TAX UPDATE

For period: 1 October 2015 to 31 December 2015

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1. INTRODUCTION

The purpose of this update is to summarise developments that occurred during the fourth quarter of 2015, 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.

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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!

2. NOTICES & REGULATIONS

2.1. Exchange of information conventions / agreements

The Exchange of Information Conventions/Agreements/Standards are divided into these categories:

- USA FATCA Intergovernmental Agreement
- Multilateral Mutual Administrative Assistance (MAA) Conventions / Agreements
- Bilateral Tax Information Exchange Agreements (TIEAs)
- Standard for Automatic Exchange of Financial Account Information in Tax Matters (CRS)

The **USA FATCA Intergovernmental Agreement** is an agreement between the governments (tax administrations) of the United States of America and the Republic of South Africa to exchange information automatically under the provisions of the double taxation agreement between these countries.

The **Standard for Automatic Exchange of Financial Account Information in Tax Matters** (also referred to as the Common Reporting Standard or CRS) is the Global Model for automatic exchange of information under the Multilateral Competent Authority Convention to which South Africa is a signatory.

The **CRS** is a standardised automatic exchange model, which builds on the FATCA IGA to maximise efficiency and minimise costs, except that the ambit is now extended to all foreign held accounts and not only those of US citizens. South Africa is also one of the early adopters of the CRS and is committed to commence exchange of information automatically on a wider front from 2017, together with over 90 other jurisdictions.

Multilateral Mutual Administrative Assistance Conventions / Agreements are agreements between the governments (tax administrations) of two or more countries to enable them to exchange tax information on request, spontaneously or automatically, as well as to provide assistance in the collection of taxes.

Bilateral TIEAs are agreements between the governments (tax administrations) of two countries to enable them to exchange tax information upon request.

USA FATCA Intergovernmental Agreement

This intergovernmental agreement (IGA) between the USA and the RSA was concluded under the provisions of the double taxation agreement (DTA) that exists between the USA and the RSA since 1997.

Standard for Automatic Exchange of Financial Account Information in Tax Matters

Many jurisdictions that have opted to implement FATCA on a 'FATCA IGA', have also shown interest in leveraging the investments made for implementing the FATCA IGA to establish automatic exchange relationships with other jurisdictions, which themselves are introducing similar rules.

Those countries recognise that, through the adoption of a common approach to automatic exchange of information, offshore tax evasion can be tackled most effectively while minimising costs for governments and financial institutions.

With the strong support of the G20, the OECD, together with G20 countries and in close cooperation with the EU and the other stakeholders, has since developed the **Standard for Automatic Exchange of Financial Account Information (the Standard or the CRS)**.

The first reporting period for financial institutions obliged to keep records, apply with the due diligence requirements, commences on 1 March 2016 and ends on 28 February 2017, followed by a due date for returns of about June 2017 and exchange of the information by South Africa by September 2017.

The **Standard** consists of the following elements:

- The **Common Reporting Standard (CRS)** that contains the due diligence rules for financial institutions to follow to collect and then report the information that underpin the automatic exchange of financial information
- The **Model Competent Authority Agreement (CAA)** that links the

CRS to the legal basis for exchange, specifying the financial information to be exchanged

- The **Commentaries** that illustrate and interpret the CAA and the CRS
- The **Guidance on Technical Solutions** to be used for exchanging the information, including an XML schema and standards in relation to data safeguards and confidentiality, transmission and encryption

In order to implement the standard on a consistent and efficient basis, the draft Tax Administration Laws Amendment Bill, 2015, proposes amendments to ensure that certain financial institutions must report on all account holders and controlling persons, irrespective of whether South Africa has an international tax agreement with their jurisdiction of residence or whether the jurisdiction is currently a CRS participating jurisdiction (ref. page 15).

Therefore, South Africa will have to take the following steps to implement the standard and the key conceptual considerations in this process:

- Translating the reporting and due diligence rules into domestic law
- Selecting a legal basis for the automatic exchange of information
- Putting in place the necessary administrative and IT infrastructure
- Protecting confidentiality and safeguarding data in respect of exchanged information

The primary enabling legislation for the CRS is the Tax Administration Act, 2011. Secondary legislation will be largely similar to those published for purposes of FATCA.

Thus, the primary legislative framework for AEOI, including FATCA and the CRS, is largely in place, barring one or two amendments that, if deemed necessary, will be implemented by December 2015 or at the latest in January 2016.

More information on CRS can be found on the OECD's website - Automatic Exchange of Information

2.2. *Mutual agreement procedure (MAP)*

What is a MAP?

MAP is a procedure which allows the Competent Authorities or designated representatives of the Competent Authorities from the governments of the Contracting States/Parties to interact with the intent to resolve international tax disputes.

MAP is provided for in an Article in a Double Taxation Agreement (DTA) and can involve matters containing juridical double taxation cases, as well as inconsistencies in the interpretation or application of a DTA.

What is a Competent Authority?

DTAs are usually concluded between the governments of two countries. These countries are then referred to as the Contracting States or Contracting Parties to such an agreement.

'Competent Authority' is a term used in tax conventions or agreements to identify a position, a person or a body to whom issues can be addressed within a Contracting State.

The Competent Authority in South Africa is the Commissioner for SARS and duties have been delegated to designated representatives in the Legislative Research & Development Subdivision within Legal & Policy.

What is the function of a Competent Authority?

The Competent Authority in a Contracting State/Party is charged with the responsibility to interact with its counterparts in any matters arising between the different Contracting States/Parties pertaining to the interpretation or the application of a DTA, and to resolve any international tax disputes that might arise.

A Competent Authority is generally committed to ensure a good faith application of a DTA. The Competent Authority endeavours to resolve requests from their counterparts in accordance with a particular DTA.

How does it work?

The DTA permits a mutual agreement procedure (MAP) for resolving difficulties arising from the application of a DTA in the broadest sense of the term.

It basically authorises the Competent Authorities or their designated representatives to communicate with each other directly, including through joint commissions, for the purpose of resolving the matters that might be brought before them.

A MAP Request for Assistance may deal with any of the following subjects:

- Transfer pricing adjustment requests
- Attribution of profits of a permanent establishment
- Dual residence of individuals and persons other than individuals
- Withholding tax levied beyond what is permitted by the applicable DTA
- Any other case in which a person considers that the taxation is not in accordance with the applicable DTA

Depending on the relevant subject, the MAP request will be routed into one of two channels, i.e.:

- Transfer Pricing MAP, or
- Interpretation MAP

<u>MAP Request for Assistance</u>

It is a request from one Competent Authority of a particular DTA's Contracting State/Party, to the Competent Authority of the other Contracting State/Party, under a particular DTA, to resolve any international tax dispute.

Step 1

In cases where the taxation which is not in accordance with the DTA has been imposed, the taxpayer must first raise the issue with the relevant State as agreement by the other State will negate the need for a MAP.

Step 2

If unsuccessful, the taxpayer may then approach the Competent

Authority of his/her country of residence to request a MAP under the relevant DTA.

If the Competent Authority in the country of residence cannot itself resolve the matter, but is in agreement with the taxpayer's request for a MAP, the Competent Authority will take up the matter with the Competent Authority of the other Contracting State/Party under the specific DTA.

What to submit & Where to submit it

SARS, as the Competent Authority, requires certain minimum information to be included in a MAP Request, whether it is for a Transfer Pricing MAP Request or an Interpretation MAP Request.

The types of MAP Requests, the minimum information required per type, and the relevant email address to be used per type, are set out in the table below.

2.3. Register for VAT

12 October 2015 - From 12 October 2015 SARS implemented system changes which now cater for the proper processing of Collective Investment Scheme (CIS) registrations and VAT Voluntary registrations which made provision for the registration of vendors who have not yet made taxable supplies exceeding R50 000 per year.

In short, voluntary registration for VAT is now allowed for taxable supplies up to R50 000 within 12 months from date of registration and reclassification of Category F VAT vendors as Category A or B vendors.

When to register?

It is mandatory for a business to register for VAT if the income earned in any consecutive twelve month period exceeded or is likely to exceed R1 million. The business must complete a VAT 101 - Application for Registration form and submit it to the local SARS branch within 21 days from date of exceeding R1 million. A business may also choose to register voluntarily if an applicant wishes to under the new provisions of section 23 (3) (b) (ii) and section 23 (3) (d) of the VAT Act.

From 12 October 2015, the following VAT legislative amendments are applicable:

<u>Voluntary Registration</u>

New VAT Regulations were recently introduced to make provision for the registration of vendors who have not yet made taxable supplies exceeding R50 000 per year.

A person carrying on an enterprise which has not made R50 000 in taxable supplies is allowed to register for VAT, if there is a reasonable expectation to exceed R50 000 in taxable supplies within the 12 month period from date of registration.

In order to register, the person must be able to satisfy SARS that one or more of the following circumstances applies as at date of application for registration:

- In the case of a person who has made taxable supplies for more than 2 months (but not exceeding 11 months), such person must prove that the average value of taxable supplies in the preceding months prior to the date of application for registration exceeded R4 200 per month;
- In the case of a person who has made taxable supplies for only one month preceding the date of application for registration, such person must prove that the value of the taxable supplies made for that month exceeded R4 200;
- In the case of a person who has not made taxable supplies, such person must have a written contract, in terms of which the person is required to make taxable supplies exceeding R50 000 in the 12 months following the date of registration;
- In any other case, the person has entered into a finance agreement with a bank, specified credit provider, designated entity, public authority, non SA resident or any other person who continuously or regularly provides

finance, wherein finance has been provided to fund the expenditure incurred or to be incurred in furtherance of the enterprise, and the total repayments in the 12 months following the date of registration will exceed R50 000; or

- In any other case, the person has proof of expenditure incurred or to be incurred in connection with the furtherance of the enterprise as set out in a written agreement or proof of capital goods acquired in connection with the commencement of the enterprise and proof of payment or extended payment agreement evidencing payment has either exceeded R50 000 at the date of application for registration or that will in any consecutive period of 12 months beginning before and ending after the date of application, exceed R50 000; or will in the 12 months following the date of application for registration exceed R50 000.

Nature of Activities

A person may apply to register as a vendor at the time that any goods or services are acquired directly in respect of the commencement of any of the following continuous and regular activities:

- Agriculture, Farming, Forestry and Fisheries
- Mining
- Ship and aircraft building
- Manufacture or assembly of plant, machinery, motor vehicles or locomotives
- Property development
- Infrastructure development
- Beneficiation

Reclassification of Category F Vendors

With effect from 1 July 2015, the 'Category F' tax period (being periods of 4 months ending June, October and February) was deleted.

In light of this change, SARS has changed existing 'Category F' vendors to 'Category B' vendors.

Your first 'Category B' tax period was for the months of July and August 2015 (VAT return and payment was due in September 2015). Going forward, your tax periods will be periods of two months ending in October, December, February, April, June and August.

Should you wish to change your tax period category from 'Category B' to any other applicable tax period you may do so by submitting a written request to your nearest SARS branch.

How to register?

The VAT 101 application for registration must be submitted in person at the SARS branch nearest to the place where your business is situated or carried on. A registered tax practitioner may appear in person on behalf of the applicant. SARS will not accept any faxed or photocopied applications for registration. Posted applications will only be processed if applicants are geographically far from the SARS branch or due to any form of disability and the applicant cannot physically present the application.

All supporting documents must be submitted, otherwise there may be a delay in finalising the VAT registration.

2.4. The Income Tax return for trusts

12 October 2015 – Changes to the ITR12T form

The form has been amended with effect from 12 October 2015 to include:

- Changes to legislation;
- Previously optional fields and sections have been changed to mandatory; and

- Automated calculations (where applicable).

What is it?

The Income Tax Return for Trusts is called the Income Tax Return for Trust (ITR12T).

When did it come into effect?

The updated form (ITR12T) is available from 12 October 2015.

What are the changes?

- New sections introduced with regards to legislative changes include:
    - Taxable income received from Real Estate Investment Trust (REIT)
    - Allowable tax deduction for Donations in terms of section 18A to an approved Public Benefit Organisation (PBO)
    - Allowable tax deduction for expenditure incurred in exchange for Venture Capital Company (VCC) shares
    - Recoupment in respect of VCC shares sold, for which a tax deduction to the trust was previously allowed
- The optional information that changed to mandatory fields are:
    - All fields in the Statement of Assets and Liabilities section
    - All fields in every section of Local and Foreign Income
    - Certain fields in the schedule of local capital gains and losses and schedule of foreign capital gains and losses
    - In 2014, for persons who transacted with the trust, only the beneficiary fields were mandatory. Now the details of all persons (individuals/company/trust) that transacted with the trust will be mandatory. If 50 or less persons transacted with the trust, the details of every person and the related transactions must be provided. If more than 50 persons transacted with the trust, then the consolidated details of all the transactions must be provided

as well as the details of every person where the aggregate of the transactions were in excess of R500 000 (limited to the top 50 persons based on aggregated transactional value)

- Auto-calculations were added for:
  - Statement of Assets and Liabilities
  - Local Income
  - Foreign Income
  - Schedule of local capital gains and losses and
  - Schedule of foreign capital gains and losses

<u>How will I get the ITR12T?</u>

The form (ITR12T) will be available on eFiling or may be captured at a SARS branch on behalf of the representative/Tax Practitioner. You need to fill in the form before sending it to the branch for capturing.

An example of the ITR12T is available for downloading. Should you visit a SARS branch for capturing, you'll need to fill it in before going to the branch. For more information on how to complete ITR12T, click here.

Top Tip: Asking for the ITR12T to be posted to you will no longer be an option and trust returns received via post will be rejected.

<u>How to submit the ITR12T?</u>

- Complete and submit ITR12T electronically on eFiling
- Submit ITR12T via a third party independent software vendor which will submit to SARS via eFiling web services
- Visit nearest SARS branch for capturing of ITR12T on SARS system. Capturing of the ITR12T at a SARS branch will only be available.If the number of persons who transacted with the trust is limited to a maximum of 10, or else the trust must register for eFiling

3. CASE LAW

3.1. Huang and others v C:SARS…

The first applicant is referred to as 'Mr Huang', the second applicant as 'Mrs Huang', the third applicant as 'Mpisi' and the respondent as 'SARS' and, collectively, 'the applicants'.

The application which led to the granting of the search and seizure warrant is referred to as 'the warrant application' or 'the *ex parte* application' and the current application as 'the reconsideration application'.

