TAX UPDATE

For period: April 2025 to June 2025

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1. FOREWORD

The purpose of this update is to summarise developments that occurred during the second quarter of 2025, specifically in relation to Income Tax and VAT. Johan Kotze, a Tax Executive at Shepstone & Wylie Attorneys, has compiled this summary.

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

Please take some time and consider the tax cases.

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

Enjoy reading on!

Not about tax, but on investment, I recommend the book of Howard Marks 'The Most Important Thing Illuminated: Uncommon Sense for the Thoughtful Investor'.

The Book in Three Sentences:

- You can't do the same things others do and expect to outperform.
- The most dependable way to outperform the market is to buy something for less than its value.
- It is price, not quality that determines value: high-quality assets can be risky, and low-quality assets can be safe.

2. AMENDMENTS TO THE REGULATIONS PRESCRIBING ELECTRONIC SERVICES FOR THE PURPOSES OF THE DEFINITION OF ‘ELECTRONIC SERVICES’ IN SECTON 1 OF THE VAT ACT

1. BACKGROUND

Effective 1 April 2019 government introduced amendments to the Regulations prescribing electronic services for the purposes of the definition of ‘electronic services’ in section 1(1) of the Value-Added Tax Act, 89 of 1991 (‘the VAT Act’). In terms of these amendments, the scope of the regulations was expanded to include all ‘services’ as defined in the VAT Act that are supplied by means of an electronic agent, electronic communication or the internet, for any consideration.

The explanatory memorandum to those amendments stated that the policy intention was to subject to VAT those services that are provided using minimal human intervention.

The regulations contained certain exclusions, such as certain educational services and telecommunications services. Since the VAT Act did not exclude supplies between businesses in a domestic context, it was deemed imprudent to exclude such supplies within the context of the regulations. However, to provide relief for administrative burdens related to the cross-border supplies of electronic services between companies within the same group, certain supplies within a group were also excluded.

Consequential amendments to the VAT Act introduced the concept of an ‘’intermediary’. An intermediary is deemed to be the supplier where such intermediary facilitates the supply of the electronic services for an underlying supplier and where such intermediary is responsible for the issuing of the invoice and the collection of the payment. The explanatory memorandum for those amendments further clarified that the requirement of the intermediary being ‘responsible for’ the issuing of the invoice or the collection of the payment would still be met even if such functions were outsourced, provided that the intermediary bore the ultimate responsibility to ensure that these occurred. The policy rationale behind this was to exclude from the scope of the regulations

and the VAT Act, those intermediaries that were pure payment platforms and did not partake in any other way with the supply.

Further, in keeping with the Guidelines developed by the Organisation for Economic Cooperation and Development ('OECD') , which guidelines have been endorsed by G20 and non G20 countries and the multinational business community, SARS had provided for a simplified VAT registration regime that reduced the compliance burden on offshore suppliers that were required to register for VAT in terms of the VAT Act and the amended regulations.

2. REASONS FOR CHANGE

Since the digital economy is constantly evolving, it is necessary to constantly review South Africa's VAT legislation in this regard. Further, as global and domestic experience in this relatively new arena of tax legislation grows, lessons are learned and amendments may be necessary, especially in the sphere of tax administration. Further, technological advances may facilitate certain amendments.

3. PROPOSALS

Certain amendments were proposed in 2020, but since the Covid 19 legislative urgencies overtook events, these proposed amendments were never enacted. It is proposed that these be included now, which relate to adding a new definition of 'content' and revising the definition of 'telecommunications services' to expand on the meaning of 'telecommunications system' that was contained within that definition. 'Content' was excluded from the definition of 'telecommunications services' hence it became necessary to define 'content'.

Taxpayers requested clarity relating to supplies between group of companies, specifically with regard to global contracts. The proposed amendment to regulation 2(c)(ii) provides this clarity. This regulation is being retained despite the new exclusion being introduced as regulation 2(c)(d) to cover situations where the domestic company may not yet be a 'vendor' as defined in the VAT Act.

The new proposed exclusion being introduced as regulation 2(c)(d) relates to services provided from a place in an export country by a non-resident person where such supplies are made solely to vendors that are registered in South Africa in terms of section 23 of the VAT Act. This is a form of 'business-to-business' ('B2B') exclusion that applies to supplies made to registered vendors.

The policy rationale behind this is to ease the administrative burden on such suppliers and recipients where there is little or no gain to the fiscus. The explanatory memorandum to the 2019 amendments stated that this was not excluded at the time due to concerns relating to fairness and equity between offshore suppliers and domestic suppliers. These concerns still exist; however, non-compliance is easier dealt with and litigated domestically than across borders. With that in mind, government has reconsidered its position and is proposing this amendment to ensure that this VAT regime is as simplified as possible for non-resident suppliers that have no physical presence in South Africa, in line with the globally accepted OECD recommendations , to encourage compliance where legal jurisdiction to enforce compliance may be a challenge. These supplies will still be liable for VAT under section 7(1)(c) which relates to the recipient declaring VAT on imported services.

Further, the intention, by using the word 'solely', is to exclude those electronic services suppliers that supply to registered vendors only. Electronic services suppliers that make supplies both to vendors and non-vendors will be subjected to these regulations (i.e. not excluded) and must utilise the value of the supplies to all vendors and non-vendors to determine registration liability. Once registered, such supplier will be required to levy VAT on all supplies of electronic services, to vendors and non-vendors. The rationale for not excluding such suppliers from these regulations (i.e. for not introducing a full B2B exclusion) is due to the complexities that would present to suppliers, in trying to identify a recipient's status on a case-by-case basis.

It is further proposed that amendments be made to section 54(2B) of the VAT Act. The first amendment relates to the requirement that the underlying supplier (the principal) is not a registered vendor. This requirement is being deleted since it is the intention to hold the intermediary responsible for all supplies made through its platform, including supplies made by principals that are not residents of South Africa, irrespective of their VAT status in South Africa, where such principal and intermediary have agreed, in writing, that the supply will be treated as being that of the intermediary. The policy rationale behind this is to ease the administrative burden on the principal, to ensure that VAT is not accounted for twice (by the principal and the intermediary) on the same supply and to facilitate ease of compliance checks and audits.

The second amendment to this section is to introduce a second sub-section that introduces the concept of a joint and several liability for both the principal

and the intermediary in instances where both parties have agreed to treat the supplies as being made by the intermediary. Both parties will be held jointly and severally liable for performing the duties of the principal or the intermediary under the VAT Act and paying the tax imposed by the VAT Act in respect of those taxable supplies that were made under the agreement.

Finally, despite the words ‘minimal human intervention’ being used in the explanatory memorandum for the 2019 amendments, these words or this concept was never introduced in either the VAT Act or the regulations. The intention was for the interpretation of these regulations to be done within the spirit of that concept. The policy rationale behind these regulations is to address the tax challenges of the digital economy from a South African VAT point of view. This is in line with the Base Erosion and Profit Shifting concerns raised by the G20 Finance Ministers and addressed through the OECD’s various guidelines dealing with electronic commerce across borders. Perhaps the 2019 Explanatory Memorandum ought to have used the words ‘electronic commerce across borders’ rather than the words ‘minimal human intervention’ since it has come to government’s attention that this term is now being challenged by non-resident suppliers who are trying to avoid VAT registration in South Africa.

For example, some developers of software believe that the development of their product took many man-hours of human intervention to develop and that the subsequent supply thereof is merely done through an electronic medium, similar to an attorney emailing his legal opinion. This interpretation is clearly contrary to the government’s policy intention when the 2019 amendments and explanatory memorandum were drafted. To combat such blatant misinterpretation, it is recommended that the interpretation of which services fall within these regulations and the VAT Act, be as strict as possible, within the confines of the legislation, with no regard to the words ‘minimal human intervention’, since these words do not appear in the legislation.

In terms of the provisions of section 23(1A), which was gazetted on 05 January 2023, via Government Gazette No. 47827, relief was granted from the requirement to register where the value of the taxable supplies reaches the threshold solely as a consequence of abnormal circumstances of a temporary nature. This provision will cater for suppliers that were not intended to be caught by the provisions of these regulations.

4. EFFECTIVE DATE

The proposed amendments come into operation on 1 April 2025.

3. AMENDMENTS TO THE REGULATIONS ON THE DOMESTIC REVERSE CHARGE RELATING TO VALUABLE METAL ISSUED IN TERMS OF SECTION 74(2) OF THE VAT ACT

1. BACKGROUND

Prior to 2014, a deduction of notional input tax on the acquisition of gold jewellery by registered VAT vendors from non-VAT vendors was allowed. This provision created an opportunity for VAT vendors to claim fraudulent input tax deductions. In 2014, Government responded by making changes to the definition of 'second-hand goods' in section 1(1) the Value-Added Tax Act, 1991 (Act No. 89 of 1991) ('the VAT Act') to the effect that vendors were excluded from claiming notional input tax on second-hand goods containing gold, unless such goods were re-sold in the same or substantially the same state as they were bought in.

Despite the amendment to the definition of 'second-hand goods' in section 1(1) of the VAT Act, vendors used a new modus operandi to extract undue VAT refunds from the fiscus and moved away from making fictitious input tax deductions under the pretence that the goods are second-hand goods, containing gold. These vendors registered businesses as vendors for VAT purposes and fabricated the documentation required for input tax purposes (invoice farms). These vendors acquired Krugerrands, illegal gold, etc. and introduced them in the production and distribution chain to manufacture mainly goods containing gold in the form of jewellery, bars, blank coins, ingots, buttons, wire, plate, granules, in a solution, residue or similar forms, for export purposes.

In order to curb these VAT fraud schemes, Government introduced the Domestic Reverse Charge Regulations1 ('DRC Regulations') in terms of section 74(2) of the VAT Act to foreclose schemes and malpractices to claim undue VAT refunds from SARS by vendors operating in the value chain relating to high-risk goods containing gold. The policy objective of the DRC Regulations

is an anti-abuse measure aimed at curbing the VAT fraud scheme, specifically aimed at goods in the form of jewellery, bars, blank coins, ingots, buttons, wire, plate, sponge, powder, granules, in a solution, sheet, tube, strip, rod, reside or similar forms, containing gold, including any ancillary goods or services.

In May 2024, government introduced further amendments to the regulations to curb further abuse, as some taxpayers in this space became more creative in their anti-avoidance schemes.

2. REASONS FOR CHANGE

It has now come to Government's attention that the exclusion in paragraph (a) to the definition of 'valuable metal' in regulation 1 has led to the schemes and malpractices being shifted to the primary gold sector.

3. PROPOSAL

It is proposed that the exclusion contained in paragraph (a) to the definition of 'valuable metal' in regulation 1 be deleted.

4. EFFECTIVE DATE

The amendments to the DRC Regulations come into effect on 1 April 2025.

4. REGULATIONS ON DETERMINING THE VAT LIABILITY IN RESPECT OF CASINO TABLE GAMES OF CHANCE ISSUED IN TERMS OF SECTION 74 OF THE VAT ACT

1. BACKGROUND

The gambling industry was permitted to account for value-added tax (VAT) by applying the tax fraction to the net betting transactions (on the amount remaining after winnings have been deducted which is known as the 'net drop method') for casino games of chance under the 'section 72 arrangement' contained in Binding General Ruling 13 (issue 2) (BGR 13) that was issued on 22 March 2013.

Section 8(13) of the VAT Act deems the person with whom a bet is placed, to have supplied a service to the person that has bet an amount on the outcome of a race, or other event/occurrence. Section 16(3)(d) of the VAT Act allows a deduction equal to the tax fraction of amounts paid by a supplier in respect of

betting services contemplated in section 8(13) of the VAT Act, as prizes or winnings to the recipient of such betting services.

The recent legislative amendment to section 72 of the VAT Act led to the expiry of BGR 13 on 31 December 2021 which has placed suppliers of table games of chance in difficulty when completing their VAT returns. As an interim measure, a decision was made under the amended provisions of section 72 of the VAT Act, which is contained in Binding General Ruling 59 that was issued on 13 December 2021, to prescribe a method for vendors to determine the VAT liability and account for VAT with regard to the supplies in relation to casino table games of chance.

The Regulations now brings that arrangement into the law.

2. REASONS FOR CHANGE

The gambling industry does not work within the usual confines of the VAT Act and South Africa is one of a few countries that taxes betting transactions. A casino/bookmaker accounts for output tax on all bets placed and may deduct input tax on any winnings paid to punters. The nature of betting transactions in the casino industry, especially the table game of chance, makes it difficult to separate bets placed by punters and winnings paid to punters. Considering the nature of the table game of chance, the number of punters, the number of bets placed, and the game's speed, all of which are essential for running a successful table operation, it is practically impossible to record each bet and pay-out for a casino table game of chance. These practicalities in respect of a table game of chance make it virtually impossible to separate bets placed by punters and winnings paid to punters by gaming operators as can be noted from the process below.

2.1 GAMING TRANSACTIONS

The gaming transactions operate as follows for table games of chance:

- Table games operate with a variety of denominations of chips, for example, R100, R500, R1 000.
- A punter wanting to play on the tables buys-in with cash, a cash plaque, being a high denomination value representation obtained from the cash desk, by way of a cash withdrawal from the punter's casino card or by buying in with chips.

- Any cash, plaques or cash withdrawal slips are placed in the drop box (a sealed box attached to each table), whilst chips received are placed in the table's chip tray, where all chips not in play, are kept.
- All bets are placed with chips, which if lost, get returned to the chip tray. All winning bets are paid out to the punter with chips from the chip tray.
- In case of a shortage of a certain denomination of chips on the table, the table obtains a 'fill' from the cash desk. The fill is documented by placing one copy of the fill slip in the drop box.
- In case of a surplus of chips in the chip tray, the table can return chips to the cash desk, which is also documented by placing one copy of the 'credit slip' in the drop box.
- Due to the number of punters, the number of bets being placed, and the speed of the game, all of which are essential for running a successful table operation, it is virtually impossible to record each bet and pay out for a casino table game.

2.2 CALCULATION OF TABLE WIN OR LOSS

In practice, the table win, or loss is calculated as follows:

- Drop (cash, plaques and cash withdrawal slips), plus closing float of chips in the chip tray, minus opening float of chips in the chip tray, minus fills, plus credits.
- The result is the table win or loss, which is relevant for accounting purposes and for determining the operator's liability for gaming tax in terms of the relevant provincial Gambling Regulations.
- The win per table is determined every 24 hours. Based on the above, the gambling industry experiences difficulties in reflecting output tax under section 8(13) of the VAT Act, separately from input tax deducted under section 16(3)(d) of the VAT Act, for purposes of completing the VAT201 return.

3. DETAILED EXPLANATION OF THE REGULATIONS

The Regulations are for prescribing the 'gross gaming revenue' as a method for determining the VAT liability in respect of casino table games of chance.

3.1 REGULATION 1: DEFINITIONS

3.1.1 'Casino' The term 'casino' means a 'casino', as defined in section 1 of the National Gambling Act, 2004 (Act 7 of 2004) ('the National Gambling Act') that is operated by a person that is 'licensed', as contemplated in section 1 of that Act, and is a registered vendor. The proposed amendment will clarify what is meant to be a 'casino' and the group of vendors affected by the Regulations.

3.1.2 'Gross gaming revenue' The term 'gross gaming revenue' is an amount determined, under the applicable provincial gambling legislation, for each table game. It is determined by the closing bankroll plus credit slips for cash, chips or tokens returned to the casino cage, plus drop, less opening bankroll and fills to the table. The proposed amendment clarifies the amount to be recognized as the 'gross gaming revenue'.

3.1.3 'Table game of chance' The term 'table game of chance' means a 'gambling game', as defined in the National Gambling Act, that -is played against the casino and operated by one or more live croupiers. The proposed amendment clarifies the type of game the Regulations refer to.

3.2 REGULATION 2: ACCOUNTING FOR VAT ON THE VAT201

A casino may account for VAT on its VAT returns in respect of table games of chance, on the 'gross gaming revenue', for the relevant tax period, subject to the following:

3.2.1 Gross gaming revenue in respect of table games of chance must be included in field 1 of the VAT return, with the tax fraction applied to that amount reflected in field 4.

3.2.2 Casinos are not entitled to any deductions under section 16(3)(d) of the VAT Act if such an amount has been included in calculating the gross gaming revenue.

3.2.3 Casinos are required to maintain adequate records to enable SARS to verify the validity and accuracy of the tax liability calculated and included in the VAT return, as set out above, and in particular, the records for the purpose of audits conducted by the provincial Gaming Boards.

4. EFFECTIVE DATE

The Regulations come into effect on 1 January 2025.

5. NOTICES / REGULATION

5.1. Media statement on the reversal of VAT increase

The Minister of Finance will shortly introduce the Rates and Monetary Amounts and the Amendment of Revenue Laws Bill (Rates Bill), which proposes to maintain the Value-Added Tax (VAT) rate at 15 per cent from 1 May 2025, instead of the proposed increase to VAT announced in the Budget in March.

The decision to forgo the increase follows extensive consultations with political parties, and careful consideration of the recommendations of the parliamentary committees. By not increasing VAT, estimated revenue will fall short by around R75 billion over the medium-term.

As a result, the Minister of Finance has written to the Speaker of the National Assembly to indicate that he is withdrawing the Appropriation Bill and the Division of Revenue Bill, in order to propose expenditure adjustments to cover this shortfall in revenue. Parliament will be requested to adjust expenditure in a manner that ensures that the loss of revenue does not harm South Africa’s fiscal sustainability.

The decision not to increase VAT means that the measures to cushion lower income households against the potential negative impact of the rate increase now need to be withdrawn and other expenditure decisions revisited. To offset the unavoidable expenditure adjustments, any additional revenue collected by SARS may be considered for this purpose going forward.

The Minister of Finance expects to introduce a revised version of the Appropriation Bill and Division of Revenue Bill within the next few weeks.

The initial proposal for an increase to the VAT rate was motivated by the urgent need to restore and replenish the funding of critical frontline services that had suffered reductions necessitated by the country's constrained fiscal position.

There are many suggestions, however some of them would create greater negative consequences for growth and employment and some of them, while worthwhile, would not provide an immediate avenue for further revenue in the short term to replace a VAT increase.

The National Treasury will, however, consider these and other proposals as potential amendments in upcoming budgets as mechanisms to increase the resources available.

5.2. Table of interest

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

DATE FROM	DATE TO	RATE
1 November 2020	28 February 2022	7,00%
1 March 2022	30 April 2022	7,25%
1 May 2022	30 June 2022	7,50%
1 July 2022	31 August 2022	7,75%
1 September 2022	31 October 2022	8,25%
1 November 2022	31 December 2022	9,00%
1 January 2023	28 February 2023	9,75%
1 March 2023	30 April 2023	10,50%
1 May 2023	30 June 2023	10,75%
1 July 2023	31 August 2023	11,25%
1 September 2023	31 December 2024	11,75%

1 January 2025	28 February 2025	11,50%
1 March 2025	30 April 2025	11,25%
1 May 2025	Until change in the Public Finance Management Act rate	11,00%

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

DATE FROM	DATE TO	RATE
1 September 2020	31 October 2020	3,25%
1 November 2020	28 February 2022	3,00%
1 March 2022	30 April 2022	3,25%
1 May 2022	30 June 2022	3,50%
1 July 2022	31 August 2022	3,75%
1 September 2022	31 October 2022	4,25%
1 November 2022	31 December 2022	5,00%
1 January 2023	28 February 2023	5,75%
1 March 2023	30 April 2023	6,50%
1 May 2023	30 June 2023	6,75%
1 July 2023	31 August 2023	7,25%
1 September 2023	31 December 2024	7,75%
1 January 2025	28 February 2025	7,50%
1 March 2025	30 April 2025	7,25%

1 May 2025	Until change in the Public Finance Management Act rate	7,00%

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

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

DATE FROM	DATE TO	RATE
1 August 2020	30 November 2021	4,50%
1 December 2021	31 January 2022	4,75%
1 February 2022	31 March 2022	5,00%
1 April 2022	31 May 2022	5,25%
1 June 2022	31 July 2022	5,75%
1 August 2022	30 September 2022	6,50%
1 October 2022	30 November 2022	7,25%
1 December 2022	31 January 2023	8,00%
1 February 2023	31 March 2023	8,25%
1 April 2023	31 May 2023	8,75%
1 June 2023	30 September 2024	9,25%

1 October 2024	30 November 2024	9,00%
1 December 2024	31 January 2025	8,75%
1 February 2025	31 May 2025	8,50%
1 June 2025	Until change in the Repurchase rate as announced by the Reserve Bank	8,25%

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

5.3. Returns to be submitted

1. General

(1) Any term or expression in this notice to which a meaning has been assigned in a 'tax Act' as defined in section 1 of the Tax Administration Act, 2011, has the meaning so assigned, unless the context indicates otherwise and the following terms have the following meaning—

'2025 year of assessment' means—

(a) in the case of a company, the financial year of the company ending during the 2025 calendar year; and

(b) in the case of any other person, the year of assessment ending during the period of 12 months ending on 28 February 2025;

'income tax return' means a return for the assessment of normal tax in respect of the 2025 year of assessment, including a turnover tax return if a person is a registered micro business under the Sixth Schedule to the Income Tax Act; and

'trust' means a trust as defined in section 1 of the Income Tax Act.

(2) Notice is hereby given in terms of section 25 of the Tax Administration Act, read with section 66(1) of the Income Tax Act, that a person specified in

terms of paragraph 2 is required to submit an income tax return within the period prescribed in paragraph 4

2. Persons who must submit an income tax return

The following persons must submit an income tax return:

(a) Every company or other juristic person, which was a resident during the 2025 year of assessment that—

(i) derived gross income of more than R1 000;

(ii) held assets with a cost of more than R1 000 or had liabilities of more than R1 000, at any time;

(iii) derived any capital gain or capital loss of more than R1 000 from the disposal of an asset to which the Eighth Schedule of the Income Tax Act applies; or (iv) had taxable income, taxable turnover, an assessed loss or an assessed capital loss;

(b) Every trust that was a resident during the 2025 year of assessment;

(c) Every company, trust or other juristic person, which was not a resident during the 2025 year of assessment, that—

(i) carried on a trade through a permanent establishment in South Africa;

(ii) derived income from a source in South Africa; or

(iii) derived any capital gain or capital loss from the disposal of an asset to which the Eighth Schedule to the Income Tax Act applies;

(d) Every company incorporated, established or formed in South Africa, but that was 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 during the 2025 year of assessment;

(e) Every natural person who during the 2025 year of assessment—

(i) was a resident and carried on any trade (other than solely in his or her capacity as an employee); or

(ii) was not a resident and carried on any trade (other than solely in his or her capacity as an employee) in South Africa;

(f) Every natural person who during the 2025 year of assessment—

(i) was a resident and had capital gains or capital losses exceeding R40 000;

(ii) was not a resident and had capital gains or capital losses from the disposal of an asset to which the Eighth Schedule to the Income Tax Act applies;

(iii) was a resident and held any funds in foreign currency or owned any assets outside South Africa, if the total value of those funds and assets exceeded R250 000 at any stage during the 2025 year of assessment;

(iv) was a resident and to whom any income or capital gains from funds in foreign currency or assets outside South Africa was attributed in terms of the Income Tax Act;

(v) was a resident and held any participation rights, as referred to in section 72A of the Income Tax Act, in a controlled foreign company;

(vi) was a resident and had taxable turnover; or

(vii) subject to the provisions of paragraph 3, at the end of the 2025 year of assessment—

(aa) was under the age of 65 and whose gross income exceeded R95 750;

(bb) was 65 years or older (but under the age of 75) and whose gross income exceeded R148 217; or

(cc) was 75 years or older and whose gross income exceeded R165 689;

(g) Subject to the provisions of paragraph 3, every estate of a deceased person that had gross income during the 2025 year of assessment;

(h) Every non-resident whose gross income during the 2025 year of assessment included interest from a source in South Africa to which the provisions of section 10(1)(h) of the Income Tax Act do not apply;

(i) Every person who is requested by SARS in writing to furnish a return, irrespective of the amount of income or nature of receipts or accruals of the person; and

(j) Every representative taxpayer of any person referred to in items (a) to (i) above.

3. Persons not required to submit an income tax return

(1) A natural person or estate of a deceased person is not required to submit an income tax return in terms of paragraph 2(f)(vii) or (2)(g) if the gross income of the person during the 2025 year of assessment consisted solely of gross income described in one or more of the following items:

(a) Remuneration (other than remuneration referred to in item (e)) paid or payable from a single employer, which does not exceed R500 000 and employees' tax has been deducted or withheld in terms of the deduction tables prescribed by SARS;

(b) Interest (other than interest from a tax free investment) from a source in South Africa not exceeding—

(i) R23 800 in the case of a natural person below the age of 65 years at the end of the year of assessment;

(ii) R34 500 in the case of a natural person aged 65 years or older at the end of the year of assessment; or

(iii) R23 800 in the case of the estate of a deceased person;

(c) Dividends that are exempt from normal tax and the natural person was a non-resident throughout the 2025 year of assessment;

(d) Amounts received or accrued from a tax-free investment; and

(e) A single lump sum benefit received from a pension fund, provident fund, pension preservation fund, provident preservation fund or retirement annuity fund, and tax has been deducted or withheld in terms of a directive issued by SARS.

(2) Subparagraph (1) does not apply to a natural person—

(a) who was paid or granted an allowance or advance as described in section 8(1)(a)(i) of the Income Tax Act other than an amount reimbursed or advanced as described in section 8(1)(a)(ii) or an allowance or advance referred to in section 8(1)(b)(iii) that does not exceed the amount determined by applying the rate per kilometre for the simplified method in the notice fixing the rate per kilometre under section 8(1)(b)(ii) and (iii) to the actual distance travelled;

(b) who was granted a taxable benefit described in paragraph 7 of the Seventh Schedule to the Income Tax Act; or

(c) who received any amount or to whom any amount accrued in respect of services rendered outside South Africa.

(3) A natural person is not required to submit an income tax return in terms of paragraph 2(f)(vii) if—

(a) the person is notified by SARS in writing that he or she is eligible for automatic assessment; and

(b) the person's gross income, exemptions, deductions and rebates reflected in the records of SARS are complete and correct as at the date of the assessment based on an estimate to give effect to automatic assessment.

