TAX UPDATE

For period: July 2025 to September 2025

Prepared by: Johan Kotze

JK TAX SPECIALISTS

Shepstone & Wylie ATTORNEYS

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1. FOREWORD

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

"An economy constrained by high tax rates will never produce enough revenue to balance the budget, just as it will never create enough jobs." – John F. Kennedy

"Government's view of the economy could be summed up in a few short phrases: if it moves, tax it. If it keeps moving, regulate it. If it stops moving, subsidize it." – Ronald Reagan

"Where there is an income tax, the just man will pay more and the unjust less on the same amount of income." – Plato

"Like mothers, taxes are often misunderstood, but seldom forgotten." – Lord Bramwell, 19th Century Jurist

"Next to being shot at and missed, nothing is quite as satisfying as an income tax refund." – F.J. Raymond

2. MEDIA STATEMENT: PUBLICATION OF THE 2025 DRAFT TAX BILLS AND DRAFT REGULATIONS FOR COMMENT

- **2025 Draft Taxation Laws Amendment Bill (2025 draft TLAB)**
- **2025 Draft Tax Administration Laws Amendment Bill (2025 draft TALAB)**
- **Draft regulations on the domestic reverse charge issued in terms of section 74(2) of the VAT Act**
- **Draft regulations prescribing the application of paragraph (d) of the definition of 'exported' in section 1(1) read with section 11(1)(a) of the VAT Act**

National Treasury and SARS today publish, for public comment, 2025 draft TLAB, 2025 draft TALAB, draft regulations on the domestic reverse charge relating to valuable metal in terms of section 74(2) of the VAT Act and draft 'export regulations'. These draft tax bills and draft regulations contain tax proposals made in the 2025 Budget on 12 March 2025 and updated on 21 May 2025.

- **2025 Draft TLAB**

The 2025 draft TLAB provides the necessary legislative amendments required to implement the tax announcements made in Chapter 4 and Annexure C of the 2025 Budget Review as well as technical corrections. Key tax proposals contained in the 2025 draft TLAB include the following:

- Reducing the threshold for ring-fencing of assessed losses
    - To close abuse and ensure fairness, government is proposing to lower the income threshold for the ring-fencing rule to ensure that losses from non-commercial trades cannot be used to avoid paying taxes.
- Tax treatment of foreign retirement benefits
    - It is proposed that an exemption be removed so that all foreign retirement benefits received by South African residents will be taxed in line with the country's residence-based tax system subject to applicable double taxation agreements.

- Refining the definition of ‘hybrid equity instrument’ in section 8E to strengthen the anti-avoidance measures
    - It is proposed that if an instrument is recognised as a debt liability for accounting purposes under International Financial Reporting Standards (IFRS), it will also be treated as debt for tax purposes.
- Reviewing asset-for-share and amalgamation transactions involving collective investment schemes to close loopholes
    - It is proposed that the corporate re-organisation rules afforded to collective investments schemes (CISs) be removed to stop the deferral or avoidance of tax that happens when shares are transferred to a CIS and later sold.
- Reviewing the VAT treatment of airtime vouchers supplied in South Africa for exclusive use in an export country
    - It is proposed that clarity be provided in law that the supply of the telecommunications service by the foreign supplier, is out of scope, resulting in only the distribution services by the South African distributors being subject to VAT at the standard rate.
- Low value importation of goods
    - It is proposed that the current tax-free limit on imported goods be removed, meaning that from now on low-value imports will be subject to VAT.

- **2025 Draft TALAB**

The 2025 draft TALAB provides legislative amendments dealing with tax administration announcements made in Annexure C of the 2025 Budget Review as well as technical corrections. Key tax proposals contained in the 2025 draft TALAB include the following:

- Clarifying the meaning of audit certificate to be issued by public benefit organisations
    - Some uncertainty exists about how the term ‘audit certificate’ must be interpreted and whether it should bear reference to terminology contained in the Auditing Profession Act (2005). It is proposed that the term be clarified in the context of this section.
- Enabling the VAT Modernisation Project

- This project forms part of a broader effort to transform tax processes, improve customer service and engagement, reduce the VAT gap and streamline tax administration for VAT traders, businesses, and SARS.

- Inspecting the business premises of a taxpayer applying for registration or approval
  - It is proposed that the provisions of the Tax Administration Act be expanded to include inspections for this purpose.
- Clarifying 'bona fide inadvertent error' for purposes of understatement penalties
  - To clarify the scope of 'bona fide inadvertent error', it is proposed that 'bona fide inadvertent error' be explicitly linked with 'substantial understatement'.

- **Draft regulations on the domestic reverse charge issued in terms of section 74(2) of the VAT Act**

The draft regulations on the domestic reverse charge contain proposals to amend the definitions of 'residue' and 'valuable metal' to resolve practical difficulties.

- Due to concerns that the previous rules for taxing gold were too broad, a new rule was introduced on January 1, 2024. This change limited the definition of 'residue' to only waste from mining and created a 1% threshold for what counts as a 'valuable metal.' It has become difficult to distinguish between mining waste and other types of gold-bearing waste. This proposed amendment seeks to address these issues.

- **Draft regulations prescribing the application of paragraph (d) of the definition of 'exported' in section 1(1) read with section 11(1)(a) of the VAT Act**

The delivery of coal at Richards Bay Coal Terminal (RBCT) by registered vendors for exportation from South Africa does not meet the requirements of regulation 8(2)(e)(ii) of the Export Regulation as RBCT is not the 'port authority' but licensed by the 'port authority'.

Therefore, the zero-rating will not find application. The draft Regulations on 'exported' propose that the wording of regulation 8(2)(e)(ii) be broadened to include any terminal

operators operating under a license of the port authority in terms of section 65 of the National Ports Act, 2005.

After receipt of written comments, National Treasury and SARS normally engage with stakeholders through public workshops to discuss the written comments on the draft tax bills and draft regulations.

With regard to the 2025 draft tax bills, the Standing Committee on Finance (SCoF) and the Select Committee on Finance (SeCoF) in Parliament will be requested to make a similar call for public comments and convene public hearings on the 2025 draft TLAB and 2025 draft TALAB, before their formal introduction in Parliament. The 2025 Rates and Monetary Amounts and Amendment of Revenue Laws Bill (the Rates Bill) was published for comment on 12 March 2025 and introduced in Parliament on 24 April 2025 (B14-2025). SCoF and SeCOF are to conduct public participation in respect of the Rates Bill.

Thereafter, a response document on the comments received will be presented at the parliamentary committee meetings, after which the draft Bills will then be revised, taking into account public comments and recommendations made during committee hearings, before they are tabled formally in Parliament for its consideration. For legal reasons, the tax amendments continue to be split into two types of bills, namely a money bill (section 77 of the Constitution) dealing with money bill issues and an ordinary bill (section 75 of the Constitution) dealing with issues relating to tax administration.

With regard to the draft regulations, after National Treasury and SARS have engaged with stakeholders through public workshops to discuss the written comments, the notices on regulations on domestic reverse charge relating to valuable metal in terms of section 74(2) of the VAT Act and regulations prescribing the application of paragraph (d) of the definition of ‘exported’ in section 1(1) read with section 11(1)(a) of the VAT Act will be published in the Government Gazette after considering public comments.

The 2025 draft tax bills, the accompanying draft explanatory memoranda containing a comprehensive description of the proposed tax amendments contained in the draft tax Bills, the draft regulations on the domestic reverse charge and draft ‘export’ regulations can be found on the National Treasury (www.treasury.gov.za) and SARS (www.sars.gov.za) websites.

More general information underlying the changes in rates, thresholds or any other tax amendments can be found in the 2025 Budget Review and Budget Overview, available on the National Treasury website.

Due date for public comments on the 2025 draft tax bills and draft Regulations National Treasury and SARS hereby invite comments in writing on the 2025 draft TLAB, 2025 draft TALAB, the draft regulations on the domestic reverse charge and draft 'export' regulations.

Please forward written comments to the National Treasury's tax policy depository at 2025AnnexCProp@treasury.gov.za and SARS at 2025legislationcomments@sars.gov.za by close of business on 12 September 2025.

ISSUED BY NATIONAL TREASURY ON 16 AUGUST 2025

3. DRAFT EXPLANATORY MEMORANDUM ON THE DRAFT TAXATION LAWS AMENDMENT BILL, 2025

3.1. Amending the definition of 'remuneration proxy'

[Applicable provisions: Definition of 'remuneration proxy' in section 1(1) of the Income Tax Act, No. 58 of 1962 ('the Act')]

Background

The term 'remuneration proxy' is defined in section 1 of the Act and is used in a variety of provisions throughout the Act. It serves as a reference point for calculating certain tax benefits, thresholds, and values where actual remuneration for the current year may not be available. It is often equated with 'remuneration' as defined in the Fourth Schedule to the Act and is particularly relevant for formula-based calculations where prior year remuneration is used as a proxy for present-year values.

Reasons for change

It has been identified that, in some instances, taxpayers who qualified for a foreign employment income exemption under section 10(1)(o)(ii) of the Act in the previous year of assessment may have an artificially reduced remuneration proxy in the current year of assessment. Since the remuneration proxy excludes exempt income, this can create unintended tax advantages in multiple contexts, including but not limited to fringe benefit calculations. Reflecting on horizontal equity considerations, this loophole creates an inconsistent tax treatment affecting numerous individual taxpayers.

Proposal

It is proposed that the definition of 'remuneration proxy' in section 1 be amended to include income that was exempt under section 10(1)(o)(ii) of the Act. This amendment would ensure that the remuneration proxy better reflects a taxpayer's actual economic participation and aligns with the broader intent behind the utilisation of the remuneration proxy concept.

Effective date

The proposed amendment will come into operation on 1 March 2026 and apply in respect of years of assessment commencing on or after that date.

3.2. Clarifying the inclusion of an amount assigned to a non-retirement fund member spouse under religious tenets

[Applicable provision: Paragraph 2(1)(b)(iA) of the Second Schedule to the Act]

Background

The Pension Funds Act No. 24 of 1956 ('the PFA') provides for certain deductions to be made from a member's benefit or minimum individual reserve. Section 37D(1)(d)(i) of the PFA previously allowed a retirement fund to deduct an amount assigned to a non-member spouse under a divorce order granted in terms of section 7(8) of the Divorce Act No. 70 of 1979. Similarly, the Income Tax Act provides that an amount assigned in terms of a divorce order under section 7(8) of the Divorce Act must be included in the recipient's gross income under paragraph (e) of the definition of gross income.

Reasons for change

In 2024, the PFA was amended to recognise the assignment of retirement fund interests to non-member spouses under religious tenets. The amendment acknowledges cultural and religious practices in asset division following marital dissolution.

However, despite the legal recognition under the PFA, the Income Tax Act has not been updated to accommodate this development. Specifically, paragraph 2(1)(b)(iA) of the Second Schedule does not explicitly include such religiously sanctioned transfers, creating uncertainty in tax treatment. Government seeks to amend the Act to accommodate court orders relating to the division of

retirement fund assets to a non-retirement fund member spouse under religious tenets.

Proposal

It is proposed that similar wording be added to the provisions of paragraph 2(1)(b)(iA) of the Second Schedule to the Act to provide for an inclusion of an amount assigned to a non-member spouse under the tenets of a religion.

Effective date

The proposed amendment will come into operation on 1 March 2026 and apply in respect of years of assessment commencing on or after that date.

3.3. Reducing the threshold for ring-fencing of assessed losses

[Applicable provision: Section 20A(2) of the Act]

Background

In general, individuals are allowed to offset losses from one trade against income from another, thereby reducing their overall tax burden. However, to prevent abuse of this principle by individuals engaging in activities that are not genuine profit-making enterprises, section 20A of the Act ring-fences losses from certain types of trades under specific conditions. Where applicable, such losses may only be set off against future income from the same trade and not against other income, such as salary income.

The purpose of this rule is to prevent taxpayers from disguising hobbies or lifestyle ventures as businesses, allowing them to reduce taxable income using expenses from these activities.

Section 20A of the Act applies only when two conditions are met:

- the taxpayer falls within the highest income tax bracket (e.g., taxable income of more than R1.817 million for the 2026 year of assessment); and
- the trade results in an assessed loss in at least three of the preceding five years or is one of nine specified listed suspect trades.

These trades include sporting activities, dealing in collectibles, performing or creative arts, gambling, farming (unless full-time), and renting out residential

accommodation, vehicles, aircraft or boats (unless at least 80% use is by unrelated parties).

Reasons for change

It has come to Government's attention that some taxpayers who are taxed only below the top marginal tax rate, are increasingly using strategies to claim losses from suspect trades to reduce their taxable income.

Section 20A of the Act currently applies to taxpayers who are taxed at the top marginal tax rate, but certain taxpayers slightly below the top marginal tax rate continue to avoid tax by offsetting losses that would otherwise be ring-fenced. When the nature of the trade falls under section 20A(2) of the Act, the rules cannot apply unless both taxable income and trade-type thresholds are met. To address this, Government intends to reduce the taxable income threshold in section 20A(2) of the Act.

Proposal

It is proposed that the taxable income threshold in section 20A(2) of the Act be lowered so that ring-fencing can apply to more taxpayers engaged in suspect trades and consistently claiming suspect trade losses in determining taxable income. This adjustment would close the avoidance by some individuals earning below the maximum tax bracket. These changes will enhance compliance and protect the integrity of the tax base.

The proposed amendment will come into operation on 1 March 2026 and apply in respect of years of assessment commencing on or after that date.

3.4. Reinstating the exemption for child maintenance payments funded from after-tax income

[Applicable provision: Section 10(1)(u) of the Act]

Background

Child maintenance payments are made by one parent to another for the support and wellbeing of a child, usually following a separation or divorce. These payments are often made from the payer's after-tax income, and traditionally, the recipient parent was not taxed on the amount received. In 2007, the PFA was amended to allow for court-ordered reductions in a member's retirement

fund for child maintenance payments. This prompted related changes to the Act, including:

- Introduction of section 7(11) of the Act, which deems such maintenance amounts to accrue to the retirement fund member.
- Reworking of paragraph (b) of the 'gross income' definition to include a new subparagraph (ii) for maintenance under a court order.
- Amendment of section 10(1)(u) of the Act to preserve the exemption for maintenance but to carve out an exception for amounts paid from a retirement fund and taxed in the hands of the member.

The intent behind the 2007 changes was to maintain the principle that withdrawals from retirement funds should be taxed under the EET (exempt-exempt-tax) system. At the same time, maintenance not funded from retirement savings remained exempt. In 2008, recurring payments were removed from the Second Schedule to the Act and treated as ordinary income for PAYE purposes. However, during this process, the exemption for non-retirement fund child maintenance payments was inadvertently removed. No explicit policy rationale was provided in the 2008 and 2009 Explanatory Memoranda to suggest that general child maintenance should become taxable.

Reasons for change

Since 2009, child maintenance payments made from after-tax income have been included in the taxable income of the recipient. It is consistent with tax principles that the payer is not entitled to a deduction for child maintenance payments, as prohibited by section 23(a) of the Act. However, taxing these payments in the hands of the recipient is an anomaly. These payments are not income intended for the recipient, but rather as financial support intended solely for the upbringing and welfare of the child. Accordingly, subjecting child maintenance payments to tax in the hands of the recipient does not align with the intended objective of the tax system. Government intends to restate its position that child maintenance payments should be tax-exempt in the hands of the recipient.

Proposal

It is proposed that the Act be amended to exempt child maintenance payments funded from after-tax income. The aim is to ensure that ordinary child

maintenance payments funded from after-tax income remain tax-exempt in the hands of the recipient.

Effective date

The proposed amendment will come into operation on 1 March 2026 and apply in respect of years of assessment commencing on or after that date.

3.5. Clarifying payment of death benefits

[Applicable provision: Definition of 'savings component' in section 1(1) of the Act]

Background

In the current legislative framework, death is treated as a 'retirement' event for tax purposes. This means that lump sum payouts from both the vested and retirement components qualify as retirement fund lump sum benefits, which are taxed according to favourable lump sum tax tables. Lump sum payouts from the savings component remain taxable as a savings withdrawal benefit subject to marginal tax rates in the hands of a nominee or dependant, upon a member's demise.

Reasons for change

It has come to Government's attention that lump sum payments from the savings component to nominees or dependants upon a member's death are being treated as a savings withdrawal benefit, i.e., taxed as ordinary income in the hands of the nominee or dependant, rather than as a retirement fund lump sum benefit. Government seeks to align all three components to have a uniform tax treatment towards death benefits.

Proposal

It is Government's intention that nominees or dependants have the flexibility to elect a lump sum payout or annuity payments without adverse tax consequences. Government proposes that the Act be amended to clarify that death benefits payable to a nominee or dependant as a lump sum from the member's interest in all three components (vested, retirement and savings), qualify as retirement fund lump sum benefits taxable at favourable lump sum tax rates.

Effective date

The proposed amendment is deemed to come into operation on 1 September 2024.

3.6. Cross-border tax treatment of retirement funds

[Applicable provision: Section 10(1)(gC)(ii) of the Act]

Background

Section 10(1) (gC)(ii) of the Act provides an exemption for certain retirement benefits received by South African residents. Specifically, it exempts any lump sum, pension or annuity received by or accrued to a resident from a source outside South Africa, if that amount is received or accrues as consideration for past employment outside South Africa. This provision was designed to prevent double taxation on retirement income already taxed in the foreign jurisdiction or earned while a person was not subject to South African tax. South African residents who worked abroad and contributed to a foreign retirement fund qualify for the section 10(1)(gC)(ii) exemption in South Africa. This applies to foreign-sourced retirement benefits as consideration for past employment outside South Africa.

Reasons for change

Call for reform

The issue of cross-border pensions and the tax treatment of foreign retirement benefits has long been recognised. In the 2013 Budget Review, it was noted that:

> ‘South African residents working abroad and foreign residents working in South Africa regularly contribute to local and foreign pension funds, giving rise to a variety of tax issues. While certain limited rules have long been in place, these rules are largely ad hoc. With overall retirement reform now in effect, cross-border pension issues need to be fully reconsidered.’

While a number of provisions have addressed cross-border pension issues over time, these have generally evolved in response to specific needs rather than through a unified framework.

Further, the 2022 Budget Review stated that:

‘A review of the exemption of foreign retirement benefits in domestic tax legislation will be conducted.’

In the 2024 Budget Review, the Government acknowledged the need to enhance the rules that currently exempt lump sums, pensions, and annuities received by South African residents from foreign retirement funds for past employment outside South Africa, so that these amounts are taxed fairly and consistently.

Current exemption rules

There are two main issues with the current blanket exemption under section 10(1)(gC)(ii) of the Act:

Issue 1

Firstly, the exemption may result in double non-taxation, particularly where the foreign jurisdiction does not tax the retirement income due to domestic law or tax treaty limitations. In these cases, neither South Africa nor the foreign jurisdiction imposes tax on the retirement benefit. This undermines South Africa's residence-based system of taxation and leads to revenue forgone to the fiscus.

Issue 2

Secondly, in instances where a DTA grants South Africa the exclusive right to tax such retirement benefits based on residence, South Africa forfeits this right by maintaining the exemption in section 10(1)(gC)(ii) of the Act. As a result, the foreign jurisdiction, despite lacking primary taxing rights under the treaty, may choose to tax the retirement benefits because South Africa does not tax them. This misalignment allows the foreign jurisdiction to benefit from taxing rights that South Africa does not exercise. The South African fiscus ultimately forgoes revenue that it is entitled to collect.

