TAX UPDATE

For period: 1 July 2015 to 30 September 2015

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1. INTRODUCTION

The purpose of this update is to summarise developments that occurred during the third 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.

Important development in this quarter is the issue of the Draft Taxation Laws Amendment Bill, 2015, (TLAB) and the Draft Tax Administration Laws Amendment Bill, 2015, (TALAB). This should be considered and one should reflect on the aspects of importance to one's affairs.

Case law is always interesting to read; to see how legislation is applied to facts. The two cases that are quite interesting is Parker's case, as to whether the non payment of VAT to SARS amounts to theft, and Medox's case, as to whether certain assessments were invalid.

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. MEDIA STATEMENT - PUBLICATION OF THE 2015 DRAFT TAXATION LAWS AMENDMENT BILL AND THE DRAFT TAX ADMINISTRATION LAWS AMENDMENT BILL

The National Treasury today publishes, for public comment, the 2015 Draft Taxation Laws Amendment Bill (TLAB) and the 2015 Draft Tax Administration Laws Amendment Bill (TALAB). These bills provide the necessary legislative amendments required to implement most of the tax proposals that were announced in the 2015 Budget on 25 February 2015.

Changes to the rates and thresholds announced in the 2015 Budget were included in the 2015 Rates and Monetary Amounts and Amendment of Revenue Laws Bill that was published on the same day as the 2015 Budget Review. The 2015 draft TLAB deals with more substantive changes to the tax laws while the 2015 draft TALAB deals with administrative provisions of tax legislation currently administered by SARS, including the Tax Administration Act, 2011.

National Treasury and the South African Revenue Service (SARS) hereby invite comments in writing on these draft bills, prior to their formal introduction in Parliament. In addition, the Standing Committee on Finance in Parliament normally makes a similar call for public comment, and convenes public hearings on the draft bills before their formal introduction in Parliament. Where deemed necessary, National Treasury and SARS will also engage separately with key stakeholders, including through workshops that may be held in early September. Thereafter, a response document on comments received will be presented to the Standing

Committee on Finance. The bills will then be revised, taking into account public comments, before they are tabled formally tabled in Parliament for its consideration.

A first batch of the 2015 TLAB was published on 5 June 2015 containing tax proposals that required an additional round of comments. These proposals included measures to counter tax-free corporate migrations, transitional tax issues resulting from the regulation of hedge funds and the tax implications of the outright transfer of collateral. The current draft TLAB includes these proposals with the amendments that have arisen from comments received on the first batch.

The 2015 draft TLAB gives effect to the following key proposals announced in the 2015 Budget Review:

- Closing a loophole to ensure consistent tax treatment on all retirement funds
- Closing a loophole to avoid estate duty through excessive contributions to retirement funds
- The tax implications of the outright transfer of collateral
- Transitional tax issues resulting from the regulation of hedge funds
- Measures to counter tax free corporate-migrations
- Withdrawal of special foreign tax credits for service fees sourced in South Africa
- Reinstatement of the controlled foreign company diversionary income rules
- Allowing municipalities to demarcate more areas as Urban Development Zones
- Monetary threshold adjustments for enterprise supplying commercial accommodation

In addition to the above amendments, it should be noted that further amendments may be effected to the *de-minimis* threshold at which individuals would be required to purchase an annuity at retirement, to take into account consultations through

NEDLAC. This will be in line with a request arising from hearings in the Standing Committee on Finance in 2014.

For legal reasons, the draft tax amendments continue to be split into two bills, namely a money bill (section 77 of the Constitution) dealing with money bill issues and an ordinary bill (section 75 of the Constitution) dealing with issues relating to tax administration.

The 2015 draft TALAB gives effect to the following key proposals:

- Medical scheme tax credits to be taken into account for PAYE
- Collection of information by South African financial institutions and an associated obligation on the financial institutions to register with SARS
- Extension of period of limitations for issuance of assessments under narrow circumstances
- Clarifying qualifying persons for voluntary disclosure, relaxing the requirements for voluntary disclosure and broadening the ambit of voluntary disclosure relief

Greater transparency and the automatic exchange of information between tax administrations is an important step forward in countering cross border tax evasion and aggressive tax avoidance. The requirement for South African financial institutions to collect certain information is necessary to allow SARS to implement agreements under international tax standards, such as the OECD Standard for Automatic Exchange of Financial Account Information in Tax Matters, which encompasses the Common Reporting Standard that was endorsed by the G20 Finance Ministers in 2014.

The draft legislation and the draft explanatory memorandum containing a comprehensive description of the draft amendments can be found on the National Treasury (www.treasury.gov.za) and SARS (www.sars.gov.za) websites.

3. DRAFT MEMORANDUM ON THE OBJECTS OF THE TAX ADMINISTRATION LAWS AMENDMENT BILL, 2015 – ONLY TAX ADMINISTRATION ACT AMENDMENTS

3.1. 1. Purpose of bill

The Bill proposes to amend the Transfer Duty Act, 1949, the Income Tax Act, 1962, the Customs and Excise Act, 1964, the Value-Added Tax Act, 1991, the Skills Development Levies Act, 1999, the Unemployment Insurance Contributions Act, 2002, the Taxation Laws Second Amendment Act, 2008, the Mineral and Petroleum Resources Royalty (Administration) Act, 2008, the Tax Administration Act, 2011, the Customs Duty Act, 2014, the Customs Control Act, 2014 and the Tax Administration Laws Amendment Act, 2014.

3.2. 2.32. Amendment of section 1 – Definitions

Ad par. (a): This amendment proposed a common term including all customs and excise legislation to avoid having to refer to each Act separately.

Ad par. (b): Greater transparency and the automatic exchange of information between tax administrations is an important step forward in countering cross border tax evasion and aggressive tax avoidance. This amendment is required to implement a scheme under which SARS may require South African financial institutions to collect information under an international tax standard, such as the OECD Standard for Automatic Exchange of Financial Account Information in Tax Matters, which encompasses the Common Reporting Standard (CRS) that was endorsed by G20 Finance Ministers in 2014. In order to implement the standard on a consistent and efficient basis, 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.

This will substantially ease the compliance burden on reporting financial institutions as they would otherwise have to effect system changes and collect historical information each time a jurisdiction is added to the CRS or South Africa concludes a new international tax agreement. The reporting financial institutions will, pursuant to this amendment, be obliged by statute to obtain the information and provide it to SARS and should not contravene any relevant data protection laws.

This amendment will come into operation on the date of promulgation of this Act.

Ad par. (c): The definition of 'tax Act' is amended to include the new definition 'customs and excise legislation'.

3.3. 2.33. Amendment of section 3 – Administration of tax Acts

Ad par. (a): See the note on paragraph 2.32 above.

Ad par. (b): The proposed amendment is a technical correction to align the current provision with the definition of 'international tax agreement' in section 1. See also the note on paragraph 2.32 above.

3.4. 2.34. Amendment of section 6 – Powers and duties

The proposed amendment is a technical correction to clarify that a SARS official may execute a task authorised by a person delegated by the Commissioner.

3.5. 2.35. Amendment of section 11 – Legal proceedings involving

Section 11(1) was essentially intended to deal with civil proceedings where the authority to institute the proceedings are not otherwise prescribed in the specific sections of the Tax Administration Act, as well as other matters such as Promotion of Administrative Justice Act ('PAJA') review applications etc.

Recent arguments surfaced that each SARS deponent in litigation must have a section 11(1) authorisation from the Commissioner. This amendment aims to clarify that an additional authorisation of a deponent by the Commissioner or the SARS official duly authorised by the Commissioner under section 11(1) to approve the institution or defending of civil proceedings, is not required. The deponent merely executes the authorisation as provided for in section 6(4).

This is also the case with most of the Tax Administration Act's payment or recovery proceedings, even if they are judicial and not only administrative in nature, for example section 163 (High Court), section 172 (including obtaining judgment in the High Court), section 177 (institution of proceedings for liquidation) and section 186 (High Court). These sections specifically prescribe who may institute the proceedings, for example a senior SARS official in the case of a section 163 application. An additional authorisation under section 11 is not required for proceedings under these sections based on the *expression unius est exclusion alterius* principle – i.e. the mention of one matter (e.g. section 163) excludes the other (e.g. section 11(1)). This is given express effect by the words *'except where otherwise regulated in this Act'* included in the proposed amendment.

3.6. 2.36. Amendment of section 22 – Registration requirements

See paragraph 2.37.

3.7. 2.37. Amendment of section 26 – Third party returns

In order to ensure that the relevant financial institutions comply with international tax standards, such as the CRS, the proposed amendment will require them to register with SARS for this purpose. This registration will assist SARS in the administration and enforcement of international tax standards, such as the CRS. A registration process currently exists for purposes of the inter-governmental agreement concluded with the United States of America and the associated Foreign Account Tax Compliance Act (FATCA).

3.8. 2.38. Amendment of section 34 – Definitions

The proposed amendment aims to include any person who is a party to an arrangement listed in a public notice by the Commissioner in terms of section 35(2) in the definition of a participant thereby imposing a reporting obligation on such persons.

3.9. 2.39. Amendment of section 36 – Excluded arrangements

The proposed amendment is a technical correction. This section still refers to the Securities Services Act, 2004 (Act No. 36 of 2004), that was repealed with effect from 3 June 2013 and replaced by the Financial Markets Act, 2012 (Act No. 19 of 2012).

3.10. 2.40. Insertion of section 42A – Procedure where legal professional privilege is asserted

In the context of information requests, interviews and field audits, legal professional privilege is often asserted in respect of information required by SARS. This section seeks to clarify the requirements that must be met for such assertion and provides for a procedure for matters where SARS does not accept the assertion of legal professional privilege.

3.11. 2.41 Amendment of section 46 – Request of relevant material

Ad par. (a): The proposed amendment clarifies that a request by SARS for relevant material from third parties is limited to information maintained or kept or that should reasonably be maintained or kept by the person in relation to the taxpayer.

Ad par. (b): The obtaining and use of information under oath or solemn declaration is a fairly common practice in most civil and criminal investigations. Under the scheme of the Tax Administration Act, only impactful decisions are reserved for senior SARS officials. Here the request is by a SARS official duly authorised by a senior SARS official to conduct an audit or criminal investigation under section 41, who is then tasked with the execution of the audit or criminal investigation as contemplated in section 6(4).

Ad par. (c): This amendment deals with foreign information requests. During the course of an audit of a South African member of a multinational group it may be necessary to obtain relevant material that is held by other members of the group located outside South Africa. While the South African members of some groups are willing to obtain and furnish such material to SARS, others assert that they are they are not in a position to do so. In Practice Note 6 of 1999 SARS noted that 'taxpayers may face difficulties obtaining information from foreign connected persons. Such difficulties would not be encountered if taxpayers were required to produce only their own documents. However, due to the relationship between the parties the Commissioner considers it reasonable to expect taxpayers to obtain such information where necessary.'

An amendment is proposed to ensure that taxpayers do not assert that they are unable to obtain and provide relevant material, only to provide it at a later stage, for tactical reasons. A minimum period for requesting relevant material held by a group member that is not in South Africa is proposed, together with a prohibition of a taxpayer's subsequent use of that material if it was not produced when requested. This prohibition may be relaxed by a competent court in subsequent proceedings but only in exceptional circumstances, which do not include the fact that the relevant material was held by a person outside South Africa.

3.12. 2.42. Amendment of section 47 – Production of relevant materials in person

The proposed amendment aims to clarify which persons may be interviewed or requested to submit relevant material where the person whose tax affairs is under verification or audit is a company or other legal entity. Hence, the proposed amendments provides that a senior SARS official may require:

- a current employee of the entity; or
- a person who holds an office in that entity;

to attend in person at a time and place designated in the notice for the purpose of being interviewed by a SARS official concerning the tax affairs of the relevant taxpayer, where the interview is intended to obtain relevant material to clarify issues of concern to SARS regarding a verification or audit. The person so interviewed may also be required to submit relevant material under his or her control and to clarify issues of concern related to the relevant material.

3.13. 2.43. Amendment of section 49 – Assistance during field audit or criminal investigation

This amendment allows SARS to request a person being questioned during a field audit to provide information under oath or solemn declaration, similar to SARS' power to do so under section 46(7)*(a)*. See further discussion in paragraph 2.41.

3.14. 2.44. Amendment of section 51 – Inquiry order

The proposed amendments will allow SARS to use inquiry proceedings under this Part to trace assets that may be executed against to satisfy an outstanding tax debt without having to first sequestrate or liquidate a taxpayer and then follow the insolvency enquiry route, which generally takes a very long time to conclude and is not under the control of SARS.

3.15. 2.45. Amendment of section 68 – SARS confidential information and disclosure

Section 21 of the Customs Control Act, 2014, is broadened to include a similar provision to that of section 68(1)*(g)*, hence the reference to the 'Customs and Excise Act' in the section 68 of the Tax Administration Act, 2011, can be deleted.

3.16. 2.46. Amendment of section 69 – Secrecy of taxpayer information and general disclosure

The proposed amendment provides that taxpayer information obtained by a current or former SARS official in the course of performance of duties under a tax may be disclosed by that official for purposes of the administration of the Customs and Excise Act, 1964, the Customs Duty Act, 2014 and the Customs Control Act, 2014.

3.17. 2.47. Amendment of section 70 – Disclosure to other entities

The proposed amendment is a technical correction.

3.18. 2.48.Amendment of section 93 – Reduced assessments

Section 93(1)(*d*) was inserted to allow taxpayers a less formal mechanism to request corrections to their returns and so reduced assessments. Experience has demonstrated that the overwhelming majority of taxpayers request a correction to their returns within six months of assessment. Other taxpayers have, however, attempted to use requests for correction to raise substantive issues that would more properly be the subject of an objection under section 104, so as to bypass the timeframes and procedures for an objection. Taxpayers and unregistered tax practitioners have also attempted to use the requests for correction to obtain fraudulent refunds for multiple years. It is therefore proposed to limit the period during which a request for correction may be submitted to six months from date of assessment, with the possibility of an extension to a year under exceptional circumstances. Matters that fall outside these timeframes will have to be subject of an objection.

3.19. 2.49. Amendment of section 98 – Withdrawal of assessments

Finality in a tax assessment is important for both taxpayers and SARS, which is why there is a period within which a SARS may revise an assessment to the benefit or otherwise of a taxpayer. This period, which is commonly known as the prescription period, is either three years for taxes assessed by SARS or five years for taxes that are self-assessed by taxpayers. Limited exceptions to prescription apply where fraud, misrepresentation or material non-disclosure exist in a tax return, in order to give effect to the outcome of a dispute resolution process – such as an objection or appeal to a court.

The original purpose of the insertion of section 98(1)*(d)* was to address problems with erroneous assessments which are often only discovered after all prescription periods and remedies have expired and it becomes apparent that it would be inequitable to recover the tax due under such assessments. An example would be that of a retiree who was assessed in error based on incorrect information supplied by an employer or a retirement fund, who fell below the tax threshold after retirement and thus ceased to submit returns to SARS and was only traced some years later in order to recover the outstanding tax debt as a result of the incorrect assessment. The insertion of the new paragraph aimed to address this problem by allowing for the withdrawal of assessments in specified narrow circumstances, which were the following:

- The assessment must be based on an undisputed factual error by the taxpayer in a return; a processing error by SARS; or a return fraudulently submitted by a person not authorised by the taxpayer;
- The assessment imposes an unintended tax debt in respect of an amount that the taxpayer should not have been taxed on;
- The recovery of the tax debt under the assessment would produce an anomalous or inequitable result;
- There is no other remedy available to the taxpayer; and
- It is in the interest of the good management of the tax system.

However, it immediately became apparent that taxpayers interpreted the section as a general mechanism to address their 'old mistakes' in assessments that were final, where the taxpayer could no longer request a reduced assessment or where the objection process as well as appeals to the tax and higher courts had been exhausted. In respect of most of these matters there was no unintended tax debt the recovery of which would be inequitable. In actual fact, if most of the assessments sought to be withdrawn were given effect to, SARS would have had to pay refunds.

The insertion of section 98(1)(*d*) was not intended as a substitute to the above procedures nor as a 'post-appeal appeal' remedy, including in one memorable case an attempt to reverse an adverse judgment by the Supreme Court of Appeal. The true intention was to address adverse assessments resulting from factors beyond the control of the taxpayer, for example the failure to submit a return or submission of an incorrect return by a third party under section 26 or by an employer under a tax Act, where the right of the taxpayer to object or seek an extension within the period referred to in section 104(3) has expired. This happens where a taxpayer only becomes aware of the problem after three years and can no longer object against the assessment, which has become final.

Accordingly, amendments are proposed to give effect to the true purpose of section 98(1)(*d*). In addition, were an assessment is withdrawn SARS may issue a revised original, additional or reduced assessment if satisfied it is required for the relevant tax period in issue. If this assessment is an agreed assessment between SARS and the taxpayer, it is not subject to objection and appeal.

3.20. 2.50. Amendment of section 99 – Period of limitation of issuance of assessments

Too many of SARS' resources are currently spent on information entitlement disputes, as opposed to conducting the audit within the period that additional assessments, if required, may be issued. This results in insufficient time to ensure SARS has all relevant information at its disposal to ensure correct assessment. In some cases, taxpayers, particularly large corporates, take more than six months to provide information required by SARS by disputing SARS' right to obtain the information, attempting to impose conditions on access to the information and attempting to require specific mechanisms for accessing the information. Information entitlement disputes, particularly if pursued in the High Court, can take more than one year to resolve. These failures to provide information or information entitlement disputes are often tactical or even vexatious, given the fact that taxpayers are very much aware of the period within which SARS must finalise the audit and issue additional assessments, if required.

Information entitlement disputes based on often convoluted or strained interpretations of the relevant provisions of the Tax Administration Act, have led to legislative changes over the past few years. As an example last year the Tax Administration Laws Amendment Act, 2014, had to clarify that a taxpayer cannot unilaterally decide the relevance of 'relevant material' and refuse to even show it to SARS.

Additionally, some matters subject to audit may be so complex that it is impossible to meet the prescription deadline, particularly in the context of audits requiring SARS to consider the application of a general anti-avoidance rule (GAAR), or transfer pricing audits. Transfer pricing audits are fundamental to counteracting the erosion of the South African tax base and the shifting of profits to other jurisdictions – generally referred to as BEPS.

It is, therefore proposed that prescription be extended for a period appropriate to cater for a failure to provide information within a reasonable period, the time required to resolve a dispute as to SARS' entitlement to information or for up to three years if the application of a GAAR, transfer pricing or similarly complex matter is involved. The extension must take place before the existing prescription period has come to an end.

3.21. 2.51. Amendment of section 105 – Forum for dispute of assessment or decision

The current wording of section 105 creates the impression that a dispute arising under Chapter 9 may either be heard by the tax court *or* a High Court for review. This section is intended to ensure that internal remedies, such as the objection and appeal process and the resolution thereof by means of alternative dispute resolution or before the tax board or the tax court, be exhausted before a higher court is approached and that the tax court deal with the dispute as court of first instance on a trial basis. This is in line with both domestic and international case law.

The proposed amendment makes the intention clear but preserves the right of a High Court to direct otherwise should the specific circumstances of a case require it.

