TAX UPDATE

For period: January 2023 to March 2023

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JK TAX SPECIALISTS

Shepstone & Wylie ATTORNEYS

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1. FOREWORD

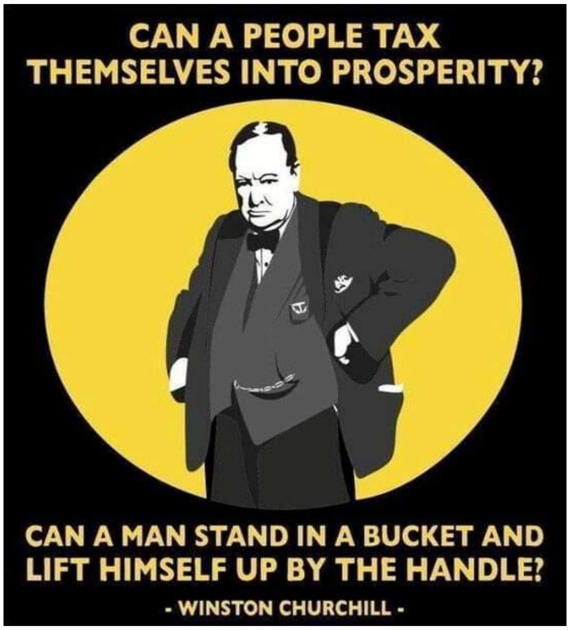
The purpose of this update is to summarise developments that occurred during the first quarter of 2023, specifically in relation to Income Tax and VAT. Johan Kotze, a Tax Executive at Shepstone & Wylie Attorneys, has compiled this summary.

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!

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BY DIK BROWNE
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HE'S DRUNK!
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IT'S POSSIBLE!
MEN WILL TRAVEL TO THE MOON... TO THE BOTTOM OF THE SEA AND TAXES WILL BE REDUCED!
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HE'S DRUNK!
DIK BROWNE
8-5
To my favorite editor and original believer in Hagar – all my best – DIK BROWNE

2. AMENDMENT ACTS PROMULGATED

The following Amendment Acts were promulgated on 5 January 2023:

- Act No 16 of 2022 – Tax Administration Laws Amendment Act, 2022 (GG 47827 – 16/01/2022)
- Act No 19 of 2022 – Rates and Monetary Amounts and Amendment of Revenue Laws Act, 2022 (GG 47825 – 19/01/2022)
- Act No 20 of 2022 – Taxation Laws Amendment Act, 2022 (GG 47826 – 20/01/2022)

3. BUDGET

3.1. Personal tax rates

2023 year of assessment		2024 year of assessment	
Taxable Income	**Rates of tax**	**Taxable Income**	**Rates of tax**
R0 – R226 000	18% of each R1	R0 – R237 100	18% of each R1
R226 001 – R353 100	R40 680 + 26% of the amount above R226 000	R237 101 – R370 500	R42 678 + 26% of the amount above R237 100
R353 101 – R488 700	R73 726 + 31% of the amount above R353 100	R370 501 – R512 800	R77 362 + 31% of the amount above R370 500
R488 701 – R641 400	R115 762 + 36% of the amount above R488 700	R512 801 – R673 000	R121 475. + 36% of the amount above R512 800

R641 401 – R817 600	R170 734 + 39% of the amount above R641 400	R 673 001 – R857 900	R179 147 + 39% of the amount above R673 000
R817 601 – R1 731 600	R239 452 + 41% of the amount above R817 600	R857 901 – R1 817 000	R251 258 + 41% of the amount above R857 900
R1 731 601 and above	R614 192 + 45% of the amount above R1 731 600	R1 817 001 and above	R644 489 + 45% of the amount above R1 817 000
Rebates		**Rebates**	
Primary	R16 425	Primary	R17 235
Secondary	R9 000	Secondary	R9 444
Third rebate	R2 997	Third rebate	R3 145
Tax threshold		**Tax threshold**	
Below age 65	R91 250	Below age 65	R95 750
Age 65 and over	R141 250	Age 65 and over	R148 217
Age 75 and over	R157 900	Age 75 and over	R16 6895

3.2. Medical tax credits

Medical tax credits will increase from R347 to R364 per month for the first two members, and from R234 to R246 per month for additional members.

3.3. Expansion of the renewable energy tax incentive

The tax incentive available for businesses to promote renewable energy will be temporarily expanded to encourage rapid private investment to alleviate the energy crisis.

The current incentive allows businesses to deduct the costs of qualifying investments over a one- or three-year period, which creates a cash flow benefit in the early years of a project. Businesses are able to deduct 50% of the costs in the first year, 30% in the second and 20% in the third for qualifying investmentsin wind, concentrated solar, hydropower below 30 megawatts (MW), biomass and photovoltaic (PV) projects above 1 MW. Investors in PV projects below 1 MW are able to deduct 100% of the cost in the first year.

Under the expanded incentive, businesses will be able to claim a 125% deduction in the first year for all renewable energy projects with no thresholds on generation capacity.

The adjusted incentive will only be available for investments brought into use for the first time between 1 March 2023 and 28 February 2025.

For a business with positive taxable income, the deduction will reduce its tax liability. For example, a renewable energy investment of R1 million would qualify for a deduction of R1.25 million. Using the current corporate tax rate, this deduction could reduce the corporate income tax liability of a company by R337 500 in the first year of operation.

3.4. Rooftop solar tax incentive

To increase electricity generation, government is also proposing a rooftop solar incentive for individuals to invest in solar PV. Individuals will be able to receive a tax rebate to the value of 25% of the cost of any new and unused solar PV panels.

To qualify, the solar panels must be purchased and installed at a private residence, and <u>a certificate of compliance for the installation must be issued from 1 March 2023 to 29 February 2024</u>.

The rebate is only available for solar PV panels, and not inverters or batteries, to focus on the promotion of additional generation.

It can be used to offset the individual's personal income tax liability for the 2023/24 tax year up to a maximum of R15 000 per individual. For example, an individual who purchases 10 solar panels at a cost of R40 000 can reduce their personal income tax liability for the 2023/24 tax year by R10 000.

3.5. Adjustment of transfer duty

As part of the periodic reviews of monetary values in tax tables, the brackets for transfer duties will all be adjusted upwards by 10% to compensate for inflation. Tax rates remain unchanged.

2022/23		**2023 /24**	
Property value	**Rates of tax**	**Property value**	**Rates of tax**
R0 – R1 000 000	0% of property value	R0 – R1 100 000	0% of property value
R1 000 001 - R1 375 000	3% of property value above R1 000 000	R1 100 001 - R1 512 500	3% of property value above R1 100 000
R1 375 001 - R1 925 000	R11 250 + 6% of property value above R1 375 000	R1 512 501 – R2 117 500	R12 375 + 6% of property value above R1 512 500
R1 925 001 - R2 475 000	R44 250 + 8% of property value above R1 925 000	R2 117 501 - R2 722 500	R48 675 + 8% of property value above R12 117 500
R2 475 001 - R11 000 000	R88 250 + 11% of property value above R2 475 000	R 2 722 501 - R12 100 000	R97 075 + 11% of property value above R2 722 500

R11 000 001 and above	R1 026 000 + 13% of property value above R11 000 000	R12 100 001 and above	R1 128 600 + 13% of property value above R12 100 000

3.6. Adjustment of retirement tax tables

As part of the periodic reviews of monetary values in tax tables, the brackets for retirement fund lump sum benefits and retirement fund lump sum withdrawal benefits will all be adjusted upwards by 10% to compensate for inflation. Tax rates remain unchanged.

Personal income tax rates: Retirement fund lump sum benefits

2022/23		**2023 /24**	
Taxable Income	**Rates of tax**	**Taxable Income**	**Rates of tax**
R0 – R500 000	0% of taxable income	R0 – R505 000	0% of taxable income
R500 001 – R700 000	18% of taxable income above R500 000	R550 001 – R770 000	18% of taxable income above R550 000
R700 001 – R1 050 000	R56 700 + 27% of taxable income above R700 000	R770 001 – R1 055 000	R39 600 + 27% of taxable income above R770 000
R1 050 001 and above	R141 750 + 36% of property value above R1 050 000	R1 055 001 and above	R143 550 + 36% of property value above R1 155 000

Retirement fund lump sum withdrawal benefits

2022/23		2023 /24	
Taxable Income	**Rates of tax**	**Taxable Income**	**Rates of tax**
R0 – R25 000	0% of taxable income	R0 – R27 500	0% of taxable income
R25 001 – R660 000	18% of taxable income above R25 000	R27 501 – R726 000	18% of taxable income above R27 500
R660 001 – R990 000	R114 300 + 27% of taxable income above R660 000	R726 001 – R1 089 000	R125 730 + 27% of taxable income above R726 000
R990 001 and above	R203 400 + 36% of property value above R990 000	R1 089 001 and above	R223 740 + 36% of property value above R1 089 000

3.7. Base erosion and profit shifting: The two-pillar solution

The 2022 Budget Review announced that legislative amendments would be proposed to implement tax rules related to digitalisation and base erosion, flowing from South Africa's role in the Steering Group of the OECD/G20 Inclusive Framework. The framework has two pillars.

Pillar One focuses on the digital economy and is expected to establish a coherent and integrated approach to the tax treatment of multinationals, with the allocation of taxing rights among jurisdictions based on their market share. Currently, no final agreement has been reached on Pillar One and OECD guidelines for this pillar have not been finalised.

Pillar Two focuses on the remaining base erosion and profit shifting matters. It proposes an approach to ensure that all internationally operating businesses with global annual revenue of more than €750 million pay an effective tax rate of at least 15%, regardless of where they are headquartered or which jurisdictions they operate in. A minimum effective tax rate for large multinationals is expected to apply in a number of countries from December 2023. During the 2023 legislative cycle, government will publish a draft position on the implementation of Pillar Two for public comment and draft legislation will be prepared for inclusion in the 2024 Taxation Laws Amendment Bill.

3.8. Two-pot retirement system

Following extensive public consultation, the first phase of legislative amendments to the retirement system is due to take effect on 1 March 2024. The intent of these amendments is to enable pre-retirement access to a portion of one's retirement assets, while preserving the remainder for retirement. Retirement fund contributions will remain deductible up to R350 000 per year or 27.5% of taxable income per year – whichever is lower. Permissible withdrawals from funds accrued before 1 March 2024 will be taxed according to the lump sum tables. Withdrawals from the 'savings pot' before retirement will be taxed at marginal rates. On retirement, any remaining amounts in the savings pot will be taxed according to the retirement lump sum table (for example, R550 000 is a tax-free lump sum on retirement).

Four areas required additional work:

- a proposal for seed capital,
- legislative mechanisms to include defined benefit funds in an equitable manner,
- legacy retirement annuity funds and
- withdrawals from the retirement portion if one is retrenched and has no alternative source of income.

The first three matters will be clarified in forthcoming draft legislation. The final matter will be reviewed as a second phase of implementation.

3.9. *Refining the research and development tax incentive*

Government's tax policy instrument supporting early-phase research and development (R&D) is the R&D tax incentive. Following public consultation on a review of the incentive published in 2021, government proposes to:

- Extend the incentive for 10 years from 1 January 2024. There will be a six-month grace period for projects to commence before the application is submitted, to allow new and smaller applicants to gather information and potentially benefit from the incentive.
- Refine the definition of R&D to make it simpler to understand and administer, resulting in an easier application process for the incentive. The incentive should apply only to activities aimed at resolving a scientific or technological uncertainty. For example, if a professional with appropriate knowledge and skills could resolve the uncertainty without R&D, then the incentive may not apply.
- Move the definition of R&D from an 'end-result' approach (for example, it must be patentable) to incorporate principles of the OECD Frascati Manual, in which activities should be novel, uncertain, systematic and transferable and/or reproducible. This change recognises that, given the risk and uncertainty involved, applicants will not know how their R&D activities will unfold when applying for the incentive. It also removes a confusing requirement on innovation.
- Remove the exclusion for internal business processes – so that if an activity is investigative or experimental with the aim of resolving a scientific or technological uncertainty and it meets the proposed (revised) definition of R&D for the purposes of this incentive, it should be considered R&D – regardless of whether it is intended for sale or the use thereof is granted to connected parties.
- Allow the Commissioner of SARS to disclose certain information to the Minister of Higher Education, Science and Innovation to improve monitoring

and evaluation.

3.10. Extending the urban development zone incentive

Public consultation as part of the policy review process for the urban development zone tax incentive will not be concluded before the 31 March 2023 sunset date. Further engagement is required to assess the incentive's results – particularly to source and evaluate municipal data on its uptake. Relatively low compliance of municipalities with annual reporting requirements has delayed the review process. As a result, the incentive will be extended for two years to 31 March 2025 while its review process is completed.

3.11. Adjusting the minimum royalty rate for oil and gas companies

In 2021, a review of the tax regime for oil and gas companies was published for public comment. Following consultation, government proposes to retain the flexibility of the royalty rate, which is determined by profitability, rather than opt for a flat rate for these companies. This decision recognises that companies face varying costs and profit levels depending on whether they are, for example, operating in deep or shallow waters.

However, to ensure that the country is adequately compensated for the loss of its finite resources, the minimum royalty rate will be increased from 0.5% to 2%, with the maximum remaining at 5%.

3.12. SARS administration

Over the period ahead, SARS intends to review the VAT administrative framework to simplify and modernise the current system, in consultation with all affected parties. In line with SARS' strategic objective of providing clarity and certainty through instruments such as advance rulings, government also proposes to introduce a legislative framework to empower SARS to conclude bilateral advance pricing agreements.

3.13. Tax research and reviews – Broadening the personal income tax base

As part of exploring the effect of remote work on the personal income tax regime, the National Treasury and SARS committed to a multiyear review of allowances. A discussion document will be released this year to outline workplace practices and policies, changes in the current environment and how different workplaces are affected by home office and travel allowance policies

3.14. Tax research and reviews – Adjustments for feed-in tariffs

The start of feed-in tariffs in some municipalities may require adjustments in the Income Tax Act (1962) to cater for additional revenue from electricity sales. The National Treasury and SARS will investigate the potential changes required.

3.15. Individuals, employment and savings – Apportioning the tax-free investment contribution limitation and limiting the retirement funds contributions deduction when an individual ceases to be a tax resident

In 2022, the Income Tax Act was amended to provide that, when an individual ceases to be a South African tax resident, the annual interest exemption applicable to individuals in terms of section 10(1)(i) is apportioned and the capital gains tax annual exclusion applicable to individuals in terms of paragraph 5(1) of the Eighth Schedule to the Act is limited.

To ensure there is alignment with the Act's other provisions for individuals ceasing to be tax residents, it is proposed that further changes be made to section

12T(4)(a) to apportion the tax-free investment contribution limitation and section 11F(2)(a) to apportion the annual limit on the deduction of the retirement funds contributions.

3.16. Individuals, employment and savings – Clarifying anti-avoidance rules for low-interest or interest-free loans to trusts

The Income Tax Act contains anti-avoidance rules aimed at curbing the tax-free transfer of wealth to trusts using low-interest or interest-free loans, advances or credit.

These rules deem any interest foregone in respect of low-interest or interest-free loans, advances or credit to a trust to be a donation subject to a donations tax. The deemed donation is calculated as the amount by which the official rate of interest exceeds any amount of interest incurred in this regard.

These anti-avoidance rules have certain exclusions.

For example, the rules do not apply if the low-interest or interest-free loan, advance or credit is used to purchase a primary residence for the person advancing that low interest or interest-free loan, advance or credit to the trust, company or spouse of such person. The above-mentioned exclusion does not fully encompass what constitutes a primary residence in terms of the Eighth Schedule of the Act.

It has also come to government's attention that, in instances where the low-interest or interest-free loan, advance or credit is denominated in foreign currency, the rules do not provide clarity on how and when this amount should be converted to South African rands. This affects the calculation of the deemed donation. It is proposed that amendments be made to the legislation to provide clarity in this regard

3.17. Retirement provisions – Clarifying the amount of employer contribution to a retirement fund to be deductible

Section 11F(4) of the Act deems an employer contribution to a retirement fund as a contribution made by the employee, and it is calculated as the amount equal to the cash equivalent of the value of the taxable benefit.

However, there is no requirement that the calculated cash equivalent be included in the employee's income, as is the case in sections 6A and 6B of the Act.

This is against the policy rationale of the Act's provisions.

To address this, it is proposed that the Act be amended to require that the cash equivalent of the taxable benefit for employer retirement fund contributions be included in an employee's income before a tax deduction is allowed.

