TAX UPDATE

For period: April 2024 to June 2024

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1. FOREWORD

The purpose of this update is to summarise developments that occurred during the second quarter of 2024, 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 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 Tax Poem

Tax his land, tax his wage,

Tax his bed in which he lays.

Tax his tractor, tax his mule,

Teach him taxes is the rule.

Tax his cow, tax his goat,

Tax his pants, tax his coat.

Tax his ties, tax his shirts,

Tax his work, tax his dirt.

Tax his chew, tax his smoke,

Teach him taxes are no joke.

Tax his car, tax his grass,

Tax the roads he must pass.

Tax his food, tax his drink,

Tax him if he tries to think.

Tax his sodas, tax his beers,

If he cries, tax his tears.

Tax his bills, tax his gas,

Tax his notes, tax his cash.

Tax him good and let him know

That after taxes, he has no dough.

If he hollers, tax him more,

Tax him until he’s good and sore.

Tax his coffin, tax his grave,

Tax the sod in which he lays.

Put these words upon his tomb,

‘Taxes drove me to my doom!’

And when he’s gone, we won’t relax,

We’ll still be after the inheritance tax.

-Author unknown.

2. NOTICES / REGULATIONS

2.1. Dispute Resolution for Trusts: Enhancements

7 June 2024 – A reminder of the automated process for Trust taxpayers that was introduced on eFiling during April 2024 to electronically submit documentation to lodge a dispute via a fully guided process. This applies to the following transactions:

- Submission of Request for Reasons,
- Request for Remission (RFR),
- Notice of Objection, and Notice of Appeal.

Note: A request for suspension of payment currently remains a manual process using the steps provided below.

Prior to this enhancement, the Trust dispute process was a fully manual process, using the ADR1 and ADR2 forms (Alternative Dispute Resolution forms).

Process for Suspension of Payment

The suspension of payment currently remains a manual process and requires one of the following:

- Submission of uploading a formal request letter (requesting the suspension of payment) when lodging a dispute on eFiling, together with other supporting documentation
- Submission of a formal request letter at SARS a branch

Important note: Trusts that submitted any of the processes mentioned above before 20 April 2024 should still conclude their dispute through the manual process.

3. TAX CASES

3.1. I-Cat International Consulting (Pty) Ltd v C:SARS (86 SATC 101)

I-Cat International Consulting (Pty) Ltd (I-Cat) had, during 2013, obtained a tax opinion from its tax advisor and had relied upon that opinion to file its tax return for the 2014 tax year.

The opinion caused I-Cat to claim an amount of R17 171 433 as an expense and as an allowable deduction in the 2014 year of assessment.

The main issue between SARS and I-Cat in respect of its 2014 year of assessment was that I-Cat, after having received advice in the aforementioned legal opinion that it was entitled to do so, had adopted the tax position that the amount of R17 171 433, paid to a third party as compensation for royalties and accounted for by I-Cat as cost of stock, could be claimed as a deduction against its taxable income in terms of section 11(a) of the Income Tax Act.

I-Cat had accounted for the entire portion of the expense incurred and which had flowed from the principal transaction in the 2014 year of assessment.

SARS, on 15 July 2015, had assessed I-Cat in respect of the 2014 year of assessment and had issued a notice of finalisation of an audit in which SARS did not agree with the position adopted by I-Cat and had disallowed the aforementioned amount as a deduction.

I-Cat lodged an objection against the additional assessment in respect of the 2014 year of assessment and thereafter SARS had disallowed I-Cat's objection against the additional assessment for 2014.

I-Cat thereafter filed a notice of appeal against the disallowance of the objection in respect of the additional assessment for 2014 and this was referred to as the 2014 assessment dispute.

Subsequently the parties entered Alternative Dispute Resolution (ADR) proceedings and the ADR Facilitator issued a report noting that the parties were unable to resolve the 2014 assessment dispute.

I-Cat then filed a notice in terms of Tax Court Rule 25(3) indicating that it intended to pursue the tax appeal to the Tax Court in respect of the 2014 assessment dispute (the 2014 income tax appeal).

On 28 October 2019, the date for the hearing of the 2014 income tax appeal, I-Cat and SARS settled the 2014 income tax appeal in respect of the 2014 year of assessment and the Tax Court made the settlement agreement between the parties a consent order of court.

In the Tax Court SARS raised as an alternative defence that only R7 997 633.05 of the claimed deduction was paid by I-Cat and was actually incurred during the 2014 tax year and that the balance of R10 152 940 was paid in the 2015 year of assessment and therefore only qualified as a deduction in terms of section 11(a) of the Income Tax Act in that year.

Part of the settlement agreement, as contained in par. 6 of the consent order, provided 'that the issues pertaining to the deductibility of the amount [claimed], as it may relate to the 2015 year of assessment, being R10 154 940, fall outside of the issues in this tax appeal. The Appellant may endeavour to address such issues in terms of section 93 of the ITA'.

Section 93 of the Tax Administration Act provided that SARS 'may make a reduced assessment if … necessary to give effect to a settlement under Part F of Chapter 9.'

Pursuant to the settlement agreement and the consent order I-Cat proceeded on 13 December 2019 to file an application for a reduced assessment in respect of the 2015 year of assessment in terms of section 93 of the Act (the 2015 reduced assessment request).

I-Cat, on 21 February 2020, gave notice of its intention to institute High Court proceedings in terms of section 11(4) of the Act in respect of the 2015 reduced assessment request.

Absent any decision in respect of the 2015 reduced assessment request, I-Cat proceeded on 14 October 2020 to institute review proceedings in the High Court.

On 26 January 2021 SARS refused the request for reduced assessment in respect of the 2015 year of assessment as SARS was of the opinion that I-Cat's 2015 assessment had become prescribed in terms of section 99(1) of the Tax Administration Act.

Section 99(1) provided that 'an assessment may not be made in terms of this Chapter…(a) three years after the date of assessment of an original assessment by SARS…'

On 13 May 2021 the parties agreed to remove I-Cat's first review application from the roll and on 20 May 2021 I-Cat gave notice to SARS of its intention to institute the present review proceedings in respect of the 21 January 2021 decision.

On 19 August 2021 I-Cat launched the present application for review, 25 days outside the 180-day prescribed period provided for in section 9 of the Promotion of Administrative Justice Act 3 of 2000 (PAJA).

On 14 December 2021 I-Cat filed its application for condonation for the late institution of the review proceedings.

The first issue considered by the court was whether it deemed it in the interests of justice to grant I-Cat condonation for the late filing of the present application for review in terms of PAJA.

The second issue before the court was whether a 3-year prescriptive period applied in respect of I-Cat's 2015 income tax assessment.

Section 99(1) of the Tax Administration Act provided that 'an assessment may not be made in terms of this Chapter 3 years after the date of assessment of an original assessment by SARS.'

The date of I-Cat's original 2015 assessment was 26 February 2016 and, in the premises, the 3-year period as provided for in section 99(1)(a) in respect of the 2015 tax assessment had expired on 25 February 2019.

In the premises the right to assess in respect of I-Cat's 2015 assessment had become prescribed unless any of the exclusions to the prescriptive period as provided for under section 99(2) of the Act applied to the facts in the present matter.

I-Cat contended that the provisions of sections 99(2)(d)(i) and 99(2)(d)(ii) were applicable to the facts in the present case.

<u>Section 99(2)(d)(i) provided that section 99(1) did not apply to the extent that it was necessary to give effect to 'the resolution of a dispute under Chapter 9.'</u>

I-Cat submitted that at the time when the parties entered the compromise, SARS not only knew of the error that affected the 2014 year of assessment but also knew of the error affecting the 2015 year of assessment prior to the lapsing of the expiry of the 2015 assessment prescription period.

Moreover, I-Cat submitted that the provisions contained in the Tax Court order that related to both the 2014 and 2015 years of assessment could not be ignored as the provisions related to the resolution of the dispute between the parties and in the premises in order to give effect to the resolution of the dispute between the parties the provisions of section 99(1) did not apply.

SARS contended that once regard was had to the correct interpretation and application of the Tax Administration Act, it was clear that I-Cat's review proceeding was ill-founded. The decision to refuse to make a reduced assessment for the 2015 income tax year of assessment was correct as the assessment had become prescribed.

SARS further contended that as it was a creature of statute, it was bound by the empowering provisions of legislation, which precluded the issuance of a reduced assessment after a period of 3 years after the original assessment was made.

Judge Vermeulen held the following:

<u>As to the application for condonation for delay in seeking review</u>

(i) That the present application for review which was instituted in terms of the provisions of the Promotion of Administrative Justice Act 3 of 2000 was filed approximately 25 days outside of the prescribed 180 days <u>but section 9 of PAJA allowed the court to extend the period in which review may be sought where the interests of justice so required</u>.

(ii) That SARS could not direct the court's attention to any prejudice caused to him because of the late filing of the application for review and also did not make any submissions in opposition to I-Cat's request for condonation.

(iii) That there was no evidence before the court to indicate that I-Cat did not at all relevant times act expeditiously in the institution of the review application. On the contrary, as indicated already, I-Cat had proceeded with an application for review during 2020, absent any decision by SARS on the 2015 request for a reduced assessment.

(iv) That the standard to be applied in assessing the delay under PAJA was whether the delay had been unreasonable. Factors that needed to be considered when granting condonation included the nature of the relief sought in the review application, the extent and cause of the delay, the effect of the delay on the administration of justice and other litigants, the reasonableness of the explanation for the delay, the importance of the issue to be raised in the intended appeal and the prospects of success.

(v) That, applying these principles in the present matter, the court was satisfied that condonation should be granted to I-Cat and stressed, inter alia, that the importance of the issue to be raised in the application for review and the prospects of success justified that condonation be granted.

(vi) That, in the premises, the court deemed it to be in the interests of justice to grant I-Cat condonation for the late filing of the present application for review.

<u>As to the merits of the application for review</u>

(vii) That the present matter came before the court on the basis that a 3-year prescriptive period in terms of section 99(1)(a) of the Tax Administration Act applied in respect of I-Cat's 2015 income tax assessment. In the premises the right to assess in respect of I-Cat's 2015 assessment had become prescribed unless any of the exclusions to the prescription period as provided for under section 99(2) of the Act applied to the facts in the present matter. I-Cat argued that the provisions of sections 99(2)(d)(i) and 99(2)(d)(iii) were applicable to the facts in casu.

(viii) That the court was of the view that the provisions of section 99(2)(d)(i) of the Act were indeed applicable to the present matter and, because of which, the prescription period of 3 years as provided for in section 99(1) of the Act was not applicable.

(ix) That the practice of making settlement agreements was well established and had existed for a long time in South Africa. In Van Schalkwyk v Van Schalkwyk 1947 (4) SA 86 (O) the court stated that 'the tradition of such orders is very strong in our legal system.' It was apparent that the parties in this matter had reached a settlement which was thereafter incorporated in a consent order by the Tax Court. In reaching their compromise the parties at the very least indirectly resolved the nature of the deduction, the amount of the deduction and that the said amount (as the balance) had been incurred in 2015, which issues were directly linked to the same issues between the parties in respect of I-Cat's 2014 year of assessment.

(x) That at the time the compromise was entered between the parties, SARS knew that the balance of the amount was incurred in 2015. On the contrary, this was their alternative defence. What was clear from the last sentence of par. 6 of the consent order was that both parties had agreed that I-Cat would have the right to approach SARS again in respect of the 2015 year of assessment. Although the parties had made it clear that SARS could not bind itself as to the outcome of such approach, by using the term ‘endeavour’, at least I-Cat had the right to apply. The court could hardly imagine that SARS would be able to successfully raise the abovementioned defences again in respect of the 2015 assessment, but the court made no finding to this effect as this was something that SARS would need to decide upon when it adjudicated upon I-Cat’s application for a reduced assessment in respect of 2015.

(xi) That the court was satisfied that the parties did not include the said par. 6 in their agreement and subsequent consent order of 28 October 2019 in error or to serve no purpose.

(xii) That the court therefore found that it was in the parties’ contemplation with par. 6 of the consent order that as part of their compromise, I-Cat could approach SARS in terms of section 93 of the Tax Administration Act in respect of the 2015 year of assessment, with an application for a reduced assessment. It was part and parcel of their resolution of the dispute which they had dealt with under Chapter 9. This would, however, only be possible if the 3-year prescription period as provided for in section 99(1) was not applicable.

(xiii) That, in view thereof that it was necessary to give effect to the resolution of the dispute under Chapter 9 as contained in the consent order, the 3-year prescription period as provided for in section 99(1) of the Act could not apply.

(xiv) That in arriving at this finding, the court had due regard to the language of par. 6 of the consent order itself, read in context and having regard to the purpose of the provision and consent order. In addition, the interpretation which this court ascribed to the relevant clause provided a sensible and business-like meaning and the interpretation contended for by SARS led to an insensible or unbusinesslike result.

(xv) That, in the premises, SARS’ finding that the 2015 assessment had prescribed in terms of section 99 of the Act and therefore that I-Cat’s application for a reduced assessment had to be declined in terms of section 99(3) of the Act read with section 99(2) of the Act, should be reviewed and set aside.

Condonation was granted to I-Cat for the late filing of this application for review.

SARS’ decision dated 26 January 2021, the subject of the present application, was reviewed and set aside.

3.2. Agenbach NO and Others v C:SARS (86 SATC 125)

Applicants, being the trustees of the Nano Trust (the Trust), had instituted review proceedings against SARS in terms of the Promotion of Administrative Justice Act 3 of 2000 (PAJA).

The Trust had been established in 2005 with its main purpose and object being the investing and transacting in and holding of strategic, global and diverse property investments.

Prior to 13 July 2017 the Trust was a South African tax resident and had held a share portfolio consisting of listed and unlisted shares.

On 15 June 2017 a Namibian Trust, the Dyer Trust, was established, being resident in Namibia for tax and exchange control purposes. The Dyer Trust had the same beneficiaries as the Trust and itself became a beneficiary of the Trust. The Dyer Trust further acquired the sole shareholding in Dyer Investments (Pty) Ltd, a Namibian company.

On 10 July 2017 the Trust concluded a Forward Sale Agreement (FSA) with Dyer Investments (Pty) Ltd and in terms of the FSA the Trust disposed of its entire share portfolio and certain claims to Dyer Investments (Pty) Ltd for an amount of almost R2 billion.

On 13 July 2017 the First to Third Applicants were appointed, together with the Fourth Applicant, as trustees of the Trust pursuant to the resignation of two of the previous trustees of the Trust. At the same meeting a resolution was passed that, with effect from the date of that meeting, the Trust would be tax resident in Namibia by virtue of the newly appointed trustees in Namibia and that the Trust would no longer be tax resident in South Africa.

Letters of Authority were issued by the Master to the three new trustees on 4 September 2017.

Pursuant to an audit conducted in 2021 relating to the 2018 year of assessment of the Trust, SARS addressed a letter of audit findings to the Trust on 12 July 2021. In the audit findings, SARS informed the Trust of proposed adjustments on the basis that a capital gain on the disposal of the shares and claims in terms of the FSA had been made by the Trust and indicated an intention to make a tax adjustment of more than R241 million.

A dispute ensued pertaining to the question whether the Trust was still a South African resident taxpayer at the disposal date of the assets of the Trust.

On 16 March 2022 the Trust commenced this review application in the High Court and on 17 March 2022 the Trust lodged its objection against SARS' impugned decisions and SARS disallowed the objection on 13 April 2022.

On 1 June 2022 the Trust lodged an appeal to the Tax Court against the disallowance of the objections by SARS. This appeal was still pending but was apparently suspended pending the outcome of the present review application before the High Court.

The main relief sought by the Trust was that the additional assessment be reviewed and set aside based on an alleged error of law committed by SARS by finding that there had been an immediate accrual of proceeds to the Trust on the conclusion of the FSA.

SARS, in opposing papers, raised the following defences:

- It denied that SARS had committed an error of law in its finding against the Trust, by finding that there had been an immediate accrual of proceeds to it on the conclusion of the FSA;
- The Trust had failed to exhaust its internal remedies as contemplated in the Tax Administration Act (the TA Act) and as required by section 7(2) of PAJA;
- The Trust had failed to make out a case that justified a deviation from the default objection and appeal process contemplated under section 105 of the TA Act.

At the commencement of the proceedings the court indicated to counsel that it required them to first address it on the two points in limine raised by SARS:

- The Trust had not exhausted the internal remedies available to it, particularly the appeal process under section 104 of The TA Act as provided for in section 7(2) of PAJA; and
- The Trust had not made out a case under section 105 of The TA Act for a deviation from the default process of objection and appeal under section 105 of the Act.

Applicants relied on two aspects that constituted exceptional circumstances in the present application that would justify an exemption from the requirement to exhaust internal remedies:

- The dispute between the parties only involved a point of law;
- It would be more convenient to approach the court in terms of PAJA because the process before the Tax Court may take longer to be resolved.

Judge Cilliers held the following:

(i) That on a proper interpretation of section 7 of PAJA it was clear that a court should not entertain a review of administrative action where internal remedies have not been exhausted, unless it was found that there were exceptional circumstances and the court granted an exemption to exhaust any internal remedy on application by the party concerned if it was found to be in the interest of justice to grant such exemption.

(ii) That in Nicol and Another v Registrar of Pension Funds and Others 2008 (1) SA 383 (SCA) at para [18] it was found that exceptional circumstances which might justify an exemption in terms of section 7(2)(c) of PAJA would exist where the available internal remedy would not be able to provide the Applicant with effective redress for his or her complaint. It would therefore be necessary to examine the nature of the internal remedy provided under the Tax Administration Act in the present case in order to establish whether the Trust had an internal remedy available that could effectively redress its complaint.

(iii) That the rationale for the duty to exhaust internal remedies had been evaluated and explained by the Constitutional Court in Koyabe v Minister for Home Affairs 2010 (4) SA 327 (CC) at paras [35]–[38] and the court in that case did warn that the requirement should not be rigidly imposed, nor should it be used by administrators to frustrate the efforts of an aggrieved person to shield the administrative process from judicial scrutiny. The requirement that a party exhaust internal remedies was therefore not absolute.

