise the taxpayer how to deal with the issue of the reduction in the proceeds of disposal in a subsequent tax period, but having regard to the basic values and principles governing public administration in terms of section 195(1) of the Constitution, one would have expected SARS' response to New Adventure's purported objection in 2012 to have been along the lines of the argument advanced by their counsel in these proceedings had there been a clear understanding by its officials of the import of the relevant legislation. SARS' responses to New Adventure were not as enlightening as they ideally should have been.

(x) That, in all the circumstances, it would be in the interests of justice to entertain the review application out of time notwithstanding, as will become apparent, the court's adverse opinion as to its merits and hence the late institution of the review application is condoned in terms of section 9 of PAJA.

As to the merits of the review application

(xi) That the merits of the review application turn on the application and proper construction of the pertinent provisions of the Eighth Schedule to the Income Tax Act 58 of 1962. The approach contended for by New Adventure would require an amendment of its 2007 tax assessment in consequence of an event that occurred in a subsequent tax year. It is common cause that there was nothing objectionable about the 2007 assessment when it was issued as it correctly reflected the amount of New Adventure's capital gain on the disposal and the amount that consequently fell to be included in New Adventure's taxable income for that year in terms of section 26A of the Income Tax Act.

(xii) That while there were valid bases to distinguish the nature of income tax and capital gains tax, there was no getting away from the fact that section 26A of the Income Tax Act drew them together in requiring the taxable capital gain of that person for that year of assessment to be included in the taxable income of a person for a year of assessment. The provisions of section 26A of the Income Tax Act militated strongly against the validity of the basis upon which New Adventure's counsel sought to distinguish the principle highlighted by SARS' counsel. SARS emphasised the well recognised principle that income tax is an annual fiscal event. The application of the principle that is evident in the wording of section 26A is carried through in the relevant provisions of the Eighth Schedule and it was, of course, the effect of the relevant provisions of the Schedule, rather than the principle, that is determinant, but the court was in agreement with SARS that being mindful of the principle can afford some assurance in resolving any difficulties encountered in construing the applicable provisions and the principle of finality that infuses our tax legislation is similarly a relevant consideration.

(xiii) That it was sufficient to state that a capital gain or loss fell to be determined with reference to a year of assessment. Ordinarily, the calculation will fall to be undertaken in terms of sub-par. (*a*) of par. 3 in respect of capital gains and in terms of sub-par. (*a*) of par. 4 in respect of capital losses in respect of the year of assessment in which the asset in question is disposed of. In that event the capital gain is equal to the amount by which the proceeds received or accrued in respect of the disposal exceed the base cost of the asset and, in the case of a capital loss, the amount by which the base cost of the asset exceeds the proceeds.

(xiv) That Part V of the Eighth Schedule sets out the various methods by which the base cost of an asset may be calculated. It was common cause in the current matter, which it will be recalled involved a 'pre-valuation date asset', that the time-apportionment base cost calculation method provided in terms of par. 30 was used by New Adventure for the purposes of its return in the 2007 tax year, being the year in which the disposal of the asset occurred.

(xv) That the bases upon which the amount of the proceeds of a disposal of an asset fell to be calculated were set out in Part VI of the Eighth Schedule. It was common ground that the general provisions set out in par. 35 of the Eighth Schedule were applicable in the current case. Paragraph 35(1) provided that the proceeds from the disposal of an asset by a person are equal to the amount received by or accrued to, that person in respect of that disposal.

(xvi) That it was also common cause that the provisions of par. 25 of the Eighth Schedule became applicable when New Adventure became no longer entitled, as a consequence of the cancellation of the contract, to part of the proceeds that had been taken into account in calculating its capital gain in the 2007 year of assessment.

(xvii) That New Adventure submitted that the redetermination that fell to be undertaken in terms of par. 25(2) and (3) of the Eighth Schedule was substitutive in character and effect; that is that it replaced the determination done in 2007, which, according to the argument, was notionally expunged, with the redetermined capital gain or loss, as the case might be, being substituted in its place. It was the effect thus contended for that underpinned New Adventure's claim for the amendment of its 2007 tax assessment. The basis for the argument was what New Adventure submitted was the effect of par. 35(3)(*c*) of the Eighth Schedule. It contended that the reduction in the proceeds which was required by par. 35(3)(*c*) had an *ex post facto* effect on the original computation of the proceeds for application in the capital gain calculation.

(xviii) That New Adventure's argument found no support in the wording of par. 25(2) and (3) of the Eighth Schedule. On the facts of the case the 'current year of assessment' within the meaning of par. 25(2) is the 2012 year of assessment. It was also clear from the context that the terms 'current year of assessment' and 'current year' were synonymous. It was plain that the rationale for the required redetermination, triggered by an event of the sort referred to in par. 25(2)(*b*), was to give effect to the generally applicable requirement of par. 35(3)(*c*). It was expressly evident that the object of the redetermination that it was common cause must be carried out was not to redetermine or amend the determination of a capital gain or loss in a previous year of assessment (2007), but to provide a basis for the result of the redetermination to be taken into account for capital gains tax purposes in the current year (2012). The way in which that fell to be done was, as indicated in par. 25(3), 'as contemplated in par. 3(*b*)(iii) or 4(*b*)(iii).' Those provisions make it even clearer that the result of the previous (2007) assessment fell to be taken into account in computing the redetermined capital gain or capital loss for the 'year of assessment' (2012). That characteristic of the exercise was wholly irreconcilable with any notion that the previous determination is expunged. On the contrary, the event in the 2012 tax period that brought about a reduction in the proceeds fell to be taken into account in that year of assessment. Regard would be had in doing so to the previous year of assessment in which the disposal had been accounted for, but the assessment in respect of such previous year would not be affected and it would remain effective.

(xix) That the redetermination exemplified in the calculation put up by SARS required the word 'or' in the expression 'as contemplated in par. 3(*b*)(iii) or 4(*b*)(iii)' in par. 25(3) of the Schedule to be construed as 'and' and that is not an altogether exceptional incident in statutory interpretation.

(xx) That if the word 'or' were to be construed in the context of par. 25(3) of the Eighth Schedule in accordance with its strictly literal meaning, which is disjunctive, it would give rise to an absurdity. As already noted, the provisions of par. 25(2) and (3) of the Schedule are there to give effect, in the particularised context of an event in a subsequent tax period, to the general principle expressed in par. 35(3) that the proceeds of a disposal must be reduced by the amounts contemplated in paras 35(3)(*a*)–(*c*). A reduction in the proceeds necessarily will give rise to either a reduction in the relevant capital gain or an increase in the capital loss. If the reductions provided for in terms of par. 35(3) were to happen in the year of assessment in which the disposal was made, it would result in a reduction in the taxpayer's net capital gain (determined in terms of par. 8), or an increase in its assessed capital loss (determined in terms of par. 9). It would be manifestly unjust were the taxpayer not to be afforded the benefit of the reduction in such circumstances for it would otherwise result in it being exposed to a capital gains tax liability calculated with regard to a gain that had become impossible to realise. The evident object of the redetermination contemplated by par. 25(2)(*b*) of the Eighth Schedule is to provide a comparable benefit to the taxpayer which experiences the events contemplated in par. 35(3)(*c*), not in the year of assessment in which the disposal of the asset occurred, but in a subsequent tax period.

(xxi) That if the redetermination in terms of par. 25 were to result, as it does in the postulated example using the amounts involved in the current case and the formula prescribed in par. 30, in a capital gain, it would not achieve the evident object of the redetermination if the taxpayer were, in addition to the assessed capital gain for which it had become liable in terms of its 2007 assessment, also to be exposed to a further liability in respect of the redetermined capital gain (R2 040 051) falling to be accounted for in the 2012 year of assessment as required by par. 25(3). If the redetermined capital gain in the amount of R2 040 051 were to be dealt with only in terms of par. 3(*b*)(iii), it would have the effect of making the taxpayer liable in the 2012 tax year for capital gains tax in that year in an amount over and above that to which it had become liable in 2007. That result would be absurd. It would defeat the obvious rationale for par. 35(3)(*c*) and produce a result in conflict with the evident purpose of the redetermination exercise provided in terms of par. 25 and it would also give rise to a manifestly unjust and irrational treatment of the taxpayer.

(xxii) That the absurdity was avoided, and the evident object of the provisions of par. 25(2) and (3) is achieved, only if the word ‘or’ in par. 25(3) is construed as ‘and’, with the result that the redetermined capital gain amount is treated in terms of par. 3(*b*)(iii) and par. 4(*b*)(iii) (and not par. 3(*b*)(iii) or par. 4(*b*)(iii)) in the manner illustrated in the calculation handed up by SARS. It is only by construing the word ‘or’ as ‘and’ that a result consistent with the manifest object of the legislation is achieved.

(xxiii) That in the circumstances the construction of the relevant legislation propounded by SARS was correct. The contesting interpretation advanced on behalf of New Adventure was inconsistent with the plain wording of the provisions. It was clear in the wording of par. 25(3) that the outcome of the redetermination exercise required to be undertaken in the 2012 year of assessment fell to be taken into account in that year. If regard is had to the provisions of paras 8–10 of the Eighth Schedule, the benefit derived by New Adventure from the redetermination fell to be realised by offsetting the effect of the determined capital loss against any capital gains realised by New Adventure in that year (2012), or, if no capital gain is made in that year, in subsequent years. There was no basis in the provisions for the expungement of the capital gains tax liability in the taxpayer's 2007 year of assessment.

(xxiv) That New Adventure therefore did not have a valid basis to object to or appeal against its 2007 income tax assessment and it had not shown any reason why that assessment should be amended.

(xxv) That, for all the aforementioned reasons, the application for review and the associated relief will be dismissed with costs, including the costs of two counsel.

5.3. ITC 1883

The taxpayer had been audited by the SARS in May 2014 and audit findings were furnished in August 2014.

The taxpayer had made representations in November 2014 and assessments had been raised against it in December 2014 in respect of Unemployment Insurance, Skills Development Levy, Employees Tax, Secondary Tax on Companies, Income tax and Value-added tax.

The taxpayer lodged an objection against the aforementioned assessments on 5 June 2015 and such objection was disallowed by SARS in a letter dated 22 June 2015 on the grounds that 'no exceptional reasons had been furnished' and the taxpayer then appealed to the Tax Court against that finding.

Section 104 of the Tax Administration Act 28 of 2011 provided at the relevant time:

'104. Objection against assessment or decision

(1) A taxpayer who is aggrieved by an assessment made in respect of the taxpayer may object to the assessment.

(2) . . .

(3) A taxpayer entitled to object to an assessment or 'decision' must lodge an objection in the manner, under the terms, and within the period prescribed in the 'rules'.

(4) A senior SARS official may extend the period prescribed in the 'rules' within which objections must be made if satisfied that reasonable grounds exist for

the delay in lodging the objection.

(5) The period for objection must not be so extended –

(*a*) for a period exceeding 21 business days, unless a senior SARS official is satisfied that exceptional circumstances exist which gave rise to the delay in lodging the objection'.

The 'rules', being the rules promulgated under section 103 of the Tax Administration Act, provide in Rule 7(1) that a taxpayer who may object to an assessment under section 104 of the Act must deliver a notice of objection within 30 business days after the dates specified in the rule.

It was common cause that the taxpayer should have objected by 2 March 2015, i.e. 30 business days from the date of assessment and it was also common cause that the taxpayer's objection was only lodged on 5 June 2015 and was accordingly out of time by 65 business days.

The taxpayer had made a number of submissions in support of its contention that exceptional circumstances existed and that these had causally contributed to the 65 business day delay:

- The assessments and objections thereto involved complex issues of law;
- The delay was due to the courts being closed over December 2014 and January 2015, during the court recess period;
- The taxpayer alleged that it was negotiating with SARS from December 2014 to March 2015;
- The taxpayer had become dissatisfied with the abilities of its auditor and stopped using his services;
- The taxpayer was only able to obtain new professional advice from a practitioner in Florida and received the name of his legal representative in April 2015, who then prepared an undated opinion for it.

The issue before the court was whether the taxpayer had discharged the *onus* of proving 'exceptional circumstances' as required in terms of section 104 of the Tax Administration Act when it sought an extension of the period allowed to it for objection to an assessment.

Judge Satchwell held the following:

(i) That section 104 of the Tax Administration Act permits a taxpayer to object to an assessment within the period prescribed in the Rules – Rule 7(1) provides that a notice of objection must be delivered within 30 days after the date of assessment – which period may be extended but not for a period exceeding 21 business days 'unless a senior SARS official is satisfied that exceptional circumstances exist which gave rise to the delay in lodging the objection.'

(ii) That the provisions of section 104(5) were peremptory and are clearly expressed – the period for objection 'must not be extended' and that was the framework within which this appeal for relief was sought.

(iii) That the *onus* was therefore on the taxpayer to satisfy the court that 'exceptional circumstances exist which give rise to the delay in lodging the objection' and this meant that unusual facts must be proven which have a causal connection to the delay which resulted.

(iv) That the taxpayer had made a variety of submissions, some of which had no relevance to the enquiry into the existence of exceptional circumstances and their causal relation to the 65 business day delay and much of its argument and many of its submissions were not contained in the written heads of argument and were made off the cuff by counsel appearing for the taxpayer and should not have been presented in such fashion.

(iv) That, further, a number of issues were argued but none were based upon documents or proof and all were no more than argument but were, regrettably, presented as though there were facts or evidence contained somewhere in the papers before the court which unfortunately could not be found.

(v) That, accordingly, none of the aforementioned submissions persuaded the court of the existence of 'exceptional circumstances' and they were neither unusual nor causally connected to the delay.

(vi) That the taxpayer should have taken its tax responsibilities seriously enough to seek tax advice from a firm of attorneys specialising in such matters as soon as the assessments were levied in December 2014 and the lapse of time is not satisfactorily explained – let alone sufficiently to discharge the *onus* of proving 'exceptional circumstances.'

