TAX UPDATE

For period: 1 January 2018 to 31 March 2018

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1. INTRODUCTION

The purpose of this update is to summarise developments that occurred during the first quarter of 2018, specifically in relation to Income Tax and VAT. Johan Kotze, 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.

This first quarter of a year is normally dominated by the National Budget, and this year was no exception, other than it being flat compared to previous years. Still, go through the table of contents and consider any aspect that may be of interest.

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.

Enjoy reading on!

Why is Santa always so jolly when he comes to the UK?
He can claim Gift Relief.

Why does Father Christmas not live in the United States?
Gift Taxes.

2. NATIONAL BUDGET

2.1. Personal income tax

2017 year of assessment		2018 year of assessment	
Taxable Income	**Rates of tax**	**Taxable Income**	**Rates of tax**
R0 – R189 880	18% of each R1	R0 – R195 850	18% of each R1
R189 881 – R296 540	R34 178 + 26% of the amount above R189 880	R195 851 – R305 850	R35 253 + 26% of the amount above R195 850
R296 541 – R410 460	R61 910 + 31% of the amount above R296 540	R305 851 – R423 300	R63 853 + 31% of the amount above R305 850
R410 461 – R555 600	R97 225 + 36% of the amount above R410 460	R423 301 – R555 600	R97 225 + 36% of the amount above R423 300
R555 601 – R708 310	R149 475 + 39% of the amount above R708 310	R555 601 – R708 310	R147 891 + 39% of the amount above R555 600
R708 311 – R1 500 000	R209 032 + 41% of the amount above R708 310	R708 311 – R1 500 000	R207 448 + 41% of the amount above R708 310
R1 500 001 and above	R533 625 + 45% of the amount above R1 500 000	R1 500 001 and above	R532 041 + 45% of the amount above R1 500 000

Rebates		Rebates	
Primary	R13 635	Primary	R14 067
Secondary	R7 479	Secondary	R7 713
Third rebate	R2 493	Third rebate	R2 574
Tax threshold		**Tax threshold**	
Below age 65	R75 750	Below age 65	R78 150
Age 65 and over	R117 300	Age 65 and over	R121 000
Age 75 and over	R131 150	Age 75 and over	R135 300

2.2. Medical tax credits

Over the next three years, below-inflation increases in medical tax credits will help government to fund the rollout of national health insurance.

Government will increase the medical tax credit from R303 to R310 per month for the first two beneficiaries, and from R204 to R209 per month for the remaining beneficiaries. The medical tax credit will be reviewed after the Davis Tax Committee presents its recommendations.

2.3. Increasing the VAT rate

Government proposes to raise VAT by one percentage point, from 14 per cent to 15 per cent, effective 1 April 2018. The increase is necessary to meet new spending commitments and prevent further erosion of the public finances. VAT was last adjusted in 1993, and is lower than the global and African averages.

2.4. Increasing the estate duty rate

In line with Davis Tax Committee recommendations, and in keeping with the progressive structure of the tax system, the 2018 Budget proposes to increase estate duty from 20 per cent to 25 per cent for estates worth R30 million and more. To limit the staggering of donations to avoid the higher estate duty rate, any donations above R30 million in one tax year will also be taxed at 25 per cent. Both measures will be effective from 1 March 2018.

2.5. Incentives to complement growth initiatives

The Minister of Finance will approve six special economic zones to benefit from additional tax incentives. The Department of Trade and Industry is driving the overall policy approach that seeks to encourage investment in the manufacturing and tradable services sectors to support exports and economic growth, and create jobs.

Coega, Dube Trade Port, East London, Maluti-a-Phofung, Richards Bay and Saldanha Bay will offer attractive incentives, including a reduced corporate tax rate for qualifying firms and an employment tax incentive for workers of all ages. The legislation will be reviewed to ensure that the granting of these additional tax incentives does not create opportunities for local companies to shift their activities and reduce their tax liability.

The Department of Planning, Monitoring and Evaluation is conducting a review of all tax incentives and grants. Tax incentives are evaluated to ensure that they are aligned with inclusive growth objectives. If not, they will be redesigned or removed.

Research and development (R&D) can lead to innovation, increased productivity and higher levels of economic growth. To encourage greater investment, the R&D tax incentive allows taxpayers to deduct 150 per cent of expenditure on qualifying projects. Over the past two years, the Department of Science and Technology has worked to reduce an application backlog that developed due to inefficiencies in the system, and has moved to an online system. Government will consider revising aspects of the legislation that have created complexity.

The employment tax incentive appears to have had generally positive results, depending on firm size. Impact analyses consistently find high impact in smaller firms, with lower or negative impacts in large firms. The incentive will be reviewed before it expires on 28 February 2019.

2.6. Reviewing the controlled foreign company comparable tax exemption

South African-controlled companies operating in countries where tax payable is less than 75 per cent of what would have been payable at home are required to include the foreign net income in their South African tax calculation. This prevents these firms from shifting profits to low-tax jurisdictions. In the context of a global trend towards lower corporate tax rates, government will review the controlled foreign company tax exemption to determine whether a reduction is warranted.

2.7. Reviewing the tax treatment of excessive debt

Government has made progress in reviewing the tax treatment of excessive debt financing. The deductibility of interest payments on debt acts as an incentive to use debt rather than equity funding, and can be used to strip profits from high-tax countries. A discussion document inviting comments will soon be published to facilitate public consultation.

Government is striving for a balance between certainty, simplicity and adequate base protection to ensure a sustainable corporate tax base.

2.8. Updating regulations prescribing foreign electronic services

The 2017 *Budget Review* announced that regulations prescribing foreign electronic services subject to VAT would be broadened to include cloud computing and other online services. Updated draft regulations prescribing foreign electronic services and supporting amendments to the VAT legislation will be published on Budget Day for public comment.

2.9. Tax deduction of fruitless and wasteful expenditure

To ensure proper governance of public entities and encourage accountability, government proposes that losses or expenditure classified as fruitless and wasteful will not qualify for a tax deduction.

2.10. Splitting of medical fees tax credits

The Income Tax Act (1962) provides a tax rebate (medical tax credit) for individuals. The medical tax credit consists of two components: medical scheme fees for approved medical scheme contributions and additional medical expenses for out-of-pocket medical payments. Government is concerned that some taxpayers may be excessively benefiting from this rebate, specifically in instances where multiple taxpayers contribute toward the medical scheme or expenses of another person (for example, adult children jointly contributing to their elderly mother's medical scheme). Where taxpayers carry a share of the medical scheme, contribution or medical cost, it is proposed that the medical tax credit should also be apportioned between the various contributors.

2.11. Clarifying the tax treatment and obligations of funds managed by bargaining councils

Bargaining councils were consulted in 2017 regarding the correct tax treatment of employee and employer contributions to, and payments from, bargaining council funds. A general consensus emerged that the majority of existing funds can be accommodated by withholding taxes on contributions at the employer level, which also has the best administrative architecture in place. Transitionary arrangements can be considered for a small minority of more complicated fund types to ensure smooth implementation.

2.12. Removing the fringe benefit for preferential interest rates to employees for housing

In 2014, legislative changes were made to remove the fringe benefit that previously applied to employees with remuneration below R250 000 for the acquisition of low-cost housing with a value below R450 000. In line with government policy to promote the provision of housing, it is proposed that the relief from this fringe benefit tax be extended to loans at preferential interest rates, which are solely for housing use, made to employees who satisfy the same remuneration criteria for loans with a value of less than R450 000.

2.13. Retirement reforms – Tax treatment of contributions to retirement funds situated outside South Africa

The Income Tax Act currently exempts all retirement benefits from a foreign source for employment rendered outside of South Africa from taxation. The interaction of this exemption with double taxation agreements and other provisions of the Income Tax Act will be reviewed to ensure that the principle of allowing deductible contributions only in cases where benefits are taxable is upheld.

2.14. Retirement reforms – Align tax treatment of preservation funds upon emigration

Upon formal emigration an individual is able to withdraw the full value of their retirement annuity, after paying the applicable taxes. Government will consider aligning the tax treatment of different types of retirement fund withdrawals in such circumstances.

2.15. Retirement reforms – Allowing transfers to pension and provident preservation funds after retirement

In 2017, amendments were made to allow the transfer of pension or provident fund amounts to a retirement annuity fund after the retirement date of an employee. These amendments expanded the choice of available retirement funds if an individual decided to postpone retirement. Pension preservation and provident preservation funds were excluded as the administration required to disallow once-off withdrawals from these funds was considered too onerous. Industry consultations indicate that the system changes will not be burdensome, thus it is proposed that transfers to pension preservation and provident preservation funds be catered for in the legislation.

2.16. Retirement reforms – Rectifying tax anomalies on the transfer of retirement funds

The transfer of fund amounts between, or within, retirement funds at the same employer has inadvertently led to a tax liability for members, due to the current wording of the legislation. In principle, there should be no additional tax consequence for members if the transfers refer to amounts that have already been contributed to the retirement fund. Legislative amendments will be retrospectively introduced to correct these unintended tax liabilities.

2.17. Business (general) – Amendments resulting from the application of debt relief rules

In 2017, the Income Tax Act was amended to address the tax consequences of applying debt relief rules. Government has noted concerns about unintended consequences that may arise from the application of these tax amendments. It is proposed that further amendments be made to address these concerns.

2.18. Business (general) – Refining anti-avoidance rules dealing with share buybacks and dividend stripping

In 2017, anti-avoidance rules dealing with share buybacks and dividend stripping were strengthened. One of the legislative provisions specified that anti-avoidance rules would override corporate reorganisation rules to prevent taxpayers from stripping dividends out of a target company, and thereby devaluing the company, before a reorganisation transaction. It has come to government's attention that these changes may affect some legitimate transactions and arrangements. As a result, it is proposed that the interaction of these anti-avoidance rules and some of the corporate reorganization rules be reviewed. In addition, anti-avoidance rules dealing with share buybacks and dividend stripping regarding preference shares should be clarified.

2.19. Business (general) – Refining rules for debt-financed acquisitions of controlling interest in an operating company

Following the proposed suspension of intra-group transactions in 2012, a special interest deduction was introduced instead of allowing implementation of debt push-down structures. Companies can claim this deduction if they used debt funding to acquire a qualifying controlling interest in an operating company. In 2015, the legislation was amended to prevent the abuse of this deduction. To qualify for this deduction, an operating company is now defined as a company where at least 80 per cent of its receipts and accruals constitute income for tax purposes. However, amendments to the current provisions are needed to clarify when this test should be applied. In addition, it is proposed that the legislation be reviewed to determine whether this test should be applied when an operating company transfers its business as a going concern to a company that forms part of the same group of companies as that operating company.

2.20. Business (general) – Addressing the abuse of collateral lending arrangement provisions

Since 2015, tax relief has been provided for the transfer of listed shares or both local and foreign government bonds in collateral lending arrangements. If a listed share is transferred as collateral in a lending arrangement, there are no income tax and securities transfer tax implications for 24 months. However, this means that foreign shareholders can reduce their dividends tax rate to zero by taking out a loan with a South African resident company and using the listed shares as collateral. The resident company receives a tax-free dividend and afterwards, per the collateral agreement, pays an amount (called a manufactured dividend) based on the dividend received by that resident company to that foreign company, free of dividends tax. It is proposed that legislation be amended to prevent this abuse.

2.21. Business (financial sector) – Clarifying the tax treatment of doubtful debts

In 2015, the South African Revenue Service (SARS) Commissioner's discretion in administering the Income Tax Act was reviewed and amended in anticipation of the move to a self-assessment income tax system. In 2015, the Commissioner's discretion on a doubtful debts allowance under section 11(j) of the act was deleted with effect from a date to be announced. The intention of such a deletion was that, in future, the allowance would be claimed according to criteria set out in a public notice issued by the Commissioner. However, no criteria have been formulated for the claiming of the allowance. To provide certainty, it is proposed that the criteria for determining the allowance should instead be included in the Income Tax Act.

2.22. Business (financial sector) – Clarifying tax amendments relating to long-term insurers

The Income Tax Act was amended to introduce the risk policy fund for long-term insurers, effective from 2016. The tax treatment of long-term insurers was also amended due to the introduction of the solvency assessment and management framework. Recent amendments affecting the risk policy fund did not take effect when the fund was introduced. It is proposed that the effective date of the relevant amendments be so changed.

2.23. Business (financial sector) – Review of the provisions of the Income Tax Act referring only to the Johannesburg Stock Exchange

Certain provisions of the Income Tax Act refer to the Johannesburg Stock Exchange (JSE) Limited or JSE Limited listing requirements. Following the introduction of additional stock exchanges in South Africa, it is proposed that the relevant tax provisions be reviewed to include the newly introduced stock exchanges, subject to certain regulatory and transparency criteria.

2.24. Business (financial sector) – Clarifying tax treatment of amounts received by portfolios of collective investment schemes

In 2009, the Income Tax Act was amended to provide for collective investment schemes operating on behalf of investors with participatory interests. Amounts (other than capital amounts) are taxable in the portfolio of a collective investment scheme unless they are distributed to participatory interest holders within 12 months of accrual. Some collective investment schemes are trading frequently and arguing, contrary to current case law, that the profits are of a capital nature.

It is proposed that the current rules be clarified to provide certainty on the treatment of trading profits in this context.

2.25. Business (incentives) – Review of venture capital company rules

The uptake of government's venture capital companies tax incentive regime, which aims to encourage investment in small and medium-sized business, has grown significantly over the past two years. However, administrative and technical issues are obstructing increased uptake.

It is proposed that the legislation be amended to address rules relating to the investment income threshold limitations in the qualifying company test, as well as when the controlled company test needs to be applied. The rules relating to the connected person test also need to be reviewed, specifically the rule for retroactive withdrawal of venture capital company status.

2.26. Business (incentives) – Reviewing the write-off period for electronic communication cables

Most companies that provide telecommunications infrastructure have been moving from copper to fibre optic cables.

To align the tax system with technological advances and international practice, government proposes reducing the period over which electronic communication lines and fibre optic cables are written off.

Government will consider further alignment between taxpayers that own these assets and those with the right to use them.

2.27. Business (incentives) – Increasing the distribution period for small business funding entities

The Income Tax Act requires small business funding entities to distribute or incur an obligation to distribute 25 per cent of all amounts received or accrued from assets held during the tax year, excluding amounts from disposing of any of the assets held during the same tax year.

However, practical difficulties arise when the small business funding entity receives an amount on the last day of the year of assessment and is consequently required to distribute or incur an obligation to distribute on the same day.

It is proposed that small business funding entities be required to distribute 25 per cent of all amounts received or accrued from assets held during the tax year within 12 months of the end of the relevant tax year.

2.28. International – Overlap in the treatment of dividend in section 1 and section 31 of the Income Tax Act

There is potential overlap between the treatment of a dividend as defined under section 1 and the treatment of a dividend under the transfer pricing provisions of section 31 of the Act.

To remove this anomaly, it is proposed that an amount should be treated as a dividend *in specie* (an amount distributed to shareholders in a form other than cash) for purposes of applying the transfer pricing provisions of section 31, unless the amount already constitutes a dividend as defined in section 1.

2.29. International – Reversing exchange difference for exchange items disposed of at a loss

Currently, the Income Tax Act provides for the reversal of foreign currency exchange differences when an exchange item becomes irrecoverable. It does this by reversing any exchange gains and losses relating to the portion of the exchange item that has become irrecoverable.

However, the legislation does not provide relief where an exchange item is disposed of at a loss as a result of market forces and not because the debtor is unable to pay. It is proposed that the application of this relief be clarified.

2.30. International – Reviewof the definition of 'international shipping income'

The definition of a South African ship limits the application of the income exemption for international shipping to South African ships only. The limitation may create unintended operational issues where a South African operator uses a replacement ship on a short-term basis, and no South African ship is available. For example, a South African shipping company may occasionally use a third-party vessel when their South African ship is undergoing maintenance, or experiencing port delays or fleet rotations.

If this ship is not registered as South African, then the operator will lose the tax exemption. It is proposed that the definition of 'international shipping income' be reviewed to take the issue described above into account under certain circumstances.

2.31. International – Taxation of short-term insurers

The Income Tax Act provisions regulating the taxation of short-term insurance apply only to short-term insurers resident in South Africa. However, the Insurance Act (2017) permits foreign reinsurers to operate reinsurance businesses in South Africa through branches rather than subsidiaries. In view of this development, the relevant provisions will be extended to apply to non-residents operating shortterm insurance business through branches in South Africa.

2.32. International – Extension of the application of controlled foreign company rules to foreign companies held through foreign trusts and foundation

The Taxation Laws Amendment Act (2017) extended the application of controlled foreign company rules to foreign companies held through foreign trusts and foreign foundations.

The draft Taxation Laws Amendment Bill (2017) developed related rules to classify distributions of discretionary foreign trusts or foreign foundations to individuals and trusts as income of the South African resident beneficiaries. This was done to discourage the use of trusts to defer tax or recharacterise the nature of income. However, due to the complexity and broadness of the proposal, the specific rules were withdrawn and postponed to 2018. These rules will now be considered.