(iv) That in Bato Star Fishing (Pty) Ltd v Minister of Environmental Affairs and Others 2004 (4) SA 490 (CC) it was also emphasised that a court should take care not to usurp the functions of administrative agencies in the above regard.

(v) That section 105 of the Tax Administration Act provided that a taxpayer may only dispute an assessment or decision as described in section 104 in proceedings under Chapter 9, unless a High Court otherwise directs. This section therefore also required from an aggrieved taxpayer to seek assistance in resolving disputes of the present nature in the manner prescribed by section 104 of the Act – unless a High Court otherwise directed, and this section also laid down a default rule that disputes should be resolved by means of the objection and appeal process provided for in section 104 of the Act.

(vi) That the Supreme Court of Appeal found in C:SARS v Rappa Resources (Pty) Ltd 85 SATC 517 that a deviation in terms of section 105 of the Tax Administration Act should only be permitted in exceptional circumstances.

(vii) That it appeared to be common cause between the parties that the Tax Court did indeed constitute an internal remedy within the ambit of section 104 of the Act for purposes of the resolution of disputes of the present nature.

(viii) That for the argument that the mere fact that a dispute involved only a point of law would constitute exceptional circumstances, the Applicants' counsel relied heavily on the decision of ABSA Bank Ltd and Another v C:SARS 83 SATC 401 where it was found that an attribute which would satisfy the element of exceptionality was where the dispute was entirely about a point of law.

(ix) That the court was not in agreement with the Applicants' submission that the abovementioned findings by the court in ABSA Bank stood uncontested by subsequent decisions. The Supreme Court of Appeal found in the Rappa case, supra, at para [22], that it was not desirable nor possible to lay down a precise rule or definition as to what would constitute exceptional circumstances and further emphasised that each case must be considered on its own facts and that the circumvention of the appeal procedure provided for in the Tax Administration Act should not be allowed without reason.

(x) That the court was of the view that a finding that the only dispute between the parties involved a point of law would be one of the factors, indeed a material factor, to be taken in consideration in the enquiry whether exceptional circumstances existed. However, the court could not agree with an approach that such finding, would on its own, in all cases satisfy the relevant enquiry relating to the question whether there were exceptional circumstances.

(xi) That the court therefore found itself in disagreement with the ABSA Bank judgment, insofar as it was held that when the dispute between the parties only related to a point of law that it would satisfy exceptionality in all cases.

(xii) That it was common cause in the present case that the Trust did not exhaust the internal remedies available in terms of the Tax Administration Act. It appeared, however, not to be common cause that the dispute between the parties only involved a point of law. SARS disputed this allegation in the opposing papers and it was also raised and denied by counsel on behalf of SARS during argument.

(xiii) That there could be no doubt that the Tax Court was in a much better position to adjudicate the dispute between the parties if there are or may be factual disputes between the parties. It was common cause that such an appeal was a wide appeal and that the Tax Court will have all the powers that this court had.

(xiv) That the court was therefore not persuaded that there were exceptional circumstances in the present application that justified the exemption of the Trust from the obligation to exhaust any internal remedy.

(xv) That the court also found that the Trust did not make out a case for the exercise of the court's discretion to direct otherwise as was contemplated in section 105 of the Tax Administration Act.

(xvi) That, accordingly, the Trust was directed to first exhaust the internal remedy available to it as provided for in the Tax Administration Act before instituting proceedings for judicial review in terms of PAJA.

Application dismissed with costs.

3.3. Henque 3935 t/a PQ Clothing Outlet (in business rescue) v C:SARS (86 SATC 136)

Henque 3935 t/a PQ Clothing Outlet (in business rescue) (Henque) was a close corporation that filed a tax return for 2017 with SARS wherein it claimed to have made a loss of R46 000 and was therefore not obliged to pay income tax.

Henque, at the same time, had accumulated tax credits for VAT and was therefore entitled to a refund.

SARS, on 29 November 2017, issued a notice of assessment in which it had recognised that Henque was due a refund. The assessment was based solely on the claims made by Henque in its return and, in the same notice, SARS informed Henque that it was to be subjected to an audit.

Henque, on 31 January 2018, commenced business rescue and the decision to commence with business rescue was voluntarily taken by its sole member and the first meeting of creditors and employees was held on 12 February 2018.

SARS continued with the audit which was only completed on 4 April 2018 and it revealed that Henque's claim that it had made a loss during the 2017 year was false.

In fact, the audit revealed that Henque had produced a taxable income of R16 793 724 for the 2017 year of assessment and SARS then issued an additional assessment to Henque on 1 May 2018 and on the same day an employee of SARS informed Henque's Business Rescue Practitioner (BRP) that its income tax liability for 2017 was R5 334 123 and this amount included penalties and interest.

The notice of the additional assessment identified the 'due date' to be 1 May 2018 and the 'second date' to be 31 May 2018. The second date is the date by when the tax due is to be paid. The amount assessed, thus, only became due and payable on 31 May 2018.

In terms of section 50 of the Companies Act the BRP must, after consultation 'with creditors, other affected persons and the management' of the entity prepare a business rescue plan and, in this case, the BRP published his rescue plan on 31 May 2018 and the plan recognised a tax liability for VAT of R2 467 810 and for PAYE at R568 728 making a total of R3 036 538. The business rescue plan did not include the income tax liability for 2017 which by that stage had been issued to Henque as an additional assessment and according to the plan SARS would receive only 15% of its claim.

The business rescue plan was adopted by the creditors at a meeting on 13 June 2018 and SARS was not present at the creditors' meeting. Those creditors whose claims were accepted by the BRP were paid but for some or other reason SARS had not been paid.

On 2 August 2018 an employee of SARS addressed a letter to the BRP stating that SARS had not been kept informed of the business rescue process and that it was in the process of approaching court for an order setting aside the business rescue proceedings.

The BRP responded to the letter and asked SARS to send a copy of its claim against Henque to him so that it could be 'adjudicated'.

SARS claimed R8 131 225 from Henque which, inter alia, included an income tax claim of R5 101 361.

SARS was finally of the view that the VAT refund due to Henque would not be paid as it had been set-off against Henque's income tax liability in terms of section 191 of the Tax Administration Act (the TA Act).

Moreover, SARS took the view that the income tax due by Henque for the 2017 year of assessment had only become due and payable on 31 May 2018 when the additional assessment with regard thereto had been completed and therefore this liability constituted a post-commencement debt.

This stance of SARS was a complete volte face from its earlier one and Henque disagreed with this view and objected to the decision to set-off the VAT refund against the income tax liability for the 2017 year of assessment.

Henque was also of the view that the liability for the 2017 income tax arose and was due on 28 February 2017 and, accordingly, it was a pre-commencement debt and thus the VAT refund of R1 018 820 could not be set-off against it.

Henque further submitted that an assessment, including an additional assessment, of the liability subsequent to 28 February 2017 only quantified the liability but did not create the liability.

The differences between the parties remained unresolved and hence Henque instituted the present application in the High Court.

Henque called on the court to declare that:

(i) the 2017 additional assessment of its tax liability dated 4 April 2018 was a pre-business rescue debt, i.e. pre-commencement debt, and that

(ii) SARS was prohibited from collecting the 2017 additional assessment by applying set-off against Henque's VAT refund payments due for the period 02/2018 to date.

The court had to consider the relevant sections of the Companies Act, the Income Tax Act and the TA Act.

Judge Vally held the following:

(i) That section 5(1)(d) of the Income Tax Act required Henque to pay tax on its income earned or accrued during each of its financial years. The tax was payable for the specific year that the income was earned. The tax was owed once the financial year was completed. Thus, Henque was required to furnish SARS with a return indicating the profit that it had earned, as well as self-assess the tax liability arising from the said profit. The onus was on Henque to honestly and correctly assess its tax liability and pay over the amount that it believed that it owed to SARS.

(ii) That in terms of section 92 of the TA Act SARS was obliged to make an additional assessment if the original assessment 'does not reflect the correct application of a tax to the prejudice of SARS or the fiscus.' In this case, the original assessment was based solely on the return of Henque. Once the decision to conduct an audit of Henque's financial affairs was taken and conveyed to Henque on 29 November 2017, the likelihood of an additional assessment was no longer a theoretical possibility, it became real, and the Business Rescue Practitioner knew or ought to have known that Henque's tax liability for the 2017 year had yet to be determined.

(iii) That in terms of section 92 of TA Act, read with section 1 of the same Act, an 'additional assessment' was simply an assessment made by SARS in a circumstance where it was satisfied that an assessment did not reflect the correct application of a tax Act to the prejudice of SARS or the fiscus. Thus, an additional assessment was no more than a reconsideration of an assessment when SARS discovered that the assessment prejudiced it or the fiscus.

(iv) That we know from section 96 of TA Act that when SARS issues a notice of assessment, as it did in this case, it had to, amongst others, specify the amount to be paid, as well as the date for when payment was to be made. Reading section 5(1)(d) of the Income Tax Act in the context of sections 1, 92 and 96 of the TA Act, it was unquestionably clear that the income tax only became due and payable when the assessment or additional assessment was made and issued to the taxpayer.

(v) That section 96(1)(f) of the TA Act, as noted, provided that SARS must issue a notice of assessment which was to include 'the date for paying the amount assessed' and in this case the additional assessment was made on 4 April 2018 and issued to Henque on 1 May 2018. The notice of the additional assessment identified the 'due date' to be 1 May 2018 and the 'second date' to be 31 May 2018. The second date was the date by when it was to be paid. The amount assessed, thus, only became due and payable on 31 May 2018 and until then it was not a ‘debt.’ Thus, it constituted a post-commencement debt or finance in the parlance of the Companies Act 71 of 2008.

(vi) That based on the analysis of the various tax legislations and authorities referred to in the judgment, the court was unable to agree with Henque’s submission that in terms of section 5(1) of the Income Tax Act the liability for the income tax arose on 28 February 2017. The court held the view that Bekker CJ’s single sentence dictum concerning liability for income tax in Esselmann v Secretary of Finance 53 SATC 285 applied with equal force to our tax legislation.

(vii) That section 5(1) of the Income Tax Act only established ‘generally the liability’ but that in terms of the relevant provisions of the TA Act the tax became due and payable when the additional assessment was made. Only when it was quantified and became due and payable did it become a debt. The additional assessment constituted the important event that transformed a general liability into an actual one. Section 5(1) of the Income Tax Act had to be interpreted in the context of the other relevant legislation, i.e. the TA Act.

(viii) That, accordingly, the 2017 additional assessment was not a pre-business rescue debt and Henque’s call for declaratory relief holding otherwise had to be rejected.

Application dismissed with costs.

3.4. C:SARS v Medtronic International Trading SARL (86 SATC 158)

Medtronic International Trading SARL (Medtronic) was an international trading company with a distribution entity in South Africa which received its products for sale and distribution in South Africa exclusively from Medtronic which was registered with SARS as a vendor in terms of the VAT Act.

For many years it appeared that Medtronic had been a model of a compliant taxpayer in South Africa until its accountant had exploited weaknesses in both SARS and Medtronic’s accounting systems to perpetrate fraud and had, during the course of June 2004 and May 2017 embezzled an amount of R537 236 176 from Medtronic and she had achieved this by submitting false VAT 201 returns to SARS and she had sought reimbursements from SARS in order to conceal her embezzlement and eventually she was arrested on 13 December 2017 following investigations and forensic audits that had been conducted.

On the same day that their accountant was arrested, Medtronic applied to the SARS voluntary disclosure unit (the VDP Unit) for relief in terms of the Voluntary Disclosure Programme (VDP) provided for in sections 225–233 of the TA Act. Pursuant to the VDP, Medtronic fully disclosed its default to SARS and the reasons therefor and had contended that it was a victim as a result of its employee's conduct and had suffered a substantial loss.

Under the VDP a taxpayer in default may obtain relief from SARS, upon meeting the prescribed requirements and avoid prosecution and payment of penalties, where they make voluntary disclosure to SARS to purge their default.

Medtronic, during its VDP discussions with SARS, had requested that SARS waive the interest incurred as a result of its default of payment of VAT to SARS taking into account the circumstances in which the loss had occurred, but the VDP Unit, in its response, had stated that it was prepared to waive all understatement and late payment penalties but that it did not have authority to waive the interest arising from the underpayment of the VAT.

Medtronic elected to proceed under the VDP programme and on 18 June 2018 the parties concluded a written VDP agreement and according to this agreement Medtronic was liable for the payment of the capital VAT amount of R286 464 756.62 and interest in the amount of R171 205 356.12 but was granted 100% relief in respect of administrative non-compliance penalties and understatement penalties and all of these amounts were calculated with reference to the facts disclosed in the VDP application by Medtronic.

In addition, SARS was permitted, in terms of clause 7 of the agreement, to issue an assessment to give effect to the agreement.

Medtronic had duly paid over the capital VAT amount and the interest due to SARS who had agreed with Medtronic that it would grant Medtronic relief in respect of the understatement and administrative non-compliance penalties in the amount of R172 000 000 and, in addition, SARS would not pursue any criminal action for any of the offences in respect of the default.

However, on 12 October 2018, Medtronic's attorneys wrote to SARS and, without reference to the VDP Unit, requested SARS to remit the interest that it had levied on the capital tax representing the amount of default. This request was made in terms of the interest remission provisions located in section 39(7) of the VAT Act read with SARS Interpretation Note 61.

SARS' terse response was that remission of interest was not catered for in the VDP programme under the TA Act and, accordingly, it asserted that the provisions regarding remission of interest contained in section 39(7) of VAT Act and section 187(6) of the TA Act itself to the extent that they might be found to apply, found no application to VDP agreements.

From the perspective of SARS, Medtronic's request was considered still-born and therefore invalid.

Thereafter Medtronic wrote to SARS imploring the VDP Unit to withdraw the refusal to consider its earlier application for remission in terms of section 9(1) of the TA Act and this request too was refused by SARS.

Medtronic then approached the High Court (see Medtronic International Trading SARL v C:SARS 83 SATC 281) to review SARS' decision and the court a quo held that a request for remission of interest was not precluded in VDP's and that SARS had a statutory duty to consider and decide on such a request.

SARS' impugned decisions were set aside by the court a quo which led to SARS being subsequently granted leave to appeal to the Supreme Court of Appeal against the High Court's orders.

In short, the court a quo held that, in the absence of an explicit provision in the TA Act proscribing remission of interest upon a discharge by performance of a VDP agreement, it followed axiomatically that SARS was vested with powers to entertain requests for remission of interest and adjudicate them on their merits.

On appeal SARS submitted that the High Court erred in finding that the TA Act did not preclude it from considering the request for the remission of interest made in terms of section 39(7), in circumstances where Medtronic had entered a VDP agreement. In advancing this argument, SARS contended that, in requesting SARS to consider remitting the interest, Medtronic was in effect seeking to reduce its liability under the VDP agreement and renege on its undertaking to pay interest. This would constitute an amendment of the VDP agreement (which was precluded under the TA Act). There was no reference to relief in the form of a remission of interest under the TA Act and, accordingly, SARS further submitted, the VDP Unit had no authority to grant such remission nor any duty to consider the request, which it believed was invalid.

The crux of SARS' case was that when the TA Act came into effect, it 'gave rise to a permanent VDP relief statutory framework in respect of which interest is now excluded.' And that whilst section 39(7) of the VAT Act remained in force, it found no application in respect of interest on outstanding VAT dealt with in terms of Chapter 16, Part B, of the TA Act.

Medtronic submitted that this appeal, in essence, raised two issues to be determined.

- Firstly, whether Chapter 16, Part B and in particular sections 225 to 233 thereof 'prohibit the remission of interest under section 39(7) of the VAT Act once a VDP agreement has been concluded and fully implemented.'
- Secondly, whether notwithstanding the conclusion and implementation of a prior VDP agreement, SARS bore a statutory duty to consider and adjudicate a taxpayer's request for remission of interest that had accrued in respect of outstanding VAT under section 39(7) of the VAT Act.

Section 39(7)(a) of the VAT Act provided inter alia that where SARS is satisfied that the failure on the part of the person concerned or any other person under the control or acting on behalf of that person to make payment of the tax within the specified periods or on the specified date referred to for payment, as the case may be, was due to circumstances beyond the control of the said person, he or she may remit, in whole or in part, the interest payable in terms of the relevant section.

Judge Petse held the following in the majority judgment:

(i) at the issue with which the court was confronted in this matter involved an interpretive exercise. Accordingly, the court proposed dealing first with the law relating to statutory interpretation. There was a notable line of cases both in the Supreme Court of Appeal and the Constitutional Court which extensively dealt with statutory interpretation and the relevant principles were usefully summarised most recently by the Constitutional Court in Minister of Police and Others v Fidelity Security Services (Pty) Ltd 2022 (2) SACR 519 (CC) at para [34].

(ii) That the dispute between the protagonists could be resolved on a narrow basis. The core issue for present purposes hinged around the question whether SARS could lawfully refuse to even consider the request for remission and to thereafter take a decision in respect thereof. In this regard it bore mentioning that Medtronic relied on various grounds of review under PAJA, but the main focus was on section 6(2)(g) read with sections 6(3) and 8(2) of PAJA that regulated reviews where the administrator failed to take a decision.

(iii) That it would be recalled that SARS steadfastly refused to even entertain Medtronic's application for remission of interest and, as a result, did not consider and determine the application on its merits. This then raised the question as to whether SARS could lawfully do so. The answer to this question was not far to seek. It could be sourced from section 33 of the Constitution and PAJA, the latter being the legislative measure contemplated in section 33 of the Constitution. In its Preamble, PAJA provided that it sought to give effect 'to the right to administrative action that is lawful, reasonable and procedurally fair…as contemplated in section 33 of the Constitution…'

(iv) That, tellingly, section 33(3)(b) of the Constitution imposed a duty on the State in all its manifestations to give effect to the rights in sections 33(1) and 33(2) of the Constitution. Accordingly, SARS' refusal to consider and determine Medtronic's request altogether undermined one of the fundamental rights entrenched in the Bill of Rights which is the bedrock of our democratic order. Such conduct was inimical to the constitutional duty that SARS bore as an organ of state in terms of which it must respect, protect, promote and fulfil the rights in the Bill of Rights as decreed in section 7(1), 7(2) and section 8(1) of the Constitution.

