TAX UPDATE **PREPARED BY: JOHAN KOTZE**

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1. INTRODUCTION

The purpose of this update is to summarise the tax developments that occurred during the first quarter of 2013 (i.e. 1 January 2013 to 31 March 2013), specifically in relation to Income Tax and Value-Added Tax (VAT). Johan Kotze, Bowman Gilfillan's Head of Tax Dispute Resolution, has compiled this summary.

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

First quarters are always dominated by the Finance Minister's Budget speech. What will be interesting is how the Minister's proposals are eventually enacted, and indeed if they are eventually enacted. It certainly happens that certain proposals take many years before they are enacted and some others are never enacted.

Important aspects are the retirement fund development and the proposed dispute rules.

The case of Bosch v C:SARS are quire interesting with regard to Davis' J and Waglay's J difference of opinion as to the application of NWK.

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

Enjoy reading on!

2. NATIONAL BUDGET

2.1 Main tax proposals

The main tax proposals for 2013 include:

- Personal income tax relief of R7 billion
- Reforms to the tax treatment of contributions to retirement savings
- An employment tax incentive targeted to support young workers and those employed in special economic zones
- Tax relief for small businesses
- Requiring foreign businesses selling digital goods in South Africa to register as VAT vendors
- Increases in fuel and excise taxes
- Alignment of the proposed carbon tax, energy-efficiency savings tax incentive and the electricity levy.

Over the next year, a tax review will assess whether present tax policy is appropriate to support government's objectives of inclusive growth, employment, development and fiscal sustainability. As the National Development Plan notes, the best way to generate resources to implement the national vision is to grow the economy more rapidly. It envisages that 'what we contribute in our taxes, we get back through the high quality of our public services'.

2.2 Individual's tax rates

The rates of tax for the 2013 tax year and those proposed for 2014 are set out below.

2013 year of assessment		2013 year of assessment	
Taxable Income	**Rates of tax**	**Taxable Income**	**Rates of tax**
R0 – R160 000	18% of each R1	R0 – R160 000	18% of each R1
R160 001 – R250 000	R28 800 + 25% of the amount above R160 000	R165 601 – R258 750	R29 808 + 25% of the amount above R165 600
R250 001 – R346 000	R51 300 + 30% of the amount above R250 000	R258 751 – R358 110	R53 096 + 30% of the amount above R258 750
R346 001 – R484 000	R80 100 + 35% of the amount above R346 000	R358 111 – R500 940	R82 904 + 35% of the amount above R358 110
R484 001 – R617 000	R128 400 + 38% of the amount above R484 000	R500 941 – R638 600	R132 894 + 38% of the amount above R500 940
R617 001	R178 940 + 40% of the amount above R617 000	R638 601	R185 205 + 40% of the amount above R638 600
Rebates		**Rebates**	
Primary	R11 440	Primary	R12 080
Secondary	R6 390	Secondary	R6 750
Third rebate	R2 130	Third rebate	R2 250

Tax threshold		Tax threshold	
Below age 65	R63 556	Below age 65	R67 111
Age 65 and over	R99 056	Age 65 and over	R104 611
Age 75 and over	R110 889	Age 75 and over	R117 111

2.3 Relief for low-cost employer-provided housing

Some businesses provide their employees with subsidised rental accommodation or home loans. There are also instances where employers build houses for their employees, initially on a rental basis, with the understanding that the house will become the property of the employee over time. Where an employer transfers a house to an employee at a price below market value, a taxable fringe benefit is triggered. The fringe benefit tax is often unaffordable for low-income employees. To contribute to a more stable workforce and adequate housing, government proposes to provide fringe-benefit tax relief for lower-income earners in such cases.

2.4 Medical tax credits

Monthly tax credits for medical scheme contributions will be increased from R230 to R242 for the first two beneficiaries, and from R154 to R162 for each additional beneficiary, with effect from 1 March 2013.

2.5 Employer-provided bursaries to relatives

The rules covering the exemption of fringe benefit taxation for bursaries given to relatives will be reviewed. Government proposes to increase the relevant monetary thresholds. Differential monetary thresholds for bursaries to students attending tertiary institutions and to learners at schools.

2.6 Non-retirement savings

In the 2012 *Budget Review*, tax-preferred savings and investment accounts were proposed as alternatives to the current tax-free interest-income caps, to encourage greater savings. A discussion document was published in

September 2012 and, after consideration of comments received, government intends to proceed with the implementation of tax-preferred savings and investment accounts. All returns accrued within these accounts and any withdrawals would be exempt from tax.

The account would have an initial annual contribution limit of R30 000 and a lifetime limit of R500 000, to be increased regularly in line with inflation. The new accounts will be introduced by April 2015. In the meantime, with effect from 1 March 2013, tax-free interest-income annual thresholds will be increased from R33 000 to R34 500 for individuals 65 years and over, and from R22 800 to R23 800 for individuals below 65 years. These thresholds will not be adjusted for inflation in future years.

2.7 Retirement savings reforms

Individuals' contributions to pension and retirement annuity funds are tax deductible. To promote savings, the deductibility of such contributions, as well as contributions to provident funds and employer contributions that will constitute fringe benefits, will be increased to 27.5% of the greater of remuneration or taxable income (excluding retirement annuity or lump sum income). For equity reasons, an annual cap on deductible contributions of R350 000 will be applied.

Tax treatment of contributions to pension, retirement annuity and provident funds will be harmonised, allowing provident fund members to receive a tax deduction on their own contributions. Vested benefits will be protected: balances in provident funds at the date of implementation, and subsequent growth, will not be required to be annuitised.

It is proposed, however, subject to public consultations, that future contributions made to provident funds after an agreed date be subject to

the same annuitisation requirements applicable to retirement annuity and pension funds. This requirement will not apply to provident fund members older than 55 years at the date of implementation. New employees can still join and contribute to existing provident funds, and new funds can be created subject to the same tax and annuitisation rules. This will reduce the complexity of the retirement system significantly.

Contributions in excess of the annual caps may be rolled over to future years. At retirement, where any non-deductible contributions remain, they will be set off against any lump sum or annuity income before tax is calculated to avoid double taxation.

Specific provisions will need to be made for defined-benefit pension plans and will require further engagement with industry.

2.8 Taxpayers with multiple sources of income

People receiving multiple incomes are often faced with a higher-than expected tax liability on assessment, due to the aggregation of these incomes. These include people with more than one job and widows/widowers on the death of a spouse. Individual employers and pension funds are typically unaware that there are two or more income streams and each calculates pay-as-you-earn (PAYE) as if there is only one. The result is that too little PAYE is deducted. Government will address this issue during 2013/14. Steps under consideration include higher levels of withholding by employers (though confidentiality is a concern); holding employees responsible for PAYE at a higher tax rate to take into account the ‘aggregation effect’; SARS informing affected taxpayers and suggesting preventative measures; and temporary relief in the case of widows and widowers.

2.9 Employment tax incentives

The introduction of a youth employment tax incentive will help young people enter the labour market, gain valuable experience and access career

opportunities. The administratively simple incentive will create a graduated tax incentive at the entry-level wage, falling to zero when earnings reach the personal income tax threshold. Protection provided by existing labour legislation, combined with oversight by the South African Revenue Service and the Department of Labour, will avoid displacement that might arise. A similar tax incentive will be made available to eligible workers of all ages within special economic zones.

2.10 Special economic zones

In certain special economic zones, the Minister of Finance will authorise the following tax incentives, after consultation with the Minister of Trade and Industry:

- A 15% corporate income tax rate for businesses in such areas.
- An employment incentive allowing for a tax deduction for employment of workers earning less than R60 000 per year.
- An accelerated depreciation allowance for buildings in these areas, based on the existing regime for urban development zones, to encourage developers to invest more in industrial premises.

2.11 Small business corporation relief and social-impact firms

Government proposes that the R14 million turnover threshold for small business corporations be increased to R20 million and that the graduated tax structure for such corporations be revised.

The application of the same rate structure to the trading activities of public-benefit organisations (PBOs) will also be explored.

The feasibility of special support for social-impact businesses, which have both profit-making and social objectives, is being explored. Encouraging

investment in such businesses is in line with the policy objectives of small business development, social solidarity and job creation.

2.12 Public-benefit organisations

Donations to PBOs working in the areas of welfare and humanitarian activities, health care, education, conservation, environmental protection, animal welfare, and land and housing are deductible up to 10% of taxable income in the year the donation is made.[1] Donations in excess of this figure cannot be carried forward, which reportedly discourages large donations. Government proposes to allow donations in excess of 10% of taxable income in any given year to be rolled over as allowable deductions in subsequent years. Also under consideration are rules governing the amount of funding that must be distributed where PBOs provide funding to other PBOs.

2.13 Reforms to the biodiversity tax incentive

Government proposes to modify the rules concerning the allowable deductions for setting aside private land as a protected area. The limitation of not allowing a rollover of donations in excess of 10% of taxable income will be scrapped. Where land has been owned for many years, the original cost of the land is generally much lower than its current market value. Presently, the incentive is calculated using the lower of cost or market value of the protected area for 99-year contracts. Government proposes that the value for the purpose of this incentive should be the lower of the municipal or market value. Capital gains will be triggered, but the taxable proportion of these gains will be set off against the deduction allowed over a period. Certain conservation capital and maintenance expenditure will be allowed as deductible tax expenses.

2.14 Medium-term proposal on old age grant

The means test for the existing *old age grant* is complex and costly to administer, generates arbitrary inequities, and creates disincentives for individuals to save for retirement. Government proposes to establish a universal old age grant, phasing out the means test, by 2016. All citizens over a designated age would be eligible for the grant, irrespective of income level. To ensure equity, adjustments to the secondary and tertiary rebates will be made to offset the costs of this change and retain broadly the same progressive tax structure.

2.15 Reforming the taxation of trusts

To curtail tax avoidance associated with trusts, government is proposing several legislative measures during 2013/14. Certain aspects of local and offshore trusts have long been a problem for global tax enforcement due to their flexibility and flow-through nature. Also of concern is the use of trusts to avoid estate duty, which will be reviewed.

The proposals will not apply to trusts established to attend to the legitimate needs of minor children and people with disabilities. The proposals are as follows:

- Discretionary trusts should no longer act as flow-through vehicles. Taxable income and loss (including capital gains and losses) should be fully calculated at trust level with distributions acting as deductible payments to the extent of current taxable income. Beneficiaries will be eligible to receive tax-free distributions, except where they give rise to deductible payments (which will be included as ordinary revenue).
- Trading trusts will similarly be taxable at the entity level, with distributions acting as deductible payments to the extent of current taxable income. Trusts will be viewed as trading trusts if they either conduct a trade or if beneficial ownership interests in these trusts are freely transferable.