SARS had brought an *ex parte* application against the applicants in terms of sections 59 and 60 of the Tax Administration Act for a search and seizure warrant and ancillary relief.

The aforesaid *ex parte* application was heard and granted in chambers and the warrant authorised SARS, *inter alia*, to search the business premises of Mpisi and the residential premises of the Huangs and to seize documentation and relevant material.

The warrant was executed on 26 April 2013 at the two premises and material which was alleged to be relevant was seized.

It was common cause that subsequent to the warrant being executed, various discussions between the parties took place and correspondence was exchanged and meetings were held during which the applicants were provided with copies of the documentation seized during the execution of the warrant and the applicants were allowed to inspect certain of the originals and the electronic data storage equipment were returned to them.

Pursuant to these exchanges between the parties, on 29 April 2013, the applicants demanded certain undertakings from SARS, *inter alia* that SARS should not take any further steps in terms of the warrant pending the matter being reconsidered; that SARS immediately return all computer server hard drives, personal computers and other relevant material; and that SARS should also not utilise the relevant material obtained as part of the warrant.

When SARS refused to accede to the demands, the applicants approached the

Gauteng High Court for the relief as set out in the notice of motion of the reconsideration application.

The warrant had been issued on the strength of allegations that there were reasonable grounds to believe that the applicants had failed in one or more or all respects to comply with their duties in terms of the Income Tax Act, the Value-Added Tax Act and/or the Tax Administration Act, or on the basis that there were reasonable grounds to believe that any one or more of them had committed certain offences in terms of the said Acts.

The reconsideration application was based on the submissions that the disputed search warrant had been improperly obtained on one or more of the following bases:

- The warrant application did not satisfy the requirements of an *ex parte* application in *inter alia* the following ways: SARS did not act in good faith; and/or SARS misled, alternatively improperly influenced the court's discretion in granting the search and seizure warrant; and/or SARS had been remiss in its duty to fully disclose all the material facts; and/or SARS had relied on selective evidence and misleading speculative conclusions based thereon.
- The main application did not satisfy the requirements of the Tax Administration Act.
- In essence the *ex parte* application was an abuse of the court process.

SARS opposed the reconsideration application and contended that the applicants had failed to make out a case in support of the relief that they sought and, in the alternative, moved for an order in terms of section 66(4) of the Tax Administration Act that it, SARS, be authorised, in the interest of justice, to retain the original or copies of the relevant material seized.

Initially, when the applicants launched the reconsideration application, they had relied on the provisions of uniform rules 6(11) or 6(8) or 6(12)(*c*) but SARS had taken issue with this approach on the basis that the applicants relied in their application on a wrong procedure and that the correct procedure that they ought to have used was in terms of section 66 of the Tax Administration Act.

However, it appeared that the applicants had abandoned their reliance on the uniform rules and agreed that the procedure under rule 6(12)(*c*) and in terms of section 66 was the same.

The applicants raised the following issues in their papers for determination:

- Whether the warrant ought to be set aside on the basis of material non-disclosures and misrepresentations in the *ex parte* application brought by the respondent;
- Whether the warrant ought to be set aside on the basis that the jurisdictional requirements of sections 59 and 60 of the Tax Administration Act were not satisfied in the *ex parte* application brought by the respondent;
- Whether the warrant ought to be set aside on the basis that the *ex parte* application brought by the respondent constituted an abuse of process.

The applicants contended that not all the material facts had been disclosed to the judge hearing the warrant application and that some of the facts provided were irrelevant, vexatious and at times spurious and were aimed at influencing the judge to issue the warrant. Moreover, had the judge been provided with all the material disclosures and the correct information, he would not have issued the warrant.

The applicants further contended that SARS did not establish the jurisdictional requirements of sections 59 and 60 of the Tax Administration Act in the *ex parte* application in that most of the allegations were not reasonable grounds as envisaged in the Act simply because the facts upon which the *ex parte* application was based were unduly contorted to artificially create an atmosphere of suspicion. Moreover, the reasonable grounds set out by SARS in the warrant application were easily disputable in that, *inter alia*, offences alleged to have been committed by the applicants had not been proved.

The applicants also submitted that SARS had opportunistically manipulated and abused the legal process by launching an *ex parte* application under the guise of alleging various income tax and VAT related offences pertaining ostensibly to importing and exporting transactions and the contention was that the transgressions SARS had relied upon in its warrant application were not tax offences as envisaged in section 60 of the Tax Administration Act but were offences under the Customs and Excise Act 91 of 1964.

Sections 59 and 60 of the Tax Administration Act provided at the relevant time that a senior SARS official may, if necessary or relevant to administer a tax Act, authorise an application for a warrant under which SARS may enter a premises where relevant material is kept to search the premises and any person present on the premises and seize relevant material. The section further provides that SARS must apply *ex parte* to a judge for the warrant, which application must be supported by information supplied under oath or solemn declaration, establishing the facts on which the application is based and in circumstances where reasonable grounds can be shown that a person has failed to comply with a tax Act or has committed a tax offence.

Section 66 of the Act provided that any person, whose relevant material has been seized in terms of a warrant for search and seizure, if SARS refuses a request for the return thereof, may approach the court for a reconsideration of the warrant and the court may, on good cause shown, make an order as it deems fit, which order may also include that a warrant be set aside.

Judge Kubushi held the following:

<u>As to the issue of procedure</u>

(i) That, as far as the issue of procedure was concerned, the application in issue had to be dealt with in terms of section 66 of the Tax Administration Act as Uniform Rule 6(12)(*c*), upon which the applicants sought to rely, did not find application in the circumstances of this matter. The Rule applied only where the application was brought to court on an urgent basis and that was not the situation in this instance. The respondent has, however, accepted that the application is properly before the court since the difference between Uniform Rule 6(12)(*c*) and section 66 of the Tax Administration Act was one of form and not substance and hence the court would deal with the application as being properly before it in terms of section 66 of Tax Administration Act .

<u>As to material non-disclosure and misrepresentation</u>

(ii) That an *ex parte* application is a serious departure from the ordinary principles applicable to civil proceedings to seek an order in the absence of notice to the respondent party. As per normal court practice an *ex parte* procedure should be invoked only where there is good cause or reason for the procedure such as when the giving of notice would defeat the very object for which the order is sought and it is, therefore, our law that an applicant in an *ex parte* application bears a duty of utmost good faith in placing before the court all the relevant material facts that might influence a court in coming to a decision. Only facts that are material and which are within the applicant's knowledge should be disclosed.

(iii) That, in this instance, SARS was enjoined by section 59(2) of the Tax Administration Act to apply *ex parte* to a judge for the search and seizure warrant and it has been correctly said that this *ex parte* application is not a species unique to the Tax Administration Act but falls squarely within the confines of the *ex parte* application in terms of Uniform Rule 6(4) and SARS was therefore bound in terms of the rules of procedure to be *bona fide* in disclosing all the relevant material facts.

(iv) That, therefore, in this instance, when determining the issues raised in the reconsideration application, if it can be shown that SARS as an applicant in the *ex parte* application had withheld material facts which might have influenced the court in coming to a decision, the court would be entitled to reconsider and rescind the issued warrant, irrespective of whether the non-disclosure was wilful or *mala fide*.

(v) That in the court's view the applicants' submissions had no merit. It is said that in vast and complex cases, such as the present, there can be no crystal-clear distinction between facts which are material and those which are not. An applicant will as such have to make a judgment call as to which facts might influence the judicial officer in reaching its decision and which, although connected to the application, are not sufficiently relevant to justify inclusion and the test of materiality should also not be set at a level that renders it practically impossible for the State to comply with its duty of disclosure, or that will result in applications so large that they might swamp *ex parte* judges.

(vi) That possibilities are that SARS may have not disclosed some facts which according to the applicants are material, however, in the court's opinion, the circumstances of this case were such that SARS had to choose from the vast information that was available, which of the facts to include and which not to include. What was also material would have depended on the facts which were readily available to SARS at the time a decision was made to apply for the warrant.

(vii) That what was in issue here was whether SARS had disclosed all the material facts within its knowledge and those facts established reasonable grounds to believe that the applicants had failed to comply with or had committed offences under the tax Acts.

(viii) That, under these circumstances, the facts disclosed in SARS' founding affidavit were sufficient.

As to failure to plead sufficient jurisdictional facts

(ix) That a warrant for search and seizure in terms of the Tax Administration Act is applied for in terms of section 59 of the said Act but before the warrant can be issued the requirements of section 60(1) of the Act must be met and, therefore, when considering whether a warrant should be set aside a court will determine first whether, on the record, the objective jurisdictional facts were present and, secondly, whether the discretion was exercised judicially. For, once the jurisdictional facts have been established, the court is not obliged to issue the warrant – it must first exercise its discretion whether or not to grant the warrant and such discretion must be properly exercised and it is thus a general requirement of the rule of law that any discretion must be exercised in good faith, rationally and not arbitrarily.

(x) That there were two jurisdictional facts which must be satisfied before a judge can issue a warrant for search and seizure. The judge issuing the warrant must have been satisfied that, firstly, there were reasonable grounds to believe that a person failed to comply with an obligation imposed under a tax Act, or committed a tax offence; and, secondly, that there were reasonable grounds to believe that relevant material to be found on the premises specified may provide evidence of that failure to comply or the commission of the offence.

(xi) That if a court finds, when considering the setting aside of a warrant, that the jurisdictional facts were not present at the time of issuing the warrant, then a court will set aside the search warrant and, if the jurisdictional facts were present, then a court will have to consider the exercise of the discretion by the judicial officer to issue the warrant. Such a court may, however, not interfere with the discretion simply because it would have reached a different conclusion to that reached by the judicial officer issuing the warrant and it may only set aside the warrant if it is persuaded that the discretion has not been exercised judicially, or flowed from a wrong appreciation of the facts or the law.

(xii) That the court’s findings that there was no material non-disclosure on the part of SARS in the warrant application would ordinarily be dispositive of the applicant’s claim but it was still necessary for the court to satisfy itself whether, on the record, SARS had established the jurisdictional requirements of section 60(1) of the Tax Administration Act in its warrant application. As a point of departure it should be assumed that the judge in the warrant application was satisfied that SARS had established the jurisdictional facts hence issued the warrant and he was correct.

(xiii) That the relevant suspected offences and failure to comply with the tax Acts were duly set out in the warrant and the grounds on which SARS had reasonably believed that the applicants had committed offences and had failed to comply in terms of the relevant tax Acts, which also satisfied the judge, were identifiable in the SARS founding affidavit as well.

(xiv) That a judge may, in accordance with section 60 of the Tax Administration Act, issue a warrant if satisfied that there are reasonable grounds to believe that a person failed to comply with an obligation imposed under a tax Act or committed a tax offence and that relevant material likely to be found on the premises specified in the application may provide evidence of the failure to comply or commission of the offence.

(xv) That whether such belief was reasonable was an objective question which will be answered on the facts before the court and the purpose of objective grounds is to enable the judicial officer to decide whether the case based upon the facts brought before it is a proper one upon which to exercise discretion and to issue a warrant to search. The judicial officer must, therefore, be satisfied that there are reasonable grounds to believe that a person failed to comply with an obligation imposed under a tax Act or committed a tax offence. Similarly, for seizure of property on reasonable grounds to be justifiable, there should exist an objective set of facts which cause the officer to have the required belief.

(xvi) That the Tax Administration Act allows for the granting of a search and seizure warrant merely on the suspicion that tax offences have been committed and that, reasonable grounds exist for the granting of such an order on an *ex parte* basis. SARS must also set out the reasonable grounds that the relevant material as defined to be seized is likely to evidence the non-compliance and that reasonable grounds must be established does not mean *prima facie* proof. What is of importance is that on the total picture presented by SARS in the warrant application, reasonable grounds to believe that the applicants had failed to comply with their obligations under the tax Acts or had committed offences under those Acts, were established.

(xvii) That the applicants' submission that the offences alleged to have been committed by them should have been proven, did not have merit and it was not necessary for SARS to show that the applicants were guilty of the offences they were alleged to have committed. In determining the issues raised in the reconsideration application, the applicants were not expected to show that they were innocent of the transgressions of which they were suspect as their guilt or innocence was not in issue in this case.

(xviii) That section 60(1) of the Tax Administration Act merely requires of SARS to place information before a judge or magistrate hearing a warrant application and there was no obligation or any duty placed on SARS by the provisions of this section to prove that less invasive means should have been used to obtain the required material or to make the judicial officer aware of other less intrusive measures and it was the duty of a judicial officer hearing the matter to determine whether it was reasonable in the circumstances for SARS to seek a search warrant and not to employ other less invasive means.

(xix) That it was trite that the present court had a wide discretion to interfere with the decision of the judge in a warrant application if he or she did not apply his or her mind to the matter and, in this instance, having discarded the applicants' submissions of material non-disclosure, there were no grounds on which it could be said that the judge in the warrant application did not apply his mind to the matter or did not exercise his discretion judicially and therefore it had to be concluded that there was sufficient information before the judge to properly exercise his discretion in forming his own opinion that it was lawful to issue the warrant and hence the judge's discretion could not be interfered with.

(xx) That the applicants were correct to submit that the exercise of discretion required the judge hearing the application to consider section 14 of the Constitution, i.e. the right to privacy. It has also been held that where jurisdictional facts exist a court has the discretion to refuse the issuing of a warrant where a person's right to privacy outweighs the interests of justice and, therefore, for the effective protection of the right to privacy, the information on which reasonable grounds are based, thus authorising a constitutional search, may not in itself have been obtained in violation of section 14 of the Constitution.

(xxi) That to the extent that SARS seized documentation falling outside the financial periods authorised in the warrant, which was specifically limited to financial periods ending on or after 1 March 2007, such documents had to be returned to the applicants. The safeguards against unjustified interference with the right to privacy include prior judicial authorisation and an objective standard, that is, whether there are reasonable grounds to believe based on information under oath that an offence has been or is likely to be committed; that articles sought or seized may provide evidence of the commission of the offence and that the articles are likely to be on the premises.

(xxii) That the essence of reasonable grounds is that they are objective and can be reviewed by a court. It was common cause that in this instance there was prior judicial authorisation in that a judge was approached to grant the warrant and the judge applied an objective test in deciding whether there were reasonable grounds and there were sufficient facts available to SARS to support its contention that there were reasonable grounds to believe that the applicants failed to comply with one or more of the obligations imposed under any of the tax Acts and that the applicants committed one or more tax offences.