3.22. 2.52. Amendment of section 109 – Jurisdiction of the board

A situation may arise where there is more than one period on appeal and the combined value of the appeals over the periods is beyond the tax board threshold (currently set at R500 000). Had the appeal for each period occurred one at a time, there would be no difficulty in referring the appeal to the tax board. In order to preserve this possibility when the appeals occur at the same time it is proposed that the tax board may hear all the appeals, if SARS and the taxpayer so agree and the amount of tax in dispute in each appeal does not exceed the tax board threshold.

3.23. 2.53. Amendment of section 111 – Appointment of chairpersons

The proposed amendment aligns this provision with similar requirements for members of the tax court under section 120(2). There appears to be no apparent rationale for the differentiation between the members of the tax court under section 120(2) and persons appointed as chairpersons of the tax board.

3.24. 2.54. Amendment of section 135 – Leave to appeal to Supreme Court of Appeal against tax court decision

The Supreme Court Act, 1959 (Act No. 59 of 1959) was repealed by the Superior Courts Act, 2013 (Act No. 10 of 2013): Section 55 read with Item No. 1 of Schedule 1 to that Act. Section 135(3) refers to section 21 of the repealed Supreme Court Act. The right to appeal is now covered by section 17 of the

Superior Courts Act, 2013 and the proposed amendment inserts the correct reference.

3.25. 2.55. Amendment of section 146 – Circumstances where settlement is appropriate

It is proposed that section 146*(b)*(ii) and (iii) be deleted in the context of settlement as those aspects relate to debt write-off.

3.26. 2.56. Amendment of section 177 – Institution of sequestration, liquidation or winding-up proceedings

The proposed amendment aligns section 177 with the institution of other High Court proceedings and impactful recovery proceedings e.g. sections 163, 179, 185 and 186, which proceedings require the authorisation of senior SARS officials.

3.27. 2.57. Amendment of section 179 – Liability of third party appointed to satisfy tax debts

Ad par. (a): Section 179 provides that SARS may by notice to a person who holds or owes (or will hold or owe) money for or to a taxpayer, require that person to pay the money to SARS in satisfaction of the taxpayer's tax debt. The current wording requires a senior SARS official to issue notices of third party appointments (Form IT88). In line with other amendments proposed in this Bill, it is proposed that the senior SARS official approve the issue of the notices. In view of SARS' substantial debt book, the issue of these notices may be automated. The proposed amendment will make it clear that if a senior SARS official has approved the system criteria for issuing the notices their issue may be automated. This only occurs under prescribed circumstances, in particular where there is an outstanding tax debt and letters of demand have been issued.

Ad par. (b): Section 179(2) and (4) provide remedies for the person required to pay the money to SARS as well as the relevant taxpayer. If the person who receives the notice of payment is unable to comply with the notice that person must advise SARS of the reasons for the inability to comply within the period specific in the notice and SARS may withdraw or amend the notice as is appropriate under the circumstances. Furthermore, a taxpayer affected by the notice may request SARS to amend the notice to extend the period over which the amount must be paid to SARS so as to allow the taxpayer to pay his or her basic living expenses or that of his or her dependents. The amendment seeks to ensure that the relevant person or taxpayer is able to exercise their respective remedies before the amount is paid to SARS. The new subsection (2) would allow for a process and system in this regard.

Ad par. (c): The proposed amendment moves the content of subsection (4) to a new subsection (2).

3.28. 2.58. Amendment of section 185 – Tax recovery on behalf of foreign governments

This proposed amendment clarifies that the senior SARS official referred to in section 185 only needs to authorise the application while the execution thereof can be done by a person referred to in section 6(4).

3.29. 2.59. Amendment of section 187 – General interest rules

Ad par. (a): The proposed amendment is a technical correction to clarify that interest accrues and is also payable.

Ad par. (b): Under section 190(5) a refund paid by SARS which was not properly payable, for example as a result of fraud, is regarded as an outstanding tax debt summarily recoverable by SARS. As with any other tax debt, interest must also accrue and be payable on this amount in respect of the time taken to recover the amount of the refund not properly payable. This requires an effective date under section 187(3) from which date the interest will accrue.

Ad par. (c): The right to request interest remittance cannot be open ended or finality will never be achieved. This limitation did apply in terms of repealed provisions of some of the tax Acts other than the Tax Administration Act.

3.30. 2.60. Amendment of section 190 – Refunds of excess payments

Ad par. (a): The proposed amendment clarifies that a taxpayer is entitled to a refund and interest thereon as provided for in a tax Act.

Ad par. (b): The current wording of section 190(4) leads to the perception that a taxpayer must, in addition, also *claim* an assessed refund, and that the taxpayer then only has 3 years for an administrative assessment or 5 years for self-assessment, within which to claim the refund. Paragraph *(b)* of subsection was incorrectly deleted as the limitation periods only apply where an erroneous overpayment of tax was made. A refund properly refundable and payable under a tax Act in terms of section 190(1)*(a)* must be paid by SARS and there is no limitation period for such payment.

If a refund of an amount erroneously paid in respect of an assessment in excess of the amount payable in terms of the assessment, is not claimed within this period, it is regarded a payment to the National Revenue Fund, as is the case with any other claim that has prescribed and may be regarded as a final payment.

Ad par. (c): The proposed amendment clarifies that interest accrues and is payable on the amount of a refund that was not properly payable from the date of such payment.

Ad par. (d): SARS and banks have an arrangement whereby banks report suspicious refunds to SARS. This is pursuant to a bank's common law duty to report suspected fraud through the use of bank accounts. Under this arrangement, the banks agreed to hold the funds for a short period to allow SARS to investigate the circumstances around the refund. If the refund is false, SARS recovers the refund directly from the bank by appointing the bank as a responsible third party under section 179 of the Tax Administration Act, 2011, as the amount under section 190(5) is regarded as an outstanding tax debt form the date of payment thereof.

In view of the high incidence of refund fraud, in particular the payment of refunds of relatively small amounts that fall under SARS' 'stopper' threshold *as well as* VAT refunds generated by fictitious transactions or inflated input tax claims, there is a clear and pressing need to preserve the arrangement between the banks and SARS. The preservation of the account is of particular importance in view of the practice to dissipate or transfer the amounts to various other accounts or the withdrawal thereof as soon as or shortly after the fraudulent refunds are deposited.

As a result of the possibility that the Protection of Personal Information Act, 2013 (POPI), now supersedes or limit the common law reporting duty of banks, the potential exposure by banks to damages claims by client for damages resulting from the temporary 'freezing' of accounts and the disclosure of personal information to SARS potentially contrary to POPI, this amendment will ensure that such preservation will be lawful and the reporting by banks to SARS will remain lawful and not subject to criminal sanctions under POPI. Although it is not absolutely clear that POPI supersedes or limit the common law reporting duty of banks, it is submitted that the proposed amendment is necessary to ensure certainty in this regard.

The Financial Intelligence Centre Act, 2001 (FICA), imposes a reporting a reporting duty on banks of certain suspicious transactions to the FIC. Currently, section 29(1)*(b)*(i) of FICA imposes a reporting duty in respect of a transaction that 'may be relevant to the investigation of an evasion or attempted evasion of a duty to pay any tax, duty or levy imposed by legislation administered by the Commissioner for the South African Revenue Service'. It is not clear that these provisions cover the reporting of fraudulent tax refunds and it is similarly submitted that the proposed amendment is necessary to ensure certainty in this regard.

Ad par. (e): The refusal of a refund under an assessment referred to in section 1*(a)* involves many factors, calculations and other aspects of determining the amount of tax or a refund. Accordingly, the whole of such assessment must be disputed under the general objection provision in section 104, and not just the decision not to authorise a refund. The amendment clarifies that the remedy under subsection (6) only applies to a decision not to refund an amount erroneously paid in respect of an assessment and a decision that acceptable security is not tendered for purposes of payment of the refund amount subject to audit.

3.31. 2.61. Amendment of section 191 – Refunds subject to set-off and deferral

Technical amendment to correct spelling of 'write off' and amendment to include new defined term 'customs and excise legislation'.

3.32. 2.62. Amendment of section 212 – Reportable arrangement penalty

A proposed amendment to section 34 aims to include any person who is a party to an arrangement listed in a public notice by the Commissioner in terms of section 35(2) in the definition of a participant thereby imposing a reporting obligation on such persons. As this is a third party reporting obligation i.e. these persons do not directly or indirectly derive or are assumed to derive a tax benefit or a financial benefit by virtue of an arrangement, it would be unreasonable to subject them to the stricter reportable arrangement penalties contained in section 212(1) and (2). Hence the new subsection (3) inserts a separate penalty provision for this category of persons.

3.33. 2.63. Amendment of section 213 – Imposition of percentage based penalty

The proposed amendment is a technical correction to cater for a non-compliance penalty imposable under a tax Act other than the Tax Administration Act.

3.34. 2.64.Amendment of section 226 – Qualifying person fo voluntary disclosure

The proposed amendment aims to clarify that an audit, unrelated to the default being disclosed by an applicant, will not disqualify an applicant for full voluntary disclosure relief. As an example, an audit of a taxpayer related to a PAYE issue is in progress. The same taxpayer may wish to submit a disclosure for an amount of VAT. There may be no correlation between these two tax issues and, as such, the enforcement action on the PAYE issue may not be a cause to restrict the relief in respect of the VAT disclosure. The proposed amendment clarifies that the audit or investigation must be related to the default the person seeks to disclose.

3.35. 2.65. Amendment of section 227 – Requirements for valid voluntary disclosure

Currently one of the requirements for a valid voluntary disclosure is that the disclosure must involve a 'default' which has not previously been disclosed by the applicant. The proposed amendment now requires that the 'default' must not be a default that occurred within five years of the disclosure of a similar 'default' by the applicant, thereby widening the scope of the voluntary disclosure regime.

Furthermore, the potential imposition of an understatement penalty as a requirement for a valid voluntary disclosure has been interpreted by SARS as meaning that in the absence of voluntary disclosure relief, an understatement penalty would be leviable. On this interpretation, a *bona fide* inadvertent error as contemplated in section 222(1) does not qualify for voluntary disclosure relief. Furthermore, a default that does not constitute a substantial understatement and where the other behaviours contemplated in section 223 are also not present would also not qualify for voluntary disclosure relief, notwithstanding that SARS may take a contrary view with regard to the assessment of the relevant behaviour. The proposed amendment aims to resolve this issue by amending the requirement to rather refer to the behaviour in Column 2 of the understatement penalty percentage table in section 223.

3.36. 2.66. Amendment of section 229 – Voluntary disclosure relief

The proposed amendment is of a textual nature and furthermore broadens the voluntary disclosure relief to include 100% relief in respect of administrative non-compliance penalties imposed under Chapter 15 of the Tax Administration Act, or another tax Act for the late payment of a tax.

3.37. 2.67. Amendment of section 236 – Criminal offences relating to filing return without authority

The proposed amendment is a technical correction.

3.38. 2.68. Amendment of section 251 – Delivery of documents to persons other than companies

The proposed amendment aims to clarify that a delivery may also be made to a registered user's electronic filing page. A registered user is a person who has registered for a SARS electronic filing service such as eFiling, e@syFile, a third party data submission channel or such like and their electronic filing page is akin to a web based e-mail used exclusively by SARS and the person to whom the page belongs.

3.39. 2.69. Amendment of section 252 – Delivery of documents to companies

See paragraph 2.68.

3.40. 2.70. Amendment of section 256 – Tax Compliance status

SARS is often approached to verify the Tax Compliance Status of an entity for periods before the current date of the request. The proposed amendment enables SARS to provide the tax compliance status of a taxpayer irrespective of the period to which the request relates in order to assist in the review of past transactions by the taxpayer's auditors and regulatory authorities.

3.41. 2.71. Amendment of section 257 – Regulations by Minister

The proposed amendment aims to align this provision with the amended wording of section 256 and furthermore enables the Minister to prescribe by regulation when SARS must report updates of or a change in the tax compliance status of certain taxpayers, for example taxpayers with government contracts.

3.42. 2.72. Amendment of section 270 – Application of Act to prior or continuing action

The proposed amendment aims to further alleviate unintended consequences of the retrospective application of an understatement penalty. Section 187(3)*(f)* provides that the effective date for purposes of the calculation of interest in relation to an understatement penalty, is the effective date for the tax understated. As Chapter 12 (together with the accompanying amendments to the interest provisions of the various tax Acts as contained in Schedule 1 to this Act) will only come into effect upon a date to be determined by the President by proclamation, the payment of interest on an understatement penalty under section 222 would have to calculated in the manner that interest on additional tax [the predecessor to understatement penalties] was calculated under the relevant interest provisions of the specific tax Act. The proposed amendment inserts a transitional provision to this effect with a specific effective date i.e. the effective date as referred to in section 187(3)*(f)*, for tax understated before the implementation date of the Tax Administration Act, will be regarded as the commencement date of the Act, i.e. 1 October 2012.

Once Chapter 12 (together with the accompanying amendments to the interest provisions of the various tax Acts as contained in Schedule 1 to this Act) has been promulgated, the accrual and payment of interest on an understatement penalty will be calculated in the manner prescribed by Chapter 12 in respect of an understatement penalty imposed after such date.

4. NOTICES & REGULATIONS

4.1. VDP – South Africans with accounts and investments in foreign tax jurisdictions

The purpose of this media statement is to provide an update on the progress made by SARS on work done on foreign bank accounts held by South African residents and to provide such residents an opportunity until 12 August 2015, to approach SARS via its Voluntary Disclosure Programme (VDP) to regularise their tax affairs.

During February 2015, various media articles referred to the release of information pertaining to South African residents who are or were HSBC accountholders. As stated by SARS at the time, early indications were that some accountholders may have utilised their accounts to evade their local and/or international tax obligations based on the information SARS had received.

SARS has completed the initial phase of matching information obtained through international exchange of information procedures with the SARS taxpayer database. This matching confirms that some accountholders may have used their accounts to evade South African tax liabilities.

Account holders who want to make use of the VDP programme are encouraged to submit their applications to the VDP unit on or before 12 August 2015. In the meantime SARS will continue analysing the data available to it, enhancing its audit capacity and will be ready to commence issuing audit notification letters from 13 August 2015.

4.2. *Table of interest rates*

In respect of the various acts administered by SARS interest rates charged on outstanding taxes, duties and levies and interest rates payable in respect of refunds of tax on successful appeals and certain delayed refunds :

Date from:	Date to:	Rate:
1 March 2011	30 April 2014	8,5%
1 May 2014	31 October 2014	9%
1 November 2014	Until change in PFMA rate	9,25%

Interest rates payable on credit amounts (overpayment of provisional tax) under section 89*quat*(4) of the Income Tax Act:

Date from:	Date to:	Rate:
1 March 2011	30 April 2014	4,5%
1 May 2014	31 October 2014	5%
1 November 2014	Until change in PFMA rate	5,25%

Where a loan is obtained by an employee from his or her employer in terms of which no interest is payable or where the interest payable is less than the 'official rate of interest', the difference between the amount which would have been payable if the loan was granted at the official rate and the amount actually paid by the employee, is taxed as a fringe benefit:

Date from:	Date to:	Rate:
1 March 2011	31 July 2012	6,5%
1 August 2012	31 January 2014	6%
1 February 2014	31 July 2014	6,5%
1 August 2014	31 July 2015	6,75%
1 August 2015	Until change in the Repo rate	7%

5. CASE LAW

5.1. Ackermans Ltd v C:SARS

Ackermans had sought relief in the North Gauteng High Court in the form of an order for the review and setting aside of a decision made by the SARS to raise the Additional Assessments to Ackermans' original assessments for the years 1998–2013.

SARS had raised the Additional Assessments on the basis, amongst others, of an allegation that Ackermans had misrepresented and failed to disclose material facts in regard to 'the true nature and substance of a series of agreements resulting in transactions that it had concluded with other entities', which, in SARS's view were simulated loans.

The issue for determination by the court was whether this decision by SARS stood to be reviewed and set aside in terms of the provisions of the Promotion of Administrative Justice Act 3 of 2000 ('PAJA') or declared unconstitutional, unlawful and invalid.

Ackermans had thus relied on the provisions of PAJA and, in the alternative, on the constitutional principle of legality.

Ackermans had, in 1997, found itself indebted to a certain company, Pepkorfin (Pty) Ltd, and through a series of inter-related agreements, including Loan Agreements, Sale of Shares Agreements and Promissory Notes, had executed transactions with various entities that led SARS to the view that there had been *inter alia* a 'simulated loan' agreement, interest deductions claimed by Ackermans on a 'simulated transaction' and an intention to disguise the true nature of the transactions between Ackermans and the other entities with the intention of the company to evade or reduce its liability for the payment of income tax.

SARS, on 15 October 2003, had requested information and documents from Ackermans relating to the aforementioned transactions and from that date up until 5 February 2005, an exchange of letters ensued between Ackermans and SARS in regard to the request and supply of the documents and information and Ackermans contended that it had supplied all the documents and information as requested, while SARS maintained that not all documents had been provided.

SARS, in February 2005, issued the first notification of its intention to raise Additional Assessments for the period 1998 to 2003 relating to the aforementioned transactions. This notice was followed by another notice on 6 July 2006 and from that date until 9 November 2011 there was no further communication between SARS and Ackermans on the question of Additional Assessments.

SARS, on 9 November 2011, issued a detailed Letter of Findings addressed to Ackermans resulting from its 2003 request for information and afforded Ackermans an opportunity to comment on the findings made by SARS and the revised assessments that SARS intended to raise in respect of Ackermans' 1998–2003 years of assessment.

The Letter of Findings raised the issues of a 'simulated loan' agreement, a series of transactions entered into to disguise the true nature of the transactions between the entities with the intention of evading or reducing liability for the payment of tax, disallowance of a portion of interest deductions claimed by Ackermans in respect of a 'simulated loan' and the imposition of additional tax in terms of s 76 of the Income Tax Act.

SARS, in the aforementioned Letter of Findings, contended that Ackermans had made misrepresentations in that tax returns rendered by Ackermans had contained incorrect statements and had been a misrepresentation of various transactions and it was on the basis of these misrepresentations that SARS had proceeded to raise the Additional Assessments for the years 1998 to 2003.

SARS, on 19 September 2012, issued the aforementioned Additional Assessments in terms of section 79 of the Income Tax Act and in terms of which Ackermans' taxable income for the years 1998–2003 was adjusted.

SARS contended that the amount of tax that was originally assessed for the 1998–2003 years of assessment was less than the amount of tax that was properly chargeable and it was satisfied that the fact that the amounts which should have been assessed to tax were not so assessed was due to the misrepresentation and/or non-disclosure of material facts.

SARS further contended that in the six-year period that had elapsed it had to wait for the judgment in a case before the Supreme Court of Appeal which had a bearing on the legal principles involved in the Additional Assessments and that case was *C: SARS* v *NWK*.

It was the aforementioned decision by SARS to raise the Additional Assessments on 19 September 2012 that was sought to be reviewed and set aside in this application.

Ackermans contended that SARS's decision stood to be reviewed and set aside on the following grounds under PAJA:

- SARS was precluded by the provisions of s 79(1) of the Income Tax Act from raising or deciding to raise the Additional Assessments;
- the raising of the Additional Assessments or the decision made after a very lengthy period of delay, was unreasonable and procedurally unfair; and

- SARS' decision was materially influenced by an error of law, took into account the relevant considerations and/or did not consider all relevant considerations, that the raising of the Additional Assessments or the decision was not rationally connected to the information before SARS, that SARS had failed to take a decision or that the raising of the Additional Assessments or the decision was so unreasonable that no reasonable person would have done so.

