TAX UPDATE **PREPARED BY: JOHAN KOTZE**

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1. INTRODUCTION

The purpose of this update is to summarise the tax developments that occurred during the second quarter of 2013 (i.e. 1 April 2013 to 30 June 2013), specifically in relation to Income Tax and Value-Added Tax (VAT). Johan Kotze, Bowman Gilfillan's Head of Tax Dispute Resolution, 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 situation. The reader is invited to contact any of the members of Bowman's tax team to discuss their specific concerns and, for that matter, any other tax concerns.

Interest deductions still capture National Treasury's and SARS' minds, more specifically excessive interest and income shifting to low-tax countries. The request for public comments is set out hereunder, and the outcome of which will be incorporated in the forthcoming 2013 TLAB.

The tax case dealing with Business Rescue vis-à-vis SARS' right to rank as a preferred creditor is very interesting, and worth a read.

The case of Computek, certainly, had a known outcome before it went on appeal, dealing with the technicality of a faulty objection.

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 a specific provision. It is however important to note that these publications are not law, but may bind SARS. Taxpayers should nonetheless consider these publications carefully to determine whether, and how, they are actually applicable to their own circumstances.

Enjoy reading on!

2. REQUEST FOR PUBLIC COMMENT – INTEREST ASPECTS

2.1 Proposed limitation against excessive interest deduction

I. Introduction

The annual tax proposals announced by the Minister of Finance in the Budget are given effect by a series of tax bills expected to be tabled during the year, including the Tax Laws Amendment Bill, 2013 ('2013 TLAB') and the Rates and Monetary Amounts and Amendment of Revenue Laws Bill, 2013.

The purpose of this Media Statement is to elicit a first round of public comment on proposed rules to limit excessive interest tax deductions in response to Government's concern over tax schemes that lead to base erosion, first raised in the section 45 proposals in 2011. As noted in a recent paper by the OECD (Base Erosion and Profit Shifting, available on http://www.oecd.org/tax/beps.htm), 'base erosion constitutes a serious risk to tax revenues, tax sovereignty and tax fairness for many countries'. Base erosion includes profit shifting schemes, like excessive deductions and income-shifting to low-tax countries.

The outcome of this first round of consultation will be incorporated thereafter into the forthcoming 2013 TLAB, expected to be released for public comment (and parliamentary hearings) in June 2013.

II. Background

Over the past several years, tax schemes by some corporates have become an increasing concern locally as well as globally. The recent OECD paper notes that '[w]hile there are many ways in which domestic tax bases can be eroded, a significant source of base erosion is profit shifting'. One of the most significant types of base erosion in South Africa comes in the form of excessive deductions by some corporates with income effectively shifted to a no-tax or low-tax jurisdiction or converted to a different type of income

in another jurisdiction. These deductions are typically channeled as interest, royalties, service fees and insurance premiums. Of greatest concern is *excessive* deductible interest. In terms of excessive deductible interest, Government has identified four recurring concerns:

1. Hybrid Debt:

    Hybrid debt instruments essentially involve instruments with the label of debt but with substantive features being more indicative of shares (equity). These instruments are typically labelled as debt in South Africa so that payments are deductible. However, these instruments are often labelled as equity in the other jurisdiction so as to benefit from cross-border arbitrage. Most of these instruments would otherwise be labelled as shares if tax were not a consideration.

2. Connected person debt:

    The relationship between creditor and debtor often becomes blurred once both parties form part of the same economic unit. This situation often arises when a parent company lends money to a wholly owned subsidiary. In this situation, the terms of the instrument are somewhat irrelevant because both parties can change the terms at will to serve the overall interests of the group. As a result, the debt label for instruments in these circumstances is often driven by tax and other regulatory factors; whereas, the payments often represent substantive capital contributions to be repaid only if the subsidiary at issue is profitable.

3. Transfer pricing:

    In a cross-border context, excessive interest can arise if the interest yield is driven by tax considerations as opposed to arm's length commercial reasons, especially if the debtor and creditor are connected persons. Also of concern is 'lending' that would not arise in a commercial context. In these cases, transfer pricing adjustments can be used to eliminate debt with excessive interest or excessive debt.

4. Acquisition debt:

While the need to obtain debt financing for acquisitions is well-understood, excessive debt becomes problematic because excessive debt (or over-gearing) is often anchored on the expectation that the interest will be paid from future profits. If allowed to extremes, the interest on the debt often eliminates taxable profits for years to come. Acquisition debt of greatest concern is mezzanine and subordinated debt (i.e. debt containing an escalating number of equity features). Besides tax concerns, excessive debt gives rise to governance concerns with the excessive debt creating excessive risk (as a number of entities and economies have 'painfully' discovered in recent years).

III. Preliminary proposal

In order to curb excessive interest deductions as outlined above, a four-part proposal is being considered for inclusion in the forthcoming draft of the Taxation Laws Amendment Bill, 2013. These proposals are an outgrowth of the section 45 debate arising in 2011 and are partially outlined in the 2013 Budget Review.

A. Hybrid debt instruments

The Income Tax Act ('the Act') presently contains certain anti-avoidance rules that seek to curb the use of hybrid debt instruments. These rules disallow an interest deduction in the hands of the payor and the instrument remains debt for purposes of the Act. This disallowance of a deduction occurs when the debt instrument has conversion features. However, for the rule to apply, the conversion feature must be exercisable within three years from the date when the debt instrument is issued.

Given the weaknesses in the current system, a broader set of hybrid rules were proposed (as contained in the draft Taxation Laws Amendment Bill, 2012). These hybrid rules fell into two parts. The first part recharacterises certain debt instruments entirely as equity, meaning that the 'debt principal' would be deemed to be the

underlying shares and the 'interest' yield would be deemed to be distributions (dividends and capital distributions). The second part merely treats certain 'interest' yields as dividends. While the 2012 proposed rules targeted many of the objects intended, the triggers and application of those rules were overly broad, thereby adding unnecessary complexities and adversely impacting commercial non-tax driven instruments. These rules were accordingly removed from the final 2012 legislation for reconsideration.

Attached is a revised version of the proposed 2012 hybrid rules that have been adjusted based on the 2012 comments received (see Annexure A (section 8F draft legislation), B (section 8FA draft legislation) and C (corresponding explanatory memorandum)). These revised rules mainly target: (i) non-redeemable debt, (ii) debt that is convertible to shares at the instance of the company issuer, (iii) debt with yields not interest-related, and (iv) debt with repayment terms or yields conditional on the solvency of the company issuer. In terms of impact, the rules simply deem interest to be dividends for both the issuer and holder without creating other deemed changes. The timing triggers associated with hybrid debt have also been clarified. Lastly, under the revised exceptions, exemptions will exist for: (i) regulatory hybrid debt (e.g. Tier II debt) of banks, (ii) subordinated hybrid debt of long-term and short-term insurers, and (iii) private and unlimited liability debtor companies owing sums to resident natural persons.

B. Debt owed to untaxed entities within the same economic unit

As noted above, debts between entities of the same economic group are problematic because both the debtor and the creditor are part of the same economic unit. Because of this unity, the actual terms of the instruments are often not fully indicative when determining the substance of an instrument because both entities will act in unison to change the terms of the instrument as the need arises. Therefore, even if an instrument has no equity features,

excessive debt between these entities remains a concern to the fiscus, especially if the creditor falls outside the tax net.

In order to curb this concern, the aggregate deductions for interest associated with debt between certain entities of the same group will be limited regardless of the terms associated with that debt. More specifically, if a company pays interest to another entity within the same IFRS group and the interest is untaxed (or taxed at a lower rate) when received or accrued by the other entity, the interest will be subject to an interest limitation. This interest limitation will similarly apply if the untaxed IFRS group entity guarantees or provides other security in respect of debt owed by the company debtor. In either of these circumstances, the deduction for interest paid or incurred in respect of the debt will be limited to:

- 40 per cent of the debtor's taxable income (disregarding interest received, accrued, paid or incurred); plus
- Interest received or accrued; reduced by
- Interest paid or incurred in respect of debt falling outside the limitation.

To the extent interest paid or incurred on debt between IFRS group entities exceeds the limitation, the excess can be carried forward for up to five years (remaining subject to the limitation).

C. Transfer pricing interpretation note and potential safe harbour

As a general matter, cross-border interest between connected persons are subject to the facts and circumstances restrictions of transfer pricing as outlined in the proposed interpretation note (see Draft Interpretation Note on: 'Determination of the taxable income of certain persons from international transactions: thin capitalisation'). However, given the general restrictions on debt as now proposed, the need for transfer pricing to address excessive debt and hybrid debt is reduced. Therefore, under consideration is a safe harbour that will be added to the transfer pricing rules (e.g. via a binding general ruling). In order to fall within this potential safe harbour,

interest on connected person cross-border debt must satisfy the following two criteria:

- Firstly, interest on the connected person debt may not exceed 30 per cent of taxable income (with no adjustment for other interest received, accrued, interest paid or incurred); and
- Secondly, the interest rate depends on the currency denomination of the loan. The interest on the debt may not exceed the foreign equivalent of the South African prime rate if denominated in foreign currency. The interest rate on the debt may not exceed the South African prime rate if denominated in Rand.

Under current law, it should be noted that amounts viewed as excessive for transfer pricing purposes are permanently denied (not merely subject to an ongoing limitation on a carryover basis).

D. Acquisition debt

Under current law, acquisition debt is subject to discretionary limitations as determined by SARS. These limitations are designed to target potential base erosion caused by excessive and hybrid debt (and to prevent the interest deduction from becoming a facilitator of unwarranted risk to the economy in the form of excessive debt). However, this discretionary system was never intended to be permanent. Taxpayers seeking debt-financing when attempting to acquire control of companies cannot be expected to obtain pre-approval from SARS in the long-run; deal-making of this nature needs clear guidelines when seeking finance before core negotiations can be undertaken.

