

## **TAX UPDATE**

**For period: 1 April 2016 to 30 June 2016**

**Prepared by: Johan Kotze**



## **TABLE OF CONTENTS**

|                                                                                                                                                           |           |
|-----------------------------------------------------------------------------------------------------------------------------------------------------------|-----------|
| <b>1. INTRODUCTION</b>                                                                                                                                    | <b>4</b>  |
| <b>2. NOTICES &amp; REGULATIONS</b>                                                                                                                       | <b>5</b>  |
| 2.1. Income Tax 2016: Notice to furnish returns for the 2016 year of assessment                                                                           | 5         |
| <b>3. CASE LAW</b>                                                                                                                                        | <b>9</b>  |
| 3.1. Krok v C:SARS                                                                                                                                        | 9         |
| 3.2. South African Reserve Bank v Shuttleworth & another                                                                                                  | 17        |
| 3.3. ITC 1879                                                                                                                                             | 28        |
| 3.4. Anglo Platinum Management Services (Pty) Ltd v C:SARS                                                                                                | 32        |
| 3.5. C:SARS v Stepney Investments (Pty) Ltd                                                                                                               | 39        |
| 3.6. ITC 1880                                                                                                                                             | 49        |
| 3.7. ITC 1881                                                                                                                                             | 56        |
| 3.8. ITC 1882                                                                                                                                             | 60        |
| <b>4. INTERPRETATION NOTES</b>                                                                                                                            | <b>66</b> |
| 4.1. Provisional tax estimates – No. 1 (Issue 2)                                                                                                          | 66        |
| 4.2. VAT treatment of the supply of goods or services to and/or from a customs controlled areas of an industrial development zone – No. 40 (Issue 3)      | 68        |
| <b>5. DRAFT INTERPRETATION NOTES</b>                                                                                                                      | <b>71</b> |
| 5.1. Exemption from income tax: foreign employment income                                                                                                 | 71        |
| 5.2. Taxation of REITs and controlled companies                                                                                                           | 72        |
| 5.3. Exemption from income tax: Remuneration derived by a person as an officer or crew member of a ship                                                   | 75        |
| <b>6. BINDING PRIVATE RULINGS</b>                                                                                                                         | <b>76</b> |
| 6.1. BPR 227 – Share subscription transaction followed by two share repurchase transactions                                                               | 76        |
| 6.2. BPR 228 – Whether an investment of preference share funding funding in a newly established business is for a 'qualifying purpose'                    | 80        |
| 6.3. BPR 229 – Employer provided accommodation to employees                                                                                               | 82        |
| 6.4. BPR 230 – Disposal of an asset in terms of an asset-for-share transaction within 18 months of its acquisition in terms of an intra-group transaction | 83        |
| 6.5. BPR 231 – Corporate restructuring by way of asset-for-share and amalgamation transactions                                                            | 85        |
| 6.6. BPR 232 – Equity shares to be issued by resultant company as part of an amalgamation transaction                                                     | 92        |
| 6.7. BPR 233 – Transfer of a part of a business to a fellow subsidiary                                                                                    | 93        |

|                                                                                                                                       |            |
|---------------------------------------------------------------------------------------------------------------------------------------|------------|
| 6.8. BPR 234 – Asset-for-share and unbundling transactions not regulated by sections 42 and 46                                        | 100        |
| 6.9. BPR 235 – Income tax consequences for parties to an unbundling transaction                                                       | 103        |
| 6.10. BPR 236 – Set-off of a loan account arising from an intra-group transaction to acquire equity shares                            | 106        |
| 6.11. BPR 237 – Reinstatement of a deregistered company to transfer immovable properties                                              | 110        |
| 6.12. BPR 238 – Taxation of receipts by or accruals to a programme of activities of a clean development mechanism project             | 113        |
| 6.13. BPR 239 – Cash contributions made to a special purpose vehicle established to provide housing to mine workers                   | 117        |
| 6.14. BPR 240 – Taxation of parties to share index linked notes                                                                       | 120        |
| 6.15. BPR 241 – Award received for a black economic empowerment (BEE) training initiative                                             | 123        |
| 6.16. BPR 242 – Venture capital company investment in qualifying companies carrying on business as hotelkeepers                       | 127        |
| <b>7. BINDING CLASS RULING</b>                                                                                                        | <b>132</b> |
| 7.1. BCR 52 – Income tax and securities tax consequences for the shareholders of a listed company following an unbundling transaction | 132        |
| 7.2. BCR 53 – Programme of activities of a clean development mechanism project                                                        | 135        |
| <b>8. BINDING GENERAL RULING</b>                                                                                                      | <b>140</b> |
| 8.1. BGR 32 – VAT treatment of specific supplies in the short-term reinsurance industry                                               | 140        |
| 8.2. BGR 33 – The Value-Added Tax treatment of the supply and importation of vegetable oil                                            | 145        |
| 8.3. BGR 34 – Management of superannuation schemes: Long-term insurers                                                                | 147        |
| 8.4. BGR 35 – The value-added tax treatment of the supply and importation of frozen potato products                                   | 155        |
| <b>9. GUIDES</b>                                                                                                                      | <b>158</b> |
| 9.1. Guide for Share Block Schemes – VAT 412                                                                                          | 158        |
| 9.2. VAT Guide for Entertainment, Accommodation and Catering – VAT411                                                                 | 159        |
| <b>10. DRAFT GUIDES</b>                                                                                                               | <b>162</b> |
| 10.1. Guide on the taxation of professional sports club and players                                                                   | 162        |
| <b>11. INDEMNITY</b>                                                                                                                  | <b>162</b> |

## 1. INTRODUCTION

The purpose of this update is to summarise developments that occurred during the second quarter of 2016, specifically in relation to Income Tax and VAT. Johan Kotze, who is a Tax Executive at Shepstone & Wylie Attorneys, has compiled this summary.

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

Consider the notice to furnish income tax returns for 2016 and your specific deadline. This notice made me think that I am glad I learned in school about parallelograms instead of how to do tax. It's really come in handy this parallelogram season. (sic.)

The cases are always interesting to read and should help you to plan your affairs.

I do find reading Mark Shuttleworth's case against the Reserve Bank quite interesting.

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

Enjoy reading on!

## 2. NOTICES & REGULATIONS

### 2.1. *Income Tax 2016: Notice to furnish returns for the 2016 year of assessment*

1. Notice is hereby given in terms of section 66(1) of the Income Tax Act, 1962 (Act No. 58 of 1962) ('the Act') read together with section 25 of the Tax Administration Act, 2011 (Act No. 28 of 2011), that a person who is required in terms of paragraph 2 to furnish a return, must furnish a return in respect of the 2016 year of assessment within the period prescribed in paragraph 4 below.
2. The following persons must furnish an income tax return:
  - (a) every company, trust or other juristic person, which is a resident;
  - (b) every company, trust or other juristic person, which is not a resident—
    - (i) which carried on a trade through a permanent establishment in the Republic;
    - (ii) which derived income from a source in the Republic; or
    - (iii) which derived any capital gain or capital loss from a source in the Republic;
  - (c) every company incorporated, established or formed in the Republic, but which is not a resident as a result of the application of any agreement entered into with the Government of any other country for the avoidance of double taxation;
  - (d) every natural person—
    - (i) who carried on any trade in the Republic (other than solely in his or her capacity as an employee);
    - (ii) to whom an allowance or advance was paid or granted as described in section 8(1)(a)(i) of the Act (other than an amount reimbursed or advanced as described in section 8(1)(a)(ii)) and whose gross income exceeded the thresholds

set out in item (viii);

- (iii) who had capital gains or capital losses exceeding R30 000;
  - (iv) who is a resident and held any funds in foreign currency or owned any assets outside the Republic, if the total value of those funds and assets exceeded R225 000 at any stage during the 2016 year of assessment;
  - (v) who is a resident and to whom any income or capital gains from funds in foreign currency or assets outside the Republic could be attributed in terms of the Act;
  - (vi) who is a resident and held any participation rights, as referred to in section 72A of the Act, in a controlled foreign company;
  - (vii) to whom an income tax return is issued or who is requested by the Commissioner in writing to furnish a return, irrespective of the amount of income of that person; or
  - (viii) who, subject to the provisions of paragraph 3, at the end of the year of assessment—
    - (aa) was under the age of 65 and whose gross income exceeded R73 650;
    - (bb) was 65 years or older (but under the age of 75) and whose gross income exceeded R114 800; or
    - (cc) was 75 years or older and whose gross income exceeded R128 500;
- (e) every non-resident whose gross income consisted of interest from a source in the Republic to which the provisions of section 10(1)(h) of the Act, do not apply; and
- (f) every representative taxpayer of any person referred to in subparagraphs (a) to (e) above.
3. A natural person is not required to furnish a return for the 2016 year of assessment in terms of paragraph 2(d)(viii) if the gross income of that

person consisted solely of gross income described in one or more of the following subparagraphs:

- (a) remuneration, other than an allowance or advance referred to in paragraph 2(d)(ii) above, paid or payable from one single source, which does not exceed R350 000 and employees' tax has been deducted or withheld in terms of the deduction tables prescribed by the Commissioner;
- (b) Interest from a source in the Republic not exceeding—
  - (i) R23 800 in the case of a natural person below the age of 65 years; or
  - (ii) R34 500 in the case of a natural person aged 65 years or older; and
- (c) dividends and the natural person was a non-resident throughout the 2016 year of assessment.

4. Returns in respect of the 2016 year of assessment must be furnished within the following periods:

- (a) in the case of any company, within 12 months from the date on which its financial year ends; or
- (b) in the case of all other persons (which include natural persons, trusts and other juristic persons, such as institutions, boards or bodies)—
  - (i) on or before 23 September 2016 if the return is submitted manually;
  - (ii) on or before 25 November 2016 if the return is submitted by using the SARS eFiling platform or electronically through the assistance of a SARS official at an office of SARS;
  - (iii) on or before 31 January 2017 if the return relates to a provisional taxpayer and is submitted by using the SARS eFiling platform; or
  - (iv) where accounts are accepted by the Commissioner in terms

of section 66(13A) of the Act in respect of the whole or portion of a taxpayer's income, which are drawn to a date after 29 February 2016, but on or before 30 September 2016, within 6 months from the date to which such accounts are drawn.

5. The forms prescribed by the Commissioner for the rendering of returns are obtainable *via* the internet at [www.sarsefiling.co.za](http://www.sarsefiling.co.za) or on request or on application from any office of SARS, other than an office which deals solely with matters relating to customs and excise.
6. Returns must—
  - (a) in the case of a company, be submitted electronically by using the SARS eFiling platform; and
  - (b) in the case of all other persons (which include natural persons, trusts and other juristic persons, such as institutions, boards or bodies), be—
    - (i) submitted electronically by using the SARS eFiling platform, provided the person is registered for eFiling;
    - (ii) forwarded by post to SARS;
    - (iii) delivered to an office of SARS, other than an office which deals solely with matters relating to customs and excise; or
    - (iv) delivered to such other places as designated by the Commissioner from time to time.
7. If a person who is required to render a return fails to do so within the period mentioned in paragraph 4 above, that person is liable on conviction to a fine or to imprisonment for a period not exceeding two years. SARS may also estimate that person's taxable income, impose a penalty in respect of the failure to submit the return within the required period or both.
8. A taxpayer who knowingly and wilfully makes any false statement in a return or evades or attempts to evade taxation, or a person who assists a taxpayer to do so, is liable on conviction to a fine or to imprisonment for a

period of up to five years. A penalty up to two times the amount of tax which was evaded may also be imposed.

9. No person is exempted from any penalty merely by reason of the fact that the person may not have been called upon personally to furnish a return.
10. For purposes of this notice, any word or expression to which a meaning has been assigned in the Act bears the meaning so assigned, and '2016 year of assessment' means—
  - (a) in the case of a company, the financial year of that company ending during the 2016 calendar year; and
  - (b) in the case of any other person, the year of assessment commencing on 1 March 2015 or ending on 29 February 2016.

### **3. CASE LAW**

#### **3.1. *Krok v C:SARS***

Mark Krok, being Mark Krok, had inherited a significant amount of assets that had originated from the Abraham Krok Trust, which had been formed out of donations made to its trustees in 1973 by Ms Sarah Krok for the benefit of Mr. Abraham Krok's six children, of whom Mr. Krok was one. In 1994, Mr. Krok's father created new separate trusts to which the assets of the Abraham Krok Trust were transferred for the benefit of each of these children.

One of the new trusts was the Mark Krok 1994 Trust ('the trust') in which Mr. Krok accumulated considerable capital assets valued at R71 713 807 as at 28 February 2003 and these assets at that stage mainly comprised shares in various listed and unlisted South African companies and cash investments.

Mark Krok emigrated to Australia in April 2002 and prior to that event he had sought professional advice on the implications of keeping the assets in the trust having regard to the South African Exchange Control Regulations, 1961 and, as a result, structured his affairs by setting up an elaborate scheme to avoid adverse exchange control implications. He claimed that he had ceded all his South African

income and assets to a company in the British Virgin Islands, Polperro Enterprises, except for the bare ownership thereof, and he had no income or capital gains on which he could be taxed by the Australian Tax Office (ATO) under the agreements.

Mark Krok, in December 2008, then emigrated from Australia to the United Kingdom and again set up a similar tax avoidance scheme in respect of which he purported to transfer to the Second Appellant, Jucool Enterprises Inc, a company incorporated in the British Virgin Islands, his assets situated in South Africa.

Mark Krok was further advised to establish a discretionary trust for UK income, inheritance and capital gains tax purposes and the necessity for asset protection. On that basis he concluded certain agreements with Jucool on 29 December 2008 and these agreements were not dissimilar to those that he had earlier concluded with Polperro, which were terminated at his instance leaving him in control of the assets.

One of the aforesaid agreements was an 'Income Sale Agreement' in terms of which Jucool purchased from Mark Krok certain specified rights and interests in the assets listed in that agreement and, effectively, the purpose of this transaction was to transfer to Jucool the income derived from the assets owned by Mark Krok and the plain objective of this was to separate the right to enjoy the assets from the bare *dominium*, the notion being that the 'beneficial ownership' of the assets would pass from Mark Krok to Jucool and he would retain only the legal ownership of the assets, which legal ownership he would hold on trust for Jucool. The other agreement was an 'Asset Sale Agreement' in terms of which Jucool purchased from Mark Krok those rights and interests in the assets which had not been sold by him to Jucool in terms of the Income Sale Agreement.

In 2009 the ATO launched an audit of Mark Krok's taxation affairs which started with his income tax submission for the income year ended 28 February 2003 and carried through to his application to the South African Reserve Bank in February 2010 for the release of funds to cover his holiday and visiting expenses in the country during 2010.

The aforementioned audit was part of a government initiative investigating participation by Australians in internationally promoted tax arrangements to identify taxpayers involved in significant offshore transactions or large transfers of funds to

or from Australia.

Consequent upon the investigation, the ATO concluded that Mark Krok had intended to conceal foreign income and avoid income tax in Australia as shown, for example, by the use of entities established in banking secrecy jurisdictions such as the British Virgin Islands and Liechtenstein.

In the ATO's view, Mark Krok had omitted assessable income from his income tax returns that was derived from assets, including those administered on his behalf by Investec, which he held in South Africa whilst an Australian resident and also concealed capital gains on disposals of those assets when he ceased to be an Australian resident.

The ATO had further determined that Mark Krok had retained legal and beneficial interests in the assets and that 'the purported assignment arrangement' of his rights and interests to the capital and income of these assets to Polperro had breached the South African exchange control regulations and was a sham.

For the aforementioned reasons the ATO accordingly amended his income tax returns for the income years and issued notices of assessment of tax and penalties and Mark Krok's objection to the assessments under the procedures provided by Australian law was disallowed in full.

The ATO thereafter requested assistance on 6 February 2013 in terms of article 25A of the Agreement for the Avoidance of Double Taxation and the Prevention of Fiscal Evasion with respect to Taxes on Income of 1 July 1999 (the DTA) between South Africa and Australia in order to collect income taxes allegedly due by Mark Krok to the Australian Commissioner, in the sum of Australian \$25 361 875,79 plus interest for the relevant income years.

The ATO thus sought the conservancy of Mark Krok's assets situated in South Africa pending the collection of the tax debt and the request was accompanied by a formal certificate, as envisaged in sections 185(2) and 3(a) and (b) of the Tax Administration Act.

Upon the ATO's request for SARS' assistance, the Respondent applied successfully to the Gauteng Division of the High Court for a provisional preservation order on an *ex parte* basis against the Mark Krok in order to secure

assets for purposes of satisfying an alleged tax debt and for the appointment of a *curator bonis* in terms of sections 163 and 185 of the Tax Administration Act and the determination of this question depended on the temporal scope of the provisions of the aforementioned double taxation agreement between South Africa and Australia which was subsequently amended by a Protocol signed on 31 March 2008 which made provision for mutual assistance in the collection of taxes.

The provisional preservation order was subsequently confirmed by the High Court (see *C:SARS v Krok and Another* 76 SATC 119) and the assets specified under the order comprised immovable property, cash investments, a motor vehicle and various listed and unlisted securities of considerable value held in Mark Krok's name or on his behalf by nominees. The rights, title and interest in these assets would vest in the *curator bonis*, to whom Mark Krok was obliged to disclose all his assets and sources of income held in South Africa and their location, until the tax debt was satisfied or proper arrangements for purposes of the tax collection were made.

In the court below the issues were characterised as follows:

- Whether SARS had proved its case in the context of section 185 of the Tax Administration Act and the Protocol;
- Whether the facts justified a reasonable apprehension of dissipation of the assets; and
- Whether the introduction of article 25A into the DTA applied to the taxes claimed by the ATO for the income years all of which arose before 1 July 2009.

Among the defenses raised on Mark Krok's behalf was that the tax claimed by the ATO fell outside the scope of the DTA and this was so, it was argued, because the Protocol came into effect on 12 November 2008, and in terms of article 13(2)(a)(ii) thereof, with regard to Australian tax applies to income, profit or gains accrued on or after 1 July on the calendar year following the date on which it came into force and the Protocol, so it was contended, therefore applied only in respect of income, profits or gains of any year of income beginning on or after 1 July 2009.

Jucool further contended that the preservation order should not be confirmed even

if the aforementioned defenses failed as it was the beneficial owner of the assets subject to the preservation order.

The court below was not persuaded by any of the aforementioned contentions and on appeal before the Supreme Court of Appeal the only argument persisted in on Mark Krok's behalf was that, on a proper interpretation of article 25A of the DTA, and article 13(2)(a)(ii) of the Protocol, article 25A could be invoked only if the taxes claimed by the ATO arose on or after 1 July 2009 and this was so, it was contended, because in terms of the common law revenue rule, any assistance that can be provided by one State to another under article 25A is limited to the collection of 'revenue claims' i.e. amounts owed in respect of taxes referred to in article 2 of the DTA. And, in the case of Australia, in terms of article 13(2)(a)(ii) read with article 3(1)(c), which defines 'Australian tax' to which the reach of article 25A is confined, the Australian taxes referred to in article 2 only apply to income, profits or gains in relation to years of income commencing on or after 1 July 2009 and as the taxes claimed here arose before the latter date, they fell beyond the scope of the DTA and there was thus no basis for the invocation of the conservancy provisions of the Tax Administration Act.

Mark Krok and Jucool further contended that the court below had overlooked the general rule of interpretation that in the absence of express provisions to the contrary, statutes should be construed as affecting future matters only and in this regard it was argued that the court had erroneously accepted SARS' contention that article 25A applied retrospectively to all taxes since the inception of the DTA notwithstanding the express provisions of article 13(2)(a)(ii).

Jucool supported the aforementioned contentions and again argued against the confirmation of the preservation order even if the defenses failed on the further basis that it was the beneficial owner of the assets subject to the order.

Judge Maya held the following:

- (i) That the DTA and the Protocol, which came into effect on 12 November 2008, were concluded in terms of section 108(2) of the Income Tax Act read with section 231(4) of the Constitution of the Republic of South Africa, 1996 and thus they became part of South African law as they were approved by the legislature under these provisions and duly gazetted.

- (ii) That, in its original form, the DTA made no provision for reciprocal assistance in the collection and enforcement of foreign taxes in the courts of the two States. It merely catered for mitigation of double taxation of taxpayers who would otherwise be liable for tax in two jurisdictions in respect of the same taxable gain or income by allocating taxation rights between convention or treaty parties. Furthermore, it provided for the exchange of any information necessary for the carrying out of its terms or the domestic law of the contracting States concerning the relevant taxes. The Protocol amended the DTA by, *inter alia*, making provision for the two States to assist each other in the collection of taxes and securing preservation orders for purposes of recovering taxes.
- (iii) That the provisions of the Tax Administration Act, which was promulgated after the Protocol came into effect ‘to ensure the effective and efficient collection of tax’ not only in respect of taxes imposed by South Africa on its subjects, but also on behalf of foreign governments, are consistent with the Protocol’s objectives.
- (iv) That before the enactment of the aforementioned provisions and the introduction of article 25A into the DTA, the revenue rule prevailed and in terms of this international law rule, which forms part of South African law, the courts of one State are precluded, in the absence of a permissive rule to the contrary, from entertaining legal proceedings involving the enforcement of the revenue laws of another State – an attribute of sovereignty. Thus a foreign State may not have a claim for taxes payable to its *fiscus* enforced in another State as this would be tantamount to derogation of the other State’s territorial supremacy. For that reason, South African courts had no power to order the attachment of assets for the purposes of enabling a foreign State to recover taxes owed to it until the rule was abrogated by the introduction of article 25A in the DTA and other double taxation agreements containing similar provisions.
- (v) That, regarding the approach to be adopted in construing the relevant provisions, consideration must be had to the rules applicable in the interpretation of treaties which are binding on South Africa and all States as

rules of customary international law.

- (vi) That it was established, as the parties acknowledged, that the revenue rule, which is concerned with the enforcement of taxes, did not constitute an absolute proscription of the recognition of foreign revenue laws and may be abrogated by convention or treaty. Evidently, the reason for the rule between South Africa and Australia ceased to exist once the two countries agreed to assist each other in the collection of taxes and in that case the rule itself had no relevance whatsoever in the determination of the meaning and scope of the Protocol.
- (vii) That similarly wrong was Mark Krok's argument relating to the South African taxpayers' purported expectations based on the revenue rule, were it relevant for present purposes. The argument obviously misconceives the nature of the rule which does not exist for the benefit or protection of taxpayers and a court's application of the rule or its abrogation is therefore not concerned with any rights of a taxpayer.
- (viii) That article 13 did not purport to form part of the DTA and its plain wording merely pronounces that the Protocol shall form an integral part of the DTA and provides the dates from which the amendments to the DTA provided by the Protocol in respect of the matters specified in article 13 would come into effect, i.e. on the date of the last notification. Article 13(2)(a)(ii), the mainstay of the appellants' argument on how article 25A should be construed, makes reference to 'other Australian tax' and this can only mean Australian tax other than the withholding tax on income mentioned in article 13(2)(a)(i). The DTA defines 'Australian tax' in article 3(c) as tax to which the DTA applies by virtue of its article 2. And as indicated above, such tax would be that specified in arts 2.1(a) of the DTA and it must follow that the 'other Australian tax' referred to in article 13(2)(a)(ii) is 'income tax, including the resource rent tax' envisaged in article 2.1 but excluding the withholding tax on income referred to in article 13.2(a)(i) and this starkly illustrated the fallacy in the appellants' interpretation of article 2 and, in particular, the term 'revenue claim'.
- (ix) That article 25 provides no temporal limitations relating to exchange of

information and in terms of article 13(2)(c) the Protocol would have effect for purposes of article 25 from the date on which the Protocol entered into force. Thus, article 25 would take effect simultaneously with the Protocol, on 12 November 2008, in respect of taxes of every kind and description and without any limitation regarding the time periods in relation to which information would be exchanged. This inevitable result certainly does not accord with what would be produced by the appellants' interpretation of article 2, i.e. that only information concerning 'other Australian tax' in respect of income profits or gains arising after 1 July 2009 may be exchanged.

- (x) That there was clearly no basis to construe article 25A as being subject to article 13(2)(a)(ii) and there was equally no merit in the retrospectivity point which the appellants properly conceded during argument. The rule against retrospectivity bears no relevance in this case. The effect of article 25A is plainly prospective as it could only be invoked when the relevant countries so agreed and its provisions came into force. Tax claims which arose in the past in respect of which assistance was sought would also be covered.
- (xi) That it was a firmly established principle of our law that a statute is not retrospective merely 'because a part of the requisites for its action is drawn from time antecedent to its passing.' The appellants' own argument supported this position because they paradoxically accepted that article 25A, which it was common cause came into force on 1 July 2010, may be applied to Australian tax in respect of income profits or gains in any year of income beginning on or after 1 July 2009.
- (xii) That, therefore, when article 25A entered into force on 1 July 2010 in terms of article 13(2)(d), it applied to a revenue claim, i.e. an amount owed in respect of taxes of every kind and description to which article 13(2)(a)(ii) had no application and hence Mark Krok's jurisdictional challenge to the preservation order accordingly failed.
- (xiii) That in regard to Jucool's claim that the preservation order should nevertheless be discharged because SARS had pursued these proceedings in total disregard of its ownership of the beneficial interest in

the assets in question, despite having notice thereof, it seemed that this issue could safely be decided simply by determining whether or not ownership in the assets passed from Mark Krok to Jucool.

- (xiv) That, assuming, without deciding, in the appellants' favour, that the agreements were binding and valid under the law of the British Virgin Islands, there was an insuperable difficulty with which Jucool had to contend. The assets were situated in South Africa and not in the British Virgin Islands and their fate must accordingly be decided in terms of the relevant South African law. In particular, as the court was concerned with the question whether the ownership of assets situated in South Africa passed from Mark Krok to Jucool, the law of South Africa (the *forum rei sitae*) governed and this was also in accordance with English common law, which is the law applicable in the British Virgin Islands.
- (xv) That none of the legal requirements appear to have been met in respect of the assets in issue – both movable and immovable property. And this also applied to the lesser rights in the incorporeal movables such as the right to income derived from the shares which would have required transfer by way of cession and hence Jucool has not shown that the court below had erred in finding that it had failed to prove its beneficial ownership in the assets and confirming the preservation order.

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

### **3.2. South African Reserve Bank v Shuttleworth & another**

The First Respondent, being Mr. Shuttleworth, applied to the Reserve Bank in 2009 for permission to transfer approximately R2,5 billion out of South Africa and the Reserve Bank granted him permission to transfer this amount on condition that he paid the exit levy provided for in Regulation 10(1)(c) of the Exchange Control Regulations of 1961.

Mr. Shuttleworth was a prominent South African entrepreneur who felt that he had fallen victim to an invalid tax and wanted it to be set aside by the courts.

In 2001, Mr. Shuttleworth had emigrated to the Isle of Man and he maintained that he left the country in order to free up his funds for investment outside South Africa. He was of the view that the exchange control system of the time was severely restrictive and had rendered cross-border investments prohibitive.

The Exchange Control Regulations blocked the transfer of Mr. Shuttleworth's assets from South Africa and the capital amount could not be transferred without authorisation of the South African Reserve Bank (Reserve Bank). He applied to the Reserve Bank to transfer out of South Africa approximately R2,5 billion blocked under the exchange control system.

The Reserve Bank, seemingly acting on a determination by the Minister of Finance, imposed an exit charge of 10% on the capital he wanted exported and he paid the charge of approximately R250 million.

Mr. Shuttleworth was later advised that the exit charge was a tax and had been imposed in a manner not permitted by the Constitution or the applicable statute. Mr. Shuttleworth also wanted the exit charge set aside for another reason as he argued that the entire exchange control system, or its specified parts, was at odds with the Constitution and was invalid.

Before coming to the Constitutional Court, this contest had been to the North Gauteng High Court, Pretoria (High Court) (see *Shuttleworth v South African Reserve Bank and Others* 76 SATC 160) and the Supreme Court of Appeal (see *Shuttleworth v South African Reserve Bank and Others* 77 SATC 145).

The High Court had held for the Reserve Bank and the Minister that the exit charge was not a revenue-raising tax and had been lawfully imposed. It did, however, hold a few and discrete exchange control legislative provisions to be unconstitutional.

The High Court held that the exit charge was not 'calculated to raise revenue' and therefore regulation 10(1)(c) was not invalid for failing to comply with section 9(4) of the Act.

The Supreme Court of Appeal then held, in the main for Mr. Shuttleworth and it set aside the order of the High Court in its entirety by concluding that the imposition of a charge on Mr. Shuttleworth's transfer of his blocked assets out of South Africa was unlawful because it had not been passed in accordance with the procedure

that the Constitution prescribed for a money Bill and it directed the Reserve Bank to repay the amount paid by him, with interest.

The Supreme Court of Appeal held that notwithstanding the fact that the regulation was intended to ensure the regulation of the outflow of funds and that conditions could be attached to the export of capital, it did not follow that the regulation was intended to or could be utilised as a revenue-raising mechanism. The exit levy was a revenue-raising mechanism for the State and it was unconstitutional for taxes or levies to be raised by delegated legislation which was not specifically authorised in a Money Bill enacted in accordance with the Money Bill provisions of the Constitution.

Furthermore, the Supreme Court of Appeal held that the reference in regulation 10(1)(c) to the power of the Treasury to impose conditions on the export of capital from South Africa could not be construed to include the power to impose a tax or levy on such export of capital and it thus found that the imposition of the 10% levy was inconsistent with sections 75 and 77 of the Constitution and thus invalid.

