TAX UPDATE

For period: October 2023 to December 2023

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1. FOREWORD

The purpose of this update is to summarise developments that occurred during the fourth 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!

'The income tax has created more criminals than any other single act of government.' — Sen. Barry Goldwater

'Income tax returns are the most imaginative fiction being written today.' — Author Herman Wouk

'You don't pay taxes — they take taxes.' — comedian Chris Rock

'The avoidance of taxes is the only intellectual pursuit that carries any reward.' — economist John Maynard Keynes

'It's income tax time again, Americans: time to gather up those receipts, get out those tax forms, sharpen up that pencil, and stab yourself in the aorta.' — humorist Dave Barry

‘Unquestionably, there is progress. The average American now pays out twice as much in taxes as he formerly got in wages.’ — journalist/essayist H.L. Mencken

‘The United States has a system of taxation by confession.’ — U.S. Supreme Court Justice Hugo Black

‘Death, taxes and childbirth! There’s never any convenient time for any of them.’ — author Margaret Mitchell

‘What is the difference between a taxidermist and a tax collector? The taxidermist takes only your skin.’ — author Mark Twain

‘There may be liberty and justice for all, but there are tax breaks only for some.’ — chief economist and contributing editor to Tax Analysts Martin A. Sullivan

‘A tax loophole is something that benefits the other guy. If it benefits you, it is tax reform.’ — Sen. Russell B. Long

‘Congress can raise taxes because it can persuade a sizable fraction of the populace that somebody else will pay.’ — economist Milton Friedman

‘You must pay taxes. But there’s no law that says you gotta leave a tip.’ — financial services firm Morgan Stanley

‘Why does a slight tax increase cost you two hundred dollars and a substantial tax cut save you thirty cents?’ — humorist Peg Bracken

‘When there is an income tax, the just man will pay more and the unjust less on the same amount of income.’ — Plato

‘The income tax has made more liars out of the American people than golf has.’ — humorist Will Rogers

‘The nation should have a tax system that looks like someone designed it on purpose.’ — Sen. William Simon

‘Dear IRS, I am writing to you to cancel my subscription. Please remove my name from your mailing list.’ — Snoopy (character created by Charles Schultz)

‘There’s no such thing as a good tax.’ — Winston Churchill

‘The best things in life are free, but sooner or later the government will find a way to tax them.’ — Anonymous

2. NOTICES / REGULATIONS

2.1. 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 2023	9,75%
1 March 2023	30 April 2023	10,50%
1 May 2023	30 June 2023	10,75%

1 July 2023	31 August 2023	11,25%
1 September 2023	Until change in the Public Finance Management Act rate	11,75%

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	30 April 2023	6,50%
1 May 2023	30 June 2023	6,75%
1 July 2023	31 August 2023	7,25%
1 September 2023	Until change in the Public Finance Management Act rate	7,75%

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	31 March 2023	8,25%
1 April 2023	Until change in Repo rate	8,75%

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.

2.2. Legal Counsel – Preparation of Legislation – Bills

2 November 2023 – National Legislation: The Minister of Finance introduced the following bills in the National Assembly on 1 November 2023:

- Rates and Monetary Amounts and Amendment of Revenue Laws Bill [B35—2023]
- Taxation Laws Amendment Bill [B36—2023]
- Tax Administration Laws Amendment Bill [B37—2023]

2.3. Collective engagement to implement the Crypto-Asset Reporting Framework

10 November 2023

Joint Statement by: Armenia, Australia, Austria, Barbados, Belgium, Belize, Brazil, Bulgaria, Canada, Chile, Croatia, Cyprus, Czech Republic, Denmark, Estonia, Finland, France, Germany, Greece, Hungary, Iceland, Ireland, Italy, Japan, Korea, Liechtenstein, Lithuania, Luxembourg, Malta, Mexico, Netherlands, Norway, Portugal, Romania, Singapore, Slovakia, Slovenia, South Africa, Spain, Sweden, Switzerland, the United Kingdom, and the United States of America; the Crown Dependencies of Guernsey, Jersey, and Isle of Man; and the United Kingdom's Overseas Territories of the Cayman Islands and Gibraltar.

> 'To keep pace with the rapid development and growth of the crypto-asset market and to ensure that recent gains in global tax transparency will not be gradually eroded, we welcome the new international standard on automatic

exchange of information between tax authorities developed by the OECD – the Crypto-Asset Reporting Framework (CARF). The widespread, consistent and timely implementation of the CARF will further improve our ability to ensure tax compliance and clamp down on tax evasion, which reduces public revenues and increases the burden on those who pay their taxes.

As jurisdictions that play host to active crypto markets, we therefore intend to work towards swiftly transposing the CARF into domestic law and activating exchange agreements in time for exchanges to commence by 2027, subject to national legislative procedures as applicable. In order to ensure consistency and a smooth implementation for both business and governments, those of us that are signatory jurisdictions to the Common Reporting Standard will also implement, in line with the above timeline and subject to national legislative procedures as applicable, amendments to this standard as agreed by the OECD earlier this year.

We invite other jurisdictions to join us with a view to enhancing the global system of automatic information exchange which leaves no hiding places for tax evasion.'

3. TAX CASES

3.1. CRRC E-Loco Supply (Pty) Ltd v C:SARS (85 SATC 463)[1]

CRRC E-Loco Supply (Pty) Ltd had been subjected to a tax audit conducted by a specialised unit of SARS, which concluded that there was prima facie evidence that E-Loco had overstated the price of locomotives sold to Transnet as part of what has since become known as 'State Capture.'

As a result, E-Loco had an assessed tax debt in excess of R3.6 billion, which had not been satisfied and only partial payment had been achieved by SARS, by the recovery of money via the third-party notices issued by SARS in terms of section

1 Gauteng Division, Pretoria

179 of the Tax Administration Act (TA Act) and which formed the subject matter of this application.

SARS had a statutory obligation to recover tax debts and pointed out that the fiscus had been under strain to maximise such recovery.

SARS had issued third-party notices in terms of section 179(5) of the TA Act prior to issuing a final demand for payment of the tax debt and submitted that it was entitled to do so in terms of section 179(6), which provided that SARS need not issue a final demand under subsection (5) if a senior SARS official is satisfied that to do so would prejudice the collection of the tax debt.

The decision of the relevant senior SARS official was taken on 28 June 2021 and was the culmination of a string of previous decisions, but the occurrence which prompted this decision was the conclusion of the IEU tax audit and its issuance of a Finalisation of Audit letter on 25 June 2021.

After the assessments had been made the IEU sent an internal memorandum to the head of the Criminal and Illicit Economic Activities Division, who was a senior SARS official as defined in the TA Act. The internal memorandum requested approval to issue third-party appointments in terms of section 179(6) of the TA Act, which request was granted by the senior SARS official and it was this decision which E-Loco sought to have reviewed and set aside by the High Court.

The consequences of the decision were that over R635 331 652 was paid over to SARS in accordance with the aforementioned notices.

E-Loco contended that the reasons advanced by SARS as to why the senior tax official took the decision in question by relying on section 179(6) of the TA Act did not constitute 'reasonable grounds' and that, absent such grounds, the decision was not rational and open to review before the High Court.

E-Loco also complained that the third-party notices had not been preceded by a final demand as provided for in section 179(5) of the TA Act and should be set aside.

SARS contended, inter alia, that it was dealing with a dishonest taxpayer, and relied on the prima facie evidence of large-scale corruption committed by the taxpayer in its dealings with Transnet as part of the reasons for its conclusion. In addition, SARS determined that there was prima facie evidence of tax fraud in excess of R4 billion on the part of E-Loco as a result of it substantially having understated its tax liability in its returns for the tax years from 2013 to 2018.

Furthermore, during the tax audits E-Loco had submitted incomplete ledgers for the tax years 2014-2016 and had failed to provide the necessary information requested during the audits and had reneged on commitments to furnish guarantees.

SARS' senior official was of the view that, since E-Loco was in any event not trading and, even if it had been trading, could not utilise the funds due to the preservation order, it could suffer no prejudice or hardship if the funds were paid over by the banks to third parties.

SARS also submitted that it had the duty to recover taxes and the payment of the funds to SARS by the banks would go some way towards satisfying SARS' obligation to recover taxes quickly and effectively, in this instance, from this particular taxpayer.

Judge Davis held the following:

(i) That, despite SARS' allegations of taxpayer dishonesty, tax fraud and breach of guarantee commitments, these were largely left uncontroverted by E-Loco and no bona fide disputes regarding those issues had been demonstrated and the best that E-Loco could do, faced with these serious and weighty accusations, was to have its attorney deal with them in the most cursory and generalised fashion.

(ii) That the attack on the reasonableness of SARS' decision, insofar as it was based on the report and memorandum from the IEU, in respect of the recoverability of tax by way of third-party payments only went so far as arguing that the memorandum only alleged that recovery of the tax debt would be prejudiced and not that recovery would be in jeopardy.

(iii) That SARS had concluded that there was a risk of the funds being expatriated once the block was lifted and no factual evidence had been produced by E-Loco whereby SARS' fears had been allayed. Furthermore, the risk or jeopardy of recovery of a tax debt by a delinquent taxpayer who might retreat back to China with its funds, appeared to the court to create such a reasonable fear that it justified an avoidance of that risk by having the third party's banks pay the funds over to SARS.

(iv) That E-Loco's attack on SARS' reliance on the decision in Hindry v Nedcor Bank Ltd and Another 61 SATC 163 when contending that sufficient opportunity had been furnished to E-Loco to be heard, was also misplaced. The limitation in the recovery proceedings of a right to be heard prior to the issuing of a third party notice, was a constitutionally justifiable limitation and when the taxpayer had been corresponding with SARS about the tax debt at issue, including the basis on which the claim had been arrived at, there could not be a valid complaint of unfairness and the non-application of the audi alteram partem principle and the Hindry principle had been followed in related recovery proceedings.

(iv) That there was little doubt that SARS had been entitled to issue the third party notices and thereby recover the funds in question to satisfy an existing tax debt. The fact that the tax debt may be subject to an objection did not detract from this.

(v) That, on the facts of this case, the senior SARS official in question had sufficient grounds to justify his decision to issue the notices without such demand as contemplated in section 179(6) of the TA Act.

Application dismissed with costs.

3.2. *South African Breweries (Pty) Ltd v C:SARS and another (85 SATC 495)*[2]

South African Breweries (Pty) Ltd (SAB) had imported Corona light beer (the goods) from Mexico over a period spanning six months from August 2018 to November 2019 utilising the services of Ocean Light Shipping CC (Ocean Light) as its clearing agent.

Ocean Light was a clearing agent established in terms of section 64B of the Customs and Excise Act (the C&E Act) and was part of the group of companies comprising the Second Respondent.

The goods were cleared in the port of Durban in 139 import transactions.

SAB subsequently discovered that the goods were fraudulently cleared by Ocean Light as traditional African beer which was a product attracting less or nil import duties in contrast to Corona beer which attracted import duties and Value-Added tax. As a result, import duties and VAT amounting to R139 million had not been paid over to SARS.

SARS had, through third party appointments and VAT refunds due to SAB, already recovered amounts from SAB and had issued letters of demand to SAB for a sum of R130 590 852.89.

SAB contended, inter alia, that Ocean Light was the agent of SARS, that Ocean Light was the importer in terms of section 1(f) of the C&E Act and that SARS should hold Ocean Light liable for the customs duties, because SAB had paid all amounts due to SARS, to Ocean Light.

SAB's internal administrative appeal was dismissed by SARS and SAB then applied in the High Court for the review and setting aside as against it, of each of SARS' decisions to reverse the original decisions to accept the declared duties, charges and VAT and clear the consignments of imported beer.

2 Gauteng Division, Pretoria

SAB also sought to review and set aside SARS' decision dismissing the internal administrative appeal.

The issue for determination before the court was whether SAB or Ocean Light was liable for payment of the outstanding customs duties.

It was common cause that the clearance and release of the goods as African traditional beer, instead of the correct classification of the product, had been influenced by fraud committed by SAB's clearing agent, i.e. Ocean Light.

SAB denied that its relationship with Ocean Light was a principal-agent relationship but did not deny that Ocean Light had acted as its clearing agent and as such was accredited by SARS as it had selected Ocean Light from the pool of approved agents designated by SARS.

SAB contended that the C&E Act created an agent-principal relationship between Ocean Light and SARS.

Judge Mali held the following:

As to the existence of a principal-agent relationship

(i) That in the present case it was common cause that Ocean Light did all what was provided for in sections 38 and 39 of the C&E Act in regard to the clearance of the goods and the payment of duties on behalf of SAB. The only role played by SARS in the above sections was to prescribe the method of importation and the obligations thereof. That, furthermore, the bill of entry is completed by the clearing agent, its correctness and the accompanying documents were a responsibility of the agent.

(ii) That the Controller, who is a customs officer, accepted as true what was presented by the agent. The court took judicial notice that this exercise was to be regarded as self-assessment and there was nothing in law prohibiting SAB from clearing its own consignments and, furthermore, the act of utilising the services of Ocean Light for reward by SAB created a contract of principal-agent relationship between the two.

(iii) That the terms of payment between SAB and Ocean Light clearly suggested a business relationship. Compared to SARS and Ocean Light, the business relationship between Ocean Light and SAB was more profound than the general regulatory terms between SARS and Ocean Light which were created by statute in section 64B of the C&E Act.

(iv) That in this case SAB did not argue against the actual authority it had over Ocean Light and even the conduct of the parties supported the principle of authority, whether ostensible or otherwise. Ocean Light handled huge amounts on behalf of SAB in order to pay SARS and SAB was in a position to be the first to discover the fraud committed by Ocean Light which attested to the control by SAB over Ocean Light arising out of a principal-agent relationship between the parties.

(iv) That, accordingly, applying the law to the facts, there was no other answer than to apply the business-like approach and to attribute a principal-agent relationship between SAB and Ocean Light and if that was so, as already found, SAB ought to pay the duties to SARS and not Ocean Light.

As to the review of the internal administrative appeal

(v) That SARS' reasons for imputing the tax liability on SAB were based on applicable legislation, i.e. sections 39(1)(b) and 44(6)(c) of the C&E Act which dealt with obligations and liabilities of SAB in its capacity as an importer and SAB was referred to section 99 of the C&E Act which dealt with the obligations and liabilities of Ocean Light as the clearing agent. Furthermore, section 98 dealt with the liability of SAB for any acts done by its appointed clearing agent.

(vi) That SARS did not punish SAB for Ocean Light's fraudulent activities as the tax amount which was the subject matter of the dispute was not a form of punishment but was fulfilment of a payment obligation on SAB's part.

(vii) That SAB had not proved that the relevant customs duty liability had ceased and had not objected to the unconstitutionality of section 77G of the C&E Act.

(viii) That, accordingly, SAB's request to review and set aside SARS' decision dismissing the internal administrative appeal had to fail.

As to the applicability of PAJA

(ix) That it was common cause that the clearance and release functions in respect of imported goods were performed electronically and the same happened in this case. The system was designed to accept a Single Administrative Document (SAD 500), a self-assessment form by the importer and or its agent for clearing of goods and attendant functions. SAD 500 was accompanied by documents compiled by the importer and or agent. Furthermore, in the present case SARS had accepted that there was a manual intervention which led to the clearance of the goods and what needed to be determined was whether the administrative exercise was a decision in terms of PAJA.

(x) That in this case the use of SARS systems, the actions of the customs officer and/or anyone who had a hand in the release of the goods was a clerical act and it was therefore concluded that PAJA was not applicable and the main application could not succeed.

Application dismissed with costs.

3.3. Motloung and another v C:SARS and others (85 SATC 504)[3]

SARS during January 2019 had conducted a full scope audit of the Second Applicant for VAT over the period covering March 2014 to July 2018 and Corporate Income Tax (CIT) for the 2015–2017 tax years.

Second Applicant, over the relevant period, had submitted all VAT and CIT returns to SARS as zero returns, each of the returns had indicated that the Second Applicant had generated no income and had incurred no expenses.

3 Free State Division, Bloemfontein

SARS had sent an audit finding letter to the Applicants setting out the findings of the audit and afforded the Applicants 21 days within which to supply reasons why understatement penalties should not be levied and the Applicants did not dispute SARS' calculation of tax liability.

Applicants admitted that SARS had suffered prejudice of R819 607.09 in relation to VAT and R493 600 in relation to CIT.

SARS levied 10% late payment penalties and further imposed 150% understatement penalties for intentional tax evasion on both Income Tax and VAT.

First and Second Applicants on 15 October 2020 were criminally charged for intentional tax evasion and in their trial in the Regional Court they had raised a special plea in terms of section 106(1)(c) of the Criminal Procedure Act (CPA), but it was dismissed by the court on the grounds that the relevant Committee's decision to levy understatement penalties did not constitute a conviction in terms of the CPA.

Applicants accordingly contended that the issue of whether it was permissible to impose both the understatement penalties and criminal penalties arising from the same conduct had been unsuccessfully argued in the criminal proceedings in the Regional Court.

Applicants then launched an application for a declaratory order in the High Court declaring that sections 222 and 235, read with section 223 of the Tax Administration Act were unconstitutional in that the impugned statutory provisions of the TAct A violated their rights to a fair trial in that the Applicants had already been found guilty of intentional tax evasion by SARS and a sanction had been imposed upon them in the form of understatement penalties.

The issue to be decided by the court was whether or not the impugned statutory provisions were unconstitutional and invalid.

The application was opposed by the SARS only and the Third and Fourth Respondents abided the decision of the court.

First and Second Respondents raised issue estoppel and contended that the permissibility of imposing understatement penalties and criminal penalties arising from the same conduct had been unsuccessfully argued in the criminal proceedings in the Regional Court and the Applicants should have appealed the Regional Court's dismissal of the special plea.

Applicants contended that the understatement penalty was a criminal punishment and hence the Tax Administration Act had distinguished it from the other administrative penalties defined in section 208 of the Act.

Applicants contended further that the administrative penalties were automated and mechanical in nature, unlike the understatement penalties which required that an enquiry be held before they had been levied and in their view the process followed in levying understatement penalties was the same as the process in the criminal court.

Held by Judge Mbhele

(i) That Double Jeopardy was a universally recognised principle in many legal systems across the world and this principle stemmed from the rule that no one may be punished for the same offence twice. The rule prevented repeated prosecutions for the same offence and it was introduced into our legal system through common law and gained statutory recognition in section 106(1)(c) of the CPA. The rule was endorsed in section 35(3)(m) of the Constitution of South Africa, 1996 as a fundamental right of the accused to a fair trial.

(ii) That the Applicants, relying on United States v Halper 490 US 1989 para [11] at 441–2, submitted that under the double jeopardy defence, a person who has already been punished in a criminal prosecution may not be subjected to an additional civil remedy based upon the same conduct where the civil remedy constituted punishment. Halper was overturned by Hudson v United States 522 US 93(1997) where the court held that the double jeopardy clause was not a bar to criminal prosecution because the administrative proceedings were not criminal in nature.