<u>Proposal</u>

It is proposed that section 10(1)(gC)(ii) of the Act be deleted to ensure that foreign retirement benefits received by South African residents are appropriately taxed in accordance with the residence basis of taxation, therefore upholding South Africa's treaty rights to tax.

Effective date

The proposed amendment will come into operation on 1 March 2026 and apply in respect of years of assessment commencing on or after that date.

3.7. Extending the anti-avoidance rules dealing with third-party backed shares

[Applicable provision: Section 8EA of the Income Tax Act]

Background

The Act contains dedicated third-party backed share anti-avoidance rules to deal with shares or equity instruments with dividend yields backed by third parties through an enforcement right. As a result, any dividend or foreign dividend received by or accrued to a person during any year of assessment in respect of a share or equity instrument, is deemed in relation to that person to be an amount of income received by or accrued to that person if that share or equity instrument constitutes a third-party backed share at any time during that year of assessment.

A 'third-party backed share', as defined in the Act, encompasses any preference share or equity instrument (the value of which is determined based on a preference share) in respect of which an enforcement right is exercisable by the holder of that preference share or equity instrument as a result of any amount of any specified dividend, foreign dividend, return of capital or foreign return of capital attributable to that share or equity instrument not being received by or accruing to any person entitled thereto.

An 'enforcement right', as defined in the Act, denotes the right of a holder or any person that is a connected person in relation to that holder of a share or equity instrument to compel the performance of obligations by third parties, in relation to that share or equity instrument, to:

- acquire that share or equity instrument from that holder;
- make any payment in respect of that share or equity instrument in terms of a guarantee, indemnity or similar arrangement; or
- procure, facilitate or assist with any of the above.

Reasons for change

The application of the 'third-party backed share' anti-avoidance rule is triggered when there is a dividend or foreign dividend received by or accrued to a person during any year of assessment and if that share or equity instrument constitutes a third-party backed share at any time during that year of assessment.

At issue is that structures have been identified that consist of transactions to circumvent these third-party backed share anti-avoidance rules through agreements that essentially includes the ability, in relation to the enforcement right of the holder, to dispense of that enforcement right in respect of a share or equity instrument. This enables the holder of a preference share or equity instrument to contractually waive any enforcement right before the dividend or foreign dividend is received by or accrued to that holder during a year of assessment. As a result, the third-party backed share trigger is avoided for the following year of assessment, as the anti-avoidance rule can no longer be applied to the subsequent dividend or foreign dividend received by or accrued in respect of that share or equity instrument in the absence of the enforcement right. The following simplified examples illustrate some of the tax avoidance structures:

Example 1:

Company A issues cumulative preference shares to Bank A in exchange for R1 million on 1 March 2026. The preference shares have a term of five (5) years, maturing on 28 February 2031. The yield on the preference shares is determined with reference to an interest rate of 2 per cent and is payable in full at the end of the term. The proceeds received by Company A in respect of the issuance of the preference shares are not applied towards any qualifying purpose.

Bank A holds a dispensable enforcement right, in the form of a third-party guarantee provided by Company H (the holding company of Company A), in respect of the yield on the preference shares.

No dividends are declared or paid during the first four years of the preference share term. Consequently, as the instrument approaches maturity, it accumulates a significant amount of rolled-up returns that become payable upon settlement at the end of year five.

The dispensable enforcement right permits Bank A to waive its right of enforcement against Company H. This waiver is exercised at the end of year four, on 28 February 2030. As a result, the preference shares cease to qualify as third-party backed shares in the subsequent year of assessment ending 28 February 2031. Given that no enforcement right is exercisable during that final year, the shares fall outside the scope of the anti-avoidance rules applicable to third-party backed shares. Accordingly, the dividend due or accrued on the preference shares may be paid free of any anti-avoidance measures upon settlement at the end of the term.

Example 2:

Company A issues cumulative preference shares to Bank A in exchange for R1 million on 1 March 2026. The preference shares have a term of six (6) years, maturing on 29 February 2032. The yield on the preference shares is determined with reference to an interest rate of 2 per cent and is payable in full at the end of every second year. The proceeds received by Company A in respect of the issuance of the preference shares are not applied towards any qualifying purpose.

Bank A holds a dispensable enforcement right, in the form of a third-party guarantee provided by Company H (the holding company of Company A or any person as agreed to between the issuer and holder from time-to-time), in respect of the yield on the preference shares.

The following structured periodic process is then applied over the following timeline:

- Preference share issued on 1 March 2026 and subject to an enforcement;
- Enforcement right waived by Bank A on 28 February 2027;
- Periodic rolled-up dividend paid free of anti-avoidance measures on 29 February 2028 to Bank A;
- Enforcement right re-enacted by Bank A on 1 March 2028;
- Enforcement right waived by Bank A on 28 February 2029;
- Periodic rolled-up dividend paid free of anti-avoidance measures on 28 February 2030 to Bank A;

- Enforcement right re-enacted by Bank A on 1 March 2030;
- Enforcement right waived by Bank A on 28 February 2031; and
- Settlement and last periodic rolled-up dividend paid free of anti-avoidance measures on 29 February 2032 to Bank A.

Proposal

Government proposes that the triggering provision, together with any related provision, be amended with additional measures to address the structuring ability of the dispensable enforcement right exercisable by either the holder or any connected person in relation to that holder in respect of a share or equity instrument.

It is proposed that section 8EA of the Act be broadened to account for the entitlement of the holder to compel the performance of obligations by third parties, during both the specific year of assessment or any previous year of assessment, in respect of that enforcement right.

As a result, if that holder or any person that is a connected person in relation to that holder of that share or equity instrument has the entitlement to compel the performance of obligations by third parties, through a enforcement right, during that year of assessment or any previous year of assessment, then any dividend or foreign dividend received by or accrued to a person, during any year of assessment in respect of a share or equity instrument must be deemed in relation to that person to be an amount of income received by or accrued to that person.

Example 3:

Using the facts from Examples 1 and 2 above:

The proposed extension essentially creates a deemed 'once-applied, always-applied' application of the third-party backed share definition if the holder has an enforcement right at any point, past or present, during period a shareholder is holding of the preference share. As such, regardless of whether Bank A's waiver of its enforcement right against a third-party is exercised at the end of year four, on 28 February 2030, as contemplated in Example 1 above, or periodically, as contemplated in Example 2 above, the application of the 'third-party backed share' anti-avoidance rule will be triggered when there is a dividend or

foreign dividend received by or accrued to a person during any year of assessment.

Effective date

The proposed amendment will come into operation on 1 January 2026 and apply to years of assessment commencing on or after that date.

3.8. Refining the definition of 'hybrid equity instrument'

[Applicable provision: Section 8E of the Act]

Background

The increasing sophistication of financial instruments presents ongoing challenges for tax authorities seeking to ensure equitable and effective taxation. Financial products are often structured with hybrid characteristics, blurring the traditional lines between debt and equity. At the main, is the specific challenge related to certain financial products, commonly referred to as 'preference shares', that exhibit characteristics of debt and often contain embedded derivatives that are designed to circumvent specific anti-avoidance provisions in tax legislation.

In general, section 8E of the Act was introduced as a crucial anti-avoidance provision to counter structures that sought to disguise what is, in economic substance, a debt instrument as an equity instrument, primarily in the form of preference shares. The core intention was to prevent companies from issuing instruments that functioned like loans but generated 'dividends' that could be received tax-exempt by certain holders, Historically, the legislation aimed to curb situations where fixed or preferential returns on these hybrid instruments allowed for tax advantages that were not aligned with their true economic nature. A key feature of the original section 8E of the Act targeted instruments with a redemption period of no longer than three years, identifying this as a characteristic indicative of a debt-like arrangement.

Reasons for change

It has come to Government's attention that financial institutions develop and issue complex financial products labelled as 'preference shares' that are listed on stock exchanges. Despite their equity label, these instruments possess fundamental characteristics more akin to debt, such as fixed or preferential

returns and often a pre-determined redemption obligation. They may also include embedded derivatives that influence their cash flows.

Crucially, while the economic substance of these instruments leads the holders to recognise them as debt for financial reporting purposes under International Financial Reporting Standards (IFRS), their legal form as ‘preference shares’ allows for potential tax arbitrage. Specifically, with reference to the anti-avoidance provision in section 8E of the Act, these products are often structured with a term exceeding the prescribed three-year period (e.g., three years and one day). This extended term is intentionally designed to circumvent the application of section 8E, which would otherwise deem dividends on such ‘hybrid equity instruments’ to be taxable income for the recipient.

Proposal

To address this challenge and align the tax treatment of these hybrid financial instruments with their economic substance, it is proposed that the definition of ‘hybrid equity instrument’ in section 8E of the Act be redefined as follows:

- To include any share or financial arrangement that is recognised according to its substance as debt (i.e., a financial liability) for financial reporting purposes by the holder of the financial instrument. This approach directly leverages the rigorous classification principles of IFRS to inform tax treatment, ensuring that the tax outcome reflects the economic reality and
- by removing the three-year requirement. This amendment would ensure that instruments that contain an obligation for the issuer to redeem them, thereby creating a financial liability for the issuer, are caught by section 8E, regardless of their duration.

As a consequence of the above amendment to the definition of ‘hybrid equity instrument’, the definitions of ‘date of issue’, ‘equity instrument’ ,’issue price’, and ‘qualifying purpose’ will become obsolete and thus deleted, whilst the definition of ‘financial instrument’ is broadened. The broadened definition will include any arrangement that gives rise to a financial asset of on entity and a financial liability of another entity, in accordance with IFRS, and any financial arrangement which has unknown or unspecified terms of repayment.

IFRS Perspective

IFRS place paramount importance on the substance over form principle when classifying financial instruments. Under IFRS, an instrument is classified based on its contractual terms and the economic reality, not merely its legal designation.

- IAS 32 Financial Instruments: Presentation is the primary standard governing the classification of financial instruments by the issuer as either financial liabilities or equity.
    - IAS 32, paragraph 11, defines a financial liability as ‘any liability that is: (a) a contractual obligation: (i) to deliver cash or another financial asset to another entity; or (ii) to exchange financial assets or financial liabilities with another entity under conditions that are potentially unfavourable to the entity; or (b) a contract that will or may be settled in the entity’s own equity instruments and is: (i) a non-derivative for which the entity is or may be obliged to deliver a variable number of its own equity instruments; or (ii) a derivative that will or may be settled other than by the exchange of a fixed amount of cash or another financial asset for a fixed number of the entity’s own equity instruments.’
    - IAS 32, paragraph 16, further clarifies that if an entity ‘does not have an unconditional right to avoid delivering cash or another financial asset to settle a contractual obligation, the obligation meets the definition of a financial liability.’ This is often the case with mandatorily redeemable preference shares or those redeemable at the option of the holder.
    - IAS 32, paragraph AG25 (Application Guidance), specifically addresses preference shares, stating that they may be classified as financial liabilities ‘because they are redeemable on a specific date or at the option of the holder, or because the dividends are cumulative and mandatory even if they are non-redeemable.’
- IFRS 9 Financial Instruments dictates the classification and measurement of financial assets (from the holder's perspective)

and financial liabilities (from the issuer's perspective), as well as the accounting for embedded derivatives.

- IFRS 9, paragraphs 4.1.2- to 4.1.4, outline the classification of financial assets. For an instrument to be measured at amortised cost (a debt-like measurement), its contractual cash flows must be ‘solely payments of principal and interest’ (SPPI test), and it must be held within a business model whose objective is to collect contractual cash flows. If the contractual terms do not give rise to cash flows that are solely payments of principal and interest (e.g., due to an embedded derivative that significantly modifies the cash flows), or if the business model is not appropriate, the instrument is often classified at Fair Value Through Profit or Loss (FVTPL), which aligns with debt instruments with complex features.
- IFRS 9, paragraphs B4.3.1 to B4.3.11 (Application Guidance), provide detailed rules on embedded derivatives. If a derivative is embedded in a host contract and is not ‘closely related’ to the host, it must be separated and accounted for as a standalone derivative at fair value through profit or loss. This separation typically occurs when the economic characteristics and risks of the embedded derivative are not clearly and closely related to those of the host contract.

Given that these instruments are already recognised as debt by the holder for financial reporting purposes, it strongly implies that their contractual terms, when subjected to the rigorous analysis of IAS 32 and IFRS 9, lead to a financial liability classification. This classification inherently means they possess characteristics that prevent them from being considered a residual equity interest and instead create a contractual obligation to deliver economic benefits (cash flows akin to interest and principal).

The above proposal directly aligns tax legislation with this established accounting substance and creates a consistent framework that reduces definitional arbitrage, simplifies compliance and ensures that instruments that

are economically debt are treated as such for tax purposes, thereby preventing the misuse of dividend exemptions to reduce tax liabilities unfairly.

Effective date

The proposed amendments come into operation on 1 January 2026 and apply in respect of years assessment commencing on or after that date.

3.9. Clarifying the ordering of set-off of balance of assessed losses and certain deductions

[Applicable provisions: Sections 18A and 29A of the Act]

Background

With effect from 2023, the set-off of the balance of assessed losses is limited to 80 per cent of taxable income for companies. Deductions for donations and transfers from policyholder funds of long-term insurers are limited with reference to 'taxable income', as defined.

Reasons for change

Government is aware of certain instances where uncertainty exists regarding the ordering of the set-off of the balance of assessed losses and deductions for donations and transfers from policyholder funds of long-term insurers.

Proposal

It is proposed that amendments be introduced to clarify the ordering of these deductions in calculating taxable income, i.e. that taxpayers should apply the limitation of a deduction from taxable income determined before the application of the said deduction and before setting off any balance of assessed losses contemplated in section 20 of the Act and that assessed loss limitation rules apply last (after all deductions have been taken into account).

Taxable income should be calculated by:

- determining the deduction limit of 10% of taxable income before the set-off of a balance of assessed loss under section 20(1)(a)(i) of the Act; and
- determining the transfer deduction before the deduction under section 18A and the setoff of a balance of assessed loss under section 20(1)(a)(i) of the Act.

Effective date

The proposed amendments will come into effect on date of promulgation of the Taxation Laws Amendment Act of 2025.

3.10. Clarifying the determination of contributed tax capital

[Applicable provision: Section 8G of the Act]

Background

Contributed tax capital (CTC) is a notional tax amount that assists in determining the ringfenced cost of a capital amount of any investment into any class of shares of a company. However, CTC is also reduced by an amount, referred to as a capital distribution, transferred back by the company to its shareholder.

Current CTC legislation contains various anti-avoidance mechanisms to counter a transaction that artificially create CTC within a resident company, which is used to avoid the payment of dividends tax by a non-resident group company.

Reasons for change

A dedicated anti-avoidance mechanism was introduced in 2017 to limit the value of the consideration received for the issue of the shares in the determination of CTC in those instances where there was an interposition of a new SA holding company (SA H-Co and the issuing company) between a foreign parent company (F-Co and the subscribing company) and its SA operating subsidiary (SA Op-Co and the target company). The anti-avoidance measure currently adjusts the value of the consideration received for the issue of the shares by the issuing company (SA H-Co), to the extent that either:

- that consideration consists of; or
- that consideration is used to directly or indirectly acquire;

shares in the target company (SA Op-Co) that also formed part of the same group of companies as the subscribing company (F-Co) prior to the transaction, to be equal to the value of the CTC in the target company (SA Op-Co).

The taxation consequences of this anti-avoidance measure may affect a limited number of legitimate corporate finance practices. At issue is that the current

anti-avoidance wording above could impede the ability of the subscribing company (F-Co) to extract the cost of capital in relation to any further legitimate corporate finance transactions through equity where, in effect, any consideration received for a further issue of shares by the issuing company (SA H-Co), within an existing group of companies, are used to acquire any already issued shares in a SA operating subsidiary, that itself is also a group company in relation to the subscribing company, at the time of the transaction, from independent minority shareholders.

The historic issue behind the insertion of the dedicated anti-avoidance measure in section 8G in the Act during 2017 was that any transaction contemplated in section 8G of the Act essentially merely reorganised ownership within the group of companies, with no or limited movement of any operational assets or utilisable cash capital funding.

Proposal

To accommodate the identified corporate financing transaction within a group structure as above, the dedicated anti-avoidance measure will specifically exclude an equity finance transaction, where at the time of the transaction, consideration is paid by the subscribing company (F-Co) to the issuing company (SA H-Co), a group company in relation to the subscribing company, for a further issue of its shares and where SA (H-Co) in turn uses that consideration to acquire additional shares in a SA operating subsidiary, a group company in relation to the subscribing company, from target company shareholders, that are (1) not connected persons to the subscribing company and (2) do not form part of the same group of companies in relation to the subscribing company, at the time of the transaction. As a result, the anti-avoidance measure contained in section 8G of the Act will not limit the 'contributed tax capital' of an issuing company in those instances where, essentially, independent minority shareholders in the target company (SA Op-Co), are bought out.

Effective date

The proposed amendments will be deemed to come into effect on 1 January 2026 and applies in respect of share acquired on or after that date.

3.11. Clarifying the rollover relief for listed shares in an asset-for-share transaction

[Applicable provision: Section 42 of the Act]

Background

Various roll-over provisions are contained in the Act and are designed to ensure that the recognition of any gain or recoupment is deferred when corporate entities are reorganised. In asset-for-share transactions, and more specifically within share-for-share reorganisations, roll-over relief is granted, subject to certain anti-avoidance provisions, where equity shares of a target company are disposed of by one or more target company shareholders to an acquiring company in exchange for newly issued shares of that acquiring company.

The roll-over provisions together with the various anti-avoidance characterisations and measures generally entails that the acquiring company obtains the target shares both in the same tax character (as either a capital asset or trading stock) and at the same applicable tax cost (as determined by the tax character mentioned above) as the target company shareholder immediately before the transaction.

However, in 2010, a unified special roll-over relief regime was introduced for listed shares-for-share reorganisations to address the practical difficulties experienced by the acquiring company of tracing the tax character and tax cost of the listed target equity shares held by numerous minority target shareholders. Under this special roll-over relief regime, relief is provided to the acquiring company to treat the listed target shares obtained as if they were acquired for cash at market value, on the date of the transaction, and without any regard to the historic nature of those listed target equity shares previously held by each target company shareholder. The impact on the acquiring company is essentially a step-up in tax cost and the elimination of the need to trace the original tax character attributable to the multiple minority shareholders who dispose of their listed equity shares to the acquiring company.

Reason for change

The 2010 unified special roll-over regime, as a policy intent, identified, amongst others, the following key conditions for the special roll-over relief to apply in share-for-share reorganisations, including that:

- the special roll-over relief applies only if the acquiring company obtains a sizeable interest in the target company because of the reorganisation. At the end of the share-for-share transaction, the acquiring company must generally hold at least 35 per cent of the shares in the listed target company. This threshold can be reduced to 25 per cent if no other shareholder holds an equal or greater shareholding in that target company as held by the acquiring; an
- more specifically, the special roll-over relief will only apply if the target company is listed and only for target shareholders not holding more than 20 per cent each of the target company before the transaction.

At issue is that current legislation does not clearly and effectively address government's policy intent and the practical tracing problem, in terms of the above-mentioned key condition, that the special roll-over relief regime in terms of tax character and tax cost of each listed target share, can only be applied by the acquiring company, on listed target equity shares obtained from each target company shareholder that holds less than 20 per cent of the listed shares in the target company before the transaction.

Proposal

It is proposed that legislation be amended to clearly align with the original policy intent and resolution of the practical tracing problem that the special roll-over relief regime for listed shares be limited only to listed target equity shares acquired from disposing target shareholders holding less than 20 per cent of the listed equity shares in the target company before the transaction.

