TAX UPDATE

For period: October 2021 to December 2021

Prepared by: Johan Kotze

TABLE OF CONTENTS

1. INTRODUCTION 4

2. BILLS PUBLISHED 6

3. TAXATION LAWS AMENDMENT BILL 6

3.1. Section 20 – Set-off of assessed losses – Income Tax Act 6

4. MEDIA STATEMENT – PHYSICAL IMPAIRMENT OR DISABILITY PRESCRIBED BY SARS 7

5. GOVERNMENT NOTICE – PUBLICATION OF EXPLANATORY SUMMARY OF THE TAX ADMINISTRATION LAWS AMENDMENT BILL, 2021 8

6. REGULATION – INCIDENCES OF NON-COMPLIANCE SUBJECT TO FIXED AMOUNT PENALTY 10

7. MEDIA STATEMENT – PERSONAL INCOME TAX: NEW PENALTY RULE AND AUTO-ASSESSMENT PROCESS 11

8. TAX CASES 12

8.1. Wenco International Mining Systems Ltd v C:SARS (83 SATC 463) 12
8.2. ITC 1946 (83 SATC 504) – Tax administration 19
8.3. ITC 1947 (83 SATC 545) – Capital Gains Tax 27
8.4. City Power (SOC) Ltd v C:SARS (83 SATC 523) 37

9. INTERPRETATION NOTES 42

9.1. Value-Added Tax consequences of points-based loyalty programmes – No. 118 42
9.2. Supplies made for no consideration – No. 70 (Issue 2) 43

10. BINDING PRIVATE RULINGS 46

10.1. BPR 368 – Payments made pursuant to an agreement relating to a permission to occupy 46
10.2. BPR 369 – Deductibility of interest incurred pursuant to liquidation of company 49
10.3. BPR 370 – Registration of shares in the name of beneficial holder 50

11. BINDING GENERAL RULINGS 53

11.1. Whether the term 'consideration' includes an amount of transfer duty for the purposes of calculating a notional input tax deduction n the acquisition of second-hand fixed property BPR – No. 57 (VAT) 53
11.2. Purchase of different types of annuities at retirement – No. 58 56
12. GUIDES 58
12.1. VAT Rulings Process – Reference Guide 58
13. DRAFT GUIDES 61
13.1. Draft Guide to the Voluntary Disclosure Programme 61
14. INDEMNITY 63

1. INTRODUCTION

The purpose of this update is to summarise developments that occurred during the fourth quarter of 2021, specifically in relation to Income Tax and VAT. Johan Kotze, a Tax Executive at Shepstone & Wylie Attorneys, has compiled this summary.

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

Please take some time and consider the tax cases.

Interpretation notes, rulings and guides are all important aspects of the developments that took place, as they give taxpayers an insight into SARS' application of specific provisions.

Enjoy reading on!

The government when you
lose money in crypto:
I told you it's risky and volatile

The government when you
make profit in crypto

2. BILLS PUBLISHED

The following Bills wer published during this quarter:

- Division of Revenue Amendment Bill
- Rates and Monetary Amounts and Amendment of Revenue Laws Bill
- Taxation Laws Amendment Bill
- Tax Administration Laws Amendment Bill

3. TAXATION LAWS AMENDMENT BILL

3.1. Section 20 – Set-off of assessed losses – Income Tax Act

Section 20 of the Income Tax Act, 1962, is hereby amended by the substitution in subsection (1) for paragraph (a) of the following paragraph:

"(a) (i) that is a company, any balance of assessed loss incurred by that person in any previous year which has been carried forward from the preceding year of assessment, to the extent that the amount of such set-off does not exceed the higher of R1 million and 80 per cent of the amount of taxable income determined before taking into account the application of this provision;

(ii) that is not a company, any balance of assessed loss incurred by that person in any previous year which has been carried forward from the preceding year of assessment: Provided that no person whose estate has been voluntarily or compulsorily sequestrated shall be entitled to carry forward any assessed loss incurred prior to the date of sequestration, unless the order of sequestration has been set aside, in which case the amount to be so carried forward shall be reduced by an amount which was allowed to be set off

against the income of the insolvent estate of such person from the carrying on of any trade;''.

Subsection (1) comes into operation on the date on which the rate of tax in respect of the taxable income of a company is first reduced after announcement by the Minister of Finance in the annual National Budget and applies in respect of years of assessment commencing on or after that date.

4. MEDIA STATEMENT – PHYSICAL IMPAIRMENT OR DISABILITY PRESCRIBED BY SARS

29 October 2021 – The Commissioner of the South African Revenue Service (SARS) is permitted by law to publish a list of qualifying medical expenditure that is necessarily incurred and paid by a person during a year of assessment as a result of any physical impairment or disability suffered by the person or any dependant of the person (Disability List).

The Disability List was updated after an extended public consultation process and published with effect from 1 March 2020 ('the 2020 Disability List'). From the latter part of 2020, SARS noted public concerns regarding the change in the method of calculating the qualifying medical expenses relating to school fees.

It is for this reason, and after much deliberation, that SARS has taken the decision to revert to the method of calculating the qualifying medical expenses for school fees as set out in the 2012 Disability List. This change will be effective retrospectively from 1 March 2020. The wording in Part F, paragraphs 7 & 8 of the revised 2020 Disability List now reads as follows:

7. Special education schools for learners with disabilities. Qualifying expenses will include –

   - school assistant or classroom costs; and
   - school fees limited to the amount in excess of the fees that would have been payable if the person attended the closest

fee-paying public school not specialising in learners with special educational needs.

8. Schools not specialising in learners with special educational needs, limited to additional expenses incurred and paid as a result of the disability.

The 2020 Disability List has been amended accordingly and was published on the SARS website on 29 October 2021. It can be accessed by clicking on this link: https://www.sars.gov.za/types-of-tax/personal-income-tax/tax-and-disability/.

Please note that taxpayers who are affected by these changes are those taxpayers whose children living with a disability attend a private special education needs school.

Affected taxpayers who have already submitted a 2021 income tax return are requested to log into their eFiling profile or visit their local SARS branch office (by appointment only) to:

- ‘request for correction’ (RFC); or
- lodge an objection*.

These options will allow the taxpayer to claim the additional benefit as outlined in the revised 2020 Disability List.

* Taxpayers must only lodge an objection if the RFC option is not available for the 2021 year of assessment.

5. GOVERNMENT NOTICE – PUBLICATION OF EXPLANATORY SUMMARY OF THE TAX ADMINISTRATION LAWS AMENDMENT BILL, 2021

Notice is hereby given in terms of Rule 276(1)(b) of the Rules of the National Assembly that the Minister of Finance intends to introduce the Tax Administration Laws Amendment Bill, 2021, in the National Assembly in the near future. The

explanatory summary of the Bill is hereby published in accordance with Rule 276(1)(c) of the Rules of the National Assembly. The Bill provides for the amendment of the:

- Income Tax Act, 1962, so as to enable the Commissioner to request certain information by public notice; to align the provision with regards to submission of a return by a foreign person in respect of withholding tax on royalties with that of withholding tax on interest; to align the refund limitation rules for dividends paid in specie with that of dividends paid in cash; to provide that the prescription periods will not apply with regards to certain deductions claimed by farmers and to provide for extended record-keeping periods; to provide for textual corrections; to provide for a penalty to be raised on an estimate of employees' tax; to provide that a first provisional tax payment and return will not be required when the duration of a year of assessment does not exceed six months; and to provide for the deletion of a penalty;
- Tax Administration Act, 2011, so as to make a textual corrections; to provide for an extension in submission of a return or relevant material with regard to assessments based on an estimate; to provide for a date from which a taxpayer may lodge an objection and appeal with regard to assessments based on an estimate; to provide for an exception to prescription; and to correct a crossreference;
- Disaster Management Tax Relief Administration Act, 2020, so as to amend certain dates in order to provide relief under the Act, and to provide for matters connected therewith.

6. REGULATION – INCIDENCES OF NON-COMPLIANCE SUBJECT TO FIXED AMOUNT PENALTY

Schedule

1. General

Any term or expression contained in this notice to which a meaning has been assigned in a 'tax Act' as defined in section 1 of the Tax Administration Act, 2011, has the meaning so assigned, unless the context indicates otherwise.

2. Incidences of non-compliance subject to fixed amount penalty

2.1 Failure by a natural person to submit an income tax return as and when required under a tax Act, for years of assessment commencing on or after 1 March 2006, where that person has, with effect from 1 December 2021—

2.1.1 two or more outstanding income tax returns for years of assessment commencing on or after 1 March 2006 but ending on or before 29 February 2020; or

2.1.2 one or more outstanding income tax returns for years of assessment commencing on or after 1 March 2020.

2.2 Failure by a natural person to submit an income tax return as and when required under the Income Tax Act, for years of assessment commencing on or after 1 March 2006, where that person has, with effect from 1 December 2022, one or more outstanding income tax returns.

7. MEDIA STATEMENT – PERSONAL INCOME TAX: NEW PENALTY RULE AND AUTO-ASSESSMENT PROCESS

THE NEW PENALTY RULE FOR NON-COMPLIANT TAXPAYERS

In line with the SARS' strategic objective of making non-compliance hard and costly, it is imperative that SARS enhances its ability to impose administrative penalties in a more responsive manner. With effect from 1 December 2021, SARS has been empowered to levy a late submission of return penalty where one or more personal income tax returns are outstanding. As a transitional measure for the first year, the one tax return or more rule will only apply to the 2021 tax return. Prior to 1 December 2021, SARS could only levy a late submission of return penalty where two or more outstanding tax returns. This older rule will remain in place for one more year for 2020 and earlier returns.

AUTO-ASSESSMENTS

As you are aware, during the month of July, SARS used the data received from employers and other third-party data providers to issue simulated assessments to a significant number of non-provisional individual taxpayers. As part of the auto-assessment process, SARS requests taxpayers to either accept or edit the simulated assessment via eFiling or the SARS MobiApp, which is then followed by an original assessment issued by SARS. A large number of taxpayers have already either accepted or edited their simulated assessments and received an original assessment from SARS.

NO RESPONSE BY DEADLINE

The deadline for individual non-provisional taxpayers is 23 November 2021. Taxpayers in the auto-assessment population, who neither accepted nor edited and submitted their simulated assessments by this date, will receive an original assessment based on an estimate in accordance with section 95 of the Tax Administration Act, 2011. This assessment is not subject to objection and appeal. However, a taxpayer who is not in agreement with his or her assessment may file a

complete and accurate tax return within 40 business days of the assessment date. Such a return will be late, which means that normal late submission penalties and interest (where applicable) will apply.

8. TAX CASES

8.1. Wenco International Mining Systems Ltd v C:SARS (83 SATC 463)

Wenco was incorporated and also had its principal place of business in British Columbia, Canada.