Appeal dismissed with costs.\

5.4. C:SARS v Capstone 556 (Pty) Ltd

Capstone, a South African special purpose vehicle, had been incorporated on 2 April 2003 and it was wholly owned by another special purpose vehicle, Business Ventures Investments No 687 (Pty) Ltd ('BVI').

Capstone, during April 2004, had disposed of approximately 17 million shares in JD Group Ltd ('JDG') and had made a profit of nearly R400 million on the sale.

The principal question in this appeal was whether Capstone was liable for tax on the amount of the profit on the basis that it had constituted income or it was a receipt of a capital nature.

The material facts were that by the end of 2001, Profurn Ltd ('Profurn'), a JSE listed company in the retail furniture industry, had run into serious financial difficulties. It owed FirstRand Bank Ltd ('FirstRand') in excess of R900 million. Profurn also owed between R70 and R90 million to Steinhoff International Holdings Ltd ('Steinhoff'). Steinhoff was then a major manufacturer and supplier of furniture to the retail industry. Its chief executive officer was Mr Markus Jooste, who was also a major shareholder in Steinhoff. Dr Theunie Lategan, head of the corporate division of FirstRand, was responsible for Profurn's account. FirstRand also had exposure to other furniture retailers. Profurn risked imminent liquidation in view of its critical financial position and this represented a serious financial risk to FirstRand and Steinhoff, as well as a major threat to the stability of the retail furniture industry in South Africa as such.

Dr Lategan, who was under immense pressure to come up with a solution to the Profurn problem, had discussed it with Mr Jooste and Mr Jooste referred him to Mr Claas Daun, a wealthy German businessman and director and shareholder of Steinhoff. Mr Daun also indirectly held a 13% shareholding in Profurn and so stood to suffer financially if Profurn was liquidated. FirstRand had determined that for Profurn to survive, it needed to reduce its debt to FirstRand to some R300 million. Hence

Profurn needed a capital injection of approximately R600 million and for this purpose Dr Lategan entered into discussions with Mr Daun early in 2002.

Mr Daun was interested but held a firm view that what was required to save Profurn, was both an injection of capital and sound management and to that end he held the managerial skills of Mr David Sussman, executive chairman of JDG, in high regard and he made it clear that he would only be prepared to invest if the management of Profurn was taken over by Mr Sussman.

FirstRand therefore approached Mr Sussman and he was agreeable but in turn insisted that the investor should be committed to remain on board as a shareholder for as long as it would take to turn the business of Profurn around and Mr Daun gave the required undertaking after discussing the matter with Mr Sussman.

These developments were followed by a series of discussions between mainly Dr Lategan, Mr Jooste, Mr Daun and Mr Sussman and they resulted in a plan to rescue Profurn and stabilise the retail furniture industry. All concerned were *ad idem*, however, that the attempt to rescue Profurn would be a difficult operation, would involve high risks and would probably require a period of three to five years.

In essence, the solution agreed upon was the following. FirstRand would underwrite a R600 million rights issue by Profurn, thereby converting R600 million of the debt owed to FirstRand into equity and this would be followed by a merger between Profurn and JDG, whereby the Profurn shares would be exchanged for JDG shares. FirstRand would then sell the JDG shares so acquired by it for R600 million to a South African special purpose vehicle, to be created in due course when needed ('Capstone'). Daun et Cie Aktiengesellschaft ('Daun et Cie'), a German private holding company controlled by Mr Daun, would invest R300 million in Capstone, which would be used to pay half of the purchase price and R200 million of the purchase price would be settled by the issue by Capstone to FirstRand of redeemable preference shares and the balance by a participating loan by FirstRand to Capstone and in this manner the required capital injection and management would be achieved.

Most of this was reflected in a memorandum of understanding ('MOU') signed by Mr Daun on 26 June 2002 at Rastede in Germany. In terms of the MOU it was naturally envisaged that final written agreements would be entered into and that the requisite regulatory approval be obtained. It was nevertheless accepted by all relevant parties that the MOU gave rise to a binding commitment by Mr Daun and his associates *via* the proposed special purpose vehicle to purchase the JDG shares from FirstRand and that the risk and reward in respect of the shares passed with effect from 26 June 2002, which was the express effective date of the MOU.

Despite some efforts by FirstRand to encourage existing shareholders of Profurn to take up the rights offer, only a handful did so, raising less than R1 million. This was an indication of the desperate position of Profurn, as was the fact that after the MOU was signed, Profurn's share price fell even further and, as a consequence, FirstRand acquired a 78.8% shareholding in Profurn and thereafter JDG and Profurn merged and FirstRand acquired approximately 42 million JDG shares.

In the agreements and amended agreements entered into following on the MOU, the rescue plan was varied in two material respects. First, FirstRand determined to retain one-sixth of its JDG shares. In the result five-sixths of the JDG shares would be transferred to Capstone and this translated to approximately 35 million JDG shares and a 20.9% interest in JDG. Second, Mr Daun invited Mr Jooste to participate in the transaction, which required some restructuring of the special purpose vehicle to keep Mr Daun's financial interests separate from those of Mr Jooste. As a result, half of the 35 million shares were sold to Daun et Cie for R250 million and the other half to Capstone for the same purchase price. In terms of these agreements the purchase price of the shares was fixed as at 26 June 2002 and the purchasers had to pay interest on the purchase price calculated from that date. Daun et Cie eventually paid R262 725 131 (R250 million plus interest) to FirstRand in cash. This constituted a significant foreign investment in South Africa and the funding of the purchase price payable by Capstone was of course the responsibility of Mr Jooste.

Daun et Cie and Capstone thereby committed themselves to a significant investment of indefinite duration, the ultimate profitability of which depended upon the ability of Mr Sussman to turn around the operations of Profurn and integrate them profitably into those of JDG.

Capstone was wholly owned by another special purpose vehicle, Business Ventures Investments No 687 (Pty) Ltd (‘BVI’). The financial interest in BVI was held by Mr Jooste and his associates. Genbel Securities Ltd (‘Gensec’) advanced the amount of R150 million to BVI on condition that it be utilized to enable Capstone to acquire the JDG shares. BVI thereafter made a shareholder's loan to Capstone in the amount of R150 million on the same terms and conditions as those contained in the loan agreement between Gensec and BVI. The balance of the purchase price was settled by the issue by Capstone of three year and one day redeemable preference shares to FirstRand. For this reason Capstone was required to comply with FirstRand's standard terms and conditions in respect of preference shares. In the result Capstone took a number of registered special resolutions, one of which, *inter alia*, provided that a special condition be inserted in Capstone's memorandum of association that until the date on which the preference shares have been redeemed in full, Capstone shall not be entitled to conduct any business whatsoever, enter into any contract or undertake any obligation whatsoever, other than in respect of the sale and subscription agreement and a voting pool agreement relating to its shares in JDG, provided however that this would not prevent the company from acquiring any additional shares in the share capital of JDG from time to time . . . without the express prior written consent of FirstRand.

The effect of this and other terms and conditions was that for the period of three years and a day from 30 May 2003, Capstone was prohibited from disposing of its JDG shares without the consent of FirstRand.

Two additional liabilities were attached to the acquisition of the JDG shares by Capstone. First, a due diligence investigation performed in respect of Profurn at the instance of JDG, revealed contingent liabilities of Profurn in respect of tax. FirstRand indemnified JDG in respect of these liabilities in the amount of R150 million and required the purchasers of the shares to carry proportionate shares of its liability in terms of the indemnity to JDG. As a result, as part of the consideration for the shares, Daun et Cie and Capstone each indemnified FirstRand in the amount of R62.5 million. The indemnities were given for a period of five years commencing in early 2003. Second, the loan agreement between Gensec and BVI provided, in addition to interest on the loan, for payment of what was referred to as an 'equity kicker'. The equity kicker was a portion of any gain in the market value of the JDG shares as on date of repayment of the loan, calculated in accordance with an agreed formula. It was payable by BVI to Gensec upon repayment of the loan, irrespective of whether or not the JDG shares had been sold. As the BVI-Capstone loan duplicated the terms of the Gensec-BVI loan, Capstone in turn was obliged to pay the equity kicker to BVI.

When Mr Daun invited Mr Jooste to participate, he made it clear that he would retain sole control over the 35 million JDG shares, which would at all times be dealt with as one package by Mr Daun. This was understood and accepted by Mr Jooste. He felt honoured by the invitation and was content that Mr Daun would be the 'captain of the boat' in which he would be the 'passenger'. For this reason Mr Daun and the manager of his South African interests, Mr Schouten, were directors of Capstone at all times material to the appeal, whilst Mr Jooste was not. The other directors of Capstone were Dr Lategan and Mr Steve Muller, who represented the interests of FirstRand and Gensec respectively. The shares in BVI were held by Daun et Cie as nominee for companies controlled by Mr Jooste and his associates. Mr Daun was also the only director of BVI and thus at all times relevant hereto also in control of BVI.

In terms of an agreement entered into on 20 June 2002, Profurn was placed under the interim management of JDG pending the final authorisation of the merger application by the Competition Tribunal. However, substantial delays occurred due to the need to obtain approval from the Competition Tribunal and on appeal, the Competition Appeal Court, as well as the South African Reserve Bank. The Tribunal approved the merger on 12 December 2002, subject to conditions which were set aside by the Competition Appeal Court on 28 May 2003. The JDG shares were ultimately paid for and transferred to Daun et Cie and Capstone only on 5 December 2003 and by that date, the share price had risen considerably from the levels at which it stood when the transaction was originally devised.

In November 2003, when Steinhoff undertook an international 'book building' exercise with the assistance of Citigroup Global Markets Ltd ('Citigroup'), Mr Jooste was having coffee with Mr Nicholas Pagden of Citigroup in San Francisco and enquired whether a similar exercise could be done in respect of the JDG shares that Daun et Cie and Capstone were in the course of acquiring. A book building exercise is a means of determining a price and acquiring institutional investors through either the issue and acquisition of new shares, or the sale of an existing block of shares in circumstances where the disposal of such a large block of shares in the market would detrimentally affect the price of the shares on a stock exchange. The institution undertaking the book building approaches institutional investors to ascertain how many shares they might buy and at what price. Once the price is determined the shares are disposed of other than through the exchange on which they are, or are to be, listed.

As a result, in March 2004, Citigroup, represented by Mr Pagden, made a presentation to Mr Daun concerning a book building. The proposed book building entailed disposal of the full block of JDG shares controlled by Mr Daun.

Mr Daun accepted the proposal in respect of the approximately 14 million shares held by each of Daun et Cie and Capstone. Each retained approximately 3,5 million shares. The sale by book building by Citigroup took place on 29 April 2004 and it realised the price of R42.50 *per* share. More or less at the same time Capstone sold its remaining 3,5 million JDG shares to Mayfair Speculators (Pty) Ltd, a company holding the interests of Mr Jooste and his family, for R45 *per* share and the shares had been purchased as at 26 June 2002 for R14.17 *per* share.

On 30 April 2004 Mr Daun, Mr Schouten and Dr Lategan resigned as directors of Capstone and on the same date Gensec and BVI entered into a further written agreement to settle the loan. In terms of this agreement the liability in respect of the equity kicker amounted to R45 123 050, calculated on the actual proceeds realised. Although BVI (and therefore Capstone) were entitled to temporarily retain a portion of the equity kicker, the liability for the full equity kicker arose on 30 April 2004. Mr Muller resigned as director of Capstone on 5 July 2004 and shortly afterwards Mr Jooste and an associate were appointed as its directors.

What remained was Capstone's contingent liability in terms of the indemnity to FirstRand. However, during July 2004 Daun et Cie and Capstone, represented by Mr Daun and Mr Jooste respectively, agreed that Daun et Cie would accept the full contingent liability of Capstone towards FirstRand in return for payment of the amount of R55 million. Capstone thus incurred liability for payment of R55 million to Daun et Cie in the 2005 year of assessment in substitution of its contingent liability towards FirstRand and this debt was settled much later, by operation of set-off.

Capstone calculated and paid capital gains tax on the proceeds of the sale of its JDG shares.

SARS had, however, issued an additional assessment in respect of the 2005 year in terms of which the proceeds were taxed as revenue on the ground that, from the outset, Capstone's intention was to acquire the shares in issue for resale at a profit and that that intention never changed and that the shares were acquired as trading stock. In addition, the Appellant had disallowed deductions from gross income of R45 123 050 in respect of the equity kicker and R55 million in respect of the settlement of the indemnity obligation (the indemnity settlement).

Capstone's objection to the additional assessments was dismissed and it appealed to the Cape Tax Court (see *ITC 1867*, 75 SATC 273, *per* Davis J).

The Tax Court held that the proceeds constituted revenue but, however, it revised the assessment to allow for the deduction of the equity kicker and the indemnity settlement from gross income in terms of section 11(*a*) read with section 23(*g*) of the Income Tax Act.

On appeal to the Full Court (see *Capstone 556* (*Pty*) *Ltd* v *C: SARS* 77 SATC 1 *per* Griesel J) Capstone's contention that the proceeds were of a capital nature was upheld and the question arose whether the equity kicker and the indemnity settlement formed part of the base cost of the acquisition of the JDG shares in terms of par. 20 of the Eighth Schedule to the Income Tax Act 58 of 1962, the base cost is deducted from the proceeds in order to determine the taxable capital gain.

The Supreme Court of Appeal granted leave to SARS to appeal against the order of the Full Court.

Subject to an exception, par. 20(2) of the Eighth Schedule provides that the base cost does not include 'borrowing costs, including any interest as contemplated in section 24J or raising fees'.

The exception is that one-third of the interest as contemplated in section 24J of the Act on money borrowed to finance the acquisition of listed shares, does form part of the base cost.

Section 24J defines 'interest' to, *inter alia*, include 'the gross amount of any interest or related finance charges, discount or premium payable or receivable in terms of or in respect of a financial arrangement'.