(iii) That the court referred to and discussed the decisions in Federal Mogul Aftermarket Southern Africa (Pty) Ltd v Competition Commission and Another 2005 (6) BCLR 613 (CAC) and Pather and Another v Financial Services Board and Others 2018 (1) SA 161 (SCA) and stated that the above authorities demonstrated that nothing precluded civil administrative proceedings and criminal proceedings from the single act. Administrative penalties and criminal proceedings did not serve the same purpose. The one is aimed at strengthening internal controls of the administrative authority and to promote compliance while the other was aimed at correcting a behaviour that caused harm to the society.

(iv) That section 222 of the TA Act prescribed that taxpayers were liable not only for the shortfall or unpaid tax for the relevant period, but, in addition to the tax payable, for an understatement penalty. Section 222 addressed the damage and shortfall flowing from an understatement. It further deterred non-compliance with tax administration laws. Section 235 criminalised an intentional evasion of tax and obtaining undue refunds by fraud or theft which did not arise in section 222. Section 235 dealt with the criminal state of mind of the taxpayer at the time of an understatement.

(iv) That an understatement is described as prejudice suffered by SARS or the fiscus as a result of impermissible conduct by a taxpayer. Prejudice is defined as harm or injury resulting from some action. The main purpose of penalty is to deter impermissible conduct that results in violation of the TA Act and to enforce compliance with the provisions thereof. It followed that the understatement penalty regime like many penalties imposed by other administrative bodies was not aimed at punishing criminal conduct but served as a regulatory function aimed at assisting SARS to meet its obligations as prescribed by the enabling legislation.

(v) That the burden of proof differed between the process of arriving at a punishment in a criminal case and a penalty imposed by an administrative body. In Pather, supra, the court held that the fact that the penalty was intended to have a deterrent effect did not mean that it was not

administrative in nature. The court found that to hold that the mere presence of a deterrent purpose rendered such sanctions 'criminal' for double jeopardy purposes would severely undermine the government's ability to effectively regulate institutions.

(vi) That section 35(3)(m) of the Constitution protects an accused's right to a fair trial and the section is available to people who have been charged with crime. It is aimed at protecting the rights of the arrested, detained and accused persons as stipulated in its heading. It was clear that the purpose of section 35(3)(m) was to protect the accused persons' rights to freedom and it mitigated against the risk of loss of liberty emanating from repeated charges for the same act. That a single act may give rise to more than one consequence is not tantamount to double jeopardy.

(vii) That taxation was one of the mechanisms through which the government sought to meet some of its objectives and the ability of the government to budget and live up to its responsibility of providing basic services to the people was dependent on the ability of SARS to enforce applicable tax laws. It would be wrong to force SARS to stick to only one legal process to enforce tax laws and SARS has a duty to maintain effective tax administration as a means to strengthen the relationship between citizens and the government.

(viii) That, having found that calling the taxpayer to account for the wrongdoing before an administrative body as well as the criminal were two distinct processes, the court was of the view that double jeopardy did not arise in the circumstances of this matter and it was unable to find that sections 222 and 235 of the TA Act offended the provisions of s 35(3)(m) of the Constitution.

Application to declare sections 222 and 235 of the Tax Administration Act unconstitutional was dismissed with costs.

3.4. C:SARS v Rappa Resources (Pty) Ltd (85 SATC 517)

SARS had, on 29 March 2021, issued assessments to Rappa Resources (Pty) Ltd (Rappa) for the payment of VAT, penalties and interest.

Rappa was advised that should it wish to lodge an objection against the assessments, the objection must comply with all of the requirements of section 104 of the Tax Administration Act (TA Act).

Rappa chose instead to launch an urgent application out of the Gauteng Division of the High Court on 28 April 2021 for an order in the following terms: (1) Reviewing and setting aside the decision of SARS to issue the assessments ('the decision'); (2) Reviewing and setting aside the assessments; (3) Declaring the decision of SARS to issue the assessments to be in conflict with the constitutional principle of legality and accordingly unconstitutional, unlawful and invalid.

Rappa also demanded that SARS disclose the record of its decision under review in terms of Uniform Rule 53(1)(*b*).

When SARS refused to so disclose, Rappa launched an application on 3 June 2021 in terms of Uniform Rule 30A for an order compelling SARS to do so (the compelling application).

SARS, in answer to both applications, denied that Rappa's application for review was competent because it had not been sanctioned by the High Court in terms of section 105 of the TA Act.

Section 105 provided that 'A taxpayer may only dispute an assessment or 'decision' as described in section 104 in proceedings under this Chapter, unless a High Court otherwise directs.'

Rappa did not in either application seek an order in terms of section 105 as it initially took the view that 'section 105 of the of the TA Act does not stand in the way of the review application.'

Rappa later asserted in its replying affidavit filed in the compelling application that the section, in any event, allowed the High Court to direct otherwise. Thereafter, in terms of an amendment to its notice of motion in the compelling application filed on

22 June 2021, Rappa sought an order in terms of section 105 'insofar as it might be necessary.'

After the compelling application came before the High Court, Rappa did not press for an order under section 105 because, so it was contended, such an order was not necessary.

The High Court postponed *sine die* the relief sought pertaining to the applicability of section 105 of the TA Act and it directed that that issue be enrolled for hearing together with the main review application.

The High Court nonetheless directed SARS to comply with Uniform Rule 53(1)(*b*) by despatching to the Registrar and Rappa, a complete record containing all documents and all electronic records relating to the decision which was the subject of the review application within 15 days of granting of this order.

The High Court granted SARS leave to appeal to the Supreme Court of Appeal on 8 November 2021 and in so doing it observed that central to this application was SARS' contention that Rappa's right to review only vested once a directive was issued in terms of section 105 of the TA Act and that the High Court had no jurisdiction to order the production of the record, in the absence of making a determination on whether the High Court had jurisdiction to consider the appeal. Moreover, SARS' sole basis for opposition to the Rule 30A application was that Rappa had no right to see the record absent a directive in terms of section 105 of the TA Act, which directive it contended should be refused.

The broad thrust of e case was: First, the High Court did not have the power to order the production of the record of a decision under review unless it had jurisdiction in the review and it had accordingly to first determine its jurisdiction in the review before making a compelling order. Second, and this was linked to the first, in terms of section 105, a taxpayer may only dispute an assessment by objection and appeal in terms of sections 104 to 107 of the TA Act, unless the High Court directed otherwise and before it made such a direction, the High Court had no jurisdiction in the review and could accordingly not make an order compelling SARS to deliver the record of its decision.

Judge Ponnan held the following:

(i) That, preliminarily, as the High Court had correctly observed in the judgment on the application for leave to appeal, the Constitutional Court had indeed held in *Competition Commission of South Africa* v *Standard Bank of South Africa* 2020 (4) BCLR 429 (CC) that an order compelling a respondent in a review to deliver the record of its decision in terms of Rule 53 was appealable and, accordingly, the High Court's order compelling SARS to deliver the record of its decision was appealable on the authority of the Constitutional Court.

(ii) That both the majority and minority of the Constitutional Court had held in *Standard Bank*, *supra*, that the court may only order the production of the record of a decision under Rule 53 after it had determined that it had jurisdiction in the review.

(iii) That Rappa had contended that it may circumvent the appeal procedure under the TA Act by taking the assessments on review to the High Court because its attack was directed at the legality of the assessments on grounds of review and not on their merit. But, as the court would endeavour to show, that was no reason, without more, to simply circumvent the appeal procedure, which involved a complete reconsideration of the assessments. This was apparent from the language of the provisions of the TA Act applicable to tax appeals.

(iv) That, firstly, section 104(1) provided that a taxpayer 'who is aggrieved by an assessment' may object to it. The language was clearly very wide. The taxpayer may object on the ground of any grievance of whatever kind. Secondly, SARS may allow or disallow the objection under section 106(2). If SARS disallowed the objection, the taxpayer may appeal against the assessment or decision to the Tax Board or Tax Court under section 107(1). Section 107(1) did not in any way limit the grounds upon which the taxpayer may do so. Thirdly, the Tax Court determined the appeal in terms of section 117(1). It had jurisdiction to determine all the issues raised in such an appeal. The Tax Court determined 'the matter', that is, the entire

appeal, in terms of section 129(1). It may, in terms of section 129(1), confirm the assessment; order the assessment to be altered; refer the assessment back to SARS or 'make an appropriate order in a procedural matter.'

(iv) That importantly, in this regard, a tax appeal was an appeal in the widest sense of the word, namely a complete rehearing of the matter. It has been described as a 'revision' and not an appeal in the ordinary sense.

(v) That this wide power of revision of the Tax Court included the power to determine the legality of an assessment on grounds of review. In *KBI* v *Transvaalse Suikerkorporasie Bpk* 47 SATC 34, which concerned an appeal to a Full Court of the then Transvaal Provincial Division against a judgment of the Special Tax Court that had upheld a taxpayer's appeal against an additional income tax assessment, SARS contended that it was not competent for a taxpayer to invoke grounds of review in a tax appeal. The Full Court had rejected SARS' argument and it held that, save in respect of decisions in relation to which a right of appeal was expressly excluded by the tax legislation, the Tax Court was empowered to take into consideration whether or not SARS had properly exercised its discretion in respect of the making of the assessments that were subject to appeal. In that context, so the court held, where the exercise of a discretion is pertinent to the making of the impugned assessment, the 'appeal' is in reality a 'review' of the decision on customary review grounds.

(vi) That *Transvaalse Suikerkorporasie*, *supra*, was followed by a Full Court of the Western Cape High Court in *South Atlantic Jazz Festival (Pty) Ltd* v *C:SARS* 77 SATC 254 where the reasoning in *Transvaalse Suikerkorporasie* was described as 'compelling' and 'conceptually consistent in all material respects' with an earlier judgment of Van Winsen J in *ITC 936* (1962) 24 SATC 361. Thereafter *Wingate-Pearse* v *C:SARS and Others* 82 SATC 21 followed and applied *South Atlantic Jazz Festival*, *supra*.

(vii) That the TA Act did not disqualify the High Court from determining tax disputes. It may, subject to section 105, determine any legal issues arising from tax disputes including reviews of assessments or other decisions. The Constitutional Court noted in *Metcash Trading Ltd* v *C:SARS* 63 SATC 13 that 'it had for many years been settled law that the Supreme Court had jurisdiction to hear and determine income tax cases turning on legal issues.' The court in *United Manganese of Kalahari (Pty) Ltd* v *C:SARS* 80 SATC 192 cited *Metcash*, *supra*, and confirmed that it was settled law that a decision of SARS was subject to judicial intervention in certain circumstances. One such circumstance was that the High Court had jurisdiction to hear and determine tax cases turning on legal issues.

(ix) That section 105 was an innovation introduced by the TA Act from 1 October 2011. It had moreover been narrowed down by an amendment made in 2015. Its purpose was to make clear that the default rule was that a taxpayer may only dispute an assessment by the objection and appeal procedure under the TA Act and may not resort to the High Court unless permitted to do so by order of that court. The High Court will only permit such a deviation in exceptional circumstances. This much was clear from the language, context, history and purpose of the section. Thus, a taxpayer may only dispute an assessment by the objection and appeal procedure under the TA Act, unless a High Court directs otherwise. The same understanding was articulated in *ABSA Bank* v *C:SARS* 83 SATC 401 where it was common cause that such appropriate circumstances should be labelled 'exceptional circumstances' and the court would require justification to depart from the usual procedure, and this, by definition, would be 'exceptional.'

(x) That the purpose of section 105 was clearly to ensure that, in the ordinary course, tax disputes are taken to the Tax Court. The High Court consequently does not have jurisdiction in tax disputes unless it directs otherwise.

(xi) That it was not strictly necessary to enter into the debate as to whether, in this case, a departure from section 105 might be justified. The High Court did not make an order under section 105 and Rappa had not cross-appealed its decision in that regard. The important point, for present purposes, was that not having made such an order, the court accordingly did not have jurisdiction in the review application and because it did not have jurisdiction in the review, it also did not have the power to issue the compelling order which was incidental to the review.

(xii) That it was open to Rappa to make out a proper case on the papers that the dispute raised was such as to warrant the High Court issuing the necessary direction in the exercise of its discretion under section 105. On this score it self-evidently chose not to make out such a case – a choice that was not without its consequence. Even as late as the appeal, Rappa continued to vacillate between: on the one hand, asserting that because of the nature of the issues raised, it was not necessary to obtain a direction in terms of section 105; and, on the other, to the extent necessary, it was entitled to such an order. An order under section 105 was not simply to be had for the asking. A case had to be made out for the High Court to authorise a departure from the default rule in the proper exercise of its discretion on a *conspectus* of all of the facts before it. Whether a direction under section 105 should issue remains a decision for the High Court.

(xiii) That a court must have jurisdiction for its judgment or order to be valid. The High Court appeared to have lost from sight that the time for determining whether a court had jurisdiction was at the commencement of the proceeding. Having postponed that question, the High Court was not empowered to issue the orders that it did. Those orders, including paragraph 1, amending the notice of motion, and paragraph 2, postponing *sine die* whether a directive under section 105 of the TA Act should issue, were nullities.

(xiv) That in granting prayers 1 and 2, the High Court, no doubt, inclined to the view that relief under section 105 was necessary. It was thus mutually

incompatible for it to have formed that view and, at the same time, deferred a decision on that question to the court hearing the review application and, what was more, in the meanwhile, to have exercised coercive powers to compel production on possible pain of contempt.

Appeal upheld with costs.

3.5. United Manganese of Kalahari (Pty) Ltd v C:SARS (85 SATC 529)

SARS had, on 24 March 2017, issued a letter to United Manganese of Kalahari (Pty) Ltd (UMK), indicating that an audit would be conducted in respect of the 2011, 2012 and 2013 years of assessment.

SARS, following several requests for information from UMK, as well as witness interviews, issued a letter of audit findings in terms of section 42(2)(*b*) of the Tax Administration Act (TA Act) setting out the outcome of the audit and the grounds of SARS' proposed additional assessments.

UMK was afforded 21 business days in terms of section 42(3) of the TA Act within which to respond in writing to the facts and conclusions set out in the letter of audit findings.

UMK and SARS thereafter agreed that considering, *inter alia*, the complexities of the audit, the 21-day period would be extended to 30 August 2019.

UMK, in the interim, had directed a letter to SARS on 16 July 2019 requesting clarity regarding certain of the allegations and findings in the letter of audit findings, to which UMK replied on 30 July 2019.

UMK, on 30 August 2019, responded to the facts and conclusions set out in the letter of audit findings as supplemented by SARS' reply.

The finalisation of the audit letter was subsequently issued by SARS five months later on 31 January 2020 and was accompanied by the additional assessments. Pursuant to the finalisation of the audit, SARS made adjustments to UMK's taxable

income and levied tax and interest in respect of the relevant income tax years of assessment.

By virtue of the provisions of section 31(2) of the Income Tax Act (IT Act) SARS further issued an assessment for dividend withholding tax in respect of the deemed *in specie* dividend arising from the adjustment made to UMK's 2013 income tax year of assessment.

The additional assessments (in the amount of R351 034 504.47 in total) provided that payment by UMK to SARS was due by 29 February 2020. This excluded interest levied on the dividend tax assessment, which SARS intended to levy with effect from 1 July 2015.

On 17 February 2020 notice was given on behalf of UMK as required in terms of section 11(4) of the TA Act of its intention to institute legal proceedings against SARS in the Gauteng Division of the High Court, Pretoria for a review of the additional assessments raised by SARS in respect of UMK's 2011, 2012 and 2013 years of assessment instead of exercising its right of appeal in the Tax Court.

In the application in the High Court that followed, UMK sought an order reviewing and setting aside the aforementioned additional assessments and requested that UMK be exempted from any obligation to exhaust any internal remedies in terms of section 7(2) of the Promotion of Administrative Justice Act and, in terms of section 105 of the TA Act, the court adjudicated all of the relief sought by UMK in the application.

Although several points *in limine* were raised by SARS in opposition to UMK's application, only one pertaining to jurisdiction needed the attention of the court, i.e. the only forum in which assessments, including additional assessments, could be challenged was the Tax Court, unless a High Court directed otherwise and the High Court would only so direct in circumstances where a litigant had clearly pleaded and made out a case for the High Court to deviate adjudication of issues in or arising from a tax dispute from the Tax Court to the High Court and in this case neither UMK's founding nor its supplementary founding affidavit made out a case for such deviation and in the circumstances the court did not have the

necessary jurisdiction to hear a review regarding the merits of the additional assessments. The net effect was that there was no justification for such direction to be made in terms of section 105 of the TA Act.

UMK denied that the court did not have the necessary jurisdiction to hear and decide the prayers contained in UMK's Notice of Motion as section 105 of the TA Act explicitly reserved the court's concurrent jurisdiction and, in addition, it was contended that the Tax Court did not have the necessary jurisdiction to review and set aside administrative action such as the impugned actions taken by SARS.

The High Court held that section 105 of the TA Act made provision for disputes concerning assessments or decisions to be heard in the High Court subject to the proviso that the High Court directed that this was so, but it was common cause in this application that the High Court had not been approached to direct that the dispute concerning the additional assessments should be heard by it. The High Court would only so direct where a litigant had clearly pleaded and made out a case for the High Court to deviate adjudication of a tax dispute from the Tax Court to the High Court.

The High Court concluded that nowhere in its affidavit did UMK make out a case for such deviation and hence the court lacked the necessary jurisdiction to hear a review regarding the merits of the additional assessments.

Ponnan held the following:

(i) That the High Court could not be faulted in its view that section 105 of the TA Act makes provision for disputes of assessment or decision to be heard in the High Court subject to the proviso that the High Court directed that this was so. It was common cause, in this application, that the High Court had not been approached to direct that the dispute about the additional assessments should be heard by it and, accordingly, in the circumstances, this court lacked the necessary jurisdiction to hear a review regarding the merits of the additional assessment and this was so because UMK had not pleaded a case for the relief sought that a High Court should direct a deviation in terms of section 105 of the TA Act.

(ii) That the court had occasion in a recent case, *C:SARS* v *Rappa Resources (Pty) Ltd* 85 SATC 517, to express the view that section 105 was an innovation introduced by the TA Act from 1 October 2011. It had moreover been narrowed down by an amendment made in 2015. Its purpose was to make clear that the default rule was that a taxpayer may only dispute an assessment by the objection and appeal procedure under the TA Act and may not resort to the High Court unless permitted to do so by order of that court. The High Court will only permit such a deviation in exceptional circumstances and this much was clear from the language, context, history and purpose of the section. Thus, a taxpayer may only dispute an assessment by the objection and appeal procedure under the TA Act, unless a High Court directed otherwise and this was reinforced by the amendment of section 105 in 2015.