(xxiii) That SARS' claim for a warrant was all encompassing and covered every eventuality and from a plain reading of section 60 of the Act, a single non-compliance or a single offence committed would suffice. What SARS was required to do was just to set out reasonable grounds in support of its contention and once the court reading the papers is so satisfied, a warrant may be issued and SARS managed to do just that.

(xxiv) That, accordingly, the applicants’ claim stood to be dismissed.

As to the abuse of court process

(xxv) That the scope and ambit of the Tax Administration Act is set out in section 4 thereof and the section stipulates that the Act is applicable to a person who is liable to comply with the provisions of a tax Act. The

Tax Administration Act defines 'tax Acts' as the Tax Administration Act or an Act or portion of an Act referred to in section 4 of the South African Revenue Service Act 34 of 1997, excluding the Customs and Excise Act 91 of 1964. It is therefore apparent from the reading of this section that matters pertaining to the Customs Act are specifically excluded from the ambit of the Tax Administration Act.

(xxvi) That the applicants in their haste to have the warrant set aside, lost sight of the provisions of section 180 of the Tax Administration Act in terms of which a person may be held personally liable for any tax debt of the taxpayer to the extent that the person's negligence or fraud resulted in his or her failure to pay a tax debt if the person controls or is regularly involved in the management of the overall financial affairs of a taxpayer.

(xxvii) That the evidence before the court was that the offences alleged to have been committed by the applicants and certain obligations that the applicants are alleged not to have complied with, fell within the tax period ending on or after 1 March 2007 and such offences or obligations would of necessity be covered by the Income Tax Act and the Vat Act as those were the relevant tax Acts for the said period until 1 October 2012.

(xxviii) That, consequently, it could not be seen how it could be alleged that SARS abused the court process by applying for the warrant to search the applicants' premises and to seize any relevant material. Similarly, the submission that SARS should have distinguished between the Tax Administration Act and the Customs Act was not correct as SARS' warrant application was based solely on the provisions of the Tax Administration Act and there was no need to mention the Customs Act.

(xxix) That the fact that the taxpayers feel that they are being targeted is no basis for them to approach the court to reconsider the warrant. The motive, if any, is irrelevant for purposes of this application.

Application dismissed with costs.

3.2. G Bank Zimbabwe Ltd v Zimbabwe Revenue Authority

Staff retrenchment costs

The taxpayer, having carried on business in Zimbabwe as a registered commercial bank, had resolved, through its board of directors, to undertake a voluntary retrenchment exercise in order to reduce its staff head count by up to two hundred and fifty-two staff members and its foreign based parent company had pledged an amount not exceeding US$7 million to bankroll the costs of the exercise.

The taxpayer headlined the exercise 'Voluntary Separation Scheme' and the board directed the roll out of an attractive package that would be of interest to all levels of employees and it had approved the rationale, process and package for the exercise before it was unveiled in country wide road shows to all members of staff.

The rationale behind the decision of the board was the down turn in economic activity that had triggered a drastic fall in business volumes in the face of static staffing levels in excess to capacity.

The process targeted all levels of staff and all interested staff were required to submit formal applications by 31 December 2009 and the taxpayer reserved the right to approve or decline applications. The separation package consisted of two months basic salary for every year served up to a cap of 21 months.

A total of 74 members of staff submitted applications for the exercise, which were received by the taxpayer between 3 and 31 December 2009 and all these applications were accepted by the taxpayer on 31 December 2009. The confirmation certificates in which each staff member affirmed voluntarily and freely terminating employment were all signed by the 74 staff members between 7 January and 14 January 2010 and each applicant was given three months' notice to termination from the date of acceptance.

The gross cost to the taxpayer of the voluntary retrenchment exercise for the 74 employees was US$1 995 402.

A further 27 staff members submitted applications between 6 January and 2 February 2010 and these applications were accepted on the respective dates that they were made and the confirmation certificates were signed by each applicant between 13 January and 4 February 2010 and each applicant served three months' notice from the date of acceptance.

The taxpayer's gross outlay for these 27 members of staff was in the sum of US$550 059.

The taxpayer then sought approval for the aforementioned exercise and such approval was granted by the Minister of Labour and Social Services in respect of 94 staff members in four letters dated between 12 January and 2 February 2010.

The taxpayer submitted applications for each employee to the respondent, being the Commissioner for the Zimbabwe Revenue Authority, (ZRA) for a tax deduction directive and the tax directives had been issued for each employee for the tax year ending 31 December 2010, between 28 January and 26 February 2010.

The taxpayer, in its tax return for the tax year ending 31 December 2009, had claimed a deduction of US$2 693 500 for the staff retrenchment costs in terms of section 15(2)(*a*) of the Income Tax Act as an expenditure incurred for the purpose of trade and for conducting its business and earning income in that year of assessment.

ZRA had disallowed the deduction but had included it in the amended assessment for the 2010 tax year.

It was common cause that the costs of the exercise were deductible in terms of section 15(2)(*a*) of the Income Tax Act and it was also agreed that the deduction was allowable in the year that the expenditure had been incurred.

ZRA had submitted that the expense in relation to the exercise had been properly disallowed as the commitment made by the board meeting was conditional on approval for the exercise being granted by the Minister of Labour and Social Services and he contended further that as such approval was only granted in January and February 2010, the expenditure could not be deducted in the tax year ending 31 December 2009.

The taxpayer, however, had submitted that the exercise was in reality a voluntary retirement or resignation scheme, which fell outside the purview of the provisions of section 12C and 12D of the Labour Act [*Chapter 28:01*].

The issue for determination before the court was whether the taxpayer had correctly brought the provision for retrenchment costs to account in its income tax return in the 2009 tax year.

Judge Kudya held the following:

As to the deduction of staff retrenchment costs

(i) That the costs of the staff retrenchment exercise were deductible in terms of section 15(2)(*a*) of the Income Tax Act [*Chapter 23:06*] and the deduction was allowable in the year that the expenditure had been incurred and the deduction was allowed where the taxpayer had incurred an unconditional legal obligation during the year of assessment and for a conditional obligation the deduction was allowable in the year in which the condition was fulfilled.

(ii) That the taxpayer had termed the exercise a voluntary separation scheme but in its documentation had referred to it as a 'voluntary retrenchment exercise' and the taxpayer had submitted that the exercise was in reality a voluntary retirement or resignation scheme which fell outside the purview of the provisions of section 12C and 12D of the Labour Act [*Chapter 28:01*]. However, the *onus* to show on a balance of probabilities that the scheme was not a retrenchment exercise fell on the taxpayer.

(iii) That in the present case the employer and employees had reached agreement on their own in accordance with section 12D(2) without the involvement of the workers committee, works council or employment council. The rationale and process followed by the taxpayer met the requirements of section 12D(1) and the exercise carried out by the taxpayer was aptly described by the board resolution as a voluntary retrenchment exercise in order to distinguish it from a compulsory or forced retrenchment. It met the requirements of section 12C and 12D of the Labour Act and, in addition, the whole exercise fell squarely into the definition of retrenchment.

(iv) That, moreover, the taxpayer had correctly described in its documentation the process as a retrenchment and that the exercise was a retrenchment was further demonstrated by the provisions of para 4(*p*) of the Third Schedule to the Income Tax Act and it cannot lie in the mouth of the taxpayer to argue that the Minister, at its behest, had approved a retrenchment scheme that was in fact a voluntary resignation scheme. The principle of substance over form satisfied the court that the purported voluntary separation scheme in form was in substance and reality a retrenchment scheme.

(iv) That the commitment to pay the expenses of the 'proposed retrenchment' scheme was conditional upon approval by the Minister and the condition was fulfilled in January and February 2010.

(v) That, accordingly, the scheme became an unconditional legal obligation for the parties once approval had been granted and the expenditure for the retrenchment scheme was accordingly incurred in the tax year ending 31 December 2010 and hence the ZRA had properly disallowed the deduction of US$2 693 500 in the tax year ending 31 December 2009.

Imputing notional interest to Nostro accounts

ZRA had assessed the taxpayer for income tax over the 2009, 2010 and 2011 tax years and he had observed 'huge' balances of non-interest bearing amounts in the Nostro accounts held by the taxpayer with related parties that were, in his view, in excess of the monthly transactional requirements of the taxpayer.

ZRA, purportedly acting in terms of section 98 of the Income Tax Act, had imputed notional interest income to these amounts at the average local rates prevailing in Zimbabwe at the time.

It was common cause that the rates in Zimbabwe were much higher than the prevailing rates in the jurisdictions in which the Nostro accounts were held.

It was clear that the taxpayer had not actually earned such interest but the ZRA deemed the taxpayer to have earned the ascribed interest income and he wrote back into the taxpayer's gross income a total of US$5 392 369,88 for the 2009 tax year, US$11 429 964,09 for the 2010 tax year and US$8 065 117,68 for the 2011 tax year.

The taxpayer had objected to the aforementioned amounts being written back into its gross income but its objection was disallowed.

The taxpayer had relied on the oral evidence of its head of corporate reporting who was responsible for all the reporting processes in the taxpayer including tax payments and the filing of tax returns.

He had defined a Nostro account as a current account (also known as a clearing account), which a bank in one jurisdiction opens in another jurisdiction to facilitate customer transactions in the currency of that jurisdiction and it was thus a current account held by a bank in the books of a correspondent bank in another country. Nostro accounts facilitated trade and transactions between countries of varied currencies and he produced the list of all the 22 Nostro accounts held by the taxpayer throughout the world.

The taxpayer held Nostro accounts with other banks of the same name worldwide (related parties) and other banks not related to it (unrelated parties). The Nostro accounts, whether with related or unrelated parties, were all held at arm's length.

The evidence revealed further that the deposits into the Nostro accounts were made by customers and not by the taxpayer and the money was deposited directly into the customer's account and had reflected in the Nostro account simply because the taxpayer was the banker to the customer. The Nostro accounts did not earn interest and it was evident that the taxpayer did not earn any interest on the deposits in the Nostro accounts.

The evidence indicated that the taxpayer could only earn interest on transfer of the deposits from the Nostro account to an investment account such as a call account and it was common cause that interest rates offered internationally on placement of funds were low as exemplified by the declared income earned on those accounts.

The taxpayer's head of corporate reporting denied that the bank did not earn interest on Nostro accounts in order to avoid paying tax and averred that the bank was in the business to earn income. He also denied that the bank had entered into transactional operation schemes with Nostro banks in order to deliberately forego interest in order to postpone and avoid paying interest. He stated that the taxpayer bank had operated Nostro accounts not as a vehicle to avoid, postpone or reduce its tax obligations but as an objective banking necessity, as would any other bank worldwide.

He maintained that the primary purpose of maintaining a Nostro account was to conduct customer business transactions and he maintained that the bank was not obliged to lend money to earn income.

ZRA contended that the justifications for the balances of liquidity risk management, safeguarding customers' deposits and prompt customer transaction settlement support did not eclipse the high balances that remained in the accounts after these reasons had been taken into account.

ZRA accepted that the Nostro accounts did not create an entitlement to interest regardless of whether they were held with related or unrelated parties.

ZRA had invoked section 98 of the Income Tax Act (Tax avoidance) because the balances in the accounts went beyond meeting liquidity and transaction purposes.

The taxpayer contended that ZRA had no legal right to intrude into its operational space in the absence of a local law that required it to move funds from the Nostro accounts into Zimbabwe to lend at the prevailing local interest rates and hence section 98 did not apply to the facts of this matter.

The issue for determination before the court was whether ZRA was entitled to act in terms of section 98 of the Act and thereby deem the taxpayer's offshore Nostro accounts as interest bearing accounts and the appropriate rate of interest.

Judge Kudya held the following:

As to the imputation of notional interest to Nostro accounts

(i) That in the present matter the taxpayer did not earn any income from the Nostro accounts and the evidence demonstrated beyond a shadow of doubt that it was not possible for the taxpayer to have earned income from those Nostro accounts unless it had moved the deposits to a call account.

(ii) That the taxpayer had lawfully opened the Nostro accounts in question and the amounts in the accounts were deposited by clients in the normal course of business and not by the taxpayer.

(iii) That ZRA had suggested that the holding of funds in excess of the transactional needs for the clients was, to the extent of the excess, a scheme, because this went unabated for three consecutive tax years. The court recognised that the words 'transaction, operation or scheme' were all-embracing and would apply to any activity carried out by a taxpayer and in the circumstances of this case the holding of excess idle funds in the Nostro accounts for three consecutive tax years constituted a scheme.

(iv) That in regard to whether the scheme had the effect of avoiding or postponing or reducing tax liability, the taxpayer did not move the funds from the Nostro accounts onshore for good reasons and those constituted the normal and usual method of operation for local banks including the central bank. Moreover, the bank had a low risk appetite and preferred to safeguard depositors' funds rather than invest the funds in a fragile and uncertain market and hence it did not appear that the scheme was entered into to avoid earning income as it was carried out to preserve the funds.

(iv) That it was the normal method of operation for any bank with a Nostro account and it was not suggested by ZRA that the Nostro accounts with unrelated parties were operated differently from the ones in issue as the treatment and balances were the same for both related and unrelated parties and no rights or obligations not normally associated with this type of account were created for the related parties.

(v) That the opinion of ZRA that the scheme was designed solely or mainly to avoid tax liability was incorrect. It was common cause that the deposit of the funds in the Nostro accounts did not create a tax liability for the taxpayer but the decision by the taxpayer to hold the funds in the Nostro accounts rather than investing them could not and did not create any tax liability for the taxpayer and, in the absence of such a tax liability, the Commissioner could not properly come to the opinion that holding the funds in the Nostro accounts was designed either solely or mainly to avoid, postpone or reduce a tax liability that did not exist.

(vi) That ZRA had lost sight of the fundamental principle behind our income tax legislation, i.e. that it was designed to tax income that had been created. The income must have accrued to or been received by the taxpayer. It is not designed to tax income which is not in and has not come into existence and, either way, income had to exist before it became liable to taxation. The income must either have accrued to or been received or deemed to have accrued or been received by the taxpayer in order to trigger tax liability.

(vii) That, in any event, stripped of all the technical points, *CIR* v *King*, amongst other things, had established that there was no obligation on any taxpayer to earn income and it was clear that where the activities of a taxpayer do not or fail to create income, it is beyond the remit of ZRA to wear the mantle of an investment adviser to the taxpayer and suggest to the taxpayer avenues for more income creation.