The Supreme Court of Appeal, in contrast, refused to decide whether any of the exchange control provisions were inconsistent with the Constitution and invalid.

The Reserve Bank and the Minister felt hard done by the order of the Supreme Court of Appeal and now sought leave to appeal against it and this constituted the main appeal in the Constitutional Court and, should the Constitutional Court grant leave, Mr. Shuttleworth, in turn, had asked for leave to cross-appeal against the decision of the Supreme Court of Appeal on the discrete question of the constitutional validity of the exchange control legislative scheme, i.e. whether section 9(1) of Act 9 of 1933 and regulation 10(1)(c) of the Exchange Control Regulations were constitutionally valid.

Leave to appeal in the main appeal was granted and leave to cross-appeal was granted but only in respect of the attack on the constitutional validity of the section of the Act that enabled the making of regulations and the provision in the regulations prohibiting the export of capital without authorisation under certain conditions.

In the Constitutional Court the decisive question was whether the exit charge, as

Mr. Shuttleworth contended, was a tax imposed for the purpose of raising revenue for the State or, as the Reserve Bank and the Minister submitted, a regulatory charge whose main object was to disincentivise the export of capital. If the charge was a tax – a revenue-raising mechanism – then the regulation that authorised the exit charge would be invalid and this would be so because the exit charge had not been enacted in accordance with prescribed constitutional and statutory strictures.

Regulation 10(1)(c) of the Currency Exchange Control Regulations ('the regulations') promulgated under the Currency and Exchanges Act 9 of 1933 ('the Act') provided that 'no person shall, except with permission granted by the Treasury and in accordance with such conditions as the Treasury may impose . . . enter into any transaction whereby capital or any right to capital is directly or indirectly exported from South Africa.' The Regulations define 'Treasury' as the Minister of Finance ('the Minister') and the practice evolved of the Minister announcing during his annual budget speech the conditions that he had imposed in relation to the export of capital from South Africa and the Reserve Bank then reducing the Minister's announcement of the conditions into public circulars.

In a budget speech delivered in 2003, the Minister imposed a 10% exit charge on capital exceeding R750 000 as a condition to the export of that capital.

In practice this meant that the regulations blocked the expatriation of Mr. Shuttleworth's assets from South Africa and the aggregate value of his blocked loan account was just over R4,2 billion.

In the result Mr. Shuttleworth paid the exit charge but he explained that he had paid the charge in the belief that it was lawfully due. However, during June 2009, he decided to transfer his remaining capital out of South Africa and, ahead of applying to the Reserve Bank for permission to do so, he sought advice on the lawfulness of the exit charge and he was advised that it was unlawful and he paid the levied amount of just over R250 million under protest pending the reconsideration of the decision and hence he approached the High Court for relief when the Reserve Bank refused to reconsider its decision to impose the exit charge.

Judge Moseneke held the following majority judgment:

As to the grant of leave to appeal

- (i) That it was in the interests of justice to grant the Reserve Bank and the Minister leave to appeal the decision of the Supreme Court of Appeal. The dispute before the court engaged constitutional guarantees related to property, administrative justice, and the procedure for the passing of a money Bill. Mr Shuttleworth claims the return of a substantial amount of money and the Minister and the Reserve Bank want to keep the money and the outcome of the dispute is likely to have consequences for other potential claimants who may be similarly situated and, depending on the outcome of this dispute, potential claims against the State may run into billions of rands.
- (ii) That, accordingly, the outcome of the appeal is a matter of considerable public interest and, importantly, the main appeal on the merits carries reasonable prospects of success.

As to the merits of the main appeal

- (iii) That the resolution of the main appeal hinged on three questions: First, was the imposition of the exit charge a decision of the Minister or the Reserve Bank? Second, was the exit charge a national tax, levy, duty or surcharge under sections 75 and 77(1)(b) of the Constitution? And third, was the exit charge 'calculated to raise revenue' as envisaged in regulation 10(1)(c) and section 9(4) of the Act?
- (iv) That the Reserve Bank and the Minister argued that the imposition of the exit charge was a decision made by the Minister in terms of section 9(1) of the Act and regulation 10(1)(c) of the Regulations and this he did in the course of a budget speech on 26 February 2003 and that budget speech was shortly thereafter tabled in Parliament and referred to the relevant Portfolio Committee for consideration and approval and the Reserve Bank had no discretion whether to impose the exit charge or what its quantum should be.
- (v) That it was accepted by all parties that since 2003 the Reserve Bank has never exercised any discretion by deviating from the Minister's decision and

it had consistently imposed the 10% exit charge on every applicant, without variation. Therefore, the Reserve Bank and the Minister argued, it was the decision of the Minister, and not of the Reserve Bank, that had to be impugned.

- (vi) That, accordingly, the decision to impose a 10% exit charge on everyone who desired to export more than R750 000 was made by the Minister and it took the form of a narrow policy formulation directed at implementing legislation and was, unlike a broad or political policy formulation, subject to administrative review. The Minister exercised his powers in terms of regulation 10(1)(c) and imposed two conditions: a 10% exit charge on the export of all capital that exceeded R750 000; and that capital exporters be subjected to an exit schedule. He gave a general permission that was subject to fixed conditions and he then delegated the power of implementation and administration to the Reserve Bank in terms of regulation 22E.
- (vii) That, in any event, a finding favourable to the Minister and the Reserve Bank on this point is not wholly dispositive of the appeal and for present purposes it matters little who made the decision to impose the exit charge. The core issues remain and they are two and interrelated. The first is whether the charge, levy or tax was of a kind that may be imposed only after due adherence to the money Bill structures imposed by the Constitution and the second was whether the charge, levy or tax was calculated to raise revenue within the meaning of section 9(4) of the Act.
- (viii) That a Bill before the National Assembly is a money Bill if it imposes 'national taxes, levies, duties or surcharges.' However, the term 'money Bill' covers more than just the raising of taxes, levies, duties or surcharges. It includes a Bill that appropriates money, or that abolishes, reduces or grants exemptions from taxes, or that authorises direct charges against the National Revenue Fund. A money Bill must be passed by the National Assembly, and only in the manner required by section 75 of the Constitution. The National Assembly may not initiate or prepare a money Bill. Only the Minister of Finance may and a money Bill must not deal with

any other matter except the prescribed subject matters of a money Bill.

- (ix) That a blissful starting point would be to affirm that the power to tax residents is an incident of, and subservient to, representative democracy. The manner and the extent to which national taxes are raised and appropriated must yield to the democratic will as expressed in law. It is the people, through their duly elected representatives, who decide on the taxes that residents must bear. An executive government may not impose a tax burden or appropriate public money without due and express consent of elected public representatives. That authority, and indeed duty, is solely within the remit of the Legislature. It is plain that in our jurisdiction a decision or law that purports to impose a tax will be invalid to the extent of its inconsistency with the limits imposed by the Constitution or other law.
- (x) That our first chore must be to assign meaning to the undefined words in section 77 of the Constitution: 'national taxes, levies, duties [and] surcharges'. Their scope is plainly limited to charges at the national level. But the use of all four terms must betray a design to cover a wide field of charges. However a trawling of our national legislative instruments using the terms tax, levy, duty, or surcharge, suggests that the terms are of wide import and are often used synonymously and interchangeably. The only minor exception is perhaps the term 'surcharge' which seems to be, at least sometimes, reserved for a charge in excess of a base tariff. This means that a literal meaning of any of the terms is less than useful. The mere label of a charge as a tax or levy or duty or surcharge tells us little about whether it is hit by the requirements of section 77(1)(b) and we must resort to the context within which the term is used and the purpose for which the tax, levy, duty or surcharge has been imposed.
- (xi) That there is a paucity of domestic judicial guidance on how one identifies charges that must be laid down only through a money Bill and three cases refer to a money Bill but none are on point. The parties before the court were in agreement, and correctly so, that a law, other than a money Bill, may authorise the executive arm of government to impose regulatory charges in order to pursue a legitimate government purpose and there is a

raft of pre- and post-Constitution legislation that routinely authorises the Executive to impose fees, tariffs, levies, duties, charges and surcharges. Section 77(1)(a) of the Constitution, which provides that a money Bill is any Bill that ‘appropriates money’, cannot be understood to refer to any instance where revenue is incidentally raised as this would be an overbroad and unworkable meaning. ‘Appropriates money’ must be understood to refer to the allocation of revenue raised as tax and not as a regulatory charge.

- (xii) That, so the recurring question is: how does one distinguish a regulatory charge from a tax that may be procured only through a money Bill? In foreign jurisprudence courts have warned that the use of the words fees, tariffs, levies, duties, charges, or surcharges in a particular statute is not conclusive of whether the statute imposes a regulatory charge or a tax and thus, aside from mere labels, the seminal test is whether the primary or dominant purpose of a statute is to raise revenue or to regulate conduct. If regulation is the primary purpose of the revenue raised under the statute, it would be considered a fee or a charge rather than a tax. The opposite is also true. If the dominant purpose is to raise revenue then the charge would ordinarily be a tax. There are no bright lines between the two. Of course, all regulatory charges raise revenue. Similarly, ‘every tax is in some measure regulatory.’ That explains the need to consider carefully the dominant purpose of a statute imposing a fee or a charge or a tax and in support of this basic distinguishing device, judicial authorities have listed non-exhaustive factors that will tend to illustrate what the primary purpose is.
- (xiii) That since the 1950s, in a small trickle, our courts have pronounced on whether certain statutes authorised a tax or regulatory charge but none of the cases is on all fours. Most of the decisions plainly shy away from defining the word ‘tax’ because it defies precise description outside the context of a specific statute and its purpose. For example, in one case, the court declined to define the term ‘tax’ and rather listed features that would make a tax easily identifiable: (i) when the money is paid into a general revenue fund for general purposes; and (ii) when no specific service is given in return for payment.

- (xiv) That none of our cases disavow the obvious need to identify the dominant object of a statute in order to typify it as fiscal or regulatory. And earlier cases demonstrate that we must avoid attaching a fiscal meaning to words like tax or duty or levy outside of a contextual and purposive understanding. There are open-ended but helpful guidelines on how to determine the dominant purpose of legislation that tends to raise revenue for the State. In each case the factors must be weighed carefully in order to reach a correct outcome. In the end it boils down to whether the dominant object of the enactment was to raise revenue to fund the State and its public operations or to regulate public conduct by charging a fee or levy.
- (xv) That here the court was dealing with exchange control legislation and its avowed purpose was to curb or regulate the export of capital from the country. The very historic origins of the Act, in 1933, were in the midst of the 1929 Great Depression, pointing to a necessity to curb outflows of capital. The domestic economy had to be shielded from capital flight and the measures were introduced and kept to shore up the country's balance of payments position and the plain dominant purpose of the measure was to regulate and discourage the export of capital and to protect the domestic economy.
- (xvi) That the exit charge was not directed at raising revenue. The uncontested evidence of the Minister was that the exit charge was part of the regulation directed at easing in the dismantling of exchange controls. The economy was on a better footing and could afford the export of some capital provided that it was not wholesale and the charge or levy was expected to slow down the extent and the frequency of capital externalisation.
- (xvii) That there were other factors that also pointed away from revenue-raising: the charge was imposed on a discrete portion of the population. Only those who had capital to externalise in excess of R750 000 were to be affected and lesser amounts were shielded from the exit charge. And, like an ordinary tax, the payment was not voluntary. While there was no evidence of the actual or properly estimated costs of the regulatory scheme related to the revenue raised, there was a close relationship between the regulatory

charge and the persons being regulated and it may be added that the exit fee was not collected through the normal machinery of collecting taxes.

- (xviii) That it was true that during its subsistence the exit charge generated revenue of approximately R2,9 billion but in the court's view that garnering of income by the Treasury was incidental to the dominant object of regulating and discouraging capital flight. In other words, the Minister was not required to follow the procedure set out in section 9(4) of the Act before imposing an exit charge as a condition authorised by regulation 10(1)(c).
- (xix) That with the advent of the Constitution, the procedural requirements of section 9(4) have become anachronistic. They have been superseded by the Constitution. If the exit charge was directed at raising revenue, and therefore was a national tax, it would be hit by the formalities for adopting a money Bill. On the other hand, if the exit charge was not calculated to raise revenue and thus was not akin to a money Bill, it would not have to comply with section 9(4). Let it suffice to note that sections 75 and 77 of the Constitution have superseded the provisions of section 9(4) of the Act and this means that a Bill that is 'calculated to raise revenue' by imposing a national tax must comply with the constitutional requirements for a money Bill.
- (xx) That, accordingly, the Supreme Court of Appeal was in error when it concluded that the dominant purpose of the exit charge was to raise revenue and it had to be subjected to the requirements of section 75 of the Constitution.
- (xxi) That, accordingly, the main appeal against the decision of the Supreme Court of Appeal succeeded.

As to the cross-appeal

- (xxii) That Mr. Shuttleworth had sought to impugn section 9(1) of the Act and regulation 10(1)(c) while section 9(1) empowered the President to make regulations on any matter affecting or related to currency, banking or exchanges. The thrust of the attack was that the section and regulation gave the Minister broad discretionary powers of the same kind that the

Supreme Court of Appeal criticised in *Dawood and Another v Minister of Home Affairs and Others* 2000 (8) BCLR 837(CC). That decision warned against broad discretionary powers that may prejudice those who may be entitled to seek relief from an adverse decision arising from an open-ended discretion.

- (xxiii) That it had to be recognised however that this court's treatment in *Dawood* of broad discretionary powers conferred by legislation was measured and nuanced and it did not hold all wide legislative discretion to be inconsistent with the constitutional norm and invalid.
- (xxiv) That the High Court had held correctly that South Africa's 'exchange control system requires a flexible, speedy and expert approach to ensure that proper financial governance prevails'. That court stated that the exchange control system may require a specific set of rules to be in place in specific circumstances and these can change at any time, requiring an adaptation of the rules in place. It stated that it would be impossible to lay down rules or set out factors in advance, and held that regulation 10(1)(c) was valid.
- (xxv) That it would be difficult to find fault with the reasoning of the High Court and the complexity of the exchange control system should not be understated and hence the court was not persuaded that the broad discretion under section 9(1) and regulation 10(1)(c) offended *Dawood* or the Constitution and hence the cross-appeal had to fail.

As to the dissenting judgment of Froneman J

- (xxvi) That national revenue of any sort, tax or not, had to be raised by way of original legislation passed in Parliament and only the manner of its implementation, not the decision to raise it, could be regulated in delegated legislation and this was because Parliament could only delegate subordinate regulatory authority to the Executive and not assign plenary legislative power.
- (xxvii) That the regulation-making power granted to the President in the Act effectively assigned plenary legislative power to the President and this was constitutionally impermissible. Even if this power could be delegated, and

even sub-delegated, no sub-delegation to the Minister was involved in the instant matter.

(xxviii) That, however, if there was a valid sub-delegation, the Minister in any event had to impose the charge by way of legislation, and therefore the imposition of the exit charge by way of announcement was constitutionally invalid and hence the appeal should have been dismissed with costs and the cross-appeal should have been granted with costs.

### **3.3. ITC 1879**

The taxpayer, being a registered vendor in terms of the VAT Act, had been involved in the construction of low cost housing and had made certain supplies to an entity 'C' in regard to the rectification of houses, the rehabilitation of damaged houses and the building of completely new houses by the taxpayer on behalf of C in terms of the Housing Subsidy Scheme referred to in section 3(5)(a) of the Housing Act (No.107 of 1997).

The taxpayer had levied VAT at the standard rate of 14% in respect of the supplies and had received payment from C and had paid the VAT over to SARS.

The taxpayer had later realised, after C had raised the issue with it, that it had committed an error in levying and collecting VAT from C and had then submitted revised VAT returns seeking to amend the declaration from the standard rate to the zero-rate on the basis that such supplies could be zero-rated in terms of section 11(2)(s) of the VAT Act and this amendment then resulted in the taxpayer being entitled to a VAT refund in the sum of R38 162 303,07.

SARS had not accepted the revised returns and had assessed the taxpayer for the full amount at the standard rate and had refused the VAT refund.

The taxpayer then objected to the aforementioned assessments and the objection was thereafter disallowed.

The taxpayer then appealed to the Gauteng Tax Court against SARS' decision to disallow its objection to the revised assessments raised by SARS for VAT periods from 07/2008 to 09/2010 on the basis that the supplies did not fall within the scope

of section 11(2)(s) of the Act.

The taxpayer contended that the payments in question were made in terms of the Housing Subsidy Scheme referred to in section 3(5)(a) of the Housing Act and that the zero-rate applied in terms of section 11(2)(s) of the VAT Act.

SARS contended that the payments in question were not made in terms of the Housing Subsidy Scheme and that the standard rate of VAT applied.

SARS contended that the services rendered by the taxpayer were not in respect of building new houses or building houses for first time owners and therefore did not qualify as a subsidy or grant in terms of the Housing Subsidy Scheme.

The issue to be determined in the appeal was whether the rectification of houses constructed between 1994 and April 2002 and the rehabilitation of 610 damaged houses and the building of completely new houses by the taxpayer on behalf of C were made in terms of the Housing Subsidy Scheme referred to in section 3(5)(a) of the Housing Act and, therefore, the taxpayer was correct to levy VAT at a zero-rate and, as such, entitled to a refund of the amount that it had paid to SARS together with interest.

Section 11(2)(s) of the VAT Act, as read with section 8(23) and as applicable at the time, provided that taxable supplies of goods or services made by a vendor, for which payment is made in terms of the Housing Subsidy Scheme referred to in section 3(5)(a) of the Housing Act shall be deemed to be a supply of services to a public authority or municipality and shall be zero-rated.

Judge Mali held the following:

- (i) That in deciding whether the rectification or revitalisation, rehabilitation and building of completely new houses fell under the Housing Subsidy, the enquiry had, of necessity, to be directed at the meaning of the words 'housing subsidy scheme' in order to understand what a housing subsidy scheme was and what it covered.
- (ii) That in neither of the VAT Act nor the Housing Act is the term 'housing subsidy scheme' defined although both Acts refer to such a scheme. A taxpayer is then required to seek the terms of reference from further official documentation and it is not an ideal situation for a taxpayer to seek clarity

from more than one source outside the Act in order to determine the VAT rate applicable.

- (iii) That the taxpayer had, *inter alia*, relied upon the correspondence from C and the agreements that it had entered with C and from the said correspondence and agreements it had understood that the services that it rendered to C fell under the housing subsidy scheme and, in this regard, the agreement in place between C and the taxpayer specifically recorded that '[the vendor] acknowledges that the services rendered in accordance with the provisions of the Housing Subsidy Scheme are zero-rated for Value-Added Tax in accordance with section 11(2)(s) of the Value-Added Tax Act 89 of 1991.'
- (iv) That the SARS officer, who gave the reasons for her assessment in this case, conceded that the purpose of the Housing Subsidy Scheme was not limited to the building of the new houses only as she had advised in her letter of assessment and stated that her reasons for assessment were based on incomplete information at the time that she had concluded the assessment. In addition, the court examined the National Housing Code and found that there were additional housing subsidy mechanisms that were not initially taken into account by SARS.
- (v) That there was no consistency, even amongst the government departments, concerning the interpretation and application of the provisions dealing with housing subsidy schemes but it was obvious that the Provincial Department, that drafted the contract, had made it clear that the VAT treatment in respect of 'services rendered in accordance with the provisions of the Housing Subsidy Scheme were to be zero-rated for VAT purposes.'
- (vi) That, as had been demonstrated, there was no cut and dry definition of what a housing subsidy scheme entailed and it varied from one person's interpretation to the other, depending upon the circumstances. Various documents had to be cross-checked and referenced to get the answer that suited a certain individual at a particular moment. Even the witnesses for SARS stated that one had to consult various Acts and non-existent policies as well as varying opinions in order to come to a conclusion that the

rectification, revitalisation and building of new houses under the emergency programme was excluded from the housing subsidy scheme.

(vii) That, *in casu*, the unambiguous language of the agreement between the parties on the VAT treatment of the transaction appeared to be an official declaration by a government department and a policy maker to the taxpayer and, having regard to all the pieces of information and evidence led in this matter, the explicit clause in the agreement dealing with the VAT treatment was to the effect that the payments in issue were made in terms of a housing subsidy scheme.

(viii) That the court appeared to invoke the *contra fiscum* rule by referring to *Badenhorst v CIR* 20 SATC 39:

‘In the case of ambiguity arising during the interpretation of fiscal legislation, the *contra fiscum* rule will be applicable. Should a taxing statutory provision reveal an ambiguity, the ambiguous provision must be interpreted in a manner that favours a taxpayer. When a taxing provision is reasonably capable of two constructions, the court will adopt the construction that imposes a smaller burden on the taxpayer.’

(ix) That, having regard to the circumstances surrounding the interpretation of the term ‘housing subsidy scheme’ adopted by various role players in this matter, including the undertaking by C, that the VAT treatment of the taxpayer’s supply was to be zero-rated, the court accepted the taxpayer’s explanation and found that the services rendered by the taxpayer to C were in terms of the Housing Subsidy Scheme and specifically as provided for in the National Housing Scheme, and, as such, attracted VAT at the zero rate.

(x) That, however, the SARS’ grounds of assessment were not unreasonable due to the confusion regarding interpretation of the term ‘housing subsidy scheme’ and hence each party was ordered to pay its own costs.

SARS was ordered to revise the assessment for the VAT periods from 07/2008 to 09/2010 and to refund to the taxpayer the sum of R38 162 303,07 with interest at 9% from the date of the order.

### **3.4. *Anglo Platinum Management Services (Pty) Ltd v C:SARS***

Anglo Platinum Management Services (Pty) Ltd (Anglo) had offered its employees an opportunity to participate in what it believed was a legitimate salary sacrifice arrangement or scheme which involved its employees sacrificing or foregoing a portion of their cash remuneration 'packages' in return for their use of company-owned motor vehicles.

Anglo's evidence revealed that the scheme was based on certain documents, the relevant ones being:

- Policy and Procedures of the Motor Vehicle Scheme ('the policy document');
- The Motor Vehicle Use Agreement ('the MVA');
- The Notional Instalment Sale Agreement ('the NISA');
- The Annual Total Package Allocation Agreement ('the AA');
- The Notional Account.

The employees had to complete the AA indicating how they wished their 'cost to the company' remuneration packages to be structured flexibly as between cash and other benefits, which included the use of a motor vehicle and this choice was available to new and to existing employees when they were offered annual increases.

Once an employee had chosen to participate in the scheme and had selected a vehicle of his choice, Anglo purchased it, and paid the dealer in cash and it then entered the vehicle in its asset register, and claimed depreciation on it. The vehicle was registered in the employee's name, but Anglo owned the vehicle until the employee had settled the finance obligation and paid the related fringe benefit tax on it.

The cost of the purchase was recovered from the employee through a monthly deduction – predetermined at the time he elected to participate in the scheme – from the portion of his salary he had to forego in return for the use of the vehicle.

However, it was the manner in which the scheme was implemented, in particular,

the entitlement of the employees to claim an amount of credit in the notional account and their contractual obligation to pay insurance premiums on the motor vehicles that lay at the heart of this dispute.

SARS had contended that the entitlement to this credit and the obligation to pay the premiums were inconsistent with a genuine salary sacrifice scheme as, in substance, the employees retained their power over their salary packages.

The method used to recover the cost of the motor vehicle was the subject of considerable disagreement between Anglo and SARS and the evidence was that Anglo and the relevant employees had entered into a NISA, as envisaged in the policy document and this had served as a mechanism whereby 'notional interest' on the amount paid to the car-dealer would be calculated over the period of the operation of the scheme, for example 48 months.

The evidence revealed that Anglo had prepared 'notional accounts' that it sent to its employees who chose the taxable benefit of the use of their motor vehicles and these accounts, which lay at the heart of the dispute between the parties, set out the 'optimal value' of the motor vehicle, defined as the 'theoretical representation' of the capital amount outstanding at the end of each month determined according to the reducing cap method. This was part of the methodology used to determine the actual value of the motor vehicle, taking into account the finance costs from the NISA. In addition to being represented as part of the capital cost of the motor vehicle, notional interest was recorded separately in the notional accounts.

The accounts also detailed actual payments that Anglo made for maintenance and running expenses, insurance premiums and licensing fees and these payments were debited to the notional account, as was the notional interest. The predetermined monthly deduction from the employees' salary appeared from month to month as a credit in the notional account.

The issue in the appeal was whether, for the years of assessment 2004 to 2008, the use of the motor vehicles ought to be taxed at a reduced scale as a taxable benefit under par. (i) of the definition of 'gross income' in section 1 of the Income Tax Act read with the Seventh Schedule to the Act, and par. (b) of the definition of 'remuneration' in par. 1 of the Fourth Schedule to the Act, as Anglo contended it should be, or on the normal scale under par. (c) of the definition instead, which was

how SARS had assessed Anglo.

SARS had raised an assessment of R11 543 041 after determining that the amounts that Anglo had allocated to the motor vehicle scheme did not qualify to be dealt with as a valid and binding salary sacrifice agreement as envisaged in par. (i).

The Tax Court, in which Mavundla J presided, seems to have misunderstood Anglo's case to be that because it had devised a legitimate salary sacrifice scheme, which did not attract liability for income tax under par. (c) of the definition of 'gross income', no tax liability on its part arose at all. It thus proceeded to adjudicate the dispute without considering whether the relevant paragraphs of the Seventh Schedule, par. (i) of the definition of 'gross income', proviso (i) to par. (c) and par. (b) of the definition of 'remuneration' in the Fourth Schedule, applied. And, having overlooked these provisions, it seems to have approached Anglo's evidence on the inarticulated premise that the scheme was a sham, disguised to conceal its true nature and it consequently dismissed Anglo's appeal against the assessment and ordered it to pay the costs of the appeal, implicitly finding that its grounds of appeal had been unreasonable.

Judge Cachalia held the following:

- (i) That, for present purposes, the effect of the relevant provisions was that where any amount is received or accrued for services rendered by virtue of any employment, it is included in the employee's gross income under par. (c) and is thus fully taxable. However, the proviso in par. (c) precludes any benefit, in respect of which the provisions of par. (i) apply, from being dealt with as having been received or accrued for services in respect of any employment under par. (c). Par. (i) of the definition of 'gross income' includes the 'cash equivalent' as determined under the Seventh Schedule, of the value of any benefit or advantage – henceforth referred to simply as a benefit – granted to the employee as part of his employment and the benefit in issue in this case was the use of a company-owned motor vehicle.
- (ii) That, thus, if the benefit met the requirements of the definition of 'gross income' in par. (i), it, and not par. (c) applied. The employer who granted the benefit to the employee, must then determine the 'cash equivalent' of

the value of the benefit according to the Seventh Schedule, and having done so, may withhold and pay employees' tax on the cash equivalent as determined.

- (iii) That in this matter Anglo determined the cash equivalent of the motor vehicles and paid employees' tax on this amount. It was not an issue in this appeal that this determination was correctly done. What was in issue was whether the scheme constituted a valid and binding salary sacrifice arrangement that gave rise to a cash equivalent to be determined in accordance with the Seventh Schedule under par. (i).
- (iv) That in the Supreme Court of Appeal SARS eschewed reliance on the Tax Court's judgment and, instead, he approached the matter on a firmer and proper foundation that in commercial practice and in the commercial world employers and employees were entitled to structure salary packages in a tax efficient manner and that salary sacrifice arrangements, whereby employees sacrifice or forego a portion of their cash salaries in return for some *quid pro quo* or fringe benefit from the employer that reduces their tax liability, are perfectly lawful.
- (v) That, in addition, SARS did not contend that the scheme was a sham or disguised to appear to be genuine, whereas in truth it was not. In other words he did not invoke the substance over form doctrine and, instead, his case was that Anglo and its employees did not achieve what they purported to achieve, namely, a valid and binding salary sacrifice agreement and, therefore, that the use of the vehicles was, in reality, a consideration that the employees received as part of their employment and formed part of their gross remuneration.
- (vi) That it was a question of fact in each case whether a salary sacrifice agreement was achieved and in this regard a court is not concerned with the subjective belief of the parties to the agreement – no matter how genuine this belief may be – but with whether the facts, objectively viewed, establish that this result was attained. It must thus consider the oral and documentary evidence to assess the probabilities. The taxpayer bears the burden of proving that SARS' decision to disallow its objection to the

assessments was wrong and, where in this case, the taxpayer's is the only oral evidence, it must be considered carefully in the light of the available documentary evidence before a court is able to conclude whether or not the taxpayer has discharged the *onus*.