3.18. Retirement provisions – Transfers between retirement funds by members who are 55 years or older

In 2022, changes were made to the Act to allow for tax-neutral transfers between retirement funds by members who are 55 years or older in instances where transfers of retirement interests in relation to a member who has reached normal retirement age has not yet opted to retire.

It has come to government's attention that there are some instances where active contributing pension and provident fund members who have reached retirement age and been subjected to involuntary transfers to another pension or provident fund may still be subject to tax.

To address this, it is proposed that members of pension or provident funds who have reached the normal retirement age as stipulated in the rules of that fund but have not yet opted to retire must, as part of the involuntary transfer, be able to have their retirement interest transferred from a less restrictive to a more restrictive retirement fund without incurring a tax liability.

The value of the retirement interest, including any growth thereon, will remain ringfenced and preserved in the receiving pension or provident fund until the member elects to retire from that fund. This means that these members will not be entitled to the payment of a withdrawal benefit in respect of the amount transferred.

3.19. Business (general) – Reviewing Practice Note 31 of 1994 and Practice Note 37 of 1995

In 1994 and 1995, the South African Revenue Service (SARS) issued Practice Note 31 of 1994, entitled Interest paid on moneys borrowed, and Practice Note 37 of 1995, entitled Deduction of fees paid to accountants, bookkeepers and tax consultants for the completion of income tax returns.

On 16 November 2022, SARS issued a notice informing the public of the intention to withdraw both practice notes, with effect from years of assessment starting on or after 1 March 2023, due to the increasing abuse of the tax deduction concession provided for in Practice Note 31 and the fact that Practice Note 37 does not incorporate the requirements of the term ‘registered tax practitioner’ contained in the Tax Administration Act (2011).

After reviewing the public comments received on the withdrawal of the practice notes, government will consider the impact of the proposed withdrawal and whether changes could be made in the tax legislation to accommodate legitimate transactions affected by such withdrawal. In light of this proposal, SARS also intends to delay and align the withdrawal of the practice notes with the effective date of any legislation arising from the proposed considerations.

3.20. Business (general) – Clarifying anti-avoidance rules dealing with third-party backed shares

The Act contains anti-avoidance rules targeting debt-like equity instruments – for example, thirdparty backed shares – and deeming any dividend or foreign dividend received by or accrued to any person in respect of a third-party backed share as income.

The anti-avoidance rules do not apply if the funds derived from the issue of the shares in question are used to directly or indirectly acquire equity shares of an operating company.

At issue is the fact that these rules do not deem any dividend or foreign dividend received by or accrued to any person in respect of a third-party backed share as income when the shares in that operating company are no longer held by the person who initially acquired them.

Government proposes that the legislation be clarified in this regard.

3.21. Contributed tax capital

Contributed tax capital is the consideration received by or accrued to a company in exchange for the issue of shares of a particular class, on or after the date on which that company becomes a resident of South Africa, and an amount equal to the market value of all the shares in that company of that class immediately before the date on which that company becomes a resident.

It is reduced by any amounts referred to as capital distributions, transferred by the company to the shareholders. It has come to government's attention that the following amendments are needed to the definition of contributed tax capital.

3.22. Contributed tax capital – Addressing the abuse of the definition of contributed tax capital

Government has identified a structure where a foreign holding company that holds shares in a valuable South African operating company through a foreign intermediary could avoid dividends tax by changing the tax residency of the foreign intermediary to South Africa.

When this takes place, the contributed tax capital is recognised as an amount equal to the market value of its shares. The South African operating company then distributes dividends to the new South African tax resident company, and such dividends are exempt from tax because dividends between South African companies are not subject to tax. When the new South African company makes distributions to the foreign holding company, the distributions are shielded by contributed tax capital and regarded as capital distributions, and are not subject to dividends tax in the hands of the foreign holding company.

These capital distributions are also not subject to capital gains tax in the hands of the foreign holding company if the underlying investment in South Africa is not in immovable property. To address this abuse, government proposes that amendments be made to the tax legislation.

3.23. Contributed tax capital – Converting contributed tax capital from foreign currency to rands

After a company changes its tax residence to South Africa, it is possible for that company's functional currency and share capital to be denominated in a currency other than the rand.

Although the Act contains specific rules dealing with the conversion of amounts denominated in foreign currency to rands, these rules do not specifically cater for the conversion of contributed tax capital to rands.

Government proposes that the legislation be clarified in this regard.

3.24. Corporate reorganisation rules - Clarifying the interaction between the debt reduction rules and the disposal of assets exclusion rule for dormant group companies

In 2017, changes were made to the debt relief rules in section 19 and paragraph 12A of the Eighth Schedule to the Income Tax Act. Section 19 deals with income tax implications for debt that was previously used to fund tax-deductible expenditure, such as operating expenses, and where deductions may be claimed for assets such as trading stock and allowance assets. Paragraph 12A of the Eighth Schedule deals with capital gains tax implications for debt that was used to acquire capital or allowance assets.

Both these rules contain a dormant company exemption, which applies when a debt is owed between companies that form part of the same group of companies.

A debtor company is regarded as being dormant if it has not conducted trading activities in the year of assessment in which the debt benefit arose nor in the year of assessment preceding that year. However, this exemption does not apply if the debt was used to fund an asset that was subsequently disposed of in terms of the corporate reorganisation transactions provided in Part III of Chapter II of the Act.

At issue is whether the disposal in terms of the corporate reorganisation transactions is envisaged to take place subsequent to the asset's acquisition, but prior to the debt reduction, or whether the disposal is meant to take place subsequent to the acquisition and the debt reduction.

When changes were made to the debt relief rulesin 2017, the policy rationale was that the exclusion from applying the dormant company rule should not restrict the timing of the disposal under the corporate reorganisation rules.

Government proposes clarifying the legislation to reflect this policy rationale.

3.25. Corporate reorganisation rules – Clarifying the interaction of provisions on the acquisition of assets in exchange for shares

The Act contains provisions dealing with the acquisition of assets in exchange for shares. These provisions prescribe a base cost for assets acquired by companies in exchange for the issue of that company's shares to the seller equal to the sum of the market value of the shares and, where applicable, the amount of the capital gain triggered by the application of the anti-value shifting rules.

In 2021, further changes were made in the tax legislation to make provision for the deemed base cost to apply to corporate reorganisation transactions.

At issue is whether allowances in respect of an asset acquired in exchange for shares issued to the seller may be determined according to the deemed base cost.

Government proposes that the legislation be clarified in this regard.

3.26. Corporate reorganisation rules – Refining the provisions applicable to unbundling transactions

In 2020, changes were made to unbundling transaction rules to curb tax avoidance where unbundling transactions are used to distribute shares of unbundled companies to tax-exempt persons or non-resident investors. As such, tax is not deferred on an unbundling transaction in respect of any equity share that is distributed by an unbundling company to any shareholder that is a disqualified person and holds at least 5% of the equity shares in the unbundling company immediately before the transaction.

These changes result in the pro-rata operation of the anti-avoidance rule and ensure a more equitable outcome in unbundling transactions, because only shares distributed to persons who are not disqualified persons will benefit from rollover relief. In 2021, further changes were made to the rules to allow shareholders in an unbundling company that only partially qualifies for tax deferral to benefit from an increase in the base cost of the shares in the unbundled company to the extent that the unbundling company did not qualify for tax deferral in accordance with its respective shareholding.

Government proposes that further consideration should be given to whether it is appropriate to apportion tax paid by the unbundling company between the unbundling company shares and the unbundled company shares, and to situations where the unbundling company is not in a taxable position due to having capital losses or assessed losses.

3.27. Clarification of the interest limitation rules

In 2021, changes were made to the Income Tax Act as part of the corporate tax package to broaden the tax base and reduce the headline corporate income tax rate in a revenue-neutral manner.

One of these measures included strengthening the rules dealing with the limitation of interest deductions for debts owed to certain persons not subject to tax in section 23M of the Act. It has come to government's attention that these measures require further clarification in the following areas.

3.28. Clarification of the interest limitation rules – Clarifying the definition of 'adjusted taxable income'

The definition of 'adjusted taxable income' in section 23M(1) of the Act means taxable income calculated before applying the interest limitation rules, including the addition of any assessed loss or balance of assessed loss allowed to be set off against income in terms of section 20.

There is uncertainty stemming from the inclusion of the terms 'assessed loss' and 'balance of assessed loss'.

Government proposes that the legislation be amended to align with the policy intent that only the balance of assessed losses from the prior year be added in the adjusted taxable income calculation.

3.29. Clarification of the interest limitation rules – Introducing a definition of the term 'creditor'

Currently, section 23M(1) of the Act defines 'debt' and 'debtor', but it does not define the term 'creditor'.

Government proposes that this definition be added to section 23M of the Act.

3.30. Clarification of the interest limitation rules – Clarifying the treatment of exchange gains and losses

Section 23M(7) of the Act provides that any exchange difference deducted from the income of a person as contemplated in sections 24I(3) or (10A) of the Act is deemed to have been incurred by that person.

While section 23M(7) deems exchange losses to be incurred, a corresponding deemed accrual does not apply to exchange gains. This could result in exchange gains not being taken into account as interest received or accrued for purposes of section 23M of the Act.

Government proposes that exchange gains be classified as interest received or accrued for the purposes of section 23M of the Act.

3.31. Clarification of the interest limitation rules – Clarifying the application of the proviso to section 23M(2) of the Act

The proviso to section 23M(2) contains a formula that reduces the amount of interest disallowed for deduction based on the extent to which withholding tax on interest must be withheld under Part IVB of the chapter.

However, it does not adequately specify that this adjustment should only apply in the case of interest flowing to non-residents.

Government proposes that the legislation be clarified in this regard.

3.32. Clarification of the interest limitation rules – Extending the provisions of section 23M(6) of the Act to apply to South African lending institutions

Section 23M(6) generally makes provision for the exemption from the application of interest limitation rules where the creditor provides a loan to a taxpayer with funds granted by a lending institution – in this instance, a foreign bank.

Government proposes that section 23M(6) of the Act be amended to extend this exemption to apply to South African lending institutions.

3.33. Clarification of the interest limitation rules – Reviewing the outcome of the interaction between the 'controlling relationship' definition in section 23M(1) and the rule in section 23M(2)(c) of the Act

In 2021, changes were made to the definition of 'controlling relationship' in section 23M(1) by adding a connected person test. In addition, further changes were made to section 23M(2)(c) by inserting a group companies test in instances where the creditor is not in a controlling relationship with the debtor.

Government will review how the definition of 'controlling relationship' in section 23M(1) and the provisions of 23M(2) interact in light of the intended policy outcome.

3.34. Business (financial sector) – Tax treatment of deposit insurance scheme

In 2020, government announced the establishment of a deposit insurance scheme to protect depositors in the event of a bank failure, which in turn will contribute to the stability of the South African financial system.

It was also envisaged that each bank would make stipulated contributions to the scheme. In 2022, Parliament passed the legislation dealing with the deposit insurance scheme.

Government proposes that tax legislation be amended to address the tax implications of the scheme.

3.35. Business (financial sector) - Reviewing the Sharia-compliant financing arrangements

In 2010, legislation dealing with Sharia-compliant financing arrangements was introduced in various tax acts.

Government proposes to extend the provisions dealing with Sharia-compliant arrangements and ensure alignment across all the tax acts.

3.36. Business (financial sector)

In 2022, changes were made in the tax treatment of short- and long-term insurers in sections 28 and 29A of the Act to accommodate the new accounting standard for insurers, International Financial Reporting Standard (IFRS) 17, to be applied to all insurance contractsfor accounting periods starting on or after 1 January 2023.

It has come to government's attention that certain third-party cell captive arrangements are treated as reinsurance arrangements for IFRS purposes. As a result, there are reinsurance assets and liabilities recognised for IFRS purposes in relation to a portion of cell profits due to or from the cell owner.

For tax purposes, these are not true commercial reinsurance arrangements, and these balances should be disregarded in determining a cell captive insurer's taxable income. In addition, cell captive arrangements effected in terms of preference share arrangements may be accounted for under IFRS17 or IFRS9. Insurance contract liabilities (IFRS17) and investment contract liabilities (IFRS9) are both included in the 'adjusted IFRS value' definition in section 29A of the Act. Where a separate liability is recognised in respect of profits due to the cell owner, it may be possible that such a liability may also be included in the 'value of liabilities' definition in section 29A of the Act, resulting in the double-counting of the liability.

To address this issue, government proposes that reinsurance contracts relating to an owner as contemplated in the definition of 'cell structure' in section 1 of the Insurance Act (2017) be disregarded. In addition, changes should be made to the definition of 'value of liabilities' in section 29A of the Income Tax Act to exclude any other liabilities relating to a cell owner.

3.37. Business (incentives) – Clarifying the meaning of 'person' in the provisions dealing with public benefit organisations, recreational clubs and associations

The Act contains special tax dispensation for public benefit organisations, recreational clubs and associations due to their non-profit status.

Because these entities enjoy a special tax dispensation, various rules exist that limit the manner in which these entities operate or require greater accountability and stricter governance. These include requirements that the entity must have three unconnected persons who accept fiduciary responsibility and that no single person may directly or indirectly control the decision-making powers of the entity. At issue is whether the word 'person' in these requirements refers to a natural person or a juristic person.

Government proposes amending the legislation to clarify that 'person' in this context refers to a natural person.

3.38. Business (incentives) – Clarifying the timeframes of compliance requirements for industrial policy projects

In 2021, changes were made to the Act to allow for a discretionary extended compliance period of up to two additional years for companies with approved industrial policy projects to comply with the provisions of section 12I in cases where there were bona fide reasons for non-compliance due to business-related disruptions caused by the COVID-19 pandemic.

At issue is the uncertainty over the interaction between the skills development criteria and the extended compliance period.

Government will consider further legislative amendments to clarify the intention of providing taxpayers with additional time to meet the section 12I requirements and the extent to which the incentive criteria should be met over the extended compliance period.

3.39. International – Extending the anti-avoidance provision to cover foreign dividends from shares listed in South Africa

Section 10B of the Act exempts foreign dividends received or accrued from shares listed on a South African stock exchange from normal tax. T

his exemption was introduced because these foreign dividends may be subject to dividends tax. It has come to government's attention that schemes have been devised to exploit this exemption. The scheme involves South Africans investing in the shares of a non-resident company listed on a South African stock exchange and the non-resident company directly or indirectly investing in interest-bearing financial instruments in South Africa.

The result is that a deduction for an interest expense is not matched with a taxable foreign dividend. It is proposed that the round-tripping anti-avoidance provision for foreign dividends be amended to include foreign dividends received or accrued from shares listed on a South African stock exchange if the foreign dividends are directly or indirectly funded by amounts that were deductible in South Africa.

3.40. International – Interaction between the anti-avoidance rule and exemption applying to foreign dividends

The Act contains an anti-avoidance rule in terms of which the participation exemption does not apply to a foreign dividend if any amount of the foreign dividend arises directly or indirectly from an amount that is deductible from the income of any person under the Income Tax Act.

The policy rationale for this measure is that a deductible amount should not be received by a resident or a controlled foreign company (CFC) as an exempt amount. A further exemption that applies to foreign dividends limits the effective tax rate for foreign dividends accruing to residents to a rate of 20 per cent. This exemption has the effect that amounts that are allowed to be deducted for income tax at a rate of 27 per cent or marginal tax rates are taxed at a rate of only 20 per cent where the antiavoidance provision applies.

It is proposed that the exemption to tax foreign dividends at 20 per cent should not apply where the anti-avoidance rule is applicable.

3.41. International – Clarifying the foreign business establishment exemption for controlled foreign companies

The Act contains anti-avoidance rules in section 9D aimed at taxing South African residents on an amount equal to the net income of a CFC.

To strike a balance between protecting the tax base and enabling South African multinationals to compete offshore, the CFC rules contain exemptions for certain types of income. For example, amounts that are attributable to a foreign business establishment of a CFC, as defined in section 9D, are excluded from the net income of the CFC.

A foreign business establishment consists of a fixed place of business located outside South Africa that is used or will continue to be used for the business of the CFC for at least one year. To be so defined, a foreign business establishment must also satisfy requirements relating to the nature of the business. For example, the fixed place of business should be suitably staffed with onsite managerial and operational employees of that CFC. The fixed place of business should be suitably equipped and have suitable facilities for conducting the primary operations of the business. The definition of a foreign business establishment allows for the structures, employees, equipment and facilities of another company to be taken into account if these are all located in the same country as the CFC's fixed place of business, the other company is subject to tax in the same country where the CFC's fixed place of business is located and it forms part of the same group of companies as the CFC. It has come to government's attention that some taxpayers are retaining certain management functions but outsourcing other important functions for which the CFC is also being compensated by its clients. This is against the policy rationale of the definition of a foreign business establishment.