4. Periods within which income tax returns must be furnished

Income tax returns must be submitted within the following periods:

(a) In the case of any company, public benefit organisation approved by SARS in terms of section 30(3) of the Income Tax Act, and recreational club approved by SARS in terms of section 30A(2) of the Act, 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 20 October 2025;

(ii) on or before 19 January 2026 if the return relates to a provisional taxpayer

(iii) on or before 19 January 2026 if the return relates to a trust; or

(vi) where accounts are accepted by SARS in terms of section 66(13A) of the Income Tax Act in respect of the whole or portion of a taxpayer's income, which are drawn to a date after 28 February 2025 but on or before 30 September 2025, within 6 months from the date to which such accounts are drawn.

5. Form of income tax returns to be submitted

The forms prescribed by SARS for the submission of income tax returns are obtainable on request via eFiling at https://www.sarsefiling.co.za or downloadable from the SARS website at https://www.sars.gov.za/find-a-form/.

6. Manner of submission of income tax returns

(1) Income tax returns must—

(a) in the case of a company, be submitted electronically by using the SARS eFiling platform;

(b) in the case of natural persons or trusts be submitted electronically—

(i) by using the SARS eFiling platform, provided the person is registered for eFiling; or

(ii) through the assistance of a SARS official at an office of SARS

(c) in the case of institutions, boards or bodies be—

(i) submitted electronically by using the SARS eFiling platform, provided the person is registered for eFiling;

(ii) submitted electronically through the assistance of a SARS official at an office of SARS;

(iii) forwarded by post to SARS; or

(iv) delivered to an office of SARS, other than an office which deals solely with matters relating to customs and excise.

(2) Returns for turnover tax must be forwarded by post to SARS or delivered to an office of SARS, other than an office which deals solely with matters relating to customs and excise.

(3) SARS may agree that a person, who is required to submit a return in the manner prescribed in subparagraph (1) or (2), may submit the return in an alternative manner.

6. DRAFT NOTICES / REGULATION

6.1. Incidences of non-compliance by a person in terms of section 210 of the TA Act that are subject to fixed amount penalty in accordance with section 210(1) and 211 of the TA Act

1. General

Any word or expression contained in this notice to which a meaning has been assigned in the Tax Administration Act, 2011, ('the Act') or the Regulations published by the Minister of Finance for purposes of paragraph (a) of the definition of 'international tax standard' in section 1 of the Act, published in Government Gazette No. 43781 of 9 October 2020 read with Government Gazette No. 48165 of 3 March 2023 ('the Regulations'), has the meaning so assigned, unless the context indicates otherwise.

2. Incidences subject to fixed amount penalty

2.1 Failure by a Reporting Financial Institution to submit a return as required by a public notice issued under section 26(1) of the Act.

2.2 Failure by a Reporting Financial Institution to comply with a due diligence requirement under the Regulations read with section 26(2)(c) of the Act.

2.3 Failure by a Reporting Financial Institution to, within 60 days of notification by SARS, provide the prescribed details of:

(a) a Reportable Person that is an Account Holder;

(b) if the Reportable Person is an Entity, any Controlling Person of that Entity;

(c) any other person; or

(d) any class of the above persons,

who has failed under section 26(4) of the Act to provide any information, document of thing that is required by the Reporting Financial Institution to comply with due diligence requirements and submit a return to SARS for purposes of the Regulations.

2.4 Failure:

(a) a Reportable Person that is an Account Holder;

(b) if the Reportable Person is an Entity, any Controlling Person of that Entity; or

(c) any other person,

listed by a Reporting Financial Institution in response to a notice contemplated in paragraph 2.3, to comply with the person's obligations under section 26(4) of the Act.

7. TAX CASES

7.1. Thistle Trust v C:SARS (87 SATC 103)[1]

Applicant, being the Thistle Trust, was a registered *inter vivos* discretionary trust and a South African tax resident.

The Thistle Trust was a beneficiary of ten vesting trusts described as the Zenprop Group (Zenprop) which was a property developer and property owner and in the course of its business it frequently bought and sold properties.

Respondent was SARS.

In the 2014, 2015 and 2016 tax years, Zenprop disposed of assets and realised capital gains, the proceeds of which it distributed to the Thistle Trust and the Thistle Trust, in turn, distributed the proceeds of those capital gains to the natural persons who were its beneficiaries.

The proceeds of the capital gains were all passed through the multi-tiered trust structure to the ultimate beneficiaries within the same tax years in which they were realised.

[1] Constitutional Court

Acting on legal advice received, Zenprop and the Thistle Trust did not account for the capital gains in their tax returns for the 2014, 2015 and 2016 tax years. They were advised that the relevant amounts were capital gains which, in terms of the common law conduit principle and the relevant provisions of the Income Tax Act (IT Act), were taxable as capital gains in the hands of the ultimate beneficiaries. The beneficiaries accounted for the capital gains in their tax returns and paid the capital gains tax for which they would have been liable in respect of these capital gains.

In the 2014 to 2016 tax years, the individual beneficiaries were liable for capital gains tax on only 33.3% of their respective net capital gains for each year of assessment. As an *inter vivos* trust, the Thistle Trust was liable for capital gains tax on 66.6% of its net capital gain for each year of assessment.

SARS conducted a tax audit of the Thistle Trust and it took the position that on a proper application of the IT Act, liability for the capital gains realised by Zenprop had passed from Zenprop to the Thistle Trust as the direct beneficiary of Zenprop, but did not pass further from the Thistle Trust to its beneficiaries. It accordingly held the Thistle Trust liable for capital gains tax in respect of the amount of the capital gains distributed to it by Zenprop.

SARS, on 21 September 2018, raised additional assessments in which it claimed capital gains tax from the Thistle Trust for these amounts and the additional assessments raised by SARS also imposed USP on the Thistle Trust in respect of the undeclared capital gains tax.

The Thistle Trust objected to the additional assessments on the basis that, having regard to the provisions of section 25B of the IT Act and par. 80(2) of the Eighth Schedule to the IT Act, the capital gains in issue ought not to have been taxed as it derived no taxable income in this regard and such gains were properly taxable in the hands of the Thistle Trust's beneficiaries under the said provisions of the IT Act.

The Thistle Trust, in addition to its primary objection to the additional assessment, also objected to the imposition of understatement penalties (USP) in the assessment.

The Thistle Trust contended that, even if the additional assessment was correct, its failure to account for these capital gains in its tax returns was a *bona fide* (good faith) inadvertent error within the meaning of section 222(1) of the Tax Administration Act (TA Act) and therefore could not give rise to USP.

SARS disallowed the Thistle Trust's objection and in March 2021 it appealed to the Tax Court (see ITC 1941 (2021) 83 SATC 387), challenging the additional assessments

raised by SARS. The Tax Court upheld the Thistle Trust's appeal relying on section 25B of the IT Act and the conduit principle, and held that the capital gains were not taxable in the hands of the Thistle Trust, but were taxable as capital gains in the hands of the beneficiaries.

SARS then appealed to the Supreme Court of Appeal with the leave of the Tax Court (see C:SARS v The Thistle Trust 85 SATC 347) and that court upheld SARS' appeal on the primary liability of the Thistle Trust for capital gains tax, but it dismissed SARS' claim for USP.

The Supreme Court of Appeal held that the facts of the present case did not present appropriate circumstances for the application of the conduit principle and upheld SARS' argument that the capital gains realised by the disposal of properties by Zenprop were taxable in the hands of the Thistle Trust and not in the hands of the ultimate beneficiaries. This, so it held, flowed from the fact that the Thistle Trust had not itself disposed of any capital asset or determined any capital gain and the Thistle Trust had only distributed moneys that vested in it from Zenprop as of right and in these circumstances the conduit principle did not apply in terms of par. 80(2) of the Eighth Schedule to the IT Act.

Although the Supreme Court of Appeal found that SARS was correct to raise the additional assessment imposing capital gains tax on the Thistle Trust in respect of the 2014 to 2016 tax years, it held that the Thistle Trust could not be liable for USP. In its judgment, it stated that SARS had conceded at the hearing that the understatement by the Thistle Trust was a *bona fide* inadvertent error and in terms of section 222 of the TA Act this precluded the imposition of any USP.

The Thistle Trust then applied for leave to appeal against the decision of the Supreme Court of Appeal to the Constitutional Court and SARS had filed a conditional counter-application for leave to appeal against the decision of the Supreme Court of Appeal in respect of USP and which was conditional upon the Thistle Trust's appeal failing.

The Thistle Trust contended that the liability for the capital gains tax lay with the individual beneficiaries in terms of the common law conduit principle, the provisions of section 25B of the IT Act and the proper application of par. 80(2) of the Eighth Schedule to the IT Act.

The Thistle Trust, relying on the common law conduit principle, contended that if a trust received an amount which it distributed to its beneficiaries within the same tax year, the amount was to be regarded as having accrued directly to the beneficiaries and not

the trust, placing tax liability on the person who ultimately received the benefits from the amount concerned.

The Thistle Trust, apart from the conduit principle, relied on the deeming provision in section 25B of the IT Act to argue that in terms of section 25B the capital gain of Zenprop was deemed to be the capital gain of the Thistle Trust when it was distributed to it and then deemed to be the capital gain of the beneficiaries when it was distributed further from the Thistle Trust to the beneficiaries.

The Thistle Trust also relied on par. 80(2) of the Eighth Schedule to argue that par. 80(2) entitled it not to be taxed on the relevant capital gains because par. 80(2) must be interpreted as an attempt to codify the conduit principle and thus, by application of the conduit principle, when a capital gain is attributed from Zenprop to its beneficiary, the Thistle Trust, which was itself a trust, the conduit was not blocked, but continued to allow that capital gain to be distributed from the Thistle Trust to its beneficiaries in whose hands it would be taxed as a capital gain.

SARS contended that section 25B did not apply to capital gains, only to other income that was relevant for income tax purposes and instead, section 26A and the Eighth Schedule to the IT Act should be interpreted to make clear that all matters relating to the calculation of the taxable capital gain of a trust were to be determined in accordance with the Eighth Schedule.

SARS pointed out that par. 80(2) contained its own codification of the conduit principle and it made clear that the conduit principle could not operate beyond the first beneficiary trust in a multi-tiered trust structure.

SARS, on the question of the imposition of USP, contended that the Thistle Trust did not have reasonable grounds for its reliance on its tax position and as it intentionally adopted this position, its 'error' could not be described as a *bona fide* inadvertent error and it should be held liable for the USP.

Hudge Chaskalson held the following:

<u>As to jurisdiction and leave to appeal</u>

(i) That the Thistle Trust's application for leave to appeal engaged this court's general jurisdiction in terms of section 167(3)(b)(ii) of the Constitution as the application raised arguable points of law of general public importance. The points of law raised concerned the proper interpretation of section 25B and par. 80(2) and the application of the common law conduit principle. As the Thistle

Trust submitted, these points of law were of general public importance because they would affect the capital gains tax liability of trusts in tiered trust structures in respect of all tax years up to 2021. They would also have implications for other trusts and their beneficiaries in cases that were affected by the application of the conduit principle.

(ii) That the Thistle Trust's proposed appeal would determine the outcome of a multi-million-rand tax dispute. The issues that it raised were of general public importance and transcended the interests of the parties to the dispute. They had implications for the tax liability of trusts and beneficiaries in countless other disputes.

(iii) That the arguments raised by the Thistle Trust were substantial. These arguments were upheld by the Tax Court before its decision was overturned by the Supreme Court of Appeal. With two competing decisions, it was accordingly clear that the interests of justice required leave to appeal to be granted.

As to the Thistle Trust's liability for capital gains tax

(iv) That the conduit principle had been adopted into our law from English common law and the first significant South African judgment to apply the conduit principle was Armstrong v CIR 10 SATC 1. In SIR v Rosen 32 SATC 249 the Appellate Division held that Armstrong did not merely interpret the relevant provisions of the IT Act but, rather, it established the conduit principle as a common law principle applicable to the taxation of trusts and beneficiaries where appropriate, albeit one that was always subject to a contrary intention in the proper construction of the revenue statute.

(v) That a review of the Commonwealth and South African cases shows that the conduit principle was developed to address two separate issues in the context of tax statutes that did not address these issues directly. The first issue concerned the identification of the taxpayer who was liable to taxation on particular income – was it to be the trustee or the beneficiary? In that context, the conduit principle was used as a mechanism to ensure that income of a particular nature was taxed in the hands of its true beneficial owner. The second issue was to protect legislative choices in respect of the favourable or prejudicial income tax treatment of particular categories of income.

(vi) That the South African and Commonwealth judgments used the conduit principle to answer questions of which taxpayer was to be taxed on particular

income and whether that income retained its tax privileged or tax prejudiced status only because the taxation statutes with which they were concerned did not address these issues directly. When a taxation statute addressed either of these issues directly, the case no longer became an exercise in applying the conduit principle. Instead, it became an exercise in giving effect to the direct legislative intention expressed in the statute.

(vii) That in South Africa, the Income Tax Act 129 of 1991 represented a watershed in relation to the conduit principle. The 1991 Act, for the first time, introduced into the IT Act provisions dealing specifically with the taxation of trusts. Since 1991, questions relating to the taxation of trusts and beneficiaries under the IT Act have accordingly become questions of the interpretation of the relevant provisions of the IT Act that deal directly with trusts and beneficiaries. Common law principles relating to the conduit principle may inform these questions of interpretation, particularly where the IT Act does not expressly regulate the respective tax treatment of trusts and beneficiaries. However, the exercise remains primarily one of statutory interpretation.

(viii) That the 1991 Act introduced various amendments into the IT Act dealing with the taxation of trusts including the insertion of section 25B into the IT Act to provide expressly for the application of the conduit principle in relation to the taxation of a 'trust fund.' The next major development in the amendment of the IT Act relevant to the application of the conduit principle took place in 2001 when capital gains tax was introduced by the Taxation Laws Amendment Act 5 of 2001 which inserted section 26A into the IT Act and introduced the Eighth Schedule to the IT Act to set out the manner in which a taxable capital gain was to be determined and in par. 80 specifically addressed the application of the conduit principle in relation to capital gains tax.

(ix) That SARS had argued that section 25B could not be applied to taxable capital gains because it was introduced at a time when those gains were not taxable. This argument was unpersuasive. At all times since capital gains became taxable, section 26A has made it clear that taxable capital gains formed part of taxable income. Accordingly, absent contrary indications in the IT Act, section 25B would have to be interpreted on the basis that capital gains are taxable income and fall within the phrase 'any amount' in section 25B.

(x) That, however, there are clear indications in the IT Act that the application of the conduit principle to the taxation of capital gains in the hands of trusts and

beneficiaries is governed not by section 25B, but by par. 80. Paragraph 80 is a provision of the Eighth Schedule that clearly goes beyond questions of quantification. It seeks to identify the taxpayer who is liable for capital gains tax on a capital gain realised by the disposal of an asset by a trust and distributed to a beneficiary in the same year of assessment in which the disposal took place and it must be interpreted accordingly.

(xi) That the Thistle Trust was correct that, given the wide meaning of the word 'determined' in the Eighth Schedule, the effect of par. 80(2) was that a capital gain was determined in the accounts of the Thistle Trust. However, the flaw in the Thistle Trust's argument was that par. 80(2) was framed so as to identify 'the trust' with reference to the fact that it was the trust that disposed of the asset, and not with reference to the fact that it was a trust in whose accounts the capital gain was determined. Recognising this problem, counsel for the Thistle Trust suggested that par. 80(2) should be read as though the phrase 'in respect of the disposal of an asset' was a parenthetical clause with commas before and after it. But there were no commas before or after these words in par. 80(2) and there were no indications in the IT Act that the relevant phrase should be read as a parenthetical clause. If a statute was not framed in a form that lends itself to the interpretation desired by a litigant, they cannot ask the court notionally to perform linguistic surgery on the statute by adding or removing commas until the desired interpretation is achieved.

(xii) That the Thistle Trust's strained interpretation was also to be avoided, because it was inconsistent with the apparent purpose of the 2008 amendment to par. 80(2), namely, to prevent the conduit principle from operating in relation to capital gains beyond the first beneficiary trust in a multi-tiered trust structure.

(xiii) That the 2008 amendment changed the introductory wording of the paragraph from 'where a capital gain arises in a trust' to 'where a capital gain is determined in respect of the disposal of an asset by a trust.' Prior to the 2008 amendment, through the operation of par. 80(2), the capital gain realised by the sale of assets by Zenprop and distributed to the Thistle Trust could be said to be a capital gain which, after distribution by Zenprop, 'arose' in the Thistle Trust. By sequential operation of par. 80(2), this capital gain would then have had to be disregarded for the purposes of calculating the aggregate capital gain of the Thistle Trust and taken into account for the purposes of calculating the aggregate capital gain of its beneficiaries.

(xiv) That, in other words, prior to the 2008 amendment, par. 80(2) provided for the conduit principle to apply through multi-tiered trusts all the way to the ultimate beneficiaries. As we have seen above, following the 2008 amendment, par. 80(2) prevented the conduit principle from operating beyond the first beneficiary trust in a multi-tiered trust structure. Therefore, on a linguistic analysis of the 2008 amendment, its clear purpose was to confine the operation of the conduit principle in this fashion. If the 2008 amendment was interpreted in the manner urged by the Thistle Trust, it is difficult to identify any change that the amendment made to the meaning of par. 80(2) or any other purpose served by the 2008 amendment.

(xv) That the purpose attributed above to the 2008 amendment was confirmed by the 2008 explanatory memorandum. It stated the following in respect of the amendment that was ultimately made to par. 80(2) with the enactment of the 2008 amendment:

> 'Some commentators have suggested that a capital gain arising under par. 80(2) can be attributed through multiple discretionary trusts. This view has not been accepted and the amendment clarifies this by referring to a capital gain determined in respect of the disposal of an asset by a trust instead of a capital gain arising in a trust.'

(xvi) That this court has frequently had regard to explanatory memoranda to bills in the process of identifying the purpose of a statute or an amendment to a statute. So too, has the Supreme Court of Appeal, including in numerous cases involving revenue statutes.

(xvii) That there was a limit to the weight that could be placed on an explanatory memorandum for the purposes of interpreting a statute. The rule of law dictated that the law should be certain and predictable so that individuals are able to organise their affairs around the law and individuals must have ready access to the law for that purpose. In order to be predictable, the law must first be accessible. If the meaning of the law depends entirely on historical research into what was and was not said in an explanatory memorandum issued decades earlier and not easily capable of identification and location, that would undermine accessibility of the law and will potentially undermine the rule of law.

(xviii) That taxation legislation represented a special category of laws in respect of which people proactively organise their affairs to conform to the predictable consequences of the law. It might therefore be thought that particular caution

should be applied before using explanatory memoranda to inform the interpretation of tax laws. However, both parties before us invoked explanatory memoranda in support of their competing interpretation arguments and the practice of using explanatory memoranda to identify the purpose of revenue statutes was well established. It was therefore appropriate to have regard to the 2008 explanatory memorandum to identify the purpose of the 2008 amendment.

(xix) That in summing up: the wording of par. 80(2) showed that the provision applied the conduit principle only to the first beneficiary trust in a multi-tiered trust structure. It was not reasonably possible to interpret par. 80(2) to allow the conduit principle to run through a multi-tiered trust structure to attribute liability for capital gains tax in respect of the disposal of an asset to a beneficiary beyond the first beneficiary of the trust that realised the capital gain by disposing of that asset. The legislative history of par. 80(2) and the 2008 memorandum both confirmed that par. 80(2) was amended into its present form for the purpose of preventing the conduit principle operating through multiple discretionary trusts in a tiered trust structure. Paragraph 80(2) must be interpreted accordingly.

(xx) That it was correct that the interpretation adopted by the court created a distinction between the operation of the conduit principle under par. 80(2) in relation to capital gains distributed through multi-tiered trust structures and the operation of the conduit principle under section 25B of the IT Act in relation to all other forms of income distributed through multi-tiered trust structures to the ultimate beneficiary that receives the income in the year of assessment.

(xxi) That the court took issue with the proposition that robust common sense required full application of the conduit principle to all situations. To the extent that the conduit principle rested on robust common sense, it did not assist the Thistle Trust at all. The Commonwealth and South African cases showed that the conduit principle was developed to address two separate concerns of ‘common sense’ in the context of tax statutes that did not address these issues directly. The first was a concern to subject the true beneficial owner of particular income to taxation on that income. The second was a concern to protect legislative choices in respect of the favourable or prejudicial income tax treatment of particular categories of income.

(xxii) That the present case did not involve any need to protect legislative choices in respect of the favourable tax treatment of particular types of income. The only legislative choice that appeared to be relevant in the present case was the legislative choice to tax the capital gains of inter vivos trusts at twice the rate of the capital gains of individuals. That legislative choice was one which, absent the provisions of par. 80(2), would have militated strongly against any application of the conduit principle to capital gains tax.

(xxiii) That, for the reasons given, the court was not persuaded by the second (minority) judgment to change its interpretation of par. 80(2) and hence the Thistle Trust's appeal had to fail. The dismissal of the Thistle Trust's appeal raised SARS' claim to USP and the conditional application for leave to cross-appeal.

<u>As to SARS' claim to USP</u>

(xxiv) That the conditional cross-appeal engaged the court's general jurisdiction. The phrase '*bona fide* inadvertent error' in section 222 of the TA Act was open to different plausible interpretations. As a result, the dispute over the correct interpretation raised an arguable point of law. This point of law was of obvious public importance, because it would affect how SARS and the courts approached the imposition of USP in thousands of future tax cases. It would also affect the attitude that SARS took to individual taxpayers who understate their income in even more cases that do not reach the level of disputes before the Tax Court.

(xxv) That notwithstanding the public importance of determining the proper interpretation of section 222, it is not in the interests of justice to grant leave to appeal. If this court was to hand down a judgment on the meaning of 'inadvertent error' in section 222, it will effectively have to do so sitting as the court of first and last instance in relation to this issue. The Tax Court did not reach the issue of penalties, because it upheld the Thistle Trust's case on the merits. The Supreme Court of Appeal did not reach the issue of penalties, because SARS did not argue the issue and was understood to have conceded the issue.

(xxvi) That it was undesirable for this court to have to determine a legal point of public importance in a matter where it had no reasoned judgment on the issue from the preceding courts. If SARS had a strong case in respect of its claim for penalties in this matter, it may nevertheless have been in the interests of justice

for this court to entertain that claim, but SARS had no sustainable case for penalties.

(xxvii) That SARS had pinned its case for the penalties which it claimed to item (iii), alternatively item (ii) of the table in section 223 of the TA Act. These were the categories of 'no reasonable grounds for 'tax position' taken' and 'reasonable care not taken in completing return.' SARS bore the onus of proving the facts that would bring the understatement of the Thistle Trust within either of these categories. It had no reasonable prospects of discharging this onus.

(xxviii) That in respect of item (iii), the tax position taken by the Thistle Trust in relation to the conduit principle was one taken on legal advice. It may have been a tax position that this court had found to be incorrect, but it cannot be said to be a tax position which the Thistle Trust had no reasonable grounds to take. The tax position was not just reasonable, it was a tax position that was upheld by the Tax Court in a reasoned judgment that engaged with the conduit principle and the relevant provisions of the IT Act. To his credit, counsel for SARS declined to submit that there were no reasonable grounds for the Tax Court to have reached the conclusion that it did.

(xxix) That in relation to item (ii), SARS argued that although the Thistle Trust was advised on its tax position, the advice that the Thistle Trust received pointed out that SARS held a contrary view. On this basis, SARS argued that if the Thistle Trust had taken reasonable care in completing its return, it would have ignored the advice given to it and followed the stated SARS position which that advice expressly considered and rejected. This argument was based on the proposition that no taxpayer can act reasonably on advice that differs from SARS' statements of its interpretation of tax legislation. The argument would elevate SARS to the status of an authority that could decree the only reasonable interpretations of tax legislation. It was an untenable argument.

(xxx) That it followed that SARS' USP claim will fail on simple factual grounds irrespective of how this court may determine the meaning of '*bona fide* inadvertent error'. In the circumstances it was not in the interests of justice for this court to sit as court of first and last instance to determine a legal issue that will have no bearing on the outcome of the appeal. Leave to appeal must therefore be refused in the conditional counter-application.

(xxxi) That, in regard to costs, in the present matter the Thistle Trust had advanced arguments of substance, even if they had not been accepted in this judgment.

One of the issues raised by the Thistle Trust was a constitutional issue relating to retrospectivity of statutes and the judgment of the Supreme Court of Appeal. The court had found it unnecessary to address the constitutional issue but did not suggest that the Thistle Trust had acted frivolously in raising it. In the circumstances the Thistle Trust should not be ordered to pay the costs of the appeal but SARS had to pay the costs of the cross-appeal.

The application for leave to appeal was granted.

The appeal was dismissed.

There was no order as to costs in the appeal.

The conditional application for leave to cross-appeal was dismissed.

SARS was ordered to pay the Thistle Trust's costs in the cross-appeal, including the costs of two counsel.

Judge Bilchitz held the following minority judgment:

(xxxii) That the majority judgment analysed the language of par. 80(2) of the Eighth Schedule of the IT Act and found that it, unambiguously, admitted of only one interpretation – that, in relation to capital gains tax, the conduit principle did not apply throughout a multi-tier trust structure and capital gains were taxable once distributed to a second-tier trust. The majority judgment reasons that this interpretation is supported by the text of the provision as well as an explanatory memorandum released by Parliament relating to the relevant amendments to the legislation in 2008. I, unfortunately, cannot agree with the approach my Colleague adopts to the interpretation of this paragraph. The text, purpose, context and presumptions of statutory interpretation require construing the provision to give full effect to the conduit principle such that capital gains are taxed in the hands of the ultimate beneficiaries.

(xxxiii) This case raises important questions surrounding the interpretation of fiscal legislation in the constitutional era. The second interpretation that I argue for is to be preferred in light of the interpretive approach adopted by our courts to statutory interpretation in the constitutional era – for this reason, I proceed as follows. First, I outline the key principles relating to statutory interpretation and emphasise the important requirement that, where there is ambiguity, statutes should be interpreted to preserve their constitutionality. Secondly, I indicate how this requirement interacts with the principles that this court has developed

in relation to the rule of law. In particular, I seek to show how statutory provisions should be interpreted, where reasonably possible to do so, to avoid rendering them arbitrary, or irrational – and, in a manner that discloses a legitimate purpose and that conforms with common sense. Thirdly, I seek to show how these principles interact with the *contra fiscum* rule in the constitutional era. Lastly, I apply these principles to par. 80(2) of the Eighth Schedule of the IT Act. I find that there are significant ambiguities in the drafting of the text of this paragraph and that the purpose and context largely support the second interpretation. Given the existence of two reasonably possible interpretations, the one I prefer is that interpretation which construes the provision in a manner that is rational and non-arbitrary – and, in accordance with the contra fiscum rule, in favour of the taxpayer.