- (vii) That, therefore, to succeed in this appeal, Anglo must establish, on the available evidence, that a genuine salary sacrifice had been concluded as a matter of fact and it would thus have to show that the employees' remuneration packages were structured in a manner that they received their remuneration partly by way of cash and the balance by way of a fringe benefit; and that Anglo unconditionally assumed liability for payments and contributions for the motor vehicles that were part of the scheme, thereby releasing the employees from any such obligation. In other words, by foregoing part of their remuneration package in return for the use of a motor vehicle, the employees antecedently divested themselves of their right to this amount of money and the implication of such divestment was that the amount would not have been received or accrued for services to be rendered by the employees as contemplated in par. (c) of the definition of 'gross income'.
- (viii) That it was the manner in which the scheme was implemented: in particular the entitlement of the employees to claim an amount of credit in the notional account, and their contractual obligation to pay insurance premiums on the motor vehicles that lay at the heart of this dispute and SARS contended that the entitlement to this credit and the obligation to pay the premiums were inconsistent with a genuine salary sacrifice scheme as, in substance, the employees retained their power over their salary packages.
- (ix) That Anglo's sole witness had testified that it had prepared 'notional accounts' that were sent to its employees who chose the taxable benefit of the use of their motor vehicles. These accounts, which lay at the heart of the dispute, set out the 'optimal value' of the motor vehicle, defined as the 'theoretical representation' of the capital amount outstanding at the end of each month determined according to the reducing cap method. This was part of the methodology used to determine the actual value of the motor

vehicle, taking into account the finance costs from the notional instalment sale agreement (NISA). In addition to being represented as part of the capital cost of the motor vehicle, notional interest was recorded separately in the notional accounts.

- (x) That the aforementioned accounts also detailed actual payments that Anglo made for maintenance and running expenses, insurance premiums and licensing fees and these payments were debited to the notional account, as was the notional interest and the predetermined monthly deduction from the employees' salary appeared from month to month as a credit in the notional account.
- (xi) That the evidence, both documentary and oral, was that, from time to time, there would be a shortfall in the notional account where the actual expenditure plus notional interest exceeded the amounts credited to an employee through the monthly deduction and, where this occurred, the outstanding amounts would be recovered from the employee. Where, however, the amount credited to the employee exceeded the expenditure, the policy allowed the employee to withdraw the money from the credit available once every quarter and any amount so withdrawn was, subject to normal taxation, part of his gross income.
- (xii) That what emerged from the evidence was that the notional accounts were for Anglo's internal recordkeeping – to keep track of the cost of providing the taxable benefit to its employees – and not for any other purpose. Its aim was to correlate the amounts that became available through the salary sacrifice with Anglo's own actual expenditure plus notional interest.
- (xiii) That SARS vigorously contested the characterisation of these accounts as fictitious or notional and he submitted that the use of either of these terms was an unjustified gloss on the true role of both the NISA and the notional accounts because they were part and parcel of the exercise of calculating the actual amount that the employees – not Anglo – were required to pay each month to cover the costs of the scheme and the notional accounts, it was contended, therefore recorded real facts – not fictional amounts.
- (xiv) That two of the 'real facts' so recorded were the insurance premiums for the

vehicles debited to the notional account and the monthly amount overspent or underspent for each employee and SARS pointed particularly to these features of the scheme as being inconsistent with a genuine salary sacrifice.

- (xv) That there appeared to be no dispute between the parties that the policy entitled each employee to withdraw the credit – the amount underspent – in the notional account every quarter and if the amount was not withdrawn it would be rolled over into the following month or quarter and at the end of the financial year this amount would be paid to the employee if there was still a credit balance subject to normal tax.
- (xvi) That, accordingly, the amounts paid in or paid out quarterly were insignificant and unanticipated amounts which could become available to the employee in the future because of inevitable future adjustments to the predetermined cost of the benefit could not and did not detract from the efficacy of the scheme.
- (xvii) That one may test this by asking what SARS' response would have been if the scheme was able to achieve a perfect symmetry between the cost of the benefit and the amount that the employee gave up, which is what the scheme in substance sought to achieve? The answer is evident: he would have accepted that this was a genuine salary sacrifice and there was no reason why, on the facts of this case, the court should come to a different conclusion.
- (xviii) That, properly understood, the credit to which an employee became entitled when he elected to participate in the scheme was not unconditional. It was a contingent right, exercisable at a later date and on the occurrence of an uncertain future event: a quarterly credit balance in the notional account. If the event did not materialise there was no right to be exercised and until it was exercised there could not have been an accrual of this income as contemplated in par. (c) of the definition of 'gross income'.
- (xix) That SARS' contention that the employees retained their right to claim such moneys 'on demand' and therefore did not unconditionally divest themselves of this right rested on the incorrect premise that the right had

vested when the AA was concluded, whereas it was in truth a contingent right.

- (xx) That, in regard to the insurance premiums, it was Anglo, and not the employees, who was liable for the premiums and the employees only needed to ensure that the premiums were paid. Anglo had assumed this obligation and had paid for the premiums from the salary sacrifice and the parties had implemented their agreement intending that Anglo would be liable for this cost.
- (xxi) That the parties had sought to fund a taxable benefit from a salary sacrifice and they were entitled to do so in accordance with the relevant provisions of the Act and they achieved this through the scheme that they agreed on and implemented. The following features of the scheme indicate that it was properly designed and implemented: The taxpayer purchased the motor vehicles, owned and claimed depreciation on them. The recovery of their total cost, including their running expenses was obtained from the salary sacrifice, not from the employees and in return for the amount they had foregone, the employees received a taxable benefit, i.e. the use of the vehicles.
- (xxii) That the credit claimable arose from a small unpredicted and unanticipated future contingency, and the insurance premiums were in fact paid for by the taxpayer. Therefore, SARS' argument that the use of the vehicles was in reality a consideration received by each employee as part of their employment and thus taxable under par. (c) of the definition 'gross income', as opposed to par. (i) as a taxable benefit by virtue of a valid salary sacrifice, had to fail.

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

### **3.5. C:SARS v Stepney Investments (Pty) Ltd**

Stepney Investments (Pty) Ltd (Stepney) had owned 4.37% of the shares in Emanzini Leisure Resorts (Pty) Ltd (ELR) which it had disposed of during the 2002 and 2003 years of assessment.

At issue in this appeal was whether the Cape Town Tax Court had been correct in setting aside the additional assessments raised by SARS, against Stepney in respect of the 2002 and 2003 years of assessment for capital gains tax and this required a determination whether Stepney had proved the base cost of the asset disposed of during those years of assessment, namely 4,37% of the shares it had held in ELR.

The shares disposed of were a pre-valuation date asset as defined in par. 1 of the Eighth Schedule to the Income Tax Act i.e. an asset acquired prior to 1 October 2001 and not sold prior to that date.

Par. 25 of the Eighth Schedule provided that:

‘[t]he base cost of a pre-valuation date asset . . . is the sum of the valuation date value of that asset, as determined in terms of paragraphs 26, 27 or 28 and [certain other expenditure]’.

Stepney elected in terms of par. 26(1)(a) to utilise ‘the market value of the asset on the valuation date, as contemplated in paragraph 29, of the Schedule’ as the method of determining the value of the shares as at 1 October 2001.

Par. 29(1)(c) provided that the market value on the valuation date of the shares would be ‘the market value determined in terms of paragraph 31 on valuation date’ (the par. 29 market value). Such market value would, in terms of par. 31(1)(g), be ‘the price which could have been obtained upon a sale of the asset between a willing buyer and a willing seller dealing at arm’s length in an open market.’

Stepney’s contention was that it had sustained a loss in respect of the disposal of the shares because the aggregate base cost of the shares had exceeded the amount of the disposal proceeds. It had placed a value of R8 686 162 on the aggregate base cost, calculated as 4.37% of the par. 29 market value of the total ELR shares, namely R198 768 000. This valuation (‘the Bridge valuation’) of the total ELR shares emanated from a valuation conducted by Bridge Capital Services (Pty) Ltd in respect of all the ELR shares, undertaken for all companies in the Tusk group (which included ELR) in order to determine the base cost of the various assets of the group as at 1 October 2001 for capital gains tax purposes.

SARS purportedly acting in terms of par. 29(7)(b) of the Eighth Schedule, had

adjusted this valuation to nil, and in additional assessments raised on 10 April 2007, as a consequence of this adjustment, Stepney was assessed for a capital gain of R2 million in its 2002 year of assessment and for a capital gain of R2.2 million in its 2003 year of assessment in respect of its disposal of the shares during those years.

SARS had disallowed Stepney's objection to these additional assessments but the Tax Court had set aside this disallowance in terms of section 3(4)(h) of the Income Tax Act.

Capital gains tax had been introduced on 1 October 2001 through the insertion of section 26A and the addition of the Eighth Schedule to the Income Tax Act. Where a capital gain accrues on the disposal of assets in the seller's possession on, or acquired after, 1 October 2001, capital gains tax is payable. The tax payable is determined by a calculation of the difference between the proceeds of the sale and the base cost of the asset disposed of.

At issue before the Supreme Court of Appeal was whether the Tax Court, sitting in Cape Town, *per* Yekiso J, had been correct in setting aside the additional assessments raised by SARS against Stepney in respect of the 2002 and 2003 years of assessment for capital gains tax and this required a determination whether Stepney had proved the base cost of the asset disposed of during those years of assessment, namely 4,37% of the shares it had held in Emanzini Leisure Resorts(Pty)Ltd (ELR) and this appeal was with the leave of the Tax Court in terms of section 86A(2) of the Income Tax Act.

The facts were that Stepney had originally held 23.73% of the shares in ELR and the latter was mainly engaged in developing, owning and operating casinos, hotels and related leisure activities. The Kwazulu Natal Gambling Board (the Gambling Board) awarded a casino licence to ELR on 21 August 2000 for a period of 15 years in respect of a defined area, namely Richards Bay. Complications arose subsequently when members of a religious grouping, known as the Richards Bay Ministers' Fraternal, litigated against ELR in respect of the site where the casino was to be erected. The awarding of the casino licence itself was, however, not in issue. The litigation, which ultimately reached the Supreme Court of Appeal and in which the Richards Bay Ministers' Fraternal was unsuccessful, caused

considerable delays in the establishment of the casino at Richards Bay. Consequently ELR acquired an alternative site at Empangeni under a temporary licence issued by the Gambling Board on 4 October 2001. At the time of the valuation for capital gains tax purposes, ELR was in possession of a permanent casino licence which it was unable to utilise and was in the process of acquiring a temporary licence.

The Bridge valuation lay at the heart of the dispute as to whether the value placed on ELR (and *a fortiori* the determination of the aggregate base cost of the shares disposed of) had been reasonable and in this regard Stepney bore the *onus* of proving that its valuation of the shares disposed of was correct and in the Tax Court it had called a number of witnesses to discharge this *onus* and SARS, in turn, adduced the evidence of several witnesses to meet this case.

The Bridge valuation had been done by utilising the discount cash flow (DCF) valuation method which was contended to be the most appropriate method in respect of the valuation of an asset such as shares and it entailed valuing the business of an entity on its future forecast free cash flows, discounted back to present value through the application of a discount factor.

SARS, on the other hand, in adjusting the base cost valuation to nil, had utilised the net asset value (NAV) valuation method. It was implicitly conceded in the court below that this valuation method was inappropriate and that the DCF method should have been used and this concession had been properly made.

Not only did SARS concede that the wrong methodology had been utilised by his official, Mr Costa, but Prof Wainer's mandate was also narrowly circumscribed, namely to analyse the Bridge valuation and to subject it to criticism but no separate independent valuation had been done by Prof Wainer or anyone else on behalf of SARS and, ultimately, the Tax Court had before it only the Bridge valuation, which was subjected to extensive criticism by Prof Wainer.

Mr Veldtman, who was responsible for the Bridge valuation, confirmed having used the DCF methodology and that he had relied on information from Tusk management, including the financial projections prepared by Deloitte. The market value of the assets of all the entities in the Tusk group, including ELR, was determined in accordance with the relevant provisions of the Eighth Schedule for

capital gains tax purposes and these assets were unlisted shares and he explained and motivated his determination of the future forecast cash flows and the discount factor that he had applied.

On behalf of SARS, Mr Costa had issued a letter of audit findings to explain why the Bridge valuation was not accepted and in which he had advanced two main reasons for the rejection of the Bridge valuation and for the raising of additional assessments. The first was that the DCF valuation method was wrongly utilised for the determination of the market value of the shares and, second, that the forecasts used by Mr Veldtman for purposes of the valuation were not reliable.

The Tax Court, having found in favour of Stepney, found that SARS did not advance the unreliability of the financial projections and assumptions made in the Bridge valuation as one of the factors that had been taken into account in raising the additional assessments.

In the Supreme Court of Appeal SARS' primary contention was that Stepney had failed to discharge its *onus* to establish the validity or reliability of the projected revenue utilised by Mr Veldtman in compiling his valuation, whereas Stepney also contended that SARS had impermissibly sought to change the grounds of assessment which he sought to have upheld in this court.

Judge Majiedt held the following:

- (i) That Stepney had submitted that on appeal against a decision of the Tax Court the Supreme Court of Appeal had limited, narrowly circumscribed powers and it placed reliance on a *dictum* in *CIR v Da Costa* but the submission was misconceived and the passage from *Da Costa* had been quoted out of context. In *Da Costa* Van Heerden JA in fact held that there is 'a full right of appeal against any decision of a Special Court on issues of fact or law' and in this regard the learned Judge referred to section 86A of the Income Tax Act and hence Stepney had incorrectly categorized the matter before the court as a 'review' as it was not a review but rather was a full appeal.
- (ii) That in regard to Stepney's contention that SARS had impermissibly sought to change the grounds of assessment, that contention could not be upheld.

Rule 12 of the Tax Court Rules provided that the issues before the Tax Court were those adumbrated in SARS' statement of grounds of assessment under Rule 10, together with those outlined in the taxpayer's statement of grounds of appeal in terms of Rule 11. In its statement of grounds of assessment SARS pertinently raised the issue that Stepney's market value of the relevant ELR shares had been 'overstated/inflated' for purposes of determining the base cost of the shares. SARS had set out a summary of the reasons why it took this view and it had therefore not merely confined itself to the methodology utilised, *i.e.* DCF versus NAV, but it had pertinently challenged the premise underlying the Stepney's valuation in several respects.

- (iii) That the nature of expert evidence and a court's approach to it was well established in that an expert's opinion represented his reasoned conclusion based on certain facts or on data which were either common cause, or established by his own evidence or that of some other competent witness. An expert's bald statement of his opinion was not of any real assistance; a proper evaluation of the opinion could only be undertaken if the process of reasoning which led to the conclusion, including the premises from which the reasoning proceeded, were disclosed by the expert. It was not the mere opinion of the witness which was decisive but his ability to satisfy the court that, because of his special skill, training or experience, the reasons for the opinion which he expresses were acceptable.
- (iv) That SARS contended that Stepney's witness, Mr Veldtman's evidence did not meet the criteria laid down in the cases cited and it was submitted that he had failed to give reasons for some of his conclusions and that much of the data upon which he had based his conclusions was shown to be fatally flawed and that, further, he had given a bald statement of his opinions without providing the underlying reasoning and the information on which Mr Veldtman had based the valuation was not sound.
- (v) That Mr Veldtman had testified that he received information from Tusk management, upon which he had relied to compile his valuation report but at the time of the valuation there was other information available which

would have had a material effect on the figures. The DCF calculation in the Bridge valuation was not based on the management accounts of 2004, but on the forecast amounts calculated by Deloitte in 2001 as part of the figures submitted to the Gambling Board in respect of the application for a temporary licence. Stepney had sought to justify the use of the 2001 Deloitte figures on the basis of them being closer to the time of the valuation date, 1 October 2001, but this approach was fatally flawed inasmuch as the actual figures which were available in 2004 (when the Bridge valuation was done) showed that the figures forecasted by Deloitte in 2001 were unreasonable. As SARS' witness, Prof Wainer, had illustrated in his expert report and in oral evidence, the forecast for 2003 was R49 million, whereas the actual figure was a R61 million negative, i.e. a variance of R110 million. The actual figures for 2004 constituted only 10% of the 2005 projected figures and only 20% of the projections for 2006 and 2007.

- (vi) That Mr Veldtman had also consciously disregarded ELR's letter to the Gambling Board dated 20 March 2003 and in this letter the challenges and travails facing the temporary casino at Empangeni had been tabulated. Revenue during the nine months of trade was a mere 43% to 46% of budget and this, together with the ongoing litigation by the Ministers' Fraternal, was said to have 'precipitated a major crisis for ELR'. As a result ELR submitted a revised project proposal to the Gambling Board in respect of the permanent casino at Richards Bay in order to 'obviate disastrous consequences' and this letter undoubtedly cast a long shadow over ELR's optimistic forecasts of 2001, and yet no regard was given to it.
- (vii) That Stepney had argued strenuously that the factors outlined above could not have been taken into account, since to do so would amount to applying hindsight. However, taking into account the actual figures which were available in 2004 and having regard to the letter above, would have been eminently reasonable in the circumstances and in doing so Mr Veldtman would have tested the reasonableness and correctness of the projections provided by management.
- (viii) That a valuer cannot just blindly accept at face value figures presented to

him or her – there is a duty to assess their reasonableness and correctness. The necessity of assessing the reasonableness of the forecasts was acknowledged in the Bridge valuation and the information available at the time of the Bridge valuation pointed clearly to a significant overstatement of revenue projected in 2001 but, as stated no regard was given to it. The information was available at the time that the valuation was conducted and the proper perspective was that the valuer was duty bound to have regard to it in order to interrogate the soundness of management's projections. It had been wrong not to take the later information into account and this resulted in a gross overstatement of the projected revenue forecast which in turn led to a material inflation of value in the Bridge valuation.

- (ix) That the next aspect to be considered was the fact that the wrong date had been utilised in the valuation and as this had become common cause in the Tax Court, it could be disposed of briefly. Instead of utilising the valuation date set out in the Schedule (1 October 2001) the relevant figures were calculated in the Bridge valuation with reference to 31 March 2002. The experts, Mr Veldtman and Prof Wainer, had agreed in their joint minute that this mistake had a 10% adverse impact on the valuation, i.e. approximately R19.8 million on ELR's total valuation and about R860 000 on the valuation of the relevant ELR shares. Whilst relatively small, the adverse impact on the aggregate base cost is self-evident.
- (x) That in respect of the tax calculations, it was uncontroverted that an understatement of the tax amount would have led to an overstatement of value in the Bridge valuation. The tax calculations had emanated from ELR management and were, on its own version, not verified for reasonableness by Mr Veldtman. The problem is that the tax calculation does not accord with an application of the relevant statutory rates and the Bridge valuation thus falls short in respect of the tax calculations as well insofar as there had been an understatement of the tax.
- (xi) That there were material shortcomings in the reliability of the projected capital expenditure as well and no additional capital expenditure for the construction of the temporary casino had been taken into account in the

Bridge valuation. It was self-evident that substantial construction had to be undertaken to convert this site into a temporary casino which was planned to operate for a period of three years and the Bridge valuation also did not include any substantial amounts for ongoing capital expenditure for the maintenance of buildings, furniture and fittings and hence the understatement of the amounts for capital expenditure had impacted materially on the Bridge valuation.

- (xii) That a further aspect for consideration in respect of the future forecast free cash flows was the reliability of the terminal value of R527 218 000 which was used in the Bridge valuation and that figure was based on revenue flows into perpetuity. It failed to take cognisance of the term of the casino licence, being 15 years and the terminal value was in effect calculated on the basis that there was no risk of the licence not being renewed upon expiry of the 15 year period and this approach was far-fetched and out of touch with reality. Prof Wainer was correct that allowance should have been made for the risk of non-renewal, or, at the very least, the costs associated with a renewal application.
- (xiii) That in regard to the discount rate that had been applied, an appropriate discount rate had to be applied to the projected cash flows for a proper application of the DCF method and Mr Veldtman had failed to furnish adequate reasons for applying a risk premium of 15% and he merely gave vague assertions in this regard. Moreover, a serious shortcoming was the fact that the same discount rate was applied to all the entities in the Tusk group and the 'one size fits all' approach of Mr Veldtman was clearly inappropriate. The failure to assess the ELR casino separately and with due regard to its own particular risk factors had an adverse impact on the discount factor that had been applied.
- (xiv) That a further problem was that certain obvious risk factors had been disregarded and these were the unresolved litigation (which by its very nature is steeped in uncertainty) and the risk of increased construction costs to erect a temporary casino. Whatever legal advice might have been received concerning the strength of Stepney's case in respect of the

litigation, a purchaser of the shares would have considered it as an additional risk factor and a valuer would be required to take that into account in applying a discount factor.

- (xv) That it was clear that the Bridge valuation was fatally flawed in the various respects already outlined and a court was entitled to reject a valuation if it was not satisfied with the investigations underpinning it.
- (xvi) That the Tax Court had been wrong in upholding the Bridge valuation and, as a consequence, Stepney had failed to discharge its *onus* of proving the par. 29 market value and thus also the aggregate base costs of the relevant shares.
- (xvii) That, however, SARS had very properly conceded that the value of the shares could not be nil as there was clearly considerable value attached to ELR's sole asset, the casino licence, and it was not seriously disputed that a casino licence which grants the holder exclusive rights in respect of the specified area for a period of fifteen years has considerable value and it was in the interests of justice that a proper valuation be calculated.
- (xviii) That the Tax Court should have remitted the matter to SARS for further investigation and assessment in terms of section 83(13)(a)(iii) of the Income Tax Act.
- (xix) That, however, the grounds of assessment were unreasonable in two respects, namely the incorrect utilisation of the Net Asset Value (NAV) methodology and SARS' valuation of the shares as nil. The former was implicitly conceded in the Tax Court and the latter was conceded at the outset before the court.
- (xx) That Stepney was therefore entitled to its costs in the Tax Court in terms of section 130(1)(a) of the Tax Administration Act 28 of 2011.

The appeal was upheld with costs, including those of two counsel.

The additional assessments in respect of the 2002 and 2003 years of assessment were set aside and the matter was remitted to SARS for further investigation and assessment.

### **3.6. ITC 1880**

The taxpayer, being a businessman, had appealed to the Gauteng Tax Court against his assessment for the 2008 year in which SARS had disallowed the taxpayer's reduction of the proceeds that he had received from a sale of shares in the calculation of his capital gains tax liability arising from the disposal of the aforementioned shares.

The taxpayer had acted as agent for A Investments Limited ('A') in November 2003 in respect of an offer to purchase received from F, in respect of shares it held in B (Pty) Ltd trading as BCD and this constituted A's entire shareholding in BCD. A sale agreement was concluded and in November 2003 A sold its 47.3% shareholding in BCD to F on the understanding that A would have no minority shareholder protection.

The taxpayer was also a shareholder in BCD and in August 2007 he also sold his 27.005% holding of 540 100 shares in BCD to F for R841 655 833 and on 3 September 2007 F paid the said purchase price into the taxpayer's bank account.

In June 2006 A had advised the taxpayer that it had discovered that the taxpayer had withheld material information from it when he had represented it during its sale of shares transaction with F in that he had failed to disclose material information to A that F would have extended minority protection rights to it and that it was therefore not compelled to sell its minority shares in BCD to F and thus the withheld information had a direct bearing on whether or not A should dispose of its entire shareholding in BCD.

As a result thereof, A instituted a damages action against the taxpayer in October 2007 and the parties finally settled the dispute and obligation by 31 October 2007 in which the taxpayer agreed to pay an amount of damages of R694 888 271 in full and final settlement of A's claim which was also made an order of court.

A had initially claimed an amount of R925 000 000 as damages on the basis that

that was the value of the shares and claims which it would have held and which it had lost by virtue of it having disposed of its shares and claims in and against BCD.

The taxpayer, in his 2008 tax return, when calculating the capital gain on the shares that he had sold in BCD, had deducted the settlement payment made to A as described above from the proceeds received from F and had only indicated the net amount of R216 218 233 as his proceeds for purposes of par. 35 of the Eighth Schedule to the Income Tax Act.

The taxpayer had acted accordingly following accounting and tax advice given to him to the effect that par. 35(3)(c) allowed for the proceeds to be reduced by any amount that was reduced from such proceeds as a result of 'any other event'.

SARS, during December 2012, had conducted an income audit on the taxpayer in respect of the 2007 and 2008 years of assessment and, as a result of the audit, had increased the proceeds from the sale of the shares of R216 218 233 by the amount of R625 437 601 and had arrived at proceeds of R841 655 833.

SARS, in addition, had raised an understatement penalty in terms of section 223 of the Tax Administration Act of 75% which had equated to R46 907 820, on the basis that the taxpayer had no reasonable grounds for the tax position that he had taken.

SARS had also raised interest on both amounts payable to it.

The taxpayer contended that the first issue in dispute was whether SARS had correctly adjusted the proceeds received by him in terms of the sale of his BCD shares to F in the 2008 year of assessment, i.e. from R216 218 233 to R841 655 833 and this encompassed two alternative sub-issues, namely:

- whether the amount of R841 655 833 was 'received by' or 'accrued to' the taxpayer as contemplated in par. 35(1) of the Eighth Schedule to the Act or whether only the amount of R216 218 233 had been received by or had accrued to the appellant; and
- if it was found that the amount of R841 655 833 was received by or had accrued to the appellant, whether that amount should be reduced by an amount of R625 437 601 in terms of par. 35(3)(c) of the Eighth Schedule.

SARS contended that the first issue in dispute was whether the taxpayer had proven that the proceeds received from the disposal of his shares to F in September 2007 should, in accordance with par. 35 of the Eighth Schedule to the Act, be reduced by the settlement amount paid to A.

SARS further contended that the words 'any other event' in par. 35(3)(c) must be interpreted in the context of the more specific stated matters in that paragraph and had to be restricted to any other events that were similar to the specifically stated events.

The parties agreed that the second issue in dispute was whether SARS had correctly imposed an understatement penalty of R46 907 820 in respect of the BCD transaction.

SARS had imposed the aforementioned penalty on the basis of 'reasonable care not taken' by the taxpayer or 'no reasonable grounds existing for the tax position taken' and the reasons cited by SARS for reaching this decision was that 'the legislation and the facts are clear.'

The parties agreed that the third issue in dispute was whether interest as contemplated in section 89*quat* of the Income Tax Act had been correctly levied.

Judge Wepener held the following:

As to the reduction of proceeds

- (i) That the issue to be determined evolved around the possible link of a sale of shares during 2003 and the sale of shares by the appellant during 2007 and during both his evidence in chief and in re-examination leading questions were put to the taxpayer regarding this particular link.
- (ii) That the fact whether there was a link between the sale of shares in 2003 and that of 2007 was, of course, not proved by the taxpayer stating that there was such a link as such are not statements of fact but conclusions by the witness. The question to be decided was whether the 2003 and the 2007 transactions were so linked as to satisfy the provisions of s 35(1) and 35(3)(c) of the Eighth Schedule to the Income Tax Act and that is the very issue which the court is called upon to determine.

- (iii) That although the taxpayer sought relief based on the fact that SARS had disallowed the deduction of an amount of R625 437 601 which amount the taxpayer had paid to A from the proceeds of his sale of shares in 2007, there was, however, no link between the two incidences of sale.
- (iv) That the provisions of par. 35 of the Eighth Schedule were clear and unambiguous in that when a taxpayer disposes of an asset, the amount received therefor is the proceeds from the disposal and in accordance therewith the amount received by the taxpayer was the sum of R841 655 833 for his 540 100 shares which he had sold to F. The taxpayer was not able to succeed in the case against him brought by A for his breach of duty as agent to it and in order to pay his debt to A the taxpayer then sold his shares in F and had received the full price of the sale from F into his bank account but the settlement or payment of A's claim was a payment made by the taxpayer that had no bearing on the sale of his shares to F, nor had it any bearing on the sale by A or the taxpayer of shares to F in 2003.
- (v) That, accordingly, the taxpayer had consequently received the amount of R841 655 833 as a result of the disposal of his shares to F in 2007 and the argument that because the taxpayer had decided to pay a portion of the proceeds of the 2007 sale to A meant that he did not receive the whole amount unconditionally, was also misplaced. There was no evidence of conditions attached to the payment by F and the taxpayer was indeed legally entitled to the proceeds of the 2007 sale to F and to dispose thereof as he deemed fit and he received the proceeds of the sale.
- (vi) That the mere fact that the taxpayer had decided to pay A's damages claim against him as a result of his breaches against A did not affect the fact that he had disposed of his shares in 2007 and had received an amount of R841 655 833 for that disposal.
- (vii) That taxpayer's second submission was that the full amount received by or accrued to him from the 2007 sale of shares could be reduced in terms of par. 35(3)(c) of the Eighth Schedule as the 2003 sale of shares was 'any other event' which could reduce the amount of the taxpayer's proceeds of

the 2007 sale. However, the words 'any other event' were not used in isolation but appeared in conjunction with a list of events which could be relied upon so as to include any other event which is related to the disposal but not mentioned in the section.

- (viii) That SARS had relied on the application of the ejusdem generis rule and this rule of construction is sometimes expressed by the maxim *noscitur a sociis*, i.e. that the meaning of a word may be ascertained by reference to those associated with it and, in other words, where two or more words which are susceptible of analogous meaning are coupled *noscitur a sociis*, they are understood to be used in their cognate sense and they take, as it were, their colour from each other, i.e. the more general is restricted to a sense analogous to the less general.
- (ix) That, on the basis of the authorities cited, SARS had submitted that the words which appear in par. 35(3)(c) refer to words of the same nature and that the group in question was divided into two. Firstly, changes to the disposing agreement, i.e. the cancellation, termination or variation of an agreement and, secondly, the group which fell under the release from an obligation, i.e. waiver of a claim or release from an obligation.
- (x) That it was in the aforementioned context that 'any other event' had to be understood and whilst 'any' may ordinarily be a broad, unlimited term, it was in this instance limited by the two categories referred to above and the taxpayer could accordingly only rely on par. 35(3)(c) if the 'event' fell under one of the aforementioned two categories and in the court's view the taxpayer's obligation to pay for his breach did not fall within the parameters of 'any other event' provided for in par. 35(3)(c) of the Eighth Schedule.
- (xi) That, accordingly, having regard to the foregoing, SARS' inclusion of the amount received by the appellant for the sale of the shares in 2007 for the 2008 year of assessment was unassailable and the appeal against the assessment fell to be dismissed.