In view of these concerns, the discretionary system will be terminated in favour of a more concrete set of rules. Under the new system, debt used for the acquisition of the assets of target companies via an indirect section 45 acquisition or a direct section 24O acquisition will be subject to a fixed overall limitation roughly comparable to the untaxed group entity limitation. This limitation will

ensure that acquisition debt does not eliminate excessive amounts of taxable income of the acquiring or target company for an indefinite period into the future.

More specifically, if an acquirer acquires the assets of a target company through the use of section 45, the deduction for interest paid or incurred in respect of the debt will be limited to:

- 40 per cent of the debtor's taxable income (before taking into account interest received or accrued and interest paid or incurred); plus
- Interest received or accrued; less
- Interest paid or incurred in respect of debt falling outside the limitation.

To the extent the interest paid or incurred on the debt used for the acquisition exceeds the limitation, the excess can be carried forward for up to five years (remaining subject to the limitation).

The interest limitation in the case of a section 24O acquisition works in similar fashion with the deductible interest of the acquiring company being limited to 40 per cent of the taxable income of the target company (taking into account the interest adjustments). The 40 per cent taxable income limitation will be further adjusted in accordance with the percentage stake being acquired if the acquirer is not acquiring all the shares of Target Company. For instance if the acquirer acquires 80 per cent of the shares of Target Company, the limit will be 80 per cent of 40 per cent of the target company's taxable income.

In addition, in the context of a section 24O acquisition, if the acquisition debt was funded or secured by another entity within the same IFRS group and the interest thereon is untaxed when received or accrued by that other entity, the limitation will be the lesser of (i) 40 per cent of the target company's taxable income or, (ii) 40 per cent of the acquirer's taxable income. The limitation method applicable must be further reduced to reflect so much of the period

that the acquired stake was held in relation to the acquiring company's year of assessment at issue. For instance where the acquiring company acquires shares of the target company half way through the acquiring company's year of assessment, the applicable 40 per cent taxable income limit must be further reduced by 50 per cent.

Lastly, it is recognised that this overall limitation may be unduly restrictive if the target assets or the assets of the target company consist of sizeable amounts of immovable property generating rental income because commercial lenders are typically more willing to lend greater proportions for acquisitions of this nature. In light of this recognition, rental income from immovable property will be subject to a notional 50 per cent uplift for purposes of determining the impact of the limitation in respect of acquisition debt.

2.2 Draft explanatory memorandum: Anti-hybrid debt instrument recharacterisation rules

I. Background

A. Overview

In the area of corporate financing, there are three basic sources of finance – equity, debt and retained profits. For commercial purposes, debt and equity are the key sources of external finance. As a general matter, debt is redeemable with a yield based on the time value-of-money (e.g. interest), and payment obligations exist without regard to the performance of the debtor company (i.e. payments are required without regard to profits or cash available). On the other hand, equity is typically non-redeemable with the yield (i.e. dividends) depending on the performance of the company (i.e. profits), and payment obligations are discretionary or can be deferred without giving rise to legal claims.

For tax purposes, interest on debt is generally deductible in the hands of the payor (e.g. if incurred in the production of income) and included as ordinary revenue in the hands of the recipient. On the other hand, dividends are not deductible by the payor nor are they includible in the hands of the shareholder. However, dividends may be subject to the Dividends Tax.

B Hybrid Instruments

Current law contains anti-avoidance rules that deal with hybrid debt instruments (i.e. debt instruments with equity features) as well as hybrid equity instruments (equity instruments with debt features). In the case of hybrid debt instruments, the anti-avoidance rules seek to re-characterise interest as dividends in the hands of the payor. However, the instrument otherwise remains a debt instrument for all other purposes of the Income Tax Act (including interest treatment for amounts received by the payee).

This recharacterisation potentially occurs when: (i) the debtor is obliged to convert the instrument to shares, (ii) the issuer has an option to convert the debt instrument to shares, (iii) the issuer can force the holder to reinvest in shares, or (iv) the holder has a deep-in-the money right of conversion. However, for this recharacterisation to apply, the conversion obligation or right must be exercisable within a three-year period from date of issue.

II. Reasons for change

When determining the debt versus equity character of an instrument, it is widely believed that most of the tax law follows form. This focus on form seemingly provides taxpayers with the freedom to choose a label for an instrument with consequential tax benefits without regard to (economic) substance. This freedom poses a risk to the *fiscus* because certain taxpayers consistently choose a combination of features that bring about unintended tax benefits. The key driver for this form of tax planning is the issuer's desire to

obtain an interest deduction for payment to financiers (as opposed to non-deductible payments of dividends).

When making payments to exempt persons, taxpayers have even a greater tendency to classify share-type instruments as debt in order to obtain an interest deduction, knowing the recipient is exempt. In this instance, the debt label is commercially neutral for the taxpayer, but the result is negative for the *fiscus* because there is no matching of deductions with inclusions.

While anti-avoidance rules exist as outlined above for debt conversions, artificial classifications go beyond the use of mere conversion features. For instance, an instrument lacking a maturity date for repayment is a strongly questionable form of debt. Moreover, even the conversion focus presently existing within the hybrid debt rules is too narrow – being limited to a three-year period.

III. Proposal

A. Overview

In order to reduce the scope for the creation of equity that is artificially disguised as debt, a two-fold regime is proposed for domestic company issuers. One set of rules focuses on features relating to the nature of the instrument itself (i.e. the corpus); the second set of rules focuses on the nature of the yield. In making these rules, it is understood that the features distinguishing debt from equity are varied and are often contextual. Nonetheless, the proposal takes aim at domestic companies that issue stated debt instruments so as to artificially generate interest deductions if clear-cut equity features exist when viewed in isolation.

In term of the anti-avoidance rules relating to the instrument (i.e. the corpus), the proposal focuses on debt-labelled instruments that (i) have features indicating that redemption for cash is unlikely within a reasonable period; or (ii) have features that enable a conversion into shares. These features will be tested on a continuous basis (i.e. not once off at the date of issue but at any time thereafter).

In terms of the anti-avoidance rules focusing on yield, the debt yield must be based on time value of money (e.g. a rate of interest) – not other factors. Lack of payment due to company insolvency is also a problem.

The effect of the application of both these anti-avoidance rules is that some or all of the yield will be treated as dividends. If the focus relates to the debt instrument itself, the full yield associated with the instrument will be treated dividends. If the focus relates solely to the yield, only the yield at issue will be treated as a dividend.

Lastly, the proposed regime will contain some exceptions to simplify administration and ensure that South Africa is not left in an uncompetitive situation. These exceptions include exceptions for certain forms of regulatory capital issued by regulated intermediaries as well as for debt owed to resident natural persons by certain ‘for profit companies’..

B. Instrument recharacterisation (section 8F)

1. Features

A key feature of debt is the holder’s ability to redeem the capital amount loaned within a reasonable period. Instruments without this key feature operate more like equity (i.e. shares), and the yield on these instruments will accordingly be treated as dividends. In order to avoid this deemed share treatment, the debt instrument (i.e. the corpus) must be fully redeemable in cash within 30 years from the year of assessment at issue (taking into account the terms of the instrument itself or any side arrangement).

The debt recharacterisation rules also target certain mechanisms commonly used to avoid required redemption. Hence, conditions allowing for the issuer to repay the debt in the form of equity (e.g. the shares of the issuer or group member) will also cause a recharacterisation. Moreover, the obligation to repay will be disregarded if conditional upon the solvency of the debtor. Like the 30-year redemption rule, these anti-avoidance rules take into

account not only the instrument itself, but side arrangements as well.

As stated above, the test for whether a debt is commercially real or artificial must be tested continuously – not merely from the date of issue or modification. If the conditions of the debt change, the debt becomes subject to the avoidance rules at the time of the change (and not before).

2. Impact of recharacterisation

If an instrument is recharacterised as outlined above, stated interest in relation to the instrument will be treated as a dividend declared by the payor as well as dividends in the hands of the payee as long as the instrument retains its hybrid features. As a result, it will also be specifically provided that the payor will no longer obtain any deduction for the stated interest. The stated interest will be treated as a dividend (potentially subject to the Dividends Tax depending on circumstances), and the interest accrual and incurral rules (e.g. section 24J) will no longer be applicable to the hybrid debt instrument.

C. Yield recharacterisation (section 8FA)

In some circumstances, the debt/equity recharacterisation will focus on the yield of the instrument without looking to the whole. Under these rules, the recharacterisation will deem the particular yield at issue to be a dividend (nothing more). In order to breach this standard, the yield at issue (taking into account all agreements) must have one of the following features:

- The yield must not be determined with reference to a specified rate of interest (e.g. instead being based on company profits) or time-value-of-money principles; or
- The timing of payment must not be subject to the solvency of the issuer of the instrument.

In terms of yield, stated interest in relation to the instrument will be treated as a dividend declared by the payor as well as dividends in the hands of the payee. It will also be specifically provided that the payor will no longer obtain any deduction for the stated interest. The stated interest will be treated as a dividend (potentially subject to the Dividends Tax depending on circumstances), and the interest accrual and incurral rules (i.e. in section 24J) will no longer be applicable in respect of a hybrid debt instrument. The instrument itself will retain its debt characterisation (unless otherwise tainted) and other payments will have to be tested separately for debt/equity recharacterisation.

D. Exemptions from reclassification

The anti-hybrid rules will be subject to certain exemptions as a matter of policy. In particular, exemptions will exist for debt owed to resident natural persons by private companies and personal liability companies as well as certain regulated debt issued by banks and insurers.

1. Relief for debt owed to resident natural persons

Private companies and personal liabilities companies (i.e. profit companies that are not public or state-owned) under the Companies Act (2008) will be eligible for relief if the debt is owed to natural persons that are South African residents. It is understood that the use of debt with share-like features is a common practice for small businesses for a variety of reasons and that the only significant tax benefit is use of the interest exemption for natural persons.