2.33. International – Interest paid to the non-resident beneficiary of a trust

In the current tax rules regarding interest paid to a non-resident beneficiary from a trust, it is unclear who bears the withholding obligation after vesting. Furthermore, the rules dealing with trust income and beneficiaries do not deem the trust to have paid interest to beneficiaries if they are non-residents. A rule will be considered to address this anomaly.

2.34. VAT – Insertion of the definition of 'face value of debt transferred'

A VAT-registered vendor is permitted to claim a deduction for VAT on taxable supplies that have to be written off, as they were provided on credit and the debt is irrecoverable, per section 22(1) of the VAT Act (1991).

If the vendor cedes or sells the debt that has been written off on a non-recourse basis for an amount that is less than the amount owing, then the sale of the debt is exempt from VAT and the vendor is not required to make any adjustments to the previous VAT deduction.

It has come to government's attention that some vendors (such as collection agents or banks) that buy the book debt in terms of the abovementioned arrangement then attempt to claim a further VAT deduction if they write off all or part of this debt in future. This results in a double VAT deduction, which is against the intention of the legislation, as seen in the definition of 'face value of a debt transferred' in the Explanatory Memorandum to the Taxation Laws Amendment Bill (1997).

To prevent this double VAT deduction, it is proposed that the term 'face value of a debt transferred' be defined in the VAT Act to take into account the policy rationale explained in the explanatory memorandum.

2.35. VAT – Postponing the abolishment of the zero-rating of the supply of goods and services for the national housing programme

In 2015, amendments were made to the VAT Act to abolish the zero-rating of the supply of goods and services for government's national housing programme, with effect from 1 April 2017.

In 2017, the legislation was amended to postpone the abolishment date for a further two years to 1 April 2019, as both the National Treasury and municipalities were not ready to enforce this change.

Due to budgetary constraints, it is now proposed to postpone the effective date for this amendment indefinitely. Once confirmed, the Minister of Finance will publish the effective date in the Government Gazette.

2.36. Tax administration – Income Tax – Adjusting 'official rate of interest' in the Income Tax Act

The 'official rate of interest' is the current repurchase rate plus 100 basis points (7.75 per cent).

This rate is used to quantify the fringe benefit of low interest rate loans provided by employers and the amount of a donation for low interest loans to trusts by connected persons.

Given that interest rates lower than prime are now uncommon, it is proposed that the official rate be increased to a level closer to the prime rate of interest. This would allow the benefit of lower rates to be measured with reference to a rate that approximates the rate offered by commercial banks to low-risk clients.

2.37. Tax Administration – Dividends tax – Repeal of requirement to submit returns by persons who received exempt dividends

In order to ease the administrative burden, it is proposed that the requirement for a person receiving a tax-exempt dividend to submit a return be repealed.

2.38. Tax Administration – VAT – Correction of tax invoices

In some cases, a vendor may issue a tax invoice that includes incorrect information in addition to correct VAT, value and supply information. As the document issued by the vendor does not qualify as a tax invoice, the recipient is unable to use it to deduct input tax, and may request a new version with the correct information so that it qualifies as a tax invoice.

An amendment is proposed to clarify that, under the circumstances described above, a vendor that cancels the initial document and reissues an invoice with the correct information will not be committing an offence. The amendment will also require the vendor to maintain a proper audit trail across the initially issued document, the manner of cancellation and the reissued invoice.

2.39. Tax Administration – VAT – Credit notes for supplies after sale of an enterprise as a going concern

It is proposed that an amendment be made to clarify issuance of credit notes when an enterprise is sold as a going concern. In this case the purchaser of the enterprise will be allowed to issue a credit note for goods supplied by the seller of the enterprise and returned to the purchaser.

2.40. Tax Administration – VAT – Special returns for VAT purposes to be retained by vendors and be available on audit

An amendment is proposed that will require a vendor to retain relevant material instead of submitting special returns to SARS.

2.41. Tax Administration – VAT – Separate treatment of branches or divisions of a juristic person for VAT debt-collection purposes

The VAT legislation allows a vendor to register branches or divisions of a juristic person separately. Furthermore, the legislation regards such branches or divisions as separate enterprises, even though they are operated by a single person. An amendment is proposed to provide legal certainty that the provisions for collecting VAT debt will apply across all branches and divisions.

2.42. Tax Administration – VAT – Extension of joint and several liability for VAT to members of a joint venture

An amendment is proposed to provide legal certainty that the members of a joint venture may also be jointly and severally liable for the VAT debts of that venture.

2.43. Tax Administration – Tax treatment of cryptocurrency transactions

Cryptocurrencies are addressed by existing provisions in South African tax law. Cryptocurrencies pose risks to the income tax system as they are extremely volatile and their sustainability is uncertain. At the same time, the supply of cryptocurrency can cause administrative difficulties in the VAT system. To address these issues, it is proposed that the income tax and VAT legislation be amended.

2.44. Tax Administration Act – Notification of commencement of an audit

It is proposed that a taxpayer be notified at the start of an audit as part of efforts to keep all parties informed.

2.45. Tax Administration Act – Deregistration of non-compliant tax practitioners

An amendment is proposed to ensure that non-compliant tax practitioners are deregistered. If a tax practitioner has not complied on a continuous or repetitive basis and does not correct their behavior after being notified by the SARS Commissioner, they will be deregistered as a tax practitioner.

3. DRAFT MEDIA RELEASES, REGULATIONS, NOTICES

3.1. Returns of information to be submittedby third parties in terms of section 26 of the Tax Administration Act

Schedule

1. General

In this notice, any term or expression to which a meaning has been assigned in a **'tax Act'** as defined in section 1 of the Tax Administration Act, 2011, has the meaning so assigned, unless the context indicates otherwise, and the following terms or expressions have the following meanings:

'interest' includes any amount treated as interest under section 24J of the Income Tax Act;

'records' means the recorded information in respect of all persons that the third party must submit; and

'SARS electronic filing service' means a SARS electronic filing service as defined in paragraph 1 of the Rules on Electronic Communication published in *Government Gazette* No. 37940 on 25 August 2014.

2. Persons required to submit third party returns

The following persons are required to submit a return as specified in paragraph 3:

2.1 Banks regulated by the Registrar of Banks in terms of the Banks Act, 1990, or the Mutual Banks Act, 1993, excluding any branch of a bank as defined in section 1 of the Banks Act, 1990;

2.2 Co-operative Banks regulated by the Co-operative Banks Development Agency in terms of the Co-operative Banks Act, 2007;

2.3 The South African Postbank Limited (Postbank) regulated in terms of the South African Postbank Limited Act, 2010;

2.4 Financial institutions regulated by the executive officer, deputy executive officer or board, as defined in the Financial Services Board Act, 1990, whether in terms of that Act or any other Act;

2.5 Companies listed on any exchange licensed under the Financial Markets Act, 2012, and connected persons in relation to those companies, that issue bonds, debentures or similar financial instruments;

2.6 State-owned companies, as defined in section 1 of the Companies Act, 2008, that issue bonds, debentures or similar financial instruments;

2.7 Organs of state, as defined in section 239 of the Constitution of the Republic of South Africa, 1996, that issue bonds or similar financial instruments;

2.8 Any person (including a co-operative as defined in section 1 of the Income Tax Act) who purchases any livestock, produce, timber, ore, mineral or precious stones from a primary producer other than on a retail basis;

2.9 Any medical scheme registered under section 24(1) of the Medical Schemes Act, 1998;

2.10 Any person, who for their own account carries on business as an estate agent as defined in the Estate Agency Affairs Act, 1976, and who pays to, or receives on behalf of, a third party, any amount in respect of—

2.10.1 an investment;

2.10.2 interest; or

2.10.3 the rental of property;

2.11 Any person, who for their own account practises as an attorney as defined in section 1 of the Attorneys Act, 1979, and who pays to or receives on behalf of a third party any amount in respect of—

2.11.1 an investment;

2.11.2 interest; or

2.11.3 the rental of property;

2.12 A person liable to pay withholding tax on interest in terms of section 50F(2) of the Income Tax Act; and

2.13 A person referred to in paragraph 2 of the Regulations issued in terms of section 12T(8) of the Income Tax Act, and who issued a financial instrument or policy in respect of a tax free investment.

3. Returns required to be submitted

Column 1: Person mentioned in paragraph	**Column 2: Information concerning**	**Column 3: Form**
2.1, 2.2, 2.3, 2.4, 2.5, 2.6, 2.7 2.10, 2.11, 2.12 and 2.14.	Amounts incurred or paid in respect of, or by way of any investment, rental of immovable property, interest or royalty; transactions that are recorded in an account maintained for another person (i.e. transactional accounts like bank accounts); and any tax withheld.	IT3(b); or Data compiled in accordance with SARS's Business Requirement Specification: IT3 Data Submission
2.1, 2.2, 2.3, 2.4, 2.6 and 2.7	Amounts paid in respect of the purchase and disposal of financial instruments.	IT3(c); or Data compiled in accordance with SARS' Business Requirement Specification: IT3 Data Submission
2.4	The purchase of, and contributions made in respect of, any retirement annuity policy.	IT3(f); or Data compiled in accordance with SARS' Business Requirement Specification: Insurance Payments

2.4	The payment of an amount that occurs upon the death of a person in terms of an insurance policy.	IT3(g); or Data compiled in accordance with SARS' Business Requirement Specification: Insurance Payments
2.8	Monies paid in respect of a purchase, sale or shipment of livestock, produce, timber, ore, mineral or precious stones, or by way of a bonus.	IT3(e); or Data compiled in accordance with SARS's Business Requirement Specification: IT3 Data Submission
2.9	Contributions made by persons in respect of a medical scheme, and all expenses paid on behalf of such persons by a medical scheme.	IT3(f); or Data compiled in accordance with SARS' Business Requirement Specification: Medical Scheme Contributions
2.13		IT3(s); or
	(a) Contributions to, withdrawals from and transfers to and from a tax free investment; and *(b)* any other amounts received or accrued in respect of a tax free investment.	Data compiled in accordance with SARS' Business Requirement Specification: IT3 Data Submission

4. Due date for submitting a third party return

Subject to paragraph 5, the returns mentioned in the above Table, containing all prescribed information in respect of the period from—

4.1. 1 March to 31 August, must be submitted by 31 October; and

4.2. 1 March to the end of February, must be submitted by 31 May.

5. Manner of submitting a third party return

5.1 Where a third party return comprises—

- 20 or fewer records, the data must be submitted electronically using the SARS electronic filing service – eFiling;
- 21 to 50 000 records, the data must be submitted electronically by using the SARS electronic filing service – hypertext transfer protocol secure (https) bulk data filing; and
- more than 50 000 records, the data must be submitted electronically using the SARS electronic filing service – Connect Direct (C:D) bulk data filing.

5.2 Declarations in respect of third party returns must be submitted electronically using the SARS electronic filing service – eFiling.

6. Alternative arrangements with SARS

SARS may agree that a person, who is required to submit a return in accordance with this Schedule, may submit a return in respect of a different period, upon an alternative date and in an alternative manner, as the case may be.

4. INTERPRETATION NOTES

4.1. Transfer Duty exemption: Public Benefit Organisations and institutions, boards or bodies – No. 22 (issue 4)

This Note provides guidance on the interpretation and application of the following sections of the Transfer Duty Act:

- Section 9(1)(*c*), which exempts from the payment of transfer duty a PBO or any institution, board or body provided the whole or substantially the whole of the property acquired is used for carrying on one or more PBAs.
- Section 9(1A), which exempts from transfer duty the transfer of property by a PBO to any other entity controlled by that PBO.

For purposes of this Note, the transactions do not constitute taxable supplies of fixed property under section 7(1)(*a*) of the Value-Added Tax Act.

Transfer duty is levied on a sliding scale on the value of any property acquired by any person under a transaction or in any other manner. The person acquiring the property (the transferee) is normally the person who is liable for the payment of transfer duty.

All the exemptions from transfer duty are contained in section 9 of the Transfer Duty Act. The exemptions in section 9(1)(*c*) and section 9(1A) of the Transfer Duty Act apply to PBOs and institutions, boards or bodies meeting the certain requirements.

This Note provides general guidelines and considers the broad principles of the legislation. The particular circumstances of each case need to be considered before an exemption from the payment of transfer duty can be approved.

4.2. *Additional investment and training allowances for industrial policy projects – No. 86 (Issue 2)*

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

This Note provides guidance on the interpretation and application of section 12I and takes into account amendments effected by the Taxation Laws Amendment Act 15 of 2016.

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

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

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

4.3. Public Benefit Organisations: The provision of funds, assets or other resources to any association of persons – No. 98

This Note provides guidance on:

- a conduit PBO carrying on PBA 10 in Part I;
- the requirement imposed under section 30(3)(*f*) on a conduit PBO providing funds to an association of persons contemplated in PBA 10(iii) in Part I; and
- the meaning of 'association of persons' contemplated in PBA 10(iii) in Part I.

Before 2001 tax-exempt organisations were allowed to make funds available only to organisations providing residential accommodation to retired persons and 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, subparagraph (iii) was included in PBA 10 under the category 'Providing of Funds, Assets or Other Resources' in Part I.3 A conduit PBO may therefore provide funds, assets or other resources contemplated in PBA 10 in Part I to an association of persons carrying on one or more PBAs, with the exception of PBA 10 in Part I, in South Africa.

A conduit PBO may provide funds, assets or other resources to an informal voluntary association of persons contemplated in PBA 10(iii) in Part I.

The Commissioner must be satisfied that, in the case of any conduit PBO providing funds to any such association of persons, has taken reasonable steps to ensure that the funds are used for the purpose for which those funds have been provided, which is to carry on one or more PBAs in Part I (other than PBA 10 in Part I) in South Africa.

4.4. Public Benefit Organisations: Trading Rules – Partial Taxation of Trading Receipts – No. 24 (Issue 4)

This Note provides guidance on the interpretation and application of section 10(1)(*c*N), which provides for the exemption from income tax of the receipts and accruals of a PBO other than receipts and accruals derived from certain business undertakings or trading activities.

Section 10(1)(*c*N) was amended in 2006 to allow for a partial taxation system for PBOs. A PBO may therefore carry on limited business undertakings or trading activities provided its sole or principal object remains the carrying on of one or more PBAs

This Note discusses only the broad principles in interpreting the legislation. Since the facts and circumstances pertaining to each PBO may differ, each case must be considered on its own merits.

4.5. Unclaimed benefits – No. 99

This Note explains the treatment of lump sum benefits classified as unclaimed benefits that accrued to members (both before and from 1 March 2009) for income tax purposes.

General Note 35 dated 8 April 2004 is hereby withdrawn.

Historically some members of a fund did not, after exiting the fund, claim the lump sum benefit to which they became entitled in terms of the rules of the fund.

These lump sum benefits were classified as an ‘unclaimed benefit’ if it was not claimed after a reasonable period of time.

The legislation did not regulate when and how a lump sum benefit should be classified as an ‘unclaimed benefit’. Fund administrators, as a result, applied different rules to determine when a lump sum benefit was classified as an ‘unclaimed benefit’.

In many instances, fund administrators only applied for a tax directive for an unclaimed benefit when the member or the member’s beneficiaries claimed the unclaimed benefit, as opposed to when the lump sum benefit accrued.

The tax treatment of a lump sum benefit, classified as an ‘unclaimed benefit’,depends on the date on which the benefit accrued to the member.

4.6. Instalment credit agreements and debtors’ allowance – No. 48 (Issue 3)

This Note provides guidance on the application and determination of the debtors’ allowance granted under section 24(2), as it applies to instalment credit agreements.

Section 24 has two main purposes.

First, in the context of a disposal by a taxpayer of trading stock under an instalment credit agreement, section 24(1) provides that the whole amount, excluding finance charges, is deemed to be included in the taxpayer’s gross income at the time of entering into the agreement. This deemed inclusion prevents any argument that the proceeds under an instalment credit agreement do not accrue because of a delay in transfer of ownership. In ITC 1900 the issue was whether the amounts received or accrued in respect of the disposal of 25 immovable properties had to be included in the appellant's gross income in the 2013 or 2014 years of assessment. The court stated that a right to payment in respect of immovable property under the *Lategan* principle vested in the Appellant, and had a value in its hands, as soon as it was in a position to be able to tender transfer to the purchasers under the agreements. The court refused to accept that the accrual took place only upon transfer when payment occurred.

Binns-Ward J stated that:

> 'the timing of the transfers and actual making of the payments, and the order in which they happen do not, in my judgment, determine when the taxpayer became 'entitled to payment' within the meaning of the Lategan principle. The taxpayer's entitlement to payment vested at the date of the fulfilment (including fictitious fulfilment in a case in which the purchaser frustrated the actual fulfilment of the condition) of any suspensive conditions to which the agreement was subject, or the date upon which the taxpayer obtained (or, acting reasonably, could have obtained) the statutory permissions necessary to enable it to tender transfer, whichever occurred later. In other words, the entitlement to payment vested in the taxpayer as soon as the contract became enforceable at the instance of either party'.