(v) That, for now, all the court was called upon to decide was whether SARS was justified in law to refuse to even consider Medtronic's request by virtue of such request having been made subsequent to the conclusion and implementation of the parties' VDP agreement.

(vi) That, in sum, the conclusion reached was that SARS bore a statutory duty buttressed by the Constitution to, at the very least, give consideration to the request and decide it on its own merits and this SARS irrefutably refused to do. In these circumstances a review under section 6(2)(g) read with sections 6(3) and 8(2) of PAJA was warranted.

(vii) That the overbreadth of counsel's contentions to the contrary and the resultant violence it did to the plain and unambiguous language of section 39(7) of the VAT Act was self-evident. Nowhere did the VAT Act nor the TA Act provide expressly or by necessary implication that a taxpayer (a vendor in the context of this case) who had entered an agreement under the voluntary disclosure programme was excluded from the benefit for which section 39(7) provided and, in particular, when such an agreement had been discharged through performance of the contractual obligations undertaken in terms of the contract.

(viii) That it should never be lost from sight that this case is primarily concerned with statutory interpretation. The proper approach to statutory interpretation had already been restated in par. [33] of this judgment. Therefore, it suffices to reiterate that what the court was confronted with in this appeal was the narrow issue of whether SARS was justified in steadfastly refusing to entertain the request for remission of interest altogether for the reasons it had advanced.

(ix) That, to sum up, the court was of the view that, at the very least, SARS was required to entertain the application for remission and to consider and adjudicate it on its merits. The question whether remission of interest should be allowed and, if so, to what extent, did not arise in this appeal. In any event, even if it did, deciding that issue would not be in the court's remit.

(x) That the final issue to consider was whether this court should itself do what SARS should have done, namely, consider the application on its merits and then adjudicate it, but obstinately refused to do. The court thought not. PAJA contemplated that a court reviewing and setting aside a decision of an administrator must, as a general rule, remit the matter to the decision-maker for reconsideration. This is the default position. Only if the reviewing court is of the view that exceptional circumstances exist will it, itself, substitute its own decision for that of the decision-maker. But the reviewing court can exercise this power only when it is just and equitable for the court to do so. This, the reviewing court will do if, in its opinion, it is in as good a position as the administrator to make the call or the decision of the administrator is a foregone conclusion. Other than that, judicial deference and the doctrine of separation of powers must predominate.

Appeal dismissed with costs, including the costs of two counsel.

Minority judgment:

(i) That the main judgment correctly observed that Part B of Chapter 16 of the TA Act does not contain a provision that a taxpayer is not entitled to seek a remission of interest in addition to the relief provided for in section 229 of the TA Act. It held that, in the absence of such provision, SARS was not entitled to refuse to consider the application made by Medtronic after the conclusion of the voluntary disclosure agreement and was thus obliged to consider it.

(ii) This approach did not take account of the purpose of section 230 of the TA Act, as well as the nature and effect of a voluntary disclosure agreement. In every instance in which a liability to pay a tax debt is established, other than in the case of a voluntary disclosure, the amount of the tax debt is determined and the tax debt becomes due and payable upon assessment.

(iii) That it was not open to a court to ignore the conclusion of a voluntary disclosure agreement. The agreement is the centrepiece of the voluntary disclosure programme, and it served as a basis upon which outstanding tax may be recovered in exchange for a waiver of punitive sanctions. The conclusion of the agreement is the culmination of a process of engagement between the taxpayer and SARS.

(iv) That in this case the VDA records, in clause 11, that it is the whole agreement. It records that no variation to any part of the agreement (which plainly includes the part that stipulates the amount of the tax debt) has any effect unless reduced to writing and signed by both parties. It also records that the agreement constitutes a legal, valid, binding and enforceable agreement on the parties.

(v) That it is a well-established principle of our law of contract that due and proper recognition is given to the bargain struck between contracting parties. A party who agrees to payment of a debt cannot escape the obligation unless the agreement was induced by misrepresentation, error or fraud or some other recognised ground of repudiation and no such instances were alleged or established.

(vi) That in this case the conclusion of the voluntary disclosure agreement established the liability for the payment of the agreed tax debt and no basis was advanced to suggest that the agreement was concluded in circumstances which would render it unenforceable. Nor was it suggested that the amount of the interest included in the tax debt occurred under reservation of rights.

(vii) That the provisions of Part B of Chapter 16 of the TA Act, properly interpreted, do not permit a taxpayer who has entered a voluntary disclosure agreement to seek a remission of interest, the amount of which was incorporated in the determined tax debt due, after the conclusion of the voluntary disclosure agreement. To hold otherwise would undermine the legal consequences that attach to the conclusion of such an agreement.

(viii) That in regard to the interplay between an application for voluntary disclosure relief and a request for remission of interest in terms of section 39(7) of the VAT Act or section 187(5) of the TA Act, they were separate forms of relief that a taxpayer may seek. Different criteria and considerations apply to each relief. The procedures may even be administered by separate units or sub-departments within SARS. None of this, however, alters the fact that the voluntary disclosure procedure involved the determination of a tax debt payable in consequence of a default and that determination necessarily includes the 'capital' of the outstanding tax and the interest payable in relation thereto. The voluntary disclosure agreement is an agreement to pay the mutually agreed tax debt, in exchange for indemnity from punitive sanctions that would ordinarily apply.

(ix) That the provisions relating to the voluntary disclosure programme do not exclude consideration of remission of interest prior to determination of the tax debt. In this instance Medtronic did not pursue such relief and it was not open to it to do so after it had concluded the agreement and SARS therefore correctly refused to consider its request for remission of interest.

3.5. C:SARS v ABSA Bank Ltd (86 SATC 195)

First Respondent, Absa Bank Ltd (Absa), and its wholly owned subsidiary, Second Respondent, United Towers (Pty)Ltd (United Towers), had entered an investment arrangement which involved a series of interlinked transactions, the details of which were as follows.

Absa and United Towers had subscribed for preference shares in PSIC Finance 3 (Pty) Ltd (PSIC3), their investment having been secured by other entities in the 'group'. PSIC3 used the proceeds of the share issue to subscribe for preference shares in PSIC Finance 4 (Pty) Ltd (PSIC4) and in turn PSIC4 made a capital contribution to Delta 1 Finance Trust (D1 Trust).

The D1 Trust applied the capital contribution to make interest-bearing loans to Macquarie Securities South Africa Ltd (Macquarie). The D1 Trust invested the interest earned on the Macquarie loans in Brazilian Government Bonds, which in terms of the Double Taxation Agreement between South Africa and Brazil, provided a tax-free income stream to the D1 Trust. The D1 Trust distributed the income stream to PSIC4.

The latter paid this to PSIC3 as dividends, and PSIC3 in turn paid dividends to Absa and United Towers.

SARS had initiated an investigation of the Macquarie Group investment scheme during 2016 and, pursuant to this investigation, it sought and obtained information from Absa and United Towers.

SARS, in May 2018, issued notices to Absa and United Towers in terms of section 42 of the Tax Administration Act (the TA Act), signifying an audit of their tax affairs for the 2015, 2016 and 2017 years of assessment. These notices stated that the audit would relate to the tax treatment of the dividends received by Absa and United Towers from PSIC3.

SARS, on 30 November 2018, issued notices to Absa and United Towers in terms of section 80J of the IT Act and the notices were, essentially, in identical terms. They indicated that SARS had completed its preliminary audit of the arrangement entered with entities in the Macquarie 'group.' The notices set out an intention to raise assessments in terms of the General Anti-Avoidance Rule (GAAR) provisions of the IT Act and Absa and United Towers were afforded a period of 60 days to respond to the preliminary audit findings.

Absa and United Towers, on 15 February 2019, had submitted a request to SARS, in terms of section 9(1) of the TA Act, to withdraw the section 80J notices. On 5 March 2019 SARS informed Absa and United Towers that it was not withdrawing the section 80J notices and it stated that any objections they had to the notices should be raised in submissions made in their responses to those notices, as required by section 80J.

On 29 March 2019 Absa and United Towers launched an application in the High Court seeking an order reviewing the decision not to withdraw the section 80J notices and directing that the decision be substituted with one withdrawing the notices, alternatively that the request for withdrawal be remitted to SARS (the section 9 review). They simultaneously submitted their responses to the section 80J notices to SARS in terms of section 80J(2) of the IT Act and the section 9 review proceedings continued while SARS was considering the responses to the section 80J notices.

On 17 October 2019 SARS issued Letters of Assessment and Additional Assessments to Absa and United Towers for the 2014, 2015, 2016 and 2017 tax years. It determined that they had participated in an avoidance arrangement and assessed their tax liability on the basis that their investment returns in the scheme constituted taxable income.

After these additional assessments were raised by SARS, Absa and United Towers applied for leave to amend the notice of motion in the section 9 review, to extend its reach to include the review and setting aside of the additional assessments (the assessment review). This application was opposed but leave was granted, and the application was broadened to include the assessment review.

The application was heard by the High Court (see Absa Bank Ltd and Another v C:SARS 83 SATC 401 per Sutherland ADJP) which granted orders setting aside the decisions not to withdraw the section 80J notices; withdrawing the section 80J notices; and setting aside the additional assessments.

The High Court concluded that the decisions refusing to withdraw the section 80J notices were subject to review based on the principle of legality notwithstanding that they were not final. It held, in relation to the assessment review, that a taxpayer was not obliged only to pursue the remedies for disputing tax liability as provided by section 104 of the TA Act. The taxpayer may apply directly to court for relief in exceptional circumstances. Exceptional circumstances would include a dispute that turned wholly upon a point of law.

The High Court found that the section 80J notices were premised upon an acceptance that Absa and United Towers were ignorant of the terms of the arrangement or scheme. Upon that premise they could not be parties to the avoidance arrangement. It held further, that since the notices of assessment were issued upon the factual premise of the section 80J notices, the assessments were tainted by an error of law and the High Court concluded that the section 80J notices and the assessments were inextricably linked and, accordingly, set aside both sets of decisions.

On appeal to the Supreme Court of Appeal the issues concerned two distinct review applications in a composite notice of motion. The first related to the refusal or failure to withdraw the section 80J notices upon a request made in terms of section 9 of the TA Act. It was founded upon the contention that SARS was wrong in its view that the objections to the section 80J notices raised by Absa and United Towers, should be addressed in their responses to the notices. It was also contended that the principle of legality was breached since the issuing of the notices was based upon an error of law. The error was that Absa and United Towers were parties to an avoidance arrangement even though they had no knowledge of the arrangement and had derived a tax benefit from it, to which they would otherwise not have been entitled.

The second review concerned the additional tax assessments raised by SARS. This review engaged the exercise of the High Court's review jurisdiction to set aside the assessments either under the Promotion of Administrative Justice Act (PAJA) or the principle of legality. It was founded upon the same grounds as the attack on the section 80J notices.

The following issues arose in relation to these two reviews:

- Is a 'decision' not to withdraw a section 80J notice reviewable in terms of section 9 of the TA Act, either prior to or after the issuing of a notice of assessment in terms of section 80B of the IT Act?
- Was the High Court correct to characterise the challenge to the assessments as wholly a question of law which entitled it to exercise its jurisdiction in terms of section 105 of the TA Act?
- Was the High Court correct in its determination of the dispute?

Judge Goosen held the following:

<u>As to the GAAR provisions</u>

(i) That tax avoidance, whether in part or in whole, was not per se unlawful or impermissible. Sections 80A to 80L of the IT Act dealt with arrangements entered by a taxpayer which had the effect of conferring a tax benefit through the avoidance of a tax liability that would otherwise accrue. These anti-avoidance provisions confer upon SARS the authority to investigate the transactions and to raise additional or compensatory assessments to counteract the consequences of such avoidance schemes or arrangements.

(ii) That section 80B allowed SARS to determine the tax consequences of any impermissible avoidance arrangement. This was done by making compensating adjustments to assessments to ensure consistent treatment of all parties to the arrangement.

(iii) That section 80G(1) provided that an avoidance arrangement was presumed to have been entered or carried out for the sole or main purpose of obtaining a tax benefit. A party obtaining a tax benefit was required to prove that, in the light of the relevant facts and circumstances, obtaining a tax benefit was not the sole or main purpose of the avoidance arrangement. Subsection (2) provided that the purpose of a step in or part of an avoidance arrangement may be different from a purpose attributable to the arrangement as a whole. In terms of section 80H, SARS may apply the GAAR provisions to steps in or parts of an arrangement.

<u>As to the section 9 review</u>

(iv) That section 9(1) of the TA Act served to describe discretionary powers which may be exercised by SARS officials. It contained an internal limiter. Decisions ‘given effect to in an assessment’ may not be withdrawn. So too, a notice of assessment that was subject to objection and appeal. The High Court ventured a construction of the first category as relating to ‘assessments already given effect to.’ There was no need to interpret this section. It was common cause that section 9 contemplated the withdrawal of a notice such as one issued under section 80J. Indeed, section 80J(3) provided explicitly that such notice may be withdrawn upon consideration of the taxpayer’s response to the section 80J notice.

(v) That the review of the refusal to withdraw the section 80J notices was launched simultaneously with the submission of responses to the notices and some months prior to the letters and notices of assessment issued in terms of section 80B of the IT Act. The application was founded upon two grounds. The first was that SARS’ contention that the objection to the notices ought to be raised in the responses to the notices was wrong in law. It was averred that this approach impermissibly limited the ambit of section 9 and that it denied a taxpayer a remedy which was available to it. The second was that disagreement about the interpretation and application of GAAR perpetuated the error of law in the issuing of the notices. Absa and United Towers contended that since the notices would have adverse effect irrespective of the issuing of assessments, the decision not to withdraw them was reviewable.

(vi) That the High Court accepted, correctly in the view of the court, that the decision to issue a section 80J notice was not a ‘final’ decision which placed any adverse burden upon the recipient. It was, the High Court held, plainly not administrative action as contemplated by PAJA. The High Court, however, found that a decision not to withdraw a notice, even if not final, had adverse consequences. It held that such a decision ‘was plainly a decision by an organ of state exercising a statutory power and its notional non-final attribute was not a bar to a review precisely because it nevertheless had an impact.’

(vii) That the circumstances of this matter were wholly different to those in C:SARS v Langholm Farms(Pty)Ltd 82 SATC 135 and C:SARS v United Manganese of Kalahari(Pty)Ltd 82 SATC 444. In this case the court was concerned with a decision not to withdraw a notice and the question was what effect or impact the decision had upon the taxpayer concerned?

(viii) That the short answer it seemed was that such decision itself could have no adverse impact or affect. Its effect was to leave the section 80J notice in place until the process contemplated by the section was completed. If the issuing of a notice did not constitute administrative action susceptible to review then, as a matter of logic, a decision to keep it extant could not constitute administrative action.

(ix) That section 80J(3) sets out the powers and obligations of SARS in relation to the application of the GAAR provisions. Section 80J(3) did not contemplate a separate decision not to withdraw the notice as a precondition for the decision to determine a tax liability under section 80B. The statutory power exercised by SARS was to determine a tax liability under the GAAR provisions. Until that determination was made the issuing of a section 80J notice or a refusal to withdraw it, could have no adverse effect or impact. These steps were not reviewable. These steps were not reviewable and the High Court had lost sight of the provisions of section 80J(3). It ought to have found that a decision not to withdraw the notice was not subject to review outside of a challenge to the decision to impose a tax liability pursuant to section 80B of the IT Act.

(x) That it was not necessary to decide the ambit of section 9 of the TA Act and to address the 'jurisprudential bristles' to which the High Court had referred. As had been stated, accepting for the sake of argument that the section 9 review was competent, was, on the facts of this case, entirely academic. Furthermore, for reasons still to be set out below, the substantive basis of the review of both the refusal to withdraw the notices and the assessments was flawed, and the orders made in relation to the section 9 review could not stand.

<u>As to the assessment review</u>

(xi) That two questions arose regarding the assessment review: Was the High Court correct to characterise the dispute as wholly a question of law, and therefore exercise jurisdiction in terms of section 105 of the TA Act? A negative answer was dispositive of the appeal since the High Court then did not have jurisdiction to review the assessments. The second question, namely whether the High Court was correct in its findings on the substantive review, only arose if the first question was answered affirmatively.

(xii) That the High Court had recognised that it could only exercise its jurisdiction in exceptional circumstances, and it considered that a dispute concerning a question of law would constitute an exceptional circumstance entitling it to exercise its jurisdiction. It held that the dispute regarding the refusal to withdraw the section 80J notices and the legality of the assessments, involved a question of law and, for this reason, it had exercised its discretion to adjudicate the dispute.

(xiii) That the Supreme Court of Appeal in C:SARS v Rappa Resources- (Pty) Ltd 85 SATC 517 had endorsed the High Court's approach to the exceptional exercise of its jurisdiction in terms of section 105 of the TA Act but the question was whether the High Court was correct in its characterisation of the nature of the dispute.

(xiv) That the High Court took the view that the section 80J notices and the assessments were 'inextricably linked'. It stated that the factual basis upon which SARS had decided to apply the GAAR provisions was set out in the notices. It held that SARS had accepted the facts disclosed in the notices. On this basis, the High Court had held that SARS did not dispute that Absa and United Towers had no knowledge of the arrangement in which they had participated. They could therefore not have been parties to an arrangement which, unknown to them, had sought to avoid the payment of tax which they would otherwise have been required to pay. The High Court therefore found that the application of the GAAR provisions in circumstances where they did not, as matter of fact, apply, was irrational and offended the principle of legality and that neither the assessments nor the section 80J notices could stand.