- Distributions from offshore foundations will be treated as ordinary revenue. This amendment targets schemes designed to shield income from global taxation.

2.16 Employment share schemes

Some employers offer staff equity schemes as part of their compensation packages. Some of these arrangements are also used as a tool to lower overall tax rates for executives and other high-income earners. Schemes for lower-income taxpayers, however, are sometimes subject to anomalies that may give rise to double taxation. A special dispensation is proposed to ensure uniform tax treatment of these schemes. The way that employers claim deductions will be examined.

2.17 Disability or income protection policies

Disability insurance policies that fall outside the ambit of retirement funds are treated differently, depending on whether they compensate for the loss of future income (deductible for employees when premiums are incurred) or compensate against loss of personal capital, such as the loss of an arm (not deductible). Many policies blur this distinction. Government proposes a more consistent treatment: all non-retirement fund disability and income protection policies will conform to the overall tax paradigm of non-deductible contributions and exempt payouts.

2.18 Restricting debt to prevent base erosion

Although debt financing is a feature of all healthy economies, debt is often used to erode the tax base. Closure of artificial and excessive debt has been on the tax policy agenda for more than two years. To bring this matter to a conclusion, government proposes the following:

- Artificial debt:

Some debt instruments will be re-characterised as shares (along with the underlying yield) if they contain certain features. The main concerns are so-called debt instruments that do not have a realistic possibility of being repaid in 30 years, or debt that is convertible into shares at the request of the issuer. Banks and insurers will be excluded from this re-characterisation.

- Connected person debt:

  Excessive debt issued to connected person creditors is of concern if the creditor is exempt from tax on the interest, because connected persons can often use debt and equity interchangeably without serious economic consequence. Limits will be imposed so that the interest on this form of debt does not exceed 40% of earnings after interest on other debts is taken into account. Excess interest will be allowed to roll over for up to five years.

- Acquisition debt:

  In corporate restructuring, use of acquisition debt against future earnings effectively eliminates taxable profits for years to come (with the debt often renewed via a new acquisition in later years). Interest on excessive debt will be allowed to roll over for up to five years. This system will replace the discretionary system applied to interest on discretionary debt.

2.19 Taxation of long-term insurers (four funds)

Policies representing the risk business of long-term insurers will no longer be taxed in the policyholder funds but in the corporate (shareholder) fund. As a result, significant amounts of policy-selling expenses will be deductible against taxable premium income from risk policies, and no longer against a relatively smaller investment-income tax base. Reserving will be allowed for this risk business on a similar basis as for short-term insurers.

2.20 Unlisted real estate investment trusts

A real estate investment trust (REIT) is a listed company or trust that invests in immovable property, receives income from rental and distributes it to investors. A REIT can deduct such distributions if it resides in South Africa and at least 75% of its gross income is rental income. This regime will be extended to unlisted REITs once they are subject to similar regulation as listed REITs. This form of regulation should initially be extended to wholly owned entities of private and government pension funds, as well as long-term insurers. Property syndication legislation is also proposed to protect investors from Ponzi schemes. REIT tax relief will similarly be extended to cover other real estate entities if they become subject to property syndication regulation.

2.21 Hedge funds

Hedge funds will fall under collective investment scheme legislation and will be regulated accordingly. While regulated hedge funds will be treated much the same as other collective investment schemes, unit holders will be required to treat their earnings as ordinary revenue when realised. This should generate the intended tax result without interfering with daily operations. A similar regime will be considered for interest-income funds.

2.22 Uniform cross-border withholding to prevent base erosion

Government proposes that the cross-border withholding regime on interest and royalties be extended to cross-border service fees, subject to treaty relief. To facilitate administration, all three sets of withholding regimes (interest, royalties and cross-border service fees) will become effective from 1 March 2014. Prior changes to interest and royalty withholding will also be deferred until this date.

2.23 Mining taxation review

The mineral and petroleum royalty regime has broadened the tax base and allowed for increased revenue during periods of high commodity prices, while providing relief to marginal mines when commodity prices and profitability are low. The broader review of the tax system will consider whether this approach is sufficiently robust and assess what the most appropriate mining tax regime is to ensure that South Africa remains a competitive investment destination.

2.24 National health insurance discussion paper

National health insurance will be phased in over a 14-year period (see Chapter 6). This will require additional funding over time. A discussion paper presenting funding options will be released during 2013.

2.25 VAT registration of foreign businesses

VAT is payable where goods and services are consumed. Consequently, exports are zero-rated and imports are subject to VAT. This principle does not lend itself to simple application for imported services or e-commerce. While the consumer bears the burden of VAT, the law requires vendors to register with SARS, collect VAT and pay it to SARS. In the case of imported services or digital supplies, such as e-books or music, no border post or post office can perform the function as collecting agent, as is the case with physical goods. The net result is that the local consumer can buy imported digital goods or services without paying VAT. Government proposes that all foreign businesses supplying e-books, music and other digital goods and services in South Africa be required to register as VAT vendors. This proposal is in line with international trends, such as regulations adopted by the European Union requiring such suppliers to register for VAT in the country where the consumer resides.

2.26 Aggressive tax planning, base erosion and profit shifting

The Group of 20 has recognised the international problems of base erosion and profit shifting. South Africa is participating in the Organisation for Economic Cooperation and Development's work in this area. South Africa has also committed to the development of a BRICS (Brazil, Russia, India, China and South Africa) mechanism to assist in countering abusive tax avoidance, as well as the abuse of tax treaty benefits, incomplete disclosure and fraudulent claims. SARS will continue with efforts to arrest aggressive tax planning, base erosion and profit shifting.

2.27 Streamlining registration and filing for businesses and individuals

A single registration process for multiple tax products will be launched to simplify registration for all businesses. VAT registration will be streamlined to ease the compliance burden while guarding against fraud. A new company income tax form will be introduced that requires fewer fields to be completed by smaller businesses. Individuals with a single source of taxable employment income currently do not have to submit tax returns if their taxable income is below a threshold of R120 000 per year. The threshold is raised to R250 000.

2.28 Tenders and tax compliance

Last year it was announced that the tax clearance system would be strengthened to ensure that non-compliant taxpayers cannot do business with the state. SARS is now testing an automated tax clearance certificate

for implementation later this year. This will enable the real-time tracking of the tax compliance of the person who tendered. SARS is also following up on payments made by the state to tenderers to check whether full tax disclosure was made.

2.29 Small and micro business registration

SARS is working with the Department of Home Affairs and other agencies to register small and micro businesses, including those operated by foreigners.

2.30 Understatement penalties

The penalty provisions will be refined and relief will be provided for bona fide errors.

2.31 Tax policy research projects

In addition to the investigations described above, the National Treasury will undertake the following research during 2013/14:

- Reviewing the VAT treatment of financial services and VAT apportionment within the financial sector.
- Exploring a sustainable framework for financing local government.
- Assessing the effectiveness of various tax incentives.
- Investigating the taxation of alternative transport fuels such as liquefied natural gas and liquefied petroleum gas.
- Reviewing the taxation of various innovative financial instruments.

2.32 Cross-border remuneration and retirement savings

Cross-border salaries and retirement savings give rise to special issues.

- Cross-border services

  South African residents are generally subject to worldwide tax, except for long-term services provided offshore (for example, for at least 183 days or more in any 12 month period). At issue is whether the worldwide tax regime of South African services should be extended (subject to appropriate credits), especially if a South African employer is involved.

- Cross-border pensions

  South African residents working abroad and foreign residents working in South Africa regularly contribute to local and foreign pension funds, which gives 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. The main issue is whether the tax focus should rely solely on the national source of the services provided or the national origin of the pension fund serving as the savings vehicle. Given the complexity of the issues involved, extensive consultation is required. Possible legislative action may occur if consensus is easily achieved (such as neutralising any unintended differences between cross-border lump sum payouts and annuities).

2.33 Share cross-issues

Share cross-issues have longstanding anti-avoidance rules. These rules prevent taxpayers from obtaining any tax cost when issuing shares for the cross-issue of other shares, because the cross-issue does not trigger tax for any party (justifying a rollover result at zero tax cost). Unfortunately, these rules are impractical in South Africa, because cross-issues are a common feature of many commercially driven share schemes (especially involving black economic empowerment). In addition, cross-issues can also be used to migrate offshore without incurring an exit charge. To mitigate

these problems, the anti-avoidance cross-issue rules will be completely reworked. The zero base cost rule will either be eliminated or narrowed. Cross-issues (and share-for-share transactions) acting as a mechanism to indirectly shift value into tax-exempt hands will trigger immediate taxation.

2.34 Banks and brokers

In 2012, mark-to-market taxation was legislatively added to income tax, but the effective date was deferred until 2014. This legislation will be refined based on further consultations. The main refinements are as follows:

- Covered persons will be extended to include most of the companies in regulated banking groups to reduce the potential for mismatches between the new mark-to-market system and the historic system
- Rules to prevent artificial losses from dividend transactions.
- Assets and liabilities will be disregarded to the extent that they are not recognised under relevant international financial reporting standards (IFRS).
- Different treatment of impairment of financial assets for accounting and bad and doubtful debt for tax purposes are under consideration.

2.35 Revised treatment of captive insurers

In 2012, a new set of rules were proposed that deny deductions for payments of insurance premiums to short-term insurers if the overall arrangement lacks any significant risk transfer. Risk transfer was measured from an IFRS perspective as opposed to a legal perspective. While these rules were conceptually correct, the focus of the risk transfer should have been on the policyholder, not the insurer. In addition, concerns continue to exist that dividends from captive insurers most likely represent the recoupment of previous reserved amounts as opposed to dividends from underlying taxable profits. The anti-avoidance rules in this area will be revised accordingly. These anti-avoidance rules will also be extended to

long-term insurer policyholders that pay premiums to reinsurers in respect of reinsurance that similarly lacks a significant element of risk transfer.

2.36 Financial intermediaries and securities transfer tax

Unlike the London Stock Exchange, only brokers can be members of the JSE and receive exemption from the securities transfer tax (STT). Other financial intermediaries, such as banks, do not receive compar.ble relief. This lack of relief for financial intermediaries inadvertently disrupts intermediary transactions where profits are small, because the STT potentially eliminates (or even exceeds) all intermediary profits. It is accordingly proposed that certain intermediaries be exempt from the STT so that transacting on the JSE remains internationally competitive.