In the result, however, the actual date of accrual under the *Lategan* principle was academic because the court found that the proceeds were deemed to accrue under section 24(1) on the date of entering into the agreements.

Secondly, section 24(2) provides the Commissioner with the discretion to grant a debtors' allowance to the taxpayer, the object of which in essence is to subject the profit under the instalment credit agreement to tax on a cash-flow basis.

Section 41 of the Taxation Laws Amendment Act 25 of 2015 proposed an amendment to section 24(2). The proposed amendment removes the Commissioner's discretion and replaces it with the debtors allowance calculation set out in a public notice issued by the Commissioner which prescribes the methods that may be used to calculate the gross profit percentage that should be used to determine the debtors' allowance. The proposed amendment is effective from a date determined by the Minister of Finance in the *Gazette*. At the date of publishing this Note, no date has been gazetted by the Minister of Finance and thus the proposed amendment is not yet effective and taxpayers should continue applying the methods prescribed in this Note.

Finance charges must be recognised on a day-to-day basis over the period of an instalment credit agreement with reference to the outstanding balance under section 24J.

This Note does not apply to the allowances granted to township developers under section 24(2), namely, the debtors' allowance and the allowance for contingent development expenditure.

The debtors' allowance does not apply to:

- sales on extended credit in the absence of a condition suspending the passing of ownership;
- sales subject to a resolutive condition, for example, when it is agreed that a sale shall be regarded as cancelled if the purchase price is not paid by a certain date; and
- leases in terms of which the lessee has an option to acquire the goods at the end of the lease. Such an option is not an agreement of sale, but merely confers on the holder the right to enter into such an agreement at an agreed price at a future date.

Section 24 also applies to lay-by agreements of not less than 12 months. Under a lay-by the buyer pays the purchase price over a period while the seller retains possession of the goods until the purchase price is paid in full. Ownership passes to the buyer on the date on which the purchase price is paid in full and the goods are delivered to the buyer.

The sale of trading stock under an instalment credit agreement could be subject to section 24(1) which determines that the whole amount should be deemed to be included in gross income at the time that the agreement is entered into. For purposes of section 24, the expression 'the whole of that amount' must exclude finance charges and VAT and will therefore be the sum total of capital instalments.

Taxpayers entering into an instalment credit agreement that are subject to section 24(1) may claim a debtors' allowance if the requirements under section 24(2) are met. The granting of the debtors' allowance is at the discretion of the Commissioner. Taxpayers must use one of the methods detailed in this Note to calculate the gross profit percentage that should be used to determine the debtors' allowance. The method chosen must be consistently applied, since SARS will not accept a taxpayer switching between methods in an attempt to exploit the allowance.

4.7. Employees' tax: Independent contractors – No. 17 (Issue 4)

This Note explains the statutory tests and the common law tests to assist SARS officials and employers to classify a worker efficiently and effectively. This Note has been updated to incorporate the latest amendments made under section 5(1)(d) of the Tax Administration Laws Amendment Act 16 of 2016, effective from 1 March 2017, to the exclusionary subparagraph (ii) of the definition of 'remuneration' as defined in paragraph 1.

Binding General Ruling (Income Tax) 40 dated 10 February 2017 'Remuneration paid to Non-Executive Directors' was issued by SARS and, along with the Non-Executive Directors FAQs on BGRs 40 and 41, addresses the independent contractor status of non-executive directors. This Note therefore does not apply to non-executive directors.

The concept of an 'independent trader' or 'independent contractor' (synonymous for practical purposes) still remains one of the more contentious features of the Fourth Schedule. A decision in favour of either independent contractor or employee status impacts on an employer's liability to deduct employees' tax.

The liability of an employer to deduct employees' tax is dependent on whether or not 'remuneration' as defined in paragraph 1 of the Fourth Schedule is paid. Subject to certain conditions, amounts paid to an independent contractor for services rendered are excluded from 'remuneration' as defined, in which case an employer has no obligation to deduct employees' tax from the amounts paid.

Two sets of tools are available to determine whether a person is an independent contractor for employees' tax purposes. The first tool is referred to as the statutory tests. There are two statutory tests, and they are both conclusive in nature.

If the first test is met, the person is deemed not to be carrying on a trade independently, with the result that the amount paid is deemed to be 'remuneration' and will be subject to employees' tax, unless the second test is met.

In the event that the second test is satisfied, the person will be deemed to be carrying on a trade independently, and the amount earned will not be 'remuneration' as defined and will consequently not be subject to employees' tax.

It is possible that a person could meet the first test, and be deemed not to be carrying on an independent trade, but meet the second test and then be deemed to be carrying on an independent trade. The second test overrides the first test.

The second tool is the common law tests, used to determine whether a person is an independent contractor or an employee. Unfortunately, the common law tests as they apply in South Africa do not permit a simple 'checklist' approach. There are no hard and fast rules in determining whether or not a person is an independent contractor. An 'overall' or 'dominant impression' of the employment relationship must be formed.

In practice, the statutory tests are considered first. The common law tests are applied to finally determine whether the person is an independent contractor or an employee only if the statutory tests are not applicable in a particular situation.

This Note includes the interpretation of the relevant legislation, an explanation of the statutory tests, an explanation of the common law tests as captured in the dominant impression test, a flow diagram explaining the structure of the legislation, the dominant impression test grid for quick reference and a historical overview of the common law principles. This Note is not intended to be exhaustive of all scenarios which may occur in practice, and may not deal with certain issues based on specific

facts. It must be accepted that this Note will be revised periodically in the light of public debate, court judgements and legislative reform.

4.8. Employees' tax: Personal service providers and labour brokers – No. 35 (Issue 4)

This Note discusses the employees' tax implications as well as the deductions that may be claimed by a personal service provider or a labour broker.

The use of labels such as 'independent contractor' and 'service company', and the perception that these were acceptable means of avoiding the deduction of employees' tax, necessitated the development of stronger anti-avoidance measures for employees' tax purposes, resulting in the concepts of 'personal service provider' and 'labour broker' being included in the definitions in paragraph 1. Both were also included as employees in the definition of 'employee' in paragraph 1. Deductions applicable to labour brokers without a certificate of exemption and personal service providers were simultaneously narrowed.

Over the years, various amendments have refined the scope of these provisions. This Note includes the latest amendments as well as amendments to the relevant rates of tax attributable to personal service providers and labour brokers.

The term 'personal service provider' is only applicable to a 'company' and 'trust' as defined in section 1(1). This means that the term is not applicable to a natural person. The effect of the legislation can therefore be eliminated by rendering the services through a natural person directly to the client. By rendering the services directly as a natural person, the normal rules relating to the status of an independent contractor or common law employee, as explained in previous guidelines issued by SARS, become relevant.

Not all companies are affected by the legislation relating to a personal service provider. Only companies that fall within the definition of a 'personal service provider' are affected by the definition, and also only when those that fall within the definition are in receipt of 'remuneration' as defined.

It is recommended that all users of services (employer or client) from potential labour brokers and personal service providers should have policies and systems in place to correctly identify and withhold employees' tax from these entities and individuals. A possible solution would be a questionnaire or an affidavit (including an affidavit or solemn declaration for a personal service provider indicating that not more than 80% of its income is derived or is likely to be derived from one client) that could be used by the service-user at the start of the engagement or contract and regularly thereafter. This will enable the client to determine whether employees' tax should be deducted or not.

5. DRAFT INTERPRETATION NOTES

5.1. Deduction in respect of commercial buildings

This Note provides guidance on the interpretation and application of section 13*quin* which provides for an allowance on any new and unused buildings or any new and unused improvements to any building, owned and wholly or mainly used by a taxpayer for purposes of producing income in the course of that taxpayer's trade.

Historically, allowances have generally been granted for movable assets used by a taxpayer in any form of trade which produces income. The general wear-and-tear allowance in section 11(*e*) historically and currently excludes an allowance in respect of buildings, other structures or works of a permanent nature. In contrast to movable assets, before the introduction of section 13*quin*, the availability of an allowance on buildings or structures of a permanent nature greatly depended on the type of trade or business activities in which the building or structure was used. Taxpayers who did not undertake trades covered by specified depreciation regimes, for example, mining and manufacturing, were generally not entitled to any depreciation for their buildings and structures of a permanent nature despite their business usage. <u>There was no policy rationale for excluding commercial buildings that were not used within the specified trades from an allowance because all buildings have a limited useful life</u>. Accordingly, section 13*quin* was introduced to grant an allowance on commercial buildings used by taxpayers in the production of income in trades that fell outside other available depreciation regimes.

The Act currently provides various capital allowances to owners and lessees for the erection of buildings or the effecting of improvements to buildings. Section 13*quin* provides for an allowance on any new and unused buildings or new and unused improvements effected to existing buildings that are used by the taxpayer wholly or mainly for the purpose of producing income in the course of a trade, other than the provision of residential accommodation.

The heading to section 13*quin* refers to a '[d]eduction in respect of commercial buildings'. Although the term 'commercial building' is not used in the wording of section 13*quin,* it provides a useful description of the type of buildings which may qualify for the allowance. A commercial building is considered to be a building that is used in commerce, for example, in a business which relates to the buying and selling of goods and services for profit. Some examples of buildings used in business activities are office buildings, warehouses, retails stores and shopping malls.

Various issues relating to the application of section 13*quin* are considered in this Note.

Section 13*quin* provides for an allowance on any new and unused building or new and unused improvement effected to an existing building if the building or improvement is wholly or mainly used by the taxpayer during the year of assessment for the purposes of producing income in the course of a trade, other than residential accommodation. In the context of section 13*quin* 'mainly' is interpreted to mean 'more than 50%'. The building or improvement must be owned by the taxpayer and it must have been contracted for on or after 1 April 2007. The construction, erection or installation of the building or improvement must also have commenced on or after this date.

In the context of section 13*quin* a building owned by the taxpayer or an improvement to a building owned by the taxpayer includes a building and a part of a building owned by the taxpayer.

The allowance available under section 13*quin* is equal to 5% per year of the cost of the building or improvement. Cost is the lesser of actual cost or cost in an arm's length transaction. Once a building has been disposed of the taxpayer is not entitled to a deduction under section 13*quin*.

The total deductions available under section 13*quin* and other sections on a building or improvement is limited to cost. This includes deductions which, although not allowed under section 13*quin* in previous years of assessment, are specifically deemed to have been allowed for purposes of section 13*quin*.

If a transferor company transfers an allowance asset in an intra-group transaction that meets the requirement of section 45 and the relief applies, the transferor company and the transferee company are deemed to be one and the same persons with regards to calculating the amount of any deduction to which the transferee company is entitled and the amount of the recoupment if, for example, the transferee company disposes of the building. Similar provisions are contained in sections 42, 44 and 47.

The deductions claimed under section 13*quin* are subject to potential recoupment under section 8(4)(*a).* The deductions deemed to have been claimed under section 13*quin*(3) are not subject to recoupment under section 8(4)(*a*).

5.2. Deduction in respect of certain residential units

This Note provides guidance on the interpretation and application of section 13*sex* which provides for an allowance on any new and unused residential unit or improvements to a residential unit used for the purpose of trade and an additional allowance on that residential unit if it qualifies as a low-cost residential unit.

Before 21 October 2008 various provisions in the Act allowed for deductions relating to residential buildings, for example, sections 11(*t*) and 13*ter* and paragraph 12(5) of the First Schedule. Section 13*sex* replaced these provisions and brought in one simplified and comprehensive provision for low-cost housing from 21 October 2008.

Section 13*sex* is subject to section 36, which means that section 36 takes precedence for the deduction of expenditure incurred in a mining operation for the acquisition, erection, construction, improvement or laying out of housing for residential occupation by the mining operation's employees and the furniture for such housing.

Section 13*sex* provides for an allowance on any new and unused residential unit or new and unused improvements effected to existing residential units that are used by the taxpayer solely for purposes of a trade. The unit or improvement must be owned by the taxpayer and it must have been acquired, or the erection commenced, on or after 21 October 2008. In addition, the unit must be situated in South Africa and the taxpayer must own at least 5 units in the Republic that are used by the taxpayer for the purposes of trade.

The allowance available under section 13*sex* is equal to 5% per year of the cost of the residential unit or improvement to the residential unit. Cost is the lesser of actual cost or cost in an arm's length transaction. Once a building has been disposed of the taxpayer is not entitled to a deduction under section 13*sex*. An additional allowance of 5% is available if the residential unit qualifies as a low-cost residential unit.

The section makes provision for an allowance on a building and part of a building owned by the taxpayer. A residential unit is defined as a building or a self-contained apartment mainly used for residential accommodation, unless it is used in carrying on a trade as a hotel keeper.

Section 13*sex* is subject to section 36, which means that section 36 takes precedence for the deduction of expenditure incurred in a mining operation for the provision of residential accommodation for employees and the furniture for such accommodation.

A residential unit which qualified for an allowance under section 13*ter* before 21 October 2008 and continues to meet the requirements of that section will still qualify for an allowance under that section. Section 13*sex* potentially applies to all acquisitions sand erections of residential units and improvements to residential units after 21 October 2008.

The total deduction available under section 13*sex* and other sections on a residential unit or improvement to a residential unit is limited to cost. This includes deductions which, although not allowed under section 13*sex* in previous years of assessment, are specifically deemed to have been allowed for purposes of section 13*sex*.

If a transferor company transfers an allowance asset in an intra-group transaction that meets the requirement of section 45 and the relief applies, the transferor company and the transferee company are deemed to be one and the same persons with regards to calculating the amount of any deduction to which the transferee company is entitled and the amount of the recoupment if, for example, the transferee company disposes of the residential unit. Similar provisions are contained in sections 42, 44 and 47.

The deductions claimed under section 13*sex* are subject to potential recoupment under section 8(4)(*a).* The deductions deemed to have been claimed under section 13*sex*(4) are not subject to recoupment under section 8(4)(*a*).

The allowance may not be claimed if the cost of the residential unit or improvement to the residential, or any part thereof, qualifies or will qualify for a deduction or allowance under any other section of the Act.

5.3. Prohibition of deductions for certain intellectual property

This Note provides guidance on the interpretation and application of section 23I, which relates to the prohibition of deductions for tainted intellectual property.

Transactions involving the use of intellectual property belonging to another person normally carry a charge in the form of a royalty. Usually the payment received will fall within the recipient's gross income and the payee will be allowed to claim a deduction under section 11(*a*) for the expenditure incurred in paying the royalty.

Instances arose in which self-developed intellectual property was sold or transferred to another party connected to the resident developer. The connected person typically paid no tax or tax at a very low rate. These transactions were designed to reduce the group's overall tax liability in South Africa. Section 23I was therefore inserted with the aim of preventing the avoidance of tax.

Section 23I prohibits a deduction of any expenditure incurred for the right or permission to use intellectual property and other expenditure which is directly or indirectly related to such expenditure.

Section 23I disallows a deduction for expenditure incurred for the use of intellectual property when income is shifted between the contracting parties so as to trigger little or no tax.

The section provides for a partial deduction when withholding tax on royalties (Part IVA of the Act) applies.

5.4. Exercise of discretion in case of late objection or appeal

This Note provides guidance on the factors that a senior SARS official will take into account when deciding whether to extend the period for lodging an objection under section 104(4) or an appeal under section 107(2). It also serves to highlight that the period during which an objection or appeal may be lodged is limited.

A taxpayer who is aggrieved :

- by an assessment made on the taxpayer; or
- by certain decisions made under the TA Act or tax Acts,

may object to and appeal against those assessments or decisions under the TA Act.

An objection against an assessment or decision must be lodged in the manner, under the terms and within the period prescribed in the rules.

A person whose objection has been disallowed may appeal to the tax board or tax court against that outcome and in such event the appeal must be lodged in the manner, under the terms and within the periods prescribed in the TA Act and the rules.

A senior SARS official may, within prescribed limits, extend the period prescribed in the rules within which an objection or appeal must be lodged.

The objection and appeal procedures, which are contained in the TA Act and the rules, apply to any dispute under, amongst others, the following tax Acts4 administered by the Commissioner:

- Diamond Export Levy Act 15 of 2007
- Diamond Export Levy (Administration) Act 14 of 2007
- Employment Tax Incentive Act 26 of 2013
- Estate Duty Act 45 of 1955
- Income Tax Act 58 of 1962
- Mineral and Petroleum Resources Royalty Act 28 of 2008
- Mineral and Petroleum Resources Royalty (Administration) Act 29 of 2008
- Securities Transfer Tax Act 25 of 2007
- Securities Transfer Tax Administration Act 26 of 2007
- Skills Development Levies Act 9 of 1999
- Tax Administration Act 28 of 2011
- Transfer Duty Act 40 of 1949
- Unemployment Insurance Contributions Act 4 of 2002
- Value-Added Tax Act 89 of 1991

The Customs and Excise Act 91 of 1964 contains its own provisions relating to dispute resolution.