(viii) That it further was the case that ZRA had no mandate to usurp the role of the onshore regulatory authority in respect of the Nostro accounts as it was up to the taxpayer to deal with the deposits as it pleased, subject, of course, to the requirements of both onshore and offshore regulatory authorities.

(ix) That, accordingly, ZRA had wrongly invoked section 98 of the Income Tax Act to bring to account notional interest to the gross income of the taxpayer in the three tax years in issue.

Attribution of interest on the offshore loans

Six local companies had purportedly executed loan agreements with the taxpayer in terms of which they had paid interest.

The evidence referred to the Master Risk Participation Agreement ('MRPA') which had been concluded on 12 June 2002 between the taxpayer and the offshore related party which had been conceived as a vehicle to provide suitable local borrowers with offshore funding at a time when Zimbabwe was experiencing endemic foreign currency challenges.

The MRPA laid the general framework for the execution of acceptance agreements between the two banks and in the event of inconsistency between the Acceptance Agreement and the Master Agreement, the provisions of the Acceptance Agreement prevailed.

The Acceptance agreements were of two forms – the first was a Funded Risk Participation agreement and the second was an Unfunded Risk Participation agreement.

There were three important designations in the MRPA – these were Grantor, Participant and Obligor. A grantor could be any one of the two banks who offered the other, the participant, a participation in the funding or in the risk associated with the non-payment of the whole or any part of the amounts loaned out and a participant could be any one of the two banks that had accepted a participation in the risk that would be assumed or the amount advanced and the obligor was the borrower of the funds.

In a funded participation the bank providing the funds was the participant and the participant was obliged to deposit the funds representing the extent of the exposure it was willing to assume with the grantor before it was disbursed to the borrower. It was required in terms of the agreement to indemnify the grantor to the extent of the risk percentage on any default by the borrower and the grantor was required to promptly allocate to the participant its share of the payments made by the borrower inclusive of interest, commission and fees accruing or expenses incurred.

In an unfunded risk participation, in terms of the MRPA, the participant would pay its *pro rata* share of the risk percentage of the principal, interest, fees, costs and expenses to the grantor in case of default by the borrower and the participant would pay the participation percentage from any recoveries made from the borrower.

The evidence clarified that a funded risk participation was invariably fully funded by the offshore related party while an unfunded risk participation was fully funded by the taxpayer with the offshore related party sharing in the risk of default to an agreed percentage. In both instances the taxpayer was the grantor while the offshore related party was the participant.

Clause 6.4 of the MRPA outlined the relationship between the parties who accepted that the MRPA or any acceptance agreement or any other agreement or understanding did not constitute the grantor an agent, fiduciary or trustee of the participant and the grantor's rights could not be transferred or assigned except for the right to sue the borrower for the whole amount owing. The participant had no rights to deal with, make payments to or receive payments from the borrower in the loaned amount and the parties were not in partnership, joint venture or association.

It was the testimony of taxpayer's head of corporate banking that, despite the contents of clause 6.4, the taxpayer considered itself an agent of the participant and this was also confirmed by the evidence of the other three witnesses who testified on this aspect and they regarded the taxpayer, being the grantor, as an agent of the offshore related party, i.e. the participant.

The taxpayer's head of corporate banking portrayed the taxpayer as an agent of the offshore related party in administering the loan and he maintained that funds were disbursed to the six onshore companies from offshore and that the borrowers also made direct interest payments offshore. His evidence was supported by the three witnesses who testified on behalf of the borrowers and they all maintained that, notwithstanding the contents of the facility letters, they had sourced offshore loans from the offshore related party and they had remitted interest to the offshore related party and the taxpayer was merely a conduit pipe who had facilitated easy access of the funds and had sought approval from the Reserve Bank of Zimbabwe on behalf of both the borrowers and the offshore lender.

The issue for determination before the court was whether the ZRA was entitled to attribute interest earned by non-resident related parties on loans made to businesses in Zimbabwe, to the taxpayer.

ZRA had been of the view that the taxpayer had been borrowing offshore funds for onshore lending and that it had earned the interest deposited into the offshore evidence account held with the offshore related party.

Judge Kudya held the following:

As to the attribution of interest on the offshore loans

(i) That it was common cause that the facility letters were all in the name of the taxpayer who set the terms and conditions for accessing the loan amounts. The parties were required to provide board of directors' resolutions, various security documents and in some instances proof of an offshore evidence account and the taxpayer was the link between the borrowers and the External Loan Coordinating Committee of the Reserve Bank of Zimbabwe ('ELCC').

(ii) That it was the taxpayer who had applied for approval of both tobacco and non-tobacco pre- and post-shipment offshore loans and the approvals had identified the taxpayer as the borrower and the offshore related party as the lender and ZRA had understandably taken the view that the taxpayer had been borrowing offshore funds for onshore lending.

(iii) That the ELCC approvals granted to the taxpayer had identified the taxpayer as the borrower of offshore funds emanating from the offshore related party for both tobacco and non-tobacco pre- and post-shipment loans and it was on the basis of the contents of the paperwork represented by the facility letters and the ELCC approvals that ZRA had maintained that the interest purportedly paid by the borrowers to the related offshore party had accrued to the taxpayer and he had forcefully contended that the facility document created legal rights and obligations between the taxpayer and the specified onshore clients, i.e. it created the cause for payment of interest to the taxpayer and did not establish a similar cause for payment to the offshore related party.

(iv) That the *onus* to show that the interest in issue had accrued to the offshore related party, in terms of section 63 of the Income Tax Act, lay on the taxpayer who contended that the interest in issue had in reality been received by the offshore related party which it established through a variety of documents.

(v) That, however, interest, like any other income, is also taxed on the basis of accrual and accrual denoted legal entitlement. The facility documents seemed to appropriate interest to the taxpayer as they pointed to the taxpayer as the provider of the credit to whom interest payments were due and, in the parlance of Watermeyer CJ in *CIR* v *Lever Bros and Unilever Ltd* 14 SATC 1 the provision of the credit was the originating cause or source of the interest.

(vi) That the taxpayer had failed to establish the basis for the remittal of interest to the offshore related party and had failed to demonstrate that it did not earn the interest deposited into the offshore evidence account held with the offshore related party.

Withholding tax

The foreign banks in which the taxpayer held its Nostro accounts had raised transaction related charges in respect of cash repatriation, cash ordering or Visa card costs and the taxpayer had paid those charges directly to the banks concerned without deducting therefrom any amount in respect of withholding tax.

ZRA contended that the charges raised by the banks holding the Nostro accounts, which were paid by the taxpayer, had constituted fees.

The taxpayer contended that the payments made were in respect of bank charges and not in respect of fees, whether of a technical, managerial or consultative nature and were not subject to the withholding tax.

The issue for determination before the court was whether the bank charges that were raised by the offshore banks holding the taxpayer's Nostro accounts had amounted to fees in terms of para 2(1) of the 17th Schedule to the Income Tax Act.

Paragraph 2(1) provided that every payer of fees to a non-resident person shall withhold non-residents' tax on fees from those fees and shall pay the amount withheld to ZRA within ten days of the date of payment or within such further time as ZRA may for good cause allow.

Fees were defined in para 1(1) of the 17th Schedule to the Act as meaning 'any amount from a source within Zimbabwe payable in respect of any services of a technical, managerial, administrative or consultative nature . . .'.

Judge Kudya held the following:

As to the withholding tax

(i) That in the present matter the charges were interchangeably referred to as fees by the taxpayer and each of the words 'technical, managerial, administrative and consultative' that are used in the paragraph under consideration were 'of wide and general import and there are few activities of a taxpayer which will not be appropriately described by one or other of them'.

(ii) That the activities that were carried out by the Nostro banks on the various Nostro accounts and by Swift clearances were administrative in nature and the clearing or processing of transactions by Swift were both administrative and technical.

(iii) That, accordingly, the charges raised by offshore banks holding the taxpayer's Nostro accounts had amounted to fees under para 1 of the 17th Schedule to the Income Tax Act and ZRA had properly raised withholding tax on the bank charges as already described.

3.3. ITC 1878

The taxpayer was incorporated in the United States of America and was an advisory group that had a global reach with offices in no less than ten foreign jurisdictions and it concentrated on the airline industry.

The taxpayer came to South Africa in 2007 to perform certain services for X, a company based in and operating from South Africa and, in order to perform these services, the taxpayer concluded a contract with X.

The taxpayer’s only purpose for coming to South Africa was to perform its obligations and earn its income or profits in terms of the aforesaid contract and, having achieved its objective, it left the country in 2008.

The taxpayer, during the course of 2007, had entered into a contract (‘the agreement’) with X in terms of which the taxpayer would provide certain strategic and financial advisory services to X and the services were to be delivered in three phases with the first phase commencing in February 2007 and the third phase ending in May 2008.

The taxpayer, during the aforesaid period, made seventeen of its employees available, who came to South Africa as and when required. However, there were three employees whose work formed a core aspect of the project and who were each in South Africa, on a rotational basis, for three weeks at a time and during the 2007 calendar year the taxpayer’s employees were in South Africa for a period exceeding 183 days.

The taxpayer was granted space inside the premises of X from where it conducted most of its activities, and at times employees of the taxpayer were based in different geographical areas within the premises of X.

X provided space in the boardroom where the taxpayer was provided with four tables and one telephone to be shared by all its employees and the employees only had access to these premises on weekdays and during working hours. Other than providing services in terms of the contract with X, taxpayer’s employees did not perform any other work of the taxpayer.

The nature of the work provided, which was consultancy services on a daily basis, required the taxpayer’s employees to be based at the premises of X and for this reason the boardroom where the taxpayer always had a presence, even if some of its employees were at times located for brief periods in another area of the X premises, constituted the ‘hub’ of the taxpayer’s business operations and was the ‘engine room’ of its business operation. It also had to be noted that the X operations were all geographically located in one place, Y.

The taxpayer derived income from X for its services rendered in South Africa (or earned a profit as a result of the services it sold to X) during its 2007 and 2008 years of assessment, and received additional income (or earned additional profits) during the period 9 April 2008 to 9 November 2009, the latter income (or profit) was not for (or as a result of) any new services that it provided during the 2009 year, but was for the success achieved (‘success fee’) by it during the performance of its obligations in terms of the agreement concluded in May 2007 and it was, in other words, part of the income (or profits) it earned for the services provided during the 2007 and 2008 years.

The total taxable amount for these years, although only earned during the period February 2007 to May 2008, according to the respondent, was R63 990 639.

SARS had assessed the taxpayer’s income (or profits) earned in South Africa during the 2007, 2008 and 2009 years of assessment for taxation and the assessments had indicated a substantial tax liability.

SARS' assessment was based on the provisions of articles 7(1), 5(1) and 5(2)(*k*) of the Double Taxation Agreement (DTA) between South Africa and the United States of America which was concluded on 17 February 1997 and the provisions thereof rank equally with domestic law.

According to the aforesaid assessments the taxpayer was liable for tax for the years in issue for the income it earned in South Africa during its stay there in 2007 and 2008.

SARS, in addition, had, in terms of the powers conferred upon him by section 76 of the Income Tax Act, imposed an additional tax upon SARS and he also intended to charge the taxpayer for interest in terms of section 89*quat*(2) of the Act for the non-timeous payment of the tax.

The taxpayer, aggrieved by the aforementioned assessments, as well as the imposition of an additional tax and the charge of interest, lodged an objection against the assessments in terms of Rule 3 of the Rules promulgated in terms of section 107A of the Act and the necessary processes for the resolution of the objection were followed and they ultimately culminated in the appeal before the Tax Court.

Article 7(1) of the DTA provided at the relevant time that the profits of an enterprise of a Contracting State shall be taxable only in that State unless the enterprise carried on business in the other Contracting State through a permanent establishment situated therein. If the enterprise carries on business as aforesaid, the profits of the enterprise may be taxed in the other State but only so much of them as is attributable to that permanent establishment.

For the taxpayer to be liable for taxation in South Africa it would have had to carry on business in South Africa through a permanent establishment and this raised the question of what is a permanent establishment and article 5 of the DTA provided direction for an answer to this question.

Article 5(1) provided that for the purposes of this Convention, the term 'permanent establishment' meant a fixed place of business through which the business of an enterprise is wholly or partly carried on.

Article 5(2)(*k*) provided that the term 'permanent establishment' includes, *inter alia*, the furnishing of services, including consultancy services, within a Contracting State by an enterprise through employees or other personnel engaged by the enterprise for such purposes, but only if activities of that nature continue (for the same or a connected project) within that State for a period or periods aggregating more than 183 days in any twelve-month period commencing or ending in the taxable year concerned.

Taxpayer contended that even if it were found that the requirements of article 5(2)(*k*) had been met in this case, but denied that they had been met, it nevertheless still had to be found that the requirements of article 5(1) had been met in order for it to be held liable for taxation for the income it earned (or the profits it made) from its operations in this country and in this regard it contended that on the facts as relayed it had to be found that it did not have a 'fixed place of business through which (its) business . . . (was) wholly or partly carried on' and for that reason it could not be found that it had a 'permanent establishment' in this country and it was therefore not amenable to being taxed for the income earned (or profits made) during its sojourn in this country.

SARS contended, on the other hand, that once it was found that the requirements of article 5(2)(*k*) were met, then *caedit questio*. In other words, a finding to the effect that the requirements of article 5(2)(*k*) had been met was automatically a finding to the effect that a 'permanent establishment' had been created by the taxpayer during its sojourn in this country.

Judge Vally held the following:

As to the purpose of double taxation agreements

(i) That the conclusion of double taxation treaties between countries resulted in a paradigmatic shift in international tax law and, in regard to these double taxation treaties, certain Conventions commonly known as *Model Conventions* on double taxation have been crafted for the benefit of all countries and using them as templates, countries have come to conclude what are commonly referred to as Double Taxation Agreements and these agreements tend to be bilateral in nature.

(ii) That the purpose of Double Taxation Agreements is to ensure that there is a free flow of trade and investment across countries, as well as a recognition that taxation is not avoided by the latitude afforded by the flow of free trade and investment. To achieve this purpose the two countries that are party to the Double Taxation Agreement agree that one of them will forego revenue and which one ultimately does so depends on the facts regarding the business enterprise's operations as well as on the interpretation of the terms of the agreement concluded between the two countries.