(xv) That the High Court's finding that SARS had accepted the facts as stated by Absa and United Towers, and in particular, their assertion that they had no knowledge of the nature and ambit of the scheme or arrangement, was incorrect. The section 80J notices did not state that SARS accepted the claim that Absa and United Towers had no knowledge of the full ambit of the scheme. The notices had set out reasons for the belief that the GAAR provisions applied, no more. They were not statements of the accepted factual basis for application of the GAAR provisions. The correspondence relating to the section 80J notices pertinently stated that SARS disputed the contentions raised by Absa and United Towers. These statements form part of the reasons given by SARS as to why it would not withdraw the section 80J notices. These averments were set out in the answering affidavits filed in opposition to the section 9 review. These affidavits were filed prior to the issuing of the notices of assessment which were the subject of the assessment review. There was accordingly no room for the conclusion that SARS accepted that Absa and United Towers were not parties to the avoidance arrangement and in the light of this the application of the GAAR provisions was not solely a question of law.

(xvi) That on the common cause facts Absa and United Towers participated in steps forming part of an 'arrangement', the full ambit of which was described in the section 80J notices. Whether they had knowledge of the full nature of the transactions which comprised the arrangement, and whether their sole or main purpose in participating was to secure a tax benefit, were matters of disputed fact. Whether the 'arrangement' constituted an 'impermissible avoidance arrangement' was a factual enquiry. The same was true in respect of the 'tax benefit' requirement. Whether Absa and United Towers had obtained a tax benefit by avoiding an anticipated tax liability that might otherwise have accrued from the transactions, was a question of fact and it was not a mere question of law, determinable upon the basis of the assessment as framed by SARS.

(xvii) That the High Court had predicated its finding that it had jurisdiction to review the assessments on the basis that the challenge to the assessments had involved solely a question of law. That was incorrect. Since the dispute did not involve solely a question of law, no exceptional circumstances existed to justify the High Court assuming jurisdiction in the matter.

(xviii) That it followed that in relation to the assessment review, the High Court did not have the required jurisdiction to deal with the matter and the High Court ought therefore to have dismissed the application.

(xix) That the merits of any challenge to the notices of assessment must be adjudicated in accordance with the dispute resolution process provided by section 104 of the TA Act.

Appeal upheld with costs, including the costs of two counsel.

3.6. Lance Dickson Construction CC v C:SARS (84 SATC 209)

Lance Dickson Construction CC (Lance Dickson) traded in properties and building work, had concluded a written sale agreement ('the agreement') with a purchaser in terms of which it sold to the latter an immovable property for R25.2 million including VAT.

At the time of the sale the property consisted of a piece of land with development rights for subdivision into 72 erven and the agreement provided that the purchase price was payable in tranches of R350 000 '…on transfer of each erf to the end user purchaser' from the purchaser.

Registration of transfer to the purchaser was subsequently effected on 27 October 2016.

The agreement was thus concluded, and transfer of the property was effected during Lance Dickson's 2017 year of assessment.

However, Lance Dickson did not declare the capital gain of the sale proceeds in its 2017 income tax return since it was of the view that the capital gain on the sale would only accrue to it on transfer of the individual erven to third party end users.

SARS conducted an internal audit on Lance Dickson and included the full capital gain on the sale proceeds in Lance Dickson's taxable income for the 2017 year of assessment in terms of section 26A of the Income Tax Act.

SARS accordingly issued an additional assessment on 29 March 2018, in which, *inter alia*, it had imposed a 25% USP of R798 372 in terms of section 222 as read with section 223 of the TA Act.

SARS in its Rule 31 Statement stated that the omission of the proceeds of R22 105 263 (vat excluded) from the disposal of an asset in Lance Dickson's income tax return for the 2017 year of assessment for capital gains purposes, resulted in a loss to the prejudice of the fiscus, rendering Lance Dickson liable for the payment of an USP at the rate of 25% for a behaviour category of 'reasonable care not taken in completing a return' on a standard case imposed in terms of section 222 read with section 223 of TA Act.

Lance Dickson, having been dissatisfied with SARS' determination, lodged an objection under section 104 of TA Act which objection eventually found its way via the Tax Board to the Cape Town Tax Court (see ITC 1949 (2021) 84 SATC 129) which upheld SARS' determination.

Lance Dickson then appealed to a Full Bench of the Western Cape High Court, with the leave of the Tax Court, where the issue was whether the conclusion arrived at by the Tax Court was correct, i.e. whether SARS had correctly categorized the understatement as being the result of 'reasonable care not taken in completing a return'.

The Tax Court had accepted that SARS had unequivocally sought to levy the penalty because of Lance Dickson's failure to take reasonable care in the completion of its tax return and that it was bound by that determination.

Lance Dickson contended on appeal that it had not acted unreasonably in adopting the tax position that it had and it was further its contention that any 'understatement' did not arise from its return completion process and therefore that the imposition of an USP on the basis of 'reasonable care not taken in completing return' was inappropriate and, rather, if an 'understatement' was present, it arose from the tax position taken by Lance Dickson and therefore SARS had identified the incorrect behaviour against which it had applied the USP. Moreover, Lance Dickson's calculation of its tax liability could not be unreasonable solely due thereto that it had interpreted the time of disposal and time of accrual rules in a manner different to SARS.

Lance Dickson further submitted that its position had been confirmed by independent expert opinion which was further support therefor that its 'tax position adopted was in fact reasonable.'

SARS contended that reasonable care required the taxpayer to take the same care in fulfilling his tax obligations that could be expected of a reasonable ordinary person in the same position.

Reasonableness required the taxpayer to have known that the sale of the property on 26 September 2016 and the subsequent registration on 27 October 2016 was a disposal event that triggered proceeds that accrued to the taxpayer during the 2017 year of assessment and, consequently, Lance Dickson's failures to make such declarations were actions that fell below the standard of a reasonable person in similar circumstances.

Judge Gamble held the following:

(i) That in circumstances where an alleged understatement of tax has occurred, a three-phase process was contemplated by the Legislature. Firstly, SARS must consider whether the understatement constituted an 'understatement' as defined in section 221 of the Tax Administration Act. If it does, SARS must then consider whether the understatement resulted from a 'bona fide inadvertent error.' If such an error is established, that is the end of the inquiry, and no USP may be levied. However, where there is no such error, SARS is then required to identify the appropriate behavioural category under which the taxpayer's conduct allegedly resorts in terms of the table set out in section 223 before it could impose a penalty.

(ii) That in the instant case SARS elected to levy a penalty of 25% under Item (ii) of the table because it held the view that Lance Dickson's understatement resulted from it not having taken reasonable care in the completion of its 2017 tax return in that it had not declared the proceeds of R22 105 263 for capital gains tax purposes. In terms of section 102(2) of the Tax Administration Act, SARS attracted the onus to justify its imposition of the relevant penalty, i.e. 25% under Item (ii) in the table.

(iii) That the essence of the dispute between the parties was whether SARS had correctly categorized the appropriate behavioural category in respect of Lance Dickson's conduct, as being the result of 'reasonable care not taken in completing a return' and in that regard the court considered the evidence adduced before the court a quo, i.e. the Tax Court, where SARS had relied on the viva voce evidence of Ms Marothodi, a risk profiler in its Specialist Audit Division, who was tasked with investigating Lance Dickson's 2017 tax return after it was referred to her by an operational manager at SARS.

(iv) That the court observed that Ms Marothodi eventually accepted that she had chosen the wrong behavioural category in assessing the USP. She vacillated between contending that the behaviour of Lance Dickson was unreasonable in failing to include the CGT figure in the 2017 tax return to unreasonable in relation to the basis for the tax position it claimed to have taken and eventually she conceded that SARS had erred in imposing a 25% penalty because of the Item (ii) behaviour that it had relied on.

(v) That the evidence clearly demonstrated that the witness manifestly did not understand the difference between the behaviour categorised in Items (ii) and (iii). In the light of the damaging concession made by SARS' only witness, Lance Dickson astutely closed its case without calling any witnesses.

(vi) That if SARS elected to impose a 25% USP under Item (ii), it was required to prove the factual basis therefor when its determination was challenged by Lance Dickson in the Tax Court. It was common cause that SARS did not do so, and in the circumstances, there was no basis, either in fact or law, for it to recover that penalty from Lance Dickson and it followed that the Tax Court was wrong in confirming the USP of 25%.

(vii) That SARS' prerogative to impose an USP was closely circumscribed by the provisions of sections 222 and 223 of the TA Act and, importantly, it must be borne in mind that that prerogative only came into consideration if it had been established by SARS that the understatement was not occasioned by a bona fide error on the part of the taxpayer.

(viii) That the non-applicability of the bona fide error proviso in section 222(1) of the TA Act was not in dispute in this case. But that did not entitle SARS to then impose any penalty it considered applicable. Section 222(2) carefully circumscribed the powers of SARS and it followed that if, for example, SARS finds that there has been an understatement based on the taxpayer's failure to take reasonable care in completing its return, it must impose the 25% penalty: it does not have any discretion to lower the percentage. Similarly, if the behaviour category relied on by SARS is the absence of reasonable grounds for the tax position taken, it must impose a 50% penalty. There is thus no statutory basis to impose a 25% penalty in respect of behaviour falling within the ambit of item (iii).

(ix) That what happened in this matter was that the Tax Court found that SARS was bound by the concession made by its witness under cross-examination and that it had thus failed to establish the factual basis for imposing the Item (ii) penalty of 25%. The Tax Court went further and found that there was no basis for it to consider whether the Item (iii) penalty of 50% had been established because this was not the case pleaded by SARS and, notwithstanding, it sustained the claim by SARS for a 25% penalty.

(x) That, in the court's view, there was no statutory basis for such a finding by the Tax Court. Once SARS had failed in its bid to discharge the onus of proving the Item (ii) penalty for which it had contended and which buttressed the case the taxpayer came to meet, that was the end of the case. In finding that SARS was entitled to retain the penalty which it had failed to prove, the Tax Court effectively deprived the taxpayer of answering a case it was not called upon to meet. Aside from the manifest unfairness of such an approach, the Tax Court, being a creature of statute bound by the limits of its jurisdiction, was not permitted to make such an order under section 129(3) of the Tax Administration Act where the confirmation of an USP is dependent on SARS discharging its burden of proof.

(xi) That, in the result, it must be concluded that the Tax Court had erred in confirming the USP and that Lance Dickson's appeal to the High Court should be upheld.

(xii) That, further, in the circumstances, the court was satisfied that Lance Dickson had established that SARS' decision to fix and impose an USP of 25% under Item (ii) was unreasonable in the circumstances and that it would be just and equitable to order it to pay Lance Dickson's costs in the Tax Court and in terms of section 130(2) of the Act, such costs were taxable on the High Court scale.

Appeal upheld with costs.

3.7. ITC 1970 (84 SATC 225)

The taxpayer, up to and until 3 September 2017, was a 'resident' of South Africa for tax purposes and prior to that date she and her father were members (holding one-third and two-third undivided shares respectively) of a partnership that owned and operated a passenger aircraft for charter purposes.

The partnership, which traded under the name and style of 'Tri-Air Aviation Partnership', was formed under and in terms of South African law. It ran a charter business using a passenger aircraft and the charter business or trade operated in and from the UK. The aircraft was not registered to operate in South Africa and did not do so as it was registered and based in the UK where the business' offices were also situated.

SARS accepted that the trade of the partnership, in which the taxpayer was a one third partner, had a 'permanent establishment' in the UK as defined in section 1 of the Income Tax Act, to which the aircraft was effectively connected.

For South African tax purposes the partnership was governed by section 24H of the Income Tax Act and that section rendered a South African partnership 'tax transparent' which, in effect, meant that the partnership was thus not assessed as a taxpayer in its own right and the taxpayer, as a partner, earned her proportionate share of the partnership gross income and was also entitled to claim a proportionate share of the partnership deductions and allowances and she was taxable directly on her proportionate share of the taxable income.

The taxpayer was not subject to income tax on the air charter business in the UK because, by virtue of Article 8(1) of the double tax treaty between South Africa and the

UK, the profits of an enterprise of a Contracting State from the operation of ships or aircraft in international traffic were taxable only in that State. Since the aircraft was an enterprise of the taxpayer and thus an enterprise of South Africa, and flew only inter-continentally, the UK had no taxing rights over the air charter trade and only South Africa had the right to tax the profits, a right which was exercised since the inception of the partnership.

The taxpayer had accordingly claimed, as deductions in prior years, a proportionate share of capital allowances, namely depreciation, permitted in relation to the aircraft under section 12C of the Income Tax Act. These deductions on an annual basis were in fact a claim annually of 20% on the cost of the aircraft. She had also deducted a proportionate share of other expenses of the air charter trade.

The said deductions resulted in the partnership trade suffering losses for South African tax purposes in prior years, i.e. the deductions allowed exceeded the partnership's gross income, giving rise to 'assessed losses' for the partnership.

The partnership losses were however not permitted to be set off against the taxpayer's other (non-partnership) South African income in the years preceding her 2018 year of assessment and, instead, they were carried forward as foreign assessed losses. This disallowance of the partnership losses was in accordance with proviso (b) to section 20(1) of the Income Tax Act. The assessed losses in the partnership commenced from 1 March 2014 and continued until 28 February 2017 and the partnership losses fell within the ambit of sub-para (b)(ii) of the proviso in that they were incurred in carrying on the air charter trade outside South Africa.

The taxpayer, because these losses could not be claimed against her South African income, at the end of the 2017 year of assessment (28 February 2017), carried forward to the 2018 year a cumulative foreign assessed loss arising out of the air charter trade of R62 596 925.

The taxpayer, on 3 September 2017, moved permanently to the UK and ceased to be a 'resident' for purposes of South African income tax. This gave rise to certain automatic tax consequences and one of these was that, by operation of section 9H(2) of the Income Tax Act, the taxpayer was treated as having disposed of all of her assets (other than immovable property in South Africa and certain other assets not relevant here) to a person that was a resident of South Africa on the date immediately before the day on which she ceased to be a resident, that being on 2 September 2017, for an amount received or accrued equal to the market value of the asset on that date.

The taxpayer was thus deemed inter alia to have disposed of her one-third share of the aircraft on 2 September 2017, at its market value.

The aforesaid deemed disposal, despite being of a capital nature, gave rise to a recoupment under section 8(4)(a) of the Income Tax Act. It was agreed upon between the parties that the amount that was 'recouped' arising from the deemed disposal of the taxpayer's one-third share of the aircraft was R67 995 951 and this amount was included in the taxpayer's income for the 2018 year of assessment which was the tax year that ended on the date prior to her emigration, i.e. 2 September 2017.

The taxpayer however claimed, as a deduction against what she alleged was her foreign income in that year, the amount of the carried-forward foreign assessed loss of R62 596 925.

The taxpayer's aforesaid claim was made on the basis that proviso(b)(ii) to section 20(1) of the Act did not disqualify the deduction and that she was entitled to set off, against her foreign trade income (i.e. the recoupment), the brought forward assessed loss of R62 296 925 arising from that self-same foreign trade in prior years.

SARS, in his additional assessment for the 2018 year of assessment, did not take into account the deduction of R62 296 925 being the assessed loss brought forward from the 2017 tax year and the taxpayer contended that she was accordingly taxed on an income substantially more than what she believed the total amount of her income for that year to have been.

Moreover, SARS, by wrongly disallowing the set-off claimed, had subjected the taxpayer to income tax on the full amount of the recoupment, being R67 995 991, rather than on only R5 699 066 thereof, being the net amount after set-off of the assessed loss.

The fundamental issue in dispute in this appeal was whether the taxpayer may, in terms of section 20(1) of the Income Tax Act, set off the balance of the foreign assessed loss from an aircraft partnership trade, as carried forward to the 2018 tax year, against the income received by or accrued to her in the form of recoupments arising from the deemed disposal, under section 9H of the Act, of partnership assets used in the conduct of a foreign trade.

The dispute between the parties also turned on the source, for purposes of proviso (b)(ii) to section 20(1) of the Act, of the recoupment income included in the taxpayer's 2018 year of assessment arising from the deemed disposal of the aircraft.

Judge Adams held the following:

(i) That the adjudication of the aforesaid dispute between the parties required a proper interpretation of section 20(1) of the Income Tax Act as well as the erstwhile sub-para (n)(ii) of the definition of 'gross income' in section 1 of the Act.

(ii) That in terms of the general provisions of section 20(1) of the Income Tax Act, a taxpayer is entitled to set off against the income derived by him or her in a tax year any balance of assessed loss incurred by that person in any previous year carried forward from the preceding year of assessment. However, proviso (b)(ii) to section 20(1) prohibits the set-off of an assessed loss incurred in carrying on any trade outside South Africa against any amount 'derived by any person from a source within the Republic.' The effect of proviso (b) is therefore to 'ring-fence' foreign assessed losses, so that they cannot be set off against South African-sourced income.

(iii) That it was because of proviso (b) that the taxpayer had built up an unused foreign assessed loss from the air charter trade. She had not been permitted to set off that 'ring-fenced' assessed loss against her South African income. The 2018 year of assessment was, however, different as in that year she had foreign income in the form of the taxable recoupment which arose from the deemed foreign disposal of the aircraft on 2 September 2017.

(iv) That the question to be considered was whether from that income the taxpayer was allowed to set off the foreign assessed loss. The taxpayer contended that the income in the form of recoupment-which related exclusively to, and arose exclusively from, the deemed disposal of the aircraft that was central to her foreign trade – was not derived from a source within South Africa. On the contrary, the recoupment was positively an amount received or accrued from a source outside South Africa in terms of section 9(4)(d) of the Income Tax Act.

(v) That, on the other hand, SARS contended that the amount represented by the recoupment was derived from a source within South Africa and he relied for this conclusion exclusively on the erstwhile sub-para (n)(ii) of the definition of 'gross income' in section 1 of the Act. He contended that, in the case of any amount required to be included in the taxpayer's income in terms of section 8(4), which was the provision in terms of which the recoupment arising from the deemed disposal of the aircraft was included in the taxpayer's income, was deemed during 2017 to have been received or accrued from a source within

South Africa notwithstanding that such amounts may have been recovered or recouped outside South Africa and this was in terms of the then para (n)(ii) of the definition of ‘gross income’ in section 1 of the Act.