2.37 Streamlining the oil and gas incentive

Oil and gas tax incentives were finalised in 2006 as part of the overall changes associated with the Mineral and Petroleum Resources Development Act (2002). With regulatory approvals now fully under way, a series of minor issues have emerged that could be streamlined for easier enforcement and compliance. In addition, certain anomalies have emerged that have left new entrants in a worse position than previous stakeholders. These anomalies will be removed and a uniform system of fiscal stability agreements will be developed.

2.38 Tenant improvements to landlord land

Many sophisticated commercial tenants undertake substantial improvements (or wholesale construction) on the fixed property of a landlord, especially in the case of long-term leases. However, none of these improvements are depreciable because depreciation is generally allowed

only on ‘owned’ property, and tenant improvements are not technically owned by the tenant. This lack of depreciation is complicating many commercial arrangements. It is proposed that the ownership test for depreciation be replaced with ‘possession and use’. Associated amendments to the taxation of the lessor and treatment of leasehold improvements will be effected.

2.39 Ancillary aspects to pipelines

As pipelines are depreciable, ancillary equipment such as electrical wiring and certain related components will be depreciable to the same extent as the underlying pipelines.

2.40 Clarification of trading stock cost calculations

The cost price of trading stock is currently calculated in line with generally accepted accounting practices, approved by the South African Revenue Service (SARS). Given recent changes to IFRS, it is proposed that the cost price of trading stock automatically comport to IFRS without the need for SARS approval.

2.41 Closure of unintended claims for the research and development incentive

Although the research and development incentive was recently adjusted, information has come to light that it is still being misused. The incentive aims to facilitate South Africa’s establishment as an innovation hub by global standards. It is not intended to assist in routine upgrades or standard adjustments to match global competition. The criteria for eligibility will be adjusted to ensure that the incentive is available only in support of the initial policy intention.

2.42 Mining dewatering association

Although the tax system contains an exemption for mining rehabilitation entities, a compar.ble exemption does not exist for a mining dewatering association, which restores water levels adversely impacted by mining. This association is funded by several mining houses in a manner similar to a mining rehabilitation fund. The exemption of this association is under consideration.

2.43 Incentives for the construction of affordable housing

A tax incentive is under consideration for developers (and employers) to build new housing stock (at least five units in compliance with prescribed standards) for sale below R300 000 per dwelling. This incentive would address challenges faced by households in the 'gap market'. An exclusion of R60 000 per qualifying house sold is proposed.

2.44 Deferral of expenditure incurred by certain connected persons

The tax system triggers income upon receipt or accrual, as well as deductible expenditure based on payment or incurral. While this system is largely appropriate, taxpayers have an incentive to accelerate deductions on incurred expenditure if a connected counterparty lacks immediate (or deferred) corresponding income. This situation often arises in the case of a South African subsidiary when expenditure is incurred in relation to a foreign parent company. To limit potential abuse, deductions will be deferred until payment.

2.45 Further easing of cross-border anomalies

Over the past several years, a number of amendments have been undertaken to eliminate double taxation in the case of South African investment into offshore active operations. While most of the issues have been resolved, certain concerns remain, such as complexities associated with the calculation of the acceptably taxed exemption, the threshold for the participation exemption and transfer pricing requirements in management activities for the benefit of foreign branches. Headquarter company relief also needs to be refined to ensure it is more effective and easier to understand. These anomalies will be removed.

2.46 Gateway subsidiary

It is not uncommon for South African multinationals to use an offshore subsidiary as a treasury operation. Unlike local treasuries, offshore treasuries can freely move currency without regulatory approvals, creating an incentive to move offshore. To eliminate this incentive, listed South African multinationals will be allowed to treat a single local subsidiary as a non-resident company for Reserve Bank purposes, so treasury operations can remain within South Africa. In addition, these entities can use their foreign functional currency, rather than the rand, as the starting point for tax calculations.

2.47 Controlled foreign company activities

Imputation for controlled foreign companies should theoretically apply only in the case of passive income and certain forms of income likely to lead to transfer pricing avoidance (known as diversionary income). Although the current rules achieve this result in most cases, certain anomalies have arisen over the years that require clarification. In particular, active offshore research and development activities appear to be inadvertently falling within

the net, as well as international shipping activities, international pipelines and commodity hedges associated with active operations. It is also a concern that intracontrolled foreign companies' insurance premiums are not receiving the same relief as their other payments. These anomalies will be removed.

2.48 Removal of source focus for initial copyright authors

Under current law, the initial author of a copyright is exempt from tax on a foreign source of income if that source is subject to foreign tax. This relief was initially enacted in line with source principles many years ago. With the shift to worldwide taxation in 2001, this relief no longer makes sense and should be removed.

2.49 Streamlining currency taxation

The current tax calculation of currency gains and losses is extremely complex and not wholly in sync with accounting principles. The currency taxation rules are being simplified in favour of a more practical approach. Changes in this area will continue along these lines, especially in regard to the capital gains tax and basic measurement methods (for example, spot versus weighted average). A longer-term shift is being considered towards an IFRS approach that simplifies the tax system without compromising enforcement.

2.50 VAT - Motor cars

The current definition of 'motor car' in the VAT Act excludes, among others, a vehicle capable of accommodating only one person. A racing car or cart that is acquired by a vendor partly for recreational use and partly for business use (for example, advertising purposes) falls into this exclusion.

As a result, the purchase of these vehicles could qualify for a deduction of input tax, even though these cars are often used for recreational (or even normal commuting) purposes. There are no policy reasons to treat these vehicles differently from that of a normal passenger vehicle and the law will be changed accordingly.

2.51 VAT - Repossession of goods

A vendor (debtor) makes a deemed supply of goods under an instalment credit agreement to the creditor if the creditor (at their discretion) repossesses those goods. With the introduction of the National Credit Act (2005), a debtor (at the debtor's discretion) may similarly surrender goods supplied under an instalment credit agreement. For VAT purposes, the rules should be the same regardless of whether the creditor or the debtor is exercising the discretion to surrender the goods.

2.52 VAT - Future supplies of services

A special time-of-supply rule exists for goods supplied under an agreement (excluding rental or instalment credit agreements). When the recipient takes possession of those goods and consideration for that supply cannot be determined upfront, the supply is deferred until the earlier of the dates when payments are due or received, or when an invoice is issued. A similar rule for services will be added when the consideration for that service cannot be determined upfront due to a contingent future event (for example, share price and exchange rate).

2.53 VAT - In-flight entertainment

Input tax deductions on entertainment expenditure are disallowed. However, this general prohibition does not apply in several circumstances where business objectives dominate. In-flight entertainment (movies and video games) is currently disallowed even though it is ancillary to the flight.

This in-flight entertainment should accordingly not be part of the prohibition (like the meals and refreshments, which are not disallowed).

2.54 VAT - Supplies between connected persons

Special time-of-supply rules apply to transactions between connected persons. The purpose of these rules is to prevent artificial deferrals. However, no apparent reason exists for this rule to apply if the transaction gives rise to an input for the purchaser that is simultaneous with the output for the seller. Relief in this area is accordingly proposed.

2.55 VAT - Tax invoices issued in foreign currency

Under current law, a valid tax invoice must be stated in rands. However, the VAT Act does not prescribe how to deal with a scenario in which the transaction is conducted in foreign currency. This will be addressed by converting foreign currency invoices to rands at the spot rate agreed upon by the parties. In the absence of an agreement, the spot rate on the date of supply will be used.

2.56 VAT - Temporary letting of residential fixed property

Developers that use the temporary relief provisions for the letting of residential fixed property are required to furnish SARS with a declaration containing certain information within 30 days of the supply. It would be more practical and appropriate if the vendors retained the information as part of their normal recordkeeping (without being required to file a declaration with SARS).

2.57 VAT - Conversion from a share block scheme to a sectional title

The conversion of a share block company to a sectional title is considered a 'non-supply' for VAT purposes (from an output tax point of view, no VAT is levied on the supply). From an input tax point of view, there is some debate on whether the shareholder is entitled to a notional input tax deduction on acquisition of the unit supplied by the share block company. This mismatch will be removed.

2.58 VAT - Home-owners association

The supply of services by a sectional title association to its members in the course of the management of the sectional title body corporate is generally exempt from VAT. However, a home-owners association lacks a similar exemption (due to previous differences in how municipalities billed sectional title body corporates versus home-owner associations). It is proposed that this unequal treatment be removed.

2.59 VAT - The right of use of fixed property

The supply of a share by a share block company falls within the definition of 'fixed property' in the VAT Act and is consequently subject to VAT at the standard rate (because a share block unit is roughly equivalent to a direct interest in property). However, a cooperative that supplies membership units falls outside the VAT Act. Property cooperatives will accordingly be treated like share block companies.

2.60 Indirect exports

The export incentive scheme will be replaced by new export regulations. Legislative amendments will be required to ensure alignment.

2.61 VAT - Imported goods – damaged or destroyed

Goods imported into South Africa are levied with VAT at the rate of 14% when those goods are entered for home consumption. In terms of the Customs and Excise Act, imported goods that are destroyed, damaged or abandoned are considered to have been entered for home consumption (with a rebate of the customs duty becoming applicable). The VAT Act does not have a similar relief mechanism for goods damaged, destroyed or abandoned, which means that when those goods are entered for home consumption, VAT applies. It is proposed that compar.ble VAT relief be provided for goods that are destroyed, damaged or abandoned.

2.62 VAT - Pooling arrangements

Pooling arrangements are mainly applicable to the agricultural and rental markets to simplify VAT administration. To address the complexities that may emanate from the 'pool' being treated as separate from its members, it is proposed that a VAT review of all pooling arrangements be undertaken, resulting in possible legislation in 2014.

2.63 VAT - Square Kilometre Array

The Square Kilometre Array, an international collaboration to build the world's largest radio telescope, is eligible for income-tax exemption under existing public-benefit provisions. VAT relief will be provided through a refund mechanism or the zero-rating of consideration received by the project and for imported goods and services.

2.64 Mineral and petroleum royalties

The Mineral and Petroleum Resources Royalty Act (2008), which has been in operation for three years, needs to be refined. Areas of ongoing concern

include the appropriate specified condition of mineral extraction acting as a reference point to calculate the mineral royalty tax base, interaction of the royalty regime rate with the income tax calculation and information reporting requirements. Concerns also exist that small business relief needs to be more administratively accessible. All of these concerns will be addressed.

2.65 Gambling tax

A national gambling tax was proposed in 2011. The tax will apply at a rate of 1% of gross gambling revenue in addition to provincial rates. This legislation will be implemented by the close of 2013.