The application of the special roll-over relief mechanism will be adjusted so that the key conditions be applied to both the tax character and tax cost of a listed target company share acquired by the acquiring company, with the same regard to any other asset-for-share transaction that is concluded on the same terms as the asset-for-share transaction and within the 90-day period after that disposal.

Effective date

The proposed amendment will come into operation on 1 January 2026 and apply in respect of years of assessment commencing on or after that date.

3.12. Reviewing asset-for-share and amalgamation transactions involving collective investment schemes

[Applicable provisions: Section 41, definitions of a 'company', 'equity share'; section 42, definitions of 'asset-for-share', 'qualifying interest' and section 44 of the Act]

Background

Collective Investment Schemes (CISs), such as unit trusts or mutual funds, are popular investment vehicles allowing individuals to pool their money to invest in a diversified portfolio of assets like shares, bonds, and property. Under the current South African Income Tax Act, CISs are treated as 'conduits' or 'flow-through' entities for income as defined for tax purposes. This means that:

- Income (like interest and REIT dividends) earned by the CIS is typically passed on to the individual investors (unitholders), who then declare and pay tax on that income in their personal tax returns.
- Capital Gains Tax (CGT) on asset sales by the CIS itself is disregarded. Specifically, paragraph 61(3) of the Eighth Schedule to the Act states that a CIS (with some exceptions) does not pay CGT when it sells assets within its portfolio. Instead, investors are liable for CGT only when they sell their units (participatory interests) in the CIS.

Furthermore, the Income Tax Act contains specific 'corporate reorganisation rules,' such as:

- Section 42 (Asset-for-Share Transactions): This provision allows a person to transfer an asset (for example shares in a company) to another company in exchange for shares in that receiving company, without immediately triggering tax (such as CGT) on the transfer. This is referred to as 'roll-over relief', deferring the tax consequences.
- Section 44 (Amalgamation Transactions): This provision provides similar tax deferral relief for certain company mergers or amalgamations, allowing assets to be transferred between merging entities without immediate tax consequences.

These provisions are designed to facilitate legitimate business restructurings by companies without creating immediate tax burdens.

Reasons for change

While the existing tax framework for CISs and corporate reorganisations serves important purpose, according to the discussion document on CISs published on 13 December 2024, transferring shares to a CIS without tax implications has allowed for unintended tax avoidance during changes of shareholdings in listed companies, as the realised gains in the shares are not taxed on transfer. To explain this in simpler terms:

- Tax-Free Transfer to CIS: An investor who holds shares that have increased in value (meaning they have unrealised gains) can transfer these shares to a CIS. By structuring this as an ‘asset-for-share’ transaction under section 42, the investor avoids paying Capital Gains Tax at the time of this transfer. Instead, the investor receives units in the CIS.
- Tax-Free Disposal by CIS: Subsequently, if the CIS then sells these same shares, for example, as part of a corporate restructuring (like a merger or acquisition involving the listed company) or simply as part of its investment strategy, the CIS itself does not pay CGT on that sale due to the specific exemption in paragraph 61(3) of the Eighth Schedule.
- The Loophole: The combined effect is that the capital gain on the original shares is ‘realised’ in the market (e.g., the listed company shares are disposed of by the investor and by the CIS, and the shares are effectively disposed of for a consideration in units or cash). However, neither the original investor nor the CIS pays tax on that gain at the point of its economic realisation. The investor's tax liability is deferred until they eventually sell their units in the CIS, which could be years later, or potentially avoided entirely by untaxed distributions by the CIS. This creates an imbalance compared to an investor who directly sells their shares and immediately pays CGT.

The realised gains are also not taxed when the CIS disposes of the shares as part of a corporate restructuring. This highlights how the interaction of these provisions can lead to a situation where significant capital gains escape the tax net at the point where they are economically realised.

As CISs are taxed on an adjusted trust basis, conceptually transactions involving CISs should not be qualifying for tax relief under corporate restructuring provisions that are focusing on transactions of companies.

Proposal

To address this unintended tax avoidance going forward and ensure a more equitable and consistent application of tax laws, it is proposed that the provisions relating to asset-for-share transactions (section 42) and amalgamations transactions (section 44), as they apply to transfers involving CISs be withdrawn to prevent the deferral or avoidance of tax on realised capital gains when shares are transferred to and subsequently disposed of by CISs in these specific circumstances.

Effective date

The proposed amendments will come into operation on 1 January 2026 and apply in respect of years of assessment commencing transactions entered on or after that date.

3.13. Refining and clarifying the meaning of 'interest' to enhance certainty

[Applicable provision: Section 23M of the Act]

Background

In 2021, the Income Tax Act (the Act) was amended to strengthen rules that govern the limitation of interest deductions. These rules are contained in section 23M of the Act to limit interest deductions when a South African debtor incurs interest; there is a direct or indirect controlling relationship between the debtor and creditor and the interest income is not taxed in the hands of the creditor. It has come to government's attention that these measures require further clarification in three areas.

Reasons for change

Refining and clarifying the definition of 'interest' to enhance certainty

There is complexity surrounding the definition of 'interest' in section 23M of the Act and its use in the calculation of 'adjusted taxable income'. Items such as foreign exchange differences were included in the definition of 'interest' to ensure that such items could not be used to deduct more interest. Section 23M targets interest deductions where there is a direct/indirect controlling relationship between the debtor and

creditor, and the ‘interest’ income is not taxable in the hands of the recipient.

Using the wider definition of ‘interest’ to determine whether interest limitation should apply creates complexity as it results in the rules applying to all foreign-denominated amounts owed, irrespective of whether the amounts bear interest (as defined in section 24J) or not, or whether the debt is between independent entities or not. In addition, all transactions involving ‘interest’ as defined would not in all instances result in the creditors/financiers receiving the same amount of interest.

Reviewing the carve-out for the interest limitation rules

The interest limitation rules do not apply to interest on debt in instances where the ultimate lending institution has no controlling relationship with the debtor and if the interest charged does not exceed the official rate of interest plus 100 basis points. However, the carve out may not apply where a creditor obtained the funding indirectly from the ultimate lending institution.

Clarifying the treatment of foreign exchange differences when there is no accrual for the creditor

The interest limitation rules acknowledge exchange differences on foreign exchange instruments under section 23M(7) of the Act. However, it is unclear how exchange differences should be treated when foreign exchange gains do not accrue to creditors. The foreign counterparty would not be within the scope of section 24I of the Act and the foreign exchange gain does not accrue to the counterparty.

Proposal

It is proposed that amendments be introduced to clarify the rules as follows:

- It is proposed that taxpayers should rely on the definition of ‘interest’ contained in section 24J of the Act to calculate ‘adjusted taxable income’ paragraph (a) of subsection (3) and in the words following paragraph (b) of subsection (3). This will remove the need to make adjustments for all the additional elements of ‘interest’ that are linked to third-party lending. There is no policy rationale to include these amounts in this calculation.

- To make it clear that the objective is to first test which debt should be focused on for the limitation of interest (i.e. there is a controlling relationship and no interest income inclusion for the creditor), before including additional interest elements, such as exchange differences thereon, 'interest' in section 23M(2) of the Act, except for the reference to interest immediately after paragraph (ii) in subsection (2) will be limited to interest, other than interest contemplated in paragraph (c) of the definition of interest in subsection (1).
- The reference to interest immediately after paragraph (ii) in section 23M(2) of the Act should still have the broader meaning of interest as defined in section 23M(1) of the Act.
- To ensure that interest deductions are not excessive, in section 23M(3) of the Act, the reference to interest before paragraph (a) will retain the wider definition of interest contained in section 23M(1) of the Act – subjecting interest deductions to the limitation test.
- It is proposed that back-to-back lending arrangements where there is no controlling relationship between the ultimate lending institution and the debtor and the creditor in relation to the debtor obtained the funding indirectly from the lending institution, also be eligible for carve-out from these rules.

Effective date

The proposed amendments will come into effect for years of assessment commencing on or after 1 April 2026.

3.14. Aligning the tax treatment of dividends with the accounting treatment by a covered person

[Applicable provision: Section 24JB of the Act]

Background

Income tax

Section 24JB of the Act was introduced to address financial instruments, as the rules governing income tax and financial accounting had significantly diverged. In summary, 'covered persons' are required to incorporate fair value

measurements and all other amounts in respect of financial assets and financial liabilities under International Financial Reporting Standards (IFRS) directly into their taxable income or loss within the same year of assessment. Specifically, they must include in taxable income the total value of all changes and amounts recognised through profit and loss for financial assets and liabilities, as defined and measured by IFRS

Accounting

IFRS 9 is central to the classification and measurement of financial instruments, including derivatives and equity investments used for hedging.

- *Classification and Measurement of Equity Investments*

  Broadly, IFRS 9, paragraph 5.7.5 (and related application guidance) states that for equity instruments not held for trading, an entity has the option to make an irrevocable election at initial recognition to present subsequent changes in fair value in Other Comprehensive Income (OCI). However, dividend income derived from such investments is generally recognised in profit or loss, unless the dividend clearly represents a recovery of a portion of the investment's cost (IFRS 9, B5.7.1). This implies that dividend income, even from an equity instrument designated to OCI, typically impacts profit or loss.

  While in summary, IFRS 9, paragraph 4.2.2 (and related guidance) states that equity instruments can be classified at fair value through profit or loss (FVPL) if they are held for trading, or if the entity makes an irrevocable designation at initial recognition to eliminate or significantly reduce an ‘accounting mismatch’. If an equity investment is held to hedge a financial liability (such as equity-linked notes) and that liability is measured at FVPL, then classifying the equity investment at FVPL would create a ‘matching’ of fair value movements directly in profit or loss. Therefore, dividends from FVPL instruments would likewise be recognised in profit or loss.

- *Hedge Accounting (Chapter 6 of IFRS 9)*

  In general, IFRS 9 establishes specific criteria for hedge accounting, which aims to align the accounting treatment of the hedging instrument (e.g., shares) and the hedged item (e.g., equity-linked notes) to accurately reflect the economic reality of the hedging relationship.

IFRS 9, paragraph 6.4.1 (and related guidance) states that in a fair value hedge, gains or losses on both the hedging instrument and the hedged item (to the extent attributable to the hedged risk) are recognised directly in profit or loss. If equity-linked notes are subject to fair value changes that affect profit or loss, and shares are formally designated as a hedging instrument in a fair value hedge, then dividend income (and fair value changes of the shares) would typically be recognised in profit or loss to achieve an accounting match.

While IFRS 9, paragraph 6.5.1 (and related guidance) states that in a cash flow hedge, the effective portion of changes in the fair value of the hedging instrument is recognised in OCI and subsequently reclassified to profit or loss when the hedged cash flows affect profit or loss. If dividends accruing on these hedges are hedging variable cash flows of the equity-linked notes, then the dividend income (or related cash flow changes) could be treated in a manner consistent with cash flow hedge accounting principles to achieve an accounting match.

IAS 12 Income Taxes

This standard dictates the accounting for income tax, encompassing both current and deferred tax. In general, IAS 12, paragraph 58 states that if a transaction is recognised in profit or loss, any related tax effects are also recognised in profit or loss. Conversely, if a transaction is recognised outside profit or loss (e.g., in OCI), any related tax effects are also recognised outside profit or loss.

Reasons for change

It has come to Government's attention that 'covered persons' are investing in shares and receiving dividends to hedge financial liabilities like equity-linked notes where the payments are tax deductible.

Proposal

Given that section 24JB of the Act already mandates the incorporation of most IFRS fair value measurements into taxable income for 'covered persons,' and considering that IFRS 9 often leads to dividend income from hedging instruments being recognised in profit or loss (especially for FVPL classifications or formal hedge accounting), it is proposed that dividends

received by ‘covered persons’ from equity investments used to hedge financial liabilities (such as equity-linked notes with tax-deductible payments) should also be subject to tax. This proposed change aims to directly align the tax treatment of such dividends with their financial accounting recognition in profit or loss, thereby mitigating existing tax mismatches and ensuring consistent treatment across financial reporting and taxation, which is further supported by the principles of IAS 12 regarding tax consequences following financial accounting treatment.

Effective date

The proposed amendment will come into operation on 1 January 2026 and apply in respect years of assessment commencing on or after that date.

3.15. Anomaly in the act relating to capital distributions by collective investment schemes

[Applicable provisions: Paragraph 61 and new paragraph 82A of the Eighth Schedule to the Act]

Background

Before 2010, unit trusts in South Africa were treated much like companies for tax purposes. Any income generated by the fund and distributed to unit holders was considered a taxable dividend from the unit trust itself. From 1 January 2010, the tax rules for unit trusts changed significantly. They now operate on a ‘conduit principle,’ which allows income (such as interest, dividends, rental income or trading income) earned by the fund to flow directly through to the individual unit holders without being taxed first at the fund level.

Generally, if the CIS fund realises a capital gain that gain is not taxed at the fund level due to the exclusion in paragraph 61 of the Eighth Schedule and also not to the investor (holder of a participatory interest) on distribution of the gain as there is no disposal by the holder. The tax on capital gains may only apply to the investor, when that investor sells units in the fund. At that point, capital gain or loss is based on the difference between the proceeds of units sold and the original cost.

Reasons for change

Despite the move to the ‘flow-through’ adjusted trust system on 1 January 2010, there's a specific area where the law is not clear: i.e. ‘capital distributions.’ These are payments made by a unit trust to its investors that come from the fund's ‘capital’, rather than from its income or trading profits from selling investments.

The existing tax law (specifically paragraph 61 of the Eighth Schedule to the Act) does not explicitly address how these ‘capital distributions’ should be treated. While rules exist for what happens when a fund is closed down (liquidated) – where payments are generally seen as proceeds from selling units – there's no distinct rule for payments made from the fund's capital while it is still actively operating.

This lack of clarity can lead to confusion for both investors and tax authorities. It creates uncertainty about how such payments should be taxed, potentially leading to inconsistent treatment or unintended tax outcomes. The current law doesn't prevent such distributions, but it doesn't provide clear guidance on their tax implications.

Proposal

To address this gap, it was proposed in the Discussion document that was published by the National Treasury in December of 2024 that ‘a new paragraph be inserted in the Eighth Schedule to the Act so that a capital distribution (distribution from a portfolio of a collective investment scheme (CIS) that is not income, prior to the disposal of a participatory interest in the CIS, the holder of that participatory interest must reduce the expenditure in respect of the participatory interest in a CIS by the amount of that distribution’.

However, based on the comments received it was stated that CISs will not be able to advise investors on the tax implications, as they do not have access to the investors’ base cost information. An alternative, and potentially simpler, approach could be to avoid adjusting the base cost of participatory interests altogether and instead treat all capital distributions as capital gains. It was noted that although this may lead to earlier tax liabilities for some investors, it would significantly reduce the complexity involved in adjusting base costs and the investors could fund the resulting tax liability from the amounts distributed. This trade-off could be worthwhile, especially considering that capital

distributions are typically infrequent and relatively minor overall. Therefore, it is proposed that all capital distributions be regarded as capital gains.

Effective date

The proposed amendment will come into operation on 1 March 2026 and apply in respect of disposals or distributions made, as the case may be, on or after that date.

3.16. Tax treatment of first loss after capital (FLAC) instruments as defined in the Financial Sector Regulation Act (2017)

[Applicable provisions: Sections 8F and 8FA of the Act]

Background

The global financial crisis of 2008 highlighted the critical need for robust resolution frameworks for financial institutions. A cornerstone of these frameworks is the enhancement of banks' loss-absorbing and recapitalisation capacity, designed to prevent the need for taxpayer-funded bailouts.

In line with these international prudential standards, South Africa has introduced First Loss After Capital (FLAC) instruments, as defined in the Financial Sector Regulation Act (2017). These instruments are designed to absorb losses and convert to equity during a bank's resolution, ensuring that the costs of failure are borne by shareholders and creditors rather than the public purse.

In general, FLAC instruments are a class of unsecured debt instruments issued by systemically important financial institutions (e.g., banks or their controlling companies). While distinct from traditional regulatory capital (Common Equity tier 1, Additional tier 1, and tier 2 capital), they serve a similar purpose of providing loss-absorbing capacity. They rank below senior unsecured debt but above regulatory capital in the creditor hierarchy, designed to convert into shares or be written off when a bank enters resolution. This mechanism facilitates an orderly resolution, ensures continuity of critical functions, and shifts the burden of bank failure to investors.

Globally, similar instruments include Total Loss-Absorbing Capacity (TLAC)-eligible debt (for Global Systemically Important Banks or G-SIBs) and Minimum

Requirements for Own Funds and Eligible Liabilities (MREL)-eligible debt (primarily in the European Union). Contingent Convertible Bonds (CoCos) and Additional tier 1 (AT1) instruments also share characteristics of loss absorption and conversion.

However, the effective implementation and market acceptance of FLAC instruments are significantly influenced by their tax treatment.

Reasons for change

The unique characteristics of FLAC instruments present several potential tax challenges under current tax legislation, which could inadvertently impede their effective issuance and prudential function. These challenges are mentioned below:

- *Issue: Application of Hybrid Debt Anti-Avoidance Rules*

  South African Context:

  Section 8F of the Act targets 'hybrid debt instruments'. This anti-avoidance provision aims to reclassify interest payments on certain debt instruments as non-deductible dividends if the instrument possesses equity-like characteristics (e.g., payments dependent on profitability, or long terms with no fixed repayment). Given the hybrid nature of FLAC instruments and tier Capital (particularly AT1, which has debt-like features but functions as equity for regulatory purposes), there is a concern that they could inadvertently fall within the scope of section 8F of the Act. If caught by section 8F of the Act, the interest payments on these vital instruments would become non-deductible for the issuing bank, significantly increasing its cost of funding.

  International Position:

  Globally, regulatory capital instruments (AT1 and tier 2) and other loss-absorbing debt (TLAC/MREL-eligible debt, which is analogous to FLAC) are designed to satisfy prudential requirements. While these instruments often have hybrid features that could trigger general hybrid anti-avoidance rules, many jurisdictions provide specific carve-outs or tailored tax treatments for them. The objective is to preserve the tax deductibility of interest paid on these instruments. For example, countries like the UK and Hong Kong have specific legislation or

administrative guidance that ensures interest on their regulatory capital and bail-inable debt instruments are treated as tax-deductible.

In UK, Finance Act 2019, Schedule 20 and The Taxation of Hybrid Capital Instruments (Amendment of Section 475C of the Corporation Tax Act 2009) Regulations 2019 (SI 2019/1250): These provisions introduced a new regime for 'hybrid capital instruments.' This legislation generally ensures that coupon payments on certain debt instruments with equity-like features (such as deferral or cancellation of interest payments, which are common in AT1 and similar bail-in able debt) are deductible for corporate tax purposes for the issuer. This broader legislation replaced previous specific regulations (like the Taxation of Regulatory Capital Securities Regulations 2013) and applies to a wider range of instruments across all sectors but is particularly relevant for banks and insurers.

Hong Kong has also taken steps to clarify and facilitate the tax treatment of regulatory capital instruments, including their deductibility. The Inland Revenue (Amendment) (No. 2) Ordinance 2016: This amendment clarified the profits tax and stamp duty treatments for 'regulatory capital securities' (RCSs) issued by banks to comply with Basel III capital adequacy requirements. The Hong Kong Departmental Interpretation and Practice Notes No. 53 (Revised) (DIPN 53): This important guidance from the Inland Revenue Department (IRD) confirms that a Regulatory Capital Security (RCS), which is defined to include Additional tier 1 (AT1) and tier 2 capital instruments, is to be treated as a debt security for Hong Kong profits tax purposes. Consequently, payments made under an RCS that are not repayments of the principal (i.e., coupon payments, premiums, or discounts) are generally treated as interest for both deduction and taxation purposes.