It is proposed that the tax legislation be clarified such that, to qualify as a foreign business establishment, all important functions for which a CFC is compensated need to be performed by the CFC or by the other company meeting the requirements listed above.

3.42. International – Taxation of non-resident beneficiaries of trusts

The gradual relaxation of exchange control regulations has led to an increase in applications to SARS for confirmation of tax compliance status of a person for purposes of transferring funds offshore via authorised dealers.

Government is concerned about the difference between the rules covering the normal tax treatment of income attributed to beneficiaries of trusts in section 25B of the Act and the rules covering the tax treatment of capital gains in relation to beneficiaries in paragraph 80 of the Eighth Schedule to the Act. Paragraph 80 makes provision for capital gains to be attributed only to beneficiaries who are South African tax residents.

The paragraph does not allow for capital gains to flow through to non-resident beneficiaries. Those capital gains for non-resident beneficiaries are taxed in the trusts and the trust is liable for the payment of the tax. Thereafter, distributions can be made to non-resident beneficiaries. In contrast, section 25B does not distinguish between beneficiaries who are and are not South African tax residents. The flow through of amounts from South African tax resident trusts to non-resident beneficiaries makes it difficult for SARS to collect income tax from those non-resident beneficiaries as it is more complicated to enforce recovery actions against non-residents.

To address this, it is proposed that changes be made to section 25B to align it with the provisions of paragraph 80.

3.43. International – Refining the participation exemption for the sale of shares in foreign companies

Paragraph 64B of the Eighth Schedule of the Act contains a participation exemption relating to the sale of shares in foreign companies and section 10B contains a participation exemption relating to foreign dividends from foreign companies.

The main aim of these exemptions is to encourage the repatriation to South Africa of foreign dividends and the proceeds on the sale of shares in foreign companies to non-connected non-residents. Government has identified certain transactions that do not achieve this aim but for which the participation exemption for the sale of shares in foreign companies applies. These transactions include, for example, instances where restructuring of a group of companies entails the sale of shares to recently formed non-resident companies although there is no change in the ultimate shareholders.

Government proposes changing the tax legislation to not grant the participation exemption if the sale of shares is to a non-resident company that formed part of the same group of companies as the company disposing of the shares, or the shareholders are substantially the same as the shareholders of any company in the group of companies disposing of the shares.

3.44. International – Refining the participation exemption for the foreign return of capital from a CFC

The participation exemption relating to the sale of shares in foreign companies is subject to certain qualifying requirements.

One of these requirements is that the South African tax resident selling the shares in a foreign company should have held those shares for at least 18 months prior to the sale. In 2012, changes were made to the Act to extend the participation exemption to apply in respect of the foreign return of capital from a CFC. However, the participation exemption for the foreign return of capital from a CFC does not have a similar 18-month holding requirement.

To close this loophole, it is proposed that a similar holding requirement be introduced for the participation exemption in respect of the foreign return of capital from a CFC.

3.45. VAT – Reviewing the VAT treatment of specific supplies in the short-term insurance industr

In 2013, SARS first issued Binding General Ruling 14, which deals with the VAT treatment of specific supplies in the short-term insurance industry.

This was updated in 2018 and 2020. In 2019, changes were made to section 72 of the VAT Act, which related to the SARS Commissioner's discretionary powers over VAT decisions. These changes affected decisions made before 21 July 2019, including Binding General Ruling 14.

Government proposes making changes to the VAT Act to clarify the VAT treatment of specific supplies in the short-term insurance industry.

3.46. VAT – Clarifying the VAT treatment of prepaid vouchers in the telecommunications industry

In the early years of the mobile telecommunications industry in South Africa, subscribers to mobile telecommunication services could use prepaid vouchers only to purchase the services offered by that mobile telecommunication company such as calls and short message services.

The evolution of the industry and technological advances have made it possible for prepaid vouchers to also be used for other services provided by third parties where the mobile telecommunication company acts as an agent of that third party – for example, data offerings and mobile money services.

The VAT Act does not provide clarity in instances where prepaid vouchers are used for services provided by a third party, the mobile telecommunication company is acting as an agent and/or those third-partyprovided services are regarded as exempt supplies or non-taxable supply in the VAT Act.

It is proposed that changes be made to the Act to provide clarity.

3.47. VAT – VAT treatment of temporary letting of residential property, clarifying the meaning of 'adjusted cost' relating to temporary letting of residential property

With effect from 1 April 2022, a new section 18D was introduced in the VAT Act to clarify the VAT treatment of temporary letting of residential property. Consequential amendments were made to other sections of the VAT Act including section 10, which deals with how to determine the value of supply of goods and services.

At issue is whether the term 'adjusted cost' contemplated in section 10(29) of the VAT Act also includes the cost of the land.

It is proposed that section 10(29) be clarified in this regard.

3.48. VAT – Clarifying the rule dealing with recovery of the previous declared output tax

In general, section 18D(5) of the VAT Act makes provision for a vendor that previously made an output tax adjustment under section 18D(2) of the Act to reclaim that tax through a deduction under section 16(3)(o) in the tax period afterthe vendor exits the temporarily applied period of 12 months.

However, section 18D(5)(c) refers to a situation in which section 18(1) of the Act applies. This creates an anomaly as section 18D(5) (c) can never apply in the given circumstances. To address this anomaly, it is proposed that section 18D(5) (c) of the VAT Act be deleted.

3.49. VAT – Clarifying VAT rules dealing with documentary requirements for gold exports

The main purpose of gold refineries is to refine and smelt gold or ore received from various customers, namely depositors. In most instances, the refineries also act as agents and sell or export gold on behalf of these depositors.

Gold from more than one depositor is typically required to make up the volume ordered for sale or export. When the depositor delivers their gold to the refinery, the refinery issues a sale of gold certificate to the depositor and the value of the gold deposited is determined using that day's morning, afternoon or spot London Bullion Market Association gold price.

After the refining or smelting, it is difficult to determine which depositor's gold is sold or exported because the gold loses its original identity during refinery and smelting.

As a result, depositors find it difficult to obtain the documentary evidence to support the application of the zero rate on a transaction-by-transaction basis in relation to their gold as contemplated in the regulations issued in terms of section 74(1) of the VAT Act read with paragraph (d) of the definition of 'exported' in section 1(1).

To address this, it is proposed that changes be made to the VAT Act.

3.50. VAT – Regulations on the domestic reverse charge relating to valuable metal

Effective from 1 July 2022, government introduced regulations aimed at foreclosing schemes and malpractices to claim undue VAT refunds from SARS by vendors operating in the value chain relating to high-risk goods containing gold.

These regulations allowed vendors a transitional period of one month – from 1 July 2022 to 1 August 2022 – to comply with the requirements. This implied that registered vendors must account for and pay VAT for transactions falling within the ambit of the regulations in the August 2022 tax period.

It has come to government's attention that the regulations require further clarification in the areas outlined below.

3.51. VAT – Clarifying the definition of 'residue'

Currently, Regulation 1 defines 'residue' to mean any debris, discard, tailings, slimes, screening, slurry, waste rock, foundry sand, beneficiation plant waste or ash. At issue is whether this definition relates only to residue as a result of mining operations and does not include residue as a general concept.

It is proposed that this be clarified.

3.52. VAT – Clarifying the definition of 'valuable metal'

Currently, Regulation 1 defines 'valuable metal' to mean any goods containing gold in the form of jewellery, bars, blank coins, ingots, buttons, wire, plate, granules, or in a solution or residue or similar forms, including any ancillary goods or services.

This definition excludes supplies of goods produced from raw materials by any holder as defined in section 1 of the Mineral and Petroleum Resources Development Act (2002) or by any person contracted to such holder to carry on mining operations at the mine where the holder carries on mining operations. It also excludes a supply of goods contemplated in section 11(1)(f), (k) or (m) of the VAT Act. At issue is the fact that some vendors interpret the phrase 'any goods containing gold in the form of jewellery, bars, blank coins, ingots, buttons, wire, plate, granules' to mean that the gold component must be in the prescribed forms, as opposed to goods containing gold supplied in the prescribed forms.

It is therefore proposed that the policy rationale for the definition be clarified.

3.53. VAT – Clarifying exclusions from the definition of 'valuable metal'

The definition of 'valuable metal' excludes supplies of goods produced from raw materials by any holder or by any person contracted to such holder as explained in the preceding proposal.

There is uncertainty over the scope of the exclusion relating to holders or persons contracted to holders.

It is proposed that the definition be clarified to remove uncertainty and curb possible abuse.

3.54. VAT – Introducing a de minimis rule in the definition of 'valuable metal'

The definition of 'valuable metal' does not take into account the gold content and leads to unintended consequences in instances where jewellery or other goods are gold plated with a thin layer of gold.

It is proposed that a de minimis rule be introduced in the definition to provide guidance in relation to this type of jewellery or other goods that are gold plated with a thin layer of gold. A de minimis rule refers to the Latin maxim, which means that law does not concern itself with trivialities, for example matters too small or insufficiently meaningful to be taken into consideration.

3.55. Tax Administration – Aligning tax registration requirements for non-resident employers

It has been noted that non-resident employers may not have representative employers in South Africa for purposes of employees tax. They are, as a result, not liable to deduct or withhold tax from the remuneration that is paid to their employees who render services in South Africa.

Nevertheless, given that they pay remuneration, they are required to register with SARS as employers. They are liable for skills development levies and unemployment insurance contributions, which many pay.

It is proposed that the various provisions be aligned to ensure consistency.

3.56. Tax Administration – Varying employees' tax withholding in respect of remuneration

The Fourth Schedule to the Income Tax Act allows employers to request a variation in employees' tax withholding to take into account foreign taxes paid.

However, such a variation does not apply to remuneration arising from share options and similar schemes. This could result in cash flow implications for the affected employees, as they will only be entitled to claim a foreign tax credit when they complete their annual tax returns.

It is proposed that SARS be empowered to vary the basis for withholding under these circumstances.

3.57. Tax Administration – Expanding the general disclosure provisions for section 18A approved organisations

In terms of the Tax Administration Act, SARS may disclose a list of public benefit organisations approved in terms of sections 18A and 30 of the Income Tax Act.

As a broader range of entities than public benefit organisations may be granted approval to issue receipts for tax-deductible donations in terms of section 18A, it is proposed that SARS be explicitly empowered to disclose all entities with a section 18A approval.

3.58. Tax Administration – Extending the time period to submit a return where taxpayers disagree with an auto-assessment

SARS may make an assessment based on an estimate where a taxpayer does not submit a return.

The taxpayer may, within 40 days from the date of the assessment, request SARS to make a reduced or additional assessment by submitting a true and full return.

It is proposed that SARS be empowered to extend the period within which the taxpayer is required to submit their request to SARS by public notice. This will allow the deadline for the request to be aligned with the end of the filing season for non-provisional taxpayers.

3.59. Tax Administration – Aligning with anti-money laundering and combating the financing of terrorism developments

Amendments are proposed to align with the National Strategy on Anti-Money Laundering, Counter Financing of Terrorism and Counter Financing of Proliferation, achieve consistency with the General Laws (Anti-Money Laundering and Combating Terrorism Financing) Amendment Act (2022) and take account of other developments related to the Financial Action Task Force.

4. NOTICES / REGULATIONS

4.1. Table of interest

Interest rates charged on outstanding taxes, duties and levies and interest rates payable in respect of refunds of tax on successful appeals and certain delayed refunds

DATE FROM	DATE TO	RATE
1 November 2020	28 February 2022	7,00%
1 March 2022	30 April 2022	7,25%
1 May 2022	30 June 2022	7,50%
1 July 2022	31 August 2022	7,75%
1 September 2022	31 October 2022	8,25%
1 November 2022	31 December 2022	9,00%
1 January 2023	28 February 2022	9,75%
1 March 2023	Until change in the Public Finance Management Act rate	10,50%

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

DATE FROM	DATE TO	RATE
1 September 2020	31 October 2020	3,25%
1 November 2020	28 February 2022	3,00%
1 March 2022	30 April 2022	3,25%
1 May 2022	30 June 2022	3,50%
1 July 2022	31 August 2022	3,75%
1 September 2022	31 October 2022	4,25%
1 November 2022	31 December 2022	5,00%

1 January 2023	28 February 2023	5,75%
1 March 2023	Until change in the Public Finance Management Act rate	6,50%

As from 1 April 2003 the 'prescribed rate' is linked to the rate determined in terms of section 80(1)(b) of the Public Finance Management Act, but for income tax purposes the rate only becomes effective as from the first day of the second month following the date on which the PFMA rate comes into operation

A taxable benefit (fringe benefit) arises if an employee incurs a debt in favour of the employer, any other person by arrangement with the employer, or an associated institution in relation to the employer, if no interest is payable or if the interest payable is less than the 'official rate of interest'. The difference between the amount which would have been payable if the debt had incurred interest at the official rate, and the interest actually paid by the employee, is taxed as a fringe benefit.

DATE FROM	DATE TO	RATE
1 August 2020	30 November 2021	4,50%
1 December 2021	31 January 2022	4,75%
1 February 2022	31 March 2022	5,00%
1 April 2022	31 May 2022	5,25%
1 June 2022	31 July 2022	5,75%
1 August 2022	30 September 2022	6,50%

1 October 2022	30 November 2022	7,25%
1 December 2022	31 January 2023	8,00%
1 February 2023	Until change in Repo rate	8,25%

The 'official rate' as defined in section 1(1) of the Act is linked to the repurchase rate plus one%. The official rate is adjusted at the beginning of the month following the month during which the Reserve Bank changes the repurchase rate.

4.2. Transfer pricing: Intra-Group Loans

Tshwane, 17 JANUARY 2023 – The SARS has today released an interpretation note titled 'DETERMINATION OF THE TAXABLE INCOME OF CERTAIN PERSONS FROM INTERNATIONAL TRANSACTIONS: INTRA-GROUP LOANS' which provides guidance on how SARS will determine arm's length pricing for intra-group loans. The Note also provides guidance on the consequences for a taxpayer if the amount of debt, the cost of debt or both are not arm's length.

A transfer price is broadly the price at which goods or services are exchanged between parties. Transfer pricing on its own is not good or bad, it is simply a necessity given that parties transact with each other. In a tax context, transfer pricing is of concern in situations where parties manipulate the transfer price to achieve a more desirable tax outcome. This is of particular concern in cross-border transactions between related parties as it is easier to manipulate the pricing and take advantage of different tax jurisdictions. This often results in tax jurisdictions not receiving the tax revenue they are rightfully entitled to receive.

The Income Tax Act contains section 31 which requires the transfer price of specified international transactions between connected persons or associated enterprises to be based on the arm's length principle when determining taxable income. It also sets out the tax consequences when the pricing is not arm's length.

An arm's length price is broadly a price negotiated on the open market between a willing buyer and a willing seller.

One of the areas of concern which has been subject to debate relates to arm's length pricing for intra-group loans, for example, a cross-border loan between companies in a multinational group of companies. The pricing of intra-group loans includes a consideration of both the amount of debt and the cost of the debt. An intra-group loan would be incorrectly priced if the amount of debt funding, the cost of the debt or both are excessive compared to what is arm's length.

It therefore remains critically important that in any intra-group transactions the principle of arms-length principle is scrupulously observed by those participating in such a transaction. SARS will act sternly to protect fiscus if the parties are found to have acted at variance with this principle. SARS would like to encourage all taxpayers who would like further detail on SARS's approach to consult the published interpretation note. Companies falling within the ambit of section 31 must have an approved transfer policy that complies with the arms' length principle and be in a position to demonstrate such compliance and that the policy has been implemented correctly.

4.3. Postponement of withdrawal of practice notes 31 and 37

SARS notified the public during November 2022 of its intention to withdraw Practice Notes 31 (Interest Paid on Moneys Borrowed) and 37 (Deduction of Fees Paid to Accountants, Bookkeepers and Tax Consultants for the Completion of Income Tax Returns) and requested that representation be made for legislative amendments as part of the Budget 2023 Annexure C process.

Numerous representations were received and are being considered.