(iii) That one such agreement is the Double Taxation Agreement between South Africa and the United States of America (the DTA) which was concluded on 17 February 1997 and it is the one that consumes our attention in this case. The purpose of the DTA is the avoidance of double taxation and the prevention of fiscal evasion in respect of taxes, whilst allowing and protecting free trade between the two countries. In concluding the DTA the South African Government acted in terms of section 108(2) of the Income Tax Act, read with section 231(1) of the Constitution of the Republic of South Africa Act and the DTA became part of South African law in terms of section 231(4) of the Constitution and the provisions of the DTA therefore rank equally with domestic law.

As to the interpretation of international treaties concerning double taxation

(iv) That there are various model treaties addressing the issue of double taxation and the most commonly known ones are: the OECD Model Tax Convention on Income and Capital ('OECD Model'), the United Nations Model Double Taxation Convention ('UN Model') and the USA Model Tax Convention. The OECD Model, however, has served as a basis for many double taxation treaties concluded by South Africa and its trading partners. Moreover, if any treaty contains the same article as that of the OECD Model, then it would not be uncommon to rely on the *Commentary* of the OECD Model to interpret that article.

(v) That the articles of a model treaty are designed to guide contracting states, but often they are adopted *verbatim* in actually concluded treaties between two states and, in these circumstances, the potential for the articles to be open to more than one interpretation is real, given that the interests of the various contracting countries are so diverse that it is impossible to cater for them all in one model treaty.

(vi) That, given that there are thousands of treaties in effect, under these circumstances it would be unusual if the interpretation of similar or same terms or articles is unanimous in the various jurisdictions where these treaties operate. Peculiarities of the tax policies of each country are bound to impact upon the interpretation of a treaty, or article in a treaty and to minimise the potential of this problem rearing its head, a model treaty is published with a *Commentary* on the articles contained therein. In this case the terms of articles 5(1) and 5(2)(*a*)–5(2)(*f*) inclusive of the DTA are identical to the same numbered articles in the OECD Model.

<u>As to the interpretation of articles 5(1) and 5(2)(k) of the DTA</u>

(vii) That the explanations provided in the *OECD Commentary* are of immense value in understanding or interpreting any article contained in the treaty and, in fact, Corbett JA in *SIR* v *Downing* drew on the *Commentary* on the *OECD Model Tax Treaty* to interpret the provisions of a treaty between South Africa and Switzerland on double taxation and, more recently, the Supreme Court of Appeal in *C:SARS* v *Tradehold Ltd* emphasised the need to interpret international treaties in a manner which gives effect to the purpose of the treaty and which is congruent with the words employed in the treaty.

(viii) That, bearing in mind that the interpretation 'must give effect to the purpose of the treaty in a manner that is congruent with the words used', it is crucial in the first instance to take note of the prominence of the phrase 'includes especially' in article 5(2) in order to give intelligent meaning to the concept 'permanent establishment' and it therefore must provide the starting point for the analysis.

(ix) That the word 'include' used in a statute is often used to extend or enlarge the meaning of a thing or concept and it brings within the scope of the thing or concept others that are not ordinarily or naturally part of the thing or concept. If this is so then it had to be inferred that by using the term or phrase 'includes especially' the drafters of the treaty intended that the factors referred to in article 5(2)(*k*) be made part of the definition referred to in article 5(1). They were particularly drawn towards making sure that those factors were given special attention when determining whether a particular business enterprise could be said to be operating through a 'permanent establishment' in a non-resident country within which it conducted business or provided services as otherwise they would not have used the words 'includes especially.'

(x) That it therefore had to be interpreted that the contents of article 5(2)(*k*) had to be read to mean that they were an integral part of article 5(1) and, on this analysis, as soon as an enterprise's activities fell within the ambit of article 5(2)(*k*) it became liable for taxation in the non-resident country and there was no need for a further or separate enquiry as to whether the requirements of article 5(1) had been met. The two articles cannot be read disjunctively. The definition, by virtue of the bridging phrase 'includes especially' was a composite one and this clearly expressed the purpose of the treaty and to break it up and treat the two articles separately would be to ignore the natural and ordinary meaning of the phrase 'includes especially.'

(xi) That the aforementioned interpretation is contrary to what was recommended by the *OECD Commentary* on the relationship between articles 5(1) and 5(2)(*a*)– (2)(*f*) but what was recommended by the *OECD* for these articles had no bearing on the issue of the relationship between articles 5(1) and 5(2)(*k*). Article 5(2)(*k*) is specific and very different from articles 5(2)(*a*)–5(2)(*f*). Unlike articles 5(2)(*a*)–5(2)(*f*) it did not refer to a place of work, but rather to a form of work and it is a different species.

(xii) That, therefore, the interpretive approach adopted with regard to articles 5(2)(*a*)–5(2)(*f*) could not be replicated without thought or input. As far as article 5(2)(*k*) was directly concerned, the *OECD Commentary* was of no assistance. Given that there was no such article in the OECD Model, its silence on the matter is understandable. However, because it was silent it did not mean that an inference to the effect that what it says or recommends with regard to the relationship between article 5(1) and articles 5(2)(*a*)–5(2)(*f*) was applicable to the relationship between 5(1) and 5(2)(*k*) and there was no room for such an inference given the material differences between article 5(2)(*k*) and articles 5(2)(*a*)–5(2)(*f*).

(xiii) That the taxpayer's reliance on the Canadian case of *The Queen* v *Dudney* WA (2000) DTC 6169 which drew upon the *Commentary* of article 5 of the OECD Model, was misplaced and bore virtually no resemblance to the present case. Furthermore, the judgment of the Canadian Federal Court of Appeal did not conform with the rules of interpretation applicable in our jurisdiction. Nor did it accord with the interpretation preferred by the Technical Explanation of the DTA and for those reasons it should not be followed in this case.

(xiv) That, as a conclusion on this issue, the interpretation given by this court with regard to the relationship between articles 5(2)(*k*) and 5(1), and the interpretation proffered by the Technical Explanation (which offers an insight into the understanding of the signatories to the DTA) coincide with one another. The Technical Explanation addresses this treaty only and is addressed to business enterprises and tax authorities in the two countries.

(xv) That, in sum then, the Technical Explanation makes it unambiguously clear that, when considering the furnishing of services by an enterprise (article 5(2)(*k*)) the analysis or interpretation accorded to the place of work (articles 5(2)(*a*)–(*f*)) is not applicable. Thus, once the provisions of article 5(2)(*k*) are met, there is no need to further examine whether the provisions of article 5(1) have also been met to determine whether the existence of a permanent establishment has been proved.

As to the application of articles 5(2)(k) and 5(1) to the facts

(xvi) That it was common cause that the taxpayer, a resident of the USA, provided consulting services to X in South Africa through its employees constituting 17 in total for a period exceeding 183 days during February 2007 and May 2008 and, on these facts, there was no dispute that the requirements of article 5(2)(*k*) were met, and if the interpretation given above is correct then it followed that the taxpayer became liable for taxation in South Africa as its operations fell within the meaning of 'permanent establishment' as used in the DTA.

(xvii) That, however, assuming for the moment that the above conclusion is legally untenable then, on the alternative interpretation, it would be necessary to examine whether the requirements of article 5(1) were also met before it could safely be concluded that the taxpayer had established a 'permanent establishment' while performing its obligations in terms of its contract with X.

(xviii) That even if the interpretation given above is wrong, the facts in this case reveal that SARS has shown that the requirements of article 5(1) were met. There is no doubt that the taxpayer had a fixed base in the boardroom of X and that throughout its stay in South Africa it had a presence in the boardroom of X. In this case, while some employees moved from one area to another the taxpayer was, at all times, present in the boardroom during the tenure of the contract and it had exclusive use of this space for the entire duration of the contract. There can therefore be no doubt that the taxpayer had established 'a fixed place of business' in South Africa while carrying out its obligations in terms of its contract with X.

(xix) That the defining characteristic in terms of article 5(1) is that a 'permanent establishment' must be 'a fixed place of business through which the business of an enterprise is wholly or partly carried on.' Thus the non-resident party (the taxpayer in this case) was not required to carry out all its business from the 'fixed place of business' so established. In this sense, even if it performed some of its obligations in terms of the contract with X from another premises, it would, nevertheless, have established 'a permanent establishment' if it performed only some of its obligations (i.e. 'partly carried on') in terms of the contract and hence, even if it only conducted part of its business from the boardroom, it would have complied with the definition.

(xx) That, accordingly, to the extent that it was necessary for there to be compliance with the provisions of article 5(1) before a finding that the existence of a permanent establishment had been proved, such has been proven in this case.

As to the levying of taxation for the 2008 and 2009 years

(xxi) That it was common cause that the taxpayer's presence in South Africa was from February 2007 and the third phase ended in May 2008, that since 1 May 2008 no employees of the taxpayer were present in South Africa and that the taxpayer's financial year commenced on 1 January 2007 and ended on 31 December 2007.

(xxii) That SARS was correct in his claim that the signatories to the treaty intended for the computation of the days to allow for double counting of the days in order to do 'away with . . . opportunities for tax avoidance.' As pointed out earlier, one of the reasons for countries to conclude these double taxation treaties was to minimise, if not eliminate, the potential for tax avoidance and the DTA is both an anti-double taxation as well as an anti-tax-avoidance measure.

(xxiii) That SARS had correctly maintained that the presence of the taxpayer in South Africa for the 2008 and 2009 years had been established beyond doubt and, as for calculating the 183 days for each year, he claimed that as the taxpayer was in South Africa during the calendar years 1 January 2007 – 31 December 2007 and 1 January 2008 – 31 December 2008, it was in South Africa for two tax years, i.e. 1 March 2007 – 28 February 2008 (the 2007 year) and 1 March 2008- 28 February 2009 (the 2008 year) and the 183 day period has to be calculated forwards from 1 March 2007 to 28 February 2008, for this was 'the commencing of the fiscal year' and then again backwards from 28 February 2009 to 1 March 2008, for this was the 'ending of the fiscal year.'

(xxiv) That, however, the taxpayer's interpretation defeated the object of the DTA, was contrary to the intention of the parties and stood in stark contrast to the interpretation proffered in the *OECD Commentary*. Finally, it bore remembering that double computation of the days in order to cater for the dislocation between the year spent by the non-resident in the Contracting State (South Africa in this case) and the fiscal year of that Contracting State, did not result in the non-resident being taxed twice for the same income (or profit) by the Contracting State.

(xxv) That, accordingly, the court declined the invitation by the taxpayer to uphold its appeal against the 2008 tax assessment.

(xxvi) That, concerning the 2009 assessment, while it was correct that the taxpayer had absolutely no presence in South Africa during any part of that calendar or fiscal year, it had only been paid part of its income earned (or profit made) during the February 2007 – May 2008 period when it clearly had 'a permanent establishment' here as the amount it earned was referred to as 'a success fee' which it would have received upon the completion of its operations in 2008 but which could only be accounted for in 2009 and hence it was deferred income or profit for the February 2007 – May 2008 period.

(xxvii) That, accordingly, SARS had correctly assessed it as part of that income or profit earned during 2007 – 2008, but since it was only paid in 2009 had treated it as a 2009 assessment and therefore the appeal against the 2009 assessment had to fail.

As to the levying of additional tax

(xxviii) That SARS, acting in terms of section 76(2)(*a*) of the Income Tax Act, had levied an additional tax upon the taxpayer to the tune of 100% of the taxation amounts due for the 2007, 2008 and 2009 years. It was common cause that the taxpayer did not render returns for the taxable years 2007, 2008 and 2009 and those were the facts that triggered the application of sections 76(1) and 76(2)(*a*) of the Act.

(xxix) That SARS had found that there were extenuating circumstances in relation to the failure to render a return and he deemed it appropriate to reduce this additional tax to 100%. However, the taxpayer must accept responsibility for its own error regardless of whether the error was *bona fide* or not and, in these circumstances, it could not be held that SARS had acted erroneously, or had failed to exercise his discretion judiciously, when only waiving part of the additional tax he was entitled to impose, or that the imposition of the additional tax at all was unduly harsh.

(xxx) That, accordingly, taking the waiver into account, it could not be said that the additional tax imposed was disproportionately punitive and the court found no fault with its imposition.

As to the appeal against the interest

(xxxi) That as the taxpayer had failed to declare and pay tax on its income for the years 2007, 2008 and 2009, SARS, acting in terms of section 89*quat* of the Income Tax Act, had deemed it appropriate to charge the taxpayer interest because of its default.

(xxxii) That the question to be resolved was this: did the taxpayer act reasonably when it did not file a tax return or pay the tax due as a result of the income earned or profits made in South Africa by virtue of the contract it had with X?

(xxxiii) That the taxpayer, as was known, was a major corporation with substantial international business operations in numerous countries and it had conducted international operations in many countries over many decades. The concept of international taxation is not alien to it and it is, or ought to be, familiar with the ideas and principles concerning double taxation agreements. It is aware that even though it is resident in the USA its operations in other countries may be subject to the taxation laws of those countries should there exist a double taxation agreement between the USA and those countries.

(xxxiv) That it was a fundamental rule of business practice that a business enterprise, especially one that operates on the scale that the taxpayer does, should familiarise itself with the taxation laws of a country in which it operates and failure to do so would be grossly negligent, and for that reason unreasonable. Moreover, the taxpayer unilaterally decided that it is not liable for taxation in South Africa and did not bother to clarify the issue with anyone, least of all SARS and hence the taxpayer's conduct fell short of what was expected of a reasonable international corporation operating on the scale it did.

(xxxv) That, for the reasons given, SARS was not wrong and did not act irrationally or unreasonably by refusing to exercise his discretion in terms of section 89*quat*(3) to the advantage of the taxpayer and hence SARS' decision not to grant the taxpayer an indulgence by waiving the interest payment for its default could not be faulted and hence the appeal against the levying of interest by SARS had to fail.

The appeals were dismissed.

3.4. Gainsford NO v C:SARS

Applicants were the joint trustees in the insolvent estate of one BD Tannenbaum.

Second Respondent, being the Commissioner for SARS, had been granted a provisional order by the Gauteng Division in terms of section 163 of the Tax Administration Act on an *ex parte* and *in camera* basis for the preservation of certain assets belonging to Dean Rees ('Rees') and Doggered Investments (Pty) Ltd ('Doggered').

SARS, in the founding affidavit in the application for the preservation order, had stated that Rees was indebted to SARS in the amount of R194 423 966, 69 and that it had sought to preserve these assets to secure such debts. Furthermore, SARS stated that Doggered was Rees' *alter ego* and therefore SARS also sought to preserve its assets in order to secure the debt.