(vi) That the aforesaid sub-para n(ii) was an anti-avoidance provision aimed at supporting the source-based tax regime for ‘gross income.’ It was necessary because the mere fact that the taxpayer was a resident would not suffice to include the recoupment in ‘gross income’ if the asset was disposed of in a foreign jurisdiction. This paragraph would under the pre-2001 ‘source’ regime has had no impact on residents who conducted a foreign trade offshore, as they would not have claimed deductions or allowances for purposes of South African tax and so would also not have had taxable recoupments.

(vii) That section 9 of the Act was introduced during the residence-based tax regime – which was not the case with sub-para n(ii) and was made ‘applicable in respect of amounts received or accrued during years of assessment commencing on or after 1 January 2012. Section 9(2) provides that an amount is received by or accrues to a person from a source within South Africa in a number of defined circumstances. Section 9(4) goes on to provide that an amount is received by or accrues to a person from a source outside South Africa in a further number of defined circumstances as per sub-paras (a) to (e).

(viii) That the new section 9 was significant in that it was made necessary by a ‘paradigm shift’ in the legislation (i.e. the move from source to residence) and it was intended to restate a new ‘uniform set of source rules’ to remedy uncertainties and anomalies. Additionally, it eliminated the concept of ‘deemed source’ that had previously existed. The ‘deemed source’ language of sub-para (n)(ii) however remained on the statute book until 2019 when the provision was repealed in its entirety. It was apparent from the associated Explanatory Memorandum that this was because the provision was obsolete and served no useful purpose.

(ix) That, for all these reasons, the court was in agreement with the submissions made on behalf of the taxpayer relative to the issue as to whether sub-para (n)(ii) applied to the taxpayer. SARS’ argument that the said paragraph deemed the recoupment to be from a source in South Africa, was a literal and isolated interpretation, disregarding the context. Since the introduction of the residence-based regime with effect from 2001, the ‘gross income’ definition dealt separately with the basis of tax liability for residents and non-residents.

(x) That the sole operative effect of the now repealed sub-para (n)(ii) was to deem an amount to be from a South African source for purposes of the gross income definition, where the provision was located. Its scope of operation was thus naturally limited to income that fell within 'gross income' by virtue of its source, namely the income of non-residents only. The provision served no useful purpose, in the context of the 'gross income' definition, in relation to residents: the recoupment income automatically accrued to them as gross income by virtue of their status as residents.

(xi) That, accordingly, the court was of the view that sub-para (n)(ii) was of no application to the taxpayer's recoupment. Moreover, the deeming of source was not intended to apply outside the realm of the 'gross income' definition. It did not apply for all purposes of the Income Tax Act, such as section 8(4) of the Act.

(xii) That the taxpayer contended further that sub-para (n)(ii) was, in any event, of no force and effect in the light of other provisions of the Income Tax Act, notably section 9(4)(d) in terms of which the income in these circumstances was from a source outside South Africa.

(xiii) That since the recoupment proceeds accrued in respect of the disposal of an asset that was not from a source within South Africa in terms of ss 9(2)(j) or (k), section 9(4)(d) positively identified the amount as having been received or accrued 'from a source outside the Republic.' For that reason, proviso (b) to section 20(1) of the Income Tax Act did not apply to disqualify the set-off of an assessed loss against the recoupment income.

(xiv) That this then meant that, if regard is had to section 9(4)(d), the taxpayer should have been allowed the deduction. Conversely, on the basis of para (n)(ii), the deduction was rightly disallowed by SARS. The question was whether section 9(4)(d) prevailed over para (n)(ii) or vice versa. How then was this irreconcilable inconsistency between the two provisions to be resolved?

(xv) That para n(ii) was the earlier provision as section 9(4)(d) was introduced many years later, and expressly applied to all receipts and accruals of a taxpayer from 2012 onwards. The general rule of statutory interpretation in this context indicated that the provisions of section 9(4)(d) should in the court's view prevail. There were also clear indications that the new section 9 provisions relating to source rendered para n(ii) to be obsolete and ineffectual.

(xvi) That, accordingly, the provisions of para n(ii) were merely remnants of a bygone era, superseded by a new manner of regulating the actual source income and allowed to remain in the Income Tax Act by way of a legislative oversight. The introduction of the comprehensive new source regime rendered them superfluous, as the legislature ultimately recognised.

(xvii) That there was another reason why the relevant provisions of the Act should be interpreted so as to support the case of the taxpayer and that related to the rule of interpretation that, in the proper interpretation of the Act, regard should be had to the impact of the two competing approaches, and to ask whether they gave rise to sensible and business-like results, as opposed to insensible or even absurd consequences that could not have been intended.

(xviii) That, for the reasons set out in the judgment, the court was of the view that unbusinesslike consequences resulted from elevating para (n)(ii) above its original purpose as a limited anti-avoidance measure under the source basis of taxation. Accordingly, the approach of the taxpayer to the interpretation of the applicable Income Tax Act provisions was to be adopted, in which case there would be a proper symmetry between the foreign income from disposal of the aircraft and the deduction of foreign losses arising from the same trade, and no unmatched income or unusable assessed losses. No anomalous, insensible or unbusinesslike consequences would arise.

(xix) That, in the result, on a proper interpretation, para (n)(ii) did not apply in the operation of proviso (b) to section 20(1). But even if para (n)(ii) was of potential application to the present facts, it cannot prevail over the more recent and comprehensive provisions of section 9(4)(d), read with section 9(2)(k) which peremptorily treated the income from the sale of the aircraft as arising from a foreign source. To regard that income as from a South African source in the face of these provisions was, as submitted on behalf of the taxpayer, absurd.

Appeal upheld.

The additional assessment pertaining to the 2018 tax year is set aside.

3.8. ITC 1971 (84 SATC 243)

The taxpayer had previously noted an appeal to the Tax Court on 12 April 2019 against the disallowance by SARS of its objection in relation to its 2017 year of assessment.

The parties had agreed to participate in alternative dispute resolution proceedings to resolve the dispute, but this was unsuccessful and following the termination thereof the parties had agreed that it had failed <u>but differed as to the date of termination and at the instance of which party it had been terminated</u>.

The taxpayer ultimately afforded SARS an extension of time to deliver its rule 31 Statement of grounds of assessment and opposing appeal by no later than 13 October 2021, but SARS had failed to deliver its statement by that date.

The taxpayer thereafter on 3 March 2022 delivered a rule 56(1)(a) notice to SARS informing it of its intention to apply to the Tax Court for a final order under section 129(2) of the Tax Administration Act 28 of 2011(TA Act) ‘in the event that SARS fails to remedy the default within 15 days’.

It was common cause that SARS had subsequently delivered the rule 31 Statement within that 15-day period provided for in the notice.

Rule 56(1) provided at the relevant time for SARS and a taxpayer to apply to the Tax Court for default judgment where either party had failed to comply with a period or obligation under the rules. However, the taxpayer had first to deliver a notice informing the defaulting party of its intention to apply for a final order under section 129(2) of the TA Act, if the defaulting party did not remedy the default within 15 days of delivery of the notice.

The taxpayer had also brought an application in terms of rule 30 of the Uniform Rules of Court, contending that SARS’ delivery of the rule 31 Statement, albeit before expiry of the 15-day notice period, constituted an irregular step.

The taxpayer contended that, absent an accompanying application for condonation for ‘late filing’ in terms of rule 52(6) of the Tax Court Rules, this constituted an irregular step on the part of SARS.

Rule 52(6) provided that a party who failed to deliver a statement as and when required under rule 31, may apply to the Tax Court for an order condoning the failure to deliver the statement and the determination of a further period within which the statement may be delivered.

The taxpayer contended, inter alia, that the plain language of rule 52(6) required that a rule 31 Statement must be accompanied by a condonation application if filed out of time in order to explain to the court why it was late, notwithstanding that a final section 129(2) order has been threatened by way of a rule 56(1)(a) notice, or that consent for late filing of the pleading had been given by the other party.

The taxpayer had also relied on Tax Court Case No IT 25117 (18 November 2021) in which SARS had failed to deliver its rule 31 Statement within the prescribed 45-day period and the taxpayer there had served a rule 56(1)(a) notice calling upon it to remedy its default. SARS then delivered its statement within the required 15-day period, but the taxpayer nonetheless applied for default judgment. It was in response to the application for default judgment that SARS had applied to have it set aside as an irregular proceeding in terms of rule 30 of the Uniform Rules of Court.

In the aforesaid case Mali J decided that SARS' failure to apply for condonation due to not complying with rule 4 of the Tax Court Rules resulted in the default judgment application being granted.

The Tax Court in the present case then considered the correct interpretation and interplay between rules 4, 52(1), 52(6) and 56 of the Tax Court Rules.

Judge Cloete held the following:

(i) That the rules promulgated under section 103 of the TA Act pertained specifically to 'the procedures to lodge an objection and appeal against an assessment or decision under Chapter 9 of the Act, the procedures for alternative dispute resolution and the conduct and hearing of appeals before a Tax Board or Tax Court.'

(ii) That rule 4(1) explicitly states that 'except where the extension of a period prescribed under the Act or these rules is otherwise regulated in Chapter 9 of…these rules, a period may be extended by agreement…' Both rules 52(6) and rule 56 fall into the category of those which 'otherwise regulate' the extension of a prescribed period. <u>Rule 52(6) is not, as the taxpayer argued, peremptory</u>. On its plain wording it stated no more than that a party who failed to deliver a statement as and when required under rules 31, 32 or 33 <u>may</u> apply to the Tax Court for condonation and the determination of a further period within which the statement may be delivered.

(iii) That rule 52(6) applied where a party was in default, the other party had done nothing about it, and the defaulting party wishes the case to proceed. By contrast, it is where the innocent party wishes to do something about the default that rule 56 comes into play. Rule 56(1) gives the innocent party the option to deliver a rule 56(1)(a) notice informing the defaulting party of its intention to apply for a final section 129(2) order if the defaulting party fails to remedy the default within 15 days. It was thus only if the defaulting party nonetheless fails to remedy the default within the 15-day period that the innocent party was entitled to apply to the Tax Court for a final order.

(iv) That rule 56(2) supported the above interpretation and made clear that it was only when the Tax Court heard the application for a final order that it must consider whether condonation should be granted. Put differently, if the defaulting party remedies the default within the 15-day period referred to in rule 56(1)(a), then the statement in question is properly before the Tax Court and there is nothing for it to consider. It is only where the defaulting party nonetheless remains in default and the innocent party applies for a final order that the Tax Court would be able to consider whether or not the defaulting party had made out a proper case for condonation.

(v) That the taxpayer's interpretation rendered rule 56(1)(a) superfluous and it also meant that the defaulting party would be obliged to deliver an application for condonation merely to satisfy the innocent party, and not the Tax Court. The court was of the view that this could not have been the intention of the rule maker, particularly given that condonation was a matter for the court, and not a party, to decide.

(vi) That, in regard to the taxpayer's reliance on Tax Court Case No IT 25117, the court noted that from a reading of the judgment it appeared that the taxpayer's argument in that matter was different from the one advanced to the court *in casu* and it was the court's view that IT 25117 did not assist the taxpayer but that, in any event, Tax Court judgments were not binding on other such courts and were at best of persuasive value only.

(vii) That, accordingly, the court agreed with SARS' interpretation and was of the view that its compliance with the taxpayer's rule 56(1)(a) notice therefore had the effect that its rule 31 Statement was properly before the court.

Application in terms of rule 30 of the Uniform Rules of Court was dismissed.

3.9. ITC 1972 (84 SATC 250)

The taxpayer was a registered VAT vendor listed on the Johannesburg Stock Exchange and held 100% of the issued share capital of Taxpayer ZAW(Pty)Ltd and various other companies; local and international.

The taxpayer, on 9 April 2014, had announced its acquisition of the entire issued share capital of Des Limited, one of Australia's oldest and most prominent department stores.

The taxpayer's board announced that it intended to raise a gross total of R10 billion through a fully underwritten, renounceable rights offer ('the Rights Offer') for purposes of repaying an Equity Bridge Facility which was used to finance the acquisition.

The Rights Offer was a rights issue wherein an invitation was extended to existing shareholders to purchase additional new shares in the company at a discount on the market price on a stated future date. The Rights Offer was made to resident and non-resident shareholders.

The taxpayer had entered an unsecured syndicated facility agreement with different local and international financial companies, for the provision of a short-term equity bridge facility in a principal amount of up to R11 billion.

The acquisition was completed on 1 August 2014 when the taxpayer acquired the entire share capital of Des Limited for a purchase consideration of R21.4 billion and it had acquired the entire share capital by using two of its Australian subsidiaries.

The acquisition was funded by a combination of existing cash, new debt facilities and equity funding raised by the Rights Offer and for the purposes of funding the acquisition on completion, the Equity Bridge facility was secured, and was repaid with the proceeds of the Rights Offer.

Service providers, both local and non-resident, assisted the taxpayer with arranging and executing the Equity Bridge Facility and the Rights Offer to assist with raising capital to acquire Des Limited.

The taxpayer had incurred expenses in respect of the Rights Offer pertaining to services supplied by the local and non-resident service providers.

Approximately six months after the acquisition, the taxpayer's longstanding tax advisors advised it that there was the potential for it to claim input tax on certain amounts paid in relation to the acquisition and that it may also be liable to pay output VAT on imported services relating to the services.

The taxpayer's tax advisors were of the opinion that it was entitled to claim an input tax credit on the acquisition of the shares in Des Limited and the attendant rights issue and while they would be liable for output tax on imported services from non-resident, non-VAT registered suppliers, they would not be liable for the full value of such services.

The taxpayer, having relied on the opinion, submitted its VAT return in issue in this case which related to the February 2015 tax period and in which it:

- Claimed a deduction of input tax in respect of services acquired from local bankers relating to the rights issue in the amount of R8 847 752.06 which it calculated at the rate of 45.56% of the sum of R18 609 841, being the amount of VAT incurred in respect of the underwriting fees. The 45.56% deduction from the input tax was claimed because 45.56% of the value of the Rights Offer was taken up by non-resident shareholders and was zero-rated VAT.
- Declared VAT on services rendered by non-resident service providers in respect of the rights issue in the amount of R15 489 266, being VAT payable in respect of 'imported services' based on the fact that 54.44% of the value of the Rights Offer was taken up by resident shareholders in effect claiming a reduction of output VAT payable in the amount of R12 883 990.78 in respect of the services supplied by non-resident service providers relating to the acquisition.

SARS, raised an additional assessment in respect of the February 2015 tax period and disallowed the R8 478 752.06 input tax deduction as well as requiring payment of the full amount of R28 373 356.90 output tax in respect of services supplied by non-resident service providers and levied a 10% understatement penalty.

The taxpayer objected to the assessment raised by SARS, but the objection was disallowed, and the taxpayer then noted an appeal to the Tax Court.

SARS had disallowed the input tax deduction and had levied additional output tax relating to the services supplied to the taxpayer in the Des Limited purchase on the basis that the services supplied were not acquired wholly for the purposes of consumption, use or supply while supplying goods or services supplied in the course or furtherance of the enterprise of the taxpayer.

SARS contended that the services supplied to the taxpayer in the Des Limited purchase were not rendered for use or supply in the course of making taxable supplies by the taxpayer as it was not engaged in any trading activities which constituted the rendering of services in respect of the issuing of shares prior to the acquisition of Des Limited and had not continued to render any services in respect of the issuing of shares. Moreover, the taxpayer did not carry on the said activity in a continuous, unchanged or uninterrupted manner and did not render the services in respect of the

Rights Offer in the course of making taxable supplies as it did not carry out these activities continuously or regularly.

SARS further contended that the shares issued, the Rights Offer and the expenses related thereto formed an isolated activity which was neither carried out continuously or regularly by the taxpayer and that its main and continuous trading activity did not constitute the rendering of services in relation to rights offers or the issuing of shares.

The taxpayer contended that the services in respect of the Rights Offer were acquired in the course and furtherance of its enterprise and the costs were incurred for the purpose of making taxable supplies as its enterprise included the management of its subsidiaries, holding investments and the making and funding of acquisitions as contemplated in the definition of input tax. Moreover, the enterprise that it conducted was wider than making Rights Offers or the issuing of shares to raise capital, but that such activities formed part of their enterprise.

Judge Grobbelaar held the following:

(i) That it was common cause that the impugned costs were incurred by the taxpayer to raise capital by means of a rights issue, to raise capital in the form of equity rather than debt to acquire an investment, Des Limited, through its subsidiaries, Entity A and Entity B, which it held and controlled.

(ii) That SARS had relied primarily on the case of C:SARS v De Beers Consolidated Mines Ltd 74 SATC 330 and had criticised the taxpayer for resorting to foreign law to try and support their case. However, this case could be determined by applying the VAT Act to the facts of the case and with reference to South African case law which dealt with the meaning of 'enterprise' as defined in the VAT Act.

(iii) That in the De Beers case, supra, the question of whether costs were incurred in the course or furtherance of De Beers' enterprise arose. De Beers had acquired services and incurred costs from local and non-resident service providers because it was the target of a takeover by related parties and it was obliged to incur these costs in order to comply with its statutory obligations and, similarly, the court had to assess whether the taxpayer had acquired the services in question for purposes of use or consumption in the course of its enterprise.

(iv) That the court in the De Beers case, supra, had held that the services acquired by it were 'unrelated' to its enterprise of 'mining, marketing and selling diamonds' and were not acquired to enable it to enhance its VAT 'enterprise' and hence such services could not 'contribute in any way' to the making of De Beers' 'taxable supplies.'

(v) That it was the view of the court in the present case that it was distinguishable from the De Beers case, supra, as the costs incurred by De Beers regarding the takeover were clearly not utilised or consumed by De Beers for making taxable supplies in the course or furtherance of its enterprise, which was the buying and selling of diamonds.