This approach prioritises financial stability, preventing tax rules from creating an undue burden that could hinder banks from building necessary loss-absorbing capacity.

- *Issue: Consequential amendment to section 8FA*

  South African Context:

  Currently, tier 1 and tier 2 capital instruments are already eligible for (or rather, benefit from) an exclusion from section 8FA of the Act. The aim

of the exclusions from hybrid debt (section 8F) and hybrid interest (section 8FA) are designed to accommodate prudential capital instruments issued by banks.

While tier 1 and tier 2 capital are crucial ‘going concern’ capital as they absorb losses before a bank fails, allowing it to continue operating. However, in a severe crisis, the losses might exceed what tier 1 and tier 2 capital can absorb. This is where FLAC instruments come in. They provide an additional, deeper layer of loss-absorbing capacity. They are ‘First Loss After Capital’ because they are designed to be written down or converted after tier 1 and tier 2 have been depleted, but before other senior unsecured creditors (like ordinary depositors or general bondholders) are hit. Therefore, similar extension of the rules should be afforded to FLAC instruments.

International Position:

The principle of ensuring tax deductibility of interest/coupons and tax neutrality on the write-down/conversion of loss-absorbing instruments is a common feature in jurisdictions that have implemented TLAC/MREL frameworks. Many countries that have domestic tax rules that, similarly to South Africa's section 8FA, would ordinarily re-characterise interest on instruments with equity-like features (like perpetual or deeply subordinated debt, or debt with contingent coupons) as non-deductible dividends. However, to prevent this for regulatory capital and loss-absorbing debt, these countries introduce specific carve-outs or exemptions in their tax legislation. These carve-outs ensure that interest paid on instruments that qualify as Additional tier 1 (AT1), tier 2, or senior non-preferred debt (which is the international equivalent of a FLAC-like instrument for TLAC purposes) remains tax-deductible for the issuing bank.

Proposal

The effective implementation of South Africa's resolution framework, particularly the reliance on FLAC instruments, necessitates a coherent and supportive tax policy. The current South African Income Tax Act, specifically sections 8F and 8FA of the Act present potential challenges that could increase the cost and complexity of issuing these vital instruments.

Drawing on international best practices, it is proposed that South Africa's tax legislation be amended to ensure that:

- FLAC instruments and tier Capital are excluded from the application of hybrid debt and hybrid interest anti-avoidance rules (i.e. sections 8F and 8FA), thereby preserving the tax deductibility of their interest payments.

Effective date

The proposed amendment will come into operation on 1 January 2026.

3.17. Extension of the UDZ tax incentive sunset date

[Applicable provision: Section 13quat of the Act]

Background

The Urban Development Zone (UDZ) tax incentive was introduced in 2003 to promote the maintenance and further development of inner cities within selected municipalities. The UDZ tax incentive was designed to encourage property investment in central business districts (CBDs) and to address the problem of urban decay in these CBDs through the promotion of investment in urban renewal. The incentive is in the form of an accelerated depreciation allowance applicable on the value of new buildings and improvements to existing buildings in qualifying municipalities demarcated as UDZs.

Since its introduction, the UDZ tax incentive has undergone several legislative amendments to extend both the sunset date and UDZ incentive structure to allow for greater uptake. The incentive was initially available from January 2004 until March 2014. Following a review of its effectiveness, the incentive was extended to 31 March 2020. Thereafter, the incentive was extended to 31 March 2021, with the latest extension ending on 31 March 2025 to allow for a comprehensive review to be concluded.

In line with the Minister’s announcement in the 21 May 2025 Budget Review, it was proposed that the UDZ tax incentive be extended for another five years, to allow sufficient time for consultations with municipalities as part of the comprehensive review, which will determine the future of the incentive.

Reasons for change

The purpose of applying a sunset date to a tax incentive is to allow Government an opportunity to review its effectiveness before that incentive comes to an end. To better understand the experiences of municipalities and developers accessing the tax incentive, an online survey was conducted as part of the review. While the survey received fewer responses than expected, it provided valuable insights into the experiences of investors/developers. However, the information gathered from the survey and SARS microdata is insufficient to draw conclusive findings regarding the effectiveness of the incentive. Further research is required, particularly to source and evaluate municipal data regarding the uptake of the incentive.

Proposal

It is proposed that changes be made in section 13quat of the Act to extend the UDZ tax incentive by another five years, to 31 March 2030. The extension of the incentive's sunset date will allow sufficient time for consultations with municipalities and the collection of data required to assess the incentive's effectiveness in achieving its objectives.

Effective date

The proposed amendment will be deemed to have come into effect on 1 April 2025 and will be applicable in respect of any building, part thereof or improvement that is brought into use on or after that date.

3.18. Energy efficiency savings incentive

[Applicable provision: Section 12L of the Act]

Background

The energy efficiency savings tax incentive was introduced on 9 December 2013 to encourage companies to implement energy efficiency savings. The section 12L incentive provides an income tax deduction for the monetary value of actual energy efficiency savings (kWh) achieved by a company in a financial year and approved by the South African National Energy Development Institute.

In the 2022 Budget, the first phase of the carbon tax and the energy efficiency savings tax incentive were extended for three years to December 2025. In the

‘Carbon Tax Discussion Paper: Phase Two of the Carbon Tax’ it was proposed to include eligible section 12L projects approved under the Energy Efficiency Savings SANS 50010 standard under the carbon offsets mechanism. This proposal was to promote investments in energy efficiency measures, reduce in-scope electricity emissions and to promote job creation.

Reasons for change

During consultations with stakeholders, there was broad support to extend the section 12L incentive. Stakeholders indicated that there would be challenges with including the section 12L energy efficiency projects in the carbon offsets mechanism because a number of section 12L projects are implemented within the taxable boundary of tax-paying entities. Additionally, the 12L energy efficiency projects are implemented on a smaller scale than the typical threshold for viability under existing international carbon standards. It was therefore proposed in Budget 2025 to extend the section 12L energy-efficiency tax incentive for five years to 31 December 2030.

Proposal

It is proposed that section 12L is amended by substituting the current sunset date of years of assessment ending before 1 January 2026 with years of assessment ending before 1 January 2031.

Effective date

The proposed amendment will come into operation on 1 January 2026.

3.19. Additional deduction for domestic production of battery electric and hydrogen-powered vehicles

[Applicable provision: Section 12V of the Act]

Background

In 2024, Government introduced a tax incentive to support investment in the local production of battery electric vehicles (BEVs) and hydrogen-powered vehicles (HPVs). This measure is intended to facilitate the transition of South Africa’s automotive industry from mainly producing Internal Combustion Engine (ICE) vehicles to a dual platform that includes the production of electric vehicles (EVs). This shift is necessary to secure South Africa's key export markets, such as the EU and UK, which have announced plans to ban the sale of new ICE

vehicles by 2035, as well as to address environmental concerns and meet emission reduction commitments under the Paris Agreement.

The tax incentive complements a broader package of measures designed to support the automotive industry's transition to producing BEVs and HPVs. Additional measures are implemented by the Department of Trade, Industry and Competition (DTIC) through the Automotive Investment Scheme (AIS). The AIS provides a 35 per cent grant support for component and tooling manufacturers as well as battery assemblers. Manufacturers of BEVs and HPVs are eligible for a 20 per cent cash grant in addition to the tax incentive.

Under the tax incentive, manufacturers of BEVs and HPVs may claim a 150 per cent accelerated depreciation allowance on qualifying capital expenditure incurred in South Africa. Eligible assets include buildings, new and unused machinery, plant, implements, and articles (including supporting structures) provided they are used in the production of BEVs and HPVs. The incentive applies to assets brought into use between 1 March 2026 and 29 February 2036.

Reasons for change

It has come to Government's attention that the term 'motor vehicle manufacturer' may be interpreted broadly to include the entire vehicle manufacturing value chain (including component manufacturers) and all types of vehicles powered by electricity or hydrogen fuel cells (i.e. golf carts).

Proposal

To ensure clarity and policy alignment, it is proposed that 'motor vehicle manufacturer' be defined to mean manufacturer of light motor vehicles as contemplated in paragraph (i) of the definition of 'final manufacturer' as set out under the Automotive Production and Development Programme Regulations contained in Government Notice No. R.80 as published in Government Gazette No. 44144 of 11 February 2021, or 'heavy motor vehicle' as referred to in item 317.07 in Part I of Schedule No.3 of the Customs and Excise Act, 1964 and to the extent of assembly provided for in Note 5 to Chapter 98 of Part 1 of Schedule No.1 to that Act.

Effective date

The proposed amendment comes into operation on 1 March 2026 and applies in respect of assets brought into use on or after that date.

3.20. Refining the definition of 'equity share' to cater for transfers by foreign companies

[Applicable provision: Definition of an 'equity share' in section 1(1) of the Act]

Background

The introduction of dividends tax in 2012, along with significant amendments to the Companies Act in 2011, necessitated adjustments to the definition of an equity share.

An 'equity share' as currently defined in the Act, refers to 'dividends' and 'returns of capital', which are terms that are both defined in the Act. The definitions of 'dividend' and 'return of capital', both only make reference to an amount that is transferred by a resident company that constitutes a dividend or a return on capital.

Reasons for change

Under the current wording of the 'equity share' definition, shares in a foreign company appear to be excluded and cannot be regarded as equity shares.

Proposal

It is proposed that the definition of equity share be updated to cater for foreign dividends and foreign returns of capital.

Effective date

The proposed amendment will come into operation on 1 January 2026.

3.21. Interaction between sections 6quat and 23(m) of the Income Tax Act

[Applicable provision: Sections 6quat and 23(m) of the Act]

Background

Section 23(m) of the Act restricts the deductibility of certain expenses when determining a taxpayer's taxable income, specifically disallowing any deduction, loss, or allowance contemplated in section 11 of the Act, which relates to any employment or office held. However, it is important to take into account the provisions of section 11(x) of the Act, which allows for the deduction

of any amounts permitted under any other provision in Part I of Chapter II of the Act.

As such, the reference to section 11 of the Act in section 23(m) of the Act must be interpreted broadly to include all deductions allowed under Part I, including those permitted under section 6quat(1C) of the Act. Section 6quat(1C) of the Act allows a deduction against income, for the purposes of determining taxable income, in respect of foreign taxes paid or proved to be payable to any sphere of government of a country other than South Africa.

Reasons for change

Currently, section 23(m) of the Act does not include section 6quat(1C) of the Act in the list of exceptions provided under subparagraphs (i) to (iv). As a result, and based on a strict interpretation of the law, employees and office holders who receive remuneration would be precluded from claiming a deduction under section 6quat(1C) of the Act, due to the prohibitions imposed by section 23(m) of the Act.

From a tax policy point of view the election granted to a resident taxpayer to get a deduction from income of taxes paid or proved to be payable to any country other than South Africa should not be restricted by section 23(m) of the Act.

Proposal

It is therefore proposed that section 23(m) of the Act be amended to expressly exclude section 6quat(1C) of the Act from its limitations by adding an additional subparagraph following the current subparagraph (iv). This amendment would provide certainty that employees and office holders are allowed a deduction for foreign taxes, should they elect to do so.

Effective date

The proposed amendment will come into operation on 1 March 2026 and apply in respect of any year of assessment commencing on or after that date.

3.22. Interaction of controlled foreign company rules in section 9D with section 9H

[Applicable provisions: Sections 9D and 9H of the Act]

Background

Broadly, section 9D of the Act serves as an anti-avoidance provision aimed at preventing South African residents from avoiding tax through passive investments in controlled foreign companies or diverting income to controlled foreign companies. If a foreign company qualifies as a controlled foreign company (CFC) as defined, the amount of its net income is proportionally attributed to any South African residents holding 10 per cent or more of the participation rights, effectively including the proportional amount in their taxable income. The provisions of section 9D(2A) of the Act play a crucial role in maintaining the effectiveness of section 9D of the Act by preventing residents from diverting or channelling income to low-tax jurisdictions to gain a tax advantage.

Section 9H of the Act, that triggers an 'exit charge', provides that when a resident ceases to be a resident or a CFC ceases to be a CFC, it is deemed to have disposed of all its worldwide assets on the date immediately before the date it ceases to be a resident or CFC.

Reasons for change

It has come to the Government's attention that the current wording of section 9H of the Act read with section 9D of the Act is not always adequate to trigger an 'exit charge' where a CFC ceases to be a CFC. At issue is the hypothesis contained in paragraph (i)(aa) of the further proviso to section 9D(2A) of the Act, which is the 'comparable tax exemption' aimed at preventing attribution of the already calculated 'net income' amount of a CFC to a resident if a comparable tax is suffered in the other jurisdiction. The proviso has the effect of reducing the net income amount of a CFC to nil if the foreign taxes payable by the CFC is at least 67.5 per cent of the normal tax that would have been payable had the CFC been a resident. A CFC may avoid the exit charge under section 9H of the Act as it is treated as a resident when determining the normal tax variable element of the comparable tax exemption. As a result, the interaction between 'net income' of CFC rules in section 9D of the Act and

ceasing to be a CFC rules in section 9H of the Act needs to be clarified and strengthened.

Proposal

It is proposed that paragraph (i)(aa) of the further proviso to section 9D(2A) of the Act be amended to add the normal tax resulting from the application of section 9H(3)(b) of the Act to the normal tax that would have been payable had the CFC been a resident.

Effective date

The proposed amendment will come into operation on 31 December 2025 and applies in respect of foreign tax years of controlled foreign companies ending on or after that date.

3.23. CFC rules and comparable tax exemption

[Applicable provision: Section 9D(2A) of the Act]

Background

Broadly, section 9D of the Act serves as an anti-avoidance provision aimed at preventing South African residents from avoiding tax through passive investments in controlled foreign companies or diverting income to controlled foreign companies. The provisions of section 9D(2A) of the Act play a crucial role in maintaining the effectiveness of section 9D by preventing residents from diverting or channelling income to low-tax jurisdictions to gain a tax advantage by ensuring the imputation of the CFC's diversionary and passive income into the South African tax net.

Section 9D(2A) of the Act contains a set of specific rules to assist in the determination of the net income of a CFC. However, the further proviso to section 9D(2A) effectively provides an exemption from imputation of the CFC's net income into the South African tax net due to the 'comparable tax exemption'. The current tax rules allow a comparable tax exemption for CFCs if they pay a comparable level of tax overseas as they would in South Africa, i.e. at least 18.225 per cent.

The comparable tax exemption contained in paragraph (i)(aa) read with paragraph (ii)(aa) of the further proviso to section 9D(2A) of the Act is based

on the aggregate amount of foreign taxes paid by a CFC, which is used to determine the effective tax rate of the CFC.

Generally, compliance with this further proviso of the Act requires calculating the hypothetical taxable income of the CFC in accordance with the South African Income Tax Act. The taxable income must be determined by considering any applicable double taxation agreements, credits, rebates, or other tax recovery rights from foreign governments, while also disregarding losses from prior foreign tax years since the foreign company became a CFC or from entities other than the CFC.

Reasons for change

It has come to the Government's attention that the current provisions in section 9D(2A) of the Act that deal with comparable tax exemption do not consider tax systems of countries that allow a refund to certain shareholders of a foreign company for tax paid by the company declaring the dividend. Under current South African law, this creates a discrepancy because a CFC may meet the requirements for the comparable tax exemption based on the tax rate, despite the fact that the ultimate tax paid on profits, after shareholder refunds, is substantially lower. Furthermore, if the refund is made to an intermediate holding company that is also a CFC, the current provisions do not take this refund into account in determining whether the exemption applies.

Proposal

It is proposed that the Act be amended to take into account tax refunds received by shareholders, including intermediate holding company CFCs, when determining whether a CFC qualifies for the comparable tax exemption under section 9D(2A) of the Act. This would ensure a more accurate assessment of the actual effective rate of tax paid on the profits and align the application of the exemption with its intended policy objective—namely, to exclude only those foreign companies that are genuinely taxed at a level comparable to South Africa.

Effective date

The proposed amendment will come into operation on 31 December 2025 and applies in respect of foreign tax years of controlled foreign companies ending on or after that date.

3.24. Taxation of trusts and their beneficiaries

[Applicable provisions: Sections 7(5) and 25B of the Act]

Background

Currently, income received by a trust is taxed in the hands of the donor, the beneficiary or the trust. When determining who will be taxed, the attribution or flow-through principle is applied. The flow-through principle ensures that the income distributed by the trust retains its nature as if it had been received directly and not through a trust. In essence, the flowthrough principle ensures that the income is taxed in the hands of the person who benefits from the income. However, the Act has attribution rules to tax income in the hands of the person that made a donation, settlement or other disposition to a trust under certain instances.

Reasons for change

In 2023, amendments were made to the rules relating to the taxation of trusts and their beneficiaries. The intention is that the flow-through principle should be limited to resident beneficiaries. As a result, income vested in or distributed to non-residents is taxed in the trust. The main reason for that policy is that Government found it challenging to identify and collect taxes from non-residents in whom the income is vested or distributed. The current wording in the Act does not meet this objective and, in some instances, may still be interpreted to include non-resident beneficiaries and donors.

Proposal

It proposed that the Act be amended to ensure that the flow-through and attribution principles only apply to income received by or accrued to resident beneficiaries and resident donors.

Example:

Facts:

ABC Trust is resident in South Africa. A, also resident in South Africa, donated R1 million to the ABC Trust and B, a non-resident, donated R1 million to the ABC Trust.

The ABC Trust invested the R2 million in interest-bearing investments that yielded R200 000 interest during the year. The

trustees did not exercise their discretion to vest the interest in any of the discretionary beneficiaries.

Result:

Section 7(5) of the Act requires donor A to include R100 000 interest (R200 000 x R1 million donated of the R2 million total invested in the interest-bearing investment) in A's income tax return.

Section 7(5) of the Act is not applicable to donor B, since B is not resident in South Africa.

Section 25B of the Act requires the ABC Trust to include R100 000 interest (R200 000 less R100 000 attributed to donor A) in its taxable income.

Effective date

The proposed amendments will come into operation on 1 March 2026 and apply in respect of years of assessment commencing on or after that date.

3.25. Refining deferral of exchange difference rules on debt between related companies

[Applicable provision: Section 24I of the Act]

Background

In general, section 24I(10A) of the Act provides for the deferral of foreign exchange gains or losses on certain exchange items, specifically in relation to long-term debt between connected persons or members of a group of companies. The provision applies where the exchange item in question—such as an intercompany loan—is not classified as a current asset or current liability for financial reporting purposes under IFRS.

When section 24I(10A) of the Act was introduced in 2012, the underlying policy was to defer the taxation of foreign exchange differences until the exchange item is realised. This was intended to ease compliance and reduce volatility in taxable income caused by unrealised foreign exchange movements.

Reasons for change

Deferral of foreign exchange gain or loss until realisation

It has come to Government's attention that this policy has resulted in unintended consequences as in some instances, taxpayers may intentionally delay realisation of exchange items in order to avoid triggering deferred foreign exchange gains. This deferral can result in distortions to taxable income and deferred recognition of revenue, thereby affecting the timing and collection of tax revenues.

Practical challenges in application of section 24I(10A)

It has come to Government's attention that in certain instances, there is a challenge in applying section 24I(10A) of the Act, particularly regarding the classification of the debt under financial reporting standards, if it is not recognised in the financial statements. For example, one of the key requirements for the deferral of exchange differences is that the relevant loan (or a portion thereof) must not be treated as a current asset or liability for IFRS purposes. Once the loan is written off and no longer reflected in the financial statements, it becomes unclear whether the condition relating to the asset classification is satisfied. The mismatch between the accounting treatment and the tax position creates uncertainty as to whether the continued deferral of exchange differences is appropriate.