(iii) That the *Explanatory Memorandum* that accompanied the Tax Administration Law Amendment Bill of 2015 described the purpose of the amendment of section 105 as follows: 'The current wording of section 105 created the impression that a dispute arising under Chapter 9 may either be heard by the Tax Court or a High Court for review. This section is intended to ensure that internal remedies, such as the objection and appeal process and the resolution thereof by means of alternative dispute resolution or before the Tax Board or the Tax Court, be exhausted before a higher court is approached and that the Tax Court deal with the dispute as court of first instance on a trial basis. This was in line with both domestic and international case law. The proposed amendment made the intention clear but preserved the right of a High Court to direct otherwise should the specific circumstances of a case require it.'

(iv) That the purpose of section 105 was clearly to ensure that, in the ordinary course, tax disputes were taken to the Tax Court. The High Court consequently did not have jurisdiction in tax disputes unless it directed otherwise. (See *Rappa Resources*, *supra*).

(iv) That it followed that the appeal had to fail and in the result it was accordingly dismissed with costs, including those of two counsel.

3.6. ITC 1969 (85 SATC 535)

The taxpayer had sought leave to amend his grounds of appeal dated 2015 ('the 2015 grounds') in the Tax Court in terms of Rules 35(2) and 52(7) of the Tax Court Rules.

SARS opposed the application on the ground, inter alia, that a new ground of appeal, i.e. the 'Incorrect Taxpayer' defence had been included in the amended grounds and was contrary to the provisions of Rule 32(3) of the Tax Court Rules promulgated under section 103 of the TA Act.

Rule 32(3) provided that the taxpayer may not include in the statement a ground of appeal that constitutes a new ground of objection against a part or amount of the disputed assessment not objected to under Rule 7.

Para. 37 to 46 of the taxpayer's amended grounds of appeal introduced the new ground of appeal, i.e. the Incorrect Taxpayer defence which had not been contained in the 2015 grounds.

The taxpayer had initially alleged in his 2015 grounds that certain payments he received were capital amounts in the form of loans, and therefore were not gross income amounts to be included in any assessment.

The taxpayer had sought to introduce a new ground of appeal, alleging that the amounts were received while he was an insolvent and, accordingly, those amounts – which SARS had regarded as his gross income – had not accrued to him, but to the trustee of his insolvent estate in terms of the provisions of the Insolvency Act and they could thus not form part of the taxpayer's gross income.

The taxpayer had indicated in the subsequent proceedings on the permissibility of the new ground of appeal that although the ground relating to the amounts of gross income having accrued to a different party was not specifically raised in the

objection under Rule 7 that preceded the appeal, the issue of the insolvency was mentioned in the prior engagements with SARS.

The taxpayer contended that although the 'Incorrect Taxpayer' defence was not specifically raised initially, the substance of it was contained in his previous allegations that during his insolvency he was in a position where he could not generate an income in his own name.

The taxpayer accordingly contended that these references would suffice to render the new ground permissible.

The taxpayer therefore sought the same outcome, i.e. that the amounts concerned could not form part of his gross income, but based it on a new ground that the amounts in question had accrued to a different party. The taxpayer's assessed gross income was therefore being placed in the hands of another by virtue of the proposed new ground.

The taxpayer further submitted that his insolvent estate and himself constituted one legal persona and the introduction by him of the new defence by way of amendment would give greater clarity to the appeal.

SARS submitted that as the taxpayer did not profess to be conducting business during his insolvency as a general trader, he did not need the authority of his trustee to generate an income and even had the taxpayer conducted a business or profession, his new income would not have been taxable in the hands of the trustee of his insolvent estate as section 23(9) of the Insolvency Act provided that the insolvent may recover for his own benefit the remuneration or reward for work done or for professional services rendered by or on his behalf after the sequestration of his estate.

SARS accordingly submitted that in those circumstances the taxpayer was liable to pay tax on any income which he generated during the period of his insolvency and this formed part of his new estate and did not affect the tax liability of the insolvent estate.

The issue before the court was whether the taxpayer was entitled to amend his grounds of appeal (i.e. the Incorrect Taxpayer defence) which was included in his amended grounds of appeal.

Judge Lopez held the following:

As to the procedure used

(i) That in his application to amend his grounds of appeal, the taxpayer did not set out each of the amendments proposed but instead he chose to amend his 2015 grounds by substituting a new document and in the result it became necessary for anyone who wished to understand the amendments to read carefully through both drafts in order to be certain as to what exactly was changed.

(ii) That in the court's view the above approach was procedurally impermissible. A taxpayer wishing to amend their grounds of appeal should set out sequentially each amendment sought to be made. Doing so will enable the reader to clearly understand which grounds were being amended, and how. No respondent should be required to troll through and compare the two documents, having to read some one hundred and forty-four pages just to be able to discern the nature of the amendments.

(iii) That, however, to deny the application on the ground of procedural irregularity alone, would, no doubt, provoke the suggestion of denying the taxpayer due process. What was particularly disturbing was that in the founding affidavit to lead the amendments, the taxpayer contended that he sought to raise a new ground of appeal, being the 'Incorrect Taxpayer' ground, which was set out in some detail and no other proposed amendments were dealt with in the founding affidavit. Somewhat disingenuously, no reference whatsoever was made to the various factual alterations and withdrawals of admissions.

As to the amendment to the statement of grounds of appeal

(iv) That with regard to the interpretation of Tax Court Rules 10(3) and 32(3), they referred, in similar terms, to the fact that a taxpayer/appellant may not

appeal on a new ground of objection against a part or amount of the disputed assessment which was not objected to by the taxpayer/appellant under Rule 7.

(iv) That the interpretation of the above Rules was dealt with by Keightley J in ITC 1912 80 SATC 417 and the court was in respectful agreement with the views of Keightley J. Thus, on the issue of a taxpayer's entitlement to raise a new ground of objection in the Rule 32 statement, it had to relate to a part or an amount in the assessment that was placed in dispute by the objection under Rule 7 and if it was not raised in his objections under Rule 7, he may not do so by amendment and, in addition, it must constitute a ground of appeal which is sustainable in law.

(v) That if the additional ground of objection in this case was raised in the taxpayer's Rule 7 notice, it was done so very obliquely. Even if it may be considered to have been raised, for the reasons set out herein, the court was of the view that the 'Incorrect Taxpayer' ground did not disclose a defence in law and the amended ground of appeal was disallowed.

As to whether the amended ground of appeal was sustainable in law

(vi) That once the estate of a person has been placed into insolvency, an insolvent is entitled to begin generating a new estate. The limitations on an insolvent from doing so were set out in section 23 of the Insolvency Act as amended and the taxpayer did not suggest that any such grounds were applicable to him. When he generated an income in his new estate, he became personally liable to pay any tax raised on that new estate. It was not clear to the court on what basis the trustee of the taxpayer's estate would have had the responsibility for rendering tax documents and making payments of tax with regard to the income of the taxpayer's new estate.

As to costs

(vii) That the court had borne in mind the manner in which the taxpayer had sought to amend his grounds of appeal and, in addition, the main purpose of the 'Incorrect Taxpayer' defence was without merit insofar as it related to

the trustee of his insolvent estate constituting the correct taxpayer for income earned after the date of the taxpayer's insolvency.

(viii) That, accordingly, the amendment was properly objected to by SARS and the conduct of the taxpayer warranted an order for costs on a punitive scale, to be calculated on the scale as between attorney and client.

4. INTERPRETATION NOTES

4.1. Pre-Trade Expenditure and Losses – No. 51 (Issue 6)

This Note provides guidance on the deduction of pre-trade expenses (sometimes also called start-up costs) under section 11A.

Expenditure and losses are generally deductible only if incurred after the commencement of trade. Trade includes every profession, trade, business, employment, calling, occupation or venture, including the letting of any property and the use of or the grant of permission to use any patent as defined in the Patents Act or any design as defined in the Designs Act or any trade mark as defined in the Trade Marks Act or any copyright as defined in the Copyright Act or any other property which is of a similar nature.

Section 11A, however, permits the deduction of expenditure and losses actually incurred prior to the commencement of and in preparation for the carrying on of that trade in subsequent years of assessment if the requirements are met. The expenditure and losses are deductible in the year of assessment in which trading commences, irrespective of the year in which it was actually incurred.

While this Note provides general guidance on the application of section 11A, the facts and circumstances of each case must be considered in determining when and if pretrade expenses will qualify for a deduction under this section.

4.2. Public Benefit Organisations: Partial Taxation – No. 34 (Issue 5)

This Note provides guidance on the interpretation and application of section 10(1)(cN), which provides for two different kinds of exemptions, namely:

- the exemption from income tax of the receipts and accruals of a PBO to the extent that the receipts and accruals are derived from:
  - carrying on its PBAs; and
  - permissible business undertakings or trading activities; and

a basic exemption to the extent that the receipts and accruals fall within the thresholds provided.

Section 10(1)(cN) applies to the receipts and accruals of only an organization approved by SARS as a PBO under section 30(3).8 Approved PBOs enjoy preferential tax treatment.

A PBO is permitted to carry on permissible business undertakings or trading activities provided its sole or principal object remains the carrying on of one or more PBAs. The receipts and accruals derived by a PBO from conducting permissible business undertakings or trading activites may qualify for exemption from income tax provided the prescribed conditions and requirements, as considered in this Note, are met.

The receipts and accruals derived by a PBO from conducting business undertakings or trading activities falling outside the permissible business undertakings or trading activities, are taxable, if such receipts and accruals exceed the basic exemption.

This Note considers only the broad principles of section 10(1)(cN) and related provisions. Each case must be considered on its own merits, since the facts and circumstances pertaining to each PBO may differ.

The onus is on a PBO to prove that it complies with the requirements as considered in this Note and must retain the necessary evidence to support the view

taken. The burden may be discharged, if requested to do so by SARS, by way of acceptable supporting evidence.

4.3. Section 18A: Audit Certificate – No. 112 (Issue 2)

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

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

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

A section 18A receipt issued by an approved organisation, agency, programme, fund, High Commissioner, office, entity, organisation or department is required to include a certification to the effect that the receipt is issued for the purposes of section 18A and that the donation has been or will be used exclusively for the object of that approved organisation, agency, programme, fund, High Commissioner, office, entity or organisation or, in the case of a department, in carrying on the relevant PBA.

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

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

As a result, the requirement for an approved organisation or department to obtain an audit certificate was introduced as a control measure to ensure that section 18A receipts were issued only for donations received or accrued during the year of assessment that would be and ultimately are used for purposes of PBAs in Part II in South Africa. It is not unreasonable to require control over donations for which an approved organisation or department issues a section 18A receipt, since this potentially entitles the donor to claim a tax deduction that has a real cost to the fiscus given that the donee is normally not subject to tax on the donation received.

Section 18A(2B) and (2C) merely refer to an audit certificate. No detailed requirements are prescribed with regards to the information that must be contained on the audit- certificate, or from whom the audit certificate should be obtained, with the exception of who must issue it in the case of a department. Thus, uncertainty exists on how to comply with the audit certificate requirement.
This Note therefore provides guidance on what would be regarded as acceptable information on an audit certificate referred to in section 18A(2B) and (2C) and from whom such a certificate may be obtained.

Strict control measures must be applied to donations received by or accrued to approved organisations, agencies, programmes, funds, High Commissioners, offices, entities, organisations and departments for which section 18A receipts are issued, since such donations may qualify for a tax deduction from the taxable income of taxpayers and as such represent a cost to the fiscus.

Approved organisations, agencies, programmes, funds, High Commissioners, offices, entities, organisations and departments are therefore required to maintain proper control over the application and spending of such donations.

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

5. BINDING PRIVATE RULINGS

5.1. BPR 395 – Termination of a venture capital company

This ruling determines the tax consequences of the termination of a venture capital company.

In this ruling references to sections are to sections of the Income Tax Act (the Act) and the STT Act applicable as at 5 July 2023. Unless the context indicates otherwise any word or expression in this ruling bears the meaning ascribed to it in the relevant Act.

This is a ruling on the interpretation and application of:

- the Act:
  - section 12J; and
  - section 44.
- the STT Act:
  - section 8(1)(a).

Parties to the proposed transaction

The Applicant: A venture capital company

Co-Applicant: A resident investment holding company

Description of the proposed transaction

The Applicant will transfer all its assets, primarily consisting of shares in qualifying companies, to the Co-Applicant by way of amalgamation.

The Applicant will distribute the ordinary shares in the Co-Applicant to its

shareholders in accordance with their effective shareholdings in anticipation of the Applicant's winding-up and deregistration.

Conditions and assumptions

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

- The Applicant will within a period of 36 months after the date of the proposed transaction, or such further period as SARS may allow, take the steps contemplated in section 41(4) to liquidate, wind-up or deregister.
- The Applicant will not at any stage withdraw any step taken to liquidate, wind-up or deregister or do anything to invalidate any step so taken with the result that it will not be liquidated, wound-up or deregistered.

Ruling

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

- The Applicant will be deemed to have disposed of its shares in the qualifying companies to the Co-Applicant at their respective base costs in terms of section 44(2)(a)(i) of the Act.
- The Co-Applicant will be deemed to acquire the shares in the qualifying companies on the same dates and for the expenditure previously allowable to the Applicant under paragraph 20 of the Eighth Schedule, in respect of the assets as contemplated in section 44(2)(a)(ii).
- The Co-Applicant's contributed tax capital will increase by an amount equal to the Applicant's contributed tax capital at the time of termination under section 44(4A).
- The transfer of the shares in the qualifying companies by the Applicant to the Co-Applicant will not be subject to securities transfer tax under section 8(1)(a) of the STT Act.
- Neither the disposal of the shares held in the qualifying companies nor the termination of the Applicant's existence will be regarded as a transgression

of the sole objective requirement in section 12J(5), and sections 12J(6) and (8) will not be triggered.

- In determining its taxable income, the Applicant must disregard the disposal of shares in the Co-Applicant to its shareholders in accordance with the provisions of section 44(8).
- The distribution of the shares in the Co-Applicant by the Applicant to its shareholders will not constitute a dividend or return of capital under section 44(6)(c).
- The distribution of the Co-Applicant's shares and cancellation of the Applicant's shares will be exempt from securities transfer tax under section 8(1)(a) of the STT Act.

5.2. BPR 396 – Settlement of shareholder's loans

This ruling determines the tax consequences for the Applicant of a proposed settlement of a shareholder's debt via set-off against the subscription price for the issue of additional shares to the shareholder.

In this ruling references to sections and paragraphs are to sections of the Income Tax Act and paragraphs of the Eighth Schedule to the Act applicable as at 6 July 2023. Unless the context indicates otherwise any word or expression in this ruling bears the meaning ascribed to it in the Act.

This is a ruling on the interpretation and application of:

- section 8(4)(a) and (l);
- section 19; and
- paragraph 12A.

Parties to the proposed transaction

The Applicant: A resident investment holding company

Company A: A foreign company that is the sole shareholder of the Applicant

Description of the proposed transaction

The Applicant is indebted to Company A following successive foreign currency denominated loans advanced by previous shareholders and other group companies that had been taken over by Company A. These loans collectively constitute "the Debt".

The Debt was used by the Applicant to fund its operational costs and invest by way of equity and loans in property developing subsidiaries. The investment income from its subsidiaries comprises interest earned on the loans as well as dividends.

Under the proposed transaction, the Applicant will reduce its total balance sheet liabilities by settling the Debt, as follows:

- The Applicant will issue shares to Company A for an amount equal to the face value of the Debt and will leave the liability for the share subscription outstanding on loan account.
- The liability to be owed by Company A to the Applicant for the share subscription will be set-off against the Debt owed by the Applicant to Company A.

Conditions and assumptions

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

Ruling

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

- Section 19(2) will apply to the portion of the Debt utilised to fund operational expenditure to the extent that a "debt benefit" as defined in paragraph (d) of such definition in section 19(1) arises.
- Paragraph 12A(2) will apply to the portion of the Debt utilised to invest in the subsidiaries by means of subscriptions for equity and the advancement of loans to the extent that a "debt benefit" as defined in paragraph 12A(1) arises.

- Section 19(5) and paragraph 12A(5) will apply to the proposed transaction to the extent that a "debt benefit" arises; however, section 19(8)(f) and paragraph 12A(6)(g) will relieve the Applicant from the consequences of section 19(5) and paragraph 12A(5) if any debt benefit arises but the relief will not apply to the capitalised interest.
- Section 8(4)(a) and (l) will not apply to recoup any historical deductions of interest granted under section 24J upon implementation of the proposed transaction.
- Section 8(4)(a) will not apply to recoup any historical deductions of foreign exchange losses granted under section 24I upon implementation of the proposed transaction.

5.3. BPR 397 – Income tax and securities tax consequences resulting from an amalgamation transaction

This ruling determines the income tax and securities transfer tax consequences resulting from an amalgamation transaction entered into between a holding company and its subsidiary.

In this ruling references to sections and paragraphs are to sections of the relevant Income Tax Act (the Act) and paragraphs of the Eighth Schedule to the Act applicable as at 7 July 2023.

Unless the context indicates otherwise any word or expression in this ruling bears the meaning ascribed to it in the relevant Act.

This is a ruling on the interpretation and application of:

- the Act:
    - section 1(1) – definition of "trading stock";
    - section 41(1) – definition of "capital asset" and "disposal";
    - section 44(1), – paragraph (a) of the definition of "amalgamation

transaction";

- section 44(2);
- section 44(3);
- section 44(4A);
- section 44(8);
- section 44(13); and
- paragraph 11 of the Eighth Schedule to the Act.

- the STT Act:
  - section 1(1) – definition of "transfer"; and
  - section 8(1)(a)(ii).

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

The Applicant A resident company

The Co-Applicant A resident company that is a wholly-owned subsidiary of the Applicant

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

The Applicant is an importer of pharmaceutical products. Its operations comprise the marketing and selling of the imported products. The Co-Applicant holds the product registrations and marketing authorisations required to import and sell the products in South Africa.

The Applicant and the Co-Applicant propose to amalgamate. The Applicant will contribute the operating assets of its business and the Co-Applicant will contribute the product registrations and marketing authorizations of the products sold by the Applicant.

The proposed transaction will be implemented in terms of the following transaction steps:

Step 1:

The Applicant will dispose of all its assets (including the shares in the Co-Applicant) and liabilities to the Co-Applicant by means of an amalgamation as contemplated in paragraph (a) of the definition of that term in section 44(1). In exchange, the Co-Applicant will issue new shares to the Applicant.

Step 2:

The Applicant will distribute the new shares in the Co-Applicant acquired in terms of Step 1 as a dividend in specie to its sole shareholder.

Step 3:

The Applicant will then liquidate, wind-up or deregister.

Conditions and assumptions

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

- The ruling will apply to the extent that the liabilities of the Applicant assumed by the Co-Applicant comply with section 44(4)(b) of the Act.
- The Applicant must within a period of 36 months after the date of the proposed transaction, or such further period as SARS may allow, take the steps contemplated in section 41(4) of the Act to liquidate, wind-up or deregister. The Applicant will not at any stage withdraw any step taken to liquidate, wind-up or deregister or do anything to invalidate any step so taken with the result that it will not be liquidated, wound-up or deregistered.