2. Relief for regulated bank capital

Banks often issue various forms of capital, including Tier I (straight equity) and Tier II (debt with equity features) capital. Increased pressure is being placed on the banks to increase these forms of capital via the international banking Basel standards. While it is understood that certain forms of Tier II capital will probably be in violation of the hybrid recharacterisation rules, these rules will be

waived for Tier I and Tier II capital so as not to place further pressure on the cost of banking capital given the global regulatory uncertainties in this regard. It is also understood that tax systems of other countries similarly exempt these forms of debt from potential recharacterisation on similar policy grounds.

3. Relief for regulated insurer capital

Short-term and long-term insurers are required to maintain a sound financial condition by maintaining adequate levels of assets to cover their regulated liability and capital requirements. As a safeguard mechanism, the redemption of certain subordinated debt instruments issued by short-term and long-term insurers is subject to approval by the Registrar of short term and long term insurance (respectively). These forms of debt operate roughly similar to Tier I and Tier II debt and will accordingly be exempt from the hybrid debt instrument reclassification rules (but not the hybrid interest rules).

IV. Effective dates

The proposed hybrid instrument recharacterisation rules will come into effective in the case of amounts accrued or incurred on or after 1 January 2014.

2.3 Section 8F

The Income Tax Act is hereby proposed to be amended by the substitution for section 8F of the following section:

‘**Amounts paid, incurred, received or accrued in respect of hybrid debt instruments deemed to be in respect of shares**

8F. (1) For the purposes of this section—

‘instrument’ means any form of interest-bearing arrangement or debt;

‘hybrid debt instrument’ means any instrument in respect of which a company owes an amount during a year of assessment if in terms of any arrangement—

(a) the company is not obliged to repay all amounts in respect of that instrument in cash in full within 30 years from the end of that year of assessment;

(b) the company may during that year of assessment—

(i) convert that amount (or any part thereof) in respect of that instrument to; or

(ii) exchange that amount (or any part thereof) in respect of that instrument for,

shares in that company or in any other company that forms part of the same group of companies as that company; or

(c) the obligation to pay that amount or any part thereof in respect of that instrument is conditional upon the solvency of the company.

(2) Any amount of interest in respect of a hybrid debt instrument—

(a) is deemed for the purposes of this Act to be a dividend declared by the company;

(b) is not deductible in terms of this Act; and

(c) must not be included in gross income in terms of section 24J.

(3) This section does not apply to any instrument—

(a) in respect of which all amounts are owed to a natural person that is a resident by a profit company, as contemplated in the Companies Act, that is not a public or state-owned company as contemplated in that Act;

(b) that constitutes a tier 1 or tier 2 capital instrument referred to in the regulations issued in terms of section 90 of the Banks Act (contained in Government Notice No. R.1029 published in *Government Gazette* No. 35950 of 12 December 2012), owed by a bank as defined in section 1 of that Act to any person that is not a connected person in relation to that bank; or

(c) that is subject to approval by the Registrar—

(i) contemplated in the Short-term Insurance Act in accordance with the conditions that the Registrar determines, in terms of section 23*(a)*(i) of that Act which is owed by a short-term insurer defined in that Act; or

(ii) contemplated in the Long-term Insurance Act in accordance with the conditions that the Registrar determines in terms of section 24*(a)*(i) of that Act which is owed by a long-term insurer defined in that Act.'.

Subsection (1) comes into operation on 1 January 2014 and applies in respect of amounts incurred or accrued on or after that date.

2.4 Section 8FA

The Income Tax Act is hereby proposed to be amended by the substitution for section 8FA of the following section:

'**Hybrid interest deemed to be dividends**

8FA. (1) For the purposes of this section—

'hybrid interest' means any interest in respect of a debt owed by any company that is a resident if—

(a) the amount of that interest is not determined with reference to—

(i) a specified rate of interest; or

(ii) the time value of money; or

(b) the obligation to pay any amount owing in respect of that interest is conditional upon the solvency of that company.

(2) Any amount of hybrid interest—

(a) is deemed for purposes of this Act to be a dividend declared by the company;

(b) is not deductible in terms of this Act; and

(c) must not be included in gross income in terms of section 24J.

(3) This section does not apply to any interest in respect of a debt—

(a) owed to a natural person that is a resident by a profit company as contemplated in the Companies Act that is not a public or state-owned company as contemplated in the Companies Act; or

(b) that constitutes a tier 1 or tier 2 capital instrument referred to in the regulations issued in terms of section 90 of the Banks Act (contained in Government Notice No. R.1029 published in *Government Gazette* No. 35950 of 12 December 2012), owed by a bank as defined in section 1 of that Act to any person that is not a connected person in relation to that bank.'

Subsection (1) comes into operation on 1 January 2014 and applies in respect of amounts incurred or accrued on or after that date.

3. REGULATIONS / NOTICES

3.1 Returns of information to be submitted by third parties in terms of section 26 of TAAct

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

- Banks regulated by the Registrar of Banks in terms of the Banks Act, 1990, or the Mutual Banks Act, 1993;
- Co-operative Banks regulated by the Co-operative Banks Development Agency in terms of the Co-operative Banks Act, 2007;
- The South African Postbank Limited (Postbank) regulated in terms of the South African Postbank Limited Act, 2010;
- 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 (including a 'financial institution' as defined in the Financial Services Board Act, 1990, other than an institution described in paragraph *(a)*(i) of the definition;

- Companies listed on the JSE, and connected persons in relation to the companies, that issue bonds, debentures or similar financial instruments;
- State-owned companies, as defined in section 1 of the Companies Act, 2008, that issue bonds, debentures or similar financial instruments;
- 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;
- Any person (including a co-operative as defined in section 1 of the Income Tax Act, 1962) who purchases any livestock, produce, timber, ore, mineral or precious stones from a primary producer other than on a retail basis;
- Any medical scheme registered under section 24(1) of the Medical Schemes Act, 1998;
- Any person, who for their own account carries on the 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 an investment, interest or the rental of property; and
- Any person, who for their own account practices 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 an investment, interest or the rental of property.

Every person mention in Column 1 must submit a third party return that relates to the information specified in Column 2, in the form specified in Column 3 of the following table:

Column 1	Column 2	Column 3
Person mentioned in paragraph	**Information concerning**	**Form**
2.1, 2.2, 2.3, 2.4, 2.10 and 2.11	Amounts paid or received in respect of, or by way of any investment, rental of immovable property, interest or royalty; and Transactions that are recorded in an account maintained for another person (i.e. transactional accounts like bank accounts).	1T3(b); or A data file compiled in accordance with SARS' Business Requirement Specification: 1T3 Data Submission
2.1, 2.2, 2.3, 2.4, 2.5, 2.6 and 2.7	Amounts paid in respect of the purchase and disposal of financial instruments.	1T3(c); or A data-file 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 or income protection policy.	IT3(f); or A data-file 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(f); or A data-file 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, precious stones, or by way of a bonus.	IT3(e); or A data-file compiled in accordance with SARS' Business Requirement Specification: IT3 Data Submission

2.9	Contributions made by persons in respect of a medical scheme, and all expenses paid for a person by a medical scheme.	IT3(f); or A data-file compiled in accordance with SARS' Business Requirement Specification: Medical Scheme Contributions

The return mentioned in the Table, containing all information required in respect of the period from:

- March to 31 August, must be submitted by 31 October; and
- March to the end of February, must be submitted by 31 May.

If a third party return comprises 20 or fewer detailed records, the declaration portion of the return and the detailed portion of the return must be submitted:

- electronically using the SARS eFiling platform; or
- manually to the SARS office closest to the person's place of business.

If a third party return comprises 21 to 50 000 detailed records, the declaration portion of the return must be submitted electronically using the SARS eFiling platform and the detailed portion of the return must be submitted electronically using the SARS hypertext transfer protocol secure (https) bulk data file platform.

If a third party return comprises more than 50 000 detailed records the declaration portion of the return must be submitted electronically using the SARS eFiling platform and the detailed portion of the return must be submitted electronically using the SARS managed data transfer platform.

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. TAX CASES

4.1 C:SARS v Beginsel No and Others

Third Respondent, a company, conducted the business of road transport and during 2011 it experienced financial difficulties and was unable to pay its debts as and when they fell due and this resulted in creditors taking legal action against the company and thereafter an order was made by the South Gauteng High Court placing the company under provisional liquidation.

Following the aforementioned proceeding and pursuant to an application by three shareholders of the company, who together owned 95% of its shares, the Western Cape High Court ordered that Third Respondent be placed under supervision and that business rescue proceedings commence, as contemplated in Chapter 6 of the Companies Act, 2008, (the Companies Act) which came into operation on 1 May 2011.

One of the declared purposes of the Companies Act is to provide for the efficient rescue and recovery of financially distressed companies in a manner that balances the rights and interests of all relevant stakeholders and at the heart of business rescue proceedings is the preparation of a business rescue plan by a business rescue practitioner for consideration and possible adoption by the relevant stakeholders and this plan should set the course for rescuing the company by achieving the goals set out in section 128(1)(*b*) of the Companies Act.

First and Second Respondents ('the BRPs') were appointed as business rescue practitioners to conduct the business of the company with all powers and duties entrusted to them in terms of the Companies Act.

The primary objective of the business rescue proceedings, stated in the application, was to restore the company to solvency and to rescue the business as a going concern and it was not anticipated at that juncture that the second aim highlighted in section 128(1)(*b*)(iii) of the Companies Act, to implement a business rescue plan that would result in a better return for the company's creditors or shareholders than would result from the immediate liquidation thereof, would have to be pursued, although it was recognised as a possibility.

At the first meeting of creditors of the company it was resolved that the BRPs should take the necessary steps to prepare and publish a business

rescue plan for the company and at that stage the Applicant, being the Commissioner for SARS, had provided the BRPs with proof of the company's indebtedness to it, which had then amounted to R11 194 677.39, for outstanding value-added tax, employees' tax, skills development levy, unemployment insurance contributions, penalties and interest.