As to penalties and interest

- (xii) That there were two further issues to be considered – they related to the

understatement penalty in terms of section 221 of the Tax Administration Act raised by SARS due to the deduction of the amount paid to A from the taxpayer's income and the imposition of interest in terms of the provisions of section 89quat of the Income Tax Act.

- (xiii) That it was common cause between the parties that the provisions of section 221 of the Tax Administration Act had been made retrospectively applicable to the taxpayer's assessment now under consideration.
- (xiv) That the 75% penalty had been arrived at by having regard to the fact that there were no reasonable grounds for the tax position taken by the taxpayer, but the decision was reached without a consideration of the full facts referred to in the Tax Administration Act which came into operation after the decision was taken and which was based on a table that had been replaced. Should the court find that the taxpayer indeed had no reasonable grounds for the tax position taken, the penalty provided for is 50%, but there was no reasonable basis for SARS to conclude that the appellant had no reasonable grounds for his deduction.
- (xv) That the unchallenged evidence of the taxpayer was that the tax position was taken as he believed that his calculation was correct and in terms of the provisions of the Eighth Schedule to the Income Tax Act. Moreover, there was no intention to evade or delay payment of tax and he sought professional advice regarding the completion of his tax returns and denied being negligent during the submissions of his returns and it was accepted that the taxpayer had obtained professional advice regarding the submission of his returns and the deduction which was the subject of the dispute in this matter.
- (xvi) That being so, the provisions of s 270(6D) of the Tax Administration Act, which it was common cause had been enacted retrospectively, were applicable.
- (xvii) That the taxpayer, having received advice, had reasonable grounds to take the tax position that he did and nor could it be said that he did not take reasonable care – he did so by consulting the experts. The table contained in section 223 of the Tax Administration Act, which requires a penalty to be

imposed based on the grounds set out therein, required that a taxpayer pays a 10% penalty if a substantial understatement is made in a tax return.

- (xviii) That it was common cause that the taxpayer's tax return did so contain a substantial understatement and it was not in dispute that the taxpayer's matter before SARS was a standard case with the result that the penalty of 10% would be applicable unless there were reasons for a different outcome.
- (xix) That there was no evidence that there were extenuating circumstances which would warrant the reduction below the provisions of section 233, i.e. a 10% penalty for a substantial understatement. It was common cause between the parties that the onus to prove that such extenuating circumstances existed was on the taxpayer but no such circumstances were shown to be present.
- (xx) That, accordingly, the taxpayer's conduct constituted a substantial understatement regarding the income from his sale of shares and the penalty fell to be reduced to 10%.
- (xxi) That in regard to the imposition of penalty interest, the parties were ad idem that the provisions of section 89quat(3) of the Income Tax Act were applicable and the section allows for SARS to exercise a discretion in certain circumstances.
- (xxii) That there was no reason not to find that the taxpayer's reliance on advice was reasonable and no facts were proved to show that the taxpayer was nevertheless unreasonable and hence, in the circumstances, SARS' decision should be substituted with an order that the interest be waived in toto.

Appeal against the assessment for the 2008 tax year by the inclusion of the amount received by the appellant for the sale of shares was dismissed.

The understatement penalty was to be levied at 10%.

The interest levied on the underpayment of provisional tax was to be remitted in whole.

### **3.7. ITC 1881**

The taxpayer had traded as importers and manufacturers of household linen products which it sold to the retail industry.

The taxpayer, on 1 March 2006, had disposed of its business operations and inventory to D Entity CC (D Entity).

The taxpayer was placed under liquidation by special resolution registered on 30 April 2010.

SARS was, upon liquidation, the only creditor who had any interest in the taxpayer's affairs and the current dispute between the parties arose from the Additional Income and Value-Added Tax Assessments issued by SARS in respect of the taxpayer's 2004, 2005 and 2006 years and periods of assessment.

The dispute between the parties ranged over many aspects of the taxpayer's business, accounting and tax affairs for the relevant periods and included challenges relating to SARS' views as to how the taxpayer had treated claims and/or deductions relating to casual wages, wear and tear on vehicles, settlement discounts, rebates, bad debts, claims for repairs, overseas travel and corrections (journal entries) to stock records during the relevant years of assessment.

The aforementioned issues resulted in affecting, in addition to income tax, the taxpayer's PAYE, Skills Development Levies (SDL), Unemployment Insurance Contributions (UIC) and Value-Added Tax (VAT) returns for the relevant periods of assessment.

At a pre-trial conference the parties agreed that, should the court permit it, the issue of prescription and the application of section 79 of the Income Tax Act to the Additional Assessments, would be dealt with as a preliminary point *in limine*.

The court agreed to hear the point *in limine* and, as the issues related to a legal point, the judge decided the point alone, without input from the additional members of the court.

The court ruled, at the conclusion of argument on the preliminary issue of prescription, that the matters relating to Income Tax for the 2004 and 2005 years of

assessment had become prescribed in terms of section 79 of the Income Tax Act and the judge indicated that the reasons for that ruling would be included in this judgment.

The dates of the original assessments for 2004 and 2005 were 1 March 2006 and 1 May 2006, respectively and the additional assessments were dated 1 November 2009 for both years of assessment.

Accordingly, more than three years had elapsed between the dates of the original assessments and the date of the additional assessments.

SARS, as a result of his investigation into the taxpayer's affairs, had determined that the amounts in dispute related to alleged unsubstantiated wear and tear on vehicles in the 2004 and 2005 years of assessment and alleged unsubstantiated expenditure on casual wages and salaries for the 2005 year.

SARS, in a letter of audit findings dated 12 August 2009, did not give any consideration to the issue of prescription and had concluded that '... it is my intention to adjust for wear and tear on assets not owned by the taxpayer' and then simply referred to the two amounts of claims and stated that '... It is my intention to adjust for 2005 income by R345 852 ... as the *onus* of proof of deductibility of the expenditure has not been discharged.'

SARS had made no reference to the lapse of time of more than three years and had merely given the explanation as quoted above.

Again, in the assessment letter that followed those audit findings, dated 30 September 2009, SARS made no reference to prescription and the lapse of time in finalising the adjustments for the wear and tear and salary expenditure.

The taxpayer had requested reasons for the assessment dated 7 October 2009 and had specifically requested whether there were '... any other reasons other than the issue of *onus* for the adjustment of the 2005 wages'.

SARS response concluded with the following:

'We are unable to provide any reason other than *onus* and we believe that the *onus* provision suffices as a basis for the assessment.'

The taxpayer contended that it was therefore clear that SARS did not give

consideration at all to the issue of prescription and had relied solely on the issue of *onus* and that it was also clear that SARS could not have been satisfied as to the fact that the necessary factors had occurred to lift the veil of prescription.

The taxpayer lodged an objection and specifically lodged objection in respect of the 2004 and 2005 years of assessment on the basis of prescription, *i.e.* as a period of more than three years had elapsed since the issue of the original assessments and noted that 'The Commissioner has placed on record that the only reason for the adjustment is one of *onus* and, accordingly, is now precluded from relying on the *proviso* to section 79 to open this assessment.'

The first occasion that SARS attempted to rely on section 79 of the Act was in the notice of disallowance of the objection where SARS noted that wear and tear claimed on assets purchased on behalf of the taxpayer's consultants and employees had amounted to misrepresentation and in terms of section 79 the veil of prescription was lifted and the assessments were correctly raised.

With regard to the issue of salary and wages, the notice of disallowance did not, however, rely on the issue of prescription being lifted but continued to assert the issue of *onus* and noted, in regard to the 'basis of disallowance of objection' that 'the taxpayer did not provide any supporting records to discharge the *onus* of proof and the objection is, therefore, disallowed.'

The taxpayer accordingly submitted that SARS had failed to assert, even at this stage, that there was a basis for lifting the veil of prescription and was relying solely on the issue of *onus* in respect of salaries and wages.

The taxpayer then noted an appeal in respect of these matters and re-emphasised the issue of prescription but SARS did not, in its notice of grounds of assessment, raise the issue of prescription in respect of the casual wages and salaries, but persisted with the issue of burden of proof.

The taxpayer contended that SARS failed to provide evidence that he was satisfied that the circumstances for displacing the immunity existed and hence he had failed to meet the requirement of satisfaction.

The taxpayer contended further that SARS had failed to address the issue of prescription at all in the letter of findings or in the letter of assessment and, in

addition, SARS confirmed in the response to the request for reasons that the only reason was that of *onus*. In fact, on the aspect of the salaries and wages, the notice of disallowance again fails to address the issue of prescription at all.

Judge Vahed held the following:

*As to the issue of prescription*

- (i) That it was plainly apparent that SARS had acted only on the basis of *onus* and had not considered any other or further factor prior to the raising of the additional assessments in issue.
- (ii) That SARS had failed to assert, even at the stage of disallowance of the objection, that there had been a basis for lifting the veil of prescription and had been relying solely on the issue of *onus* in respect of salaries and wages and hence the necessary tests to lift the veil of prescription had not been met in respect of the 2005 salaries and wages adjustment.
- (iii) That in *Natal Estates Ltd v SIR* it was held that there must be some evidence before the court that SARS was satisfied that an amount was not previously assessed because of fraud or misrepresentation or non-disclosure of material facts otherwise there is no displacement of the immunity conferred on the taxpayer by the *proviso* to section 79(1) of the Act.
- (iv) That a convenient time and place for indicating SARS' satisfaction would be in the additional assessment itself or in a covering letter or in the notice which SARS is required by section 81(4) to send to the taxpayer, if the latter's objection to the assessment is disallowed and it should state the particular conduct of the taxpayer to which it relates, *i.e.* whether fraud or misrepresentation or non-disclosure of material facts. (See the *Natal Estates* case, *supra*.)
- (iv) That, further, the taxpayer should not have to grope inferentially SARS' satisfaction, or the particular form of dereliction of duty to which it relates, and, in particular, he should not be left to infer from the mere receipt of an additional assessment that SARS was satisfied that the taxpayer's fraud or

misrepresentation or material non-disclosure had caused a non-assessment. (See the *Natal Estates* case, *supra*.)

- (v) That in the present matter, SARS did not contend anything with regard to the issue of prescription prior to the additional assessments being issued and, in fact, when asked whether there were any reasons other than that of *onus*, confirmed categorically that there was no other reason beyond *onus* and, as such, could not be said to have applied his mind to the issue of prescription prior to the raising of the additional assessment.
- (vi) That the court could find nothing to infer that SARS had been satisfied at the time of the assessment or during the process because it was fair to say that the question of prescription was not part of SARS' focus. Furthermore, SARS had not shown any evidence of this satisfaction and, as such, the statutory immunity ought to prevent the raising of the additional assessment.
- (vii) That the belated reference in the correspondence to a material non-disclosure was clearly an afterthought, made only after the taxpayer had raised the issue and a belated reference in the correspondence to material non-disclosure could not satisfy the requirements of section 79 as explained in the *Natal Estates* case, *supra*; moreover, that assertion in and of itself did not provide sufficient and adequate evidence that the 'satisfaction' was established at the relevant time.
- (viii) That, accordingly, SARS had failed to meet all the requirements of the 'satisfaction' as provided for in section 79 of the Act and hence the statutory immunity provided for in section 79 ought not to be displaced.

### **3.8. ITC 1882**

The taxpayer was a lady aged 73 years, who was a retired housewife and mother.

The taxpayer had derived income as beneficiary of four *inter vivos* trusts, namely the A Trust, the B Trust, the C Trust and the D Trust and she was not only the beneficiary of the trusts, but also a trustee of all four trusts.

The taxpayer's tax affairs for the 2009 tax year were subjected to an audit by SARS and it was found that the taxpayer had under-declared her income for the 2009 year of assessment.

The taxpayer had admitted through her tax representative to having omitted approximately R27 million of income in the 2009 tax year and this amount was not in dispute.

The only issue in dispute before the court was the *quantum* of the additional taxes levied by SARS as a result of the under-declaration.

It was common cause that a penalty of R5 456 484,60 had been imposed on the taxpayer on 15 September 2011 by SARS' Objection Committee in terms of section 76(1)(c) of the Income Tax Act when the Committee had decided to reduce the penalty by 50% and had levied a 50% penalty, after SARS had imposed a 100% penalty and after having considered the aggravating and mitigating factors.

The evidence revealed that the taxpayer's accountant had engaged with SARS, as the representative of the taxpayer and he had indicated at various stages during the audit that when the first return had been submitted the financial statements for the respective trusts had not been available yet and the correct return had only been submitted two years late during May 2011.

The taxpayer had stated that her accountant, Mr Z, filed her tax returns and he was solely responsible for doing so. She admitted to having signed the financial statements of the trusts and to having received the money from the trusts, although she had left the payment of taxes to her accountant. She conceded that as a taxpayer she had to declare all her taxes but was of the opinion that the penalty amount of R5,4 million was too much and 'unfair' and she placed the blame squarely on her accountant's shoulders and her evidence was to the effect that although she was a trustee of the trusts, she had no knowledge of the responsibilities of a trustee.

The taxpayer's accountant, Mr Z, a chartered accountant, had been involved in her

financial affairs for ten years and his evidence was that when he sent the return in error he had known that there was still some information lacking but had failed to inform SARS immediately and thereby gave the impression that nothing was owed.

He testified further that the under-declaration consisted of the fact that all the documents from the various trusts had not yet become available and that he was to blame for the under-declaration and he conceded that he had not requested an amendment of the return after he had filed it erroneously.

Prior to the hearing of this matter, two points *in limine* were argued on 19 November 2015, a week before the hearing commenced, and a ruling was made on 23 November 2015.

The two points *in limine* that were argued were:

- The incidence of the burden of proof pertaining to the imposition of the additional tax;
- Whether the duty to commence the proceedings was on the taxpayer or on the Respondent.

Section 76 of the Income Tax Act, dealing with penalties, was repealed by section 271 of the Tax Administration Act on 1 October 2012.

Section 82 of the Income Tax Act, dealing with the incidence of the *onus* in tax matters, was repealed by section 271 of the Tax Administration Act on 1 October 2012.

It was common cause that in this matter the objection, disallowance of the objection and the appeal were all lodged prior to 1 October 2012 when the Tax Administration Act came into operation.

Section 270 of the Tax Administration Act is a provision regulating transitional matters, such as the present matter, and deals with procedural matters as well.

Section 270(2)(d) provided at the relevant time:

*'270. Application of Act to prior or continuing action.*

- (2) The following actions or proceedings taken or instituted under the provisions of a tax Act repealed by this Act but not completed by the

commencement date of the comparable provisions of this Act, must be continued and concluded under the provisions of this Act as if taken or instituted under this Act –

- (d) an objection, appeal to the tax board, tax court or higher court, alternative dispute resolution, settlement discussions or other related High Court application;'

Judge Pretorius held the following:

As to the points in limine

- (i) That section 82 of the Income Tax Act dealing with the incidence of the onus in tax matters was repealed by section 271 of the Tax Administration Act on 1 October 2012. SARS had imposed a 100% additional tax in terms of section 76 of the Income Tax Act and this decision was made by SARS in terms of the law as it prevailed at the time, prior to 1 October 2012 and in terms of section 82 the burden of proof was always on the taxpayer.
- (ii) That section 270 of the Tax Administration Act was a provision regulating transitional matters, such as the present matter, and dealt with procedural matters as well. Section 270(2)(d) provided clearly that an appeal which was launched prior to 1 October 2012 and not completed before 1 October 2012 was to be concluded under the provisions of the Tax Administration Act.
- (iii) That it was quite clear that in this instance the additional tax had been imposed, assessed and levied at the commencement of the Act and the appeal proceedings to the Tax Court were not included and, therefore, section 270(6A) of the Tax Administration Act did not assist SARS in its argument.
- (iv) That as we were only now dealing with the appeal three years after section 270(2)(d) came into operation, the court found that the provisions of section 270(2)(d) were applicable and the result was that the provisions of section 102(2) and section 129(3) of the Tax Administration Act, pertaining to the burden of proof were applicable when dealing with penalties imposed and applied to the current proceedings and due to this finding the rules

promulgated under section 103 of the Tax Administration Act applied to the procedure in these proceedings.

- (iv) That the provisions of section 102(2) of the Tax Administration Act have reversed the onus and SARS has now to prove the case and this is exactly what the sole issue in the present appeal is about.
- (v) That, accordingly, in regard to the points in limine, the burden of proof pertaining to the imposition of additional tax was upon SARS in terms of section 102(2) read with section 129(3) of the Tax Administration Act and the duty to commence the proceedings was on SARS.

As to the legal framework

- (vi) That in CIR v Da Costa the court found that the Tax Court must exercise its own, original discretion, irrespective of the penalty imposed by SARS and it entailed that the Tax Court must deal with the matter without having regard to the findings of SARS and the key words of section 76(2)(a) were 'any act or omission of the taxpayer . . . done with the intent to deceive.'

As to the evidence

- (vii) That it was quite evident from the evidence of the taxpayer's accountant, Mr Z, that he was taking the blame for the under-declaration of the taxpayer's income to SARS and the question was whether the taxpayer must be held accountable for the under-declaration, and, if so, to what extent must she be held liable for paying the penalties as it was quite clear that Mr Z did not account for the tax timeously as after twenty months SARS still did not have the correct information.
- (ix) That counsel for SARS had argued that the ultimate responsibility to submit the correct tax return timeously was that of the taxpayer and that was indeed so and there could be no exception to this at all.
- (x) That the court had to agree that Mr Z's behaviour as an accountant in this matter was less than exemplary and the question was whether the taxpayer should be punished for Mr Z's dilatory behaviour, or only because she did not make enough enquiries as to whether the correct tax return had been submitted timeously and making sure that all was done to have the correct

tax return furnished to SARS timeously.

- (xi) That although the taxpayer had tried to convince the court that she was a clueless, retired housewife, it was clear that she was the trustee of the trusts and had previously owned a business. She had a duty not to leave all her financial affairs in the hands of her attorney and her accountant, without overseeing their actions and ascertaining that all her taxes were paid timeously. There was a duty on her to ensure that the tax return was correct and submitted timeously to SARS. She further failed to enquire as to why her tax liability was so much less than the amounts that she had paid the previous year.
- (xii) That the court had to be careful, especially in this instance, not to punish the taxpayer for her accountant's actions, but had to consider her actions in isolation in this regard but there was a duty on taxpayers to ensure that the professionals they employ are diligent and not to leave it to the tax consultants and it was ultimately the duty of the taxpayer to ensure that the correct amount of tax was paid timeously.
- (xiii) That the court had considered all the facts, as well as the fact that SARS itself was not blameless and found in the present instance that due to the fact that the *fiscus* did not lose any income and this fact was not placed before the Objections Committee, it was mitigating and therefore the court was of the view that the 50% additional tax should be reduced to 35% additional tax.

*As to the legal costs*

- (xiv) The taxpayer had contended that SARS should pay the costs on an attorney and client scale but the court could not find in this instance that SARS had erred in imposing a penalty and did not find that SARS had acted vexatiously or wrongly by contesting the appeal and therefore the proper order would be to make no order as to costs as SARS did not seek costs.

The appeal succeeded and the taxpayer was directed to pay additional tax of 35% in the amount of R3 819 539.

## 4. INTERPRETATION NOTES

### 4.1. *Provisional tax estimates – No. 1 (Issue 2)*

This Note provides guidance on the interpretation of the law relating to provisional tax and considers:

- who is a provisional taxpayer;
- the calculation of provisional tax including how estimates of taxable income must be made;
- the consequences of an incorrect or late submission of estimates;
- the consequences of a late payment of provisional tax; and
- the consequences of failure to submit an estimate on time.

Employees who earn remuneration generally pay tax in the form of employees' tax (PAYE) on a monthly basis. This results in the collection of an employee's normal tax liability being spread throughout the year with a potential additional payment or a refund at the end of the year of assessment. However, for people who do not earn 'remuneration' as defined in the Fourth Schedule, for example, a self-employed person earning business income, in the absence of a provisional tax system the full amount of tax would be payable only on assessment at the end of the year of assessment, without the option or obligation of making interim payments like those paying PAYE monthly.

Provisional tax is not a separate tax payable by certain persons. It is merely a method used to collect normal tax, that will ultimately be payable for the year of assessment concerned, during the year. Otherwise stated, provisional tax is an advance payment of a taxpayer's normal tax liability. A provisional taxpayer is generally required to make two provisional tax payments, one six months into the year of assessment and one at the end of the year of assessment, but has the option to make an additional payment, generally known as the third or top-up payment, after the end of the year of assessment.

Provisional tax payments are calculated on estimated taxable income (which

includes taxable capital gains) for the particular year of assessment. These estimates of taxable income are submitted to SARS on an IRP6 return. The returns, which can be obtained through e-Filing, the SARS contact centre or a SARS branch office, must be submitted even if the amount of the provisional tax payment is nil. The normal tax payable on the estimated taxable income is calculated at the relevant rate of tax that is in force on the date of payment of provisional tax. This would generally be the rate of tax as prescribed in the tax tables which are fixed annually by Parliament. The Commissioner may, from time to time, prescribe alternative tax tables for optional use by provisional taxpayers falling within a certain category.

Provisional tax payments may not be refunded or reallocated to different periods or different taxpayers. However, at the end of the year of assessment the provisional tax payments, together with any PAYE withheld during the year, are set off against the taxpayer's liability for normal tax. Any excess of provisional tax and PAYE over the liability for normal tax is refunded to the taxpayer and any shortfall is payable by the taxpayer to SARS. Interest is generally payable from the effective date, by SARS in the case of a refund and by the taxpayer in the case of a shortfall.

There are certain rules that must be adhered to when making estimates of taxable income for provisional tax purposes. Certain penalties and interest will be imposed if the estimates are inaccurate or if the submission of the estimates or the payment of provisional tax is late. This Note discusses these rules and the interest and penalties which may be imposed.

Provisional tax is a method used to collect normal tax which will ultimately be payable for a particular year of assessment. There are potentially three payments, two of which are compulsory. The first compulsory payment must be made within the first period which ends six months after the start of the year of assessment. The second compulsory payment must be made on or before the end of the second period which ends on the last day of the year of assessment. A third payment, which is voluntary, must generally be made within seven months of the end of the year of assessment for persons with a year of assessment ending on the last day of February and by companies with a different financial year, within six months of the end of such financial year.

The calculation of the amount of a provisional tax payment involves estimating taxable income for the year concerned. Depending on which payment (first, second or third) and on the facts and circumstances of the case, certain penalties may be imposed and interest levied if the estimates are not accurate.

The Act permits a refund of provisional tax payments previously made only if the taxpayer's liability for normal tax has been assessed by the Commissioner and the sum of employees' tax deducted and provisional tax paid in respect of that period exceeds the total liability for normal tax as assessed.

SARS has a range of guides available on its website which provide further practical guidance on provisional tax matters, such as completing an IRP6 return.

#### ***4.2. VAT treatment of the supply of goods or services to and/or from a customs controlled areas of an industrial development zone – No. 40 (Issue 3)***

The purpose of this interpretation note is to set out the VAT implications concerning the various types of supplies of goods or services to and/or from a CCAE/IDZ Operator located in a CCA of an IDZ.

The Department of Trade and Industry (the Department) developed an IDZ Programme with the aim of attracting foreign and local direct investment intended to develop the economic potential of specific geographical areas in the Republic. The IDZ Programme was established in Government Notice R. 1224 on 1 December 2000 by the Minister of Trade and Industry under section 10(1) of the Manufacturing Development Act, No. 187 of 1993 by the promulgation of the IDZ Regulations, concerning the regulation, development and operation of IDZs.

In terms of the IDZ Regulations, the Minister of Trade and Industry may, by notice in the *Government Gazette*, designate a geographical area adjacent to an international harbour or airport, as an IDZ. An IDZ can be described as a geographically designed, purpose-built industrial estate that is linked to an international harbour or airport in an area in the Republic which has been designated by the Minister of Trade and Industry and which contains a delimited

fully secured CCA (or multiple CCAs) where CCAEs will operate and obtain certain benefits and privileges.

An IDZ will be built and operated by an IDZ Operator to whom an IDZ Operator permit was issued by the Minister of Trade and Industry. The IDZ Operator will be responsible for the development, security and maintenance of the IDZ (including the CCA). The IDZ Operator will offer facilities tailored for the manufacture, storage and distribution of goods to boost beneficiation, investment, economic growth and, most importantly, the development of skills and employment in these regions.

Within an IDZ, the areas of operation, which are diagrammatically illustrated below, are as follows:

- CCAs, being designated areas within an IDZ which, upon application by the IDZ Operator, have been approved and designated by the Commissioner in concurrence with the Director General: Trade and Industry as CCAs and which have entrance and exit points that are physically controlled by the IDZ Operator who must also provide support measures and facilities for CCAEs located within the CCA.

Only CCAEs and IDZ Operators that are licensed and/or registered (as applicable) with SARS: Customs will be authorised to operate within a CCA and will be permitted to acquire certain goods exempt from the VAT levied on importation into the Republic, and to acquire certain goods or services from the local market at the zero rate of VAT.

CCAs are controlled by SARS: Customs to the extent that licensing or registration in terms of the Customs and Excise Act is required. In these cases, only the premises where approved enterprise and business activities will be conducted will be controlled by SARS: Customs.

- The area outside the CCA but within an IDZ (also referred to as the industries and services area), being an industrial or office park type environment surrounding the CCAs and which is occupied by service providers or industries supplying local services or raw materials to CCAEs and IDZ Operators.

*The SEZ Programme*

The Department began a review of the IDZ Programme in 2007 that was brought about by developments in the national economic policies and strategies such as the Industrial Policy Framework and the New Growth Path as well as developments in the global economic environment. This review has led to the development of a SEZ Programme by the Department which aims to address the challenges of the current IDZ Programme in order to achieve the national and regional industrial development policy objectives.

A Special Economic Zone (SEZ) is defined as a 'geographically designated area of a country set aside for specifically targeted economic activities, which are then supported through special arrangements and support systems to promote industrial development'.

The implementation of the SEZ Programme will be carried out in conjunction with other departments and agencies with the purpose of achieving certain defined objectives. SEZs may be either sector specific or multi-product specific and will include free ports, free trade zones, industrial development zones and sector development or specialised zones. Each of these different categories of SEZs are meant to complement one another and can be integrated into a single zone plan.

The Department has established a legislative framework for SEZs with the promulgation of the Special Economic Zones Act, No. 16 of 2014 (the SEZ Act) which came into effect on 27 January 2016. This framework has been complemented by regulations made under section 42 of the SEZ Act which were also promulgated on 27 January 2016.

Changes to the VAT Act to accommodate the introduction of the SEZ Act have been promulgated in terms of the Tax Administration Laws Amendment Act, No. 44 of 2014 but these changes will only come into effect once the Customs Control Act, No. 31 of 2014 comes into operation. The interpretation note will then be updated accordingly.

This interpretation note endeavours to provide guidance and clarity on the VAT implications of transactions where goods and/or services are supplied to and/or from a CCA.

## 5. DRAFT INTERPRETATION NOTES

### 5.1. *Exemption from income tax: foreign employment income*

This Note discusses the interpretation and application of the foreign employment remuneration exemption in section 10(1)(o)(ii) of the Income Tax Act.

The correct method of apportionment is also examined, as well as how the exemption affects gains included in income upon the vesting of any equity instrument under section 8C.

The terms of tax treaties vary from treaty to treaty, and so the possible effects of tax treaties are not discussed in this Note.

The potential for an exemption under section 10(1)(o)(ii) does not automatically waive the obligation of an employer to deduct employees' tax under the Fourth Schedule. An employer that is satisfied that the provisions of section 10(1)(o)(ii) will apply in a particular case may, however, elect not to deduct employees' tax in a particular case. In the case where the exemption was not applicable, the employer will be liable for the employees' tax not deducted as well as the concomitant penalties and interest.

For employees' tax certificate (IRP5 certificate) purposes, each remuneration item qualifying for the section 10(1)(o)(ii) exemption must be disclosed under the relevant foreign service income source code. For example, foreign salary income must be disclosed under code 3651, bonus payments under code 3655 and medical aid contributions under code 3860. Code 3652 may not be used for any remuneration item that may qualify for exemption under section 10(1)(o)(ii).

An employer that has deducted or withheld employees' tax where it subsequently transpires that the remuneration qualifies for exemption under section 10(1)(o)(ii) may not refund over-deducted employees' tax to an employee. The employee must claim a refund on assessment. Supporting documentation in the form of, for example, a passport and an employment contract, may be requested from the employee to substantiate the exemption claimed on assessment.

Remuneration that is exempt under section 10(1)(o)(ii) is not 'remuneration' as defined in paragraph 1 of the Fourth Schedule. As such amounts are not

'remuneration', they are not subject to unemployment insurance fund contributions under the Unemployment Insurance Contributions Act No. 4 of 2002 or the skills development levy under the Skills Development Levies Act No. 9 of 1999 unless the Minister of Higher Education and Training, by notice in the Gazette, determines a different basis for the calculation of the levy, which basis included such exempt amounts. Any remuneration that remains taxable in South Africa will still be subject to the deduction or withholding of levies or contributions under these statutes.