Ruling

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

- The disposal by the Applicant of its assets and liabilities to the Co-Applicant will constitute an "amalgamation transaction" as defined in paragraph (a) of that definition in section 44(1) of the Act.
- Section 44(2) and (3) of the Act will apply to the disposal of the Applicant's assets to the Co-Applicant.

- The contributed tax capital of the Co-Applicant will increase by an amount equal to the contributed tax capital of the Applicant at the time of its termination as envisaged in Step 3 in respect of the issue of the new shares by the Co-Applicant as contemplated in section 44(4A) of the Act.
- The Applicant must disregard the disposal of the shares in the Co-Applicant under Step 2 in determining the taxable income or losses of the Applicant as contemplated in section 44(8) of the Act.
- The cancellation by the Co-Applicant of its own shares following the receipt thereof under Step 1 will not constitute a disposal for purposes of paragraph 11 of the Eighth Schedule.
- No securities transfer tax will be payable in respect of the transfer of shares in the Co-Applicant in Step 1 under section 8(1)(a)(ii) of the STT Act.

5.4. BPR 398 – Disposal of shares pursuant to a property development arrangement

This ruling determines the tax consequences of a disposal of ordinary shares in a property company, and the redemption of newly issued capitalisation preference shares in that company at a later stage.

In this ruling, references to sections and paragraphs are to sections of the relevant Income Tax Act and paragraphs of the Eighth Schedule to the Act applicable as at 12 July 2023.

Unless the context indicates otherwise any word or expression in this ruling bears the meaning ascribed to it in the relevant Act.

This is a ruling on the interpretation and application of:

- the Act:
  - section 1(1) – definitions of “contributed tax capital”, “gross income”, “dividend” and “equity share”;

  - section 8E;
  - section 8EA;
  - section 40C; and
  - paragraph 43A.
- the STT Act:
  - section 1;
  - section 2; and
  - section 6.

Parties to the proposed transaction

The Applicant: A resident company

PropCo: A resident company that is a wholly-owned subsidiary of the Applicant

DevelopCo: A resident company that is not a "connected person" in relation to the Applicant

Description of the proposed transaction

PropCo is a property holding company, which owns land. The shares in PropCo, held by the Applicant, were received by the Applicant in terms of an "unbundling transaction" as defined in section 46(1) more than four years ago and are held on capital account.

PropCo and the Applicant are not equipped with the requisite development expertise to further develop the land. Accordingly, the Applicant will partner with a property developer with the relevant experience, expertise and local market knowledge.

The Applicant and DevelopCo intend to work together to unlock the inherent value of the land by means of an incorporated joint venture. This will entail the installation of services across the land and may include the realisation of certain portions of the land to third parties.

Given the underlying uncertainty around the ability to unlock the inherent value in

the land through the intended development, a third-party buyer would not be willing to pay for the speculative value of the land. It was, therefore, proposed that capitalisation preference shares be issued to the Applicant giving it a preferential right equal to the speculative value of the land.

The Applicant will divest itself of control over PropCo (subject to certain reserved aspects), in favour of DevelopCo in the hope that the underlying development is a-success, and which will over time, generate significant gains for PropCo.

In order to protect the Applicant against this divestiture of control in the shareholding of PropCo, the preference shares will enable the Applicant to have a preferential claim which will be secured by the land, enabling it to have direct access to the land as security in the event that the joint venture is not successful and the preference shares cannot be redeemed.

The parties intend to formalise their shareholding in PropCo and their commercial objectives, by entering into the following proposed transaction:

- PropCo will issue preference shares to the Applicant as a capitalization share issue in terms of section 47 of the Companies Act 71 of 2008 (the Companies Act); and
- Thereafter, the Applicant will dispose of 51% of the ordinary shares in PropCo to DevelopCo, but may subsequently dispose of (or reduce its effective interest in PropCo) by an additional 9%.

The proposed steps for implementing the arrangement are as follows:

Step 1

- PropCo will issue the preference shares to the Applicant as a capitalization share issue in terms of section 47 of the Companies Act.
- The preference shares will have the following terms:
    - each preference share will have a specified capital value so that, in aggregate, the preference shares' value equals the speculative market value of the ordinary shares in PropCo;

  - the preference shares shall rank in priority with respect to, amongst others, distributions by PropCo in relation to other shares and the repayment of shareholder loans;
  - each preference share shall be or may be redeemable, as the case may be:
    - on a scheduled redemption date (which will be five years after the original date of issue); or
    - at the voluntary and sole discretion of the board of PropCo; or
    - if a Trigger Event, Illegality Event or a Sanction Event arises;
  - only if a Trigger Event occurs will a dividend rate of 7% be applied to any outstanding payments in respect of the preference shares; and
  - the preference shares do not have any voting rights except in respect of:
    - a resolution which affects:
      - the rights attaching to the preference shares; or
      - the interests of the Applicant;
    - a Potential Trigger Event or Trigger Event that has occurred; or
    - circumstances in which the Companies Act prescribes that the preference shares shall have a vote.
- As security for the timeous redemption of the preference shares, PropCo will enter into the Pledge and Cession Agreement whereby it (i) pledges all shares and other securities it holds or will hold; and (ii) cedes, in securitatum debiti, its non-interest-bearing bank accounts and claims against third parties, to the Applicant.

On redemption, the preference shares will be redeemed out of profits and not out

of capital (as a return of capital).

Step 2

- The Applicant will then dispose of 51% (and up to an additional 9%) of its ordinary shares in PropCo to DevelopCo on the fulfilment of the conditions precedent in the Share Purchase Agreement. The consideration to be paid by the Purchaser to the Seller for the 51% ordinary shares, will be R1.00.
- The respective parties will also enter into the following two cession agreements:
  - A first ranking pledge and cession agreement, securing the obligations of PropCo in respect of the overdraft facility provided to PropCo; and
  - A second ranking pledge and cession agreement, securing the preference shares and the obligations of PropCo in respect of the preference shares.

Conditions and assumptions

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

Ruling

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

- The exchange of rights resulting in the acquisition of the capitalization shares, must be disregarded for capital gains tax purposes.
- Securities Transfer Tax (STT) will be levied under section 2 of the STT Act on the market value of the ordinary shares of PropCo transferred to DevelopCo. PropCo will be liable for the payment of STT (if any) under section 6 of the STT Act which may be recovered under section 7(2) from-DevelopCo.
- The preference share dividends and / or redemption amounts received by or accrued to the Applicant will be "dividends", as defined in section 1(1) of

the Act.

- The preference shares are neither:
    - hybrid equity instruments" as defined in section 8E(1) and the dividends are not deemed to be income under section 8E(2) of the Act; nor
    - third-party backed shares” as defined in section 8EA(1) of the Act and the dividends are not deemed to be income under section 8EA(2) of the Act.
- As soon as the Applicant becomes entitled to compel PropCo to redeem the preference shares within three years of the date of issue, the preference shares will constitute "hybrid equity instruments" as contemplated in section 8E(1)(a)(ii) of the Act.
- Paragraph 43A will apply to the dividends that will arise in respect of the preference shares, which include the redemption amount.
- The Applicant will be required to take the preference share dividends into account in determining if an “extraordinary dividend” arises under paragraph (b) of that definition in paragraph 43A(1) in relation to the ordinary shares disposed of and to the extent there is an extraordinary dividend that must be taken into account as part of proceeds from the disposal of the ordinary shares under paragraph 43A(2).
- The Applicant will not also be required to take those preference share dividends into account in determining if an “extraordinary dividend” arises under paragraph (a) of that definition in paragraph 43A(1) in relation to the preference shares.
- STT will be payable on the redemption of the preference shares.

The ruling does not express any view on the Companies Act and its application.

5.5. *BPR 399 – Asset-for-share transaction and replacement asset*

This ruling determines the consequences where, almost simultaneously, an asset acquired in an asset-for-share transaction is disposed of and an election is made under paragraph 66 for its replacement with another asset.

In this ruling references to sections and paragraphs are to sections of the Income Tax Act and paragraphs of the Eighth Schedule to the Act applicable as at 14 August 2023.

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

This is a ruling on the interpretation and application of:

- section 8(4)(e);
- section 12C;
- section 42(7);
- paragraph 10; and
- paragraph 66.

Parties to the proposed transaction

The Applicant: A resident company

Description of the proposed transaction

The Applicant is held 100% by Mr X.

Mr X operates a business as a sole proprietor through diverse locations throughout South Africa.

One of the assets that Mr X owns for purposes of his business is an aircraft (the Existing Aircraft). Mr X is in the process of selling the Existing Aircraft and purchasing a new aircraft (the New Aircraft) to replace the Existing Aircraft. He has already entered into an agreement:

- of sale for the sale of the Existing Aircraft. The agreement is governed by foreign law. It will become effective upon closing which is expected to be on or about 15 August 2023; and
- for the purchase of the New Aircraft which will be delivered in August 2023.

It is proposed that Mr X transfer his entire business to the Applicant, including the Existing Aircraft, by way of an asset-for-share transaction contemplated in section 42, effective from 1 August 2023.

The proposed transaction will be achieved as follows:

- Mr X will transfer his entire business to the Applicant in exchange for shares in the Applicant in terms of an "asset-for-share transaction" as defined in paragraph (a) of that definition in section 42(1). The asset-for-share agreement to be entered into on 1 August 2023 will not contain any suspensive conditions.
- One of the assets to be transferred to the Applicant is the Existing Aircraft which is the subject matter of the agreement of sale mentioned above. The closing of the agreement of sale will occur after the conclusion of the assetfor-share transaction. The deemed disposals and acquisitions under section 42, read with paragraph 13, would by then have occurred. Accordingly, pursuant to the asset-for-share transaction, the Applicant will be substituted as the:
    - seller in the agreement of sale of the Existing Aircraft (currently the seller is Mr X) in terms of a deed of assignment; and
    - purchaser in the agreement for the purchase of the New Aircraft (currently the purchaser is Mr X) in terms of a deed of assignment.
- Within a period of 18 months after the Applicant has entered into the assetfor-share transaction, the Applicant will dispose of the Existing Aircraft and acquire the New Aircraft. The Applicant will make an election for the application of paragraph 66 to the disposal of the Existing Aircraft in its return for the 2024 year of assessment.

The disposal of the Existing Aircraft will give rise to a recoupment of the allowances

previously claimed by Mr X under section 12C, as well as to a capital gain under

the Eighth Schedule.

Conditions and assumptions

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

Ruling

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

- The Applicant will satisfy the requirements of paragraph 66(1) in relation to the disposal of the Existing Aircraft and may make the election under that provision.
- The Applicant will be entitled to claim an allowance under section 12C in respect of the New Aircraft.
- Section 8(4)(e) will apply to the recoupment that arises as a result of the disposal of the Existing Aircraft.
- Paragraph 66(2) of the Eighth Schedule will apply to disregard the capital gain derived from the disposal of the Existing Aircraft when determining the Applicant's aggregate capital gain or the aggregate capital loss but paragraph 66(4), subject to subparagraphs (5), (6) and (7) of paragraph 66 will apply to that disregarded capital gain.
- Section 42(7) will apply to the disposal of the Existing Aircraft by the Applicant but will have no adverse consequences due to the rulings in paragraphs (c) and (d) above.

5.6. *BPR 400 – Donations tax implications on the issue of shares at nominal value to enhance BBBEE credentials*

This ruling determines whether donations tax will be payable on the amendment of a company's memorandum of incorporation (MOI) to allow for the issue of shares at nominal value to a Corporate Social Investment (CSI) trust in order to enhance the BBBEE status of a group of companies.

In this ruling, references to sections are to sections of the Act applicable as at 14 August 2023. 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 54;
- section 55;
- section 56; and
- section 58.

Parties to the proposed transaction

The Applicant: A resident trust benefitting employees of a group and who currently holds all the issued share capital in Company A

Company A: A resident company who currently holds shares in the listed holding company of the group (Listco) CSI Trust: A resident CSI trust

Description of the proposed transaction

The Applicant and Company A were established with the principal objective of acquiring and holding (directly or indirectly) Listco shares. These shares shall be utilised directly or indirectly for the benefit of the beneficiaries of the broader group's BBBEE transaction.

The Applicant has not as yet nominated, identified and/or appointed specific beneficiaries.

The Applicant intends to enter into a transaction whereby cash and Listco shares

currently held by Company A and additional Listco shares to be acquired by Company A will be allocated, by amending the MOI of Company A, as follows:

- Beneficiaries of the Applicant which will be the employees of the Group in terms of an employee share ownership plan (ESOP); and
- Beneficiaries of CSI Trust which will be Black People as envisaged in the definition of "Black Participants" in the trust deed of the Applicant (BEE Plan).

The ESOP will be established by way of the incorporation of the terms of the ESOP into the Applicant's founding documents and is intended to exist for a finite number of years. All the employees of the group who are in South Africa will participate in the ESOP.

The Applicant will subscribe for additional shares in Company A. Company A will in turn acquire additional Listco shares for the benefit of the Applicant. The Applicant will have an indirect interest in the Listco Shares.

For purposes of the BEE Plan, a new trust (CSI Trust) has been established as a discretionary inter-vivos trust. It is intended that CSI Trust will exist in perpetuity. CSI Trust will have an indirect interest in the Listco shares held by Company A, together with further Listco shares to be acquired by Company A for the benefit of CSI Trust's beneficiaries. In terms of the trust deed of CSI Trust, the majority of the value of benefits allocated by CSI Trust to its beneficiaries in any financial year, must accrue to Black Persons (as defined in the trust deed).

In terms of the ESOP, following the vesting period, the Listco shares will be distributed to the beneficiaries of the Applicant and the ESOP will terminate. CSI Trust will however continue to (indirectly) hold the remaining Listco shares on the basis that it is intended to be a perpetual scheme.

The Applicant and CSI Trust are not "connected persons", as defined in section 1(1) of the Act in relation to each other.

Conditions and assumptions

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

assumptions:

- CSI Trust is a registered Public Benefit Organisation.
- No beneficiary of the CSI Trust is a connected person in relation to any beneficiary of the Applicant.

Ruling

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

No donations tax liability arises under section 54 as a result of the proposed

transaction comprising:

- the amendment of Company A's MOI;
- the amendment of the Applicant's trust deed to incorporate the provisions of the ESOP; and
- the issue of shares by Company A to CSI Trust for a nominal consideration.

General Note

No view is expressed in relation to the deductibility of the contributions to the Applicant or the capital gains tax consequences of the proposed transaction

5.7. BPR 401 – Leasehold improvement allowance

This ruling determines the tax consequences for a lessor in respect of improvements effected by a lessee.

In this ruling references to sections are to sections of the Income Tax Act applicable as at 11 September 2023. Unless the context indicates otherwise any word or expression

in this ruling bears the meaning ascribed to it in the Act.

This is a ruling on the interpretation and application of section 11(h).

Parties to the proposed transaction

The Lessor: A resident company

The Lessee: A resident company, which is independent of the Lessor

Description of the proposed transaction

The Lessor, a company that is a member of an international group, wishes to upgrade its current warehouse to a facility that can accommodate its required capacity and maximize its distribution efficiencies. To achieve this, the Lessor considered various options, bearing in mind its business strategy, operational needs, and the transactional implications of each option.

The Lessor's corporate philosophy is driven by the group's global strategy and approach to capital expenditure, being to focus its capital expenditure on its main business, by spending its allocated capital budget on machinery and equipment to manufacture its product and not to build or acquire buildings. The reason for choosing the proposed structure is, therefore, driven by global guidance, business and capital investment strategy.

The proposed transaction entails the Lessor leasing the lease area to the Lessee under a ground lease and the Lessee subletting the lease area back to the Lessor under a sub-lease. The intention of the parties is that the Lessee should act as landlord of the lease area.

In terms of the provisions in the ground lease read with the sub-lease the Lessee will have the obligation to erect a warehouse on the lease area.

The following are the salient terms of both lease agreements:

- The lease area is to be leased by the Lessor to the Lessee in terms of the ground lease, for a period of 50 years for a nominal rental amount.
- One of the conditions precedent to the ground lease, is that the sub-lease is concluded simultaneously between the Lessor and Lessee.
- When read together, the ground lease and the sub-lease provide that the Lessee will erect, at its own cost, certain improvements upon the lease area, being a warehouse. As such the Lessee will procure the construction, installation, and completion of a warehouse.

- The lease area, along with the warehouse, are to be sublet by the Lessee to the Lessor in terms of the sub-lease for an initial period, which may be extended on three occasions for 5-year periods each, at the option of the Lessor.
- The sub-lease is subject to the suspensive condition that the ground lease becomes unconditional and that the site development plan of the warehouse is approved by the relevant authorities.
- The Lessor is entitled to terminate the ground lease prior to the end of the 50-year period, either at the end of the initial period of the sub-lease or at the end of an applicable renewal period.
- Should the ground lease be so terminated, the Lessor will be obliged to pay the Lessee an amount equal to the market value of the lease area and warehouse.
- Should the Lessor not exercise its early termination right but elect not to renew the sub-lease, the ground lease will continue to operate for the balance of the 50-year lease period and the Lessee will be entitled to sublet the lease area to third parties.
- Should the ground lease be terminated for any reason the sub-lease will also be terminated.
- Should the ground lease be terminated prior to the expiry of the initial period of the sub-lease resulting from a material breach:
    - by the Lessee, then the Lessee will be entitled to claim an amount equal to the balance of the monthly rental payable in terms of the sub-lease which would have been payable up to the expiry of the initial period of the sub-lease, from the Lessor; or
    - by the Lessor, then the Lessee will be entitled to claim an amount equal to the market value of the lease area and the warehouse erected thereon from the Lessor, plus an amount equal to the net present value of the monthly rental payable in terms of the sub-

lease, which would have been payable up to the expiry of the initial period of the sub-lease.

- Should the ground lease terminate prior to the expiry of the relevant renewal period but after the initial period of the sub-lease as a result of a material breach by either party, then the Lessee will be entitled to claim an amount equal to the balance of the monthly rental payable in terms of the sub-lease, which would have been payable up to the expiry of the relevant renewal period of the sub-lease, from the Lessor.

Conditions and assumptions

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

- The Lessee will be granted a deduction under the provisions of section 11(g) over 25 years; and
- The value of the improvements will be included in the Lessor's "gross income" (Inclusion Amount) under paragraph (g) or paragraph (h) of the definition of "gross income" in section 1(1).

Ruling

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

In respect of the Inclusion Amount, the Lessor may deduct from its income an allowance under section 11(h), equal to the difference between the Inclusion Amount and the present value of the Inclusion Amount, which present value is determined by discounting the Inclusion Amount at 6% over the number of years taken into account in the determination of the relevant allowance granted to the Lessee under the provisions of section 11(g).

5.8. BPR 402 – Transfer of long-term insurance business to a local branch of a foreign reinsurer

This ruling determines the tax implications of the transfer of life reinsurance business from a resident reinsurer to a local branch of a foreign company.