Pursuant to the preservation order, First Respondent, being the *curator bonis*, had taken control and possession of the assets, *inter alia* the 322 shares ('the shares') owned by Doggered in Promac Paints (Pty) Ltd ('Promac').

The Gauteng Division granted the joint trustees in the insolvent estate of BD Tannenbaum leave to intervene in the aforementioned matter on 29 September 2014 and the trustees then instituted the present application for an order excluding the aforementioned shares from the operation of the provisional preservation order and discharging the order in respect thereof, on the basis that the Sheriff had already attached them in August 2011.

The latter attachment had occurred in terms of the court order that the trustees had obtained in July 2011 to found or confirm the court's jurisdiction in their action against Rees and Doggered ('the attachment order').

In the aforementioned action the trustees had sought the setting aside and repayment to the insolvent estate of BD Tannenbaum of approximately R160 million that Tannenbaum had paid to Rees in the course of his and Rees' operation in an illegal Ponzi scheme.

The main issue before the court in the present application was, if the preservation order was not discharged, and if the court had found that SARS had established that Doggered was Rees' *alter ego*, whether the trustees had attached the shares in August 2011 in terms of the attachment order and it was submitted by the trustees that it was common cause that if they had done so, the *curator bonis* would not have been entitled to take possession and control of the shares on 13 August 2014 in terms of the preservation order.

The question considered by the court was therefore whether the shares had been validly attached to found jurisdiction.

Pursuant to obtaining the attachment order on 3 August 2011, the trustees had instructed the Sheriff to attach the shares and the attachment order had specifically authorised the Sheriff to do so at the address specified in the attachment order. The Sheriff allegedly attached the shares at such address *inter alia* by notifying Promac (i.e. the company in which Doggered held the shares) of the attachment order, and issued a notice of attachment wherein he recorded 'I attach *ad fundandam jurisdictionem* alternatively *ad confirmandam jurisdictionem* . . . [Doggered's] shares and loan account in the amount of R5 961 103 [Promac] at care of Henk Strydom of Strydom Bredenkamp.'

The trustees, Promac and Doggered acknowledged that the shares were attached in the aforesaid manner.

However, First and Second Respondents, being SARS and the *curator bonis*, contended that the aforesaid attachment was neither proper nor lawful as it did not take place at the situs of the share register or share certificates, and because the Sheriff did not take the certificates into his possession or cause an entry to be made into Promac's share register.

The trustees, however, contended that there was no such requirement in the Uniform Rules of Court to support the aforementioned contention and they maintained that the essential requirement for the attachment of shares in a company for the purpose of founding or confirming jurisdiction was that notice of the attachment must be given to the company and it was common cause that notice of the Sheriff's attachment was given to Promac as well as Doggered and the trustees, none of whom had ever disputed its validity, so it was contended.

The trustees, accordingly, submitted that in the circumstances the attachment of the shares had been valid and that the *curator bonis* was not entitled to take possession and control thereof.

First Respondent, being the *curator bonis*, contended that rule 45(8) applied to the present dispute and that for purposes of an effective attachment of shares, there had to be compliance with the provisions of rule 45(8) and such attachment would only be complete once the Sheriff had given notice of the attachment in writing to all interested parties and had taken possession of the share certificates, or had certified that he could not locate them despite a diligent search.

First Respondent further contended that an attachment of incorporeal property required the Sheriff to attach the document evidencing such rights and an incorporeal moveable asset could not be attached merely by the intention or decision of the Sheriff. Even though the right was incorporeal, some document or similar item representing the right had to be attached.

It was also pointed out that the share certificates or share register was not kept at the address where notice of the attachment was given and the Commissioner agreed with this argument and therefore contended that there had been no valid attachment on 3 August 2011.

The trustees further contended that rule 45(8) only applied to execution proceedings and that all that was required to found jurisdiction was written notice and that this had been given to relevant interested parties. Moreover, although physical possession of the share certificates had not been proven, this was not necessary.

Judge Fabricius held the following:

(i) That the purpose of an attachment of property *ad fundandam iurisdictionem* is twofold: first, to found, i.e. create jurisdiction where no other ground of jurisdiction exists at all, and, secondly, to provide an asset in respect of which execution can be levied in the event of a judgment being granted in favour of the Plaintiff. The purpose of an attachment of property *ad confirmandam iurisdictionem* is to strengthen or confirm jurisdiction which already exists and in this case, too, the object is to furnish an asset on which execution can be levied in total or partial satisfaction of the Plaintiff's judgment (Erasmus, *Superior Court Practice*, A1-31).

(ii) That an attachment to found or confirm jurisdiction is not based on statutory provision but on the common law and there are no exact requirements for the form of the writ. The Supreme Court Rules contain no express provision for attachment *ad fundandam* or *confirmandam iurisdictionem* but they do contain a form of such attachment, which is Form H (see *Thermo Radiant Oven Sales (Pty) Ltd* v *Nelspruit Bakeries (Pty) Ltd* [1969] 2 All SA 338 (A); 1969 (2) SA 295 (A)).

(iii) That it was abundantly clear that rule 45 of the Uniform Rules of Court deals with a writ of execution in respect of 'generals and movables' and, as far as incorporeals are concerned, these are dealt with in rule 45(8), (9) and (10) but this rule does not deal with attachment to found or confirm jurisdiction and the provisions of rule 45 are not relevant to the present issue between the parties. Moreover, actual possession of the relevant property is required in attachment proceedings to found or confirm jurisdiction.

(iv) That it was clear from the old authorities that 'the object is to lay an arrest upon some asset within the jurisdiction belonging to the Defendant, which is his property, and which is capable of being sold to satisfy the judgment of the court'. (*Rothschild* v *Lowndes* 1908 TS 493 at 497).

(iv) That it was clear, and also logical, having regard to the purpose of an attachment, that some type of restraint must be imposed on the particular asset and that upon due attachment of the goods of a judgment debtor, the possession, custody and control of such goods pass into the hands of the officer entrusted with the execution of the warrant of execution and the *dictum* also applies to attachment to found or confirm jurisdiction, having regard to the purpose thereof.

(v) That in *Birgitta Weaving (born Schmidt)* and *Dieter Schmidt* Case No 79/07, Desai J held correctly that rule 45(8) had no application to attachment to found or confirm jurisdiction as the common law deals with such attachments and in that respect the submissions made by the Respondents are rejected.

(vi) That, accordingly, having regard to the purpose of attachment and the requirements of the common law, it was clear that an actual attachment was required to found or confirm jurisdiction and there must be the element of possession or control present and it was common cause that this did not occur herein.

Application dismissed with costs.

3.5. Lifman v C:SARS

The applicants in this matter were taxpayers and First Applicant, Mark Lifman, had represented all the other Applicants in these proceedings as they were juristic persons and he had been the sole member of the close corporations concerned.

The applicants had been indebted to First Respondent, SARS, for an undisputed tax debt of R13 215 062, 21 which had spanned a period of some ten years.

SARS had conducted an enquiry in terms of section 50(1) of the Tax Administration Act against First Applicant and its thirty-five entities under the Lifman Group between 26 May 2014 and 25 February 2015 and during this enquiry the Applicants had submitted outstanding tax returns based on their own declarations and the combined tax debt of the Applicants amounted to R13 215 062, 21 and it was not in dispute that this tax debt arose from voluntary submissions made by the Applicants in their income tax and value-added tax returns.

According to SARS the aforementioned tax debt did not include further tax debt of the Applicants that it had addressed in its letters of finding that were issued in consequence of SARS' inquiry process.

It was undisputed that during the period of engagement between Applicants and SARS, the Applicants had indicated their desire and commitment to be tax compliant and to settle any amount that had become due and payable which may have been raised through assessment, or through an inquiry or otherwise.

As a result of the aforementioned, Applicants and SARS had entered into a security agreement by which SARS had registered *caveats* on some of Applicants' properties with their consent.

SARS, on 3 March 2015, had held a meeting with First Applicant at its Head Office in Pretoria, wherein the Applicants were notified in writing of SARS' intention to seek a civil judgment on their outstanding tax debt, should they fail to adhere to the agreed payment date, that was, 31 March 2015. At that time, a previous letter had already been dispatched to the Applicants on 5 February 2015 that had notified them of the same debt that needed to be settled before the end of March 2015.

Applicants, on 31 March 2015, had failed to honour their undertaking to pay the aforementioned tax debt as agreed and as a result SARS proceeded to obtain civil judgment against them on 1 April 2015 in terms of section 172 of the Tax Administration Act.

As a result of the judgment that had been taken against them by SARS, the Applicants had approached the Western Cape Division of the High Court for an urgent interim interdict against SARS for an order that the default judgments that SARS had obtained in terms of section 172 of the Tax Administration Act on 1 April 2015 against First Applicant and the other applicants be set aside, or alternatively, be suspended and that SARS be interdicted and restrained from executing on, or taking any further steps pursuant to the judgments.

The issue to be determined by the court was whether the interim relief sought by the Applicants was justifiable in the circumstances.

Section 172(1) of the Tax Administration Act provided at the relevant time:

'If a person has an outstanding tax debt, SARS may, after giving the person at least 10 business days notice, file with the clerk or registrar of a competent court a certified statement setting out the amount of tax payable and certified by SARS as correct.'

Section 174 continues to provide that:

'A certified statement filed under section 172 must be treated as a civil judgment, lawfully given in the relevant court in favour of SARS for a liquid debt for the amount specified in the statement.'

Section 162(1) of the Act stipulated as follows:

'Tax must be paid by the day and at the place notified by SARS or as specified in a tax Act, and must be paid as a single amount or in terms of an instalment payment agreement under Section 167.'

Applicants contended that there were jurisdictional and procedural requirements that had to be met prior to SARS taking civil judgments and, in particular, there was a peremptory stipulation in section 172(1) which compelled SARS to give ten business days' notice to the taxpayer prior to filing a certified statement with the clerk or registrar of a competent court.

Applicants contended further that SARS had failed to give the required ten business days' notice to them and, furthermore, that the warning in the letter dated 3 March 2015 given by SARS did not constitute a 'notice' as required by section 172(1) of the Act and, in essence Applicants had been deprived of their *prima facie* right to be notified in terms of the statute.

Applicants contended that it was only when there was failure by the taxpayer to pay the debt on the due date, that the requirement of section 172(1) that 'a person has an outstanding tax debt' is met, and it was only at that time, in this case being 1 April 2015, that SARS was entitled to give notice of ten days prior to applying for judgment in terms of section 172.

Applicants moreover submitted that SARS was not entitled to pre-empt the tax debt becoming due by giving a taxpayer a 'general notice' that it will apply for judgment in terms of section 172, more than ten days before it actually becomes outstanding. SARS would have been empowered to actually give the Applicants notice on 1 April 2015 and only ten days later SARS would be entitled to act in terms of section 172(1) of the Act and hence SARS' actions prior to 1 April 2015 were clearly premature.

SARS contended that, firstly, it could not be disputed that each of the Applicants in respect of whom a certified statement had been filed with the Registrar had an outstanding tax debt and, secondly, the letters of 20 February 2015 and 3 March 2015 constituted a written notice that satisfied the jurisdictional requirement for the exercise by SARS of the empowering terms of section 172(1) of the Act.

Moreover, the Applicants, as taxpayers, were well aware of the precise amount that was due, owing and payable by each of them in respect of which assessments had been issued and, as the facts currently stood, Applicants were faced with an insurmountable hurdle in seeking interdictory relief against the enforcement of their tax liability.

Judge Mantame held the following:

(i) That it was common cause that SARS had been tasked by legislation to provide for the effective and efficient collection of tax, to make provision in respect of tax assessment and to make provision for the payment of tax and to provide for the recovery of tax and to recover interest on outstanding tax debts amongst other requirements.

(ii) That in the course of SARS executing his mandate, it became apparent to the Applicants that their rights had been trampled upon and hence they deemed it fit to come before the court and seek an interim interdict. For the Applicants to be successful in their interim interdict, they should satisfy the court that they had established the trite principles such as a *prima facie* right, the balance of convenience, any irreparable harm and that there was no alternative remedy, other than this interdict.

(iii) That interdicts in their nature are based on rights to sustain a cause of action and the right upon which the Applicants base their application is that SARS had failed to give notice to the Applicants as required by the provisions of section 172(1) of the Tax Administration Act in that the letter dated 3 March 2015 that was relied upon by SARS did not constitute a 'notice' as required by section 172(1) of the Act.

(iv) That the word ‘notice’ in the *Oxford Dictionary* means ‘notification or warning of something especially to allow preparations to be made’ and hence the court should have due consideration to the background circumstances preceding the sending of the letters to the Applicants in order for it to arrive at a correct finding. As early as 3 November 2014 an agreement had been entered into between SARS and the Applicants wherein they had indicated their desire to be fully compliant and to pay to SARS any amount due and payable which may be raised through assessment and Applicants had further tendered as security some of the assets or property and SARS had registered the *caveats* by consent of the parties and hence the Applicants were more than willing to settle any tax debt resultant on those assessments.

(v) That in their replying papers the Applicants did not take issue with the fact that SARS had intended to seek civil judgment but only took issue with the fact that no notice had been given to the Applicants as required in terms of section 172(1) of the Act and that leads on to the question of whether the Applicants were not given ‘notice’ within the confines of section 172(1) or even after employing the meaning of the word ‘notice’ in the *Oxford Dictionary*.

(vi) That, after a careful consideration of section 172(1) of the Act, the conclusion reached is that the Applicants have been disingenuous in their reading and interpretation of this section. Firstly, they do not dispute the fact that they have an outstanding tax debt and, secondly, that SARS intended to take a civil judgment, amongst others, should they fail to make payment by the end of March 2015. The applicants were not upfront with this court as to what would empower SARS to rely on these two underlined undisputed points, amongst others, if it was not section 172(1) of the Act.

(vii) That the Applicants had taken issue with the ten business days’ notice that they were not given by SARS but this point was absurd as the purpose of giving notice was to give notification or warning to that person or entity in order to allow preparations to be made and in this case preparations started when the applicants and SARS entered into an agreement on 3 November 2014, to when he was advised on the current debt on 5 February 2015. The letter of 3 March 2015 gave the Applicants more than enough notice to do whatever they intended to do to structure their affairs.