Second Applicant was also incorporated in British Columbia, Canada, but had its principal place of business and registered address in Centurion, South Africa and had been registered as a branch of the Wenco in South Africa.

Wenco specialised in the development of software for the mining industry and it supplied its clients with management systems software, maintenance, safety and machine guidance to manage mining operations.

Second Applicant was responsible for rendering services such as training, system support, site visits and installation to South African and other African clients of Wenco and these services were rendered by the Second Applicant for and on behalf of Wenco. All contracts between Wenco and its clients were concluded and signed in Canada and the Second Applicant was paid a management fee by Wenco for the services supplied to Wenco.

Wenco, in order to obtain certainty on its VAT registration obligations, had submitted an application to SARS for a VAT Ruling in terms of section 41B of the VAT Act.

Wenco had requested a ruling confirming that the Second Applicant, its South African branch, should register for VAT as opposed to Wenco, as envisaged in the definition of 'enterprise' in section 1(1) of and that the Second Applicant should

account for VAT at the zero rate on the services supplied to Wenco in terms of section 11(2)(o) and section 11(2)(k) of the VAT Act.

SARS issued the VAT Ruling on 21 February 2019 and held the view, as appeared from the ruling, that Wenco had to register as a VAT vendor in South Africa to the extent of the Second Applicant's activities and that Wenco should charge VAT at the standard rate in respect of the services rendered to clients in South Africa and the services physically rendered by Wenco in other African countries should be zero rated, provided that section 11(3) of the VAT Act was complied with.

The Ruling, based on the information as provided, was of the view that Wenco, being a non-resident of South Africa, carried on an activity partly in South Africa that was continuous or regular and that its services were required to be supplied to any other person for a consideration in the course or furtherance of that 'enterprise' or activity. Accordingly, the second proviso to the definition of 'enterprise' in section 1(1) of the VAT Act had to be satisfied in order to regard the 'branch enterprise' in South Africa as a separate person from its main business situated permanently outside South Africa but the provisions of section 8(9) of the VAT Act were only applicable when there was an 'enterprise' and therefore supplies resulting from section 8(9) could not create an 'enterprise.'

Accordingly, the second proviso to the definition of 'enterprise' in section 1(1) of the VAT Act never intended to create a situation where a branch is registered or required to register in South Africa purely for supplies that it makes to its business permanently situated outside South Africa.

Applicants brought a review application in the High Court in terms of section 8(1)(c)(ii)(aa) of the Promotion of Administrative Justice Act 3 of 2000 in which they applied for the review and declaring unlawful and setting aside of the VAT Ruling dated 21 February 2019 issued by SARS to Wenco.

Applicants also sought to direct the Commissioner to issue a VAT Ruling in terms of which the Second Applicant should register for VAT as envisaged in the definition of 'enterprise' in section 1(1) of the VAT Act.

Applicants had pleaded various grounds of review and the substance of these grounds could be summarised as follows:

- The content of and conclusions reached in the VAT Ruling were materially influenced by an error of interpretation and application of the law to the information that was provided in the application;
- The VAT Ruling was not rationally connected to the purpose as envisaged in the specified provisions of the VAT Act, the information before SARS and the reasons given for it by SARS;
- If the VAT Ruling was to be implemented, it would render the registration of the Second Applicant nugatory and the Second Applicant would not be in a position to deduct any input VAT incurred by it which would impact negatively on the profitability of the Second Applicant.

The dispute in the case centred mainly on the interpretation of the definition of 'enterprise' in section 1(1) of the VAT Act as read with section 8(9) of that Act.

Applicants contended, in supporting their review application, that they could be separately identified and that they maintained an independent system of accounting and they were therefore to be viewed as separate persons in terms of the VAT Act.

They contended that the Second Applicant rendered the services referred to and not Wenco and they also pointed out that the Second Applicant had a distinct company registration number and income tax registration number in South Africa and, in addition, they also relied on a balance sheet and income statement of the Second Applicant to submit that an independent system of accounting was maintained.

They also contended that SARS had failed to consider the activities of the Second Applicant with reference to the relevant provisions contained in the VAT Act.

Taking into account the provisions of section 1(1) of the VAT Act, supplies made by a branch or main business situated outside South Africa were not subject to VAT. Such branch or main business was deemed to be a separate person for VAT

purposes and any supplier of goods or services by a South African branch to such an independent main business situated outside South Africa would attract VAT, unless the supply was exempt or zero-rated.

They contended that the definition of 'enterprise' in section 1(1) of the VAT Act, read together with section 8(9) of the VAT Act, meant that where any vendor carrying on an 'enterprise' in South Africa provides any service to or for the purpose of his branch or main business situated outside South Africa and the branch or main business can be separately identified and maintained an independent system of accounting, the vendor is deemed to have supplied the goods and services in the course of carrying on that 'enterprise.'

They contended, accordingly, that the approach followed by SARS in the VAT Ruling ran counter to the definition of 'enterprise' in section 1(1) of the VAT Act read with section 8(9) of the VAT Act.

SARS, however, contended that the legal person constituting the Applicants (the company incorporated in Canada) conducted an 'enterprise' in South Africa for VAT purposes in the sense that, using locally situated resources, it continuously and regularly carried on activities in the course or furtherance of which it provided software support and training services to clients both in South Africa and elsewhere in Africa in exchange for consideration.

SARS pointed out that the primary question was whether the Second Applicant (i.e. the alleged South African 'branch' of the legal person) could be said to be conducting such an enterprise separately from Wenco in the sense envisaged in proviso (ii) to the definition of 'enterprise' in the VAT Act. SARS believed not and concluded that Wenco (the foreign entity) conducted an enterprise in South Africa and that the enterprise could not be separately attributed to the Second Applicant for VAT purposes.

SARS submitted that it was Wenco that conducted the enterprise and that it should accordingly be registered as a VAT vendor to the extent that it did indeed carry on an enterprise in South Africa.

Judge Fourie held the following:

(i) That the dispute between the parties centred mainly on the interpretation of the definition of 'enterprise' in section 1(1) of the VAT Act read with section 8(9) thereof but it was necessary to also understand the Applicants' structure.

(ii) That in C: SARS v Respublica (Pty) Ltd 81 SATC 175 reference was made to the general principle as recognised in other VAT jurisdictions 'that the VAT consequences of a supply must be assessed by reference, first and foremost, to the contractual arrangements under which the supply is made.'

(iii) That the contractual arrangement between the Applicants was contained in a service level agreement (SLA) that was entered into on 17 September 2018 and in terms of this agreement Wenco appointed the Second Applicant as the 'service provider' to 'solely and exclusively…provide the services'. The services were defined in clause 1.1.9 as 'services provided by the Service Provider to Wenco for the operation of Wenco's business as detailed in clause 3…' and in clause 3 the services, duties and powers of the service provider were set out in more detail.

(iv) That, taking into account the aforesaid contractual arrangements under which the supply was made, it did not appear that the Second Applicant (as the service provider) was providing services 'to South African and other African clients of Wenco' as maintained by the Applicants. According to the SLA in clause 2 it should be accepted that the Second Applicant was appointed by Wenco to provide the services 'solely and exclusively' to Wenco. This appeared in the definition of 'services' (clause 1.1.9) where it was stated that these 'services' are to be provided by the Second Applicant (service provider) to Wenco (Wenco) for the operation of Wenco's business and not that of the Second Applicant.

(v) That apart from the contractual arrangement between the Applicants, the court also looked at the geographical arrangement between them and noted that it was clearly stated in the founding affidavit that the services were rendered by the Second Applicant for and on behalf of Wenco. Put differently, the rendering of services by the Second Applicant may

constitute the physical act of doing so in South Africa, but viewed from a legal viewpoint it seemed that the position of the Second Applicant as a branch of Wenco in South Africa, was merely that of an agent acting on behalf of Wenco 'for the operation of Wenco's (First Applicant's) business' in South Africa and, usually, no rights or obligations ensue between an agent and third parties and this may also explain why all contracts were concluded and signed between Wenco and its clients in Canada.

(vi) That, taking into account the Applicants' business structure as well as the geographical arrangement between them, it was important to understand the context within which the VAT Ruling had been requested. Taking into account the formulation of the request, the question arose whether it was the idea that only one of the applicants should register for VAT and, if so, with regard to which enterprise was a ruling sought?

(vii) That, taking into account a previous Ruling that was sought in an application of 7 April 2017, it appeared that the Applicants had the following in mind: Wenco (Wenco Canada) would not be required to register as a VAT vendor as it was not conducting an enterprise in South Africa but Second Applicant (Wenco SA) should be required to register for VAT as it was conducting an enterprise in South Africa and it would be required to zero-rate on the supply of services to Wenco which was physically rendered by Wenco to South African customers.

(viii) That, accordingly, it was not difficult to understand what the Applicants had in mind with the first request for a VAT Ruling: remove Wenco from the VAT arena and register the Second Applicant for VAT who would then be required to zero-rate on the supply of services and the result would be that neither Wenco, nor the Second Applicant would be liable for the payment of any VAT on the supply of services to the mining industry in South Africa. Also, there appeared to be no material difference between both the rulings that were sought by the Applicants. The remaining question to be answered was: Can this approach be justified in terms of the relevant provisions of the VAT Act?

(ix) That both parties accepted that the interpretation of statutes was a unitary exercise to be conducted in accordance with the approach set out in Natal Joint Municipal Pension Fund v Endumeni Municipality 2012 (4) SA 593 (SCA) at para [18].

(x) That the term 'enterprise' in section 1(1) of the VAT Act was defined as any enterprise or activity which is carried on continuously or regularly by any person in South Africa in the course of which goods or services are supplied to any other person for a consideration. The primary question was, in the court's view, whether the Second Applicant could be said to be conducting such an enterprise separately from Wenco in the sense envisaged in proviso (ii) to the definition of 'enterprise' in the VAT Act already referred to.

(xi) That in accordance with the SLA the services provided by the Second Applicant to Wenco were for the operation of Wenco's business. Put differently, the Second Applicant cannot be separately identified from Wenco as it only serves Wenco as described in the SLA, being no more than an agent of Wenco.

(xii) That, according to the SLA, it appeared to be common cause that the supplies upon which Second Applicant relied were supplies only to Wenco. It therefore seemed that the Second Applicant only served Wenco. The Second Applicant supplied no service 'to any other person' as required by the definition of 'enterprise' in section 1(1) of the VAT Act and it could therefore not be said that the Second Applicant was conducting an 'enterprise' in South Africa.

(xiii) That, furthermore, taking into account the wording 'in the Republic or partly in the Republic' as they appear in the definition of 'enterprise', one cannot seriously contend that the second proviso to the definition contemplates a situation where a branch is registered in South Africa purely for supplies that it makes to its business permanently situated outside South Africa.