2.66 Research projects - Company restructurings

In 2012, the National Treasury (in consultation with SARS) began a series of workshops to review the tax rules relating to domestic and foreign reorganisations so that these rules can be streamlined (while continuing to safeguard against undue tax avoidance). These engagements will continue in 2013, with legislative focus on urgent matters and anomalies.

2.67 Research projects - Dividend cessions and manufactured dividends

The tax impact of a dividend transfer depends on whether the transfer is a cession or a dividend compensation payment (even though the economic impact is largely the same). In the case of a cession, the dividend generally retains its tax nature. In the case of a dividend compensation payment, the payment is largely deductible by the payor and largely includible by the payee. Both sets of rules continually give rise to tax avoidance or mismatches that reduce the ultimate tax due before the economic profit. Under consideration is a single unified treatment for both forms of transfers

and certain anti-avoidance rules to eliminate the shifting of income from taxable parties to exempt parties.

2.68 Research projects - Relief for international shipping

In 2006, the possibility of a tonnage tax for international shipping was mooted (as a substitute for the 28% income tax on companies). Upon review and extensive consultation with the industry, relief in the form of an outright exemption for shipping income appears to be the most viable option to attract international shipping, given recent trends. However, for any tax incentive to be viable, compar.ble relief mechanisms will be required. The National Treasury will continue to engage with other national departments to ensure that any tax incentive proposed is part of a regulatory package.

2.69 Research projects - Debt relief

The payback provisions within the VAT Act seek to claw-back input tax claimed on supplies received by a vendor if the vendor has not discharged the debt for that supply within a period of 12 months. This claw-back is often onerous when debts are relieved to help the debtor avoid potential or actual insolvency. Debt relief to assist distressed debtors (such as business rescue) is under consideration. The question is whether the need for this relief can be balanced against potential misuse (deliberate input deductions without any subsequent output).

2.70 Research projects - Apportionment – non-financial sectors

The default apportionment method, which is based on turnover, appears to be inequitable at times because there may not be a direct correlation

between expenditure incurred versus turnover generated. It is proposed that the default application of this method be re-evaluated.

2.71 Research projects - Collateral for share lending

The pension fund rules were recently amended to tighten the margin required if a borrower pledges a non-cash margin as security to a pension fund that undertakes a share lending transaction. This heightened level of security triggers income tax and the STT. Given these adverse tax consequences, the new pension margin requirements will be postponed so that they can be properly coordinated with the related tax rules.

3. RETIREMENT REFORM PROPOSAL FOR FURTHER CONSULTATION

Executive summary

It is becoming ever clearer that employers which take greater responsibility for the overall financial well-being of their workers, including through the design of their retirement funds, reap the rewards of a more stable and happier work force.

The overall approach of these policy proposals is therefore to alter the defaults implicit in retirement fund design, where appropriate, to nudge, rather than force, individuals into making decisions which serve their long-run interests.

3.1 Taxation of retirement funds

- From an effective date, on or after 2015, called T-day, employer contributions to retirement funds will become a fringe benefit in the hands of employees for tax purposes. Individuals will be able to receive a tax deduction on employer and employee contributions to a pension fund, provident fund or retirement annuity fund up to 27.5% of the greater of remuneration and taxable income. A ceiling of R350

000 will apply. This proposal is described in more detail in Chapter 4 of the Budget Review.

3.2 Governance

- The duties of trustees to act independently, and free from conflicts of interest, will be strengthened by elevating PF Circular 130, which deals with the governance of retirement funds, to a Directive. A draft will be published for consultation later this year.
- The FSB is to monitor trustee appointments, including ensuring that trustees meet 'fit and proper' requirements.
- The current Trustee Toolkit may be elevated into a basic, independent, compulsory and free training kit for Trustees.
- The Financial Services Laws General Amendment Bill, 2012, which contains various provisions pertaining to governance, is currently in Parliament.
- The Minister is to convene a trustee conference, with a view to further strengthening the governance of retirement funds.

3.3 Preservation

- Full vested rights with respect to withdrawals from retirement funds will be protected. Amounts in retirement accounts at the date of implementation of the legislation, called P-day, and growth on these, can be taken in cash, but from a preservation fund, and subject to taxation as currently.
- After P-day, all retirement funds will be required to identify a preservation fund and transfer members' balances into that fund, or another preservation fund, when members withdraw from the fund before retirement.

- Existing rules on preservation funds will be relaxed to allow one withdrawal per year, but the amount of each withdrawal will be limited. Unused withdrawals in any year may be carried forward to future years. Withdrawal limits will account for vested rights as described above.
- Payments resulting from divorces will also need to be paid into preservation funds rather than being paid in cash.

3.4 Annuitisation

- The annuitisation requirements of provident funds and pension funds will be harmonised. However, the new annuitisation rules will only apply to new contributions made to provident funds after P-day, and growth on these contributions. Existing balances in provident funds, and growth on these, will not be subject to annuitisation.
- In addition, members of provident funds who are older than 55 on the date of implementation will not be required to annuitise any of their balance at retirement, provided they remain in the same provident fund until they retire.
- To lessen the impact on provident fund members, the means test for the old age grant will be phased out by 2016, and the *de minimis* requirement for annuitisation will be raised from R75 000 to R150 000.
- Trustees will be required to guide members through the retirement process, to identify a default retirement product in accordance with a prescribed set of principles, and to automatically shift members into that product when they retire, unless members request otherwise. The fund itself may provide the default product, or it may use an externally-provided product.
- Living annuities will be eligible for selection as the default product, provided certain design tests, including on charges, defaults, investment choice and drawdown rates, are met.

- Trustees that make commission-free financial advice available to members on retirement, paid for out of the fund on a salaried basis, will be given some legal protections in respect of the choice of the default. To increase competition, providers other than registered life offices will be allowed to sell living annuities.

3.5 Non-retirement savings

- Government intends to proceed with the implementation of tax-preferred savings and investment accounts. All returns accrued within these accounts and any withdrawals would be exempt from tax. The account would have an initial annual contribution limit of R30 000 and a lifetime limit of R500 000, to be increased regularly in line with inflation. The new accounts will be introduced by 2015, and will co-exist with the current tax-free interest income dispensation.
- With effect from 1 March 2013, tax-free interest-income annual thresholds will be increased from R33 000 to R34 500 for individuals 65 years and over, and from R22 800 to R23 800 for individuals below 65 years. These thresholds may not be adjusted for inflation in future years.

3.6 Broader reforms

- In addition to the proposals described above, Government is exploring ways to increase retirement fund coverage to all workers. This is a complex issue, given the large proportion of uncovered workers who earn below the tax threshold, who work for small employers, or who have a tenuous connection to the formal labour force, for instance because they work in construction or domestic service.
- A process is currently underway to bring public pension funds currently not governed under the Pension Funds Act, including the

Government Employees Pension Fund (GEPF), Transnet, Telkom and Post Office retirement funds, into the purview of the Act.

- Any biases in retirement funds which may discourage individuals from working past the retirement age of their funds will be identified and removed.

4. REGULATIONS / NOTICES

4.1 Notice in terms of section 13quat(8) of area demarcated by City of Cape Town as UDZ

Particulars of the area which has been demarcated as an urban development zone by the City of Cape Town as set out in the Annexure thereto, the municipality having proved that the area so demarcated complies with section 13quat(6) of the Income Tax Act.

4.2 Determination the daily amount in respect of meals and incidental costs for purposes of section 8(1)

With effect from 1 March 2013 the following amounts will be deemed to have been actually expended by a recipient to whom an allowance or advance has been granted or paid:

- where the accommodation, to which that allowance or advance relates, is in the Republic and that allowance or advance is paid or granted to defray:
  - incidental costs only, an amount equal to R98,00 per day; or
  - the cost of meals and incidental costs, an amount equal to R319,00 per day; or

- where the accommodation, to which that allowance or advance relates, is outside the Republic and that allowance or advance is paid or granted to defray the cost of meals and incidental costs, an amount per day will be allowed depending on the country in which the accommodation was located, for instance :

  Australia – Austrialian$208

  Brazil – US$382

  China – Renmindi 939

  Etc.

4.3 New fees for binding rulings and binding class rulings

New fees for Binding Private Rulings and Binding Class Rulings

In terms of section 81(1) of the Tax Administration Act, 2011, SARS for the South African Revenue Service, may determine application and cost recovery fees for binding private rulings and binding class rulings issued under the advance tax ruling system. These fees are set out below:

Application fees:

Applicant	Application fee
Small, medium and micro enterprises (SMME)	R2 500
Any other taxpayer	R14 000

Cost recovery fees:

Cost recovery fees will be charged at R650 per hour for all non-urgent applications. A fee of R1 000 per hour will be charged for all urgent applications.

Category	Estimated fee range	Estimation deposit (20% of higher amount)	Hourly rate
Standard	R10 000 to R35 000	R7 000	R650
Involved	R35 000 to R70 000	R14 000	R650
Complex	R70 000 to R105 000	R21 000	R650
Extraordinary	Case-by-case	Case-by-case	R650
Urgent applications	Case-by-case	Case-by-case	R1 000

In addition to the above, any direct costs incurred in connection with an application will be recovered. These will however be subject to prior written approval being obtained from the applicant.

5. DISPUTE RULES

The Minister of Finance is proposing a new set of rules to govern the procedures to lodge an objection and appeal against an assessment or decision subject to objection and appeal referred to in section 104(2) of the Tax Administration Act, the procedures for alternative dispute resolution and the conduct and hearing of appeals before a Tax Board or Tax Court.

The following draft rules are worth highlighting:

5.1 Rule 4. Extension of time periods

(1) Except where the extension of a period is otherwise regulated in these rules, a period prescribed under these rules may be extended by agreement between—

(a) the parties;

(b) a party or the parties and the clerk; or

(c) a party or the parties and the registrar.

(2) A party who requires an extension of a period may apply to the tax court under Part F for an order under rule 52(2), if the other party does not agree to a request for an extension of a period.

(3) An application under sub rule (2) must be brought within 20 days after delivery of the notice by the other party of not agreeing to a request for an extension or, in any other case, before the expiry of the prescribed period.

(4) If a period is extended under this rule, the period within which a further step of the proceedings under these rules must be taken commences on the day that —

(a) the extended period ends; or

(b) an agreement under sub rule (1) or an order under sub rule (2) is varied by agreement between the parties.