In this ruling references to sections and paragraphs are to sections of the Income Tax Act (the Act) and the VAT Act, and paragraphs of the Eighth Schedule to the Act applicable as at 1 January 2023. Unless the context indicates otherwise any word or expression in this ruling bears the meaning ascribed to it in the relevant Act.

This is a ruling on the interpretation and application of:

- the Act:
  - section 1(1) – definition of "gross income";
  - section 11(a);
  - section 25B(1);
  - section 28(1), – definitions of "short-term insurer", "short-term insurance business", "short-term policy" and "branch policy";
  - sections 28(2);
  - section 28(3A);
  - section 28(4);
  - section 29A(1), – definitions of "adjusted IFRS value" and "negative liability";
  - section 29A(12);
  - paragraph 11(1); and
  - paragraph 11(2)(a).
- the VAT Act:
  - section 2(1)(c);

- section 2(1)(d);
- section 2(1)(f);
- section 2(1)(i);
- section 8(16);
- section 10(4);
- section 12(a);
- section 16(3)(h); and
- section 23(1).

Parties to the proposed transaction

The Applicant: A resident and licensed life reinsurer that is a wholly-owned subsidiary of Company A

Company A: A resident that is a wholly-owned subsidiary of Company B Company B: A foreign reinsurance company that is the ultimate holding company of the group to which the Applicant and Company A belongs

The Branch: A permanent establishment of Company B in South Africa

The Trust: A resident trust established for insurance regulatory purposes as required by section 40 of the Insurance Act 18 of 2017

Description of the proposed transaction

The Applicant has active business operations (including employees, facilities, and infrastructure) in South Africa. Its main business is long-term reinsurance and it, in turn, reinsures a significant portion of its business with foreign group companies.

The Applicant is currently registered for Value-Added Tax (VAT). The Applicant currently makes both taxable and exempt supplies and its main business (i.e. more than 50%) is to provide long-term insurance which is an exempt supply for VAT purposes. The Applicant applies the standard turnover-based method to apportion VAT incurred on mixed-use expenses.

In addition to its reinsurance business, the Applicant also earns fee income relating

to services performed by the Applicant for the benefit of foreign group companies. Most of which relates to the reinsurance business which the Applicant has reinsured with foreign group companies and a small proportion of which relates to services rendered to foreign group companies unrelated to the business underwritten by the Applicant.

The introduction of the Insurance Act 18 of 2017 (the Insurance Act), effective from 1 July 2018, affords foreign reinsurers the opportunity to conduct long-term reinsurance business in South Africa through a branch of the foreign reinsurer, provided the relevant licence is acquired.

Company B wishes to convert the ownership of its operations in South Africa from a company to a Branch, a foreign connected person in relation to the Applicant for tax purposes.

The Applicant will implement the proposed transaction on terms set out in the Sale of Enterprise Agreement (the Agreement) between the Applicant and the Branch.

The salient terms of the agreement are as follows:

- The Applicant will make a cash payment to the Branch in exchange for the Branch assuming all the Applicant's liabilities. The cash consideration will be equal to the market value of the liabilities assumed, net of any negative liabilities as defined in section 29A of the Act.
- The Applicant will dispose of all its assets (other than certain cash balances) at market value to the Branch in exchange for the Branch making a cash payment. Assets required to be held as security for regulatory purposes by the Trust will be transferred directly to the Trust by the Applicant.

Regulatory approval is required from the Prudential Authority (PA) to proceed with the restructure of the Applicant. It is a regulatory requirement that a South African trust be established to hold certain assets of the Branch as security. The legal-structure of the Trust must be approved by the PA and must comply with the legislative requirements of the Trust Property Control Act 57 of 1988 and the Insurance Act.

The Branch will continue to carry on the business previously conducted by the Applicant in South Africa in the same manner but as a foreign reinsurer conducting an insurance business through a Branch in South Africa in terms of section 6 of the Insurance Act. It is intended that the Branch be registered for VAT in South Africa prior to the transaction being implemented. The enterprise activities of the Branch will consist of, amongst others, premiums received from both local and cross border insurers, interest income earned on invested assets, cash and inter unit charges paid for services rendered to the Branch by other Company B group companies.

The Branch will be required to ensure that assets are held in the Trust at all times to the extent that such assets are at least equal to the technical provisions for the reinsurance business of the Branch calculated in accordance with the Insurance Act, as contemplated in section 40(1) of the Insurance Act (the Security). For these purposes, it is envisaged that the Branch may transfer further assets to the Trust to ensure that this requirement remains satisfied.

The Trust Deed will stipulate that the assets and income of the Trust will be held as security in a representative capacity on behalf of the Branch and that any of the assets, claims and rights comprised in the Security, interest and other returns on the Security, proceeds of any disposal by the Trust of any assets, claims and rights comprised in the Security, shall not be received by or otherwise accrue to the Trust, but shall be received by or otherwise accrue to the Branch. However, the Insurance Act requires that the Branch must comply with all requirements under the Insurance Act before giving instruction to the trustee(s) to release assets, claims and rights comprised in the Security held in Trust to the Branch, including the requirement that the Branch may not access or withdraw funds held in the Trust without the approval of the PA.

Conditions and assumptions

This binding private ruling is subject to the additional condition and assumption that the Branch will meet the requirements to be deemed a person separate from the Company for the purposes of paragraph (ii) of the proviso to the definition of "enterprise" in section 1(1) of the VAT Act.

<u>Ruling</u>

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

The Act

- The difference in the market value of net insurance liabilities assumed by the Branch from the Applicant and the IFRS value of such net insurance liabilities must be allocated to the Untaxed Policyholder Fund and the Risk Policy Fund. Any surplus in those funds must then be transferred to the Corporate Fund and taxed in the Corporate Fund in accordance with section 29A(7).
- The cash payment received by the Branch from the Applicant as consideration for the assumption of insurance liabilities of the Applicant constitute a receipt of a capital nature and must not be included in the gross income of the Branch as defined in section 1(1).
- The Branch will constitute a short-term insurer conducting short-term insurance business as contemplated in section 28 and should be taxed in accordance with the provisions of section 28.
- The claims paid in respect of the short-term insurance policies issued and or assumed from the Applicant are deductible under section 11(a) read with section 28(2)(c).
- The Branch will be allowed a deduction for technical liabilities assumed in terms of section 28(3A) in respect of the Branch policies transferred and must include such amounts deducted in income in the following year of assessment under section 28(4).
- The amount in respect of liabilities to be deducted in terms of section 28(3A) must be determined in accordance with IFRS as prescribed in the formula in section 28(3A).
- The transfer of non-cash capital assets by the Branch to the Trust to ensure the required level of assets are held as security by the Trust for regulatory purposes will not be a disposal under paragraph 11(2)(a) for purposes of

the Eighth Schedule.

- As the transfer of assets by the Branch to the Trust will not result in a disposal for purposes of the Eighth Schedule, any income and gains attributable to the assets held in the Trust will be attributed to the Branch and taxed accordingly.

The VAT Act

- Paragraph (v) of the proviso to the definition of "enterprise" specifically excludes from the definition any activity to the extent that it involves the making of exempt supplies and as such, to the extent that any assets are applied exclusively for exempt purposes, those assets would not form part of the enterprise of a vendor.

  As the enterprise or business is being sold and such enterprise consists of assets and liabilities, section 8(16) applies to the supply of the enterprise as a whole and does not apply to the individual assets. Notwithstanding the Agreement the assets exclusively used for exempt purposes will not form part of the enterprise for VAT purposes.

  The supply of the remainder of the business as a whole (which includes the mixed-use assets) will be deemed to be made wholly in the course or furtherance of the Applicant's business and VAT must be accounted for on the full selling price at the standard rate of 15%.

  The Applicant can therefore claim an input tax deduction under section 16(3)(h) in respect of the mixed-use assets sold by the Applicant to the Branch, if the documentary requirements under Interpretation Note 92 are obtained.

- The payment by the Applicant to the Branch for the Branch assuming the insurance liabilities of the Applicant, subsequent to reducing the insurance liabilities with the negative liabilities, will not be consideration in respect of a separate supply of services. Consequently, the Applicant and the Branch do not need to account for VAT.

- The Delegation Payment which relates to the Branch assuming other freestanding liabilities of the Applicant will be an exempt supply and as a result the Branch does not need to account for VAT on that portion of the Delegation Payment.
- The Branch will be required to register for VAT if it will have taxable supplies exceeding R1 million in a 12-month period in South Africa and Company B will not be required to register as a VAT vendor in South Africa.
- To the extent that the supply of the assets comprises financial services which are exempt supplies, the supply of those assets for regulatory purposes will be exempt from VAT and therefore the value of supply rules for connected parties will also not apply.

5.9. BPR 403 – Taxation of covered persons in respect of equity linked notes

This ruling determines the tax treatment of amounts causally connected to financial assets and financial liabilities of a “covered person” which is subject to section 24JB(2).

In this ruling, references to sections are to sections of the Income Tax Act applicable as at 10 November 2023. 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 24JB.

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

The Applicant: A resident company

Noteholder: Various resident companies

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

The business activities of the Applicant pertain to, amongst others, the provision of financing to clients using debt and equity instruments. The Applicant constitutes an

"authorised user" as defined in section 1 of the Financial Markets Act 19 of 2012 and a "covered person" as defined in section 24JB(1).

The proposed transaction entails the Applicant issuing an Equity Linked Note ("ELN") to a Noteholder in the course of its business.

The terms of the ELN are as follows:

- the Noteholder will pay an amount to the Applicant on the subscription (the "Subscription Amount");
- the Applicant will undertake to pay the Noteholder an amount (the "Redemption Amount"), calculated with reference to the value of a specified index or a basket or portfolio of listed shares or participatory interests in a Collective Investment Scheme ("Equity Basket"), subject to a minimum Redemption Amount equal to a percentage of the Subscription Amount on the date the ELN is redeemed by the Applicant ("Redemption Date");
- the ELN will be issued for an indefinite term, subject to a minimum term of five years after which the ELN will be redeemable at the option of the Noteholder;
- the ELN will reference the performance of the Equity Basket;
- the Noteholder will not be entitled to any distributions in respect of the ELN prior to the Redemption Date;
- the Redemption Amount will be determined in accordance with a formula which references, amongst others, the Subscription Amount, the performance or change in value of the Equity Basket in the period between the date of issue of the ELN and the relevant Redemption Date, and the capital guaranteed portion of the Subscription Amount;
- the Applicant will bear the risk pertaining to its ability to make payment to the Noteholder of the Redemption Amount on the Redemption Date and will be liable for any losses that may arise to the extent that it is not able to comply with its obligations in this regard. To the extent that the Applicant is able to generate profits in respect of a particular Equity Basket which

exceed the Redemption Amount payable to the Noteholder, the Applicant will retain such excess return.

The Applicant will use the Subscription Amount for speculative and profit-generating purposes. The Applicant will, therefore, carry on trading activities to generate the return required to meet its obligation to pay the Noteholder the Redemption Amount on the Redemption Date.

The ELN will be recognised as a financial liability at fair value by the Applicant in its Statement of Financial Position in terms of IFRS 9. Subsequently, the ELN will be measured at fair value with changes in the fair value, over the term of the ELN, being recognized in profit or loss in the Applicant's Statement of Comprehensive Income in accordance with IFRS 9.

Conditions and assumptions

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

- The Applicant constitutes a "covered person" as defined in section 24JB(1)(a).
- Sections 8F, 8FA and 24JB(4) do not apply to the ELN.

Ruling

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

- The provisions of section 24JB(2) will apply to the ELN.
- All amounts recognised in profit or loss in the Applicant's Statement of Comprehensive Income in respect of the ELN measured at fair value, must be included in or deducted from the Applicant's income in terms of section 24JB(2).
- Section 24JB(3) will apply to the Subscription Amount and the Redemption Amount.
- The Subscription Amount will not be included in the "gross income" of the Applicant in the year of assessment in which the ELN is issued.

- The Redemption Amount payable by the Applicant on the Redemption Date will not be deductible from the income of the Applicant in terms of section 11(a) read with section 23(g).

6. BINDING CLASS RULINGS

6.1. Consequences for shareholders upon termination of a venture capital company – No. 87

This ruling determines the tax consequences for shareholders of a venture capital company upon termination of the company's corporate existence.

In this ruling references to sections are to sections of the Income Tax Act applicable as at 5 July 2023. Unless the context indicates otherwise any word or expression in this ruling bears the meaning ascribed to it in the Act.

This is a ruling on the interpretation and application of:

- section 8(4)(a);
- section 9C(5);
- section 12J; and
- section 44.

Class

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

Parties to the proposed transaction

The Applicant: A venture capital company

The Co-Applicant: A resident investment holding company

Investors: The shareholders of the Applicant

Description of the proposed transaction

The Applicant will transfer all its assets, primarily consisting of shares in qualifying companies to the Co-Applicant, by way of amalgamation.

The Applicant will distribute the ordinary shares in the Co-Applicant to its shareholders in accordance with their effective shareholdings in anticipation of the Applicant's winding-up and deregistration.

Conditions and assumptions

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

- The Applicant will within a period of 36 months after the date of the proposed transaction, or such further period as SARS may allow, take the steps contemplated in section 41(4) to liquidate, wind-up or deregister.
- The Applicant will not at any stage withdraw any step taken to liquidate, wind-up or deregister or do anything to invalidate any step so taken with the result that it will not be liquidated, wound-up or deregistered.
- The class members held the equity shares in the Applicant on capital account and will acquire the equity shares in the Co-Applicant on capital account.

Ruling

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

- Shareholders of the Applicant that held their shares in the Applicant, for more than three years but less than five years, at the time of the amalgamation must include the amount, previously deducted under section 12J(2), in income under section 9C(5). The Applicant's shareholders are deemed, in terms of section 44(6)(b)(i), to dispose of their shares in the Applicant, for an amount equal to the base cost of their shares in terms of paragraph 20 of the Eighth Schedule, taking into account the deduction under section 12J(2) and any inclusion in income under section 9C(5).
- The Applicant's shareholders are deemed, in terms of section 44(6)(b)(ii), to

acquire their shares in the Co-Applicant for an amount equal to the base cost of the Applicant shares referred to in (a) above.

- The distribution of the shares in the Co-Applicant by the Applicant to its shareholders will not constitute a dividend or return of capital under section 44(6)(c).
- If a former shareholder of the Applicant disposes of shares held in the Co-Applicant that it received following the amalgamation transaction, no recoupment or inclusion in income will arise under section 8(4)(a) or section 9C(5) in respect of deductions previously granted to that shareholder under section 12J(2) in respect of expenditure incurred to acquire the Applicant's shares.

7. BINDING GENERAL RULINGS

7.1. VAT implications of securities lending arrangements – No. 62 (Issue 2)

For the purposes of this ruling:

- "instrument" means "instrument", as defined in section 24J(1) of the Income Tax Act 58 of 1962;
- "manufactured payment" means any distribution in respect of a security which that lender would have been entitled to receive during the lending period had the securities lending arrangement not been entered into, for example, manufactured dividends and manufactured interest;
- "scrip-lending fee" means any amount paid by the borrower to the lender under a securities lending arrangement and includes a manufactured payment;
- "security" means a "security" as defined in section 1 of the Securities Transfer Tax Act 25 of 2007;

- "securities lending arrangement" means an arrangement under which a person lends any security or an instrument to another person and the borrower in return undertakes to return a security or an instrument of the same kind and of the same quality to the lender, whether or not such arrangement qualifies as a "lending arrangement" as defined in the STT Act;
- "section" means a section of the VAT Act;
- "STT Act" means the Securities Transfer Tax Act 25 of 2007;
- "VAT" means value-added tax; and
- "VAT Act" means the Value-Added Tax Act 89 of 1991

Purpose

This BGR clarifies the VAT consequences for the lender in respect of the consideration that the lender charges in terms of a securities lending arrangement.

Background

Practice Note 5/1999 "Tax Implications for Lending Arrangements in respect of Marketable Securities", deals, in brief with, amongst others, the VAT consequences for a lender in respect of these arrangements. This BGR replaces the VAT content of said Practice Note. The VAT content of the Practice Note is withdrawn with effect from 1 April 2023.

Discussion

Section 2(1)(f) deems the activity of the provision of credit by any person under an agreement whereby money or money's worth is provided to another person that agrees to repay in future, a sum or sums exceeding in total, the amount of such money or money's worth, to be "financial services".

Under a securities lending arrangement, the borrower is required to pay to the lender, a "scrip-lending fee" as quid pro quo for the use of the security or instrument during the period, in addition to returning a security or instrument of the same kind and of the same quality.

The proviso to section 2(1) states that the activity under section 2(1)(f) is not deemed to be a financial service to the extent that the consideration payable in respect of the financial service is any fee, commission, merchant's discount or similar charge.

However, in the case of a securities lending arrangement, the "scrip-lending fee" does not relate to any other service forming part of the activity of the securities lending arrangement. The fee is only a charge for the use of the security or instrument during the period and therefore represents the amount exceeding the money's worth that was borrowed, much like interest. It does not relate to any other service, and therefore, the proviso to section 2(1) does not apply to the scrip-lending fee.

The transfer of ownership of the security or instrument is not an independently cognisable supply of goods in the form of the security or the instrument. It is rather considered necessary to give effect to the provision of money's worth to be part of the activity envisaged under section 2(1)(f). This also applies to the return of the security or instrument at the end of the lending period.

Based on the above, the securities lending arrangement whereby the security or instrument, being monies worth, is provided to another person who further agrees to pay a scrip-lending fee in respect of the securities lending arrangement, falls within the ambit of section 2(1)(f). Therefore, the scrip-lending fee constitutes consideration in respect of an exempt supply, and is not subject to VAT.

Vendors that continue to charge VAT on any scrip-lending fee on or after 1 April 2023 as a result of existing contractual arrangements, are required to account for the VAT accordingly [refer to section 31(1)(e)]. However, should the provisions of section 21 be met, credit notes may be issued, and adjustments made under section 21(2), read with section 16(3)(a)(v), (b)(iii) and 16(2)(a).

The issuing of credit notes in respect of securities lending arrangements made before 1 April 2023 would be contrary to the "practice generally prevailing" contemplated in sections 1 and 5 of the Tax Administration Act 28 of 2011, read with the definition of "official publication" in section 1 of that Act.

Ruling

Securities lending arrangements constitute "financial services" envisaged in section 2(1)(f), the supply of which is exempt under section 12(a). The scrip-lending fee due by the borrower constitutes consideration for an exempt supply, and is therefore not subject to VAT.

7.2. Value-Added Tax implications of overpayments on the importation of goods – No. 66

For the purposes of this ruling:

- "assessment" refers to "assessment" as defined in the TAAct as a determination of the amount of a tax liability or refund, by way of self-assessment by the taxpayer or assessment by SARS;
- "clearing agent" means a person that lodges a Customs Clearance Declaration for reward on behalf of a principal;
- "CCD" means Customs Clearance Declaration such as a bill of entry;
- "principal" means the person deemed to have made an importation of goods as contemplated in section 54(2A)(a), and a vendor;
- "VOC" means voucher of correction, being a document to correct any incorrect particulars declared on a bill of entry

Purpose

This BGR clarifies the VAT consequences for a clearing agent and a principal in the event of an overpayment of VAT on the importation of goods due to an erroneous CCD made by the clearing agent, on behalf of the principal.