In view of the Budget announcement, the withdrawal of the two Practice Notes is postponed to 1 March 2024

4.4. Further information required in terms of section 18A(2)(a)(vii) for purposes of a receipt issued under section 18A(2)(a) of the Income Tax Act

The following further information must be included on a receipt issued in terms of section 18A(2)(a) of the Income Tax Act:

- Donor nature of person (natural person, company, trust, etc.);
- Donor identification type and country of issue (in case of a natural person);
- Identification or registration number of the donor;
- Income tax reference number of the donor (if available);
- Contact number of the donor;
- Electronic mail address of the donor;
- A unique receipt number; and
- Trading name of the donor (if different from the registered name).

5. TAX CASES

5.1. C:SARS v Airports Company South Africa (85 SATC 1)

SARS during December 2015 to February 2016, had conducted an income tax audit in respect of ACSA's 2011 year of assessment and had issued a Letter of Audit Findings on 8 February 2016.

ACSA had been advised that SARS intended to:

- disallow a deduction claimed by ACSA in respect of corporate social investment (CSI) expenditure in terms of section 11(*a*), read with section 23(*g*), of the Income Tax Act 58 of 1962 (the Act);
- disallow an allowance claimed by ACSA in terms of section 13*quin* of the Act;

- disallow an allowance claimed by ACSA in terms of section 12F of the Act; and
- impose understatement penalties (USPs) in terms of the TA Act.

ACSA, in a letter dated 8 March 2016, addressed the adjustments in relation to (a) and (b) above and sought an extension to deal with (c). A week later, on 15 March 2016, ACSA addressed a further letter to SARS in which it indicated that it 'deemed it appropriate to concede to the findings made by SARS in the Letter of Findings in respect of the application of section 12F.'

SARS, on 30 March 2016, issued a Finalisation of Audit Letter in respect of ACSA's 2011 year of assessment and issued an additional assessment wherein it disallowed the CSI expenditure, as well as the section 13*quin* and section 12F allowance, and imposed USPs and interest in terms of the Tax Administration Act.

ACSA, on 12 May 2016, lodged an objection to the additional assessment and it only objected to the disallowance of the CSI expenditure. No objection was lodged to the section 13*quin* and section 12F allowances and the imposition of USPs and interest.

The objection to the disallowance of the CSI expenditure did not find favour with SARS and on 28 October 2016 ACSA lodged a notice of appeal in respect of the disallowance of the CSI expenditure.

SARS, on 22 January 2019, issued a Letter of Audit Findings in respect of ACSA's 2012 to 2016 years of assessment and consistent with its earlier stance adopted in respect of the 2011 tax year, it indicated that it intended to disallow the deductions claimed by ACSA in respect of the CSI expenditure, the 13*quin* and 12F allowances, and to impose USPs and interest, in terms of the TA Act.

ACSA, in a reply to the Letter of Audit Findings, queried the disallowances and imposition of the USPs and interest.

SARS, on 29 March 2019, issued a Finalisation of Audit Letter and disallowed the aforementioned deductions and allowances claimed, and imposed USPs and interest, in terms of the TA Act.

ACSA, on 6 September 2019, addressed a letter through its newly appointed attorneys to SARS seeking an indulgence to amend the objection that it had lodged in May 2016 in respect of the 2011 year of assessment.

ACSA sought to object to the adjustments effected by SARS in respect of the allowances claimed in terms of sections 13*quin* and 12F, as well as the imposition of USPs and interest.

SARS refused to allow the objection as it was of the opinion that section 104 of the TA Act, read with Rule 7 of the Tax Court Rules precluded such an amendment and that ACSA was seeking to introduce new grounds of objection, which was impermissible in terms of Rule 32(3) of the Tax Court Rules.

As neither the Act, nor the Tax Court Rules, made provision for the amendment of an objection to an additional assessment, ACSA applied to the Tax Court, Johannesburg, for leave to amend in terms of Uniform Rule 28(1), read with Tax Court Rule 42(1).

ACSA had asserted that Uniform Rule 28(1) was the most appropriate Rule under the Rules of the High Court, which stated that 'any party desiring to amend a pleading or document other than a sworn statement, filed in connection with any proceedings, shall notify all other parties of his intention to amend and shall furnish particulars of the amendment.'

The Tax Court held that ACSA was permitted, under Rule 42(1) of the Tax Court Rules, read with Rule 28(1) of the Uniform Rules of Court, to amend its objection against an additional assessment issued by SARS on 30 March 2016 in respect of ACSA's 2011 year of assessment and the appeal to the Supreme Court of Appeal by SARS was with the leave of the Tax Court.

The court on appeal had to determine whether it was permissible to amend the grounds of objection against an additional assessment issued by SARS after the expiry of the periods prescribed in the Tax Court Rules.

Judge Windell held following:

(i) That the Tax Court held that 'rule 42 of the Tax Court Rules permits an applicant to approach a court for an amendment in terms of Rule 28 of the Uniform Rules of Court.' This constituted the full extent of the Tax Court's analysis of the applicable provisions. It failed to address the legal arguments advanced on behalf of SARS and made no findings as to the legal basis for its conclusion. The approach adopted by the Tax Court, which offered no guidance, was regrettable.

(ii) That Uniform Rule 28(1) was applicable to pleadings and documents filed once legal proceedings had commenced. Uniform Rule 28(1) did not, for example, apply to correspondence or notices exchanged between the parties, before the commencement of legal proceedings. Rule 42(1) specifically caters for a situation where the Tax Court Rules do not provide for 'a procedure in the tax court.' This suggests that should Uniform Rule 28(1) find application at all in the Tax Court, it will only apply to pleadings and documents that have been filed once legal proceedings have commenced.

(iii) That if regard is had to the procedure outlined in the TA Act and the Tax Court Rules, legal proceedings before the Tax Court only commence once the appeal is noted to the Tax Court. The objection phase was part of the pre-litigation administrative process referred to by Kriegler J in *Metcash Trading Ltd* v *C:SARS* 63 SATC 13.

(iv) That an objection was therefore part of the pre-litigation administrative process and was not a pleading. It was also not a document filed in connection with judicial proceedings envisaged in terms of Uniform Rule 28(1). Furthermore, Rule 42(1) only comes into play when the Tax Court Rules do not make provision for a procedure in the tax court. Rule 42(1) does not apply to those procedures governed under Part B of the Tax Court Rules, which constitute pre-litigation administrative procedures such as an objection to an assessment and the Tax Court thus erred in granting leave to ACSA to amend its notice of objection in terms of Uniform Rule 28.

(iv) That, moreover, once an objection has been disallowed, Rule 10(2)(*c*)(iii) of the Tax Court Rules makes provision for a taxpayer to introduce a new ground upon which it appeals against an assessment. Rule 10(3), however, provided that such new ground cannot constitute a new objection against a part or amount of the disputed assessment not objected to in the notice of objection under Rule 7.

(v) That the effect of the amendment sought by ACSA would be to extend the period for the filing of an objection (or the filing of new grounds of objection) long after the peremptory periods prescribed in section 104 of the TA Act, read with Rule 7, had expired.

(vi) That the prescribed time periods provided for in the TA Act, read with Rule 7, taken together with the ability of a taxpayer to secure an extension of time within the permitted parameters, achieved a fair balance between SARS and the taxpayer. To permit amendments to an objection would unjustifiably undermine the principles of certainty and finality referred to in *C:SARS* v *Brummeria Renaissance (Pty) Ltd and Others* 69 SATC 205, which underpinned a revenue authority's duty to collect taxes. It would also permit the taxpayer to impermissibly introduce new grounds of objection to the additional assessment.

(vii) That in terms of section 100(1) of the TA Act an assessment or a decision referred to in section 104(2) was final if, in relation to the assessment or decision no objection has been made, or an objection has been withdrawn or after the decision of an objection, no notice of appeal has been filed or a notice has been filed and is withdrawn.

(ix) That the term 'assessment' was defined in section 1 of the TA Act as 'the determination of the amount of a tax liability or refund, by way of self-assessment by the taxpayer or assessment by SARS.' In *First South African Holdings (Pty) Ltd* v *C:SARS* 73 SATC 221 Harms DP stated that an assessment was a determination by SARS of 'one or more matters'. This was expressly contemplated in section 104 of the TA Act, read with Rule 7(2)(*b*) of the Tax Court Rules, which clearly and unambiguously stated that a taxpayer who lodges an objection must specify the grounds of the objection in detail, including the part or specific amount of the disputed assessment objected to. As no objection was made against the disallowance of the allowances in terms of sections 13*quin* and 12F of the Act and the USPs, that assessment became final and conclusive.

(x) That ACSA had contended that the order of the Tax Court was interlocutory and thus not appealable. As the court had shown, the Tax Court had wholly misconceived the matter and, as a result, the order issued was plainly wrong and it could hardly be in the interests of justice to permit it to stand.

Appeal upheld with costs.

Order of the Tax Court was set aside.

5.2. C:SARS v Van der Merwe (85 SATC 10)

Respondent, Ms Candice-Jean van der Merwe, had approached the Cape Town Tax Court under Rule 56(2) of the Tax Court Rules seeking default judgment against SARS based on SARS' alleged failure to file a statement disclosing its grounds for dismissing her objection to the additional income tax assessment raised by SARS in February 2016 concerning the 2014 year of assessment and, in addition, she sought an order reducing this assessment to nil and an order compelling SARS to repay the amount that she had paid on the assessment.

The Tax Court (see *ITC 1946* 83 SATC 504 *per* Rogers J) dismissed the application for default judgment on the basis that the jurisdictional requirements for an application in terms of Rule 56(2) of the Tax Court Rules were not satisfied, insofar as Ms van der Merwe's Rule 56 application had not been preceded by a valid objection and valid notice of appeal and it also ordered Ms van der Merwe to pay the costs of the application on a punitive scale.

Ms van der Merwe then approached the Western Cape Division of the High Court (see *Van der Merwe* v *C:SARS* [2020] ZAWCHC 140 (30 October

2020) *per* Mantame J, with Ndita J concurring and Cloete J dissenting) on appeal which was successful and that court found that the appeal ought to succeed.

SARS then approached the Supreme Court of Appeal which granted it special leave to appeal.

The issue before the Supreme Court of Appeal was whether the High Court had correctly upheld Ms van der Merwe's appeal.

The facts of the case were that Ms van der Merwe's tax return for the 2014 tax year reflected taxable income of R365 919. She also declared a receipt of R142 901 673 as a 'gift from her companion abroad.' In January 2015 SARS raised an original assessment in accordance with this return and the 'donation' was not subjected to tax.

SARS, in February 2015, had started a process of interrogating the tax return and the foreign 'donation'. Settlement was also explored.

On 7 December 2015 MacRobert Attorneys (MR), who represented SARS, wrote to Werksmans Attorneys (Werksmans), who represented Ms van der Merwe, enclosing a draft letter of audit findings. The view expressed in the draft findings was that the amount of some R142.9 million was not a gratuitous donation and was subject to income tax.

On 18 December 2015 Werksmans sent a settlement proposal to MR, the essence of which was that:

- of the R142.9 million, a sum of about R110.3 million be treated as taxable income;
- the balance be treated as a foreign donation not subject to tax;
- SARS not raise interest or penalties on the late payment of tax on the sum of R110.3 million; and
- the funds which Ms van der Merwe's foreign benefactor would pay to enable her to meet the tax on the sum of R110.3 million be recognised as a foreign donation not subject to tax.

On 18 February 2016 MR wrote to Werksmans stating that SARS had approved the settlement proposal. The amount payable was R44 175 675. MR confirmed that no penalties or interest would be raised and that the money received by Ms van der Merwe from her benefactor to enable her to meet the tax obligation would not in itself be subject to any tax.

On 10 March 2016 Werksmans sent MR 'proof of payment of the settlement consideration'. The attached proof of payment showed that the sum was paid from a Werksmans' account.

On 10 September 2018 Ms van der Merwe lodged a notice of objection to the additional assessment of 17 February 2016 together with an application condoning the late filing of the objection. This set in motion the events leading to the application for default judgment by Ms van der Merwe that served before the Tax Court, in terms of which Ms van der Merwe had sought to reverse what her attorneys had plainly agreed on her behalf.

Ms van der Merwe lodged her objection *via* her electronic filing (SARS eFiling) profile. She had not obtained an extension of time prior to doing so.

Ms van der Merwe, in the objection itself, gave the following as the reasons for her late submission:

- the additional assessment to tax that was raised by SARS was not provided to her,
- was for the first time ever seen when same was accessed and printed on her e-filing profile, and
- had not been provided to her for objection as provided for in the Tax Administration Act (TA Act).

Ms van der Merwe's 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.'

SARS, on 21 September 2018, had granted the condonation sought by Ms van der Merwe, but thereafter on 14 December 2018 wrote to Ms van der Merwe informing her that the decision to allow the late submission was 'under review' for various reasons*, inter alia* that the additional assessment was raised in terms of section 95(3) of the TA Act and was not subject to objection or appeal.

SARS, on 22 February 2019, addressed a letter to Ms van der Merwe stating that in terms of section 9 of the TA Act it was withdrawing its condonation for her late objection.

SARS, on 25 February 2019, issued, *via* Ms van der Merwe's SARS eFiling profile, a 'notice of invalid objection'. The notice 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 TA Act and not subject to objection and appeal.

Ms van der Merwe, on 5 March 2019, caused a notice of appeal to be filed in which she asserted that SARS' reliance on section 95(3) was rejected and she *inter alia* asserted that 'there was no estimation of assessment raised, but rather an additional assessment on which the tax was paid on the basis of pay now, argue later.'

SARS, on 8 March 2019, responded to the notice of appeal and advised that the objection that had previously been submitted had been declared invalid and, accordingly, the appeal was also invalid as it did not comply with the TA Act read with the Rules. A notice of appeal had to be preceded by an objection.

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

Ms van der Merwe, on 6 June 2019, delivered her application for default judgment and SARS delivered a notice of opposition on 1 July 2019.

SARS contended that there was no basis in fact or law for the application for default judgment; that the assessment in question was issued by agreement in terms of section 95(3) of the TA Act; and that SARS' view of the application was that it was 'cynical, vexatious and an abuse of the court procedures.'

Judge Molemela held the following:

(i) That SARS had contended that the assessment against which Ms van der Merwe had objected was an agreed assessment in terms of section 95(3) of the TA Act, which was 'not subject to objection or appeal.' This contention was largely based on correspondence exchanged between SARS' attorneys and those of Ms van der Merwe. It was clear from that correspondence that the settlement negotiations had culminated in an agreed income tax assessment being raised.

(ii) That the letters sent on behalf of SARS made it pertinently clear that the pending litigation would only be withdrawn on certain conditions, which included payment of the money on a full understanding that the provisions of section 95(3) would be applicable. In short, the settlement agreement provided that section 95(3) would apply to the agreed assessment.

(iii) That, under these circumstances, Ms van der Merwe's assertion (in the notice of appeal) that the amount was paid on a 'pay now, argue later' basis was simply untrue.

(iv) That on the *conspectus* of all the relevant facts, the inference was irresistible that Ms van der Merwe had paid the agreed amount within the contemplation of section 95(3) and not on the basis of the 'pay now, argue later' principle, as alleged in Ms van der Merwe's notice of appeal.

(v) That once it was accepted, as it must, that the provisions of section 95(3) were applicable, it followed that Ms van der Merwe's additional assessment could not be the subject of an objection or appeal as an appeal had to be preceded by a valid objection and a decision thereon.

(vi) That there could be no doubt that SARS was correct in asserting that Ms van der Merwe's objection was invalid. In this regard, it was important to bear in mind the provisions of Rule 7(4), which empowered SARS to regard an objection that does not comply with the requirements of subrule (2) as invalid and this, in substance, was what SARS had conveyed to Ms van der Merwe in terms of the notice of invalid objection.

(vii) That, as stated before, Ms van der Merwe's application for default judgment was predicated on Rule 56. However, the stumbling block for Ms van der Merwe was that she had failed to show that, notwithstanding SARS' notification about Ms van der Merwe's invalid objection, she was entitled to lodge an appeal. To reiterate, an appeal must be preceded by a valid objection and a decision thereon. In the absence of any one of those, there can be no appeal. Ms van der Merwe simply did not meet the jurisdictional requirements that warranted the consideration of an application, which presupposes compliance with all the prerequisites.

(viii) That, accordingly, the application in the Tax Court was premature, because SARS was not in default as envisaged in Rule 56(1). Therefore, the jurisdictional requirements for an application in terms of Rule 56(2) were not satisfied. In the court's view the Tax Court's finding that Ms van der Merwe's Rule 56 application was not preceded by a valid objection and valid notice of appeal was unassailable and the Tax Court was entitled to make that finding even on an unopposed basis.

Appeal upheld with costs.

Order of the High Court set aside.