SARS contended *in limine* that the High Court did not have jurisdiction to decide this matter because the issues raised were complex matters requiring the expertise of the Tax Court. Moreover, it submitted that the Tax Court had powers of review for the relief sought by Ackermans alternatively that Ackermans had not exhausted its internal remedies before the Tax Court and therefore in terms of section 7 of PAJA its application for review should not be entertained and it further contended that there were disputes of fact which should be resolved by the Tax Court.

Both SARS and Ackermans had raised points *in limine* which, if upheld, would dispose of this application.

Judge Mothle held the following:

As to the points in limine

(i) That both SARS and Ackermans had raised points in limine which if upheld, would dispose of the present application, at least in its present form in this court.

(ii) That Ackermans' contention was that the delay in the decision to raise the additional assessments was so unreasonable as to justify the review and setting aside of the decision to raise them on the grounds of PAJA, alternatively non-compliance with the principle of constitutional legality. SARS, in turn, raised the questions of jurisdiction, failure to exhaust the internal remedies as well as disputes of fact as grounds for the application to be dismissed in its present form and the objection and appeal process to continue in the Tax Court.

As to the issue of jurisdiction

(iii) That the Tax Court is a creature of statute and as such its powers were limited to those specified in the relevant tax statutes such as the Income Tax Act, the Value-Added Tax Act and the Tax Administration Act.

(iv) That this review application under PAJA raised an issue concerning the protection of a fundamental right in terms of section 33 of the Constitution and section 169 of the Constitution empowered the High Court to decide on any constitutional matter and this included matters relating to the protection and enforcement of fundamental rights, unless that matter was assigned to a court of equal status to the High Court.

(iv) That on the strength of the authorities cited, the High Court has the jurisdiction to hear this review application and consequently the objection by SARS that the present court did not have jurisdiction to hear this application had no merit and had to fail.

As to the delay in raising the additional assessments

(v) That as regards Ackermans' submission that the delay in raising additional assessments can potentially prejudice a taxpayer, there was, however, no evidence submitted by Ackermans that the relevant documents *in casu* have since been lost or destroyed, or that memories of witnesses had faded. On the contrary, Ackermans' deponents to the founding affidavit and further affidavits did not demonstrate faded memories. Similarly, the bundles of documents attached to the application were clearly not lost or destroyed and, in fact, Ackermans insisted that all documents requested by SARS in regard to this matter had been submitted and hence any alleged prejudice on the part of Ackermans appeared perceived and not real.

(vi) That it is indeed imperative that all Constitutional obligations executed by organs of State in the exercise of public power, must be performed diligently and without delay. An unreasonable delay will result in a procedurally unfair administrative action, which is a reviewable conduct in terms of section 6 of PAJA. The decision to raise Additional

Assessments is an administrative action which is an exercise of public power and it fell within the ambit of section 237 of the Constitution.

(vii) That the courts frown upon unreasonable or inordinate delay in the exercise of public power and performance of public duties and it is thus generally accepted in these court decisions that such inordinate and unreasonable delays in the exercise of public power or performance of public functions, prolong the element of uncertainty on the part of all concerned and resulted in the interest of justice not being served.

(ix) That it was not disputed that there had been an approximately six-year delay from July 2006 up until 19 September 2012, for SARS to raise the Additional Assessments and the question was whether this delay was unreasonable.

(x) That section 273 of the Constitution, correctly so, did not state what period would constitute unreasonable delay in any given situation and this is left to the courts to determine, having regard to the circumstances of each case.

(xi) That the raising of Additional Assessments is an exercise of statutory authority in terms of section 79 of the Income Tax Act , which provides for time periods within which it will be permissible to raise the Additional Assessments and a determination of the reasonableness or otherwise of the delay requires a consideration of the provisions of section 79 of the Act.

(xii) That the essence of section 79(1) of the Income Tax Act was that any Additional Assessments had to be effected within three years from the date of the original assessment and SARS is not entitled to raise additional assessments after the three years of the original assessment, unless the circumstances stated in sub-par. (*aa*) or (*bb*) of subs 1(*c*)(i) to section 79 exists. In other words, SARS must have been satisfied, after the expiry of the three-year period from the date of the last assessment that the failure to assess an amount of tax was the result of fraud, misrepresentation or misstatement of material fact.

(xiii) That Ackermans contended that there had been no fraud, misrepresentation or non-disclosure of material facts as contemplated in section 79(1)(*c*)(i)(*aa*) in respect of any relevant year but SARS, on the other hand, contended that there were misrepresentations on the part of Ackermans, amongst others to the effect that a portion of the interest deductions claimed in the tax returns were represented to be in respect of interest payable in terms of the 'simulated loan' when in reality there were repayments of capital of the true loan.

(xiv) That there was clearly a dispute of fact on this part of the evidence, which is relevant in deciding whether, apart from other explanations, the delay in raising Additional Assessments fell or did not fall within the proviso in section 79(1)(*c*)(i)(*aa*). If it is concluded on the resolution of the disputed facts, that there was misrepresentation or non-disclosure of material facts on the part of Ackermans, the delay by SARS will be covered by the proviso in par. (*aa*) and will thus be reasonable. If, however, it is found that there were no misrepresentations and that there was a disclosure of the material facts, the delay from 2006 to 2012 when Additional Assessments were raised, would constitute an unreasonable delay in contravention of section 79(1)(*c*)(i) of the Act.

(xv) That, in essence, the oral evidence necessary to adjudicate the review application is the same evidence that would be required to adjudicate the merits of the challenge on the Additional Assessments and such adjudication will entail examination of the oral and documentary evidence relating to the allegations of misrepresentations and non-disclosure of material facts, within the context of the relevant agreements and transactions conducted by Ackermans and other entities.

(xvi) That while there appears to be very few authorities supporting the contention that a review application filed on papers should be referred to the hearing of oral evidence, there are nevertheless no rules which prohibit such. However, the disputed facts and issues raised in this application require the expertise of a tax court to adjudicate and therefore the adjudication of the disputed facts on the allegations of misrepresentations and non-disclosure of material facts, will bring this matter to finality.

(xvii) That it would therefore be appropriate to defer to the internal remedies in the Income Tax Act, to which Ackermans may resort by way of appeal to the Tax Court, should it not be satisfied with the decision on the objection and, consequently, in view of the conclusion reached by the court, there is no need for this court to consider other points of argument raised by both SARS and Ackermans in this application.

Application dismissed and each party to pay its own costs.

5.2. BT (PVT)LTD v Zimbabwe Revenue Authority

BT was a producer of gold bullion from its underground mining operations in Zimbabwe.

Respondent was the Zimbabwe Revenue Authority (ZRA), a corporate body created in terms of section 3 of the Revenue Authority Act [*Chapter 23:11*] charged with the responsibility of collecting revenue for the Republic of Zimbabwe.

BT came onto the local mining scene in 2006 and became one of the largest three producers of gold in the country.

BT, at various dates during the 2008 calendar year, had sold gold bullion to Fidelity Printers and Refiners (Pvt) Ltd, being a wholly owned subsidiary of the Reserve Bank of Zimbabwe (the central bank) and the law, contract and practice obliged the central bank to pay BT for all the gold bullion delivered to Fidelity.

BT's evidence detailed the two-tier system for payment of gold deliveries in existence before the onset of the multi-currency monetary regime in the country wherein one component of the payment was in local currency while the other was in United States dollars and payment in local currency was on delivery and through bank transfer on an implied exchange rate set unilaterally by the central bank.

Payment in foreign currency was slow and lethargic and was done through transfer into foreign currency denominated bank accounts of BT usually after a monetary policy statement. The foreign currency component was set against the price of gold on the London afternoon fix and the central bank always unilaterally fixed the gold support price from time to time in local currency.

BT was not paid the foreign currency component for all the deliveries it had made in 2008.

The central bank would without fail always analyse the gold sector in its bi-annual monetary policy statements and in one such statement in January 2009 the governor of the central bank unilaterally converted all outstanding amounts to the gold sector into 'Special Goldbacked Foreign Exchange Bonds' with a tenor of twelve months. The other terms attaching to the bonds were interest of 8% *per annum* on maturity applied in retrospect from the date each amount fell due, tradable to any interested counterparty locally, regionally and internationally at the agreed time-to-maturity discounts.

The central bank unequivocally undertook to honour the full principal plus interest on maturity to the holders of the bonds and BT saw the conversion for the first time in the monetary policy statement.

As at 31 January 2009, the central bank owed BT US$2 794 318,18 for bullion deliveries and the central bank sought written confirmation of the total debt inclusive of interest owing to BT in the sum of US$2 945 388,32, 'before the Reserve Bank issues you with one-year bonds for the amount due'.

The aforementioned gold bonds were duly issued in the preferred denominations and each was depicted as a Reserve Bank of Zimbabwe Gold Backed Tradable Bond. On the face of it was an issue and redemption date, the denomination, the tenor, annual interest, the promise to honour on presentation and the signatures of the governor and deputy governor. Each stated that 'the Reserve Bank of Zimbabwe promises to pay the bearer of this bond the sum of (amount in United States dollars) plus interest at the Reserve

Bank of Zimbabwe Harare on the (date) against presentation of this Bond' and each bond bore the date of issue of 1 February 2009 and due date of 1 February 2010.

BT duly investigated the marketability of the bonds on the local market as they were received with scepticism and were perceived to be high-risk paper susceptible to non-payment and the local market was highly illiquid and inactive.

BT took the decision that it was not in its best interest to trade the gold bonds at such huge discounts based on its status and responsibilities as a foreign listed company and there were no liquid and serious buyers and hence BT was happy to wait for the payment of the face value.

The central bank did not redeem the gold bonds on due date and it unilaterally rolled over the bonds, ostensibly for six months, but did not issue out replacement bonds. A monetary policy statement revealed that the debt owed to gold producers was actually a central government debt and that the rollover was necessitated by the need for the central bank and central government to agree on best initiatives to redeem the outstanding debts and, indeed, the gold bonds have never been redeemed and as at the date of the appeal were still outstanding.

BT averred that the capital debt denominated in United States dollars was brought to account as income in local currency in the financial statement ending 31 December 2008 and BT testified that the gold sales had been reflected as income even though payment had not yet been received. At the time, BT's accounts were required by law to be reflected in Zimbabwe dollars and not in United States dollars.

BT, in its financial statement for the year ended 31 December 2009, had made provision for a trade receivable of part of the outstanding money from the central bank in the sum of US$2 391 147 and the decision was predicated upon the failure by the central bank to redeem the debt over a period of up to two years and the likelihood of payment ever eventuating. Again, in its financial statements for the year ending 31 December 2010, BTwrote off the remaining portion in the sum of US$1 032 380 as bad debts because the amount was potentially uncollectable.

The reasons advanced for the aforementioned decision included the financial dire straits of the central bank, the gloomy outcome of discussions with the Treasury and failure by the central bank to honour the gold bonds to other gold miners despite lobbying through the Zimbabwe Chamber of Mines.

Furthermore, BT was impotent to enforce payment and it did not see value in pursuing litigation and, instead, it always presented the bonds for redemption on the due dates. In any event, BT took the practical view that any judgment obtained would be a *brutum fulmen* in the face of section 63B of the Reserve Bank Act [*Chapter 22:15*] which precluded the attachment and execution of the central bank's assets to satisfy such judgment.

BT adopted a purely accounting solution to the debt by making provision for the doubtful debt in terms of section 15(2)(*g*)(ii) of the Income Tax Act [*Chapter 23:06*], before it was repealed, for the year ending 31 December 2009, and writing-off the balance as a bad debt in terms of section 15(2)(*g*) of the same Act for the year ending 31 December 2010.

BT still held the bonds and, once honoured, would be added back to income and the necessary tax would be paid.

BT, in its income tax return for the year ending 31 December 2009, had claimed an allowance for doubtful debt in terms of section 15(2)(*g*)(ii) of the Act in the sum of US$2 391 147 due but not paid by the Reserve Bank of Zimbabwe and in its return for the period to 31 December 2010 had claimed a deduction for bad debt in the sum of US$3 423 527.

ZRA had disallowed the claims for doubtful debt for 2009 of US$2 391 147 and bad debt for 2010 of US$1 032 380.

BT noted its objection in full against the assessments and it was common cause that pending the determination of the appeal the BT paid to ZRA in four equal instalments the additional principal amount of the amended assessments of income tax together with interest thereon.

ZRA had treated the bonds in issue in the hands of Appellant as an investment and not debt and it contended, firstly, that the debt had been converted into an investment by the Special Tradable Gold-backed Foreign Exchange Bonds and, secondly, that the acceptance of the conversion constituted a full repayment of the debt and hence it determined that such payment precluded the ZRA from invoking the provisions of s 15(2)(*g*) of the Act.

BT contended that the central bank lacked the legal authority to issue bonds and that, in the absence of such power, the bonds issued by the central bank had no legal standing and were unlawful and void.

BT contended further that such invalid bonds could not and did not preclude it from claiming the debt as a doubtful debt in one year and the balance as a bad debt, in the subsequent year.

The issue for determination before the court was whether or not the debt due to Appellant by the central bank had been correctly claimed as a doubtful debt in the 2009 year of assessment and the balance as a bad debt in the 2010 year of assessment in terms of section 15(2)(*g*)(ii) and s 15(2)(*g*), respectively, of the Income Tax Act [*Chapter 23:06*].

Judge Kudya held the following:

(i) That the central bank lacked the legal authority to issue bonds and that in the absence of such power, the bonds issued by the central bank had no legal standing and were unlawful and void. The central bank was a creature of statute and it was trite that it could only exercise such power and authority as conferred by statute and it was impossible to find any provision in the Reserve Bank Act [*Chapter 22:15*] which would entitle it to meet its financial obligations by issuing bonds.

(ii) That the bonds issued in this matter by the central bank were little different from a bill of exchange or a promissory note or even a post-dated cheque to pay an outstanding debt and they fitted the mould of these financial instruments and while it appeared from the architectural design of the Act that any person is qualified to issue them, it seemed that the central bank was precluded from doing so by its own constitutive Act and it was common cause that BT was not a banking institution and hence the central bank was not empowered to issue bills, notes or other debt securities to BT.

(iii) That, accordingly, in the absence of statutory authority to issue bonds, the bonds *in casu* were not lawful tender and could not discharge a debt and they remained, at best, acknowledgements of debt and hence BT had demonstrated on a balance of probabilities that the bonds issued by the Reserve Bank of Zimbabwe were invalid for want of statutory authority and had no legal effect.

(iv) That the issue for determination was whether BT's claims for the deduction of both doubtful and bad debts in the two respective years were correctly made and whether such claims conformed to the requirements set out in section 15(2)(*g*)(ii) of the Act for doubtful debts and section 15(2)(*g*) for bad debts. Further, it had to be borne in mind that the provision for doubtful debts was no longer part of the law as it had been repealed by sectopm 14(*a*) of the Finance Act (No 3) (Act 10 of 2009) with effect from 1 January 2010 but it was, however, still operational in 2009 and therefore fell for consideration.

(iv) That the essential factors for proof on a balance of probability for a claim for both doubtful debts and bad debts were that:

(1) the amount claimed must be due and payable;

(2) the Commissioner is satisfied that the amount is unlikely to have been recovered at the end of the financial year;

(3) the amount must have been included in the taxable income of the taxpayer in the current or any previous year of assessment; and

(4) once the claim is allowed it will have to be added back to income in the following year of assessment.

(vi) That in regard to whether the amount claimed was due and payable, it was the uncontroverted evidence before the court that the law, contract and practice concerning the delivery of gold was that payment would be due immediately on delivery. The issue of the gold bonds was prescriptive and commanding rather than persuasive and compromising and when the bonds were issued they contained issue and due dates unilaterally set by the central bank and, stripped of all technicalities, the creation of the bonds merely constituted a unilateral rescheduling of the debt.

(viii) That BThad clearly established that the debt was due for payment on the delivery of the gold bullion to which it related in 2008 and BT had further established that it had been coerced by the monetary policy statement of January 2009 to consent to the rescheduling of the debt at the end of December 2009.

(ix) That the debt in issue was due and payable during the course of the 2009 tax year and hence ZRA's contention that BT did not expect and was therefore not entitled to payment until 1 February 2010 must fall away as it cannot stand in the face of the court's finding that the bonds were invalid. It must also fail on the ground that the permissible final date for inclusion of the doubtful debt into BT's financial statement was the date that the accounts were prepared: post the financial year-end.

(ix) That in regard to whether ZRA ought to have been satisfied that the central bank was in all probability unlikely to make payment of the amount claimed as a doubtful debt in the course of the 2009 tax year, in law, on appeal, ZRA's discretion is supplanted by that of the Special Court and the judge may substitute his discretion for that of ZRA.

(x) That the ordinary commercial and accounting practice was that financial statements were prepared after the close of the financial year and in this regard *COT* v *A Company* was binding on the court. The underlying assumption in those cases was that the bad debts remained due and payable. Likewise, in the present case, the uncertainty that existed in 2009 that the debt was unlikely to be paid was confirmed on 17 May 2010 to have been prescient. That uncertainty was predicated on the issuance of the invalid bonds with a maturity date of 1 February 2010, contrary to the 31 December 2009 date promised in the January monetary policy statement. The amount claimed had been outstanding for up to two years and the central bank had demonstrated its inability to pay and was in poor standing in the local market.

(xi) That, accordingly,BT had established on a balance of probabilities that there was a likelihood that the debt would not be paid by the central bank in the course of 2009.

(xii) That, in the court's view, any reasonable person submitting the return to the ZRA would have doubted the likelihood of the debt being paid even though he might recognise an outside and remote possibility that such payment might take place. There was no reasonable probability of payment occurring but this did not completely exclude that payment might happen – a likelihood of lack of collectability existed and it was a doubt as opposed to a certainty.

(xiii) That the last essential element for determination was whether the amount provided for was included in the gross income of BT for that tax year or any of the previous tax years. The sole witness for the BT had stated that the amount was included in the 2008 tax return in Zimbabwe dollars and the evidence of the sole witness in this matter was not controverted by any witness called by ZRA or by any of the documentary trail exchanged between the parties and filed of record and, accordingly, it was established from the oral evidence and the documents filed of record that the amount owed had been included in the 2008 tax return as taxable income.

(xiv) That, accordingly, BT had established on a balance of probabilities all the three elements necessary to qualify the claim for deduction as a provisional bad debt.

(xv) That the next issue to decide was whether the claim for the bad debt for 2010 should have been allowed and, for the reasons stated above under the provision for the 2009 bad debt, the court was satisfied that the amount claimed as a bad debt in 2010 had been rendered in the 2008 tax return.

(xvi) That in regard to whether the amount of the bad debt in 2010 was due and payable during that year, the answer is that it was. The purported gold bonds were null and void and they were of no force or effect and did not exist in law. They could not therefore constitute a payment for the debt and, even if they were valid, the court would have found them to be akin to mere rescheduled acknowledgments of debt and did not constitute payment of the debt, a debt does not become an investment merely because it also records terms of payment. The debt remained and still remained due and payable, writing it off as a bad debt did not extinguish it.