Background

Due to the volumes of transactions processed by clearing agents on behalf of multiple principals, it sometimes happens that an incorrect CCD is made by the clearing agent, resulting in the amount of VAT calculated, declared, and paid on

the importation of goods being incorrect. Examples are the application of an incorrect exchange rate or incorrect currency, principals giving duplicate clearing instructions etc. In the case of an underpayment, a VOC is submitted to remedy the declaration, and payment.

However, in the case of an overpayment of VAT, VOCs are processed by SARS only in certain specific circumstances for the purposes of a refund as set out in the Customs Refund Policy contained in the SC-DT-C-13 Refunds and Drawbacks – External Guide.

If SARS does not allow a VOC to be processed for the VAT overpaid on the importation of goods, and refund such VAT overpaid, uncertainty arises as to whether the clearing agent or the principal is entitled to an input tax deduction in this regard.

Discussion

VAT is levied under section 7(1)(b) on the importation of goods, by any person, into South Africa (subject to any exemptions or exceptions that may apply). The value on which VAT is payable on importation is based on the value determined under the Customs Act (section 13(2) of the VAT Act). Under section 7(2), the person liable for the payment of the VAT so levied, is the person that imports the goods (the principal or importer). The fact that a clearing agent lodges a CCD on behalf of a principal, does not alter the position that the principal is the importer and is the person liable for the payment of VAT on importation.

Only a vendor that acquires goods for the purpose of consumption, use or supply in the course of making taxable supplies, may deduct the VAT paid on the importation as “input tax” as defined in section 1(1), during the tax period that the requirements under sections 16(3)(a)(iii) or (b)(ii) and 16(2)(d) or (dA) are met. The clearing agent merely facilitates the payment of the VAT in question to SARS on behalf of the principal in terms of a contractual agreement for services between the principal and the clearing agent.

Therefore, it is only the principal that can meet these aforementioned requirements, and only the principal is entitled to deduct the VAT paid on importation as "input tax", and not the clearing agent.

Since SARS will not, in the case of a vendor, process a VOC in respect of the VAT overpaid because of an incorrect CCD on the importation of goods, there is no need to make any adjustments from a VAT perspective.

Ruling

In the event that SARS does not allow a VOC to be processed for VAT purposes, when the clearing agent has made an error on the CCD, the principal is entitled to deduct the VAT incurred on the full amount declared on the importation of the goods, including the overpayment, to the extent that it qualifies as "input tax" as defined in section 1(1), and subject to sections 16(3)(a)(iii) or (b)(ii) and 16(2)(d) or (dA).

7.3. *Standard turnover-based method of apportionment (VAT) – No. 16 (Issue 3)*

For purposes of this ruling:

- "capital asset" means the asset described in E3 in the Annexure;
- "extraordinary income" means the income defined in E4 in the Annexure;
- "ICA" means an instalment credit agreement as defined in section 1(1) and includes a floorplan which complies with this definition;
- "JIBAR" means the Johannesburg Interbank Average Rate and includes reference to ZARONIA where applicable (refer to N3);
- "STB" means the standard turnover-based method of apportionment;
- "ZARONIA" means the South African Overnight Index Average;
- any other word or expression bears the meaning ascribed to it in the VAT Act.

Purpose

This BGR prescribes the method to be used in determining the ratio contemplated in section 17(1).

Background

Section 17(1) provides that the extent to which a vendor may deduct tax payable in respect of goods or services acquired partly for the purpose of making taxable supplies and partly for some other purpose (for example, exempt supplies, private use or other non-taxable purposes) is determined by means of a ratio determined by the SARS in terms of a ruling contemplated in Chapter 7 of the TA Act (that is, a binding general ruling) or a ruling under section 41B (that is, a VAT class ruling or a VAT ruling).

Ruling

The formula set out below, being the STB and the default method, which applies to all vendors in the absence of an alternative method approved by SARS in terms of a ruling as described above, constitutes a BGR under section 89 of the TA Act.

Formula:

$y = a / (a + b + c) \times 100$

Where, having regard to the exclusions and adjustments listed below:

"y" = the apportionment ratio or percentage.

"a" = the value of all taxable supplies (including deemed supplies) made during the period.

"b" = the value of all exempt supplies made during the period.

"c" = the sum of any other amounts of income not included in "a" or "b" which was received or accrued during the period, whether in respect of a supply or not.

The following are **excluded** from the formula set out above:

E1	Foreign exchange differences that do not form part of any hedging activities
E2	Accounting entries, such as fair value adjustments, resulting in income reflected in the AFS4 to ensure compliance with relevant Regulatory Frameworks.
E3	The supply of capital assets.
E4	Extraordinary income.
E5	The value of any goods or services supplied where input tax on those goods or services was specifically denied under section 17(2).
E6	Specific to the provision of finance: • The cash value of goods supplied under an ICA. • The portion of a rental payment relating to the capital value of goods supplied under a rental agreement which is entered into as a mechanism of finance. • Capital value of loans
E7	Change-in-use adjustments under sections 18, 18A, 18C and 18D.
E8	Indemnity payments received as envisaged under section 8(8) to the extent that the indemnity payments relate to extraordinary income or capital assets.
E9	Manufactured interest and dividends received by the borrower of a securities lending transaction.
E10	The value of equities, debentures or bonds issued as a manner of raising funds.
E11	Interest earned from:

4 Annual Financial Statements, generally compiled to comply with relevant regulatory requirements as set out in the Companies Act 71 of 2008

	• the vendor's current account (meaning, the account used for day-today business operations); and • the SARS

Adjustments to the value of certain income streams included in the formula set out above:

A1	Interest, other than the interest excluded from the formula in E11: • Interest from sections 8F and 8FA5 instruments must be regarded as dividends for apportionment purposes and be included in the formula by applying the (prime rate − JIBAR) proxy as set out in A3 below, to such interest. • Net interest must be included on funds that are borrowed with the objective to on-lend. Refer to the discussion on A1 in Annexure A on what "net interest" entails. Notes to the net interest adjustment: 1) If actual values are not available to determine the net interest value to be included, the following proxies must be used: a) Proxy 1 – If no interest is received on the loan – use loan value × prime interest rate b) Proxy 2 – If there is no interest paid value – use loan value × JIBAR 2) If the lending arrangement is between "connected persons" – the higher of the interest using actual values or the loan value × (prime rate − JIBAR) must be used.

5 Of the Income Tax Act.

	• Interest received on any investments, including savings accounts, must be included as follows: Interest received for the year × (prime rate − JIBAR)
A2	Trading in financial assets Include a 3-year moving average of the gross trading margin (selling value − buying value) on the trading of financial assets.
A3	Dividends • Dividends from sections 8E and 8EA[6] instruments must be regarded as interest for apportionment purposes and be included in the formula by applying the (prime rate − JIBAR) proxy as set out in A1 above, to such dividends. • Dividends received from investment activities (including investments held in subsidiaries, associates, ad-hoc or minority investments) must be included by applying the following formula: 3-year moving average of dividends received/accrued during the year × (prime rate − JIBAR)
A4	Profit share from joint venture or partnership The amount to be included in the formula must be determined using the following formula: 3-year moving average of a profit share received/accrued during the year × (prime rate − JIBAR)
A5	Debt securitisation transactions The amount to be included in the formula must be determined using the following formula: Proceeds on the sale of debts under a securitisation transaction during the

6 Of the Income Tax Act.

	year × (prime rate − JIBAR) Note to this adjustment: In addition to the above, a proxy equal to the origination fees charged on the loan must be included in the apportionment formula to ensure that the exempt supply of granting credit is appropriately reflected, only where the loan is sold immediately after origination and before the vendor earning any interest or other consideration in relation to this exempt supply.

General notes for using the formula set out above:

N1	The exclusions and adjustments to the formula are subject to the further explanations and discussions as set out in Annexure A.
N2	"c" in the formula will typically include items such as dividends and statutory fines (if any).
N3	The prime rate to be used for all the adjustments listed above is the applicable prime rate at the end of the financial year. The JIBAR rate to be used for all adjustments listed above is the 12-month term rate quoted on the last day of the financial year. Where more appropriate for the vendor, or should the JIBAR no longer be applicable, the ZARONIA may be used; the rate being the equivalent to the above stated JIBAR. For ease of reference, the reference to JIBAR in this document includes reference to the ZARONIA. Where it is applies to loans, the relevant ratio must be applied to the loan balance on a monthly basis. Should this be impractical, the vendor may use an average value of the loan over the year and apply such average value to the relevant ratio stated above.
N4	The term "value" excludes the VAT component of the supply.

N5	The apportionment ratio must be rounded off to two decimal places.
N6	If the formula yields an apportionment ratio of 95% or more, the full amount of VAT incurred on mixed expenses may be deducted (referred to as the de minimis rule and effected under proviso (i) to section 17(1)).
N7	Vendors using their previous year's turnover to determine the current year's apportionment ratio are required to make an adjustment (that is, the difference in the ratio when applying the current and previous year's turnover) within nine months after the end of the financial year, that is, the adjustment must be made in the VAT201 return submitted at the latest nine months after the financial year end.
N8	This formula may only be used in the following circumstances: • If the method is fair and reasonable to the vendor's business activities. It is the vendor's responsibility to first determine this. If the method is not fair and reasonable, it is the vendor's further responsibility to approach SARS for an alternative method7. SARS is unable to retrospectively approve an alternative apportionment method and will only approve the method from a prospective date or such other date falling within the limitations set out in proviso (iii) to section 17(1). • The vendor submits to vatrulings@sars.gov.za the following information on an annual basis at the time the annual adjustment referred to in N7 is reflected in the VAT201 return: o The vendor's name o VAT registration number o Apportionment method and formula used o Apportionment ratio for the year. The first time that this

7 Refer to the VAT Rulings Process Guide for the process of application.

	formula is applied, the method and apportionment ratio for the past three (3) years must be submitted.
N9	The STB may not be used by a vendor if: • such vendor operates in an industry for which an alternative apportionment method has been approved (and that method is specified as the default method for that industry); and • • an alternative apportionment method has been approved for the vendor, whether by way of a VAT ruling or VAT class ruling.

Period for which this ruling is valid

This BGR applies with effect from all financial years commencing on or after 1 January 2024, and will apply until it is withdrawn, amended or the relevant legislation is amended. The apportionment formula as set out in in Issue 2 of this BGR (the Issue 2 formula) is withdrawn effective from the aforementioned date.

Transitional rules

The Issue 2 formula applies to all financial years preceding those financial years commencing on or after 1 January 2024. If an alternative apportionment method has been approved for use by a vendor in a VAT ruling or VAT class ruling and the vendor regards the apportionment formula set out in this BGR to be fair and reasonable, that vendor can approach SARS to have the VAT ruling or VAT class ruling to be withdrawn from the financial year commencing on or after 1 January 2024. The request for withdrawal must be submitted to vatrulings@sars.gov.za before the end of the financial year commencing on or after 1 January 2024.

The provisional ratio to be applied for the financial year commencing on or after 1 January 2024 may be based on the actual financial results of the preceding financial year using the Issue 2 formula. The adjustment to be made in the tax period, which ends no later than nine months after the end of the 2024 financial year must be based on the actual financial results of such financial year using the apportionment formula set out in this BGR. In the event that a vendor determines

its apportionment on a monthly basis, the vendor must apply the apportionment formula set out in this BGR from the first month of its financial year commencing on or after 1 January 2024; no adjustment after year end is required.

Annexure – Application of the exclusions and amendments to the apportionment formula as set out in paragraph 3 of the Ruling

Exclusions:

E1	**Foreign exchange differences that do not form part of any hedging activities** Due to the ever-changing nature of the economy, it is becoming more prevalent for vendors to trade with customers or suppliers in currencies other than the South African Rand (ZAR). Due to the differing currencies used by the relevant parties for purposes of accounting records and financial transacting, foreign exchange differences must be accounted for to ensure that the accounting records of a vendor reflect the correct value of each transaction entered into. In these circumstances, the foreign exchange difference that is reflected is merely an accounting entry (refer also to the discussion in E2 below) to properly reflect the sale transaction and does not arise of any further activity by the vendor. As such, these foreign exchange differences must be excluded from the apportionment formula. The exclusion above is limited to a foreign exchange difference that is a natural consequence of a sales transaction and requires no additional effort from a vendor. Should a vendor decide to hedge its risk against foreign currency exposure, such decision would require the vendor to enter into another transaction and apply resources in developing the most effective hedging strategy whilst continuously developing and ensuring proper implementation of said strategy. Hedging foreign exchange

	transactions are used to address various risks identified (such as the risk of future or short-term cash flows, or the risk of income) and could take many forms, including forward contracts or options. In order to ensure that the use of resources and all transactions are properly reflected in the apportionment formula, any foreign exchange differences that result from a hedging transaction must be included in the formula. As hedging in essence is a form of trading in financial instruments, the manner of inclusion in the apportionment formula should be in line with A2 below. It is important to note that, where a foreign exchange is hedged, the profit/loss on the underlying foreign exchange may not be set off against the profit/loss on the hedge as these are separate and distinct transactions from a VAT perspective, as explained above.
E2	**Accounting entries, such as fair value adjustments, resulting in income reflected** in the AFS to ensure compliance with relevant Regulatory Frameworks The International Financial Reporting Standards (IFRS) require certain value adjustments to be made in the accounting records of a person to ensure the true economic value of assets or liabilities are reflected in that person's AFS. From a VAT apportionment perspective, the value adjustments made are not income intended to be included in the formula – no actual income will- be received by the vendor as the adjustment is merely a revaluation of an asset or liability at a specific point in time and not consideration for any activity as a result of a separate supply of goods or services. For this reason, any value adjustment made for IFRS purposes is excluded from the apportionment formula. Examples of accounting entries are as follows: • Revaluation of a transaction in foreign currency (also refer to E1 above, (excluding hedges); and

	• Fair value adjustment of fixed and/or intangible assets
E3	**The supply of a capital asset** The VAT incurred on capital expenditure is generally deducted as a once-off at the time when a vendor acquires the said asset. Although the asset is used throughout the trading process, it is not one of the resources that, on an on-going basis, forms part of the pool of expenses that are- subject to the apportionment ratio. It is also accepted that vendors earning trading income are not in the business of selling off their capital assets on an on-going basis, as that would be unbusiness like and would severely influence the ability of the vendor to continue trading. Therefore, the sale of capital assets is generally an extraordinary event that is not expected to occur continuously. Having regard to the extraordinary nature of the supply (such as a sale) of capital assets together with the possible substantial values attached thereto, the inclusion of the income earned on the sale of capital assets in the apportionment formula would distort the apportionment ratio in that it would not fairly reflect the use of those resources to which the apportionment ratio is applied. It is worth highlighting that, due to the significant costs involved in acquiring capital assets, it may be necessary for vendors to determine whether an alternative apportionment method is required for specific capital assets. The vendor must evaluate the specific circumstances and intended use of the capital asset to determine the most appropriate method for the specific asset and, if need be, apply for an alternative method. What is a capital asset? In short, a capital asset is an asset that enables a vendor to trade but is not the trade itself. Consider a vendor selling ovens. To this vendor, the ovens are the trade itself and therefore constitute trading stock which is

	not capital of nature. However, should a bakery buy the oven, the oven enables the bakery to produce baked goods; the baked goods being its trade. To the bakery, the oven is a capital asset. The circumstances of each case must be evaluated to determine the nature of a specific asset. The most important factor to consider is the intention of the vendor when acquiring and subsequently using the asset. As intention is a very subjective test, various factors must be used to determine and substantiate that intention. Some factors that may assist in determining whether an asset is capital in nature, is as follows: • Trading stock is not a capital asset. • The asset is held with a certain degree of permanency. • Linked to the above, the asset is held for a lengthy period of time. Although this test is not conclusive on its own, it could be convincing when deliberated with other factors. • The type of asset is not commonly bought and sold by the vendor on a regular basis. • An asset which stays mostly intact, and which is rather used to produce wealth. The distinction between trading income and income of a capital nature is not a new concept in tax and has been the subject of various disputes and court cases over the years. Chapter 2 of the Comprehensive Guide to Capital Gains Tax provides in-depth examples and discussions on how to distinguish between income and capital. These principles can also be applied as guidance in determining whether an asset is capital in nature for VAT apportionment purposes.
E4	**Extraordinary income** Extraordinary income is non-recurring income received due to exceptional circumstances that are unlikely to be repeated.

	From a VAT apportionment perspective, extraordinary income would have a significant impact on the quantum of income received by a vendor without affecting the normal expenses incurred- year on year. The inclusion of such income in the apportionment formula would therefore severely distort the apportionment ratio as there would be a material fluctuation from one year to another whilst the mixed expenses, and the use thereof in the vendor's business, would have remained unchanged. Based on the above, extraordinary income should be excluded from the apportionment formula. In order to give effect to this, "extraordinary income" is defined for VAT apportionment purposes as non-recurring income received due to exceptional circumstances that are unlikely to be repeated. An example of extraordinary income is dividends received as a result of a reorganisation or liquidation of a company under sections 44, 46 or 47 of the Income Tax Act (see also the discussion on dividends in A3 below).
E5	**The value of any goods or services supplied where input tax on those goods or services was specifically denied under section 17(2)** A vendor is prohibited from deducting input tax on certain items listed in section 17(2). These include, among others, the following: • Goods or services acquired for purposes of entertainment; and • The acquisition of "motor car" as defined in section 1(1). In both the above instances, those vendors that do not generally supply entertainment or "motor car" as defined (and are therefore allowed the deduction), would not normally buy and sell the items on a regular basis. The goods or services purchased would be of a capital nature and the subsequent supply thereof would automatically be excluded from the apportionment formula as a result thereof. In addition, it would be inequitable to include the income on the sale of such goods or services (or any indemnity payment received therefrom) where the vendor was

	originally disallowed (by legislation) any input tax deduction in relation thereto.
E6	**Specific to the provision/receipt of finance** • <u>The capital value of loans</u> Receipt of finance Vendors often obtain finance from financiers such as banks, as a mechanism to raise funds for future business operations or expansions. The receipt of the funds is not regarded as "income" for apportionment purposes and should therefore not be included in the apportionment formula. Provision of finance (section 2(1)(f)) Any finance given, regardless of the form of the agreement entered into, must be repaid by the borrower8. A finance agreement typically makes provision for the original lending amount (the capital amount) to be repaid at a later date as a once-off amount or by way of instalments, together with interest and/or fees. The interest is typically the lender's consideration for granting the borrower the use of the funds for a specific period of time, whilst the fees are charged by the lender for the administrative functions associated with the granting of finance. Both the interest and fees are charged periodically. The income earned by a vendor for the provision of finance is therefore interest and fees which are included into the apportionment formula as and when they are charged to the borrower to appropriately represent the different activities of the lender in providing finance to the borrower (refer to A1 for a more in-depth discussion on the value of the interest to be included).