Proposal

It is proposed that where an exchange item is not recognised for financial reporting purposes, exchange differences in respect of that exchange item should not qualify for deferral.

In relation to the deferring of exchange differences, it is proposed that the policy be reconsidered so that deferred exchange differences are triggered on the portion of an exchange item realised during the year of assessment.

Effective date

The proposed amendments will come into operation on 1 January 2026 and applies in respect of years of assessment commencing on or after that date.

3.26. VAT Act - Debit and credit notes relating to a going concern as per section 8(25)

[Applicable provision: Section 21(1)(d)(ii) of the Value-Added Tax Act, No. 89 of 1991 ('the VAT Act')]

Background

In terms of section 21(1)(d)(ii) of the VAT Act, where an enterprise is sold as a going concern as contemplated in section 11(1)(e) of the VAT Act, the purchaser of the enterprise is allowed to issue debit and credit notes in respect of goods or services that were supplied by the seller of the enterprise. but which are returned to the purchaser.

Reasons for change

In the event that goods or services are returned (debit and credit note events) to the transferee of an enterprise that was transferred as a going concern in terms of section 8(25) of the VAT Act read together with section 42 or 45 of the Income Tax Act, where the transferor and the transferee are deemed to be one and the same person for VAT purposes section 21(1)(d)(ii) of the VAT Act currently does not allow the transferee to issue debit and credit notes. The section currently caters only for debit and credit note events where the going concern transaction was concluded in terms section 11(1)(e) of the VAT Act and not section 8(25) of such Act.

Proposal

It is proposed that section 21(1)(d)(ii) of the VAT Act be expanded to include the return of goods or services that were supplied by the transferor of a business as a going concern under section 8(25) of the VAT Act, read together with sections 42 or 45 of the Income Tax Act, where the goods or services are returned to the transferee.

Effective date

The proposed amendment will come into operation on 1 April 2026.

3.27. VAT Act – Reviewing vat rules dealing with documentary requirements for silver exports

[Applicable provision: Section 54(2C) of the VAT Act]

Background

In terms of section 54(2C) of the VAT Act, where gold is supplied as contemplated in section 11(1)(f) of the VAT Act or where gold is exported from South Africa in the circumstances contemplated in paragraph (a) or (d) of the definition of 'exported' in section 1(1) of the VAT Act and in accordance with section 12 of the of the Precious Metals Act, 2005 (Act No. 37 of 2005), by an agent who is acting on behalf of another person who is the principal for the purposes of that supply and:

- the agent is a registered vendor; and
- the principal is a resident of South Africa and a registered vendor,

the agent must, subject to other conditions contained in that section, obtain and retain the documentary proof as acceptable SARS.

Reasons for change

The main purpose of refineries is to refine and smelt certain 'precious metals', as defined in the VAT Act, or ore received from various customers, namely depositors / principals, for sale or export. After the refining or smelting silver, as is the case with gold, it is difficult to determine which depositor's silver or ore is sold or exported because the silver or ore loses its original identity during refinery and smelting. As a result, depositors find it difficult to obtain the documentary evidence to support the application of the zero rate on a transaction-by-transaction basis. In most instances, as with gold, the refineries also act as agents and sell or export silver and ore on behalf of these depositors.

Currently, section 54(2C) of the VAT Act is only applicable to the exportation of gold. However, since similar difficulties arise in respect of silver as with gold, and on the basis that there are adequate reporting and record keeping requirements in place, it is proposed that the dispensation for gold be extended to silver.

Proposal

Section 54(2C) of the VAT Act should be expanded to also apply to the exportation of silver by an agent on behalf of a principal.

Effective date

The proposed amendment will come into operation on 1 April 2026.

3.28. VAT Act – Reviewing the vat treatment of testing services supplied to non-residents who are outside South Africa at the time of the supply, where services are supplied directly in connection with movable property situated in the South Africa

[Applicable provision: New sections 11(1)(x) and 11(2)(z) of the VAT Act]

Background

Subject to certain conditions, section 11(2)(l) of the VAT Act provides for services supplied by a vendor to a person who is not a resident of South Africa to be zero-rated. Subparagraph (ii) excludes services supplied 'directly in connection with' moveable property situated inside South Africa, save for two exceptions. Subparagraph (iii) excludes services supplied to the recipient or any other person who is in South Africa at the time the services are rendered.

Reasons for change

Based on the literal interpretation of the words 'directly in connection with', the clinical trial service which involves testing, amongst others, the effectiveness of the medicine/device/item, may be regarded as being in connection with moveable property. This would then mean that the exclusion contained in subparagraph (ii) to section 11(2)(l) of the VAT Act would apply (the two exceptions which may override this exclusion not being applicable in these circumstances) and as a result the supply would not qualify for zero-rating. Similarly, because of the use of the words 'directly to the said person or any other person who is in South Africa at the time the services are rendered', tests including tests performed on a patient in South Africa will be excluded from the zero-rating because of subparagraph (iii) to section 11(2)(l) of the VAT Act. The testing may also involve 'kits' containing needles and vials, for example.

In light of the above, even though it may be argued that the clinical reports are consumed offshore by the non-resident where the non-resident is situated, section 11(2)(l) of the VAT Act does not find application on the clinical trials or testing services. The same issue arises for any other good that may be tested in South Africa, for example, aircraft, machines and weapons.

Proposal

In order to address the difficulties faced by suppliers of testing services to offshore clients and in order to ensure that South African suppliers in this regard remain competitive on the global scale, it is proposed that a new section 11(2)(z) be introduced to zero-rate the supply of testing services and reporting to non-residents. Furthermore, a new section 11(1)(x) should also be introduced to zero-rate the goods utilized to provide the testing services.

Effective date

The proposed amendment will come into operation on 1 April 2026.

3.29. VAT Act – Reviewing the definition of 'insurance'

[Applicable provision: Section 1(1) Definition of the VAT Act Definition of 'insurance]

Background

The definition of 'insurance' in section 1(1) of the VAT Act means insurance or guarantee against loss, damage, injury or risk of any kind whatever, whether pursuant to any contract or law, and includes reinsurance; and 'contract of insurance' includes a policy of insurance, an insurance cover, and a renewal of a contract of insurance, provided that nothing in this definition shall apply to any insurance specified in section 2 of the VAT Act.

Reasons for change

In the matter of Capitec Bank Limited v C:SARS (CCT 209/22) [2024] ZACC 1 (the Court case), the Constitutional Court ruled that the supply of insurance for no consideration by the appellant is indeed a taxable supply, or at least partly a taxable supply, due to the fact that the appellant provided the insurance free of charge when it granted a loan to a customer. This then means that the provision of free credit cover gives a lender in the same position as the appellant, a competitive advantage over other lenders who require that the

customer takes out credit insurance, even though the cost of premiums is indirectly recovered from the customers on the premiums paid. This has the effect that the appellant could claim a deduction, in terms of section 16(3)(c) of the VAT Act, on indemnities paid/credited to the customer's account upon a successful claim by the customer. The implication of the judgment is that where any vendor acquires exempt credit life insurance from a life insurer and that vendor stated in the credit agreement that it on-supplies same at no charge, such vendor will be entitled to claim the said VAT deduction on insurance 'payouts' made to its customer. The above will result in undue profits from the VAT system, which is premised on the fact that short-term insurers charge premiums in excess of 'payouts', for the appellant and similar institutions.

Proposal

In light of the decision in the Court case, it is proposed that the definition of 'insurance' be revised to include the requirement that a premium be charged.

Effective date

The proposed amendment will come into operation on 1 April 2026.

3.30. VAT Act – Clarifying the vat treatment of temporary letting of residential properties

[Applicable provision: Section 18D of the VAT Act]

Background

In terms of section 7(1)(a) of the VAT Act, the supply of residential fixed property by a VAT vendor (being a property developer) is subject to VAT at the standard rate of 15 per cent. Depending on market conditions, residential fixed property developers are at times unable to dispose of newly built residential fixed properties for extended periods of time. In order to maintain expenses incurred in developing such fixed property, such as bank loan repayments, property developers often enter into short term temporary leases for such fixed property until a buyer can be found.

The leasing of a residential fixed property is an exempt supply, in terms of section 12(c) of the VAT Act, which would generally result in the VAT incurred being denied. The VAT Act requires a change in use adjustment in terms of

section 18(1) of the VAT Act where property developers apply fixed property developed for resale, in residential letting.

Property developers are entitled to deduct input tax on the VAT costs incurred to build residential fixed property (dwellings) for sale. However, where the property developer is unable to sell the residential fixed property and enters into a lease, until a buyer is found, the property developer is currently required to make an output tax adjustment based on the open market value (OMV) of the residential fixed property when the residential fixed property is leased for the first time. In 2010, an announcement was made in Chapter 4 of the 2010 Budget Review (Heading entitled: “VAT and residential property developers” on page 79 of the Budget Review) to investigate and determine an equitable value and rate of clawback for property developers as the VAT treatment was disproportionate to the temporary rental income. As a result, changes were made to the VAT Act by inserting new section 18B, for a short period, from 10 January 2012 to 31 December 2017. This section ceased to apply on 1 January 2018. Section 18B of the VAT Act was a temporary measure with a limited lifespan.

In light of the above, a more permanent relief mechanism in the form of section 18D of the VAT Act (together with associated provisions, being sections 9(13), 10(29) and 16(3)(o)) were introduced with effect from 1 April 2022 to deal with temporary letting by developers. In short, section 18D of the VAT Act provides relief, for only 12 months, to the developer to suspend the adjustments under section 18(1) of the VAT Act based upon the OMV of the property, for the change in application to the exempt use, if newly developed residential properties are temporarily let.

Upon temporarily applying any newly developed residential unit for an exempt supply (residential letting under lease agreement), the developer must declare output tax, based on the adjusted costs of developing that unit (land and building), under section 18D(2) of the VAT Act. If the unit is sold during the temporarily applied period, the output tax previously declared under section 18D(2) of the VAT Act can be recovered in the form of deduction under section 16(3)(o) of the VAT Act, based on the circumstances in section 18D(5) of such Act. Section 18D(3) provides that such supply will be a taxable supply under section 7(1)(a) of the VAT Act.

With effect from 1 April 2024, section 18D(6) of the VAT Act was introduced to make it clear that when the letting of a dwelling extends beyond the “temporarily applied” period or when the developer applies the dwelling permanently for exempt or other than non-taxable purpose during the “temporarily applied” period, an output tax adjustment based on the OMV of the property concerned must be made under section 18(1) of the VAT Act. Section 18D(6) of the VAT Act also provides for a transitional rule to deal with a situation where a sale agreement for the property was concluded during the temporarily applied period, but the time of supply for the property under section 9(3)(d) of the VAT Act is only triggered after the end of 12-month period. In such a case, the supply is regarded as a taxable supply, and no adjustment is required under section 18(1) of the VAT Act.

Reasons for change

There is a lacuna in the VAT Act regarding the access to the deduction under section 16(3)(o) of the VAT Act, in a case where an adjustment is required under section 18(1) of such Act, if the 12-month period for temporary letting is exceeded or there is a permanent change in use for exempt supplies during the 12-month period. In these instances, as the unit is not sold as contemplated under section 18D(3) read together with section 18D(5)(a) of the VAT Act, the vendor is not entitled to a deduction under section 16(3)(o) of the VAT Act. However, if the property originally fell into the temporarily applied period, the vendor would have had to make an adjustment under section 18D(2) of the VAT Act. This adjustment is made at the time prescribed under section 9(13), i.e. the date within the tax period in which the agreement or the letting and hiring of accommodation in a dwelling comes into effect or in which the dwelling is occupied, whichever is earlier.

It follows that a vendor who originally intended to only lease the property for 12 months, would have had to make the adjustment under section 18D(2) of the VAT Act at the adjusted cost. If the temporary leasing period is subsequently exceeded or there is a permanent change in use for exempt purposes, section 18(1) of the VAT Act applies and the vendor will be required to make another adjustment, at the OMV. Therefore, the adjustment under section 18D(2) of the VAT Act must be neutralized under section 16(3)(o) of that Act.

As a result of the above difficulty, SARS Binding General Ruling 64: “Temporary application of new dwellings for exempt supplies simultaneously held by

developers for taxable purposes (Issue 2)" (BGR 64), was amended to contain a decision under section 72 of the VAT Act in terms of which it is clarified that a developer that is required to make an adjustment under section 18(1) of such Act after having temporarily applied a newly developed property for an exempt supply will also be allowed a deduction undersection 16(3)(o) of such Act, to recover the output tax that was previously declared under section 18D(2) of the VAT Act. The same rule will apply if the agreement for the sale of property is concluded during the period of temporary application for an exempt supply, but the time of supply only occurs after the 12- month period has expired. Proposal For ease of administration, it is proposed that the VAT treatment of the temporary letting of residential properties under section 18D of the VAT Act and consequential sections of this Act, be reviewed and updated.

Effective date

The proposed amendment will come into operation on 1 April 2026.

3.31. VAT Act – Reviewing the vat treatment of airtime vouchers supplied in South Africa for exclusive use in an export country

[Applicable provision: New section 8(30) of the VAT Act]

Background

A non-resident distributor acquires airtime vouchers from a non-resident telecommunications services provider and then sells the same to resident distributors. The resident distributors sell airtime vouchers to customers in South Africa. In turn, the customers in South Africa forward airtime vouchers to family and/or friends in an export country, which is the only place where the airtime vouchers can be used. The infrastructure to make and receive calls/use data for which the airtime vouchers are sold is situated outside South Africa. It is evident that the telecommunication services can only be consumed outside South Africa.

In light of the above, it is clear that the supply of airtime vouchers through the distribution chain comprises of two components, namely:

- Distribution services of the airtime vouchers in South Africa; and
- Telecommunication services to be provided outside of South Africa.

Reasons for change

In the past SARS issued decisions in terms of section 72 of the VAT Act whereby only the fees in relation to distribution services of the airtime vouchers in South Africa were subjected to VAT at the standard rate in terms of section 7(1)(a) of the VAT Act and the remainder of the value was attributed to telecommunication services to be provided outside of South Africa, the supply of which was zero-rated.

However, with the amendment to section 72 of the VAT Act on 21 July 2019, SARS is unable to renew the above or issue new decisions under section 72 of the VAT Act to zero-rate the supply of the airtime vouchers used in an export country due to the facts that the:

- zero-rating provisions do not permit the zero-rate to be applied to the supply of airtime vouchers that can only be used outside South Africa; and
- granting of such requests will result in a change in the rate of tax from standard rated to zero rated, thus resulting in a reduction in the liability for VAT.

Regardless of whether the resident distributor contractually acts as agent or principal, the non-resident distributor acquires airtime vouchers from a non-resident telecommunications services provider or distributor at a discount. On the basis that the discount represented consideration for a distribution service, this amount was taxed at the standard rate under section 72, whilst the supply of the airtime itself was zero-rated.

It is proposed that the law be changed to give effect to the following, explained by way of example:

- Foreign telecommunications services provider ABC sells an airtime voucher with a face value of R100 to a distributor CDE in South Africa for R80, that on supplies the voucher to a customer in South Africa.
- CDE has to declare VAT at the standard rate on the difference between the face value of the airtime voucher and the amount at which it acquired such voucher from ABC, as being consideration for distribution services supplied to ABC (i.e. on R20).
- The supply of the airtime by ABC is out of scope for VAT purposes as this activity is not conducted in South Africa.

Proposal

It is proposed that provision be made in the legislation to subject only the deemed distribution services in South Africa to VAT at the standard rate.

Effective date

The proposed amendment will come into operation on 1 April 2026.

3.32. VAT Act – Supplies of educational services

[Applicable provisions: new sections 8(2H), 12(h)(iv) and 40E and sections 12(h)(i) and (ii)]

Background

Section 12(h)(i) of the VAT Act exempts from VAT the supply of educational services by:

- a school registered under the South African Schools Act, 1996 (Act No. 84 of 1996) or a public college or private college established, declared or registered as such under the Further Education and Training Colleges Act, 2006 (Act No.16 of 2006); and
- an institution that provides higher education which is established or deemed to be established as a public higher education institution under the Higher Education Act, 1997 (Act No. 101 of 1997), or is declared as a public higher education institution under that Act or is registered or conditionally registered as a private higher education institution under that Act.

Section 12(h)(ii) of the VAT Act further exempts from VAT, the supplies made by an educational institution solely or mainly for the benefit of its leaners or students of goods or services (including domestic goods and services) that are necessary for and subordinate and incidental to the supply of services referred to in section 12(h)(i) of the VAT Act, if such goods or services are supplied for consideration in the form of school fees, tuition fees or payment for lodging and boarding.

Reasons for change

The reference to Further Education and Training Colleges Act, 2006 (Act No.16 of 2006) in section 12(h)(i)(aa) of the VAT Act is obsolete as the Act has been

renamed to the Continuous Education and Training Act, 2006 (Act No.16 of 2006). That Act makes reference to a private college as meaning a private college registered or provisionally registered as a private college under Chapter 6 of that Act. The current wording of section 12(h)(i)(bb) of the VAT Act refers to institutions that are registered or conditionally registered as higher education institutions, and this creates uncertainty as to whether the exemption applies to private schools or colleges provisionally registered by the respective Departments.

Further the policy intent was always to exclude schools from the VAT net and having regard to the changes in the manner in which the educational services are provided and charged for, the amendment seeks to provide clarity that these services are all exempt.

There are numerous schools registered for VAT that will now cease to be vendors. As a consequence, basic education institutions that are currently on register and become liable to deregister for VAT (as of the effective date, in terms of section 8(2) of the VAT Act) will be given a concession to pay over the VAT liability in twelve equal monthly instalments or in so many instalments as SARS may decide in terms of the newly introduced section 8(2H).

Since this extension of the period to make payment does not change the time of supply under section 8(2), it results in penalties and interest being due when the extended period is allowed. Consequently, a new section 9(14) is now proposed and the time of supply will be deemed to take place as when each payment is due, prescribed or paid under such payment arrangements.

As a result of this extension, the proposed insertion of new section 40E seeks to ensure that past assessments that have been finalised for the periods prior to 1 January 2026 are not reopened either by SARS or the vendor. However, with regard to past assessments that have not been finalised, applications may be made to SARS to consider reviewing the assessment. However, the review of such assessment may not result in a refund paid to the vendor. Further, no new assessment may be issued by SARS in this regard.

Proposal

A textual amendment to section 12(h)(i)(aa) to refer to the correct Act and that the wording in section 12(h)(i)(bb) in respect of “registered or conditionally registered” be aligned with the wording used by the educational authorities which is “registered or provisionally registered”. It is further proposed that the

provisional registration allowed in section 12(h)(i)(bb) be extended to section 12(h)(i)(aa).

To extend the scope of the exemption to all supplies made by basic educational institutions.

To provide relief to institutions that are required to deregister by introducing section 8(2H) along with new time of supply rules in relation to any such arrangement by the introduction of section 9(14).

A provision be introduced to ensure that past assessments that have been finalised for the periods prior to 1 January 2026 are not re-opened either by SARS or the vendor by the introduction of section 40E.

Effective date

The proposed amendment will come into operation on 1 January 2026.