Subsequent thereto the BRPs had made several unsuccessful attempts to reach a compromise with SARS and at all material times during these negotiations the BRPs were of the view that SARS was a preferent creditor in the business rescue proceedings.

The BRPs advised creditors that the company was experiencing problems in securing work and that it had suffered a loss of about R300 000 in February 2012 and thereafter the creditors were informed that the company's estimated loss in March 2012 amounted to R2.9 million, mainly due to a significant decline in the volumes of fuel to be transported.

A further extension for the publication of the business rescue plan was applied for and granted and eventually the proposed business rescue plan was circulated under cover of a letter dated 18 June 2012.

The proposed business rescue plan informed interested parties that as a result of the changed circumstances of the company, it had not been possible to obtain a purchaser for the entire business of the company as a going concern, or to present a business rescue plan which would trade the company out of its difficulties and the company would accordingly cease trading on 31 July 2012.

The BRPs expressed the view that, having taken legal advice, SARS was not a preferred creditor in terms of business rescue proceedings and it was consequently reflected as a concurrent creditor in the annexures to the business rescue plan, SARS' claim being valued at R12 392 706.26. It was further apparent from the business rescue plan that, if the distributions it envisaged were made, SARS would not enjoy preference over any of the other creditors – in this regard the business rescue plan stated that claims would be made in the 'usual order of preference', i.e. payment of any

secured claims, followed by preferent claims of employees in agreed amounts and thereafter payment of the concurrent claims, as contemplated in section 150(2)(*b*)(v) of the Companies Act.

Applicant, in a subsequent letter to the BRPs, insisted that it should be ranked as a preferent creditor and that, consequently, the meeting of creditors scheduled for 17 July 2012, should be postponed so that the BRPs could submit a revised business rescue plan for consideration by all affected parties, taking into account the attitude of itself regarding its status as a preferent creditor.

The BRPs refused Applicant's request for a postponement of the meeting of creditors and informed Applicant that they had taken senior counsel's advice, to the effect that the classification of creditors in the Insolvency Act was not applicable to Chapter 6 of the Companies Act, which contained no statutory preferences such as are to be found in sections 96–102 of the Insolvency Act and they added that, irrespective of whether Applicant was a preferent or concurrent creditor, it did not impact on SARS' voting on the proposed business rescue plan and that the implementation of the plan should not be interrupted.

Applicant, at the creditors' meeting of 17 July 2012, voted against the adoption of the business rescue plan but 87% of creditors' voting interests were in favour of the adoption of the proposed business rescue plan.

Applicant then applied urgently for the following substantive relief:

- An order declaring unlawful and invalid the decision taken at the meeting of creditors of the company held on 17 July 2012 to approve the business rescue plan of the company proposed by the BRPs;
- An order interdicting the BRPs from distributing any monies of the company pursuant to the business rescue plan;
- An order declaring that the BRPs were obliged to take the steps as specified in section 141(2)(*a*)(i) and (ii) of the Companies Act, *viz* to apply to court for an order discontinuing the business rescue proceedings and placing the company in liquidation.

Applicant accepted that Chapter 6 of the Companies Act did not oblige the BRPs to propose a business rescue plan which conferred on it a preference upon the distribution of the free residue over the other unsecured creditors but Applicant contended that Chapter 6 of the Companies Act also did not oblige the BRPs to treat it as a concurrent creditor and in this regard it contended that section 150(2)(*b*)(v) of the Companies Act permitted a business rescue plan to create and specify the order of preference in which the proceeds of property will be applied to pay creditors if the business rescue plan is adopted, subject to the preferences conferred by section 135 of the Companies Act on the different classes of post-commencement finance creditors, described in that section and it accordingly contended that there was no reason why it could not have been specified as a preferent creditor and in such event it would obviously have voted for the business rescue plan as its interests would have remained protected.

Applicant further contended that its status as a preferent creditor under section 99 of the Insolvency Act had an important implication for the voting on a business rescue plan and submitted that, by treating its voting power as the same as that of the concurrent creditors, who would get nothing if the company was liquidated, despite section 145(4) of the Companies Act, and by ranking its claim as the same as those of the concurrent creditors, despite the possibility of giving it preference under section 150(2)(*b*)(v) of the Companies Act, the business rescue plan was adopted and facilitated what amounted to a liquidation of the company, in which Applicant was deprived, against its will, of the statutory preference to which it was entitled when companies were liquidated and in the result the adoption of the business rescue plan by the creditors on 17 July 2012 was unlawful and invalid.

Applicant contended that all preferent creditors, as contemplated by sections 96 to 102 of the Insolvency Act, were to be categorised as unsecured creditors under section 145(4)(*a*) of the Companies Act, while all other concurrent creditors, as envisaged by section 103 of the Insolvency Act, were concurrent creditors who would be subordinated on liquidation, as envisaged by section 145(4)(*b*) of the Companies Act.

Judge Fourie held the following:

As to whether Applicant was to be treated as a preferent creditor in business rescue proceedings

(i) That SARS' construction of the provisions of section 145(4) of the Companies Act is not only contrary to the ordinary grammatical meaning of the words used in the said section, but also leads to an illogical result that fails to balance the rights and interests of all relevant stakeholders, as envisaged in section 7(*k*) of the Companies Act.

(ii) That the business rescue provisions contained in Chapter 6 of the Companies Act do provide for certain preferences in respect of claims of creditors but no statutory preferences are created in Chapter 6 of the Companies Act, such as are contained in sections 96 to 102 of the Insolvency Act and it would have been expected that, if it were the intention of the legislature to confer a preference on SARS in business rescue proceedings, it would have made such intention clear and this could easily have been done but no trace of such an intention on the part of the legislature is found in the Companies Act; moreover, the language of the aforesaid provisions of the Companies Act, read in context, and having regard to the purpose of business rescue proceedings, justified only one conclusion, namely that SARS was not, by virtue of its preferent status conferred by section 99 of the Insolvency Act, a preferent creditor for purposes of business rescue proceedings under the Companies Act.

(iii) That section 145(4)(*a*) of the Companies Act 71 of 2008 referred to secured or unsecured creditors who have a voting interest equal to the value of the amount owed to them by the company and this categorisation of creditors was uncontentious and well-known in legal parlance. Secured creditors are those who hold security over the company's property, such as a lien or mortgage bond and unsecured creditors are those whose claims are not secured, including concurrent creditors. The unsecured creditors are either preferent or concurrent creditors and the term 'preferent creditor', used in the wide

sense, refers to any creditor who has a right to receive payment before other creditors and to this extent a secured creditor also qualified as a preferent creditor.

(iv) That it followed from the aforesaid that our insolvency law in practice recognised unsecured creditors as comprising, *inter alia*, unsecured preferent creditors and unsecured non-preferent, or concurrent, creditors. There was, accordingly, no reason to interpret the phrase 'unsecured creditor' in section 145(4)(*a*) as including only unsecured preferent creditors, but not unsecured non-preferent or concurrent creditors and such an interpretation was clearly contrary to the ordinary meaning of the phrase 'unsecured creditor', which, according to its ordinary meaning, included all concurrent creditors, whether preferent or non-preferent.

(v) That, hence, the term 'unsecured creditor' should be read as including non-preferent concurrent creditors since the legislature must be assumed to have intended the term to bear its ordinary meaning in circumstances where there is no indication at all in the Companies Act that a different meaning is to be assigned to it.

(vi) That the reference in section 145(4)(*b*) of the Companies Act to a concurrent creditor 'who would be subordinated in a liquidation' did not attach to all concurrent creditors but only to those concurrent creditors who had subordinated their claims in a liquidation in terms of a subordination or back-ranking agreement and this is the ordinary meaning of the concept of subordination which is similarly uncontentious and well-known in South African law, and, in particular, in our insolvency law.

(vii) That, in the result, in terms of section 145(4) of the Companies Act, each concurrent creditor, save for the category of concurrent creditors who would be subordinated in a liquidation by virtue of a prior existing subordination agreement, has a voting interest equal to the value of the amount owed to that creditor by the company and, therefore, Applicant would enjoy no greater voting interest than the other concurrent creditors of the company, with the result that there was no

basis upon which to impeach the voting procedure followed in the adoption of the business rescue plan.

As to the content of the business rescue plan

(viii) That section 150(2) of the Companies Act provided that a proposed business rescue plan must contain all the information reasonably required to facilitate affected persons in deciding whether or not to accept or reject the plan and to this end the section details certain background information, proposals, assumptions and conditions which the business rescue plan should contain.

(ix) That a perusal of section 150(2) of the Companies Act showed that the legislature had prescribed the content of a proposed business rescue plan in general terms and the content could, by its very nature, not be exactly and precisely circumscribed as it would differ from case to case, depending on the peculiar circumstances in which the distressed company found itself and it followed that, upon a proper construction of section 150(2), substantial compliance with the requirements of the section would suffice and this would mean that, where sufficient information, along the lines envisaged by section 150(2), had been provided to enable interested parties to take an informed decision in considering whether a proposed business rescue plan should be adopted or rejected, there would have been substantial compliance.

(x) That although the detail regarding the identity of the creditors referred to in the Companies Act may not have been provided, there had been substantial compliance, in the sense that the information provided in the annexures, read with the plan, enabled the interested creditors to decide whether to accept or reject the business rescue plan.

(xi) That, accordingly, there was no merit in the submission that the business rescue plan was invalid and unlawful due to the alleged non-compliance with the requirements of section 150 of the Companies Act.

As to whether business rescue proceedings should continue.

(xii) That the court accepted, without deciding, that it had the power to intervene where it is shown that the BRPs have committed a material mistake in concluding that the continued implementation of the business rescue plan would result in a better return for the creditors of the company, as envisaged in section 128(1)(*b*)(iii) of the Companies Act.