(xxxiv) That where it was possible to do so, provisions in legislation should be interpreted so as to be rational and non-arbitrary. That requires legislation to be construed in a way that is consonant with a legitimate government purpose, and demonstrative of a nexus between the legislative means adopted and its purpose. Where there are two possible interpretations, preference should be given to an interpretation of legislation that renders provisions non-arbitrary and rational rather than one that simply upholds a naked exercise of legislative power.

(xxxv) That, in short, in the constitutional era, legislation should be interpreted to accord with the requirements that this court has articulated in relation to the rule of law. That too harmonises the constitutional imperatives with the well-known common law presumption that statutory law is not unjust, inequitable or unreasonable. This approach also accorded with what has become known as the contra fiscum rule (that legislation must be interpreted against the fiscus). The rule originated from the idea that legislation giving effect to taxation involved the exercise of significant power over individuals – as a result, just like in criminal matters, the Legislature has a duty to ensure that the law is clear and those subject to the law understand what is required of them. Where rules are ambiguous, they should be interpreted in favour of the taxpayer.

(xxxvi) That the reasoning related to the rule of law provides a strong foundation for the contra fiscum rule in the sphere of taxation which was a specific application of the general rule that all legislation imposing a burden upon the subject should, in the case of an ambiguity, be construed in favour of the subject. That

there was also no excuse for arbitrary rules in the realm of taxation. Whilst the Legislature no doubt wished to raise revenue, specific provisions and distinctions must clearly be capable of justification in realising a legitimate government purpose and being a non-arbitrary and justifiable means to achieve that purpose.

(xxxvii) That I agree with my colleague Chaskalson AJ's analysis that, in the context of capital gains tax, par. 80(2) of the Eighth Schedule (as it read between 2014 and 2016) is the applicable provision to determine in whose hands a capital gain must be taxed. The question then becomes whether par. 80(2) is clear and no interpretation other than the one my colleague arrives at is reasonably possible. In my view there is significant ambiguity in par. 80(2) when construed in light of the applicable principles and how it applies to multi-tier trust structures. The ambiguity is borne out by the differences between SARS and the legal opinions of senior tax advisors relied on by the Thistle Trust as well as academic commentary on the provision which is divided on its interpretation and implications.

(xxxviii) That the difficulty that has arisen in this case concerns the application of the conduit principle in the context of multi-tier trust structures. The Thistle Trust contends that intervening trusts remain conduits so long as distributions to beneficiaries happen in the same tax year as the capital gain arrives in the account of the intervening trust. SARS, however, contends that the conduit is effectively blocked at the first beneficiary to whom the capital gain is distributed – in the case of a multi-tier trust structure, that would render the second-tier trust liable for taxation on capital gains received and their argument is rooted in a construction of the language of par. 80(2).

(xxxix) I do not consider par. 80(2) to be a model of clear legal drafting: difficulties in interpretation arise from the use of the passive voice, indefinite articles, lack of punctuation and complexity of the drafting. There are two reasonable constructions of the provision: the first, which is the holding of the majority judgment, requires the capital gain to be determined in the same trust that disposes of the asset. The trust referred to in the first line of the provision thus is the first-tier trust and it is the trust referred to in sub-par. (a). The beneficiary would on this reading be the second-tier trust. This interpretation focuses on reading the words 'disposal of an asset' together with 'by a trust', thus linking the capital gain with the disposal of the asset. The conduit pipe would be

blocked once a distribution is made to a second-tier trust and taxation on capital gains in multi-tier structures would take place in relation to second-tier trusts and not the ultimate beneficiaries.

(xl) In my view, a second plausible reading is to see the provision as applying to any trust – including a second-tier trust – which receives a capital gain from the disposal of an asset. If that trust distributes the capital gain to a beneficiary, it is only the ultimate beneficiary that is taxed. That reading requires linking the word 'determined' in the first line with 'by a trust' which can be any trust (first, second or third tier) which, in its financials, reports on such a capital gain. Put differently, 'determined' and 'by a trust' would link up thus: 'where a capital gain is determined…by a trust.' On this reading, the disposal does not have to be done by the same trust as the trust in which the gain is 'determined.' This reading appears to me to be plausible even without the insertion of parenthetical commas after the word 'determined' and the word 'asset.'

(xli) That par. 80 is a legislative encapsulation of the conduit principle. The whole point of the principle, as indicated above, is that an intermediary entity which distributes a gain to a beneficiary is a mere conduit and does not hold onto the amount it receives. If we attempt to apply SARS' statement to dividends such as in the cases of Armstrong and Rosen, a company obviously generated the dividends and distributed them to a second trust. If the logic of SARS is to be applied, then they should be taxed at the level of the second trust – but, the conduit principle, that the legislature has enshrined in statute, has recognised that they are taxed in the hands of the ultimate beneficiaries. There is no attempt to explain why the conduit should be blocked in relation to capital gains but not in relation to dividends or interest.

(xlii) That the interpretation I adopt utilises the rationales behind the conduit principle to understand the meaning of par. 80(2). As was common cause, the Legislature sought to give effect to the conduit principle through this provision. Given the rationale behind the principle is not to reify intervening trusts but to tax accruals in the hands of the ultimate beneficiaries, there is no good reason why the Legislature should be understood arbitrarily to restrict the operation of the principle to the second-tier trust in a multi-tier trust structure. If, as the majority judgment suggests, the Legislature wished to tax capital gains at the higher rate applicable to trusts, it is unclear why it should have legislatively incorporated the conduit principle at all. Indeed, had there been no intermediary

trust or the gain vested immediately in the beneficiaries were the Thistle Trust to have been constituted as a vesting trust, then the capital gain would have been taxed in the hands of the beneficiaries. If the Legislature had wished to tax capital gains at the higher rate applicable to trusts, then, it failed to adopt an efficient means to achieve that end. An interpretation of the provision rooted in such a purpose would thus fail to construe the provision in a manner that meets the constitutional standard of rationality.

(xliii) That, apart from purpose, the interpretive principles adopted by the courts require an examination of various contextual factors. Paragraph 80(2) appears in the context of the Eighth Schedule that deals with capital gains tax. It also co-exists with section 25B in the IT Act. The latter provision, it is common cause, applies the conduit principle to all other forms of income throughout a multi-tier trust structure. If we are to construe the provisions of the IT Act harmoniously, it would seem that section 25B and par. 80(2) should be interpreted to reinforce one another, rather than as enshrining different approaches to the conduit principle in the same statutory scheme. That is particularly the case given that there seems to be no good reason for interpreting par. 80(2) differently.

(xliv) That much was made by the majority judgment of the 2008 explanatory memorandum which, it was claimed, evinced a clear intention for the conduit to be stopped at the second-tier trust. It seems to me that limited weight should be placed on such a memorandum: the Legislature is duty-bound due by the requirements of the rule of law to ensure that the legislation it passes is as clear as possible and enables individuals to know how to order their affairs. The Legislature must, in the legislative instrument itself, say what it means and cannot cure an ambiguity by relying on an explanatory memorandum. This is particularly so where there is very limited treatment of this issue in an explanatory memorandum.

(xlv) That where an explanatory memorandum fails to articulate the rationale for a provision but simply asserts an interpretation of the statutory provision, the weight to be attached to such a document is very limited. Reference to such an explanatory memorandum alone cannot cure an ambiguity in the language of the provision itself and dislodge the need to interpret legislation in light of the applicable interpretive principles and in a manner so as to preserve its constitutionality.

(xlvi) That we are required to interpret legislation in such a way that ensures conformity with the Constitution and its foundational values. This court should be hesitant to adopt an interpretation of legislation that renders sections thereof arbitrary and involving distinctions that have no rational purpose. The contra fiscum rule required that fiscal legislation must be clear and, in the event of an ambiguity, interpreted to favour the tax subject. The court was thus duty bound in light of the interpretive principles I have discussed to prefer the interpretation that renders this legislation rational, non-arbitrary and in favour of the taxpayer. That interpretation is the second one I have explicated that does not arbitrarily restrict the operation of the conduit principle in the context of capital gains tax. I have sought to show why this interpretation is preferable when the text of par. 80(2) is construed in light of its statutory context and in relation to its manifest purpose.

(xlvii) That apart from the need to construe legislation in a non-arbitrary and rational manner, I believe this reasoning also conforms to the equities involved: given the lack of clarity of the legislation relating to multi-tier trust structures, it is unjust and inequitable retrospectively to impose a large tax bill on a second-tier trust. Indeed, expert tax advisors were unable to ascertain its true meaning (as was evident from the differing opinions in this case), and academics have noted the lack of clarity in this regard. The Tax Court and the Supreme Court of Appeal reached completely different conclusions about the applicable tax regime. In these circumstances, once again, it is equitable to adopt an interpretation in favour of the taxpayer.

(xlviii) That for these reasons, had I commanded the majority, I would have found in favour of the Thistle Trust and upheld the appeal. In these circumstances, there would be no need to decide the cross-appeal though I concur with the reasoning of my colleague Chaskalson AJ in that regard.

7.2. Coronation Investment Management SA (Pty) Ltd v C:SARS (87 SATC 150)[2]

CIMSA was Coronation Investment Management SA (Pty) Ltd (CIMSA) being a private company incorporated and registered in South Africa and a South African taxpayer.

[2] Constitutional Court

Coronation Global Fund Managers (Ireland) Limited (CGFM) was a foreign subsidiary of CIMSA.

Coronation Fund Managers Limited (Coronation) was a South African public company listed on the Johannesburg Stock Exchange (JSE). It had various subsidiaries, here and abroad, that operated in the sphere of fund management and investment management.

At all material times, CIMSA was a 100% subsidiary of Coronation and held all the shares as the holding company of Coronation Management Company (RF) (Pty) Limited (CMC) and Coronation Asset Management (Pty) Limited (CAM), both registered as tax residents in South Africa. CIMSA was also the 100% holding company of Coronation Fund Managers (Isle of Man) Limited, tax resident in the Isle of Man. The latter, which has since been deregistered, in turn, was the 100% owner of CGFM and Coronation International Limited (CIL), which were registered and tax resident in Ireland and the United Kingdom (UK) respectively. CIMSA explained that Ireland had been selected because of its highly regarded regulatory regime.

CGFM had been established in 1997 as a fund management company in Dublin, Ireland, to provide foreign investment opportunities in Irish collective investment funds (often referred to as unit trusts). CIMSA did so because Irish law did not permit it or any of its South African subsidiaries to manage Irish domiciled collective investment funds – it had to establish an Irish fund management company to do so.

It was common cause that tax considerations played no role in the decision to establish CGFM in Ireland.

The business model chosen by CIMSA in relation to CGFM in Ireland was an exact replica of the business model it used in relation to its fund management business in South Africa, where CMC was established as a fund manager (or ‘management company’) for a South African-domiciled collective investment fund. CMC did not conduct investment trading activities, because it was not licensed to perform investment trading that would require it to obtain a licence from South Africa’s Financial Services Board (FSB). It contracted with CAM which was a specialist investment manager (that was licensed under a different licensing regime) to conduct investment trading activities. Similarly, in Ireland, CGFM did not conduct investment trading activities because it was not licenced to do so. It contracted with CIL and CAM, which were specialist investment managers licensed to conduct investment trading activities within their respective jurisdictions.

On the evidence, the business model used by CIMSA in South Africa and Ireland was one used by most South African and Irish fund managers.

In its business plan, CGFM enumerated the managerial functions that it was licensed and required to perform – these were identified by the Central Bank of Ireland (CBI) as operational functions. They were decision-taking, monitoring compliance, risk management, monitoring of investment performance, financial control, monitoring of capital, internal audit and supervision of delegates. In 2011, the business plan was updated to add complaints handling and accounting policies and procedures as functions.

CGFM had a licence, issued by the CBI under the European Communities (Undertakings for Collective Investment in Transferable Securities) (UCITS) Regulations, that authorised it to manage various collective investment funds in Ireland, but the licence did not authorise CGFM to conduct investment management trading activities itself. CGFM was thus a UCITS fund management company. CGFM adopted as a business model in its business plan, which formed part of its licence application (as the licence in effect required it to do), the delegation of investment management trading activities to third parties. As stated, CGFM had delegated these functions to CAM and CIL in South Africa and the UK respectively. CAM and CIL were appropriately licensed and independently regulated specialist investment managers. They made all the decisions and performed all the tasks in respect of the collective investment funds in South Africa and the UK respectively, but under the supervision of CGFM. The latter established the investment objectives and policies in an offering document, the prospectus. The CBI reviewed the prospectus which CGFM would usually have shared with investors. CGFM retained overall responsibility for the prospectus.

In Dublin CGFM executed its business activities in terms of its licence through its directors who held quarterly meetings to set its business strategy, and through its executive team who managed the daily operations. Oversight and supervision of the investment management functions, outsourced to CAM and CIL, formed a significant part of CGFM's tasks.

The central issue before the court was whether the net income of CGFM, being a foreign subsidiary of CIMSA, was exempted from tax for the 2012 year of assessment in accordance with the provisions of section 9D of the Income Tax Act (the IT Act). The exemption would apply if, at that time, CGFM had met the requirements for constituting a 'foreign business establishment' (FBE) as defined in section 9D(9)(b). It was not in

issue that at that time CGFM was a ‘controlled foreign company’ of CIMSA, as defined in section 9D.

SARS in respect of the 2012 tax year, had assessed CIMSA’s tax liability to include in its income an amount equal to the entire ‘net income’ of CGFM. In doing so, SARS sought to apply section 9D(2) read with section 9D(2A) of the IT Act. In its Finalisation of Audit Letter, SARS concluded that CGFM did not meet the requirements for recognition as an FBE as the primary functions of its business had been outsourced.

The Tax Court in Cape Town (see ITC 1952 84 SATC 251) had held that CGFM was an FBE as defined and, accordingly, qualified for a tax exemption. It upheld CIMSA’s objection to the additional assessment.

The Tax Court distinguished between fund management and investment management and noted that CGFM was not an investment management company which it delegated outside of Ireland, but a fund management company which it conducted in Ireland.

The Tax Court thus set aside SARS’ additional assessment against CIMSA and ordered it to issue a reduced tax assessment, excluding therein any amount that was included in CIMSA’s income under section 9D of the IT Act pertaining to CGFM’s income.

The Tax Court granted SARS leave to appeal to the Supreme Court of Appeal.

The Supreme Court of Appeal (see C:SARS v Coronation Investment Management SA (Pty) Ltd 85 SATC 413) upheld the appeal and disagreed with the Tax Court in respect of the question as to whether CGFM had met the definition of an FBE as defined in the IT Act. It held that CGFM did not meet the requirements for an FBE exemption and, instead, the net income of CGFM was imputable to CIMSA for the 2012 tax year under section 9D(2). It thus upheld SARS’ appeal to the extent that it directed CIMSA to pay the income tax on CGFM’s income and the interest in terms of section 89(2) of the IT Act. However, the Supreme Court of Appeal found that SARS’ claim for understatement penalties and underestimation penalties had to fail.

The Supreme Court of Appeal understood the primary operations of CGFM’s business to be investment management which it conducted outside of Ireland and it reasoned that if these outsourced operations were central to the business of CGFM, because they go to the very nature of what its business did, then CGFM did not conduct its primary operations in Ireland.

CIMSA sought leave to appeal to the Constitutional Court against the judgment of the Supreme Court of Appeal. There was also an application by SARS for leave to cross-appeal against parts of the judgment and order of the Supreme Court of Appeal relating to the penalties.

CIMSA submitted, inter alia, that the Supreme Court of Appeal had erred in its interpretation of the FBE definition. It drew a distinction between what it termed the Supreme Court of Appeal's 'notional-business interpretation' and its own 'actual-business interpretation.' The latter interpretation meant that the business of a controlled foreign company and the primary operations of that business must be determined by having regard to what the company in fact does. The Supreme Court of Appeal's interpretation, on the other hand, adopted the approach that the business of a controlled foreign company and the primary operations of that business must be determined by having regard to what the company could in theory perform and not what it actually does.

SARS submitted, inter alia, that CGFM had outsourced all its core functions for which it was licensed as a management company, including its primary function of investment management, to offshore entities – CAM and CIL.

SARS contended that the proviso to the FBE definition expressly permitted outsourcing of various functions in relation to the location permanence and the economic substance of a controlled foreign company to other structures provided that the requirements of the proviso were met and contended further that CGFM did not meet the requirements of the FBE definition.

Judge Majiedt held the following:

<u>As to jurisdiction and leave to appeal</u>

(i) That this matter engaged the jurisdiction of the Constitutional Court. The fundamental enquiry was this: what was the proper interpretation of 'the business of that controlled foreign company' and 'the primary operations of that business' as they appeared in section 9D of the IT Act for purposes of applying the FBE exemption? That was a question of law. In the present instance, the interpretation of these key concepts in the statute was a question of law as it involved forming a view on the meaning of section 9D of the IT Act.

(ii) That this was a question that transcended the interests of the parties and was of general public importance. It had an impact on all South African resident companies which held controlled foreign companies and which relied on the

existence of an FBE to avoid being subjected to tax on an amount equal to the controlled foreign company's net income under section 9D of the IT Act. The interests of justice required that leave be granted so that certainty regarding a question of significant importance to the South African economy could be attained in light of the diverging conclusions of the Tax Court and the Supreme Court of Appeal.

As to the merits

(iii) That the central enquiry concerned whether CGFM's business activities in Dublin during the 2012 year of assessment had the requisite economic substance envisaged in section 9D of the IT Act. Before answering that question, it was useful for the contextual background to understand the rationale behind the enactment of section 9D. Section 9D did not seek to subject a foreign company to South African tax. It subjected the South African holding company or shareholders of a controlled foreign company to tax on an amount equal to the net income of that controlled foreign company.

(iv) That section 9D of the IT Act was an anti-avoidance provision that was introduced by the Revenue Laws Amendment Act 59 of 2000. That section was introduced to deal with the taxation of South African taxpayers on their income earned abroad, particularly income earned by South African owned foreign corporate entities. In respect of foreign-earned company income, the section sought to strike a balance between the opposing paradigms of pure anti-deferral (warranting complete taxation) and international competitiveness (warranting exemption). It did so by favouring international competitiveness where the income emanated from active operations abroad.

(v) That the Explanatory Memorandum explained that section 9D was enacted as an anti-avoidance provision with a general objective to deter South Africans from moving tainted forms of taxable income beyond South Africa's taxing jurisdiction by investing through a controlled foreign company. The section further had as its purpose to permit South African multinationals to establish corporate entities abroad in a way that would enable them to compete there. Its aim was to strike a balance between offshore competitiveness and protecting the South African tax base.

(vi) That key to section 9D was competitiveness abroad for controlled foreign companies and the means of achieving that without jeopardising the South African tax base was the FBE exemption. Active income of controlled foreign

companies was exempt from tax under section 9D(9) of the IT Act in order to ensure that foreign businesses remained competitive with local businesses in the foreign country from a tax point of view. The Treasury Explanation required that 'the location of the business establishment must additionally contain further substance.' That 'economic substance' must be demonstrated in terms of operations and business purpose.

(vii) That CGFM had been established in Ireland as a fund manager, and not an investment manager. The function of investment trading was delegated (or 'outsourced' as the Supreme Court of Appeal phrased it), as CGFM was legally entitled to do. The undisputed evidence showed that this business model was also common commercial practice in Ireland and other fund domiciles. In terms of that delegation model, a fund management company establishes a highly specialised business to hold and maintain a licence to perform fund management which included the supervision and oversight of services provided by third parties on a delegated basis. The trust deeds of the collective investment funds in respect of which CGFM fulfilled the role of fund manager also recognised the delegation of the investment management trading activities to third parties, the specialised investment managers.

(viii) That SARS had misconceived the distinction between fund management and investment management and that was a fundamental misconception in respect of the central issue in the case and the Supreme Court of Appeal had committed the same error, leading to its conclusions with which, for the reasons that follow, the present court disagreed.

(ix) That a good place to start was the distinction between fund management and investment management trading, also called here investment management in the narrow sense to emphasise the distinction. In sum, managing a collective investment fund involved the governance of and ultimate responsibility for all regulatory, legal and other investor-related aspects of a collective investment fund. That entailed administration of the fund, trusteeship or custodianship, the management of investments and distribution or marketing. CGFM did all of this as a fund manager under the auspices and control of the regulatory authority, the CBI. This was 'investment management in the wide sense' – the oversight and setting of policies, mandate and restrictions for investments. CGFM's responsibilities arose from the regulatory responsibility to the CBI to comply

with laws and regulations which apply to its business and to the Irish regulatory authorities.

(x) That investment trading, on the other hand, entailed professionally and expertly allocating the funds invested in a collective investment fund. These allocations were made strictly within the parameters, policies, mandate and limits set out in the prospectus issued by the fund manager. Thus, CAM and CIL, as delegates of CGFM, would elect which assets to buy, hold or sell on behalf of the collective investment fund. They would do so subject to the policies, mandate and restrictions imposed by CGFM as the fund manager. This was 'investment management' in the narrow sense – the actual trading of investments.

(xi) That the distinction can be explained in a different way – fund management in the present instance included investment management in the wide sense, but not in the narrow sense. CGFM performed the former and not the latter – that had been delegated to CAM and CIL. Numerous features pointed to what CGFM's core business as a fund manager entailed and conclusively proved that this core business did not extend to investment trading activities.

(xii) That, in summary, these three features, the licence conditions, prudential considerations and the uncontested evidence, compellingly showed that at all material times CGFM had conducted the business of a fund manager. It performed the core functions of a fund manager, including the management, oversight and supervision of the delegated investment management trading activities. These features also overwhelmingly pointed to CGFM's primary operations being that of a quintessential fund manager operating in terms of a delegation business model. That was in accordance with the overwhelming majority of Irish fund managers and, for that matter, in other similar fund management domiciles, like South Africa. It was also in accordance with the business model used by CIMSA within South Africa.

(xiii) That, moreover, the evidence clearly showed that the performance of investment trading activities was not the main source of CGFM's income. In terms of the prospectus of the relevant collective investment fund (or unit trust) CGFM earned its fees as a percentage based on the market value of that fund's assets. The confidence that the investors have in CGFM as the regulated fund manager and the responsible execution of its tasks like administration and the

oversight of the allocation of investor funds as per the prospectus, provide the basis for CGFM to earn the fees that it does.

(xiv) That, to sum up, in accordance with its business plan, presented as part of its licence application, CGFM employed a delegated business model through which it would conduct specified fund management functions, and would delegate investment management trading activities (which it is not authorised to do by its licence) to competent third parties, CAM and CIL, while retaining overall supervision of and responsibility to the regulator for those functions. CGFM performed a number of core management functions under its licence, including the supervision of delegates like CAM and CIL as investment managers. Its day-to-day operations from its Dublin office in pursuit of these management functions met the 'economic substance' requirements of the FBE definition, namely that the company must have a fixed place of business which is suitably staffed and equipped to conduct the primary operations of its business – the provision of fund management in accordance with the delegation model.

(xv) That, for these reasons, the Tax Court was correct in holding that CGFM qualified for a tax exemption and that SARS must issue a reduced tax assessment, excluding in it any amount that was included in CIMSA's income under section 9D of the IT Act pertaining to CGFM's income. What bore consideration next were the flaws in the reasoning and ultimate outcome of the Supreme Court of Appeal.

(xvi) That, for the reasons stated, the Supreme Court of Appeal had misconceived CGFM's actual business as a fund manager. Instead of determining what CGFM's business actually was, the court examined CGFM's licence and the delegation provisions under the UCITS Regulations. In adopting this 'notional business' approach, the Supreme Court of Appeal had erred and it had failed to draw the important distinction between investment management in its wide sense and investment management trading, the narrower concept.

(xvii) That the ultimate effect of the Supreme Court of Appeal's erroneous 'notional business' approach was that CGFM's primary business was that which it calculatedly chose not to do, did not apply to do and by law was not able to do, namely investment management trading. The fallacy of that reasoning was self-evident. It was inconceivable that the business of a controlled foreign company envisaged in section 9D was everything that the controlled foreign company

could do in theory and notionally do in pursuing a commercial endeavour, even if that company did not actually do it.

(xviii) That the approach of the Supreme Court of Appeal led to insensible and unbusinesslike results that did not achieve section 9D's objects, nor did it suppress the mischief at which the section was directed. CGFM had to set up offshore, due to the legal constraints of performing fund management in respect of Irish collective funds outside Ireland – thus the income was not diversionary. This was not income derived from royalties, dividends or interest – so it was not passive income and it was certainly not mobile income derived from a shell business with a post-box. The company was adequately staffed to perform the functions which it sought to do. The fact that the separation of fund management and investment trading was standard practice in the industry fortified the view that CIMSA's contentions in respect of CGFM as a qualifying FBE were sound. CGFM's fund management business plainly had the requisite economic substance.

(xix) That apart from the fact that the approach adopted by the Supreme Court of Appeal was legally and factually unsustainable, it did not make commercial sense at all. It effectively meant that, on this interpretation of what 'business' and 'primary operations' of that business meant, there was only a single, ideal notional concept of what a business entailed. There was no scope at all for delegation that trenches on the core functions of the ideal notional 'business' – the insurmountable strictures imposed by that narrow approach in setting up an FBE were self-evident. Requiring South African companies to set up an FBE within this anti-competitive limitation was illogical, did not make business sense and undermined the objects of section 9D. It would inadvertently discourage legitimate business practices that contributed to the efficiency and competitiveness of South African companies on a global stage.

(xx) That the FBE definition was not an anti-outsourcing enactment, as the Supreme Court of Appeal appeared to approach it. Instead, it aimed to ensure that an offshore business, regardless of its chosen business model, had economic substance in that foreign country and was not merely an illusory or 'paper' business and its objects were to ensure that the offshore company remained competitive with its foreign rivals.