3.33. VAT Act - Low value importation of goods

[Applicable provision: Paragraphs 1(v) and 2 of Schedule 1 of the VAT Act]

Background

Due to the growth globally of small or negligible value goods across borders that were primarily being carried by courier and express mail services in the early 1990s, the World Customs Organization (WCO) developed a set of release/clearance procedures (provisions) to assist both customs administrations and trade with expediting the clearance of these goods. The provisions were aimed at assisting WCO members' customs administrations in standardising the processing of goods purchased online and across borders. One of the provisions was that low-value goods below a specified threshold attracted no customs duties or VAT.

Since then, though, the volume of these goods has increased significantly, more especially since the lock-down periods of the Covid 19 pandemic. As noted by the OECD, "more than 131 billion parcels were shipped globally in 2020, representing a 27% year-on-year growth."

In terms of section 13(3) of the VAT Act, proviso to section 38(1) of the Customs and Excise Act, No. 91 of 1964 ("the Customs and Excise Act") and paragraph 1(v) of Schedule 1 to the VAT Act, goods of a value of R500 or less for customs duty purposes, are exempt from the VAT imposed under section 7(1)(b) of the

VAT Act, provided that no customs duty is payable in terms of Schedule 1 of the Customs and Excise Act. Further, goods, being printed books, newspapers, journals and periodicals that are imported into South Africa by post not exceeding R100 in value, are exempt from VAT imposed under section 7(1)(b) of the VAT Act as per section 13(3) read together with paragraph 2 of Schedule 1 to the VAT Act.

Reasons for change

Government noted legitimate concerns that have been expressed by the domestic industry relating to the uneven playing field between domestic and offshore suppliers of these low value goods, especially where the provisions of the VAT Act are concerned. Since domestic industry can be held to account for not complying with the VAT Act in South Africa and government relies on the voluntary compliance of offshore suppliers, it is now necessary that amendments be made in the legislation to level the playing field in this regard.

Proposal

It is proposed that the legislation be amended to remove the thresholds below which no VAT will be levied on the importation of goods (including books). The Customs procedures will also be simplified for the clearance of such goods.

Effective date

The proposed amendment will come into operation on a date to be announced by the Minister.

3.34. VAT Act – Clarifying the vat treatment in respect of payments made under the national housing programme

[Applicable provision: Section 8(23) of the VAT Act]

Background

Section 8(23) of the VAT Act provides that a vendor shall be deemed to supply services to any public authority or municipality to the extent of any payment to or on behalf of that vendor in terms of the National Housing Programme (NHP). Section 11(2)(s) of the VAT Act provides for a zero rating of services where the services are deemed to be supplied to a public authority or municipality in terms of section 8(23) of the VAT Act. The supply of a dwelling under a rental

agreement is an exempt supply in terms section 12(c)(i) of the VAT Act and as such, input tax deductions are denied.

Reasons for change

Section 8(23) of the VAT Act currently applies to any payment to or on behalf of a vendor in terms of the NHP. The purpose of the provision was to zero rate the supply of services by a vendor to a public or local authority in respect of what was then known as the Reconstruction and Development Programme which was more commonly known as RDP housing. In an attempt to simplify the application and interpretation of this section the reference to specific programmes under the NHP was deleted. The result was unintended fiscal leakage (in effect vendors inadvertently extended the scope of the zero rating to, amongst others, exempt supplies of rental stock and then consequentially deducting input tax on these supplies) without resolving the issues around the different interpretations on the scope and the application of the zero-rating.

Proposal

In order to address this confusion, it is proposed that section 8(23) of the VAT Act be amended so that the section 11(2)(s) zero-rating is narrowed. It is proposed that this be done by deleting the reference to “a national housing programme contemplated in the Housing Act” in section 8(23) and replacing it with the words “Housing Subsidy Scheme referred to in section 3(5)(a) of the Housing Act”.

Effective date

The proposed amendment will come into operation on 1 April 2026.

4. EXPLANATORY MEMORANDUM ON THE EXPORT REGULATIONS

[Applicable Provision: Regulation 8(2)(e)(ii) of the Export Regulations published in the Government Notice R.316 of 2 May 2014]

BACKGROUND

Part Two – Section A of the Export Regulations published in the Government Notice R.316 of 2 May 2014 (the Export Regulations) provides a procedure to be followed by a vendor who elects to supply movable goods at the rate of zero per cent to a qualifying

purchaser, where the movable goods are initially delivered to a harbour, an airport, or supplied by means of a pipeline or electrical line in South Africa before being exported.

Regulation 8(2)(e) of the Export Regulations states that a vendor may only elect to levy VAT at the zero rate where the vendor supplies movable goods to a qualifying purchaser or registered vendor and the movable goods are:

- situated at the designated harbour or airport;
- delivered to either the port authority, master of the ship, a container operator, the pilot of an aircraft or are brought within the control area of the airport authority; and
- destined to be exported from South Africa.

Richards Bay Coal Terminal (RBCT) is privately owned and operates the coal terminals at RBCT within the Richards Bay harbour. The coal terminals operated by RBCT are within the Richards Bay harbour precinct. In terms of the National Ports Act, No 12 of 2005 (the NPA), the term “port” is defined to mean any of the ports of Richards Bay, Durban, East London, Nqura, Port Elizabeth, Mossel Bay, Cape Town, Saldanha Bay, Port Nolloth or a port which has been determined as such in terms of section 10(2). Section 10(2) of the NPA states that the Minister of Transport may by notice in the Gazette determine ports in addition to the ports contemplated in subsection (1) which fall under the jurisdiction of the Authority, being Transnet National Port Authority (the TNPA).

The Minister has, in terms of section 80(d) of the NPA, issued the Ports Limits Regulations in which the port limits of Richards Bay have been clearly provided in Appendix 1 to the regulations. The coal terminals operated by RBCT fall within the Richards Bay port limits.

RBCT uses the port infrastructure (the berths, channels and other services) provided by the TNPA in terms of a lease agreement concluded between the TNPA and RBCT, which also stipulates the obligations of RBCT in relation to security, handling and safety. RBCT also operates the coal terminals under a dry bulk terminal operator license from the TNPA.

Once coal is delivered onto a stockpile at RBCT, it can only be loaded onto a ship for exportation from South Africa. There are no facilities to upload the coal onto trains or vehicles for inland transport. Furthermore, all dry bulk terminal operators must hold a license from the TNPA in terms of section 57 read with section 65 of the NPA to operate

a bulk terminal at a port. Similarly, container termina operators must hold a license from TNPA in terms of section 65 of the NPA.

REASONS FOR CHANGE

The strict interpretation of regulation 8(2)(e)(ii) of the Export Regulation requires that the coal must be delivered to the port authority (being the TNPA) and the TNPA must take possession of the coal supplied for the supply to qualify for zero-rating,. The mere delivery of coal at RBTC to registered vendors (generally foreign enterprises with no employees or fixed places of business in South Africa) for exportation from South Africa does not meet the requirements of regulation 8(2)(e)(ii) of the Export Regulation and zero-rating will not find application.

In light of the above, the wording of regulation 8(2)(e)(ii) of the Export Regulations seems to be causing practical difficulties in application.

PROPOSAL

It is proposed that the wording of regulation 8(2)(e)(ii) be revised to include any terminal operators operating under a license of the port authority in terms of section 65 of the NPA.

EFFECTIVE DATE

The proposed amendment will come into operation on 1 April 2026.

5. EXPLANATORY NOTE ON PUBLICATION OF DRAFT CARF REGULATIONS

Regulations for purposes of paragraph (c) of the definition of "International Tax Standard" in section 1 of the Tax Administration Act, 2011 (Act No. 28 of 2011), promulgated under section 257 of the Act, specifying the changes to the OECD Crypto-Asset Reporting Framework International Standard for the Exchange of Tax-Related Information between Countries (CARF)

The Draft CARF Regulations contains the Crypto-Asset Reporting Framework (CARF) as approved by the OECD's Committee on Fiscal Affairs over the course of 2022/2023.

The CARF was adopted as part of a comprehensive review of the Standard for Automatic Exchange of Financial Account Information in Tax Matters. This Standard, initially developed in response to a G20 request, was embodied in the OECD Recommendation on the Standard for Automatic Exchange of Financial Account

Information in Tax Matters and adopted by the OECD Council on 15 July 2014 and calls on jurisdictions to obtain information from their financial institutions and automatically exchange that information with other jurisdictions annually.

The CARF provides for the automatic exchange of tax relevant-information on Crypto-Assets and was developed to address the rapid development and growth of the Crypto-Asset market and to ensure that recent gains in global tax transparency will not be gradually eroded. The CARF consists of three distinct components:

- Rules and related Commentary and Guidance that can be transposed into domestic law to collect information from Reporting Crypto-Asset Service Providers with a relevant nexus to the jurisdiction implementing the CARF. These Rules and Commentary have been designed around four key building blocks:
    - the scope of Crypto-Assets to be covered;
    - the Entities and individuals subject to data collection and reporting requirements;
    - the transactions subject to reporting, as well as the information to be reported in respect of such transactions; and
    - the due diligence procedures to identify Crypto-Asset Users and Controlling Persons and to determine the relevant tax jurisdictions for reporting and exchange purposes.
- a Multilateral Competent Authority Agreement on Automatic Exchange of Information pursuant to the CARF (CARF MCAA) and related Commentary (or bilateral agreements or arrangements); and
- an electronic format (XML schema) to be used by Competent Authorities for purposes of exchanging the CARF information, as well as by Reporting Crypto-Asset Service Providers to report CARF information to tax administrations (as permitted by domestic law).

6. EXPLANATORY NOTE ON REVISED DRAFT CRS REGULATONS

New Draft Regulations for purposes of paragraph (a) of the definition of "international tax standard" in section 1 of the Tax Administration Act, 2011, (Act No. 28 of 2011), promulgated under section 257 of the Act, specifying the changes to the OECD Standard for Automatic Exchange of Financial Information in Tax Matters

The "Standard for Automatic Exchange of Financial Account Information in Tax Matters (hereinafter "the Standard") encompasses the "Common Reporting Standard" (hereinafter "the CRS"). The Standard, initially developed in response to a G20 request, was embodied in the OECD Recommendation on the Standard for Automatic Exchange of Financial Account Information in Tax Matters, adopted by the OECD Council on 15 July 2014 and calls on jurisdictions to obtain information from their financial institutions and automatically exchange that information with other jurisdictions annually.

Developed alongside the CARF, the first comprehensive review of the CRS has resulted in amendments to bring new financial assets, products, and intermediaries within its scope, because they are potential alternatives to traditional financial products, while avoiding duplicative reporting with that foreseen in the CARF. The amendments to the CRS ("the Revised CRS") contain a set of amendments to the CRS, along with associated Commentaries and exchange of information frameworks (collectively referred to as the International Standards for Automatic Exchange of Information in Tax Matters), as approved by the OECD's Committee on Fiscal Affairs over the course of 2022/2023.

The CRS was amended to bring certain electronic money products and Central Bank Digital Currencies in scope. Changes have also been made to ensure that indirect investments in Crypto-Assets through derivatives and investment vehicles are now covered by the CRS. In addition, amendments have been made for purposes of the following:

- To strengthen the due diligence and reporting requirements (including the reporting of the role of each Controlling Person) and to foresee a carve-out for genuine non-profit organisations.
- To enhance the reporting outcomes under the CRS, including through the introduction of more detailed reporting requirements, the strengthening of the

due diligence procedures, the introduction of a new, optional Non-Reporting Financial Institution category for Investment Entities that are genuine non-profit organisations and the creation of a new Excluded Account category for capital contribution accounts.

- In addition, further details have been included in the Commentary to the CRS in a number of locations to increase consistency in the application of the CRS and to incorporate previously released Frequently Asked Questions and interpretative guidance.

The Revised CRS comprises the following:

- The amendments to the CRS;
- An Addendum to the Multilateral Competent Authority Agreement on Automatic Exchange of Financial Account Information (CRS MCAA);
- The revised Commentaries on the CRS;
- The revised CRS-Related FAQs; and
- Model Mandatory Disclosure Rules for CRS Avoidance Arrangements and Opaque Offshore Structures.

7. NOTICES / REGULATION

7.1. Media release: Trusts Filing 2025/2026

11 September 2025 – SARS reminds trustees and the public of the official filing season for trusts that runs from 20 September 2025 to 19 January 2026.

All trusts must file a tax return annually, including those that are not economically active. A trust is included under the definition of a “person” in terms of the Income Tax Act, no.58 of 1962, and is therefore regarded as a taxpayer. A trustee is the representative taxpayer of a trust and is liable to file on behalf of the trust or appoint a registered tax practitioner to do so.

A provisional taxpayer is any person who receives income, or to whom income accrues, other than remuneration. Trustees should be aware of the requirements to submit provisional tax returns. In addition, trustees are also required to submit an IT3(t) third-party data return that provide details of amounts vested to beneficiaries. This return is due by 30 September 2025. For further details, visit the SARS website.

Trustees must submit their returns and mandatory supporting documents during filing. These documents include the trust instrument, annual financial statements, Letters of Authority, resolutions/minutes of trustee meetings, and an organogram depicting the beneficial ownership of the trust. Additionally, beneficiaries of trusts should declare their income, including income derived from a trust, in their personal income tax returns.

SARS has made it easy for taxpayers to comply through online filing. The Personal Income Tax Return (ITR12) and Trust Income Tax Return (ITR12T) are available on eFiling. Alternatively, an appointment to visit a SARS Service Centre can be made on the SARS website. Please take note that there are specific requirements should you wish to submit your tax return at a SARS Service Centre. Taxpayers are encouraged to refer to the SARS website for further information on their tax obligations, including trusts, and Provisional Tax.

SARS takes a zero-tolerance approach to taxpayers who do not register for the applicable tax, file tax returns, declare income accurately, or pay their tax debt. Non-compliance with these obligations is a criminal offence and will attract penalties and interest.

7.2. 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 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	31 Aug 2025	11,00%
1 September 2025	31 October 2025	10,75%
1 November 2025	Until change in the Public Finance Management Act rate	10,50%

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 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	31 August 2025	7,00%
1 September 2025	31 October 2025	6,75%
1 November 2025	Until change in the Public Finance Management Act rate	6,50%

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

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

DATE FROM	DATE TO	RATE
1 August 2020	30 November 2021	4,50%
1 December 2021	31 January 2022	4,75%
1 February 2022	31 March 2022	5,00%
1 April 2022	31 May 2022	5,25%
1 June 2022	31 July 2022	5,75%
1 August 2022	30 September 2022	6,50%
1 October 2022	30 November 2022	7,25%
1 December 2022	31 January 2023	8,00%
1 February 2023	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	31 August 2025	8,25%
1 September 2025	Until change in the Repurchase rate as announced by the Reserve Bank	8,00%

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.

8. TAX CASES

8.1. C:SARS v Candice-Jean Poulter (87 SATC 287)

Appellant, Ms Poulter, had come on appeal to a Full Bench of the High Court from a decision of a Tax Court confirming the original assessment of her taxable income for the 2018 year of assessment and ordering her to pay the Respondent's (being SARS) costs on the scale as between attorney and client, including the fees of two counsel.

The Tax Court's orders were made without hearing Ms Poulter who did not attend the proceedings in that court, or her father, Mr Gary Van der Merwe, who had sought audience there as Ms Poulter's authorised representative.

The Tax Court held that Mr Van der Merwe, who was not an admitted legal practitioner, was not entitled to appear on her behalf in the Tax Court which was 'a court of law'.

The Tax Court invoked the line of authority confirming that, save very exceptionally, only legal practitioners may represent natural persons in proceedings before a court of law in support of its approach.

Ms Poulter then successfully appealed the Tax Court's decision to a Full Bench of the Cape High Court (see *Candice-Jean Poulter* v *C:SARS* 86 SATC 415) where it held that Tax Courts were courts of revision, not courts of law. It held that the bar against lay representation in courts of law consequently did not apply in proceedings in a Tax Court. The effect of the Full Bench's judgment was that Ms Poulter may proceed with her appeal in a Tax Court represented by her chosen and duly authorised lay representative on a date to be advised by the Registrar of the Tax Court.

SARS in the present proceedings then applied to the Full Bench for leave to appeal to the Supreme Court of Appeal (SCA) from its judgment upholding Ms Poulter's appeal to it from the Tax Court.

The question that needed to be addressed in SARS' application for leave to appeal was whether the Full Bench had jurisdiction to adjudicate SARS' application for leave to appeal.

Ms Poulter contended that if SARS sought to appeal the Full Bench's judgment in the principal proceedings, SARS required special leave from the SCA in terms of section 16(1)(*b*) of the Superior Courts Act 10 of 2013 to be able to do so.

Section 16(1)(*b*) of the Superior Courts Act provided that:

'Subject to section 15(1), the Constitution and any other law–

…

(*b*) an appeal against any decision of a Division on appeal to it, lies to the Supreme Court of Appeal upon special leave having been granted by the Supreme Court of Appeal'.

Section 15(1) was not applicable in the circumstances of this case and the only 'other law' of relevance was the Tax Administration Act 28 of 2011 (TA Act), the pertinent provisions of which were considered in the present proceedings.

Ms Poulter gave notice, in terms of Uniform Rule 30, that she objected to SARS' application to the Full Bench for leave to appeal as an irregular step.

Judge Binns-Ward held the following:

(i) That the jurisdictional issue turns on whether the judgment of the Full Bench in the principal proceedings was 'a decision…on appeal to it' within the meaning of those words in section 16(1)(*b*) of the Superior Courts Act. If it was, then SARS has sought leave to appeal in the wrong forum and the court lacked the jurisdiction to decide their application.

(ii) That the word 'appeal' was specially defined in section 1 of the Superior Courts Act and, for current purposes, the term therefore bore its ordinary meaning, determined with regard to the context in which it had been employed.

(iii) That it was well established that in the context of legal proceedings the word 'appeal' can have different connotations and Trollip J famously identified three of those possible meanings in *Tikly and Others* v *Johannes NO and Others* 1963 (2) SA 588 (T), i.e. an appeal in the wide sense, an appeal in the ordinary strict sense and a review.

(iv) That an appeal to a Tax Court in terms of section 107 of the TA Act was another example of an appeal in the wide sense. It was not an appeal of the sort that Trollip J, in the second of his taxonomy, called 'an appeal in the ordinary strict sense.' Appeals from lower courts to courts higher up in the forensic hierarchy

were, by contrast, invariably appeals in the ordinary strict sense. That appeals to the Tax Court fell under the first, rather than the second, of the aforementioned categories no doubt explained the repeatedly made observation that the Tax Courts are courts of revision rather than courts of appeal in the ordinary sense.

(iv) That appeals from a Tax Court in terms of section 133 of the TA Act, whether to a Full Court of a division of the High Court, as in the appeal to this court, or directly to the SCA, were, by contrast, appeals in the ordinary strict sense of the word in the second category of appeal described in *Tikly*. They are decided on the basis of the record of the proceedings in the Tax Court, applying the same principles as those applied by any court of law sitting on appeal from a lower court.

(v) That an appeal from a Tax Court, whether to a Full Court of the High Court or directly to the SCA, is dealt with in both of those fora indistinguishably from the manner in which those courts would deal with an appeal from the judgment in a trial before a single judge in the High Court. Moreover, such an appeal falls, in terms of the TA Act, to be dealt with procedurally in terms of the Rules of those courts pertaining to appeals. The rules pertain to appeals within the meaning of that word in sections 16 and 17 of the Superior Courts Act.

(vi) That save in respect of cases in which three judges have sat in the appeal to the Tax Court in which event there is an automatic right of appeal directly to the SCA, an appeal in terms of section 133 of the TA Act lies directly to the SCA only upon leave granted by the President of the Tax Court concerned. The considerations to be taken into account equate with those that a single judge sitting at first instance in the High Court would take into account when deciding whether an appeal from his or her judgment should lie to a Full Court or directly to the SCA.