(xvii) That the last element for consideration was whether ZRA ought to have been satisfied that the claimed amount was bad. The Act did not define a bad debt but it is however defined in ordinary commercial and accounting practice as an amount that is unlikely to be paid. BT had established on a balance of probabilities that by 31 December 2010 the claimed amount had been outstanding for more than 26 months. The purported gold bonds had been issued and rolled over time without number and the swan song from the debtor was familiar: it was clear that it was unable to pay and had no funds to pay.

(xviii) That, accordingly, the requisite elements for a bad debt found in section 15(2)(*g*) of the Act were satisfied by BT and ZRA should have allowed them. In consequence, the interest and penalties imposed by ZRA could not stand and are set aside.

(xix) Appellant is entitled to an order of costs as contemplated by section 15(2)(*aa*) of the Income Tax Act.

Appeal upheld in respect of both claims.

5.3. *Director or Public Prosecutions, Western Cape v Parker*

Parker, being the sole representative of Step-in-Time Supermarket CC ('the CC'), and the CC, a registered VAT vendor, were both charged in the regional court, Bellville, Western Cape with a number of counts under the Income Tax Act and the VAT Act, respectively.

Apart from the aforementioned charges, they were charged with 16 counts of (common law) theft of money allegedly collected in respect of VAT.

The charges under the VAT Act related to the CC's failure to submit VAT returns under section 28(1)(*a*) of the VAT Act between the specified periods while the theft charges were based on the CC's failure to pay VAT over the same period.

Parker and the CC pleaded guilty to all the charges and were duly convicted after Parker had submitted a written plea in terms of section 112 of the Criminal Procedure Act ('the CPA') on behalf of both.

The magistrate, for purposes of sentence, had grouped the convictions and had sentenced Parker, *inter alia*, to five years' imprisonment in terms of section 276(1)(*i*) of the CPA in respect of the sixteen charges of common law theft.

The trial court had granted Parker leave to appeal against the sentence imposed in respect of the theft to the Western Cape High Court and prior to the scheduled hearing of the appeal both the State and Parker were requested by the court to prepare and argue the question whether Parker should have been charged with common law theft in view of the judgment in *AJC Olivier* v *Die Staat* (A153/2005, 22 September 2006, unreported).

Parker, in consequence thereof, had successfully applied to the regional court for leave to appeal against the convictions for theft and it was common cause that Parker, representing the CC, had not paid VAT to the South African Revenue Service (SARS).

The court *a quo* (*per* Dlodlo J and Van Staden AJ) held that Parker did not commit theft of the VAT, essentially on the basis that the money in question had belonged to the vendor and not to the SARS and the convictions for theft were consequently set aside together with the sentence in terms of s 276(1)(i) of the CPA.

The State then lodged an appeal and requested the Supreme Court of Appeal to decide the following legal question: Whether a VAT vendor who had misappropriated an amount of VAT which it had collected on behalf of SARS could be charged with the common law crime of theft.

The State submitted that the motivation for the question arose from the fact that a failure to pay VAT was a statutory crime under section 28(1)(*b*) read with section 58 of the VAT Act, which was punishable with a sentence of two years' imprisonment and the reason why it had approached the court was because the penalty and punishment prescribed by the Act were too lenient for certain cases of misappropriation of VAT and it followed that a conviction for theft would pave the way for sterner sanctions and that was what the prosecuting authority had sought.

The State submitted that the court *a quo* had erred by asking whether SARS became the owner of the money in question. In collecting VAT the VAT vendor acted as an agent for SARS and it followed that a VAT vendor who used VAT for purposes other than to pay to SARS misappropriated those funds and was therefore guilty of theft, despite the fact that the vendor may have been the owner of that money.

The State sought to rely on the proposition that where X holds money in trust on Y's behalf or receives money from Y with instructions that it be used for a specific purpose and X misappropriates that money by using it for a different purpose, X commits theft of the money and in these types of cases the rule that one cannot steal one's own money is no bar to a conviction.

The State put forward the proposition that the VAT vendor who collected VAT was in a position of trust *vis-à-vis* SARS with regard to that money.

Judge Pillay held the following:

(i) That section 7(1) of the VAT Act did not, either expressly or impliedly create a relationship of trust between the VAT vendor and SARS. On the contrary, it was clear that the relationship created by the Act was one of a debtor and his creditor and at the time Parker was charged, section 40 of the Act was still in operation and that section pertinently described VAT 'when it becomes due or is payable' as a 'debit to the State.' Consequently it was clear that the VAT Act provided for a debtor-creditor relationship as between the vendor and SARS.

(ii) That the procedures allow SARS to resort to litigation in order to recover tax debts and even institute sequestration, liquidation or winding-up proceedings, as the case may be. Therefore, should a vendor fail to pay any tax, penalty or interest, SARS is entitled to sue the vendor for payment and the vendor can also, simultaneously, be charged in terms of section 58 of the Act for failing to comply with it and, significantly, the offences referred to in section 58 were confined to non-compliance with the Act and did not include common law theft.

(iii) That the State's argument based on *Metcash Trading Ltd* v *C:SARS* was misconstrued and quoted out of context the comments made by Kriegler J and the learned judge certainly did not suggest that a trust relationship or one resembling that as between a trustee and a beneficiary of a trust, had been created. Moreover, the State misconceived the import of the *Metcash* decision in citing the judgment as authority for the proposition that VAT vendors are involuntary tax-collectors on behalf of SARS and were therefore in a position of trust and would commit theft if they appropriated such collected VAT for uses other than to submit it to SARS.

(iv) That all that the learned judge was conveying in *Metcash* was that VAT was payable on every sale and that details of the manner of calculation of VAT, the timetable for periodic payment and the amount to be paid were statutorily controlled and it was left for the vendor to ensure compliance therewith and this was quite different from imposing the status of a formal tax-collector or a trustee of SARS on a registered vendor.

(iv) That the State's reliance upon *Estate Agency Affairs Board* v *McLaggan* [2005] JOL 14050 (SCA) (2005 (4) SA 531 (SCA)) was also wrong as this case related to the cancellation of McLaggan's fidelity fund certificate and the element of dishonesty was of importance on appeal not to determine whether or not he was guilty of theft and the submission made by the State on the strength of this case that Parker's misappropriation of VAT was seen as dishonest and therefore it amounted to theft was clearly misplaced.

(v) That the concept of a trust relationship between the vendor and SARS which forms the bedrock of the State's argument is clearly unsustainable. It is clear that the Act is a scheme with its own directives, processes and penalties and the relationship that it creates between SARS and the registered vendor is *sui generis* – one with its own peculiar nature. The Act does not confer on the vendor the status of a trustee or an agent of SARS and, if it did, the vendor would either have to keep separate books of account or alternatively would have to be sufficiently liquid at any given time in order to cover the outstanding VAT but the Act makes no provision for this situation nor did it seek to compel a vendor to keep separate books of account in respect of VAT.

(vi) That to find that the Act created a trust relationship (in whatever form) would require an innovative approach as the Act, in particular section 58, did not incorporate theft as an offence and for the courts to extend the crime of theft to resolve the State's difficulties, would be contrary to the principle of *nullum crimen*, *nulla poena sine praevia lege poenali* (without a law, no charge is possible).

(vii) That, for the aforementioned reasons, the question of law as formulated by the State must therefore be answered in the negative and, in the event, the appeal against the judgment of the court *a quo* must fail.

Appeal dismissed with costs, including the costs occasioned by the employment of two counsel.

5.4. *Medox Ltd v C:SARS*

Medox had been provisionally wound-up in terms of an order of the High Court in 1995, but had continued trading and in 1996 the winding-up order was set aside by the High Court when it sanctioned a scheme of arrangement between Medox and its creditors in terms of section 311 of the Companies Act.

Medox had submitted a return to the SARS in respect of the income accrued to it during the 1996 tax year and SARS' assessment for this tax year had reflected an assessed loss of R46 622 063.

Medox did not submit a return to SARS for the 1997 tax year, but thereafter had submitted its income tax returns for the tax years 1998 up to and including 2010 but excluding 2003.

Medox, in respect of each of the returns submitted in the tax years subsequent to 1997, did not seek to carry forward the assessed loss incurred in the 1996 tax year and to set it off against profits earned during the subsequent tax years.

SARS duly issued income tax assessments to Medox in respect of those subsequent tax years without reflecting the assessed loss.

Medox had made no objection against the assessments issued by the Commissioner in respect of the 1998 and subsequent tax years but it alleged that during 2009 it had realised that it had not submitted a return in respect of the 1997 tax year and that the income tax assessments issued by SARS in respect of the 1998 and subsequent tax years had failed to set off the assessed loss of R46 622 063 incurred by it in the 1996 tax year.

Medox then took the view that the 1998 and subsequent income tax assessments were void as SARS had acted *ultra vires* by issuing same in disregard of the mandatory provisions of s 20(1)(*a*) of the Income Tax Act, requiring him to set off assessed losses of a taxpayer against income derived by the taxpayer in subsequent years.

SARS denied the aforementioned allegation and this resulted in Medox approaching the court *a quo*, being the Gauteng Division of the High Court (see *Medox Ltd v C: SARS* 76 SATC 369 *per* Teffo J) for declaratory relief in the form of an order declaring that all income tax assessments issued to it by SARS in respect of the years of assessment following its 1997 year of assessment were null and void.

SARS had opposed the application in the court *a quo* and Teffo J concluded that the High Court did not have jurisdiction to entertain the dispute and, accordingly, dismissed the application with costs.

The court *a quo*, in essence, held that the dispute should have been pursued by way of an objection to the assessments, lodged with the Commissioner and, if necessary, followed by an appeal to the Tax Court, as the appropriate forum to deal with matters of this kind,

Medox applied for and was granted leave to appeal to the Supreme Court of Appeal.

Section 81 of the Income Tax Act (Objection against assessment) provided, *inter alia*, at the relevant time:

'(1) Objections to any assessment made under this Act shall be made in the manner and under the terms and within the period prescribed by this Act and the rules promulgated in terms of s 107A by any taxpayer who is aggrieved by any assessment in which that taxpayer has an interest.

(5) Where no objections are made to any assessment or where objections have been allowed in full or withdrawn, such assessment or altered assessment, as the case may be, shall be final and conclusive.'

Section 83 provided at the relevant time that any person entitled to object to an assessment, may appeal against such assessment to the tax court established in terms of the provisions of sectopm 83 and the tax court may, in the case of an assessment appealed against, confirm the assessment or order that it be altered or referred back to the Commissioner for further investigation and assessment.

Judge Fourie held the following:

(i) That it is trite that an appeal is directed at the order of the court of first instance and not the reasons for the order as appeals do not lie against the reasons for judgment but against the substantive order of a lower court.

(ii) That, for the reasons given in the judgment, there was no merit in the Medox's application for a declaratory order and, in view of this conclusion, there was no need to enter into the debate as to whether or not the learned Judge in the court *a quo* had correctly held that the High Court did not have the necessary jurisdiction to entertain the application and it will be assumed that the court *a quo* did have the jurisdiction to adjudicate upon the application.

(iii) That, in order to obtain declaratory relief in the court below, Medox had to show that it had an existing, future or contingent right to have the assessments for the 1998 and subsequent tax years declared null and void.

(iv) That as it was common cause that Medox did not object in terms of section 81 of the Act to any of the assessments issued in respect of the 1998 and subsequent tax years, it will immediately be apparent that Medox's contention that it had a right to have these assessments declared null and void, flew in the face of the provisions of section 81(5) of the Act.

(iv) That the latter subsection expressly provided that, where no objection is made to an assessment, such assessment shall be final and conclusive and, in addition, it should be borne in mind that more than three years have lapsed from the date of each of these assessments, with the result that, by virtue of the provisions of section 81(2)(*b*) of the Act, SARS is precluded from re-opening the assessments.

(v) That this Court has over the years dealt with provisions worded similarly to section 81(5) of the Act and confirmed that, where no objection is made to an assessment issued by the relevant tax authority, the assessment is final and conclusive as between the tax authority and the taxpayer and these decisions have been collected in *CIR* v *Bowman NO*.

(vi) That Medox's argument that section 81(5) only applies to 'valid' assessments and not to 'invalid' assessments, gives considerable difficulty and this appeared to be a distinction without any difference.

(vii) That on Medox's aforementioned argument virtually any assessment in which SARS erroneously refuses to allow a deduction, rebate or exemption provided for in the Act, could be regarded as invalid and therefore not subject to the provisions of sections 81 to 83 of the Act and this would render the mechanisms provided for in sections 81 to 83 for objections to and appeals against assessments nugatory and grant aggrieved taxpayers *carte blanche* to approach the High Court in virtually every instance where they disagree with an assessment made by SARS.

(ix) That Medox's submission required the word 'assessment' in section 81 of the Act, and in particular in sections 81(2)(*b*) and 81(5), to be read as being a reference to a 'valid' assessment and there was no basis upon which it could be said that the reading in of the word 'valid' in section 81 was necessary to give effect to the section as it stood. On the contrary, such a construction would be in conflict with the intention of the legislature as appeared from the clear language of the subsections.

(x) That, finally, and in any event, the premise from which Medox departed in its quest to have these assessments set aside, was fatally flawed as it had contended that it was the duty of SARS to take the necessary steps to have the assessed loss of 1996 set off against profits earned by it during the subsequent tax years. As the court understood the provisions of the Act, it was the taxpayer who had to render a return in which any loss incurred in any previous year is carried forward to be set off against income derived by the taxpayer from carrying on any trade. That this was the taxpayer's duty was made clear in section 20(2A)(*b*) of the Act and section 82(*b*) of the Act placed the burden of proof upon the person claiming such set-off, *ie* the taxpayer.

(xi) That it followed that the application for declaratory relief was correctly dismissed by the court *a quo* and that the appeal, accordingly, fell to be dismissed.

(xii) That, in regard to costs, the circumstances set out in the judgment justified a departure from the general rule that a successful litigant should normally be entitled to its costs but the court believed that an appropriate sanction for the flagrant disregard of the rules of the court by the State Attorney would be to disallow SARS' costs of appeal.

Appeal dismissed.

No order is made as to costs.

5.5. South Atlantic Jazz Festival (Pty) Ltd v C:SARS

South Atlantic Jazz Festival (Pty) Ltd (South Atlantic) had staged annual international jazz festivals in Cape Town during the period in question and in the course of that enterprise it had concluded sponsorship agreements with South African Airways, the City of Cape Town, the South African Broadcasting Corporation and Telkom in terms of which the sponsors paid money towards and provided goods and services for the festivals, in return for which South Atlantic provided goods and services to the sponsors in the form of branding and marketing and South Atlantic and each of the sponsors were registered as ‘vendors’ in terms of the Value-Added Tax Act.

South Atlantic was liable to declare and pay output tax on the goods and services provided to the sponsors in terms of the aforementioned sponsorship agreements and its failure to have done so was identified in the course of a tax audit by the SARS which had resulted in the assessments in issue.

South Atlantic did not dispute its liability for output tax on the transactions but the matter in contestation was whether it should be entitled to offset that liability with a deduction in respect of the input tax in respect of the ‘supplies’ made to it by the sponsors but the SARS had declined to allow any deduction of input tax in the particular circumstances.

It was common ground between the parties that, despite their part cash components, the transactions in terms of the sponsorship agreements may be regarded essentially as barter transactions.

The sponsors had been required in terms of s 7(1)(*a*) of the Value-Added Tax Act to levy value-added tax on the supply by them of the goods and services concerned to the South Atlantic and in terms of s 20(1) of the Act the sponsors were obliged within 21 days of the supply of the goods or services concerned to issue the South Atlantic with a tax invoice in respect of the supply. The tax invoice was required to set out, amongst other things, either the value of the supply, the amount of tax charged and the consideration for the supply or where the amount of tax charged was calculated by applying the tax fraction to the consideration, the consideration for the supply and either the amount of the tax charged, or a statement that it included a charge in respect of the tax and the rate at which the tax was charged, and the South Atlantic would, subject to the applicable provisions of the Act, be entitled to deduct the tax thus levied on it by the sponsors from its liability to the SARS in respect of output tax.

It was common ground that, notwithstanding requests by South Atlantic that they should do so, the sponsors had not provided South Atlantic with tax invoices and no documents of the nature described in s 16(2)(*b*) of the Act had been issued.

It was also common ground that SARS was aware of the sponsors' failure to comply with their obligation to issue tax invoices, but, that notwithstanding his responsibility in terms of sectopm 4(1) of the Act 'to carry out' the provisions of the Act, he had taken no steps to procure compliance by the sponsors with their obligation, or to have them prosecuted for their failure to do so.

The court *a quo* (see *ITC 1871* (2013) 76 SATC 109 *per* Yekiso J) held that in the aforementioned circumstances South Atlantic could not make deductions in respect of the input tax and further held that the sponsors had in point of fact not charged VAT on the value of the goods and services supplied and that South Atlantic had not paid VAT to the sponsors in respect of the supply of such goods and services and hence the court *a quo* had dismissed Sout

Atlantic's appeal to that court brought in terms of section 33 of the Act against certain assessments made by SARS in respect of its liability to pay VAT in the relevant 2006 and 2007 periods of assessment and the appeal to the High Court was brought in terms of s 133(2)(*a*) read with s 270(2)(*d*) of the Tax Administration Act 28 of 2011.

The only question that the court *a quo* was called upon to decide was whether, in the context of the failure, despite demand, by the sponsors to have issued tax invoices, the provisions of either section 20(7)(*b*) or 16(2)(*f*) of the VAT Act should have been applied to allow Sout Atlantic the deductions in respect of input tax.

In terms of section 20(7)(*b*) of the Act SARS must be able to be satisfied as to two things before he may direct that a tax invoice is not required to be issued:

(i) the existence or availability of sufficient documentary records and

(ii) the impracticability of requiring a full tax invoice to be issued.

Sout Atlantic contended that the sponsorship contracts afforded 'sufficient records' of the supplies concerned and it would be 'impractical to require that a full tax invoice be issued.'

Section 16(2)(*f*) of the VAT Act provided that no deduction of input tax in respect of a supply of goods or services, the importation of any goods into the South Africa or any other deduction shall be made in terms of the Act unless the vendor, in any other case, is in possession of documentary proof, as is acceptable to SARS, substantiating the vendor's entitlement to the deduction at the time a return in respect of the deduction is furnished.

SARS advanced contentions to counter Sout Atlantic's reliance on section 16(2)(*f*) of the VAT Act on three base:

(i) the provision was not of application to deductions claimed in respect of input tax;

(ii) that 'although the documentation (ie the sponsorship contracts) refers to amounts, there was no evidence on record that the amounts referred to can in any way be equated to the value of the services rendered or the consideration paid therefor'; and

(iii) that Sout Atlantic's challenge to the assessment on the grounds that the respondent should have allowed the input tax deduction in terms of s 16(2)(*f*) came down to seeking to judicially review the SARS' decision not to accept the contract documents as proof of Sout Atlantic's entitlement to a deduction and it was submitted that the Tax Court had no jurisdiction to entertain review applications in terms of the Promotion of Administrative Justice Act 3 of 2000.