5.2 Rule 12. Test cases

(1) A senior SARS official must upon designating an objection or appeal as a test case or staying a similar objection or appeal by reason of a designation under section 106(6) of the Act, inform the taxpayers or appellants accordingly by notice before—

(a) the objection is decided under rule 9;

(b) if the appeal is to be dealt with by the tax board, a decision by the chairperson of the tax board is given under section 114 of the Act; or

(c) if the appeal is to be dealt with by the tax court, the appeal is heard by the tax court.

(2) The taxpayers or appellants may within 30 days of the delivery of the notice under sub rule (1), deliver a notice—

(a) opposing the decision that an objection or appeal is designated as a test case;

(b) opposing the decision stayed pending the final determination of a test case on a similar objection or appeal before the tax court; or

(c) if the objection or appeal is to be stayed, requesting a right of participation in the test case,

which notice must set out the grounds of opposition or for participation, as the case may be.

(3) If no notice under sub rule (2) is received by SARS, the designation of the test case or suspension of the objection or appeal by reason of the designation is regarded as final.

(4) Within 30 days after receipt of the notice under sub rule (2) a senior SARS official may—

(a) withdraw the decision to select the objection or appeal as test case or to stay the objection or appeal pending the outcome of a test case;

(b) agree that a taxpayer or appellant requesting participation may do so; or

(c) apply to the tax court under Part F for an order under rule 51(2) that the—

(i) objection or appeal be selected as test case;

(ii) objection or appeal stayed pending the determination of the test case; or

(iii) taxpayer or appellant requesting participation should not be allowed to do so.

(5) The stay of an objection or appeal terminates on the date of the—

(a) expiry of the 30 day period prescribed under sub rule (4), if a taxpayer or appellant has delivered a notice under sub rule (2) and the senior SARS official has not within the period withdrawn the decision under sub rule (4)*(a)* or made an application under sub rule (4)*(c)*;

(b) delivery of the notice by the official that the decision has been withdrawn under sub rule (4)*(a)*;

(c) agreement between the taxpayer or appellant and the official that the stay of the objection or appeal is terminated; or

(d) expiry of 15 days following the day on which the tax court, or higher court dealing with an appeal against the judgment of the tax court,

(i) dismisses an application by the official under subsection (4)*(c)*; or

(ii) makes a decision in the test case designated under section 106(6)*(a)* of the Act.

(6) For the period during which an objection or appeal is stayed under section 106(6)*(b)* of the Act—

(a) a period prescribed under these rules (other than under this rule) in relation to the objection or appeal, does not apply; and

(b) if the staying of an objection or appeal terminates, a period prescribed under these rules is treated as if the period was extended by the same period that the suspension of the objection or appeal was suspended.

(7) Proceedings in an objection or appeal under these rules which have been instituted but not determined by the tax board, tax court or any other court of law are stayed with effect from the delivery of the notice under sub rule (1) until the stay of an objection or appeal is terminated under sub rule (5).

(8) A test case designated under section 106(6) of the Act must be heard by the tax court.

(9) For purposes of a cost order by the tax court, or higher court dealing with an appeal against the judgment of the tax court, in a test case designated under section 106(6) of the Act, the appellants in the test case include:

(a) the appellant whose appeal was selected as the test case; and

(b) an appellant who participated in the test case.

(10) In the event that a tax court under section 130 of the Act or a higher court dealing with an appeal against the judgment of the tax court in the test case awards costs and—

(a) SARS is substantially successful in a test case, the appellants in the test case will each be responsible for their own legal costs and for the legal costs of SARS on the proportionate basis as may be determined by the tax court; or

(b) the appellants are substantially successful in a test case, SARS will be liable for the legal costs of the appellants.

5.3 Rule 31. Statement of grounds of appeal

(1) The appellant must deliver a statement of the grounds of appeal to SARS within 45 days after—

(a) the date of an agreement under rule 23 or settlement under rule 24 in terms of which the parties agreed on the unresolved issues that the appellant may continue on appeal to the tax court;

(b) the date of termination of alternative dispute resolution proceedings under rule 25;

(c) if the matter was decided by the tax board, the delivery of the notice by a party of the *de novo* referral of the appeal to the tax court under rule 29; or

(d) in any other case, the date of delivery of the notice of appeal by the appellant under rule 10.

(2) The statement must be divided into paragraphs—

(a) setting out a clear and concise statement of the grounds upon which the appellant appeals;

(b) stating the material facts and the legal grounds upon which the appellant relies for such appeal; and

(c) stating which of the facts and legal grounds in the grounds of assessment and the disallowance of the objection are disputed.

5.4 Rule 32. Statement of grounds of opposing appeal

(1) SARS must, within 45 days after receipt of the statement of the grounds of appeal, deliver to the appellant a statement of the grounds of opposing the appeal.

(2) The statement of the grounds of opposing the appeal must be divided into paragraphs—

(a) setting out a clear and concise statement of the grounds upon which the appellant's appeal is opposed;

(b) stating the material facts and legal grounds upon which SARS relies; and

(c) stating which of the facts and legal grounds alleged in the statement of the grounds of appeal under rule 31 are admitted and which of those facts and legal grounds are denied.

5.5 Rule 33. Reply to statement of grounds of opposing appeal

(1) The appellant may deliver a reply to the statement of grounds of opposing the appeal under rule 32 within 20 days after receipt of the statement of grounds of opposing the appeal.

(2) The reply to the grounds of opposing the appeal must be divided into paragraphs setting out a clear and concise reply to new statements or allegations that may be contained in the statement of the grounds of opposing the appeal.

5.6 Rule 34. Issues in appeal

The issues in an appeal to the tax court will be those contained in the statement of the grounds of appeal read with the statement of the grounds of opposing the appeal and, if any, the reply to the grounds of opposing the appeal.

6. TAX CASES

6.1 Bosch and another v C:SARS

Bosch, together with other employees and ex-employees of the Foschini Group of Companies, had been participants in the Foschini 1997 Share Option Scheme ('1997 Scheme').

In 1990 the Foschini Group of companies had decided to introduce an Employee Share Incentive Scheme which, because of certain unsatisfactory features, led to the approval of a new scheme on 10 December 1997.

The justification for the 1997 Scheme was that a share incentive scheme was necessary to motivate and maintain 'the focus and commitment of the senior management team' and it was classified as a deferred delivery scheme that was structured around certain fundamental requirements. There had to be an exercise of the right of acquisition in respect of the shares and the agreements, which were entered into between the parties, had to be unconditional.

The tax advantage of the 1997 scheme, as Foschini understood it, was that the employees would gain an advantage provided that he or she exercise the option within a relatively short period after it was granted, so that the taxable amount in terms of section 8A would be relatively small, particularly as any gain made between the date of exercise and the date at which the shares were delivered would not be subject to income tax although it could constitute a capital gain. The advantage to the employer was that in order

to arrive at the same benefit, it could grant less options and issue less shares.

In terms of the scheme the object was to give employees an incentive to promote the continued growth of the company by giving them the opportunity to acquire shares in the company. The scheme provided for the granting of options by the Foschini Group, which had to be exercised in writing within 21 days of the relevant notice date. Shares, which were the subject of the option that had been exercised, were referred to as sale shares. Shares, which had been delivered after the implementation date, were referred to as scheme shares. A participant was not required to pay consideration immediately upon the exercise of the option but only against delivery to the participant of the scheme shares. A participant was entitled to delivery of the scheme shares in three equal tranches, being on the second, fourth and sixth anniversaries of the relevant notice date against payment of the portion of the consideration attributable thereto. Each of the second, fourth and sixth anniversaries of the relevant notice date were referred to as an implementation date. Prior to the delivery of the shares in the three equal tranches, a participant was not entitled in any way to alienate, transfer, cede, pledge or encumber his or her rights in terms of the scheme, including the right to delivery of the shares in question. The risks and benefits of the shares did not pass to the participant and a participant was not entitled to participate in any cash dividends declared in respect of the shares and the participant was not entitled to exercise or dispose of any voting rights in respect of the shares.

After the establishment of the Foschini Share Incentive Trust on 27 July 1999 the Foschini Group assigned its rights and obligations in terms of the scheme to the trustees of the trust.

Initially, the Foschini Group, and later the trust, acting in terms of the provisions of the scheme, granted options to certain employees to acquire scheme shares at stipulated prices, being either the middle market price of the scheme shares on the relevant notice date or such price, less a discount of up to 10%. The notice days, which were initially granted by the Foschini Group to first and second appellants and which are relevant to this

appeal, were 14 August 1998 and 2 December 1998. The notice dates in respect of options which were granted by the trust and which are relevant to the first appellant's appeals were 19 March 2001 and 1 April 2003. All of the options were exercised by the appellants.

SARS had in 2008 raised additional assessments against the Appellants, together with some 115 other employees and ex-employees of the Foschini Group of companies, who were participants in the 1997 scheme and sought to tax these participants in terms of section 8A of the Income Tax Act in respect of various years of assessment. The additional assessments were raised upon the difference between the cost of the shares of each of the Appellants on the dates when each of them exercised options under the scheme ('the strike price') and the market value of these shares on the second, fourth and sixth anniversaries of the dates of the granting of the options and these were the dates, set out in terms of the scheme, whereby the shares would be delivered to Appellants in equal tranches against payment.

SARS' amended statement of the grounds of assessment in respect of the first Appellant and the statement of the grounds of assessment in respect of second Appellant, SARS had invoked par. 2(*a*) of the Seventh Schedule to the Act as an alternative ground for a liability in respect of shares delivered prior to 26 October 2004. In these statements, which set out the grounds of assessment, SARS also invoked section 8C of the Act as an alternative basis for liability in respect of shares delivered after 26 October 2004 and raised par. 2(*a*) of the Seventh Schedule as a further alternative basis in respect of these shares.

First Appellant was assessed in respect of the 2001, 2003, 2005 and 2006 years of assessment, all of which assessments were adjudicated upon by the court *a quo*.

Second Appellant was assessed in respect of the 2001, 2003, 2004, 2005 and 2006 years of assessment. However, in this case, it was agreed that only the additional assessment issued in respect of 2005 would be adjudicated upon by the court *a quo*. The two appeals were heard together.

The court *a quo* (see *ITC 1856*) decided to set aside the additional assessments in respect of the first Appellant for the 2001 and 2003 years of assessment and upheld the additional assessments in respect of the 2005 and 2006 years of assessment as well as the additional assessment in respect of the second Appellant for the 2005 assessment.

The present appeal against the decision of the court *a quo* was defined so as to canvass only the additional assessments in respect of the first Appellant for the 2005 and 2006 years of assessment, and, regarding the second Appellant, in respect of the 2005 year of assessment.