(xiv) That section 8(9) of the VAT Act presupposed the existence of an 'enterprise' and as the court had concluded that Second Applicant did not conduct an 'enterprise' in South Africa as defined in the VAT Act, therefore, in the court's view, section 8(9) did not come into play.

(xv) That, accordingly, there was no basis to set aside the VAT Ruling or to direct the making of a different ruling. The second question which involved the VAT treatment of a zero rating was therefore no longer relevant as these issues only arose if the Applicants in fact fell to be treated as separate persons for VAT purposes.

Application dismissed with costs.

8.2. ITC 1946 (83 SATC 504) – Tax administration

The taxpayer's tax return for her 2014 tax year reflected taxable income of R365 919 and she also declared a receipt of R142 901 673 as a 'gift from her companion abroad'.

SARS had raised an original assessment in accordance with this return wherein the 'donation' was not subjected to tax and, after rebates, tax credits and adjustments, the net amount payable was R13 807 which the taxpayer paid.

Thereafter, in 2015, SARS started a process of interrogating the tax return and the foreign 'donation' and this led to the preparation of a draft letter of audit findings by SARS which expressed the view that the amount of some R142,9 million was not a gratuitous donation and was subject to income tax.

The parties then approved a settlement proposal and SARS issued an agreed assessment in terms of section 95(3) of the TA Act' which provided that the tax payable was R44 175 675 and no penalties or interest was raised and the money received by the taxpayer from her benefactor to settle the tax would not itself be subject to any tax.

The additional assessment was dated 17 February 2016 and accorded with the settlement communications summarised above and both sides knew that the settlement was a 'done deal.'

However, notwithstanding the above, some 31 months later on 10 September 2018 the taxpayer lodged a notice of objection to the additional assessment of 17 February 2016 and this set in motion the events leading to the present application by the taxpayer for default judgment in terms of rule 56 of the Tax Court Rules and thereby reversing what her attorneys so plainly had agreed on her behalf.

In terms of rule 7(1)(*b*) a notice of objection must be delivered within 30 days after the date of the assessment and in terms of section 104(4) of the TA Act read with rule 7(3), a senior SARS official may extend the period for objection if reasonable grounds existed for the delay. Section 104(5)(*a*) stated that an extension may not exceed 30 business days unless a senior SARS official was satisfied that exceptional circumstances existed to explain the delay.

The taxpayer had lodged her objection *via* her e-filing profile and she had not obtained an extension of time prior to doing so. Her ground for challenging the additional assessment on its merits was that tax was imposed on non-taxable income and paid on the basis of 'the pay now argue later rule.'

Even more surprising than the lodging of the objection and the making of certain statements by the taxpayer was that on 21 September 2018 SARS had issued a letter that the late submission of the objection had been allowed, *ie* condoned, and that the dispute would now be processed.

However, on 14 December 2018 SARS wrote to the taxpayer informing her that the decision to allow the late submission was 'under review' for various reasons and these included that no exceptional circumstances existed to allow an extension of more than 30 days and that SARS disputed that the taxpayer only became aware of the assessment on 7 September 2018 and that the additional assessment had been raised in terms of section 95(3) of the TA Act and was not subject to objection or appeal.

SARS further stated that although it was not obliged to do so, it was affording the taxpayer until 15 January 2019 to make representations on the matter. The letter in question was posted to the postal address given by the taxpayer in her notice of objection and it was also emailed to an email address for her which SARS had obtained from the attorneys.

The taxpayer, thereafter, on 20 February 2019, delivered a notice in terms of rule 56 of the Tax Court Rules to SARS putting it to terms for its failure to respond to her objection in accordance with the Rules. She stated that she did not receive SARS' letter and emails of 18 and 19 December 2018 and alleged that those documents were later fabrications.

SARS thereafter withdrew its condonation of the taxpayer's late objection and on 25 February 2019 SARS issued a 'notice of invalid objection' which stated that her objection did not comply with the rules because the assessment in question was an agreed assessment raised in terms of section 95(3) of the TA Act and was not subject to objection or appeal.

The taxpayer, on 5 March 2019, filed a notice of appeal against the additional assessment and in this notice she stated *inter alia* that SARS' reliance on section 95(3) was 'rejected' and warned SARS to comply with time limits as no indulgence would be allowed.

Thereafter SARS wrote to the taxpayer advising that the notice of appeal did not comply with the TA Act or the Rules and was invalid. A notice of appeal had to be preceded by an objection and the objection previously lodged by the taxpayer had been declared invalid.

The taxpayer, on 15 May 2019, delivered a further notice in terms of rule 56 regarding SARS' alleged failure to respond to her notice of appeal by delivering its grounds of assessment in terms of rule 31 and SARS was informed that if it failed to remedy its default within 15 days, the taxpayer would seek a default judgment and final order in terms of section 129(2) of the TA Act.

The taxpayer thereafter delivered her application for default judgment and SARS delivered a notice of opposition on 1 July 2019.

SARS took the view that there was no basis in fact or law for the application as the assessment in question had been issued by agreement in terms of section 95(3) and that in SARS' view the application was ‘cynical, vexatious and an abuse of the court procedures.’ The taxpayer was invited to withdraw the application by 15 July 2019, failing which SARS would file an answering affidavit and request a punitive costs order.

The taxpayer did not withdraw her application and instead on 15 July 2019 she delivered a notice requesting the Registrar to issue a hearing date and on 19 July SARS delivered its opposing papers.

The court had to consider whether the slightly late filing of SARS' opposition to the application could be condoned.

SARS' primary contention was that since it issued a notice of invalid objection, the taxpayer was not entitled to file a notice of appeal or to seek default judgment in consequence of SARS' failure to file a statement of grounds of assessment in terms of rule 31 of the rules contemplated in section 104(2) of the TA Act.

Underlying this primary contention, which is procedural in nature, was SARS' substantive assertion that the assessment against which the taxpayer objected was an agreed assessment in terms of section 95(3) of the TA Act against which the taxpayer was not entitled to pursue an objection. In other words, following the notice of invalid objection of 25 February 2019, the taxpayer could not pursue an appeal without establishing the validity of the objection. This she could have done by bringing an application to the Tax Court in terms of rule 52(2)(*b*) or a review application in the High Court but, what she could not do, SARS submitted, was ignore the notice of invalid objection and proceed with a notice of appeal as if her objection had been disallowed on its merits.

The issue before the court was whether the taxpayer was entitled to default judgment in terms of rule 56 on her own case.

Judge Rogers held the following:

As to the 'late' opposing papers

(i) That if the taxpayer's rule 56 application was duly delivered on 6 June 2019, the earliest date which the notice of motion could have specified for delivery of a notice of opposition was 10 days thereafter, ie 21 June 2019. The taxpayer's notice of motion specified 20 June 2019 as the date and the notice of opposition from SARS was in fact delivered on 1 July 2019.

(ii) That if a notice of opposition had been delivered on 21 June 2019, the earliest date which the notice of motion could have specified for the delivery of answering papers was 12 July 2019 and this was in fact the date specified. SARS had served its answering papers on 19 July 2019 – a calendar week (five business days) late.

(iii) That, however, the provisions of the rules presuppose that one is dealing with an application which may permissibly be brought in terms of those rules. SARS in its opposing papers had placed this squarely in issue, contending that the objection and notice of appeal were invalid. The taxpayer's rule 56 application is only a proper application under that rule if it was preceded by a valid objection and valid notice of appeal. If not, one is dealing with a wholly irregular application to which no time limits in terms of the rules strictly apply.

(iv) That, furthermore, SARS' opposing papers were not significantly late. By the time she launched her rule 56 application, the taxpayer knew SARS' attitude to her purported appeal and it was not unreasonable for SARS, through its attorneys, to invite the taxpayer to withdraw the application and once it became clear that she would not do so, there was no undue delay on SARS' part and the modest delay has not caused the taxpayer material prejudice.

(iv) That, accordingly, and to the extent that the opposing papers should have been delivered by 12 July 2019, the court condoned the late filing.

As to the notice of invalid objection

(v) That SARS' primary argument was that, following the notice of invalid objection of 25 February 2019, the taxpayer could not pursue an appeal without establishing the validity of the objection. This she could have done by bringing an application to the Tax Court in terms of rule 52(2)(b) or a review application in the High Court. What she could not do, SARS argued, was ignore the notice of invalid objection and proceed with a notice of appeal as if her objection had been disallowed on its merits.

(vi) That the alleged withdrawal of condonation and resultant non-compliance with the time period for lodging the objection, was not the only ground on which SARS treated the objection as invalid. More fundamentally, SARS contended that the assessment in issue was not one against which the taxpayer was entitled to object in relation to the contentious assessment, a 'taxpayer who may object' as contemplated by rule 7(1) and section 104(3) of the TA Act. Even if the taxpayer had lodged an objection within 30 days of the additional assessment of 17 February 2016, SARS would have regarded her objection as invalid and the taxpayer would then not have had the right to file a new notice of objection in terms of rule 7(5).

(vii) That the court accepted SARS' submission that the taxpayer's remedy, if she disputed the grounds on which SARS had treated her objection as invalid, was to have the Tax Court resolve the disputed validity of her objection by way of proceedings in terms of rule 52(2)(b) of the Tax Court Rules. The rules, read with the TA Act, make a determination on the merits of an objection (by way of disallowance or partial or complete allowance) a jurisdictional prerequisite for lodging a notice of appeal. If SARS declines to rule on the merits of an objection because it regards the objection as invalid, the stage of allowance or disallowance cannot be reached without resolving the disputed validity of the objection and rule 52(2)(b) was the means by which this should be done.

(viii) That SARS' notice of invalid objection dated 25 February 2019 referred only to the fact that by virtue of section 95(3) of the TA Act the additional

assessment was not one which was subject to objection or appeal. The notice did not record that the objection was also invalid because, with the withdrawal of condonation, the objection was out of time but SARS did give notice of reliance on both grounds by way of its attorneys' letter of 4 March 2019.

As to the validity of the taxpayer's notice of appeal

(ix) That if the court was wrong that the taxpayer was required to follow the rule 52(2)(b) procedure, it was still satisfied that the Application must fail. In order to obtain default judgment, the taxpayer must show that SARS was in default of an obligation to file a rule 31 statement and that depended on whether she was entitled to deliver a notice of appeal. On the assumption that SARS' decision to treat her objection as invalid could be viewed as a constructive disallowance of the purported objection, the right to pursue the appeal turned on whether she had filed a valid objection.

(x) That SARS submitted that for two reasons there was no valid objection. First, because condonation was withdrawn, the objection was filed out of time and, second, the effect of the agreement of February 2016 was that the taxpayer was not entitled to object to the assessment.