The Full Court found that the equity kicker constituted interest as defined and, on this basis, it concluded that R30 082 033, that is two-thirds of the amount of R45 123 050, fell to be included in the capital gain and the parties were *ad idem* that this conclusion was correct.

However, the Full Court found that the indemnity settlement in the amount of R55 million did not constitute part of the base cost and consequently Capstone noted a cross-appeal against this finding and it also noted a conditional cross-appeal in the event of a finding that the proceeds were not of a capital nature.

Judge van der Merwe held the following:

<u>As to the test on appeal</u>

(i) That the parties in the present matter were rightly agreed that the appeal from the tax court was governed by the provisions of Part E of Chapter 9 of the Tax Administration Act and the provisions of section 86A of the Income Tax Act, which dealt with appeals from a tax court, and of Part E of Chapter 9 of the Tax Administration Act were substantially the same.

(ii) That in terms of section 134(2)(b) of the Tax Administration Tax a notice of intention to appeal against the decision of a tax court must indicate the findings of fact or rulings of law appealed against and section 139(3)(b) of the Act required the same of a notice of cross-appeal and in the court's judgment the principles set out in CIR v Da Costa were equally applicable to appeals from a tax court in terms of the Tax Administration Act.

(iii) That such appeal was on the same footing as an appeal from a division of the High Court and it followed that the full court was bound by the factual findings of the tax court, unless they were affected by material misdirection or the full court was convinced that they were wrong and in exercising its powers on appeal in terms of section 19 of the Superior Courts Act 10 of 2013, this court essentially has to consider what order the full court should have made on application of these principles.

<u>As to the distinction between revenue or capital</u>

(iv) That in terms of section 82 of the Income Tax Act(now section 102 of the Tax Administration Act) the burden of proving that the decision of SARS subject to appeal was incorrect, rested on Capstone. Our courts have taken the view that any receipt or accrual must be either income or capital, and 'there is no third category or halfway house.' It followed that Capstone could only discharge the onus by showing, on a balance of probabilities, that the proceeds were capital and that is a question of law to be decided on the particular facts of each case, for which there is no single infallible test.

(iv) That whilst recognising that it is not universally valid, our courts have in circumstances such as the present consistently applied the test that a gain made by an operation of a business in carrying out a scheme of profit-making, is income and vice versa. The mere intention to profit is not conclusive. There must be 'an operation of business in carrying out a scheme for profit-making' for a receipt to be income and that expression refers to the use of the taxpayer's resources and skills to generate profits, usually, but not always, of an on-going nature.

(v) That where a profit is the result of the sale of an asset, the intention with which the taxpayer had acquired and held the asset is of great importance and may be decisive. In essence, the question is whether the asset was acquired for the purpose of reselling it at a profit and assumed the character of trading stock.

(vi) That in determining this intention the court 'is not concerned with that kind of subjective state of mind required for the purposes of the criminal law, but rather with the purpose for which the transaction was entered into'.

(vii) That the purpose or dominant purpose of the acquisition of an asset is a question of fact and it must be determined objectively in the same manner that any fact is determined by a court of law. The credibility and reliability of the evidence of the witnesses for the taxpayer must be determined in the light of the objective facts and inferences drawn therefrom, the probabilities and any evidence put up in contradiction thereto.

(ix) That apart from the intention of the taxpayer, a number of factors must be considered. First, the nature of the business activities of the taxpayer must be scrutinised. The line of demarcation between the realisation of an asset at a capital gain and turning an existing asset to the purpose of generating revenue may be a fine one. So close regard must be paid to the nature of the business activities in which the taxpayer is ordinarily engaged.

(x) That, second, the period for which the asset is held and the period for which it was anticipated it would be held at the time of acquisition will be relevant. In general the longer that period the more likely it is that the disposal is a realisation of capital rather than a receipt of income.

(xi) That, third, when dealing with an investment, the nature of the risk undertaken has a bearing on whether the exercise is one directed at building up the value of the taxpayer's capital or directed at generating revenue and profit.

(xii) That, finally, it had to be recognised that in many commercial situations there may be no clear intention at the outset and any endeavour to discern one or select one as more prominent that another, rather than accepting that the taxpayer's future intentions were indeterminate, may be artificial and unhelpful. In such circumstances a better approach is to accept the indeterminacy and factor that into the enquiry.

<u>As to the effective date</u>

(xiii) That the Tax Court had rightly noted that it had been accepted by all the relevant parties that the MOU gave rise to a binding commitment to acquire the JDG shares at the purchase price to be determined as at 26 June 2002 and bearing interest from that date. The full court found that the effective date of the transaction as a whole dated back to 26 June 2002, that ‘it is accordingly at that date that one must look when considering the period for which the asset was held’ and that the shares were effectively acquired during June 2002, not December 2003.

(xiv) That the court agreed with what was said by McCreath J in CIR v General Motors SA (Pty) Ltd that the correct approach in a matter of this nature was not that of a narrow legalistic nature. What has to be considered is the commercial operation as such and the character of the expenditure arising therefrom and this was perhaps but another way of expressing the concept that it is the substance and reality of the original transaction that was the decisive factor.

(xv) That if the receipt or accrual arose from a detailed commercial transaction the transaction must be considered in its entirety from a commercial perspective and not be broken into component parts or subjected to narrow legalistic scrutiny. In substance and in commercial reality the purpose of the acquisition of the shares must be determined as at 26 June 2002, in the context of events leading to the MOU.

<u>As to the directing mind</u>

(xvi) That the Tax Court had found that Mr Jooste was the ‘brain’ and the ‘mind’ of Capstone and the full court, on the view that it took of the matter, found it unnecessary to decide the issue but the present court was convinced that this finding of the Tax Court was wrong. Mr Daun had been de facto in control of the shares from their effective acquisition to their disposal. Mr Daun therefore determined the purpose of their acquisition and at the time of their disposal, he, aided by Mr Schouten, was in any event the controlling director of Capstone and whether or not the shares should be sold was solely the decision of Mr Daun.

<u>As to Mr Daun's intention</u>

(xvii) That Mr Daun's intention at the time of effective acquisition of the shares had to be determined and it was the present court's view that the approaches in this regard of both the Tax Court and the full court were flawed. In the Tax Court the fact that, if the turnaround strategy involved in the takeover of Profurn by JDG was successful, Mr Daun, as an investor and entrepreneur, wanted to recover his investment together with an increase in its value, did not mean that a profit-making intention was his purpose in making the investment, much less the predominant purpose. Nor was it correct to say that this was not a long term investment as the duration of the investment was dependent on Mr Sussman's skills in merging the two businesses as well as factors beyond the control of either Mr Daun or Mr Sussman, such as the general economic climate. On the other hand, the full court stopped its enquiry at the first stage, without exploring further the implications of the strategic investment made by Mr Daun and a more rounded and complete consideration of the whole transaction was called for.

(xviii) That Mr Daun had obviously made the investment because he was of the opinion that the rescue operation could be successful and it was naturally anticipated that a turnaround of the business would result in an increased share price but this was neutral, it said nothing about the aim of the acquisition. Virtually every capital asset is purchased in the hope and anticipation that it will increase in value and in contemplation of the possibility that it may in future be sold at a profit. Mr Daun contemplated a resale of the shares at a profit as one of several possibilities and these possibilities were to be explored at the appropriate time in future.

(xix) That it was clear from the evidence that the first and primary purpose of the acquisition of the shares was to rescue a major business in the retail furniture industry by long term investment of capital and this involved a commitment of capital for an indeterminate period involving considerable risk and only a very uncertain prospect of a return. Assuming the rescue was successful, it was uncertain what would happen next. In effect all options were open and all of this was consistent with an investment of a capital nature that was realised sooner than initially expected because of skilled management and favourable economic circumstances. It was not a purchase of shares as trading stock for resale at a profit. The factual findings of the Tax Court in respect of the intention with which the shares had been purchased, were therefore clearly wrong. Although the full court did not say so in so many words, it was convinced on appeal that the findings were wrong.

(xx) That, accordingly, Capstone had proved on a balance of probabilities that the proceeds of the sale of shares were of a capital nature and the appeal must therefore be dismissed.

As to the cross-appeal

(xxi) That, as to the indemnity settlement, it was beyond question that the contingent liability of Capstone in terms of the indemnity to FirstRand formed part of the consideration for the acquisition of the shares. Had payment in terms thereof taken place during the 2005 year of assessment, it would have constituted part of the base cost of the shares. The unconditional obligation in terms of the indemnity settlement to pay R55 million to Daun et Cie was undertaken in substitution of the contingent obligation to FirstRand and the full court had rightly said that the liability to FirstRand was 'converted' into liability to Daun et Cie.

(xxii) That the causal link with acquisition of the shares was not broken and the acquisition of the shares remained the causa causans of the indemnity settlement and the present court was therefore unable to agree with the conclusion of the full court that the indemnity settlement was 'entirely separate from the acquisition of the JDG shares' and therefore a novus actus interveniens. It was the mechanism by which the contingent liability incurred as part of the acquisition of the shares was monetised and rendered a quantifiable component of the cost of the shares. The Commissioner had accepted that the liability in terms of the indemnity settlement had been incurred during July 2004, that is, in the 2005 year of assessment.

(xxiii) That, accordingly, the liability incurred by Capstone to pay the amount of R55 million to Daun et Cie was an 'expenditure actually incurred' in respect of the acquisition of the shares and it followed that the cross-appeal had to succeed.

5.5. C:SARS v Brown

Mr Brown was an adult male residing in Port Elizabeth and it was common cause that he was not a registered taxpayer, nor had he ever submitted any tax returns.

SARS had launched proceedings on a semi-urgent basis in the Eastern Cape Division of the High Court for an order, *inter alia*, directing Mr Brown to comply with section 46(4) of the Tax Administration Act by submitting his response to a Lifestyle Questionnaire served on him on 19 October 2015.

SARS had delivered the questionnaire to Mr Brown on 19 October 2015 and he was expected to return the completed questionnaire to the appropriate SARS offices within 21 business days.

The letter accompanying the questionnaire was signed by the Hendrickse and one Mayezana and the letter also stated, *inter alia*, that the period of investigation of Mr Brown was the 2011 to 2015 tax years and that SARS was in the process of reviewing his tax file and that the information was requested in terms of section 46(1) of the Tax Administration Act.

The questionnaire comprised some 26 pages and the first page drew Mr Brown's attention to the provisions of section 72(1) of the Tax Administration Act which provided that a taxpayer may not refuse to complete and file a return on the basis that to do so might incriminate him or her. The information sought from Mr Brown related, *inter alia*, to his and his spouse's personal particulars and circumstances; personal and private investments and assets; properties owned by him and his spouse; income received during the period under review and expenses.

SARS, on the same date, had also caused a letter to be served on Mr Brown wherein he was given notice that SARS intended to commence an investigation into his tax affairs and that the investigation was based on confidential and statutorily protected third party information which suggested that certain income had not been disclosed; that expenses had been incorrectly claimed for tax purposes and that declarations made to SARS by other taxpayers suggested a tax risk.

Mr Brown replied to SARS' letter on 5 November 2015 by reminding SARS of its statutory obligations towards taxpayers and stated that he would fully co-operate with SARS in respect of ‘any lawful audit, gathering of information or questionnaire, investigations and/or order’ but required confirmation that SARS would keep him informed of the progress and findings of any audit and that he would be given reasonable opportunity to respond to the findings.

Mr Brown, however, also required certain further information from SARS before he would reply to the questionnaire and he further stated that he would submit a formal request for the abovementioned information under the Promotion of Access to Information Act 2 of 2000 (PAIA) and a copy of the request was annexed to the letter. The further information requested by Mr Brown included ‘adequate reasons for the questionnaire, investigation and audit and why it is being conducted, including the underlying risk analysis for the industry the taxpayer is in, on which this audit is based’.

SARS responded, *inter alia*, by stating that it was impermissible for Mr Brown to make his response to the questionnaire conditional upon the furnishing of the information requested in terms of the PAIA and, subsequently, SARS pointed out in a letter that Mr Brown was under a statutory obligation, in terms of section 46(1) of the Tax Administration Act, to respond to the questionnaire and that a failure to do so by 15 January 2016 would result in SARS seeking ‘appropriate remedy against Mr Brown together with a punitive costs order’.

Mr Brown responded and stated that the request to submit the questionnaire constituted administrative action and was subject to the principle of legality and he had just cause not to respond to the request for information because the requested information had not been provided and he was entitled to assume that the exercise by SARS of the power in terms of section 46 of the Tax Administration Act had not been properly authorised and he was therefore entitled to ignore the request and SARS was also obliged to give reasons for its decision to issue the questionnaire.

Mr Brown consequently made a new PAIA application requesting ‘new and additional information’ and pending the outcome of the complaint to the Tax Ombudsman, any action taken by SARS would be premature.

It was common cause that Mr Brown had failed to submit the completed questionnaire as requested by SARS and had, in fact, asserted his constitutional and statutory right to comply only once the information requested in terms of PAIA had been provided by SARS.

SARS had responded to the second request for information in terms of PAIA by granting the request for copies of the identification cards but refusing access to the remainder of the records and information on the basis that the disclosure of the information would 'jeopardise the effectiveness of SARS auditing procedures and methods used by SARS to identify taxpayers'.

SARS contended that the provisions of section 46 were peremptory and where a taxpayer is required to submit 'relevant material' to SARS under that section then he or she 'must submit the relevant material to SARS at the place and within the time specified in the request'.

Moreover, the stated objective of the questionnaire was clearly covered by the definition of the term 'administration of a tax Act'.

Mr Brown, at the commencement of the proceedings, raised two points *in limine*:

- that SARS had failed to establish sufficient urgency to justify the truncation of the time periods prescribed in the Uniform Rules of Court; and
- that Keith Hendrickse had not established that he had been properly authorised to institute the proceedings.