An objection against an assessment or decision must be lodged within 30 business days of the date of assessment or decision unless the taxpayer requested reasons for the assessment in which case the period runs from a later date. Similarly, an appeal against the disallowance of an objection must be lodged within 30 business days after delivery of the notice of disallowance of the objection.

A senior SARS official may extend the date for lodging an objection by:

- 30 business days if satisfied that reasonable grounds exist for the delay in lodging the objection; and

- between 31 business days and three years if satisfied that exceptional circumstances exist which gave rise to the delay in lodging the objection.

No extension can be granted for :

- a delay of more than three years from the date of assessment or decision; or
- an objection that relates to a change in the practice generally prevailing at the date of assessment or decision.

A senior SARS official may extend the date for lodging an appeal by:

- 21 business days, if satisfied that reasonable grounds exist for the delay; or
- up to 45 business days, if exceptional circumstances exist that justify an extension beyond 21 business days.

5.5. Section 18A: Audit certificate

This Note provides guidance on the interpretation and application of section 18A(2B) and (2C) in relation to the audit certificate which must be obtained and retained in specified circumstances for section 18A receipts issued by an approved organisation or department.

Section 18A(1) and (2) potentially provide a taxpayer with a deduction for *bona fide* donations paid or transferred to any approved organisation, agency or department, if the donation is supported by a section 18A receipt issued by that approved organisation, agency or department.

Generally speaking, under section 18A(2A) a PBO, an institution, board or body, an agency or a department may issue section 18A receipts only to the extent that the donation will be used to carry on PBAs in Part II or, in the case of a conduit PBO, that 50% of the donations will be distributed within 12 months and that the funds will be used to fund PBOs, or institutions, boards or bodies, which carry on PBAs in Part II.

A section 18A receipt issued by an approved organisation, agency or department is required to include a certification to the effect that the receipt is issued for the purposes of section 18A and that the donation has been or will be used exclusively for the object of that organisation or the agency or department's relevant PBA.5

Part I of the Ninth Schedule lists a variety of activities which are recognised as PBAs for purposes of section 30(1). Part II of the Ninth Schedule lists some, but not all, of

the activities listed in Part I for the purposes of section 18A. An organisation may conduct a combination of PBAs in Part I and PBAs in Part II. In this situation section 18A receipts can be issued only for donations which will be used for purposes of carrying on PBAs in Part II. Concerns arose regarding whether approved organisations and departments in these situations would restrict the issuing of section 18A receipts to donations which would be used for PBAs in Part II.

As a result, the requirement for an approved organisation or department to obtain an audit certificate was introduced as a control measure to ensure that section 18A receipts were issued only for donations received or accrued during the year of assessment6 that would be and ultimately are used for purposes of PBAs in Part II.

This Note provides guidance on the information required in an audit certificate referred to in section 18A(2B) and (2C) and from whom such certificate may be obtained.

Strict control measures must be applied to donations received by or accrued to approved organisations, agencies and departments for which section 18A receipts are issued, since such donations may qualify for a tax deduction from the taxable income of taxpayers and as such represent a cost to the *fiscus*.41 Approved organisations, agencies and departments are therefore required to maintain proper control over the application and spending of such donations.

Approved organisations and departments must obtain and retain, or submit as appropriate, an audit certificate confirming that such donations were used in conducting PBAs in Part II and, in the case of conduit PBOs, also confirm that donations were distributed in accordance with section 18A(2A)(*b*)(i).

5.6. *Lease premiums*

This Note provides guidance on the application of paragraph (*g*) and the related deductions under section 11(*f*) and (*h*).

A number of the court cases that considered whether an amount fell within the scope of the above-mentioned paragraph and sections dealt with leases of land and buildings. The use of the following terminology: rent, lease, lease period, lease premium, lessor and lessee, and sub-lessor and sub-lessee; is therefore common in this Note. The use of this terminology is not intended to imply that the scope of the above-mentioned paragraph and sections is always limited to situations involving the use or occupation or right of use or occupation of land and buildings. The above-mentioned paragraph and sections are wider than land and buildings and cover other property, for example, machinery, motion picture films, patents and trademarks. The specific paragraph or section must be referred to in order to determine the specific property covered. Although other terminology may be used in the context of the other types of property, if the same principles apply, the requirements of the above-mentioned paragraph and sections may be met requiring an inclusion in gross income or entitling the taxpayer to a deduction. For example, under an agreement of use a licensee may pay a patent owner a monthly royalty for the use of the patent as well as an upfront lump sum for entering into the agreement of use. The upfront lump sum is an amount that is paid for the use of the patent and it is distinct from and in addition to the royalty. It therefore falls within the scope of a premium for the right of use of a patent under paragraph (*g*)(iii) and requires a full inclusion in gross income.

Lessors that receive lease premiums are obliged under paragraph (*g*) to include the full amount of the premium in their gross income in the earlier of the year of assessment of receipt or accrual. Lessees who pay the premium to a lessor for the right of use or occupation are generally allowed an allowance under section 11(*f*) over the period of the lease. Although there are differences, paragraph (*g*) and section 11(*f*) are complementary.

In limited circumstances a lessor may be entitled to a special allowance under section 11(*h*) in respect of lease premiums included in gross income under paragraph (*g*). The amount of the allowance, if it applies, is equal to such amount as the Commissioner deems reasonable, taking into account the special circumstances of the case and the length of the lease.

Depending on the facts, an allowance granted under sections 11(*f*) and 11(*g*) may be recouped under section 8(4)(*a*).

5.7. Leasehold improvements

This Note provides guidance on the application of paragraph (*h*) and the related deductions under section 11(*g*) and (*h*).

A lessee that incurred rent as an expense for the use of an asset will be entitled to claim a deduction for income tax purposes under section 11(*a*) provided the expenditure meets the requirements of that section. The lessor, on the other hand, who receives the rent or to whom it accrues, must declare the rent as gross income.

The lease agreement may stipulate that the lessee is obliged to effect improvements to the lessor's land or buildings. This expense, in the case of the lessee, and receipt or accrual, in the case of the lessor, are subject to specific provisions in the Act which are discussed in this Note.

This Note dealt with the tax treatment of leasehold improvements for lessors and lessees.

Paragraph (*h*) applies when a right to have improvements effected on land or to buildings by a lessee accrues to the lessor under an agreement. Depending on the facts, the amount included in the agreement as the value or cost of the improvements or the fair and reasonable value of the improvements will be included in the lessor's gross income in the year the right to have the improvements effected accrues to the lessor. Under section 11(*g*) the lessee, who is obliged to effect improvements under the lease agreement, may, subject to certain limitations, deduct the expenditure actually incurred over the remaining period of the lease calculated from the date of completion of the improvements.

In limited circumstances a lessor may be entitled to a special allowance under section 11(*h*) in respect of leasehold improvements included in gross income under paragraph (*h*). The amount of the allowance, if it applies, is equal to such amount as the Commissioner deems reasonable, taking into account the special circumstances of the case and the length of the lease. For example, an allowance may be granted when there is a significant delay for the lessor between the time of accrual of the leasehold improvement under paragraph (*h*) and the time when the lessor physically receives the benefit of the improvement.

Depending on the facts, an allowance granted under sections 11(*g*) and 11(*h*) may be recouped under section 8(4)(*a*).

5.8. Deductions in respect of buildings used by hotelkeepers

This Note provides guidance on the interpretation and application of section 13*bis,* which deals with deductions in respect of buildings used in the trade of hotelkeeper.

Section 13*bis* provides a deduction for buildings used by hotelkeepers if specified requirements are met. The deduction is comprised principally of an annual allowance on the cost of erecting hotel buildings and the cost of effecting improvements to such buildings. A grading allowance, while theoretically still available in some exceptional circumstances, is unlikely to be currently relevant because the buildings and improvements on which it was calculated are likely to have been fully written off by 2012.

The traditional concept of a hotel has changed in recent years. It is therefore necessary to consider the requirements of section 13*bis* as it applies to the modern concept of hotelkeeping.

Different write-off rates apply to buildings erected or improvements effected to buildings used in the trade of hotelkeeper during specified legislated periods.

Taxpayers incurring a cost in erecting or improving a building which they, or a lessee, use for the purposes of conducting the business of hotelkeeper will qualify for the annual allowance on the cost incurred if the requirements of section 13*bis* are met. Section 13*bis* contains detailed requirements in relation to when the erection of the building or the effecting of the improvements was commenced by the taxpayer, when the building was brought into use and, depending on the preceding detail, whether it was wholly or mainly used, or to the extent it was used, by the taxpayer or lessee in carrying on the trade of hotelkeeping during the year of assessment.

The following should be noted in relation to the annual allowance:

- The definition of 'hotel keeper' in section 1(1) requires the person concerned to conduct the business of a hotel, boarding house or lodging house in circumstances in which both meals and sleeping accommodation are supplied by that person for consideration.
- The building must be erected. Purchased buildings do not qualify for the annual allowance but improvements to purchased buildings could qualify.
- The annual allowance is granted on the cost to the taxpayer, after adjusting for deferred recoupments and amounts which may qualify for an allowance under section 11(*g*), of erecting a hotel building or of effecting improvements to such a building. There is no requirement that the taxpayer own the building or improvements. Thus the annual allowance applies to a taxpayer who erects a hotel building or effects improvements to such a building:
    - for own use as a hotelkeeper;
    - as lessor when the lessee is a hotelkeeper; or
    - as lessee to the extent that the building or improvements do not qualify for the leasehold improvements allowance under section 11(*g*).
- The annual allowance is available at different rates depending on when erection of the building or the improvements commenced.

- The annual allowance is not apportioned if the building or improvement is used as required for only part of the year.
- The annual allowance on dual-purpose buildings must be apportioned. For example, apportionment would be required when a building is used for both hotelkeeping and for domestic purposes.
- The aggregate of all deductions which may be allowed or deemed to have been allowed under section 13*bis* or any other section in respect of the cost to the taxpayer of the building or improvement may not exceed that cost. The limitation includes, for example, those allowances deemed to have been allowed for years of assessment when the accruals and receipts of the taxpayer were not included in the taxpayer's income.

An additional grading allowance was available but is unlikely to be relevant after 2012, since the relevant building or improvements should in most instances have been fully written off by that date.

The annual and grading allowances are subject to recoupment under section 8(4)(*a*) but this recoupment can be excluded from income under section 13*bis*(6)(*a*) at the election of the taxpayer by reducing the cost of erecting a replacement hotel building which qualifies for the annual allowance.

5.9. Meaning of 'bulk' in schedule 2

This Note provides clarity on the interpretation and application of the word 'bulk' as contained in Schedule 2 of the Mineral and Petroleum Resources Royalty Act.

A person must pay a royalty for the benefit of the National Revenue Fund in respect of the transfer of a mineral resource extracted from within the Republic.

The Act distinguishes between refined mineral resources (Schedule 1) and unrefined mineral resources (Schedule 2). Each Schedule contains a list of mineral resources. Apart from separating the mineral resources into refined and unrefined mineral resources, the Schedules also specify a condition for each mineral resource. The condition specified differs depending on the type of mineral and whether it is refined or unrefined.

The term ‘unrefined mineral resource’ is defined in section 1 and means a mineral resource:

- listed solely in Schedule 2; or
- listed in Schedule 1 and Schedule 2 that has not been refined to or beyond the condition specified in Schedule 1 for that mineral resource.

The condition specified represents the point at which the mineral is considered to be in an acceptable condition for transfer and is important in determining the royalty payable under the Act. The gross sales for a particular mineral resource will therefore be determined when that mineral has reached the condition specified in the Schedules.

The condition specified is generally represented by a numeric value contained in Schedule 1 (refined mineral resources) and Schedule 2 (unrefined mineral resources). However, the conditions specified for the following unrefined mineral resources listed in Schedule 2 do not have a numeric value attached to them and merely refer to ‘bulk’:

- Aggregates
- Clay used for bricks
- Kaolinite clay used by paper and ceramic sectors
- Granite
- Sandstone
- Slate
- Shale
- Gneiss
- Marble
- Sand
- Other minerals not listed elsewhere not rendered in a concentrate

The word 'bulk' is not defined in the Act and may result in inconsistent interpretation and application when determining gross sales. Differing views exist on 'bulk' as a condition specified in Schedule 2. This Note sets out what SARS's view is.

Section 6A allows for adjustments to the gross sales amount when an unrefined mineral resource has been transferred below or beyond the condition specified in Schedule 2. These adjustments will be applied in the determination of gross sales to determine the arm's length price for that mineral resource.

The gross sales amount of any unrefined mineral resource disposed of that has 'bulk' specified as its condition in Schedule 2 is equal to the amount received or accrued as set out in section 6(2)(*a*). Such amount is not subject to adjustment under section 6A because the legislature did not envisage 'bulk' to comprise a range of values.

5.10. The taxation of foreign dividends – No. 93 (Issue 2)

Issue 1 of Interpretation Note 93 'The Taxation of Foreign Dividends' has been updated primarily to reflect legislative amendments. Some of the more significant amendments include the following:

- The ratios applied in section 10B(3) to calculate the partial exemption applicable to foreign dividends were amended.
- The circumstances in which the exemption is no longer available under section 10B(5) and section 10B(6) were amended.

This Note provides guidance on the interpretation and application of various provisions of the Act relating to foreign dividends. The Note does not deal with the income tax consequences of a dividend paid by a headquarter company, since this topic is addressed in Interpretation Note 87 'Headquarter Companies'.

This Note reflects the income tax and tax administration legislation (as amended) at the time of publishing and includes the following:

- The Taxation Laws Amendment Act 17 of 2017 which was promulgated on

18 December 2017 (as per *Government Gazette* 41342).

- The Tax Administration Laws Amendment Act 13 of 2017 which was promulgated on 18 December 2017 (as per *Government Gazette* 41341).
- The Rates and Monetary Amounts and Amendment of Revenue Laws Act 14 of 2017 which was promulgated on 14 December 2017 (as per *Government Gazette* 41323).

With effect from 1 January 2011, a definition of 'foreign dividend' was introduced into section 1(1) and, combined with the insertion of the definition of 'foreign company' and changes to the definition of 'dividend', had the result that on or after that date foreign dividends no longer fell within the definition of 'dividend' in section 1(1). A dividend and a foreign dividend are mutually exclusive. A dividend relates solely to specified amounts transferred or applied by a resident company. A foreign dividend relates solely to specified amounts paid or payable by a foreign company, which by definition is a non-resident.

Broadly speaking, a foreign dividend is included in a person's gross income but may qualify for a full or partial exemption from normal tax under section 10B. With effect from March or April 2012(1)(*i*)(xv)(*aa*) for foreign dividends and foreign interest not otherwise exempt, was deleted and a partial exemption was introduced under section 10B(3). The partial exemption under section 10B(3) is intended to ensure that the maximum effective rate of tax on taxable foreign dividends does not exceed the dividends tax rate applicable to local dividends. With effect from years of assessment commencing on or after 1 March 2017, the exemptions available for foreign dividends meeting the relevant criteria under section 10(1)(*k*)(ii)(*aa*) to (*dd*) were moved to section 10B(2) and underwent some amendment. In addition, the basic exemption available to natural persons of R3 700 under section 10 the maximum effective rate of tax on taxable foreign dividends increased from 15% to 20%.

A foreign dividend received by or accrued to a person is included in that person's gross income under paragraph (*k*) of the definition of 'gross income' in section 1(1).

Section 10B provides for exemptions of foreign dividends received by or accrued to a person. The exemptions under section 10B(2) are applied separately to each foreign dividend received or accrued while the partial exemption under section 10B(3) applies to the aggregate amount of foreign dividends not exempt under section 10B(2). The partial exemption is determined by applying the applicable ratio to a specific type of person. The exemptions will not apply to the extent that section 10B(4), (5) or (6) applies.

With effect from years of assessment commencing on or after 1 March 2017, the maximum effective rate of tax on taxable foreign dividends increased from 15% to 20%.

Foreign dividends received by or accrued to a person constitute income from a foreign source under section 9(4)(*a*). Foreign tax paid on foreign dividends potentially qualifies for a tax rebate under section 6*quat*(1).

Under section 25D a foreign dividend received by or accrued to a person is translated from a foreign currency to rand at the spot rate, or at the average exchange rate if a natural person or non-trading trust so elects. Special rules apply to foreign permanent establishments, CFCs, headquarter companies, domestic treasury management companies and international shipping companies. Foreign tax payable on a foreign dividend is translated to rand on the last day of a year of assessment at the average exchange rate for that year of assessment under section 6*quat*(4).

Section 23(*q*) prohibits the deduction of expenditure incurred in the production of foreign dividends which are not exempt from normal tax under section 10B. Section 23(*f*) prohibits the deduction of any expenses incurred in respect of amounts received or accrued which do not constitute 'income' as defined in section 1(1), such as foreign dividends exempt under section 10B.

For the purposes of determining the net income of a CFC, a CFC is deemed to be a resident for purposes of the definition of 'gross income' in section 1(1). Foreign dividends received by or accrued to a CFC are therefore included in its gross income. Section 10B also applies to foreign dividends received by or accrued to a CFC for purposes of determining its net income for inclusion in a resident's income. Special rules apply to a CFC in calculating its net income and in determining the cost price or base cost of the right in a CFC when foreign dividends are distributed by the CFC or by another CFC in which the first-mentioned CFC has an interest.