(xi) That section 9(1) of the TA Act expressly stated that a decision may be withdrawn or amended either at the discretion of a SARS official (ie mero motu) or at the request of a taxpayer and in section 9(2) the three-year restriction was clearly enacted for the benefit of taxpayers, and necessarily implicit therein was that the power to withdraw or amend decisions may be exercised adversely to the taxpayer. Hence section 9 was not capable of being interpreted in the way contended for by the taxpayer, ie that SARS could only invoke section 9 if so requested by a taxpayer and the power could only be exercised for the benefit of a taxpayer.

(xii) That the parliamentary materials referred to by the taxpayer did not support her argument but rather confirmed that the lawmaker intended to confer a power which might be exercised adversely to the taxpayer. SARS' power to

withdraw or vary a decision, as conferred by section 3(2) of the Income Tax Act, was always recognised as one which SARS could exercise mero motu in a way adverse to the taxpayer and this power was retained in section 9 of the TA Act with the insertion of an additional right on the part of an affected person to request the withdrawal or variation of a decision.

(xiii) That SARS' decision to grant condonation was not a decision to which it thereafter gave effect in an assessment or notice of assessment. It was thus a decision which SARS could in principle withdraw or amend mero motu. The three-year limit in section 9(2) was inapplicable as the condonation decision was made only a few months before its withdrawal. Moreover, the taxpayer did not allege that the withdrawal decision was not made by a competent SARS official, and, by virtue of section 9(3) it was presumed, unless the contrary was proved, that the official was duly authorised.

(xiv) That the withdrawal decision was justified on its merits scarcely required comment as the explanation offered by the taxpayer for her late submission was not candid and, in the absence of further disclosure, her explanation would have conveyed to an official unacquainted with the history that the taxpayer had only recently become aware of the additional assessment.

(xv) That SARS officials do not have an unfettered statutory power to extend the period for objecting to an assessment. For there to be any extension at all, the official must be satisfied that reasonable grounds exist for the delay. For there to be an extension of more than 30 days, the official must be satisfied that the delay is attributable to 'exceptional circumstances.' In this case the taxpayer was seeking an extension of about 30 months. There were no reasonable grounds for the delay and certainly no exceptional circumstances. The satisfaction contemplated in sections 104(4) and 104(5)(a) is a state of mind formed with reference to the true facts and this was a classic blunder which SARS was entitled to correct by way of the section 9 power.

(xvi) That, accordingly, condonation was validly withdrawn by SARS and from which it followed that there was no valid objection for SARS to disallow or for the taxpayer to pursue by way of a notice of appeal and the application must thus be dismissed.

As to costs

(xvii) That in terms of rule 50(5)(a) of the Tax Court Rules the Tax Court may, in motion proceedings, make an order as to costs that it thinks fit and in the court's view the taxpayer had to pay SARS' costs. The employment of two counsel was a reasonable precaution, having regard to the large amount at stake and the serious allegations made against SARS and its attorneys.

(xviii) That SARS had asked for a punitive costs order and the taxpayer was warned that such an order would be sought if she did not withdraw the application. The court agreed with SARS' characterisation of the application as a whole as being insupportable and an abuse of process. Furthermore, the taxpayer had made unsubstantiated allegations of serious misconduct against SARS officials and the attorney at Y Inc having the conduct of the case. In the circumstances the court was of the view that a punitive costs order was warranted.

8.3. ITC 1947 (83 SATC 545) – Capital Gains Tax

The taxpayer had acquired considerable wealth from operations and from businesses outside of the borders of South Africa.

The taxpayer held an 82% shareholding in a company by the name of BCD Corporation, an offshore company registered and incorporated in the British Virgin Islands.

The taxpayer, during 2003, had made an application for amnesty in terms of the Exchange Control Amnesty and Amendment of Taxation Laws Act 12 of 2003 and thereby had commenced the process of repatriating back to South Africa his wealth and assets, which at that stage was residing offshore. The purpose of the amnesty

application was obviously to regularise his tax affairs and to bring his assets back to South Africa.

The taxpayer accordingly disclosed to the Revenue Authorities that he owned 82% of the shares in BCD Corporation which were valued at R95 389 436, 60 and the acceptance of this valuation by the South African Reserve Bank played an integral part in the taxpayer's case when he contended the amount which should form the basis for the assessment of the base cost of the BCD SA shares which were disposed of during January 2009.

The taxpayer, during the 2009 year of assessment, had disposed of his shares in BCD (Pty) Ltd ('BCD SA') making him liable for Capital Gains Tax (CGT) in addition to interest and additional penalty taxes. BCD SA was a South African company which was registered and incorporated during 1998, but was reportedly dormant until about 2003–4.

SARS had issued the taxpayer with a revised assessment in respect of the 2009 year of assessment which was in the form of and titled 'Finalisation of Audit Letter: Revised Assessment' and the effect of the revised assessment was in essence to adjust the taxpayer's assessed income for the 2009 tax year and to bring into account additional income earned by the taxpayer during that year which he purportedly omitted to disclose, i.e. the disposal of his shares in BCD SA.

In terms of the aforesaid revised assessment the taxpayer was held liable for additional taxes and the total amount of his tax liability, inclusive of the additional taxes, amounted to R23 124 966, of which R10 618 223 related to 'capital gain on disposal of business interest.'

The taxpayer, on 2 November 2012, had objected to the revised assessment and his objection was eventually disallowed by SARS in respect of the capital gains tax levied and the related interest imposed in terms of section 89*quat*(2) of the Income Tax Act and additional penalty taxes.

The taxpayer, following the decision by SARS to disallow his objection, appealed to the Gauteng Tax Court.

The transaction under consideration was entered into on 29 January 2009 ('the agreement') when all of the BCD SA shares were disposed of in terms of a written sale of shares agreement between all of the shareholders of BCD SA, including the taxpayer, and Sail Group Limited ('the Sail Group'). The agreement expressly provided for the sale to the Sail Group of 100% of the issued share capital of BCD SA, comprising 1000 ordinary shares with a par value of one rand each. Five hundred and thirty-one of those BCD SA shares, representing 53.1% thereof, were owned at the date of the sale of the shares by the taxpayer.

The aggregate purchase price 'due and payable to' the taxpayer for the sale of his BCD SA shares 'in cash and/or in SAIL Shares' was the sum of R66 364 587, payable as follows:

- R27 944 485 in cash on the implementation date – that being 8 January 2009 and seven days after fulfilment of all of the suspensive conditions of the agreement.
- R15 264 000 – by the allotment and issue to the taxpayer of the equivalent of Sail Group shares to the value of R16 591 304; and
- R23 156 102 – on the third anniversary of the implementation date, therefore during January 2012, subject to certain warranty clauses and breach provisions in the agreement.

Simultaneously with the sale of the BCD SA shares, and as part and parcel of the same written agreement of sale dated 29 January 2009, the taxpayer also sold to the Sail Group all of his shares in BCD corporation, which, as already indicated, was an offshore company registered and incorporated in the British Virgin Islands.

The issue in this appeal was whether the taxpayer was liable for capital gains tax (CGT) as a result of the sale of his shares in January 2009 in BCD SA and, if so, the question was then how that CGT was to be calculated and, in that regard, the issues to be decided were: What were the proceeds from the sale of the shares and what was the base cost of the shares?

Judge Adams held the following:

<u>As to the accrual and calculation of CGT</u>

(i) That, reduced to the essentials, the essential factor to which regard is had in the calculation of CGT is the difference between the amount at which a person acquires a capital asset and the amount of the proceeds received on its subsequent disposal. Should such proceeds exceed the amount at which it was acquired, there is a capital gain. Conversely, should the proceeds from the subsequent disposal of the asset be less, there will be a capital loss. The aggregate of capital gains and capital losses are then taken into account to calculate a net capital gain (this being the difference between the aggregate capital gain of a year and the aggregate capital loss of the previous year) and a percentage then applied to the net capital gain to calculate the taxable capital gain for the year of assessment. In terms of section 26A of the Income Tax Act, that taxable capital gain then falls to be included in the taxable income of the person concerned.

(ii) That, in the words of par. 35 of the Eighth Schedule to the Income Tax Act , the taxpayer had disposed of his BCD SA shares on 29 January 2009 and the proceeds from such disposal in the form of the purchase price undoubtedly amounted to R66 364 578. The point was that as a result of the sale of his shares to the Sail Group an amount of R66 364 578 had accrued to the taxpayer on the said date – that much was clear from the express wording of the agreement and no interpretation thereof was required. As was held by the Supreme Court of Appeal a century ago in *Lategan v CIR* 2 SATC 16 the words in the Act 'has accrued to or in favour of any person' simply meant 'to which he has become entitled.'

(iii) That, moreover, in *Mooi v SIR* 34 SATC 1 it was held that a contingent right conditional upon the fulfilment of certain conditions could not be regarded as an 'amount' for the purposes of the definition of 'gross income', even though such a right possesses a money value at the time it was acquired by a taxpayer. Such a contingent right did no more than 'set up the machinery for creating a benefit', and the benefit accrued only when all conditions attaching to the right were fulfilled.

(iv) That what was beyond doubt was that the taxpayer had failed to disclose to SARS the aforesaid disposal in circumstances in which he was undoubtedly under a legal obligation to do so and his explanation for not making such disclosure, notably that he relied on advice received from professional advisors and that he viewed the fact that the sale agreement was subject to a number of suspensive conditions as an indication that the purchase had not yet accrued, was untenable.

(iv) That the suspensive conditions contained in the agreement provided that certain events must take place before 30 January 2009 and/or 2 February 2009. The taxpayer gave evidence that he received the first payment from the Sail Group in February 2009 and therefore the ineluctable inference to be drawn was that all of the suspensive conditions were fulfilled. If not, there would not have been payment to him of the first instalment payable. Therefore, in the court's view, the amount of R66 364 578 had 'accrued' to the taxpayer when he sold his shares in BCD SA on 29 January 2009 and that amount therefore represented 'the proceeds received or accrued' in respect of the disposal of the BCD SA shares.

(v) That insofar as the taxpayer placed reliance on the so-called 'warranty claims' that reduced the share price, SARS argued that those ought to have been dealt with in terms of par. 35(3)(*c*) of the Eighth Schedule and the court was in agreement with that submission. In any event, there was no evidence before the court that the agreed sales price, in terms of the agreement, had been reduced as a result of warranty claims.

(vi) That the starting point of the adjudication of the appeal, as SARS argued, was that, during the 2009 tax year, the taxpayer had disposed of his BCD SA shares for an amount of R66 364 578 and the only question that remained was what was the base cost of those shares that were disposed of in order to establish the amount of the capital gain that was not included in the taxpayer's income.