Mr Brown, on the merits, contended that SARS had failed to establish the prerequisite for an interdict in that, *inter alia*, the request for him to complete a Lifestyle Questionnaire was an unlawful 'fishing expedition' which infringed on his constitutional and statutory rights. Moreover, he was, by virtue of section 33 of the Constitution and the provisions of the Promotion of Administrative Justice Act 3 of 2000, or the principle of legality, entitled to expect fair, reasonable and lawful conduct on the part of SARS.

Held

<u>As to the preliminary points in limine</u>

(i) That it was trite that an Applicant who wanted to have a matter enrolled and heard as one of urgency in terms of the Uniform Rules of Court, must satisfy the court that the extent of the modification or relaxation of the Rules is not any greater than the exigencies of the case demanded.

(ii) That it must have been abundantly evident from the foregoing that the extent of the deviation, if any, from the time periods prescribed by the Court Rules was negligible. In fact, Mr Brown had longer to file his answering affidavit than he would ordinarily have been allowed if the matter were enrolled in the ordinary course.

(iii) That, unsurprisingly therefore, Mr Brown had not been able to show any prejudice resulting from the enrolment and hearing of the matter on a semi-urgent basis and SARS has been more than reasonable in specifying the extent of the truncation of the time limits in his notice of motion, and has in the event been amenable to agree to further opportunity for Mr Brown to file his answering papers.

(iv) That, accordingly, the extent of the modification of the Rules was justified by the circumstances of the case and the factual bases provided in Hendrickse's founding affidavit and this point in limine could accordingly not be upheld.

(iv) That, in regard to Mr Brown's challenge to Hendrickse's authority to institute the proceedings in issue, Hendrickse asserted that he had been authorised in terms of section 11(1) of the Tax Administration Act to institute the proceedings.

(v) That section 11(2) of the Act provided that where a SARS official instituted legal action on behalf of the Commissioner, it must be presumed that that official had been duly authorised in terms of section 11(1), unless the contrary is proven. That section thus explicitly puts the onus on the party challenging the official's authority. Moreover, section 11(1) did not require that the authority must be in writing, since it was not a delegation of the Commissioner's powers contemplated in terms of section 6 of the Act.

(vi) That the provisions of sections 10(a) and 10(b) of the Act, which required a delegation to be in writing and signed by the Commissioner before it became effective, were thus not of application and for the purpose of establishing whether or not Hendrickse had been duly authorised to institute the proceedings, the fact that the document may or may not have been signed by the Commissioner was accordingly of no consequence.

(vii) That Mr Brown had not established any factual basis for his assertion that Hendrickse had not been duly authorised and what he had done was merely to disavow any knowledge of that fact and put Hendrickse to the proof thereof and such an approach can never be sufficient to rebut a fact deemed by statute.

(ix) That, in the event, it was abundantly clear from a reasonable reading of the document in question that the intention was indeed to authorise Senior Managers to institute legal proceedings on behalf of the Commissioner.

(x) That the document in question constituted a proper delegation of the Commissioner's powers under the Tax Administration Act and it must be accordingly assumed that whoever signed the document on behalf of the Commissioner had been duly authorised to do so.

(xi) That the court was accordingly satisfied that the document in question constituted a proper delegation of the Commissioner's powers in terms of section 6(3) of the Act, read with section 10 and that Hendrickse was accordingly duly authorised to issue the questionnaire and to institute these proceedings and this point in limine must accordingly also fail.

<u>As to the merits of the application</u>

(xii) That there could be little doubt, having regard to the 'language used in the light of ordinary rules of grammar and syntax, the context in which the provision appears and the apparent purpose of the Act' that the provisions of section 46 of the Tax Administration Act were peremptory as the explicit and unambiguous wording of the section simply did not allow for any other interpretation.

(xiii) That it was similarly manifest that the information sought in the questionnaire constituted 'relevant material' since it pertained to Mr Brown's assets, liabilities and expenses. Furthermore, the questionnaire could hardly have been more specific regarding the information which Mr Brown was required to provide and the court was accordingly satisfied that adequate specificity had been provided as required by the Act.

(xiv) That there could also be little doubt that the issuing of the questionnaire was done in the course of the ‘administration of a tax Act’ since the information sought therein manifestly related to ‘the liability of a person or persons for tax in respect of a previous, current or future tax year’.

(xv) That, accordingly, the Applicant had established all the requisite jurisdictional facts mentioned in section 46 of the Act and Mr Brown's contention that the issuing of the questionnaire was a ‘fishing expedition’ was thus untenable. The questionnaire was issued against the background of information to the effect that there may have been non-disclosure of relevant information by Mr Brown, coupled with the fact that he did not register as a taxpayer or submit tax returns and these factors constituted a sound basis for the issuing of the questionnaire and could not by any stretch of the imagination be regarded as ‘a fishing expedition’.

(xvi) That Mr Brown's argument that the provisions of the Tax Administration Act did not authorise SARS to enforce a section 46 request by virtue of a mandatory interdict was not supportable. The proceedings referred to by Mr Brown all had some unusual or sui generis elements and were clearly intended to bestow upon SARS extraordinary powers in order to facilitate the efficient and expeditious collection of taxes. The right to institute civil action to enforce compliance with a request for relevant material, on the other hand, is ancillary to the powers bestowed on SARS in relation to the administration of a tax Act, including the power to request relevant material in terms of section 46 of the Act. That remedy is accordingly available to SARS in terms of the common law and does not require specific statutory sanction.

(xvii) That, in respect of Mr Brown's contention that the decision to issue the questionnaire constituted administrative action, the request for information in terms of section 46 of the Act was a preliminary investigation by SARS which may or may not lead to a more formal audit or inquiry under the Act and it was only when SARS has been placed in possession of the requested information that it will be able to determine whether or not there are indeed grounds for a further inquiry or an audit and it is at that stage that the principles of administrative justice must be observed.

(xviii) That the request for information can accordingly not adversely affect any of Mr Brown's rights and, in the event, our courts have found that an investigation of this nature does not constitute administrative action.

(xix) That, in the event, SARS has provided sound reasons for its decision to issue the questionnaire and the third party information, which suggested that there may not have been full disclosure of income by Mr Brown, coupled with the fact that he had not registered as a taxpayer or submitted tax returns, constituted a rational basis for the issuing of the questionnaire and Mr Brown's contention that SARS had failed to observe the principle of legality could accordingly also not be upheld.

(xx) That, in regard to Mr Brown's entitlement to the additional information sought in his second PAIA request, SARS' objection to the disclosure of the information on the basis that it constituted 'SARS confidential information' protected in terms of section 68 of the Tax Administration Act, was justified under the circumstances.

(xxi) That, in regard to Mr Brown's right to privacy, guaranteed in terms of section 14 of the Constitution, may have been infringed by the issuing of the questionnaire, the court was of the view that the provisions of section 46 of the Act constituted a justifiable limitation to that right as envisaged in section 36 of the Constitution and further, that his contention that his personal information was protected by his constitutional right to privacy was also untenable.

(xxii) That all that SARS was required to show was that the information sought was 'relevant material' necessary for the administration of a tax Act and for the reasons already mentioned, the information sought by virtue of the questionnaire was manifestly relevant for that purpose.

(xxiii) That, accordingly, SARS had established a clear right and a reasonable apprehension of harm and he also had no other satisfactory remedy available. Moreover, the other more invasive procedures, which were rather ironically suggested by Mr Brown, were not justified under the circumstances, neither would the institution of criminal proceedings assist SARS with its stated objective, namely the expeditious acquisition of the relevant material and, in the event, Mr Brown cannot prescribe to SARS which legal remedy it must pursue.

Application upheld.

5.6. *ITC 1884*

The taxpayer, during December 2009, had concluded a purchase and sale agreement with 'D Co' in terms of which D Co paid the taxpayer the sum of US $3 950 000 for the assets purchased from it.

The aforementioned amount did not include value-added tax ('VAT') as D Co did not pay VAT on the transaction as it had been advised, and believed, that the transaction qualified to be zero-rated for value-added tax purposes and, accordingly, no VAT was paid by the taxpayer to SARS and none was claimed by D Co as an input tax.

The taxpayer and D Co eventually accepted that VAT was payable on the sale and purchase of the assets and the taxpayer paid over the VAT to SARS on 9 November 2012 and thereafter D Co claimed the amount as an input tax credit.

It was common cause that the VAT should have been paid during the period ending on 25 March 2010 but it was only paid on 9 November 2012.

SARS accordingly imposed, in terms of section 39(1)(*a*)(i) of the Value-Added Tax Act a penalty of 10% of the VAT owing and in terms of section 39(1)(*a*)(ii) he imposed interest on the amount of VAT calculated at the prescribed rate from the first day of the month following the month during which the VAT was liable to have been paid.

SARS accordingly called on the taxpayer to pay the penalty and the interest of R938 927,78 and the interest was calculated from 1 April 2010 until 9 November 2012.

SARS, pursuant to representations made by the taxpayer, agreed to remit the penalty and the taxpayer also requested that the interest charged be remitted in terms of the provisions of section 39(7) of the Act, before the section was amended, but SARS declined to do so.

SARS disallowed Appellant's objection to his decision not to waive the interest and the taxpayer then appealed to the Durban Tax Court.

In terms of the Act the taxpayer was required to make payment of its VAT obligations on the 25th day of January, and on the 25th day of each alternate month thereafter.

If the taxpayer failed to make payment timeously, section 39(1) of the Act provided for the imposition of a penalty, and, where the VAT was paid after the end of the month during which it should have been paid, interest calculated from the first day of each such subsequent month or part thereof.

Where a penalty or interest was imposed, the taxpayer could, in terms of section 39(7) of the Act, apply for remission of both the penalty and the interest.

In terms of section 39 of the Taxation Laws Second Amendment Act 18 of 2009, the Value-Added Tax Act was amended and this amendment changed, from 1 April 2010, the basis upon which SARS could remit interest imposed in terms of section 39(1) of the Act, and applied to interest imposed on or after that date.

The issue before the court was whether the decision by SARS not to remit the interest imposed by him was to be decided in terms of the provisions of section 39(7) of the Act as they existed prior to the amendment on 1 April 2010 or in terms of the amended section 39(7) that was of application on or after 1 April 2010.

The taxpayer contended that SARS, in deciding whether interest should or should not be remitted, should have only considered one set of facts – i.e. those existing at the time the VAT was to have been paid on 25 March 2010 and, having applied his mind, SARS should then have reached a decision based on the law at that time and not on the law prevailing on or after 1 April 2010 which was the incorrect decision.

SARS contended that in terms of section 39(2) of the Taxation Laws Second Amendment Act 18 of 2009 the new section 39(7) of the Value-Added Tax Act came into operation on 1 April 2010, <u>and applied to interest imposed in terms of section 39(1)(*a*)(ii) of the Act on or after that date</u>. In this matter VAT was payable on 25 March 2010 but it was in fact paid on 9 October 2012. Moreover, in terms of section 39(1)(*a*)(ii), interest could only be imposed on or after the first day of the month following the 25 March 2010, i.e. on 1 April 2010, which was also the date upon which the amended section 39(7) came into effect.

Judge Lopez held the following:

(i) That in litigating for the imposition of interest, the legislature provided the taxpayer with what may be viewed as an indulgence not to have to pay interest for the period between the date upon which the VAT was paid and the end of that month and thereafter the taxpayer was required to pay interest and the payment of interest was triggered by the non-payment of the VAT, and continued on a monthly basis until the VAT was paid.

(ii) That, in all the circumstances, the interpretation contended for by SARS was the correct one. Interest was imposed in terms of section 39(1)(*a*)(ii) of the Act on the first day of the month following the month during which the VAT was payable. The basis upon which that interest could be remitted was amended, and also came into operation on 1 April 2010 and applied to interest imposed on or after that date.

(iii) That there could be no doubt then that any possible remission of the interest imposed on 1 April 2010 could only be considered by SARS on the basis of the amended provisions applying on that date and, that being so, the main and alternative arguments of the taxpayer had to fail.

(iv) That the matter should be remitted to SARS as the taxpayer had not had an opportunity to consider and react to SARS' assessment in terms of the amended provisions of section 39(7) of the Act. Each party appeared to believe that both sides had agreed to the proposal they put forward and the court was obviously unable to resolve that dispute between the parties and the court accordingly made a decision which was least prejudicial to the taxpayer.

(iv) That accordingly that the provisions of section 39(7)(*a*) of the Act as substituted by section 39(2) of the Taxation Laws Second Amendment Act 18 of 2009 were applicable on and from 1 April 2010, regarding any consideration of the remission of the interest imposed.

(v) That the attitude of the taxpayer to the interpretation of the applicable legislation was not unreasonable and therefore each party should pay its own costs.

5.7. Malema v C:SARS

The applicant, Mr Malema, had been assessed to pay income tax, with interest, in the amount of R18 192 295, 36 in respect of the 2005 to 2011 years of assessment.

He had objected to the assessments on the basis that the amounts in respect of which he had been assessed constituted donations or dividends in regard to which he could not be assessed to tax.

He had addressed four requests to the SARS for a compromise of which three had failed.

SARS, almost immediately after rejecting the second settlement agreement, had issued sequestration proceedings against Malema and he was provisionally sequestrated on 11 February 2014. SARS had also taken judgment against Malema for the disputed tax by filing a statement as provided for by section 172 of the Tax Administration Act.

Thereafter, on 4 March 2014, SARS had obtained a preservation order against Malema in terms of section 163 of the TAA and a *curator bonis* was appointed.

Malema, on 14 May 2014, had made a third request for a compromise, which request was similarly rejected by SARS, as it was of great importance for him not to be sequestrated as he had taken up a seat in Parliament.

SARS, during this period, had launched various investigations and enquiries into the Malema's tax affairs as well as into the affairs of persons and entities linked to him.

The main reason for the rejection of the third request was because it was contingent upon a R4 million donation to be made to Malema in order to enable him to finance a part of the compromise amount.