(xiii) That, in practical terms, nothing will be achieved if the business rescue proceedings are now to be converted into a liquidation, and, on the contrary, it was inevitable that, by placing the company in liquidation, all that would be achieved would be to add the costs of liquidation to those already incurred in the business rescue proceedings.

(xiv) That if the business rescue proceedings would now be terminated, the liquidation process would have to be re-introduced in terms of section 131(6) of the Companies Act and this would entail, *inter alia*, the appointment of liquidators, the proof of claims by some two hundred creditors, meetings of creditors and the preparation of a liquidation and distribution account. However, the court was satisfied that the continuation of the business rescue proceedings would result in a better return for the company's creditors as a whole, than would result from the re-introduction of the liquidation process.

(xv) That there was no practical reason for the conversion of the business rescue proceedings to liquidation and on a conspectus of the evidence as a whole, there was much to be said for the BRPs' contention that the only purpose of converting this business rescue to liquidation, would be to ensure that Applicant was treated as a preferent creditor.

(xvi) That, accordingly, the BRPs should not be ordered to take the steps specified in section 141(2)(*a*)(i) and (ii) of the Companies Act.

Application dismissed.

4.2 Computek (Pty) Ltd v C:SARS

Computek had been the subject of a VAT audit conducted by SARS in respect of its tax affairs and the audit revealed that it had under-declared and, in consequence, had underpaid value-added tax to SARS in terms of the Value-Added Tax Act (the VAT Act).

Computek was thus assessed to tax in the total sum of R4 040 377.28, consisting of a capital amount of R1 246 177.57 being under-declared output tax, additional tax of R2 492 355.06 levied on the capital amount in terms of section 60 of the VAT Act, a penalty of R124 617.75 levied on the capital amount in terms of section 39(1)(*a*)(i) of the VAT Act and interest of R177 226.90 levied on the capital amount in terms of section 39(1)(*a*)(ii) of the VAT Act.

Computek, represented by its sole member, filed a notice of objection on the regulation form ADR1 on which it ticked the boxes indicating that the objection covered the penalty, the additional tax, the interest and 'other'. However, Computek's representative did not tick the box marked 'There is a miscalculation on the assessment in that an amount(s) was taken into account /not taken into account to determine the liability for tax'.

Computek, in an *addendum* to ADR1, described the grounds of objection as:

'1. Unfair application of procedural matters by SARS Special Investigations.

2. Excessive add tax of 200% plus penalties and interest charges.

3. Interference of SARS Special Investigation officer into the affairs of the businesses including HR & Associates without any form of negotiations or consultations.

4. Reparations of damages caused by SARS interference and actions in the said businesses in order to put things right.

5. SARS contraventions of its own SARS CHARTER and SARS SSMO and Dispute Resolution processes.'

Computek, in an attachment referred to by it next to the tick box 'other' at the foot of ADR, dealt with a range of issues but its primary focus was on the conduct of one of the special investigators in the employ of SARS.

SARS thereafter informed Computek that its objection had been disallowed and this was followed by a letter to SARS on behalf of Computek in which it was stated *inter alia* that 'we are in agreement with your turnover figures. The difference between your figures and those of the VAT returns relate to different methods of accounting for VAT liabilities. A further letter in this matter will be addressed to you'.

Computek, after the lapse of nearly three years, on 22 January 2007 filed a notice of appeal (form ADR2) in respect of SARS' disallowance of its objection and it advanced the following grounds of appeal:

> Unfair imposition of 200% additional tax; unfair imposition and incorrect penalty; unfair imposition and incorrect interest charge and unfair tax procedural matters.

However, Computek had made no mention therein of the capital amount of the tax.

SARS, in the statement of the grounds of assessment, in terms of rule 10 of the tax rules, contended that when the objection and the appeal are considered it was clear that Computek did not dispute liability for the capital amount and the only amounts of the assessment that Computek had objected to and appealed against were the levying of additional tax at 200%, interest and penalty.

However, in response thereto, Computek filed a rule 11 statement which for the first time asserted that in calculating its VAT liability SARS had included the turnover figures of a related entity.

At a pre-trial conference the parties agreed that the following preliminary point had to be argued and determined by the court before the trial on the main issues commenced:

Whether or not Computek had objected to the capital portion (i.e. dispute amount minus additional tax, penalties and interest) in its Notice of

Objection (ADR1 form) read with the letter of Grounds of Objection attached to the Notice of Objection.

The court a *quo*, being the Johannesburg Tax Court, had decided the preliminary point against Computek but had granted it leave to appeal to the Supreme Court of Appeal.

Computek contended that the court *a quo* had erred in its conclusion '. . . that the notice of objection and the letter accompanying it does not cover the issue which Computek now wishes to raise, namely, that the capital amount levied for VAT is wrong'.

Judge Ponnan held the following:

(i) That the conclusion of the court *a quo* (i.e. the Johannesburg Tax Court) was unassailable as in its notice of objection read together with the letter that accompanied it was quite clear that Computek had not objected to the capital amount and its representative could quite easily have done so by ticking the first box which read: 'There is a miscalculation on the assessment in that an amount(s) was taken into account/ not taken into account to determine the liability for tax.'

(ii) That the aforementioned letter, far from objecting to the revised capital assessment, went so far as to refer to the capital assessment of R1 246 177.60 as being 'uncontested' and in disallowing the objection SARS had made it clear to Computek that it had not objected to 'the *quantum* of additional VAT output raised'. In the face of that Computek had intimated through its representative that it was in agreement with SARS' turnover figures and that was followed by its notice of appeal where once again no mention was made of a challenge to the revised capital assessment.

(iii) That the provisions of section 107A of the Income Tax Act and any rules made under that Act apply to objections and appeals (sections 32(2) and 33(4) respectively of the VAT Act). Rule 4 states that the notice of objection must be in a form prescribed by the Commissioner for SARS and must 'be in writing specifying in detail the grounds upon which it is made'.

(iv) That the thrust of Computek's case was that in referring to the globular amount of R4 040 377 as being the 'amount of tax in dispute in terms of the assessment' it had by necessary implication raised an objection to the capital assessment, which was but one component of that globular sum but that, as the court sought to show, misconceived the inquiry.

(v) That it followed that not having raised an objection to the capital assessment in its notice of objection, Computek had been precluded from raising it on appeal before the court *a quo* and that found support in Rule 6(3)(*a*) which provided that in the taxpayer's notice of appeal he or she must indicate in respect of which of the grounds specified in his or her objection in terms of Rule 4 he or she is appealing.

(vi) That when Computek challenged the capital amount for the first time in its Rule 11 statement, it effectively raised a 'new objection' directed at an individual assessed amount that had not previously been objected to and it remained to add that in terms of section 32(5) of the VAT Act as no objection had been lodged against SARS' assessment that Computek was liable to SARS for additional VAT output tax in the sum of R1 246 177.60, that assessment became final and conclusive in April 2007 and as a period of three years had elapsed (section 31A) Computek could not now lawfully require SARS to revisit its assessment even if it was wrong to have included the turnover of a related entity in calculating Computek's VAT liability and it followed that Computek's appeal had to fail.

(vii) That although SARS had sought the costs of two counsel on appeal, the matter was devoid of any factual or legal complexity and there was thus no warrant for the employment of two counsel by SARS and in those circumstances it would be unjustified to mulct Computek with those costs and accordingly the costs of one counsel were allowed.

Appeal dismissed with costs.

5. INTERPRETATION NOTES

5.1 VAT – Approval to end a tax period on a day other than the last day of a month – No. 52 (issue 2)

This Note serves to:

- set out those instances when tax periods may end on a day other than the last day of a month (hereinafter referred to as cut-off dates);
- provide, in terms of the BGR, the necessary approval to change cut-off dates; and
- withdraw and replace under section 86(1) of the TA Act, Interpretation Note No. 52 dated 14 December 2009, including the BGR contained therein, with effect from the date of issue of this Note.

A supplier, being a vendor, making a taxable supply of goods or services in the course or furtherance of its enterprise is required to levy VAT at the applicable rate on the value of the supply. Furthermore, a supply is deemed to have been made in terms of the time of supply provisions. The general rule is that the time of supply occurs at the earlier of the date of receipt of the consideration or an invoice is issued in relation to a supply. In all other instances, section 9 provides for specific time of supply rules.

A vendor is required to declare output tax on supplies to the extent that those supplies occur in a specific period. This period is referred to as a tax period.

The following categories of cut-off dates of a vendor's tax periods, listed below, are approved by the Commissioner in terms of proviso (ii) to section 27(6):

- A fixed day, being a specific day of the week;
- A fixed date, being a specific date in a calendar month; or

- A fixed day determined in accordance and consistent with the ‘commercial accounting periods’ applied by the vendor.

The approval is conditional upon the following:

- In respect of the cut-off dates set out in the last-mentioned category, the vendor is required to retain the necessary proof that the cut-off dates required are in accordance and consistent with its commercial accounting periods (for example, the minutes of a board meeting in which a decision was made regarding the entity’s commercial accounting period or proof of cut-off dates for management reporting purposes).
- In all instances where a change in cut-off dates is allowed, the first day of the next tax period is the day following the last day of the previous tax period, or the fixed day as approved by the Commissioner.
- Any cut-off date that is changed in accordance with this ruling must be for a future tax period and remain unchanged for a minimum period of 12 months;
- Notwithstanding any of the above concessions, the 10-day will apply.
- Failure to comply with the above will result in the imposition of interest under section 39 of the VAT Act and penalties under sections 210 and 213 of the TA Act, where applicable.

Vendors that comply with the provisions of this ruling do not need to apply for a specific VAT ruling. However, a vendor that intends changing its cut-off date and that date does not fall within one of the categories must apply for a VAT ruling.

A vendor that intends changing the date on which its tax period ends, and the date does not fall within one of the categories, may apply for a VAT ruling or VAT class ruling. The cut-off dates requested should fall within the ambit of the 10-day rule.