(vii) That SARS contended that the base costs should simply be calculated on the basis that the taxpayer had acquired the 531 shares in BCD

Corporation on 1 September 2004 – the date on which the shares were issued – at R1,00 par value, therefore R531, and the capital gain assessed on that basis. The taxpayer's case, in regard to the base cost of the asset disposed of, was to a large extent grounded on the amnesty application that he filed with the Reserve Bank during 2003. His case on the pleadings was that the valuation done for the amnesty application, of the BCD Corporation shares, constituted a valuation as required and therefore there was a capital loss when the BCD Corporation shares were disposed of. The court was of the view that the value of the shares in BCD Corporation as *per* the amnesty application should be accepted as the market value thereof at the time of the application for amnesty.

(ix) That, in the court's view, there was merit in the approach proposed by the taxpayer, that being that all of the shares held by the taxpayer in the group of companies should, for purposes of the assessment of CGT, be treated as one 'asset' as defined in the Eighth Schedule. When the court referred to a 'group of companies' it did so in the context of CGT and therefore to companies in which the taxpayer held shares. The point was that the case put forward by the taxpayer was exactly that the two companies in which he was a shareholder should be treated as if he held shares in one company. The point was that these two companies were, for purposes of this dispute a 'group'. The case related to shares in an offshore company, which the taxpayer, by the amnesty application process, intended to repatriate.

(x) That, therefore, the base cost of that asset should be determined on the basis that it was acquired on 1 September 2004 – the date on which the shares in BCD SA were issued to the taxpayer. The market value of those shares should be established and that was done by reference to the amount declared to and accepted by the *Fiscus*, as being the fair value of those shares, pursuant to the amnesty application, which was approved by the Reserve Bank. The declaration by the taxpayer in support of the amnesty application was made on 25 February 2004 and related to the period as and at 28 February 2003. In terms of this declaration, the

taxpayer had an 82% shareholding in the BCD Group of Companies – that being BCD Corporation at that stage – valued at R95 389 436,60. The court agreed that this can and should be accepted as a basis for the base cost of the asset disposed of by the taxpayer on 29 January 2009, subject to the provisos as set out in the judgment.

(xi) That, importantly, as and at 28 February 2003 or thereabout, the taxpayer owned 82% of the shares in the BCD Group of Companies, consisting at that stage only of BCD Corporation. On 29 January 2009 only 53.1% shareholding in the Group – then consisting of BCD SA and BCD Corporation – was disposed of, which meant that the base cost of 53.1% of the shareholding should be determined by pro-rating the value as follows: US$14 557 632 x 7,99 (exchange rate) x 53.1% =R61 763 519,70, i.e. being the value of a 53.1% shareholding. The court concluded that what the taxpayer had disposed of during January 2009 was only 53.1% of the 82% shareholding that he owned during 2004, the balance having been disposed of between 2003 and 2009.

(xii) The court was inclined to agree that the aforesaid approach accorded with the letter and the spirit of the relevant provisions of the Eighth Schedule to the Act and it translated into a calculation which included the CGT inclusion rate of 25% which was common cause between the parties and therefore CGT was payable by the taxpayer on the amount of R3 641 339, 58.

(xiii) That, therefore, the court was of the view that the taxpayer's tax liability ought to have been assessed on the basis that a net capital gain was realised by the sale of the shares in an amount of R14 565 367, 29, making him liable for CGT on R3 641 339, 58 and an order to that effect followed.

(xiv) That from the aforegoing it was clear that the assessment before the court did not correctly reflect the capital gain realised by the taxpayer when he disposed of his BCD SA shares and, for that matter, of his BCD Corporation shares and, as indicated, the capital gain to be included in the taxpayer's income was the amount of R14 565 367, 29.

<u>As to the taxpayer's failure to disclose the capital gain realised by it</u>

(xv) That in view of the fact that the taxpayer's assessment before the court did not correctly reflect the capital gain realised by him the court had the jurisdiction to alter the assessment in terms of section 129 of the Tax Administration Act. Section 129(2)(*b*) provided that in the case of an assessment or 'decision' under appeal the tax court may order the assessment or 'decision' to be altered. In *Africa Cash and Carry (Pty) Ltd v C: SARS* 82 SATC 73 the Supreme Court of Appeal held that 'the question whether an alteration of an assessment is competent must, like the issue of reasonableness of an assessment or the methodology used to determine the amount of an estimated assessment, be answered in the light of the facts and circumstances of each case.'

(xvi) That it was stated in the *Africa Cash and Carry* case, *supra*, that 'the point of departure should always be that the Tax Court is a court of revision and 'not a court of appeal in the ordinary sense.' The Legislature intended that there could be a rehearing of the whole matter by the Special Court and that the court could substitute its own decision for that of SARS, if justified on the evidence before it. A Tax Court accordingly rehears the issues before it and decides afresh whether an estimated assessment is reasonable. It is not bound by what SARS found. In rehearing the case it can either uphold the opinion of SARS or overrule it and substitute it with its own opinion. The powers of the Tax Court and its functions are unique and it places itself in the shoes of the functionary and re-evaluates the facts and circumstances of the subject matter on which the assessments were based….'

(xvii) That, *in casu*, and applying the aforesaid principles, the court ordered the assessment to be altered in terms of section 129(2)(*b*) of the Act. The court did not think that the matter should be referred back to SARS in terms of section 129(2)(*c*) as it would be unfair and unreasonable to do so for the simple reason that, in the circumstances of this matter and if one considers the time period which has elapsed since the revised assessment, that being

some nine years, the matter and the parties require finality. Moreover, in the court's judgment, there was no need for any further examination and investigation – all of the issues had been thoroughly and extensively canvassed by all concerned, including the taxpayer himself, and were therefore adequately ventilated and in the interests of fairness and reasonableness, the assessment stood to be altered.

(xix) That, as regards additional tax, the provisions of section 76 of the Income Tax Act (which has since been repealed) were applicable. The taxpayer's liability for additional taxes arose in the main from his failure to disclose the disposal of his shares during the 2009 tax year. His reason for this omission he placed at the door of his professional advisors and he also placed undue emphasis on the fact that he had been granted amnesty by the South African Reserve Bank on 27 October 2004. The court had difficulty in understanding how the taxpayer, given his vast experience and exposure in the business world, could have been under the impression that the once-off amnesty exonerated and relieved him from acting in the future as a responsible taxpayer.

(xix) That *in casu* the taxpayer did not disclose in his income tax return for the 2009 year of assessment that he had realised a capital gain on the sale of the BCD SA shares. The taxpayer did, however, disclose a capital loss in his 2011 return when he disposed of the Sail shares acquired in terms of the sale of shares agreement of 2009. The taxpayer therefore wanted to claim a capital loss but failed to disclose the capital gain that, on his own version, he had realised already in 2009.

(xx) That the taxpayer's contention that there were suspensive conditions that first had to be fulfilled before he could declare the proceeds from the sale of the shares, was misplaced. There was an actual receipt of money and the balance of the money was not subject to any suspensive condition, or at least no evidence was tendered that there was a suspensive condition that was not fulfilled.

(xx) That the point was that there was no justification for the taxpayer's failure to disclose to SARS that during the 2009 tax year he disposed of an asset and realised from such disposal a substantial sum of money running into tens of millions of rand and this was so despite the taxpayer's claim that he was of the view that the disposal should be disclosed only after the suspensive conditions were fulfilled and the warranties complied with.

(xxii) That what did however count in favour of the taxpayer and what may possibly amount to an extenuating circumstance was the fact that the CGT he was assessed to be liable for was way in excess of what the tax court determined such liability to be and the taxpayer, during the assessment and appeal processes, was at all times fully cooperative in resolving the dispute. The court's inclination, therefore, was not to confirm the 200% additional tax imposed by SARS but to reduce it to 25%.

(xxiii) That, as regards the interest payable in terms of section 89*quat*(3) of the Income Tax Act, there was no basis to remit the section 89*quat* interest imposed by SARS, albeit that the interest would be payable on the reduced amount of CGT liability.

(xxiv) That as regards the penalty imposed for the taxpayer's failure to submit an estimate of taxable income timeously, SARS had imposed a penalty in terms of par. 20A of the Fourth Schedule to the Income Tax Act for his failure to submit provisional tax returns. The point was, however, that the taxpayer did not believe that he should disclose the disposal of the shares for the reasons alluded to and he was now being penalised for that and it seemed innately unfair for him to be punished twice, hence the penalty in terms of par. 20A of the Fourth Schedule stood to be remitted *in toto* and, for the same reasons, the par. 20 penalty also stood to be remitted.

(xxv) That, as regards the award of costs, the court was not persuaded that the taxpayer's grounds of objection were unreasonable and that he should be ordered to pay the costs of the appeal. The court ordered that each party should therefore bear his own costs.

The taxpayer's appeal against the revised assessment for the 2009 year of assessment was dismissed.

8.4. City Power (SOC) Ltd v C:SARS (83 SATC 523)

City Power (SOC) (Pty) Ltd (City Power) was a state-owned company, registered as such in terms of the Companies Act.

SARS had issued income tax assessments in respect of the 2010–2012 years of assessment and had disallowed doubtful debt allowances claimed by City Power.

City Power had contended that, because it was a municipal entity and performed the functions that would otherwise have been performed by the City of Johannesburg (the City), it qualified for an exemption under section 10(1)(*a*) of the Income Tax Act, with effect from 1 January 2011, and section 10(1)(*b*), prior to that date.

City Power accordingly objected to the assessment and, upon the objection being disallowed, it appealed to the Gauteng Tax Court (*per* Victor J).

By agreement between the parties, this issue was determined *in limine* and separately from the merits by the Tax Court.

Section 10(1)(*a*) was promulgated after 1 January 2011 while section 10(1)(*b*) applied prior to that date.

Prior to 1 January 2011 the section 10(1)(*b*) exemption related to 'the receipts and accruals of municipalities' while as from 1 January 2011 the section 10(1)(*a*) exemption related to 'the receipts and accruals of the government of the Republic in the national, provincial or local sphere.'

Section 5 of the Income Tax Act provided that income tax (normal tax) shall be payable in respect of the taxable income received by or accrued to or in favour of any person during the year of assessment or any company during every financial year of such company.

Section 10 of the Income Tax Act is an exemption provision and provides that certain specified receipts and accruals are exempt from normal tax and the list is a closed one, with the result that, unless specifically mentioned in section 10, the receipts and accruals are taxable in terms of section 5 of the Act.

Resulting from the various amendments to the Income Tax Act, after 1 January 2011, City Power had to qualify as 'the government of the Republic in the…local sphere' for it to be exempt from normal tax.

In terms of section 40(1) of the Constitution of the Republic of South Africa 1996, the Government of the Republic of South Africa was constituted as national, provincial and local spheres of government, which were distinctive, interdependent and interrelated. Chapter 7 of the Constitution provides, among other things, for the establishment of municipalities for the whole of the territory of South Africa and municipalities established throughout the territory of South Africa constitute the local sphere of government. In terms of section 155(6) of the Constitution, each provincial government must establish municipalities in its province in a manner consistent with the legislation enacted in terms of section 155(2) and (3).