Malema had failed to identify the donor and had failed to address the payment of donations tax and, as a result, he had supplemented his request and submitted a fourth request to SARS in which he had identified the donor who would pay the donations tax, failing which he would be jointly liable for the payment thereof.

Malema's fourth request for a compromise, dated 21 May 2014, was successful and had resulted in the compromise agreement being entered into with SARS.

The aforementioned compromise agreement included an undertaking by Malema to make full and frank disclosure of all material facts and to keep his tax affairs current and included an express guarantee that the facts advanced were true.

In terms of the aforesaid agreement Malema had warranted that the information provided to SARS was accurate, verifiable and complete.

It bears mention that Malema was provisionally sequestrated on 10 February 2014 and the return day of the sequestration order was initially set for 26 May 2014 but was, from time to time, extended.

The final date for compliance with the compromise agreement was 30 November 2014 and by 1 December 2014 Malema had paid the amount of R7 259 953,79 to SARS in tranches as stipulated in the compromise agreement and Malema had thus complied fully with all his payment obligations in terms of the compromise agreement.

SARS, however, on 13 March 2015, had contended that he was no longer bound by the compromise agreement as set out in an affidavit by a senior SARS official as contemplated in section 6(3) of the TAA, on the ground that Malema had not, as was required by the agreement, made full, verifiable and complete disclosure of all material facts nor had he kept his tax affairs current.

At the stage when the compromise agreement had been entered into, the applicant had stated that he would pay the anticipated assessments in respect of the 2011 and 2012 tax years and these amounts were assessed, respectively, as R1 569 492,35 on 26 July 2014 and R11 985 248,72 during August 2014 for the years 2011 and 2012 respectively and in terms of the compromise agreement it was agreed that these assessments would be dealt with in the normal course.

Section 200 of the TAA authorised a senior SARS official to effect a compromise but only if the purpose thereof was to secure the highest net return from the recovery of the tax debt and only when the compromise was consistent with considerations of good management of the tax system and administrative efficacy.

The compromise agreement included the provisions of section 205 of the TAA in that it stipulated that SARS would not be bound thereby:

- If the applicant failed to disclose a material fact to which the 'compromise' related;
- If the applicant supplied materially incorrect information to which the 'compromise' related;
- If the applicant failed to comply with a provision or condition in the agreement referred to in section 204; or
- The applicant is liquidated or his estate is sequestrated before he has fully complied with the conditions contained in the agreement referred to in section 204.

The compromise agreement also stipulated that in the event of a breach, SARS could cancel the agreement and claim the full tax debt owing before the compromise agreement was entered into, or claim specific performance of the compromise agreement.

Malema, following SARS' decision to no longer honour the compromise agreement, approached the High Court in Pretoria for a declaratory order to the effect that SARS was bound to the said agreement entered into by him with SARS on 26 May 2014 in terms of the provisions of the TAA.

The crisp issue to be decided by the court was whether SARS, as a result of alleged non-disclosures and misstatements made by the applicant, who expressly had warranted the truth of the facts furnished by him, was no longer bound by the compromise agreement in terms of section 205(*a*) to (*c*) of the TAA.

SARS contended that he was no longer bound by the compromise agreement on the following grounds:

- Malema had failed to identify the donor who had offered to donate R4 million to him and to see that donations tax was declared and paid resulting from the compromise amount being allegedly paid by donations;
- Malema had failed to keep his tax affairs current and paid up to date as

provided for in the compromise agreement, in that he, *inter alia*, had failed to see to it that the donations tax resulting from part of the compromise amount being paid by donations had been paid and had failed to make payment of the previously acknowledged liability for the additional 2011 and 2012 assessments and, in fact, subsequently proceeding to object against the said assessments and had failed to declare the donations received by his attorney.

- Malema had made further misstatements in the request for the compromise, in that, for instance, he was a beneficiary of the JSM Trust and that the Trust had been formed to assist him to pay his tax liability, although that was not the case and it was also alleged that the JSM Trust had failed to keep its tax affairs in order.

The applicant had contended, *inter alia*, as follows:

- That SARS' decision that he was no longer bound by the compromise agreement was unlawful;
- That the matter could have been treated as unlawful administrative action but Malema had elected to treat it as one of private and not public law;
- That SARS, as an organ of state, played a special role and had to conform with the prescripts of the Constitution and his rights to human dignity, freedom of trade, occupation and profession, property and administrative action, had to be complied with by SARS;
- That he had not unequivocally accepted liability for the 2011 and 2012 assessments and, in any event, the amounts were not taxable as income in his hands as they were dividends or donations;
- That the issue whether the JSM Trust's tax affairs were regularised or otherwise had nothing to do with his rights and obligations under the compromise agreement.

Judge Jansen held the following:

<u>As to the origin of the tax dispute</u>

(i) That the real dispute between Malema and SARS was how the donations and dividends received by the applicant during the period 2005 to 2012 should be classified. These donations and dividends were classified by SARS as income in the applicant's hands and SARS had raised the aforementioned assessments. The applicant had contended that the amounts in question were not taxable income and that the donations were made out of generosity or disinterested benevolence and that the dividends received were not taxable.

(ii) That the dispute between Malema and SARS seemed to be purely factual, i.e. were the monies indeed donations and/or dividends.

(iii) That the high water mark of SARS' case seemed to be the allegations that the applicant did not make full and frank disclosure and failed to keep his tax affairs current and these allegations are in dispute.

<u>As to the provisions of the Tax Administration Act 28 of 2011</u>

(iv) That in terms of section 192 of the TAA, a compromise of a debt can only take place when the liability to pay the debt is not disputed by the debtor.

(iv) That one of the pitfalls of a compromise for a taxpayer is that he or she loses their right to object to a debt and the right to appeal an assessment. Hence, SARS cannot be allowed to enter into a compromise with a taxpayer only to deny its validity based on unwarranted grounds. An onus lies on SARS as well, to secure the highest net income from a tax debt and to enter into compromises on an informed basis. Thus section 100(4) of the TAA entitles senior SARS officials to require that an application for compromise be supplemented by further information.

(v) That a SARS official entering into a compromise has all the obligations set out in section 202 of the TAA and in terms of section 203(b) when a debtor's tax affairs are not up to date, no senior SARS official may compromise a tax debt.

(vi) That in terms of section 200(4) of the TAA, once a senior SARS official and a debtor have signed a compromise agreement setting out the amount to be paid in full satisfaction of the debt, SARS must give an undertaking that it will not pursue the recovery of the balance of the tax debt and the only circumstances when SARS is not bound by a compromise are set out in section 205 of the Act.

(vii) That in order to determine whether a term is 'material' to a contract, it must be gauged as to how 'vital' the term is, as was held in O'Connell v Flischman [1948] 4 All SA 74 (1948 (4) SA 191) (T).

(ix) That, regarding the non-disclosure of the Bendor Property, SARS claimed that the applicant intentionally did not disclose his interest and noted that such fraud would always be material. In regard to the other four grounds relied upon by SARS to state that it was no longer bound by the compromise agreement, SARS did not contend that Malema had intentionally misled it. As already pointed out, negligence was alleged on the part of Malema in respect of the R2,4 million paid to Brian Kahn attorneys but SARS did state in its heads of argument that it was not for this court to decide this issue.

(x) That, what was apparent though, was that SARS had alleged that any misstatement or failure to make a disclosure was automatically material but, as stated, it was then not understood why the word 'material' was necessary or used in section 205 of the Act.

(xi) That when the applicant made his first request for a compromise, he had informed SARS of the existence of the Bendor property and thus SARS knew about the offer to purchase yet nonetheless had deemed it fit to enter into a compromise agreement with Malema.

<u>As to the referral to trial</u>

(xii) That at the hearing Malema requested that not only the issue of the Bendor property but the entire application be referred to trial because of the factual disputes in the application.

(xiii) That, in addition to the issue of the Bendor Property, which the court was not in a position to decide on affidavit, the other issues, which gave rise to SARS declaring that it was no longer bound by the compromise agreement, were equally difficult to decide on the conflicting versions set out in the affidavits.

(xiv) That even though SARS sought to argue that it was merely a matter of interpretation, it could not be discounted that the information available to the parties and the reasons and facts upon which they had entered into the compromise agreement may be relevant.

(xv) That the less said about the correct legal interpretation of section 205 of the Act, at this stage, the better. Whether SARS' or Malema's interpretation of the compromise agreement was correct, cross-examination in respect of the parties' knowledge of the facts and the circumstances attendant upon the compromise being entered into, will bring clarity to matters of great importance to all the parties.

(xvi) That cross-examination may even demonstrate that SARS would in any event have entered into the compromise agreement had it been aware of all the facts which SARS contended Malema did not disclose or had disclosed inaccurately or incompletely – to prove the exact opposite.

(xvii) That to reach a conclusion on the facts set out in the affidavits may very well lead to an incorrect conclusion and the use of the word 'material' in section 205 of the Act must be given some meaning and whether facts are to be termed 'material' does not, necessarily, merely entail an objective test.

(xviii) That the facts which persuaded SARS to enter into the compromise agreement and, thereafter, to adopt the stance that it is no longer bound thereby, will contextualise the said agreement and give rise to fertile grounds for cross-examination as may the knowledge on the part of Malema when he entered into the compromise agreement and furnished, or failed to furnish, certain facts.

(xix) That when regard is had to the evidence before the court, it is a veritable quagmire and there were genuine disputes of fact that had arisen that warranted a referral of the application to trial. Moreover, Malema had seriously engaged with the factual allegations it sought to challenge and had furnished not only an answer but also countervailing evidence, where such facts fell within his personal knowledge.

(xx) That motion proceedings, unless concerned with interim relief, are about the resolution of legal issues based on common cause facts. Factual issues cannot be resolved to establish probabilities and in circumstances where Malema's version cannot be rejected as being clearly without merit, the only way in which the factual issues can be resolved is by way of viva voce evidence.

(xxi) That to what extent the alleged flaws in the facts provided to SARS can be attributed to intent on the part of Malema, and to which extent they can be termed material to allow SARS to assert that it is no longer bound by the compromise agreement, were issues that SARS wished to have resolved on affidavit. Put simply, the only conclusion that can be drawn for SARS' argument was that any non-compliance with the terms of the compromise agreement was material but logic dictated that this was not the case but depended on the facts attendant upon the compromise agreement being entered into. In any event, fraud cannot be decided on affidavits but SARS was careful not to allege fraud in relation to the other four grounds which caused it to adopt the attitude that it was no longer bound by the compromise agreement.

(xxii) That it did not avail SARS to state that it mattered not whether the non-disclosures and inaccuracies were intentional. By adopting this stance SARS was seeking to force the matter to be heard on the affidavits and, given the fact that the fifth ground advanced by SARS was, in any event, fraud, this issue had to be referred to trial. Moreover, all the issues should then be referred to trial in order to obtain clarity regarding the correct facts upon which the matter should be adjudicated. Should the conduct of the applicant have been fraudulent in all respects, SARS would then have no difficulty in persuading a court that it was not bound by the compromise agreement.

(xxiii) That, accordingly, for the aforementioned reason, and in an exercise of the court's discretion, the matter is referred to trial.

6. INTERPRETATION NOTES

6.1. Small Business Corporations (SBC) – No. 6 (Issue 2)

This Note provides guidance on the interpretation and application of section 12E which provides accelerated depreciation allowances for a taxpayer that qualifies as an SBC.

This Note does not address other sections in the Act which contain provisions that refer to or are applicable to a 'small business corporation' as defined in section 12E. For example, section 8FA(3)(*a*) provides that section 8FA, which deems hybrid interest to be a dividend in specie, does not apply to a debt owed by an SBC. Section 8FA is not discussed in this Note.

Section 10(1)(*z*K) and section 23O apply when an amount of funding has been received by or accrued to an SBC from a 'small business funding entity' as defined in section 1(1). Generally, these sections provide for the exemption of such receipts and accruals and the reduction of the deduction available for related expenditure. In this regard, this Note considers only the impact of such receipts and accruals on the allowances available under section 12E(1) and section 12E(1A).

Some of the requirements in section 12E refer to the Companies Act. This Note discusses those requirements with reference to that Act, but does not discuss the requirements, which may have been different in some respects, when the Act previously referred to the Companies Act No. 61 of 1973.

Section 12E sets out the requirements which must be met in order for a specified entity to qualify as an SBC. It provides accelerated depreciation allowances on certain capital assets brought into use by an SBC.

In addition, section 5(2) and the annual Rates and Monetary Amounts and Amendment of Revenue Laws Acts provide for concessionary tax rates which follow a graduated marginal structure (0%, 7%, 21% and 28%)[1] as opposed to a flat corporate rate of 28%.

The ITR14 return contains a question asking taxpayers whether they are an SBC as referred to in section 12E. The question must be answered 'yes' if a taxpayer meets the requirements of an SBC as stipulated in section 12E. If the question is answered 'yes', a further set of questions relating to section 12E will be asked within the return. The answers to these additional questions will determine whether the taxpayer will be assessed as an SBC for that year of assessment.

Section 12E sets out the requirements for a 'close corporation', 'co-operative' or 'private company' as defined in section 1 of the Companies Act to qualify as an SBC. All the holders of shares in the SBC must be natural persons who may not hold shares in other unlisted companies (with some exceptions), its turnover for the year may not exceed R20 million and not more than 20% of its receipts and accruals, other than those of a capital nature, plus capital gains may consist of 'investment income' and income from rendering a 'personal service'. In addition, the entity may not be a 'personal service provider' as defined in the Fourth Schedule.

Section 12E provides for an accelerated depreciation allowance on certain capital assets acquired and brought into use by an SBC. There are two sets of accelerated depreciation rates which may apply. Subject to certain conditions, assets used directly in a process of manufacture or process of a similar nature, may qualify for a 100% write-off of cost in the year of assessment in which the asset is brought into use. Assets that do not fall into this category may be subject to a write-off under section 12E(1A), the amount of which may, at the election of the SBC, be calculated under the provisions of section 11(*e*) or over a period of three years at a rate of 50%, 30% and 20% of cost in the respective years. The term 'cost' is specifically defined in section 12E(2). In addition to the accelerated depreciation allowance the section also deals with the deduction of costs incurred in moving assets which fall within the ambit of the section.