6. BINDING PRIVATE RULINGS

6.1 BPR 142 – Deduction of interest expenditure

This ruling deals with the tax treatment of interest expenditure incurred by a subsidiary in a group of companies (the group) on amounts borrowed and on-lent to other subsidiaries within the group.

In this ruling, references to sections are to sections of the Act applicable as at 12 November 2012 and unless the context indicates otherwise, any word or expression in this ruling bears the meaning ascribed to it in the Act.

This is a ruling on the interpretation and application of the provisions of section 24J.

Parties to the proposed transaction

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

Description of the proposed transaction

The Applicant proposes to fund the capital investment in various operations of the group through a loan facility from a financier. The loan facility will be advanced directly to the Applicant. In turn the Applicant will on-lend the funds to other subsidiaries within the group at no margin.

The Applicant has in the past met the short term and long term funding needs of the other subsidiaries in the group. Unlike the other subsidiaries, the Applicant has assets which it will use as collateral for the loan facility.

The proposed funding will be used by the subsidiaries in respect of the:

- new development of operational infrastructure;
- replacement of operational infrastructure;
- development of supporting structure; and
- upgrade of existing operational structure.

Ruling

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

- The interest payable by the Applicant on the loan facility will be allowed as a deduction under section 24J.
- The ruling does not express a view in respect of other costs, for example funding costs, and is limited to the interest expenditure to be incurred by the Applicant.

6.2 BPR 143 – Preference shares constituting equity shares in relation to a headquarter company

This ruling deals with the question as to whether preference shares held will qualify as equity shares for purposes of applying the definition of 'headquarter company' in section 1 of the Act.

In this ruling legislative references to sections are to sections of the Act applicable as at 25 November 2011 and unless the context indicates otherwise, any word or expression in this ruling bears the meaning ascribed to it in the Act.

This ruling has been requested under the provisions of section 1, the definitions of 'equity share' and 'headquarter company'.

Parties to the proposed transaction

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

Description of the proposed transaction

The Applicant holds preference shares in an off shore company. The preference shares confer on the holder the right to participate in a return of capital only to the extent of the subscription price as well as any arrear dividends.

The right to participate in dividends, although expressed in the articles of association as a rate on the subscription price, is effectively unlimited and unrestricted as the rate is at the discretion of the directors, and the dividend

is thus not restricted to a pre-determined amount or coupon. In effect, it is open to the directors to declare the same dividend on preference shares as on ordinary shares. The right to participate in dividends is not restricted.

The Applicant intends to list a certain percentage of its shares on an international stock exchange should it qualify as a 'headquarter company' as defined in section 1. 2

Ruling

The ruling made in connection with the proposed transaction is that the preference shares in question will be regarded as equity shares for the purpose of applying the definition of 'headquarter company' in section 1.

6.3 BPR144 – Write-off period in respect of the increase in either the cost or the value of assets pursuant to a section 45(4) de-grouping

This ruling deals with the write-off period to be allowed in respect of the increase in either the cost or the value of assets initially acquired under section 45, as a result of a de-grouping of companies as contemplated in section 45(4).

In this ruling references to sections are to sections of the the Act applicable as at 27 March 2013 and unless the context indicates otherwise, any word or expression in this ruling bears the meaning ascribed to it in the Act.

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

- section 45(4)(*b*),
- section 11(*e*),
- section 12C, and
- section 13.

Parties to the proposed transaction

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

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

Description of the proposed transaction

The Applicant is the holding company of Company A and both companies form part of the same group of companies. The Applicant and Company A previously entered into an intra-group transaction in terms of which Company A acquired certain assets from the Applicant under section 45.

The Applicant proposes to sell its shareholding in Company A. As a result of this sale Company A will, within six years of Company A having acquired the assets in terms of the intra-group transaction, cease to form part of the same group of companies as the Applicant.

Ruling

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

For purposes of calculating the allowances to be deducted under sections 11(*e*), 12C or 13 on either the increased cost or value of the assets, as contemplated in section 45(4)(*b*)(i) and (ii), the following will apply:

- An allowance may be claimed in respect of the increase in cost or value of the asset over the remaining write-off period of the asset, as determined by the relevant section.
- If an asset is fully written off at the time of de-grouping, the allowance may be deducted in full in the year of assessment during which the de-grouping takes place.

6.4 BPR 145 – Allowances – Assets forming part of a sale and leaseback arrangement

This ruling deals with the write-off period under section 11(*e*) of assets forming part of a sale and leaseback arrangement and the deductibility thereof.

In this ruling legislative references to sections are to sections of the Act applicable as at 12 December 2012 and unless the context indicates

otherwise, any word or expression in this ruling bears the meaning ascribed to it in the Act.

This is a ruling on the interpretation and application of the provisions of section 11(*e*).

Parties to the proposed transaction

The Applicant: A company incorporated in and a resident of South Africa whose receipts and accruals are taxable

Company X: A company incorporated in and a resident of South Africa whose receipts and accruals are taxable

Description of the proposed transaction

The Applicant intends to provide financing to Company X by way of a sale and leaseback arrangement (arrangement) in relation to certain plant and machinery (specified assets) currently owned and used in a process of manufacture by Company X.

In terms of the arrangement:

- The Applicant will purchase the specified assets from Company X. The purchase price to be paid by the Applicant will be determined with reference to a valuation conducted by an independent third party.
- The specified assets will be leased back to Company X for a period of 7 years.
- Company X shall, within 30 days after the termination of the lease for whatever reason, be entitled to purchase the specified assets from the Applicant at their market value at that time.

Ruling

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

- The Applicant may deduct allowances under section 11(*e*) in respect of the specified assets which form part of the sale and leaseback arrangement over each individual asset's expected useful life.

6.5 BPR 146 – Mining Tax – Contract mining agreement

This ruling deals with:

- whether a company appointed as a contractor in terms of a contract mining agreement is conducting mining operations and entitled to deductions under section 11(*a*), 15 and 36 of the Act during a transition period when the company is awaiting the transfer of mining rights to it; and
- the deductibility of contributions made by such company under section 37A(1)(*d*)(ii) in respect of environmental obligations.

In this ruling references to sections are to sections of the Act applicable as at 10 July 2012 and unless the context indicates otherwise, any word or expression in this ruling bears the meaning ascribed to it in the Act.

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

- section 1, definition of 'mining operations' and 'mining';
- section 11(*a*);
- section 15(*a*);
- section 23(*g*);
- section 36; and
- section 37A(1)(*d*)(ii).

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

The Applicant: A company incorporated in and a resident of South Africa that is the ultimate holding company of Co-Applicant A and Co-Applicant B (all forming part of a group of companies that carry on mining activities) (the A Group)

Co-Applicant: A limited liability company that is incorporated in and a resident of South Africa and a wholly owned subsidiary of the Applicant

Co-Applicant B a limited liability company that is incorporated in and a resident of South Africa and a wholly owned subsidiary of the Applicant

Description of the proposed transactions

In order to streamline the mining operations of the A Group, the Applicant intends to restructure and consolidate the current mining operations conducted by Co-Applicants A and B within Co-Applicant A.

In terms of the proposed restructure:

- Co-Applicant B will transfer certain mining assets (including mining rights) and liabilities to Co-Applicant A in terms of section 42, in exchange for equity shares to be issued by Co-Applicant A.
- Under the Mineral and Petroleum Resources Development Act No 28 of 2002 (the MPRD Act) the transfer of the mining rights will be subject to the consent of the Minister of Mineral Resources and the registration of the transfer of the mining rights will be done in the Mining and Petroleum Titles Registration Office. Accordingly, it is envisaged that there will be a delay in completing the proposed restructure until such time as the registration of the transfer of the mining rights is affected.
- In view of the fact that the provisions of the MPRD Act do not allow anyone who does not hold a mining right to mine for its own account, it is proposed that Co-Applicants A and B enter into a contract mining agreement for the period between the effective date of the transfer of the mining assets and the actual date of transfer of the mining rights (the interim period) in terms of which Co-Applicant A will mine on behalf of Co-Applicant B.
- Co-Applicant A will be appointed as a contractor in terms of section 101 of the MPRD Act and the applicable legislation to conduct and to perform the mining operations in favour of and for the benefit of Co-Applicant B will apply.
- For the purposes of the contract mining agreement the term ‘mining operations’ will mean all procedures, operations, functions and duties

conducted, undertaken or performed in the normal course or in connection with or implicit in the recovery of ore from mining operations in accordance with the mine plan.

- Co-Applicant A will receive a contract mining fee for performing such mining operations. This fee will be a cost recovery fee for all the costs and expenses to be incurred by Co-Applicant A in terms of the contract mining agreement to perform the mining operations. The fee will include value-added tax (VAT) thereon at the applicable rate, as well as all amounts to be paid by Co-Applicant A on behalf of Co-Applicant B as royalties in terms of the MPRD Act.
- In terms of the contract mining agreement the ore to be mined will belong to Co-Applicant B. However, the contract mining agreement stipulates that Co-Applicant B will sell the ore to Co-Applicant A, and Co-Applicant A will purchase the ore to be mined from Co-Applicant B. Co-Applicant A will sell the same to the external market on the following basis:
  - The purchase price for the ore to be sold to Co-Applicant A will be an amount equal to the contract mining fee which includes the royalties referred to in the contract mining agreement, which will be payable monthly by Co-Applicant A to Co-Applicant B.
  - Co-Applicant A will dispose of all minerals and/or products derived from the exploitation of the minerals at competitive market prices which will mean, in all cases, non-discriminatory prices or non-export prices in accordance with the terms and conditions of the mining rights held by Co-Applicant B.
- Following the transfer of the mining rights from Co-Applicant B to Co-Applicant A, Co-Applicant B will distribute the equity shares to be received in Co-Applicant A to the Applicant in an unbundling transaction under section 46.