'Municipality' is defined in section 1 of the Income Tax Act as meaning:

> '[a] municipality which is within a category listed in section 155(1) of the Constitution…and which is an organ of state within the local sphere of government exercising legislative and executive authority within an area determined in terms of the Local Government: Municipal Demarcation Act 1998 (Act 27 of 1998).'

The issue before the court was whether City Power was exempted from paying tax on its income by virtue of the provisions of section 10(1)(*a*) and previously section 10(1)(*b*) of the Income Tax Act.

City Power contended that the word 'municipality' in the erstwhile section 10(1)(*b*) of the Act and the term 'local sphere of government' in section 10(1)(*a*) of the Act included a 'municipal entity' such as City Power and, if so, the section 10(1)(*a*) exemption applied and even prior to 1 January 2011 the section 10(1)(*b*) exemption applied.

City Power contended that it was to be considered a local sphere of government by virtue of *inter alia* the tight control exercised by the City.

SARS contended that City Power was not a municipality and thus not exempt from paying tax on its income and hence disputed that City Power qualified to be a local sphere of government.

Judge Ponnan held the following:

(i) That City Power plainly did not qualify as a municipality as defined in section 1 of the Income Tax Act and that ought to be the end of the enquiry insofar as the section 10(1)(*b*) exemption was concerned. However, it was contended that the exemption found application because, in discharging the constitutional functions that the City was obliged to perform, City Power acted *qua* City. Accordingly, so the argument went, its receipts and accruals fell to be treated on the same footing as those of a municipality.

(ii) That what the aforementioned contention boiled down to was that City Power must, for all intents and purposes, be deemed to be a municipality, with the result that the section 10(1)(*b*) exemption applies. Although by no means persuaded, the court assumed in City Power's favour that it was permissible to approach the enquiry in that fashion as it seemed to the court that even on this footing City Power had failed to bring itself within the exemption.

(iii) That *ITC 327* 8 SATC 254 was instructive in that the court had to there consider whether an individual who was employed by a Board that was established by and on behalf of Government was a 'government employee' for the purposes of qualifying for an exemption and found that an employee of a Board formed by the Government was nonetheless the Board's employee and not a government employee notwithstanding that Government had formed the Board.

(iv) That *in casu* the City simply enjoyed the ordinary powers of a shareholder over City Power which had an independent Board of Directors which was

autonomous, exercised its powers independently and was enjoined to act in the interests of City Power. Its powers, as appear in City Power's memorandum of incorporation, are wide and substantial and were, crucially, in the nature of those ordinarily associated with private companies.

(iv) That City Power may also form and have an interest in any company or companies, amalgamate with other companies and take part in the management, supervision and control of the business or operations of any similar company or business. It may also enter into partnerships. In terms of the Service Delivery Agreement concluded between City Power and the City on 1 September 2006, the services to be provided by the former were electricity distribution services, which constituted its core business. It may however undertake any business other than its core business, albeit with the City's consent, which consent shall not be unreasonably withheld.

(v) That, moreover, Parts 5 and 6 of Chapter 8A of the Local Government: Municipal Systems Act contain a range of measures that are designed to ensure the independence of the Board. Section 93A(*b*) provides that the parent municipality of a municipal entity 'must allow the board of directors and chief executive officer of the municipal entity to fulfil their responsibilities' and section 93E regulates the appointment of Directors of the Board and provides that the board of directors of a municipal entity must have the requisite range of expertise to effectively manage and guide the activities of the municipal entity.

(vi) That the Local Government: Municipal Finance Management Act was also of relevance in that it provided that a municipal entity must open and maintain at least one bank account in the name of the entity and all money received by a municipal entity must be paid into its bank account or accounts and the bank account must be administered by the accounting officer (the CEO) who is accountable to the Board for the entity's bank accounts. As such, the fact that City Power might have agreed, through a service level agreement, to grant the City access to its accounts, did not

change the fact that any decision over that bank account is exercised solely by the Accounting Officer and the Board.

(vii) That City Power's business was to be run along commercial lines, its object being to generate profit in the course of distributing electricity. There appeared to be no restriction on City Power generating a profit and the effect of creating a private company for purposes of performing the functions of electricity distribution was that the receipts and accruals were those of the company, whereas in instances where the City itself directly distributed electricity (i.e. after purchasing in bulk from Eskom for downstream on-selling to consumers within its geographical jurisdiction), the receipts and accruals in relation to the supply of electricity would fall into the general funds of the municipality.

(ix) That it was not in dispute that the income from the supply of electricity by City Power was the income of City Power, notwithstanding that the City may have access to such monies. Such income was reflected in City Power's financial statement and the funds thus accrued to City Power. What it decided to do with such funds at a later stage did not change its character.

(x) That the court then considered whether City Power fell within the concept of the 'local sphere of government.' The Constitutional Court explained that a 'sphere of government' is a clearly defined concept and did not necessarily include an organ of state which performs a function that would ordinarily have been performed by the government. In a similar vein the Supreme Court of Appeal held that the Office of the Public Protector was 'not a department of state or administration and neither could it be said to be part of the national, provincial or local spheres of government.

(xi) That the aforementioned considerations apply equally to City Power. It was not part of the local sphere of government and was thus not located within such sphere. The mere fact that it performed constitutional functions, which would ordinarily have been performed by the City, did not mean that it was part of or located within the local sphere of government.

(xii) That City Power had relied on *Grinpal* and *Joseph* and contended that in those judgments the Constitutional Court had 'characterised [City Power] through its functions.' City Power's reliance on these judgments was, however, misplaced as those judgments merely reiterated a trite principle, namely that City Power performed a public function. That much is not in dispute. *Grinpal* and *Joseph* do not state that simply because City Power performs a public function it fell within the local sphere of government and nor did *Allpay*.

(xiii) That, accordingly, there was no merit in the suggestion that City Power fell within the local sphere of government. As the receipts and accruals of City Power are not those of 'the government of the Republic' in any of the spheres (i.e. the national, provincial or local spheres), and were at no stage the 'receipts and accruals of municipalities', the section 10(1)(*a*) and 10(1)(*b*) exemptions do not apply in respect of the income in issue.

Appeal dismissed with costs, including those of two counsel.

9. INTERPRETATION NOTES

9.1. Value-Added Tax consequences of points-based loyalty programmes – No. 118

This Note clarifies the VAT implications resulting from the participation in loyalty programmes based on the current provisions of the VAT Act. This Note does not attempt to list and analyse all the loyalty programmes available. Loyalty programmes differ from each other, evolve and change because of continuous changes in market conditions, competition etc. For this reason, the general VAT principles applicable to loyalty programmes as contained in this Note must be analysed and subsequently applied to each transaction in a loyalty programme in accordance with that specific loyalty programme's characteristics or nature.

Notwithstanding that this Note may in certain instances highlight the VAT implications of other benefits generally associated with loyalty programmes, the

main focus of this Note is to address the VAT implications of points-based loyalty programmes.

More specifically, this Note concentrates on loyalty programmes that regard loyalty points as a form of payment or part-payment for goods or services, in line with the nature of loyalty points. Should any of the agreements contain provisions that specifically contradict this, for instance where the relevant agreements evidence loyalty points to be regarded as a discount on future purchases, this Note does not apply to the specific circumstances.

All examples contained in this Note are based on the assumption that the relevant parties of a loyalty programme are all vendors.

The policies and further applications associated with vouchers, tokens or stamps are not discussed in detail in this Note.

This Note sets out the VAT treatment of the most common transactions in loyalty programmes currently in operation in South Africa. Whilst there may be other types of loyalty programmes, the focus of this Note is to provide legislative certainty to the stakeholders participating in a loyalty programme on the VAT consequences of pointsbased loyalty programmes, specifically where the loyalty points are regarded as payment or part-payment for goods or services. It is the responsibility of each participant in a loyalty programme to establish the nature of its involvement (or role) in a specific loyalty programme in order to determine the VAT treatment of each transaction.

9.2. Supplies made for no consideration – No. 70 (Issue 2)

This Note:

- sets out the legal framework for the VAT treatment of supplies of goods or services which are made by vendors for no consideration in certain circumstances; and
- provides guidance to vendors, on whether:

- input tax may be deducted in respect of any VAT incurred on goods or services acquired to make supplies for no consideration; and
- output tax must be declared on any goods or services supplied for no consideration.

The definition of 'enterprise' in section 1(1) is one of the most important definitions in the VAT Act. This definition's main purpose is to include all types of activities but equally, sets out specifically the type of persons, activities and supplies which are intended to form part of the tax base, as well as those that are meant to be excluded. Under paragraph (a) of this definition, there is a general requirement that enterprises participating in the VAT system must charge a consideration (price) for the goods or services they supply.

The implication of not meeting this requirement is that supplies made for no consideration are not made in the course or furtherance of an enterprise, and hence, will not be a taxable supply. However, there are many different circumstances under which enterprises will, for purely commercial reasons, make a supply without charging a consideration.

This raises the question as to whether there are certain circumstances under which a supply for no consideration may be regarded as a taxable supply, and consequently, whether it will be possible for the supplier to deduct input tax on any expenses incurred for the purpose of making those supplies.

The ability to correctly characterise a particular supply as being taxable or not is important because the vendor will generally have a right to deduct the VAT incurred on any goods or services acquired for the purposes of making taxable supplies, but will not be able to do so if the supplies are exempt, out-of-scope, or in connection with any other non-taxable activities conducted by the vendor.

In order to fully understand the VAT treatment of supplies made for no consideration under the South African VAT system, it is necessary to understand the underlying framework which influences the design of the VAT system, as well as the general international characteristics and principles upon which a VAT system of taxation is based. This is important because, although the different

countries that have a VAT regime have very similar core features, there are often a number of differences in the detail of how the features and designs of those systems apply.

This Note explains the factors to consider when determining whether a supply made for no consideration is a taxable or non-taxable supply, and consequently, whether there is a liability to declare output tax, or an entitlement to deduct input tax on any goods or services acquired to make those supplies.

Supplies made for no consideration can be made under many different circumstances and as it is not possible to include every situation. The approach of the Note is to provide a general rule to illustrate the circumstances under which the VAT incurred in such cases may be deducted as input tax. Further specific scenarios are also discussed to demonstrate how this rule works in practice within the context of the meaning of an 'enterprise' as defined in section 1(1). Further context is provided with reference to some of the generally accepted international principles upon which a VAT system of taxation is based. Of particular importance in this regard is the general requirement that supplies must be made for a consideration.

Most of the difficulties arise when supplies made for no consideration are made by associations not for gain, PBOs and welfare organisations, as they sometimes have a mixture of enterprise and non-enterprise activities. Such organisations may have difficulty in characterising the supplies correctly as taxable or non-taxable, or have difficulty in correctly allocating their expenses in this regard.