The anti-avoidance provisions of sections 8E, 8EA, 22B and paragraphs 19 and 43A are relevant when entering into share or dividend transactions.

6. BINDING PRIVATE RULINGS

6.1. BPR 288 – Consecutive asset for share transactions within 18 months

This ruling determines whether shares are acquired as capital assets or trading stock pursuant to a corporate reorganisation and whether consecutive asset-for-share transactions concluded within a period of eighteen months will render the anti-avoidance provision in section 42(7) applicable.

In this ruling references to sections are to sections of the Income Tax Act applicable as at 26 July 2017. 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:

- section 1(1) – paragraph (*a*)(i) of the definition of 'trading stock';
- section 42(1), paragraph (*a*) of the definition of 'asset for share transaction'; and
- section 42(7).

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

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

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

Company B: A shareholder of the Applicant and of Company A, incorporated outside South Africa and a non-resident. Company B holds 89.8% of the Company A shares

MD: The managing director of Company B who holds 10.2% of that company

SPV: A special purpose vehicle, to be incorporated as a private company and to be resident in South Africa

Description of the proposed transaction

As a result of changes to the applicable black economic empowerment framework, the shareholders of Company A have decided to take steps to improve the company's BEE scorecard and agreed to introduce a new BEE shareholder.

The steps to implement the proposed transaction will be as follows:

- The BEE participant will acquire 6.5% of Company A's shares at market value from each of the Company A shareholders in quantities proportionate to their respective shareholdings.
- The BEE participant will then dispose of its 6.5% shareholding in Company A to the SPV in exchange for shares in the SPV.
- The Company A shareholders will dispose of 19.5% of their Company A shares directly to the Applicant in exchange for shares in the Applicant in quantities proportionate to their respective shareholding in Company A. Company B will do so in terms of an asset for share transaction as contemplated in section 42. MD will not hold a qualifying interest in the Applicant. His share swap will therefore not afford him any section 42 relief.
- The Applicant will dispose of the 19.5% shareholding in Company A to the SPV in terms of an asset-for-share transaction contemplated in section 42. After this transaction the Applicant will hold 75% of the issued share capital of the SPV. The Applicant stated that it intends holding the shares in Company A on capital account.

Conditions and assumptions

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:

Disposal of Company A Shares by Company B to the Applicant

- The disposal by Company B of its 19,5% shareholding in Company A to the Applicant will be an asset-for-share transaction as contemplated in paragraph (*a*) of the definition of that term in section 42(1);
- Based on the specific facts of this application, the Company A shares will be regarded as having been acquired and held by the Applicant on capital account even though the equity shares in Company A will be disposed of to the SPV shortly after its acquisition. The facts and circumstances of this matter, taking into account the proposed steps before and after the acquisition of the Company A shares by the SPV, are very specific, and in the context of the corporate rules contained in Part III of Chapter II, indicate that the SPV, and the group as a whole, will not deal with the Company A shares as trading stock.
- Section 42(7) will apply as the disposal by the Applicant of the shares in Company A in terms of the proposed transaction will take place within eighteen months of the acquisition of those shares in terms of the asset-for-share transaction. No gain or loss will however arise. The shares will be transferred at the cost at which they would have been acquired.

Disposal of Company A Shares by the Applicant to the SPV

- The disposal by the Applicant of its 19,5% shareholding in Company A to the SPV will be an asset-for-share transaction as contemplated in paragraph (*a*) of the definition of that term in section 42(1).

6.2. BPR 289 – Base cost of loan claim and tax implications of acquisition transaction

This ruling determines the tax implications of a corporate restructuring involving, amongst others, the declaration of a dividend that is settled by the issue of debt and the implementation of a share acquisition transaction.

In this ruling references to sections and paragraphs are to sections of the Income Tax Act and paragraphs of the Eighth Schedule to the Act applicable as at 20 September 2017. 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:

- section 10(1)(*k*);
- section 24O;
- section 45(4B);
- section 64F(1)(*a*);
- section 64G(2)(*b*);
- paragraph 20(1)(*a*); and
- paragraph 35(3)(*a*).

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

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

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

Company A: A company incorporated in and a resident of South Africa, also a wholly-owned subsidiary of the applicant

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

The applicant intends to introduce a black economic empowerment entity as a shareholder of the co-applicant. In order to facilitate the entry of that shareholder, the equity value of the co-applicant must be reduced in order to decrease the level of funding required by the new shareholder.

The proposed steps to implement the transaction will be as follows:

- The co-applicant will declare a dividend to the applicant, which will be paid by creating a loan claim and the issuing of a note evidencing that claim (Note A) in favour of the applicant. The salient terms of the note will be that it will be payable on thirty days written notice to the co-applicant, non-interest bearing and rank *pari passu* with all of the co-applicant's unsecured obligations, except for obligations which are mandatorily preferred by law.

- The applicant will dispose of all its equity shares in Company A to the co-applicant in terms of an intra-group transaction contemplated in section 45(1) on loan account (Note B). The salient terms of the note will be as follows:
  - Note B will be subject to interest at a rate to be agreed, however, the parties will agree not to charge interest for the immediate future.
  - The applicant may not distribute or otherwise deal with Note B within a period of two years from the effective date of the intra-group transaction.
  - Note B will in principle be repayable on thirty days written notice, although it will in fact not be paid within two years of the transaction.
- The co-applicant will obtain interest-bearing bank funding to repay Note B after two years from the effective date of the intra-group transaction. The applicant will use the amount received from the repayment of Note B to make a cash distribution to its shareholders that do not form part of the same group of companies.

<u>Conditions and assumptions</u>

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

- The transaction in terms of which the applicant will dispose of all of its shares in Company A to the co-applicant in exchange for Note B will comply with the requirements of an '*intra-group transaction*' as defined in paragraph (*a*) of the definition of that term in section 45(1) and the relief contemplated in section 45(2) will apply to the applicant and the co-applicant, as the context requires.

- The applicant and the co-applicant will not elect that section 45 will not be applicable to the transaction as contemplated in section 45(6)(*g*).

Ruling

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

- The dividend declared by the co-applicant to the applicant will be exempt from income tax under section 10(1)(*k*) and will be exempt from dividends tax under section 64F(1)(*a*) read with section 64G(2)(*b*).
- The dividend declaration by the co-applicant and settlement of the dividend by the creation of Note A in favour of the applicant will not result in a capital gain in the hands of the applicant.
- The base cost of Note A will be equal to the market value of the applicant's erstwhile right to claim the dividend payment.
- Section 45(4B) will not apply to any portion of the cash proceeds that will be received by the applicant from the repayment of Note B by the co-applicant after a period of two years from the effective date of the intra-group transaction and which will be distributed by the applicant to its shareholders.
- Any interest incurred on the interest-bearing bank loan that will be obtained to re-finance Note B will be deemed to have been incurred in the production of the co-applicant's income and laid out or expended for purposes of its trade in terms of section 24O.

6.3. BPR 290 – Distribution of shares to employee share scheme participants

This ruling determines the tax consequences for the Participants in an employee share scheme on the distribution to them of shares by a share scheme trust.

In this ruling references to paragraph are to a paragraph of the Eighth Schedule to the Income Tax Act applicable as at 28 August 2017. 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 paragraph 38.

Parties to the proposed transaction

The applicant: A trust registered in and a resident of South Africa

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

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

Participants: Beneficiaries of the applicant

Description of the proposed transaction

The applicant was established for purposes of a broad based BEE initiative that was implemented by Company A in order to facilitate the participation of historically disadvantaged employees of Company A and its subsidiaries in the BEE Initiative by way of a Staff BEE scheme. The scheme is regulated by the provisions of the trust deed of the applicant as well as the scheme rules.

Company B, another special purpose vehicle through which the BEE Initiative was implemented, acquired and held shares in Company A ('BEE shares') for the ultimate benefit of its BEE shareholders, which included the applicant. Following a lock-in period and the repayment by Company B of all funding for the acquisition of the BEE shares, Company B distributed the remaining BEE shares to its shareholders, including the applicant. In terms of the scheme rules, the Applicant is obliged to distribute those remaining BEE shares received by it from Company B to the participants on certain vesting dates. The proposed transaction relates to the distribution of the remaining BEE shares by the Applicant to the participants.

Upon distribution of the remaining BEE shares, an amount equal to the market value of the shares at the time of vesting will be included in the income of the relevant participants in accordance with the provisions of section 8C.

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:

- paragraph 38(1) will not apply to the disposal of the remaining BEE shares by the applicant to the scheme participants in accordance with the scheme rules.

6.4. BPR 291 – Deemed expenditure on meals and incidentals

This ruling considers a subsistence allowance paid by an employer in terms of its subsistence and travel policy.

In this ruling references to sections are to sections of the Income Tax Act applicable as at 19 October 2017. 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 section 8(1)(*a*)(i)(*bb*) read with section 8(1)(*c*).

Parties to the proposed transaction

The applicant: A resident employer

Employees: Employees of the applicant

Description of the proposed transaction

In terms of the applicant's subsistence and travel policy (the policy), employees who are required to spend at least one night away from their usual places of residence on local travel for business purposes are paid, in respect of meals and incidental subsistence expenditure, 80% per night of the prescribed maximum daily amount determined and gazetted in respect of meals and incidental costs under section 8(1)(*c*)(ii).

The applicant arranges and pays for the accommodation separately. In some cases the price of the accommodation includes meals while in others it does not. The Applicant pays 80% of the gazetted amount regardless of whether or not the price of accommodation includes a meal.

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:

- An amount paid by way of an allowance in terms of the applicant's policy which is less than the gazetted amount contemplated in section 8(1)(*c*)(ii) will fall within the deeming provisions of section 8(1)(*c*)(ii) only when the applicant has not borne any of the expenses in respect of which the allowance is paid.
- If the applicant bears any of the expenses in respect of which the allowance is paid, the maximum amount deemed to be expended under section 8(1)(*c*)(ii) will be the gazetted amount, reduced by the amount of expenses borne by the applicant. For example, in determining the maximum amount that will be deemed to be expended under section 8(1)(*c*)(ii), the gazetted amount must be reduced by the breakfast charge when the accommodation paid for by the applicant includes breakfast as a separate charge.
- The applicant must retain documentary proof in the form of invoices, of the expenditure incurred by the applicant in order to establish the reduced deemed amounts as contemplated in section 8(1)(*c*)(ii).
- This ruling is not applicable to employees who have accepted permanent assignments for extended periods, due to the nature of the business of the applicant, such as employees at the applicant's offsite facilities.
- This ruling is also not applicable to subsistence allowances paid in respect of travel outside the Republic.

6.5. *BPR 292 – Tax consequences of a debt restructuring*

This ruling determines the income tax consequences of a discharge of debt by set-off, the waiver of a right to the payment of a dividend, and the acquisition and immediate disposal of associate company shares.

In this ruling references to sections are to sections of the Income Tax Act and paragraphs to paragraphs of the Eighth Schedule to the Act applicable as at 9 November 2017. 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:

- section 19;
- section 42;
- paragraph 12A; and
- paragraph 38.

Parties to the proposed transaction

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

Co-applicant 1: A public company incorporated in and resident of South Africa

Co-applicant 2: A public company incorporated in and resident of South Africa

Co-applicant 3: A public company incorporated in and resident of South Africa

Description of the proposed transaction

The applicant is a wholly-owned subsidiary of co-applicant 2. Co-applicant 1 holds 20% of the ordinary share capital of co-applicant 2. Co-applicant 1 also holds 100% of the ordinary shares in a group company which in turn holds 100% of the ordinary shares in co-applicant 3. In addition, co-applicant 1 holds preference shares in the applicant.

While the applicant remains a viable business, its operating cash flow has been less than debt service obligations due to the economic downturn in the sector in which it operates. Accordingly, the applicant's debt has reached a highly burdensome level and this is creating acute liquidity pressures.

To alleviate the financial pressure, the applicant, its creditors, as well as other invested stakeholders have agreed to enter into the proposed transaction as a financial and debt restructuring of the applicant.

The following debts are owed by the applicant to the co-applicants prior to the proposed transaction:

- a mezzanine loan to co-applicant 3 (First Mezzanine Loan);
- a mezzanine loan to co-applicant 1 (Second Mezzanine Loan); and
- an inter-company loan to co-applicant 2.

Immediately before the proposed transaction, co-applicant 1 held all of the preference shares in the applicant. Co-applicant 1 had subscribed for them in the previous year. They are cumulative redeemable non-participating no par value preference shares.

The transaction steps will be as follows:

Step 1 – the first mezzanine loan delegation

- The applicant will delegate a portion of the first mezzanine loan owing to co-applicant 3 to co-applicant 1 and co-applicant 1 will consequently become indebted to co-applicant 3 for the delegated amount, including the outstanding balance on that loan from time to time. The applicant will remain indebted to co-applicant 3 for the amount not delegated. This debt will be interest-free and subordinated.

Step 2 – redemption of Applicant preference shares

- The applicant will elect to redeem the preference shares held by co-applicant 1 in the applicant. • Under the Preference Share Terms:
    - The applicant is obliged to declare and pay all accrued and / or accumulated preference dividends immediately prior to redemption of the preference shares.

- If any preference dividend is not declared and or paid on any applicable dividend date the amount of the undeclared or unpaid preference dividend will be accumulated until declared and paid in full or until the redemption date of the last preference share, whichever is the earlier.

- No dividends have been declared or paid in respect of the preference shares. To the extent that any dividends may over this period have accrued or been accumulated, they will be waived by co-applicant 1 in terms of the proposed transaction**.**

- The applicant will finance the redemption through an intraday bridge loan from a bank. The applicant will pay the redemption amount to co-applicant 1 in cash and at the same time delegate to co-applicant 1 its liabilities to the bank arising out of the loan. Upon receipt of the redemption amount, co-applicant 1 will immediately pay over to the bank, as a repayment of the intraday bridge loan delegated, an amount equal to the loan balance. As a consequence of the delegation, a loan claim will exist against the applicant and in favour of co-applicant 1 for the amount which co-applicant 1 will pay to the bank (the redemption loan).

Step 3 – Inter-company loan and set-off

- The applicant is indebted in terms of an inter-company loan account to co-applicant 2. Co-applicant 2 will subscribe for additional ordinary shares in the applicant for an amount equal to the outstanding inter-company loan amount (Applicant subscription shares) which will be a debt which is due, owing and payable to the applicant on the closing date. The applicant will issue the applicant subscription shares to co-applicant 2 and credit them as fully paid up by setting-off the outstanding subscription price against the outstanding inter-company loan amount. Co-applicant 2 will thereafter have no further claims on inter-company loan account against the applicant.

Step 4 – Applicant share subscription and set-off

- The applicant is indebted to co-applicant 1 in terms of the second mezzanine loan.

- Co-applicant 1 will subscribe for additional ordinary shares in the applicant (applicant designated shares) for a subscription price equal to all the debt owing to co-applicant 1 by the applicant. The total debt owing to co-applicant 1 by the applicant comprises the applicant's claim arising out of the first mezzanine loan less the excluded amount, the second mezzanine loan and the redemption loan (the designated debt).
- The amount owing in respect of the subscription price will be set-off against the designated debt thereby constituting full discharge of the designated debt.

Step 5 - Asset for share exchange

- Co-applicant 1 will exchange the applicant designated shares in consideration for the issue of ordinary shares in co-applicant 2 and the parties will agree that section 42 will apply to the transaction.
- Co-applicant 3 will sell the ordinary shares which it holds in co-applicant 2 to co-applicant 1 on loan account.

Step 6 – Unbundling

- Co-applicant 1 will unbundle all of the equity shares held in co-applicant 2 (which include the equity shares it held prior to the proposed transaction) to all its shareholders by distributing the co-applicant 2 shares to its shareholders as a dividend *in specie,* as contemplated in section 46.

<u>Conditions and assumptions</u>

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

<u>Ruling</u>

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

- Section 19 and paragraph 12A of the Eighth Schedule will not apply to the settlement of the inter-company loan and designated debt by set-off against the share subscription obligations in steps 3 and 4 of the proposed transaction.

- The applicant designated shares that will be acquired by co-applicant 1 in step 4 and disposed of in step 5 will be regarded as having been acquired and held by co-applicant 1 as capital assets for purposes of paragraph (*a*)(ii)(*bb*) of the definition of 'asset-for-share transaction' in section 42(1).
- Paragraph 38 of the Eighth Schedule will not apply to the waiver of any accumulated dividends in step 2 of the proposed transaction.

6.6. BPR 293 – Disposal of shares by a non-resident individual

This ruling determines some of the tax consequences of the disposal of shares held by a non-resident individual.

In this ruling references to sections and paragraphs are to sections of the relevant Act and paragraphs of the Eighth Schedule to the Act applicable as at 16 November 2017. 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 Income Tax Act:
  - section 9C;
  - paragraph 2(1)(*b*) read with paragraph 2(2) of the Eighth Schedule to the Act.
- the STT Act:
  - section 2;
  - section 6; and
  - section 7.