The court *a quo* held that section 8A of the Act applied to gains made on delivery of the relevant scheme shares when delivery took place prior to 26 October 2004, as taking delivery constituted the exercise of the right to acquire a marketable security for the purposes of section 8A of the Act. The court also held that, as section 8A was applicable, par. 2(*a*) of the Seventh Schedule was thus inapplicable and that section 8C applied to gains made upon delivery of the relevant scheme shares when delivery took place after 26 October 2004 as taking delivery constituted the vesting of equity instruments acquired during the relevant years of assessment as contemplated by the provisions of section 8C of the Act.

In the present appeal the issues were defined as follows:

- In respect of the 2005 additional assessments, insofar as they related to the delivery of the relevant scheme shares before 26 October 2004, the issue was whether the first and second appellants became liable for tax in terms of section 8A of the Act upon delivery of the scheme shares and whether the first and second appellants became liable for tax in terms of par. 2(*a*) of the Seventh Schedule upon delivery of the scheme shares.
- In relation to the 2005 additional assessment, insofar as they are related to delivery of the relevant scheme shares after 26 October 2004 as well as in respect of the 2006 additional assessment, whether the first and second appellants became liable for tax in terms of section 8A on delivery of the scheme shares; whether the first and

second appellants became liable for tax in terms of section 8C and whether they became liable for tax in terms of par. 2(*a*) on delivery of the scheme shares.

Hence the starting point for an analysis by the court in the present case had to be section 8A of the Income Tax Act and it was common cause that, for section 8A to apply, the taxpayer 'must exercise . . . a right to acquire' the relevant shares.

SARS contended that the employee only acquired an unconditional right to delivery of the relevant shares upon the arrival of the defined implementation dates and, if at those dates, the sale had been an unconditional one, that is there would be no termination of the employee's employment prior to the anniversary date, the middle market price of the shares at the anniversary date was higher than the specified consideration, or, if lower, the employee had not made an election.

SARS contended further that, even if the mere exercise of an option, rather than the assertion of a claim for delivery of the shares, fell within the meaning of the phrase 'exercise of a right to acquire' shares and, even if the exercise of an option in these circumstances would be the only possible event which would trigger section 8A, this could only be so if, upon the exercise of the option, the employee had obtained an unconditional right to obtain delivery of the shares on a future date.

Furthermore, the exercise of the short term option of the 1997 scheme did not give rise to any such unconditional right and, accordingly, section 8A was not triggered 'upfront' but only when the claim to the shares became unconditional; that is when, on arrival of the deferred implementation date, the employee, who was still employed, claimed the shares against tender of the payment of the purchase price. Alternatively, section 8A would not be triggered at all and the benefit, which accrued to the employee on the deferred implementation date, was taxable in terms of par. 2(*a*) of the Seventh Schedule to the Act.

SARS further contended that the various agreements were subject to suspensive conditions. In particular, SARS argued that Clause 7.3, which

provided that a participant was not entitled to acquire the shares unless he or she was still employed at the implementation date (save for various restricted reasons), was no more than a suspensive condition. In SARS' view the terms of the resale process in terms of clause 7.3 was unrelated to a general commercial consideration, for, regardless of the current value of the shares at the time that the participant's employment ends, the resell price was identical to the original purchase price and the condition was therefore a suspensive one because there could not be any implementation until the requirement of the continued employment was fulfilled as at the implementation date.

SARS contended that when the relevant clauses were read together the substance was that there was a fundamental uncertainty prior to the implementation date as to whether the deferred sale would ever be implemented. Accordingly, when Appellants concluded their deferred purchase agreements within the initial 21-day period, they did not exercise a right to acquire shares within the meaning of section 8A.

It was SARS' view the true substance of what the parties intended revealed that a suspensive condition of continued employment had been created and that Clause 7.3 read with clause 10.2 had been formulated in order to disguise this fact and thereby justify an argument that the participants could avoid tax in terms of section 8A of the Act and in this regard SARS relied on the decision in *C: SARS* v *NWK Ltd*.

Appellants contended, however, that the right to acquire shares in terms of the scheme was triggered, for the purposes of section 8A, when the relevant option to purchase shares was exercised and accordingly they contended that the right to acquire shares was exercised for the purpose of section 8A only when the shares were delivered.

The key question for determination in respect of the dispute between the parties was whether the 1997 scheme conferred on a participant a definite and unconditional entitlement to acquire shares upon the exercise of the option pursuant to Clause 7.1 of the scheme agreement or whether the entitlement could only be determined upon the relevant implementation dates.

Appellants referred to clause 7 of the scheme agreement in support of their contention that unconditional sales of the scheme shares took place upon the exercise of the option. Clause 7.1 specifically provided that the participants shall become entitled to delivery thereof against payment of the portion of the consideration attributable thereto on the various anniversary dates. In addition, Clause 7.1.4 specified, in the case of a participant whose service with the Foschini Group was terminated for specific reasons, the Foschini Group would be entitled to effect earlier delivery of the sale shares to the participant against payment of the consideration by the participant, who was, in turn, obliged to effect payment thereof on the particular dates as determined. Clause 7.3 provided that, if at any prior time to the implementation date in respect of any sale shares, a participant's service with the Foschini Group was terminated for any other reason, the participant would be obliged to sell his or her shares to the Foschini Group which would be obliged to purchase such shares at a purchase price equal to the consideration which would have been payable by the participant on the implementation date in respect of these sale shares and set-off would then apply.

Judges Davis and Baartman held the following:

(i) That it was common cause that, for section 8A of the Act to apply, the taxpayer 'must exercise . . . a right to acquire' the relevant shares and the key question for determination in respect of the central argument between the parties was whether the 1997 scheme had conferred on a participant, such as first and second appellants, a definite and unconditional entitlement to acquire shares upon the exercise of the option pursuant to Clause 7.1 of the scheme agreement or whether the entitlement could only be determined upon the relevant implementation dates.

(ii) That the judgment in *SIR* v *Kirsch* represents a correct interpretation of section 8A of the Act – *i.e.* the learned judge in that case concluded that there was no reason 'to limit the operation of section 8A to rights in the strict sense of options' and this approach was followed in *ITC 1493* and it therefore requires a different form of enquiry to that which

is employed to determine the meaning of 'actually incurred' pursuant to section 11(a) of the Act and as Coetzee J held in *Kirsch*, *supra*, the word 'right' is not a right '*strictu sensu*.'

(iii) That in this connection W N Hohfeld's classic work *Fundamental Legal Conceptions as applied in Judicial Reasoning* (1946) proves a very useful point for analysis. In Hohfeld's analysis, the concept 'right' could be expanded to four different meanings: right, privilege, power or immunity. Whereas a right has a correlative of a duty, the correlative of privilege is a no-right, the correlative of power is a liability and the correlative of immunity is a disability.

(iv) That, in the case of section 8A, the word 'right' appears to be better analysed as a privilege given to the employee and it then followed that the arguments raised about conditional obligations imposed upon the employee who enjoys a privilege are not applicable. Furthermore, the attempt to apply the analysis of 'actually incurred' to a privilege is clearly still born and is not relevant to the present transaction.

(v) That clearly, what the legislature had in mind was the acquisition of an option to acquire shares which revealed an entirely different set of analytical requirements to that which must be used to parse section 11(a) and, accordingly, the argument with regard to bilateral obligations was not relevant to the determination of the meaning of 'right to acquire' in terms of section 8A of the Act.

(vi) That the fact that the approach advocated by the Appellant as to the meaning of 'right to acquire' in section 8A had been followed by SARS ever since *Kirsch's* judgment is an added factor to be taken into account and as Marais JA said in *Nissan SA* (*Pty*) *Ltd* v *CIR* 60 if there is at least room for the interpretation in the language of the provision, as advocated in this case by the Appellant, and that interpretation is the one which has been accorded to the words for sufficiently long, without being gainsaid, this provides a good reason for concluding that that is what the phrase was intended to mean.

(vii) That a further interpretive aid is to have recourse to section 8C which, on 26 October 2004, superseded section 8A and that provision drew a distinction between an unrestricted equity instrument and a restricted equity instrument and had section 8A carried the meaning that 'acquire' does not take place until the participant has fulfilled his or her obligations, then there would have been no need for section 8C to draw the clearly crafted distinction between restricted instruments and unrestricted instruments.

(viii) That this then brought the enquiry back to the question of the conditionality of deferred purchase agreements and SARS' argument that the 1997 scheme did not confer a definite and unconditional entitlement to acquire shares in any participant and the question was whether a participant would be entitled to acquire the shares only on the relevant implementation dates.

(ix) That, turning to the question of conditionality, the key submission of SARS was that there were two relevant suspensive conditions, namely the requirement of continued employment and the stop loss provision.

(x) That contrary to the submission of SARS that the condition is suspensive because there will never be an implementation until the requirement of continued employment has been fulfilled on the implementation date, an implementation of the terms of the contract does take place, albeit within the specific terms of the framework as provided for in Clause 7.3

(xi) That the relevant clauses did not sustain an argument that the sale was subject to conditions, namely that the agreement was suspended until the fulfillment of the condition. Unconditional sales of the shares took place upon the exercise of the option, albeit that the method of payment would differ, depending upon which clause was triggered by the events which superseded Clause 7.1 and it was specified clearly that, upon the exercise of an option, the participant shall become entitled to delivery thereof against payment of the portion of consideration attributable thereto on specified dates.

(xii) That, furthermore, an examination of the stop loss mechanism revealed that it did not operate until such time as a participant decided to invoke it and sell the shares back to the Foschini Group or the trust.

(xiii) That, given the finding that the sale agreements did not trigger conditions which would justify the argument that 'no right to acquire' had taken place in terms of the meaning of section 8A, SARS invited the court to examine the substance of the transactions in order to conclude that, in substance, the various provisions were subject to the kind of conditions which justify SARS' contention regarding the applicability of section 8A of the Act.

(xiv) That while accepting the fundamental principle that a taxpayer is entitled to arrange his or her affairs so as to remain outside the provisions of the Act, Lewis JA held in *C: SARS* v *NWK Ltd* that a court will not be deceived by the form of a transaction but will examine its true nature and substance and, accordingly, the *onus* which rests upon a taxpayer in terms of s 82(*a*) of the Income Tax Act is not discharged simply by a party showing that effect was given to the contract in accordance with its terms.