(vi) That the taxpayer's business in the present case was not that of a consumable goods retailer. It indeed conducted business as an investment company, but its business was not limited to holding shares in companies and earning dividends. An integral part of its business was providing financial and management services to its subsidiaries for remuneration, thereby adding value to its subsidiaries in the taxpayer's Group to the benefit of the subsidiaries and ultimately the taxpayer.

(vii) That a further part of the taxpayer's business was to acquire shares in further subsidiary companies, not only earning it dividends but earning it income by providing it with financial and management services. The costs incurred in the acquisition of the shares in Des Limited by way of Entity A and Entity B was for the benefit of both its investments (its subsidiaries or businesses) to which it rendered financial and management services for remuneration and itself by way of increased management fees and dividends to make its business better and more valuable.

(viii) That in the latter case of Consol Glass (Pty) Ltd v C:SARS 83 SATC 186 the court had to decide a similar issue, i.e. whether, in respect of services acquired relating to a debt restructuring, Consol had been entitled to an input tax deduction in respect of costs incurred from local service providers and whether Consol was obliged to pay output tax on services acquired from non-resident service providers because such services met the definition of imported services. In that case the Supreme Court of Appeal considered the question of how closely the services acquired should be associated with the enterprise for them to be considered for the 'purpose of making taxable supplies', i.e. in the 'course or furtherance of conducting an enterprise.' The court referred to a '<u>functional link</u>' between the costs/services and the enterprise.

(ix) That the evidence in the present case established that the taxpayer’s business enterprise was that of an active, investment holding company and this encompassed inter alia the supply of capital management services and financial services for remuneration and the question then was whether there was a functional link or connection between the services acquired and the taxpayer’s enterprise, to which was the purpose of the services acquired sufficiently closely linked to the taxpayer’s enterprise to be considered ‘in the course or furtherance’ thereof.

(x) That the court found that such a functional link or connection existed in that the taxpayer had acquired the services for the purpose of raising capital and, ultimately, for the purpose of acquiring Des Limited and that its actions in expanding its business and incurring costs, both local and foreign, in the course thereof had a functional link to the making of its VAT taxable supply of management services to its subsidiaries and that the expenses incurred in this regard were incurred wholly for the purpose of consumption, use or supply in the course of supplying goods and services (taxable supplies) and in the course or furtherance of its enterprise.

(xi) That, accordingly, in regard to the Des Limited acquisition, the taxpayer was entitled to deduct the impugned input tax paid by it in the calculation of its VAT and was not liable to pay VAT on the impugned services supplied by foreign entities.

(xii) That in view of the above decision, the court could not find any reason why the additional assessment should be referred back to SARS for further examination and assessment in terms of s 129(2)(c) of the Tax Administration Act.

Appeal upheld.

The additional assessment dated 14 December 2017 for the tax period February 2015 was set aside.

4. INTERPRETATION NOTES

4.1. Deductions in respect of buildings used by hotel keepers – No. 105 (Issue 2)

This Note provides guidance on the interpretation and application of section 13bis, which provides for an allowance on any buildings used in the trade of hotel keeper.

Section 13bis provides an annual allowance on the cost of erection of buildings or improvements to such buildings used by the taxpayer in the trade of hotel keeper.

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

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

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

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

- The definition of 'hotel keeper' in section 1(1) requires the person concerned to conduct the business of a hotel, boarding house or lodging house in circumstances in which both meals and sleeping accommodation are supplied by that person for consideration.
- The building must be erected. Purchased buildings do not qualify for the annual allowance but improvements to purchased buildings could qualify.
- The annual allowance is granted on the cost to the taxpayer, after adjusting for deferred recoupments and amounts which may qualify for an allowance under section 11(g), of erecting a hotel building or of effecting improvements to such a building. There is no requirement that the taxpayer own the building or

improvements. Thus, the annual allowance applies to a taxpayer who erects a hotel building or effects improvements to such a building:

  - for own use as a hotel keeper;
  - as lessor when the lessee is a hotel keeper; or
  - as lessee to the extent that the building or improvements do not qualify for the leasehold improvements allowance under section 11(g).

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

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

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

4.2. Exemption of income relating to South African ships used in international shipping – No. 131

This Note provides guidance on the interpretation and application of section 12Q, which provides for an exemption from normal tax, capital gains tax, dividends tax and withholding tax on interest for an international shipping company meeting the requirements of the section.

As part of the National Transport Policy, government aims to promote the development of an efficient and productive South African maritime industry capable of competing internationally and to encourage ships to carry the South African flag. To give effect to this strategic objective, section 12Q was inserted with effect from 1 April 2014 and applies to years of assessment commencing on or after that date, providing certain tax relief for qualifying international shipping companies. Since the introduction of the section, amendments were effected to some of the definitions fundamental to the application of section 12Q.

The issue of double taxation and the application of various double tax treaties is not dealt with in this Note as double taxation relief measures vary from treaty to treaty.

Section 12Q provides for an exemption from normal tax, capital gains tax, dividends tax and withholding tax on interest for international shipping companies if the requirements of the section are met. In determining whether an international shipping company qualifies for these exemptions, the definitions of 'South African ship', 'international shipping', 'international shipping company' and 'international shipping income' should be considered and applied to the relevant tax under section 12Q.

5. DRAFT INTERPRETATION NOTES

5.1. Income Tax exemption: Water services providers

This Note provides guidance on the interpretation and application of the definition of 'water services provider' in section 1(1) for purposes of the exemption of the receipts and accruals of a qualifying water services provider from normal tax under section 10(1)(t)(ix).

The Bill of Rights in the Constitution guarantees everyone the right to access to sufficient water. It is the responsibility of the state to take reasonable legislative and other measures, within its available resources, to achieve the progressive realisation of this right. To give effect to this constitutional responsibility the Water Services Act was promulgated.

Every water services authority under the Water Services Act has a duty to all consumers or potential consumers in its area of jurisdiction to progressively ensure efficient, affordable, economical and sustainable access to water services. The Water

Services Act, amongst other things, provides for the monitoring of water services and intervention by the Minister or by the relevant Province to ensure that every water service institution complies with:

- all applicable national standards prescribed under that Act;
- all norms and standards for tariffs prescribed under that Act; and
- every applicable development plan, policy statement or business plan adopted under that Act.

To assist a water services provider to fulfil its obligations under the Constitution and the Water Services Act, section 10(1)(t)(ix) of the Income Tax Act exempts the receipts and accruals of any water services provider from normal tax provided certain requirements are met. This Note considers the requirements of the definition of 'water services provider' to qualify for this exemption. The reporting obligations of a qualifying water services provider under the Act and the TA Act are also considered.

This Note provides general guidelines and considers the broad principles of the legislation. In conclusion:

- any person meeting the requirements of the definition of 'water services provider' in section 1(1) will be exempt from the payment of income tax under section 10(1)(t)(ix);
- the receipts and accruals of a water services provider is fully exempt from the payment of income tax under section 10(1)(t)(ix);
- the exemption is not subject to the discretion or approval of SARS;
- a water services provider bears the onus of proving that it complies with the requirements of the definition of 'water services provider' and must retain the necessary supporting evidence;
- a water services provider must comply with reporting requirements SARS may determine; and
- a water services provider is potentially exempt from other taxes such as transfer duty, dividends tax, securities transfer tax, skills development levies and capital gains tax.

6. BINDING GENERAL RULING

6.1. VAT treatment of specific supplies in the short-term (non-life) insurance industry – No. 14 (Issue 4)

For the purposes of this ruling, unless the context indicates otherwise:

- 'bordereau' means a document issued by an insurer or intermediary in the form of a memorandum, statement or invoice, which contains detailed information such as:
  - insurance premiums collected;
  - commission and fees payable in respect of intermediary services supplied; and
  - claims paid;
- 'inbound insurance policy' means a travel policy that provides insurance cover in respect of a passenger transported from an export country into the Republic or between two places in the Republic as part of an international journey;
- 'indemnity payment' means a payment made by the insurer under an insurance policy to indemnify the insured on the occurrence of the insured event;
- insurer' means any vendor supplying 'insurance' as defined in section 1(1);
- 'intermediary' means any broker or agent supplying intermediary services to an insurer or insured;
- 'intermediary services' has the meaning assigned thereto in section 1 of the Financial Advisory and Intermediary Service Act 37 of 2002 and includes the management and administration of a policy as well as the collection of premiums and processing of claims;
- 'international journey' means a journey commencing from the 'point of departure' in the Republic to a destination outside the Republic (and vice versa), including (where applicable) stopovers en route to the destination, time spent in the destination country and the return journey;
- 'outbound insurance policy' means a travel policy that provides insurance cover in respect of a passenger transported from the Republic to a destination in an

export country or from a place outside the Republic to another destination outside the Republic as part of an international journey;

- 'policy document' means a document which is evidence of a contract of insurance, including any renewal notice, premium notification or endorsement in respect thereof;
- 'temporary presence' means a period of six months or less;
- 'third-party supplier' means a supplier of goods or services that receives a trade payment from an insurer;
- 'trade payment' means a payment made under a contract of insurance by an insurer to a third-party supplier to replace or repair the insured's goods which were lost, damaged or destroyed

Purpose

This BGR sets out the VAT treatment of the issues listed below:

- The time of supply in relation to the supply of insurance and related intermediary services
- International transport insurance including stock throughput, goods in transit and marine insurance policies
- Hull and associated liability insurance
- Insurance cover provided in respect of fixed property and movable property located in an export country
- Excess payments
- Indemnity payments
- Third party payments
- Recoveries
- Group accident claims
- Intermediary services
- Documents accepted as alternatives to tax invoices in respect of the supply of insurance and related intermediary services

- Approval to issue recipient-created tax invoices, debit and credit notes

Background

This BGR is updated because of the amendments to section 8(8) and the introduction of a new provision being section 8(8A) which came into effect from 1 January 2024. The amendments were necessary because of earlier amendments to section 72 made in terms of section 73 of the Taxation Laws Amendment Act 34 of 2019.

Ruling

This ruling constitutes a BGR issued under section 89 of the Tax Administration Act insofar as it relates to rulings hereunder.

Time of supply – Insurance

An insurance policy, renewal notice or endorsement that does not notify the insured of an obligation to make payment is not regarded as an invoice and will therefore not trigger the time of supply. In instances where the insurer (or its intermediary) does not issue an 'invoice', the supply of insurance is deemed to be on the date the insurer (or the insurer's intermediary) receives the insurance premium in respect of that supply.

International transport insurance

The supply of insurance under any inbound or outbound insurance policy, including insurance cover during periods in which 'ancillary transport services' are supplied, may be zero-rated under section 11(2)(d).

Stock throughput insurance

The supply of stock throughput insurance is regarded as international transport insurance to the extent that insurance cover is provided in respect of goods transported from an export country to South Africa (and vice versa) as part of an international journey.

Insured goods transported or stored in South Africa

The supply of insurance under a stock throughput policy which provides cover for insured goods whilst the goods are transported between places in South Africa (including periods during which 'ancillary transport services' are supplied in respect of those goods) is subject to VAT at the zero rate under section 11(2)(d). The zero-rating is only applicable if the transport service (including any 'ancillary transport services') is supplied by the same supplier providing the international transport services as envisaged by section 11(2)(c).

Insured goods in South Africa but not transported or stored

Insurance cover provided while insured goods are in South Africa and not being transported (or stored) as part of an international journey does not qualify for zerorating under section 11(2)(d).

Single insurance premium

Insurers that levy a single premium in respect of the single supply of stock throughput insurance relating to both standard and zero-rated supplies are, under section 8(15), required to allocate the premium to the various risk components which were used to determine the premium and to apply the applicable VAT rate to each component. The same ratio must be used in respect of subsequent adjustments to the premium unless the insurer can determine the allocation more accurately. The insurer is required to notify the insured and, where applicable, the intermediary of the original allocation of the premium between the standard and zero-rated portions as well as any subsequent adjustments in respect thereof. The insurer is required to retain proof of such notification.

Hull insurance

The supply of hull insurance is regarded as a service provided in connection with the operation or management of a 'foreign-going aircraft' or 'foreign-going ship' and may therefore be zero-rated under section 11(2)(h)(ii) if supplied directly (that is, not through an agent or other person) to a non-resident that is not a vendor.

The temporary presence of the underlying insured foreign-going ship or aircraft in- South Africa will not disqualify the supply from being zero-rated.

Insurance cover for fixed property situated in an export country

Insurance is regarded as being supplied directly in connection with the insured land, or any improvement to it, situated in an export country and is therefore subject to VAT at the zero rate under section 11(2)(f).

Insurance cover for movable property situated in an export country

Insurance is regarded as being supplied directly in respect of the insured movable property and is subject to VAT at the zero rate under section 11(2)(g)(i), provided that the insurer obtains and retains proof that the movable property is situated outside South Africa during the period for which the insurance cover is provided. Such proof may be reflected in the insurance contract or a declaration provided by the insured.

The temporary presence of the movable property in South Africa will not disqualify the supply of insurance relating to the property from being zero-rated.

Indemnity payments

General

Historically there has been some uncertainty on the application of section 8(8) regarding the VAT treatment of indemnity payments made by insurers and the payment of excess by the insured. Although the term 'indemnity payment' refers to a payment made by the insurer under an insurance policy to indemnify the insured on the occurrence of the insured event, it is a general term used in the insurance industry. It can therefore refer to a so-called trade payment that is paid to a third-party supplier to reinstate goods or services lost, stolen or damaged that are covered under a contract of insurance, or it can refer to a monetary settlement payment made either to the insured, or to another person on behalf of the insured to cover that loss. Another issue was that in the case of reinstated goods or services, it was not clear whether the third-party supplier made a supply to the insurer or the insured, or to both parties. This aspect, in turn, led to uncertainty regarding the issuing of tax invoices and the deduction of input tax.

Section 8(8) was therefore amended with effect from 1 January 2024 to clarify the application of the law, and section 8(8A) was introduced to specifically deal with reinstatements. As a result, from 1 January 2024 it has been clarified that section 8(8) does not deal with the reinstatement of goods or services (except to provide an exclusion) as this is now covered by section 8(8A). The VAT implications in this regard are explained below.

Payment and receipt of indemnity payments (monetary settlements) – sections 8(8) and 16(3)(c)

The insurer

If an insurer makes an indemnity payment in the form of a monetary settlement as a result of a claim under a taxable contract of insurance, the implication for the insurer is that a deduction may be claimed under section 16(3)(c) by applying the tax fraction to the amount paid. The deduction may be made in the tax period in which the payment was made to the insured, or to another person on behalf of the insured.

The insurer in this case must issue a document to the insured informing that person of a potential output tax liability that may arise under section 7(1)(a) read with section 8(8). This requirement applies irrespective of whether the insured is a vendor or not.

The insured

If the insured (being a vendor) receives an indemnity payment in the form of a monetary settlement as a result of a loss incurred in the course or furtherance of an enterprise, section 8(8) will deem the insured to make a taxable supply and output tax must be declared on the supply at the standard rate. The output tax must be declared in the tax period in which the payment was received. However, no output tax is declared by the insured on an indemnity payment received (or part of it) in the following cases:

- If the indemnity payment is made in consequence of a claim made under a contract of insurance that is not subject to tax under section 7(1)(a).
- To the extent that the payment is made to a third-party supplier as consideration for the supply of goods or services being reinstated under the contract of insurance as contemplated in section 8(8A).
- To the extent that the payment relates to a loss of goods or services on which the insured (being a vendor) was denied an input tax deduction section 17(2) when those goods or services were acquired.

Payment and receipt of indemnity payments (trade payments) – sections 8(8A) and 16(3)(a)

The insurer When a third-party supplier is contracted to reinstate goods or services to the insured as a result of a claim under a taxable contract of insurance, the third-party supplier is deemed to make a supply to each person that is liable to pay any part of the consideration in respect of said consideration. (That is, both the insurer and the insured.) The insurer will make an indemnity payment in the form of a trade payment to the third-party supplier to cover its part of the obligation. If the supply is taxable, the insurer will be entitled to a tax invoice reflecting that part of the consideration paid to supply the reinstated goods or services and a deduction may be claimed as a normal input tax deduction (subject to the usual documentary requirements and limitations in respect of the claiming of input tax).

The insured

Following from what has been stated above, no deemed supply arises under section 8(8) in the hands of the insured whose goods or services are being reinstated. Therefore, no output tax is payable by the insured when a trade payment is made to the third-party supplier by the insurer on behalf of the insured.

The third-party supplier

The third-party supplier is deemed to make a supply to both the insured and the insurer to the extent that each party has an obligation to make a payment towards the total consideration for the reinstated goods or services. As such, if the supply is taxable, a separate tax invoice must be issued to both the insurer and the insured reflecting the consideration paid or payable by each person. Output tax must be declared at the standard rate on each part of the consideration paid or payable.

Excess payments

Monetary settlements – section 8(8)

If the insured pays an amount of excess to the insurer as a result of a claim under a taxable contract of insurance (or the excess is deducted by the insurer from the amount- of the claim) and a monetary payment is made by the insurer to settle the claim as contemplated in section 8(8), there is no input tax deduction for the insured. No output tax is declared by the insurer in respect of the excess amount as it does not constitute consideration for any taxable supply and merely forms part of the calculation of the net monetary settlement to be paid.

Reinstatements – Insured pays the excess directly to the third-party supplier – section 8(8A)

Under section 8(8A), if the third-party supplier of goods or services is a vendor and those goods or services are supplied to reinstate the insured under a contract of insurance, that vendor (the third-party supplier) is deemed to make a supply to each person that is liable to pay any part of the consideration in respect of said consideration. The third-party supplier must therefore issue two tax invoices, that is, one to the insured to the extent of the excess payment, and one to the insurer to the extent of the trade payment. The insurer and the insured (being vendors) may each deduct their respective portions of input tax based on the tax invoices concerned.