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

The applicant: A natural person who is not a resident of South Africa

The co-applicant: A private company incorporated in and a resident of South Africa, which owns no immovable property, but leases the premises on which it carries on business

The purchasers: Two natural persons who are residents of South Africa (A and B)

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

On 1 March 2007, the applicant acquired 330 shares in the co-applicant. It has been resolved that the shares held by the applicant be purchased by the purchasers who, together with the applicant, are fellow directors of the co-applicant.

The shares will be purchased as follows:

- A will purchase 170 shares and payment will be effected 30 days after conclusion of the purchase and sale agreement.
- B will purchase the remaining 160 shares. The purchase price will be paid to the applicant in 48 equal monthly instalments commencing on the 1st day of the month following the month in which the purchase and sale agreement will take effect.

The co-applicant will pay the Securities Transfer Tax in respect of each transaction and recover it from the respective purchasers.

<u>Conditions and assumptions</u>

This binding private ruling is subject to the additional condition and assumption that the co-applicant did not, during the last three years before the proposed disposal of the shares, acquire any asset in respect of which amounts were paid or are payable by any person to any other person other than the co-applicant in respect of the use of that asset, as contemplated in section 9C(3)(*b*).

<u>Ruling</u>

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

- The amounts received by or accrued to the applicant from the disposal of his shares in the co-applicant will be deemed to be of a capital nature under the provisions of Section 9C(2).

- The disposal of the shares will not be subject to the Eighth Schedule by virtue of paragraph 2(1)(*b*) read with paragraph 2(2).
- Despite that the consideration in terms of one of the transactions will be payable in instalments, Securities Transfer Tax will be payable by the co-applicant in full in respect of each transfer of shares from the applicant to the purchasers.
- The tax will be calculated at a rate of 0.25% on the consideration in respect of each transaction unless the market value of the shares exceeds the consideration, in which case it must be calculated on the market value.

6.7. BPR 294 – Amalgamation transaction between non-resident companies

This ruling determines whether the proposed merger under foreign law constitutes an amalgamation transaction.

In this ruling references to sections are to sections of the Income Tax Act applicable as at 9 November 2017. 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

- section 44(1) – paragraph (*c*) of the definition of 'amalgamation transaction'; and
- section 44(2) and (3).

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

The applicant: A resident company

Partnership A: A foreign registered limited partnership

Partnership B: A foreign registered limited partnership

Company A: A non-resident company, which is wholly-owned by Partnership B

Company B: A non-resident company, which is a wholly-owned subsidiary of Partnership B

Company C: A non-resident company, which is wholly-owned by Company A

Description of the proposed transaction

The Applicant is a 100% limited partner in Partnership A. Partnership A is a 100% limited partner in Partnership B. Partnership B conducts trading activities in its own right.

Partnership B has two wholly-owned subsidiaries, Company A and Company B. Company A holds all of the shares in Company C.

Company A is a holding company. Companies B and C carry on manufacturing activities.

All of the non-residents referred to above are subject to group taxation.

Partnerships A and B each constitutes a 'foreign partnership' as contemplated in paragraph (*a*) of the definition of that term in section 1(1). The income received by or accruing to the partnerships is therefore subject to South African income tax in the Applicant.

The Applicant proposes to rationalise its offshore investments by undertaking the following transaction steps:

- Step 1: Company B will transfer all of its assets and liabilities to Company C. No other consideration will be paid in respect of the disposal.
- Step 2: Company B will be terminated by the operation of law of its country of incorporation.

Conditions and assumptions

This binding private ruling is subject to the additional condition and assumption that the shares held in Companies B and C are all held as capital assets by the respective shareholders of these companies.

Ruling

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

- The disposal of assets by Company B to Company C will constitute an 'amalgamation transaction' as contemplated in paragraph (*c*) of that definition in section 44(1).
- The roll-over relief provided for in section 44(2) and (3) will apply in respect of the disposal of assets by Company B to Company C.

6.8. BPR 295 – Distribution **in specie** *of a share*

This ruling determines the dividends tax and capital gains tax consequences of the proposed distribution *in specie* of a share to the government.

In this ruling references to sections and paragraphs are to sections of the Income Tax Act and paragraphs of the Eighth Schedule to the Act applicable as at 11 December 2017. 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:

- section 64F(1)(*b*);
- section 64FA(1)(*a*); and
- paragraph 75.

Parties to the proposed transaction

The applicant: A state-owned company which is a resident

Company A: A resident company that is a wholly-owned subsidiary of the applicant

Description of the proposed transaction

The applicant is a state-owned company listed in Schedule 2 of the Public Finance Management Act 1 of 1999. It is the sole shareholder of Company A.

Company A is subsidised by the government and funded by the applicant. It:

- is a loss-making company;

- has been approved by the Commissioner of the South African Revenue Service under section 10(1)(*c*A)(ii) as a tax-exempt entity and may issue tax certificates under section 18A;
- has since inception never declared any dividends to its shareholder; and
- projects that it will continue making losses in the future.

It is proposed that Company A should be directly held by the government and no longer by the applicant. It is therefore proposed that the Applicant's directors will resolve to declare the share held in Company A as a dividend *in specie* to its shareholder, whereafter the share will be distributed without any consideration.

Conditions and assumptions

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

Ruling

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

- The applicant will be exempt from dividends tax under section 64FA(1)(*a*) read with section 64F(1)(*b*).
- The market value of the share in Company A for purposes of paragraph 75 of the Eighth Schedule will be a nominal value.

6.9. BPR 296 – Disposal by a German limited partnership of its assets to its sole member

This ruling determines whether the disposal by a German Kommanditgesellschaft limited partnership of its assets to its sole member and the immediate disposal of the assets by that member to another German Kommanditgesellschaft limited partnership of which that person is also a sole member results in a disposal for that member, a resident, for capital gains tax purposes.

In this ruling references to sections and paragraphs are to sections of the Income Tax Act and paragraphs of the Eighth Schedule to the Act applicable as at 20 October 2017. 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:

- section 1(1) – definition of 'company', 'foreign partnership' and 'person';
- section 24H; and
- paragraph 11(1).

Parties to the proposed transaction

The applicant: A resident of South Africa

KG A and KG B: Two German Kommanditgesellschaft limited partnerships

Description of the proposed transaction

The applicant has a 100% interest as a limited partner in both KG A and KG B. The general partner of both KGs is a company incorporated and tax resident in Germany. KG A holds mainly listed shares.

The general partner holds nil percent of the interest in the assets of the KGs. The KGs are not liable for or subject to any German tax on income, other than a trade tax levied by municipalities to the extent that they receive commercial income. The KGs do not accrue or receive commercial income and are therefore not liable for the trade tax.

The applicant is required to take into account the income and gains of the KGs for purposes of the applicant's personal German income tax liability, according to the member's interest of the Applicant in the KGs. Any German tax liability that will arise from the income of the KGs will therefore be due by the applicant and not the KGs.

Proposed transaction

The applicant will enter into a withdrawal agreement with KG A and a contribution agreement with KG B in terms of which–

- the applicant will make a withdrawal of the assets from KG A against the applicant’s capital account at book value; and
- the applicant will immediately contribute the assets withdrawn from KG A to KG B at market value.

On the basis that the Applicant has similar limited partnership interests in KG A and KG B, the applicant’s interest in the assets will remain the same.

The proposed transaction is not regarded as a realisation for German tax purposes on the basis that the applicant had already been taxed on these assets when the applicant ceased to be a German tax resident, and hence no German tax liability will arise.

Conditions and assumptions

This binding private ruling is subject to the additional condition and assumption that the assets of the KGs and the interest in the KGs are held on capital account.

Ruling

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

- The proposed transaction will not result in disposals for purposes of the Eighth Schedule as each KG qualifies as a ‘foreign partnership’, as defined in section 1(1) and is not regarded as a ‘person’ as defined in that section. The applicant is treated as the owner of the partnership assets for purposes of the Act.

6.10. BPR 297 – Amalgamation transaction involving conversion of share block companies to private companies

This ruling determines the tax consequences of an amalgamation transaction involving the conversion of share block companies to private companies in a group of companies controlled by a REIT.

In this ruling references to sections and paragraphs are to sections of the Income Tax Act and paragraphs of the Eighth Schedule to the Act applicable as at 19

January 2018. 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:

- section 1(1) – definition of 'dividend' and 'REIT';
- sections 25BB and 44; and
- paragraph 11.

Parties to the proposed transaction

The applicant: A listed company incorporated in and a resident of South Africa operating as a REIT

Company A: A company incorporated in and a resident of South Africa that is a wholly-owned subsidiary of the applicant

Company B: A company incorporated in and a resident of South Africa that is a wholly-owned subsidiary of the applicant

Company C: A company incorporated in and a resident of South Africa in which the applicant has a 50% shareholding. The remaining 50% of the shares are held by Company A

Company D: A company incorporated in and a resident of South Africa that is a wholly-owned subsidiary of Company A

Description of the proposed transaction

The applicant is a company listed as a REIT on the JSE.

It is proposed that various properties owned by some of the subsidiaries of the applicant will be transferred either from Company A or Company C (the amalgamated companies), to either Company B or Company D (the resultant companies), in pursuance of the rationalisation of the group of companies of which the applicant is the controlling company. All of the proposed transfers will be made to fellow subsidiaries, not by a subsidiary to its holding company.

The proposed transfers will be of all of the assets and liabilities of the amalgamated companies to the resultant companies, without the resultant companies issuing any shares as consideration for the transfers, which will be undertaken by way of mergers in accordance with sections 113 and 116 of the Companies Act 71 of 2008 (the Companies Act). It is intended that section 44 will apply to the above transactions.

Certain of the subsidiaries to be rationalised are share block companies regulated by the Share Blocks Control Act 59 of 1980. These share block companies will first be converted into for-profit companies before the merger transactions can be undertaken.

The proposed transaction is achieved through the following transaction steps:

<u>Step 1 – Registration as vendors</u>

Each of the share block companies will be registered as a vendor under the Value-Added Tax Act 89 of 1991 (the VAT Act).

<u>Step 2 – Adoption of new memorandum of incorporation (MOI)</u>

It is required that the share blocks be cancelled and the rights of use and occupation vested back in the relevant companies, therefore there will in each case be an adoption of a new MOI in accordance with section 16 of the Companies Act as follows:

- In terms of an agreement of assignment to be entered into between the holder of the share block and the share block company itself, the member will:
  - assign its rights of use and occupation of the property and its obligations in respect thereof to the share block company; and
  - contemporaneously with the assignment, assign to the share block company all of the leases then in existence between the member (as landlord) and the tenants.
- Under sections 16(1)(*c*) and 16(5) of the Companies Act, the members will in each case pass special resolutions authorising the following:
  - the conversion of the share block company to a private company;

- the adoption of a new MOI;
- a change of name to delete the reference to 'Share Block Company' and to include the reference to 'Proprietary Limited'; and
- the contemporaneous cancellation of shares in the share block company and the issue of new ordinary shares in the private company.

- The special resolutions and the new MOIs will be lodged at the Companies and Intellectual Property Commission (CIPC). The CIPC is expected to amend the registration number of each converted company to reflect its new status.

Step 3 – Amalgamation transactions

All the converted share block companies, together with those designated property-owning companies that were always for-profit companies, will transfer all of their assets and liabilities to the resultant companies, by way of mergers in accordance with sections 113 and 116 of the Companies Act and section 44, without the resultant companies issuing shares as consideration for the disposals.

The amalgamated companies will be deregistered by the CIPC in terms of section 116(5)(*b*) of the Companies Act as a result of the merger.

Conditions and assumptions

This binding private ruling is subject to the additional condition and assumption that the immovable properties are held as capital assets by the respective amalgamated companies.

Ruling

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

- The cancellation of the share blocks in terms of section 16 of the Companies Act, with the corresponding transfer of the right of use and occupation from the share block holder in the share block company to the share block company, will in each case give rise to a disposal by the shareholders under paragraph 11. The capital gains or losses arising from the disposals must be disregarded in terms of section 25BB(5)(*c*).

- The transfer of all of the assets and liabilities of each amalgamated company to each resultant company, namely, Company B and Company D respectively, will in each case qualify as an 'amalgamation transaction' as defined in paragraph (*a*) of the definition of that term in section 44(1).
- The transfer of the assets and liabilities of each amalgamated company as contemplated in (b) will not constitute a 'dividend', as defined in section 1(1).

6.11. BPR 298 – Waiver of debt

This ruling determines the donations tax consequences of the waiver of debt.

In this ruling references to sections are to sections of the Income Tax Act applicable as at 12 February 2018. 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:

- section 55; and
- section 58.

Parties to the proposed transaction

The applicant: A resident company

Trust X: A resident vesting trust, whose interest is held in equal proportions by the applicant and the shareholders of the applicant

Trust Y: A resident vesting trust, whose interest is held by Trust X

Company A: A resident company, which is 100% held by Trust Y

Company B: A non-resident company, which is 99.5% held by Company A

Description of the proposed transaction

The applicant has, over the years, supplied services to Company B on loan account. None of the fees have been recovered from Company B. These fees have been recorded as revenue in the applicant's financial records at all times and thereby included in the applicant's gross income.

The applicant has not charged Company B any interest in respect of the trade debt accumulated to date.

The applicant proposes to waive a portion of the debt, as Company B has persistently suffered cash flow issues and is currently insolvent. It does not make commercial sense for the applicant to carry the entire debt, given that Company B may in fact never be in a position to repay the debt in full.

The waiver of a portion of the debt is proposed in an effort to maintain the solvency of Company B.

<u>Conditions and assumptions</u>

This binding private ruling is subject to the additional condition and assumption that the trusts in the corporate structure are vested trusts.

<u>Ruling</u>

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

- Donations tax will not be levied on the waiver of a portion of the debt owing by Company B to the applicant.

6.12. BPR 299 – Dividend distribution

This ruling determines the income tax consequences for a company that makes dividend distributions to its holding company.

In this ruling references to sections are to sections of the Income Tax Act applicable as at 10 January 2018. 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:

- section 1(1) - definition of 'dividend'

Parties to the proposed transaction

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

Company X: A company incorporated offshore, which holds 90% of the ordinary shares in the applicant

Company Y: A company incorporated and resident in South Africa which holds 10% of the issued ordinary shares in the applicant

Company Z: A newly incorporated South African resident company

Description of the proposed transaction

The applicant is a privately held South African resident company that owns various subsidiaries, some of which do business in South Africa, and some which do so in other African countries. The applicant will conduct the proposed transaction by way of the following steps:

Pre-transaction step

> Company Z, a newly incorporated South African resident company, will allot and issue 9 ordinary no par value shares to Company X and 1 ordinary no par value share to Company Y, at a subscription price of R1 per share. After such issue of shares, the ordinary shares in Company Z will be held in the same ratio as the ordinary shares are held (before the steps below) in the applicant.

Transaction step 1

> Company X will dispose of its ordinary shares (of R1 par value each) in the applicant to Company Z, in exchange for ordinary no par value shares in Company Z. Company Y will dispose of its ordinary shares (of R1 par value each) in the applicant to Company Z at market value in exchange for ordinary no par value shares in Company Z. The transaction between Company Y and Company Z will take place under the provisions of section 42 of the Act.

Transaction step 2

The applicant will declare two distributions in respect of the ordinary shares of the applicant to Company Z, as follows:

- the first distribution approximating the market value of the applicant's subsidiaries' African operations.
- the second distribution approximating the market value of the applicant's South African operations and subsidiaries.

These distributions will be payable when steps 3, 4, 5 and 6 become effective and are implemented, by way of set-off as indicated below. The board of directors of the applicant will not determine that the distributions will be transfers of contributed tax capital, as contemplated in the definition of 'contributed tax capital' in section 1(1).

Transaction steps 3, 4 and 5

The applicant will dispose of 100% of the ordinary shares in the three companies holding its African operations, to Company Z. The three disposals will be at their combined market values equating to the amount of the first distribution noted in step 2. The amount due by Company Z for the acquisition of shares will be settled by set-off against the first distribution.

Transaction step 6

The applicant will allot and issue 'A' preference shares ('preference shares') to Company Z, at a subscription price of R1 per share. These shares will be cumulative redeemable non-participating preference shares.

The subscription price owing by Company Z will be settled by set-off against the second distribution.

Transaction step 7

The applicant will allot and issue 20 ordinary shares (of R1 par value each) at a nominal cash subscription price of R1 per share, of which 10 will be issued to Company Z and 10 to a BEE shareholder.

After the proposed transaction, Company Z will hold 90 ordinary shares and a number of 'A' Preference Shares in the applicant. The BEE shareholder will hold 10 ordinary shares in the applicant.

Conditions and assumptions

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

Ruling

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

- The distributions will constitute dividends as defined in section 1(1).

6.13. BPR 300 – Intra-group transaction and conversion of debt to equity

This ruling determines the tax consequences of an 'intra-group transaction' contemplated in paragraph (*b*) of that definition in section 45(1) and a conversion of debt to equity.