(xv) That in the *NWK case*, *supra*, the court had been confronted with a starkly clear set of simulated transactions and the facts of the case illustrated, without doubt, that the parties had not created genuine rights and obligations but had constructed a loan for R95 million as opposed to R50 million, purely to enable the taxpayer to obtain a greater tax benefit. Beyond this finding there is nothing in the careful judgment of Lewis JA which supports the argument that the reasoning as employed in *NWK* was intended to alter the settled principles developed over more than a century regarding the determination of a simulated transaction for the purposes of tax.

(xvi) That the key paragraph relied upon by SARS in the *NWK case*, *i.e.* par. [55], needed to be read in context so as to ensure that the body of precedent is read coherently rather than reading *NWK* as being an unexplained rupture from more than a century of jurisprudence.

(xvii) That it appeared that the intention of par. [55] of the *NWK* judgment was to point in the direction which the mandated enquiry must take in such cases namely to examine the real commercial sense of the transaction and if there was no commercial rationale, in circumstances where the form of the agreement sought to present a commercial rationale, then the avoidance of tax as the sole purpose of the transaction, would represent a powerful justification for approaching the set of transactions in the manner undertaken by the court in *NWK*.

(xviii) That, without an express declaration to that effect, *NWK* should be interpreted to fit within a century of established principle, rather than constituting a dramatic rupture.

(xix) That the evidence in the present case was congruent with the scheme agreements read as a whole and the various clauses which had been subjected to scrutiny by SARS were not drafted to disguise the true intention of the parties. Indeed, all of the documents which were prepared were consistent with an intention to conclude various agreements in accordance with their terms and reveal a clear commercial purpose; moreover, there is no evidence to suggest that the parties pretended that the sale agreement was subject to express terms contained therein or that there was a disguise as to the fundamental structure of the various agreements and their legal implications.

(xx) That the various clauses upon which SARS relied to argue that, in substance, the transactions were different from the form, cannot be justified either on the basis of the evidence of the parties or the clear wording of the particular clauses as they are what they purported to be and thus stand upon an entirely different footing from the situation where a R50 million loan is increased to a R96 million loan by way of a transaction which, in substance, reveals that the loan was for the former amount and as was the case in the ‘sale and lease back’ dispute between *CIR* v *Conhage* (*Pty*) *Ltd*, in this case the parties had

every intention of entering into the agreements and of putting these agreements into effect.

(xxi) That the aforementioned conclusion meant that the analysis was driven back to the earlier examination as to whether a right, sufficient to trigger section 8A, was created by way of agreements which stood clearly to be analysed in terms of their express tenor and, given the conclusion to which the court had arrived with regard to section 8A, there was nothing in the argument with regard to substance over form as advanced by SARS that should alter this initial analysis and for this reason section 8A was triggered by the exercise of the option by the two Appellants and it followed that delivery of the scheme shares to Appellant did not constitute the exercise by him or her of a right to acquire the shares for the purpose of section 8A.

(xxii) That both par. 2(*a*) of the Seventh Schedule to the Act and section 8C of the Act were not applicable to this dispute: if it is accepted that the right to acquire a share for the purpose of section 8A is exercised upon accepting the offer or the exercise of the option to purchase the share, then the application of par. 2(*a*) is excluded in terms of the proviso. On the evidence the relevant scheme shares were acquired by the exercise of rights which were granted to Appellant before 26 October 2004 and section 8A therefore applies pursuant to the court's analysis and therefore section 8C was not applicable to this dispute.

Judge Waglay held the following:

(i) That there was one difficulty with the judgment of Davis J and that related to his interpretation of the judgment referred to as the *NWK* judgment and in particular his statement that there was nothing in that judgment which supported the argument that the reasoning as employed in *NWK* was intended to alter the basic principles developed over more than a century regarding the determination of a simulated transaction for the purpose of tax.

(ii) That E Broomberg SC in his analysis of *NWK* in 2012 *The Taxpayer* (60) p 187 had correctly contended that the *NWK* judgment sought to

hold previous judgments involving alleged simulated transactions as being wrong and Davis J's interpretation was somewhat strained; *NWK* was a dramatic reversal of what had been a consistent view of what constituted a simulated transaction and *NWK*, considered in its entirety, not by extraction of words and phrases out of their real context, did in fact lay down the rule that any transaction which has as its aim tax avoidance will be regarded as a simulated transaction irrespective of the fact that the transaction is for all purposes a genuine transaction.

(iii) That there was no doubt that the scheme implemented by the Foschini Group which benefitted the applicants was a scheme devised at tax avoidance and not tax evasion and the fact that the transaction entered into between the applicants and the Foschini group was a complete transaction without any suspensive conditions cannot save the applicants from SARS' assessment because in terms of the *NWK* judgment, the transactions would amount to a simulated transaction and SARS' reliance on the *NWK* judgment is therefore not without merit.

(iv) That Appellants on the other hand argued that the *NWK* judgment had no application in the present dispute because it dealt with transactions that are concluded to evade tax rather than avoid it.

(v) That before one is bound to a precedent setting judgment and is obliged to follow it, the judgment must be clear and unequivocal, it must be plain, unmistakable and explicit in its rejection of previous judgments which it seeks to reverse and it must be applicable to the facts in the matter before the court confronted with its possible application: *NWK* does not in my view do so and it does not provide any reasons why the judgments aptly dealt with by Davis J in para [79] to [83] are no longer good law and this is further compounded by the troubled equivalence in the judgment of the phrases 'tax avoidance' and 'tax evasion' two very distinct concepts.

(vi) That, having regard to the above, *NWK* cannot be read to serve as a precedent in this case where evasion is not the issue and, in any

event, any transaction which has its purpose tax evasion is unlawful as tax evasion constitutes a criminal offence in terms of the Income Tax Act and *NWK* cannot therefore be authority for setting aside a transaction as simulated by reason of being a vehicle for tax evasion as this is automatic in terms of the law. On the other hand, if the words 'evasion of tax' are to be substituted with 'avoidance of tax' then the *dictum* goes against the accepted practice in our income tax law which permits transactions aimed at tax avoidance. Furthermore, the confusion created by the judgment mitigates against it serving as a precedent binding upon the lower courts.

6.2 ITC 1862

The taxpayer was at all material times listed on the Johannesburg Securities Exchange and the Listings Requirements (LR) of the JSE contain several rules which are applicable in circumstances where a company or a subsidiary wishes to acquire shares in itself.

The taxpayer, after the introduction of the Companies Amendment Act in 1 July 1999, and which permitted a company to acquire shares in itself subject to certain requirements, had resolved on 24 August 1999 to amend its articles of association in order to permit the acquisition of its own shares and to give a general authority to the directors to make such acquisitions up to a maximum of 10%.

The taxpayer, at its next AGM on 21 September 2000, had renewed the general authority of the directors in this regard and resolutions authorised the taxpayer or any subsidiary of the taxpayer to acquire shares in the taxpayer and at the same time a share incentive scheme for employees was also approved.

The taxpayer's share incentive scheme was duly established and shares were to be delivered to employees at future dates. However, if the taxpayer shares increased in value the cost to the company of procuring shares for delivery would also increase in due course and it was therefore decided

that it would be prudent to acquire shares in itself in order to hedge its liability.

The taxpayer therefore procured a shelf company, ALS, as a wholly owned subsidiary and it eventually acquired 7.4 million the taxpayer shares and the idea was to buy and hold the shares as it made no sense to acquire the shares and cancel them. ALS's acquisition of these and later shares was funded following the pattern of funding in general within the taxpayer group, i.e. the treasury company in the group – a subsidiary of the taxpayer – granted ALS interest-free loan funding to acquire the shares in the taxpayer.

The taxpayer had appointed X as its Chief Financial Officer and it was put to him in cross-examination that his evidence that the 8.15 million the taxpayer shares acquired by ALS were to be utilised for the purposes of the share incentive scheme was false.

X in fact testified, and his evidence in this regard was not challenged that ALS in fact sold and transferred its treasury shares to the share incentive trust and this was also reflected in the relevant financial statements and tax schedules. Minutes were also located of a meeting of the taxpayer's remuneration committee which expressly recorded a request from the committee for proposals with regard to the repurchase of the taxpayer shares to hedge the group's position in respect of the share incentive scheme.

Thereafter ALS continued to acquire new parcels of the taxpayer shares and was approaching the 10% statutory limit of a holding in the taxpayer. X emphasised that the repurchase of the taxpayer shares should be considered in the same way as any other investment opportunity and he argued that it was not a return of capital but a rational investment decision and there was no intention of securing any tax benefit. There was also no debate about whether the shares should be bought by the taxpayer or ALS and, it seemed, X took it for granted that the taxpayer would continue using ALS to buy and hold the taxpayer shares.

In the taxpayer's annual report for the year ended 30 June 2004 its chairman reported that the taxpayer had screened many potential investment opportunities but deals offering superior returns and meeting the taxpayer's criteria were not always readily available and, as a result, it had used a significant part of its South African cash to purchase the taxpayer shares.

In its financial statements for the year ended 30 June 2004 ALS reflected it's a Ltd shares as an investment with a market value of R502 340 901 million and it noted that all the transactions were on market related terms and X confirmed that the shares had been bought by ALS as a long-term investment.

Further shares were purchased on 5 October 2004 and 30 June 2005 bringing ALS's shareholding in the taxpayer to 8.64% and the latter was the last purchase of treasury shares.

SARS had issued an assessment on 29 August 2008 in which STC of R213 911 343.91 had been raised on the taxpayer in consequence of dividend declarations which took place on various dates from 2004-6. SARS had, in effect, disallowed the exemptions from STC claimed by the taxpayer in terms of section 64B(5)(*f*) of the Income Tax Act in respect of the dividends declared as such on the basis that the exemptions were claimed pursuant to a transaction, operation or scheme as contemplated in section 103(1) of the Act.

The taxpayer's objection to the assessment was disallowed by SARS and it then noted this appeal to the Tax Court.

SARS contended that the taxpayer had entered into a unitary scheme or series of transactions, commencing in March 2002, to avoid its having to pay STC on the repurchase of the shares – these comprised the establishment of ALS as a subsidiary, its funding through interest-free intra-group loans, the acquisition by ALS of the taxpayer shares on the market (transactions which did not attract STC) and the eventual sale by ALS of the shares to the taxpayer and their cancellation, the latter being transactions which were exempt from STC.

Judge Desai J held the following:

(i) That section 103 of the Income Tax Act was the old anti-avoidance provision in the Act which was repealed with effect from 2 November 2006 and was replaced by sections 80A to 80L of the relevant Act. However, as the transactions which SARS sought to impeach in the present case occurred prior to 2 November 2006, the old section 103 remained applicable.