5.3. ITC 1959 (85 SATC 35)

The Taxpayer, being Taxpayer H, was a private company and described itself as an investment holding company with its assets comprising, in the main, unlisted shares in subsidiary entities, loans advanced to the subsidiaries and cash.

The Taxpayer, in addition to being an investment holding company, claimed that during the time germane to this appeal, i.e. the 2011 year of assessment, it had conducted a trade in money lending with the specific purpose of making a profit from on-lending borrowed funds to its subsidiaries. All money borrowed free of interest, according to the Taxpayer, was used for share investing activities, while interest bearing borrowings were applied towards lending to the subsidiaries.

The present dispute could be traced to SARS issuing a letter of audit findings (the letter) dated 14 December 2014 in which it had intimated its intention to disallow the interest deduction of R68 133 602 claimed by the Taxpayer and, instead, limit it to the amount of interest received of R34 936 000, which was informed by its long standing practice as set out in its Practice Note 31 read with section 5(1)of the Tax Administration Act (TA Act).

SARS, in addition, imposed an understatement penalty of 10% on the ground that the Taxpayer had made a substantial understatement.

The letter recorded that SARS had come to the conclusion that the interest had not been incurred whilst carrying on a trade, nor was it incurred in the production of income and on this basis the requirements set out in section 24J(2) of the Income Tax Act had not been complied with and the interest was therefore not deductible and, in this regard, SARS identified the following common cause facts as the basis for its conclusion that the interest was not deductible:

- The Taxpayer borrowed funds at an interest rate of 8.29% *per annum*, yet it extended loans to its subsidiaries at interest rates ranging between 0%, 5.29%, 6.22% and at times 8.29% *per annum*;
- The Taxpayer' borrowings were far less than its receivables;
- The Taxpayer's lending transactions extended only to its subsidiaries;
- The interest rates imposed by the Taxpayer demonstrated no commercial sagacity and exposed its transactions as nothing more than furthering the group's interests, by enhancing the earning capacity of the subsidiaries and, according to SARS, the transactions were about funding unproductive loans and the Taxpayer had structured its lending transactions so that it could earn neither income nor profit.

SARS had also referred to the fact that the individual loans carried no security, were not recorded, and had no terms and, in addition, the Taxpayer had not incurred any other expense and had no staff to demonstrate how it managed the loans in question.

SARS further contended, in regard to the understatement penalty, that the Taxpayer's incorrect deduction which was not permissible in terms of section 24J(2) of the Income Tax Act was prejudicial to SARS and the *fiscus* and that SARS had appropriately levied the penalty.

The letter also invited the Taxpayer to provide reasons in the event that it disagreed together with any material that may support its case.

t, in its letter of response dated February 2015, had disputed SARS's conclusions and its main contention was that, notwithstanding that its lending rate was not profitable in 2011, it was profitable in 2012 and its ultimate point in support of its profit motive was that for approximately five of the six years post 2011, it had demonstrably made a profit and in its view the interest expense had been incurred whilst it was carrying on its trade of money lending and it had incurred the interest expense in the production of income and the interest expense incurred was thus deductible in full and, further, there was no basis for SARS to have levied the understatement penalty.

SARS finalised its audit on 8 April 2015 and issued the additional assessment on 28 April 2015.

The Taxpayer's objection was disallowed and this was followed by a notice to appeal which led to the present appeal.

The issues to be determined by the court were:

- Whether the interest sought to be deducted by the Taxpayer was incurred whilst carrying on a trade;
- Whether the interest was incurred in the production of income;
- Whether SARS was justified in imposing an understatement penalty.

Judge Bam held the following:

As to whether Practice Note 31 was an issue in the appeal

(i) That it was not common cause, and it was not correct that SARS had relied on Practice Note 31 in disallowing the interest deduction. The undisputed facts were that the interest expense, in SARS's view, based on the requirements of section 24J(2), was not deductible. On the contrary, in allowing the partial deduction, SARS had relied on the Practice Note as its common practice.

(ii) That whether SARS was correct in its assertions in disallowing the interest deduction was the subject matter of this appeal and this was plain from a cursory reading of the parties' Rule 31 and 32 Statements. This then made the Practice Note a non-issue in this appeal and, after all, the court did not understand the Taxpayer's contentions to mean that it rejected the partial allowance of the interest, and the Taxpayer was correct in stating that this was never an issue and there was no need to take the issue of the Practice Note any further.

As to whether the Taxpayer was carrying on a trade as a money lender

(iii) That the courts had repeatedly cautioned that the question of whether a person was carrying on a lending trade was to be established from the facts of each case.

(iv) That the court referred to the guidelines set out in Solaglass Finance Co (Pty)Ltd v CIR 53 SATC 1 as a means of establishing whether one was carrying on a trade as a moneylender or banker and there had to be an intention to lend to all and sundry provided that they were, from the taxpayer's point of view, eligible. Moreover, the lending had to be done on a system or plan which disclosed a degree of continuity in laying out and getting back the capital for further use and which involved a frequent turnover of the capital and the obtaining of security was a usual, though not essential, feature of a loan made in the course of a moneylending business.

(iv) That in the judgments in ITC 1771 66 SATC 205 and ITC 812 20 SATC 469 the courts stated, i*nter alia*, that 'A long-term loan without any repayment terms, in my view, lacks the essential characteristics of floating capital which, if it becomes irrecoverable, constitutes a loss of a capital nature' and 'The main difference between an investor and a money lender appears to consist in the fact that the latter aims at the frequency of the turnover of his money and for that purpose usually requires borrowers to make regular payments on account of the principal. This has been described as a system or plan in laying out and getting in his money.'

(v) That it was noteworthy to point out that throughout its correspondence with SARS and in its Rule 32 Statement, the Taxpayer's case was founded on a claim that the interest expense was deductible in full because it was incurred whilst carrying on a trade in money lending with the purpose of producing income, specifically, from interest generated from its on-lending activities. Faced with the stark conclusions to be drawn from applying the law to the facts of its own case, it was plain from a simple reading of the Taxpayer's heads of argument that the Taxpayer no longer wished to identify with its claims of carrying on a trade in moneylending and it now relied on the rather vague phrase of 'interest earning and interest incurring activities' to describe its trade.

(vi) That the Taxpayer did not dispute that the individual loans to its subsidiaries were not memorialised and carried no terms including repayment terms. It could provide no Board minutes or documents evidencing its lending policy and there was no security provided for the loans. The Taxpayer could not provide evidence of a plan of laying out and getting in its money as evidence of continuity. Given these undisputed facts, it must now be pellucid why the Taxpayer no longer wishes to make a case that it was carrying on a trade in money lending because it fell woefully short in meeting the test espoused in cases such as Solaglass, *supra*, to sustain its claim. Indeed, other than the claim that it was engaged in a trade of money lending with its transactions to the subsidiaries, the Taxpayer had not provided a single piece of evidence in substantiation.

(vii) That when one brought into the equation the declaration recorded in its tax return of 2011 that it had not concluded any transaction in terms of section 24J of the Income Tax Act, it became even more difficult for the Taxpayer to sustain its claims of carrying on a trade in moneylending.

(ix) That in regard to whether the Taxpayer had a profit motive in its lending activities, SARS testified that the Taxpayer's lending transactions demonstrated no profit-making motive and it was plain that the Taxpayer could never earn any interest income, let alone profit and it had subjugated its profit earning opportunity to advancing the profit interests of its subsidiaries.

(x) That the Taxpayer was correct in its reasoning that, boosting the earning capacity of the subsidiaries made commercial sense for it as an investor and sole shareholder, as it was placed in a position to reap lofty dividends. However, this court was not concerned with what makes commercial sense for the Taxpayer as an investor, but it was interested in commercial expediency and the indirect facilitation of the Taxpayer's trade as a money lender.

(xi) That it was common cause that the Taxpayer, at the time relevant to this appeal, was an investment holding company with no staff. It had not incurred a single expense other than the interest expense in question. It also could not demonstrate how it managed the loans. Money lenders demonstrate their profit-making purpose by charging remunerative interest rates and fixing terms when lending. In addition, they use a plan or system of laying out and getting back their capital to demonstrate continuity.

(xii) That money lenders do not borrow at high interest rates and lend at either nil or substantially low interest rates or at the very same interest they incurred, and look to the *fiscus* to finance the growth of the borrower and enhance its profitability, in the comfort that they will reap lofty dividends. The court found SARS' argument, that the Taxpayer's lending transactions were about funding unproductive loans for the Taxpayer to reap exempt income, compelling.

(xiii) That, on the evidence, there was no objectively ascertainable system for the Taxpayer to recover its capital nor the interest and it was now plain that the Taxpayer's transactions demonstrated no profit motive.

(xiv) That, further, on the issue of profit making purpose, the Taxpayer placed reliance on section 24J(3) but, in the court's view, section 24J(3) had no relevance to the Taxpayer's case as it dealt with an income instrument. It was never the Taxpayer's case that it had either issued or was the holder of an income instrument. One of the defining terms of an income instrument was a term that exceeded or was reasonably likely to exceed one year. It was common cause that the Taxpayer lent only to its subsidiaries, without terms. There was no basis to add interest from the bank when evaluating the Taxpayer's profit-making purpose on its money lending.

<u>As to whether the interest expense was incurred in the production of income</u>

(xv) That in order to determine whether expenditure was incurred in the production of income, the important and sometimes overriding factor was the purpose for which the expenditure was incurred and what it actually effects. In this regard the court must assess the closeness of connection between the expenditure and the income earning operations undertaken by the Taxpayer.

(xvi) That the Taxpayer had maintained that the interest had been incurred in the production of income on the loans advanced as part of its lending trade, whether such income was earned during the 2011 tax year or later. It further submitted that the mere fact that the interest earned on the loans made to the group in 2011 did not exceed the interest incurred did not mean that the interest was not incurred in the production of income and stated that it had met the 'in production of income' requirement of section 24J(2) of the Income Tax Act.

(xvii) That SARS argued that the purpose of the borrowing was to provide the Taxpayer's subsidiaries with advantageous loans to benefit the group by increasing their earning capacity and that the Taxpayer had led no evidence to demonstrate that interest had been incurred in the production of income.

(xviii) That however one analysed the Taxpayer's lending transactions, they demonstrated neither a profit-making purpose nor the intention to produce income and the court concluded that the Taxpayer had failed to demonstrate that the interest expense had been incurred in the production of income.

As to the understatement penalty imposed

(xix) That SARS had stated that the Taxpayer adopted a tax position that the interest expense was deductible in full and it further stated that by claiming the interest deduction, which it was not entitled to, the Taxpayer had understated its income. The Taxpayer knew that it had no records to substantiate its moneylending trade and the Taxpayer had failed to lead evidence to demonstrate that the understatement of its income was as a result of a *bona fide* inadvertent error and also had failed to lead evidence to contradict SARS' findings that the penalty was appropriately levied.

(xx) That the Taxpayer had affirmed its position by stating that the interest expense was fully deductible and that there was no understatement. It stated further that in the event that the court were to disagree with its conclusions that the interest was deductible, and consequently, that there was indeed an understatement, such understatement was as a result of a *bona fide* inadvertent error.

(xxi) That the Taxpayer further contended that it was for SARS to satisfy itself that the understatement did not result in such an error, this being a jurisdictional fact for SARS to overcome prior to imposing any understatement penalty.

(xxii) That the court did not accept the Taxpayer's contention that, prior to levying the understatement penalty, SARS had a duty to satisfy itself that the understatement did not result from a *bona fide* inadvertent error. The Taxpayer's assertion amounted to turning the burden of proof set out in section 102(2) of the TA Act on its head. The burden remained with the Taxpayer to prove that the interest expense was deductible and hence no understatement of its income. In the event that the Taxpayer had provided evidence that the understatement was due to an inadvertent *bona fide* error, in terms of section 221 of the Act, it would not be competent for SARS to levy the understatement penalty, but the Taxpayer had led no such evidence and had led no evidence to demonstrate that it had relied on expert evidence.

(xxiii) That, on the other hand, SARS had highlighted the Taxpayer's failure to demonstrate that it was conducting a trade and the court concluded that the understatement penalty had been appropriately levied in the circumstances of this case.

Appeal dismissed with costs.

5.4. ITC 1960 (85 SATC 53)

The Taxpayer was registered as an employer as contemplated in section 3 of the Employment Tax Incentive Act ('the ETIA') for the purposes of the withholding and payment of employees' tax by virtue of par. 15 of the Fourth Schedule to the Income Tax Act ('the ITA').

The Taxpayer, as such, was eligible to receive the Employment Tax Incentive (ETI) instituted in terms of section 2(1) of the ETIA in respect of its qualifying employees.

In each month falling within a six-month ETI tax period, being 1 September 2017 to 28 February 2018 ('the relevant period) the Taxpayer was eligible to receive the ETI in respect of all its qualifying employees as envisaged by section 6 of the ETIA, which amount was determined in terms of section 7.

There was no dispute between the parties that monthly returns in the form of monthly employer declarations ('EMP 201') were submitted timeously by the Taxpayer during the relevant period.

Paragraph 14(2)(*b*) of Part 11 of the Fourth Schedule to the ITA obligates every employer when making any payment of employees' tax, to submit a return to SARS and this return was the EMP501 reconciliation.

For purposes of the appeal it was common cause between the parties that for the relevant period ETI of R3 757 633 was available to the Taxpayer and that in the return, being an employer reconciliation declaration EMP501 ('the original EMP501') submitted by the Taxpayer to SARS, on 31 May 2018, the Taxpayer only claimed R2 344 503 of its available ETI as a reduction of its PAYE debt to SARS.

The original EMP501 was the return which the Taxpayer was required to render for the relevant period in terms of par. 14(3)(*a*) of the Fourth Schedule to the ITA and was a 'self-assessment.'

The Taxpayer objected to its self-assessment and submitted a revised EMP501 on 19 July 2018 in order to correct the determination of its tax liability or refund as contained in the original EMP501.

The Taxpayer, in the revised EMP501, included the understated amount of R1 413 130 and requested SARS to refund that amount.

SARS disallowed the objection which resulted in the noting of the present appeal.

The Taxpayer sought the alteration of its assessment in the EMP501 and costs in terms of, respectively, section 129(2)(*b*) and section 130(1)(*a*) of the Tax Administration Act (the TA Act).

The present appeal pertained to the understated ETI amount of R1 413 130, being 'the understated amount.'

The issues to be determined by the court were:

- The proper application of the relevant legal principles and mechanisms relating to the payment of the ETI;
- The proper construction of the relevant statutory provisions that informed such principles and the recovery mechanisms to claim payment of the ETI;

- Whether or not the Taxpayer was entitled to claim and receive payment of the agreed quantum of ETI.

SARS contended that on a proper interpretation of section 9(4) and section 10(3) of the ETIA and the deeming provisions contained therein, the Taxpayer was not entitled to recover the understated amount.

SARS contended that the deeming provisions in the aforesaid sections created a time bar clause, that no amounts could be claimed once the prescribed periods had expired and that any unclaimed amounts would be forfeited.

SARS contended further that the Taxpayer was only entitled to deduct the monthly qualifying ETI amounts from the PAYE payable by it when it submitted the monthly EMP201 returns. The submission of the assessment EMP501 which was due on 31 May 2018 for the relevant period, afforded the Taxpayer the last opportunity to adjust for, claim and recover ETI for the relevant period under the ETIA. As the Taxpayer had failed to claim the understated amount on any of the permissible occasions, sections 9(4) and 10(3) in essence provided that any unclaimed amount of ETI was deemed to be nil thereafter and, consequently, the Taxpayer was not entitled to claim any understated amount thereafter.

The Taxpayer contended that it was entitled to recover the understated ETI amount, being an amount contemplated in section 2(2) of the ETIA and it being entitled to receive payment of that amount as one contemplated in section 10(2) in respect of the relevant period ending February 2018.

The Taxpayer contended further that the deeming provisions in section 9(4) and section 10(3) of the ETIA, read in context and in the light of that Act as a whole, did not result in it having forfeited its right to claim the understated ETI amount.

Judge Dippenaar held the following:

(i) That the central issue in the case was whether SARS was correct in contending, as in its dismissal of the Taxpayer's objection, that on a proper interpretation of section 9(4) and section 10(3) of the ETIA and the deeming provisions contained therein, the Taxpayer was not entitled to recover the understated amount.

(ii) That it was apposite to first consider the context within which the ETIA was promulgated and the circumstances attendant upon its coming into existence. The context of the statutory provisions and ETIA cannot be considered in isolation, but must be considered against the backdrop of other applicable legislation pertaining to employees' tax as the legislature employed the statutory regime already available for the deduction, withholding and payment of employees' tax as a convenient vehicle for administering the claiming and receiving of ETI by eligible employers in respect of eligible employees in their employment.