SBCs are subject to concessionary tax rates which follow a graduated marginal structure and are not taxed at the corporate tax rate of 28%.

In order to qualify as an SBC an entity must meet the requirements of section 12E in each year of assessment.

6.2. *VAT treatment of the supply of goods or services to and / or from a Customs Controlled Area of an Industrial Development Zone – No. 40 (Issue 3)*

The purpose of this interpretation note is to set out the VAT implications concerning the various types of supplies of goods or services to and/or from a CCAE/IDZ Operator located in a CCA of an IDZ.

The Department of Trade and Industry (the Department) developed an IDZ Programme with the aim of attracting foreign and local direct investment intended to develop the economic potential of specific geographical areas in South Africa. The IDZ Programme was established in Government Notice R. 1224 on 1 December 2000 by the Minister of Trade and Industry under section 10(1) of the Manufacturing Development Act, No. 187 of 1993 by the promulgation of the IDZ Regulations, concerning the regulation, development and operation of IDZs.

In terms of the IDZ Regulations, the Minister of Trade and Industry may, by notice in the *Government Gazette,* designate a geographical area adjacent to an international harbour or airport, as an IDZ. An IDZ can be described as a geographically designed, purpose-built industrial estate that is linked to an international harbour or airport in an area in South Africa which has been designated by the Minister of Trade and Industry and which contains a delimited fully secured CCA (or multiple CCAs) where CCAEs will operate and obtain certain benefits and privileges.

An IDZ will be built and operated by an IDZ Operator to whom an IDZ Operator permit was issued by the Minister of Trade and Industry. The IDZ Operator will be responsible for the development, security and maintenance of the IDZ (including the CCA). The IDZ Operator will offer facilities tailored for the manufacture, storage and distribution of goods to boost beneficiation, investment, economic growth and, most importantly, the development of skills and employment in these regions.

6.3. Year of assessment of a company: Accounts accepted to a date other than the last day of a company's financial year – No. 90

This Note provides guidance on the application of section 66(13C) and the discretionary power vested in SARS to accept financial accounts of a company for a period ending on a day which differs from the last day of the company's financial year.

Section 3(1) provides that the powers conferred and duties imposed upon SARS by or under the provisions of the Act, may be exercised or performed by the Commissioner or by any officer under the control, direction or supervision of the Commissioner.

The equivalent of a year of assessment for a foreign company is a 'foreign tax year' as defined in section 1(1). The closing date of financial accounts of a foreign company does not fall within the scope of this Note.

Interpretation Note No. 19 (Issue 4) dated 15 February 2016 'Year of Assessment of Natural Persons and Trusts: Accounts Accepted to a Date other than the Last Day of February', provides guidance on SARS' discretionary power to grant permission to a natural person or trust to submit financial accounts for a period which differs from the year of assessment ending on the last day of February.

Companies are occasionally required to close their financial accounts earlier or later than the last day of their financial year owing to various reasons. Section 66(13C) was introduced into the Act with effect from 3 July 2008 to allow companies to align reporting for tax purposes with the period ending on the day on which their financial accounts are closed.

7. BINDING PRIVATE RULINGS

7.1. BPR 243 – Termination of a subcontracting agreement and implementing of a toll manufacturing arrangment

This ruling determines whether the termination of a subcontracting agreement including a concomitant supplies plan between connected persons and the implementation of a toll manufacturing arrangement will have capital gains tax consequences.

In this ruling references to paragraphs are to paragraphs of the Eighth Schedule to the Income Tax Act applicable as at 9 May 2016. Unless the context indicates otherwise any word or expression in this ruling bears the meaning ascribed to it in the Act.

This is a ruling on the interpretation and application of the provisions of:

- paragraph 1 – definition of 'asset'; and
- paragraph 11(1)(*b*).

<u>Parties to the proposed transaction</u>

The Applicant: A company incorporated in and a resident of South Africa

The Co-Applicant: A company incorporated in and a resident of South Africa which is a wholly-owned subsidiary of the Applicant

<u>Description of the proposed transaction</u>

The Applicant's business involves the marketing of agriculture related raw material and products that can be manufactured therefrom and logistics concerning those.

The Co-Applicant's business constitutes the processing of the agricultural related raw material, marketing and distributing of the processed products and the management of logistics at loading facilities at a local port of entry.

As part of the Applicant's ordinary business operations it entered into a memorandum of agreement (MOA) with Company X, a non-resident entity, for the sale of one of its products (product A) on, amongst others, the following material terms:

- The Applicant is authorised to subcontract the supply of product A under the MOA to the Co-Applicant, provided that in so doing, the Applicant shall not –
  - in any way be relieved from its obligations under the MOA; or
  - be entitled to any greater protection from liability under the MOA than it otherwise would have had if it had not subcontracted the supply of product A to the Co-Applicant.
- The Applicant may authorise the Co-Applicant to issue an invoice to Company X and to collect payment in the Co-Applicant's own name from Company X after which Company X's obligation to the Applicant is fully performed.
- The MOA shall have an initial term of two years. It will automatically be renewed for a further year on the same terms and conditions, unless either party gives written notice to the other party of its intention not to renew prior to the expiry of the initial two year term.

In terms of its current business model, and specifically with reference to the MOA, the Applicant implements its contract of its manufacturing business of product A with the Co-Applicant as follows:

- The Applicant enters into a 12 month supplies plan with the Co-Applicant in terms of which the Applicant supplies the raw material to the Co-Applicant for consideration. Ownership of the raw material passes to the Co-Applicant upon the supply thereof.
- The Applicant does not have formal written agreements in place with the Co-Applicant. The supplies plan is entered into in advance and is updated throughout the year to meet the Co-Applicant's distribution requirements. The Co-Applicant's production plan per week or month becomes the raw material order that the Applicant is required to supply to the Co-Applicant.
- The Co-Applicant processes the raw material. This process of manufacture produces product A.

The Co-Applicant may therefore effectively sell product A to Company X for consideration, issue invoices and collect payments.

On the renewal of the MOA, Company X was informed that the Applicant intends changing its business model. The Applicant will no longer subcontract its rights under the MOA, but it will supply raw material to the Co-Applicant under a toll manufacturing arrangement. The relevant terms of the toll manufacturing arrangement will be as follows:

- The Co-Applicant will manufacture product A for the Applicant in terms of the toll manufacturing arrangement, in accordance with the Applicant's specifications. Ownership of the raw material will remain with the Applicant.
- The Co-Applicant will charge a fee for the services rendered to the Applicant.
- The Applicant will sell the manufactured product A directly to various third party buyers, including Company X. The Applicant will undertake all the business functions, such as the marketing and distribution, previously performed by the Co-Applicant.
- The Co-Applicant will continue to manage the loading logistics at the local port of entry and to charge a fee to the Applicant. Other administrative duties related to orders placed by Company X will be carried out by the Applicant.

Conditions and assumptions

This binding private ruling is not subject to any additional conditions and assumptions.

Ruling

The ruling made in connection with the proposed transaction is as follows:

- The termination of the subcontracting agreement including the concomitant supplies plan between the Applicant and the Co-Applicant, and the implementation of the toll manufacturing arrangement in accordance with the proposed transaction will not constitute a disposal of an asset as contemplated in the Eighth Schedule. The proposed transaction will not give rise to a capital gains tax liability for the Applicant.

7.2. BPR 244 – Disposal of an undivided interest in immovable property by way of an amalgamation transaction

This ruling determines whether the proposed transaction will qualify as an 'amalgamation transaction' as defined in section 44(1) and whether the resultantcompany will qualify to claim the allowance under section 13*quin*.

In this ruling references to sections are to sections of the Income Tax Act applicable as at 21 June 2016. Unless the context indicates otherwise any word or expression inthis ruling bears the meaning ascribed to it in the Act.

This is a ruling on the interpretation and application of the provisions of:

- section 1(1) – definition of 'trading stock';
- section 13*quin*;
- section 41(1) – definition of 'trading stock'; and
- section 44(1), (3) and (6).

<u>Parties to the proposed transaction</u>

The Applicant: A company incorporated in and a resident of South Africa

The Co-Applicants: Companies incorporated in and residents of South Africa and a trust established in and a resident of South Africa

The Amalgamated Companies: Companies incorporated in and residents of South Africa that are collectively 100% held by the Co-Applicants

The Rental Company: A company incorporated in and a resident of South Africa that is 100% held by the Amalgamated Companies collectively

<u>Description of the proposed transaction</u>

The current shareholder structure of the parties consists of the Co-Applicants, the Amalgamated Companies and the Rental Company (group).

The Amalgamated Companies own an undivided interest in properties that form part of the same property complex. This creates complexities to obtain funding at competitive interest rates and on terms for further development and improvements to the properties.

The proposed transaction (merger) is aimed to reduce the number of existing entities in the group and to rationalise the ownership and management of assets in a manner that reflects the commercial reality of the property interests owned by the companies in the group.

Prior to the merger, the only assets that will be owned by the Amalgamated Companies will be the undivided interests in the properties and the shares in the Rental Company. The Rental Company acts as a rental collection agency. None of the Amalgamated Companies will have any liabilities at the time of the proposed merger.

Certain improvements on the properties owned by the Amalgamated Companies qualify for the allowance under section 13*quin*.

The steps for implementing the merger will be as follows:

- The Amalgamated Companies will dispose of their assets to the Applicant. As consideration, the Applicant will issue shares to the Amalgamated Companies (consideration shares). The Amalgamated Companies will take the necessary steps, set out in section 41(4), to deregister.
- The Amalgamated Companies will distribute the consideration shares to their shareholders (Co-Applicants).
- Once deregistration of the Amalgamated Companies have been completed, the shares held by the Co-Applicants in the Amalgamated Companies will be cancelled for no consideration.
- The Co-Applicants do not intend to dispose of the shares in the Applicant subsequent to the merger.
- The proposed transaction will form part of and involve a merger as contemplated in section 113 of the Companies Act, 2008.
- After the merger the Co-Applicants will hold shares in the Applicant that, in turn, will own the undivided interest in the property complex.
- The Applicant will incur significant improvement and expansion expenditure

in respect of the property complex following the merger, to be funded partly by its shareholders and partly by external funders.

Conditions and assumptions

This binding private ruling is not subject to any additional condition and assumption.

Ruling

The ruling made in connection with the proposed transaction is as follows:

- The proposed transaction to be entered into by each of the Amalgamated Companies will each be an 'amalgamation transaction' as defined in section 44(1);
- The Applicant will be entitled to claim the section 13*quin* allowance on the buildings in respect of which the respective Amalgamated Companies were entitled to claim that allowance;
- No ruling is made as to whether the Co-Applicants will hold the consideration shares on capital or revenue account, but the Co-Applicants will qualify for the relief under section 44(6) in either event.

7.3. BPR 245 – Time of accrual of short-term insurance premiums and time of supply of security provide to the master of the High Court

This ruling determines the time of accrual of gross income and time of supply of any service in relation to a guarantee policy for security issued to the Master of the High Court by a liquidator.

In this ruling references to sections are to sections of the Income Tax Act and the VAT Act applicable as at 15 June 2016. Unless the context indicates otherwise any word or expression in this ruling bears the meaning ascribed to it in the relevant Act.

This is a ruling on the interpretation and application of the provisions of:

- the Act
    - section 1(1) – definition of 'gross income'.
- the VAT Act
    - section 1(1) – definition of 'invoice';
    - section 9; and
    - section 20.

Parties to the proposed transaction

The Applicant: A company incorporated in and a resident of South Africa

The Liquidators: Liquidators and Trustees of insolvent estates, Executors of deceased estates and Curators

The Master: The Masters of the various divisions of the High Court

Description of the proposed transaction

The Applicant is a short-term insurer registered with the Financial Services Board under the Short-Term Insurance Act. It specialises in the field of providing security to the Master for the due compliance with their statutory obligations by Liquidators in terms of, amongst others, sections 56 and 57 of the Insolvency Act and section 23 of the Administration of Estates Act.

The Applicant provides security in the form of security bonds to the satisfaction of the Master on behalf of the Liquidators by issuing a security bond on behalf of the Liquidators for the proper performance of their duties.

The terms on which the security bond is provided are contained in prescribed form J468 (known as an undertaking and bond of security) which is duly signed by the Liquidator read with the security details provided by the Applicant. Should the Liquidator fail to perform his or her obligations as required, a certificate under the hand of the Master stating the amount of resulting loss or damage shall then be accepted as *prima facie* proof of that failure and of the extent of the loss or damage.

The security bond makes no reference to any premium in respect thereof. The Applicant provides the Liquidator with a confirmation of bond of security details notice. This notice confirms the existence of the guarantee policy as well as the manner in which any premium is to be calculated.

The Applicant and the Liquidator agree as follows with regards to payment of any premium that might become due and payable:

> 'The Insurer shall remain fully on risk with regard to the provision of the security bond and shall only become unconditionally entitled to raise any premium(section) in respect of the full duration that the security bond remains in place as is required by the Master, as and when the Liquidator has ascertained that there are sufficient funds in the estate to make payment thereof and the Liquidator is in a position to provide satisfactory proof to the Insurer that the duties of the appointment for which the court bond is required, has been completed.'

The Applicant is at risk from the date on which the bond of security is issued for an indefinite period until the liquidation of the estate is finalised. Only once the estate has funds and has made payment to the Applicant, or when the estate has been finalised and funds have become available, whichever is the earlier, will a tax invoice be issued by the Applicant to the Liquidator.

The Applicant provides the Liquidator with a confirmation of bond of security details notice on an annual basis, as the Master may have amended the amount of the security bond required.