(xxi) That, accordingly, CGFM met all the requirements of an FBE in terms of section 9D of the IT Act. Its net income ought to have been exempted from tax for the

2012 year of assessment and the appeal must succeed and it was thus not necessary to deal with the cross-appeal. Costs had to follow the outcome.

Appeal upheld.

Respondent to pay the costs, including the costs of two counsel.

7.3. C:SARS v J Company (87 SATC 176)[3]

Applicant, being SARS, had, on 4 September 2018, addressed a letter to the taxpayer, requesting it, in terms of section 46 of the TA Act, to provide copies of specified relevant material to SARS within 21 business days from the date of the letter.

The aforementioned letter requested copies of the taxpayer company's 2017 and 2018 annual financial statements and asked the taxpayer to explain the nature of each amount comprising the sales and other expenses reflected in the ITR 14 returns filed by the taxpayer in respect of its 2017 and 2018 years of assessment. It also requested supporting documentation of whatever nature that referred to or was related to any such amount, including but not limited to any invoice, legal agreement or related documentation, payment advice, internal or external memorandum or correspondence of any nature, including emails.

The taxpayer responded to the request in a letter dated 28 September 2018 and attached the requested annual financial statements to its response. It also annexed an income statement analysis for the 2017 year of assessment, consisting of some 21 items and a similar income statement analysis in respect of the 2018 year of assessment, consisting of some 44 items.

However, both schedules, whilst reflecting each item of income and expenditure, omitted the identity of the supplier or recipient of the services to which each item related. Supporting invoices relating to the income statement analysis schedules were attached but these invoices were heavily redacted. For instance, on some invoices, the identities of the debtors were redacted, as were the nature of the services rendered, including their VAT numbers.

Redacted documents were likewise attached to the income statement analysis schedule for 2018. The redactions affected eight invoices for advisory fees and various expenses incurred for professional services rendered in relation to the instructing of

[3] Western Cape Division, Cape Town

attorneys and a consulting service. Similarly, the identity of the attorney dealing with the matter was redacted, as was the subject matter of the professional services rendered and, in some instances, the attorney's bank details were also redacted.

There were some complete invoices without redaction, whilst in others, the name of the client was retained, however the nature of the services rendered, the invoice number, their reference details, as well as their bank details, were redacted.

The taxpayer did not explain the reason for the redactions but merely stated, inter alia, that it noted that it 'had not been notified of any audit by SARS and would therefore technically speaking not have been obliged to respond to the Request at this time.'

Various correspondence ensued between the parties wherein SARS contended that the taxpayer was non-compliant with section 46 of the TA Act and again requested it to provide it with the un-redacted copies of all documents within specified time limits.

The taxpayer stated that it was inter alia of the view that SARS' request for relevant material was only in respect of the taxpayer, and that the redacted information on the invoices supplied related solely to the identity of the taxpayer's clients and suppliers and the details of services provided by the taxpayer to its clients – in other words, parties other than the taxpayer, whilst the taxpayer was the sole taxpayer in respect of which the Request had been made.

SARS thereafter brought an application in the High Court in which it sought an order from the court compelling the taxpayer to comply with its obligation to respond fully to requests directed to it in terms of section 46 of the TA Act by furnishing to SARS all the information furnished to SARS by it in purported compliance with the section 46 notice in a form free of redaction or alteration.

SARS contended that in seeking the un-redacted documentation, it was lawfully exercising its powers in terms of section 46 of the TA Act. It required the taxpayer to produce certain material 'in respect of the taxpayer' and it argued that it did not limit the enquiry only to the tax affairs of the taxpayer and stated that it was entitled to require the taxpayer, or another person to submit relevant material.

SARS contended that the refusal of the taxpayer to comply with the section 46 notice was untenable and that the taxpayer was not entitled to withhold information or documentation from it, nor to unilaterally delete, and thereby conceal from SARS, information that appeared on the documentation.

SARS further argued that the section 46 notice was aimed at establishing the nature of the business undertaken by the taxpayer and the parties with whom it transacted such business. It contended that the ascertainment of that information was a matter that fell legitimately within section 46, especially in this case, since how a taxpayer interacts with its clients and service providers, and who those clients and service providers were, was an issue that ostensibly went to the administration of a tax Act in relation to a taxpayer. Thus, on a proper construction of section 46, a taxpayer cannot *mero motu* decide what information it will provide to SARS or what information was relevant for the administration of tax Acts.

SARS further contended that it was incorrect to say that a clarification or expansion of the target of the request to, in this instance, the taxpayer, its clients and service providers was impermissible as constituting a fishing expedition.

The taxpayer contended that it had provided the information as requested by SARS and had, on legal advice provided by its attorneys of record, redacted those parts of the documentation provided that fell outside the 'legitimate ambit of section 46.'

The taxpayer contended that SARS had failed to state on what basis it had purportedly formed an opinion that the requested information was 'foreseeably relevant for the administration of a tax Act'.

The taxpayer further contended that SARS' Requests amounted to nothing more than an open-ended fishing expedition in relation to its clients which exceeded the legitimate bounds of section 46 of the TA Act. It argued that the unspecific reference to 'clients and service providers' of the taxpayer did not meet the requirements of an 'objectively identifiable class of taxpayers.'

Judge Kusevitsky held the following:

(i) That, from a reading of section 46 of the TA Act, it was clear that a request for relevant material for purposes of administering a tax Act, related to a taxpayer, whether 'identified by name' or 'otherwise objectively identifiable.' Furthermore, if one had regard to the definition of 'administration of a tax Act' as provided for in section 3 of the TA Act, the powers granted to SARS in relation to the establishment of the identity of a person for purposes of determining liability for tax related to its powers as found in section 3(2)(c) of the TA Act. The administering of a tax Act in section 3 of the TA Act also inter alia included obtaining full information regarding anything that may affect the liability of a person for tax; the obligation of a person to pay for tax, to determine the liability

of a person to pay tax; to investigate whether a tax offence has been committed; to give effect of the obligation of South Africa to provide assistance under international tax agreements and to give effect to an international tax standard.

(ii) That the question thus that needed to be answered was whether SARS was entitled to demand, without more, the un-redacted information from the documents already provided and which, as contended by the taxpayer, did not relate to it as the taxpayer but rather to its clients and suppliers – and as a consequence – did not fall within the definition of 'relevant material.' Secondly, and in any event, if it is found to be material, then this court has to ascertain whether there has been non-compliance of the TA Act by SARS in determining an 'objectively identifiable class of taxpayers' as required in sections 46(1) and (2)(a) of the TA Act and as a result, whether the Request amounted to a so-called 'fishing expedition.'

(iii) That in regard to the general principle of interpretation: As was stated in C:SARS v Brown 78 SATC 255, there could be little doubt, having regard to the language used in the light of ordinary rules of grammar and syntax, the context in which the provision appeared and the apparent purpose of the Act, that the provisions of section 46 were peremptory. The explicit and unambiguous wording of the section simply did not allow for any other interpretation. This approach accorded with international tax practice and in this regard the court was referred to Australia and New Zealand Banking Group Ltd v Konza [2012] FCA 196 where it was held: 'It is…for the recipient to decide for himself, difficult though the task may be, which of the documents answer the description. If his decision is wrong, he exposes himself to prosecution and penalty. The existence of this hazard is not a sufficient basis for the conclusion that the section requires SARS to give notice in such terms as would enable the recipient on reading it and on examining the documents in his custody or control to determine whether they fall within the ambit of SARS' powers. To so hold would be to impose an impossible burden on SARS. In many, if not most cases, he will be unaware of the contents of the documents of which he seeks production.'

(iv) That, in a domestic context, SARS, referred to a passage from LAWSA which stated, inter alia: 'It would be impractical for SARS to provide reasons in every request for information as to why the relevant material requested is considered relevant…Information is the lifeblood of SARS' taxpayer audit activity, and the

whole rationale of taxation would break down with the burden of taxation falling on the diligent and honest taxpayers if SARS had no effective powers to obtain confidential information about taxpayers who may be negligent or dishonest.'

(v) That the Memorandum on the Objects of the then Tax Administration Laws Amendment Bill 2014 which set out the purpose of the definition of 'relevant material' that was in force at the time SARS issued the section 46 notice to the taxpayer in this matter, noted that the test of what was 'foreseeably relevant' followed the following broad grounds, being: Whether at the time of the request there was a reasonable possibility that the material was relevant to the purpose sought; Whether the required material, once provided, actually proved to be relevant was immaterial; An information request may not be declined in cases where a definitive determination of relevance of the material to an ongoing audit or investigation can only be made following receipt of the material; There need not be a clear and certain connection between the material and the purpose, but a rational possibility that the material will be relevant to the purpose and the approach is to order production first and allow a definite determination to occur later.

(vi) That if the above broad grounds are adopted, then the scope of uncertainty would be curtailed. The golden thread which emerged was that, in most cases, SARS did not know what information or documentation there was in order for it to fully discharge its function of assessing a taxpayer's tax liability. It therefore stood to reason that if SARS did not know, then it required a mechanism to be able to fulfil its constitutional mandate of fiscus collection in a manner that was open and transparent and within the bounds and scope of its power.

(vii) That there, however, also has to be a reciprocal obligation on the part of the taxpayer to play its part, since it could hardly be considered fair if a dutiful and law-abiding tax citizen is penalised for its compliance with the tax laws vis a vis aggressive tax planners with the sole purpose of evading tax laws or simply to avoid tax altogether. As contemplated in the Memorandum, it is accepted that information is the lifeblood of a revenue authority's taxpayer audit activity and the whole rationale of taxation would break down and the whole burden of taxation would fall on diligent and honest taxpayers if a revenue authority had no effective powers to obtain confidential information about taxpayers who may be negligent or dishonest.

(viii) That, with regard to the taxpayer's claim that SARS had failed to pass the second hurdle of identifying an 'objectively identifiable class of taxpayer', this aspect did not need to be considered by the court if it found that the taxpayer itself and identified by name, was obliged to provide information and documents in an un-redacted form of persons or entities which it dealt with and which pertained to it since this may impact on SARS' ability to properly assess the taxpayer's liability…given the fact that the majority of the redacted invoices related to clients and suppliers of the taxpayer who seem to be in the legal field, the court would find that there was sufficient information, notwithstanding the taxpayer's obstructive conduct in redacting the relevant information and concealing same from SARS, in order for the taxpayer to identify the class of taxpayers, i.e. the attorney and law firms, which forms the ambit of SARS' enquiry and to which the notice or request pertained.

(ix) That, ultimately, it is the plain language and context of section 46 of the TA Act which guides us to the conclusion that it is the opinion of SARS that is of relevance and not that of the taxpayer. The powers afforded to SARS under section 46 entitles a decision-maker to call for documents that it considers may be relevant. The fact that the taxpayer has deemed to conceal a large part of the information contained in the documents, in the court's view, only strengthens the perception that the attempted concealment might either be nefarious or not be bona fide, although the court made no pronouncements in this regard.

(x) That the nature of the taxpayer's business and the parties with whom it conducted business in order to generate taxable income and claim allowable deductions was a matter by its very nature relevant to the tax affairs of the company. It was not a pre-requisite or incumbent on SARS to first determine that the tax affairs of a taxpayer are not in order prior to making a request. That was not the purpose of section 46. Nothing prohibited SARS from broadening its scope of material or information sought, since the very purpose of section 46, which falls within the scope of Chapter 5, deals with the ambit of information gathering and the like. It would be an absurd proposition to restrict a fiscus gathering institution to one request in terms of section 46 for information sought and for it later to be precluded from issuing further notices in the event that information initially provided yields more questions or necessitates further investigation or inquiry.

(xi) That, in regard to the withholding of information relating to the taxpayer's attorney who rendered legal services to it, attorneys are first and foremost officers of the court and one can hardly imagine a situation where work done by them, in their professional capacity and unless declared privileged, would be rendered outside the reach of the taxing authority and not susceptible to scrutiny by either a legislative functionary, or a court of law for that matter. In any event, the taxpayer has not claimed a right to legal privilege as was the case in the matter of A Company v C:SARS 76 SATC 321.

(xii) That, accordingly, the taxpayer was ordered to provide SARS with the unredacted documents as referred to in para 1 of the notice of motion within 21 days of the date of the judgment.

Application upheld.

7.4. Avin Liebenberg Trust v C:SARS (87 SATC 222)

Avin Liebenberg Trust (the Trust) was an *inter vivos* discretionary trust.

The Trust's tax return for the 2012 tax period, in which a taxable capital gain was disclosed as nil, was assessed by the SARS on 31 January 2013.

SARS, on 6 March 2018, and based on certain tax audit findings, issued the Trust with an additional tax assessment in respect of the 2012 tax year of assessment, in terms of which a capital gain of R47 329 834 was included in the Trust's taxable income for that year.

The aforesaid additional assessment was in fact included in a 'finalisation of audit' letter from SARS advising the Trust of composite adjustments in respect of the tax period from 2010 to 2016.

The Trust, on 6 September 2018, objected to the aforesaid 2012 additional assessment 'only to the extent of the understatement penalty of R1 707 531 levied on the amount of R8 537 637.'

SARS, on 10 October 2018, disallowed the aforesaid objection, as well as objections relating to the additional assessments for the 2013 to 2015 tax years of assessment.

The Trust, on 9 November 2018, 'noted' an appeal to the Tax Court, as provided for in terms of section 107(1) of the Tax Administration Act ('TA Act'), against SARS' decision

to disallow the aforesaid objection. The appeal was stated to be in respect of all of the grounds of objection set out in the objection letter of 6 September 2018.

The Trust, on 28 June 2019, delivered a further letter of objection to the 2012 additional assessment, 'on the ground that the period of limitations for the issuance of an additional assessment had expired prior to 6 March 2018, having regard to the provisions of section 99(2)(a) of the TA Act.' The Trust was therefore of the view that the purported additional assessment dated 6 March 2018 was invalid. This latter objection was also disallowed by SARS on 4 September 2019 and on 18 September 2019 the Trust appealed to the Tax Court against this disallowance of the objection.

SARS, in its statement of grounds of assessment in terms of Rule 31 of the Rules promulgated under section 103 of the TA Act ('Tax Court Rules'), averred that the Trust had impermissibly raised further grounds of objection to the assessment in addition to disputing the imposition of the understatement penalty (raised in the 6 September 2018 objection letter) and the prescription issue raised by the Trust in the 28 June 2019 objection letter. The further ground of objection related to the so-called 'merits' or the 'capital' of the additional assessment in terms of which the Trust endeavoured to make out a case that it was not liable to pay tax on the additional income which took into account the alleged capital gain of R47 329 834.

Before the Tax Court this preliminary issue was argued as an interlocutory matter and, in that regard, the Tax Court was called upon to decide whether the Trust was entitled to raise an objection to the additional assessment on the ground that it was not liable to pay additional tax on the basis of taxable income, which included the aforesaid sum of R47 329 834.

These were 'new' grounds of appeal in that the Trust did not rely thereon in its objection to the disputed income tax assessment for its 2012 year of assessment, which objection was filed in accordance with the procedure set out in Chapter 9 of the TA Act, that being the procedure leading up to the underlying dispute between the parties being referred to the Tax Court in respect of the 2012 year of assessment.

The Tax Court (see ITC 1976 86 SATC 398 per Bam J) on 6 July 2023 found in favour of SARS on that aspect of the matter and, in the process, dismissed the Trust's application in terms of section 117(3) of the TA Act, read with Tax Court Rule 51(2), in which it sought inter alia an order directing that the Trust was entitled to rely, in respect of its 2012 year of assessment, on the grounds of appeal in effect relating to the 'merits' or the 'capital' of the additional assessment.

The Trust appealed against the aforesaid judgment and the order of the Tax Court to the Full Court of the Gauteng Division of the High Court.

In issue in this appeal was whether the Trust should be permitted to raise in its appeal the so-called 'new' grounds of appeal not raised in its objection letters. The aforesaid issue was to be decided against the factual backdrop of the matter and the facts, most of which were common cause.

It was common cause between the parties that in its objection letters the Trust, in relation to the 2012 additional assessment, raised objections only in respect of the understatement penalties and the fact that, according to them, SARS was time-barred from raising an additional assessment three years after the first assessment was issued.

Rule 32 of the Tax Court Rules governed what a taxpayer's Rule 32 statement must, and what it may, contain and this was the only pleading filed by a taxpayer in a Tax Court appeal, and it was filed after SARS had filed its Rule 31 statement of the grounds of assessment and opposing the appeal.

Rule 32(3) was amended with effect from 10 March 2023, namely after the launch of the interlocutory application but before the judgment in the court a quo. It was therefore appropriate to quote Rule 32(3) both prior to and subsequent to its amendment with effect from 10 March 2023.

Prior to its amendment with effect from 10 March 2023, Rule 32(3) provided as follows: 'The Trust may not include in the statement a ground of appeal that constituted a new ground of objection against a part or amount of the disputed assessment not objected to under rule 7.'

The amended Rule 32(3) now reads as follows: 'The Trust may include in the statement a new ground of appeal unless it constitutes a ground of objection against a part or amount of the disputed assessment not objected to under rule 7.'

Judge Adams held the following:

(i) That the amended Rule 32(3) found application in this matter. That was so for the simple reason that Rule 66(2) of the new Rules of the Tax Court effective from 10 March 2023 provided that: 'An interlocutory application or application in a procedural matter taken or instituted under the previous rules but not completed by the commencement date of these rules, must be continued and concluded under these rules as if taken or instituted under these rules.'

(ii) That when the Trust objected to the additional assessment made by SARS in respect of its 2012 year of assessment in accordance with Rule 7, its ground of objection was that the period of limitations for the issuance of assessments had expired in terms of section 99(1)(a) of the TA Act, and that the additional assessment made by SARS in respect of its 2012 year of assessment, in terms of which an amount of R47 329 834 was included in its taxable income as a 'taxable capital gain' in terms of section 26A of the Income Tax Act, as amended ('the Act'), was therefore invalid. A more colloquial way of expressing this was to say that the Trust's ground of objection was that its original assessment for the 2012 year of assessment had 'become prescribed' due to expiry of the relevant three-year period laid down in section 99(1)(a) of the TA Act.

(iii) That in its Rule 32 statement, the Trust relied on the new ground of appeal in relation to the 2012 year of assessment, which it considered it was entitled to do in terms of the previous Rule 32(3) of the Tax Court Rules. This was also done in the Trust's notice of appeal in terms of Rule 10(3).

(iv) That SARS' additional assessment in dispute in relation to the 2012 year of assessment was, and is, based on the very same factual and legal grounds as those relied on by SARS in relation to the disputed 2013 to 2016 additional assessments. In addition, SARS relied for the 2012 assessment on the ground that it was entitled to disregard prescription in terms of section 99(2)(a) of the TA Act, that being on the basis of fraud, misrepresentation or non-disclosure of material facts on the part of the Trust.

(v) That when the Trust delivered its Rule 32 statement in respect of all of the aforesaid appeals, it accentuated the fact that it relied on the new grounds of appeal in respect of the 2012 year of assessment. The new ground of appeal is the same as the grounds of appeal relied on in respect of the 2013 to 2016 years of assessment, which new ground will, if this appeal succeeds, be argued at the same hearing as the appeals in relation to the 2013 to 2016 years of assessment.

(vi) That in a Rule 33 statement of reply to the Rule 32 statement of the ground of appeal, SARS took issue with the Trust's reliance on the new grounds of appeal in respect of the 2012 year of assessment, maintaining that it was prohibited from doing so in terms of Rule 32(3) prior to its amendment on 10 March 2023. On this basis SARS contended in the Rule 33 statement, and in the

interlocutory application before the Tax Court, that the new ground was not in issue before the Tax Court in relation to the 2012 year of assessment.

(vii) That each of the additional assessments in dispute, namely those relating to the 2012, 2013, 2014, 2015 and 2016 years of assessment, concerned the taxation of a 'taxable capital gain' – a single, globular amount, one amount for each year of assessment – derived by the Trust due to its vested rights thereto, and distributed by the Trust in the same year of assessment to its discretionary beneficiaries.

(viii) That the main issue between the parties in the underlying appeal was whether, in accordance with the so-called 'conduit-pipe principle', the taxable capital gain in a single amount for each year of assessment is taxable in the hands of the Trust or whether it was taxable in the hands of the Trust's beneficiaries to whom it was distributed by the Trust during the same year of assessment as that in which it arose. In other words, so the contention on behalf of the Trust goes, the dispute was not as to the taxability of the taxable capital gain, as such, but rather as to the identity of the 'person' (as defined) in whose hands the gain is taxable. On SARS' version, the Trust was the person taxable thereon.

(ix) That in respect of the 2012 year of assessment, so the Trust's contention continued, the one and only amount of the taxable capital gain was the amount of R47 329 834, and, apart from the prescription issue, the issue was whether, on SARS' version, this amount ought to have been subjected to tax in the hands of the Trust, or whether it ought to have been taken into account by the Trust's beneficiaries to whom it was awarded and distributed by the Trust in the same year of assessment.

(x) That it was the case of the Trust that, when it objected to the 2012 additional assessment, it objected to the disputed part or specific amount of the assessment, that being the determination in terms of which a 'taxable capital gain' of R47 329 834 was included in its taxable income along with the concomitant tax liability arising therefrom. The Trust argued that there were in fact three parts or amounts assessed, namely: (1) the amount of R47 329 834, which determination is disputed by the Trust, and the new ground related exclusively to this amount; (2) an amount arising from the disposal of the Trust's own assets, in relation to which there was no dispute between the parties; and (3) the imposition of penalties and interest by SARS, which have been objected

to and appealed against separately. The only relevant determination in dispute, so the submissions on this aspect of the matter is concluded, is the inclusion of a taxable capital gain of R47 329 834 in the Trust's taxable income and the resulting tax thereon and the ground of the objection was that the period of limitations for the issuance of assessments had expired.

(xi) That the court agreed with the aforesaid submissions. The determination objected to was the inclusion in the Trust's taxable income of the amount of a 'taxable capital gain' of R47 329 834 and the tax liability arising therefrom. It was therefore the determination of this amount of a tax liability to which the Trust objected. The simple point was that the part of the disputed 2012 assessment objected to under Rule 7 – as contemplated in Rule 32(3) – was the determination in terms of which the disputed 'taxable capital gain' of R47 329 834 was included in the Trust's taxable income along with the resulting tax liability, and the basis for the objection, or the ground of objection, was prescription.

(xii) That, as submitted by the Trust, the additional assessment in dispute was 'the determination of the amount of a tax liability by way of assessment by SARS.' This necessarily involved the determination of both taxable income and the tax liability that resulted therefrom once the applicable rate of tax was applied. It therefore followed, in the court's view, that the Trust's objection was, necessarily, an objection to the amount of the taxable income, being the amount of R47 329 834, giving rise to the tax liability determined by SARS and, as a matter of course, the tax liability resulting therefrom.

(xiii) That, moreover, it followed that the amount of the disputed assessment objected to under Rule 7 – as contemplated in Rule 32(3) – was the amount of R47 329 834 determined by SARS as being the 'taxable capital gain' to be included in the Trust's taxable income and giving rise to the tax liability flowing therefrom. It was so, as argued by the Trust, that there was only one amount in dispute, that being the amount of R47 329 834 included in the Trust's taxable income giving rise to the tax liability flowing therefrom.

(xiv) That, in sum, the fact that the Trust objected to the inclusion of the said amount in its taxable income on the ground of 'prescription' did not mean that it did not object to the inclusion of the said amount in its taxable income. That was precisely what it objected to, albeit on the grounds of 'prescription.'

(xv) That the court therefore concluded that the new ground of appeal did not constitute a ground of objection against an amount of the disputed assessment not objected to under Rule 7, as contemplated in Rule 32(3).

(xvi) That the court did not accept the contention on behalf of SARS, which was accepted by the Tax Court, that the Trust did not object to the capital amount of R47 329 834 in respect of the 2012 year of assessment. Neither could the court accept the submission that the Trust did not raise 'an objection on the merits' for the 2012 tax year. This submission was clearly a reference to the 'conduit-pipe principle' not having been raised in relation to the capital amount. However, this did not mean that the objection based on prescription did not challenge the inclusion of the capital amount of R47 329 834 in the Trust's taxable income in the additional assessment.

(xvii) That Rule 32(3) made it perfectly clear that a taxpayer may rely on a new ground unless such ground constitutes a ground of objection against a part or amount of the disputed assessment not objected to under Rule 7. In the court's view it could not be said with any conviction that the new ground of objection, based on the 'conduit-pipe principle', constituted a ground of objection against a part or an amount not objected to under Rule 7. The simple point was that the new ground relied on by the Trust related to the same part (the capital gain) and the same amount (R47 329 834) of the disputed assessment objected to. The new ground was nothing more than an additional ground in support of the same part and the same amount of the disputed assessment objected to under Rule 7.

(xviii) That this conclusion accorded with what Keightley J held in ITC 1912 80 SATC 417 at para [36] and the court was furthermore bolstered in this conclusion by the findings of the Supreme Court of Appeal in C: SARS v Free State Development Corporation 86 SATC 289 at par. [40] and [47].

(xix) That, borrowing from Free State Development Corporation, supra if the Trust is not allowed the relief sought in the Tax Court, the true issue between the parties would not be ventilated – that being whether the Trust's taxable income for the 2012 tax year of assessment included the capital gain of R47 million. What is more is that a situation may arise in which SARS, contrary to its legal obligation, would levy taxes which are not payable in terms of the law.

(xx) That, in any event, on a proper interpretation and having regard to the plain wording of Rule 32(3), the Trust ought to be allowed to rely on the new grounds

in relation to the additional assessment for its 2012 year of assessment and for all these reasons, the appeal to the Full Court should succeed.

(xxi) That there was a further reason why the appeal should be upheld and that related to the ratio decidendi in the very recent judgment by the Constitutional Court in Capitec Bank Ltd v C: SARS 86 SATC 369 at par. [93] and [94] which was handed down after the date on which the appeal was heard by the Full Court. The principle iterated by this judgment was simply that a 'new' ground of objection should be allowed if not to do so could result in SARS exacting tax which was not due to it.

(xxii) That, as for costs, same should be awarded to the Trust for the simple reason that SARS, in refusing to accept that the Trust was entitled to rely on the new grounds of appeal, acted unreasonably.

Appeal upheld with costs.