(iii) That the purpose of the ETIA was thus to support employment growth in the private sector by creating an employment tax incentive to eligible employers in respect of eligible employees, especially young people, to curb the high unemployment rate in the country.

(iv) That the *Explanatory Memorandum* on the Taxation Laws Amendment Bill 17B of 2016 reflects that the ETI scheme had been effective in promoting employment, especially by young workers, justifying the extension of the program. In its express terms, there was no indication that it was intended that an employer lose the benefit entirely at the end of a period. Rather, it envisaged that at the end of each six-month reconciliation, any excess would become available as a refund to the employer and the *Memorandum* did not in its terms envisage the forfeiture of the benefit.

(iv) That it was apposite to note that the ETIA contained no express forfeiture provision particularising any circumstances under which an eligible employer forfeited the ETI. The only provision particularising circumstances under which an employer cannot claim the ETI are contained in section 8 which, it was common cause, was not applicable.

(v) That the relevant provisions requiring interpretation were sections 2, 9, and 10 of the ETIA, which must be interpreted in the context of the ETIA as a whole. As stated in *Natal Joint Municipal Pension Fund* v *Endumeni Municipality* 2012 (4) SA 593 (SCA), consideration must be given to the language used in the relevant statutory provisions in light of the ordinary rules of grammar and syntax, the context of the provisions, the apparent purpose at which it was directed and the material known to those responsible for its production.

(vi) That the Taxpayer's claim was predicated on section 2(2) and its entitlement under section 10(1) of the ETIA to claim an excess amount at the end of the relevant period from SARS in its EMP501. On its interpretation the deeming provisions in section 9(4) and section 10(3) were aimed at preventing an employer from benefitting twice from the same ETI.

(vii) That SARS relied on the deeming provisions in section 9(4) and section 10(3) in contending that the Taxpayer forfeited the ETI benefit in May 2018. SARS argued that the legislative purpose of sections 9 and 10 of ETIA was to promote a 'use it or lose it policy' by effectively establishing a time bar for either claiming the excess, if there was one, or, if employers had already successfully reduced their PAYE liability, then by clearly precluding them from claiming any ETI that was unclaimed at the expiry of the period when the time bar is activated, i.e. on 1 March 2018. According to SARS, on 1 March 2018, the amount was already nil, i.e. non-existent and the Taxpayer could not claim as it did in the amended EMP501 on 19 July 2018.

(ix) That the precise meaning, and especially its effect, of the deeming provisions here in issue, must thus be ascertained from its context and the ordinary canons of construction. Applying the relevant principles and considering the context, the court agreed with SARS that the deeming provisions in both section 9(4) and section 10(3) were exhaustive but the court was not however persuaded that such conclusion assisted SARS.

(x) That the court agreed with the Taxpayer that there was a distinction between the return for the relevant period in May 2018 and the relevant period itself, which ended on 28 February 2018. This distinction was ignored by SARS in its argument that the Taxpayer forfeited its unclaimed ETI benefit from May 2018 as it disregarded the first relevant period, which ended at 28 February 2018 and the date of the EMP501, being 31 May 2018. A distinction must also be drawn between the date on which the relevant period ends and the date on which the deeming provisions in section 9(4) and section 10(3) take effect, being 1 March 2018 and March 2018 respectively.

(xi) That, read purposively and in context, the import of section 9(4) was to achieve that there was no rolling over of an excess amount at the end of the period. It did not mean that it could not be claimed as of that date. The deeming provision in section 9(4) meant that on the first day of the month following the end of the period to which the relevant EMP501 related, i.e. 1 March 2018, any unclaimed amount was deemed to be nil. There is no rolling forward of the amount and at that time, the employer cannot roll the unutilised ETI amount forward by adding it to the ETI in the next period, which is achieved by the excess period being deemed to be nil in the month following that period, being March 2018. The next period thus starts with a clean slate. The employer now needs to claim such amount in terms of section 2(2) read with section 10. The provision does not have the intention that the employer loses the benefit of the unclaimed amount entirely. It is precluded from rolling forward that benefit but not from claiming it as a payment.

(xii) That as at 28 February 2018 an unclaimed amount is not yet deemed to be nil, either under section 9(4) or section 10(3). Therefore, any unclaimed amount existing on that date is an excess amount that can be recovered as a payment from SARS for the relevant period ending on that date. Read in context, it cannot be concluded that the deeming provisions intended the benefit to be lost to the employer entirely, but only from rolling forward the benefit and receiving that benefit twice.

(xiii) That there was no link between the deeming provisions in either section 9(4) or section 10(3) and the date on which the Taxpayer was obliged to render the EMP501, being 31 May 2018. The deeming provisions of sections 9(4) and 10(3) only come into play on 1 March 2018 and do not apply in respect of the relevant period, which terminates on 28 February 2018.

(xiv) That applying the relevant principles and interpreting the provisions purposely and in context in their terms, it was concluded that the effect of sections 9(4) and 10(3) was that an employer could not use a reimbursed unclaimed amount to reduce a further PAYE debt, i.e. to benefit twice from the same ETI which was the mischief that the Legislature had sought to prevent. Considering the entire tenor of the ETIA, it was not intended at the end of the period that the employer loses the benefit of the excess amount entirely and whilst an employer is precluded from rolling over that benefit, it was not precluded from recovering such benefit as a payment of an excess amount or a deemed excess amount.

(xv) That such interpretation was consistent with the stated purpose of ETIA, being to provide employers with a benefit that encourages employment creation. It is also consistent with the *Explanatory Memorandum*, which militates against the time bar interpretation contended for by SARS. The forfeiture of a benefit is an important consideration with substantial consequences which cannot be lightly inferred and an issue which the Legislature would have expressly addressed if that was the intention. If SARS was permitted to withhold that benefit from the Taxpayer in the present circumstances it would be inconsistent with the purpose of ETIA as a whole and the relevant provisions providing for the recovery of that benefit by the Taxpayer.

(xvi) That on SARS' interpretation it would result in the forfeiture by the Taxpayer of a benefit given to it, in circumstances where there is no provision in ETIA for such forfeiture and the circumstances under which it will occur. SARS' interpretation will create uncertainty and place taxpayers in the position where they are unable to be certain that a tax benefit provided for in ETIA can be relied on by them.

(xvii) That, for these reasons, it was concluded that SARS' contention that the Taxpayer had forfeited the unclaimed amounts was not sustainable and that the Taxpayer was entitled to claim and receive payment of the agreed *quantum* of ETI.

(xviii) That the Taxpayer had sought a costs order against SARS in terms of section 130(1)(*a*) of the TA Act on the basis that SARS' grounds of assessment were unreasonable. Considering all the facts and the dearth of authority on the issue, the court was not persuaded that SARS' basis of opposition could be characterised as unreasonable or that an adverse costs order should be granted.

Appeal upheld.

No order made in relation to costs.

5.5. ITC 1961 (85 SATC 71)

SARS following an audit conducted by it, had raised additional assessments in respect of the Taxpayer's 2016 to 2018 years of assessment.

In terms of rule 6 of the Tax Court rules a taxpayer aggrieved by an assessment may, prior to the lodging of an objection, request SARS to provide reasons, which request must be delivered within 30 days from date thereof.

The Taxpayer duly requested reasons within the 30-day period on 2 April 2020.

SARS was required to provide its reasons within 45 days of delivery of the request in accordance with rule 6(5) but had failed to do so.

In terms of rule 6(6) this initial 45-day period may be extended by SARS if its official was satisfied that more time was required to provide reasons due to 'exceptional circumstances, the complexity of the matter or the principle or the amount involved.'

However, rule 6(7) stipulated that the notice of such an extension must be delivered to the Taxpayer prior to expiry of the initial 45-day period and the extension may not exceed a further 45 days.

However, SARS only notified the Taxpayer of the extension it required some 16 days after expiry of the initial 45-day period. It finally delivered its reasons on the very last day of the extension which it had unilaterally imposed, and this was despite the fact that it had raised the additional assessments as a result of its own audit almost 6 months earlier.

The Taxpayer, upon receipt of the reasons, delivered its notice of objection within 30 days thereafter in accordance with rule 7(1)(*a*) and, in turn, rule 9(1)(*a*) required SARS to deliver a decision on an objection within 60 days. Again, SARS failed to meet this deadline, and it was only after the Taxpayer put it to terms by delivery of a rule 56(1)(*a*) notice, that SARS transmitted its decision, which was a partial disallowance of the objection.

The Taxpayer's notices of appeal had to be delivered within 30 days thereafter in accordance with rule 10(1)(*a*) and the notices of appeal were duly delivered.

SARS was required to deliver its rule 31 statement, being its statement of grounds of assessment and opposing appeal within 45 days thereafter in terms of rule 31(1)(*d*).

SARS' rule 31 statement was not delivered within the prescribed time limit and one day after it had expired SARS notified the Taxpayer that the appeal in respect of the years of assessment 2016 to 2018 had been referred to the Tax Court Litigation Unit for litigation in the Tax Court and no request was made therein for condonation for the late filing of the rule 31 statement, and, as had been the case previously, nor was any explanation given for the delay.

The Taxpayer thereafter delivered its rule 56(1)(*a*) notice putting SARS to terms to remedy its default within the prescribed 15-day period, failing which it intended to apply for a final order under section 129(2) of the Tax Administration Act (the TA Act).

An official from the SARS Litigation Unit acknowledged by letter to the Taxpayer that the time period to deliver the rule 31 statement had lapsed prior to the matter being allocated to her and she advised that it had now become evident that she would not be able to finalise the rule 31 statement within the requisite period as per the notice in terms of rule 56(1)(*a*) and she requested an extension of the time period within which to file the rule 31 statement.

The Taxpayer thereafter advised that it was willing to grant an extension of one month and later tried to accommodate SARS with a further extension provided that the rule 31 statement covering all three tax years would be provided on that day. However, the rule 31 statement was not delivered and SARS advised the Taxpayer that the matter had been re-allocated to another official in the same unit and it was also advised that SARS had briefed counsel to assist it with finalising its rule 31 Statement and accordingly requested a further extension.

The Taxpayer, who had finally had enough, refused the request and informed SARS that it would have to bring an application for condonation in terms of rule 52(6).

The Taxpayer placed on record *inter alia* that no proper reasons for the further delay had been provided (nor for any of the prior delays) and the Taxpayer then launched its application for a final order on 10 August 2021.

SARS ultimately only served its rule 31 Statement on 21 September 2021, which was 36 days after the agreed extended deadline and 15 days after the expiration of the deadline which it itself had thereafter requested.

This matter involved two inter-related applications:

- the first was that of the Taxpayer for a final order against SARS due to the latter's failure to deliver its rule 31 Statement timeously, and
- the second was SARS's counter-application for condonation and the determination of a further period for delivery of that Statement and both applications were opposed.

The first issue to be determined by the court was whether SARS's delay was so egregious that it should not be countenanced and the second issue was whether the Taxpayer was entitled to the substantive relief which it sought, namely the upholding of its appeal in relation to its 2016 to 2018 years of assessment.

The additional assessments raised totalled some R8.4 million and on 11 June 2020, i.e. the day after expiry of the initial period in which SARS was required to provide reasons but failed to do so, the Taxpayer had submitted a request to SARS in terms of section 164(2) of the TA Act for suspension of payment of the amounts owed in terms of the additional assessments.

Section 164(6) stipulated *inter alia* that during the period commencing on the day that SARS received a request for suspension under section 164(2) until 10 business days after notice of SARS' decision, or revocation of suspension, has been issued, no recovery proceedings may be taken by SARS unless it holds a reasonable belief that there is a risk of dissipation of assets by the taxpayer concerned.

There was no suggestion in its papers that any SARS official held such a belief, yet SARS nonetheless proceeded with collection steps and issued the Taxpayer with a final demand for payment. After its error was pointed out by the Taxpayer, SARS eventually formally approved the payment suspension request. Accordingly, from that date onwards, SARS was obliged to reflect the Taxpayer's status as compliant on the e-filing platform, which may be viewed by any person who requests the taxpayer's permission to do so. This, notwithstanding, SARS nonetheless insisted that the Taxpayer first pay the disputed (yet suspended) tax debt before it would reflect it as compliant in relation to its tax affairs.

The Taxpayer had accordingly notified SARS in terms of section 11(4) of the Act that it would be approaching the High Court for an order compelling SARS to reflect its status as tax compliant and SARS finally corrected the status to 'tax compliant' on 29 January 2021.

However, SARS again altered the Taxpayer's tax status to non-compliant and by the time when it launched the present application for final relief, this was still the case.

Judge Cloete held the following:

<u>As to SARS' disregard for and non-compliance with the time limits in the rules</u>

(i) That SARS had displayed a persistent disregard for the time limits prescribed in the rules of the Tax Court. Of particular significance was its failure to seek the extension it required to provide reasons to the Taxpayer before the period for furnishing reasons expired: its failure to request an extension to file its rule 31 Statement before the prescribed time limit expired; its failure to provide any explanation whatsoever to the Taxpayer for these delays; and its woefully inadequate, generalised explanation furnished 10 days later that the matter had only been allocated to its official after expiry of the prescribed time limit for the filing of the rule 31 Statement 'due to backlog as a result of Covid-19, lack of capacity and no filling of vacancies across SARS.'

(ii) That, also significant, was SARS' misleading of the Taxpayer that its official had been allocated the appeal for all three additional assessments when, according to her, she had only been allocated one of them; its misrepresentation to the Taxpayer of the date of the extension to which the latter had agreed; and its misrepresentations to the Taxpayer of the reason why the appeal had been re-allocated to another official and that counsel had 'recently' been briefed.

(iii) That, further, it cannot reasonably be gainsaid that much, if not all, of the information required to prepare the rule 31 Statement should have been available to SARS long before expiry of the period in which it was obliged to file that statement. Presumably, at each of the relevant stages, the SARS officials concerned would, or should, have properly applied their minds to all of the information, along with their knowledge and understanding of the relevant statutory provisions.

(iv) That the most recent series of delays were simply the perpetuation of a pattern of disregard for the rules and what was required of administrative functionaries such as the SARS officials in the present matter.

<u>As to SARS' application for condonation of its non-compliance with the rules</u>

(v) That it was settled law that the standard to be applied in determining an application for condonation was the interests of justice which was a wide and elastic concept and included a consideration of '…the nature of the relief sought; the extent and cause of the delay; the effect of the delay on the administration of justice and other litigants; the reasonableness of the explanation for the delay; the importance of the issue to be raised…; and the prospects of success.'

(vi) That section 195 of the Constitution dealt with basic values and principles governing public administration and in terms of section 195(2) thereof these principles apply *inter alia* to administration in every sphere of government as well as organs of State. One of the purposes of the TA Act was to ensure the effective and efficient collection of tax by prescribing the powers and duties of persons engaged in the administration of a tax Act such as the TAA.

(vii) That in Buffalo City Metropolitan Municipality v Asia Construction (Pty) Ltd 2019(4)SA331 (CC) the Constitutional Court held that if the delay is unreasonable and no satisfactory explanation has been provided, it is necessary to consider whether the delay should be overlooked, which is a flexible approach. One of the factors to be taken into account is the conduct of the Taxpayer concerned, particularly for State litigants (which would be SARS in the present case) because they are often best placed to explain the delay and are subject to a higher duty to respect the law.

(viii) That the court was not aware of any authority which would militate against applying the same principles to SARS in the instant matter, particularly since section 33 of the Constitution entrenches the right of everyone to administrative action that is lawful, reasonable and procedurally fair and this led the court to the issue of prejudice to the Taxpayer.

(ix) That it was undisputed that the nature of the Taxpayer's business was such that it was crucial to its operations to be reflected on the SARS' e-filing system as tax compliant. The additional assessments raised in total some R8.4 million, which was a substantial amount. The Taxpayer had also submitted a request to SARS in terms of section 164(2) of the TA Act for suspension of payment but after a series of errors on the part of SARS the Taxpayer notified SARS in terms of section 11(4) of the TA Act that it would be approaching the High Court for an order compelling SARS to reflect its status as tax compliant and SARS, despite having finally corrected the status to 'tax compliant' failed to implement this by the time that the Taxpayer launched the present application for final relief.

(ix) That the Taxpayer had set out the respects in which SARS' conduct in relation to its tax compliance status had caused it severe prejudice. From a regulatory perspective the Taxpayer was required to be registered with certain regulatory bodies in order to be able to obtain specific export permits whereby it may export its products for sale abroad. A tax compliance status confirmation was a prerequisite.