The Applicant will reinsure its risks with a third party, but no premiums will become payable or will accrue to the reinsurer until such time as a conclusion is reached, as to the assets and liquidity within the estate. Once a conclusion is reached, a tax invoice will be issued and payment will be made in the normal course.

<u>Conditions and assumptions</u>

This binding private ruling is not subject to any additional conditions and assumptions.

<u>Ruling</u>

The ruling made in connection with the proposed transaction is as follows:

- The premiums will accrue to the Applicant as 'gross income', as defined in section 1(1) of the Act, as follows:

- in relation to the free residue of an estate – when it is ascertained that there are sufficient funds in the estate to pay the pplicant's costs; and
- in relation to a sale of property subject to security (a special mortgage, landlord's legal hypothec, pledge, or right of retention) – the date that the proceeds on the sale of secured assets are received, as provided for by section 89(1) of the Insolvency Act, and if the proceeds are sufficient to cover the costs of security.

- The confirmation of bond of security details notice will not constitute an 'invoice' as defined in section 1(1) of the VAT Act.
- For purposes of the VAT Act the time of supply of the service will be the time any payment or consideration is received in accordance with Binding General Ruling (VAT): No. 14 (Issue 2) dated 18 March 2016.

7.4. BPR 246 – Debt reduction and capitalisation

This ruling determines the tax consequences for the Applicant of a proposed settlement of a shareholder's debt and the subsequent issue of preference shares.

In this ruling references to sections and paragraphs are to sections of the Income Tax Act and paragraphs of the Eighth Schedule to the Act applicable as at 4 August 2016. Unless the context indicates otherwise any word or expression in this ruling bears the meaning ascribed to it in the Act.

This is a ruling on the interpretation and application of the provisions of:

- section 8(4)(*a*);
- section 19; and
- paragraph 12A.

<u>Parties to the proposed transaction</u>

The Applicant: A private company incorporated in and a resident of South Africa

The Partnership: An *en commandite* partnership formed in and a resident of South Africa

Description of the proposed transaction

The Partnership holds 64,69% of the ordinary shares in the Applicant. The remainder is held by seven different shareholders. Some years ago, the Partnership advanced funding to the Applicant by way of unsecured, fixed rate debentures (the debentures).

The precarious financial position of the group, of which the Applicant forms part, has necessitated a debt restructuring. As part of that debt restructuring the following steps will be implemented:

- The Applicant will obtain bridging funding from a bank for the amount due under the debentures.
- The Applicant will redeem the debentures for their full value, including all accrued but unpaid interest together with all other amounts that may be payable by the Applicant in accordance with the terms of the debentures (redemption proceeds), by way of electronic funds transfer into a banking account designated by the Partnership.
- The Partnership will subscribe for preference shares and will direct the designated bank to pay, by way of electronic funds transfer, an amount equal to the redemption proceeds into a banking account designated by the Applicant.
- The Applicant will allot and issue the preference shares to the Partnership as fully paid-up and will deliver the share certificates to the Partnership.
- The Applicant will repay the external bridging funding, using the proceeds from the issue of the preference shares.

Conditions and assumptions

This binding private ruling is not subject to any additional conditions and assumptions.

Ruling

The ruling made in connection with the proposed transaction is as follows:

- The redemption of the debentures at full value will not be subject to the provisions of section 19 or paragraph 12A of the Eighth Schedule. Accordingly, section 19(6) will not deem an amount to have been received or recouped by the Applicant for purposes of section 8(4)(*a*), to the extent that the amount outstanding on the debentures includes interest for which a deduction or allowance was permitted in terms of the Act.
- In the absence of section 19 applying, section 8(4)(*a*) will also not apply in consequence of the redemption of the debentures for an amount that includes accrued but unpaid interest, since there will be no amount to be recovered or recouped by the Applicant.

Note

This ruling does not cover the application of any general anti-avoidance provision to the proposed transaction.

7.5. BPR 247 – Employer contribution to foreign social and pension funds in respect of a non-resident

This ruling determines the tax consequences of employer contributions to a foreign social and pension fund in respect of a non-resident person working in South Africa.

Unless the context indicates otherwise any word or expression in this ruling bears the meaning ascribed to it in the Income Tax Act.

This is a ruling on the interpretation and application of the provisions of the Act:

- section 1(1) – definition of 'gross income'; and
- paragraph 1 of the Fourth Schedule – definition of 'remuneration';
- paragraph 2(1) of the Fourth Schedule; and
- paragraph 2(*k*) and (*l*) of the Seventh Schedule.

Parties to the proposed transaction

The Applicant: A company incorporated in and a resident of South Africa

Person A: A natural person who is not a resident of South Africa

Company B: A company incorporated outside and not a resident of South Africa, which is the parent company of the Applicant

Description of the proposed transaction

The Applicant intends to employ Person A on a three year fixed term employment contract, in terms of an inter-company work permit arrangement. The Applicant will be responsible for the payment of the remuneration of Person A.

Company B currently employs Person A, whose employment is regulated by a collective bargaining agreement. This agreement stipulates, amongst other things, that social protection for nationals expatriated outside the country of residence of Person A must be equivalent to that which that person would have received in his or her country of residence.

Because there is no social security system in South Africa, the group must maintain social security contributions for Person A, through accredited parastatal service providers. These contributions are compulsory. Neither the host company nor the employee can opt out of these contributions.

The contributions are to be paid to parastatal service providers, recognised by the national social security system, which administer the relevant social funds. The social funds provide cover in the form of a pension fund, workman's compensation, base medical coverage, death, disability and unemployment insurance.

In addition to the social funds, the group has also set up a private pension fund to which an amount is to be paid over as an employer contribution. The contributions to the pension fund are not compulsory under the bargaining agreement but are required by virtue of the employment contract.

The obligations in respect of the social funds and the pension fund rest solely upon the employer. No co-contributions will be required from the employee and no amounts are to be paid on the employee's behalf in respect of such contributions.

Company B will pay the contributions in respect of the social funds and pension fund to the relevant service providers and will recharge these costs to the

Applicant, which will be obliged to reimburse Company B.

Conditions and assumptions

This binding private ruling is not subject to any additional conditions and assumptions.

Ruling

The ruling made in connection with the proposed transaction is as follows:

- The social security and pension fund contributions to be made by the Applicant to Company B in respect of Person A will not be subject to income tax in the hands of Person A.
- The social security and pension fund contributions to be made by the Applicant to Company B in respect of Person A will not give rise to a withholding obligation on the Applicant under the Fourth Schedule to the Act.

8. BINDING CLASS RULING

8.1. BCR 54 – Employer-provided accommodation

This ruling determines whether vacant stands to be acquired by qualifying employees from their employer will constitute 'immovable property' as contemplated in paragraph 5(3A) of the Seventh Schedule to the Act.

In this ruling references to paragraphs are to paragraphs of the Seventh Schedule to the Income Tax Act as at 15 October 2015. Unless the context indicates otherwise any word or expression in this ruling bears the meaning ascribed to it in the Act.

This is a ruling on the interpretation and application of the provisions of:

- paragraph 2(*a*); and
- paragraph 5(1), (2) and (3A).

Class

The class members to whom this ruling will apply are qualifying employees.

Parties to the proposed transaction

The Applicant: A company incorporated in and a resident of South Africa

Qualifying Employees: Permanent employees of the Applicant

Description of the proposed transaction

The Applicant is a mining company that is subject to the Mineral and Petroleum Resources Development Act No. 28 of 2002 (MPRDA) and the broad-based socio-economic empowerment Charter for the South African mining and minerals industry (mining charter). It follows that the Applicant is required to comply with its obligation under the MPRDA and the mining charter to improve the housing standards of its employees.

The Applicant intends to sell vacant stands (stands) to its Qualifying Employees on terms that, amongst others, oblige each Qualifying Employee purchaser to erect a house on the stand at the employee's own cost within a specified time period.

The purchase price of each stand will be less than the market value of the stand.

Conditions and assumptions

This binding class ruling is not subject to any additional condition and assumption.

Ruling

The ruling made in connection with the proposed transaction is as follows:

- The stands constitute 'immovable property' as envisaged in paragraph 5(3A). No value will be placed on a stand so acquired by a Qualifying Employee if:
    - the market value of the stand does not exceed R450 000 on the date of acquisition;
    - the remuneration proxy of the employee does not exceed R250 000 in relation to the year of assessment during which the stand is so acquired; and
    - the employee is not a connected person in relation to the Applicant.

9. GUIDES

9.1. Guide on the Determination of Medical Tax Credits

This guide provides general guidelines regarding the medical scheme fees tax credit and additional medical expenses tax credit for income tax purposes. It does not delve into the precise technical and legal detail that is often associated with tax, and should, therefore, not be used as a legal reference.

Expenditure of a personal nature may generally not be taken into account in determining a taxpayer's income tax liability, under South Africa's tax system. One of the notable exceptions relates to medical expenditure. South Africa is aligned with the practice in many other countries of granting tax relief for medical expenditure.

There are a number of reasons that tax systems provide such relief. One of the reasons is that serious injury or illness can present taxpayers with disproportionately high medical bills in relation to income, which can be difficult to meet. The resulting hardship affects a number of economic areas for taxpayers, including the ability to settle obligations to the *fiscus*, such as a tax bill.

Historically, South Africa utilised a deduction system to facilitate tax relief for medical expenditure. Allowances, subject to certain limits, were permitted to be deducted from income for contributions to medical schemes, as well as for out-of-pocket medical expenditure.

In 2012, tax relief for medical expenditure began a phased-in conversion from a deduction system to a tax credit system. The reason for the change was to eliminate vertical inequity relating to medical contributions: those at higher marginal tax rates received a larger reduction of tax payable than those on lower marginal rates, in respect of the same amount of medical expenditure. The purpose of the change was to spread tax relief more equally across income groups, thus bringing about horizontal equity – those who pay equal values for medical expenditure receive absolute equal tax relief.

A tax credit system differs from a deduction system in that, instead of permitting a deduction of the medical allowance against a taxpayer's income, the relief is granted as a reduction in tax payable. It therefore operates as a tax rebate.

The new dispensation has been phased in, and consists of a two-tier credit system:

1. A medical scheme fees tax credit (MTC) will apply in respect of qualifying contributions to a medical scheme; and
2. An additional medical expenses tax credit (AMTC) will apply in respect of other qualifying medical expenses.

The application of the additional medical expense tax credit system falls into three categories:

- Taxpayers under 65 years of age
- Taxpayers aged 65 years and older
- Taxpayers with a disability

In order to qualify for the 65 years and older category, the taxpayer must be 65 years or older on the last day of the relevant year of assessment, or would have been 65 years or older had the taxpayer died on the last day of the relevant year of assessment.

9.2. Guide on the Taxation of Franchisors and Franchisees

This guide considers the income tax implications of income received and expenditure incurred by franchisors and franchisees.

The growing franchise industry in South Africa is a major contributor to the South African economy. The rapid rate at which new franchises are entering the market has given rise to a need for clarity concerning the tax implications that arise in relation to franchise arrangements. More particularly, there is a need to examine the tax treatment of income received and expenditure incurred by both franchisors and franchisees. This guide focuses mainly on transactions between franchisors and franchisees that are resident in South Africa. The aim of this guide is to assist in clarifying uncertainties that may arise on the application of the tax laws to a franchise arrangement.

This guide is intended to provide clarity regarding some of the general issues pertaining to franchisors and franchisees in South Africa. Note that each case has to be considered on its own merits when determining the taxability of a franchisor and a franchisee. The terms and conditions of the franchise agreement, as well as the manner in which payments are construed, will be important in determining the tax implications of the different types of amounts received, or expenses incurred, by franchisors and franchisees.

9.3. Basic Guide to Tax-Deductible Donations

This guide has been prepared to assist organisations in understanding the basic requirements for obtaining and retaining approval under section 18A to issue receipts for tax-deductible donations. It does not go into comprehensive technical and legal detail and should therefore not be used as a legal reference. For comprehensive information on the tax treatment of PBOs see the *Tax Exemption Guide for Public Benefit Organisations in South Africa* (Issue 5).

Government has recognised that organisations are dependent on the generosity of the public and to encourage that generosity has provided a tax deduction for certain donations made by taxpayers.

The eligibility to issue section 18A receipts is restricted to specific organisations approved by the Commissioner which use the donations to fund specific PBAs.

9.4. Basic Guide to Income Tax Exemption for Public Benefit Organisations

This guide has been prepared to assist organisations in understanding the basic requirements to obtain and retain approval as a public benefit organisation.

The mere fact that an organisation has a non-profit motive or is established or registered as an NPO registered under the NPO Act, or is established as an NPC, does not mean that it automatically qualifies for preferential tax treatment or approval as a PBO.

An organisation will enjoy preferential tax treatment only after it has applied for and been granted approval as a PBO by the Commissioner, and continues to comply with the relevant prescribed requirements.

9.5. Guide to the Employment Tax Inventive

The employment tax incentive was introduced by the Employment Tax Incentive Act 26 of 2013 which was promulgated on 18 December 2013. This guide provides general guidance on the incentive.

The ETI is a temporary tax incentive that may be claimed by eligible employers and is aimed at encouraging such employers to employ young employees between the ages of 18 and 29, and employees of any age in special economic zones and in any industry identified by the Minister by notice in the *Government Gazette*. Payment of the incentive is effected by eligible employers being able to reduce the employees' tax due by them by the amount of the ETI that they may claim - provided of course that they meet the requirements of the ETI Act. The ETI is administered by SARS through the employees' tax system that is deducted and withheld and accounted for to SARS (usually monthly) via the Pay-As-You-Earn (PAYE) system.

As mentioned, the ETI is a temporary programme covering a period of three years in which an eligible employer may claim the ETI for a maximum of 24 individual months per qualifying employee. The ETI will be subject to continuous review of its effectiveness and impact in order to determine the extent to which its core objective of reducing youth unemployment is achieved. The ETI commenced on 1 January 2014 and will end on 1 January 2017. It applies to qualifying employees employed on or after 1 October 2013 by eligible employers.