Conditions and assumptions

This ruling is made subject to the conditions and assumptions that:

- Co-Applicant A will not qualify for the partial relaxing of the ring fencing provisions of section 36(7F) as a result of the application of section 36(7G) in respect of the mining assets to be acquired from Co-Applicant B.
- Co-Applicant A must obtain approval from SARS Mining Tax division for the amount sought to be deducted under section 37A(1)(*d*)(ii) prior to the contribution being made to the designated rehabilitation trust or company for the years of assessment that Co-Applicant A will mine on a contract basis. It is noted that only approved amounts qualify for the deduction provided for in section 37A(1)(*d*)(ii).

Rulings

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

- Co-Applicant A will be recognised as holding the necessary mining rights to carry on mining activities on the mine areas of Co-Applicant B and will, therefore, be treated as carrying on 'mining operations' and/or 'mining' for the purposes of the Act.
- The contract mining fee payable to Co-Applicant A by Co-Applicant B in terms of the contract mining agreement will be regarded as income directly connected to such mining operations and as such will be regarded as income derived from mining.
- The revenue derived by Co-Applicant A from the sale of any ore during the interim period will be regarded as income directly connected to such mining operations and as such will be regarded as income derived from mining.
- Co-Applicant A will be entitled to capital expenditure deductions under section 15(*a*) read with section 36 against such mining income during the interim period.
- Expenditure incurred by Co-Applicant A in acquiring the ore from Co-Applicant B during the interim period, in terms of the contract mining agreement, will be regarded as a deductible expense under section

11(*a*) against the income derived by Co-Applicant A from the mining operations.

- Co-Applicant B will be regarded as carrying on trade during the interim period for the purpose of section 11(*a*), despite the absence of any profit, and will be entitled to claim the contract mining fee to be paid to Co-Applicant A in terms of the contract mining agreement as a section 11(*a*) deduction against the income earned from the sale of the ore to Co-Applicant A.
- Co-Applicant A will qualify in principle to claim as a deduction under section 37A(1)(*d*)(ii) contributions to be made in respect of environmental obligations, provided that the required approval is obtained from SARS. Notwithstanding the foregoing, a positive ruling is given to the effect that the payment of the contributions will not be regarded as part of any transaction, operation or scheme designed solely or mainly for purposes of shifting the deduction contemplated in this subsection from Co-Applicant B to Co-Applicant A.

6.6 BPR147 – Consideration received for the surrender of a right to acquire shares

This ruling deals with the income tax consequences for a taxpayer in respect of consideration to be received for the surrender of a right to acquire shares.

In this ruling references to sections are to sections of the Act applicable as at 2 November 2011 and unless the context indicates otherwise, any word or expression in this ruling bears the meaning ascribed to it in the Act.

This ruling has been requested under the provisions of:

- section 1, definition of 'gross income'; and
- section 8C.

Parties to the proposed transaction

The Applicant: A natural person who is a 'resident' as defined in section 1

The Employer: The Applicant's employer

Description of the proposed transaction

The Applicant was the chief executive officer and managing director of Subco, a wholly owned subsidiary of Holdco. Subco disposed of its business, with all its assets and liabilities, as a going concern.

At the time of negotiating the sale of the business, the Applicant received and accepted an offer of employment from the purchaser of the business. The offer of employment provided, *inter alia*, that the purchaser was to:

- transfer the acquired business to a new company (Newco);
- employ the Applicant as the chief executive officer of Newco; and
- transfer an equity share in Newco to the Applicant for no consideration. However, the transfer of the shares was subject to a restriction, requiring the Applicant to complete an uninterrupted period of 5 years employment within the purchaser's group of companies.

Shortly after the offer of employment was accepted, the Applicant received a letter from his Employer, stating that the Employer intends to dispose of some parts of Newco's business to a company outside the Employer's group of companies.

As a result of the intended disposal, the Applicant's right to acquire an equity share in Newco would be significantly less in value. The Employer, therefore, proposes to enter into an agreement with the Applicant, whereby the Applicant will be compensated for surrendering his right to acquire an equity share in Newco. In terms of this agreement, the Employer is to transfer an amount in rands to the Applicant, equal to the value of the equity share the Applicant had a right to receive in terms of his employment agreement, on the date of the sale of the said parts of the business of Newco. The compensation is to be payable from the proceeds of the sale mentioned in the previous paragraph.

Ruling

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

- The consideration to be received by or accrued to the Applicant will constitute a gain that is to be included in the Applicant's income as contemplated in section 8C(1).

6.7 BPR 148 – Dividends tax rate – permanent establishment in South Africa

This ruling deals with the appropriate dividends tax rate applicable to a permanent establishment in South Africa of a company which is not a resident of South Africa, having regard to the application of Article 10(2) and the non-application of Article 10(4) of the South Africa/Japan DTA.

In this ruling, references to sections and Articles are to sections of the Act and Articles of the South Africa/Japan DTA' applicable as at 7 March 2013 and unless the context indicates otherwise, any word or expression in this ruling bears the meaning ascribed to it in the Act or the South Africa/Japan DTA, as the case may be.

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

- section 64G(3)*(b)*(i) of the Act; and
- Articles 10(2) and 10(4) of the South Africa/Japan DTA, and in particular the phrase "effectively connected with such permanent establishment" used in Article 10(4).

Parties to the proposed transaction

The Applicant: A corporation established in and a resident of Japan

The Branch: A South African branch of the Applicant

The Head Office: The head office of the Applicant, located in Japan

The Investee: A private company incorporated in and a resident of South Africa, in which the Applicant holds 49% of the equity shares 2

Description of the proposed transaction

The Applicant forms part of a group of companies headquartered in Japan. The group is an international conglomerate operating across continents through businesses that are a combination of incorporated subsidiaries and branches.

The Applicant conducts business in South Africa through the Branch, which constitutes a permanent establishment for purposes of the South Africa/Japan DTA. The Branch acts primarily as agent between the Applicant and potential buyers/sellers of commodities, including metals, both locally and internationally. In this respect, the bulk of the Branch's income is commission earned.

In relation to its business as buying agent of metals on behalf of the Applicant, the Branch's responsibilities include:

- transmission of proposals;
- delivery of contract sheets;
- delivery of transportation documents;
- communication with carriers in respect to a vessel's schedule, cargo readiness, loading and unloading;
- assistance in relation to a principal's travelling;
- providing notice of claims, if any, and suggesting possible resolutions thereof;
- handling all related communication; and
- providing other services necessary or appropriate to be rendered by the Branch as buying agent on behalf of the principal.

In consideration for the rendering of these services, the Branch earns commission, calculated at a percentage of the free on board value of the metals sourced.

The Investee holds a significant stake in a major supplier of metals to the Applicant. The Applicant, in turn, holds 49% of the equity in the Investee as follows:

- 47% is held by the Head Office; and
- 2% is held by the Branch.

The Branch enjoys the right to dividends and capital gains in relation to the 2% investment in the Investee. Funding expenditure in relation to the acquisition of the 2% investment is allocated to the Branch.

In terms of its shareholding in the Investee, dividends will be declared to the Branch from time to time, attracting dividends tax.

Conditions and assumptions

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

- Both the declaration and the written undertaking, required in terms of section 64G(3), have been submitted to the Investee prior to the date specified by the Investee; or, if no such date has been specified, by the date of payment of the first dividend after the issue of this ruling.
- The shares in the Investee are held as a passive investment by the Applicant.

Ruling

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

- Based on the facts, the 2% share investment held in the Investee via the Branch is not effectively connected to the Branch and Article 10(4) of the South Africa/Japan DTA is therefore not applicable.
- In terms of Article 10(2) of the South Africa/Japan DTA, the appropriate rate of dividends tax to be withheld by the Investee on dividends payable to the Applicant through the Branch, will not exceed 5% of the gross amount of the dividends.

Period for which this ruling is valid

This binding private ruling is valid in relation to dividends payable to the Branch whilst the Applicant's current 49% shareholding in the Investee (2% via the Branch and 47% via the Head Office) continues without change.

7. BINDING GENERAL RULING

7.1 BGR (VAT) 19 – Approval to end a tax period on a day other than the last day of a month

This BGR reproduces paragraph **5** of Interpretation Note No. 52 (Issue 2) 'Approval to End a Tax Period on a Day other than the Last Day of a Month' (30 April 2013), which comprises a BGR under section 89 of the TA Act. In this regard, the BGR relates to the approval to end tax periods on a day other than the last day of the month.

Ruling

The following categories of cut-off dates of a vendor's tax periods, listed below, are approved by the Commissioner in terms of proviso (ii) to section 27(6):

- A fixed day, being a specific day of the week
- A fixed date, being a specific date in a calendar month
- A fixed day determined in accordance and consistent with the 'commercial accounting periods' applied by the vendor

Conditions for the Commissioner's approval

The approval set out above is conditional upon the following:

- In respect of the cut-off dates set out in the last-mentioned category, the vendor is required to retain the necessary proof that the cut-off dates required are in accordance and consistent with its commercial accounting periods (for example, the minutes of a board meeting in which a decision was made regarding the entity's commercial accounting period or proof of cut-off dates for management reporting purposes).
- In all instances where a change in cut-off dates is allowed, the first day of the next tax period is the day following the last day of the previous tax period, or the fixed day as approved by the Commissioner.

- Any cut-off date that is changed in accordance with this ruling must be for a future tax period and remain unchanged for a minimum period of 12 months under proviso (ii) to section 27(6).
- Notwithstanding any of the above concessions, the cut-off date must fall within 10 days before or after the end of the tax period.
- Failure to comply with the above will result in the imposition of interest under section 39 of the VAT Act and penalties under sections 210 and 213 of the TA Act, where applicable.

A vendor who intends changing the date on which its tax period ends, and the date does not fall within one of the categories listed above, may apply for a VAT ruling or VAT class ruling.