In this ruling references to sections and paragraphs are to sections of the Income Tax Act and paragraphs of the Eighth Schedule to the Act applicable as at 1 January 2018. 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:

- section 1(1) – definitions of 'group of companies', 'foreign company', 'foreign dividend and 'contributed tax capital';
- section 10B(2)(*a*);
- section 44(5);
- section 45;
- paragraph 1 – definition of 'base cost';

- paragraph 12A;
- paragraph 20(1)(*a*); and
- paragraph 75.

Parties to the proposed transaction

The applicant: A listed company, which is a resident

Co-applicant 1: A resident company that is a wholly-owned subsidiary of the applicant

Co-applicant 2: A company that is not a resident that is a wholly-owned subsidiary of the applicant

Description of the proposed transaction

Co-applicant 2 is the holding company of some of the applicant's strategic foreign investments and all of the equity investments held by co-applicant 2 are held as long-term capital investments.

More than 18 months ago, co-applicant 2 entered into a cross-border merger by way of absorption. For South African tax purposes, the merger was implemented in terms of an amalgamation transaction as contemplated in section 44 and co-applicant 2 participated as the 'resultant company' in that merger.

Co-applicant 2 proposes to dispose of its equity investments in a number of its foreign held companies (target companies) to co-applicant 1.

The proposed steps to implement the transaction will be as follows:

Step 1: Co-applicant 1 and co-applicant 2 will enter into a purchase and sale agreement (the sale) in terms of which co-applicant 2 will dispose of its shares held in the target companies (target companies' shares) at market value to co-applicant 1 in terms of an 'intra-group transaction' as defined in paragraph (*b*) of that definition in section 45(1). The consideration will remain outstanding on loan account (consideration loan).

Step 2: Co-applicant 2 will distribute out of its distributable reserves by way of an *in specie* distribution, all of its rights in the consideration loan to the applicant (*in specie* distribution).

Step 3: The applicant will subscribe for additional ordinary shares in co-applicant 1 for a subscription consideration equal to the consideration loan (subscription price).

Step 4: The applicant will demand repayment of the consideration loan from co-applicant 1.

Step 5: The applicant and co-applicant 1 will agree that the applicant's obligation to pay the subscription price will be set off against co-applicant 1's obligation to pay the consideration loan.

The salient terms of the sale will be as follows:

- The effective date will be the last business day of the month in which all conditions precedent are fulfilled (effective date).
- The consideration loan will be repayable on demand and carry interest at a market related rate.
- Co-applicant 1 will acquire the target companies' shares as capital assets.

With respect to transaction steps 2 to 5 above, the following will apply:

- The *in specie* distribution will be implemented immediately following the implementation of the agreement on the effective date (distribution date).
- The *in specie* distribution will be implemented by way of a cession and assignment of rights arising out of the consideration loan by co-applicant 2 to the applicant. Co-Applicant 1 will owe the consideration loan to the applicant pursuant to the cession and assignment.

Conditions and assumptions

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

- Each of the ordinary shares of the applicant, co-applicant 1 and co-applicant 2 constitutes an 'equity share' as defined in section 1(1).

- Each of the ordinary shares of the target companies constitutes an 'equity share' as defined in section 1(1) and the equity shares are held as capital assets by co-applicant 2.
- The market values of the target companies' shares will exceed the base costs of those shares as at the effective date of the agreement.
- The *in specie* distribution will be treated as a dividend for purposes of the tax and company laws of the jurisdiction of co-applicant 2 and the amount will not be deductible from taxable income by co-applicant 2.

Ruling

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

- The disposal of the target companies' shares will constitute an 'intra-group transaction' as envisaged in paragraph (*b*) of that definition in section 45(1) and co-applicant 1 and co-applicant 2 will qualify for the relief contemplated in section 45(2) because, amongst others, co-applicant 1 and co-applicant 2 form part of the same 'group of companies' as contemplated in section 1(1).
- Section 45(3A) will not apply to deem the consideration loan to have a base cost of Rnil in the hands of co-applicant 2 because co-applicant 2 does not form part of the same 'group of companies' as co-applicant 1 as contemplated in section 41(1). The consideration loan will have a base cost equal to its face value on the effective date.
- Section 44(5) will not apply to the disposal of the target companies' shares by co-applicant 2.
- The distribution of the consideration loan by co-applicant 2 to the applicant will, under paragraph 75, result in co-applicant 2 being deemed to have disposed of the consideration loan to the applicant for expenditure equal to the market value of the loan and the applicant will be deemed to have acquired the consideration loan for proceeds equal to the market value of the loan on the distribution date.

- The *in specie* distribution will constitute a 'foreign dividend' as defined in section 1(1), which will be exempt from tax in the applicant in terms of section 10B(2)(*a*).
- The *in specie* distribution will not result in the application of section 45(4B) as the applicant and co-applicant 2 do not form part of the same 'group of companies' as contemplated in section 41(1).
- The subscription price payable by the applicant to co-applicant 1 for the issue of additional shares in co-applicant 1 will constitute 'contributed tax capital' as defined in section 1(1) in co-applicant 1.
- The subscription price payable by the applicant to co-applicant 1 will constitute expenditure actually incurred by the applicant for purposes of paragraph 20(1)(*a*).
- Paragraph 12A will not apply to co-applicant 1 in relation to the set-off of the consideration loan against the subscription price as both companies are part of the same 'group of companies' as contemplated in paragraph 12A(6)(*f*) and defined in paragraph 12A(1) read with section 41(1).

7. BINDING GENERAL RULING

7.1. BGR 47 (Employment tax incentive) – Meaning of month in the definition of 'monthly remuneration' for employers remunerating employees or a weekly or fortnight basis

For the purposes of this ruling –

- 'EMP201' means the employees' tax return;
- 'ETI' means employment tax incentive;
- 'ETI Act' means the Employment Tax Incentive Act 26 of 2013; and
- 'section' means a section of the ETI Act; and

Purpose

This BGR determines the meaning of ‘month’ in the definition of ‘monthly remuneration’ under section 1(1) for eligible employers that remunerate employees on a weekly or fortnightly basis.

Background

Section 2 provides that an employer that is eligible to receive the ETI relating to a qualifying employee in respect of a month may reduce the employees’ tax payable by that employer in an amount determined under section 7. The meaning of a ‘month’ is fundamental to establish firstly whether an employer is eligible to claim the ETI and secondly to determine the ETI. The definition of ‘monthly remuneration’ and various sections in the ETI Act refer to a month.

The word ‘month’ is, however, not defined in the ETI Act and it is therefore necessary to refer to the Interpretation Act 33 of 1957 in which ‘month’ is defined as ‘a calendar month’. may vary in duration between 28 and The Collins Dictionary defines a ‘calendar month’ as ‘one of the twelve months of the year’. A calendar month 31 days. A calendar month can therefore not be specified in terms of a fixed number of days, but one has to have regard to the calendar.

Subject to meeting all the other requirements under the ETI Act, an eligible employer is entitled to claim the ETI only in the month in which the monthly remuneration is paid or payable to a qualifying employee.’Monthly remuneration’ is defined as the amount paid or payable in respect of a month that an employer employs and pays remuneration to a qualifying employee for at least 160 hours in a month, or an employer employs and pays remuneration to an employee for less than 160 hours in a month the amount as determined under section7(5).

Interpreting the reference to month in the definition of ‘monthly remuneration’ as a calendar month results in practical challenges where employees are paid on a weekly or fortnightly rather than a monthly or other basis. Depending on how the payroll is split, a week at the end or beginning of a calendar month may fall over two calendar months. Aportion of the week’s wage will relate to the one calendar month’s remuneration while the other portion relates to the following calendar month's remuneration for ETI purposes. A mis alignment between applying different periods for claiming the ETI and reporting for employees' tax creates a risk for employers as well as SARS.

The practical challenges resulting from using different periods relating to the ETI and employees' tax can be resolved by applying the reference to month in the definition of 'monthly remuneration' as set out in the ruling below. Applying the reference to month in this definition differently from the reference to month in all the other sections in the ETI Act may affect eligibility to claim the ETI in some instances.See the Annexure for examples demonstrating such an application.

Ruling

Eligible employers that pay employees on a weekly or fortnightly basis may apply a month referred to in the definition of 'monthly remuneration' under section1(1) to align with the period used for purposes of employees' tax. Employer selecting to use this method must apply it consistently throughout all periods during which weekly or bi-weekly pay rolls are run. Should an employer at any time decide to revert to ac alendar month, this ruling will no longer be available to such an employer.

Reference to 'month' in any other section of the ETI Act is interpreted and applied to mean a 'calendar month'.

Annexure – Examples

Example 1 – Age requirement with employee turning 30 years old [section 6(a)]

Facts:

Employer Y, an eligible employer, employs and remunerates employees on a weekly basis. Employer Y thus submits the EMP201s based on a four- or five-week period. Employee X, a qualifying employee, was employed by Employer Y on 1 March 2018. Employee X turned 30 years old on 30 April 2018. The four-week period for completion of the EMP201 for April 2018 begins on 2 April 2018 and ends on 29 April 2018.

Result:

Employer Y cannot claim the ETI for Employee X in the EMP201 for April 2018 since Employee X turned 30 years old in the calendar month of April 2018 and thus did not meet the age requirement in that month.

Example 2 – Age requirement with employee turning 18 years old [section 6(a)]

Facts:

Employer Y, an eligible employer, employs and remunerates employees on a weekly basis. Employer Y thus submits the EMP201s based on a four- or five-week period. Employee Z was employed by Employer Y on 1 March 2018. Employee Z turned 18 years old on 1 April 2018. The four-week period for completion of the EMP201 for March 2018 begins on 5 March 2018 and ends on 1 April 2018.

Result:

Subject to Employee Z meeting all the other requirements of a qualifying employee provided for under section 6, Employer Y can claim the ETI for Employee Z only in the EMP201 which will be submitted for April 2018 and later months. Employee Z turned 18 years old in the calendar month of April 2018 and thus did not meet the age requirement in March 2018 even though his birthday on 1 April 2018 fell within the period reported in the EMP201 submitted for March.

Example 3 – Requirement of monthly remuneration [section 6(g)]

Facts:

Employer Z, an eligible employer, employs and remunerates employees on a weekly basis. Employer Z thus submits the EMP201s based on a four- or five-week period. For completion of the EMP201 for May 2018, the month begins on 30 April 2018 and ends on 3 June 2018. Employee G was employed by Employer Z on 1 May 2018, was remunerated for 37 ordinary hours per week for five weeks in May 2018 and was paid a wage of R6 500 for this five-week period.

Result:

Employer Z cannot claim the ETI for Employee G in the EMP201 for May 2018 since the employee received more than R6 000 remuneration for May 2018 and thus exceeded the maximum monthly remuneration requirement under section 6(g). Since the amount contemplated in section 6(g) is that of monthly remuneration, remuneration paid for the five-week period, and not for the calendar month, should be used for purposes of determining the R6 000 threshold amount.

<u>Example 4 – Determination of ETI if an employee is employed for less than 160 hours and works overtime [section 4(b)(ii) and section 7]</u>

<u>Facts:</u>

Employee B was employed by an eligible employer, Employer Y, in April 2018. Employer Y employs and remunerates employees on a weekly basis. Employer Y thus submits the monthly EMP201s based on a four- or five-week period. There was no wage-regulating measure that applied to the employer. Employee B was employed and remunerated for 35 ordinary hours per week for four weeks in April 2018 and was paid a wage of R1 800 for this four-week period. Employee B also worked 30 hours of overtime and was paid R400 for these extra hours.

<u>Result:</u>

Since Employee B was employed and paid remuneration for less than 160 ordinary hours in the month (35 × 4 = 140 hours), the minimum monthly wage of R2 000 prescribed by section 4(1)(b)(i) had to be apportioned under section 4(1)(b)(ii) so as to arrive at the applicable minimum monthly wage. The applicable minimum monthly wage had to be calculated as follows:

R2 000 × 140 / 160 = R1 750

As the actual wage paid to Employee B (R1 800) was greater than the determined minimum monthly wage of R1 750, the eligible employer could claim the ETI in relation to Employee B under section 4.

Employee B’s monthly remuneration for April 2018 is R2 200 (R1 800 + 400), was paid remuneration for 170 hours (140 + 30 hours) and thus no gross up is required in terms of section 7(5).

Because Employee B earned R2 000 or more but less than R4 000 during the first 12-month period, the incentive amount was R1 000.

The eligible employer was therefore entitled to claim an ETI of R1 000 for Employee B for April 2018.

Example 5 – Employee employed for less than 160 hours in a month [section 4(b)(ii) and section 7]

Facts:

Employer Z employs and remunerates employees on a weekly basis. Employer Z thus submits the EMP201s based on a four- or five-week period. On 14 May 2018, Employer Z, an eligible employer, appointed a qualifying employee, Employee H. Employee H was employed and remunerated for 30 hours per week for the last three weeks in the five-week period for May 2018. The employer was not subject to a wage regulating measure as contemplated in section 4.

Employee H's employment contract provided for remuneration of R18 per hour. Employee H was remunerated a total of R1 620 for the hours worked in May 2018.

Result:

Since Employee H was employed and paid remuneration for less than 160 hours in the month, the minimum monthly wage of R2 000 prescribed by section 4(1)(b)(i) must be apportioned under section 4(1)(b)(ii) so as to arrive at the applicable minimum monthly wage. The applicable minimum monthly wage is calculated as follows:

R2 000 × 90 / 160 = R1 125

Since the actual wage paid to Employee H (R1 620) was greater than the determined minimum monthly wage of R1 125, the eligible employer could claim ETI in relation to Employee H under section 4.

Employee H's monthly remuneration for May 2018 was arrived at by grossing up the actual remuneration to 160 hours in the month (R1 620 × 160 / 90 = R2 880).

Because Employee H earned R2 000 or more but less than R4 000 during the first 12-month period, the incentive amount was R1000.

Apportionment according to the number of hours employed and paid remuneration for:

R1 000 × 90 / 160 = R562,50

The eligible employer was therefore entitled to claim the ETI of R562,50 for Employee H for May 2018.

8. BINDING CLASS RULING

8.1. BCR 60 – Consequences of an employee share trust disposing of the underlying shares and distributing the net proceeds to the beneficiaries

This ruling determines the tax consequences for an employee share trust and its beneficiaries resulting from the disposal by the employee share trust of the underlying shares and the resulting distribution of the net proceeds to the beneficiaries.

In this ruling references to sections and paragraphs are to sections of the Income Tax Act and paragraphs of the Eighth Schedule to the Act applicable as at 28 September 2017. 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:

- section 1(1) – definition of 'gross income';
- section 8C;
- paragraph 56; and
- paragraph 80 of the Eighth Schedule to the Act.

<u>Class</u>

The class members to whom this ruling will apply are the beneficiaries referred to hereunder.

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

The applicant: An unlisted company, incorporated in and a resident of South Africa

The co-applicant: A listed company, incorporated in and a resident of South Africa and the holding company of the applicant

The trust: A trust, settled by the applicant, registered in and a resident of South Africa

The beneficiaries: Qualifying employees who are permanent employees of the companies that form the group of which the co-applicant is the controlling company

Description of the proposed transaction

The applicant settled the trust for the benefit of the beneficiaries during 2012. From time to time the trustees allocate units to qualifying employees in accordance with their participation percentages at the commencement of a term. The allocation date is the date upon which an allocation of units is made.

A unit is defined as a vested right to receive a number of shares in a relevant tranche in accordance with a beneficiary's participation percentage on each delivery date (being each of the fifth, sixth and seventh anniversaries of the relevant allocation date) and to receive distributions declared and paid in respect of the shares.

The participation percentage of a beneficiary in respect of a specific tranche is the aggregate number of units which have been allocated to and are held by a beneficiary in respect of a tranche, in a specific term, divided by the total number of units which have been allocated to and are held by all beneficiaries in respect of that tranche during that term, expressed as a percentage.

The term, in relation to each tranche, is defined as a period commencing on the allocation date and terminating on the seventh anniversary of that date.

A tranche is defined as the pool of trust shares which have been acquired by the trustees at the commencement of each term and in respect of which units are allocated to qualifying employees during that term.

The trust deed provides for the dates upon which the relevant shares in a particular tranche, attributable to a beneficiary, will become deliverable to that beneficiary. In particular:

- 25% of the relevant shares are deliverable on the fifth anniversary of the allocation date;
- a further 25% of those shares on its sixth anniversary; and
- the balance of 50% on the seventh anniversary.

The settlement date means, in relation to each delivery date, the date occurring on the fourth business day after that delivery date.

The trust is funded by the employer companies through capital contributions which are used to acquire the shares in the co-applicant in respect of each tranche.

Beneficiaries acquire vested rights in respect of their units from the allocation date. A qualifying employee becomes a beneficiary once a ‘form of acceptance and adherence’ has been completed.

To date all distributions in respect of the shares held by the trust (the trust shares) have been paid to beneficiaries on the basis that the dividends tax is borne by the beneficiaries.