7.5. ITC 1982 (87 SATC 255)

The taxpayer had set down a tax appeal for hearing in the Tax Court in which it sought an order that an additional income tax assessment be referred back to SARS for re-assessment on the grounds that the taxpayer was entitled to include certain items of expenditure disregarded by SARS in the calculation of an allowance claimed by the taxpayer in terms of section 24C of the Income Tax Act (the IT Act) and also that there was no basis for SARS to impose understatement penalties in terms of sections 221 and 223 of the Tax Administration Act (the TA Act) or levy interest in terms of section 89quat of IT Act.

The taxpayer, on 27 January 2023, had called upon SARS to make discovery in terms of rules 36(3) and (4) of the Tax Court Rules (the Rules) promulgated under section 103 of the TA Act within 20 days thereof and SARS duly complied and discovered certain documents requested.

The taxpayer then requested the delivery of other documents in possession of SARS that could be relevant to its original request and that had not been discovered and accordingly gave notice of further discovery and delivered a notice in terms of rule 36(6) of the Rules calling upon SARS to make <u>further and better discovery</u> ('the Rule 36(6) notice'), <u>but the said notice was not delivered within the period envisaged in Rule 36(6), i.e. being within 10 days of the original discovery</u>.

The taxpayer delivered the Rule 36(6) notice 96 days late without having sought SARS' agreement in terms of rule 4 of the Rules and did so without having approached the court in terms of rule 52 for condonation of the non-compliance with the period prescribed.

In terms of rule 36(6) the taxpayer was obliged to deliver a notice in terms of rule 36(6) within 10 days of the original discovery and thereafter the consent of SARS would have been required to extend the period under rule 4, or, upon the taxpayer securing an order from the court to extend the period subsequent to a successful application in terms of rule 52 for condonation.

SARS delivered a notice in terms of rule 30 of the Uniform Rules of Court read with rule 42 of the Rules in which it was recorded that the Rule 36(6) notice constituted an irregular step to the extent that it was delivered outside the prescribed period stipulated in Rule 36(6) of the Rules.

It was then agreed between the parties that the irregular step proceedings would be held in abeyance pending the final determination of an application for condonation by the taxpayer to the Tax Court in terms of rule 52, which application was made 134 days after the expiry of the 10-day period referred to in rule 36(6).

SARS opposed the condonation application on the grounds that the taxpayer had failed to adhere to the primary principle applicable to condonation applications in that it had failed to provide a full explanation for all periods of delay and all instances of non-compliance with the Rules.

SARS also contended that the taxpayer had failed to provide a detailed and accurate account of the nature of the documentation that it sought and the relevance of the documents sought to the matter at hand and had thus also failed to show prospects of success in the appeal as well as failing to show any prejudice should condonation not be granted.

The taxpayer contended that SARS had failed to make full and complete discovery and was thus in default of its obligation under rule 36(4) to make discovery of all documents relating to the material issues arising from the grounds of assessment and the opposition to the appeal.

Moreover, the taxpayer contended that the delay occurred because the discovered documents were extensive and complex and necessitated an exhaustive and careful examination by its counsel and legal team in order to discern the relevance and implications of the material within the context of the broader dispute. In addition, the

delay in the analysis of the existing discovery was exacerbated by the need for consultation with the taxpayer's liquidators and former employees.

Judge Ingrid Opperman held the following:

(i) That the court was not called upon to make a definitive finding on each and every document sought in the Rule 36(6) notice. The court must decide whether it should condone the late filing of the Rule 36(6) notice which would result in SARS being obliged to respond to such notice. If the documents were not relevant to the issues in dispute, what was sought to be achieved and this fed into the 'prospects of success' requirement in condonation applications which an applicant for condonation was obliged to address.

(ii) That the prospects of success in this case were whether, but for the lateness of the request, a court would, on a prima facie basis, have compelled SARS to provide a response to the Rule 36(6) notice. That being so, the court needed to be satisfied, not that all the documents were relevant and ought to have been discovered from the outset but rather, that there was a prospect, at a prima facie level, that the taxpayer was entitled to the documents sought and that a court will in the fullness of time, compel SARS to produce such documents or some of them.

(iii) That SARS has denied that every single document sought was relevant. That being so, in the court's view, it need find only that one single document (or category of document) is potentially relevant, on a prima facie basis, in order to conclude that the taxpayer had prospects of success.

(iv) That although the criticisms levelled against the lack of averments in the founding affidavit have merit, the taxpayer is saved by the fact that relevance is determined objectively with reference to the issues as distilled from the pleadings.

(v) That the facts underpinning the understatement penalties were disputed and one of the disputes in the appeal was whether SARS was correct in imposing an understatement penalty of 10% on the taxpayer in relation to the reduction of the allowance referred to in the case before the court and thus the taxpayer was entitled to the documents sought to test the correctness of the decision reached in this regard.

(vi) That, in respect of this first category of documents, the court was thus satisfied, on a prima facie basis, that they were relevant and that there would be a 'point'

to granting condonation as there appeared to be some prospect of success in respect of at least this category of document.

(vii) That in regard to the other factors that a court should have regard to in exercising its discretion in granting condonation, it examined the explanation for the delay by the taxpayer in giving notice in terms of Rule 36(6) and noted the voluminous and technical nature of the documents which could not be completed within the period prescribed in terms of the Rules and this complexity necessitated the time taken to arrive at a conclusive decision regarding the need for additional discovery as well as bearing in mind that instructions had to be taken from the liquidators of the taxpayer who did not have access to all the historical information.

(viii) That the taxpayer's account of the discovery process and the explanation behind the timing of the delivery of the Rule 36(6) notice, demonstrated that the delay was not unreasonable and that it was justified in the circumstances.

(ix) That, given the volume of documents, the complexity of the issues and the fact that instructions had to be obtained from the liquidators, the taxpayer could never have responsibly approached the matter and delivered the rule 36(6) notice within the very short period of ten days as envisaged in rule 36(6) and thus the taxpayer was always going to be out of time.

(x) That condonation was not there for the asking but had SARS simply condoned the late filing and had it filed its response in which it objected to the documents on the basis of relevance, the substance of the matter could have been dealt with at this hearing.

(xi) That on the facts before it the court could not conclude that the taxpayer was not bona fide and there was no factual basis to conclude that the taxpayer had intentionally flouted the Rules. The Rule 36(6) notice appeared to have been issued in good faith and was motivated at obtaining clarity as to the basis upon which SARS had issued the additional assessment so that it could properly prepare for the tax appeal.

(xii) That the fundamental consideration was whether it would be in the interests of justice to grant condonation to an applicant. It was manifestly in the interests of justice that relevant documents should be produced and SARS could point to no tangible prejudice were it obliged to respond to the Rule 36(6) notice which

the condonation currently sought was aimed at ensuring. If relevance was the issue, it could be raised. There could be no prejudice to SARS.

(xiii) That although the court was urged to compel the production of the documents sought, it declined to accept such invitation. SARS came to court to meet a condonation application, and to shift the goal posts to production of documents during the hearing was unjust.

(xiv) That, in regard to costs, these were reserved until after the issue of relevance was properly ventilated which was once a response to the Rule 36(6) notice was delivered.

Late delivery of the taxpayer's notice in terms of Rule 36(6) of the Rules was condoned.

7.6. ITC 1983 (87 SATC 1983)

The taxpayer university, back in 2009, had concluded two agreements with a Developer, a Head Lease and a Sub-Lease of land that it owned whereby it leased land to the Developer, which was then obliged to build a student residence on the land and the taxpayer would then lease the land back from the Developer in order to use the improvements as a residence for its students.

Under the Head Lease, the taxpayer leased property to the Developer for twenty years and the consideration for the lease of the property was twofold. The Developer would construct a student residence worth at least R84.5 million (defined as 'the Improvements'), and it would pay the taxpayer R25 000 (excl. VAT) in rent each year. The taxpayer was required to make an initial payment of R19.220 million three days after the construction, described as a 'contribution to the Improvements.'

The Sub-Lease then required the Developer to lease the property – with the residence it had built, back to the taxpayer for fifteen years. The taxpayer would pay the Developer an escalating rental starting at R877 340 in March 2011, and ending at R2 493 209 at the Sub-Lease's end in 2026 (both VAT inclusive). The taxpayer would also be responsible for interior maintenance and pay the Developer operating charges to maintain the exterior and provide security.

The relationship between the parties was a financing arrangement, i.e. the Developer made its profit on the construction of the residence under the Head Lease through the rental paid over fifteen years under the Sub-Lease and the taxpayer would be responsible for managing the Sub-Lease, which would require substantial expenditure

and it accepted that all expenditure under the Sub-Lease was for the provision of exempt supplies. By contrast, the taxpayer accepted that it incurred negligible expenditure to manage its obligations under the Head Lease.

The taxpayer, as a university, was an example of a vendor who provided both taxable and exempt supplies as its primary business was to provide education and related services to students and under section 12(h)(i) and (ii) of the Value-Added Tax Act (VAT Act) the supply of 'educational services' was an exempt supply as was the supply of board and lodging to students. However, it also conducted commercial research and made other taxable supplies.

The taxpayer consequently had to determine how much of the VAT on its inputs it was entitled to deduct from its VAT liability bearing in mind that section 17(1) of the VAT Act did not permit the deduction of input tax on goods and services acquired by the vendor for non-taxable supplies and VAT paid on goods and services to make 'exempt supplies' was not deductible.

Section 17(1) of the VAT Act empowered SARS to determine the 'ratio' of goods and services a vendor intended to use for taxable supplies as compared to other uses.

In 2011 Higher Education South Africa (HESA) approached SARS for a section 17 class ruling in terms of section 41B of the VAT Act for all universities, including the taxpayer. SARS granted the requested ruling (the VCR) which separated universities' research activities, allowing them to claim VAT inputs at different rates for different types of research.

For all other expenses, it created a formula for calculating the ratio at which universities could claim VAT input deductions and it then set a cap: no matter the outcome of the formula, universities cannot deduct more than 12.5% of the VAT that they spent on goods and services. The VCR was agreed between HESA and SARS.

The issue to be determined by the court in this application was how, if at all, the Head Lease, which was entered into in 2009 and before the taxpayer agreed to the VCR, affected the taxpayer's ability to claim VAT input deductions.

The taxpayer contended that its obligations under the Head Lease were taxable supplies and that it should be entitled to claim the VAT on those obligations as input tax deductions.

SARS contended that the agreement, i.e. the Head Lease and the Sub-Lease, as a whole, was for the purpose of providing the student residence – an exempt supply – and therefore the taxpayer was not entitled to any input tax deduction.

In addition to this central dispute, the taxpayer raised another complaint, i.e. was the 12.5% cap in the VCR lawful?

The taxpayer took the view that SARS could not impose caps on apportionment ratios under section 17(1) but only apply formulae or methodologies and had to live with the results.

SARS contended that the taxpayer had not properly pleaded its attack on the VCR and that there was, in any event, nothing wrong with the 12.5% cap which fairly reflected how universities operated.

The taxpayer, in 2019, had applied for a ruling under section 41B of the VAT Act on the ground that the VAT incurred in acquiring the supplies under the Head Lease should be included in the calculation of its apportionment, which would then exceed the 12.5% cap, which, in its view, SARS should allow.

The taxpayer in essence argued that its supply of the property to the Developer under the Head Lease was a taxable supply. The consideration was the annual rental, and the construction services. The Head Lease was a barter transaction – construction services for possession of the property. The rental that the taxpayer paid under the Sub-Lease reflected the market value of the improved property for both agreements and therefore the value for which it had to account for output tax for its supply under the Head Lease. The taxpayer acquired the leasehold improvements (the residence) not to provide accommodation to its students but to enable it to make the taxable supply to the Developer under the Sub-Lease. Accordingly, the VAT on the improvements, which was equal to the VAT on the rentals it paid under the Sub-Lease, must be accounted for as input tax and included in the apportionment formula under the VCR and as this would increase the ratio under the varied input formula above 12.5%, that cap should be lifted to cater for the taxpayer's special circumstances.

The taxpayer did not argue that the 12.5% cap was inherently unlawful and it did not challenge the legality of the VCR. It accepted it as a given but asked for an exemption in its special circumstances.

SARS decided not to grant the ruling requested by the taxpayer and the taxpayer unsuccessfully objected which then led to the taxpayer's appeal and so the dispute

found its way to the Tax Court where the relief sought by the taxpayer was to grant the ruling that it had sought in its initial section 41B application.

SARS' reasons for not granting the ruling were:

- The Head Lease and the Sub-Lease were intertwined transactions and their joint purpose was the provision of exempt supplies
- Even if the supplies under the Head Lease were taxable, including them would distort the apportionment ratio
- The supplies were capital expenditure not under a rental agreement and were therefore excluded by the VCR.

Throughout this process the dispute between the parties remained one primarily about whether and how the Head Lease should be factored into the taxpayer's section 17(1) apportionment ratio.

Judge Bishop held the following:

<u>As to the validity of the 12.5% cap in the SARS Ruling (VCR) applicable to all universities</u>

(i) That section 17(1) of the VAT Act empowered SARS to determine the 'ratio' of goods and services that a vendor intends to use for taxable compared to other uses. The question was not what percentage of the business, the turnover, or the profit was for taxable supplies, but what ratio of its inputs the vendor used to make its taxable versus non-taxable supplies. The ratio was the relationship that 'the intended use of such goods or services in the course of making taxable supplies bears to the total intended use of such goods or services.'

(ii) That section 17(1) allowed SARS to determine the ratio, and expressly permitted a class ruling under section 41B of the VAT Act. Section 17(1) did not dictate to SARS how it must calculate the ratio. It did not require it to use any particular formula or methodology and it plainly envisaged that the method will differ between vendors and between classes of vendors.

(iii) That, while the VCR, applicable to all universities, was a class ruling under section 41B, it remained possible for any taxpayer to request a separate, individual ruling if it believed that the application of the VCR was not 'fair and reasonable' and that is what the taxpayer did in this matter.

(iv) That the taxpayer, in its Heads of Argument, challenged not only the refusal by SARS to grant its separate ruling, but also the validity of the 12.5% cap. The taxpayer submitted that it was irrational and ultra vires for SARS to impose a cap on the apportionment ratio that universities could claim under section 17(1) and it also persisted with its arguments that the Head Lease should be factored into its ratio, which should be allowed to exceed 12.5%.

(v) That, in regard to the validity of the 12.5% cap, the first question was whether the 12.5% cap was lawful and this raised two distinct questions:

- Was the legality of the 12.5% cap properly put in issue in the pleadings?
- If it was, had the taxpayer laid a basis for reviewing and setting it aside?

(vi) That the relief sought by the taxpayer was inconsistent with a finding that the 12.5% cap was unlawful. The taxpayer's Ruling application had accepted the validity of the 12.5% cap, and it relied on it as a mechanism to calculate the apportionment formula. The Rule 32 statement refers back to the Ruling application to define the relief sought and the finding that the taxpayer now seeks – that the 12.5% cap is unlawful – is inconsistent with its own relief.

(vii) That the 12.5% cap was contained in the VCR and the taxpayer never asked for a finding that the VCR itself was in any way unlawful. Its application and its appeal were always structured as a request for a departure from the VCR, the validity of which was otherwise assumed. It is an ordinary rule of pleading that if you wish to challenge the validity of an administrative act, you must identify the decision you are attacking, the facts upon which the cause of action is based, and the legal basis for the review.

(viii) That despite alleging that the 12.5% cap was 'arbitrary' and 'ultra vires' the taxpayer never sought an order that it should be declared unlawful. The relief it did seek assumed its validity.

(ix) That the Ruling application was the foundation of the dispute. It may be that the taxpayer was entitled to depart from the Ruling application in its objection or its Rule 32 statement but then it must do so expressly so as to alert SARS that it was making a different case, and challenging a different, additional decision. It did not do so.

(x) That, moreover, the result was that SARS had not properly defended the 12.5% cap because it was only placed on notice that it was required to do so when

the taxpayer submitted its heads of argument. That was prejudice. It would be unfair to decide the issue when SARS had not been properly alerted to the challenge.

(xi) That, in conclusion, it was not open to the taxpayer to now seek to attack the 12.5% cap as being inherently ultra vires. SARS was denied a fair opportunity to defend it, and this court did not have all the information before it to decide the question. Nonetheless, in case the court was wrong on that issue, it considered whether the 12.5% cap was permitted by section 17(1) of the VAT Act.

(xii) That there was nothing in section 17(1) that stated that SARS must use a formula and cannot specify a percentage. Nor was there any reason to interpret 'ratio' to mean 'formula'. The court agreed with SARS that it should have the flexibility to use formulae, methodologies, or directly impose ratios. What will be appropriate will depend on the nature of the vendor and its business. As long as the outcome reflects the relationship of the vendor's use of taxable and mixed supplies, it is permissible. Interpreting section 17(1) to limit SARS' discretion to calculate apportionment did not serve any identifiable purpose of the provision.

(xiii) That, in any event, any formula that SARS adopted under section 17(1) must ultimately produce a percentage or a ratio. The formula is the means to the end. But the end will always be a ratio, not a formula and that is the case here. SARS was entitled by section 17(1) to determine that ratio in any manner that reflected 'the intended use of such goods or services in the course of making taxable supplies bears to the total intended use of such goods or services.' That is what it did here – the ratio of 12.5% was the outcome of the method it used to investigate universities, as described in the evidence.

(xiv) That setting the cap at 12.5% was anything but arbitrary. It was based on detailed study and agreement, including with the taxpayer. It was set at a level that reflected the actual practice of universities. Relying blindly on a formula without considering whether that formula produced results that aligned with practice would be far more arbitrary than the course that SARS followed.

(xv) That it was important to remember what was at issue here. What SARS was trying to figure out was how much of a university's running costs are being used for exempt supplies, and how much for taxable supplies. The ratio determines what percentage of input tax it can deduct on all the taxable goods and services

it uses in a year. A high value transaction that does not meaningfully alter the university's overheads should not entitle it to claim a higher apportionment. It would effectively permit it to deduct input VAT it used to make exempt supplies.

(xvi) That, in sum, the taxpayer's attack on the 12.5% cap was bad on its merits and even if it had pleaded it properly, the court would still have rejected it.

As to the deductibility of the input VAT on the taxpayer's supplies under the Head Lease

(xvii) That the taxpayer sought to treat the two agreements as separate agreements with separate VAT consequences. It argued that the Head Lease was, in effect, a barter transaction and the court should close its eyes to the Sub-Lease and analyse the VAT consequences of the Head Lease purely on its own terms.

(xviii) That the facts in C:SARS v Respublica (Pty) Ltd 81 SATC 175, while they also concerned student residences, were quite different and fell under the exception contemplated in Respublica, supra, i.e. 'when assessing the VAT consequences of a particular contractual arrangement, the court should, at least normally, characterise the relationship by reference to the contracts and then consider whether that characterisation is vitiated by [any relevant] facts.'

(xix) That the facts here were that the Head Lease and the Sub-Lease were, in truth, a single commercial arrangement. Commercially, the purpose of the construction the Developer trades as consideration for possession of the land under the Head Lease was to enable it to perform under the Sub-Lease. It recoups the costs of construction only because of the rental it will receive under the Sub-Lease. The Sub-Lease rentals were set in order to ensure that the Developer profited from its construction of the Residence. Without the two going together, the relationship would make no commercial sense.

(xx) That these were not two separate commercial agreements. They were a single commercial arrangement divided into two contracts. The provision of the leasehold improvements served no separate purpose. They were never intended for any purpose other than supplying a residence. The consequence was that the leasehold improvements were not acquired 'for the purpose of consumption, use or supply in the course of making taxable supplies.' They were acquired for the purpose of providing student accommodation. That is an exempt supply. The VAT that the taxpayer pays to obtain those supplies was not deductible as input tax.

(xxi) That this case was very different from Respublica, supra. There are only two parties in both agreements – the taxpayer and the Developer. In Respublica the lessor sought to rely on the relationship between the TUT and the students, with whom it had no relationship. It was in that context that the Supreme Court of Appeal held Respublica to its actual agreement. The case also did not concern the question of whether the supplies were made for taxable or exempt supplies.

(xxii) That this was not a case of the court improperly peering behind the terms of the parties' contract. To the contrary, the court was taking the parties' contracts seriously. Those contracts, on their own terms, show that the purpose of all the taxpayer's expenditure under both agreements was solely to provide accommodation to its students. That was an exempt supply, for which it was not entitled to an input tax deduction and that on its own was enough to dismiss the taxpayer's appeal.

(xxiii) That, accordingly, the taxpayer's attempt to separate the Head Lease from the Sub-Lease was artificial. They were a single, composite agreement which, from the taxpayer's perspective, had a single purpose – providing a residence. That was an exempt supply. Anyway, the Head Lease did not alter how the taxpayer used the goods and services that it acquired throughout the year. Even if the Head Lease could be separated from the Sub-Lease to manufacture a taxable supply, the taxpayer was not entitled to include it in the calculation of its apportionment ratio.

Appeal dismissed.

There was no order as to costs.

7.7. Pather v C:SARS (87 SATC 197)

During 2017 the Applicant, Ms Pather, received a payment of R21.5 million into her Standard Bank account from her husband, Mr Pather, who was a director of Impulse Trading International (Pty) Ltd (Impulse). It would appear that the amount of R21.5 million came from Mr Pather's alleged loan account in Impulse, but SARS disputed the existence of the loan account.

It was common cause that the aforementioned funds were used to purchase a property which was duly registered to Ms Pather at the deeds office. It was clear that the payments made to Ms Pather had originated from Impulse.

It was common cause that Mr and Mrs Pather were married, but were divorced on 20 September 2000.

Ms Pather explained that she had accepted all such funds as alimony, which had been due and payable to her and based on Mr Pather's word. She also contended that these payments were funded from Mr Pather's loan account in Impulse. Pursuant to the aforesaid payments, Ms Pather sold her house which she owned at the time and proceeded to purchase the property to which SARS then wanted to lay claim.

On Ms Pather's version, she was an innocent recipient of the aforementioned funds and when she acquired the property her former husband took up residence in the garden cottage and she received an income from him in respect of his living there.

SARS treated the aforesaid with some suspicion and regard must be had to the following facts: A certain Mr Koko who was employed by Eskom and was a former CEO was alleged to have assisted Mr Pather in obtaining several contracts in the name of Impulse and it earned massive amounts from contracts awarded by Eskom. It was also reported that Mr Koko's stepdaughter, Ms Choma, was a director, shareholder and beneficiary of Impulse and that, during the period May 2016 to April 2017, Impulse was awarded multi-million rand Eskom contracts and during this period Koko was the head of generation at Eskom and later its interim CEO.

During the period when these contracts were awarded to Impulse, Mr Koko had not declared Ms Choma's directorship in Impulse and the media had started reporting on the issue and this was before any payments were made to Ms Pather by Mr Pather from his alleged loan account in Impulse.

As far as the timing was concerned, SARS submitted that the payments to Ms Pather commenced two months after the media had reported on the relationship between Mr Koko and Impulse and not long after the SARS audits had commenced.

During the period 14 September 2018 to 30 September 2019 SARS conducted a company tax audit of Impulse and a VAT audit was also conducted from 14 September 2018 to 8 November 2019, as well as a personal income audit of Mr Pather. Assessment letters were then issued and SARS imposed additional taxes in various categories, which indicated that Mr Pather and Impulse were then indebted to SARS for tax in excess of R251 461 181.05.

Both Mr Pather and Impulse failed to pay the tax debt, whereafter SARS entered civil judgments against them on 10 December 2019 and 13 January 2020, respectively.

SARS was of the view that it was constitutionally obliged to collect the aforesaid funds for the benefit of the *fiscus* and it effectively demonstrated this by an analysis of the Tax Administration Act (TA Act), which it then used as a backdrop giving rise to the reasons and events leading to the application of section 183 of the TA Act and Ms Pather's alleged liability as a person who knowingly assisted in dissipating Impulse's assets in order to obstruct the collection of a tax debt owing by Impulse.

SARS proceeded to hold Ms Pather jointly and severally liable for the tax debt of Impulse and invoked sections 179 and 183 of the TA Act to do so and recover the payment of R21.5 million from Mr Pather to Ms Pather.

The issue before the court was the lawfulness and procedural fairness of SARS' conduct in holding Ms Pather jointly and severally liable for the tax debt of a third party, i.e. Impulse. In her notice of motion she requests the court to declare unlawful SARS' decision to impose personal liability on her for the amount of R21 500 000 in terms of the Notice of Personal Liability dated 17 March 2021. Further, she requests that the funds taken from her by way of the section 179 Third-Party Appointment be declared unlawful and returned to her together with interest thereon in terms of the TA Act from the date of the Third-Party Appointment being implemented.

Ms Pather contended that SARS' conduct was unlawful and procedurally unfair and stood to be reviewed and set aside in terms of the provisions of the Promotion of Administrative Justice Act.

SARS specifically alleged that Ms Pather knowingly assisted Impulse in the dissipation of assets. In support thereof it stated that she had no working relationship with Impulse during the period that the amount of R21.5 million had been paid and it also submitted that she had concealed the payments from SARS and never declared same at the time and hence it was argued that this conduct was indicative of her knowingly assisting Impulse in avoiding its tax debt.

SARS further submitted that for a period of 17 years after her divorce from Mr Pather, Ms Pather received no payments from him or Impulse and the first time that she had received payments was once the irregularities in Impulse's contracts became public and once investigations were instituted into such contracts.

SARS asserted that Ms Pather ought to have known about the investigations and information regarding Impulse and Eskom that was in the public domain, and that such

investigations would attract investigation from SARS and a possible tax liability and this presupposed that she knew that Impulse never paid tax or never duly discharged its tax debts as and when they occurred.

SARS regarded the explanations for the payments which Ms Pather received from Impulse to be indicative of the fact that she was aware that Mr Pather was in the process of dissipating Impulse's assets when he transferred Impulse's funds to her.

SARS was of the view that Ms Pather had elected to close her eyes to the obvious facts and had failed to make the necessary enquiries to establish why Impulse, who she had no dealings with, was transferring millions of rands to her.