## **5.2. *Taxation of REITs and controlled companies***

This Note:

- provides guidance on the interpretation and application of section 25BB which deals with the taxation of REITs and controlled companies;
- considers other selected provisions of the Act that are particularly relevant to REITs, controlled companies and the holders of shares or linked units in these companies;
- does not discuss all the sections which apply to REITs and controlled companies, such as sections 42, 45 and 47 of the corporate rules which, while not specifically referring to REITS and controlled companies, are nevertheless applicable to REITS and controlled companies; and
- reflects the amendments introduced by the Taxation Laws Amendment Act No. 25 of 2015.

Before the introduction of specific REIT legislation in South Africa, two forms of listed property investment entities existed in South Africa, namely, property loan stock companies and property unit trusts (collective investment schemes in property). These entities were subject to different regulatory controls and tax treatment. A collective investment scheme in property operated as a trust both in reality and for income tax purposes, while a property loan stock company operated as a company. A unified approach was adopted and REITs were introduced in South Africa with effect from 1 April 2013. The REIT is the international standard and more than 25 countries in the world use a similar REIT model.

South African REITs own several kinds of commercial property like shopping centres, office buildings, factories, warehouses, hotels, hospitals and, to a lesser extent, residential property, in South Africa. Some REITs also invest in property in other countries. The objective of a REIT is to provide investors with steady rental income and capital growth in the underlying properties.

A REIT may be a company as commonly understood or may be deemed to be a company for taxation purposes.

Both corporate and trust (collective investment schemes in property) REITs that comply with the JSE Limited Listings Requirements may be listed and publicly traded on the JSE REIT board. Once the shares in a company or a trust which is deemed to be a company for tax purposes are listed as shares in a REIT as defined in paragraph 13.1(x), the company or trust will qualify as a REIT for income tax and CGT purposes.

A REIT, and a 'controlled company' as defined<sup>8</sup> in relation to a REIT, are subject to a specific tax regime under section 25BB. In essence a REIT and a controlled company are treated as a conduit for the income derived by it, with the REIT or controlled company being granted a deduction, subject to various limitations, for the distributions it makes of such income. A resident investor is subject to normal tax on those distributions. By contrast, a non-resident investor would be liable for dividends tax on those distributions, not normal tax.

A REIT or controlled company is also subject to other specific tax provisions, for example dividends tax, transfer duty and securities transfer tax.

Section 25BB introduced a uniform set of rules for the taxation of REITs and their controlled companies as well as the holders of shares or linked units in such REITs and controlled companies with effect from years of assessment commencing on or after 1 April 2013. In order to qualify as a REIT, a company or portfolio of a collective investment scheme in property must be a resident, be listed on the JSE as a REIT and meet the JSE's listings requirements. A REIT in reality can be a trust if it takes the form of a portfolio, but for income tax purposes it is deemed to be a company.

The effect of section 25BB is to treat a REIT or a controlled company as a flow-

through entity for income tax purposes. This treatment is achieved by allowing the REIT or a resident controlled company a deduction for a 'qualifying distribution.' The deductible amount of the qualifying distribution is limited to the taxable income of the REIT or controlled company before taking into account:

- the qualifying distribution;
- any assessed loss brought forward from the previous year of assessment;  
and
- any taxable capital gain.

A distribution by a REIT or a controlled company that was in existence at the end of the preceding year of assessment will constitute a deductible qualifying distribution only if at least 75% of any gross income derived by the REIT or controlled company for the preceding year of assessment consists of 'rental income'. A similar rule applies during the first year of assessment in which a company qualifies as a REIT or controlled company, but in such event the gross income derived by the REIT or controlled company for that year of assessment is used. Rental income includes dividends from another REIT, dividends or foreign dividends from a property company, a qualifying distribution from a controlled company and income from the use of immovable property.

The REIT and controlled company must disregard any capital gain or capital loss on disposal of shares or linked units in another REIT or a property company as well as any capital gain or capital loss on disposal of immovable property. However, a REIT or a controlled company must account for other capital gains and losses while proceeds of a revenue nature on the disposal of assets are included in gross income.

Interest received by or accrued to a person during a year of assessment on a debenture forming part of a linked unit in a REIT or a controlled company that is a resident is deemed to be a dividend. Such dividends are fully taxable for normal tax purposes in the hands of resident holders of shares but are exempt from dividends tax. Non-residents are exempt from normal tax on such dividends but are instead subject to dividends tax.

Interest received by or accrued to a person during a year of assessment on a

debenture forming part of a linked unit in a non-resident controlled company is deemed to be a foreign dividend.

The other provisions of the Act and other legislation dealing with REITs, controlled companies and the holders of shares or linked units, as discussed in this Note, should also be considered.

### ***5.3. Exemption from income tax: Remuneration derived by a person as an officer or crew member of a ship***

This Note provides guidance on the circumstances under which section 10(1)(o)(i) exempts the remuneration derived by a person as an officer or crew member of a ship from normal tax.

Section 10(1)(o)(i) was inserted into the Act in 1993, to bring the provisions of the Income Tax Act in line with that of other major maritime nations, which exempt certain seafarers from normal tax if they are absent from their home countries for a period or periods exceeding 183 days in aggregate during the year of assessment.

In 2007, the definition of 'Republic' in section 1(1) was amended, and the effect of that amendment is discussed in this Note. The impact of any agreement for the avoidance of double taxation is not discussed, as the terms of such agreements vary from treaty to treaty.

The remuneration of officers or crew members of ships engaged for reward in the international transportation of passengers or goods, or ships engaged in the prospecting, exploration, mining or production of minerals if employed solely for the passage of such ships, is exempt from taxation if those officers or crew members are outside South Africa for a period or periods exceeding 183 full days in total during a year of assessment.

In certain circumstances, the remuneration of officers or crew members may not be sufficient to qualify for the exemption in section 10(1)(o)(i). It may, however, be possible that the remuneration of these officers or crew members qualify for the exemption under section 10(1)(o)(ii).

## 6. BINDING PRIVATE RULINGS

### 6.1. *BPR 227 – Share subscription transaction followed by two share repurchase transactions*

This ruling determines the income tax, capital gains tax, dividends tax and securities transfer tax consequences resulting from a share subscription transaction followed by two share repurchase transactions.

In this ruling references to sections and paragraphs are to sections of the relevant Act and paragraphs of the Eighth Schedule to the Income Tax Act applicable as at 15 February 2015. Unless the context indicates otherwise, any word or expression in this ruling bears the meaning ascribed to it in the relevant Act.

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

- the Act:
  - section 1(1) – definition of 'contributed tax capital' and 'gross income';
  - section 9C;
  - section 10(1)(k);
  - section 64E;
  - section 64EA;
  - section 64F; and
  - paragraph 1 – definition of 'disposal';
  - paragraph 3;
  - paragraph 4;
  - paragraph 11; and
  - paragraph 35.
- the STT Act –
  - section 1 – definition of 'transfer' and 'security';

- section 2; and
- section 6.

Parties to the proposed transaction

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

Co-Applicant A: A state-owned company incorporated in and a resident of South Africa

Co-Applicant B: A private company incorporated in and a resident of South Africa

Description of the proposed transaction

The parties consider that a share subscription transaction followed by two share repurchase transactions will be the most commercially efficient manner for implementing the Applicant's exit, as a shareholder, from Co-Applicant A.

The Applicant is one of three shareholders of Co-Applicant A. Co-Applicant A is a state owned company that is the shareholder of Co-Applicant B.

For operational and strategic reasons the Applicant intends to divest from Co-Applicant A to manage its investment in Co-Applicant B directly.

The proposed transaction will be implemented as follows:

- The Applicant will obtain intra-day funding from Bank A.
- The Applicant will use the intra-day funding and its own funds to subscribe for equity shares in Co-Applicant B.
- Co-Applicant B will use the proceeds received from the Applicant to enter into a share repurchase transaction for a specified number of equity shares held by Co-Applicant A (first share repurchase transaction). The repurchase consideration will be settled in cash and the securities transfer tax paid.
- Co-Applicant A will use the proceeds received from Co-Applicant B to enter into a share repurchase transaction for all the shares held by the Applicant (second share repurchase transaction). The repurchase consideration will be settled in cash and the securities transfer tax paid.

- The Applicant will use the proceeds received from Co-Applicant A to repay Bank A.

The Boards of Directors of Co-Applicant B and Co-Applicant A will elect that portions of the proceeds to be received by Co-Applicant A and the Applicant in terms of the first share repurchase transaction and second share repurchase transaction respectively, will be applied as returns of capital.

The shares which Co-Applicant A holds in Co-Applicant B and the shares which the Applicant holds in Co-Applicant A have been held for a period of at least 3 years for purposes of section 9C(2) of the Act.

#### Conditions and assumptions

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

#### Ruling

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

- The subscription price to be received by Co-Applicant B for the issue of the shares will constitute 'contributed tax capital' as defined in section 1(1) of the Act.
- The issue of the shares by Co-Applicant B will not constitute a disposal for purposes of the Eighth Schedule to the Act and hence no capital gain will arise on their issue.
- No securities transfer tax will be payable on the issue of the shares by Co-Applicant B.
- A portion of the proceeds to be received by Co-Applicant A for the disposal of the shares in Co-Applicant B will be deemed to be of a capital nature under section 9C(2) of the Act.
- The balance of the proceeds to be received by Co-Applicant A for the disposal of the shares in Co-Applicant B will be regarded as a 'dividend' as defined in section 1(1) of the Act and must be included in the gross income of Co-Applicant A.

- The dividend to be included in the gross income of Co-Applicant A will be exempt from normal tax under section 10(1)(k)(i) of the Act.
- The repurchase of the equity shares held by Co-Applicant A in Co-Applicant B in terms of the first share repurchase transaction will be regarded as a disposal of assets by Co-Applicant A for purposes of the Eighth Schedule to the Act.
- The proceeds for purposes of the Eighth Schedule to the Act will be reduced by the amount which is regarded to be a dividend and consequently included in the gross income of Co-Applicant A.
- No liability for dividends tax will arise in respect of the first share repurchase transaction as Co-Applicant A is a resident company.
- A liability for securities transfer tax will arise in respect of the first share repurchase transaction on the transfer of the shares in Co-Applicant B.
- A portion of the proceeds to be received by the Applicant for the disposal of the shares in Co-Applicant A will be deemed to be of a capital nature under section 9C(2) of the Act.
- The balance of the proceeds to be received by the Applicant for the disposal of the shares in Co-Applicant A will be regarded as a 'dividend' as defined in section 1(1) of the Act and must be included in the gross income of the Applicant.
- The dividend to be included in the gross income of the Applicant will be exempt from normal tax under section 10(1)(k)(i) of the Act.
- The repurchase of the equity shares held by the Applicant in Co-Applicant A in terms of the second share repurchase transaction will be regarded as a disposal of assets by the Applicant for purposes of the Eighth Schedule to the Act.

- The proceeds for purposes of the Eighth Schedule to the Act will be reduced by the amount which is regarded to be a dividend and consequently included in the gross income of the Applicant.
- No liability for dividends tax will arise in respect of the second share repurchase transaction, as the Applicant is a resident company.
- A liability for securities transfer tax will arise in respect of the second share repurchase transaction on the transfer of the shares in Co-Applicant A.

## **6.2. BPR 228 – Whether an investment of preference share funding funding in a newly established business is for a 'qualifying purpose'**

This ruling determines whether:

- a newly established company will be regarded as an 'operating company';  
and
- an indirect investment into such company will be for a 'qualifying purpose'.

In this ruling references to sections are to sections of the Income Tax Act applicable as at 31 October 2015. Unless the context indicates otherwise, any word or expression in this ruling bears the meaning ascribed to it in the Act.

This is a ruling on the interpretation and application of the provisions of section 8EA(1) – definition of 'operating company' and 'qualifying purpose'.

### Parties to the proposed transaction

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

The Co-Applicant: A finance provider

The Project company: A newly established company that is incorporated in and a

resident of South Africa

Description of the proposed transaction

The Project company will undertake a business project as it intends to produce goods and services and to sell these goods and services for consideration. The Project company will fund the business project costs necessary by means of 80% debt and 20% equity.

The Applicant will hold 25% of the ordinary shares in the Project company as a BEE partner. The shares in the Applicant are held 100% by its holding company.

The Applicant will fund the subscription price of the ordinary shares in the Project company out of the proceeds of:

- issuing ordinary shares to its holding company; and
- issuing preference shares to the Co-Applicant.

The Co-Applicant requires that the Applicant's holding company provides the Co-Applicant with:

- a guarantee for any amount which the Applicant has contracted to pay to the Co-Applicant, but fails to pay in respect of the preference shares; and
- a cession and pledge by the Applicant's holding company of its shares in the Applicant.

At the time of the investment in the Project company, the Project company will not be operating and will not be providing the goods or services it intends to provide for consideration. The Project company is expected to be operational within eighteen months from the commencement of the construction of its plant.

Conditions and assumptions

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

Ruling

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

- The use of funds derived from the issue of the preference shares to subscribe for the ordinary shares in the Project company will not be applied

for a 'qualifying purpose' as defined in section 8EA(1), as the Project company will not be an 'operating company' as defined.

### **6.3. BPR 229 – Employer provided accommodation to employees**

This ruling determines whether vacant stands to be acquired by qualifying employees from their employer will constitute 'immovable property' as contemplated in paragraph 5(3A) of the Seventh Schedule to the Act.

In this ruling references to paragraphs are to paragraphs of the Seventh Schedule to the Income Tax Act applicable as at 15 October 2015. Unless the context indicates otherwise, any word or expression in this ruling bears the meaning ascribed to it in the Act.

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

- paragraph 2(a); and
- paragraph 5(1), (2) and (3A).

#### Parties to the proposed transaction

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

#### Description of the proposed transaction

The Applicant is a mining company that is subject to the Mineral and Petroleum Resources Development Act No. 28 of 2002 (the MPRDA) and the Broad-Based Socio-Economic Empowerment Charter for the South African Mining and Minerals Industry (the Mining Charter). It follows that the Applicant is required to comply with its obligations under the MPRDA and the Mining Charter to improve the housing standards of its employees.

The Applicant intends to sell vacant stands (stands) to certain of its employees (qualifying employees) on terms that, amongst others, oblige each qualifying employee purchaser to erect a house on the stand at the employee's own cost within a specified time period.

The purchase price of each stand will be less than the market value of the stand.

### Conditions and assumptions

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

### Ruling

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

- The stands constitute 'immovable property' as envisaged in paragraph 5(3A). No value will be placed on a stand so acquired by a qualifying employee if –
  - the market value of the stand does not exceed R450 000 on the date of acquisition;
  - the remuneration proxy of the employee does not exceed R250 000 in relation to the year of assessment during which the stand is so acquired; and
  - the employee is not a connected person in relation to the Applicant.

## **6.4. BPR 230 – Disposal of an asset in terms of an asset-for-share transaction within 18 months of its acquisition in terms of an intra-group transaction**

This ruling determines the income tax consequences under section 45(5) in respect of the disposal of an asset in terms of an asset-for-share transaction, within 18 months of the acquisition of the asset in terms of an intra-group transaction.

In this ruling references to sections are to sections of the Income Tax Act applicable as at 2 March 2016. Unless the context indicates otherwise, any word or expression in this ruling bears the meaning ascribed to it in the Act.

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

- section 42(1), paragraph (a)(i)(aa) of the definition of 'asset-for-share transaction';

- section 42(2); and
- section 45(5).

#### Parties to the proposed transaction

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

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

Company B: A company incorporated in and a resident of South Africa that is a wholly-owned subsidiary of the Applicant

Company C: A company incorporated in and a resident of South Africa, in which the Applicant holds an equity interest

#### Description of the proposed transaction

Company A previously held an equity interest in Company C as a capital asset, that it transferred to the Applicant at market value. The transaction was treated as an intra-group transaction under section 45. The Applicant holds the shares in Company C as a capital asset.

In order to streamline the corporate and operational structure of the group in South Africa, the Applicant will transfer its shareholding in Company C to Company B by way of an asset-for-share transaction as contemplated by section 42.

#### Conditions and assumptions

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

#### Ruling

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

- The disposal by the Applicant of the shares in Company C in terms of the proposed transaction, within 18 months of the acquisition of those shares in terms of the 'intra-group transaction', will not result in a capital gain under section 45(5)(a)(i).

## **6.5. BPR 231 – Corporate restructuring by way of asset-for-share and amalgamation transactions**

This ruling determines the income tax and securities transfer tax consequences resulting from a corporate restructuring by way of an asset-for-share and three amalgamation transactions.

In this ruling references to sections and paragraphs are to sections of the Income Tax Act and the STT Act and paragraphs of the Eighth Schedule to the Act applicable as at 31 March 2016. Unless the context indicates otherwise, any word or expression in this ruling bears the meaning ascribed to it in the relevant Act.

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

- the Act:
  - section 42;
  - section 44; and
  - paragraph 11(2)(b)(i).
- the STT Act:
  - section 8(1)(a)(ii).

### Parties to the proposed transaction

**Holdco:** A company incorporated outside of South Africa, and not a resident, the controlling company of a group of companies (the group) which includes the Applicant and some of the Co-Applicants

**The Applicant:** A company incorporated in and a resident of South Africa that is held 74% by Foreignco and 26% by black economic empowerment (BEE) shareholders

**The Co-Applicants:**

**Foreignco:** A company incorporated outside of South Africa, and not a resident, that is a wholly-owned subsidiary of Holdco

**Mineco1:** A company incorporated in and a resident of South Africa that is a wholly-owned subsidiary of Holdco

Mineco2: A company incorporated in and a resident of South Africa that is a wholly-owned subsidiary of Holdco

Beeco1: A company incorporated in and a resident of South Africa that is held 51% by BEE shareholders and 49% by Holdco

Beeco2: A company incorporated in and a resident of South Africa that is a wholly-owned subsidiary of Beeco1

Beeco3: A company incorporated in and a resident of South Africa that is held 87% by BEE shareholders and 13% by Mineco2

#### Description of the proposed transaction

The Applicant and the relevant subsidiary Co-Applicants intend to rationalise its South African group structure so as to simplify the structure by eliminating:

- unnecessary companies and structures; and
- complex BEE structures.

In two unincorporated joint ventures (UJVs) the BEE companies and the Holdco subsidiaries participate as follows:

- Mineco1 and Beeco2 jointly participate in the mining operation of Mine 1 in the ratio of 74:26; and
- Mineco2 and Beeco3 jointly participate in the mining operation of Mine 2 in the ratio of 70:30. Mineco2 also holds 13,33% of the equity in Beeco3. It therefore effectively holds 73,99% (70% directly and 3,99% indirectly through Beeco3) in the UJV.

The group proposes to enter into the following transactions in order to eliminate these UJVs and unnecessary companies in its structure:

#### Transaction 1: Amalgamation transaction between the Applicant and Foreignco

The group wishes to eliminate the intermediate holding of the Applicant's shares by Foreignco as follows:

- Foreignco will dispose of its shares in the Applicant for a new issue of shares in the Applicant in terms of an 'amalgamation transaction' as defined in section 44(1) of the Act.
- The new shares in the Applicant will be distributed by Foreignco to its sole shareholder, Holdco, in terms of the relevant amalgamation agreement.
- Foreignco will then be liquidated in terms of that amalgamation agreement.

#### Transaction 2: Amalgamation transaction between Beeco1 and Beeco2

- Beeco1 will dispose of its shares in Beeco2 for a new issue of shares in Beeco2 in terms of an 'amalgamation transaction' as defined in section 44(1) of the Act.
- The new shares in Beeco2 will be distributed by Beeco1 to its shareholders in terms of the relevant amalgamation agreement.
- Beeco1 will then be liquidated in terms of that amalgamation agreement.

#### Transaction 3: Asset-for-share transaction between Beeco2 and Mineco1

- Beeco2 will dispose of its 26% stake in Mine 1 UJV to Mineco1 in exchange for (what will be after the share issue) 26% of the equity shares in Mineco1 in terms of an 'asset-for-share transaction' as defined in section 42(1) of the Act.
- The UJV will consequently dissolve.

#### Transaction 4: Amalgamation between Beeco3 and Mineco2

- a) Beeco3 will dispose of its 30% stake in Mine 2 UJV to Mineco2 in exchange for (what will be after the share issue) 28.85% of the equity shares in Mineco2 in terms of an 'amalgamation transaction' as defined in section 44(1) of the Act.
- b) Beeco3 will in terms of the relevant amalgamation agreement distribute

the shares received in Mineco2 to its shareholders.

c) Beeco3 will then be liquidated in terms of that amalgamation agreement.

The result of the above transactions is that Mineco1 and Mineco2 will exclusively operate the mining operations of Mine 1 and Mine 2 respectively, with Beeco2 and the previous BEE shareholders of Beeco3 respectively holding their BEE stake by way of shares in those companies.

#### Conditions and assumptions

This binding private ruling is made subject to the additional condition and assumption that the disposal of shares in the Applicant by Foreignco referred to in transaction 1 and the disposal of shares in Beeco2 by Beeco1 referred to in transaction 2 will be done in two tranches as provided for in the relevant amalgamation agreements.

#### Ruling

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

##### Transaction 1: Amalgamation transaction between the Applicant and Foreignco

The transfer by Foreignco of its shares to the Applicant (being its only remaining assets) under the amalgamation agreement between the two parties will constitute an 'amalgamation transaction' as defined in paragraph (b) of the definition of that term in section 44(1) of the Act. Consequently:

- Foreignco will be deemed to have disposed of its shares in the Applicant for an amount equal to their base cost, as contemplated in section 44(2)(a)(i). The shares in the Applicant will be cancelled upon acquisition by the Applicant.
- No dividends tax will be payable on the distribution by Foreignco to its shareholder of its newly-acquired shares in the Applicant.
- No securities transfer tax (STT) will be payable by virtue of section 8(1)(a)(ii) of the STT Act on the transfer of the Applicant's shares from Foreignco to the Applicant or on the distribution by Foreignco

of its newly-acquired shares in the Applicant to its shareholder.

Transaction 2: Amalgamation transaction between Beeco1 and Beeco2

The transfer of the assets by Beeco1 to Beeco2 under the amalgamation agreement between these two parties will constitute an 'amalgamation transaction' as defined in paragraph (a) of the definition of that term in section 44(1) of the Act. Consequently:

- Beeco1 will be deemed to have disposed of its shares in Beeco2 for an amount equal to their base cost, as contemplated in section 44(2)(a)(i) of the Act, therefore, no capital gain or loss will arise on the disposal of Beeco2's shares by Beeco1. The shares in Beeco2 will be cancelled upon acquisition by Beeco2.
- Beeco1 must, when determining its taxable income, disregard any capital gain or loss on the disposal of its newly-acquired shares in Beeco2 when it distributes these shares to its shareholders, as contemplated in section 44(8) of the Act.
- No dividends tax will be payable on the distribution by Beeco1 to its shareholders of its newly-acquired shares in Beeco2 as the distribution is deemed not to be a dividend under section 44(6)(c) of the Act.
- No STT will be payable by virtue of section 8(1)(a)(ii) of the STT Act on the transfer of Beeco2 shares from Beeco1 to Beeco2 or on the distribution by Beeco1 of its newly-acquired shares in Beeco2 to its shareholders.

Transaction 3: Asset-for-share transaction between Beeco2 and Mineco1

The proposed transaction between Beeco2 and Mineco1 will be an 'asset-for-share transaction' as defined in paragraph (a) of the definition of that term in section 42(1) of the Act. Therefore section 42 of the Act will be applicable to the transaction. Consequently:

- Beeco2 will not:

- recover or recoup any allowances (including the allowance under section 15(a) of the Act read with section 36 of the Act) previously deducted by it in respect of the applicable allowance assets as contemplated in section 42(3)(a)(i) of the Act, nor
  - realise a taxable capital gain as a result of the transfer of any capital assets as contemplated in section 42(2)(a)(i) of the Act.
- Mineco1 will be entitled to the same capital allowances in respect of the applicable allowance assets to which Beeco2 was previously entitled as contemplated in section 42(3)(a)(iii) of the Act.
- Trading stock to be disposed of by Beeco2 will be deemed to be disposed of at the cost determined under section 22(1) or (2) of the Act read with section 11(a) of the Act. Mineco1 will be deemed to acquire the trading stock at the said cost. Beeco2 and Mineco1 will be deemed to be one and the same person as envisaged in section 42(2)(b) of the Act.

#### Transaction 4: Amalgamation between Beeco3 and Mineco2

The transfer by Beeco3 of all its assets to Mineco2 under the amalgamation agreement will constitute an 'amalgamation transaction' as defined in paragraph (a) of the definition of that term in section 44(1) of the Act. Consequently:

- Beeco3 will not:
  - recover or recoup any allowances (including the allowance under section 15(a) of the Act read with section 36 of the Act) previously deducted by it in respect of the applicable allowance assets as contemplated in section 44(3)(a)(i) of the Act, nor
  - realise a capital gain as a result of the transfer of any capital assets as contemplated in section 44(2)(a)(i) of the Act.

- Mineco2 will be entitled to the same capital allowances in respect of the applicable allowance assets to which Beeco3 was previously entitled as contemplated in section 44(3)(a)(ii) of the Act.
- Trading stock to be disposed of by Beeco3 will be deemed to be disposed of at the cost determined under section 22(1) or (2) of the Act read with section 11(a) of the Act. Mineco2 will be deemed to acquire the trading stock at the said cost as contemplated in section 44(2)(b) of the Act.
- When Beeco3 distributes its newly-acquired shares in Mineco2 to its shareholders, Beeco3 must disregard any capital gain or loss on the disposal of the shares in Mineco2, in determining its taxable income as contemplated in section 44(8) of the Act.
- No dividends tax will be payable on the distribution by Beeco3 to its shareholders of its newly-acquired shares in Mineco2, as the distribution is deemed not to be a dividend under section 44(6)(c) of the Act.
- Mineco2 and Beeco3 will not be prejudiced by the fact that Mineco2 is a shareholder of the amalgamated company, Beeco3, and therefore receives shares in itself, which will be cancelled when Beeco3 distributes the resultant company's shares to its shareholders pursuant to the amalgamation. Section 44 of the Act will therefore still apply.
- Pursuant to the cancellation of the shares in Mineco2, there will be no disposal of an asset as provided for in paragraph 11(2)(b)(i) of the Eighth Schedule to the Act when Mineco2 receives shares in itself which are then cancelled. Consequently, no capital loss will arise on that cancellation.
- No STT will be payable on the transfer of the shares from Beeco3 to Mineco2 by virtue of section 8(1)(a)(ii) of the STT Act.

## **6.6. BPR 232 – Equity shares to be issued by resultant company as part of an amalgamation transaction**

This ruling determines whether the shares of each class to be issued by a resultant company following an amalgamation transaction will be equity shares as defined in section 1(1) of the Income Tax Act.

In this ruling references to sections are to sections of the Act applicable as at 1 June 2015. Unless the context indicates otherwise, any word or expression in this ruling bears the meaning ascribed to it in the Act.

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

- section 1(1) – the definition of 'equity share'; and
- section 44(1) – the definition of 'amalgamation transaction'.

### Parties to the proposed transaction

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

The Co-Applicants:

- Shareholders: Companies incorporated in and residents of South Africa that will be the shareholders of the Amalgamated companies
- Amalgamated companies: Companies incorporated in and residents of South Africa that will be wound up as part of the amalgamation transaction
- Resultant company: A company incorporated in and a resident of South Africa that will remain in existence after the amalgamation transaction

### Description of the proposed transaction

The Applicant and the Co-Applicants decided to rationalise the administration of their businesses, of which the underlying nature is identical, by amalgamating the businesses in a single entity and terminating the existence of the existing companies.

The Applicant and the Co-Applicants have significant interests in investments in fixed properties, which they hold individually or jointly. The nature of the

investments is in each case similar, comprising of shares in companies that own fixed property which is let to derive rental income. As new projects are identified, the traditional approach has been to form a new entity to own the fixed property, construct improvements and enter into lease agreements with tenants.

The amalgamation will result in the transfer of the assets and liabilities of the Amalgamated companies to the Resultant company, in exchange for shares in its corporate structure. Those shares will be issued on behalf of the Amalgamated companies, after which the Amalgamated companies will be wound up.

The Resultant company will issue shares of different classes. Each class of shares will be linked to a designated property investment. The holders of these shares will each be entitled to a distribution of income and capital, attributable to the income and capital generated by the designated property. The distributions will not be limited to specified amounts.

In the event of a winding-up, if there is any surplus remaining after satisfying the interests of the shareholders of each class, each share shall be entitled to share equally in the surplus. The rights of each class of shareholder will be documented in the memorandum of incorporation.

#### Conditions and assumptions

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

#### Ruling

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

- The disposal by the respective Amalgamated companies of their businesses to the Resultant company will meet the requirements of an 'amalgamation transaction' as defined in section 44(1).
- The shares of the different classes to be issued by the Resultant company will each constitute an 'equity share' as defined in section 1(1).

### **6.7. BPR 233 – Transfer of a part of a business to a fellow subsidiary**

This ruling determines the tax consequences for the seller and the buyer upon the transfer of a part of the seller's business, specifically:

- whether the settlement of the seller's actual obligations by the buyer will result in a recoupment for the seller;
- whether an amount accrues to or is received by the buyer as gross income if the seller transfers an cash amount to the buyer in order to take over certain of the seller's contingent liabilities; and
- whether, in that event, the buyer will be entitled to an allowance in respect of future expenditure on the relevant contracts.