In terms of the trust deed:

- ownership of the relevant trust shares is delivered to a beneficiary on each delivery date;
- a beneficiary is not entitled to dispose of the relevant shares so transferred for a period of seven days after the transfer of ownership by the trust to the beneficiary; and
- the trust may act as an agent to dispose of the shares after the seven day period.

However, a beneficiary should then have timeously delivered a duly executed sale instruction.

The applicant considers that the difficulty with the current construction is that all shares are firstly transferred to a beneficiary and then sold on behalf of a beneficiary. This requires each beneficiary to have a central securities depository participant (CSDP) account in order to take transfer of the relevant shares and to sell them.

The matter is further considered to be complicated by a rights issue by the co-applicant during 2017. It was decided by the trustees and the board of directors of the co-applicant that the beneficiaries should benefit from it.

This is to be effected in the following manner:

- The trust is currently the registered holder of the shares in the co-applicant and entitled to exercise its rights in respect of the rights issue.
- The applicant will advance a loan to the trust to enable it to exercise its rights under the rights issue (the rights issue loan).
- It will attract interest at the official rate of interest for tax purposes (currently 7.75%).
- The trust will be obliged to repay the capital and accrued interest. The applicant may however waive a portion of the loan.

After the rights issue the trust will hold approximately 0.5% of the total issued share capital of the co-applicant.

The proposed transaction

The following two transactions are proposed:

- a revised mechanism to deal with the conferral of benefits by the trust on beneficiaries on delivery date and settlement date; and
- arrangements concerning the treatment of the proposed rights issue loan as well as the shares acquired by the trust pursuant to the rights issue (the rights issue shares).

Revised unwinding mechanism

In terms of the proposed revised unwinding mechanism, both the trust shares and the rights issue shares will become deliverable to a beneficiary in accordance with the already-mentioned 25/25/50 methodology in years five, six and seven.

A beneficiary must indicate prior to section 8C vesting whether or not the trust shares must be delivered to him or her or sold for his or her benefit.

If the beneficiary's shares are to be transferred, it will be done on the delivery date. If a beneficiary does not pay cash to settle the costs of transfer and the resultant tax liability, a number of the beneficiary's shares will be sold to cover that liability out of the proceeds.

If no election has been made by a beneficiary or a beneficiary has delivered a sale instruction, the trust will, whilst it is still the registered shareholder, sell all of the shares for the benefit of the beneficiary. The proceeds less costs and taxes for which the beneficiary is liable, will be paid to the beneficiary on the settlement date, to allow the trust sufficient time to sell the shares and to collect the proceeds.

Rights issue shares

A beneficiary will not be entitled to elect to take transfer of the rights issue shares. Those shares will be sold by the trust for the benefit of beneficiaries, who will become entitled to the sale proceeds. However, two liabilities will arise in this context, namely:

- the income tax liability under section 8C; and
- a proportionate amount to enable the trust to settle at least a portion of the rights issue loan and accrued interest, depending on whether or not a portion of the loan is waived. Set-off will apply to the obligation of the trust to pay the proceeds from disposal of the rights issue shares, and the obligation of the beneficiary to pay the income tax and the beneficiary's contribution amount. In this regard, the trust deed provides that each beneficiary shall become obliged to make a contribution to the trust on the settlement date, which will be calculated by reference to the outstanding loan amount in respect of the beneficiary's rights issue shares.

Conditions and assumptions

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

Ruling

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

- The market value for purposes of section 8C(2)(*a*)(ii) is the amount which will be received by each beneficiary on the settlement date.
- All direct costs payable by each beneficiary relating to the disposal of the trust shares and the rights issue shares linked to the units, must be taken into account in determining the gain under section 8C(2)(*a*)(ii).
- Paragraph 80(2A) will not apply to the transaction. Under the provisions of paragraph 80(2), if the trust derives any capital gains from the disposal of the trust shares and rights issue shares, those gains will not be taxable in the trust.
- The amount contributed by each beneficiary to the trust to enable the trust to repay a portion of the rights issue loan will form part of the consideration payable by that beneficiary in respect of that equity instrument.
- The contributions received by the trust from each beneficiary relating to the rights issue shares will not be included in the gross income of the trust.
- To the extent that the aggregate of the beneficiary's contribution amounts are insufficient and the balance of the rights issue loan is waived by the applicant, the provisions of paragraph 56 will not apply.

8.2. BCR 61 – Foreign return of capital

This ruling determines the interpretation of the definition of 'foreign return of capital' in section 1(1) in the context of a foreign unbundling of a part of the business of a dual-listed company to South African resident shareholders.

In this ruling references to sections are to sections of the Act applicable as at 21 December 2017. 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 definition of 'foreign return of capital' in section 1(1).

Class

The class members to whom this ruling will apply are the shareholders of the applicant, who are residents, as defined in section 1(1).

Parties to the proposed transaction

The applicant: A listed company, incorporated in and a resident of a foreign country and listed in that foreign country and South Africa, amongst other places

Description of the proposed transaction

The applicant owns all of the shares in a foreign subsidiary company in which it houses its business interests in the foreign country. The applicant performed a strategic review of the whole group and concluded that the interests of the shareholders would be best served by separating its businesses. Part of the separation involves the unbundling of this subsidiary.

The proposed transaction will be implemented by way of an unbundling by the applicant to all of its shareholders (including the class members) of its investment (unbundled shares) in the subsidiary company.

The proposed transaction will be implemented pursuant to a specific term to be incorporated into the founding document of the applicant, which will provide that the applicant can transfer specified assets (including some, or all, of the applicant's shareholding in one or more of its subsidiaries) to its shareholders for no consideration, or to a company which issues shares to the shareholders as consideration, otherwise than by way of declaring a dividend in a specified amount.

The proposed transaction will be achieved either by way of:

- the transfer of the unbundled shares to the shareholders (including the class members) without declaring a cash dividend made out of the applicant's distributable reserves (e.g. retained earnings) (option 1); or
- the transfer of the unbundled shares to the shareholders by way of a combination of a reduction of capital (expected to comprise a relatively small proportion) and a distribution out of other reserves such as retained

earnings and/or merger reserve (option 2). Option 2 will be implemented as one combined step.

The choice between the two options will be determined in part by the levels of the relevant reserves at the time of the proposed transaction.

The transfer of the unbundled shares will be governed by specific legislation that provides for the transaction to be tax neutral in the foreign jurisdiction. In consequence, the transaction will not constitute a taxable distribution for purposes of the foreign jurisdiction's laws in respect of the taxation of companies.

Conditions and assumptions

This binding class ruling is subject to the additional condition and assumption that the proposed transaction complies with the requirements set out in the specific foreign legislation and therefore that the proposed transaction qualifies as an exempt distribution for purposes of the tax laws on companies in that jurisdiction.

Ruling

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

- The proposed transfer of the unbundled shares by the applicant to the class members will constitute a 'foreign return of capital' as defined in section 1(1).

8.3. BCR 62 – Research and development conducted on behalf of a taxpayer

This ruling determines the deductibility under section 11D(4) read with section 11D(2) of levy payments made by members of an association which will in turn use the levy to fund research and development (R&D) activities approved by the Minister of Science and Technology in terms of section 11D(9).

In this ruling references to sections are to sections of the Act applicable as at 11 January 2018. 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 section 11D(2), (4) and (9).

Parties to the proposed transaction

The applicant: An association incorporated in and a resident of South Africa, which is an institution, board or body that is exempt from normal tax under section 10(1)(*c*A)

The class members: Companies incorporated in and residents of South Africa, who are members of the applicant association

Description of the proposed transaction

A research division of the applicant carries out extensive scientific research to sustain and enhance the manufacture of a product of its members.

The research division of the applicant, on behalf of the class members, submits R&D project applications to the Department of Science and Technology (DST), from time to time, for approval as mandated by section 11D(4)(*d*) and (9). These R&D projects are undertaken on behalf of the class members. Each class member is required by the DST to submit individual applications, albeit that the applications all relate to the same R&D projects.

If the applications are successful, each individual class member will receive a letter from the DST confirming that the relevant R&D projects are approved by the Minister of Science and Technology for purposes of section 11D. The class members are required to pay a mandatory levy to the applicant. The levy is used to fund the various activities and functions of the applicant, including those of its research division. The levy is determined based on the budgets of the various divisions of the applicant; hence the applicant is able to determine the portion of the levy that funds the activities of its research division. The research division, which conducts the R&D is, in turn, able to determine on an accurate basis how much of the determined portion of the levy relates to section 11D approved projects. The research division is able to determine accurately whether the monthly levy is paid by the class members to the applicant before or after the date when the DST has received the section 11D application for approval.

Conditions and assumptions

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

Ruling

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

- The class members may claim a deduction in terms of section 11D(2) read with (4) equivalent to 150% of the levy incurred by each class member, to the extent only:
  - of the portion of the levy that will actually be used directly and solely for R&D activities by the applicant;
  - that the R&D has been approved by the Minister of Science and Technology in terms of section 11D(9); and
  - of the levy portion that will be incurred on or after the date of receipt of the application by the DST for approval of that R&D in terms ofsection 11D(9).
- Any of the class members which has a year-end that is different to that ofthe applicant may nonetheless deduct the levy portion that is actually incurred expenditure in respect of R&D in the course of its financial yearand approved in terms of section 11D(9).

9. GUIDES

9.1. Guide on the Taxation of Professional Sports Clubs and Players

This guide is a general guide regarding the taxation of professional sports clubs and sports players in South Africa. It also refers briefly to the position of visiting professional sports players.

It does not delve into the precise technical and legal detail that is often associated with tax, and should, therefore, not be used as a legal reference.

The professional sports industry is one of the fastest growing industries internationally. The main aim of this guide is to explain the South African tax consequences for professional sports clubs and sports players in South Africa.

A growing number of sports players now earn their livelihood from a diverse range of income sources, sometimes from a number of different countries. Consequently, depending on the nature of the income derived, different tax rules will apply. The tax treatment will also depend on whether players are employed by clubs or are considered to be independent contractors.

Clubs may also earn income from various sources, for example, ticket sales and the sale of advertising rights. As these clubs employ players and other staff, they must comply with the general employees' tax obligations for employers as provided for in the Act. Should the clubs be required to account for employees' tax in relation to their staff and players, they will in all likelihood also be liable to account for SDL and UIF. Clubs will, in most instances, be liable to register as VAT vendors and will therefore incur a range of tax obligations that will be considered in this guide.

This guide is meant to provide clarity on some of the issues and situations experienced by sports clubs and sportspersons in South Africa. Since not every situation can be addressed, the guide seeks to provide guidance on those matters most commonly experienced. Note that each case has to be considered independently and on its particular facts when deciding on the taxability of a specific activity or income source.

9.2. Guide to the Urban Development Zone (UDZ) Allowance (Issue 6)

This guide is a general guide about the urban development zone (UDZ) allowance provided for in section 13*quat* of the Income Tax Act 58 of 1962 (the Act).

The guide, amongst others, provides:

- general guidance regarding the application and interpretation of the provisions of the Act that pertain to the allowance;

- an overview of the income tax consequences associated with the disposal of a building on which the allowance was previously allowed or the ceasing of a taxpayer to use such a building solely for the purposes of that person's trade; and
- particulars of municipalities that have demarcated areas for purposes of the allowance, as well as the process of demarcation that was followed.

In line with many countries, South Africa has a number of urban areas that are impoverished and suffering from extensive urban decay. In order to address these concerns and maintain existing infrastructure, governments internationally have increasingly used tax measures to support efforts aimed at regenerating these urban areas.

In 2003, the Minister of Finance announced a tax incentive in the form of an accelerated depreciation allowance under section 13*quat* to promote investment in 16 designated inner cities, 15 of which now have demarcated UDZs within their boundaries. The core objectives of the allowance are to address dereliction and dilapidation in South Africa's largest cities and to promote urban renewal and development by promoting investment by the private sector in the construction or improvement of commercial and residential buildings, including low-cost housing units situated within demarcated UDZs. The allowance is also intended to encourage investment in highly populated areas, central business districts or inner city environments and areas with existing urban transport infrastructure for trains, buses or taxis.

The allowance, when deducted, reduces the taxable income of a taxpayer. Further, it is not limited to the taxable income of a taxpayer and can create an assessed loss.

Municipalities will be given the opportunity to apply for extensions to existing designated zones and to apply for an additional demarcated UDZ in that municipal zone. Only areas which have a specific and necessary need for an extra zone will be granted UDZ status, and will be subject to Ministerial approval. This allowance is available until 31 March 2020.

In summary:

- Section 13*quat* provides for an accelerated depreciation allowance on the cost of the erection, extension, addition or improvement of any commercial or residential building or a part of a building.
- There are a number of requirements that must be met before the allowance is granted.
- A taxpayer that purchases a building or part of a building directly from a developer will be able to deduct an allowance provided the developer did not deduct any allowance on the cost of the building or part of the building within the usage or rental period. If the developer had used or let the property for longer than three years after completion, the subsequent purchaser may not deduct the allowance (even if the developer did not deduct an allowance) as the developer will no longer constitute a 'developer' as defined.
- In the event of a purchase of a building or part of a building from a developer:
  - 55% of the purchase price of that building or part of a building, in the case of a new building erected, extended or added to by the developer; and
  - 30% of the purchase price of that building or part of a building, in the case of a building improved by the developer,

  will be deemed to be costs incurred by the person for the erection, extension, addition to or improvement of the building or part of the building.
- Depending on the type of development involved, that is, new, improved or low-cost, the allowance is calculated at different rates.
- A lessee that effects improvements to a building that is owned by a party contemplated in section 12N, will, as the deemed owner, be able to deduct an allowance on the costs incurred in erecting, adding to, extending or improving such building.

- Taxpayers deducting the allowance must be in possession of the necessary UDZ forms, a location certificate and, if applicable, a certificate of occupation.
- Attention must be paid to all the reporting requirements provided under section 13*quat*.

9.3. Guide to the Determination of Medical Tax Credits (Issue 9)

This guide provides general guidelines regarding the medical scheme fees tax credit and additional medical expenses tax credit for income tax purposes.

Expenditure of a personal nature may generally not be taken into account in determining a taxpayer's income tax liability, under South Africa's tax system. One of the notable exceptions relates to medical expenditure. South Africa is aligned with the practice in many other countries of granting tax relief for medical expenditure.

There are a number of reasons that tax systems provide such relief. One of the reasons is that serious injury or illness can present taxpayers with disproportionately high medical bills in relation to income, which can be difficult to meet. The resulting hardship affects a number of economic areas for taxpayers, including the ability to settle obligations to the *fiscus*, such as a tax bill.

Historically, South Africa utilised a deduction system to facilitate tax relief for medical expenditure. Allowances, subject to certain limits, were permitted to be deducted from income for contributions to medical schemes, as well as for out-of-pocket medical expenditure.

In 2012, tax relief for medical expenditure began a phased-in conversion from a deduction system to a tax credit system. The reason for the change was to eliminate vertical inequity relating to medical contributions: those at higher marginal tax rates received a larger reduction of tax payable than those on lower marginal rates, in respect of the same amount of medical expenditure. The purpose of the change was to spread tax relief more equally across income groups, thus bringing about horizontal equity – those who pay equal values for medical expenditure receive absolute equal tax relief.

A tax credit system differs from a deduction system in that, instead of permitting a deduction of the medical allowance against a taxpayer's income, the relief is granted as a reduction in tax payable. It therefore operates as a tax rebate.

The new dispensation consists of a two-tier credit system:

- A **medical scheme fees tax credit (MTC)** that applies in respect of qualifying contributions to a medical scheme; and
- An **additional medical expenses tax credit (AMTC)** that applies in respect of other qualifying medical expenses.

The application of the additional medical expenses tax credit system falls into three categories:

- Taxpayers under 65 years of age
- Taxpayers aged 65 years and older
- Taxpayers with a disability

In order to qualify for the AMTC in the '65 years and older' category, the taxpayer must be 65 years or older on the last day of the relevant year of assessment or, had he or she lived, would have been 65 years or older on the last day of the relevant year of assessment.

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How to claim the medical scheme fees tax credit and additional medical expenses tax credit

- Persons registered for income tax
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How to object to the disallowance of an medical scheme fees tax credit or additional medical expenses tax credit

Other information

- Relief of customs and excise duty on a motor vehicle adapted for a physically disabled person

10. DRAFT GUIDES

10.1. Draft guide to understatement penalty

This guide is a general guide on understatement penalties.

The purpose of this guide is to assist people who use it to gain an understanding of the understatement penalties contained in the Tax Administration Act.

The purpose of penalties under the Tax Administration Act is to encourage voluntary compliance and deter unwanted behaviour such as non-compliance and tax evasion. A rational person will not undertake an activity if the punitive sanctions flowing from it outweigh the prospective gain to be had from engaging in it.

11. INDEMNITY

Whilst every reasonable care has gone into the preparation and production of this update, no responsibility for the consequences of any inaccuracies contained herein or for any action undertaken or refrained from taken as a consequence of this update will be accepted.