8 A "borrower" means a person that obtains finance from a lender.

Each repayment made by the borrower may therefore consist of three parts: the capital portion of the loan, interest and fees. As the income earned from the provision of finance is already included in the apportionment formula, the repayment of the loan must be excluded from the formula.

- <u>The cash value of goods supplied by a financier under an ICA</u>

It is common practice for retailers to offer goods to their customers on credit. To reduce their risk, retailers outsource the provision of credit to financiers. Financiers would then purchase the goods from the retailer and immediately on-supply the said goods to the customer (at the exact same price) by way of an instalment credit agreement. The financier does not enter into these agreements to make a profit, but rather to provide finance to the customer on which interest and fees will be charged. The supply of the underlying goods by the financier is therefore merely a facilitating supply; meaning, the financier is required to buy and sell the underlying goods in order to enable the provision of credit.

In order to recognise the financier's purpose/intent of entering into these agreements, the sale of the underlying goods must be excluded from the apportionment formula. The financier as a result, will apply net interest as set out in A1.

It is important to note that this exclusion does not apply where the retailer also fulfils the role of the financier; meaning, the retailer supplies the goods directly to the customer by way of an ICA. In these circumstances, the retailer's main purpose is to make a profit on the sale of the underlying goods by adding a specific profit margin, unlike the financier's purpose explained above. As the retailer is allowed to include the value of the gross sales in the formula in full, the net interest is not justified, and the gross interest must be included (also refer to A1).

	• <u>The portion of a rental payment relating to the capital value of goods supplied under a rental agreement which is entered into as a mechanism of finance</u> Any arrangement which falls within the ambit of a "rental agreement" which is entered into as a mechanism of finance must, for apportionment purposes, abide by similar rules to that of an ICA. That means that the value of the supply (the value of the rental payments) to be included in the apportionment formula must be reduced by the value of the underlying asset. Only the interest and fees charged on the finance arrangement must be included in the formula (refer to A1 for a more in-depth discussion on the value of the interest to be included in the formula). Following the logic of net interest in A1, the rental payment must further be reduced by the cost of funding relating to the rental agreement. Any rental agreement entered into which involves the letting of goods owned by the lessor and which is not entered into as a mechanism of providing finance to a customer (such as a normal operating lease with no financing element), does not form part of the exclusion. The full rental value must be included in the apportionment formula.
E7	**Change-in-use adjustments under sections 18, 18A, 18C and 18D** A change-in-use adjustment adjusts the input tax deducted to reflect the actual use as opposed to the intended use of goods or services. Change-in-use adjustments should be excluded from the apportionment formula.
E8	**Indemnity payments received as envisaged under section 8(8) to the extent that the indemnity payments relate to extraordinary income or capital assets** Subject to certain exceptions, a vendor is deemed to make a supply of

	services upon receipt of an indemnity payment (or indemnification of a loss paid to a third party) from an insurer9. Section 8(8) further deems that supply to be made in the furtherance of the vendor's enterprise. Any indemnity payment received as a result of a capital asset (such as a factory), or extraordinary income should not be included in the formula in keeping with the exclusions in E3 and E4.
E9	**Manufactured interest and dividends received by the borrower of a securities lending arrangement** Securities lending arrangements10 are becoming more prevalent as a manner for vendors to make a profit on the buying and selling of securities (which includes equity shares). This means that the borrower borrows the security with the intention to almost immediately on-sell. The borrower may be in possession of the security for a period, however small, before the security is on-sold. A borrower is required to make manufactured payments to the lender to ensure the lender is placed in the same position had the securities lending transaction never taken place. Should the borrower receive any interest or dividends on the security in the short period that the security is held, such interest and dividends are not really the borrower's as it must, contractually, be paid to the lender. As the manufactured payments are not included as part of the profit and loss on the trading transaction, any dividends or interest received on these lending arrangements should also be excluded from the formula by the borrower. The lender of the securities must include the manufactured interest or dividends received from the borrower in its apportionment formula as follows: Manufactured interest/dividend × (prime rate − JIBAR)

9 See section 8(8).
10 As defined in Binding General Ruling 62 "Value-Added Tax Implications of Securities Lending Arrangements". All terminology in this paragraph follows the terminology of the said rulin

E10	**The value of equities, debentures or bonds issued as a manner of raising funds** One of the methods of raising funds is to increase an entity' s equity, generally by way of issuing equities, debentures or certain bonds. Under section 2, the issuing of these instruments is deemed to be financial services, being an exempt supply under section 12(a). It is not common for an entity to issue new equity on a regular basis as this is generally a very expensive form of raising capital and there is a risk attached to diluting the value of that entity's share capital. As this is regarded as being extraordinary, the income derived from the issuing of equity should not be included in the apportionment formula.
E11	**Interest** • Earned from the vendor's current account(s) (meaning, the account used for day-to-day business operations) It would be hard for any business to function without a bank account used every day to both receive and make payments. The vendor's intention when opening a transactional bank account is therefore never to earn the interest thereon, but rather to facilitate transactions within its business. The income in this account is generally as a result of payments received from third parties or customers as a result of trading activities and not investment activities by the vendor. As the interest rates on a transactional account is very low, businesses rarely hold money in a transactional bank account for earning interest. A vendor would rather transfer any excess funds to a call or similar account where the interest rates are much higher. The business decision to effect such transfer reflects a vendor's purpose of earning investment income in the form of interest. It is for this reason that any interest earned from a call or other investment

	account is included in the apportionment formula (refer also to A1). • SARS Interest.

Adjustments to the value of certain income streams included in the formula set out above:

A1	**Interest, other than the interest excluded from the formula in E11** Interest is generally earned as a result of one of the following activities: • Investment activities • Lending activities These activities are more often than not conducted by a vendor on a continuous basis, even though it might not be a vendor's main purpose. To ensure that the purpose for which the VAT incurred on goods or services is fairly reflected in the apportionment formula, one must have cognisance of the wholistic purpose of the entity, and all activities associated in achieving that purpose. For this reason, interest must be included in the formula. It is however accepted that interest received is dependent on external factors, such as external interest rates, a customer's risk profile and macro-economics to name but a few. These external factors can result in material fluctuations in interest received from year to year even though a vendor's expenses in earning that interest have not significantly changed. For this reason, the interest to be included in the formula must be determined using the guidelines below. • Interest deemed to be dividends The purpose of sections 8F and 8FA of the Income Tax Act is to give effect to the creation of certain equity instruments that may be

	disguised as debt. In this regard, the relevant provisions consider the nature of the instrument itself as well as the nature or character of the yield resulting from the instrument. Based on the provisions and requirements set out in sections 8F and 8FA of the Income Tax Act, any: o interest received from a "hybrid debt instrument" (section 8F of the Income Tax Act); and o "hybrid interest" from an "instrument" as defined (section 8FA of the Income Tax Act), will be deemed to be dividends in specie for purposes of the apportionment formula (refer to A3). • <u>Net interest</u> Where a vendor provides finance, the vendor acts as an intermediary between lenders and borrowers. Its main objective in this regard is the borrowing and lending of money (which constitutes a single activity) for a profit. This single activity can fairly be reflected in the apportionment formula by including a net interest rather than the gross interest received by the vendor. "Net interest" refers to interest received from lending *less* interest paid on funds borrowed to on-lend and the interest portion of bad debts written off. No other expenses may be deducted from the net interest received. For instance, where a vendor offers a product that consists both of a lending and trading element, each of these elements should be included separately in the formula regardless of the fact that the ultimate profit made by the vendor is the net of the two activities. The following is applicable in respect of the net interest to be included in the apportionment formula: *Limited to borrow to on-lend*

	The interest paid to be deducted from interest received must be in respect of funds borrowed that are used to on-lend. Should borrowed funds be partly applied towards the funding of a vendor's business operations itself (meaning, not used for the lending of funds), an appropriate method must be applied to determine the portion of the interest paid that relates to funds being on-lent by the vendor. This is achieved by multiplying the capital amount on-lent to the interest rate the funds were borrowed at to determine the interest paid to be applied in the formula. *Negative net interest margin* Where the net interest amount is a negative for a specific year, a vendor must include the value as an absolute value in the formula. *Zero-rated interest income* The principle of net interest is extended to offshore lending where a vendor earns zero-rated interest. This means that the interest paid in relation to the funds used to provide offshore lending must be used to reduce the interest received from such activities. Where a vendor is unable to directly identify and allocate interest paid to the respective interest income streams (that is, either taxable or exempt), a formula must be applied to determine the value of the interest paid relating to zero-rated interest income. This formula can either be based on the interest income values earned by the vendor during the year, or the value of the respective loans from which the interest is earned, granted by the vendor during the year. Where the value of the loans is used as basis, and either the exempt or zero-rated net interest margin is a negative value, the inclusion of an absolute value will create a distortion. In this instance, the following formula may be used to split the net interest margin between exempt and zero-rated interest:

	c = d x e / (e + f) where− “c” = The portion of the net interest margin to be included in “A” of the formula. “d” = The total net interest margin (expressed as an absolute value where applicable). “e” = The net interest margin relating to zero-rated interest (expressed as an absolute value where applicable). “f” = The net interest margin relating to exempt interest (expressed as an absolute value where applicable). Bad debts/Impairments Having regard to the fact that a lender incorporates a risk element into the interest charged to a customer, the actual amount of bad debts written off during a year (not an estimated amount) may be used to reduce income already included in the apportionment formula (whether current or previous years) as follows: o The interest portion of the bad debts written off must be applied towards reducing the net interest income (exempt and zero-rated interest respectively) included in the formula; and o The portion of the bad debts written off relating to fee income must be applied towards reducing the fee income included in “A” in the formula. No portion of the capital amount written off as bad debts may be applied towards reducing income included in the apportionment formula. This is on the basis that the capital value of loans is excluded from “A” and “B” in the formula (see E7). In the event that bad debts are recovered by the vendor, and the

	bad debts were used to reduce the interest and fee amounts in the formula whether in the same or previous years, the vendor must include the portion of the bad debts recovered that relates to interest and fees accordingly. Proxies for interest received/paid The prime rate to be used for all the adjustments listed above is the applicable prime rate at the end of the financial year. The JIBAR rate to be used for all adjustments listed above is the 12-month term rate quoted on the last day of the financial year. o Where a vendor provides interest-free funding to another entity (generally within a group scenario), there is still a lending activity to be reflected in the formula regardless of the fact that no income is received therefor. For this reason, a proxy of interest income to be determined using the formula set out below, must be used: Loan value × prime rate This does not apply to extended payment terms for the supply of goods or services, such as where a retailer allows a customer to pay for his or her goods within 30 or 60 days with no liability for paying interest. This is subject to the relevant contractual terms and conditions of the retailer specifying this fact. o Where a vendor provides finance from its own cash reserves or borrow on an interest-free basis it will not have any interest paid to reduce the interest income in the formula. A proxy must then be used to ensure that these vendors are not disadvantaged in the calculation of an appropriate apportionment ratio: Loan value × JIBAR

	○ It goes without saying that where a vendor lends funds to a borrower interest-free from its own cash reserves, the proxy to be included in the formula will be calculated as follows: Loan value × (prime rate − JIBAR) ○ Where a vendor lends funds to a "connected person" as defined in section 1(1), the higher of the actual interest values received and paid, or the loan value × (prime rate − JIBAR) must be included in the formula. • Investment interest All investment activities of a vendor, whether investing in cash, equities or other instruments, must be appropriately reflected in the apportionment formula. As previously mentioned, it is acknowledged that the gross interest received is not reflective of how a vendor applies its resources. For this reason, any interest received from investments not otherwise specifically mentioned in the formula, must be included as follows: Interest received for the year × (prime rate − JIBAR) The interest received includes interest on any cash investment placed by a vendor, such as a savings, cash management or fixed deposit account. • Debtor interest Any vendor selling goods or services to a customer on credit, being a section 2(1)(f) supply, includes the gross sale value of such goods or services in its apportionment formula. In order to ensure equity in the manner of which these income streams are included in the formula, the gross interest levied on the debtors' accounts must be included in the formula. This extends further to any "penalty interest" charged to a customer that does not fall under section 2(1)(f), to be

	included in "c" of the formula.
A2	**Trading in financial assets** "Financial asset" refers to any commodity and other financial asset which can be traded on an exchange or over the counter and includes, but is not limited to, repurchase agreements, debt securities, equity securities and derivatives. "Trading" refers to the continuous buying and selling of financial assets by a vendor and does not include the selling of an investment held as a capital asset (refer to E3). "Gross trading margin" refers to the gross profit of buying and selling financial assets, being the selling value less the buying value of the said assets, as recorded in the accounting records as being realised (where the vendor is unable to determine the realised gross trading margin, the values may include both realised and unrealised profit/loss for the year). No other expenses may be deducted from the said margin. Furthermore, any income received on the financial assets while held in trading stock (such as dividends or interest) must be regarded as a separate transaction and be included in the apportionment formula based on the principles set out in A1 and A3.This principle further applies to where a financial asset is subject to a hedge or other transaction such as lending – each aspect of the transaction should be reflected separately in the formula. The objective of a vendor that trades in financial assets is to make the highest profit possible. Due to the fact that there is a continuous sale of financial assets, and the value of those supplies will be significant in comparison to the activities of trading, the purpose of the vendor will not be fairly reflected should the gross selling amount of all the trades be included in the formula. For this reason, the gross trading margin must be included in the formula. Furthermore, the value of financial assets is significantly influenced by external factors such as market value, economics etc. In order to address a possible significant fluctuation in the

	value of the gross trading profit from year to year (which could adversely affect the apportionment ratio of a vendor), a 3-year moving average of the gross trading margin must be included in the formula. This means that the gross trading margin for the current year and two previous years must be calculated individually, and then averaged to determine the value to be included in the formula. Negative gross trading margin Should a vendor's gross trading margin for any of the 3 years be a loss, the absolute value of that loss must be included in the calculation of the 3-year moving average. Due to the interconnectivity of local and foreign trading activities, difficulties may arise in splitting local (exempt) and foreign (zero-rated) profit and losses. The following formula may be used to split the gross trading margin between trading activities with local and foreign counterparties: c = d x e / (e + f) where – "c" = The portion of the gross trading margin to be included in "A" of the formula. "d" = The total gross trading margin (expressed as an absolute value where applicable). "e" = The gross trading margin in relation to trading with non-resident counterparties (expressed as an absolute value where applicable). "f" = The gross trading margin in relation to trading with local counterparties (expressed as an absolute value where applicable).
A3	**Dividends** In order to ensure financial security, entities invest in various instruments both for the yield and financial growth associated with certain markets.

	Dividends, including dividends in specie, are the yield paid on investments in equity and similar instruments. In keeping with the principle of reflecting all investment activities in the formula as set out in A1, dividends received must be included in the formula to reflect the investment activity in said instruments (even though dividends are not consideration for any supply made by a vendor). • <u>Dividends deemed to be interest</u> The purpose of sections 8E and 8EA of the Income Tax Act is to give effect to the substance of certain share transactions which may contain certain characteristics usually associated with debt. As a result, dividends received from preference shares or any other similar instrument complying with the criteria as set out in the aforementioned sections, are deemed income for income tax purposes unless the consideration is applied towards a qualifying purpose (that is, the direct or indirect acquisition of equity shares in an operating company). Based on the provisions and requirements contained in sections 8E and 8EA of the Income Tax Act, dividends received from shares which fall within the ambit of a: o “hybrid equity instrument” (section 8E of the Income Tax Act); o “preference share” (section 8EA of the Income Tax Act); or o “third-party backed share” (section 8EA of the Income Tax Act) will be deemed to be “interest received” for purposes of the apportionment method (refer to A1). • <u>Investment dividends</u> The investment activity associated with the holding of investments (whether in subsidiaries, associated companies or minority shareholdings held through an asset manager), must be fairly

	reflected in the formula. Having regard to the fact that an entity declares and pays dividends based on various requirements and factors (such as a group's dividend policy or economic and market conditions), it is accepted that the quantum of dividends does not fairly reflect the investment activity of holding the investments as capital assets. In addition, significant fluctuations may be experienced in the value of dividends declared from year to year. Similarly, as was explained in A2, instruments held for trading have a different purpose than for earning a yield and financial growth; the purpose being reflected in the formula based on the principles set out in A2. Any dividends received while holding the instruments as trading stock should not be included in the formula in full. In order to appropriately reflect a vendor's investment activity in the formula, the value of dividends to be included in the formula must be determined as follows[11]: 3-year moving average of dividends received × (prime rate − JIBAR) o The 3-year moving average is determined by calculating the average of dividends received during the current financial year and two immediately preceding financial years. o If a vendor does not receive dividends during the current financial year, a 3-year moving average of the 3 preceding years may be used as proxy. o If a vendor receives no dividends for at least 2 out of the 3 years, a 5-year moving average must be used instead of the 3-year moving average where dividends were received for at least 2 of the 5 years.

11 The reference to dividends received for purposes of determining the below, is the dividends received by a vendor for all investments collectively and does not refer to the receipt of dividends per investment held.

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If a vendor has not received dividends for 2 out of the 5 years as required above, and the vendor is a holding company charging management fees to its subsidiaries, the vendor must include a value equal to the management fees charged for that financial year in the formula as proxy for dividend income. No 3-year moving average will be applied in this instance.
If a vendor has not received dividends for 2 out of the 5 years as required above, and the vendor is not a holding company charging management fees to its subsidiaries, the vendor must approach SARS for an alternative manner of determining a value to be included in the formula that appropriately reflects its investment activities. The application must comply with the time limitations set out in the proviso to section 17(1).
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<tr><td>A4</td><td>
Profit share from joint venture or partnership

Entities often enter into joint venture or partnership agreements to, amongst others, share the initial financial burden of a capital or resource intensive project. This is especially prevalent in the mining industry but can occur in any industry between two or more persons. The contract entered into creates an unincorporated body which, for VAT purposes, is regarded as a separate person. The enterprise is conducted in the body and what is distributed to the various partners are only the partners' share of the profits (often referred to as a product-sharing arrangement).