Judge van Nieuwenhuizen held the following:

<u>As to the existence of a tax debt as required in section 183 of the TA Act</u>

(i) That SARS had submitted that the tax debt of Impulse arose over many years and, if it had submitted its tax returns timeously or correctly, the amounts would have been declared, and it would have been expected to have been paid long ago. Accordingly, SARS submitted that, in terms of section 169 of the TA Act, the word 'due' simply meant 'owing' and no more. SARS concluded thus that, on the facts of this matter, the tax debt of Impulse was at all material times since the 2013 tax year payable to SARS in the sense that, at the close of each year of assessment, there was a liability on Impulse to pay tax to SARS. This was a present liability, and all that the assessment did was simply to particularise the exact sum, which Impulse at all material times had to pay.

(ii) That, consequently, SARS submitted that the tax debt of Impulse was, at all material times since the 2013 year, due as it was, at all material times, in existence as a debt and owing to SARS (albeit only quantified in the final assessments referred to above). The court found itself in agreement with the above approach of SARS as to the existence of a tax debt on the part of Impulse specifically during 2017.

(iii) That SARS thus took the stand that Ms Pather could not contend that there was no tax debt to the extent that same was a jurisdictional pre-requirement for the imposition of liability under section 183 of the TA Act. She nevertheless disputed this. The court was not persuaded that Ms Pather's dispute as to the existence of the tax debt was *bona fide*. The massive amount earned by Impulse from the contracts awarded by Eskom were such that even without the subsequent quantification of the debt a tax debt would have arisen. The exact

extent of the tax debt at the time of the alleged dissipation was another matter. To the extent that Ms Pather disputed the existence of the tax debt, the court found that a tax debt existed at the time that she received the payments in issue from Impulse, but the court made no finding as to the quantum due to SARS at the time that she received the payments.

As to whether the Ms Pather had knowingly assisted in dissipating assets

(iv) That, in addition to the aforesaid, SARS more specifically alleged that Ms Pather knowingly assisted Impulse in the dissipation of assets. In support thereof, it stated that she had no working relationship with Impulse during the period that the amount of R21.5 million was paid to her and it also submitted that Ms Pather had concealed the payments from SARS and never declared same at the time. Hence it was argued that such conduct was indicative of her knowingly assisting Impulse in avoiding the tax debt although same was denied.

(v) That, after reviewing the factual dispute, the court noted that all of which was important but not necessarily conclusive of any knowledge by Ms Pather so that it could be said that she had assisted in dissipating funds from Impulse 'knowingly.' The word 'knowingly' in the context in section 183 of the TA Act most certainly had to be reflective of her actual knowledge, or supposed knowledge, or circumstances under which she should have had knowledge in the sense of *dolus eventualis* that some tax debts existed.

(vi) That SARS' assertion that Ms Pather ought to have known or would have known that Impulse was the subject of investigation if she had taken reasonable steps, should have placed her on her guard and, hence, some or other suspicion should have arisen regarding Impulse's potential tax debts or liabilities and that, in that sense, she had acted knowingly and had assisted in dissipating assets, could not fully persuade the court that it could come to this conclusion on motion despite the mass of evidence SARS had produced and the 'fanciful defence' raised.

(vii) That the court could understand why SARS regarded Ms Pather's explanation of why she had failed to declare the receipt of R21.5 million from Impulse in her personal tax returns as somewhat fanciful, i.e. she had regarded the payments as alimony payments.

(viii) That SARS further submitted that it was not for it to prove Ms Pather's state of mind at the time when she received the payments from Impulse. The court was

in disagreement with SARS in this regard. Whilst the burden of proof normally rests upon the taxpayer, section 183 as a stand-alone means of recovery, to the court's mind demanded proof by SARS. It cannot rely on section 102 of the TA Act.

(ix) That despite the suspicions raised by SARS regarding Ms Pather, the court was not fully persuaded that Ms Pather had acted 'knowingly.' Returning to the issue of *mens rea* or the correct meaning of 'knowingly', a proper reading of section 183 suggested that 'knowingly' had a bearing on the dissipation of assets in circumstances where there are tax debts. There was not a single fact before the court which suggested that Ms Pather had any knowledge of the tax affairs of Impulse, but only suspicions and inferences and, of course, this did not mean that she had no knowledge.

(x) That if indeed there was a loan account, the effect of a payment by Mr Pather from his loan account to his own account or that of Ms Pather, would not amount to a dissipation of any asset of Impulse and this would be so because funds would simply have moved from the bank account to extinguish a debt of the company.

<u>As to the Ms Pather's remedies under section 184 of the TA Act</u>

(xi) That Ms Pather had contended that section 184 of the TA Act granted her the same rights and remedies which the main taxpayer, i.e. Impulse, had against SARS. On this basis she contended that she was entitled to lodge a request for suspension of payment of the tax allegedly due in terms of section 164(2) of the TA Act and that SARS' failure to do so was part of the procedural irregularities that the court had to review.

(xii) That, given the layout of the TA Act and the fact that it differentiated in its different chapters between the various steps of taxation, and that recovery was dealt with in a separate chapter and separate parts, section 184 seemed to regulate the position in toto and SARS was thus only obliged to comply with sections 155, 157, 179, 180, 181, 182 or 184 as the case may be. In other words, the tax was not due under an assessment, but under section 183 and hence the remedy sought here by Ms Pather was simply not available to her. Her remedies were set out in section 184 and did not include the remedies available to a taxpayer who owed tax under an assessment.

<u>As to the collection of tax in terms of section 179 of the TA Act</u>

(xiii) That Ms Pather had also attacked the collection of tax from her bank account in terms of section 179 of the TA Act. The criticism was that SARS had not complied with section 179(5) in that its demand under this section, did not set out the available debt relief mechanisms under the TA Act in that same was peremptory. SARS was of the view that this non-compliance did not render the section 179(1) notice invalid.

(xiv) That the court was of the view that SARS did substantially comply with section 179(5) of the TA Act by setting out the recovery steps in Annexure DP1. To insist on literal compliance with section 179(5) of the TA Act in the specific circumstances seemed to be overly formalistic.

As to the application of PAJA

(xv) That the only effective legal remedy Ms Pather could invoke in this matter were court proceedings in terms of PAJA. Given that PAJA prescribes an application proceeding, it could hardly be held against her or her legal advisers that, in circumstances where factual disputes must have been foreseen, this matter now has reached a stage where there is at least a factual dispute between Ms Pather and SARS as to the existence of a loan account, an issue which is material as to whether or not any assets have been dissipated as alleged.

(xvi) That the fact that this is a PAJA review does not change that this is a motion application, and the question is whether or not Ms Pather should be penalised for the fact that there was, before argument ensued, no application for a referral to trial or evidence. After much consideration, having regard to the fact that it is in the interests of justice, the court took the view that this matter should be referred to trial and, in the circumstances this matter is referred to trial in terms of the discretion of the court under Rule 6(5)(g) of the Uniform Rules of Court.

(xvii) That the review application based on section 164 of the TA Act is dismissed as is the review application based on non-compliance with section 179 of the TA Act.

(xviii) That this matter be referred to trial with regard to the question whether Ms Pather had knowingly assisted in dissipating the assets of Impulse in order to obstruct the collection of a tax debt of the aforesaid taxpayer and was therefore jointly and severally liable with Impulse for its tax debt to the extent that Ms Pather's assistance reduced the assets available to pay the taxpayer's tax debt.

8. INTERPRETATION NOTES

8.1. Additional deduction for learnership agreements – No. 20 (Issue 9)

This Note provides clarity on the interpretation and application of section 12H which provides for deduction of annual and completion allowances for registered learnership agreements meeting the requirements.

This Note takes into account legislative amendments introduced by the Taxation Laws Amendment Act 20 of 2021, effective from 1 April 2022 and amended by the Taxation Laws Amendment Act 42 of 2024.

Section 12H provides additional deductions to employers for qualifying learnership agreements entered into before 1 April 2027. These additional deductions are intended as an incentive for employers to train employees in a regulated environment in order to encourage skills development and job creation. Training contracts qualifying for these deductions are learnership agreements and apprenticeships registered with a SETA. These additional deductions consist of an annual allowance and a completion allowance and the amount of the allowance will depend on the NQF level held by the learner before entering into the learnership agreement.

Section 12H provides an annual allowance and a completion allowance to employers that are a party to a qualifying learnership agreement with an employee which has been registered with a SETA and entered into before 1 April 2027.

Section 12H distinguishes between learners holding NQF levels 1 to 6 and NQF levels 7 to 10 qualifications. The pre-existing qualifications of the learner entering the learnership agreement as well as persons with a disability will determine the value of the claim.

8.2. Year of assessment of persons other that companies: Accounts accepted to a date other than the last day of February – No. 19 (Issue 6)

This Note provides guidance on the application of section 66(13A) and the discretionary power vested in SARS to grant approval to a person, for example, a natural person or trust, to submit accounts for a period that differs from the year of assessment ending on the last day of February.

The Note deals primarily with natural persons and trusts carrying on a trade. A brief consideration is also included on the application of section 66(13A) to share purchase arrangements, public benefit organisations (PBOs), small business funding entities (SBFEs), the estate of a deceased person and insolvent estates.

The position of companies under section 66(13C) is dealt with in Interpretation Note 90 'Year of Assessment of a Company: Accounts Accepted to a Date other than the Last Day of a Company's Financial Year'.

Section 66(1) provides that SARS must issue a public notice each year prescribing who is required to furnish income tax returns. For example, not all natural persons are required to submit an income tax return, while a trust that is a resident is required to submit an income tax return regardless of whether income is generated.

Save for a few exceptions (for example, when a person dies or ceases to be a resident, or a trust is terminated), the income tax return of a person must be for the whole period of 12 months ending on the last day of February. In most instances, therefore, the year of assessment runs from 1 March of a year to the last day of February of the succeeding year.

Section 66(13A), however, provides that a person may apply to SARS for approval to draw up accounts to a date other than the last day of February. If SARS is satisfied that the whole or some portion of the taxpayer's income cannot be conveniently returned for any year of assessment, SARS may, subject to such conditions that may be imposed, approve the application.

Under section 66(13A) a person who cannot conveniently return income from a business or profession to the last day of February may apply at a SARS service centre for approval to draw up accounts to a closing date other than the last day of February. Any request of this nature is subject to conditions that SARS may impose. Generally, the approved closing date will determine the year of assessment that the results for the accounting period must be included and the dates that provisional tax payments must be made.

8.3. Year of assessment of a company: Accounts accepted to a date other than the last day of a company's financial year – No. 90 (Issue 3)

This Note provides guidance on the application of section 66(13C) and the discretionary power vested in SARS to accept financial accounts of a company for a period ending on a day that differs from the last day of the company's financial year.

The position of persons other than companies, for example, natural persons or trusts is dealt with in Interpretation Note 19 'Year of Assessment of Persons other than Companies: Accounts Accepted to a Date other than the Last Day of February'.

A company's year of assessment is generally its financial year.

Companies are occasionally required to close their financial accounts earlier or later than the last day of their financial year for various reasons. Section 66(13C) allows companies to align reporting for tax purposes with the period ending on the day their financial accounts are closed.

A company intending to close its financial accounts either within 10 days before or after the end of a year of assessment must submit an application to a SARS service centre for approval to draw up financial accounts to a closing date other than the end of its financial year.

Section 66(13C) relates only to a situation in which a company obtains approval from SARS to close its accounts on a date other than the last day of its financial year. This approval does not result in a change in the company's financial year-end and therefore does not change its year of assessment.

8.4. Game Farming – No. 69 (Issue 4)

This Note provides guidance on the application of selected sections of the Income Tax Act and paragraphs of the First Schedule to persons carrying on game farming, with its primary focus being the provisions applicable to livestock. It is not intended to deal with farming in general.

Section 26(1) provides that the taxable income of any person carrying on pastoral, agricultural or other farming operations shall, in so far as the income is derived from such operations, be determined in accordance with the Act but subject to the First

Schedule. The First Schedule details the computation of taxable income derived from pastoral, agricultural or other farming operations.

The taxable income from farming operations is combined with the taxable income from other sources to arrive at the taxpayer's taxable income for the year of assessment.

The First Schedule applies regardless of whether a taxpayer derives an assessed loss or taxable income from farming operations. The First Schedule may also apply even after farming operations have been discontinued.

Section 26 and the First Schedule apply to game farming, since it comprises farming operations.

The same principles used to determine whether a person carries on farming operations apply to game farmers. The test for this purpose is based on the taxpayer's intention.

Income from the sale of game, game meat, carcasses and skins and fees related to hunting constitutes farming income. However, income from accommodation, catering and admission charges is not farming income. Income not constituting farming income will be relevant when applying the ring-fencing provisions of paragraph 8 to game livestock. Game viewing fees may not constitute farming income depending on the facts and circumstances.

The rules governing the deduction of expenditure, including capital development expenditure, are similar to those applying to normal farming operations.

A farmer is required to bring to account the value of game livestock in opening and closing stock. No standard values have been prescribed by regulation for game livestock, but SARS accepts that game livestock may be allocated a standard value of nil. Game livestock acquired by donation is included in opening stock in the year of acquisition at market value under paragraph 4.

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

A farmer ceasing to carry on game farming must generally continue to deal with any game livestock under the First Schedule.

Special rules apply for income tax and CGT purposes upon the death or sequestration of a farmer and the transfer of trading stock, livestock or produce between spouses.

9. VAT RULINGS

9.1. Application of the zero rate to the services supplied directly in respect of investments located outside South Africa and not listed on a South African stock exchange – VR 009

This VAT ruling is published with the consent of the Applicant(s) to which it has been issued and is binding only upon SARS and applies only to the Applicant and any Co-applicant(s). This ruling is published for general information and does not constitute a practice generally prevailing.

The Applicant supplies administration and management services to customers (the clients) based in South Africa directly in respect of investments located outside of South Africa. The zero rate of VAT, under section 1(2)(g)(i) of the VAT Act, applies to the services supplied to the clients if the investments are not listed on South African Stock Exchange.

In this ruling, references to sections are to sections of the VAT Act applicable as at the date of the ruling of which this is the sanitised version. Unless the context indicates otherwise, any word or expression in this ruling bears the meaning ascribed to it in the VAT Act.

This is a ruling based on SARS' interpretation of the application of the following sections of the VAT Act:

- Section 11(2)(g)(i)
- Section 11(3)

Parties to the application

The Applicant: A collective investment scheme service provider and resident of South Africa trading in the financial services industry

Background and facts

The Applicant is an independent collective investment scheme (CIS) service provider in South Africa and provides own-brand and co-branded CIS portfolios to wealth managers. Wealth managers' clients would procure units in the CIS portfolios, administered and managed by the Applicant, as investments in participatory securities.

The Applicant supplies administrative and management services (the services) directly in respect of the assets of the CIS portfolios, for a consideration in the form of a service

fee charged to each individual CIS portfolio (that is, the members and/or trustees of the individual CIS portfolio). The service fee is based on a percentage of the assets under management.

The Applicant and the trustees of the CIS portfolios enter into certain agreements or deeds. The deeds, amongst others, set out the investment policies of the CIS portfolios. The investment policies allow CIS portfolios to invest in offshore and local financial instruments. The investment policies also allow CIS portfolios to invest in financial instruments that are either listed or unlisted on a South African Stock Exchange.

The Applicant is appointed as a discretionary financial services provider by CIS portfolios (represented by their trustees) to supply the services in accordance with the abovementioned investment policies.

Conditions and assumptions

This VAT ruling is subject to the Standard Terms, Conditions, and Assumptions issued by SARS, and the provisions of Chapter 7 of the Tax Administration Act, excluding sections 79(4)(f), (k), (6) and 81(1)(b).

Ruling

The VAT ruling issued to the Applicant is as follows:

- SARS is of the view that the Applicant may apply the zero rate, under section 11(2)(g)(i) of the VAT Act, to the services supplied in terms of the deeds that govern the applicant's management of CIS portfolio assets located outside South Africa and which are not listed on a South African Exchange.
- The Applicant must, in terms of section 11(3) of the VAT Act, read with Interpretation Note 31,obtain, and retain the relevant documentary proof mentioned below:
    - Tax invoice
    - Proof of payment
    - Written confirmation from the recipient (that is, the CIS portfolio represented by its trustees) that the movable property was situated in an export country at the time the services were rendered

9.2. Apportionment – VR 010

This VAT ruling approves the method of apportionment being a varied input-based method which is applied to the Applicant that is a South African short-term insurance company operating in the field of domestic and international credit insurance. The Applicant provides domestic and international trade credit insurance cover to its policyholders who sell goods or provide services to other businesses on credit terms in order to protect them against non-payment risks.

In this VAT ruling, all references to sections hereinafter are to sections of the VAT Act unless otherwise stated. Unless the context indicates otherwise any word or expression in this VAT ruling bears the meaning ascribed to it in the VAT Act.

This VAT ruling concerns the interpretation and application of the following provisions of the VAT Act:

- Section 1(1) – definition of 'input tax'
- Section 16
- Section 17(1)

Parties to the application

The Applicant is a short-term insurance company operating in the field of domestic and international credit insurance.

Description of the transactions

The Applicant provides domestic and international trade credit insurance cover to its policyholders who sell goods or provide services to other businesses on credit terms in order to protect them against non-payment risks The Applicant conducts the following activities:

- Provides various surety and bonding services via its specialised business unit. Its speciality lies in the ability to secure relevant and vital information incorporated with market intelligence, as a tool for a synergistic communique to support the business of its clients in both local and international markets.
- Has a specialised business salvage and recovery unit dedicated to dealing with intricate restructuring needed to ensure both their clients' and shareholders' interests are met.

The following income streams are received:

Taxable supplies

- Premium income (local and foreign)
- Reinsurance claims received
- Salvages received
- Commission income
- Administration fee income
- Credit limit fees

Exempt and non-taxable income

- Interest and other investment income
- Foreign indemnity receipts and salvages

The SARS is requested to issue a ruling in terms of section 41B, read with section 17(1) confirming that the Applicant may apply a varied input-based method with the following variations:

- Excluding the VAT incurred on expenses relating to reinsurance recoveries
- Excluding expenses incurred for salvage from the apportionment calculation
- Excluding the VAT incurred on expenses relating to foreign reinsurance recoveries

Conditions and assumptions

This VAT ruling is subject to the Standard Terms, Conditions and Assumptions issued by SARS, and the provisions of Chapter 7 of the Tax Administration Act, excluding sections 79(4)(f), (k), (6) and 81(1)(b).

Ruling

The VAT ruling made in connection with the transactions are as follows:

The Applicant may, for the purpose of determining the ratio to be applied to the VAT incurred relating to mixed expenses, apply the varied input-based method of apportionment as set out below:

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

where:

y = Apportionment ratio/percentage;

a = VAT incurred on goods or services acquired wholly for purposes of making taxable supplies:

- excluding the VAT incurred on expenses relating to reinsurance recoveries (that is, reinsurance premiums);

b = VAT incurred on goods or services acquired wholly for purposes of making exempt supplies;

c = VAT incurred on goods or services acquired wholly for purposes of making non-supplies (that is, other than exempt or taxable):

- excluding the VAT incurred on expenses relating to salvage; and
- excluding the VAT incurred on expenses relating to foreign reinsurance recoveries.

9.3. Apportionment – VR 011

This VAT ruling approves the method of apportionment being the varied turnover-based method which is applied to the Applicant a South African Real Estate Investment Trust (REIT) which is listed on the Johannesburg Stock Exchange (JSE) in the Real Estate Holdings and Development Sector.

In this VAT ruling, all references to sections hereinafter are to sections of the VAT Act unless otherwise stated. Unless the context indicates otherwise any word or expression in this VAT ruling bears the meaning ascribed to it in the VAT Act.

This VAT ruling concerns the interpretation and application of the following provisions of the VAT Act:

- Section 1(1) – definition of ‘input tax’
- Section 16
- Section 17(1)

Parties to the application

The Applicant is a listed South African REIT in the Real Estate Holdings and Development Sector.

Description of the transactions

The Applicant is a REIT which conducts the following activities:

- To acquire investments in offshore commercial property-owning companies
- Hold investments in offshore commercial property-owning companies

- trades in asset-based financial services

The following income streams are received:

- Interest received on loans provided to foreign entities, which includes profit-participating loans, loans to foreign associates and joint ventures and intercompany bridge loans.
- Exempt income in the form of interest received from local banks on surplus funds.
- Foreign exchange gains and losses resulting from hedging transactions.
- Gains and losses resulting from derivative instruments.
- Dividend income received from offshore investments.

The SARS is requested to issue a ruling under section 41B, read with section 17(1), confirming that the Applicant may apply the varied turnover-based method which includes all income streams with the following variations:

include:

- in taxable supplies, the greater of net interest received on loans to foreign entities or the interest margin (being the Prime Interest Rate less JIBAR) multiplied by the loan amount;
- in exempt supplies, a five-year moving average of net realised foreign exchange gains resulting from hedging transactions, which include net realised foreign exchange gains in relation to interest rate and cross currency swaps. In the event that a net loss is realised in a particular year, the Applicant will include such net realised loss as an absolute amount in the calculation of the five-year moving average;
- in exempt supplies, a five-year moving average of the net realised margin in relation to interest rate and cross currency swaps, being the net realised interest margin in relation to these instruments. In the event that a net loss is realised in a particular year, the Applicant will include such net realised loss as an absolute amount in the calculation of the five-year moving average;
- in non-taxable and non-supplies, dividend income to the extent of the difference between the Prime Interest Rate less JIBAR, multiplied by the five-year moving average of dividends received;

exclude:

- in exempt supplies, operational bank account interest;
- in non-taxable and non-supplies, exchange gains and losses not subject to hedging activities;
- in non-taxable and non-supplies, fair value adjustments to the extent that the amounts in relation thereto are unrealised gains or losses,

with effect from the commencement of the 2024 financial year.

Conditions and assumptions

This VAT ruling is subject to the Standard Terms, Conditions and Assumptions issued by SARS, and the provisions of Chapter 7 of the Tax Administration Act, excluding sections 79(4)(f), (k), (6) and 81(1)(b).

Ruling

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

The Applicant may, for the purpose of determining the ratio to be applied to the VAT incurred relating to mixed expenses, apply the varied turnover-based method of apportionment as set out below:

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

where:

y = Apportionment ratio/percentage;

a = The value of all taxable supplies made during the period:

including –

- the greater of net interest received on loans to foreign entities or the interest margin (being the Prime Interest Rate less JIBAR) multiplied by the loan amount;

b = The value of all exempt supplies made during the period:

including:

- the greater of net interest on loans to local entities or the interest margin (Prime Interest Rate less JIBAR) multiplied by the loan amount;
- including a five-year moving average of the net realised margin in relation to cross-currency swaps;

- including a five-year moving average of net realised foreign exchange gains resulting from hedging transactions. In the event that a net loss is realised in a particular year, the Applicant should include such net realised loss as an absolute amount in the calculation of the five-year moving average;

excluding:

- bank interest received on current accounts with financial institutions which are used for the day-to-day operations of the Applicant;
- any realised foreign exchange gains and losses that do not result from trading or hedging activities, such as entering into forward exchange contracts; and

c = The sum of any other amounts of income not included in 'a' or 'b' in the formula, which were received, or which accrued during the period (whether in respect of a supply or not):

including:

- a percentage of dividend income received from subsidiaries/foreign investments by applying the Prime Interest Rate less JIBAR, multiplied by the dividend amount. A five-year moving average of the dividend income received from foreign investments should be used as the dividend amount;

excluding:

- excluding fair value adjustments to the extent that the amounts in relation thereto are unrealised gains or losses.

Note: All income streams should be taken into account when determining the apportionment ratio based on the formula above, except as otherwise provided in the formula. All the other notes in respect of the formula for the standard turnover-based method contained in BGR 163 shall apply (where applicable).

Note: The Prime Interest Rate and JIBAR are the annual respective rates at the end of the financial year for which the apportionment ratio is calculated.

9.4. Apportionment – VR 012

This VAT ruling approves the method of apportionment being the varied turnover-based method which is applied to the Applicant that is a holding company for a group of companies which operate in the electronics and low-voltage electrical engineering industries.

In this VAT ruling, all references to sections hereinafter are to sections of the VAT Act unless otherwise stated. Unless the context indicates otherwise any word or expression in this VAT ruling bears the meaning ascribed to it in the VAT Act.

This VAT ruling concerns the interpretation and application of the following provisions of the VAT Act:

- Section 1(1) – definition of 'input tax'
- Section 16
- Section 17(1)

Parties to the application

The Applicant is a listed company incorporated in and a resident of the Republic.

Description of the transactions

The Applicant is a company which conducts the following activities:

- Holds an equity interest in a number of subsidiary companies
- Holds preference share interests in various group companies
- Leasing of rental space to its subsidiaries
- trades in manufacturing and engineering services

The following income streams are received:

- Significant amounts of inter-company ordinary dividend income
- Preference dividend income
- Rental income from its subsidiaries

SARS is requested to issue a ruling under section 41B, read with section 17(1), confirming that the vendor may apply the varied turnover-based method which includes all income streams with the following variations:

including:

- dividend income only to the extent of the difference between the Prime Interest Rate and JIBAR, and

excluding:

- interest received on surplus funds on local operating bank accounts;
- foreign exchange gains and losses (realised and unrealised) which do not result from hedging transactions; and
- the profit/loss on the sale of shares,

with effect from the commencement of the 2023 financial year.

Conditions and assumptions

This VAT ruling is subject to the Standard Terms, Conditions and Assumptions issued by SARS, and the provisions of Chapter 7 of the Tax Administration Act 28 of 2011, excluding sections 79(4)(f), (k), (6) and 81(1)(b).

Ruling

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

The Applicant may, for the purpose of determining the ratio to be applied to the VAT incurred relating to mixed expenses, apply the varied turnover-based method of apportionment as set out below:

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

where:

y = Apportionment ratio/percentage;

a = The value of all taxable supplies made during the period;

b = The value of all exempt supplies made during the period:

excluding:

- bank interest received on current accounts with financial institutions which are used for the day-to-day operations of the Applicant (all other interest should be included);
- any realised foreign exchange gains and losses which do not result from hedging transactions; and
- the profit/loss on the sale of shares;

c = The sum of any other amounts of income not included in 'a' or 'b' in the formula, which were received, or which accrued during the period (whether in respect of a supply or not):

including:

- a percentage of dividend income received from subsidiaries, that is, the difference between the Prime Interest Rate and JIBAR; and

excluding:

- any unrealised foreign exchange gains or losses not arising as a result of hedging activities.