(viii) That, furthermore, it was not necessary for SARS to expressly state that he was giving the Applicants ten days' notice of his intention to apply for a civil judgment and he had in fact afforded more than the ten business day period for that purpose. In any event, a further ten days after 1 April 2015 would not have made any difference as the applicants had struggled with payment of this debt for over three months.

(ix) That, moreover, SARS had complied with the jurisdictional and procedural requirements as stipulated in section 172(1) of the Act and, for these reasons, the court was satisfied that the Applicants had been given adequate notice within the confines of section 172(1) and had not established a *prima facie* right to be granted an interim interdict and, as a result, the application before the court failed.

Application for interim interdict dismissed with costs, including costs of three counsel.

3.6. Marshall v C:SARS

Applicants were the seven trustees for the time being of the SA Red Cross Air Mercy Service Trust ('the Trust'), who brought the application on behalf of the Trust for a declaratory order in terms of which:

- Section 8(5) of the Value-Added Tax Act applies not only to services deemed to be rendered but also to actual services rendered;
- The services rendered by or on behalf of the SA Red Cross Air Mercy Service Trust to the various health departments of provincial governments situated within South Africa should be zero-rated in terms of section 11(2)(*n*) of the Value-Added Tax Act.

The Trust had since 1994 provided an aero-medical service throughout South Africa which consisted of the flying doctor and rural health outreach service, the air ambulance service and rescue service.

The Trust had entered into agreements with various health departments of provincial governments to provide services to the provinces and the provincial government departments pay a fee to the Trust as agreed by the parties in the relevant written contracts which generally consisted of a fixed monthly fee and an agreed hourly rate in respect of each flight.

The Trust had applied to the SARS for a private binding VAT ruling regarding the VAT status of the services supplied by the Trust to the provincial government departments and the Ruling was to the effect that the supply of such services were in the course of furtherance of the Trust's enterprise and were subject to VAT at the standard rate of 14% in terms of section 7(1)(*a*) of the Act.

The dispute between the parties related to the interpretation and application of section 8(5) of the Act and resulted from SARS' refusal to reconsider its private binding ruling.

Section 8(5) of the Act provided at the relevant time:

'For the purposes of this Act a designated entity shall be deemed to supply services to any public authority or municipality to the extent of any payment made by the public authority or municipality concerned to or on behalf of that designated entity in the course or furtherance of an enterprise carried on by the designated entity.'

Section 11(2)(*n*) of the Act provided at the relevant time:

'(2) Where, but for this section, a supply of services would be charged with tax at the rate referred to in section 7(1), such supply of services shall, subject to compliance with subsection (3) of this section, be charged with tax at the rate of zero *per cent* where–

(n) the services comprise the carrying on by a welfare organisation of the activities referred to in the definition of 'welfare organisation' in section 1 and to the extent that any payment in respect of those services is made

> in terms of section 8(5) those services shall be deemed to be supplied by that organisation to a public authority or municipality.'

It was common cause that the Trust was a 'designated entity' and that the provincial governments from which it received payments were 'public authorities.' Likewise, the Trust was a 'welfare organisation' and its activities qualified as activities referred to in the definition of 'welfare organisation.'

SARS had relied on the definition of 'grant' which specifically excluded payments made by public authorities for the actual supply of goods and services to public authorities and was limited to a gratuitous payment with no reciprocity of goods and services in return.

SARS contended that section 8(5) of the Act will only apply if no actual supply of goods and/or services was made to the respective provincial Departments of Health in turn for the payment received by the Trust. The availability and usage fees paid to the respective Departments of Health are thus actual payments and not deemed payments as it is an availability fee as well as for actual services rendered and is therefore not a grant.

SARS further contended that the provisions of section 11(2)(*n*) of the Act only apply where it is 'a deemed supply' and not an actual supply and hence the Trust did not qualify for zero-rating in terms of section 11(2)(*n*) of the Act, as it is not deemed to supply to a public authority in terms of section 8(5).

Judge Pretorius held the following:

(i) That section 11(2)(*n*) of the Act is clear that it deals with 'services' supplied by a welfare organisation to a 'public authority' which will include the respective Departments of Health of the provinces with which the Applicant had contracted.

(ii) That in the present instant the Trust, a welfare organisation, receives payment by a 'public authority', the various contracted provincial departments of health and section 8(5) provided that such an entity as the Trust shall be deemed to make a supply of services to the public authority in the furtherance of the enterprise carried on by the Trust.

(iii) That the services provided by the Trust to the provincial government departments of health have not been granted to the respective provincial government departments, but the right to use the aircraft remained with the Trust.

(iv) That section 11(2)(*n*) of the Act did not provide that the zero rate is only applicable to deemed supplies falling within the ambit of section 8(5). The Afrikaans translation for deem should be 'geag' and, if that is so, then section 8(5) merely sets out that if services were supplied by a designated enterprise to the various provincial departments of health for payment, then those services are deemed to make a taxable supply of services to the furtherance of an enterprise, which is a welfare organisation.

(iv) That the argument that section 8(5) must be used to qualify for zero rating in terms of section 11(2)(*n*) is not supported by the meaning of the wording of section 11(2)(*n*) of the Act. Section 8(5) makes provision in regard to the use of the word 'deem', deemed the supply of services to be made and deemed the supply of such services to be made to the relevant authority or municipality concerned.

(v) That a 'designated entity' must be a vendor in terms of the Act and involved with the actual supply of services or goods to be able to claim a zero rating in terms of section 11(2)(*n*). If that was not the case then the provisions of section 8(5) and section 11(2)(*n*) would not have been necessary.

(vi) That section 1 of the Act made it clear that the term 'consideration' included payments by one entity to another in respect of supplies made to the other entity, which was the case in the present instance.

(vii) That the argument that the purpose of the deeming provision contained in section 8(5) of the Act was to deem payments received by a designated entity from a public authority or municipality to be consideration in respect of 'services' as opposed to 'goods' was accepted.

(ix) That in the present instance the wording of section 8(5) and section

11(2)(*n*) of the Act was quite clear when the ordinary meaning of the words in these sections are examined in the context of the Value-Added Tax Act.

(x) That it could not be found that an additional purposive approach was required as there were no ambiguous or unclear words in these sections which should be clarified as the words in these sections were clear as they stood.

(xi) That, having applied the principles enunciated in the authorities and having considered the context and the wording in these two sections objectively, there was no reason why the wording should not be given its ordinary meaning in this context once an objective process has been followed.

(xii) That SARS' argument that 'deem' in section 8(5) meant that this section did not deal with actual services had to be rejected. The payments received by the Trust from the provincial governments, being public authorities as defined, were received in the furtherance of the enterprise activities of the Trust, being a designated entity as defined and the payments received from the provincial governments were subject to VAT.

(xiii) That, therefore, section 11(2)(*n*) of the Act applied as the services rendered by the Trust qualified for the zero rate of VAT. The services rendered by the Trust comprised the activities listed in para 1(*e*) of *Government Notice* 112, i.e. 'the rescue or care of persons in distress' under the heading 'welfare and humanitarian.'

(xiv) That section 11(2)(*n*) further provided that to the extent that the payment in respect of the services was made in terms of section 8(5), it was deemed to be supplied to the particular provincial governments and therefore these payments received by the Trust for the services should be subject to VAT at zero *per cent* in terms of section 11(2)(*n*) of the Act.

(xv) That, accordingly, section 8(5) of the Act applied not only to services deemed to be rendered but also to actual services rendered and the services rendered by or on behalf of the SA Red Cross Air Mercy Service Trust to the various health departments of provincial governments situated within South Africa should be zero rated in terms of section 11(2)(*n*) of the Act and SARS was ordered to pay the costs of the application.

4. INTERPRETATION NOTES

4.1. Additional deduction for learnership allowance – No. 20 (Issue 6)

This Note provides clarity on the interpretation and application of section 12H which provides deductions for registered learnership agreements.

The amendments to section 12H by the Taxation Laws Amendment Act No. 43 of 2014 have been taken into account in this Note and are effective from 20 January 2015 and applicable to all learnership agreements entered into on or after that date.

Section 12H provides additional deductions to employers for qualifying learnership agreements. These additional deductions are intended as an incentive for employers to train employees in a regulated environment in order to encourage skills development and job creation. Training contracts that qualify for these deductions are learnership agreements and apprenticeships registered with a SETA. These additional deductions consist of an annual allowance and a completion allowance.

Section 12H provides a deduction to an employer in addition to any other deductions allowable under the Act for any registered learnership agreement if all the requirements referred to in section 12H are met.

In some cases more than one employer may be a party to a registered learnership agreement. In such event, only the 'lead employer' identified in the learnership agreement may claim the allowances under section 12H. In practice, the 'lead employer' will usually be the employer that pays the learner's remuneration, although this is not stated in section 12H, and the matter is left to agreement between the employers.

It is not a requirement of section 12H that the employers be registered with the same SETA. The allowance is not linked to the Skills Development Levy so employers who are not levy payers may still claim the allowance.

Two types of deductions are available, namely:

- an **annual allowance**, to which the employer is entitled in any year of assessment in which a learner is a party to a registered learnership agreement [section 12H(2)]; and
- a **completion allowance** during any year of assessment in which the learner successfully completes the learnership [section 12H(3) and (4)].

The key features of these allowances are that:

- the annual allowance is subject to a *pro rata* reduction if the registered learnership agreement does not cover the full 12 months during any year of assessment [section 12H(2)(*b*)];
- different rules apply in determining the completion allowance for registered learnership agreements spanning periods of less than 24 months, and those which cover a longer period [section 12H(3) and (4)]; and
- the quantum of these allowances is increased if the learner is a person with a disability [section 12H(5)].

Section 12H provides an annual allowance and a completion allowance to employers that are a party to a qualifying learnership agreement with an employee. The annual allowance of R30 000 is subject to a *pro rata* reduction when the number of full months in a year of assessment is less than 12. The completion allowance is limited to R30 000 when the learnership is for a period of less than 24 full months. For longer agreements the completion allowance is R30 000 multiplied by the number of consecutive 12-month periods covered by the agreement. The allowances are increased to R50 000 for learnerships entered into with employees having a disability.

4.2. Limitation of allowances granted to lessors of affected assets – No. 53 (Issue 2)

This Note provides clarity and guidance on the application of section 23A, which ring-fences specified capital allowances granted to a lessor for certain aircraft, ships, machinery, plant, implements, utensils and articles ('affected assets') let under a lease that is not an 'operating lease'.

Before the introduction of section 23A in 1984, it was commonplace for certain taxpayers to acquire assets such as plant and machinery and aircraft for the purpose of letting in order to take advantage of capital allowances. The resulting accelerated capital allowances generated large assessed losses, which were used to shield other taxable income from taxation.

Section 23A limits the deduction of the specified capital allowances to a lessor’s taxable income derived from the letting of 'affected assets', before taking into account the specified capital allowances. Any specified capital allowances not allowed because of the limitation are carried forward to the next year of assessment and, subject to any section 23A limitation, are available for set-off against any net rental income from the letting of affected assets. A loss attributable to capital allowances is thus ring-fenced, and cannot be set off against other taxable income earned by the taxpayer.

In summary:

- section 23A limits capital allowances claimed by a lessor under sections 11(*e*) and (*o*), 12B, 12C, 12DA, 14*bis* or 37B(2)(*a*) on any 'affected asset' to the net rental income derived from the letting of those assets;
- the limitation does not apply to an asset let under an 'operating lease';
- in determining net rental income from letting affected assets, expenditure relating to both rental income and other income must be apportioned on some reasonable basis; and
- any specified capital allowances disallowed are carried forward to the succeeding year of assessment when they will again be considered for

deduction, and subjected to limitation under section 23A(2).

4.3. Additional investment and training allowances for industrial policy projects – No. 86

Section 12I provides for the deduction of additional investment and training allowances from the income of a company carrying on an 'industrial project' which qualifies as an 'industrial policy project'.

This Note provides guidance on the interpretation and application of section 12I and also considers the amendments proposed by the Taxation Laws Amendment Bill, 2015.

Section 12C(1)(*a*), read with paragraph (*c*) of the proviso to section 12C(1), allows for the deduction of the cost to a taxpayer of machinery or plant used by a taxpayer directly in a process of manufacture or any other similar process at a rate of 40:20:20:20 over four years. Section 12H, in turn, allows the taxpayer an additional deduction of R30 000 per learner in respect of any registered learnership agreement entered into between the learner and an employer.

Section 12I, which provides for an additional investment allowance and an additional training allowance, was introduced with the aim of supporting the main objectives of the National Industrial Policy Framework to diversify South Africa's industrial output, support a knowledge-based economy and nurture labour intensive industries. These incentives are aimed solely at benefitting projects within the manufacturing sector.

Section 12I aims to encourage investment in industrial projects, predominantly large industrial projects, in order to improve productivity within the manufacturing sector and thus support South Africa's industrial strategy. This is done by allowing an additional investment allowance on manufacturing assets and an additional training allowance for the training of employees engaged in providing services in relation to the qualifying industrial policy project.

5. DRAFT INTERPRETATION NOTES

5.1. Year of assessment of a company: Accounts accepted to a date other than the last day of a company's financial year

This Note provides guidance on the application of section 66(13C) and the discretionary power vested in the Commissioner 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 the Commissioner 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 3) dated 9 October 2013 'Year of assessment of natural persons and trusts: Accounts accepted to a date other than the last day of February', provides guidance on the Commissioner's 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.

6. BINDING PRIVATE RULINGS

6.1. BPR 207 – Merger of two controlled foreign companies (CFCs)

This ruling determines certain income tax consequences resulting from the merger of two CFCs which are wholly-owned by a resident company.

In this ruling references to sections are to sections of the Income Tax Act applicable as at 1 July 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:

- section 44(1) – the definition of 'amalgamation transaction';
- section 44(2), (3), (4) and (6);
- section 9H(6); and
- section 24BA.

Parties to the proposed transaction

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

The First Co-Applicant: A CFC incorporated in and a resident of a foreign country

The Second Co-Applicant: A CFC incorporated in and a resident of another foreign country

Description of the proposed transaction

The Applicant directly wholly-owns the two Co-Applicants.

The First Co-Applicant is a listed holding company and its principal activity is to serve as and to conduct all activities of a passive holding company.The Second Co-Applicant is a private company and serves as an intermediate holding company. The Applicant's group wants to consolidate the investments currently held through the First CoApplicant under one holding company. In order to achieve the consolidation, all the assets and liabilities of the First Co-Applicant will be transferred to the Second Co-Applicant by way of a cross-border merger.