In this ruling references to sections and paragraphs are to sections of the Income Tax Act and paragraphs of the Eighth Schedule thereto applicable as at 8 December 2015. Unless the context indicates otherwise, any word or expression in this ruling bears the meaning ascribed to it in the Act.

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

- section 1(1) – definition of 'gross income';
- section 8(4)(a);
- section 11(a) read with section 23(g);
- section 24C;
- section 45(4B);
- paragraph 3(a);
- paragraph 4(a); and
- paragraph 4(b)(ii)(aa).

Parties to the proposed transaction

The Applicant: A company incorporated in and a resident of South Africa that will be disposing of a part of its business to the Co-Applicant

The Co-Applicant: A new company incorporated in and a resident of South Africa that will acquire a part of the business from the Applicant

Newco: A new company incorporated in and a resident of South Africa that will be the holding company of the Applicant and the Co-Applicant

### Background

The Applicant provides business process services and software solutions to, amongst others, the automotive insurance industry in South Africa, which can be divided into two categories, financial services and non-financial services business.

The non-financial services business includes, amongst others:

- the issuing of motor vehicle service plans and motor vehicle maintenance plans to customers (customer contracts). The Applicant bears the cost of the services and/or maintenance of the motor vehicles covered by the respective plans. It also provides related administrative services; and
- the administration and management of motor vehicle service plans and motor vehicle maintenance plans issued by, amongst others, the motor vehicle manufacturers and other third party corporate entities (corporate client contracts).

The customer contracts are entered into directly between the Applicant and the customer. The contracts provide cover for the duration of the relevant plan for the following items:

- all specified motor vehicle manufacturer services;
- the replacement of certain maintenance items to motor vehicles;
- labour charges for the services and maintenance rendered; and
- consumables and sundry charges.

The Applicant's obligation under the customer contracts is to settle the costs of the motor vehicle service as covered by the plan and to provide the administration services necessary for the implementation of the plan. The obligations are conditional upon the customer taking his or her motor vehicle for a service. As consideration for the cover provided, the customer is required to pay either a premium in advance or monthly premiums.

The service plan terminates on the earlier of reaching either the stipulated contract kilometre limit or the stipulated contract period. In the event that a customer cancels the plan, and if a refund is due, all costs incurred will be deducted and the balance refunded to the customer on a *pro rata* basis within 30 days.

The corporate client contracts are entered into between the Applicant and various corporate clients. Similar administration services as in the case of the customer contracts are provided. The Applicant also provides additional administrative services to the corporate clients. Upon a corporate plan being issued by a corporate client to a motor vehicle owner the Applicant becomes obliged to perform policy loading, policy administration and premium collection and reconciliation services. Similar to the customer contracts described above, the obligations of the Applicant are conditional upon the owner taking his or her motor vehicle for a service. As consideration, the corporate client either pays a premium in advance or monthly premiums.

The Applicant will transfer the relevant contracts where the customers and clients have paid premiums in advance (hereafter referred to as prepaid customer contracts or the prepaid corporate client contracts, where applicable) to the Co-Applicant.

The Applicant has historically claimed the section 24C allowance relating to the administration services in respect of income received in advance.

#### Description of the proposed transaction

The proposed restructuring entails the incorporation of two new companies, a new South African holding company (Newco) and the Co-Applicant to whom the Applicant will sell a part of its business. The proposed series of transactions to achieve this restructuring is set out below:

##### Incorporation of Newco

The current holding company of the Applicant will transfer its shares in the Applicant to Newco in return for shares in Newco in the same proportion as its shareholding in the Applicant.

##### Sale of the shares of operating subsidiaries to Newco

The Applicant will sell its shares in its operating subsidiaries to Newco. Newco will function as the holding company for the South African operating subsidiaries. The sale will take place at book value and the Applicant will undertake a return of capital to Newco. The purchase price and return of capital distribution will be paid in cash.

Incorporation of the Co-Applicant and the sale of the Applicant's non-financial services business

The Co-Applicant will be incorporated with 100% of its shares being held by Newco. The Applicant will sell its non-financial services business (the business) and the group's common infrastructure to the Co-Applicant by way of a section 45 intra-group transaction. The agreement of sale will provide that the Applicant sells to the Co-Applicant the business, comprising of:

- the assets, being the movable assets identified, the accounts receivable, cash, inventories, intangible assets, intellectual property, prepaid expenses and deposits;
- the business contracts which consist of contracts between the Applicant and third parties (corporate client contracts) and the Applicant and customers (customer contracts), excluding the prepaid corporate client and the prepaid customer contracts;
- the rights pertaining to and vested in the business, including any transferable authorisations, if any; and
- the e-mail addresses and the telephone and fax numbers relating to the business as at the effective date,

but, excluding the 'excluded assets', as defined in the agreement of sale.

The purchase price for the sale of the business will be the book value of the assets comprising the business of the Applicant plus R1. Payment is to be made by the assumption by the Co-Applicant of certain liabilities of the Applicant plus a cash payment, if necessary. The liabilities to be delegated by the Applicant to the Co-Applicant, as the payment method of the

purchase price, are defined as the amounts owing by the Applicant to its creditors in respect of:

- finance leases for desktop computers and monitors; and
- accounts payable and sundry creditors.

The excluded liabilities which remain with the Applicant and are not part of the payment, include, amongst others, the contingent liabilities.

As part of the agreement of sale and as required by section 40 of the Basic Conditions of Employment Act No. 79 of 1997 read with section 197 of the Labour Relations Act No. 66 of 1995, the Co-Applicant will take-over the Applicant's leave pay obligations to the employees who are to be transferred from the Applicant to the Co-Applicant. The Applicant will pay a cash amount equal to the value of those obligations to the Co-Applicant.

#### Dividend declaration

The Applicant will declare a cash dividend to Newco out of the sale proceeds.

#### Service level agreement with respect to the group infrastructure

The Applicant and the Co-Applicant will enter into a service level agreement in terms of which the Co-Applicant will make the group infrastructure available to the Applicant. This agreement will stipulate that the parties provide each other with:

- the use of certain of their infrastructure and assets; and
- the services of certain of their employees.

#### Assumption of contingent liabilities

The Co-Applicant will assume the contingent liabilities of the Applicant.

The contingent liabilities of the Applicant relate to performing administrative services and paying the costs of motor vehicle services in terms of the prepaid customer contracts and prepaid corporate client contracts. These obligations may become actual liabilities on the happening of various uncertain future events.

The Applicant has indicated that the reason for not delegating the contingent liabilities as part of the purchase price for the sale of the business is a commercial necessity. The Applicant will make a cash payment to the Co-Applicant equal to the cash value of these obligations as reflected in the Applicant's contingent obligation effective date management accounts

#### Loan agreement

The Co-Applicant will lend part of the cash received from the Applicant to Newco on an interest free basis in terms of a loan agreement.

#### Conditions and assumptions

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

#### Ruling

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

##### The Applicant

The settlement of the Applicant's actual obligations by the Co-Applicant will not result in a recoupment for the Applicant under section 8(4)(a) or under any other provision of the Act, in respect of obligations for which deductions were allowed to the Applicant.

##### The Co-Applicant

The receipt by or accrual of an amount as consideration for the assumption of contingent obligations under the prepaid customer contracts and prepaid corporate client contracts will be included in the Co-Applicant's 'gross income' as defined in section 1(1) in the year of receipt or accrual, whichever occurs first.

The Co-Applicant will be entitled to a section 24C allowance, calculated on the amount so included in its 'gross income'.

The Co-Applicant will be entitled to a deduction when the actual expenses relating to the performance of the prepaid customer contracts and prepaid corporate client contracts are incurred.

The amount to reimburse the Co-Applicant for assuming the leave pay obligations in respect of the Applicant's transferring employees as at the effective date of the sale of business will be a capital receipt or accrual by or in favour of the Co-Applicant.

The Co-Applicant will not be entitled to a deduction in respect of the incurral or payment of actual leave pay obligations, existing at the effective date and taken over from the Applicant in terms of the sale of business agreement.

The Co-Applicant will not realize a capital gain or loss in respect of the receipt of cash payments from the Applicant, relating to its assumption of the Applicant's actual leave pay obligations in respect of employees transferred to it.

Both the Applicant and the Co-Applicant

The loan to be provided by the Co-Applicant to Newco, using a portion of the cash payment received from the Applicant in terms of the sale of business agreement, will not trigger the deemed de-grouping provisions of section 45(4B).

**6.8. BPR 234 – Asset-for-share and unbundling transactions not regulated by sections 42 and 46**

This ruling determines the income tax and securities transfer tax (STT) consequences of an asset-for-share exchange and an unbundling of shares that will not qualify for relief under sections 42 and 46 respectively, of the Act.

In this ruling references to sections and paragraphs are to sections of the relevant Income Tax Act and the STT Act and paragraphs of the Eighth Schedule to the Act applicable as at 3 February 2016. Unless the context indicates otherwise, any word or expression in this ruling bears the meaning ascribed to it in the relevant Act.

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

- the Act:

- section 1(1) – definition of 'contributed tax capital';
- section 42(1) – definition of 'asset-for-share transaction';
- section 46(1) – definition of 'unbundling transaction'; and
- paragraphs 11(2)(b), 39 and 75 of the Eighth Schedule.
- the STT Act:
  - section 2; and
  - section 8(1)(a).

#### Parties to the proposed transaction

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

First Co-Applicant: A foreign unlisted company

Second Co-Applicant: An unlisted company incorporated in and a resident of South Africa

#### Description of the proposed transaction

The Applicant holds 100% of the equity shares in the First Co-Applicant and the Second Co-Applicant. The latter being a dormant company.

The Applicant initially subscribed for shares in the First Co-Applicant constituting 100% of the initial share capital prior to 2013 (initial shares). During the 2013 to 2015 years of assessment the First Co-Applicant issued the Applicant with further shares (additional shares).

The parties propose to implement the following transactions:

- The Applicant will dispose of its entire interest in the First Co-Applicant (the sale shares) to the Second Co-Applicant in return for the issue of shares in the Second Co-Applicant (the consideration shares).
  - The requirements of an 'asset-for-share transaction' as defined in paragraph (a) of that term in section 42(1) are not met, as the market value of the sale shares disposed of will be less than the base cost of the sale shares on the date of the disposal. The disposal will result in a capital loss.

- The Applicant will hold 100% of the shares in the Second Co-Applicant indirectly, instead of directly.
- Subsequent to the asset-for-share transaction, the Applicant proposes to enter into a transaction in terms of which the Applicant will unbundle approximately 20% of its total shareholding (unbundling shares) in the Second Co-Applicant to its shareholders.
  - The unbundling transaction will not be effected under section 46 of the Act, as the Applicant will distribute approximately 20% only of its total equity shares in the Second Co-Applicant to its shareholders. (Paragraph (a)(i) of the definition of 'unbundling transaction' in section 46(1) requires that all the equity shares must be distributed to the shareholders).
  - The transaction will be treated as a distribution of shares to its shareholders.
  - The Applicant will elect that the distribution of the shares in the Second Co-Applicant will constitute a return of capital or a reduction of contributed tax capital in respect of the shares held by the shareholders in the Applicant.
  - The unbundling transaction will be effected in accordance with the JSE's listings requirements and by applying the prescribed 'standard rounding convention' method.
  - As a result of the unbundling the Applicant's shareholding in the Second Co-Applicant will be diluted to approximately 80%.
  - The shares in the Second Co-Applicant will thereafter be listed on the JSE.

#### Conditions and assumptions

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

#### Ruling

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

- The initial shares subscribed for in the First Co-Applicant by the Applicant and the additional shares issued to the Applicant as consideration for the recapitalisation of the First Co-Applicant will be regarded as capital assets in the hands of the Applicant.
- Any capital loss on the disposal of the sale shares by the Applicant to the Second Co-Applicant will be ring-fenced under paragraph 39 of the Eighth Schedule to the Act.
- The distribution of the equity shares in the Second Co-Applicant by the Applicant will constitute a reduction of the Applicant's contributed tax capital and not a dividend *in specie*, hence it will constitute a 'return of capital' as defined in section 1(1) of the Act.
- Paragraph 75 of the Eighth Schedule to the Act will apply to the distribution of the unbundling shares.
- The STT Act does not apply to the transfer of the sale shares to the Second Co-Applicant, as the sale shares constitute shares in a foreign unlisted company.
- Section 8(1)(a) of the STT Act will not apply to exempt the transfer of the unbundled shares to the Applicant's shareholders from STT.
- There is no disposal by the Second Co-Applicant in respect of the issue of the consideration shares as contemplated in paragraph 11(2)(b) of the Eighth Schedule to the Act.

## **6.9. BPR 235 – Income tax consequences for parties to an**

## ***unbundling transaction***

This ruling determines certain income tax consequences for the parties to an unbundling transaction that follows asset-for-share transactions.

In this ruling references to sections and paragraphs are to sections of the Income Tax Act and paragraphs of the Eighth Schedule thereto, applicable as at 13 April 2016. Unless the context indicates otherwise, any word or expression in this ruling bears the meaning ascribed to it in the Act.

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

- section 1(1) – definition of 'company', 'foreign company' and 'resident';
- section 9D;
- section 9H;
- section 42;
- section 46; and
- paragraph 12.

### Parties to the proposed transaction

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

The Co-Applicant: A public company incorporated in and a resident of South Africa and a wholly-owned subsidiary of the Applicant, to be listed pursuant to the proposed transaction

### Description of the proposed transaction

The Applicant intends to unbundle the shares in the Co-Applicant.

The steps to implement the proposed transaction are as follows:

- The Applicant will unbundle all the shares in the Co-Applicant to the Applicant's shareholders.
- The JSE Listing Requirements and specifically the 'standard rounding convention' will be applied to the proposed transaction, resulting in the

allocation of whole securities and no fractional entitlements.

- The Co-Applicant will be listed at the commencement of trade on the day following the last day to trade of the proposed transaction.
- The Applicant and the Co-Applicant will remain South African residents subsequent to the proposed transaction.

Prior to the proposed transaction, several asset-for-share transactions as referred to in section 42 and other unbundling transactions as referred to in section 46 are to take place in order to consolidate industry specific local and international businesses under the Co-Applicant. It is specifically noted that these transactions fall outside the scope of this binding private ruling.

#### Conditions and assumptions

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

#### Ruling

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

- If the asset-for-share transactions met the requirements of the definition of an 'asset-for-share transaction' in section 42(1) of the Act, section 42(5) and (6) will not apply to the disposal of equity shares in terms of the proposed transaction, as it is an unbundling transaction as referred to in section 46 of the Act and, therefore, specifically excluded from the ambit of section 42(5) and (6).
- The proposed transaction will not result in controlled foreign companies (CFCs) of the Co-Applicant and their subsidiaries ceasing to be CFCs for purposes of section 9D(1) and (2)(b) of the Act. Subsequent to the proposed transaction the Co-Applicant will remain a resident and will continue to hold the same interests in these specified companies.
- The proposed transaction will not result in a deemed disposal of the assets of specified CFCs at their market value for purposes of section 9H(3)(b)

and (d) of the Act as those companies that qualify as CFCs will not cease to be CFCs subsequent to the proposed transaction.

- The proposed transaction will not result in deemed disposals of assets by specified CFCs or their subsidiaries for purposes of paragraph 12 of the Eighth Schedule to the Act.

#### ***6.10. BPR 236 – Set-off of a loan account arising from an intra-group transaction to acquire equity shares***

This ruling determines the income tax consequences resulting from the acquisition of equity shares by setting-off a loan account, arising from an intra-group transaction, against the subscription price.

In this ruling references to sections and paragraphs are to sections of the Income Tax Act and paragraphs of the Eighth Schedule thereto applicable as at 14 April 2016. Unless the context indicates otherwise, any word or expression in this ruling bears the meaning ascribed to it in the Act.

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

- section 1(1) – definition of 'contributed tax capital';
- section 10(1)(k)(i);
- section 24J;
- section 41;
- section 45;
- section 55 – definition of 'donation';
- section 56;
- section 58;
- section 64D;
- section 64E;

- section 64FA;
- paragraph 11;
- paragraph 20;
- paragraph 35; and
- paragraph 75.

#### Parties to the proposed transaction

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

The Applicant: A company incorporated in and a resident of South Africa that is a wholly-owned subsidiary of Holdco

African Holdco: A company incorporated in and a resident of South Africa that is a wholly-owned subsidiary of Holdco

Foreign Holdco: A company incorporated outside South Africa and not a resident that is a wholly-owned subsidiary of African Holdco

Company Y: A company incorporated outside South Africa and not a resident

#### Description of the proposed transaction

Holdco, the Applicant, African Holdco, and Foreign Holdco are part of the same group of companies (the group). African Holdco was formed to be the holding company for the group's investments in Africa. Foreign Holdco and Company Y are residents of the same foreign country.

During 2015 the Applicant acquired 23% of the equity in Company Y. Subsequently Foreign Holdco acquired 37% of the equity in Company Y.

The Applicant intends to sell its 23% shareholding in Company Y to Foreign Holdco at a price equal to the base cost expenditure of the shares in Company Y, on loan account under an intra-group transaction as contemplated in section 45(1). The purchase price will remain outstanding on an interest-bearing loan account on commercial terms to be settled on demand within a maximum period of 30 days. The interest rate will be determined in terms of the group's transfer pricing policy with no provision to be made for the deferral of interest.

The group proposes to capitalise the loan obligation of Foreign Holdco into equity share capital through the following transaction steps:

- The Applicant will distribute the loan account to Holdco as a dividend *in specie*.
- Holdco will then subscribe for further ordinary shares in the capital of African Holdco for a subscription price equal to the face value of the loan account.
- The obligation of Holdco to pay the subscription price to African Holdco in terms of the subscription agreement will be discharged by the transfer of the loan account to African Holdco.
- African Holdco will in turn subscribe for further ordinary shares in the capital of Foreign Holdco for a subscription price equal to the face value of the loan account.
- The obligation of African Holdco to pay the subscription price to Foreign Holdco in terms of the subscription agreement will be discharged by way of set-off against the loan account, resulting in the loan account being extinguished.

#### Conditions and assumptions

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

#### Ruling

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

- In respect of the sale of the shares in Company Y by the Applicant to Foreign Holdco on loan account:
  - The transaction will be an 'intra-group transaction', as defined in paragraph (b) of that term in section 45(1).
  - The Applicant will be deemed to have disposed of the shares in Company Y for an amount equal to the base cost of those shares on

the date of the disposal, under section 45(2)(a)(i).

- The Applicant and African Holdco will, for purposes of determining any capital gain or capital loss in respect of the disposal of the shares in Company Y by African Holdco, be deemed under section 45(2)(a)(ii) to be one and the same person with respect to the date of acquisition of the shares in Company Y by the Applicant and the amount and the date of incurral by the Applicant of any expenditure in respect of the shares allowable in terms of paragraph 20 of the Eighth Schedule.
- Section 45(6)(d) will not apply to the disposal of shares to be distributed by the Applicant to Foreign Holdco.
- Section 45(3A) will not apply to the loan account.
- The sale of the shares in Company Y at a base cost value that is less than its market value will not constitute a 'donation' as defined in section 55(1), nor will it be deemed to be a donation under section 58.
- The loan account will, under section 24J(12), not fall within the ambit of section 24J, therefore, none of the parties to the transaction will be required to account for any accrual amount or adjusted gain or loss in respect of the transfer or redemption of the loan account.
- The distribution of the loan account by the Applicant to Holdco as a dividend *in specie* will:
  - not give rise to any capital gain in the Applicant;
  - be exempt from dividends tax under section 64FA(1)(b); and
  - be exempt from normal tax in Holdco under section 10(1)(k)(i).
- In respect of the subscription for further shares in African Holdco by Holdco for a subscription price equal to the face value of the loan account:
  - The further shares to be acquired by Holdco in African Holdco will

be treated, for purposes of paragraph 20 of the Eighth Schedule, as having been acquired by Holdco for an expenditure equal to the subscription price of the shares and will increase African Holdco's contributed tax capital by the same amount.

- The transfer of the loan account to African Holdco in setting-off against Holdco's obligation to pay the subscription price will not give rise to any capital gain in Holdco.
- In respect of the subscription for further shares in Foreign Holdco by African Holdco for a subscription price equal to the face value of the loan account:
  - The further shares to be acquired by African Holdco in Foreign Holdco will be treated, for purposes of paragraph 20 of the Eighth Schedule, as having been acquired by African Holdco for an expenditure equal to the subscription price of the shares and will increase Foreign Holdco's contributed tax capital by the same amount.
  - The set-off of the loan account against African Holdco's obligation to pay the subscription price will not give rise to any capital gain in African Holdco.

#### ***6.11. BPR 237 – Reinstatement of a deregistered company to transfer immovable properties***

This ruling determines that the re-instatement of a deregistered company in order to complete the transfer of immovable properties pursuant to an amalgamation transaction will not be a step taken to withdraw or invalidate the deregistration of

that company as envisaged in section 44(13) of the Act.

In this ruling references to sections are to sections of the relevant Acts applicable as at 24 February 2016. Unless the context indicates otherwise any word or expression in this ruling bears the meaning ascribed to it in the relevant Act.

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

- section 44(13) of the Income Tax Act;
- section 8(25) of the VAT Act; and
- section 9(1)(l)(iB) of the Transfer Duty Act.

#### Parties to the proposed transaction

The Applicant: A company incorporated in and a resident of South Africa with which Company A amalgamated in terms of an amalgamation transaction

Company A: A company incorporated in and a resident of South Africa and formally deregistered as a result of an amalgamation transaction entered into with the Applicant

#### Description of the proposed transaction

The parties wish to reinstate Company A after it was deregistered pursuant to an 'amalgamation transaction' as defined in section 44(1)(a) of the Act. The purpose of the reinstatement of Company A is to give effect to the transfer of immovable properties which was not previously attended to by the parties due to a *bona fide* error.

During 2013 Company A sold its entire business together with all its assets, including immovable properties, as a going-concern to the Applicant in terms of the amalgamation transaction.

As a necessary element of the amalgamation transaction, Company A was required to deregister. Company A was formally deregistered during 2014 by the Companies and Intellectual Properties Commission (CIPC).

The Deeds registry still reflects Company A as the owner of the immovable properties, notwithstanding the conclusion of the amalgamation transaction. The re-instatement of Company A will be subject to the completion of the following

steps:

- The Applicant will approach National Treasury and the Department of Public Works to ensure that there is no objection to the re-instatement of Company A, as any assets (including immovable property) of a de-registered company are forfeited to the state as *bona vacantia* at the time of deregistration.
- The Applicant will advertise its application to the CIPC for the re-instatement of Company A in a local newspaper (giving 21 days' notice for any third party objections to the re-instatement of Company A).
- Thereafter, the Applicant will apply for the re-instatement of Company A. The requirements for re-instatement in terms of the Companies Act No. 71 of 2008 are set out in the CIPC Practice Note No. 6 of 2012.

Once Company A has been re-instated the immovable properties will be transferred to the Applicant in terms of the existing sale of business agreement. Following completion of the conveyance of the immovable properties Company A will be deregistered.

#### Conditions and assumptions

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

#### Ruling

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

- The transfer of the immovable properties from Company A to the Applicant forms part of the amalgamation transaction already concluded in terms of section 44 of the Act and, accordingly, the 'rollover relief' set out in section 44 will continue to apply.
- Due to the circumstances under consideration the 36 month period allowed by section 44(13)(a) to complete the steps contemplated in section 41(4) to
- liquidate, wind up or deregister will be extended by 6 months ending on 31 December 2016.

- The reinstatement and subsequent deregistration of Company A will not be a step to invalidate or withdraw any of the steps to liquidate, wind up or deregister Company A as contemplated in section 44(13)(b) of the Act, as it will not result in Company A not being liquidated, wound up or deregistered.
- Section 8(25) of the VAT Act will continue to apply to the amalgamation transaction as the immovable properties were intended to be transferred from Company A to the Applicant pursuant to the amalgamation transaction.
- Section 9(1)(l)(iB) of the Transfer Duty Act will apply to the transfer of the immovable properties which were intended to be transferred from Company A to the Applicant pursuant to the amalgamation transaction.

#### ***6.12. BPR 238 – Taxation of receipts by or accruals to a programme of activities of a clean development mechanism project***

This ruling determines the taxability of receipts of a managing entity that manages a 'Clean Development Mechanism project' as defined in section 12K carried on under a programme of activities modality.

In this ruling references to sections are to sections of the Income Tax Act applicable as at 10 February 2016. Unless the context indicates otherwise any word or expression in this ruling bears the meaning ascribed to it in the Act.

This is a ruling on the interpretation and application of the provisions of section 1(1), the definition of 'gross income'.

##### Parties to the proposed transaction

The Applicant: A non-profit association of green energy producers

Project developer: Project developer and sponsor of the registration of the Clean Development Mechanism project (CDM project) with the Executive Board of the United Nations Framework Convention on Climate Change (UNFCCC)

CPA owners: Owners of the CDM projects registered under a programme of

activities

Description of the proposed transaction

The Applicant is a non-profit organisation established as a collaborative entity of concerned parties interested in raising awareness and facilitating the transition to a climate resilient society within South Africa. The Applicant achieves its objectives by:

- creating a platform for voluntary and mandatory carbon disclosure through the Kyoto Protocol Registry; and
- providing an independent platform for the hosting of programmes of activities for CDM projects registered under the Kyoto Protocol.

The Applicant acts as the coordinating and management entity for these programmes of activities.

The Applicant and the Project developer who is also a CPA owner have established a CDM project in a programmatic form, contemplated in Article 12 of the Kyoto Protocol.

The Kyoto Protocol is an international agreement under the UNFCCC. Its main feature is that it sets binding targets for 37 industrialised countries for reducing greenhouse gas emissions. In order to reach these targets the UNFCCC allows industrialised countries with emission-reduction commitments to meet part of their commitments by investing in projects in developing countries that reduce greenhouse gas emissions while contributing to the local sustainable development needs of the host country.

The CDM project is registered with the CDM executive board.

The CPA owners intend to produce carbon emission reduction credits under the programme of activities which will be sold to industrialised countries. The sale of carbon emission reduction credits is to be undertaken in terms of emission reduction purchase agreements.

The relationship between the parties will be governed by a programme of activities agreement with the following salient terms:

- The programme of activities is to be registered with the CDM executive

board together with the first CDM project undertaken by the Project developer. Other potential CPA owners who wish to participate in the programme of activities will be invited to do so upon payment of an inclusion fee and will be added by way of supplemental deeds of inclusion to the programme of activities in the manner provided for by the CDM rules.

- The Applicant will:
  - act as the coordinating and management entity for the programme of activities;
  - provide the framework and incentives for the CDM project activities to achieve greenhouse gas emission reductions;
  - enter into a programme of activities agreement with the CPA owners in order to regulate the rights, duties and obligations of the parties in relation to the development and operation of the programme of activities;
  - act as the point of contact with the CDM executive board on all matters pertaining to the programme of activities; and
  - develop a programme of activities design document setting out, amongst others, the eligibility criteria, concept, methodology and management aspects of the programme of activities.
- The object of the programme of activities will be to coordinate and implement several voluntary CDM project activities carried on by the CPA owners to generate carbon emission reduction credits for their individual benefit.
- The carbon emission reduction credits sales process will be managed by the Applicant and the revenue (carbon revenue) will be collected by it in its capacity as manager of the programme of activities on behalf of the CPA owners.
- The Project developer will fund the development phase budget to establish the programme of activities. All CPA owners will pay an annual fee to cover

expenses of the programme of activities.

- The carbon emission reduction credits generated by the programme of activities will be jointly owned by the Project developer and the other CPA owners on the following basis:
  - The carbon emission reduction credits of the programme of activities are generated by the carrying on and operation of the programme of activities by the CPA owners in collaboration with one another.
  - Ownership of a certain specified percentage of the gross carbon emission reduction credits will accrue to the Project developer as the project sponsor (project sponsor carbon emission reduction credit accrual) and the balance will be jointly owned by all CPA owners and will accrue individually to each CDM project of activities proportionally according to each ones contribution of carbon emission reduction credits in the relevant period.
- The Applicant will pay all the expenses related to the running of the programme of activities from the inclusion fees, annual fees and carbon revenue if required. The surplus will be distributed to the CPA owners according to their proportional share of revenue calculated based on the carbon emission reduction credits contributed in the relevant period.
- The Applicant will receive a fee for services rendered as manager of the programme of activities.

#### Conditions and assumptions

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

#### Ruling

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

- The proceeds from the sale of carbon emission reduction credits will accrue to the CPA owners.

- The inclusion fee and the annual fee to be received from the CPA owners and the funding to be received from the Project developer as the sponsor of the programme of activities for the development phase will be received by the Applicant as an agent on behalf of the CPA owners to defray the expenses of administering the programme of activities. Any surplus will therefore accrue to the CPA owners and will not be taxable in the Applicant.

### ***6.13. BPR 239 – Cash contributions made to a special purpose vehicle established to provide housing to mine workers***

This ruling determines the income tax consequences resulting from cash contributions to be made by the Applicant (as a party to a mining joint venture) to a special purpose vehicle established to provide housing for the employees of the joint venture and the group of companies of which the Applicant forms part (the group).

In this ruling references to sections and paragraphs are to sections of the Income Tax Act and paragraphs of the Eighth Schedule thereto applicable as at 4 May 2016. Unless the context indicates otherwise any word or expression in this ruling bears the meaning ascribed to it in the Act.