9.6. VAT 404 – Guide to Vendors

The information in this guide is based on the VAT Act and the TA Act as at the time of publishing and includes the amendments contained in the Taxation Laws

Amendment Act 25 of 2015 and the Tax Administration Laws Amendment Act 23 of 2015 which were promulgated on 8 January 2016 as per *Government Gazette* 39588 and *Government Gazette* 39586, respectively.

Some of the amendments as per GG 39588 and GG 39586 which came into effect from 8 January 2016 are briefly discussed below.

(a) Period of limitation for issuance of additional VAT assessments

Section 41(d) has been deleted to give effect to the provisions of the TA Act that SARS may not assess an amount of tax after five years from the date the amount became payable, subject to a few exceptions.

(b) The particulars required on a full tax invoice

A fully compliant tax invoice envisaged in section 20 can now reflect either the words 'Tax invoice', 'VAT invoice' or 'invoice'. Also, although the words 'Tax invoice' or 'VAT invoice' or 'invoice' do not have to appear in a prominent place, they must nevertheless appear on the document.

The amendments below came into effect from 1 April 2016:

(a) Commercial accommodation activities

Certain changes have been made to the VAT Act regarding enterprises which supply commercial accommodation, as follows:

- Enterprise supplying commercial accommodation

  Paragraph (a) of the definition of 'commercial accommodation' (lodging or board and lodging, together with domestic goods and services) was amended to remove the monetary threshold required to be met in order for the supply thereof, to constitute the supply of commercial accommodation. The definition of 'enterprise' now contains a monetary threshold of R120 000 which is required to be met for commercial accommodation activities to be regarded as an enterprise.

- Domestic goods or services

  The definition of 'domestic goods or services' provided as part of an enterprise supplying commercial accommodation referred to above has been expanded to include 'water'.

(b) Documentary proof to substantiate input tax and other deductions

The following changes have been made to the VAT Act regarding documentary proof required to substantiate deductions in the calculation of the tax payable or refundable by a vendor:

- Section 16(2)(f)

  The VAT Act has been amended to set out the documentary requirements which must be met to substantiate the entitlement to other deductions referred to in section 16(3)(c) to (n). These documentary requirements are set out in an interpretation note.

- Section 16(2)(g)

  Section 16(2)(g) has been introduced to provide relief to recipient vendors who are unable to obtain the prescribed documentation under section 16(2)(a) to (f). The relief is available under certain circumstances prescribed by the Commissioner provided the minimum required information is held at the time a return in respect of the deduction is furnished.

(c) Zero-rating the supply of vocational training services

The VAT Act was amended to ensure that vocational training services provided for the benefit of an employer (who is not a resident) via a third party vendor which complies with all the other requirements of section 11(2)(r), will be subject to the zero-rate.

(d) Time of supply rules for connected persons and undetermined amounts

When a supply is made between connected persons, special time of supply rules set out in section 9(2)(*a*) apply. For example, in the case of the supply of goods, the time of supply is triggered when the goods are removed or made available. However, if the value of the supply of goods or services cannot be determined at the time the supply is deemed to be made under this provision, the correct amount of output tax cannot be calculated.

However, in terms of the proviso added to section 9(2)(*a*), these special time of supply rules will not apply if the supply is between wholly taxable connected persons and the consideration cannot be determined at the time that the supply is deemed to be made. The special time of supply rules under section 9(2)(*a*) however apply where the recipient is not able to deduct the VAT incurred as input tax in full. In this instance, under the amended section 10(4)(*a*), the consideration is deemed to be the open market value (OMV).

(e) The services supplied by a cartage contractor

The wording of section 11(1)(m)(ii) was amended to align with Interpretation Note 30 'The Supply of Movable Goods as Contemplated in Section 11(1)(*a*)(i) read with Paragraph (*a*) of 'Exported' and the Corresponding Documentary Proof'. The phrase 'main activity' was changed to read 'activities include' to allow the zero-rating of goods to apply even if the goods were delivered by a cartage contractor whose activities are not solely the transportation of goods. The enterprise activity of the person delivering the goods merely has to include the transportation of goods. The cartage contractor is also no longer required to be a registered vendor in South Africa.

The following amendment becomes effective from 1 April 2017:

(f) Removing the zero-rating for the National Housing Programme

Sections 11(2)(*s*) and 8(23) will deleted.

In addition to the amendments as per GG 39588 and GG 39586, the following regulations have been promulgated, or amendments became effective since the last publication of the VAT 404:

(g) Voluntary VAT registration

The VAT Act was amended by expanding the scope of voluntary registration by allowing persons who meet certain conditions set out in regulations issued under section 23(3)(*b*) and (*d*) to apply for voluntary registration. The regulations as contemplated under section 23(3)(*b*)(ii) were issued by the Minister of Finance (the Minister) under Government Notice R447 published in *Government Gazette* 38836 of 29 May 2015 (R447). These regulations set out the exceptional circumstances under which a person who has not made taxable supplies in excess of R50 000 may be allowed to register voluntarily. The Minister also issued regulations as contemplated in section 23(3)(*d*) under Government Notice R446 published in *Government Gazette* 38836 of 29 May 2015 (R446). These regulations set out business activities in respect of which a person may be allowed to voluntarily register where it is only possible to make taxable supplies after a certain period of time.

(h) Elimination of the four monthly tax period for small businesses

With effect from 1 July 2015, the four monthly tax period known as 'Category F' is no longer available.

10. DRAFT GUIDES

10.1. Updated draft guide: Special Voluntary Disclosure Programme

- This is a preliminary guide which is subject to Parliamentary legislative processes, and this version is based on the proposals to Parliament following the latest round of public comments.
- The guide is meant to assist prospective applicants in preparing for the commencement of the Special Voluntary Disclosure Programme that was proposed by the Minister of Finance in his 2016 Budget.
- Historical exchange rates against selected foreign currencies are available here: http://www.resbank.co.za/Research/Rates/Pages/SelectedHistoricalExchan

geAndInterestRates.aspx

- Depending on the final outcome of the Parliamentary legislative process, the guide will be updated if necessary. An updated guide may differ from this guide in form and content. Please regularly check the VDP page on the SARS website for updates, at: http://www.sars.gov.za/Legal/VDP/Pages/default.aspx
- The current draft tax-related SVDP legislation is available here: http://www.treasury.gov.za/public%20comments/RMTAB2016/
- For information regarding the Exchange Control SVDP, please visit the following web page: http://www.resbank.co.za/RegulationAndSupervision/FinancialSurveillanceAndExchangeControl/Pages/Special-Voluntary-Disclosure-Programme.aspx
- Enquiries regarding the Exchange Control SVDP may be directed to SARB-SVDP@resbank.co.za
- Enquiries regarding the Tax SVDP may be directed to vdp@sars.gov.za

1. Background

In terms of the new global standard for the automatic exchange of information between tax authorities, it is expected that the South African Revenue Service (SARS) will start receiving offshore 3rd party financial data from other tax authorities from September 2017 on a regular basis. This created a window to propose a Special Voluntary Disclosure Programme (SVDP) to give opportunity for non-compliant taxpayers to voluntarily disclose offshore assets and income, thereby regularising both their tax and exchange control affairs. The SVDP will be open for applications from 1 October 2016 until 30 June 2017.

The SVDP will run concurrent to the permanent Voluntary Disclosure Programme (VDP) of SARS.

SARS and the South African Reserve Bank (SARB) are working together to ensure that SVDP applications are evaluated and processed through one joint process, i.e. for both tax non-compliance and exchange control contraventions.

2. <u>SVDP Legislative Design</u>

a) Window

- Applications for relief under the SVDP will apply for a limited window period of nine months starting on 1 October 2016 and closing on 30 June 2017;
- Applications submitted prior to 1 October 2016 or after 30 June 2017 will be processed under the normal VDP rules, i.e. the SVDP rules cannot be applied.

b) Eligibility

- Individuals and companies may apply.
- Settlors, donors and beneficiaries of foreign discretionary trusts (including deceased estates) may participate in the SVDP if they elect to have the trust's offshore assets and income deemed to be held by and accrued to them. These also include persons who, despite the form, are in substance settlors, donors or beneficiaries.
- Amounts in respect of which SARS obtained information under the terms of any international exchange of information procedure will not be eligible for the SVDP. An applicant will be informed by SARS if this is the case.
- Disclosures where it is argued by the applicant that all or part of the seed money / subsequent deposits / funding of foreign assets are not taxable in South Africa or have already been taxed in South Africa, are excluded from the SVDP. The normal VDP channel remains open for disclosures of this nature.

c) Relief Granted

	SARS	SARB
Capital that funded the asset (“seed money” , capitalised returns and subsequent deposits)	• The undeclared income that originally gave rise to the foreign asset will be exempt from income tax, donations tax and estate duty liabilities arising in the past. • 40% of the highest value of the aggregate of all assets situated outside South Africa between (or deemed to be between) 1 March 2010 and 28 February 2015 that were derived from undeclared income will be included in taxable income and subject to tax in South Africa in the 2015 tax period. The value referred to above is the highest market value as at the end of each tax period, in the relevant foreign currency translated to South African Rand at the spot rate at the	• A levy of 5 per cent on the value of the unauthorised foreign assets or the sale proceeds thereof as at 29 February 2016, if such assets are repatriated to the Republic of South Africa. The 5 per cent levy must be paid from foreign sourced funds. • A levy 10 per cent the value of the unauthorised foreign assets as at 29 February 2016, if such assets are retained abroad. The 10 per cent levy must be paid from foreign sourced funds. • A levy of 12 per cent on the value of the unauthorised foreign assets as at 29 February 2016 in circumstances where the 10 per cent levy is not paid from foreign

	end of the tax period in which the highest value fell	sourced funds.
Investment returns & other taxable events	Investment earnings & other taxable events prior to 1 March 2015 will be exempt from tax	Not applicable
Interest on SARS debt	Interest on tax debts arising from the disclosure only commence from the 2015 year of assessment	Not applicable
Understatement penalties	No understatement penalties will be levied	Not applicable
Other SARS penalties	Same as current VDP	Not applicable
Criminal Prosecution	Same as current VDP	Not applicable

Where the disclosure is in respect of an asset that was both acquired and disposed of prior to the 2011 tax period, the asset must be treated as if it was acquired during the five year period ending 28 February 2015.

d) Required supporting documentation for SVDP applications

- Supporting documentation must be submitted as attachments to the SVDP application forms. The functionality to attach is available on the SARS eFiling VDP platform.
- For information relating to supporting documents required when submitting exchange control SVDP applications and a copy of the prescribed declaration to be completed by

prospective applicants, please visit the SARB SVDP webpage at: http://www.resbank.co.za/RegulationAndSupervision/FinancialSurveillanceAndExchangeControl/Pages/Special-Voluntary-Disclosure-Programme.aspx

- To determine the amount of relief for tax purposes, information in the table format below must be submitted together with the VDP01 application form. In this regard:
  - **Part A** is used by SARS to determine the amount that must be exempt from tax in terms of section 15(1) of the Rates and Monetary Amounts and Amendment of Revenue Laws Act, 2016;
  - **Part B** is used by SARS to determine the amount that must be included in taxable income terms of section 16(1) of the Rates and Monetary Amounts and Amendment of Revenue Laws Act, 2016.

Table to Determine Tax Relief				
Tax period	**PART A** Asset acquisition value and subsequent additional funding		**PART B** Market value of aggregate of all foreign asset(s)	
	Per foreign currency	Per ZAR	Per foreign currency	Per ZAR
Pre 2011 *, **, ***				
2011				
2012				
2013				

2014				
2015				

* Sum of the highest value(s) per asset up to 28 Feb 2010, translated to South African Rand at the spot rate at the end of the tax period in which the highest value was held

** Where accurate figures are not practically possible to determine, use a reasonable estimate & explain

*** It is not necessary to attach the calculations, but it should be kept in case SARS requests it

- A description of the source of the undeclared income that gave rise to the foreign asset.
- Documentation in evidence of the existence of the foreign asset (e.g. bank account details, property registration papers);
- Confirmation of the date on which the asset was acquired (e.g. letter from the bank in case of a bank account, shareholder certificates, property registration papers). If it is practically impossible to obtain the date then a reasonable estimate of the date, together with an explanation of why it is impractical and how the date was estimated, can be submitted;
- Nature of the applicant's connection to the asset (e.g. owner, director, shareholder, beneficiary);
- A description of the structure that was utilised to create the asset;
- Power of attorney (where required).

3. <u>SVDP application and processing</u>

a) Application process

For SVDP purposes, SARS & SARB have agreed to a single point of entry for applications, which is the SARS eFiling VDP application process. The current VDP application form (VDP01) will be enhanced to accommodate the SVDP tax related disclosures, while a second form (SVDP01) form will be available for exchange control disclosures. Both forms will be available on-line on the SARS eFiling platform.

Typically, an applicant will complete both forms, but if only tax relief is required, or if only exchange control relief is required, then only one form needs to be completed.

b) Resources

In addition to the SARS VDP staff, a compliment of SARB staff will be seated at the SARS VDP office. Enquiries regarding the Exchange Control SVDP may be directed to 012 647 2243 or alternatively SARB-SVDP@resbank.co.za .

c) Evaluation of applications

Tax-related disclosures will be routed to SARS staff and exchange control disclosures will be routed to SARB SVDP unit.

d) Approval / Rejection of applications: Process

Tax-related disclosures will be approved or rejected on the same basis as the current VDP process. Exchange control SVDP applications will be dealt with in terms of Exchange Control Regulation 24, read in conjunction with exchange control Circular No. 6/2016 dated 13 July 2016

11. INDEMNITY

Whilst every reasonable care has gone into the preparation and production of this update, no responsibility for the consequences of any inaccuracies contained herein or for any action undertaken or refrained from taken as a consequence of this update will be accepted.