The First Co-Applicant has liabilities, but all of those have been incurred in the ordinary course of its business.

The salient terms of the merger are:

- The First Co-Applicant will be the transferor company and the Second CoApplicant the transferee company.
- On the effective date of the merger, the First Co-Applicant will merge into the Second Co-Applicant. The ownership of all the assets of the First Co-Applicant as well as its liabilities will pass to the Second Co-Applicant by operation of law.
- Following the completion of the merger, the First Co-Applicant will automatically be dissolved (without going into liquidation) and will cease to exist.
- The Second Co-Applicant will issue one ordinary share at nominal value (the consideration share) to the Applicant in exchange for the transfer of all the assets and liabilities of the First Co-Applicant to the Second Co-Applicant. The consideration share will rank *pari passu* in all respects to the current issued share capital of the Second Co-Applicant, and will entitle the holder to participate, without restriction, in the profits of the Second Co-Applicant from the effective date of the merger.

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 merging of the First Co-Applicant in the Second CoApplicant, resulting in the transfer of the assets and liabilities of the First Co-Applicant to the Second Co-Applicant, the dissolution of the First Co-Applicant and the issuing of one (1) ordinary share at nominal value in the share capital of the Second Co-Applicant to the Applicant, will be an amalgamation transaction as envisaged in paragraph (*c*) of the definition of 'amalgamation transaction' in section 44(1) to which the provisions of section 44 will apply as follows:

- Section 44(2) and (3) will apply to the transferred assets. The issue of the consideration share and the assumption of the First Co-Applicant's liabilities by the Second Co-Applicant will not render those provisions inapplicable by virtue of section 44(4).
- Under section 44(6)(*a*), the Applicant must be deemed to have disposed of the shares held by it in the First Co-Applicant (the FCA shares) at the base cost thereof and to have acquired the consideration share issued by the Second Co-Applicant at the base cost of the FCA shares.
- Under section 44(6)(*c*), the consideration share acquired by the Applicant is deemed not to be an amount transferred or applied by the First Co-Applicant for the benefit or on behalf of the Applicant in respect of the FCA shares.
- The provisions of section 9H(6)(*a*) will apply in respect of the merger of the First Co-Applicant in the Second Co-Applicant and the issue of the consideration share by the Second Co-Applicant.
- The provisions of section 24BA will not apply in respect of the merger of the First Co-Applicant in the Second Co-Applicant and the issue of the consideration share by the Second Co-Applicant.

6.2. BPR 208 – Repayment of shareholder's loan from proceeds of a new share issue

This ruling determines the income tax consequences of a repayment of a shareholder's loan from the proceeds of a new share issue by a company.

In this ruling references to sections and paragraphs are to sections of the Income Tax Act and paragraphs of the Eighth Schedule thereto applicable as at 18 September 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:

- section 19; and
- paragraph 12A.

Parties to the proposed transaction

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

The Seller: A company incorporated in and a resident of South Africa which is a 50% shareholder of the Applicant

The Purchaser: A company incorporated and resident outside South Africa which is the other 50% shareholder of the Applicant

Description of the proposed transaction

The Seller and the Purchaser have concluded a share purchase agreement (the agreement) in terms of which the Purchaser will acquire the Seller's 50% shareholding in the Applicant (the transfer shares). An incorporated division of the Seller had previously granted loans to the Applicant for purposes of financing its business operations. These loans, consisting of capital and accrued interest, have been transferred to the Seller prior to the conclusion of the agreement. The Applicant is, therefore, indebted to the Seller (the Seller's shareholder loan).

It was always the Purchaser's intention to acquire the transfer shares only in the Applicant, therefore, the Seller's shareholder loan will have to be settled prior to the Purchaser acquiring the transfer shares.

The agreement is subject to certain suspensive conditions, amongst others, that:

- The capitalisation transaction is to be implemented in full. It follows that the subscription shares are to be issued to the Purchaser and Seller, the Seller's shareholder loan have to be repaid and the outstanding value thereof has to be reduced to nil.
- The Applicant has to obtain a binding private ruling in relation to the repayment of the Seller's shareholder loan from funds received by the Applicant from the capital contribution.

The proposed transaction will be achieved through the following transaction steps:

(a) The Seller and the Purchaser will each subscribe for one share in the Applicant.

(b) The Purchaser will subscribe for one share at a nominal value of R1.00 and the Seller will subscribe for one share at a premium equal to the face value of the Seller's shareholder loan at the time of the subscription.

(c) The Applicant will use the cash proceeds of the capital contribution to repay and discharge the Seller's shareholder loan in full.

(d) The outstanding value of the Seller's shareholder loan will, therefore, be reduced to nil before the sale of the transfer shares to the Purchaser.

<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 provisions of section 19 and paragraph 12A of the Eighth Schedule will not be applicable to the proposed transaction.

<u>Additional note</u>

This ruling does not cover the application of any general anti-avoidance provision to the proposed transaction.

6.3. BPR 209 – Dividends tax: Distribution of dividends to employees through a discretionary trust

This ruling determines whether dividends tax is to be withheld from the dividends to be distributed in cash by a company to a discretionary trust, which will distribute those dividends to the beneficiaries of the trust who are employees of that company or its subsidiaries.

In this ruling references to sections are to sections of the Income Tax Act applicable as at 14 September 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 :

- section 1(1) – definitions of 'dividend', 'gross income' and 'income';
- section 10(1)(*k*)(i)(*ii*);
- section 64D;
- section 64F(1)(*l*); and
- section 64G(2)(*a*).

Parties to the proposed transaction

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

The Co-Applicant: A Black Economic Empowerment trust (the BEE trust) established by the Applicant and a resident of South Africa 2

The Beneficiaries: Any black person (including any black person who is an employee of the Applicant or its subsidiaries), or groups of black people, whether or not they are employed by the Applicant or its subsidiaries

Description of the proposed transaction

The Co-Applicant, being a discretionary trust, was established by the Applicant to pursue Black Economic Empowerment initiatives through the provision of financial and other assistance to the Beneficiaries. The trustees are empowered to determine in any given year of assessment who the beneficiaries will be. They are not named in the trust deed.

The trustees are black persons employed by the Applicant or any of its subsidiaries, as well as independent trustees. Trustees may be beneficiaries of the trust.

The trustees may not make any distribution to a beneficiary who is an employee unless (pursuant to a BEE initiative) its purpose is to incentivise that employee or to retain his or her services within the Applicant or its subsidiaries, provided that under no circumstances shall such distribution be made with a view to replacing, in whole or in part, normal compensation and benefits that such Beneficiary would otherwise have received in his or her capacity as an employee within the Applicant or its subsidiaries.

The Applicant intends to distribute dividends in cash to the Co-Applicant (the BEE trust), which will in turn distribute those dividends to its Beneficiaries.

Ruling

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

- This ruling only applies to dividends to be distributed to the following Beneficiaries:
  - black employees of the Applicant or its subsidiaries; and
  - the trustees of the Co-Applicant, who are also black employees of the Applicant or its subsidiaries.
- The dividends to be received by the Beneficiaries mentioned in (a) above will not be exempt from normal tax, as section 10(1)(*k*)(i)(*ii*) will apply.
- The dividends to be distributed to the Beneficiaries mentioned in (a) above will be exempt from dividends tax under section 64F(1)(*l*).
- The Applicant will therefore not be required to withhold dividends tax, as contemplated in section 64G(2)(*a*), from the dividends to be paid to the Beneficiaries mentioned in (a) above, provided they have submitted their declarations and written undertakings, as contemplated in section 64G(2)(*a*), to the Applicant.

6.4. BPR 209 – Dividends tax: Distribution of dividends to employees through a discretionary trust

This ruling determines the tax consequences of a liquidation distribution followed immediately by an amalgamation transaction.

In this ruling references to sections are to sections of the Income Tax Act applicable as at 27 August 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:

- section 44; and
- section 47.

Parties to the proposed transaction

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

Subco: A company incorporated in and a resident of South Africa

Description of the proposed transaction

The Applicant and the Co-Applicant are fellow subsidiaries and have common shareholders. Subco is a wholly owned subsidiary of the Applicant. The proposed transaction is to amalgamate the Applicant and the Co-Applicant in order to consolidate their operations, as there is no longer any commercial rationale for the operation of separate companies.

The transaction steps to achieve the amalgamation will be as follows:

Step 1: Subco, which does not have any liabilities, will first distribute all its assets to the Applicant as a 'liquidation distribution' as defined in section 47(1), thereafter its corporate existence will be voluntarily terminated within 36 months.

Step 2: The Applicant and the Co-Applicant will be amalgamated in terms of an amalgamation agreement under section 113 of the Companies Act 2008, as follows:

- The Applicant will transfer its business and all of its assets to the Co-Applicant as a going concern.
- The Co-Applicant will, as consideration for the transfer of the Applicant's

business and all of its assets to the Co-Applicant:

- ○ assume all debts (including the intra-group loans currently owing by the Applicant to the Co-Applicant) and the contingent liabilities of the Applicant; and
- ○ issue equity shares to the Applicant.

- The Applicant will distribute the Co-Applicant shares, received as consideration, to its shareholders *pro rata* to their shareholding in the Applicant.
- The Applicant will be deregistered under section 116 of the Companies Act.

Conditions and assumptions

This ruling is subject to the additional condition and assumption that the shareholders of the Applicant hold the shares in the Applicant on capital account.

Ruling

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

(A) The distribution of Subco's assets (the distributed assets) to the Applicant will be a 'liquidation distribution' as contemplated in paragraph (*a*) of the definition thereof in section 47(1) and consequently:

- Subco will not –

  (i) recover or recoup allowances previously deducted by it in respect of the applicable allowance assets as contemplated in section 47(3)(*a*)(i), or

  (ii) realise any capital gain arising out of the transfer of those assets as contemplated in section 47(2)(*a*).

- The Applicant and Subco will, under section 47(3)(*a*)(ii), be deemed to be one and the same person for the purposes of –

  (i) claiming allowances on allowance assets in the future; and

  (ii) the recovery or recoupment of allowances in respect of allowance assets on the future disposal of those assets by the Applicant.

- The Applicant must, under section 47(5), disregard, for the purposes of determining it's taxable income, assessed tax loss, aggregate capital gain or aggregate capital loss resulting from –

  (i) the disposal of the equity shares held by the Applicant in Subco as a consequence of the liquidation, winding-up or deregistration of Subco; and

  (ii) any return of capital which the Applicant receives from Subco by way of a distribution of cash or an asset *in specie*.

(B) The transfer by the Applicant of all its assets to the Co-Applicant in terms of the amalgamation agreement will constitute an 'amalgamation transaction' as contemplated in paragraph (*a*) of the definition thereof in section 44(1) and, accordingly:

- The Applicant will not:

  (i) recover or recoup any allowances previously deducted by either the Applicant or Subco in respect of the applicable allowance assets, as contemplated in section 44(3)(*a*); or

  (ii) realise a taxable capital gain as a result of the transfer of any capital assets, as contemplated in section 44(2)(*a*)(i).

- The transfer by the Applicant of the distributed assets to the Co-Applicant will not result in the application of section 47(4).

- The Co-Applicant will be entitled to the same capital allowances in respect of the applicable allowance assets to which the Applicant was previously entitled, as contemplated in section 44(3)(*a*)(ii).

- The shareholders of the Applicant will be deemed to have disposed of their shares in the Applicant for their base cost amount, as contemplated in section 44(6)(*b*)(i).
- The shareholders of the Applicant will be deemed to have acquired the equity shares in the Co-Applicant at the base cost value of the Applicant's shares, as contemplated in section 44(6)(*b*)(ii).
- The shareholders of the Applicant will be deemed to have acquired the equity shares in the Co-Applicant on the date that they had acquired the shares in the Applicant, as contemplated in section 44(6)(*b*)(iii).
- The equity shares acquired in the Co-Applicant by a shareholder of the Applicant will be deemed not to be an amount transferred or applied by the Applicant for the benefit or on behalf of that person in respect of the shares held by that person in the Applicant, as contemplated in section 44(6)(*c*). The acquisition of equity shares in the Co-Applicant will therefore not be subject to dividends tax or normal tax in the shareholder's hands. 4
- All the liabilities to be assumed by the Co-Applicant in terms of the amalgamation agreement, including:

(i) the contingent liabilities;

(ii) the liabilities under contracts; and

(iii) the debts currently owed by the Applicant to the Co-Applicant that will be discharged by merger,

will qualify as 'debts' assumed by the Co-Applicant as consideration for purposes of section 44(4).

7. GUIDES

7.1. Guide on the Determination of Medical Tax Credits (Issue 6)

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.

This guide includes the amendments effected by section 3(1) of the Taxation Laws Amendment Act 43 of 2014 and by section 4(1) of the Rates and Monetary Amounts and Amendment of Revenue Laws Act 42 of 2014, both promulgated on 20 January 2015. As the year of assessment of an individual ends on the last day of February, these amendments apply to the years of assessment commencing on or after 1 March 2014 (that is, the 2015 year of assessment).

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 over the last three years. The deduction system has been completely repealed, and has been replaced by 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

The two types of credits are dealt with separately in this guide, namely:

(i) Part A – the MTC, dealing with contributions to a medical scheme; and

(ii) Part B – the AMTC (which replaced the deduction of the medical allowance)1 dealing with other qualifying medical expenses, including out-of-pocket expenses.

7.2. *Comprehensive Guide to CGT (Issue 5)*

The purpose of this guide is to assist the public and SARS' personnel in gaining a more in-depth understanding of CGT. The foundation for this guide can be found in the various Explanatory Memoranda that supported the legislation. These initial explanations have been completely revised, with the addition of many more explanations, examples and illustrations. Much of the additional material was inspired by the many e-mail and written queries submitted by the public.

This guide is not an 'official publication' as defined in section 1 of the Tax Administration Act and accordingly does not create a practice generally prevailing under section 5 of that Act. It is also not a binding general ruling under section 89 of Chapter 7 of the Tax Administration Act. Should an advance tax ruling be required, visit the SARS website for details of the application procedure.

This work reflects the law as at 20 January 2015 as amended by the Taxation Laws Amendment Act 43 of 2014 and the Tax Administration Laws Amendment Act 44 of 2014. The 2015 tax rates have been used in this guide. These rates apply to companies with years of assessment ending between 1 April 2014 and 31 March 2015 and to persons other than companies with years of assessment commencing on 1 March 2014.

8. 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.