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

- section 1(1) – definition of 'gross income';
- section 15(a) read with section 36;
- section 36(11) – definition of 'capital expenditure' in particular paragraphs (d) and (e) of that term;
- paragraph 1 – definition of 'disposal';
- paragraph 3; and
- paragraph 11.

#### **Parties to the proposed transaction**

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

Co-Applicant: A mining company incorporated in and a resident of South Africa

Joint Venture (JV): A mining joint venture between the Applicant and the Co-Applicant

Propco: A company incorporated in and a resident of South Africa that is a wholly owned subsidiary of the Applicant

Description of the proposed transaction

The holder of a mining right is required under section 25(2)(f) of the Mineral and Petroleum Resources Development Act No. 28 of 2002 (MPRDA) to comply with the requirements of the prescribed social labour plan (SLP) in order to apply for and be granted a renewal of its mining right. It is also obliged to comply with the broad-based social-economic empowerment Charter, referred to in section 100 of the MPRDA. The Charter obliges mines to establish measures for improving the standard of housing (including the upgrading of hostels, conversion of hostels to family units and the promotion of home ownership options) for mine employees.

The JV has, in terms of its SLP, agreed to the implementation of a housing scheme for the benefit of the employees of the JV and the group.

Propco was established exclusively for purposes of the housing scheme. It obtained loan funding from a financial institution.

The funding agreement requires that the housing scheme is to be conducted in a legal entity separate to the JV participants and the entity is to be capitalised with a certain amount.

The JV proposes to fund Propco by way of a cash contribution that is neither a loan nor equity share capital. The funding agreement further provides for a restriction on the distributions that may be made to the shareholder of Propco. The board of directors of the Applicant's holding company resolved that any surplus cash and profits remaining in Propco after completion of the housing scheme and repayment of the loan should be utilised for social spending to further improve the lives of employees and the communities where the group conducts mining operations.

The memorandum of incorporation of Propco therefore specifically provides that:

- Upon completion of the housing projects undertaken by Propco, as set out

in the group's housing policy or prior to any voluntary liquidation proceedings which may be undertaken by Propco, all surplus cash and profits shall be applied to one or more programmes that have as its/their object the improvement of the social conditions of the communities in or around the area in which the Applicant carries on its business.

- Propco shall not be entitled to undertake voluntary liquidation proceedings without having first applied all surplus cash and profits of Propco as set out above.

#### Conditions and assumptions

This binding private ruling is made subject to the additional condition and assumption that the clauses in the memorandum of incorporation of Propco relating to the utilisation of surplus cash and profit are strictly adhered to.

#### Ruling

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

- The cash contribution to be made by the JV to Propco for purposes of the housing scheme will qualify as 'capital expenditure', as defined in paragraph (e) of the definition of that term in section 36(11), for each member of the JV, to the extent that the cash contribution relates to housing for persons employed by the JV. Any part of the cash contribution that relates to housing for persons not employed by the JV will not be deductible and an apportionment of the expenditure must be made.
- The cash contribution will not result in a disposal of an asset by any member of the JV. Consequently, the cash contribution will not give rise to a capital gain contemplated in paragraph 3 of the Eighth Schedule.
- The cash contribution to be received by Propco will constitute a receipt of a capital nature and will not constitute 'gross income', as defined in section 1(1).
- The receipt of the above cash contribution from the JV will not give rise to a capital gain contemplated in paragraph 3 of the Eighth Schedule.

Accordingly, no inclusion of a taxable capital gain will be made in the taxable income of Propco under section 26A.

#### **6.14. BPR 240 – Taxation of parties to share index linked notes**

This ruling determines the income tax consequences resulting from the issue of notes that provide a return determined with reference to a share index, issued by a special purpose vehicle to its holding company that is an insurer.

In this ruling references to sections are to sections of the Income Tax Act applicable as at 10 May 2016. Unless the context indicates otherwise any word or expression in this ruling bears the meaning ascribed to it in the Act.

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

- section 1(1) – definition of 'gross income';
- section 8(4)(a);
- section 11(a) read with section 23(g);
- section 23H;
- section 24C;
- section 24J;
- section 24L;
- section 24M; and
- Part VI of the Eighth Schedule.

##### Parties to the proposed transaction

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

Co-Applicant: A company incorporated in and a resident of South Africa whose shares are wholly owned by the Applicant

##### Description of the proposed transaction

The Applicant carries on the business of a registered long-term insurer and is registered as such under the Long-Term Insurance Act No. 52 of 1988. The Applicant wishes to provide its policyholders with a zero tracking error investment which tracks a specified share index.

The Applicant proposes to enter into transactions with the Co-Applicant in terms of which the Co-Applicant will issue notes to the Applicant that will track a specified share index.

The Co-Applicant's business will be to carry on hedging and other speculative transactions in order to enable it to perform its obligations under the note.

The Applicant will be the holder of the note, and the Co-Applicant will be the issuer of the note. The Co-Applicant will use the subscription proceeds (subscription amount) to enter into various hedging activities in order to enable it to pay the relevant return to the Applicant on the redemption date concerned. In this regard, the note will provide for an obligation undertaken by the issuer to provide exposure to a specified index with a zero tracking error. The Applicant will be exposed to the specified index for the duration of the term of the note.

Additional terms of the note will be as follows:

- The underlying reference asset of the note will be either the SATRIX 40 or another similar index and will not include any bonds or other similar instruments.
- The note will be issued for an indefinite term, subject to a minimum of 5 years. Only in exceptional circumstances would it be possible to redeem the note prior to the initial 5 year period.
- The note will be redeemable at the option of the Applicant.
- The note will be redeemed for an amount determined with reference to the performance of the relevant index.
- The Applicant will not be entitled to any distributions in respect of the note during the term of the note.

- The Co-Applicant will bear all risk pertaining to the ability to provide a zero tracking error to the Applicant in respect of the reference index. To the extent that it is not able to do so, the Co-Applicant will be liable for the loss. Equally, any profit from over-performing in relation to the index will be retained and will be subject to tax.

#### Conditions and assumptions

This binding private ruling is made subject to the additional condition and assumption that the Co-Applicant will carry on a trade.

#### Ruling

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

- The subscription amount for the note must be included in the 'gross income', as defined in section 1(1), of the Co-Applicant in the year of assessment in which the note is issued.
- The amount payable by the Co-Applicant to the Applicant on the redemption of the note will be deductible from the income of the Co-Applicant under section 11(a) read with section 23(g). The deduction, based on a reasonable estimate of the amount payable in the future (estimated redemption amount), will be allowed in the year of assessment in which the note is issued.
- Any estimated redemption amount so deducted that exceeds the actual redemption amount payable at the date of redemption will be recouped in the Co-Applicant under section 8(4)(a) in the year of assessment in which the note is redeemed.
- If the amount payable at the date of redemption exceeds the estimated redemption amount deducted a further deduction will be allowed under section 11(a) read with section 23(g) in the year of assessment in which the note is redeemed.
- No further deduction under section 11(a) or inclusion in gross income under section 8(4)(a) in respect of the change in the value of the estimated

redemption amount of the note may be made in the years of assessment between the year of assessment in which the note was issued and the year of assessment in which the note is redeemed.

- The note will not constitute an 'instrument', as defined in section 24J(1).
- Sections 23H, 24C, 24L and 24M will not apply to the note.
- The subscription amount paid by the Applicant for the note will be regarded as expenditure incurred on the acquisition of a capital asset in respect of the Applicant's policy holder business. The subscription amount paid will therefore not be deductible under section 11(a). Further, the receipt on redemption of the note must be treated as proceeds on disposal of a capital asset under Part VI of the Eighth Schedule to the Act.

#### **6.15. BPR 241 – Award received for a black economic empowerment (BEE) training initiative**

This ruling determines the income tax and capital gains tax consequences for the recipient of an award of participation units in a trust received in pursuance of a BEE training initiative and its entitlement to claim a section 24C allowance against the award.

In this ruling references to sections and paragraphs are to sections of the Income Tax Act and paragraphs of the Eighth Schedule thereto applicable as at 26 January 2016. Unless the context indicates otherwise any word or expression in this ruling bears the meaning ascribed to it in the Act.

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

- section 1(1) – definition of 'gross income';
- section 10(1)(k);
- section 24C;

- section 25B;
- paragraph 11(1)(d);
- paragraph 13(1)(a)(iiA);
- paragraph 38;
- paragraph 75; and
- paragraph 80(1).

#### Parties to the proposed transaction

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

Trust A: A trust established in and a resident of South Africa of which the Applicant is a beneficiary

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

SPV Co: A private company incorporated in and a resident of South Africa

BEE Co: A private company incorporated in and a resident of South Africa that is the majority shareholder of the Applicant

Company B: A public company incorporated in and a resident of South Africa within the same group of companies as Company A

#### Description of the proposed transaction

Company A implemented a BEE initiative. For this purpose SPV Co was incorporated. SPV Co acquired 10% of the issued ordinary shares (shares) of Company A at market value. The acquisition of the shares was funded by third party funding. The funding was to be repaid from dividends received by SPV Co from the shares and the proceeds from the disposal of some or all of the shares.

Upon settlement of the funding SPV Co is required to distribute the remaining shares, if any, as a dividend *in specie* to its shareholders.

Three trusts with specific BEE aims were established as the shareholders of SPV Co. Trust A holds 49% of the ordinary shares in SPV Co. Trust A was established to facilitate the participation of qualifying business partners of Company A

(business partners) in the BEE initiative.

In terms of the deed of Trust A (the deed):

- A number of units were created, conferring on their holders *pro rata* entitlements to participate in the net assets of Trust A (trust fund).
- The trustees are obliged to make an *in specie* distribution of the trust fund.
- The trust fund vests in the holders of the units on the same date on which SPV Co distributes the remaining shares to Trust A and the other shareholders (distribution date).

BEE Co and Company B incorporated the Applicant for the purpose of recruiting, appointing and training individuals to become economically independent (training initiative).

The Applicant received an award of units from Trust A. The award was made unconditional, free of charge and subject to the terms and conditions of the deed and it entitles the Applicant to participate in the trust fund.

The memorandum of incorporation of the Applicant and the shareholders agreement entered into by the Applicant's shareholders limit the activities of the Applicant to that of conducting the training initiative and provide that the benefits available from participation in the trust fund are used only for this purpose.

The Applicant will not operate to generate any profit or earn any income for its shareholders. Any subsequent amounts generated through its operations must be used in full for the training initiative.

SPV Co settled its funding obligation and subsequently made an *in specie* distribution of the remaining shares to its shareholders.

In accordance with the terms of the deed a number of the shares proportionate to the Applicant's unit-holding vested in the Applicant on the distribution date.

The Applicant's operational activities will be funded by the benefits accruing to it pursuant to the receipt of the *in specie* distribution of the shares. The Applicant will dispose of a sufficient number of shares annually to fund its operations.

Until such time as the Applicant is in a position to dispose of some of the shares its

shareholders or a company within the group will provide bridging finance to the Applicant. This financing will be settled by the Applicant from the proceeds realised from the disposal of the shares.

#### Conditions and assumptions

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

#### Ruling

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

- The award of the Units gives rise to an amount that must be included in the gross income of the Applicant.
- The Applicant will qualify for an allowance in respect of future expenditure under section 24C against the amount referred to in a) to be included in gross income. The amount of the allowance in each year of assessment remains subject to the discretion of SARS.
- The shares to be distributed to the Applicant and any surplus cash vesting in the Applicant will constitute income in the form of a dividend *in specie*, which will be regarded as having accrued to the Applicant under section 25B(1). The shares and surplus cash will retain their nature as a dividend. The market value of the shares and the cash distribution must be included in the gross income of the Applicant in the year of assessment in which the distribution is made.
- The shares and any surplus cash vesting in the Applicant as a dividend *in specie* will be exempt under section 10(1)(k).
- Trust A will be deemed to have acquired the shares distributed to it by SPV Co (and which include the Applicant's shares) on the distribution date for an expenditure equal to the market value of those shares on that date, for purposes of paragraph 75(1)(b). The expenditure must be treated as an amount actually incurred for the purposes of paragraph 20(1)(a).

- Trust A must be treated as having disposed of the shares to the Applicant immediately upon receipt of those shares as a dividend *in specie*, for purposes of paragraph 11(1)(d), read with paragraph 13(a)(iiA).
- Paragraph 38 will apply to the vesting and resultant disposal of the shares. Therefore Trust A will be deemed to have disposed of the shares for proceeds equal to the market value of those shares on the distribution date and the Applicant will be deemed to have acquired the shares for a cost equal to the market value of those shares on the distribution date.
- No capital gain will arise or be attributed to the Applicant for purposes of paragraph 80(1) on the basis that the shares will be treated as having been acquired at their market value and simultaneously treated as having been disposed of by Trust A at their market value.
- The cancellation of the units following the distribution of the shares and any surplus cash will not give rise to any capital gains tax in the Applicant.

#### **6.16. BPR 242 – Venture capital company investment in qualifying companies carrying on business as hotelkeepers**

This ruling determines:

- the meaning of 'controlled group company' and 'equity share' with reference to companies that propose to issue different classes of ordinary shares;
- the application of section 12J(6A)(b)(ii) in relation to the granting of an option to purchase additional assets once qualifying shares have been issued to the venture capital company and the subsequent exercising of the option; and
- the meaning of 'hotel keeper' and the allowances that a hotel keeper may claim.

In this ruling references to sections are to sections of the Income Tax Act as at 17 May 2016. Unless the context indicates otherwise any word or expression in this

ruling bears the meaning ascribed to it in the Act.

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

- section 1(1) – definition of 'controlled group company', 'equity share' and 'hotel keeper';
- section 11(e);
- section 12C(1)(d);
- section 12J(1) – definition of 'qualifying company' and 'qualifying share'; and
- section 12J(6A)(b)(ii).

Parties to the proposed transaction

The Applicant: A company incorporated in and a resident of South Africa that has been approved as a 'venture capital company' as defined in section 12J(1)

Co-Applicant 1: A company incorporated in and a resident of South Africa

Co-Applicant 2: A company incorporated in and a resident of South Africa

Co-Investor: A company incorporated in South Africa

Description of the proposed transaction

The Applicant intends to invest in qualifying companies that will carry on the business of hotel keepers.

The Co-Applicants intend to carry on the business of hotel keepers. They will each appoint a company (manager) to operate and manage their respective hotels. The manager will guarantee each of them a certain level of earnings before interest, tax, depreciation and amortisation (the guaranteed EBITDA) per annum.

The Applicant intends to exit this investment on or before the fifth anniversary of the investment. The Co-Applicants will endeavour to sell their respective hotels with the intention to distribute the proceeds to their shareholders.

The steps to implement the proposed transaction are as follows:

- Transaction 1

- The Applicant will subscribe for A class ordinary shares and the Co-Investor will subscribe for B class ordinary shares in Co-Applicant 1. The total subscription proceeds will be less than R50 million. The Applicant will always hold less than 70% of the total number of shares in issue in Co-Applicant 1 but will contribute more than its proportionate share in monetary terms to the share capital of Co-Applicant 1.
- The A and B class shares will carry the following distribution rights:
  - The A class shares will be entitled to a profit distribution on an annual basis in an amount equal to the guaranteed EBITDA, less any third party debt payments.
  - The B class shares will be entitled to a distribution of the remaining profits on an annual basis.
  - On exit, the holders of the A and B class shares will be entitled to a return of capital distribution of their respective amounts contributed together with a cumulative compound annual return linked to prime, with the A class shares ranking ahead of the B class shares. The A and B class shares will then participate in the remaining assets of Co-Applicant 1 on a *pari passu* basis, *pro rata* to their number of shares held. The B class shares may receive, as a distribution *in specie*, the common areas in lieu of the cash distribution.
- Co-Applicant 1 will use the subscription proceeds to acquire in cash from a seller hotel rooms held under sectional title in an existing hotel (first tranche) together with their undivided shares in various common areas, including the reception area, the restaurant, canteen and parking areas as a going concern for a purchase price equal to the subscription proceeds.
- The seller will grant Co-Applicant 1 an option to acquire additional sectional title units in the hotel (second tranche) which acquisition

will be funded by third party debt. The option will be granted at no charge and will be exercisable for a period of four months from the signature date of the sale of the first tranche. The purpose of the option is to allow the third party financier sufficient time to evaluate the performance and trading results of the business of Co-Applicant 1 before agreeing to advance a loan to Co-Applicant 1 to fund the acquisition of the second tranche. The aggregate cost of the sectional title units in the first tranche and the second tranche will exceed R50 million.

- The seller will cede and assign its rights and obligations under a hotel management agreement to Co-Applicant 1 in terms of which the manager has been appointed as agent and exclusive operator of the hotel from which sectional title units will be acquired by Co-Applicant 1. The manager will control and manage the sectional title units as a hotel business in exchange for a management fee. Guests who use the sectional title units will have the same access to all the hotel's facilities, including the restaurant, as any other guest who might occupy a room owned by the seller.
- Transaction 2
  - The Applicant will subscribe for A class ordinary shares and the Co-Investor will subscribe for B class ordinary shares in Co-Applicant 2. The total subscription proceeds will be less than R50 million. The Applicant will always hold less than 70% of the issued shares in Co-Applicant 2 but will contribute more than its proportionate share in monetary terms to the share capital of Co-Applicant 2.
  - The A and B class shares will carry the same distribution rights as the A and B class shares under transaction 1 save that on exit, the B class shares will not be entitled to receive, as a distribution *in specie*, the common areas in lieu of the cash distribution.
  - Co-Applicant 2 will use the subscription proceeds to acquire in cash newly developed rooms to be held under sectional title in a hotel from a property developer, together with the sectional title units'

undivided shares in various common areas including the reception area and the parking areas for a purchase price equal to the subscription proceeds. Co-Applicant 2 will be granted the right of use of the remaining common areas including the restaurant area, canteen and gym.

- Co-Applicant 2 will enter into a hotel management agreement with the manager in terms of which the manager will be appointed as agent and exclusive operator of the hotel from which Co-Applicant 2 will acquire sectional title units. The manager will control and manage the sectional title units as a hotel business and will be paid a management fee. Guests who use the sectional title units will have the same access to all the hotel's facilities, including the restaurant.

#### Conditions and assumptions

This binding private ruling is subject to the additional condition and assumption that the asset book values of each of the Co-Applicants do not exceed R50 million immediately after the issue to each of them of qualifying shares.

#### Ruling

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

- For purposes of the definition of 'qualifying share' in section 12J(1), each share of the Co-Applicants will constitute an 'equity share' as defined in section 1(1).
- For purposes of the definition of 'qualifying company' in section 12J(1), neither of the Co-Applicants will constitute a 'controlled group company' for so long as the number of equity shares to be held by the Applicant in each of them will constitute less than 70% of the total number of equity shares, irrespective of the fact that the Applicant may invest more than 70% of the aggregate share capital in each of the Co-Applicants in monetary terms.
- The existence of the option granted to Co-Applicant 1 to acquire additional sectional title units will not constitute non-compliance with section 12J(6A)(b)(ii) nor will the exercise of the option immediately after the

acquisition of the first tranche of sectional title units constitute non-compliance with section 12J(6A)(b)(ii).

- The Co-Applicants will each carry on the business of an 'hotel keeper' as defined in section 1(1) through the agency of the manager.
- The Co-Applicants will be eligible to claim allowances in respect of assets that will be used by them in their businesses under section 12C(1)(d) or 11(e), as specified in an annexure to the ruling letter, which is not published herewith.

## **7. BINDING CLASS RULING**

### ***7.1. BCR 52 – Income tax and securities tax consequences for the shareholders of a listed company following an unbundling transaction***

This ruling determines the tax consequences for resident and non-resident shareholders of a listed company in terms of an unbundling transaction in relation to the shares of the Co-Applicant company.

In this ruling references to sections and paragraphs are to sections of the relevant Act and paragraphs of the Eighth Schedule to the Income Tax Act applicable as at 11 April 2016. Unless the context indicates otherwise, any word or expression in this ruling bears the meaning ascribed to it in the relevant Act.

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

- the Income Tax Act:
  - section 46; and
  - paragraph 76B.
- the STT Act:
  - section 8(1)(a)(iv).

#### **Class**

The class members to whom this ruling will apply are the resident and non-resident shareholders of the Applicant on the last day to trade for shareholders to participate in the proposed transaction.

Parties to the proposed transaction

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

The Co-Applicant: A public company incorporated in and a resident of South Africa and a wholly-owned subsidiary of the Applicant to be listed as part of the proposed transaction

Class members: The shareholders

Description of the proposed transaction

The Applicant intends to unbundle the shares in the Co-Applicant.

The steps to implement the proposed transaction are as follows:

- The Applicant will unbundle all the shares in the Co-Applicant to the Class members.
- The JSE Listing Requirements and specifically the 'standard rounding convention' will be applied to the unbundling transaction, resulting in the allocation of whole securities and no fractional entitlements.
- The Co-Applicant will be listed at the commencement of trade on the day following the last day to trade (LDT+1) for shareholders to participate in the unbundling.
- The Applicant and the Co-applicant will remain South African residents subsequent to the unbundling transaction.

It is intended that immediately prior to the unbundling transaction the separately identifiable and industry specific local and international businesses will be housed under the Co-applicant, in several sub-groups.

As at 31 December 2015, more than 50% of the shareholders of the Applicant were non-residents for tax purposes.

Conditions and assumptions

This binding class ruling is subject to the following additional condition:

- The shares in the Co-Applicant are to be listed at the commencement of trade on LDT+1 in relation to the unbundling transaction.

#### Ruling

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

- The distribution of the shares in the Co-Applicant to the Class members will constitute an 'unbundling transaction', as defined in paragraph (a) of the definition of that term in section 46(1) of the Act.
- The unbundling of the equity shares in the Co-Applicant will be effected in terms of paragraph (a) of the definition of an 'unbundling transaction' in section 46(1) of the Act, notwithstanding the fact that the 'standard rounding convention' prescribed by the JSE Listings Requirements will be applied to the allocation of securities.
- Provided that no Class member that is a disqualified person, either alone or together with a connected person(s) in relation to that Class member, that is or are a disqualified person(s) holds more than 20% of the shares in the Co-Applicant, section 46(7) will not apply to the unbundling transaction.
- In the light of the particular circumstances of this unbundling transaction, for the purposes of section 46(3)(a)(v) of the Act and with reference to the market values of the unbundling shares (Applicant's shares) and unbundled shares (Co-Applicant's shares), 'as at the end of the day after that distribution' means in relation to the shares unbundled under section 46 of the Act by the Applicant:
  - the closing price of the unbundling shares (Applicant's shares) on LDT+1; and
  - the closing price of the unbundled shares (Co-Applicant's shares) on LDT+1.

Therefore, each Class member must allocate a portion of the expenditure and any market value attributable to the equity shares held in the Applicant

to the unbundled shares in the Co-Applicant. The proportionate amount of the expenditure and market value to be allocated to the unbundled shares in the Co-Applicant must be determined in accordance with the ratio that the market value of these shares in the Co-Applicant, using the closing price on LDT+1, bears to the sum of the market value, using the closing price on LDT+1, of the Applicant's shares and of the unbundled shares in the Co-Applicant.

Each Class member must also reduce the expenditure and market value attributable to the Applicant's shares by the amount so allocated to the unbundled shares in the Co-Applicant.

- The distribution of equity shares in terms of the unbundling transaction by the Applicant will be disregarded in determining any liability for dividends tax.
- Paragraph 76B of the Eighth Schedule to the Act will not apply to the unbundling transaction.
- The transfer of the equity shares in the Co-Applicant to the Class members will be exempt from securities transfer tax under section 8(1)(a)(iv) of the STT Act, as the unbundling transaction will be an unbundling transaction as referred to in section 46 of the Act.

## ***7.2. BCR 53 – Programme of activities of a clean development mechanism project***

This ruling determines the tax consequences for the participants in a 'Clean Development Mechanism project', as defined in section 12K of the Act, carried on under a programme of activities modality.

In this ruling references to sections are to sections of the relevant Acts applicable as at 10 February 2016. Unless the context indicates otherwise any word or expression in this ruling bears the meaning ascribed to it in the relevant Act.

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

- the Income Tax Act:
  - section 12K; and
  - section 22.
- the VAT Act:
  - section 11(2)(f).

#### Class

The class members to whom this ruling will apply will be the participants referred to as CPA owners, registered under a programme of activities.

#### Parties to the proposed transaction

The Applicant: A non-profit association of green energy producers

Project developer: Project developer and sponsor of the registration of the Clean Development Mechanism project (CDM project) with the Executive Board of the United Nations Framework Convention on Climate Change (UNFCCC)

CPA owners: Owners of the CDM projects registered under the programme of activities

#### Description of the proposed transaction

The Applicant is a non-profit organisation established as a collaborative entity of concerned parties interested in raising awareness and facilitating the transition to a climate resilient society within South Africa. The Applicant achieves its objectives by:

- creating a platform for voluntary and mandatory carbon disclosure through the Kyoto Protocol Registry; and
- providing an independent platform for the hosting of programmes of activities for CDM projects registered under the Kyoto Protocol.

The Applicant acts as the coordinating and management entity for these programmes of activities.

The Applicant and the Project developer who is also a CPA owner have established a CDM project in a programmatic form, contemplated in Article 12 of

the Kyoto Protocol.

The Kyoto Protocol is an international agreement under the UNFCCC. Its main feature is that it sets binding targets for 37 industrialised countries for reducing greenhouse gas emissions. In order to reach these targets the UNFCCC allows industrialised countries with emission-reduction commitments to meet part of their commitments by investing in projects in developing countries that reduce greenhouse gas emissions while contributing to the local sustainable development needs of the host country.

The CDM project is registered with the CDM executive board.

The CPA owners intend to produce carbon emission reduction credits under the programme of activities which will be sold to industrialised countries. The sale of carbon emission reduction credits is to be undertaken in terms of emission reduction purchase agreements.

The relationship between the parties will be governed by a programme of activities agreement with the following salient terms:

- The programme of activities is to be registered with the CDM executive board together with the first CDM project undertaken by the Project developer. Other potential CPA owners who wish to participate in the programme of activities will be invited to do so upon payment of an inclusion fee and will be added by way of supplemental deeds of inclusion to the programme of activities in the manner provided for by the CDM rules.
- The Applicant will
  - act as the coordinating and management entity for the programme of activities;
  - provide the framework and incentives for the CDM project activities to achieve greenhouse gas emission reductions;
  - enter into a programme of activities agreement with the CPA owners in order to regulate the rights, duties and obligations of the parties in relation to the development and operation of the programme of activities;

- act as the point of contact with the CDM executive board on all matters pertaining to the programme of activities; and
  - develop a programme of activities design document setting out, amongst others, the eligibility criteria, concept, methodology and management aspects of the programme of activities.
- The object of the programme of activities will be to coordinate and implement several voluntary CDM project activities carried on by the CPA owners to generate carbon emission reduction credits for their individual benefit.
- The carbon emission reduction credits sales process will be managed by the Applicant and the revenue (carbon revenue) will be collected by it in its capacity as manager of the programme of activities on behalf of the CPA owners .
- The Project developer will fund the development phase budget to establish the programme of activities. All CPA owners will pay an annual fee to cover expenses of the programme of activities.
- The carbon emission reduction credits generated by the programme of activities will be jointly owned by the Project developer and the other CPA owners on the following basis: i) The carbon emission reduction credits of the programme of activities are generated by the carrying on and operation of the programme of activities by the CPA owners in collaboration with one another.
- Ownership of a certain specified percentage of the gross carbon emission reduction credits will accrue to the Project developer as the project sponsor (project sponsor carbon emission reduction credit accrual) and the balance will be jointly owned by all CPA owners and will accrue individually to each CDM program of activities proportionally according to each ones contribution of carbon emission reduction credits in the relevant period.
- The Applicant will pay all the expenses related to the running of the programme of activities from the inclusion fees, annual fees and carbon revenue if required. The surplus will be distributed to the CPA owners

according to their proportional share of revenue calculated based on the carbon emission reduction credits contributed in the relevant period.

- The Applicant will receive a fee for services rendered as manager of the programme of activities.

#### Conditions and assumptions

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

#### Ruling

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

- The programme of activities will be a qualifying 'Clean Development Mechanism project' as defined in section 12K(1) of the Act.
- The CPA owners and the first CDM project owner will be the persons carrying on the 'qualifying CDM project' as defined in section 12K(1).
- The proceeds from the disposal of the carbon emission reduction credits (carbon revenue) generated by the programme of activities will be exempt from income tax under section 12K(2) of the Act in the hands of the CPA owners. The exemption is not affected by virtue of the fact that the carbon revenue will be received by the Applicant acting in its capacity as manager of the programme of activities.
- Only carbon revenue from the carbon emission reduction credits that the first CDM project owner derives from conducting its own CDM project of activities will qualify for exemption under section 12K(2) of the Act. Consequently, the carbon revenue from the disposal of the extra carbon emission reduction credits accrued in terms of the programme of activities agreement will not be exempt from normal tax under section 12K(2) of the Act.
- The carbon emission reduction credits need not be accounted for as 'trading stock' as defined in section 1(1) of the Act.
- The sale of carbon emission reduction credits to non-resident purchasers will be subject to VAT at a zero rate under section 11(2)(l) of the VAT Act,

provided all the requirements of that section are complied with.