(x) That, in addition, the Taxpayer had credit facilities with two major banking institutions, both of which required proof of consistent tax compliance for credit purposes; and in order for the Taxpayer to qualify for funding from the Department of Trade and Industry to attend international trade exhibitions, it must be able to produce proof that its status was tax compliant.

(xi) That the Taxpayer thus asserted that while its dispute with SARS was still pending there was an ongoing risk of its status being unlawfully indicated as non-compliant. This rendered finalisation of the dispute urgent, and the time and costs incurred in having to force SARS to comply with its statutory obligations had also caused prejudice to it.

(xii) That whatever gloss SARS sought to put on it, the facts set out demonstrated, in the court's view, that the delay was egregious; there had been no reasonable explanation for the delay; and the consequent prejudice to the Taxpayer (which prejudice SARS admitted, since it sought to ameliorate it) was severe.

(xiii) That, put simply, the evidence showed that in the present case SARS had failed dismally to fulfil its obligations, both under section 195 of the Constitution as well as the TA Act and its rules. It has displayed an egregious lack of regard for the Taxpayer's constitutionally entrenched right to fair administrative action and, cut to its bare bones, had been reduced to relying on what it considered to be a novel issue of public importance to persuade this court to grant condonation.

<u>As to the prospects of success on the merits of the additional assessments</u>

(xiv) That in considering this factor there was an overlap between the condonation sought by SARS and the Taxpayer's application for final relief and the parties were thus given the opportunity to address the court on the merits as well.

(xv) That the crux of the dispute between the parties pertained to the income tax treatment of various aspects of an insurance product taken out by the Taxpayer. SARS had refused a deduction of insurance premiums paid by the Taxpayer to RMB Structured Insurance Limited (RMB) and it was apparent that the refusal was based on the application of section 23L(2) of the Income Tax Act which had been introduced with effect from 1 April 2014.

(xvi) That the parties were in agreement that there was no specific International Financial Reporting Standard (IFRS) dealing with the accounting treatment of insurance contracts from the perspective of the policy holder and the Taxpayer thus obtained the expert opinion of accounting specialists on the application of IFRS and contended that payment of the insurance premium by it resulted in a decrease in its asset base and thus constituted an expense.

(xvii) That, against this, and despite SARS having previously agreed that IFRS 4 did not apply here, in both its affidavit as well as its heads of argument, reliance was placed squarely on IFRS 4 to support the additional assessments. Moreover, in argument SARS confirmed that in its view IFRS 4 did not apply, but that the dispute centred around 'what then does apply.' Put plainly therefore the defence which SARS raised in its papers was contradicted by, and was at odds with, its own argument. In these circumstances the only reasonable inference to be drawn was that, on its own version, SARS lacked prospects of success on the merits of its defence as currently formulated.

(xviii) That, in the court's view, the Taxpayer's case had sufficient merit to enable it to grant it final relief and it was also supported by independent expert opinion. During the hearing the parties were in agreement that if the Taxpayer was to succeed on the 'sole issue' then its remaining grounds of appeal would logically have to succeed as well.

(xix) That, in the result, the Taxpayer was entitled to the final order it sought by default against SARS.

(xx) That, in regard to costs, the Taxpayer had sought costs against SARS on the party and party scale and no mention had been made of a request for a punitive costs order in its papers. However, in its heads of argument filed on its behalf, costs were sought against SARS on the attorney and client scale. While in tax matters an award of costs was the exception rather than the norm, having regard to the facts in this matter, the court was of the view that a costs award in favour of the Taxpayer was warranted on the scale as between party and party as taxed or agreed.

6. INTERPRETATION NOTES

6.1. Determination of the taxable income of certain persons from international transactions: Intra-group loans – No. 127

This Note provides taxpayers with guidance on the application of the arm's length principle in the context of the pricing of intra-group loans. The pricing of intra-group loans includes a consideration of both the amount of debt and the cost of the debt.

An intra-group loan would be incorrectly priced if the amount of debt funding, the cost of the debt or both are excessive compared to what is arm's length. The Note also provides guidance on the consequences for a taxpayer if the amount of debt, the cost of debt or both are not arm's length.

The guidance and examples provided are not an exhaustive consideration of every issue that might arise. Each case will be decided on its own merits taking into account its specific facts and circumstances.

The application of the arm's length principle is inherently of a detailed factual nature and takes into account a wide range of factors particular to the specific taxpayer concerned.

Section 31 was substituted by the Taxation Laws Amendment Act, 2011 with effect from years of assessment commencing on or after 1 April 2012. Practice Note 2 of 14 May 1996 and its Addendum of 17 May 2002, which gave guidance on section 31(3), were withdrawn for years of assessment commencing on or after 1 April 2012, since they were no longer applicable from the date the legislation changed.

Taxpayers are broadly financed in two ways, namely using equity and debt. The returns on equity capital and debt capital are treated differently for tax purposes. Interest payments incurred in the production of income by a person carrying on a trade are, subject to certain conditions, exceptions and restrictions, deductible in determining taxable income while dividends and returns of capital are not deductible.

The way in which a taxpayer is financed has an impact on the calculation of the taxpayer's taxable income. This raises tax concerns regarding the balance between the amount of equity capital and debt capital. A taxpayer that is considered to have too much debt when considered against the amount of its equity is said to be thinly capitalised for tax purposes.

Thin capitalisation becomes a potential issue where a South African taxpayer is directly or indirectly funded by a non-resident relevant party. The funding of a South African taxpayer with excessive intra-group, back-to-back or intra-group-guaranteed debt may result in excessive interest deductions thereby depleting the South African tax base when there is a mismatch with the taxability of the interest income because of interest exemptions and reduced rates of withholding tax on interest.

South Africa introduced thin capitalisation rules in 1995. Under these rules, which were contained in section 31(3), SARS was empowered to have regard to the international financial assistance rendered and if it was considered excessive in proportion to the particular lender's fixed capital in the borrower, the interest, finance charges or other consideration relating to the excessive financial assistance were disallowed. SARS's views on what constituted excessive international financial assistance were documented in Practice Note 2 of 14 May 1996. These rules and Practice Note 2 have been repealed and are only applicable to years of assessment commencing before 1 April 2012.

For years of assessment commencing on or after 1 April 2012, thin capitalisation is no longer dealt with by a separate subsection of section 31 and is instead governed by the general transfer pricing provisions of section 31(2). Section 31(2) applies to, for example, the amount of the intra-group loan and the rate of interest incurred during years of assessment commencing on or after 1 April 2012 irrespective of whether the underlying loan was initially granted before, on or after that date.

One of the most significant changes is that taxpayers must determine the acceptable amount of debt applying arm's length principles. The application of the arm's length principle to intra-group loans will be considered further in this Note.

The pricing of intra-group loans includes a consideration of both the amount of debt and the cost of the debt.

This Note deals with the provisions of section 31 which, as noted above, are applicable for years of assessment commencing on or after 1 April 2012. For example, in the case of a year of assessment ending on 31 December, the first year of assessment to which the new legislation applies is the year of assessment commencing on 1 January 2013 and ending on 31 December 2013.

In summary:

- Section 31 applies to affected transactions which are broadly cross border33 transactions between relevant parties that have been concluded on terms and conditions that would not have existed if the parties had been independent persons dealing at arm's length and those terms and conditions result or will result in a tax benefit.

- For years of assessment commencing on or after 1 April 2012, taxpayers must determine the acceptable amount of debt from affected transactions applying arm's length principles.
- Taxpayers are required to calculate taxable income based on the arm's length terms and conditions that should have applied to the affected transaction. This means that the interest and other charges relating to the non-arm's length amount of affected transaction debt and the amount of interest which is nonarm's length must be disallowed as deductions in computing taxable income.
- In addition to a disallowed deduction for the interest and other charges, the amount of the disallowed deduction will in certain cases be deemed to be a dividend which is subject to dividends tax or a donation subject to donations tax.
- Taxpayers must be able to substantiate their view of the extent to which the relevant party debt is considered to be arm's length and accordingly must retain appropriate documentation.
- The transfer pricing provisions have been relaxed in relation to certain transactions involving financial assistance and headquarter companies, with a corresponding limitation on the amount of the related interest deductions.
- South Africa does not currently have advance pricing agreements.
- Section 31 applies prior to considering the impact, if any, of section 23M and section 23N.
- Section 31(2), if applicable, does not deem the underlying transaction to have been conducted at an adjusted amount for purposes of the Act as a whole and accordingly any 'adjustment' to taxable income or tax payable

under section 31(2) will not impact on the calculation of withholding tax on interest under Part IVB of Chapter II of the Act.

6.2. Employees' tax: Personal service providers and labour brokers – No. 35 (Issue 5)

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

Previously, it was a popular tax-saving method for employees to offer their services to their employers through the medium of private companies, close corporations or trusts, or by utilising labour brokers, none of which could be classified as 'employees' as defined in paragraph 1.

The use of labels such as 'independent contractor' and 'service company', and the perception that these were acceptable means of avoiding the deduction of employees' tax, necessitated the development of stronger anti-avoidance measures for employees' tax purposes. In order to discourage the use of corporate entities, trusts or labour brokers as intermediaries to provide personal services to a client that are, in essence, services provided under a contract of employment, the concepts of 'personal service provider' and 'labour broker' were included in the definitions in paragraph 1.

Both were also included as employees in the definition of 'employee' in paragraph 1.

This required that the remuneration paid or payable to such personal service provider or labour broker to be subject to the deduction or withholding of employees' tax.

Deductions applicable to personal service providers and labour brokers without a certificate of exemption were simultaneously narrowed.

Over the years, various amendments have refined the scope of these provisions.

This Note includes the latest amendments and amendments to the relevant rates of tax attributable to personal service providers and labour brokers.

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

Not all companies are affected by the legislation relating to a personal service provider. Only companies that fall within the definition of a ‘personal service provider’ are affected by the definition, and also only when those that fall within the definition are in receipt of ‘remuneration’ as defined. It is recommended that all users of services (employer or client) from potential labour brokers and personal service providers should have policies and systems in place to correctly identify and withhold employees’ tax from these entities and individuals.

A possible solution would be a questionnaire or an affidavit (including an affidavit or solemn declaration for a personal service provider indicating that not more than 80% of its income is derived or is likely to be derived from one client) that could be used by the service-user at the start of the engagement or contract and regularly thereafter. This will enable the client to determine whether employees’ tax should be deducted or not.

7. BINDING PRIVATE RULINGS

7.1. BPR 388 – Application of the de-grouping rule following previous intra-group transactions under section 45

This ruling determines the tax consequences for the Applicants following the proposed distribution by a holding company of shares in an intermediate holding company to its shareholders in terms of the de-grouping rules in section 45(4).

In this ruling references to sections are to sections of the Income Tax Act applicable as at 13 December 2022. Unless the context indicates otherwise any word or expression in this ruling bears the meaning ascribed to it in the Act.

This is a ruling on the interpretation and application of:

- section 1(1), – definitions of 'group of companies', 'controlling group company', and 'controlled group company';
- section 9D(1), – definition of 'controlled foreign company';
- section 41(1), – definition of 'group of companies';
- section 45(1) – paragraphs (a) and (b) of the definition of 'intra-group transaction'; and
- section 45(4)(a), (b) and (bA).

<u>Parties</u>

The Applicant: A resident company

Holdco 1: A resident company and a wholly owned subsidiary of the Applicant

Holdco 2: A resident company and a wholly owned subsidiary of Holdco 1

Company A: A resident company, held more than 70% by Company B, with the remainder of the shares held by a minority shareholder

Foreign Holdco: A non-resident company that is a wholly owned subsidiary of Company B

Foreign Opco 1: A non-resident company that is a wholly owned subsidiary of Foreign Holdco

Company B: A resident company that is a 100% subsidiary of Holdco 2

Company C: A wholly owned resident subsidiary of Company A

Holdco 3: A resident intermediate holding company and wholly owned subsidiary of Company A

Foreign Opco 2: A non-resident company that is a wholly owned subsidiary of

Foreign Holdco

Foreign Opco 3: A non-resident company that is a wholly owned subsidiary of Foreign Holdco

S.45 Entities: Company C and five other companies, all South African resident companies controlled by Company A

Description of the proposed transaction

The Applicant received an offer from a purchaser to acquire the entire issued share capital of the Applicant. In preparation for the sale to this purchaser, the Applicant will undertake an internal restructuring as set out below, to be followed by the sale.

As the last step of the internal restructuring, the Applicant intends to distribute all the shares in Holdco 1 to its shareholders (the Distribution).

Historic intra-group transactions:

During the six years before the Distribution, there were several intra-group transactions implemented under section 45 (Intra-group Transactions) that are relevant. The following list summarises these Intra-group transactions:

- Item 1: Company A transferred 100% of Foreign Opco 1 to Foreign Holdco five years before the Distribution.
- Item 2: Company C transferred 10% of the issued share capital of a nonresident company (the Minority Interest) to Foreign Holdco three years before the Distribution.
- Item 3: Holdco 3 transferred 100% of Foreign Opco 2 to Foreign Holdco four years before the Distribution.
- Item 4: Holdco 3 transferred 99.9% of Foreign Opco 3 to Foreign Holdco three years before the Distribution.
- Item 5: The S.45 Entities transferred business assets, other than equity shares, amongst one another within six years before the Distribution.

Items 1 to 4 involved Intra-group Transactions in respect of shares held in foreign companies by the relevant transferors to Foreign Holdco. All the transferors were South African tax resident companies. These transactions all qualified as 'intragroup transactions' under paragraph (b) of the definition of that term in section 45(1).

Item 5 involved various Intra-group Transactions in respect of the group's business assets amongst the S.45 Entities. These transactions qualified as 'intra-group transactions' under paragraph (a) of the same definition.

For purposes of the proposed Distribution, the past Intra-group Transactions listed above require further consideration, considering the effect of some of the steps forming part of the internal restructuring.

It is important to note that the above structure came about as a result of previous restructurings. At the time of the Item 1 Intra-Group Transaction, the only controlling group company in relation to the transferor was Company B. Holdco 1, Holdco 2 and the Applicant were not yet controlling group companies. In relation to the IntraGroup Transactions that comprise Item 5 and at the time of those transactions, only Company A and Company B were controlling group companies in relation to the transferors in those Intra-group Transactions.

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

- Step 1: Foreign Holdco will distribute the shares in Foreign Opco 1 to Company B.
- Step 2: Company A will consolidate Holdco 3 and the S.45 Entities under Company C.
- Step 3: Company A will distribute the shares in Company C to Company B and the minority shareholder.
- Step 4: Company B will distribute the shares in Foreign Holdco and Company C to Holdco 2, which will distribute them to Holdco 1, which will distribute them to the Applicant.
- Step 5: The Applicant will distribute the shares in Holdco 1 to its

shareholders.

Conditions and assumptions

This binding private ruling is subject to the additional condition and assumption that at all relevant times the assets that were subject to relief under section 45 under Items 1 to 5 are held on capital account by their various holders.

Ruling

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

In respect of Item 1

- Section 45(4)(b) will not apply because the Intra-group Transaction in Item 1 occurred under paragraph (b) of the definition of 'intra-group transaction' and consequently section 45(4)(bA) is relevant.
- Section 45(4)(bA) will not apply in consequence of the Distribution, on the basis that:
  - under section 45(4)(a)(ii), Company B is considered to be the transferee company as contemplated in paragraph (b) of the definition of 'intra-group transaction'; and
  - Company B will not cease to form part of the group of companies in relation to the transferor (Company A) or a controlling group company (Company B) in relation to the transferor when the shares in Holdco 1 are distributed by the Applicant.

In respect of Items 2, 3 and 4:

- Section 45(4)(b) will not find application upon the Distribution as all the Intragroup Transactions comprising Items 2, 3 and 4, were transactions contemplated in paragraph (b) of the definition of 'intra-group transaction' in section 45(1).
- Section 45(4)(bA) will find application upon the Distribution by the Applicant on the basis that this distribution results in Foreign Holdco (section 45 transferee) exiting the groups of companies of which Company A, Company

B, Holdco 2 and Holdco 1 were controlling group companies. This de-grouping will trigger the de-grouping charge for Foreign Holdco for purposes of section 9D. Consequent upon the de-grouping, the base cost of the Minority Interest, the shares in Foreign Opco 2 and Foreign Opco 3 must be increased by a proportionate allocation of the de-grouping charge paid by Foreign Holdco.