(vii) That an appellant from the judgment of a Tax Court dissatisfied with a decision of the President of the court not to allow an appeal directly to the SCA could apply to the SCA to have the decision varied, and a party who considers a decision by a President to allow an appeal directly to the SCA to be inappropriate could apply to the SCA to have it set aside. In this regard, section 17 of the Superior Courts Act is made applicable, in terms of section 135(3) of the TA Act, to appeals from a Tax Court and the provisions of the section

apply *mutatis mutandis* in the same manner as they do in respect of civil appeals from a single judge of the High Court.

(ix) That the word 'appeal' was presumed, wherever it appeared in section 17 of the Superior Courts Act, to bear the same meaning as it had in section 16 of the Act and it followed plainly from the incorporating cross-references in Part E of Chapter 9 of the TA Act to the Superior Courts Act and the Rules of Court made under the latter Act to procedurally regulate the appeals with which ss 16 and 17 of the Superior Courts Act were concerned that an appeal in terms of section 133 of the TA Act was not a horse of a different colour from any other appeal within the meaning of section 16 of the Superior Courts Act.

(x) That, to sum up, the express engagement of section 17 of the Superior Courts Act and the appeal rules of the SCA and the High Court in Part E of Chapter 9 of the TA Act, as well as the character of an appeal to either of those courts in terms of section 133 of the TA Act, provided strong contextual confirmation that the principal proceedings in this court were an 'appeal' within the meaning of that word as employed in the Superior Courts Act.

(xi) That the conclusion reached by the court in this respect found support in the jurisprudence in *C:SARS* v *Capstone 556 (Pty) Ltd* 78 SATC 231 and the clear import was that an appeal from a Tax Court presided over by a single judge to the SCA was of the same type of appeal as an appeal from the judgment of a single judge of the High Court to the SCA. There was obviously no difference in the character of an appeal from a Tax Court to a Full Court and an appeal from the Tax Court directly to the SCA. They were both of the same sort of appeal with which ss 16 and 17 of the Superior Courts Act were concerned.

(xii) That all of the forementioned considerations impelled the conclusion that any appeal from this court's judgment in the principal proceedings may only be prosecuted subject to section 16(1)(*b*) of the Superior Courts Act.

(xiii) That SARS had contended that section 16(1)(*b*) of the Superior Courts Act did not apply by reason of this court's finding that the Tax Court's functions were predominantly administrative in character. He contended that the application for leave to appeal was properly directed to this court, *i.e.* the Full Court, because it, as the first court of law seized of the case, had heard the matter 'at first instance.' The argument was somewhat paradoxical and placed SARS on the horns of a dilemma because it flew in the face of the principal contention that SARS wanted to pursue on further appeal, *viz* that the Tax Court was the

first court of law seized of Ms Poulter's appeal. If SARS were to be held true to his principal contention, he would self-evidently be in the wrong forum for his application for leave to appeal.

(xiv) That the question before the Full Court in the principal application was not whether a Tax Court is an administrative tribunal; it was whether a Tax Court was 'a court of law.' This court, relying on the eminent local and international authority that was canvassed extensively in the judgment, drew heavily, but not entirely, on the predominantly administrative character of the Tax Court's functions to categorise those courts as falling outside the judicial system established in terms of section 166 of the Constitution, and, consequently, not to be 'courts of law.' The Full Court did not hold that Tax Courts were not courts in any sense of the word. On the contrary, having found that the Tax Courts established in terms of the TA Act were indistinguishable in form and function from their statutory predecessors, the so-called Special Tax Courts, it followed a hallowed line of Higher Court authority in holding that the Tax Courts were courts of revision, not ordinary courts of appeal.

(xv) That enough had been said to explain the court's conclusion that section 16(1)(*b*) of the Superior Courts Act did apply in the current matter and that this court consequently did not have jurisdiction to determine an application for leave to appeal from its judgment in the principal proceedings.

(xvi) That in the circumstances the court had no reason to address the merits of the application for leave to appeal. Suffice it to say, however, that it should be evident from the court's judgment in the principal proceedings that SARS' contention that the Tax Courts were courts of law went against the weight of authority and the court considered that it would be difficult for a further court of appeal to uphold the contention in the face of the finding by the Constitutional Court in *Metcash Trading Ltd* v *C:SARS and Another* 63 SATC 13 that appeals to the Special Courts involve a first level of adjudication that takes place 'outside the normal forensic hierarchy.'

(xvii) That SARS stressed that the characterisation of the Tax Courts was a matter of public interest sufficiently compelling to warrant the attention of a higher court. Whilst it may indeed be a matter of public interest, the prospects of success 'remain vitally important and are often decisive' when evaluating whether there is a compelling reason why an appeal should be heard.

(xviii) That Ms Poulter was entitled to her costs in the abortive proceedings and it seemed to the court, having regard to the nature of the questions involved and the seniority of counsel appropriately engaged by SARS, that the costs should be awarded on Scale B, such costs to include the costs incurred by Ms Poulter in raising an objection to the court's jurisdiction to decide the application.

SARS' application for leave to appeal was struck from the roll.

8.2. Citibank NA and another v C:SARS (87 SATC 321)

First Applicant, 'Citibank SA', was a corporation chartered in the United States of America and it carried on the business of a bank in South Africa by means of a branch and was registered for value-added tax in South Africa.

Second Applicant was a private company registered in accordance with South African law and was also part of Citigroup Inc. It was a wholly owned subsidiary of Citigroup Financial Products Incorporated (USA) and was a member of the Johannesburg Stock Exchange and was also registered for value-added tax.

SARS and responsible for the administration of the Value-Added Tax Act (the VAT Act) together with the Tax Administration Act (TA Act).

Applicants had made an application to the Gauteng Division of the High Court for an order declaring that payments made by the First and Second Applicants to the Citigroup home country sending entities in relation to seconded employees on 'expatriate assignments' with the Applicants comprised the reimbursement of salary costs which fell outside the scope of value-added tax in terms of section 7(1)(*c*) read with section 14(5)(*d*) of the VAT Act and were not for the supply of imported services as defined in section 1 of the VAT Act which were vatable.

Citigroup had a global presence and persons employed by members of Citigroup were seconded to constituents of Citigroup in other countries. The constituent companies were described as 'Home Country Entities' and a Home Country Entity in a country may second its employees to a Home Country Entity in a different country by concluding an assignment agreement with employees who are to be seconded to another Home Country Entity.

The Home Country Entity that seconds the employee is 'the Sending Home-Entity' and the Home Country Entity that receives an employee is 'the Receiving Home-Entity.'

The assignment agreement stipulates that the Sending Home-Entity lends the services of the seconded employees to the Receiving Home-Entity. The lending is done in terms of an inter-company agreement between the Sending Home-Entity and the Receiving Home-Entity, and the inter-company agreement is 'for the supply of employee services.'

The assignment agreement also provides that a seconded employee will be on an 'expatriate assignment' and a person seconded remains an employee of the Sending Home-Entity and will not be an employee of the Receiving Home-Entity. A seconded employee is also not an employee of Citigroup NA which administers the 'expatriate salary and benefits' of a seconded employee.

Applicants contended that the seconded employees were their employees for the following reasons:

(a) the seconded employees placed their productive capacity at the disposal of the Applicants and furthered the enterprise of the Applicants in the course of their employment,

(b) the Applicants had the right of supervision and control over the seconded employees for the duration of their secondment to the Applicants,

(c) Applicants paid the Sending Home-Entity for the supply of the seconded employees' services to the Applicants who in turn made payment to the seconded employees, and

(d) the seconded employees received remuneration for the supply of their services to the Applicants and the Applicants deducted and withheld employees' tax from such remuneration as their employer.

Applicants contended that they were not liable for value-added tax on the supply by the seconded employees of services to the Applicants. because value-added tax was not payable in respect of a supply by a person of services contemplated in proviso (iii)(*aa*) of the definition of 'enterprise' in section 1 of the VAT Act, i.e. the rendering of services by an employee to his employer in the course of his employment, to the extent that remuneration is paid to such employee.

Applicants further contended that services rendered by the seconded employees were not 'imported services' as defined in section 1 of the VAT Act. They further contended that even if the services could be regarded as 'imported services', value-added tax that would be chargeable in terms of section 7(1)(*c*) of the VAT Act would not be payable

where the seconded employees provide services to the Applicants in the course of their employment with the Applicants as contemplated in section 14(5)(*d*) of the VAT Act.

Applicants accordingly concluded that no value-added tax was chargeable or payable by the Applicants to SARS in respect of the services supplied to the Applicants by the seconded employees.

SARS contended that the question was not whether seconded employees were employees in terms of South African law but rather whether the Applicants were liable to pay VAT on such imported services and this entailed a determination of whether the Applicants were employers of the seconded employees in terms of the definition of employer in the relevant Tax Acts.

SARS disputed that the seconded individuals were employees of the Applicants as the Sending Home-Entity paid the salaries of these individuals on behalf of the Applicants and the Applicants, in turn, reimbursed the Sending Home-Entity.

SARS further contended that the inter-company agreements confirmed that seconded individuals remained the employees of the Sending Home-Entity and that salaries were administered by another overseas constituent company on behalf of the employer, i.e. the Sending Home-Entity.

'Imported services' was defined in section 1 of the VAT Act as being 'a supply of services that is made by a supplier who is resident or carries on business outside South Africa to a recipient who is a resident of South Africa to the extent that such services are utilised or consumed in South Africa otherwise than for the purpose of making taxable supplies'.

In terms of section 7(1)(*c*) of the VAT Act, VAT of 15% was payable on the acquisition of imported services.

Section 14(5)(*d*) of the VAT Act exempted the payment of VAT on imported services on a supply by a person of services as contemplated in terms of proviso (iii)(*aa*) to the definition of 'enterprise' in section 1 of the VAT Act, i.e. remuneration paid by an employer to an employee.

Judge Mooki held the following:

(i) That, given that the relief in this matter dealt with a taxation issue, it required consideration of the meaning of the concepts 'employee', 'employer' and

'remuneration' as these concepts were dealt with in the taxation statutes for purposes of the subject-matter of the relief sought by the Applicants.

(ii) That the Applicants did not deal with the meaning of 'employer' or 'employee' as defined in para 1 of the Fourth Schedule to the Income Tax Act in addressing the nature of the relationship between themselves and the seconded employees. This would have been expected to be factored into the Applicants' persuasion of the court as to the nature of the relationship between the Applicants and the seconded employees.

(iii) That the Applicants were expected to show why the court ought to have regard, in determining the nature of the relationship between themselves and the seconded employees, to the definition of 'employer' and 'employee' only, according to the labour laws and this was not done.

(iv) That the Applicants had to show that proviso (iii)(*aa*) to the definition of 'enterprise' in section 1 of the VAT Act applied as regards the relationship between the Applicants and the seconded employees (i.e. that it was an employer-employee relationship) for the Applicants not to otherwise be liable for VAT.

(v) That the Applicants accordingly had to show that they were 'employers' as contemplated in proviso (iii)(*aa*) and that the seconded employees were 'employees of the Applicants', also as contemplated in the proviso. The Applicants also had to show that the seconded employees rendered services in the course of their employment with the Applicants and that they had paid the seconded employees 'remuneration'.

(vi) That the Applicants did not substantiate what constituted 'supervision and control' of the seconded employees. For example, they say nothing about what restrictions, if any, they must impose on seconded employees as this was the usual form of 'supervision and control' that an employer had over an employee. Moreover the Applicants, in using the formula 'supervision and control' in relation to the seconded employees, did nothing more but recite the wording of a statute.

(vii) That the Applicants did not address the assignment agreement other than in general terms, by saying that the seconded employees were also employed by the home country entities in terms of their contracts of employment. This did not address the specific injunction in the assignment agreement that seconded

employees do not become employees of the entity to which they have been assigned.

(viii) That there was also no further explanation such as, for example, how the salary of the seconded employees was treated in the light of the fact that the Sending Home-Entity, according to the assignment agreement, remained liable for the salaries of the seconded employees paid by Citigroup NA as agent for the Sending Home-Entity.

(ix) That the present application faulters at two levels:

- First, the Applicants have not shown that they were 'employers' of the seconded employees.
- Second, the Applicants have not shown that payments by them to the Sending Home-Entity constituted 'remuneration' within the meaning contemplated in proviso (iii)(*aa*) to the definition of 'enterprise.'

Application dismissed.

Applicants ordered to pay costs.

8.3. ITC 1984 (87 SATC 331)

The taxpayer had applied to the Cape Town Tax Court to have the statement of grounds of assessment and opposing the appeal delivered SARS in terms of Tax Court Rule 31 of the rules promulgated under section 103 of the Tax Administration Act (the TA Act), set aside as an irregular step in terms of High Court Rule 30(1), alternatively to be struck out in terms of High Court Rule 23(2).

The taxpayer relied on the High Court Rules, i.e. the Uniform Rules of Court, by virtue of Tax Court Rule 42, which permitted the use of High Court Rules where the procedure in question was not covered by the Tax Court Rules.

The taxpayer had entered into a series of intricate and complex transactions from 2014, which were viewed by SARS as being the impermissible tax avoidance arrangement that gave rise to the dispute in the present matter.

In October 2014 the taxpayer, who was an employee and director of the Company A group of companies ('Company A') started the process of restructuring its affairs ('the restructuring') and at the time he held Company A shares both directly (i.e. in its own

name) and indirectly through two companies, Company B (Pty) Ltd ('Company B') and Company C Investments (Pty) Ltd ('Company C'). He was also a discretionary beneficiary in 'the trust' which would feature in the restructuring.

The objective of the first of two groups of transactions was to move the taxpayer's assets, both directly, and indirectly held, to a holding company and to achieve that objective it embarked on a series of transactions. First, the taxpayer acquired all the shares in Company D (Pty) Ltd (the Company D shares acquisition and 'Company D'), a process that was completed by 25 November 2014. Second, in December 2014, Company D acquired the taxpayer's assets, including its directly and indirectly held Company A shares in return for shares in itself ('the taxpayer EJP's assets acquisition'). Third, in March 2015, Company D distributed R1 391 276 400 to the taxpayer ('the distribution'). Company D funded the distribution by issuing 955 A-Class ordinary shares to the trust for R1.39 billion ('the subscription proceeds'). The aspect of the first group of transactions that featured prominently in what followed was the distribution by Company D to the taxpayer and the fact that it was funded by the subscription proceeds.

The purpose of the second group of transactions was to deal with the acquisition by Company E International Holdings Limited ('Company E'), or a nominated subsidiary, of Company A. While the taxpayer's indirect shareholding in Company A via Company B was initially excluded, during January 2015 Company E commenced negotiations with Company B to acquire its Company A shares. Negotiations were successful. In pursuance of the successful negotiations, on 19 February 2015, it was agreed that Company B would buy the Class C ordinary shares in Company A from Company D ('the Company B repurchase'). Company D used the proceeds of the Company B repurchase ('the Company B repurchase proceeds') to subscribe for new Class E ordinary shares in Company B. Company D then exchanged its shares in Company A and Company B for Company E shares ('the Company AE share exchange'). On 17 April 2015 the second group of transactions became unconditional and by 20 April 2015 all the transactions in the second group had taken place. The relevant part of the second group of transactions was the Company B repurchase and the utilisation of the Company B repurchase proceeds by Company D to subscribe for shares in Company B rather than funding the distribution.

SARS, four years after the transactions in issue, on 20 March 2019, and acting in terms of section 46 of the Tax Administration Act 28 of 2011, made a 'request for relevant information' regarding the taxpayer's 2015 to 2018 tax years.

The taxpayer responded with supporting documentation to the requests and told SARS about the taxpayer asset acquisition, i.e. that he had sold its directly and indirectly held shares in Company A to Company D for shares in the latter and expressed the view that section 42 (keeping the taxpayer informed) was applicable. He disclosed receipt of the distribution and explained that, but for R167 696 542, the distribution did not reduce Company D's contributed tax capital ('CTC'). He also responded that of the three distributions that made up the distribution as defined, the first qualified as a 'return on capital' and the taxpayer had reduced its 'base cost' by a similar amount. The other two distributions, he said, qualified as tax exempt dividends. He further responded that the first two distributions making up the distribution as defined were used to pay the call option premium and the third was used by him to pay living expenses.

SARS, on 30 July 2020, and possessed of all the knowledge and documents provided in the taxpayer's three responses and being of the view that the GAAR was applicable, issued a notice in terms of section 80J(1) of the Income Tax Act ('the GAAR notice').

The GAAR provisions empower SARS to impose a tax liability on a taxpayer where it has been a party to an impermissible avoidance arrangement.

SARS, in the GAAR notice, expressed the view that the parties planned and anticipated the Company B repurchase and the Company B repurchase proceeds were intended to flow to the taxpayer and the trust and the taxpayer and the trust anticipated a dividends tax liability arising from the Company B repurchase and they facilitated a dividend strip in order to contrive a situation where the Company B repurchase dividend would flow to the taxpayer and the trust, where dividends tax liability could be offset by the STC credits. The remedy envisaged by SARS in terms of section 80B(1) of the Act was the disregarding of all transactions except for the Company B repurchase and an imposition of dividends tax and penalties on the taxpayer. SARS had thus, despite everything it had been told in the responses to the requests for relevant information, decided not to believe the taxpayer that the subscription proceeds had funded the distribution.

The taxpayer responded to the GAAR notice on 28 September 2020 and flagged the proposed remedy as an issue. He informed SARS that the distribution was funded by the subscription proceeds arising from the trust subscription and that the proceeds of the Company B repurchase were 're-invested by Company D in a different class of shares in Company B and which shares were subsequently exchanged for shares in Company E.'

The taxpayer, under the heading 'SARS' proposed remedy' and as part of its conclusion, again stated that the Company B repurchase proceeds did not flow to the taxpayer and thus that 'the proposed remedy cannot be applied'.

After the taxpayer's response to the GAAR notice, SARS again requested additional information, this time in terms of section 80J(3)(*a*) which was the information gathering provision within the GAAR and the taxpayer had responded on 25 January 2021.

SARS, on 24 February 2021, notified the taxpayer that he was not dissuaded from its findings in the GAAR notice and assessed the taxpayer for dividends tax and penalties as envisaged in the GAAR notice.

The taxpayer challenged the assessment raised by SARS by way of review proceedings in the Western Cape High Court which was struck from the roll in a judgment delivered on 8 August 2023.

The taxpayer thereafter objected to the assessment which objection was disallowed, and he subsequently filed its appeal to the Cape Tax Court and thereafter SARS filed its Rule 31 statement (statement of grounds of assessment and opposing appeal) on 28 July 2023 which led to the taxpayer's present interlocutory application in the Tax Court.

The taxpayer contended that SARS had introduced changes in its Rule 31 statement which rendered it an irregular step to be set aside in terms of Tax Court Rule 42 read with High Court Rule 30(1), alternatively to be struck out in terms of High Court Rule 23(2).

Judge Myburgh held the following:

(i) That the GAAR was different to most fiscal provisions in that SARS must call for the taxpayer to make representations before it may issue an assessment and this it did by way of the GAAR notice which must conform to the prescripts contained in section 80J of the Income Tax Act.

(ii) That section 80J is peremptory, both in the sense that a GAAR notice must be given, and as regards what a GAAR notice must contain. The GAAR notice must detail the arrangement and explain why SARS holds the view that it is an impermissible avoidance arrangement and this can only be done with reference to section 80A which defines an impermissible tax avoidance arrangement. A GAAR notice must also explain what SARS proposes to do where it has determined that there is such an arrangement, i.e. what it proposes as a

remedy. Here section 80B is the reference point. It is only possible to give content meaning to section 80J(1) by reading it with reference to its immediate statutory context which is, *inter alia*, sections 80A and 80B.