Reinstatements – Insurer acting on behalf of the insured pays the full consideration to the third-party supplier and recovers the excess from the insured – sections 8(8A), 54(2) and 54(3)

Under section 8(8A), if the insurer acts on behalf of the insured as contemplated in section 54(2) by acquiring the reinstated goods and services, paying the excess amount to the third-party supplier and recovering the amount later from the insured, the same outcome as explained above applies. However, the insurer is required to issue a statement to the insured containing the information specified in section 54(3) regarding the deemed supply made to the insured.

Recoveries

An insurer is not liable to account for output tax on amounts recovered from a third-party or the third-party's insurer under a subrogation claim, irrespective of whether the whole or only a portion of the claim is recovered.

Group personal accident insurance

Insurer

An insurer may deduct VAT under section 16(3)(c) in respect of indemnity payments made to the insured under group personal accident insurance.

Employer acting as principal

An employer, being a vendor, may deduct input tax in respect of the taxable supply of group personal insurance acquired to the extent it is acquired for the purpose of making taxable supplies.

Any indemnity payments received by the employer (as principal) under a contract of insurance will result in the employer being liable to account for output tax under section 8(8). The employer will not be entitled to deduct any VAT in respect of amounts subsequently paid to the employee.

Employer acting as agent on behalf of employees

The employer, when acting as the agent of its employees in entering into a group personal accident insurance contract with an insurer, will not be entitled to deduct input tax in respect of that contract. The employer will not be required to account for output tax under section 8(8) if the employee receives an indemnity payment from the insurer, irrespective of whether the payment is made through the employer or directly to the employee.

Intermediary services

The zero rate may be applied to services consisting of the arranging of:

- the insurance of goods or passengers transported internationally under section 11(2)(d); or
- hull insurance in respect of a foreign-going aircraft or ship under section 11(2)(i)(ii) if the arranging service is supplied to a non-resident that is not a vendor.

An intermediary arranging stock throughput insurance may however only zero rate the supply of intermediary services to the extent that the underlying stock throughput insurance qualifies for zero-rating under section 11(2)(d).

Tax invoices, credit and debit notes

Supply of insurance

SARS directs, under section 20(7)(a) and 21(5)(a), that the policy document, although not an invoice, is regarded as a tax invoice, debit note and credit note which need not contain the words ‘tax invoice’, ‘VAT invoice’, ‘invoice’, ‘debit note’ and ‘credit note’ (as the case may be) provided:

- the insurer retains proof that the insured paid premiums in accordance with the policy document; and
- the policy document reflects all the other information as required by section 20(4); and
- the policy document contains the following statement (or substantially similar wording):

  ‘In terms of Binding General Ruling 14 this document constitutes a tax invoice, debit note and credit note as contemplated in sections 20(7)(a) and 21(5)(a) of the VAT Act.’

Supply of intermediary services

SARS directs, under sections 20(7)(a) and 21(5)(a), that the document (generally known as a bordereau) issued by the intermediary to the insurer in respect of the supply of intermediary services does not have to contain the words ‘tax invoice’, ‘VAT invoice’, ‘invoice’, ‘credit note’ or ‘debit note’ (as the case may be). However, the bordereau must reflect the other information as prescribed in sections 20(4) and 21(3) respectively.

Recipient-created tax invoices, credit and debit notes

An insurer that is required to determine the consideration payable in respect of intermediary services may, under sections 20(2) and 21(4), issue recipient-created tax invoices, credit or debit notes in respect of the supply of intermediary services.

This approval is subject to:

- the recipient-created tax invoice, credit or debit note (as the case may be) complying with sections 20(4), (5), 21(3) or the special approval, as applicable; and
- the insurer complying with all other requirements listed in Interpretation Note 56 'Recipient-created tax invoices, credit and debit notes'.

In addition, permission is granted under sections 20(7)(a) and 21(5)(a) that the bordereau issued by the insurer to the intermediary in respect of the supply of intermediary services does not have to contain the words 'tax invoice', 'VAT invoice', 'invoice', 'credit note' or 'debit note' (as the case may be).

<u>Conditions</u>

<u>Zero-rating</u>

The zero-rating of supplies contained in this BGR is conditional upon the insurer and intermediary (as applicable) obtaining and retaining the documentary proof as provided for under section 11(3) read with Interpretation Note 31 'Documentary Proof Required for the Zero-Rating of Goods and Services' (Interpretation Note 31). Failure to obtain and retain the required documentary proof within the required time period will result in the vendor being required to make the relevant adjustments as stipulated in Interpretation Note 31.

<u>Input tax and other deductions</u>

The statements contained in this BGR regarding input tax and other deductions are conditional upon the vendor obtaining and retaining the documentary proof contemplated in section 16(2) (including the bordereau referred to in 3.12) by the time the relevant VAT return is submitted. The deductions are subject to sections 16 and 17. Failure to obtain and retain the required documentary proof will result in the vendor not being entitled to make the deduction.

6.2. Documents and records to be retained and maintained by agent under section 64(2C) and (3) – No. 69

For the purposes of this ruling:

- 'customs documentation' means the export documentation prescribed under the Customs and Excise Act 91 of 1964;
- 'depositor' means a vendor that delivers gold to a refinery for refining or-smelting purposes;
- 'principal' or 'principal depositor' means the vendor deemed to have made a supply under section 54 and on whose behalf gold is supplied as contemplated in section 54(2C);
- 'recipient' means the depositor's customer in respect of the supply of gold;

<u>Purpose</u>

This BGR sets out the further particulars prescribed by SARS under section 54(2C) that the agent must obtain and retain on behalf of the principal depositor, as well as the records to be maintained under section 54(3).

<u>Background</u>

The main purpose of gold refineries is to refine and smelt gold or ore received from depositors. In most instances, the refineries also act as agents and sell or export gold on behalf of these depositors. The agent is allowed to issue invoices in relation to the supplies made on behalf of the depositors under section 54. However, under the same section it is confirmed that the depositor remains the principal in respect of the supply of gold, as well as the export of the gold. Gold from more than one depositor is typically required to make up the volume ordered for sale or export.

It is accordingly not possible for each depositor to have its gold or ore treated separately from the gold or ore of other depositors. It follows that once a specific depositor's gold or ore enters the refining or smelting process, it is co-mingled with the gold or ore of other depositors and effectively loses its identity as belonging to a specific depositor.

Given that gold is a highly regulated commodity and that the refinery or smelter continuously sells gold as an agent on behalf of the depositors to potential buyers that are limited to the members of the London Bullion Market Association based in London (the Bullion Bank) in the form of export sales (direct or indirect) as envisaged in section 11(1)(a), sales to the South African Reserve Bank, the South African Mint Company (Pty) Ltd. and Banks registered under the Banks Act 94 of 1990, as envisaged in section 11(1)(f), it is important that vendors are able to properly and accurately account for VAT.

Discussion

Section 54(2C) provides that SARS will prescribe the acceptable documentary evidence the agent must obtain and retain for purposes of gold being supplied as contemplated in section 11(1)(f) or when gold is exported from South Africa in the circumstances contemplated in paragraph (a) or (d) of the definition of 'exported' in section 1(1) and in accordance with section 12 of the of the Precious Metals Act 37 of 2005.

Under section 54(3), the agent must maintain sufficient records in respect of tax invoices, debit notes, or credit notes issued on behalf of a principal under section 54(1).

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

Ruling

Section 54(3)

The agent will issue a tax invoice to the recipient under section 54(1) and in respect of this supply issue to the principal a document as prescribed by section 54(3) (for example, a Sale of Gold Certificate) containing the following particulars:

- Value of ounces of gold sold
- Purchase order number
- Name, address and VAT registration number of the principal depositor
- Statement that the gold was sold subject to VAT at the zero-rate

Section 54(2C)

In instances of a sale by the agent on behalf of the principal depositor as contemplated under section 54(2C), and SARS is satisfied that the agent has issued the principal with a document as prescribed in 4.1 above, the agent is required to obtain and maintain the following:

- A copy of the zero-rated tax invoice for both exports and supplies under section 11(1)(f)

In the case of exports, the agent is further required to obtain and retain the following:

- The recipient's order or the contract between the recipient and the agent
- Proof that the agent paid the transport costs
- A copy of the airfreight transport documentation
- The customs documentation
- Proof of payment for the gold supplied to the recipient

The agent would be liable to account for output tax in the event that the agent is not in possession of the above documentation to substantiate the zero rate.

6.3. Issue of a single section 18A receipt to a donor taxpayer for multiple **bona fide** *donation – No. 70*

For the purposes of this ruling:

- 'section 18A-approved organisation' means any public benefit organisation, conduit public benefit organisation, institution, board or body, agency, programme, fund, High Commissioner, office, entity, organisation, or the government approved by SARS for purposes of section 18A envisaged in section 18A(1)(a) to (c);
- 'section 18A receipt' means a receipt with prescribed requirements issued under section 18A(2) by a section 18A-approved organisation potentially entitling the donor taxpayer to an income tax deduction for bona fide donations made

Purpose

This BGR provides clarity on whether a section 18A-approved organisation is entitled to issue a single section 18A receipt for multiple bona fide donations actually paid or transferred by the same donor taxpayer during a year of assessment.

Background

Section 18A(1) provides that a donor taxpayer is allowed in the determination of taxable income, notwithstanding the provisions of section 23, to deduct the sum of any bona fide donations actually paid or transferred to a section18A-approved organisation during a year of assessment. The deduction of the sum of the bona fide donations made during a year of assessment may not exceed 10% of the taxpayer's taxable income subject to certain provisions.

Section 18A(2)(a) prescribes the mandatory information that must appear on a section 18A receipt for the receipt to be valid. Any claim for a deduction in the determination of taxable income for the sum of any bona fide donations by a donor taxpayer will be allowed only if supported by a section 18A receipt issued by the section 18A-approved organisation containing the mandatory information.

Section 18A-approved organisations may receive multiple bona fide donations during a year of assessment from the same donor taxpayer. Section 18A(2) is silent on whether a separate section 18A receipt must be issued for each bona fide donation actually paid or transferred by the same donor taxpayer during the year of assessment. The issuing of a separate section 18A receipt for each bona fide donation actually paid or transferred may create administrative challenges for section 18A-approved organisations.

Ruling

Applying a businesslike5 interpretation and application to section 18A, a single section 18A receipt, complying with the mandatory information listed in section 18A(2)(a) issued to a donor taxpayer for the sum of bona fide donations actually paid or transferred by that donor taxpayer to a section 18A-approved organisation during a year of assessment, is acceptable. The sum of the multiple bona-fide donations reflected in separate section 18A receipts must be the same amount as the sum of bona fide donations reflected in a single section 18A receipt.

The single section 18A receipt issued by a section 18A-approved organisation to a donor taxpayer, however, must contain the mandatory information and a breakdown listing the following information of each bona fide donation making up the sum of the multiple bona fide donations actually paid or transferred by that donor taxpayer during the year of assessment:

- The date of receipt of each bona fide donation

- The amount of each bona fide donation if the donation was made in cash
- The nature and value of each bona fide donation if the donation is a non-cash donation

The above will ensure substantial compliance with the requirements under section 18A.

This ruling constitutes a BGR issued under section 89 of the Tax Administration Act 28 of 2011. This ruling applies for the third-party reporting under section 26 of the Tax Administration Act, 2011 in accordance with Public Notice 3631 in Government Gazette 48867 of 30 June 2023.

6.4. Section 18A receipt: Donation of property in kind – No. 71

For the purposes of this ruling:

- 'donation of property in kind' means a donation of property made in a form other than cash but excludes a donation, which constitutes, or is subject to any fiduciary right, usufruct or other similar right, or which constitutes an intangible asset or financial instrument, unless that financial instrument is a share in a listed company, or issued by an 'eligible financial institution' as defined in the Financial Sector Regulation Act;
- 'public notice' means the Public Notice 3631 in Government Gazette 48867 of 30 June 2023;
- 'section 18A-approved organisation' means any public benefit organisation, conduit public benefit organisation, institution, board or body, agency, programme, fund, High Commissioner, office, entity, organisation, or the government approved by SARS for purposes of section 18A envisaged in section 18A(1)(a) to (c);
- 'section 18A receipt' means a receipt with mandatory information issued under section 18A(2) by a section 18A-approved organisation potentially entitling the donor taxpayer to an income tax deduction for bona fide donations made

Purpose

This BGR provides clarity on the detail that must appear on a section 18A receipt issued by a section 18A-approved organisation to a donor taxpayer for a donation of any property in kind to comply with section 18A(2), and third-party reporting requirements under the TA Act.

Background

Section 18A(1) and (2) provide a donor taxpayer with a deduction in the determination of taxable income subject to the stated income limitation for the sum of any bona fide donations in cash or of property made in kind, actually paid, or transferred to any section 18A-approved organisation during the year of assessment.

Any claim for a deduction by a donor taxpayer will, however, be allowed only if supported by a section 18A receipt issued by the section 18A-approved organisation containing mandatory information. The amount of the donation or the nature of the donation, if not in cash, is mandatory information that must appear on a section 18A receipt.

Uncertainty exists whether only the nature of the donation of property in kind must appear on the section 18A receipt or whether the amount of such a donation determined under section 18A(3) or (3A) must also be contained on a section 18A receipt.

Discussion

SARS is responsible for the administration of the TA Act under the control or direction of SARS. SARS may, in order to administer a tax Act, obtain full information relating to anything that may affect the liability of a person for tax for any tax period, tax event, or the obligation of a person, whether personally or on behalf of another person, to comply with a tax Act. SARS may also perform any other administrative function necessary to carry out the provisions of the tax Act.

To give effect to the above responsibility, SARS may by public notice, at the time and place and by the due date specified, require a person that employs, pays amounts to, receives amounts on behalf of, or otherwise transacts with another person, or has control over assets of another person, to submit a third-party return by the date specified in the notice. A person required to submit a third-party return must do so in the prescribed form and manner and the third-party return must, amongst other things, contain the information prescribed by SARS.

A section 18A-approved organisation that issued a section 18A receipt from 1 March 2024 must submit to SARS a return of any amount donated for which such a receipt has been issued. The public notice does not distinguish between a donation in cash or a donation of property in kind. The requirement is therefore that a third-party return must be submitted on information relating to 'any amount donated'.

The third-party return containing all the prescribed information for the period from:

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

A deduction claimed by any donor taxpayer for any donation of property in kind is deemed to be an amount determined under section 18A(3). A deduction claimed by any donor taxpayer for a donation of immovable property of a capital nature if the lower of market value or municipal value exceeds cost, will be determined in accordance with the formula provided in section 18A(3A).

The amount of the deduction, deemed to be an amount determined under section 18A(3) or (3A) of a donation of property in kind, is therefore required to enable a donor taxpayer to calculate the allowable deduction subject to the income limit to be claimed from taxable income during a particular year of assessment under section 18A(1). SARS may for purposes of the administration of a tax Act require a taxpayer to submit relevant material that SARS may require. Thus, SARS may require evidence to support the determination of the deemed amount of the donation under section 18A(3) or (3A)

The amount of the deduction deemed to be an amount determined under section 18A(3) or (3A) of a donation of property in kind is also required for purposes of third-party reporting by section 18A-approved organisations. The sum of the amount of the deduction deemed to be an amount determined under section 18A(3) or (3A) claimed on submission of the donor taxpayer's income tax return must therefore match the amount contained on the section 18A receipt issued by a section 18A-approved organisation and reported to SARS on submission of the third-party return.

<u>Ruling</u>

Having regard to the provisions of section 18A(1), (2), (3), and (3A), and the purpose of third-party reporting requirement under the TA Act, the information relating to a donation of property in kind that must, in addition to the other mandatory information, be contained on a section 18A receipt is the:

- nature of the donation, which is an adequate and accurate description of the donation of property in kind; and

- amount deemed to be an amount of the deduction of the donation of property in kind determined under section 18A(3) or (3A).

This ruling constitutes a BGR issued under section 89 of the TA Act.

6.5. Particulars to be contained in a credit note for a valid deduction under section 16(3)(a)(v) for prepaid vouchers – No. 72

For the purposes of this ruling:

- 'SMS' means Short Message Service;
- 'telecommunications company' means an 'electronic communications service licensee' as defined in section 1 of the Electronic Communications Act 36 of 2005

Purpose

This BGR sets out the particulars that are acceptable in a credit note that the telecommunications company is required to issue to the prepaid subscriber in the circumstances contemplated in section 21(1)(f) for the purposes of sections 16(2)(a) and 16(3)(a)(v).

Background

In the early years of the mobile telecommunications industry in South Africa, prepaid subscribers to mobile telecommunication services could use prepaid vouchers only to purchase the services offered by that mobile telecommunications company such as calls and SMS. The prepaid vouchers are generally sold to retailers and distributors who sell prepaid vouchers to the subscribers. The evolution and technological advances in the telecommunications industry have made it possible for subscribers to utilise the prescribed services purchased from the telecommunications company to acquire other services from third-party service-providers. Examples include, the supply of financial services (long-term and short-term insurance), as well as downloads of music or movies, and mobile money services supplied by third-party service providers.

Should the subscriber acquire other services, the telecommunications company cannot issue a credit note, as the telecommunications company cannot meet the requirements of paragraph (i) to section 21(1). This is because it was not the supplier that provided the tax invoice to the subscriber as these vouchers are sold to subscribers via various intermediaries.

If the prepaid subscriber acquires services from a third-party supplier, the third-party supplier is required to account for output tax on that supply, provided it is a taxable supply.

The implication, therefore, is that both the telecommunications company and the third-party supplier account for output tax to SARS; the telecommunications company at the point that the prepaid voucher is sold, and the third-party to the extent that services are supplied by the third-party. In such instances, the telecommunications supplier transfers the money collected in respect of the supply by the third-party supplier to such supplier, with no remedy for the telecommunications company to issue a credit note under section 21 or write off irrecoverable debts under section 22.