Judge Binns-Ward held the following:

(i) That, accepting as one may, that the transactions in issue were at arms' length, the value of the goods and services provided by the appellant to the sponsors in each case fell to be taken as the same as that of the counter performance by the relevant sponsor and SARS had been able to assess the sum of South Atlantic's liability for output tax on the basis of the information contained in the respective sponsorship contracts.

(ii) That in an ordinary arms' length barter transaction the value that the parties to it have attributed to the goods or supplies that are exchanged would, in the absence of any contrary indication, be a reliable indicator of their market value and it was thus plain that the value of the goods and services provided to South Atlantic by the sponsors was equally determinable from the sponsorship contracts.

(iii) That the approach of both the Tax Court and SARS that the sponsors had in point of fact not charged VAT on the value of the goods and services supplied overlooked that what required to be determined in respect of South Atlantic's claim to be entitled to a deduction for input tax was the 'open market value' of the supplies given by the sponsors in consideration for the services provided by South Atlantic. In the context of what was accepted by the parties to have been akin to a barter transaction, the value of the goods and services supplied by the sponsors fell for tax purposes to be determined in terms of section 10 of the VAT Act.

(iv) That section 10(3)(*b*) of the Act provided that for the purposes of the Act the amount of any consideration referred to in this section shall be, to the extent that such consideration is not a consideration in money, the open market value of that consideration.

(iv) That there has not been any dispute between the parties on the SARS' computation of the open market value of the goods and services in question and, on the contrary, the value of the non-cash benefits received by South Atlantic from each of the sponsors was common cause in the Tax Court and there was also no contention in the Tax Court that the sponsors had not supplied the goods and services stipulated in the sponsorship agreements.

(v) That notwithstanding any contractual arrangements that were in place, the sponsors did not account separately for the tax on the consideration given by South Atlantic and the tax levied by them was thus deemed to have been an amount equal to the tax fraction of the open market value of the goods and services supplied. By virtue of its counter-prestation in terms of the barter transaction, South Atlantic must be taken to have paid the tax and it should have been issued with the relevant tax invoices by the sponsors.

(vi) That, in the circumstances, the only question that the court *a quo* was called upon to decide was whether, in the context of the failure, despite demand, by the sponsors to have issued tax invoices, the provisions of either sections 20(7)(*b*) or 16(2)(*f*) of the Act should have been applied to allow the South Atlantic the deductions in respect of input tax.

(vii) That, having accepted South Atlantic's argument that the sponsorship contracts afforded 'sufficient records' of the supplies concerned, and there being no contention that the stipulated goods and services had not been supplied and no dispute that the contract documents record their open market value, but the court was unable to find that it would be 'impractical to require that a full tax invoice be issued'. No basis for any such finding is apparent on the record and the fact that the sponsors have failed to issue the invoices did not make it impractical to require that they be issued. On the contrary, it was the SARS' responsibility in the circumstances to compel their issue and the evidence provided no basis for the court to find that SARS could reasonably have been satisfied as to the requirement of impracticability.

(ix) That it was evident that SARS had predicated his calculation of the output tax on the information provided in the contracts and South Atlantic's contention was well – made that the contracts also served as proof of its entitlement to a deduction for input tax and if the documents were good enough for SARS to assess South Atlantic's output tax liability, it was impossible to conceive, having regard to the character of the particular transactions, why they should not also have been sufficient for the purpose of computing the input tax which should have been deemed to have been levied by the sponsors.

(x) That South Atlantic had invoked the provisions of section 16(2)(*f*) of the VAT Act in its representations to SARS and in the circumstances he was bound to take them into account in making the assessment. SARS could not reasonably have decided that the information in the contracts did not in the circumstances provide sufficient proof substantiating South Atlantic's entitlement to the deductions claimed. He had disallowed the deductions because South Atlantic was not in possession of relevant tax invoices which was also the only ground for disallowing the deductions expressly advanced by SARS in his Statement of Grounds of Assessment filed in terms of Rule 10 of the rules issued in terms of s 107A of the Income Tax Act and its replacement, section 103 of the Tax Administration Act and he did not explain why section 16(2)(*f*) should not have applied.

(xi) That in regard to the SARS' contention that there was no evidence on record that the amounts referred to in the sponsorship contracts could in any way be equated to the value of the services rendered or the consideration paid therefor, it was not open to SARS, in circumstances when the point was not clearly taken earlier, to contend for the first time at this stage that South Atlantic should have adduced evidence on the value of the consideration given for the goods and services provided by the sponsors. Moreover, not only was the point not taken, as described, but SARS had proceeded for his own purposes using the information in the documentation as sufficient for computing the output tax.

(xii) That as had recently been observed by Ponnan JA in *C: SARS v Pretoria East Motors (Pty) Ltd* 76 SATC 293 at par. [11], the raising of an additional assessment must be based on proper grounds for believing that, in the case of VAT, there has been an under – declaration of supplies and hence of output tax, or an unjustified deduction of input tax and it was only in this way that SARS could engage the taxpayer in an administratively fair manner, as it was obliged to do and provide grounds for raising the assessment to which the taxpayer must then respond by demonstrating that the assessment was wrong.

(xiii) That SARS' reliance on non-compliance with section 20(4) of the Act was wholly without merit – section 20(4) prescribed the particularity that must be set out in a tax invoice – but, as it was, the identity of the suppliers was evident from the contract documents and it was not in issue that they were registered vendors. They all happen to be organs of state and their addresses were well – known, or readily ascertainable and the quantity or volume of the goods and services supplied was also determined in terms of the contractual documentation. It was also not in contention that the sponsors were obliged to issue South Atlantic with tax invoices and that they had failed to do so despite request.

(xiv) That SARS also argued, in an effort to counter South Atlantic's reliance on section 16(2)(*f*), that South Atlantic's challenge to the assessment on the grounds that SARS should have allowed the input tax deduction in terms of section 16(2)(*f*), came down to seeking to judicially review SARS' decision not to accept the contract documents as proof of South

Atlantic's entitlement to an input tax deduction and he contended that his decision in that regard constituted 'administrative action' as defined in the Promotion of Administrative Justice Act (PAJA) and if it was to be impugned may be done only in terms of an application in terms of section 6 of that statute and not by appeal in terms of the Value-Added Tax Act and it was further submitted by SARS that the Tax Court had no jurisdiction to entertain review applications in terms of PAJA.

(xv) That in *KBI v Transvaalse Suikerkorporasie Bpk* the full court of the Transvaal Provincial Division held that save in respect of decisions in relation to which a right of appeal was expressly excluded by the tax legislation, the Tax Court was empowered to take into consideration whether or not SARS had properly exercised his discretion in respect of making assessments that were subject to appeal and, in that context, so the court held, where the exercise of discretion is pertinent to the making of the impugned assessment, the 'appeal' is in reality a 'review' of SARS' decision on customary review grounds. The full court's reasoning in the aforementioned case was compelling.

(xvi) That there had been no suggestion by SARS that the assessments in issue in the current case were not susceptible to appeal and SARS' decision not to allow a deduction in terms of section 16(2)(*f*) of the Act was integral to the making of the assessments. The matter was thus in all respects relevant for the jurisdictional argument directly analogous to that which presented in the *Transvaalse Suikerkorporasie* case. Indeed, SARS was unable to distinguish the matter in principle, save to say that the earlier cases were decided before the enactment of PAJA and in this regard he laid emphasis on the definition of 'court' in section 1 of PAJA and submitted that it did not include the Tax Court.

(xvii) That there was nothing in the aforegoing argument. PAJA regulated the bringing and determination of review applications in terms of section 6 of the statute and was not directed at the bringing and determination of appeals in terms of the tax laws administered under the Tax Administration Act. South Atlantic in the current matter was exercising a right of appeal to the Tax Court against the assessments and it was not seeking the review and setting aside of a decision in terms of section 16(2)(*f*) of the Act.

(xviii) That the fact that the determination of the appeal might entail the Tax Court in considering the legality of an administrative decision that was integral to the making of the assessment did not deprive the court of its jurisdiction to decide the appeal. To interpret and apply the legislation as requiring the dichotomous procedures enjoined in the argument advanced on behalf of SARS would in many cases defeat the very purpose of the establishment of the specialist Tax Court and the jurisdiction of the Tax Court to determine tax appeals is conferred without any limitation in section 117(1) of the Tax Administration Act. The court must be taken to have been invested with all the powers that are inherently necessary for it to fulfil its expressly provided functions.

(xx) That in the result the appeal had to succeed. The additional assessments had to be set aside and remitted for reconsideration by SARS in the light of this judgment.

Appeal upheld with costs.

5.6. ITC 1877

The taxpayer was a wholly owned operating subsidiary of a Johannesburg Stock Exchange listed company and had been in the business of conducting software research and development for twenty-seven years. It developed software programmes for its customers in freight forwarding, customs clearing agents and cargo transport companies to control the clearance of consignments of goods, both imported and exported into South Africa, from origin to the ultimate destination and SARS, i.e. its Customs Division, was one of the taxpayer's customers.

The programmes developed by the taxpayer were designed to meet the specific customer's particular needs and, for this reason, it licensed its software to the users of the software developed for the specific customer, billing the customer on a monthly basis for the software utilized in the particular month, by the particular customer.

The taxpayer’s software enabled its customers to comply with all the statutory requirements relating to the import and export of goods into South Africa as well as the requirements by the government agencies such as SARS' Customs Division, the Ports Authority and the Airports Company of South Africa and it also enabled its customer’s operating systems to interface with the SARS customs operating systems to verify data relating to the import and export of goods.

The nature of the taxpayer’s business was such that research and software development was an integral part of its activities and was a major source of its income earned by way of license fees calculated on the number of transactions the software utilizes and, to this end, all research and development processes commenced with a request from a customer. The taxpayer had to then determine whether the particular request could not be satisfied by its existing computer programmes and once the request was approved it was allocated a developer to perform the preliminary testing. The development programmer’s development, duly informed by the preliminary testing is then subject to further testing by the project manager before the new computer programme is released to the customer for use.

The taxpayer, in each year of tax assessment, submitted to the Minister of Science and Technology (‘the Minister’), in accordance with s 11D(11) of the Income Tax Act, all information required relating to the research and development undertaken and it was undisputed that in the 2010 year of assessment, the research and development was funded by the taxpayer in the course of its business operations, and it had incurred expenses in the sum of R19 968 378 and the income generated from the licence fees charged to clients amounted to R33 238 982.

The taxpayer had initially claimed the actual expenditure incurred in respect of research and development and which expenditure had been allowed as a deduction by SARS on assessment.

However, between the period September and December 2011, the taxpayer had requested that the assessment be re-opened and claimed additional expenditure for research and development in terms of section11D of the Act which allowed for the deduction of 150% of the amount qualifying thereunder. The relevant expenditure in issue that was claimed in respect of research and development of computer programmes amounted to R6 581 936 and the additional claim for deduction of 50% thereof, amounted to the sum of R3 290 968.

SARS had disallowed the additional 50% claimed for research and development on various grounds and it was that very disallowance that formed the subject-matter of this appeal.

SARS, in his grounds of assessment, had readily acknowledged that the taxpayer's activities for the 2010 year of assessment included software research and development and that it had incurred expenditure of R6 581 936 for developing and creation of a computer programme as defined in section 1 of the Copyright Act, but submitted that the 150% deduction for such expenditure had been disqualified by section 11D(5)(*b*) of the Inome Tax Act because the research and development expenditure incurred by the taxpayer for purposes of devising, developing or creating the computer programmes related to management or internal business processes and this was applicable regardless of whether the software is developed for use in-house or is developed for the purpose of sale to end-users.

Section 11D(5) provided at the relevant time:

'*Notwithstanding any other provision of this section, no deduction shall be allowed in terms of subsection (1) or (2) in respect of expenditure or costs relating to–*

(a) exploration or prospecting;

(b) *management or internal business processes;*

(c) *trade marks;*

(d) *the social sciences or humanities; or*

(e) *market research, sales or marketing promotion*.'

SARS further submitted that the taxpayer's research and development and the concomitant expenditure incurred by it was the development of software programmes with its key business enabling features allowing freight forwarders, customs clearing agents and cargo transportation companies to conduct their core business more effectively and hence the purpose of the programmes was to enhance a client's management of its assets and/or its internal business processes involving the optimal use of its resources.

For the aforementioned reason, contended SARS, the taxpayer's expenditure was not deductible in terms of section 11D(1) of the Income Tax Act but, whereas the taxpayer's expenditure did not qualify for the section 11D deduction of 150%, the taxpayer was entitled in terms of section 11(*a*) of the Act, to a deduction of the research and development expenditure actually incurred by it in the 2010 year of assessment and in order to determine whether a taxpayer was entitled to a general deduction, section 11(*a*) had to be read with section 23B(3) of the Income Tax Act which provided that '*no deduction shall be allowed under section 11(a) in respect of any expenditure or loss of a type for which a deduction or allowance may be granted under any other provisions of this Act . . .*'

The crisp issue between the parties was the interpretation of section 11D(1) read with section 11D(5) of the Income Tax Act in order to establish whether the expenditure incurred by the taxpayer as contemplated in section 11D(1)(*b*)(iii) of the Act was precluded by section 11D(5)(*b*) because it related to management or internal business processes.

The taxpayer contended that the management or internal business processes envisaged in section 11D(5)(*b*) were, in the context of this appeal, limited to the management or internal business processes of the taxpayer and excluded the users of the computer programmes for which the computer programmes were developed.

The taxpaeyr contended that when section 11D(5) was read with section 11D(1), it was clear that the restriction intended by the legislature in section 11D(5) related to expenditure incurred by taxpayers in the production of its income and hence the limitations set out in section 11D(5) related to expenditure incurred by taxpayers in the course of their own business operations and hence the words '*expenditure relating to management or internal business processes*' could only refer to the taxpayer's management or internal business processes.

Judge Ndita held the following:

<u>As to the effect of s 23B(3) of the Income Tax Act</u>

(i) That SARS' contention was correct that the effect of section 23B(3) of the Act was that, if a deduction or allowance may be granted under any other provision of the Act then no deduction may be allowed under section 11(*a*) as section 23B(3) prevents taxpayers from claiming a '*double deduction*' for the same expenditure and the section gives priority to any other provision of the Income Tax Act in terms of which a deduction or allowance may be granted. In other words, where section 11D is applicable, the taxpayer may claim only under section 11D, but if sectuib 11D is not applicable, a deduction can be claimed under section 11(*a*), if it applies. The effect of section 23B(3), therefore, is that 100% expenditure incurred by the taxpayer can be deducted in terms of section 11(*a*) but the additional deduction of 50% cannot be claimed under section 11D of the Act. Hence, either section 11D applies to justify a deduction of 150% of the expenditure in question or if section 11D does not apply at all, section 11(*a*) applies. However, the appeal would not be dismissed on this basis as it was clear from the nature of the taxpayer's claim, as well as argument, that the real issue was a claim lodged under the provisions of section 11D of the Act.

<u>As to the interpretation of s 11D of the Income Tax Act</u>

(ii) That the crucial question in this appeal was whether the expenditure incurred by the taxpayer as contemplated in section 11D(1)(*b*)(iii) was precluded by section 11D(5)(*b*) because it related to management or internal business processes and whether the words '*expenditure relating to management or internal business processes*' can only refer to the taxpayer's management or internal business processes as contended for by the taxpayer.

(iii) That the approach to statutory interpretation is stated in *Natal Joint Municipal Pension Fund* v *Endumeni Municipality* [2012] 2 All SA 262 (SCA) at 273 where, *inter alia*, it is stated that '*whatever the nature of the document, consideration must be given to the language used in the light of the ordinary rules of grammar and syntax; the context in which the provision appears; the apparent purpose for which it is directed and the material known to those responsible for its production . . . The process is objective, not subjective. A sensible meaning is to be preferred to one that leads to insensible or unbusinesslike results or undermines the apparent purpose of the documen*t'.

(iv) That on an examination of section 11D(5) of the Act in the context of its setting and surrounds and keeping in mind the purpose of section 11D(1), the clear intent of section 11D was to provide an incentive in respect of research and development in the field of science and technology and, when examining the ambit of the exclusion of '*management or internal business processes*' from eligibility for the incentive in the context of computer programme development, the phrase must '*take its colour, like a chameleon, from its settings and surrounds in the Act*'.

(iv) That it had to be accepted that the legislature sought to incentivise the development of innovative computer programmes, but not where these related *inter alia* to '*management or internal business processes*.' Moreover, the Income Tax Act contained no definition of the phrase ‘*expenditure relating to management and internal processes*’ and, that being the case, the words in the phrase must be given their ordinary meaning, unless such a meaning is contrary to the intention of the legislature and this approach is in line with the principles of statutory interpretation set out in *Public Carriers Association and others v Toll Road Concessionaries* (*Pty*) *Ltd and others* 1990 (1) SA 925 (A).

(v) That it followed that what was prohibited by section 11D(5) was expenditure ‘*which is connected with*’ the items listed in section 11D(5) as provided in par. (*a*) to (*e*). The taxpayer had strenuously argued that there was no ambiguity in the language used in section 11D(1), read with section 11D(5) and, according to the interpretation proffered by the taxpayer, it was the nature of the expenditure that was excluded in section 11D(5) and not the capacity of the software.

(vi) That if the aforementioned interpretation is correct, the relevant words must be read to mean ‘*expenditure relating to the management or internal business processes of the taxpayer*.’ But that is not what the words say. In the court’s view, a proper interpretation is to be found in the words ‘*expenditure . . . relating to*’ and this made sense because what was prohibited was the expenditure ‘*which is connected with*’ any of the items listed in par. (*a*) to (*e*) thereof and, on this score, the court agreed with submissions by SARS, the ‘*connectedness*’ arising from ‘*relation to*’ had to be determined with reference to the use for which the computer programme resulting in the expenditure incurred by the developer was developed and this was a sensible approach.

(vii) That, therefore, ‘*the expenditure . . . relating to management or internal business processes*’ can only refer to expenditure which is connected with management or internal business processes in the sense of the use for which the computer programme was developed and hence the interpretation contended for by the taxpayer was wrong for two reasons:

(1) The words '*of the taxpayer*' after '*management and internal business processes*' have been specifically excluded by the legislature and cannot be read into the prohibition and

(2) such an interpretation would render the prohibition so narrow that it would be nugatory and that could not have been intended by the legislature.

(ix) That, accordingly, the correct interpretation was that of SARS, i.e. to the effect that the internal business processes were not restricted to the taxpayer's internal business processes but applied to the nature of the computer programme.

(x) That whereas it is permissible to have recourse to foreign jurisprudence when interpreting a statutory provision, this should be done cautiously as foreign *dicta* may at times be at odds with an express purpose of the Act, the result of which would lead to an interpretation which is at war with the express words of the section. In the matter at hand, the intention of the legislature is discernible from the setting and surrounds in the Act and the court was fortified in this view by the *dictum* in *Western Platinum Ltd* v *C: SARS* where that court stated that in determining the extent of class privileges, one had to adopt a strict construction of the empowering legislation.

(xi) That, by parity of reasoning, it had to be accepted that section 11D created a class privilege for certain categories of research and development expenditure, by permitting the deduction of 150% thereof, whereas the norm was that only the actual amount of qualifying expenditure could be deducted and such an approach should be applied in a matter such as the present. Section 11D(5) places a curb on the class privilege available to such categories of research and development expenditure and section 11D(5) must be interpreted, as the court has done, in the manner set out by Conradie J in *CIR* v *D & N Promotions* (*Pty*) *Ltd* 57 SATC 178.