When considering the VAT implications of supplies (including supplies made for no consideration), vendors should be careful to characterise the supply correctly in accordance with the definition of 'enterprise' as defined in section 1(1). This requires a distinction to be made between taxable supplies made in the course or furtherance of an 'enterprise' and any exempt, out-of-scope or other non-taxable supplies.

A distinction must also be made between a situation where supplies are made for no consideration and a situation where no activity or 'enterprise' is conducted,

because no supplies are made to any other person. In drawing this distinction it should be kept in mind that section 10(23) is a valuation rule which merely provides that the valuation of a supply may be nil in certain circumstances and cannot be used to characterise a supply as being taxable or non-taxable.

Activities conducted without giving rise to a supply of goods or services to another person, or which primarily involve the making of supplies for no consideration are generally not regarded as activities conducted in the course or furtherance of an enterprise. Consequently, the VAT incurred in conducting such activities is generally not deductible as input tax. However, where promotional supplies made for no consideration are attributable to the taxable activities conducted by the enterprise, the VAT incurred to make those supplies may generally be deducted as input tax to the extent that the supplies are made with a commercial rationale in mind. This must be distinguished from a situation where the supplies concerned are purely benevolent in nature. In such a case, the supplies are not regarded as being made in the course or furtherance of an enterprise unless they are made by a 'welfare organisation' in the course of conducting its 'welfare activities'.

10. BINDING PRIVATE RULINGS

10.1. BPR 368 – Payments made pursuant to an agreement relating to a permission to occupy

This ruling determines the income tax and donations tax consequences resulting from payments to be made pursuant to an agreement relating to a permission to occupy.

In this ruling references to sections are to sections of the Income Tax Act applicable as at 30 June 2021. Unless the context indicates otherwise any word or expression in this ruling bears the meaning ascribed to it in the Act.

This is a ruling on the interpretation and application of:

- section 11(a) read with 23(g);

- section 11(f);
- section 54;
- section 55, definition of 'donation'; and
- section 58.

Parties to the proposed transaction

The applicant: A resident company

The trust: A resident trust

Description of the proposed transaction

The trust holds certain land for the benefit of a community. The trustees granted Permissions to Occupy (PTOs) in respect of two properties to a third party financing house (Financier) for the purpose of developing and leasing out the properties to the applicant.

The Financier let the properties to the applicant in terms of a long-term lease and the same parties also concluded a development agreement on the same day, in terms of which the applicant was appointed to develop the properties on the lessor's behalf. In terms of the development agreement, the applicant was required to construct, on each property, business premises for its use together with certain ancillary facilities to be used by other businesses.

The applicant carries on a business operation on each property. The Financier paid for the costs incurred by the applicant to develop the properties out of funding which it obtained from a bank. In terms of the lease agreement, the applicant was to pay rentals during the first 10 years of the term of the lease agreement that were sufficient to enable the Financier to repay the bank loan together with interest thereon. Thereafter it paid a nominal rental as per the lease agreement. The applicant was also obliged to pay annual rental due in respect of the PTOs.

The PTOs provided for the payment of a nominal annual rental and furthermore provided that the rental amount may be renegotiated every three years.

The traditional authority representing the community engaged with the applicant

and expressed the view that the trust has not been adequately compensated in accordance with the relevant clauses of the PTOs read together with the terms of the lease agreement for the privilege of occupying the properties and therefore requested the applicant to adequately compensate the community for its use of the properties.

The applicant acknowledges that:

- The properties it occupies together with the improvements that have been constructed on it are valuable for both the applicant and sublessees who hire ancillary facilities on the properties.
- It has enjoyed the benefit of occupying the properties at relatively insignificant rentals.

The applicant wishes to retain the use of the properties for the remaining term of the lease agreement, which exceeds 10 years, and does not wish to become involved in protracted and costly disputes with the community and the trust and, in the circumstances, it has agreed to make payments envisaged in an in principle agreement it has entered into with the trust. The payments will consist of a once-off initial lump sum payment and additional monthly payments for the remainder of the lease term.

In return for the payments that the applicant will make to the trust in terms of the agreement, the traditional authority will confirm that the PTOs, in respect of the properties, remain valid and enforceable and undertakes that it shall do certain additionally agreed things to ensure that the applicant can enjoy its rights under the lease agreement and to ensure that the PTOs remain in place.

Conditions and assumptions

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

Ruling

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

- The proposed initial lump sum payment will qualify for the allowance under

section 11(f). In calculating the amount that will be deductible in each year of assessment, paragraph (aa) of the proviso to section 11(f) will apply.

- The proposed monthly payments will be deductible under section 11(a) read with section 23(g).
- Neither of the proposed payments will be regarded as a 'donation' as defined in section 55(1) or deemed to be a donation as envisaged under section 58(1) for donations tax purposes.

10.2. BPR 369 – Deductibility of interest incurred pursuant to liquidation of company

This ruling determines that interest that arose, out of the investment proceeds of assets sold in the course of a liquidation and is paid to trade creditors in terms of sections 95 and 103 of the Insolvency Act 24 of 1936 (the Insolvency Act), is not deductible in the determination of taxable income.

In this ruling references to sections are to sections of the Income Tax Act applicable as at 23 June 2021. Unless the context indicates otherwise any word or expression in this ruling bears the meaning ascribed to it in the Act.

This is a ruling on the interpretation and application of:

- section 11(a); and
- section 24J(2).

Parties to the proposed transaction

The applicant: A resident company in liquidation and its liquidators

The creditors: Creditors with proved claims against the company

Description of the proposed transaction

The company ceased trading and the liquidators commenced with its winding-up and the realisation of its assets.

The resultant proceeds were invested and consequently earned interest.

The liquidators are legally required to apply the nett proceeds against the capital and interest of all proven claims. The proven claims all related to trade debt. Only one of the trade debts carried any provision for interest and hence no interest was incurred by the applicant in relation to the trade debts, with the exception of the one creditor.

The applicant will therefore actually incur interest in relation to the proved claims when the Master of the High Court (the Master) confirms the Liquidation and Distribution account.

Conditions and assumptions

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

Ruling

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

- The interest payable by the applicant will be actually incurred in the year of assessment when the Master confirms the Liquidation and Distribution Account.
- The interest payable by the liquidators will not qualify for any deduction under sections 24J or 11(a) on the basis that it will not be incurred in the production of income.
- Practice Note 31 does not apply to the proposed transaction.

10.3. BPR 370 – Registration of shares in the name of beneficial holder

This ruling determines the donations tax, securities transfer tax and transfer duty consequences for the co-applicant on the registration of shares held in the name of the co-applicant, the registered holder, in the name of the applicant, the beneficial

owner.

In this ruling references to sections and paragraphs are to sections of the Income Tax Act and paragraphs of the Eighth Schedule to the Act, and to sections of the STT and TD.

Acts, as at 22 October 2021. 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 Act
  - section 54;
  - section 55(1);
  - section 57;
  - section 58;
  - paragraph 11; and
  - paragraph 35.
- the STT Act
  - section 2(1)(a)(i) read with the definition of 'transfer' in section 1.
- the TD Act
  - section 2(1)(b)(i).

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

The applicant: A natural person who is a resident

The co-applicant: A natural person who is a resident

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

The applicant needed a property on which to conduct his business and arranged with his attorney that it be acquired on his behalf and registered in the name of one of the employees of the attorney. The attorney and employee acted as a nominee of the applicant with the acquisition and registration of the property. The property

was later transferred to a company and the shares were similarly held in name only, by one of the employees of the attorney.

At all times since the acquisition of the property, and at all times when the shares in the company were held, the applicant had control of the property. The applicant funded and maintained the property, paid all rates and taxes on the property and incurred all costs of renovations and extensions. Consequently, the applicant had possession and control of the property since its acquisition.

The proposed transaction involves the registration of the shares in the name of the applicant who is and always was the beneficial owner and holder of the shares in question.

Conditions and assumptions

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

Ruling

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

- The registration of the shares in the name of the applicant and the contemporaneous deregistration of the co-applicant will not constitute a disposal for purposes of the Eighth Schedule.
- Paragraph 38 of the Eighth Schedule will not apply to the proposed transaction.
- The registration of the shares in the name of the applicant will not constitute a 'donation' by the co-applicant as defined in section 55(1) of the Act, nor a deemed donation as envisaged in section 58(1).
- No Securities Transfer Tax will be payable on the proposed transaction.
- No Transfer Duty will be payable on the registration of the shares in the name of the applicant.

11. BINDING GENERAL RULINGS

11.1. Whether the term 'consideration' includes an amount of transfer duty for the purposes of calculating a notional input tax deduction n the acquisition of second-hand fixed property BPR – No. 57 (VAT)

For purposes of this ruling:

- 'notional input tax deduction' means an amount of input tax calculated under paragraph (b) of the definition of 'input tax', which may be available to a vendor on the acquisition of second-hand goods (including second-hand fixed property) under section 16(3)
- 'section' means a section of the VAT Act;
- 'tax fraction' means the fraction calculated in accordance with the formula:

  r / 100 + r

  in which formula 'r'1 is the rate of tax applicable under section 7(1);
- 'Transfer Duty Act' means the Transfer Duty Act 40 of 1949;

Purpose

This BGR clarifies whether the term 'consideration' includes an amount of transfer duty paid or payable on the acquisition of second-hand fixed property for the purposes of calculating a notional input tax deduction.

Background

When second-hand fixed property is supplied by a person that is not a VAT vendor, transfer duty will usually be payable on that transaction, subject to any exemptions or exceptions that may apply under the Transfer Duty Act. Transfer duty is only applicable if the supply of fixed property is not a taxable supply under the VAT Act.

If the person acquiring the fixed property is a registered VAT vendor and is using that property for taxable purposes in an enterprise, that vendor will, in principle

(and subject to certain requirements), be entitled to a notional input tax deduction. The deduction is made under section 16(3)(a)(iiA) if the vendor is registered on the invoice basis of accounting or section 16(3)(b)(i) if the vendor is registered on the payments (or cash) basis of accounting.

The issue that arises in this regard is whether the transfer duty on the transaction is included in the meaning of the term 'consideration' as defined in section 1(1) of the VAT Act, for the purposes of claiming a notional input tax deduction.

Discussion

Consideration

The definition of the term 'consideration' is explained in Interpretation Note 70 'Supplies Made for no Consideration' (IN 70). In particular, paragraph 5.1.2 of IN 70 explains the characteristics as follows:

- That it can include any payment which is 'in respect of, in response to, or for the inducement of' a supply of goods or services.
- There must be a sufficient nexus between the supply and any payment of consideration.
- The payment of consideration can be made in money or in kind, and can be made by any person.

Whilst the term suggests a broader scope to encompass any payment, in simple terms, the consideration refers to the purchase price that must be paid to the supplier of goods or services by the recipient.