Discussion

Due to the difficulty described above, section 21(1) was amended with effect from 1 April 2024 to provide for instances that prepaid vouchers contemplated in section 10(19) have been issued by any registered vendor that is an 'electronic communications service licensee', and the nature of the supply specified on such voucher has been fundamentally varied or altered. In this instance, the telecommunications company would have furnished a return in which an incorrect amount of output tax was declared as contemplated in paragraph (ii) to section 21(1). As a consequence, the telecommunications company is allowed to make an adjustment under section 21(2).

Section 21(3)(a)(iii) requires the particulars of the recipient to be reflected on a tax invoice unless the credit note relates to a supply under R5 000 for which a tax invoice was issued under section 20(5).

Due to the uncertainty in the industry relating to the particulars required on a credit note as a result of the introduction of section 21(1)(f), this BGR clarifies the acceptable format of the credit note and the particulars which must be reflected on such invoice in order to comply with the requirements for a deduction under section 16(3)(a)(v) read with section 16(2)(a).

Ruling

Particulars relating to the agent and acceptable documentary evidence

The telecommunications company must issue a credit note to the subscriber in an electronic format whereby the subscriber will be notified by SMS that the said credit note is available for download. The credit note must contain the following particulars:

- The words 'credit note'
- The name, address and VAT registration number of the vendor
- The name, address and, if the recipient is a registered vendor, the VAT registration number of the recipient, except if the credit note relates to a supply in respect of which a tax invoice contemplated in section 20(5) was issued
- The date on which the credit note was issued
- Either:
    - the amount by which the value of the said supply shown on the prepaid subscriber's account has been reduced and the amount of the excess tax; or
    - if the tax charged in respect of the supply is calculated by applying the tax fraction to the consideration, the amount by which the consideration has been reduced and either the amount of the excess tax or a statement that the reduction includes an amount of tax and the rate of the tax included
- A brief explanation of the circumstances giving rise to the issuing of the credit note
- Information sufficient to identify the transaction to which the credit note refers

The abovementioned credit note, which includes the relevant particulars, must be retained for a period contemplated in compliance with section 55 read with Part A of Chapter 4 of the Tax Administration Act.

In the event that the supply exceeds R5 000, and the telecommunications company does not have all the details required under section 21(3)(a)(iii), the telecommunications company is allowed to request the prepaid subscriber to complete his or her personal details and VAT registration number before downloading the credit note from the system.

7. GUIDES

7.1. Frequently Asked Questions – Domestic Reverse Charge Regulations

A VAT domestic reverse charge (DRC) on valuable metal was introduced in the regulations published in Government Gazette 46512 on 8 June 2022. See Regulations on Domestic Reverse Charge Relating to Valuable Metal, issued under of section 74(2) of the VAT Act, Notice 2140 (the DRC Regulations). The DRC Regulations came into effect on 1 July 2022. Amendments to the DRC Regulations were made in Government Gazette 50642 published on 10 May 2024 (Notice 4793) and came into effect on 1 January 2024 (the amendments). The amendments mainly relate to the definition of 'valuable metal' and 'residue' as well as to certain administrative requirements regarding documentation. For more detailed information on the DRC Regulations, see the Explanatory Memorandum and Media Statement published 8 June 2022. These three documents are available on the SARS website. The frequently asked questions (FAQs) in this document have been compiled on the basis of questions that vendors and the public at large have or are likely to have about the implications of the DRC Regulations.

The FAQs are drafted purely to assist vendors and the public at large to obtain clarity and to ensure consistency on certain practical and technical aspects relating to the DRC Regulations. The FAQs are therefore not intended to be used as legal reference.

The FAQs and the SARS landing page (VAT Regulations on Domestic Reverse Charge relating to Valuable Metal) will be updated periodically to address questions. In light of this, it is not envisaged that VAT Rulings in relation to the DRC Regulations will be issued.

The return and the ruling referred to in the FAQs are available on the SARS website. Unless indicated otherwise, the latest issues of these documents should be consulted.

	Question	Answer
1.	Why were the Domestic Reverse Charge (DRC) Regulations introduced?	The DRC Regulations were introduced as a mechanism to curb the use of the VAT system as a tool to enable the legitimisation of gold where such gold was sourced by illegal means and thereby to stop the registration of a chain of fictitious businesses to secure undue VAT refunds.
2.	What is the effective date of the DRC Regulations as well as the amendments the regulations?	1 July 2022 and 1 January 2024 respectively.
3.	What is the implementation date?	A transition period of one month from 1 July 2022 (the effective date of the DRC Regulations) was allowed for affected vendors to ensure that they made the necessary adjustments to invoicing, accounting systems and other requirements under the DRC Regulations. In light of the invoicing and system practicalities and the circumstances prevailing, the DRC Regulations apply to all supplies of valuable metal from 1 August 2022. All affected vendors were required to have their systems updated during the transition period provided. Also see Questions 33 and 36. Regarding the amendments to the DRC Regulations, the view is held that transactions that have a time of supply before 10 May 2024, must be treated in accordance with the DRC Regulations before the amendments. Affected vendors are given time until 30 June 2024 to amend their systems and issue the correct documentation. Therefore, supplies made

		from 1 July 2024 must comply with the amended DRC Regulations. See Question 23.
4.	Who do the DRC Regulations apply to?	The DRC Regulations apply to all vendors that buy and sell gold and goods containing gold in the specified forms as provided in the definition of 'valuable metal' as defined in regulation 1. Examples of affected vendors are mines, manufacturing businesses, dealers in gold, dealers in second-hand goods (especially those that buy and sell jewellery), gold scrappers, manufacturing, wholesale and retail jewellers, vendors that consume or use gold to manufacture articles containing gold, and coin shops. See also Question 6 for exclusions to the definition of 'valuable metal'.
5.	When does a supply fall within the DRC?	For a supply to fall within the parameters of the DRC, the following four requirements must be met: • The supplier must be a registered vendor. • The recipient must be a registered vendor. • The supply must be of a 'valuable metal' as defined – see Question 6. In short, the good must contain gold and must be in the forms specified in the said definition. • The supply must be taxable at the standard rate, which is currently 15%. This means that any supply that is zero-rated, such as the export of a valuable metal, does not fall in the DRC.

		If any of these four requirements are not met, the supply is not subject to the DRC but is rather subject to the normal provisions of the VAT Act.

6.	What is ‘valuable metal’?	Any goods containing gold in the form of jewellery, bars, blank coins, ingots, buttons, wire, plate, sponge, powder, granules, in a solution, sheet, tube, strip, rod, residue or similar forms, including any ancillary goods or services but excluding supplies:
		• of goods produced from raw materials by any ‘holder’ as defined in section 1 of the Mineral and Petroleum Resources Development Act 28 of 2002 (MPRDA), or by any person contracted to such ‘holder’ to carry on mining operations in respect of the mine where the ‘holder’ carries on mining operations;
		• contemplated in section 11(1)(f), (k) or (m) of the VAT Act; that is, the supply :
		  o to certain entities such as the South African Reserve Bank (SARB) and banks of gold in specified forms such as bars, blank coins, ingots, buttons, wire, plate or granules or in a solution, which has not undergone any manufacturing process, save the refining, manufacture or production of the specified forms;
		  o of gold coins issued by SARB; and

		○ of certain movable goods to a customs controlled area enterprise or a Special Economic Zone (SEZ) operator which are physically delivered to such customs controlled area enterprise or SEZ operator; • of valuable metal containing less than 1% of gold in gross weight; • jewellery plated with gold where the gold is present as a minor constituent only
7.	What forms of goods containing gold are subject to the DRC?	The goods that contain gold must be supplied in one of the forms listed in the definition of ‘valuable metal’ and as set out in Question 6. This means that the good that is supplied must be in the form of jewellery, a bar, blank coin, ingot, button, wire, plate, sponge, powder, granule, in a solution, sheet, tube, strip, rod, residue or similar form
8.	What is ‘residue’?	The term is defined in the DRC Regulations and includes debris, discard, tailings, slimes, screening, slurry, waste rock, foundry sand, beneficiation plant waste or ash derived from, or incidental to, a mining operation.
9.	What does the term ‘similar forms’ in the definition of ‘valuable metal’ refer to?	The term refers to those goods that have similar qualities, characteristics or appearances to those forms already listed. In short, the supply of goods that are alike to the specified forms, but not identical, should fall within the ambit of the DRC.
10.	What is included in ‘ancillary goods or services’?	The term ‘ancillary goods or services’ is not defined but refers to a supply of goods or services that is supplied together with the good

		containing gold and has a sufficient link to the supply of the said good, which would not have been made to the recipient, in the absence of the supply of the valuable metal. The supply of 'ancillary goods or services' on its own, is not subject to the DRC. For example, where a person brings in a wristwatch to a jeweller for cleaning and polishing. Other examples are packaging, alteration, beneficiation services or things such as storage services and other ancillary goods or services supplied together with the good containing the gold.
11.	Are fees charged for assembling, design, engraving, finishing, manufacturing or moulding of valuable metal, part of the consideration payable for valuable metal as 'ancillary goods and services'?	Yes, if the supplier supplies the good containing gold together with these services, the full value charged relates to the supply of 'valuable metal' subject to the DRC.
12.	If I sell a bracelet consisting mainly of platinum, with a small amount of gold, is the supply subject to the DRC?	Before the amendments, the quality and content of the gold contained in the good were of no relevance for purposes of the DRC. The DRC applied to any good that contained gold, regardless of the quality, quantity or content of the gold contained in the good. In terms of the amendments, a de minimis rule has been introduced, resulting in valuable metal containing less than 1% of gold in gross weight being excluded from the ambit of the DRC Regulations. See Question 6.
13.	Is the sale of a finished gold product, for example, a diamond tennis bracelet,	The supply of the entire bracelet (including the diamonds) constitutes 'valuable metal'. It is

	included in the DRC or is it excluding the value of the diamonds in the bracelet?	thus not only the value of the gold element that is subject to the DRC.
14.	Does concentrate fall under the DRC Regulations?	Yes, it falls under 'similar forms'.
15.	Does carbon or coal fall under the DRC Regulations?	The supply of carbon or coal itself generally does not contain gold and therefore falls outside the parameters of the DRC Regulations. However, if the coal or carbon is used as a mechanism to safely package and transport a solution that contains gold, the supply of this solution falls under the DRC. The coal or carbon would then form part of the supply that falls under the DRC Regulations. See Questions 10 and 11.
16.	Does the purchase of silver scrap containing gold content that is immaterial and not charged for, comprise 'valuable metal' as defined?	Before the amendments, the quality, quantity or content of the gold did not matter, as the supply was of a good containing gold. The entire supply of the silver scrap was subject to DRC. However, in terms of the amendments, a de minimis rule has been introduced, resulting in valuable metal containing less than 1% of gold in gross weight being excluded from the ambit of the DRC Regulations. See Question 6.
17.	How will the DRC impact pawnshops that also deal in second-hand jewellery etc that contains precious metals?	To the extent a pawnshop deals in gold products, it must follow the validation process. Supplies of 'valuable metal' made to registered vendors, are subject to the DRC. Supplies to non-registered vendors are not subject to the DRC, but will be subject to VAT under the normal rules.
18.	Does the DRC affect notional input tax claims?	No, the DRC only applies to supplies of valuable metal between registered vendors (suppliers and recipients) whereas notional

		input tax is only allowed where goods are acquired from nonvendors. See guidance on second-hand goods consisting of gold in Binding General Ruling 43 'Deduction of Input Tax in respect of Second-hand Gold'.
19.	Do I need to show the DRC inputs (accumulated from my supplier invoices) separately on my VAT 201 return when selling to the public?	The purchase of a valuable metal and subsequent sale of the said valuable metal are two different transactions for VAT. For the sale transaction, the DRC is only applicable on supplies between registered vendors. Therefore, the DRC will not apply to sales made to the public, which are generally not registered vendors. The retail jeweller will still be liable to levy VAT and reflect such on its tax invoice issued and submit VAT returns as normal. The DRC will apply to the purchase transaction if the goods were acquired from a registered vendor. The DRC does not take away the recipient's entitlement to deduct input tax. The recipient will be required to declare the VAT on the supply of the goods on behalf of the supplier (see regulation 6(b) in Field 12 of its VAT 201 return) and then simultaneously be entitled to make the input tax deduction in Field 18 of its VAT 201 return. Doing it in this manner results in a VAT neutral position. The supplier in this instance will, however, still be required to declare the value of the goods supplied subject to the DRC in Field 3 of its VAT 201 return.
20.	If an invoice has both loose diamonds and finished jewellery, will there be a need to have a line for VAT	Yes.

	on the loose diamonds and separately for the goods that are subject to the DRC at the bottom of the invoice?	
21.	Will vendors that are selling to other vendors as well as the general public need to track the split in their sales between sales to vendors and the general public?	Yes, vendors will have to keep records to track the split, as both the supplier and recipient have different responsibilities for normal supplies vs supplies under the DRC. Supplies to the general public that are not registered vendors, are not subject to the DRC. The supplier must keep a list of all supplies subject to the DRC [see regulation 2(f)]
22.	Would local VAT-registered vendors selling valuable metal to registered vendors fall under the DRC even if all their products are imported?	Yes, the origin of the product is not important for purposes of the DRC. The test is rather whether the supply of the goods (being a 'valuable metal' as defined in the DRC) is supplied by a registered vendor to a recipient which is also a registered vendor. The importation itself would not be subject to the DRC, on the basis that it is acquired from a foreign supplier that is not a registered vendor.
23.	When must the supplier and recipient respectively account for supplies subject to the DRC?	The supplier must issue a tax invoice and account for the VAT-exclusive value of the valuable metal in Field 3 of the VAT 201 return for the tax period in which the time of supply is triggered (generally the earlier of payment received or invoice issued). The recipient must account for the VAT on the supply of valuable metal in Field 12 on the VAT 201 return for the tax period in which the tax invoice in respect of the supply of valuable metal is held by the recipient. The recipient may deduct the VAT so declared and reflect same in Field 18 of the VAT 201 return, subject to the normal documentary requirements for input tax.

24.	Must a purchaser first physically pay the VAT (reverse charged) to SARS?	No, the DRC does not require the purchaser who is a vendor to first pay the VAT. However, the seller must reflect the value of the sale on its VAT 201 return under Field 3. The output tax (Field 12) and input tax (Field 18) is accounted for on the recipient's normal VAT 201 return, and the recipient will calculate the VAT payable to, or refundable by, SARS as normal. Depending on whether the return results in a refund or a payment, the normal rules for the payment of tax or the refund of tax apply.
25.	When can a purchaser claim the input tax?	In the tax period in which the recipient is in possession of a valid tax invoice. Input tax is not deductible if the output tax in Field 12 in respect of the purchase, is not declared, irrespective of whether payment for that supply is made to the supplier.
26.	What wording must be contained in the statements to be included in invoices, credit notes and debit notes?	The DRC Regulations do not contain prescribed wording, save to say that there must be a statement that the supply is subject to the DRC (see regulation 4).
27.	What should the layout of invoices, credit notes and debit notes look like if VAT is charged but not included in the total payable by the purchaser?	The DRC Regulations do not prescribe these.
28.	Is the list of all supplies of valuable metal that are subject to the DRC that must be kept by the supplier and the statement to be provided by the purchaser to the supplier, the same?	No, the first is a list that must be kept by the supplier under regulation 2(f), and the second is a statement that must be issued by the recipient to the relevant supplier under regulation 3(e).

29.	Regulation 3(a) requires that the recipient of a supply of valuable metal furnishes the supplier with proof that the recipient is a registered vendor for VAT purposes. Is this required for each supply or once for each supplier?	The DRC Regulations do not specify that this is a requirement for each supply. However, the supplier and recipient must have control measures in place to ensure that the counter-party's registration status is updated, if applicable.
30.	Under regulation 3(c), the DRC is only accounted for in the tax period in which the recipient obtains or creates a tax invoice, irrespective of when payment or part-payment was made. If no tax invoice with the required information in section 20(4) and regulation 4 is obtained, must the recipient account for the VAT charged by the supplier?	If the recipient is in possession of a tax invoice stating that the supply is subject to the DRC, the recipient is required to account under the DRC. Should the tax invoice be deficient for purposes of deducting input tax, for example, the recipient's VAT registration number is not on the tax invoice, the recipient must request the supplier to correct same [see section 20(1B)]. The recipient can only deduct the input tax once in possession of a tax invoice that complies with section 20. See Question 25.
31.	If a valid tax invoice for the supply of valuable metal is obtained, must the VAT be accounted for accordingly in that tax period, notwithstanding the fact that the invoice may be disputed?	Yes, see Question 23.
32.	Is the number of days referred to in regulation 3(e) calendar days or business days?	Calendar days.

33.	How do the transitional rules work?	For details on how the transitional rules work for different categories of tax periods, please click on this link, VAT DRC transitional measures, available on the landing page (VAT regulations on Domestic Reverse Charge relating to valuable metal) on the SARS website. Also see Question 3.
34.	I am a supplier of valuable metal to a registered vendor that will be unable to account for these supplies due to system constraints. Can I continue levying and accounting for VAT on supplies made to this vendor?	No, the supplier and the recipient are required to comply with the DRC Regulations. If there is a failure to comply, the supplier and the recipient are jointly and severally liable for any loss suffered by the fiscus. The supplier, however, will not be held liable, should the supplier satisfy SARS that reasonable steps were followed to comply with the relevant obligations (see regulation 7).
35.	Do I need to wait for my validation certificate before I commence complying with the DRC Regulations?	No, regardless of whether you have received any correspondence from SARS regarding revalidation, you are required to comply with the DRC Regulations as stipulated in Question 3. The onus remains on the vendor to re-validate their registration status.
36.	When will I get feedback or progress updates regarding my re-validation?	You will not receive progress updates regarding your re-validation but may receive requests for further information. Once the re-validation process is completed, you will be informed whether or not your re-validation has been successful. Should your re-validation be incomplete or deficient in any way, you will be required to re-apply with the correct or updated information. An incomplete or deficient re-validation request does not mean that you are exempt from applying the DRC Regulations.

8. 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.