From a VAT apportionment perspective, entering into a joint venture or partnership agreement is seen as being similar to investing in another entity where dividends are earned. For this reason, the profits distributed to partners are included in the formula using a similar logic to investment dividends (refer to A3).
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	It is important to note that this adjustment does not apply to circumstances where, under agreement, a partner makes an undivided right of use in an asset available to the joint venture or partnership in return for the distribution as a consideration. In these instances, the supply of the right should be appropriately reflected in the formula by including it in full. In order to appropriately reflect a vendor's investment activity in the formula, the value of the profit share to be included in the formula must be determined as follows: 3-year moving average of the profit share received/accrued × (prime rate − JIBAR) • The 3-year moving average is determined by calculating the average of the profit shares received during the current financial year and two immediately preceding financial years. • If a vendor does not receive a profit share during the current financial year, a 3-year moving average of the 3 preceding years may be used as proxy. • If a vendor receives no profit shares for at least 2 out of the 3 years, a 5-year moving average must be used instead of the 3-year moving average where profit shares were received for at least 2 of the 5 years. • If a vendor has not received a profit share for 2 out of the 5 years as required above, the vendor must approach SARS for an alternative manner of determining a value to be included in the formula that appropriately reflects its investment activities. The application must comply with the time limitations set out in the proviso to section 17(1).
A5	**Debt securitisation transactions** A "debt securitisation transaction" is a mechanism of raising capital that

	typically involves the transfer of a debt security book to a separate legal entity, a special purpose vehicle (SPV) specifically created to acquire the said book, generally by way of sale of the debt. The sale is generally done at the market value of the book debt, being the face value of the assets transferred (that is, the risk adjusted aggregate value of the cash balance of the securitised debt security) (the capital value of the loans). The amount received from the securitisation transaction does not constitute additional turnover for the vendor. Essentially, the proceeds are seen as payment for previous supplies or repayment of existing advances, although not received from the original borrower. Notwithstanding the purpose for which securitisation transactions are entered into by vendors, the full exclusion of the capital value of debt sold in a securitisation transaction will not fairly reflect the activities and resources incurred in the sale of these debts to the SPV. As all the activities associated with the sale of the debts collectively constitute a separate "financial service", the supply of which under section 2(1)(c), is exempt under section 12(a). This exempt supply must be fairly reflected in the apportionment formula. It is however acknowledged that the inclusion of the full sale value of the debts sold by a vendor in the formula is distortive and the following formula must be applied to determine a suitable value in the formula to appropriately reflect the activities associated with debt securitisations: Capital value of debts sold under a securitisation transaction during the year × (prime rate − JIBAR) <u>Interest on debts sold immediately after origination</u> The origination of a debt, such as a loan, is a financial service under section 2(1)(f), and therefore the supply is exempt under section 12(a). Generally, the interest received from the granting of credit over a time period is sufficient to reflect this exempt activity in the apportionment formula. However, where a debt is sold immediately after origination, no

	amount of income relating to the granting of credit, being the exempt supply of financial services, is earned by the vendor. As a result, this activity relating to the making of the exempt supply is not sufficiently reflected in the apportionment formula. Having regard to the above, a proxy equal to the origination fees charged on the debt (and which is included in “a” in the formula) must be included in “b” of the apportionment formula to ensure that the exempt supply of granting credit is appropriately reflected, only where the debt is sold immediately after origination and prior to the vendor earning any interest or other consideration in relation to this exempt supply. This inclusion is separate from the sale of the debt securities described above and must be included in the formula in addition thereto.

7.4. Income tax exemption of a grant received under the clothing, textiles, footwear and leather growth programme – No. 67

For the purposes of this ruling:

- “CTCP” means the Clothing and Textiles Competitiveness Programme;
- “CTFLGP” means the Clothing, Textiles, Footwear and Leather Growth Programme;
- “Eleventh Schedule” means the Eleventh Schedule to the Income Tax Act;
- “IDC” means the Industrial Development Corporation of South Africa Limited established by the Industrial Development Corporation Act 22 of 1940, which is wholly owned by the government; and
- “the dtic” means the Department of Trade, Industry and Competition.

Purpose

This BGR determines the income tax treatment of a government grant received under the CTFLGP that replaced the CTCP.

Background

Clothing and Textiles Competitiveness Programme

The CTCP is a programme of the dtic administered at the CTCP Desk of the IDC on behalf of the dtic. The purpose of the CTCP is to stabilise employment and to improve overall competitiveness in the clothing, textiles, footwear, leather and leather goods manufacturing industries.

The Minister of Finance gave notice in Regulation 538 in Government Gazette 35516 of 13 July 2012 that any grant received by or accrued to a person by virtue of the CTCP administered by the dtic will be exempt from income tax under section 10(1)(y) with effect from 1 April 2009.

The CTCP is listed as item 11 in the Eleventh Schedule, which exempts any government grant received under that programme from income tax under section 12P.

A government grant received under the CTCP is therefore exempt under both section 10(1)(y) and section 12P(2).

The name of the CTCP was changed by the dtic to the CTFLGP on 12 January 2022. The name was changed to include the footwear & leather sectors. which have always benefitted from the CTCP, but the name never indicated such, which created confusion.

Clothing, Textiles, Footwear and Leather Growth Programme

The CTFLGP is also administered at the IDC on behalf of the dtic. The dtic confirmed that the CTFLGPreplaces the CTCP and is an amended version of the CTCP although it has been simplified, revised and introduced a new loan component allowing for the repayment of funds to the dtic. The CTFLGP therefore has the same objectives and addresses the same

issues as the CTCP. The name merely changed to be inclusive of all the sectors benefitting from the programme to prevent any confusion.

Ruling

Since the CTFLGP is only an amended version of the CTCP and the name of the programme merely changed to be more inclusive of the sectors benefitting from the programme and to prevent confusion, any government grant received by or accrued to under the CTFLGP must for income tax be treated similarly to a government grant received by or accrued to under the CTCP.

7.5. Acceptable documentation for input tax on upward adjustments on imports (VAT) – No. 68

For the purposes of this ruling:

- "CEB01" means a Customs and Excise Billing Declaration;
- "SAD 500" means the Single Administration document 500 form;
- "VOC" means voucher of correction;

Purpose

This BGR sets out the documentation acceptable to SARS to substantiate an input tax deduction on an upward pricing adjustment in respect of goods previously imported into South Africa.

Background

SARS is often asked to make a retrospective adjustment of a vendor's customs duty values for a prior period to rectify the customs duty values incorrectly declared and bring the additional import VAT and customs duties to account. Importers that realise that they have submitted an invalid entry or an entry that does not in every respect comply with section 39 of the Customs and Excise Act, have an obligation under section 40(3) of the said Act to correct any incorrect particulars declared on

the entry by means of a VOC. In this regard some vendors submit a CEB01 form to effect the amendment to the original declaration.

Discussion

Under section 16(3)(a)(iii), a vendor may deduct the VAT incurred on the upward pricing adjustments in relation to the goods acquired by it from a supplier and imported into South Africa during a prior period, provided:

- the VAT incurred falls within the ambit of paragraph (a)(ii) of the definition of "input tax" in section 1(1) in relation to the vendor;
- the goods have been released under the Customs and Excise Act; and
- the said deduction complies with all other requirements for the deduction of "input tax" set out under sections 16, 17 and 20.

At the time of making the deduction, referred to above, the vendor must be in possession of a customs release notification (i.e. the 'EDI Customs Status 1 Release Message') to prove that the goods have been released for customs purposes and, under section 16(2)(d), hold a bill of entry or other prescribed documents (such as a VOC) under the Customs and Excise Act together with the receipt of payment for the VAT, in order to substantiate the deduction.

The CEB01 in the vendor's possession does not fall within the ambit of the customs documentary proof and therefore the vendor cannot substantiate the deduction based on the said documentation for purposes of section 16(2)(d).

Acceptable documentary proof

Having regard to the above, SARS is satisfied that:

- a vendor has, under section 16(2)(g)(ii)(aa), taken reasonable steps to account for the VAT with SARS Customs where it obtained the prescribed documentary proof required under section 16(2)(d) when the goods were originally imported but was unable to obtain the required documentation for the upward pricing adjustments due to the utilisation of a CEB01 form; and

- no other provision of the VAT Act can be applied to satisfy SARS that the documentation in the vendor's possession is acceptable for purposes of making a deduction.

Decisions under section 72

Section 72 makes provision for SARS to make a decision to a vendor or class of vendors to overcome difficulties, anomalies or incongruities that have arisen or may arise in regard to the application of any of the provisions of the VAT Act. SARS may therefore only invoke the provisions of section 72 where he is satisfied that there is a difficulty, anomaly, or incongruity that exists. Furthermore, a decision made under this section to overcome such difficulty, anomaly, or incongruity must not:

- have the effect of reducing, or increasing the liability for tax levied under the VAT Act; or
- be contrary to the construct and policy intent of the VAT Act as a whole or any specific provision in the VAT Act.

It is evident, given the construct of the VAT Act, that the legislator intended to allow the vendor a deduction of the "input tax" on VAT declared under section 7(1)(b) at the time goods are imported and on any subsequent adjustments based on the wording of section 16(2)(d).

The legislator did not, however, envisage that vendors may experience difficulties regarding the required documentation and be rendered unable to obtain the necessary documentary proof to substantiate the input tax deduction for purposes of section 16(2)(d).

SARS generally accepts the documentation under section 16(2)(g) which, however, necessitates that the vendor requests a ruling from SARS to confirm the acceptance of the alternative documentation acceptable to SARS. Therefore, waiving the requirement for each vendor to request a ruling from SARS where the vendor is in possession of the acceptable

documentation as set out below to substantiate the input tax deduction will not have the effect of:

- reducing or increasing the liability for tax levied under the VAT Act; or
- be contrary to the construct and policy intent of the VAT Act as a whole or any specific provision in the VAT Act.

Prescription in respect of the deduction of input tax

Section 13(6) provides that the provisions of the Customs and Excise Act relating to, amongst others, the importation and clearance of goods and the payment of duty, apply mutatis mutandis as if enacted in the VAT Act. This applies regardless of whether any customs duty is levied.

The term "entry for home consumption" is defined in section 1 of the Customs and Excise Act to include an entry under any item in Schedule 3, 4 or 6 to the Customs and Excise Act. The Customs and Excise Act further defines "home consumption" to mean the consumption or use in South Africa.

Based on the above, in the case of the importation of the goods in question, proviso (i)(bb) to section 16(3) provides that any vendor that is entitled under section 16(3)(a)(iii) to deduct any input tax in respect of any tax period, may deduct that amount from the amount of output tax attributable to a later tax period that ends no later than five years after the end of the tax period during which the goods were entered for home consumption under the Customs and Excise Act.

<u>Ruling</u>

Section 72

An arrangement is made under section 72 that a vendor is not required to apply for a specific ruling as required under section 16(2)(g) in relation to transactions to which this BGR applies.

Section 16(2)(g)

SARS hereby exercises his discretion under section 16(2)(g) to allow a vendor a deduction of the "input tax" in respect of the upward pricing adjustments of goods acquired by it from a supplier and imported into South Africa based on the vendor being in possession of the following documentation when the VAT return containing such a deduction is submitted to SARS:

- SAD 500
- Electronic Data Interchange form
- Invoices received by the vendor in respect of the adjustment
- Letter disclosing the upward pricing adjustment to SARS and application to bring VAT and duties to account
- Letter of demand and permission letter to make adjustments, issued by SARS • CEB01 form
- Proof of payment of the import VAT in respect of the upward pricing adjustment paid to SARS

The deduction referred to above:

- must be within the five-year prescription period provided for in proviso (i)(bb) to section 16(3); and
- may only be made in the tax period during which this ruling was issued or any subsequent tax period thereafter.

8. GUIDES

8.1. Basic Guide to Section 18A Approval

This guide has been prepared to assist organisations in understanding the basic requirements for obtaining and retaining approval under section 18A of the Income Tax Act.

Government has recognised that certain organisations are dependent on the generosity of the public and to encourage that generosity has provided a tax deduction for certain donations made by taxpayers. The eligibility to issue section 18A receipts is restricted to specific organisations approved by SARS that use the donations to carry on or fund specific PBAs in South Africa. The aforementioned specific organisations must apply to SARS for approval under section 18A to issue such receipts for donations received. A section 18A receipt may be issued by a section 18A-approved organisation only from the date SARS has confirmed section 18A approval. SARS issues a reference number for purposes of section 18A which must appear on the section 18A receipts.

8.2. VAT 409 – Guide for Fixed Property and Construction for Vendors

This guide is a general guide concerning the application of the VAT Act in connection with fixed property and construction transactions in South Africa.

The fixed property industry consists of many role-players, including architects, builders, developers, property speculators, quantity surveyors, engineers, plumbers, electricians, municipalities, public entities, financial institutions, estate agents etc. Although these role-players are mentioned in this guide, the content deals primarily with vendors that are involved in transactions concerning the development, construction and selling of fixed property.

VAT is an indirect tax which is levied on the supply of any 'goods' or 'services' supplied by a 'vendor' in the course or furtherance of any enterprise carried on by that vendor. 'Goods' is defined to include 'fixed property' and any real right in any such fixed property but excluding any right under a mortgage bond or pledge of any fixed property. The scope of transactions with which this guide is concerned with is therefore those described in the definition of 'fixed property', which means:

- land (together with improvements affixed thereto);
- any unit as defined in section 1 of the Sectional Titles Act 95 of 1986;

- any share in a share block company which confers a right to or interest in the use of immovable property under the Share Blocks Control Act 59 of 1980;
- in relation to a property time-sharing scheme, any time-sharing interest as defined in section 1 of the Property Time-sharing Control Act 75 of 1983; and
- any real right in any such land, unit, share or time-sharing interest.

It will therefore be found that most transactions which have some connection with the acquisition of rights to fixed property (excluding rights under a mortgage bond or pledge of fixed property) will fall within the ambit of the definition and will be subject to VAT if the supplier is a vendor.

Other examples of rights falling within the definition include:

- Certain rights of use such as usufructs, usus or habitatio
- Bare dominium rights of ownership
- Servitudes, encroachments and other encumbrances
- Exclusive use areas in sectional title developments
- Rights to minerals or rights to mine for minerals
- Leases or sub-leases of rights to minerals, or to mine for minerals.

Although most supplies of fixed property by a vendor will be subject to VAT, there are certain instances when such supplies will not be. In these cases, the transactions will be subject to transfer duty. It is therefore important that vendors can distinguish between the different types of supplies to establish whether VAT or transfer duty applies. The VAT Act and the Transfer Duty Act 40 of 1949 (the Transfer Duty Act) therefore both contain special rules to deal with these situations. (See the Transfer Duty Guide.)

The approach of this guide in dealing with the topics is set out below:

Chapter 1 – This chapter sets out the scope of the most common transactions falling within the definition of 'fixed property'.

Chapter 2 – Introduces the reader to the most important concepts, terms and definitions mentioned in the guide so that the VAT treatment of supplies which are explained in later chapters can be understood. A key point addressed in this chapter is the concept of an 'enterprise' and the different circumstances under which certain activities conducted will render a person liable to register for VAT.

Chapter 3 – Deals with the interaction between VAT, transfer duty and securities transfer tax. This chapter explains which types of transactions are subject to VAT and when the other taxes will apply.

Chapter 4 – Explains the VAT treatment of the different types of supplies and the VAT accounting in respect thereof. The chapter includes a discussion on the application of the special time and value of supply rules with regard to the declaration of output tax and input tax. It also explains the rules which apply for deducting notional input tax on the acquisition of second-hand goods constituting fixed property.

Chapter 5 – Deals with a number of adjustments which apply in connection with fixed property based on the extent of taxable use. These include annual adjustments in regard to the use of capital goods and services as well as situations which give rise to a change in use or application or change of intention with regard to the taxable use of the fixed property after the initial acquisition.

Chapter 6 – Explains the specific application of the VAT law which has been set out innprevious chapters to transactions in the construction industry. The focus is specifically on those vendors that supply construction services only and deals mainly with quoting of prices, costing of projects, invoicing, agent and principal relationships, and certain other aspects such as penalties and retentions which are unique to the construction industry.

Chapter 7 – Deals mainly with the issues faced by developers and property speculators. The focus is therefore on supplies of newly constructed properties and second-hand properties that have been renovated before being sold, or properties

that are bought and sold on a speculative basis. Included is a discussion on the consequences of temporarily applying residential properties for exempt supplies whilst they are being marketed for sale (taxable supplies). Other topics include the sale of shares and members' interests in fixed property, fractional ownership-type developments and land restitution transactions.

Chapter 8 – Deals with the VAT treatment of rental pools. The chapter contains a detailed explanation of the special rules set out in section 52 and how these apply in practice to override what would otherwise be viewed as supplies made by an agent.

Chapter 9 – Discusses some other aspects regarding the supply of fixed property which are not dealt with in the other chapters.

8.3. Guide on the Taxation of Farming Operations

This guide is a general guide regarding the taxation of farming operations in South Africa.

Farming contributes largely to job creation and is a major contributor to the gross domestic product. Just as there are many different types of farming operations, for example pastoral farming, crop farming, plantation farming, aquaculture and game farming, there are also a variety of different methods of conducting farming operations, such as free-range farming, organic farming and conventional farming.

Various factors such as the climate, demand for products as well as the high costs associated with farming have an impact on successful farming. These factors can potentially negatively impact a farmer's income and expenditure on a regular basis.

To assist farmers, a beneficial set of tax rules applies to farming operations and the income and expenses emanating from such operations. Section 26(1) of the Income Tax Act provides that the taxable income of any person carrying on farming operations shall, in so far as the income is derived from such operations, be determined in accordance with the Act but subject to the First Schedule.

The First Schedule details the computation of taxable income derived from farming operations. The taxable income from farming operations is combined with the taxable income from other sources to arrive at the taxpayer's taxable income for the year of assessment. The First Schedule applies regardless of whether a taxpayer derives an assessed loss or a taxable income from farming operations. The First Schedule may also apply even after farming operations have been discontinued.

The main aim of this guide is to highlight the tax consequences for persons conducting farming operations in South Africa.

Farming can be a very lucrative business in South Africa. It is, however, very dependent on various factors such as the climate, demand for a product and the weather, amongst others. This may result in fluctuations in taxable income with farmers not producing any yield in one year but exceeding expectations in the next.

To assist farmers, a beneficial set of tax rules applies to farming operations and the income and expenses emanating from such operations. Section 26 stipulates the persons and circumstances that this section will find application while the First Schedule sets out how to compute the taxable income of the persons engaged in farming operations.

Generally, the farmer will be required to bring to account the value of livestock and produce in opening and closing stock. In the event that standard values have been prescribed by regulation, these must be used, unless the farmer has entered into an agreement with SARS that other values may be used. Livestock and produce which are acquired by donation or through inheritance must also be included in opening stock in the year of acquisition at market value under paragraph 4.

The deduction under section 11(a) for the cost of livestock and produce is ring-fenced under paragraph 8, while an assessed loss or balance of assessed loss from farming is subject to potential ring-fencing under section 20A.

8.4. Basic Guide to Section 18A Approval (Issue 5)

This guide has been prepared to assist organisations in understanding the basic requirements for obtaining and retaining approval under section 18A.

Government has recognised that certain organisations are dependent on the generosity of the public and to encourage that generosity has provided a tax deduction for certain donations made by taxpayers. The eligibility to issue section 18A receipts is restricted to specific organisations approved by SARS that use the donations to carry on or fund specific PBAs in South Africa.

The aforementioned specific organisations must apply to SARS for approval under section 18A to issue section 18A receipts for donations received. A section 18A receipt may be issued by a section 18A-approved organisation only from the date SARS has confirmed section 18A approval. SARS issues a reference number for purposes of section 18A which must appear on the section 18A receipts.

9. 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.