## **8. BINDING GENERAL RULING**

### **8.1. *BGR 32 – VAT treatment of specific supplies in the short-term reinsurance industry***

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

- 'bordereau' means a document issued by a cedent, intermediary or reinsurer in the form of a memorandum, statement or invoice which contains detailed information such as:
  - reinsurance premiums collected;
  - claims paid; and
  - fees and commission payable in respect of intermediary services supplied;
- 'cedent' means the short-term insurer that reinsures part, or all, of its claims risk associated with insurance policies held;
- 'cedent commission' means the amount paid or payable by a reinsurer to the cedent in terms of a reinsurance contract;
- 'claims risk' means the risk of the cedent incurring a loss as a result of paying a claim submitted by its client under a policy of insurance;
- 'facultative reinsurance' means the reinsurance of a single risk or a defined package of risks which are individually underwritten by the reinsurer;
- 'indemnity payment' means a cash payment made under a contract of reinsurance by the reinsurer to the cedent to indemnify the cedent in respect of a reinsured claims risk;
- 'intermediary' means the reinsurance broker who serves as agent of the reinsurer to facilitate reinsurance contracts;
- 'intermediary services' has the meaning assigned thereto in section 1 of the Financial Advisory and Intermediary Service Act No. 37 of 2002 and includes the management and administration of a policy as well as the

collection of premiums and processing of claims on behalf of the cedent or reinsurer;

- 'inward reinsurance' means the acceptance of any reinsurance risk by a South African reinsurer under a contract with a non-resident cedent;
- 'local reinsurance' means reinsurance services supplied by a South African reinsurer to a South African cedent;
- 'non-proportional treaty reinsurance' is also known as excess reinsurance and involves the reinsurer bearing risk once the cedent's loss exceeds an agreed threshold;
- 'proportional treaty reinsurance' is treaty reinsurance which involves the proportional sharing of risk;
- 'recoveries' means any amount paid or payable by a cedent to a reinsurer, in accordance with a reinsurance contract, through the exercising of the cedent's right of subrogation or the sale of salvaged insured goods;
- 'reinsurance' means short-term insurance in terms of which the cedent reinsures part, or all, of its claims risk associated with insurance policy documents with a reinsurer. For purposes of this BGR, reinsurance includes retrocession, facultative and treaty reinsurance;
- 'reinsurance contract' means a document which is evidence of a contract of reinsurance, including any renewal notice, premium notification, slip, certificate or endorsement in respect thereof;
- 'reinsurance premium' means the consideration paid or payable by the cedent to the reinsurer in respect of a supply of reinsurance service;
- 'reinsurer' means the person that supplies short-term reinsurance to a cedent under a reinsurance contract;
- 'retrocession' means an agreement in terms of which a reinsurer transfers reinsured risks to another reinsurer;
- 'section' means a section of the VAT Act;
- 'treaty reinsurance' means reinsurance provided under a pre-negotiated

agreement between the cedent and the reinsurer in terms of which the cedent agrees to cede all risks within a defined class or classes to the reinsurer and, in return, the reinsurer agrees to provide reinsurance on all risks ceded without individual underwriting.

This BGR deals with the following:

- Taxable supplies made by reinsurers, cedents and intermediaries.
- Reinsurance claims and recoveries.
- The time of supply in relation to the supply of short-term reinsurance, intermediary services and cedent services.
- Information to be reflected on a tax invoice, debit and credit note as contemplated in sections 20(7) and 21(5) respectively, in respect of the supply of short-term reinsurance, cedent services and the related intermediary services.
- Approval to issue recipient-created tax invoices, debit and credit notes.

It is recommended that this BGR is read in conjunction with the *VAT 421 – Guide for Short-Term Insurance*.

#### Ruling

##### Reinsurance premiums

The taxable supply of reinsurance by a local reinsurer to a non-resident cedent is subject to VAT at the zero rate under section 11(2)(l).

##### Cedent commission

The supply of cedent services to a non-resident reinsurer may be zero-rated under section 11(2)(l), provided the requirements of that section are met.

##### Indemnity payments

A reinsurer's deduction in respect of indemnity payments under section 16(3)(c), must be reduced by the tax fraction of any recoveries received

from the South African cedent during that tax period.

A cedent's output tax liability in respect of indemnity payments received during a tax period is determined by applying the tax fraction to the total value of indemnity payments received during the tax period less any recoveries paid to a VAT-registered reinsurer during that tax period.

#### Recoveries

A reinsurer is not liable to account for output tax on recoveries received to the extent the amount is offset against indemnity payments made by the.

The cedent may not deduct the tax fraction of recovered amounts paid to a reinsurer to the extent this amount is offset against indemnity payments received.

#### Time of supply

##### Supply of short-term reinsurance

The reinsurance contract or any other document disclosing the premium amount without imposing an obligation to make payment is not regarded as an invoice.

Facultative and non-proportional treaty reinsurance:

Facultative and non-proportional treaty reinsurance are deemed, under section 9(1), to be supplied at the earlier of the time a bordereau is issued or consideration is received in respect of that supply, unless the reinsurance contract requires the premiums to be paid periodically. In this instance, the reinsurance services are, under section 9(3)(a), deemed to be successively supplied when (and to the extent) that the premiums become due or are received, whichever is earlier.

Proportional treaty reinsurance:

The time of supply in respect of the supply of proportional treaty reinsurance is, under section 9(4)(b), when and to the extent that any payment in terms of the reinsurance contract is due or is received, or the bordereau relating to that supply is issued by the

supplier or the recipient, whichever is earliest.

Supply of intermediary or cedent services

The supply of intermediary and cedent services is deemed to take place, under section 9(1), at the earlier of the time payment is received or an invoice (including a bordereau) is issued in respect of that service.

Tax invoices, credit and debit notes

The Commissioner directs under sections 20(7)(a) and 21(5)(a), that the document (generally known as a bordereau) issued by the reinsurer, cedent or intermediary in respect of the supply of reinsurance, intermediary and cedent services does not have to contain the words 'tax invoice', 'VAT invoice', 'invoice', 'credit note' or 'debit note', as the case may be, provided the document reflects all the other information as required by section 20(4) or 21(3).

In the case of local reinsurance, the bordereau must contain the following statement (or substantially similar wording) confirming the Commissioner's direction under section 20(7) and 21(5), as the case may be:

'In terms of Binding General Ruling No. 32 this document constitutes a tax invoice, debit note or credit note as contemplated in sections 20(7)(a) and 21(5)(a) of the VAT Act respectively.'

Intermediaries are, under section 20(1), required to issue tax invoices in respect of any other taxable supplies made to their clients, unless these supplies are reflected in the relevant bordereau.

Recipient-created tax invoices, credit and debit notes

Reinsurers, intermediaries, reinsurance brokers and cedents that are required to determine the consideration payable in respect of reinsurance, intermediary or cedent services may, under sections 20(2) and, where applicable, 21(4), issue recipient-created tax invoices, credit and debit notes. This decision is on condition that the recipient of the services complies with the requirements of Interpretation Note No. 56 'Recipient-

Created Tax Invoices, Credit and Debit Notes' and that the bordereau contains the information stipulated above.

Conditions

Zero rating

The zero rating of supplies contained in this BGR is conditional upon the reinsurer, cedent or intermediary (as applicable) obtaining and retaining the documentary proof as provided for under section 11(3) read with Interpretation Note No. 31 'Documentary Proof Required for the Zero-Rating of Goods and Services' (Interpretation Note No.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 No.31.

Input tax and other deductions

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) by the time the relevant VAT return is submitted. Failure to obtain and retain the required documentary proof will result in the vendor not being entitled to the deduction.

## **8.2. *BGR 33 – The Value-Added Tax treatment of the supply and importation of vegetable oil***

For the purpose of this ruling:

- 'cooking' means to prepare food for eating with the application of heat;
- 'Item 14' means Item 14 in Part B of Schedule 2 to the VAT Act;
- 'section' means a section of the VAT Act;
- 'vegetable oil' means oil derived from a plant or any fruit of a plant, excluding olive oil

### Purpose

This BGR sets out the VAT rate applicable to the supply and importation of vegetable oil.

### Ruling

#### Zero-rated supplies

The supply of certain vegetable oil (excluding olive oil), is zero-rated under section 11(1)(j) read with Item 14, provided the vegetable oil is marketed and supplied for use in the process of cooking food.

In order for the zero rate to apply, the oil must be a 'vegetable oil' that is marketed and supplied for use in the process of cooking food. There is no specific legislation that requires vegetable oil to be labelled as oil for use in the process of cooking food. As a result, vegetable oil that is normally displayed with other cooking oils will be regarded as being supplied and marketed for use in the process of cooking food.

The vendor must obtain and retain a valid tax invoice substantiating the vendor's entitlement to apply the zero rate under section 11(3).

#### Standard-rated supplies

The supply of vegetable oil in the following instances is excluded from Item 14 and is therefore subject to VAT at the rate of 14%:

- Vegetable oil not marketed and supplied for use in the process of cooking food, for example, coconut oil displayed where toiletries are sold.
- Olive oil.
- Vegetable oil blends that contain olive oil.
- Any vegetable oil to which a standard-rated item has been added, for example, canola oil and butter blend.
- Any of the vegetable oils or blends marketed and supplied as salad dressing.
- Any vegetable oil to which another vegetable, in its natural state or

processed, is added for purposes of flavouring, that is, a whole garlic clove or chilli added to canola oil.

- Vegetable oils supplied in the course of carrying out any agreement for the furnishing or serving of any meal, refreshment, cooked or prepared food, as the case may be, so as to be ready for immediate consumption when so supplied.

#### The importation of vegetable oil

The importation of vegetable oil, provided the vegetable oil is marketed and supplied for use in the process of cooking food, is under section 13(3) read with paragraph 7(a) of Schedule 1 to the VAT Act, exempt from the VAT levied under section 7(1)(b).

The importation of vegetable oil, standard rated above, is subject to VAT at the rate of 14% under section 7(1)(b).

### **8.3. BGR 34 – Management of superannuation schemes: Long-term insurers**

For purposes of this ruling:

- 'ASISA' means the Association of Savings and Investment South Africa;
- 'direct costs' means costs incurred on independent third party suppliers by the long-term insurer which are ultimately borne by the superannuation scheme. Generally these costs are incurred for purposes of compliance with regulatory obligations imposed by various regulatory bodies and include, but are not limited to, external audit fees, levies paid to the FSB and Independent Trustees fees;
- 'FSB' means the Financial Services Board, being a public entity listed in Part A of Schedule 3 to the Public Finance Management Act No. 1 of 1999;
- 'indirect costs' means both taxable and non-taxable overhead costs incurred by the long-term insurer which may consist of employee costs, office costs and general overhead expenses;

- 'long-term insurer' means a person that supplies an insurance service under a 'long-term insurance policy' as defined in section 2(2) of the VAT Act;
- 'long-term insurance policy' includes an assistance policy, a disability policy, fund policy, health policy, life policy, sinking fund policy (also referred to as an investment policy) as well as any re-insurance policy relating to long-term insurance;
- 'section' means a section of the VAT Act

#### Purpose and scope

The Commissioner hereby grants long-term insurers permission to use the method set out in the ruling hereunder in determining the consideration for the supply of management services to a superannuation scheme where the consideration for such supply is not separately reflected but is embedded in the premium payable in terms of a long-term insurance policy.

#### Difficulties experienced by long-term insurers

Under section 12(a), read with section 2(1)(i), the provision or transfer of ownership of a long-term insurance policy is exempt from VAT as it constitutes the supply of financial services. However, the proviso to section 2(1)(i) specifically excludes the activity of managing a superannuation scheme from qualifying as financial services. The value to be placed on the supply comprising the management of a superannuation scheme is determined by applying section 10(22A), which deems the consideration in money for that supply to be the greater of the cost of making that supply or any consideration for that supply.

Due to the fact that the consideration for the management of a superannuation scheme is not separately reflected from the premium payable to the long-term insurer, the provision in section 10(22A) pertaining to the consideration for the supply cannot be met. The long-term insurer is therefore required to determine the cost of making the said supply. A difficulty however exists relating to the identification of specific expenses incurred for the management of a superannuation scheme, other than direct costs, as this activity is not distinct from the activities conducted in the course or furtherance of providing long-term

insurance policies.

All costs incurred in the course or furtherance of the administration activities fall within the scope of the provision of a long-term insurance policy, that is, an exempt supply, whereas the costs incurred in the course or furtherance of the management activities fall within the scope of managing a superannuation scheme, that is, a taxable supply. The different activities associated with each supply are set out in the Annexure.

### Ruling

In light of the fact that the consideration for the management services supplied to superannuation schemes included in the premium payable is not determinable as no specific consideration is charged for the said management services, the consideration for the supply made must be determined with reference to the cost of making that supply.

Direct costs relating to the management of a superannuation scheme are incurred by the long-term insurer on behalf of the superannuation scheme and therefore do not form part of the cost of supplying management services to a superannuation scheme. As a result, these costs are excluded from the scope of this ruling. The calculation set out below therefore only applies to the indirect costs incurred by the long-term insurer.

#### Calculation of the long-term insurer's output tax liability relating to the management of a superannuation scheme

Having regard to the difficulties experienced by long-term insurers in applying section 10(22A), long-term insurers may, under section 72, apply the formula below in calculating the cost attributable to the supply of superannuation scheme management services where the consideration for such services is not separately identifiable.

Indirect costs must be allocated to the superannuation scheme management services using an appropriate method based on assumptions with regard to estimated time spent or cost incurred (using the structure of the long-term insurer's operations and accounting or reporting systems).

The sum of the indirect costs allocated to the management of

superannuation schemes must then be used to determine the cost per policy for which the management activities (refer to the Annexure) were performed. In this regard, the following formula must be applied:

$$Y = A / B$$

Where:

- Y = Cost of supplying management services to a superannuation scheme per policy
- A = The total annual indirect costs attributable to the management activities set out in the Annexure for the –
- previous financial year using the actual financial results; or
  - the budgeted figures of the current year.
- B = The number of long-term insurance policies managed under a superannuation scheme –
- in force for the previous financial year; or
  - budgeted for the current year.

With regard to the amounts included in the formula set out above, the:

- actual results of the previous financial year may not be used should the business model of the current year differ from that of the previous year;
- budgeted figures of the current year may only be used if the budgeted figures of the previous year differ no more than 5% with the actual results of the previous year; and
- long-term insurer may only use either the actual results of the previous year or the budgeted figures for the current year and may not use a combination of both during a specific financial year.

In determining the amount that must be declared for the current year as consideration for the supply of the superannuation scheme management services, the cost per policy calculated above must be used in the following

formula:

$$Z = (Y \times C) \times 14 / 114$$

Where:

- Z = Output tax liability for the supply of management services to superannuation schemes
- Y = Cost of supplying management services to a superannuation scheme per policy
- C = Number of long-term insurance policies managed under a superannuation scheme during the specific tax period

This arrangement is conditional upon:

- there being no separate charge for the supply of services comprising the management of a superannuation scheme and the only consideration received by the long-term insurer in relation thereto is embedded in the premium payable for the supply of a long term insurance policy;
- the long-term insurer allocating expenditure incurred according to the categories set out in the Annexure; and
- an adjustment being made for any shortfall or over-declaration of output tax for the current year (based on the cost per policy value using the actual figures of the current year) within six months after year-end.

Annexure – Activities relating to the management and administration of superannuation schemes funded exclusively by individual long-term insurance policies

| <b>Summary of management and administration activities related to superannuation schemes funded exclusively by individual long-term insurance policies</b> | <b>Management<br/>(Taxable)</b> | <b>Administration<br/>(Exempt)</b> |
|------------------------------------------------------------------------------------------------------------------------------------------------------------|---------------------------------|------------------------------------|
|                                                                                                                                                            |                                 |                                    |

|                                                                                                                                                                                                                   |   |  |
|-------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|---|--|
| <b>Legal services rendered to the superannuation scheme</b>                                                                                                                                                       |   |  |
| Drafting of rules and rule amendments.                                                                                                                                                                            | X |  |
| Legal consultation, documentation and communication (only to the extent that it relates to fund governance and not the underlying policy products).                                                               | X |  |
| <b>Reporting in respect of the superannuation scheme</b>                                                                                                                                                          |   |  |
| Administration and management reports (only to the extent that it is in addition to standard information produced per policy).                                                                                    | X |  |
| Preparing financial statements for the superannuation scheme.                                                                                                                                                     | X |  |
| South African Reserve Bank reporting (only to the extent that it is in addition to standard information produced per policy).                                                                                     |   |  |
| Determining and payment of FSB levies (only to the extent that it is not a direct cost).                                                                                                                          | X |  |
| <b>Member communication</b>                                                                                                                                                                                       |   |  |
| Produce superannuation scheme rule booklets and information (often only available on the internet).                                                                                                               | X |  |
| Produce benefit and investment statements, incorporating regulatory requirements specific to a superannuation scheme (only to the extent that it is in addition to the standard information provided per policy). | X |  |
| <b>Trustee meetings (limited to cost of</b>                                                                                                                                                                       | X |  |

|                                                                               |   |   |
|-------------------------------------------------------------------------------|---|---|
| <b>provision of the venue and independent trustees)</b>                       |   |   |
| <b>Secretarial services</b>                                                   | X |   |
| <b>POLICY ADMINISTRATION</b>                                                  |   |   |
| <b>Financial Control – Investments</b>                                        |   |   |
| Bank reconciliations in respect of premiums.                                  |   | X |
| Asset and liability reconciliations performed by actuaries.                   |   | X |
| Administration and risk reconciliations.                                      |   | X |
| <i>Ad-hoc</i> payments.                                                       |   | X |
| Attend to transfers in and unallocated deposits.                              |   | X |
| Updating and reconciling contribution payments from funds.                    |   | X |
| Updating, reconciling and allocation of contributions to individual policies. |   | X |
| <b>Day-to-day policy administration</b>                                       |   |   |
| Recordal of claims.                                                           |   | X |
| Apply for tax directives.                                                     |   | X |
| Dealing with queries regarding claims.                                        |   | X |
| Make payments                                                                 |   | X |
| Submit payment advice, IT3B and IRP5.                                         |   | X |
| Unclaimed benefits administration.                                            |   | X |
| Maintenance of member/policyholder data.                                      |   | X |
| Compliance/Internal audits of internal processes.                             |   | X |
| Processing of individual applications and policy                              |   | X |

|                                                                                                                                        |                                  |                                          |
|----------------------------------------------------------------------------------------------------------------------------------------|----------------------------------|------------------------------------------|
| issue.                                                                                                                                 |                                  |                                          |
| Processing of individual policy servicing requests, e.g. contribution changes, beneficiary nominations, recording divorce orders, etc. |                                  | X                                        |
| <b>Internal Processes</b>                                                                                                              |                                  |                                          |
| Risk assessments                                                                                                                       |                                  |                                          |
| For example, medical underwriting, assessment of risk and rider benefits.                                                              |                                  | X                                        |
| <b>INVESTMENT ADMINISTRATION</b>                                                                                                       |                                  |                                          |
| Determine investment policy and strategy.                                                                                              |                                  | X                                        |
| Set investment instructions and mandates.                                                                                              |                                  | X                                        |
| Analyse and review investment manager reports.                                                                                         |                                  | X                                        |
| Monitor investment performance.                                                                                                        |                                  | X                                        |
| Reconciliations in respect of investments and the return thereon.                                                                      |                                  | X                                        |
| Review calculations of and make payment of investment fees to third party asset managers.                                              |                                  | X                                        |
| Prepare member statements and returns and reflect investment cost allocation.                                                          |                                  | X                                        |
| Action investment switches timeously.                                                                                                  |                                  | X                                        |
| Request disinvestment of funds for payment of claims.                                                                                  |                                  | X                                        |
| <b>Asset Manager</b>                                                                                                                   | <b>Third Party Asset Manager</b> | <b>Insurer Performs Asset Management</b> |

|                                                                                 |   |   |
|---------------------------------------------------------------------------------|---|---|
| <b>Financial Control</b>                                                        |   |   |
| Bank reconciliations in respect of cash transferred to, invested and withdrawn. | X | X |
| Enter into safe custody agreement with bank and make payments.                  | X | X |
| Registration of investments in name of insurer.                                 | X | X |
| Open a bank account for investments in name of the insurer.                     | X | X |
| Deposit all investment amounts in bank account.                                 | X | X |
| Liquidate/purchase investments as directed by the insurer.                      | X | X |
| Conclude the relevant electronic banking functions.                             | X | X |
| <b>Reporting</b>                                                                |   |   |
| Monthly reports on all receipts and payments on bank account.                   | X | X |
| Reports on changes in investments held as well as cash.                         | X | X |
| Month-end portfolio valuation of all investments.                               | X | X |
| Consultation with management.                                                   | X | X |
| Record keeping of investments etc.                                              | X | X |
| Assistance during audit and verification of investments.                        | X | X |

#### **8.4. BGR 35 – The value-added tax treatment of the supply and**

## ***importation of frozen potato products***

For the purposes of this ruling:

- **'formed potato product'** means a potato product that has been produced through the reconstitution of a potato, such as a potato product that has gone through the process of pureeing, mashing, mincing, shredding or crushing, and to which other ingredients such as flour, seasoning or flavourants are added;
- **'Item 12'** means Item 12 in Part B of Schedule 2 to the VAT Act;
- **'made from potato'** in relation to a potato product means a potato is present in the product in any form, and is:
  - the only ingredient in the product; or
  - where it is not the only ingredient in the product, the main ingredient in the product;
- **'potato product'** means a product made from potato;
- **'section'** means a section of the VAT Act;

### Purpose

This BGR sets out the VAT rate applicable to the supply and importation of frozen potato products.

### Zero-rated supplies

The supply of the following frozen potato products is subject to VAT at the zero rate under section 11(1)(j) read with Item 12:

- Potato products that are blanched in hot water, steam or oil for the purpose of preserving the product in its natural state. For purposes of this BGR, blanching of potato products in order to:
  - stop the action of enzymes that can cause loss of flavour, colour and texture;
  - make the potato product safer for the end-user from a microbiological aspect;

- brighten the colour and help to prevent the loss of the natural sugars and vitamins present in the potato product;
  - soften the potato product and make it easier to pack; or
  - prepare the potato product for freezing,
- is regarded as being performed for the purpose of preserving the product in its natural state.
- Potato products that have been treated with a preservative to prevent the potato product from naturally darkening.

In this regard, section 11(3) requires a vendor to obtain and retain documentary proof substantiating the vendor's entitlement to apply the zero rate.

Interpretation Note No. 31, dated 22 March 2013, or as updated, sets out the documentary proof that is acceptable to the Commissioner for the purposes of section 11(3). A copy of the supplier's zero-rated tax invoice setting out a proper description of the goods supplied is acceptable for the application of the zero rate contemplated in section 11(1)(j).

#### Standard-rated supplies

The supply of the following frozen potato products is specifically excluded from Item 12 and is subject to VAT at the rate of 14% under section 7(1)(a), irrespective of whether such products have also been treated in the same manner as the products listed in above:

- Potato products that have been treated with an additive, excluding dextrose, for a purpose other than to preserve the potato product in its natural state, such as flavourings, sweeteners, spices and salt.
- Potato products that are coated with a layer of batter in order to increase the crispiness.
- Formed potato products, such as hash browns and röstis.

#### Importation of fruit and vegetables

The importation of the frozen potato products listed as zero-rated is under section 13(3) read with paragraph 7(a) of Schedule 1 to the VAT Act, exempt from the VAT

levied under section 7(1)(b).

The importation of frozen potato products listed in standard-rated, is subject to VAT at the rate of 14% under section 7(1)(b).

## **9. GUIDES**

### **9.1. *Guide for Share Block Schemes – VAT 412***

The VAT 412 is a general guide concerning the application of the VAT Act to share block schemes in South Africa. Although fairly comprehensive, the guide does not deal with all the legal detail associated with VAT and is not intended for legal reference.

This guide deals with the VAT implications of share block schemes in South Africa and the various types of supplies related to these schemes. The intention of this guide is not to cover each and every type of transaction that can take place, but rather to deal with the basic principles and their effect from a VAT point of view.

The approach of this guide is:

- Chapter 1 – Describes the scope of topics that will be covered in the guide, as well as the approach adopted.
- Chapter 2 – Sets out the basic legal principles and explains the functioning of a share block scheme. It is important, for the purposes of this guide, to first understand the nature and operation of a share block scheme before dealing with the VAT consequences of the typical supplies which can be expected in such a scheme.
- Chapter 3 – Introduces the reader to the most important VAT concepts, definitions and other terms mentioned in the guide so that the VAT treatment of supplies which are explained in later chapters can be understood. Key points addressed in this chapter include an explanation of the terms, amongst others, 'enterprise', 'supply', 'taxable supply' and the meaning of 'fixed property'.
- Chapter 4 – Deals with how VAT should be accounted for in respect of the

different types of supplies made by share block schemes. Sets out the general rules with regard to classifying supplies, record-keeping, invoicing and documentation required. It discusses the VAT treatment of the core transactions of a share block company in terms of the most recent amendments to the VAT Act.

Chapter 5 – Provides a brief overview with subsequent VAT implications of the formation, conversion, termination or deregistration of a share block scheme. This is important since the termination, conversion or deregistration of a share block scheme may create a liability for VAT which is often overlooked.

Annexure A – Provides a brief overview of the historical changes to the VAT Act and other legislation as it relates to share block schemes. This information is included as an annexure to the guide as it provides a detailed analysis of the amendments and their effect on the various parties which may be involved in transactions relating to share block schemes without detracting from the purpose of this guide which is to explain the current VAT treatment.

## **9.2. *VAT Guide for Entertainment, Accommodation and Catering – VAT411***

This guide is a general guide concerning the application of the Value-Added Tax (VAT) law regarding supplies of goods or services which fall into the category of 'entertainment' and serves as a supplement to the VAT 404 – Guide for Vendors which deals with the general operation of VAT. Although fairly comprehensive, the guide does not deal with all the legal detail associated with VAT and is not intended for legal reference. Technical and legal terminology has also been avoided wherever possible.

As the term 'entertainment' covers a very wide array of goods and services, it is not possible for the guide to cover all aspects of entertainment. It focuses its attention, for the most part, on businesses which supply accommodation, food, beverages and other goods and services which are necessary to provide some form of

hospitality or entertainment experience.

The term 'entertainment' covers a very wide array of goods and services. To illustrate, the definition of 'entertainment' in section 1(1) means:

'the provision of any food, beverages, accommodation, entertainment, amusement, recreation or hospitality of any kind by a vendor whether directly or indirectly to anyone in connection with an enterprise carried on by him'.

If one thinks of all the different types of entertainment supplies, and all the direct or indirect ways in which a person can be *supplied* with 'any food, beverages, accommodation, entertainment, amusement, recreation or hospitality' as contemplated by the definition, the permutations are almost infinite. It has, therefore, been necessary to limit the scope of this guide to focus, for the most part, on hospitality type businesses which supply entertainment in the form of accommodation, food, beverages, and associated goods and services.

Typically, this includes:

- different types of supplies made by accommodation establishments, including meals and other domestic goods and services supplied together with the accommodation (where applicable);
- supplies of food and beverages in restaurants, bars, hotels or other entertainment environments; and
- catering services supplied to customers or employees at events and places of work, as well as some of the outsourcing arrangements in respect of those supplies.

The term '*entertainment*' when used in this guide is therefore intended to focus on these limited areas, but the reader should remember that the term has a much wider meaning when applying the VAT Act in a more general sense.

The approach of this guide is:

Chapter 1 – Explores the scope of the topic and some of the general rules regarding supplies of entertainment.

Chapter 2 – Introduces the reader to the most important concepts, terms and

definitions mentioned in the guide so that the VAT treatment of supplies of entertainment which are explained in later chapters can be understood.

- Chapter 3 – Provides a brief overview of the legal concepts 'agent' and 'principal'. This is important as the VAT consequences of a transaction cannot be determined until the contractual relationship between the parties is established. These concepts are particularly important with regard to supplies of accommodation, catering and travel, which are often arranged through agents.
- Chapter 4 – Deals with supplies of entertainment in general and focuses on the special rules which deny the deduction of input tax on entertainment expenses, as well as the exceptions to these rules.
- Chapter 5 – Provides a detailed analysis of the definition '*commercial accommodation*' and highlights the different types of supplies and accommodation establishments contemplated in this definition.
- Chapter 6 – Explains the VAT treatment of the different types of supplies made by accommodation establishments.
- Chapter 7 – Deals with matters pertaining to the time and value of supplies, as well as the issuing of invoices and tax invoices, and how this impacts on the accounting of VAT.
- Chapter 8 – Focuses on the issues faced by catering businesses which supply food and beverages to customers as their main business, or as an ancillary part of carrying on another activity. Examples include restaurants, commercial caterers, employee and student canteens, and businesses which supply meals and refreshments as part of a transportation service.
- Chapter 9 – Discusses the supplies made by welfare organisations, clubs, associations not for gain, societies and similar bodies, as well as some special rules which apply to these entities.
- Chapter 10 – Discusses some of the other aspects regarding the supply of entertainment which are not dealt with in the other chapters.

## **10. DRAFT GUIDES**

### ***10.1. Guide on the taxation of professional sports club and players***

This guide is a general guide regarding the taxation of professional sports clubs and sports players in South Africa. It also refers briefly to the position of visiting professional sports players.

The professional sports industry is one of the fastest growing industries internationally. The main aim of this guide is to explain the South African tax consequences for professional sports clubs and sports players in South Africa.

## **11. 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.