In respect of Item 5:

- Section 45(4)(b) will apply upon the Distribution on the basis that this distribution results in Company C and the S.45 Entities that are section 45 transferees exiting the groups of companies of which Company A, Company B, Holdco 2 and Holdco 1 were controlling group companies. Consequent upon the de-grouping, the base cost of the relevant section 45 assets must be increased by a proportionate allocation of the de-grouping charge paid.
- Section 45(4)(bA) will not find application upon the Distribution, on the basis that none of the transferee companies are companies as contemplated in paragraph (b) of the definition of 'intra-group transaction' in section 45(1)

8. BINDING GENERAL RULING

8.1. Further particulars prescribed by SARS under section 20(8A)(c) (VAT) – No. 63

For the purposes of this ruling:

- 'debtor' means a lessee or purchaser of goods under an ICA;
- 'creditor' means a lessor or seller of goods under an ICA that is a registered vendor;
- 'ICA' means an 'instalment credit agreement' as defined under section 1(1);
- 'NC Act' means the National Credit Act 34 of 2005;

- 'section' means a section of the VAT Act;
- 'VAT' means value-added tax;
- 'VAT Act' means the Value-Added Tax Act 89 of 1991; and
- any other word or expression bears the meaning ascribed to it in the VAT Act.

Purpose

This BGR sets out the further particulars prescribed by SARS under section 20(8A)(c) that the creditor must obtain to deduct input tax in instances in which a debtor makes a deemed supply to the creditor (not being a taxable supply) of goods repossessed or surrendered under section 8(10).

Background

Section 8(10) deems a repossession or surrender of goods that were initially supplied by a creditor to a debtor under an ICA, to be a supply by the debtor to the creditor at the time prescribed under section 9(8) 1 and for a consideration in money as set out under section 10(16).

In the event that the repossessed or surrendered goods were not used by the debtor in the course or furtherance of an enterprise before such repossession or surrender of such goods, or the debtor is not a vendor, the creditor is entitled to a 'notional input tax' deduction under section 16(3)(a)(i) or (b)(iii),respectively,read with paragraph (c) of the definition of 'input tax' in section 1(1).The purpose of this deduction is to enable the creditor to recoup some of the output tax declared at the time the goods were initially supplied under the ICA and is subject to compliance with the documentary requirements under section 16(2)(c).

Discussion

Section 16(2)(c) provides that the creditor may not make the abovementioned input tax deduction unless certain records are maintained by that creditor as required under section 20(8A).

Section 20(8A) requires the creditor to maintain sufficient records to enable the following particulars to be ascertained where a deemed supply (not being a taxable supply) is made to the creditor by the debtor under section 8(10):

- The particulars prescribed under section 20(8A)(a) and (b).
- Any further particulars in the form and manner to be prescribed by SARS under section 20(8A)(c).

The creditor must maintain and retain the relevant records in accordance with section 55, read with Part A of Chapter 4 of the Tax Administration Act 28 of 2011.

<u>Ruling</u>

Particulars relating to the debtor and the cash value

The following further particulars prescribed by SARS under section 20(8A)(c) apply to instances in which a debtor is deemed to make a supply to a creditor in the case of a surrender or repossession of goods, and are as follows:

Debtoris not a vendor

- Proof that, at the time that the repossession or surrender takes place, the debtor is not a vendor. This confirmation can be contained in any written correspondence obtained during the repossession or surrender process; or
- Written confirmation from the debtor that the debtor is not a registered vendor at the time of entering into the ICA as contained in either the debtor's application, the ICA agreement or any other correspondence; and
- Written communication from the creditor informing the debtor of the latter's obligation to disclose any change of that debtor's VAT registration status. This must be contained in the debtor's application, the ICA or any other correspondence.

Debtoris a vendor

- Proof that, at the time of repossession or surrender, the debtor is a vendor that used the goods other than for purposes of making taxable supplies. This confirmation can be obtained in any written correspondence obtained during the repossession or surrender process; or

- Written confirmation that the debtor (being a vendor) acquired the goods other than for purposes of making taxable supplies, at the time of entering into the ICA, as contained in either the debtor's application, the ICA or any other correspondence; and

- Written communication from the creditor informing the debtor of the latter's obligation to disclose to the creditor if the goods are subsequently applied for the purposes of making taxable supplies. This must be contained in the debtor's application, the ICA or any other correspondence.

Outstanding cash value

Proof of the outstanding 'cash value' 3 amount deemed under section 10(16) to be the consideration for the supply made under section 8(10) at the time of supply under section 9(8). The outstanding cash value must be contained in a system generated statement setting out the 'cash value' at the time of the supply, being:

- the day on which the goods are repossessed or surrendered; or

- in the case that the debtor's rights and obligations under the ICA may be reinstated under any law, the day following the last day of any period during which the debtor may be legally reinstated.

Surrender

In the case of a surrender, the following particulars are required, in addition to those in above:

- A copy of the written notice to terminate the agreement required to be issued by the debtor to the creditor under section 127(1)(a) of the NC Act or any other applicable statute; or
- The relevant terms and conditions as agreed upon in the ICA.

Repossession

In the case of a repossession, the following particulars are required, in addition to those above:

- A copy of the written notice required to be issued by the creditor to the debtor under sections 86(10) or 129(1)(a) of the NC Act, or any other applicable statute, or the relevant terms and conditions as agreed upon in the ICA, and
- A copy of the relevant court order for the attachment of the goods.

8.2. Electronic Services: Specific requirements relating to credit and debit notes, exchange rates, and advertised or quoted prices (VAT) – No. 18 (Issue 3)

For the purposes of this ruling :

- ‘electronic services recipient’ means a recipient of electronic services supplied by an electronic services supplier;
- ‘electronic services supplier’ means a vendor supplying electronic services ontemplated in paragraph (b)(vi) of the definition of ‘enterprise’ in section 1(1);
- ‘VAT Notice’ means Public Notice 1594 published in Government Gazette 45624 on 10 December 2021; and

- any other word or expression bears the meaning ascribed to it in the VAT Act.

Purpose

This BGR sets out the:

- minimum information that must be contained on a credit or debit note in order to satisfy the requirements of section 21(5);
- exchange rate that must be applied in order to determine the amount of the VAT charged in the currency of South Africa; and
- manner in which prices must be advertised or quoted,

for the supply of electronic services by an electronic services supplier.

Specific requirements relating to credit and debit notes, exchange rates, and advertised or quoted prices

Credit and debit notes

Under section 20(5B), an electronic services supplier is required to issue a tax invoice for the supply of electronic services that contains, as a minimum, the particulars as set out in the VAT Notice.

Currently, the VAT Act does not contain a provision similar to section 20(5B) dealing with the particulars that must be contained on a credit or debit note in instances in which an electronic services supplier:

- has issued a tax invoice complying with the requirements of the VAT Notice; and
- is subsequently required to issue a credit or debit note.

In these circumstances, an electronic services provider will have to issue a credit or debit note under section 21(3), but may not be able to issue a full credit or debit note with all the particulars required under section 21(3).

Under section 21(5), SARS may direct that any one or more of the particulars required under section 21(3) shall not be contained on a credit or debit note.

SARS must, however, be satisfied that there are or will be sufficient records available to establish the particulars of any supply or categories of supplies made by an electronic services supplier and that it would be impractical to require that a full credit or debit note be issued under section 21(3).

Exchange rates

Under section 20(5B), the VAT Notice deals only with tax invoices issued by electronic services suppliers and the details that must be contained on tax invoices issued.

Electronic services suppliers do not have guidance with regards to the exchange rate that must be applied in order to determine the amount of VAT charged in the currency of South Africa in instances in which electronic services suppliers issue a credit or debit note, and the VAT charged is not in currency of South Africa.

Advertised or quoted prices

Section 65 requires prices advertised or quoted by electronic services suppliers in respect of a taxable supply of electronic services to include VAT and the electronic services supplier must state in its advertisement or quote that the price is inclusive of VAT.

However, under proviso (iii) to section 65, SARS has a discretion to approve another method of displaying prices of electronic services by electronic services suppliers.

Ruling

Credit and debit notes

Subject to an electronic services supplier obtaining and retaining sufficient records to establish the particulars of the supply or categories of supplies, SARS is satisfied that it would be impractical to require an electronic services supplier to issue a full credit or debit note containing all the particulars required under section 21(3).

An electronic services supplier that:

- has issued a tax invoice as contemplated in the VAT Notice; and
- is subsequently required to issue a credit or debit note as required by section 21(3), but is unable to do so;

must issue a credit or debit note containing, as a minimum, the following particulars:

- The name and VAT registration number of the electronic services supplier.
- The name and address1 of the electronic services recipient.
- The date of issue.
- A brief explanation of the circumstances giving rise to the issuing of the credit or debit note.
- The increased or decreased consideration together with the increased or decreased amount of tax, as the case may be. In instances in which the consideration is reflected in the currency of:
    - South Africa, the increased or decreased amount of the VAT or a statement that the consideration includes the increased or decreased amount of VAT and the rate at which the VAT was charged; or
    - any country other than South Africa, the increased or decreased amount of tax in the currency of South Africa or a separate document issued by the electronic services supplier to the electronic services recipient reflecting the increased or decreased amount of tax in the currency of South Africa.

- The exchange rate used, being the exchange rate used in the tax invoice issued as contemplated in the VAT Notice.

The credit or debit note containing the aforementioned information satisfies the requirements of section 16(2)(b)(ii) for purposes of deducting input tax.

Exchange rates

An electronic services supplier that issues a credit or debit note reflecting the consideration in money in the currency of any country other than South Africa must convert the tax charged to the currency of South Africa. The exchange rate that must be applied is the rate as published by either one of the following three sources:

- The South African Reserve Bank (www.resbank.co.za);
- Bloomberg (www.bloomberg.com);or
- The European Central Bank (www.ecb.europa.eu).

One of the following three options must be used to determine the applicable exchange rate:

- Daily exchange rate on the date that the time of supply occurs;
- Daily exchange rate on the last day of the month preceding the time of supply; or
- Monthly average rate for the month preceding the month during which the time of supply occurs.

Advertised or quoted prices

SARS directs under proviso (iii) to section 65 that an electronic services supplier may advertise or quote the price of its electronic services exclusive of VAT on condition that it has a statement on its website indicating that VAT will be levied on supplies of electronic services to electronic services recipients.

9. GUIDES

9.1. Customs Duty and Value-Added Tax treatment of goods forward free as a donation

This guide enhances the understanding of the payment of the customs duty and VAT treatment of goods forwarded free as a donation.

Many organisations are increasingly dependent on donor assistance from abroad for the upliftment of indigent people. However, import VAT and customs duty may be leviable on goods that are imported into South Africa. The VAT Act and Schedule 4 of the Customs and Excise Act provide for an exemption of VAT and a rebate of customs duty on goods forwarded free as donation to certain organisations in South Africa subject to certain conditions.

Section 7(1)(b) of the VAT Act imposes VAT on the importation of any goods into South Africa by any person. Section 13 of the VAT Act provides for the collection of VAT on importation of goods, determination of value of such goods and exemptions from VAT. Paragraph 5 of Schedule 1 to the VAT Act provides for an exemption from the payment of VAT on imported goods forwarded unsolicited and free of charge by a non-resident subject to certain conditions.

9.2. Frequently Asked Questions: Solar panel tax incentive for individuals

This note sets out the basic characteristics and requirements for the solar panel incentive announced by the Minister of Finance on 22 February 2023. This is meant to help individuals in their immediate decision making, rather than postponing any solar installation until the legislative process can be finalised.

WHAT IS THE OBJECTIVE OF THE INCENTIVE?

Government proposes this programme to encourage households to invest in clean electricity generation capacity which can supplement electricity supply. The incentive will only be available for 1 year to encourage investment as soon as possible.

WHO CAN CLAIM THE INCENTIVE?

Individuals who pay personal income tax can claim the rebate against their tax liability. This rebate is not intended for solar installations at business premises.

WHAT CAN BE CLAIMED?

Individuals will be able to claim a rebate to the value of 25% of the cost of new and unused solar photovoltaic (PV) panels, up to a maximum of R15 000 per individual.

For example, a person buys 10 solar PV panels, at a cost of R4000 per panel (so total cost of R40 000). That person would be able to claim 25% of the cost up to R15 000, so R10 000.

A different person is able to buy 20 panels at a cost of R4000 per panel (so total cost of R80 000). The calculation of 25% adds up to R20 000, but they can only claim R15 000.

WHAT ARE THE REQUIREMENTS?

- Only new and unused solar PV panels qualify, to ensure that the capacity is in addition to what the country already has in place. The panels can be installed as part of a new system, or as an extension of an existing system.
- Only solar PV panels with a minimum capacity of 275W per panel (design output) qualify for the rebate. Other components of a system – batteries, inverters, fittings or diesel generators – and installation costs do not qualify. Portable panels will also not qualify.
- Solar PV panels must be installed at a residence that is mainly used by an individual for domestic purposes. The installation will have to be proved with a certificate of compliance in terms of the Electrical Installation Regulations, 2009 to ensure safety of the installation and compliance to electric regulations.

- The solar PV panels must form part of a system that is connected to the mains distribution of the private residence.
- The rebate applies to qualifying solar PV panels that are brought into use for the first time in the period from 1 March 2023 to 29 February 2024.

HOW CAN PEOPLE CLAIM THE INCENTIVE?

Individuals will be able to claim the rebate if they have:

- A VAT invoice that indicates the cost of the solar PV panels separately from other items, along with proof of payment.
- Certificate of Compliance evidencing that the solar PV panels were brought into use for the first time in the period from 1 March 2023 to 29 February 2024.

PAYE taxpayers will be able to claim the rebate on assessment during 2023/24 filing season. Provisional taxpayers will be able to claim the rebate against provisional and final payments.

WHY ONLY SOLAR PANELS, AND NOT DIESEL GENERATORS, INVERTERS, BATTERIES AND INSTALLATION COSTS?

Diesel generators are often used as emergency back-up, but are not a sustainable solution to generate additional power. They increase demand for fuel and have negative environmental impacts. Including generators would detract from the climate objectives government is committed to, where fiscal instruments like the carbon tax play an important role.

While an inverter and batteries are required to use solar panels, inverters and batteries can be operated without solar panels – in which case they offer no additional capacity to the system. The focus on solar PV panels is to maximise the use of limited government funds to get as much additional generation capacity as possible – and recognises that government will have to focus on a partial rebate of the components that are most directly linked to generation . This is why installation costs are not included either.

WHAT ABOUT PEOPLE WHO RENT THEIR HOMES?

There is no ownership limitation for the incentive, so installations by landlords or renters would be eligible, but only the party that pays for the solar panels can claim the rebate.

WHAT ABOUT SECTIONAL TITLES / BODY CORPORATES?

If occupants are enabled to install their own panels, then the tax incentive applies as for all other individuals. A body corporate will not be able to claim this incentive. It is not clear whether many body corporates will be purchasing solar installations instead of using leasing or other options to avoid up-front costs for members. Government will be consulting on this aspect. If there is widespread interest in body corporates purchasing and installing solar panels, then payment (e.g special levies) for solar installations levied from the occupants would have to indicate the cost of the solar panels separately – as would be the case for any other claimant.

The applicable Certificate of Compliance data would also have to be shared with SARS. Because there would be some adjustments to ensure that the right people could claim the right amounts, there will be consultation to determine the required approach and documentation.

WILL I NEED TO PAY SARS BACK IF I SELL MY HOME AFTER INSTALLING SOLAR PV PANELS?

No, there will be no recoupment if you sell your house after having benefitted from this incentive as the solar panels will likely remain fixed to the house and used by the following owner – still enabling an expansion in generation. There will, however, be a claw-back of the rebate if you sell the panels themselves within one year after they were first brought into use to counter potential abuse.

WHEN WILL THIS BECOME PART OF TAX LEGISLATION?

This incentive will be included in the annual tax amendments. A draft version of the legislation will be published for public comment no later than the publication date of the 2023 Draft Taxation Laws Amendment Bill. The Minister tables tax bills during the Medium Term Budget Policy Statement (MTBPS) in October each year.

Parliament considers the amendments after which the President can assent to the amendments – usually by January of the year after the announcement.

The aim of this note and the draft legislation to follow is to provide as much upfront clarity as possible so that individuals do not feel they need to wait for the tax bills later in the year before making a decision to invest and benefit from the incentive. The guidance provided is, nevertheless, subject to the outcome of the consultative process on the proposal and Parliament's ultimate decisions on the legislation giving effect to the proposal.

10. 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.