Appeal dismissed.

6. INTERPRETATION NOTES

6.1. Income Tax Exemption: Bodies corporate, share block companies and associations of persons managing the collective interest common to all members – No. 64 (Issue 3)

This Note provides guidance on the application and interpretation of section 10(1)(*e*) of the Income Tax Act.

Section 10(1)(*e*) exempts from income tax the levy income of a body corporate, a share block company and an association of persons. It also provides a basic exemption for these qualifying entities.

Levy income received by or accrued to qualifying entities is exempt from income tax.

Expenditure incurred by a qualifying entity in relation to the management of the collective interests of members and which is funded by the levies from the members is not allowable as a deduction in determining its taxable income because it is incurred in the production of exempt income. Consequently, such expenditure in excess of the levy income may not be set off against other income which is subject to income tax and must be disregarded in determining taxable income.

Receipts and accruals from a source other than levy income will be subject to income tax. Examples include:

- fees charged for the use of facilities and equipment such as squash courts, tennis courts, and washing machines;
- rental income from the letting of immovable property such as parking bays, servants' quarters and a demarcated area for a cell phone mast;
- investment income;

- amounts charged on unpaid levies or late payment of levies;
- income received for services rendered; and
- fines paid for not adhering to the management rules excluding building penalties.

Receipts and accruals derived from these sources (less the basic exemption), less allowable expenditure attributable to them, will constitute taxable income which is subject to tax.

The exemption for interest income under section 10(1)(*i*) does not apply to qualifying entities since the application of that section is limited to natural persons.

Expenditure relating directly to the receipts and accruals not qualifying for exemption will qualify for deduction in determining taxable income provided it meets the requirements for deductibility under the Act.

General expenditure incurred, such as bank charges and audit fees, will be allowable as a deduction to the extent that it meets the requirements for deductibility under the Act, for example, it is not of a capital nature.

The use of a fixed percentage of the general expenditure for the purpose of allocating it to a particular source of income is not acceptable. General expenditure must be allocated to the various sources of income on a logical, fair and reasonable basis. For example, depending on the facts, it may be acceptable to allocate the general expenses *pro rata* by applying the ratio that a particular source of receipts and accruals bears to the total receipts and accruals derived by the entity.

Since the basic exemption applies to receipts and accruals other than levies, the taxable portion of those receipts and accruals must be determined before calculating allowable deductions.

In conclusion:

- only the levy income of qualifying entities is fully exempt from income tax;

- the sum of other income received by qualifying entities is subject to a basic exemption;
- qualifying entities are excluded from the payment of provisional tax and are not required to submit provisional tax returns;
- bodies corporate and share block companies qualify for an automatic exemption from income tax and no pre-approval by the Commissioner is required; and
- associations of persons are required to apply for approval with the Commissioner at the TEU in order to qualify for exemption from income tax under section 10(1)(*e*)(i)(*cc*).

6.2. Skills Development Levy Exemption: Public Benefit Organisations – No. 10 (Issue 2)

This Note provides guidance on the interpretation and application of section 4(*c*) of the SDL Act, which exempts any PBO contemplated in section 10(1)(*c*N) from the payment of SDL, provided the PBO:

- solely carries on qualifying PBAs; or
- solely provides funds to PBOs that solely carry on qualifying PBAs.

The SDL Act imposes an SDL levy on the total 'remuneration' paid or payable by the employer to the employee during any month as determined in accordance with the Fourth Schedule.

Section 4 of the SDL Act contains a number of exemptions from the SDL levy. This Note, however, concentrates on the exemption under section 4(*c*) of the SDL Act.

SARS is responsible for the administration of the SDL Act, in so far as it relates to the collection of the levy payable by employers.

Section 4(*c*) of the Skills Development Levies Act provides:

4. Exemptions.—The levy is not payable by—

(*c*) any public benefit organisation contemplated in section 10(1)(*c*N) of the Income Tax Act, which—

(i) solely carries on any public benefit activity contemplated in paragraphs 1, 2(*a*), (*b*), (*c*) and (*d*) and 5 of Part I of the Ninth Schedule to that Act; or

(ii) solely provides funds to public benefit organisations contemplated in subparagraph (i);

A PBO may qualify for exemption from the payment of SDL under section 4(*c*) of the SDL Act, provided certain requirements are met.

6.3. Rules for the translation of amounts measured in foreign currencies by section 24I and the 8th Schedule – No. 63 (Issue 2)

This Note provides guidance on the application of the foreign currency translation rules contained in the Act, except for those in:

- section 24I; and
- the Eighth Schedule to the Act.

Residents are subject to normal tax on their worldwide taxable income, that is, taxable income derived from sources within and outside South Africa. A person that is not a resident is subject to normal tax only on taxable income derived from a source within South Africa.

In determining taxable income, foreign currency amounts must be translated to an equivalent amount in rand using either a spot rate or an average exchange rate. The Act generally prescribes which rate must be used depending upon the nature of the underlying transaction and the type of taxpayer involved.

This Note discusses the translation rules in sections 6*quat*(4) and (4A), 6*quin*(4), 9A, 9D(6), 25D, 35A(5), 47J, 49H, 50H, 51H and 64N. Depending on the circumstances, the determination of a person's normal tax liability may require the application of more than one of these provisions. For example, a natural person may use the spot rate to translate foreign currency amounts includable in taxable income for a year of assessment in accordance with section 25D(1). In addition, assuming some of the foreign currency amounts were from a foreign source and the natural person qualified for a foreign tax rebate on the foreign tax paid on that income, the natural person would apply the average exchange rate to translate the amount of foreign tax to rand under section 6*quat*.

In general, subject to the specific provisions governing foreign tax rebates, dividends tax rebates, blocked foreign funds, hyperinflationary currencies, exchange items and capital gains and losses:

- the spot rate must be used by:
  - any natural person and non-trading trust, unless that person or trust elects to use the average exchange rate in a year of assessment in accordance with section 25D(3);
  - any person to translate any foreign currency amount which has been deducted or withheld from amounts payable to a non-resident in accordance with section 35A (sales of immovable property), section 47J (amounts paid to entertainers or sportspersons), section 49H (royalties), section 50F (withholding tax on interest) or section 51F (withholding tax on services, effective in 2016);
  - any foreign PE, CFC, HQC, DTMC or ISC to translate amounts recognised by it in foreign currencies other than its functional currency to its functional currency;
  - any domestic PE; and
  - any foreign PE with a functional currency in a CMA currency to translate other foreign currencies to rand, unless the person is an individual or non-trading trust which has elected to use an average exchange rate; and

- the average exchange rate must be used by:
  - any natural person or non-trading trust that elects to use it in a year of assessment in accordance with section 25D(3); and
  - any foreign PE, CFC, HQC, DTMC or ISC to translate its taxable income in its functional currency to rand.

Depending on whether the person has or is a foreign PE, CFC, HQC, DTMC or ISC, amounts in rand must either be left as is or be translated to the foreign PE, CFC, HQC, DTMC or ISC's functional currency at spot before being translated back to rand at an average exchange rate.

7. DRAFT INTERPRETATION NOTES

7.1. Reduction of debt

This Note provides guidance on the interpretation and application of section 19 and paragraph 12A which deal with the reduction of debt.

Debt relief occurs in, for example, insolvency, business rescue, similar statutory proceedings or informal workouts, and can occur within and outside of a group of companies.

The reduction of debt during years of assessment commencing before 1 January 2013 was subject to the following income tax, CGT and donations tax provisions:

- Section 8(4)(*m*)
- Paragraph (ii) of the proviso to section 20(1)(*a*)
- Section 54
- Paragraph 2(*h*) of the Seventh Schedule
- Paragraph 3(*b*)(ii)
- Paragraph 12(5)

- Paragraph 20(3)(*b*)

The various taxes imposed upon persons receiving the benefit of debt relief may have effectively undermined the economic benefit of the relief. A new uniform system that provides relief to persons under financial distress in certain circumstances was introduced in the form of section 19 and paragraph 12A with effect from years of assessment commencing on or after 1 January 2013. Section 8(4)(*m*), paragraph (ii) of the proviso to section 20(1)(*a*) and paragraph 12(5) which previously dealt with the reduction of debt were simultaneously deleted. The new rules also provide clarity on the ordering of the various provisions and a more explicit set of demarcations between the different provisions.

The new rules are aimed at ensuring that a reduction of debt is not subject to more than one of the following taxes:

- estate duty
- donations tax
- income tax on a fringe benefit received by an employee
- income tax on income
- CGT

Sections 8(4)(*a*), 9C(5), 24J(4A)(*b*) and paragraphs 3(*b*)(ii), 20(3)(*b*)(iii) and 56(2)(*a*) have been amended with effect from years of assessment commencing on or after 1 January 2013 to prevent the recoupment of the same amount, or the reduction of the base cost of an asset, under more than one provision when a debt has been reduced or cancelled. In essence, these provisions ensure that the same reduction amount of a debt does not result in double taxation.

Section 19 and paragraph 12A contain ordering rules for dealing with debt relief and replace the previous rules that were contained in section 8(4)(*m*), the proviso to section 20(1)(*a*) and paragraph 12(5).

The new ordering rules apply to trading stock, other deductible expenditure, allowance assets and capital assets financed by debt which is subsequently reduced. Briefly the rules provide as follows upon a reduction of such debt:

- Trading stock held and not disposed of:

  Any section 11(a) deduction or the value of opening stock as well as any closing stock is reduced by the debt reduction. Any excess is treated as a recoupment for the purposes of section 8(4)(a).

- Trading stock not held and not disposed of at the time of the reduction of the debt and other deductible expenditure excluding allowance assets:

  The debt reduction is treated as a recoupment for the purposes of section 8(4)(a) to the extent that the expenditure was allowed as a deduction.

- Allowance assets:

  The debt reduction first reduces any base cost expenditure after which any excess is treated as a recoupment for the purposes of section 8(4)(a). Future capital allowances will be limited to the cost of the asset less the reduction amount and any previous allowances claimed on the asset.

- Capital assets that are not allowance assets:

  The base cost of the asset is reduced by the reduction amount of the debt. Any excess reduces any assessed capital loss.

A special rule applies to debt that financed the acquisition of a pre-valuation date asset. The effect of the rule is to treat the asset as a post-valuation date asset by re-establishing its base cost as expenditure which can be reduced by the reduction amount of the debt.

The ordering rules do not apply to tax debt or debt that has been reduced by donation, bequest or by an employer. Paragraph 12A contains additional exemptions for debt reduced within a group of companies and debt reduced in the course or in anticipation of liquidation, winding up, deregistration or final termination of a company when the debtor company and the creditor are connected persons in relation to each other.

Consequential amendments to prevent double taxation have been made to sections 8(4)(*a*), 9C(5), 24J(4A)(*b*) and paragraphs 3(*b*)(ii), 20(3)(*b*)(i) and (iii) and 56(2)(*a*).

Section 19, paragraph 12A and the consequential amendments referred to above apply to years of assessment commencing on or after 1 January 2013.

7.2. Public Benefit Organisations: The provision of funds, assets or other resources to associations of persons contemplated in public benefit activity 10(iii)

This Note provides guidance on:

- the provision of funds, assets or other resources to an association of persons;
- the monitoring requirement imposed under section 30(3)(*f*) on a PBO providing funds, assets or other resources to an association of persons contemplated in PBA 10(iii); and
- the interpretation of 'association of persons' contemplated in PBA 10(iii).

Before 2001 tax-exempt organisations were allowed to make funds available only to organisations providing residential accommodation to retired persons, religious, charitable and educational institutions of a public character that were formally constituted and exempt from income tax.

This restricted exemption resulted in many informal community projects not qualifying to benefit from such funding.

In order to address the exclusion of informal community projects from receiving funding, PBA 10(iii) was included in the Ninth Schedule. It provides that funds, assets or other resources may be provided to an association of persons carrying on one or more PBA contemplated in Part I in South Africa for the benefit of the general public.

Section 30(1) and PBA 10(iii) both refer to 'association of persons' which has resulted in uncertainty in the interpretation and application of the requirements that must be met by an association of persons contemplated in PBA 10(iii).

A PBO may provide funds, assets or other resources to any association of persons which carries on one or more PBAs in South Africa, even though such an association of persons is not approved as a PBO. The Commissioner must, however, be satisfied that the PBO has taken reasonable steps to ensure that the funds, assets or other resources are used by the association of persons to carry on one or more PBAs in South Africa.

8. BINDING PRIVATE RULINGS

8.1. BPR 195 – Securities transfer tax exemption where election has been made that section 42 of the Income Tax Act will not apply

This ruling deals with the exemption from securities transfer tax of a share transfer in terms of an asset-for-share transaction under which the parties have elected that the relief provided for under section 42 of the Act will not apply.

In this ruling references to sections and paragraphs are to sections of the relevant Acts and paragraphs of the Eighth Schedule to the Act applicable as at 21 April 2015 and unless the context indicates otherwise, any word or expression in this ruling bears the meaning ascribed to it in the relevant Act.

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

- the STT Act:
    - section 8(1)(*a*); and
- the Income Tax Act:

- section 1(1), definition of 'contributed tax capital' and 'permanent establishment';
- section 40CA;
- section 42; and
- paragraphs 2(1)(*b*) and 20(1)(*a*) of the Eighth Schedule.

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

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

The Co-Applicants: HoldCo, a foreign incorporated company, and non-resident of South Africa

Company A, a public company incorporated in and resident of South Africa

Company X, a private company incorporated in and a resident of South Africa

Company Y, a private company incorporated in and a resident of South Africa

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

HoldCo is a non-resident for South African tax purposes as it is neither incorporated nor effectively managed in South Africa. HoldCo holds 100% of the shares in the Applicant, 100% of the shares in Company X, and 90% of the shares in Company Y.

HoldCo holds 57% of the shares in Company A through its subsidiaries, Company X and Company Y, which each holds 30% of the shares in Company A. For regulatory reasons it is required of HoldCo to consolidate its shareholding in Company A by creating one 'significant owner' of Company A’s shares in the South African jurisdiction.

HoldCo therefore proposes to enter into an agreement with the Applicant in terms of which the Applicant is to acquire all of the shares held by HoldCo in Company X and Company Y (the Company X and Company Y shares), in exchange for the issue to HoldCo of new shares in the Applicant (the Applicant shares). The Applicant will become the controlling shareholder of Company A shares for regulatory purposes.

HoldCo and the Applicant will, in writing, agree that the provisions of section 42 will not apply.

Conditions and assumptions

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

Ruling

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

- Section 8(1)(*a*)(i) of the STT Act will be applicable to the transfer of the Company X and Company Y shares to the Applicant pursuant to the proposed transaction.
- The Company X and Company Y shares held by HoldCo will not fall within the ambit of paragraph 2(1)(*b*) of the Eighth Schedule
- The base cost of the Company X and Company Y shares to be acquired by the Applicant will equal the market value of the Applicant shares issued to HoldCo immediately after the proposed transaction.
- The market value of the Company X and Company Y shares to be acquired by the Applicant from HoldCo will constitute the amount of 'contributed tax capital' for the Applicant shares issued to HoldCo.

8.2. *BPR 196 – Employees' tax – Monthly pension benefits in respect of foreign service's rendered*

This ruling deals with whether or not a pension fund will be liable to deduct employees' tax from the monthly pension benefits payable to its retired members who are residents of South Africa in respect of services rendered outside South Africa (foreign services).

In this ruling references to sections and paragraphs are to sections of the Act and paragraphs of the Fourth Schedule thereto as at 19 May 2015 and 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 following provisions of the Income Tax Act:

- section 1(1), definition of 'income';
- section 9(2)(*i*);
- section 10(1)(*g*C)(ii);
- paragraph 1, definition of 'remuneration'; and
- paragraph 2(1).

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

The Applicant: A pension fund established, managed and administered in South Africa

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

The Applicant pays monthly pension benefits to its members after their retirement. Some of the retired members would have rendered services in South Africa, others in South Africa and in foreign countries and others exclusively in foreign countries, as a result of the secondment of employees from a South African employer to one of its associated foreign companies (foreign employer). The secondment terms determine that the foreign employer remunerates the seconded employees and pays their pension fund contributions directly to the Applicant.

The members would have returned to South Africa on retirement and would be residents of South Africa.

<u>Conditions and assumptions</u>

This ruling is subject to the following additional conditions and assumptions:

- The ruling applies to monthly pension benefits which will be received by or accrue to residents.

- The ruling does not apply to lump sums, death benefits or payments in respect of termination of service prior to date of retirement which will be received by or accrue to residents.

Ruling

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

- The Applicant will not be liable to deduct or withhold employees' tax under paragraph 2(1) from the monthly pension benefits which will be received by or accrue to residents in respect of foreign services.

8.3. BPR 197 – Exemption from donations tax and net value of an estate

This ruling deals with the donations tax consequences arising from the onward or subsequent donation of funds received by way of a donation from a foreign source (foreign sourced funds). In addition, it also deals with the estate duty consequences should any of the foreign sourced funds be retained or used to acquire 'property', as defined in section 3(2) of the Estate Duty Act, that is located and will remain outside South Africa.

In this ruling references to sections are to sections of the relevant Acts applicable as at 19 March 2015 and unless the context indicates otherwise, any word or expression in this ruling bears the meaning ascribed to it in the relevant Act.

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

- section 56(1)(*g*)(ii) of the Income Tax Act; and
- section 4(*e*)(ii) and (iii) of the Estate Duty Act.

Parties to the proposed transaction

The Applicant: An individual who is a resident of South Africa

Foreign Trust: A trust formed in a foreign country

Donees: Individual persons

Description of the proposed transaction

The Applicant is, and always has been, a 'resident', as defined in section 1(1) of the Act. The Applicant is one of a number of beneficiaries of the Foreign Trust. The funds held by this trust consist only of funds which have been sourced outside South Africa.

The Trustees have agreed to award a certain amount of the funds held by the Foreign Trust to the Applicant, following which the Applicant will be removed as a beneficiary. After the award has been transferred to the Applicant's offshore bank account, the Applicant intends to donate an amount therof to each of the Donees.

The Applicant will invest and retain the balance of the award offshore.

The Applicant intends to acquire property located outside South Africa, with the remaining portion of the award.

Conditions and assumptions

This ruling is subject to the additional condition and assumption that the property that the Applicant intends to acquire, will be located outside South Africa, and will remain outside South Africa.

Ruling

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

- The award by the Foreign Trust to the Applicant will not be subject to income tax in the hands of the Applicant.
- The donations made by the Applicant to the Donees will be exempt from donations tax under section 56(1)(*g*)(ii) of the Act.
- The remaining portion of the award received and/or the property acquired using the proceeds of the award from the Foreign Trust will be excluded from the net value of the Applicant's estate for Estate Duty purposes under section 4(*e*)(ii)(*aa*) or (iii) of the Estate Duty Act.

Additional Note

Whether or not this proposed transaction is connected with any arrangement implemented, or to be implemented for the avoidance of tax is outside the scope of this ruling.

8.4. BPR 198 – Distribution of a debit loan account in anticipation of deregistration of a company

This ruling deals with the distribution of a loan account, which is the only asset of the Co-Applicant, a wholly owned subsidiary of the Applicant. This distribution will comprise of a distribution of all of the Co-Applicant's accumulated profits and a return of its share capital to the Applicant in anticipation of the Co-Applicant's deregistration.