8. BINDING CLASS RULING

8.1 BCR 39 – Reduction of an STC credit and section 64G(2)(a) and 64H(2)(a) declarations

This ruling deals with the obligation of a company or a regulated intermediary to notify a beneficial owner of a dividend to be paid in cash or distributed *in specie* of the amount by which the dividend will reduce the STC credit of the company paying the dividend and the publication of that notice.

In this ruling references to sections are to sections of the Act applicable as at 1 August 2012 and unless the context indicates otherwise, any word or expression in this ruling bears the meaning ascribed to it in the Act.

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

- section 64G;
- section 64H and
- section 64J.

Class

The class members to whom this ruling will apply will be the beneficial owners of dividends paid or distributed from time to time.

Parties to the proposed transaction

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

Class Members: The beneficial owners of the dividends associated from time to time with the Applicant's shares and the regulated intermediaries through whom those dividends are to be paid or distributed

Description of the proposed transaction

The Applicant proposes to pay cash or *in specie* dividends on its shares from time to time. Payments are to be made via regulated intermediaries, as defined in section 64D.

Those payments or distributions will for some time not exceed the Applicant's STC credit, as determined under section 64J(2).

The Applicant's issued share capital consists of ordinary shares and 'B' class ordinary shares. The ordinary shares are listed and traded on the JSE.

The Applicant customarily declares an interim dividend and a final dividend each year. From time to time it also declares special dividends which can take the form of cash payments or distributions *in specie*.

All declarations of dividends are communicated via the JSE Ltd's news service SENS, as well as via the Applicant's website. Information on dividends is also communicated to shareholders who hold their shares in electronic (dematerialised) format via the central securities depository system of Strate Ltd. Those shareholders have an option to indicate whether or not they want to receive electronic communications from the Applicant (or any other company).

Information on all dividends for the year is also published with the interim and annual financial results of the Applicant in the national press.

As at the date of the application, the Applicant and its subsidiaries have available STC credits. Although this balance will be reduced by dividends declared, it is anticipated that certain dividends the Applicant will receive will be added to the available STC credit balance as contemplated by section 64J(2)(*b*), read with section 64J(3).

Conditions and assumptions

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

- Nothing contained in this ruling discharges the obligation to submit returns under the provisions of section 64K(1)(*d*) or section 69(1) or the obligation to keep records under section 73C, or any provision substituted for these provisions by the Tax Administration Act No. 28 of 2011, promulgated on 4 July 2012 in GG 35491, when they come into operation, in particular the provisions of sections 25, 29(1) and 30(2) of the last mentioned Act.
- This ruling is not made in the exercise of any of the Commissioner's powers to prescribe the form and contents of returns to be rendered.

Ruling

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

Provided that the Applicant pays dividends that do not exceed its STC credit:

- Dividends to be declared and paid by the Applicant will be payable in full to their beneficial owners without dividends tax being withheld if the dividends are paid in cash, or without the Applicant being liable to pay dividends tax if the distributions are *in specie*.
- The Applicant, or any regulated intermediary that is to pay dividends, need not obtain any declaration contemplated in section 64G(2)(*a*) or section 64H(2)(*a*) that qualifies any beneficial owner to obtain any benefit from the STC credit, and beneficial owners need make no declarations to qualify for the benefit.
- Prior to paying a dividend to a beneficial owner who is a company, the Applicant, or the relevant regulated intermediary (as the case may

be), must comply with the notice requirements prescribed by section 64J(2)*(b)*.

- The following methods of publication by the Applicant of the notice contemplated in section 64J(1)(*b*), together with the publication of the details of a dividend declared, will serve as sufficient notice to the person to whom the dividend is paid of the amount by which the dividend reduces the STC credit:
  - communication via SENS;
  - communication via the Applicant's Internet website;
  - communication to shareholders holding shares in electronic format via the central securities depository system of Strate Ltd; and
  - publication of full details on all dividends paid during the year at the time that the Applicant's interim and annual results are published in the national financial press.

8.2 BCR40 – Investors acquiring rights in a completed film

This ruling deals with the tax consequences for an investor who will acquire rights in a completed film.

In this ruling legislative references to sections are to sections of the Act, applicable as at 21 April 2011 and unless the context indicates otherwise, any word or expression in this ruling bears the meaning ascribed to it in the Act.

This ruling has been requested under the provisions of sections 10(1)(*z*G), 23(*n*) and 24F.

Class

The class members to whom this ruling will apply will be investors as described below.

Parties to the proposed transaction

The Applicant: The producer of the film

Filmco: A film production company which will be a special purpose vehicle for the production of the film

The Financier: A registered financial services provider

The Investors: Investors who will acquire film rights in a completed film from Filmco

Description of the proposed transaction

The Applicant will incorporate Filmco and transfer the film rights in the film to be produced to Filmco. Filmco will obtain an interest bearing loan from the Financier to cover the production costs of the film and utilise the funds to produce the film. On completion of the production of the film and when it is in a form in which copies thereof can be made and distributed for presentation to the general public, the producer, along with distributors and sales agents, will source the Investors to invest in the ownership of the film rights.

Filmco will apply for and claim the film incentive rebate available from the Department of Trade and Industry known as the Large Budget Film and Television Production Rebate Scheme (DTI film rebate). Filmco will distribute the DTI film rebate received to the Investors as contractually agreed.

The Investors will each acquire a share in the ownership of the film rights in their individual capacities. The Investors will use their own cash resources or obtain loan funding to acquire the film rights. Where loan finance is utilised, the loan will be repayable within a period of 10 years.

The net revenues from the world wide exploitation of the film will be distributed to the film owners according to their percentage share in the film rights.

Ruling

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

- An Investor who purchases a share of the rights in the completed film will qualify as a ‘film owner’ defined in section 24F(1).
- An Investor who purchases film rights with the use of borrowed funds will also qualify as a ‘film owner’.
- An Investor will be eligible to claim the section 24F allowance in the year of assessment in which the film rights are acquired and any subsequent year of assessment, subject to the provisions of section 24F(4).
- The purchase price of the film rights will be the basis for calculating the section 24F allowance. The receipt of the DTI film rebate will not affect the calculation of the section 24F allowance.
- Section 23(*n*) is not applicable to the DTI film rebate and will accordingly not be applicable to the section 24F allowances.
- The provisions of section 10(1)(*z*G) will be applicable to the DTI film rebate that the Investors will receive from Filmco.

9. GUIDES

9.1 Short Guide to the Tax Administration Act

This publication is provided to assist taxpayers to understand their obligations and entitlements under the Tax Administration Act, 2011 (Act No. 28 of 2011) (the Act), which commenced on 1 October 2011. It is not a binding general ruling, interpretation note, practice note or other official publication as referred to in the Act and should therefore not be used as a legal reference.

The drafting of a Tax Administration Act was announced by the Minister of Finance in the 2005 Budget Review. The first draft of the Tax Administration Bill was published in 2009, which was followed by an extensive public consultation process and the Tax Administration Act, 28 of 2011 (the Act), was promulgated on 4 July 2012.

The Act came into operation on 1 October 2012 by Proclamation No. 51 of 2012, published in Government *Gazette* 35687 on 14 September 2012.

In terms of the law that has created SARS, the South African Revenue Service Act, 1997 (the SARS Act), SARS' objectives include the efficient and effective collection of revenue. Tax legislation, such as the Tax Administration Act, 2011, seeks to achieve this objective. Tax legislation typically comprises two aspects:

- Tax liability provisions or 'tax charging' provisions; and
- Tax administration provisions.

The Act only deals with tax administration, and seeks to:

- incorporate into one piece of legislation administrative provisions that are generic to all tax Acts and currently duplicated in the different tax Acts;
- remove redundant administrative provisions;
- harmonise the provisions as far as possible.

Note: Some administrative provisions that only apply and are unique to the administration of a specific tax type remain in the tax Act that imposes that tax. In certain instances, therefore, both this Act and a tax Act prescribe administrative procedures and a taxpayer must comply with both. For example, the record keeping requirements in this Act for value-added tax are supplemented by additional record keeping requirements in the Value-Added Tax Act, 1991 (the VAT Act), which are unique to value-added tax.

The Act seeks to simplify administrative provisions. It is an established principle that simplified law enhances clarity. It is easier for a taxpayer to fully comply with law he or she understands, than with law that is too technical and therefore difficult to understand and comply with.

The Act seeks to promote a better balance between the powers and duties of SARS and the rights and obligations of taxpayers and to make this relationship more transparent. This balance will greatly contribute to the equity and fairness of tax administration. International experience has demonstrated that if taxpayers perceive and experience the tax system as

fair and equitable, they will be more inclined to fully and voluntarily comply with it.

The Act also seeks to provide a foundation for further and future modernisation and development of tax administration, such as single registration, self-assessment and accounting transformation. Single registration means that taxpayers will only need to register once with SARS and the basic registration information will then apply for all tax types. A self-assessment system seeks to reduce administration. For example, currently a taxpayer submits an income tax return. SARS then determines the tax liability and assesses the taxpayer – the Act builds a platform for a full self-assessment regime where a taxpayer determines his own tax liability and pays the tax. Accounting transformation involves, for example:

- a move to accrual accounting from the current cash basis;
- a single account for a taxpayer with a rolling balance, including payment allocation rules across taxes;
- the alignment of interest across tax types and its calculation on a compounded basis.

The Act seeks in numerous ways to enhance tax compliance to ensure that every person pays his or her fair share. The Act gives recognition to the fact that:

- the majority of taxpayers are compliant and want a more modern and responsive revenue administration;
- there is a minority who seek to evade tax or defraud the government.

Most taxpayers are compliant and for them the Act should ensure better service and a lower compliance cost. Tax evaders, however, will face stricter enforcement, assessment and collection powers.

10. INDEMNITY

Whilst every reasonable care has been taken in the production of this update we cannot accept responsibility for the consequences of any inaccuracies contained herein or for any action undertaken or refrained from taken as a consequence of this update.