Notional input tax deduction

As provided for in paragraph (b) of the definition of 'input tax', a notional input tax deduction on the acquisition of second-hand goods is calculated by applying the tax fraction at the time of acquisition to the lesser of:

- any consideration in money given by the vendor; or
- the open market value of the goods.

Other requirements, for example, that the goods must be acquired by the recipient in the course or furtherance of carrying on an enterprise and that the requisite documentary proof must be held in accordance with section 20(8) must also be met before a notional input tax deduction may be allowed.

Extent to which consideration has been paid

Paragraph (b) of the definition of 'input tax' must be read together with section 16(3)(a)(iiA) or 16(3)(b)(i) when calculating the deductible amount of notional input tax. Under these provisions, the payment in money is recognised to the extent that it has the effect of reducing or discharging any obligation relating to the purchase price for the supply during the tax period concerned.

If payment of the consideration (purchase price) for the property is made in terms of the contract by the recipient or any other person to:

- the supplier; or
- any other person at the request of the supplier,

such payment towards the purchase price is recognised for the purposes of calculating the notional input tax deduction.

Transfer duty

Transfer duty is levied under section 2 of the Transfer Duty Act for the benefit of the National Revenue Fund on the value of any 'property' acquired by any person. Under section 3 of that Act, transfer duty is a charge levied against the person acquiring the property and is payable to SARS by that person. As such, transfer duty does not form part of the purchase price of the property. Consequently, the payment of transfer duty cannot be regarded as an amount which reduces or discharges any obligation of the recipient relating to the purchase price of the property

Ruling

The term 'consideration' as defined in section 1(1) does not include any transfer

duty imposed under section 2 of the Transfer Duty Act. As a result, the amount of transfer duty paid or payable by a vendor to acquire second-hand fixed property for taxable purposes cannot be included in the calculation of any notional input tax deduction which may be available to that vendor under section 16(3)(a)(iiA) or 16(3)(b)(i).

11.2. Purchase of different types of annuities at retirement – No. 58

For the purposes of this ruling:

- 'retirement fund' refers collectively to a 'pension fund', 'pension preservation fund', 'provident fund', 'provident preservation fund' or 'retirement annuity fund' as defined in section 1(1); and
- 'the Pension Funds Act' means the Pension Funds Act 24 of 1956.

<u>Purpose</u>

The purpose of this BGR is to confirm that, for income tax purposes, any annuity purchased or provided by any retirement fund must be compulsory, non-commutable, payable for and based on the lifetime of the retiring member or the value of the member's retirement interest, if applicable.

It is further to confirm that the annuity may not be transferred, assigned, reduced, hypothecated or attached by creditors as contemplated by the provisions of sections 37A and 37B of the Pension Funds Act.

<u>Background</u>

General Note 12, issued on 20 July 1995, confirmed that even though some approved pension, provident and retirement annuity funds were, in terms of the rules of those funds, terminating that retirement fund's liability to pay an annuity, the retirement fund could not terminate its liability to pay an annuity. General Note 18 replaced General Note 12 with effect from 1 September 2008.

General Notes 18 and 18A were issued following discussions held with various

representatives of the retirement fund industry. By virtue of an agreement, retirement funds were permitted to terminate their continued liability in respect of a retiring member once an annuity was purchased, subject to certain terms and conditions as laid out in General Notes 18 and 18A. Both General Notes 18 and 18A were withdrawn on 26 February 2021.

This BGR is now issued to provide clarity after the withdrawal of General Notes 18 and 18A.

Discussion

The provisos to the definition of the different types of retirement fund permit the Commissioner to prescribe additional limitations and conditions for the approval of rules of retirement funds. This discretion may be exercised whenever the Commissioner deems it necessary. General Notes 18 and 18A were issued in terms of this discretion of the Commissioner.

Any annuity so purchased in the name of the retiring member, in the name of the retirement fund or paid directly by such a retirement fund must be compulsory, noncommutable, payable for and based on the lifetime of the retiring member or the value of the member's retirement interest, if applicable. The annuity may not be transferred, assigned, reduced, hypothecated or attached by creditors as contemplated by the provisions of sections 37A and 37B of the Pension Funds Act.

This is in line with Regulation 39 of the Pension Funds Act that requires trustees to have an annuity strategy for members, which may include the methods listed below.

It is, however, not something specifically governed by the Income Tax Act, but rather by the provisions in the Pension Funds Act, as stated above.

The definitions of each type of retirement fund state that up to one-third of the member's total retirement interest may be commuted for a single payment and the remainder must be paid in the form of an annuity (including a living annuity). These provisions in the Act do not prescribe whether the annuity must be provided by the retirement fund or purchased from an insurer, nor do they prescribe the nature or characteristics of such an annuity.

It should, however, be noted that there is no distinction between member owned annuities and fund owned annuities purchased when the member retires from the retirement fund.

Ruling

It is accepted that, as per the agreement with the retirement fund industry and the practice generally prevailing at this point, the following practice still prevails and is in line with an exercise of the Commissioner's discretionary power in the definitions of all types of retirement funds in section 1(1). The rules of retirement funds may therefore provide for:

- the retirement fund paying the annuity directly;
- purchasing the annuity in the name of the retirement fund;
- purchasing the annuity in the name of a retiring member; and
- any combination of the aforementioned methods, provided that multiple annuities of each type may be provided for.

It is further confirmed that an annuity provided on retirement may not be transferred, assigned, reduced, hypothecated or attached by creditors and must be compulsory, non-commutable, payable for and based on the lifetime of the retiring member.

12. GUIDES

12.1. VAT Rulings Process – Reference Guide

This guide provides information and guidelines on the value-added tax (VAT) rulings process.

It sets out the steps to be followed when applying for a VAT class ruling or a VAT ruling (collectively referred to as a VAT ruling, or a ruling, unless the context indicates otherwise) and explains certain terms.

This guide does not deal with the process to be followed when applying for an advance tax ruling (ATR) that is, a binding class ruling or binding private ruling issued by the ATR unit, which process is also published on the SARS website. This guide also does not deal with the process to be followed in applying for a decision under section 72. See Binding General Ruling (BGR) 56: Application for a Decision under Section 72 and VAT Section 72 Decision Process Reference Guide on the SARS website in this regard. The issuing of a VAT ruling is governed by section 41B of the VAT Act read with Chapter 7 of the TA Act. The information in this guide is based on the VAT and TA Acts as at the time of publishing and includes the amendments contained in the Taxation Laws Amendment Act 23 of 2020, the Rates and Monetary Amounts and Amendment of Revenue Laws Act 22 of 2020 and the Tax Administration Amendment Act 24 of 2020, promulgated on 20 January 2021 in Government Gazettes (GGs) 44083, 44082 and 44080, respectively.

A decision should be distinguished from a VAT ruling, the main distinction being that a VAT ruling pertains to the interpretation of the VAT Act whereas a decision constitutes the exercising of a discretion (see section 9 of the TA Act). Certain decisions are subject to objection and appeal as set out in section 32 of the VAT Act and section 104 of the TA Act.

The difference between a VAT ruling and a decision is illustrated by the examples set out below.

Example 1 – Application for a decision

Facts:

A vendor, registered on the invoice basis, makes a written application to be registered on the payments basis under section 15(2) by completing and submitting the prescribed VAT117 form.

Does the request qualify as an application for a VAT ruling or a decision?

Result:

The Commissioner is required to exercise discretion in directing that the vendor may be registered on the payments basis. The Commissioner will give effect to the decision by changing the accounting basis to the payments basis (should the vendor qualify to be on the payments basis) and issue a notification accordingly. The application qualifies as a request for a decision.

Example 2 – Application for a VAT ruling

Facts:

A vendor, supplying marketing services to a non-resident, wants to confirm whether VAT may be levied at the zero-rate under section 11(2)(l). Does the request qualify as an application for a VAT ruling or a decision?

Result:

The question relates to the interpretation of the law with reference to a specific set of facts. The vendor may therefore apply for a VAT ruling.

In certain instances, the law provides guidance, but does not allow for discretion to be exercised. In these instances, the matter cannot be dealt with either as a decision or a VAT ruling.

Example 3 – Guidance in law

Facts:

A vendor supplies holiday accommodation that includes daily transport by road to points of interest, for a single consideration. The vendor wants to confirm how to attribute the consideration charged partly to the making of the taxable supply (the accommodation) and partly to an exempt supply (the transport of fare-paying passengers) under section 10(22).

Does the request qualify as an application for a VAT ruling or a decision?

Result:

The request does not qualify as an application for either a VAT ruling nor a decision. This is on the basis that there is no discretion afforded to the Commissioner as to how to determine the different parts of the consideration as contemplated in section 10(22).

13. DRAFT GUIDES

13.1. Draft Guide to the Voluntary Disclosure Programme

The VDP was introduced as a permanent measure to increase voluntary compliance in the interest of enhanced tax compliance, good management of the tax system and the best use of the SARS resources. The VDP is intended to encourage taxpayers to voluntarily disclose tax defaults. The VDP is administered under Part B of Chapter 16 and contains the requirements for a valid voluntary disclosure and available relief.

One of the main benefits of the VDP is the granting of relief for an understatement penalty under Chapter 16. The VDP provisions in Part B of Chapter 16 do not override the other specific provisions in the TA Act. The VDP is applicable to all taxes administered by SARS except for the customs and excise legislation. Taxpayers qualifying for the VDP will be granted relief on applicable understatement penalties, qualifying administrative penalties, criminal prosecution in relation to a valid voluntary disclosure, and the conclusion of the voluntary disclosure agreement.

A strict interpretation is applied to determine whether an applicant meets the requirements under Part B of Chapter 16 to qualify for voluntary disclosure relief. This principle was confirmed in Western Platinum Ltd v C: SARS in which the Supreme Court of Appeal held that it is a well established principle of interpretation when dealing with provisions creating tax privileges to reject a construction of such a provision that implied the extension of such privilege and to interpret the provision strictly.

Contents:

- Applying for voluntary disclosure relief
  - Definition of 'default
  - Persons that may apply for voluntary disclosure relief
  - Disqualification of person subject to audit or criminal investigation
  - Requirements for a valid voluntary disclosure
    - Disclosure
    - Voluntary Involves a default which has not occurred within five years of the disclosure of a similar default
    - Full and complete in all material respects
    - Must involve a specific behaviour
    - Does not result in a refund due by SARS
    - Prescribed form and manner
- Voluntary disclosure agreement
  - Entering into voluntary disclosure agreement
  - Reporting of voluntary disclosure agreements
- Voluntary disclosure relief
  - Types of voluntary disclosure relief granted
  - Withdrawal of voluntary disclosure relief
- Assessment or determination
- Objection and appeal
- Confidentiality of information

14. INDEMNITY

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