In this ruling references to sections are to sections of the Act applicable as at 16 May 2014 and 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 following provisions of the Income Tax Act:

- section 10(1)(*k*);
- section 47;
- sections 64D; and
- section 64FA(1)(*b*).

Parties to the proposed transaction

The Applicant: A company incorporated in and a resident of South Africa and the holding company of the Co-Applicant

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

Description of the proposed transaction

The Applicant proposes to deregister dormant companies in its group to simplify its group structure. The Co-Applicant is one such dormant company that has a loan account owing to it by the Applicant and the loan is the Co-Applicant's only asset, representing both its share capital and distributable reserves in its books of account. The Co-Applicant has no liabilities.

The Co-Applicant will distribute this loan account to the Applicant and then deregister.

Conditions and assumptions

This ruling is subject to the following additional conditions and assumptions:

- the Co-Applicant will, as required by section 47(6)*(c)*(i), within 36 months from the date of the liquidation distribution comply with the steps contemplated in section 41(4) to liquidate, wind up or deregister and will at no stage withdraw any steps to liquidate, wind up or deregister;

- the parties will not agree in writing to opt out of the provisions of section 47; and

- the Co-Applicant must notify the Applicant in writing what amount of the liquidation distribution constitutes a return of capital as contemplated in paragraph 76(4) of the Eighth Schedule to the Act.

Ruling

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

- The distribution of the loan account by the Co-Applicant to the Applicant will qualify as a 'liquidation distribution' as defined in section 47(1)(*a*). The disposal will accordingly fall within the ambit of section 47(2)(*a*). The distribution of the loan account by the Co-Applicant to the Applicant will be a dividend *in specie* to the extent that it is not a 'return of capital' as defined in section 1(1).

- The dividend amount will be exempt from dividends tax under section 64FA(1)(*b*).
- To the extent that the distribution of the loan account by the Co-Applicant to the Applicant is a 'return of capital' as defined in section 1(1), such return of capital must under section 47(5)(*b*) be disregarded in determining the Applicant's taxable income, assessed loss, aggregate capital gain or aggregate capital loss.
- The subsequent disposal by the Applicant of the equity shares held by it in the Co-Applicant as a result of the liquidation, winding up or deregistration of the Co-Applicant must under section 47(5)(*a*) be disregarded for the purposes of determining the Applicant's taxable income, assessed loss, aggregate capital gain or aggregate capital loss.
- The dividend received by the Applicant as a dividend *in specie* will be exempt from normal tax under section 10(1)(*k*)(i).

8.5. BPR 199 – Exemption from income tax of dividends received by virtue of restricted equity instruments

This ruling deals with whether the participation rights held by beneficiaries of an incentive trust are restricted equity instruments and, accordingly, whether the dividends they will receive by virtue of those rights are to be taxed as income or as dividends.

In this ruling references to sections are to sections of the Act applicable as at 20 February 2015, and 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 8C(*7*), definition of 'restricted equity instrument'; and
- section 10(1)(*k*)(i).

Parties to the proposed transaction

The Applicant: An incentive trust formed for directors of a private company and which is a resident of South Africa

Beneficiaries: Directors and certain employees of the private company, and otherwise eligible individuals (qualifying employees)

Description of the proposed transaction

The Applicant was formed to purchase shares in the company for the benefit of its Beneficiaries. The Applicant acquired, and currently holds, ordinary shares in that company.

The Applicant was established prior to 26 October 2004 and the first Beneficiaries accepted their entitlements under the trust deed prior to that date. Subsequently, more Beneficiaries were added under the provisions of the trust deed.

Beneficiaries hold their interests on a proportional basis. Those interests are represented by participation units.

A participation unit entitles the Beneficiary to, amongst others, a portion of the dividends received by the Applicant. It does not entitle the Beneficiary to receive any of the shares held by the Applicant.

The qualifying employees had to satisfy certain requirements in terms of criteria set out in the Trust Deed, to become Beneficiaries of the Applicant. The Initial Beneficiaries had to make cash contributions (nominal amount) to the Applicant to acquire participation rights to the income and capital of the Applicant.

The participation units are subject to the following restrictions:

- If a Beneficiary ceased to be a Beneficiary, the relevant Beneficiary will be deemed to have offered his or her participation units for sale to parties specified in the Trust Deed and the Offerees shall be entitled (but not obliged) to purchase the relevant Beneficiary's interest on the basis set out in the Trust Deed.

- The purchase price to be paid will be an amount equal to the fair market value, which will be agreed or determined in accordance with the Trust Deed. The parties will seek to agree on a fair market value, failing which, after 10 days, the fair market value will be determined with reference to the ultimate underlying investments in which the shares, held by the Applicant, are invested.
- None of the deemed offerrees is obliged to purchase a participation interest so offered.
- No Beneficiary may dispose of a participation interest without the permission of the board of directors of the company, who may not unreasonably withhold its permission.

The Applicant is anticipating receiving a dividend distribution. The dividend will further be distributed by the Applicant to all the Beneficiaries in proportion to their respective Trust Ratios.

<u>Conditions and assumptions</u>

This 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 participation rights held by the Beneficiaries are considered to be 'restricted equity instruments', as defined in section 8C(7).
- The dividends vested by the Applicant in the Beneficiaries are exempt from income tax in the hands of the Beneficiaries under section 10(1)(*k*)(i).

8.6. BPR 200 – Source of income of commission payable to non-resident junket agents

This ruling deals with the source of income of commission payable to non-resident junket agents by a resident casino operator.

In this ruling references to sections are to sections of the Act applicable as at 22 June 2015 and 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 following provisions of the Income Tax Act:

- section 1(1), definition of 'gross income';
- section 47A; and
- section 51A.

Parties to the proposed transaction

The Applicant: A company incorporated in and a resident of South Africa which is a casino operator

Junket Agents: Non-residents who promote junkets among non-residents

Description of the proposed transaction

The Applicant intends to engage with Junket Agents who are non-resident to arrange junkets in order to attract non-residents to conduct gaming activities at the Applicant's various casino operations in South Africa.

The Junket Agents are to identify and persuade wealthy gamblers (VIP patrons) in their jurisdiction and other countries outside South Africa to go on a junket at a casino of the Applicant and to conclude a Buy-in Agreement (agreement) with the Applicant in terms of which:

- the VIP patron must commit to wager a specified minimum amount that is paid to the Applicant as a deposit; and
- the VIP patron will receive food and accommodation at a discount for the period of his or her stay at the casino.

Junket Representatives in the employ of the Junket Agents will accompany the VIP patron on the junket to facilitate the financial transactions at the casino, accompany them to the casino floor, monitor the turnover on behalf of the Junket Agent and generally assist the VIP patron on the junket.

The Applicant will pay a commission to the Junket Agents for services rendered, based on the aggregate of the bets wagered by the VIP patron (turnover) or as a share of the Casino's profits from the gaming.

Conditions and assumptions

This binding private ruling is subject to the additional condition and assumption that the Junket Agents and the Junket Representatives are non-residents.

Ruling

The rulings made in connection with the proposed transaction are as follows:

- For purposes of the definition of 'gross income' in section 1(1), the commission earned by the Junket Agent will be partly sourced in South Africa.
- The commission payable to the Junket Agent will not be subject to withholding tax on foreign entertainers and sportspersons under section 47A or to withholding tax on service fees under section 51A.
- No ruling is made as to whether the activities of the Junket Agent and the Junket Representative will result in a permanent establishment having been created in South Africa.
- No ruling is made on whether or not the activities of the Junket Agent and the Junket Representative are carried on through a fixed base in South Africa.

8.7. BPR 201 – Issue of capitalization shares

This ruling deals with the issue of capitalisation shares by a company to its sole shareholder.

In this ruling references to sections and paragraphs are to sections of the Act and paragraphs of the Eighth Schedule thereto applicable as at 14 May 2015 and 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 following provisions of the Income Tax Act:

- section 1(1) – definition of 'gross income', paragraphs (*c*) and (*k*); 'contributed tax capital'; 'dividend' and 'return of capital';
- section 8C;
- section 40C;
- section 42(5) and (6); and
- paragraph 11 of the Eighth Schedule.

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

The Applicant: A natural person who is a resident of South Africa

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

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

BEE Co: A private company incorporated in and a resident of South Africa

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

The Applicant currently holds 100% of the equity shares in the Operating Company. In order for the Operating Company to achieve certain Black Economic Empowerment (BEE) credentials, it is imperative to introduce a minimum of 25.1% direct or indirect BEE shareholding in the Operating Company.

The Applicant proposes to interpose the Co-Applicant (currently dormant and 100% owned by the Operating Company) as the holding company into which the BEE Co will acquire shares which will allow the BEE Co to participate indirectly in the ownership and profits of the Operating Company. The BEE Co is 100% held by a BEE trust.

The following transactions will be implemented:

- **Step 1:** The Operating Company will dispose of its shares in the Co-Applicant to the Applicant for a nominal consideration.
- **Step 2:** The Applicant will dispose of his ordinary shares in the Operating Company to the Co-Applicant in exchange for ordinary shares in the Co- Applicant.
- **Step 3:** The Co-Applicant will issue 10 000 participating, cumulative, redeemable preference shares to the Applicant as capitalisation shares (the capitalisation shares) for no consideration.

  The key terms of the capitalisation shares will be as follows:

  - The capitalisation shares will be redeemable at the discretion of the Co-Applicant, at a price equal to 100% of the current equity value of the Operating Company (the redemption price).
  - The Co-Applicant will have no obligation to redeem the capitalisation shares, other than in the event of default triggered as a result of the Co-Applicant falling into financial distress.
  - The Applicant will be entitled to receive the following distributions:
    - cumulative profit distributions equal to the unredeemed balance of the redemption price (plus any arrear distributions) multiplied by 72% of the prime lending rate; and
    - 1% of all distributions made in respect of the ordinary shares.
- **Step 4:** The Co-Applicant will issue 25.1% ordinary shares to the BEE Co for a negligible subscription price.

<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 receipt of the capitalisation shares by the Applicant will not result in a 'disposal' of the ordinary shares held by the Applicant in the Operating Company, and consequently section 42(5) will not be triggered when the capitalisation shares are issued.
- Upon receipt of the capitalisation shares, section 42(6) will not be triggered as the Applicant will continue to hold a 'qualifying interest' as defined in section 42(1).
- The receipt of the capitalisation shares by the Applicant will not constitute 'gross income' in the hands of the Applicant.
- The receipt of the capitalisation shares by the Applicant will not constitute a specific inclusion under paragraph (*c*) of the definition of 'gross income' in the hands of the Applicant.
- The receipt of the capitalisation shares by the Applicant will not be subject to section 8C.
- The issue of the capitalisation shares will not qualify as a 'dividend' or a 'return of capital' as defined in section 1(1).

8.8. BPR 202 – Application of section 13quin subsequent to an intra-group transaction under section 45

This ruling deals with whether the transferee company will be entitled to claim the section 13*quin* allowance for the commercial buildings on the property that will be transferred to it by way of an intragroup transaction.

In this ruling references to sections are to sections of the Act applicable as at 10 June 2015 and 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 following provisions of the Income Tax Act:

- section 13*quin*, and
- section 45.

Parties to the proposed transaction

The Applicant: A private company incorporated in and a resident of South Africa. It is the holding company of Company A and Company B. Together they constitute 'the group'

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

Company B A private company incorporated in and a resident of South Africa

Description of the proposed transaction

Company A currently owns two properties. On one property two commercial buildings have been erected which house head office functions of the Applicant. The other property is a vacant stand.

Company A currently claims the section 13*quin* allowances on the two commercial buildings.

As part of a rationalisation process, the group proposes to transfer the two properties from Company A to Company B.

The transfer of the properties will constitute an 'intra-group transaction' as defined in section 45 and, therefore, qualify for the relief under that section.

Company A and Company B will not agree in writing that section 45 will not apply to the disposal of the properties, as contemplated in section 45(6)(*g*).

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:

- Company B will be deemed to be one and the same person as Company A for purposes of determining the allowance under section 13*quin*.

8.9. BPR 203 – Renunciation of a usufruct over shares

This ruling deals with whether securities transfer tax is payable on the renunciation of a usufruct over shares.

In this ruling references to sections are to sections of the STT Act applicable as at 21 May 2015 and unless the context indicates otherwise, any word or expression in this ruling bears the meaning ascribed to it in that Act.

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

- section 1, the definition of 'security' and 'transfer';
- section 2; and
- section 5.

Parties to the proposed transaction

The Applicant: A natural person who is a resident of South Africa

The Co-Applicants: Three separate trusts formed in and residents of South Africa

Description of the proposed transaction

The Applicant was married to N, who is deceased. The last will and testament of N bequeathed a share portfolio to the three children born of the marriage, with a life-long usufruct in favour of the Applicant.

The three children each transferred their bare dominium in the shares to three separate trusts (the Co-Applicants).

All the shares over which the Applicant has the usufruct are currently administered by a broker in one account in the name of the Applicant.

The Applicant intends to renounce the usufruct over the shares, so that full ownership of the shares of the children will vest in the respective Co-Applicants and that the shares must be transferred by the broker into accounts in the name of each of the Co-Applicants.

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:

- Securities transfer tax will not be payable by the Applicant on the renunciation of the usufruct over the shares.

8.10. BPR 204 – Definition of 'disposal' for purposes of asset-for-asset and amalgamation transactions; 'qualifying distribution' upon conversion to a corporate real estate investment trust

This ruling deals with:

- the conversion of a portfolio of a collective investment scheme in properties, currently listed as a Real Estate Investment Trust (REIT) on the JSE, to a corporate REIT. Prior to the conversion, immovable property will be transferred to a property company;
- whether the date of transfer of ownership in immovable property in the Deeds Office into the name of the property company impacts on the time of disposal of that immovable property for purposes of the asset-for-share transaction and the amalgamation transaction; and
- whether the declaration date of a distribution, as opposed to the date of payment, is the relevant time for determining if the distribution is a 'qualifying distribution' under section 25BB.

In this ruling references to sections and paragraphs are to sections of the Act and paragraphs of the Eighth Schedule thereto, applicable as at 23 June 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 following provisions of the Income Tax Act:

- section 1(1), definition of 'REIT';
- section 25BB;
- section 42;
- section 44;
- paragraph 1;
- paragraph 11(1)(*a*); and
- paragraph 13(1)(*a*).

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

The Applicant: A listed collective investment scheme in properties (CISP) with its financial year ending on 31 December

The First Co-Applicant: A private property company incorporated in South Africa, and a wholly-owned subsidiary of CISP (Property Company)

The Second Co-Applicant: A corporate REIT, a public company incorporated in South Afica, with its financial year ending on 31 December, which will be listed on the JSE as a REIT pursuant to the proposed transaction (Corporate REIT)

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

The proposed transaction is the effective conversion of the CISP to a corporate REIT in accordance with the procedure set out in Notice 42 of 2014 (Notice 42) issued by the Registrar of Collective Investment Schemes in terms of the Collective Investment Schemes Control Act No. 45 of 2002 (the CISC Act).

The CISP directly holds letting enterprises in relation to the immovable properties, which includes:

- immovable properties;
- the rights and obligations of the CISP as the lessor in terms of leases of the properties;
- assets which include cash on hand and certain contracts;
- liabilities which include all actual and contingent liabilities and obligations of the CISP relating to the properties and letting enterprises;
- goodwill; and
- shares in and loan accounts against wholly-owned subsidiaries, including the Property Company.

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

1) The CISP transfers the letting enterprises to the Property Company as going concerns by means of an asset-for-share transaction under section 42, in return for the issue of equity shares in the Property Company. A written asset-for-share agreement between the CISP and the Property Company was concluded and not subject to any suspensive conditions.

2) Two days prior to the effective date of the amalgamation transaction under section 44 (see 4 below), the subsidiaries will declare a distribution in relation to the first and second quarters of the current financial year to the CISP, as the beneficial shareholder of those subsidiaries.

3) One day before the effective date of the amalgamation transaction under section 44 (see 4 below), the CISP will declare a final profit distribution for the period 1 January 2015 to the date of the declaration, to be paid subsequently by the Corporate REIT to shareholders, once the audited financial statements of the CISP have been finalised.

4) The CISP will transfer all of its assets and liabilities, excluding bonds registered over the property which will remain in place until the date of transfer in the Deeds Office, to the Corporate REIT by means of an amalgamation transaction under section 44, in return for the issue of equity shares in the Corporate REIT. The assets include equity shares and loan accounts in the CISP's subsidiaries (including the shares and loan accounts in respect of the Property Company). The amalgamation agreement was concluded prior to the asset-for-share agreement, but contains a number of suspensive conditions, some of which were unfulfilled at the time of the conclusion of the asset-for-share agreement.

5) The CISP will declare a dividend *in specie* in respect of the equity shares in the Property Company, prior to it ceasing to be a REIT.

6) The existence of the CISP will be terminated once the equity shares in the Corporate REIT have been distributed on behalf of the CISP and the process has been completed to wind up the CISP pursuant to the requirements of the Registrar of Collective Investment Schemes, under the CISC Act.

7) The Corporate REIT is scheduled to be listed on the JSE as a REIT shortly after the effective date of the amalgamation transaction.

8) The units of the CISP will be suspended and delisted at the commencement of trade on the same day on which the Corporate REIT is listed.

It follows that the time and date on which the CISP will cease to be a REIT for income tax purposes is the commencement of trade on the listing date of the Corporate REIT. Therefore, the CISP's year of assessment will be deemed to end on that date, under section 25BB(7). There will, however, be no income derived by the CISP from the effective date of the amalgamation transaction to the deemed end date of its year of assessment.

<u>Conditions and assumptions</u>

This binding private ruling is subject to the following additional conditions and assumptions:

- The Corporate REIT complies with the JSE Listing Requirements for REITs.
- The CISP holds the immovable property and the shares in the wholly-owned subsidiaries on capital account.
- The amalgamation agreement becomes unconditional prior to the listing date of the Corporate REIT and the suspension of the CISP's units from the JSE.
- The CISP does not derive any imputed income from any controlled foreign company under section 9D.
- At least 75% of the gross income received by or accrued to the CISP or a 'subsidiary' (as defined in the International Financial Reporting Standards) of the CISP as a REIT, in the previous year of assessment, consisted of 'rental income', as defined in section 25BB(1).
- The amount of the CISP's final distribution as a REIT will be determined with reference to the financial results of the CISP, as reflected in the financial statements prepared for the year of assessment commencing on 1 January 2015 and deemed to end on the date on which the CISP ceases to be a REIT for income tax purposes.

<u>Ruling</u>

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

- In respect of the asset-for-share transaction under section 42, paragraph 13 of the Eighth Schedule will apply to the disposal of the immovable properties to the Property Company. The disposal of the immovable properties will be deemed to have occurred for income tax purposes on the date that the asset-for-share agreement is concluded.