Note: That no ruling is made with regards to the type of supplies made by the Applicant and whether such supplies are taxable, exempt or non-taxable for VAT purposes.

Note: All income streams should be taken into account when determining the apportionment ratio based on the formula above, except as otherwise provided in the Formula. All the other notes in respect of the formula for the standard turnover-based method contained in BGR 163 shall apply (where applicable).

9.5. Zero-rating of medical health insurance cover – VR 013

This VAT ruling confirms that the premiums charged by the Applicant as consideration for the provision of medical health cover to the employees of foreign employers and the dependents of the employees who are located in a foreign country, in the event of medical emergencies, where the foreign employer contracts with the Applicant as principal, qualify for VAT at the rate of zero per cent in terms of the provisions of section 11(2)(ℓ).

In this VAT ruling, all references to sections hereinafter are to sections of the VAT Act unless otherwise stated. Unless the context indicates otherwise any word or expression in this VAT ruling bears the meaning ascribed to it in the VAT Act.

This VAT ruling concerns the interpretation and application of the following provision of the VAT Act:

- Section 11(2)(ℓ)

<u>Parties to the application</u>

The Applicant is an insurer and provides short-term insurance cover.

Background and facts

The Applicant provides insurance cover in terms of a medical health insurance policy for employees of foreign employers where the employees are employed in foreign countries.

In terms of the policy, the Applicant provides health and medical cover to persons, generally a group of employees of an employer, where the employees are employed and reside outside South Africa. Accordingly, persons who are ordinarily resident outside South Africa and expatriate personnel who provide services on a contractual basis and who are present in any country other than South Africa may enjoy cover under the policy.

The policy covers the employees and the dependents of the employees (collectively referred to as the 'beneficiaries') in the event of a medical emergency as defined in the policy. In such case the Applicant will cover the cost of emergency evacuation of the beneficiary who suffered the emergency, the cost of treatment of the beneficiary in a medical facility and the cost of repatriation of the beneficiary.

The premiums payable in terms of the direct policies are determined in relation to each beneficiary listed in the policy. The premiums are charged to foreign employer companies in foreign currency and are payable annually in advance.

Conditions and assumptions

This VAT ruling is subject to the Standard Terms, Conditions and Assumptions issued by SARS, and the provisions of Chapter 7 of the Tax Administration Act 28 of 2011, excluding sections 79(4)(f), (k), (6) and 81(1)(b).

Ruling

The binding private ruling issued to the Applicant is as follows:

- The medical health insurance cover provided by the Applicant to the foreign employers may be zero-rated under section 11(2)(ℓ).
- The VAT ruling is subject to:
    - the services being supplied directly to the foreign employer;
    - the foreign employers not being present in the Republic at the time the services are rendered;
    - no other person to whom the services are rendered being present in the Republic at the time such services are rendered; and

- the Applicant obtaining and retaining the necessary documentary proof required in terms of section 11(3), read with Item M of Interpretation Note 31.

10. BINDING PRIVATE RULINGS

10.1. Application of the proviso to section 8EA(3) – BPR 414

This ruling determines how the proviso to section 8EA(3) will apply in certain circumstances where equity shares in an operating company that were acquired by a person through the application of preference share funding, are no longer held, directly or indirectly, by that person.

In this ruling references to sections are to sections of the Income Tax Act applicable as at 25 March 2025. Unless the context indicates otherwise any word or expression in this ruling bears the meaning ascribed to it in the Act.

This is a ruling on the interpretation and application of section 8EA.

Parties to the proposed transaction

The Applicant: A resident company

The Co-Applicants: Resident companies A, B and C, being the parties that hold preference shares in the Applicant.

Description of the proposed transaction

The Applicant is an investment holding company wholly owned by an *inter vivos* trust, duly established in South Africa (the Trust). The Trust holds shares in private companies and various listed companies (Trust shares).

The Applicant holds ordinary shares in a private company and indirect interests in various South African operating companies through a newly incorporated company, Company D.

In 2015 the Co-Applicants subscribed for 1 450 cumulative redeemable preference shares in the Applicant (the Preference Shares) for an aggregate subscription price of R1 450 000 000 (the Preference Share Subscription Consideration). Between 2015 and the date of this ruling letter, some of the 1 450 Preference Shares were redeemed such that at the date of this ruling letter, 1 133 Preference Shares were in issue. The Co-Applicants acted jointly as subscribers for the Preference Shares in the following proportions:

- Company A: 73.32%
- Company B: 13.34%; and
- Company C: 13.34%.

The above percentages remained the same since 2015 even after the historical redemptions of some of the Preference Shares.

The Preference Share Subscription Consideration of R1 450 000 000 was applied by the Applicant for various purposes including, amongst others, the Applicant refinancing a bridge loan which it used to acquire a minority portion of the equity shares in Company E, for R101 111 706. Company E was listed on the JSE in 2015. The Preference Share Subscription Consideration was also applied by the Applicant to make investments in other operating companies (Opco(s)), each application of which constituted a 'qualifying purpose' as defined in section 8EA(1). Company E and the other Opco's are collectively referred to as the Applicant Assets.

The Applicant's acquisition of the Company E shares accounted for 6.97% of the application of the Preference Share funding obtained, being R101 111 706 / R1 450 000 000. The balance of the R1 450 000 000 was used to acquire the equity shares in the other Opco's, of which the Applicant remains the holder at the date of this ruling letter, on an indirect basis, as a result of a restructure described below.

The Trust guaranteed the obligations of the Applicant vis-à-vis the Preference Shares in the event of a default by the Applicant (the Trust Guarantee). The Trust pledged and ceded a portion of its Trust shares, and amounts held in an interest-bearing bank account, to the Co-Applicants as security in respect of the Trust Guarantee.

In 2022 the Applicant implemented an internal asset restructure (the Applicant Asset Restructure), which resulted in most of the Applicant Assets being held under Company D. At the time of the Applicant Asset Restructure, the offer to acquire the entire issued share capital in Company E (other than specifically excluded shares) and its delisting had already been announced.

All the Applicant's equity shares in Company E were sold in 2023 and Company E was subsequently delisted from the JSE. The proceeds from the disposal of Company E were not used to redeem any of the Preference Shares. The equity shares in Company E were not substituted for other listed share(s).

The disposal of the Company E shares took place before the introduction of the proviso to section 8EA(3), which was enacted with effect from 1 January 2024, and is

applicable in respect of any dividend received or accrued during any year of assessment commencing on or after 1 January 2024.

It is now proposed by the Applicant that 6.97% of the Preference Shares be redeemed (Voluntary Redemption). As the Preference Shares in issue at the date of this ruling letter total 1 133, 6.97% of 1 133 equates to 79 Preference Shares to be redeemed in terms of the Voluntary Redemption.

Conditions and assumptions

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

- At the time that a dividend is received by or accrues to a Co-Applicant in respect of a Preference Share, in each instance, such share in respect of which the dividend is received or accrues, constitutes a 'preference share' as defined in section 8EA(1), in respect of which an 'enforcement right', as defined, is exercisable by the holder;
- The funds derived from the issue of the Preference Shares were applied for a qualifying purpose as contemplated in 8EA(3)(a) read with the definition of 'qualifying purpose' in section 8EA(1); and
- The 'enforcement rights' were exercisable against the Trust, being a person contemplated in section 8EA(3)(b).

Ruling

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

- The 79 Preference Shares currently in issue that are traced to the acquisition of Company E, are 'tainted Preference Shares'.
- Dividends in respect of 57 tainted Preference Shares, that accrue to Company A from 1 January 2024 up to the Voluntary Redemption, will be subject to income tax in that Co-Applicant's hands.
- Dividends in respect of 11 tainted Preference Shares, that accrue to Company B from 1 January 2024 up to the Voluntary Redemption, will be subject to income tax in that Co-Applicant's hands.
- Dividends in respect of 11 tainted Preference Shares, that accrue to Company C from 1 July 2024 up to the Voluntary Redemption, will be subject to income tax in that Co-Applicant's hands.

- After the Voluntary Redemption of the 79 tainted Preference Shares, no portion of a Preference Share dividend that accrues to the Co-Applicants will be subject to the proviso to section 8EA(3), if the Applicant continues to hold the remaining equity shares in the Opco's as contemplated in section 8EA(3)(a) while the Preference Shares remain in issue.

11. BINDING CLASS RULINGS

11.1. Application of the proviso to section 8EA(3) – No. 92

This ruling determines how the proviso to section 8EA(3) will apply in certain circumstances where equity shares in an operating company that were acquired by a person through the application of preference share funding, are no longer held, directly or indirectly, by that person.

Relevant tax laws

In this ruling references to sections are to sections of the Income Tax Act applicable as at 27 February 2025. Unless the context indicates otherwise any word or expression in this ruling bears the meaning ascribed to it in the Act.

This is a ruling on the interpretation and application of section 8EA.

Class

The class members to whom this ruling will apply are the members of a trade association.

Parties to the proposed transaction

The Applicant: The trade association who applied on behalf of its members.

Description of the proposed transaction

The class members subscribe for preference shares in companies in circumstances where the issuer applies the subscription proceeds for a qualifying purpose as envisaged in section 8EA(3). As such, equity shares are acquired directly or indirectly in an 'operating company' as defined in section 8EA(1). In the course of such a process, security is typically given by third parties, amongst others, the operating company and/or the shareholders of the Issuer.

The introduction of the proviso to section 8EA(3) may impact existing preference share arrangements of the class members where preference shares were issued for a

'qualifying purpose' but some, or all, of the operating company shares were disposed of by the acquiror thereof, and the proceeds from that disposal were not applied to redeem the outstanding preference shares or settle the outstanding dividends. The disposal of the operating company shares in these circumstances would have been undertaken for commercial reasons.

Consequently, certain existing preference shares, which met the requirements of section 8EA(3) prior to the introduction of the proviso, now fall into the ambit of the proviso to section 8EA(3) (Tainted Preference Shares).

The class members propose the following transactions, depending on the circumstances:

- Continue with the existing preference share arrangements;
- Call for the redemption of the outstanding capital and accrued dividends in respect of the Tainted Preference Shares; or
- Where the outstanding capital and accrued dividends are not so redeemed, if appropriate, amend the security arrangement(s) to release the third party from the security in respect of the Tainted Preference Shares.

Conditions and assumptions

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

- At the time that a dividend is received by or accrues to a person in respect of the preference shares referred to in this application, in each instance, such share in respect of which the dividend is received by or accrues to its holder, constitutes a 'preference share' as defined in section 8EA(1) in respect of which an 'enforcement right', as defined in section 8EA(1), is exercisable by the holder.
- The funds derived from the issue of the preference shares were applied for a qualifying purpose at the time of the issue of the preference share as contemplated in section 8EA(3)(a).
- The enforcement rights were exercisable at the time of the issue of the preference share against the persons contemplated in section 8EA(3)(b).
- Section 8E does not apply.

Ruling

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

- If a share in an operating company that was acquired by any person referred to in the proviso to section 8EA(3) is no longer held, directly or indirectly, by that person at the time of the receipt or accrual of a dividend in respect of the preference share, the funds from the issue of which were applied in acquiring that share in the operating company, and the funds from the disposal of that share in the operating company are not used in redeeming that preference share in full, and the settlement of an amount of dividends or foreign dividends, if any, in respect of that preference share, within 90 days of the disposal, section 8EA(3) will not apply. In terms of section 8EA(2), any dividends received or accrued in respect of that preference share, that is a 'third-party backed share', at any time during the year of assessment will be deemed to be income.
- If a share in an operating company that was acquired by any person referred to in the proviso to section 8EA(3) is no longer held, directly or indirectly, by that person at the time of the receipt or accrual of a dividend in respect of the preference share, the funds from the issue of which were applied in acquiring that share in the operating company, and the funds from the disposal of that share in the operating company are used in redeeming that preference share in full, and the settlement of an amount of dividends or foreign dividends, if any, in respect of that preference share, within 90 days of the disposal, the proviso to section 8EA(3) will not apply to the preference share, with the result that section 8EA(3) will apply.
- In applying the proviso to section 8EA(3), it is necessary to trace the share in the operating company to the preference share or shares, the funds from the issue of which were used to acquire that share in the operating company that is no longer held, directly or indirectly, as per the proviso to section 8EA(3). Depending on the facts, if direct tracing is not possible, a method that is appropriate to the facts may be used to perform the tracing in another manner.
- The proviso to section 8EA(3) will not apply to prevent the application of section 8EA(3) in respect of a preference share (Untainted Preference Share), the funding of which is traced to the acquisition of a share in an operating company which is still held, directly or indirectly, by the person referred to in the proviso to section 8EA(3) at the time of receipt or accrual of a dividend in respect of the preference share. If the preference share is not a 'third-party backed share' at

any time during the year of assessment, then section 8EA(2) will not deem any dividends received in respect of that preference share during that year of assessment to be income.

- No view is expressed on the legal consequences of any proposed amendment of security arrangement(s), because any proposed amendment will have to be considered on its own terms.

12. BINDING GENERAL RULINGS

12.1. Apportionment methodology to be applied by a municipality (VAT) – No. 4 (Issue 4)

For the purposes of this ruling:

- 'capital asset' means the asset described in E3 in the Annexure
- 'extraordinary income' means the income defined in E4 in the Annexure
- 'JIBAR' means the Johannesburg Interbank Average Rate, and includes reference to ZARONIA where applicable (see N3)
- 'mixed expenses' means goods or services acquired partly for the purpose of consumption, use or supply in the course of making taxable supplies and partly for another intended use
- 'MFMA' means the Municipal Finance Management Act 56 of 2003
- 'MSA' Municipal Systems Act 32 of 2000
- 'municipality' means any municipality falling within any of the categories of municipalities described in section 155 of the Constitution of the Republic of South Africa, Act 108 of 1996

Purpose

This BGR prescribes the apportionment method that a municipality must use to determine the ratio contemplated in section 17(1) to calculate the amount of VAT that may be deducted as input tax on mixed expenses.

Background

Municipalities receive several different types of income to finance their operations. Some income streams result from supplies made by the municipality whilst others are

received due to statutory requirements placed on, for instance, residents. The VAT treatment of each income stream must be evaluated separately, determined based on either special rules contained in the VAT Act (such as grants) or general VAT principles.

The VAT incurred on expenses to earn the aforementioned income may only be deducted to the extent that it constitutes 'input tax' as defined in section 1(1), more specifically, that the goods or services must be acquired for consumption, use, or supply in the course of making its taxable supplies. A municipality is therefore required to directly attribute the VAT on goods or services acquired to the intended purpose for which the goods or services will be consumed, used, or supplied.

The income streams, with subsequent input tax deductions based on direct attribution, can be categorised as follows for VAT purposes:

- Taxable supplies

  Supplies subject to VAT at either the standard or zero rate and in relation to which the municipality can deduct input tax on expenses incurred. Examples include grants, municipal property rates, and the supply of water, or electricity.

- Exempt supplies

  Supplies made that are not subject to VAT, and the municipality is also not entitled to deduct any VAT on expenses incurred for this purpose. Examples include the earning of interest, transportation of passengers in a bus, and rental of dwellings.

- Out-of-scope income streams

  Income that does not result from any supplies made by the municipality. These income streams are not subject to VAT and no VAT may be deducted on expenses incurred to earn the income. Examples include dividends, statutory fines, and penalties.

It is accepted, however, that municipalities incur operating expenses that cannot be directly attributed to a specific purpose, also referred to as mixed expenses. In these instances, municipalities are required to apportion the VAT incurred on such expenses to determine the extent to which such VAT relate to the making of taxable supplies, and which therefore may be deducted as input tax.

Discussion

Section 17(1) provides that the extent to which a municipality may deduct input tax in respect of mixed expenses is determined by means of a ratio determined by SARS for

the SARS in terms of a ruling contemplated in Chapter 7 of the Tax Administration Act, 2011 (that is, a binding general ruling) or a ruling under section 41B (that is, a VAT class ruling, or a VAT ruling).

Ruling

The formula set out below, being the default method of apportionment to be applied by all municipalities in the absence of an alternative method approved by SARS in terms of a ruling as described above, constitutes a BGR under section 89 of the Tax Administration Act 28 of 2011.

Formula:

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

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

‘y’ = the apportionment ratio or percentage;

‘a’ = the value of all taxable supplies (including deemed supplies) made during the period;

‘b’ = the value of all exempt supplies made during the period; and

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

The following are excluded from the formula set out above:

E1	Foreign exchange differences that do not form part of any hedging activities
E2	Accounting entries, such as fair value adjustments, resulting in income reflected in the Annual Financial Statements to ensure compliance with relevant Regulatory Frameworks
E3	The supply of capital assets
E4	Extraordinary income
E5	The value of any goods or services supplied if input tax on those goods or services was specifically denied under section 17(2)
E6	Change-in-use adjustments under sections 18, 18A, 18C, and 18D

E7	Indemnity payments received as envisaged under section 8(8) to the extent that the indemnity payments relate to extraordinary income or capital assets
E8	The value of municipal bonds issued as a manner of raising funds
E9	Interest earned from: • the municipality's current account (meaning, the account used for day-to-day business operations); and • the SARS

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

A1	Interest, other than the interest excluded from the formula in E11, from any investments, including savings accounts, must be included as follows: Interest received for the year × (prime rate − JIBAR)
A2	Dividends The amount to be included in the formula on dividends received from investment activities (including investments held in municipal entities, public private partnerships and ad-hoc or minority investments) must be determined using the following formula: 3-year moving average of dividends received/accrued during the year × (prime rate − JIBAR)

General notes for using the formula set out above:

N1	The exclusions and adjustments to the formula are subject to the further explanations and discussions as set out in Annexure A.
N2	'c' in the formula will typically include, but is not limited to, items such as statutory fines, penalties, dividends etc. However, traffic fines are only included in 'c' to the extent that payment has actually been received by the municipality.
N3	The prime rate to be used for all the adjustments listed above is the applicable prime rate at the end of the financial year.

	The JIBAR rate to be used for all adjustments listed above is the 12-month term rate quoted on the last day of the financial year. If more appropriate for the municipality, or should the JIBAR no longer be applicable, the ZARONIA may be used; the rate being the equivalent to the above stated JIBAR. For ease of reference, the reference to JIBAR in this document includes reference to the ZARONIA.
N4	The term 'value' excludes the VAT component of the supply
N5	The apportionment ratio must be rounded off to two decimal places.
N6	If the formula yields an apportionment ratio of 95% or more, the full amount of VAT incurred on mixed expenses may be deducted [referred to as the de minimis rule and effected under proviso (i) to section 17(1)] as input tax.
N7	Municipalities using their previous year's turnover to determine the current year's apportionment ratio are required to make an adjustment (that is, the difference in the ratio when applying the current and previous year's turnover) within nine months after the end of the financial year, that is, the adjustment must be made in the VAT201 return submitted at the latest nine months after the financial year-end.
N8	This formula may only be used in the following circumstances: • If the method is fair and reasonable to the municipality's business activities. It is the municipality's responsibility to first determine this. If the method is not fair and reasonable, it is the municipality's further responsibility to approach SARS for an alternative method. SARS is unable to retrospectively approve an alternative apportionment method and will only approve the method from a prospective date or such other date falling within the limitations set out in proviso (iii) to section 17(1). • The municipality submits to VATRulings@sars.gov.za the following information on an annual basis at the time the annual adjustment referred to in N7 is reflected in the VAT201 return: o The municipality's name o VAT registration number o Apportionment method and formula used

	○ Apportionment ratio for the year. The first time that this formula is applied, the method and apportionment ratio for the past three (3) years must be submitted.
N9	A grant that is received partly for taxable purposes and partly for non-taxable purposes must be attributed accordingly. For example, if 70% of a grant is for subsidising the taxable supply of water and electricity to customers, and 30% is for subsidising the municipality's exempt public transport business, the grant amount will have to be split into its respective taxable and non-taxable components in accordance with section 10(22). In this example, 70% of the grant amount will be subject to VAT at the zero rate and will be included in 'a' in the formula. The remaining 30% of the grant will be applied for exempt purposes and will be included in 'b' in the formula.
N10	Notwithstanding any permission which may have been granted by SARS to allow a municipality to account for VAT on the payments basis under section 15(2)(a)(v), the amounts to be included in 'a', 'b', and 'c' in the Formula for each tax period and for the annual adjustment contemplated in N7 are to be calculated on the invoice basis and in accordance with the principles set out in the Accounting Standards Board's Standard of Generally Recognised Accounting Practice (GRAP) on Revenue from Non-exchange Transactions (Taxes and Transfers), commonly referred to as GRAP 23. In terms of GRAP 23, income from government grants and subsidies is only recognised when the conditions (if any) are met. Grant income will therefore only be included in the formula to the extent that such funds are reflected in the income statement of the municipality for the financial year concerned.
N11	It is the responsibility of a municipality to determine whether the supplies made by it are as principal or agent: • If functions have been formally assigned to a national or provincial municipality, the municipality makes these supplies as principal. As a result, these supplies fall within the ambit of the 'enterprise' activities carried on by a municipality, provided the activity does not fall within the ambit of section 12. Any consideration charged, must be included in 'a' in the formula if it relates to a taxable supply and in 'b' in the formula if it relates to an exempt supply.

	• If a municipality is appointed as agent by provincial government, only the amount charged for the taxable supply of such agency service to the provincial government must be included in 'a' in the formula. Any payment received as a result of the national or provincial government providing financial assistance to enable the municipality to carry out the formally assigned activity is regarded as a 'grant' as defined. The inclusion in the formula will depend on whether the grant relates to the enterprise activities of the municipality (to be included in 'a' in the formula) or otherwise (to be included in either 'b' or 'c' in the formula).
N12	The VAT incurred and paid for directly on the supply of goods or services associated with 'unfunded mandates', is regarded as being incurred in the course or furtherance of the municipality's enterprise, provided the mandated activity is not exempt under section 12. The VAT may be deducted in full if the expenses concerned are incurred wholly for purposes of use, consumption, or supply in the course of making taxable supplies. Alternatively, the VAT may be deducted in part in accordance with the formula if the expenses concerned are incurred for mixed purposes.
N13	The deduction of input tax in all cases (including on mixed expenses) is subject to the documentary and other requirements set out in sections 16(2), 16(3), 17, and 20 being met.

Period for which this ruling is valid

This BGR applies with effect from all financial years commencing on or after 1 July 2025, and will apply until it is withdrawn, amended or the relevant legislation is amended. The apportionment formula as set out in Issue 3 of this BGR (the Issue 3 formula) is withdrawn effective from the aforementioned date.

Transitional rules

The Issue 3 formula applies to all financial years preceding those financial years commencing on or after 1 July 2025. If an alternative apportionment method has been approved for use by a municipality in a VAT ruling or VAT class ruling and the municipality regards the apportionment formula set out in this BGR to be fair and reasonable, that municipality can approach SARS to have the VAT ruling or VAT class

ruling withdrawn from the financial year commencing on or after 1 July 2025. The request for withdrawal must be submitted to VATRulings@sars.gov.za before the end of the financial year commencing on or after 1 April 2025.

The provisional ratio to be applied for the financial year commencing on or after 1 July 2025 may be based on the actual financial results of the preceding financial year using the Issue 3 formula. The adjustment to be made in the tax period, which ends no later than nine months after the end of the financial year that commenced on or after 1 July 2025, must be based on the actual financial results of such financial year using the apportionment formula set out in this BGR. In the event that a municipality determines its apportionment on a monthly basis, the municipality must apply the apportionment formula set out in this BGR from the first month of its financial year commencing on or after 1 July 2025. No adjustment after year-end is required.

Annexure – Application of the exclusions and amendments to the apportionment formula as set out in paragraph 4 of the Ruling

Exclusions:

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

	effective hedging strategy whilst continuously developing and ensuring proper implementation of said strategy. Hedging foreign exchange transactions are used to address various risks identified (such as the risk of future or short-term cash flows, or the risk of income) and could take many forms, including forward contracts or options. In order to ensure that the use of resources and all transactions are properly reflected in the apportionment formula, any foreign exchange differences that result from a hedging transaction must be included in the formula. If a foreign exchange is hedged, the profit or loss on the underlying foreign exchange may not be set off against the profit or loss on the hedge as these are separate and distinct transactions from a VAT perspective, as explained above.
E2	<u>Accounting entries, such as fair value adjustments, resulting in income reflected in the AFS to ensure compliance with relevant Regulatory Frameworks</u> The GRAP requires certain value adjustments to be made in the accounting records of a person to ensure the true economic value of assets or liabilities are reflected in that person's AFS. From a VAT apportionment perspective, the value adjustments made are not income intended to be included in the formula – no actual income will be received by the municipality as the adjustment is merely a revaluation of an asset or liability at a specific point in time and not consideration for any activity as a result of a separate supply of goods or services. For this reason, any value adjustment made for GRAP purposes is excluded from the apportionment formula. Examples of accounting entries are: • revaluation of a transaction in foreign currency (also refer to E1 above, (excluding hedges); and • fair value adjustment of fixed and/or intangible assets.
E3	<u>The supply of a capital asset</u> The VAT incurred on capital expenditure is generally deducted as a once-off at the time when a municipality acquires the said asset (if a municipality is registered on a payments basis, deduction of the asset is made to the extent of payment). Although the asset is used throughout the municipality's

	operations, it is not one of the resources that, on an on-going basis, and forms part of the pool of expenses that are subject to the apportionment ratio. It is also accepted that municipalities are not in the business of selling off their capital assets on an on-going basis, as that would be un-business like and would severely influence the ability of the municipality to continue its operations. Therefore, the sale of capital assets is generally an extraordinary event that is not expected to occur continuously. Having regard to the extraordinary nature of the supply (such as a sale) of capital assets together with the possible substantial values attached to them, the inclusion of the income earned on the sale of capital assets in the apportionment formula would distort the apportionment ratio in that it would not fairly reflect the use of those resources to which the apportionment ratio is applied. It is worth highlighting that, due to the significant costs involved in acquiring capital assets, it may be necessary for municipalities to determine whether an alternative apportionment method is required for specific capital assets. The municipality must evaluate the specific circumstances and intended use of the capital asset to determine the most appropriate method for the specific asset and, if need be, apply for an alternative method. What is a capital asset? In short, a capital asset is an asset that enables a municipality to operate but is not the operation itself. Consider a municipality selling office furniture. To this municipality, the furniture enables the municipality to conduct its operations as it is not the mandate or purpose of a municipality to buy and sell office furniture for a profit. To the municipality, the office equipment is a capital asset. The circumstances of each case must be evaluated to determine the nature of a specific asset. The most important factor to consider is the intention of the municipality when acquiring and subsequently using the asset. As intention is a very subjective test, various factors must be used to determine and substantiate that intention. Some factors that may assist in determining whether an asset is capital in nature, is as follows: • Trading stock or consumables are not capital assets. • The asset is held with a certain degree of permanency.