(iii) That, on receipt of a GAAR notice, the taxpayer, in terms of section 80J(2), is given an opportunity to respond. Sections 80J(1) and (2) are linked, as a question and answer are linked. What must be addressed depends on what is said in the GAAR notice. The section 80(J)(2) response must address SARS' understanding of the arrangement and the factual and legal basis for the imposition of the GAAR notice as well as the application of the GAAR, i.e. the remedy.

(iv) That in terms of section 80J(4), SARS, if additional information comes to its knowledge, may, at any stage after it has issued a GAAR notice, revise or modify its reasons for applying the GAAR or if it withdrew the GAAR notice, issue a new GAAR notice.

(v) That Tax Court Rule 31(3) provided that SARS may include in its Rule 31 statement a new ground of assessment unless it constitutes a novation of the whole of the factual or legal basis of the disputed assessment or required the issue of a revised assessment.

(vi) That the court was in accord with the general proposition that SARS may not broaden its case in its Rule 31 statement from that set out in the GAAR notice and assessment, in a manner that negates the taxpayer's right to procedurally fair administrative action as catered for in section 80J(1) to (3) of the Act.

(vii) That section 80J(4) must be read within its immediate statutory context, i.e. section 80J as a whole. Section 80J(4) permitted SARS to do two things if additional information came to its notice. It may revise or modify its reasons for applying the GAAR (i.e. revise or modify the underpinning of the assessment), or if it has withdrawn the GAAR notice, issue a new one. Those are the two options and, in both cases, the jurisdictional fact for the revision or modification of the reasons for applying the GAAR, or the giving of a new GAAR notice, is additional information coming to SARS' notice.

(viii) That in this instance SARS opted to revise or modify its reasons for applying the GAAR in its Rule 31 statement, without issuing a new GAAR notice or issuing a new assessment.

(ix) That information is 'knowledge' or 'intelligence' given. In section 1 of the TA Act 'information' is defined as including 'information generated, recorded, sent, received, stored or displayed by any means.' A written document or a recording is the repository of knowledge. In simple terms SARS must have learnt something new, and it did not. Additional information did not come to SARS' notice; it changed its mind about what it already knew at the time it issued the GAAR notice. Thus, the jurisdictional fact underpinning SARS' right to revise or modify its reasons for applying the GAAR was absent.

(x) That section 80J(4) could not justify introducing a new GAAR assessment through a Rule 31 statement, which was a document defending the grounds and basis of that GAAR assessment. This is not any assessment; it is a GAAR assessment and must comply with the provisions peculiar to the GAAR. To interpret the provisions in question, so as to allow the circumvention of the GAAR provisions would make them inoperative.

(xi) That SARS' argument that the taxpayer's right to *audi alteram partem* was not affected in this instance because he had the right to contest an assessment by way of the objection and appeal processes set out in the Tax Administration Act and the Tax Court Rules was not correct.

(xii) That the dispute resolution processes under the Tax Administration Act cannot remedy the failure to permit a taxpayer a statutorily enshrined opportunity to be informed of SARS' proposed intention to apply the GAAR and to address SARS' proposed exercise of its GAAR power before assessment. This interpretation rendered the GAAR notice provisions superfluous.

(xiii) That, accordingly, the changes that SARS sought to introduce in its Rule 31 statement required the issue of a new GAAR notice and a new assessment, and thus the Rule 31 statement constituted an irregular step which fell to be set aside in terms of High Court Rule 30(1) and SARS was ordered to pay the taxpayer's costs, including the costs of two counsel.

9. INTERPRETATION NOTES

9.1. Assessed losses: Companies: The 'trade' and 'income from trade' requirements – No. 33 (Issue 6)

This Note clarifies when a company may forfeit its right to carry forward its assessed loss from the preceding year of assessment as a result of it:

- not carrying on a trade during the current year of assessment, or
- having carried on a trade during the current year of assessment, but not deriving any income from trade during that year of assessment.

Under section 20(1)(a) a company that does not carry on a trade during a year of assessment forfeits the right to carry forward its assessed loss from the immediately preceding year of assessment (the 'trade' requirement). The question arises whether a company that has traded during the current year but has derived no income from trade during that year may forfeit the opportunity to carry forward its assessed loss from the preceding year (the 'income from trade' requirement).

SARS is of the view that section 20 contains a trade requirement and an income from trade requirement. Both these requirements must be satisfied before an assessed loss may be carried forward. SARS does, however, accept that this may have some unintended results. In dealing with the problem, SARS will accept that as long as the company has proved that a trade has been carried on during the current year of assessment, the company will be entitled to set off its balance of assessed loss from the preceding year, notwithstanding the fact that income may not have accrued from the carrying on of that trade.

This concession is limited to situations in which it is clear that trade has been carried on. SARS will apply an objective test in order to determine that a trade has in fact been carried on. It will not be sufficient that there was a mere intention to trade or some preparatory activities. The fact that no income was earned during the year of assessment must be incidental or result from the nature of the trade carried on by the company.

Although SARS is prepared to accept that the absence of income from trade (that is, gross income less exempt income) should not in all cases prevent the set-off of a balance of assessed loss, a company that derives no income from trade will have to discharge the onus that it did in fact trade during the current year. The absence of

income from trade may well indicate that the company did not trade during the year in question.

While the views of SARS as contained in this Note provide direction in interpreting the legislation, each case will be considered on its merits in deciding whether a company has commenced or carried on a trade and much will depend upon the nature and the extent of the company's activities.

Cognisance should be taken of the view expressed in 5 when a company has clearly carried on a trade during the current year of assessment but has not derived any trade income during that year.

9.2. Taxation of amounts received by or accrued to missionaries – No. 39

This Note provides clarity on the tax treatment of amounts received by or accrued to missionaries who are performing religious or related activities.

A missionary is a member of a religious mission. A religious mission comprises a group of people sent by a religious body to perform religious and social work, educational or hospital work, or to spread that religious body's faith. Often, missionaries operate under the 'banner' of a missionary organisation.

Typically, a missionary is not employed by a missionary organisation, and depends on contributions to meet costs related to both the missionary work undertaken and personal expenditure. The contributions are usually made by a community or members of a missionary organisation of which the missionary is a member. Often, these amounts are paid directly by individuals to the missionary organisation, which controls and administers the amounts received for its own benefit and on its own behalf, and then passes on all or part of the amounts to the relevant missionary. In other instances, the contributions can either be made directly to the missionary, or the missionary organisation may simply act as a conduit for the amounts received.

This Note clarifies the correct income tax treatment of the amounts received by or accrued to missionaries. Any donations tax implications of amounts paid to missionaries, as well as the implications of any tax treaty, are beyond the scope of this Note.

Amounts received by or accrued to missionaries for missionary services rendered in South Africa must be included in the missionary's 'gross income' and will be subject to

normal tax. Employed missionaries may qualify for a tax exemption if missionary services are rendered outside of South Africa. Missionaries outside of the employees' tax system must consider whether they are provisional taxpayers.

9.3. Skills development levy exemption: Public Benefit Organisations – No. 10 (Issue 5)

This Note provides guidance on the interpretation and application of section 4(c) of the SDL Act, which exempts any PBO contemplated in section 10(1)(cN) from the payment of SDL, provided the PBO solely

- carries on qualifying PBAs; or
- provides funds to PBOs solely carrying on qualifying PBAs.

SARS is responsible for the administration of the SDL Act in so far as it relates to the collection of SDL payable to SARS by employers. The SDL Act imposes on every employer an SDL on the total amount of remuneration paid or payable or deemed to be paid or payable by an employer to its employees during any month. The amount of such remuneration is the same as the amount of remuneration determined under the Fourth Schedule from which an employer is obligated to withhold employees' tax taking into consideration certain exclusions in the SDL Act.

The SDL is not payable, amongst other things, by any PBO contemplated in section 10(1)(cN), which solely:

- carries on any qualifying PBAs; or
- provides funds to PBOs solely carrying on the qualifying PBAs.

An employer liable to pay SDL must apply in such manner as SARS may determine to be registered as an employer for the purposes of SDL. Even an employer, that is a PBO, which is exempt from the payment of SDL must register with SARS.

This Note considers only the exemption of the payment of SDL by any PBO meeting the requirements of section 4(c) of the SDL Act.

An organisation approved by SARS as a PBO is not automatically exempt from the payment of SDL under the SDL Act. The exemption from the payment of SDL under section 4(c) of the SDL Act will apply only if the requirements of that section are met.

The obligation will be on the PBO to prove that it meets the strict requirements of section 4(c) of the SDL Act.

9.4. Capital gains tax: Public Benefit Organisations – No. 44 (Issue 4)

This Note provides guidance on the interpretation and application of paragraph 63A dealing with the disregarding of a capital gain or capital loss on the disposal of an asset by a PBO.

A PBO must disregard any capital gain or capital loss determined on the disposal of an asset if:

- that PBO did not use that asset on or after valuation date in carrying on any business undertaking or trading activity; or
- substantially the whole of the use of that asset by that PBO on and after valuation date was directed at:
    - a purpose other than carrying on a business undertaking or trading activity; or
    - carrying on a permissible business undertaking or trading activity.

Any capital gain or capital loss on the disposal of an asset used in a business undertaking or trading activity falling outside the ambit of the permissible business undertakings or trading activities and which is subject to the basic exemption will not be disregarded.

This Note applies broad principles in interpreting the legislation. Since the facts and circumstances pertaining to a specific PBO may differ, each case must be considered on its own merits.

9.5. Deductions in respect of improvements to land or buildings not owned by a taxpayer – No. 119 (Issue 2)

This Note provides guidance on the interpretation and application of the following:

- Section 12N, which facilitates allowances under specified sections of the Act for improvements made to land or buildings not owned by a taxpayer but over which the taxpayer holds a right of use or occupation. The improvement must be effected under a PPP, a lease agreement with the state or certain other tax-

exempt statutory bodies and the state or that body owns the land or building, or under the Independent Power Producer Procurement Programme.

- Section 12NA, which deals with deductions for improvements effected under a PPP by a person to land or to a building over which the state holds the right of use or occupation.

Other sections in the Act, which potentially provide an allowance on improvements to land or buildings not owned by the taxpayer, include section 11(g) and section 13bis. These sections are not dealt with in this Note. See Interpretation Note 110 “Leasehold Improvements” and Interpretation Note 105 “Deductions in respect of Buildings used by Hotel Keepers”.

The Act provides for a variety of depreciation allowances for the creation or acquisition of qualifying movable or immovable assets. In order to qualify for these allowances, the taxpayer must generally be the owner of the assets. Under the common law principle of superficies solo cedit (owner by accession), buildings or other structures affixed or attached to land become the property of the owner of the land.

Often lease agreements of immovable property require the lessee to effect improvements on land or to buildings as part of the obligations under the agreement. The problem with such an arrangement is that the land belongs to the lessor and the improvements become the property of the lessor when effected. The lessor is not entitled to use the improvements until the lease expires and as the lessee is not the owner, many allowances are not applicable. In order to address these issues, the Act contains specific provisions relating to leasehold improvements.

In relation to the lessee, section 11(g) provides for a deduction of expenditure actually incurred by a lessee in pursuance of an obligation to effect improvements on land or to buildings under an agreement under which the right of use or occupation of the land or buildings is granted by the lessor.

The allowance under section 11(g) does not, however, apply if the value of the improvements effected by the lessee does not constitute income of the lessor.3 A taxpayer effecting leasehold improvements to land owned by the state would not be able to secure a deduction under section 11(g), since the state is exempt from tax under section 10(1)(a). In order to encourage private sector participation in government projects it was therefore necessary to introduce specific legislation to enable taxpayers to secure deductions for leasehold improvements effected to state-owned land or buildings.

Section 12N does not provide for a deduction, however, it was introduced to facilitate allowances available under other sections on improvements not owned by a taxpayer. The expenditure incurred by a lessee may be made under an obligation or voluntarily to effect improvements on leased land or buildings.

Section 12NA was introduced to provide for a deduction when a person has an obligation under a PPP to effect an improvement to land or a building over which the state holds the right of use or occupation.

Under section 11(g) a lessee is entitled to write off obligatory improvements over the period of the lease or 25 years, whichever is the lesser. Section 11(g) does not, however, apply when the lessor is a tax-exempt person and thus excludes, for example, lessees that effect improvements to state-owned property.

Section 12N was introduced to enable a lessee to claim capital allowances on leasehold improvements effected to land or buildings for which the taxpayer has a right of use or occupation and effects the improvements under a PPP, a lease agreement with the state or certain other tax-exempt statutory bodies if the state or entity owns the property, or under the Independent Power Producer Procurement Programme. It deems the lessee to be the owner of the improvements for the purposes of specified allowance provisions and the Eighth Schedule. Banks, financial service providers and insurers are excluded from section 12N. The improvement is deemed to be disposed of on the later of when the right or use or occupation is terminated or the use or occupation terminates. Depending on the facts, taxpayers may need to consider a potential recoupment or scrapping allowance, and capital gain or loss consequences. Sub-letting is impermissible except in specified circumstances between members of the same group of companies.

Section 12NA applies when government holds a right of use or occupation for land or buildings and a person effects obligatory improvements to that land or those buildings under a PPP. The amount deductible in any year of assessment is determined on a straight-line basis by dividing the expenditure actually incurred in effecting an improvement by the lesser of the number of years over which the taxpayer will derive income under the PPP agreement or 25 years.

A grant received or accrued for the purposes of effecting the improvements may be exempt from normal tax if it meets the requirements of section 10(1)(zI) (before 1 January 2016). Before 1 January 2016 the person must reduce the cost of the improvements for the purpose of determining the amount that may be claimed as a deduction under section 12NA(3). On or after 1 January 2016 the aggregate amount

that may be claimed as a deduction is limited to the cost of the improvements less the amount of the grant under section 12P(4). Banks, financial service providers and insurers are excluded from section 12NA.

10. DRAFT INTERPRETATION NOTES

10.1. Income tax exemption: bodies corporate, share block companies and associations of persons managing the collective interests common to all members – No. 64 (Issue 5)

This Note provides guidance on the interpretation and application of section 10(1)(e).

Section 10(1)(e) exempts from income tax the levy income of a body corporate, a share block company and any other association of persons. The section provides also for a basic exemption. Expenditure incurred in respect of the levy income is not an allowable deduction.

In conclusion:

- bodies corporate and share block companies qualify for an automatic exemption from income tax under section 10(1)(e)(i)(aa) and (bb), respectively, therefore no approval by SARS is required;
- associations of persons must apply to SARS for approval under section 10(1)(e)(i)(cc);
- retrospective approval may be considered by SARS provided the conditions and requirements as considered in this Note are met by an association of persons;
- a person is disqualified from managing the collective interests common to all the members of an association of persons if that person is disqualified under the Trust Property Control Act, the NPO Act or the Companies Act;
- the levy income of bodies corporate, share block companies and associations of persons approved by SARS is fully exempt from income tax under section 10(1)(e)(i);
- the sum of any other income, other than levy income, received by or accrued to bodies corporate, share block companies or associations of persons is subject to a basic exemption under section 10(1)(e)(ii);

- an assessed loss created when the allowable expenditure exceeds income from sources other than levy income and the basic exemption of bodies corporates, share block companies or other associations of persons is carried forward to a future year of assessment and a balance of assessed loss is not forfeited if bodies corporate, share block companies and any other associations of persons receive only levy income;
- bodies corporate, share block companies and associations of persons are excluded from the payment of provisional tax and are not required to submit provisional tax returns;
- donations made by or to a body corporate, share block company or an association of persons are exempt from donations tax under section 56(1)(h);
- bodies corporate, share block companies and associations of persons are not permitted to issue section 18A receipts for levies or donations received;
- the transfer of immovable property in a share block company to a holder of shares in the company will not give rise to a capital gain or capital loss in the company under paragraph 67B(3)(a) of the Eighth Schedule;
- a cash dividend paid to a body corporate, share block company or an association of persons is exempt from dividends tax under section 64F(1)(a); and
- a dividend in specie declared and paid by a share block company that comprises a disposal contemplated in paragraph 67B(2) of the Eighth Schedule is exempt from dividends tax under section 64FA(1)(d).

11. GUIDES

11.1. Guide to the Urban Development Zone Allowance (Issue 10)

This guide is a general guide about the urban development zone (UDZ) allowance provided for in section 13quat of the Income Tax Act.

Similar to many other countries, South Africa has a number of urban areas that are impoverished and suffering from extensive urban decay. In order to address these problems and maintain existing infrastructure, governments internationally have increasingly used tax measures to support efforts aimed at regenerating these urban areas.

In 2003, the Minister announced a tax incentive in the form of an accelerated depreciation allowance under section 13quat which sought to promote investment in designated inner cities. The core objectives of the allowance are to address dereliction and dilapidation in South Africa's largest cities and to encourage urban renewal and development within these cities. This is achieved by promoting investment by the private sector in the construction or improvement of commercial and residential buildings, including low-cost housing units situated within demarcated UDZs. The allowance is also intended to encourage investment in highly populated areas, central business districts or inner-city environments and areas with existing urban transport infrastructure for trains, buses or taxis. Currently, 15 cities in South Africa have one or more demarcated UDZs within its boundaries making up a total of 16 UDZs.

The allowance, when deducted, reduces the taxable income of a taxpayer and is not limited to the taxable income of a taxpayer. It can therefore create an assessed loss. The allowance is available for buildings brought into use on or before 31 March 2030.

11.2. Tax Exemption Guide for Recreational Clubs (Issue 5)

This guide provides general guidance on the:

- approval by SARS of aa recreational club under section 30A; and
- partial taxation of approved recreational clubs under section 10(1)(cO) of the Income Tax Act

The underlying principle in establishing a recreational club is that members provide money by way of membership fees or subscriptions that in turn are used by the club to finance amenities or facilities for their collective enjoyment. Members therefore contribute to share the cost of providing a collective benefit, namely, the social or recreational amenity or facility. Essentially no business or trade is carried on and there is no personal financial gain for the individual members. Under this principle, the sharing of expenses by various members joining based on mutuality does not generate additional taxable income for a recreational club.

A recreational club will enjoy preferential tax treatment only after it has been granted approval by SARS and continues to comply with the relevant prescribed requirements. These prescribed requirements must continuously be met to retain this status. The qualifying receipts and accruals of an approved recreational club are exempt from income tax under section 10(1)(cO). The receipts and accruals of an approved recreational club derived from any other source are exempt from income tax if they do

not in total exceed the greater of the amounts contemplated in the basic exemption. In addition to being partially exempt from income tax on qualifying receipts and accruals, eligible clubs may also enjoy the benefit of being exempt from certain other taxes and duties. These tax benefits are designed to assist recreational clubs by augmenting their financial resources and providing them with an enabling environment in which to achieve their object.

Recreational clubs fall outside the scope and tax rules for PBOs. The main difference between a recreational club and a PBO is that a PBO operates for the benefit of the general public at large, while a recreational club operates for the benefit of its members. A PBO predominantly relies on donations, grants, or bequests to fund its objects, while a club receives its income from its members who contribute by way of membership fees or subscriptions.

Bona fide donations made to recreational clubs are not tax-deductible under section 18A(1). A recreational club may therefore not issue section 18A receipts to donor taxpayers. Donor taxpayers to whom such invalid section 18A receipts have been issued may therefore not claim a deduction under section 18A(1) in determining their taxable income.

12. 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.