- Irrespective of whether the transfer of ownership of the immovable properties has been registered in the name of the Property Company in the Deeds Office:
    - the Property Company will be entitled to issue the agreed number of equity shares to the CISP in exchange for the disposal of the letting enterprises as going concerns for income tax purposes to the Property Company, as the immovable properties would have been disposed of for income tax purposes;
    - the CISP will be regarded as having disposed of all of its assets for purposes of the amalgamation transaction under section 44, which would exclude such properties as already have been disposed of in terms of the asset-for-share transaction for income tax purposes; and
    - the Corporate REIT will be entitled to issue the agreed number of equity shares to the CISP as consideration for the disposal of the CISP's assets, in terms of the amalgamation transaction, for income tax purposes.
- For income tax purposes, at the time that the CISP ceases to be a REIT, the CISP will have disposed of all of its assets. Those assets include:
    - the immovable properties which have been disposed of to the Property Company in terms of the asset-for-share transaction (irrespective of the fact that the transfer of ownership of these properties may not yet have been registered in the Deeds Office);
    - the equity shares in and loans to the subsidiaries which have been disposed of to the Corporate REIT; and
    - the equity shares in the Corporate REIT which have been disposed of to the unit holders.

It follows that no capital gains tax consequences will arise for the CISP pursuant to section 25BB(7).

- On the basis that the CISP declares the final profit distribution prior to its ceasing to be a REIT, the CISP will be able to deduct the distribution from its income for that year of assessment to the extent that all the requirements of the definition of 'qualifying distribution', in section 25BB(1), are met, even though payment in respect of the distribution will be made by the Corporate REIT in consequence of the proposed assignment of the liability to pay the distribution as part of the conversion to a corporate REIT under Notice 42.
- The settlement of the assumed liability under the CISP's final profit distribution to shareholders by the Corporate REIT is not a 'qualifying distribution', as defined in section 25BB(1), for the Corporate REIT and is, therefore, not deductible by the Corporate REIT under section 25BB(2)(*a*).
- Subsequent to its listing on the JSE, the Corporate REIT will qualify as a REIT for purposes of the Act. To the extent that the Corporate REIT then distributes an amount that is a 'qualifying distribution' as defined in section 25BB(1), that amount will be deductible under section 25BB(2)(*a*).

8.11. BPR 205 – Meaning of 'controlled group company' and 'equity share'

This ruling determines the meaning of 'equity share' and 'controlled group company' with reference to a company that proposes to issue different classes of ordinary shares. It further determines the meaning of 'investment income', as defined in section 12E(4)(*c*).

This is a binding private ruling issued in accordance with section 78(1) and published in accordance with section 87(2) of the Tax Administration Act No. 28 of 2011.

In this ruling references to sections are to sections of the Act applicable as at 22 June 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 'controlled group company' and 'equity share';
- section 12E(4)(*c*); and
- section 12J.

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

The Applicant: A private company incorporated in and a resident of South Africa which is an approved 'venture capital company' as defined in section 12J(1) and licensed in terms of section 7 of the Financial Advisory and Intermediary Services Act No. 37 of 2002

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

Investor B: A company incorporated in and a resident of South Africa

RentalCo: A private company to be incorporated in and which will be a resident of South Africa and will be a 'qualifying company' as defined in section 12J pursuant to the proposed transaction (the leasing company)

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

Company A's main business is the marketing and sale of certain goods that are movable property. It wishes to expand its business by leasing some of the same goods under operating leases as defined by International Financial Reporting Standards.

Material terms of the proposed transaction are as follows:

- The Applicant, Investor B and Company A propose to incorporate RentalCo which will lease product A to Company A's clients on a medium term basis under operating leases.

- The Applicant will subscribe for 20% of the issued shares (Class A ordinary shares) at a subscription price equalling 75% of the entire issued share capital. Company A and Investor B will subscribe for Class B and C ordinary shares respectively.

- All the ordinary shares will carry the same votes.

- As the Applicant has contributed a disproportionate amount of share capital, the Class A ordinary shares will be entitled to a first distribution of profits or capital equal to the capital invested and a return to the equivalent of prime plus 2%.

- Upon settlement of the Class A ordinary shares, the Class B and Class C ordinary shares subscribed for by the Company A and Investor B respectively will be entitled to a second distribution of profits or capital equal to a return to the equivalent of prime plus 2%, paid in proportion to their respective shareholding.

- Thereafter, the Class A, B and C ordinary shares will rank *pari passu* in all respects.

The Applicant also proposes to enter into similar transactions with companies which are suppliers of goods that are movable assets, establishing a leasing company that will be a qualifying company in collaboration with the supplier. The actual shareholding proportions in the leasing company will be negotiated, but the Applicant will always hold less than 70% of the shares in issue, given that a qualifying company may not be a controlled group company in relation to the Applicant. The supplier will pay the subscription price in cash and / or by the transfer of its trading stock, to be leased out under operating leases by the leasing company, while the Applicant will subscribe for cash only.

<u>Conditions and assumptions</u>

This binding private ruling is subject to the additional condition and assumption that all the investments to be made by the Applicant must substantially be in the form as described above.

Ruling

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

- For purposes of the definition of 'qualifying share' in section 12J(1), the Class A shares to be held by the Applicant in RentalCo will constitute 'equity shares', as defined in section 1(1).

- For purposes of the definition of 'qualifying company', as defined in section 12J(1), the qualifying company (such as RentalCo) into which the Applicant invests will not constitute a 'controlled group company' for so long as the number of equity shares held by the Applicant constitutes less than 70% of the total number of equity shares in issue, notwithstanding that the Applicant invests more than 70% of the aggregate share capital.

- The receipt of rental income under operating leases in respect of movable assets by the qualifying company into which the Applicant invests, will not constitute 'investment income', as defined in section 12E(4)(*c*).

No consideration has been given to whether RentalCo will be carrying on an 'impermissible trade', as defined in section 12J(1).

8.12. BPR 206 – Disposal by a share block company of its sectional title units to its share block holders

This ruling determines the tax consequences of a disposal by a share block company of its sectional title units to its share block holders in exchange for the surrender of their share block certificates and their rights of use of the units.

In this ruling references to sections and paragraphs are to sections of the relevant Act and paragraphs of the Eighth Schedule to the Income Tax Act, applicable as at 3 July 2015. Unless the context indicates otherwise, any word or expression in this ruling bears the meaning ascribed to it in the relevant Act.

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

- section 64FA of the Act;
- paragraph 67B of the Eighth Schedule;
- sections 8(19) and 10(27) of the VAT Act; and
- section 9(19) of the Transfer Duty Act.

Parties to the proposed transaction

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

The Trust: A trust formed in and a resident of South Africa

The Share Block Company: A share block company, incorporated in and a resident of South Africa

Description of the proposed transaction

The Share Block Company owns three sectional title units (the units). The share block holders (the Applicant and the Trust) each hold an undivided share in all of those units.

The Share Block Company intends to dispose of all the units to the Applicant and the Trust. In return, the Applicant and the Trust will surrender to the Share Block Company their share block certificates and their rights of use of the units, which will be cancelled. The shares in the Share Block Company will thus be replaced by direct holding of the units in the sectional title scheme as joint owners.

Conditions and assumptions

This binding private ruling is made subject to the additional condition and assumption that the Applicant and the Trust currently hold their shares in the Share Block Company as capital assets.

<u>Ruling</u>

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

- Paragraph 67B of the Eighth Schedule will be applicable to the disposal of the sectional title units by the Share Block Company to the Applicant and the Trust, as the shareholders in the Share Block Company, in exchange for the surrender of their share block certificates and their rights of use of the units held by them, and consequently:
  - the Share Block Company must disregard any capital gain or capital loss in respect of that disposal; and
  - the disposal will be exempt from dividends tax under section 64FA(1)(*d*) of the Act.
- The supply of the units by the Share Block Company to its shareholders will be deemed to have been made in the course or furtherance of an enterprise under section 8(19) of the VAT Act and, therefore, the value of the supply will be nil as provided for under section 10(27) of the VAT Act.
- No transfer duty will be payable by the shareholders of the Share Block Company on the transfer of the units to them as provided for under section 9(19) of the Transfer Duty Act.

9. BINDING GENERAL RULING

9.1. BGR 29 – Unbundling transactions: Meaning of 'as at the end of the day after that distribution'

This BGR addresses the interpretation of the words 'at the end of the day after that distribution' as used in section 46(3)(*a*)(v) in relation to an unbundling company listed on the JSE. It does not address consecutive unbundling transactions occurring on the same day or the determination of the market value of shares in an unlisted unbundled company.

Section 46 provides parties to an unbundling transaction with relief from various taxes that would otherwise become payable.

A shareholder who acquires unbundled shares through an unbundling transaction must allocate a portion of the expenditure and any market value on valuation date attributable to the unbundling shares to the unbundled shares under section 46(3)(*a*)(i)(*aa*).

In making this allocation, section 46(3)(*a*)(v) requires that the shareholder must use the ratio that the market value of the unbundled shares, *'as at the end of the day after that distribution'*, bears to the sum of the market values, as at the end of that day, of the unbundling shares and the unbundled shares.

Application of the law

The JSE Equities Rules are binding on members of the JSE, their clients and agents. Under these rules shares in an unbundling company trade inclusive of the right to the unbundled shares up to and including LDT and begin trading exclusive of that right on the first business day after LDT.

Shares in a listed unbundled company begin trading independently of the shares in the unbundling company on LDT + 1. A holder of unbundling company shares on LDT takes delivery of the unbundled company shares only on record date + 1, that is, LDT + 6. Such a holder is nevertheless able to trade in the unbundled company shares from the commencement of LDT + 1 by contractual arrangement, with settlement being made on a rolling 'T + 5' basis. In other words, the seller is obliged to deliver the shares to the buyer on the fifth business day following the day on which the shares were disposed of.

The prices of the unbundling and unbundled company shares tend to fluctuate during the initial period of trading on LDT + 1 owing, amongst other things, to the number of sellers entering the market but should settle by the close of business on that day.

In order to achieve a fair allocation between the unbundling and unbundled shares, the market values as at the end of the first business day after LDT must be used when applying the ratio as specified in section 46(3)(*a*)(v).

Thus if LDT falls on a Friday, the first business day after LDT will fall on the Monday of the next week and the closing prices on the Monday must be used (assuming the Friday and Monday are both business days).

The same listed prices should be used in performing the allocation for certificated listed shares since such shares can be traded on the JSE only after they have been dematerialised.

Ruling

For the purposes of section 46(3)(*a*)(v) and with reference to the market values of the unbundling and unbundled company shares, 'as at the end of the day after that distribution' means in relation to shares unbundled under section 46 of the Act by an unbundling company listed on the JSE:

- the closing price of the unbundling company shares on LDT +1; and
- the closing price of a listed unbundled company's shares on LDT + 1.

10. BINDING CLASS RULINGS

10.1. BCR 47 – Limitation of dividend exemption

This ruling deals with the limitation of the exemption from income tax of dividends accruing to the issuer of a derivative, in circumstances where those dividends are referenced in that derivative.

In this ruling references to sections are to sections of the Act, applicable as at 30 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 10(1)(*k*)(i)(*hh*).

Class

The class members to whom this ruling will apply will be the members of a trade association of South Africa.

Parties to the proposed transaction

The Applicant: A Class member who applied on its own behalf and on behalf of the remaining members of a trade association

Description of the proposed transaction

A Class member physically holds (and beneficially owns) equity instruments, like listed shares, on which dividends are declared. The Class member will receive an interim dividend in respect of these listed shares at the end of the first quarter of its financial year.

The Class member will issue a derivative, for example an exchange traded note, at the end of the second quarter of its financial year. In terms of the derivative contract, the Class member has a contractual obligation to pay the holder a return, linked to the performance of the listed shares that the Class member beneficially owns and dividends declared on those shares for a specified period that commences on the issue date. This contract is referred to as 'a derivative' in this document.

At the end of the third quarter of the Class member's financial year (therefore within the same year of assessment), the Class member will incur a deductible expense or will have a reduction in income by virtue of an amount which is taken into account under section 24JB(2), for the derivative in respect of the final dividend declaration by a listed company. For accounting purposes, the Class member will mark to market the listed shares and the derivative under the provisions of International Financial Reporting Standards issued by the International Accounting Standards Board.

In the context of the proposed transaction, the question for consideration is whether the reduction of income or the deduction of the expenditure in respect of the final dividend to be received by the Class member will negate the exempt nature of the interim dividend that accrues to the Class member.

Conditions and assumptions

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

Ruling

The question whether an interim dividend that accrues on a share prior to the issue of a derivative that references that share and subsequent dividends is taxable, depends on whether deductible expenditure, or an amount that has the effect of reducing income in the application of section 24JB(2), is determined directly or indirectly with reference to the dividend.

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

- The income tax exemption of the interim dividend declared by a listed company, and which is not referenced in the derivative, will not be limited by virtue of section 10(1)(*k*)(i)(*hh*). However, the final dividend, which is referenced in the derivative, will be taxable up to the amount of any deductible expenditure incurred or any amount taken into account that has the effect of reducing income in the application of section 24JB(2), as referred to in section 10(1)(*k*)(i)(*hh*).

10.2. BCR 48 – Deductibility of expenditure incurred by a portfolio of a collective investment scheme in securities

This ruling determines the deductibility of expenditure incurred by a portfolio of a Collective Investment Scheme in Securities (CISS) as defined in section 1 of the Collective Investment Schemes Control Act, No. 45 of 2002 (the CISC Act), from income retained by it.

In this ruling references to sections are to sections of the Income Tax Act applicable as at 22 June 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) – definition of 'income';
- section 11(a);
- section 23(*f*); and

- section 25BA.

Class

The class members to whom this ruling applies are described in point 4 below.

Parties to the proposed transaction

The Applicant: An Association not for gain

The Class Members: Portfolios of Collective Investment Schemes in Securities

Description of the proposed transaction

A CISS (and therefore each Class Member) issues participatory interests to its unit holders who invest in the investment portfolio. A Class Member derives income mainly by way of dividends and interest and incurs expenditure, principally the fees payable to its manager. A Class Member typically retains income sufficient to meet its expenses and distributes the remainder of its income to its participatory interest holders.

These activities together constitute the proposed transaction in respect of which this ruling is made.

Conditions and assumptions

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

Ruling

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

- Amounts retained by a Class Member will, under section 25BA(1)(*b*), constitute 'income' as defined in section 1(1). Section 23(*f*) does not apply to the expenditure sought to be deducted from that income. Consequently, the expenditure of a Class Member will be fully deductible from the amounts retained if that expenditure qualifies under section 11(*a*).

11. DRAFT GUIDES

11.1. Employement Tax Incentive

The employment tax incentive was introduced by the Employment Tax Incentive Act 26 of 2013 which was promulgated on 18 December 2013. This guide provides general guidance on the incentive.

While this guide reflects SARS' interpretation of the law, taxpayers who take a different view may use the normal avenues for resolving such differences.

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 should, therefore, not be used as a legal reference. It is also not a binding general ruling.

The ETI is a temporary tax incentive awarded to eligible employers aimed at encouraging them to employ young employees between the ages of 18 and 29, and employees of any age in special economic zones and in any industry identified by the Minister by notice in the Government *Gazette*. Payment of the incentive is effected by eligible employers being able to reduce the employees' tax due by them by the amount of the ETI that they may claim - provided of course that they meet the requirements of the ETI Act. The ETI is administered by SARS through the employees' tax system that is deducted and withheld and accounted for to SARS (usually monthly) via the Pay-As-You-Earn (PAYE) system.

It is a temporary programme covering a period of three years in which an eligible employer may claim the ETI for a maximum of 24 individual months per qualifying employee. The ETI will be subject to continuous review of its effectiveness and impact in order to determine the extent to which its core objective of reducing youth unemployment is achieved. The ETI commenced on 1 January 2014 and will end on 1 January 2017. It applies to qualifying employees employed on or after 1 October 2013 by eligible employers.

11.2. Guide on valuation for Capital Gains Tax purposes – Issue 3

This guide provides general guidance on valuations. It does not go into the precise technical and legal detail that is often associated with tax, and should not, therefore, be used as a legal reference.

The rules for determining capital gains and losses for CGT purposes are largely contained in the Eighth Schedule and apply on or after 1 October 2001.

A capital gain or loss on disposal of an asset is determined by subtracting its base cost from the proceeds.

Pre-valuation date assets

The base cost of an asset acquired before valuation date is equal to its valuation date value plus any further allowable expenditure incurred on or after the valuation date under paragraph 20.

The valuation date is generally 1 October 2001 but for certain previously exempt entities it can be a later date. For example, the valuation date of a public benefit organisation approved by SARS under section 30(3) is the first day of its first year of assessment commencing on or after 1 April 2006. The valuation date of a recreational club which applied for approval under section 30A on or before 31 March 2009 is the first day of its first year of assessment ending on or after 1 April 2007.

A recreational club approved under section 10(1)(*d*)(iv) that failed to apply for approval under s 30A by 31 March 2009 will have a valuation date equal to the first day of its first year of assessment ending after 30 September 2010.

Three methods are potentially available for determining the valuation date value of a pre-valuation date asset, namely:

- 20% × (proceeds less allowable expenditure incurred on or after valuation date) (generally used when no records have been kept and no valuation was obtained at valuation date);
- market value; or

- Time-apportionment (This method of calculating the value of the asset takes into account how long you have owned it before and after valuation date.

Post-valuation date assets

The base cost of an asset acquired on or after valuation date is generally equal to the qualifying expenditure listed in paragraph 20, which includes amongst other things, the cost of acquiring or improving the asset and specified costs of acquisition and disposal. In some situations, however, a post-valuation date asset will be deemed to be acquired at market value, such as when it is acquired by donation or at a non-arm's length price from a connected person. Assets acquired by inheritance from a resident testator are deemed to be acquired at market value on the date of death of the testator plus any further qualifying expenditure incurred by the executor while an asset inherited from a non-resident is deemed to be acquired at market value.

In some circumstances a taxpayer is deemed to dispose of an asset for an amount received or accrued equal to market value. Some examples include:

- the disposal of an asset by donation, for a consideration not measurable in money or to a connected person at a non-arm's length price (paragraph 38);
- cessation of residence (section 9H);
- commencement of residence [paragraph 12(2)(*a*)];
- asset ceasing to be part of a person's permanent establishment otherwise than by disposal under paragraph 11 [paragraph 12(2)(*b*)]
- conversion of a capital asset to trading stock [paragraph 12(2)(*c*)];
- asset that becomes a personal-use asset [paragraph 12(2)(*e*)]; and
- upon the death of a person (paragraph 40).

11.3. Guide to the taxation of special trust

The purpose of this guide is to assist users in gaining a more in-depth understanding of the taxation of special trusts.

This guide has been prepared to assist those involved with special trusts to gain an understanding of the provisions of the Act relating to such special trusts, with particular reference to the income tax and CGT provisions. A brief summary of other taxes relating to special trusts has also been included. This guide focusses mainly on the tax implications for a special trust and not on the tax implications for its beneficiaries.

Unlike conventional trusts which are taxed at a flat rate of tax, a special trust is taxed on the same sliding scale applicable to natural persons.

The Act makes provision for two types of special trust which will be referred to as type-A and type-B trusts. In essence a type-A trust is created for a person or persons having a disability while a type-B trust is created on the death of the testator and can only subsist while it has a minor as a beneficiary.

The distinction between a type-A trust and a type-B trust is important because a type-A trust qualifies for certain relief from CGT while a type-B trust does not qualify for such relief. The definition of "special trust" contained in paragraph 1 applies for CGT purposes only.

12. 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.