	• Linked to the above, the asset is held for a lengthy period of time. Although this test is not conclusive on its own, it could be convincing when deliberated with other factors. • The type of asset is not commonly bought and sold by the municipality on a regular basis. • An asset which stays mostly intact, and which is rather used to produce wealth. The distinction between trading income and income of a capital nature is not a new concept in tax and has been the subject of various disputes and court cases over the years. Chapter 2 of the Comprehensive Guide to Capital Gains Tax provides in-depth examples and discussions on how to distinguish between income and capital. These principles can also be applied as guidance in determining whether an asset is capital in nature for VAT apportionment purposes.
E4	<u>Extraordinary income</u> Extraordinary income is non-recurring income received due to exceptional circumstances that are unlikely to be repeated. From a VAT apportionment perspective, extraordinary income would have a significant impact on the quantum of income received by a municipality without affecting the normal expenses incurred year-on-year. The inclusion of such income in the apportionment formula would therefore severely distort the apportionment ratio as there would be a material fluctuation from one year to another whilst the mixed expenses, and the use these mixed expenses in the municipality's operation, would have remained unchanged. Based on the above, extraordinary income should be excluded from the apportionment formula. In order to give effect to this, 'extraordinary income' is defined for VAT apportionment purposes as non-recurring income received due to exceptional circumstances that are unlikely to be repeated. An example of extraordinary income is dividends received as a result of a liquidation of a municipal entity (see also the discussion on dividends in A2 below). Examples of income that are NOT regarded as being extraordinary in the hands of a municipality:

	• Grant income • Dividends received from investments not as a result of the liquidation of a municipal entity
E5	<u>The value of any goods or services supplied if input tax on those goods or services was specifically denied under section 17(2)</u> A municipality is prohibited from deducting input tax on certain items listed in section 17(2). These include, amongst others – • goods or services acquired for purposes of entertainment; and • the acquisition of a 'motor car' as defined in section 1(1). In both the above instances, municipalities would not generally supply entertainment or a 'motor car' as defined (and are therefore allowed the deduction), and would therefore not normally buy and sell the items on a regular basis. The goods or services purchased would be of a capital nature and the subsequent supply these good or services would automatically be excluded from the apportionment formula as a result of their capital nature. In addition, it would be inequitable to include the income on the sale of such goods or services (or any indemnity payment received from such sale) if the municipality was originally disallowed (by legislation) any input tax deduction in relation to the sale.
E6	<u>Change-in-use adjustments under sections 18, 18A, 18C and 18D</u> A change-in-use adjustment adjusts the input tax deducted to reflect the actual use as opposed to the intended use of goods or services. Change-in-use adjustments should be excluded from the apportionment formula
E7	<u>Indemnity payments received as envisaged under section 8(8) to the extent that the indemnity payments relate to extraordinary income or capital assets</u> Subject to certain exceptions, a municipality is deemed to make a supply of services upon receipt of an indemnity payment (or indemnification of a loss paid to a third party) from an insurer. 5 Section 8(8) further deems that supply to be made in the furtherance of the municipality's enterprise. Any indemnity payment received as a result of a capital asset (such as an office

	building), or extraordinary income should not be included in the formula in keeping with the exclusions in E3 and E4.
E8	<u>The value of municipal bonds issued as a manner of raising funds</u> One of the methods of raising funds available to a municipality is to issue municipal bonds. Although this is not a very common manner for municipalities to raise long-term debt, certain municipalities have opted in recent years to issue municipal bonds for special projects, such as the acquisition of capital assets. Under section 2, the issuing of these instruments is deemed to be financial services, being an exempt supply under section 12(a). As this is regarded as being extraordinary, the income derived from the issuing of municipal bonds should not be included in the apportionment formula.
E9	<u>Interest</u> • Earned from the municipality's current account(s) (meaning, the account used for day-to-day business operations) It would be hard for any municipality to function without a bank account used every day to both receive and make payments. The municipality's intention when opening a transactional bank account is therefore never to earn the interest thereon, but rather to facilitate transactions within its business. The income in this account is generally as a result of payments received from third parties or customers as a result of trading activities and not investment activities by the municipality. As the interest rates on a transactional account is very low, businesses rarely hold money in a transactional bank account for earning interest. A municipality would rather transfer any excess funds to a call or similar account where the interest rates are much higher. The business decision to effect such transfer reflects a municipality's purpose of earning investment income in the form of interest. It is for this reason that any interest earned from a call or other investment account is included in the apportionment formula (refer also to A1). • SARS Interest.

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

A1	<u>Interest, other than the interest excluded from the formula in E11</u> Investment activities are more often than not conducted by a municipality on a continuous basis, even though it might not be a municipality's main purpose. This often happens when a grant is received by a municipality for activities to be conducted over a certain period. The excess funds not to be used immediately are held in a savings account for later use, whilst also maximising the investment benefit from these excess funds. To ensure that the purpose for which the VAT incurred on goods or services is fairly reflected in the apportionment formula, one must have cognisance of the wholistic purpose of the entity, and all activities associated in achieving that purpose. For this reason, interest must be included in the formula. It is however accepted that interest received is dependent on external factors, such as external interest rates. These external factors can result in material fluctuations in interest received from year to year even though a municipality's expenses in earning that interest have not significantly changed. For this reason, the interest to be included in the formula must be determined using the guidelines below: • Investment interest All investment activities of a municipality, whether investing in cash, equities or other instruments, must be appropriately reflected in the apportionment formula. As previously mentioned, it is acknowledged that the gross interest received is not reflective of how a municipality applies its resources. For this reason, any interest received from investments not otherwise specifically mentioned in the formula, must be included as follows: Interest received for the year × (prime rate − JIBAR) The interest received includes interest on any cash investment placed by a municipality, such as a savings, cash management or fixed deposit account. • Debtor interest

	Any municipality that has outstanding debtor accounts in their accounting records, have included the full value of the original supply in their apportionment formula. In order to ensure equity in the manner of which these income streams are included in the formula, the gross interest levied on the debtors' accounts must be included in the formula. This extends further to any 'penalty interest' charged to a customer that does not fall under section 2(1)(f), to be included in 'c' of the formula.
A3	<u>Dividends</u> The MSA allows municipalities to provide services through other entities, referred to as municipal entities. These entities are generally owned by one or more municipality. Furthermore, to ensure financial security, municipalities may also invest in various instruments both for the yield and financial growth associated with certain markets. Dividends, including dividends in specie, are the yield paid on investments in equity and similar instruments. In keeping with the principle of reflecting all investment activities in the formula as set out in A1, dividends received must be included in the formula to reflect the investment activity in said instruments (even though dividends are not consideration for any supply made by a municipality). The investment activity associated with the holding of investments (such as shareholdings held through an asset manager), must be fairly reflected in the formula. Having regard to the fact that an entity declares and pays dividends based on various requirements and factors (such as a group's dividend policy or economic and market conditions), it is accepted that the quantum of dividends does not fairly reflect the investment activity of holding the investments as capital assets. In addition, significant fluctuations may be experienced in the value of dividends declared from year to year. In order to appropriately reflect a municipality's investment activity in the formula, the value of dividends to be included in the formula must be determined as follows: 3-year moving average of dividends received × (prime rate − JIBAR)

	• The 3-year moving average is determined by calculating the average of dividends received during the current financial year and two immediately preceding financial years. • If a municipality does not receive dividends during the current financial year, a 3-year moving average of the 3 preceding years may be used as proxy. • If a municipality receives no dividends for at least 2 out of the 3 years, a 5-year moving average must be used instead of the 3-year moving average where dividends were received for at least 2 of the 5 years. If a municipality has not received dividends for 2 out of the 5 years as required above, the municipality must approach SARS for an alternative manner of determining a value to be included in the formula that appropriately reflects its investment activities. The application must comply with the time limitations set out in the proviso to section 17(1)

13. GUIDES

13.1. Withholding tax on royalties return (WTR01)

This guide provides guidelines regarding the completion of the Withholding Tax on Royalties return (WTR01), how to make payment on eFiling and apply for a refund using the Rev16 form.

Sections 49A-49H of the Income Tax Act was introduced to deal with Withholding Tax on Royalties. It is common practice for a country to subject payments made to a foreign person (non-resident) to a withholding tax, such taxes are payable to SARS by the South African resident who pays the amount on behalf of the non-resident.

A ‘foreign person / non-resident’ is defined in section 49A as ‘any person that is not a resident’ in that country and it includes a natural person, a deceased estate, an insolvent estate, a company, and a trust.

A ‘royalty’ is defined as ‘any amount that is received or accrues in respect of the:

- Use or right of use of or permission to use any intellectual property as defined in section 23I; or

- Imparting of or the undertaking to impart any scientific, technical, industrial or commercial knowledge or information, or the rendering of or the undertaking to render any assistance or service in connection with the application or utilisation of such knowledge or information'.

Any person making payment of any amount of royalties to or for the benefit of a foreign person must withhold an amount of Withholding Tax on Royalties from that payment.

Royalties paid or which became due and payable on or after 1 July 2013 but before 1 January 2015 attracted a withholding rate of 12% of the amount of royalties paid.

For all royalties paid or which become due and payable on or after 1 January 2015, the Withholding Tax is calculated at a rate of 15% of the amount of royalties paid.

13.2. Guide for Motor Dealers – VAT 420 (Issue 3)

This guide concerns the application of the value-added tax (VAT) legislation in respect of vendors that supply motor cars and other vehicles (motor dealers).

For the most part, the general VAT principles as set out in the VAT 404 – Guide for Vendors will apply to motor dealers. The information in this guide should therefore be read together with the VAT 404 – Guide for Vendors. This guide expands on the application of the normal VAT principles with regard to specific types of transactions which are of interest to motor dealers1 and the motor industry in general.

The approach to the topic and the layout of the material in this guide is set out as follows:

Chapter 1 – This chapter sketches the general VAT principles concerning the VAT treatment of the supply of motor vehicles in the Republic. An important aspect in this regard is that, as a general rule, a vendor may not deduct input tax on the acquisition of a 'motor car' as defined in the VAT Act. However, this rule does not apply to a vendor that supplies motor cars for a consideration in the ordinary course of conducting an enterprise. A brief overview is also provided on the basic principles of VAT and how it applies to motor dealers.

Chapter 2 – This chapter introduces the reader to some of the more important concepts and definitions contained in the VAT Act. It also deals with terminology used in the motor industry which is relevant for the purposes of certain topics to be discussed in later chapters.

Chapter 3 – In this chapter the various types of supplies which are made by motor dealers are discussed in some detail. In particular, the focus is on the nature of the supplies and whether output tax must be declared by the motor dealer, or by some other vendor in the case where the motor dealer has acted as agent.

Chapter 4 – It is important for motor dealers that are involved in exporting vehicles to draw a distinction between direct and indirect exports, as well as new and second-hand motor vehicles exported, as the VAT treatment differs. This chapter therefore discusses the rules for applying the zero rate of VAT to different types of exports, the applicable documentation which a vendor is required to hold to justify the charging of VAT at the zero rate on exports, and the possible VAT adjustments which may be required when the export documentation is not received timeously.

Chapter 5 – The different circumstances under which goods are imported into the Republic are discussed. As the normal rules in this regard are discussed in the VAT 404 – Guide for Vendors, this chapter focuses on specific types of imports which may apply to motor dealers. For example, the temporary import of vehicles for the purpose of servicing or repair, transshipment of vehicles destined for export countries, and certain aspects concerning warranties.

Chapter 6 – This chapter focuses on the different types of supplies acquired or goods imported by motor dealers in the course of conducting an enterprise and sets out the rules with regard to the deduction of input tax in that regard.

13.3. VAT Connect – Issue 19 – June 2025

Recent amendments

The public was alerted to the publication of the 2024 draft tax bills and the draft Regulations on 31 August 2024 in VAT Connect Issue 18. These bills and draft Regulations have since been promulgated and the following Acts containing amendments to the VAT Act as well as the Regulations were published. These amendment Acts were all promulgated on 24 December 2024 as per *Government Gazettes* (*GGs*) 51826, 51827, 51829, and 51828 respectively. The amendments come into effect on 1 April 2025 unless otherwise stated.

A summary of some of the more important VAT amendments is provided below:

- Resident of the Republic:

  Before the amendment, the definition of 'resident of the Republic' referred to the definition of 'resident' in section 1(1) of the Income Tax Act, which in turn, in the case of a person other than a natural person, includes a person that has its place of effective management in South Africa.

  Consequently, supplies by South African companies to its foreign subsidiaries that had their place of effective management in South Africa, were excluded from the zero-rating provisions under section 11(2)(ℓ) despite these foreign subsidiaries being incorporated and having a fixed place of business in a foreign country with no consumption of such services taking place in South Africa.

  Since the foreign subsidiaries do not conduct any enterprise activities in South Africa, these subsidiaries are unable to register as vendors to unlock the VAT charged. This resulted in a permanent cost for businesses.

  The amendment to the definition of 'resident of the Republic' now excludes a person that is a 'resident' under the Income Tax Act, solely as a result of having its place of effective management in South Africa and that does not carry on any 'enterprise' in South Africa.

- Cross border leases of foreign owned ships, aircraft, rolling stock and parts thereto:

  On 1 April 2021 the definition of 'enterprise' was amended, and proviso (xiii) was added to clarify that a non-resident lessor of foreign owned ships, aircraft, and rolling stock are not considered to be conducting an enterprise in South Africa.

  Effective from 1 April 2023, this proviso was extended to include foreign owned parts relating to such foreign owned ships, aircraft, or rolling stock if those parts are leased under a separate agreement. As a result, foreign lessors that no longer carried on an 'enterprise' were required to deregister as vendors.

  This led to an unintended consequence as these foreign lessors had to account for output tax on the deemed supply of any goods that formed part of the enterprise assets retained upon deregistration, even though these foreign lessors were not entitled to a deduction of input tax on the importation of those goods (see paragraph (cc) of proviso (xiii) to the definition of 'enterprise').

To address this issue, proviso (vii) to section 8(2) has been inserted with the intention of releasing foreign lessors from the obligation to account for VAT on enterprise assets retained upon deregistration as a result of the aforementioned amendment, provided the requirements in the said proviso are met.

- Foreign donor funded projects (FDFPs):

  Significant changes to the registration regime for FDFPs took effect on 1 April 2020. These changes required an implementing agency to register a branch separate from the implementing agency's own registration, for each FDFP managed and administered by that implementing agency.

  This created a considerable administrative burden for both SARS and the implementing agencies, especially those managing and administering multiple FDFPs. On the basis that international donor funding agreements typically require strict record-keeping, and approval is required for a FDFP from the Minister of Finance, the risk of abuse is mitigated.

  To ease the administrative burden, section 8(30) now allows for multiple FDFP VAT branches managed and administered by an implementing agency to be merged into a single FDFP VAT branch, provided the implementing agency complies with the additional documentary requirements under the amended section 50(2A).

  Section 50(2A) also includes special transitional rules for those FDFP projects that were already registered as separate VAT branches of the implementing agency before 1 January 2025.

  These amendments came into effect on 1 January 2025. For further information on this topic see the updated VAT Reference Guide for Foreign Donor Funded Projects (Issue 3).

- Mudaraba Sharia Financing Arrangements:

  Various tax acts were amended to place Islamic finance on equal footing with traditional western finance from a taxation perspective.

  Given the diversity of Islamic finance, the focus was on the more prevalent Sharia compliant arrangements in South Africa at the time, namely, Mudarabah, Murabaha, and Diminishing Musharaka. However, section 8A that has been inserted with effect from 1 January 2013, initially made special provision only for Murabaha and Diminishing Musharaka.

Section 8A(3) now clarifies that the return of profit under a Mudaraba arrangement will also be exempt from VAT. However, this exemption does not extend to any consideration in the form of a fee, commission, or similar charge.

- Irrecoverable debts subsequently recovered:

  A vendor is allowed to deduct VAT on taxable supplies on which output tax has been previously accounted for to the extent of any amount subsequently written off as irrecoverable debts under section 22(1).

  If the vendor later recovers any of these amounts or any portion of those amounts, section 22(2) requires the vendor to repay the previously deducted VAT.

  Proviso (iv)(aa) to section 22(1) prevents a transferor of an account receivable at face value, on a non-recourse basis, from making a deduction based on the transfer.

  Whilst the recipient of such account was allowed to make a deduction of the tax amounts written off as irrecoverable, there was no rule for repaying these deductions if the amounts were later recovered. Section 22(2) has now been updated to include this rule.

- Fuel levy goods and illuminating kerosene:

  Consequential amendments have been made to sections 11(1)(h) and (ℓ), as well as Schedule 1 due to amendments made to Schedule 1 of the Customs and Excise Act. These amendments are effective from 1 January 2002.

- Electronic services and intermediaries:

  Section 54(2B) effective from 1 April 2019, required an intermediary to report and account for VAT on ‘electronic services’ supplied on behalf of a foreign electronic services provider that was not registered for VAT (the principal) in the intermediary’s own VAT return.

  The foreign electronic services supplier that exceeded the VAT registration threshold, but failed to register, however, remained principally liable to register and account for the VAT in its own return.

  Section 54(2B) now allows the intermediary and the principal to agree in writing to treat a supply of electronic services by the intermediary on behalf of the principal, as being made by the intermediary. In this instance, both the intermediary and principal will be held jointly and severally liable for performing

the relevant duties under the VAT Act and for paying the relevant tax on the taxable supplies made under such agreement.

These amendments also apply to principals already registered for VAT (in their own capacity) to reduce the administrative burden on the principal, prevent double accounting of VAT by both the principal and the intermediary on the same supply, and facilitate compliance checks and audits.

For more information on electronic services and intermediaries, see the Frequently Asked Questions: Electronic Services.

- Imported services:

Before the amendment to section 14(1), VAT on imported services had to be accounted for and paid within 30 days of the earlier of receipt of the invoice issued by the supplier or the recipient or the time any payment is made by the recipient in respect of that supply.

Taxpayers experienced various practical difficulties in adhering to the 30-day rule, resulting in penalties and interest due.

To alleviate the burden, the 30-day period under section 14(1) was extended to 60 days with effect from 24 December 2024.

- Overpayments on imported services or the importation of goods:

VAT is payable on ‘imported services’, and the importation of goods by any vendor within prescribed timelines.

However, these VAT amounts may be reduced due to subsequent events such as the granting of a discount, an error in stating the original amount, a reduction in consideration charged, or the cancellation of the supply.

Following the introduction of the Tax Administration Act, reductions in the amount of tax chargeable due to subsequent events in respect of the importation of goods by persons who are not registered as vendors (non-vendors), or in respect of imported services without an assessment, were not adequately catered for.

This has now been rectified by allowing a vendor to make a deduction of the excess tax under section 16(3)(o) in respect of imported services.

In addition, section 44(1) now provides for a refund on application by non-vendors of excess tax paid on imported services or the importation of goods,

provided the claim is received within five years from the date the excess tax was paid.

These amendments came into effect on 24 December 2024. See Binding General Ruling (BGR) 66 for more details on overpayments on the importation of goods by vendors.

- Representative vendor and South African bank account:

  Section 23(2) deemed a person who is not a 'resident of the Republic' to not have applied for registration until such person has appointed a representative vendor that is a resident in the Republic and opened a South African bank account.

  Many foreign entities, despite having no physical presence in South Africa, were required to register as vendors due to the wide definition of 'enterprise'.

  These entities faced difficulties complying with these registration conditions. To provide relief, section 23(2) has now been amended to assist non-resident vendors with limited or no presence in South Africa, in the circumstances specified in the proviso to section 23(2).

  These entities (including foreign suppliers of electronic services) must appoint a representative under the newly inserted section 46(2), although such natural person need not be a resident in South Africa.

  However, under the newly inserted section 23(2B), this relief is withdrawn if the entity no longer meets the requirements of sections 23(2)(b) and 46(1).

  These amendments are effective from 24 December 2024.

13.4. Guide to Advance Tax Rulings (Issue 2)

This guide provides:

- guidance in respect of the application for an advance ruling; and
- an overview of the Advance Tax Ruling (ATR) process.

The purpose of the advance ruling system is to promote clarity, consistency and certainty regarding the interpretation and application of a tax Act administered by SARS.

14. DRAFT GUIDES

14.1. Draft tax exemption guide for benefit funds

Taxation of benefit funds was developed piecemeal over a number of years and therefore not designed as a coherent whole, was complex, contained anomalies and was open to abuse. In 1994 the Katz Commission was tasked, amongst other things, to review and provide recommendations relating to the tax regime applicable to benefit funds. The relevant findings were published in the Sixth Report of the Katz Commission on Benefit Funds. This report provides the following background information and recommendation relating to friendly societies:

> ‘Friendly societies are essentially mutual organisations, in the sense that the members are the owners. They were once known as mutual aid societies. No employer - employee relationship is required. They have a long history in South Africa, legislation regulating them having been enacted as early as 1882 in the Cape and 1897 in Natal. The present Act dates from 1956 and their supervision is now in the hands of the Financial Services Board.
>
> In theory the range of services that may be provided to its members and their dependants by a friendly society is very wide - so wide, in fact, that most stokvels would have to register were it not for an exemption granted societies with annual incomes below R100 000. The range includes relief during minority, old age, widowhood and sickness; the granting of annuities and endowments; payments on the birth of a child or death of a family member; funeral expenses; insurance of implements used in a member's trade; financial assistance on resignation or dismissal; unemployment relief and the provision of sums of money for the advancement of the education or training of members or of the children of members.
>
> In practice, however, severe limitations are placed on what friendly societies may actually do. Despite being allowed to offer relief in old age they may not provide retirement benefits. Despite being allowed to pay annuities, no annuity may exceed . . . without falling foul of the Insurance Act. No death, disability, endowment or other benefit (which the Registrar of the Insurance considers to be an insurance benefit) may be offered . . . . A society is precluded from regularising the matter by registering as an insurer, as only companies may register as insurers - and friendly societies are not companies.

> The predictable result of these limitations is that the friendly society movement, while old and stable, has not flourished. There are no grounds for believing that it does, or can, provide a significant tax shelter. The Commission accordingly recommends that the existing exemption remain in place.'

The report provides the following background information and recommendation relating to medical schemes:

> 'The Registrar of Medical Schemes, in conjunction with a Council appointed by the Minister of Health, administers the Medical Schemes Act of 1967. Certain departments of state (defence, police, prisons) are not subject to its provisions; and certain industrial schemes are registered in terms of the Labour Relations Act. The latter are required to supply the Registrar with statistical information on a regular basis, so his Reports contain figures relating to about 85% of the industry.
>
> The medical schemes industry is clearly much the bigger - with an asset base 25 times, and an annual contribution rate 400 times, larger.
>
> The comparatively small volume of assets in the medical schemes industry leads to the same conclusion that was reached in the context of friendly societies. There is no significant danger of the industry being used to shelter other income, and no significant scope for tax arbitrage. The existing exemption from tax on the investment roll-up should remain in place. The Commission recommends accordingly, but places on record that the matter should be kept under continuous review if medical schemes in due course become vehicles for pre-funding post-retirement medical expenses. Such a development would necessarily involve the accumulation of substantial volumes of assets and change the situation fundamentally.'

The Katz Commission report on benefit funds made various recommendations, amongst other things, that friendly societies and medical schemes falling within the ambit of the definition of 'benefit fund' qualify for preferential tax treatment. The tax status of benefit funds was described in the report as follows:

> 'Benefit funds have an income tax regime of their own. Benefit funds are exempt from income tax. This exemption extends to contributions received and to investment income earned on amounts accumulated - the so-called 'roll-up'.'

Preferential tax treatment includes the advantage of an absolute exemption under section 10(1)(d)(ii) on all receipts and accruals. The exemption under section

10(1)(d)(ii) does not require any approval and is not subject to SARS' discretion, therefore, SARS does not issue letters to confirm the exemption of the receipts or accruals of a benefit fund under section 10(1)(d)(ii). All the receipts and accruals of a qualifying benefit fund are therefore automatically exempt from income tax.

In addition to being fully exempt from income tax, a qualifying benefit fund may also enjoy exemption from certain other taxes and duties.

In view of the above, it is critical that friendly societies contemplated in paragraph (a) and medical schemes contemplated in paragraph (b) meet the requirements of the definition of 'benefit fund'.

14.2. Draft guide to section 18A approval for specific United Nations Entities

The UN is an international organisation founded in 1945. The purpose of the UN can briefly be summarised as:

- maintaining international peace and security;
- developing friendly relations between nations based on respect for the principle of equal rights and self-determination of people;
- strengthening universal peace;
- achieving international co-operation in solving international problems of an economic, social, cultural, or humanitarian character;
- promoting and encouraging respect for human rights and for fundamental freedoms for all without distinction as to race, sex, language, or religion; and
- a centre for harmonising the actions of nations in the attainment of these common goals.

The UN is part of the UN System comprising many funds, programmes and specialised agencies each having their own area of work, leadership and budget. The UN co-ordinates its work with these separate UN System entities to achieve its goals.

Membership of the UN is in accordance with the UN Charter open to all peace-loving states accepting the obligations set out in the UN Charter, and in the judgment of the UN are able to carry out those obligations.

The status of the UN, its assets, officials, and the privileges and immunities member states must grant them are set out in the 1946 Convention. The 1946 Convention remains in force between the UN and a member state, which has deposited an instrument of accession, for as long as that member remains a member of the UN, or until a revised convention is approved by the General Assembly.

South Africa is one of the original founding members of the UN.South Africa's accession (with reservations) to the 1946 Convention took effect on 30 August 2002. South Africa is required as a member state to give effect to the 1946 Convention under law.

The co-ordination of the policies and activities of specialised agencies are recommended by the UN in the 1947 Convention. South Africa's accession to the 1947 Convention was approved by Parliament on 27 June 2001. South Africa is required to give effect to the terms of the 1947 Convention under law.

15. 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.