(ii) That section 103(1) may be invoked by SARS if he is satisfied that a 'transaction, operation or scheme' had certain characteristics and that decision was subject to objection and appeal (section 103(4)) and the question that confronted the court was whether it was satisfied that the impugned transaction had the necessary characteristics.

(iii) That in order to succeed SARS had to establish the following:

- That the taxpayer had engaged in a transaction, operation or scheme;
- That the transaction had the effect of avoiding or postponing liability for tax;
- That the transaction was entered into or carried out in a manner which would not normally be employed for bona fide business purposes other than obtaining a tax benefit; or created rights or obligations that would not normally be created between persons dealing at arm's length under a transaction of the nature of the transaction in question; and
- That the transaction was entered into or carried out solely or mainly for the purpose of obtaining a tax benefit.

(iv) That the *onus* to establish the existence of a transaction complying with the effect and abnormality requirements was on SARS and the *onus* in respect of the purpose requirement was on the taxpayer, section 103(4)(*a*) of the Act.

(v) That a taxpayer is entitled to arrange his affairs so as to pay the least tax. In other words, if the same commercial result can be achieved in

different ways, the taxpayer may choose the way which does not attract tax. The subjective purpose of those who entered into the transaction is a question of fact and to fall under the category 'mainly' the said purpose must be the dominant purpose in the sense of being dominant over any other purposes.

(vi) That the test was objective with regard to the abnormality requirement and the evidence of other similarly placed persons engaging in transactions of the kind in question was permissible evidential material in determining whether a particular transaction had been entered into in a manner not normally used for *bona fide* business purposes. However, rights and obligations which may be abnormal as between strangers may not be normal as between parties with a pre-existing special relationship such as in this instance where ALS was a wholly owned subsidiary of the taxpayer.

(vii) That each purchase by ALS of shares on the market was a 'transaction' in the ordinary contractual sense and each sale of shares by ALS to the taxpayer was likewise a 'transaction'. What SARS needed to establish on a balance of probabilities was that each of these individual steps formed part of a single scheme of transactions. Even though the ultimate steps in a scheme need not be in contemplation from the very outset, there must be sufficient unity between the ultimate steps and the earlier steps so that, having regard to the ultimate objective, they can be regarded together as part of a single scheme or transaction.

(viii) That the evidence simply did not establish any such unitary scheme and there were several reasons why the said scheme did not exist: ALS had been established to acquire the taxpayer shares to hedge the group's obligations under its share incentive scheme. This predated by some months the commencement of the investment-driven repurchase programme. There had been no intention that the shares so acquired should be on-sold to the taxpayer and cancelled, nor were they in fact on-sold to the taxpayer and cancelled and in July and August 2003 they were sold by ALS to the share incentive trust.

(ix) That the repurchase programme, when conceived and implemented, did not envisage the eventual sale of treasury shares to the taxpayer and their cancellation. The possibility of cancellations only arose as ALS's holdings neared the statutory 10% limit. When that occurred, the taxpayer repurchased some of its shares held by ALS to create space for ALS to purchase more shares on the market. The outstanding treasury shares were finally resold and cancelled in circumstances that were clearly not foreseen when the programme commenced.

(x) That therefore the sale of shares by ALS to the taxpayer was not under any circumstances part of a 'scheme' which started with the purchase by ALS of shares in the taxpayer and the questions relating to effect, abnormality and purpose need not be considered, since the premise of SARS' pleaded case disappears.

(xi) That identifying SARS' true case was important because of the nature of section 103 as it involved the exercise of an extraordinary administrative power enabling SARS to overturn the express and ordinary consequences of applying the Act. The exercise of that power involved his 'determining' a liability for tax and an appeal in this context was against the Com-missioner's 'decision', namely his determination of a tax liability and its amount.

(xii) That the basic jurisdictional requirement for the exercise of the power was that SARS is 'satisfied' of the various requirements and once SARS reaches the requisite level of satisfaction, and exercises the power to determine the tax liability on the strength of such satisfaction, an appeal must of necessity go to whether he was justified in being so satisfied. He must stand and fall by his reasons for exercising the power and if he did not make his tax determination on the basis of being 'satisfied' about an alternative scheme, he cannot rely on the alternative when his section 103(1) determination is challenged on appeal.

(xiii) That the taxpayer's contention was that the arguments which SARS now urged upon the court deviated materially from the substance of

the Rule 10 statement, that he attempts now to justify his exercise of the section 103 power by reference to facts and arguments – in essence, a new conception of the impugned scheme – that were not the basis for the exercise of the section 103 power in the first place. The pleaded scheme was that from the very outset it was always intended for the taxpayer to acquire the shares (step one) through section 85, but it established and interposed ALS as a conduit so that when the shares were repurchased and cancelled (step two) as had always been the intention, there would be no STC liability.

(xiv) That SARS' pleaded case did not allow it to advance its alternative contention as such a version was not to be found in SARS' Rule 10 statement. In addition, the present case was an appeal in terms of section 103(4) against SARS' section 103(1) decision. The only thing that the court had jurisdiction to determine in the appeal was whether SARS' actual decision was right or wrong. His actual decision comprised the various aspects of which he was 'satisfied' in terms of section 103(1) and the composite scheme alleged in SARS' pleaded case was the only 'scheme' on the existence of which SARS claimed to be satisfied when assessing the taxpayer.

(xv) That the pleaded scheme simply could not be established because there was no evidence that the share repurchase programme was always intended to end with the cancellation of the shares, let alone that ALS was merely conceived and interposed to facilitate what was always intended as a section 85 repurchase. Furthermore, when the programme had been conceived as a commercial strategy, the section 64B(5)(*f*) exemption was not in place and it was assumed that there would be STC on any subsequent repurchase. The taxpayer's conduct had also been entirely inconsistent with a plan to achieve a tax benefit, with no regular selling and particularly no immediate selling even when it was learned that the section 64B(5)(*f*) exemption may be lost. Finally, the commercial rationale and normality of the purchase and holding of treasury shares were conceded.

(xvi) That it was already clear that SARS had failed to establish the transaction requirement as pleaded and the taxpayer's case was equally good insofar as the other requirements were concerned.

(xvii) That there were several reasons why the 'effect' requirement had not been met in this case. SARS had to prove that the alleged scheme had the effect of avoiding liability for STC – this being the tax allegedly avoided. The taxpayer had been under no compulsion to buy its own shares and its shares would only have been bought if management thought that it made good commercial sense; moreover, if financial analysis showed that a purchase of the taxpayer shares would not be a good investment, the shares would simply not have been bought. If the taxpayer had directly bought on the market the shares that ALS bought, STC would have been payable by the taxpayer. However, would the taxpayer have bought the shares and paid STC? STC would have added a cost of 12.5% to the purchase of the shares and, despite the *onus*, SARS made no attempt to establish through cross-examination that with this additional cost the taxpayer would have bought the shares.

(xviii) That the evidence overwhelmingly demonstrated that the taxpayer's sole or main purpose in concluding the various transactions was not to obtain a tax benefit as the share repurchase programme had been entered into for the purpose of making a long-term investment in its own shares. The shares were to be acquired by a subsidiary and held in treasury, not immediately cancelled; moreover, the evidence was that there was no intention to obtain a tax benefit. The impugned sales in fact only occurred in circumstances that were not anticipated at the time the repurchase programme commenced.

(xix) That, as regards the normality requirement, SARS' own expert confirmed that it was quite normal for companies to repurchase their shares in subsidiaries and the taxpayer's expert witness demonstrated, from her research sample of listed companies over the period 1999–2009 that only a small percentage of companies that repurchased their shares did so exclusively on a direct basis;

moreover, the share repurchase programme as a whole was not shown to be abnormal in the sense of being any different from how other companies went about acquiring shares in treasury.

(xx) That, having regard to the circumstances in which the repurchase programme was entered into and carried out, it was not entered into and carried out in a manner that would not normally be employed for *bona fide* business purposes, other than the obtaining of a tax benefit and it was carried out in a normal fashion for achieving *bona fide* business purposes.

Appeal upheld and the disputed STC assessments were set aside.

7. INTERPRETATION NOTES

7.1 Income Tax - Right of use of motor vehicle – No. 72

This Note provides guidance on the income tax consequences that arise for an employee when an employer (or an associated institution in relation to an employer) grants that employee the right of use of a motor vehicle, commonly known as a 'company car fringe benefit', with specific reference to the latest legislative amendments to the Fourth and Seventh Schedules to the Act.

Employers often grant employees a travelling allowance or the use of an employer-provided motor vehicle (or both) by virtue of the employees' employment, as a reward for services rendered by the employees or due to the employees' duties. The right of use of a motor vehicle provided by an employer to an employee for private or domestic purposes is regarded as a taxable benefit in the hands of the employee. The value of this benefit is included in the employees' gross income under paragraph (*i*) of the definition of 'gross income' in section 1(1).

Paragraph 2(*b*) read with paragraph 7 deals with the cash equivalent of the value of this taxable benefit.

The latest legislative changes to employer-provided motor vehicles (company cars) are effective from 1 March 2013 and are applicable to years of assessment commencing on or after that date (that is, from the 2014 year of assessment).

The use of a company car for private or domestic purposes gives rise to a taxable benefit under the Seventh Schedule of the Act. The cash equivalent of the taxable benefit which must be included in the employee's gross income is equal to the value of the private use less any consideration paid by the employee for that benefit.

The value of private use of a vehicle held by an employer otherwise than under an 'operating lease' is generally equal to 3,5% per month of the determined value of the motor vehicle. The amount calculated must be apportioned if the motor vehicle is only used for part of a month (that is, 3,5% of the determined value of the motor vehicle multiplied by the number days of use of the motor vehicle in the month divided by the number of days in the month). The percentage may be reduced to 3,25% if the motor vehicle was the subject of a maintenance plan when it was acquired by the employer. The value of private use may not be reduced for temporary absences such as when the employee is away on work or the car is in for a car service.

The value of private use of a vehicle held by an employer under an 'operating lease' is equal to the actual cost incurred under the operating lease plus the cost of fuel incurred on the same vehicle.

The calculation of the value of private use assumes the employee only uses the motor vehicle for private purposes and that the employer bears all the operating costs. However, on assessment an employee may, depending on the circumstances, qualify for a reduction in the value of private use to the extent the motor vehicle:

- is used for business purposes;
- to the extent the employee has borne the full costs of licence, insurance or maintenance (reduction not available if the vehicle is held under an operating lease); and

- to the extent the employee has borne the cost of fuel for private use (reduction not available if the vehicle is held under an operating lease).

Employees must maintain detailed records of business travel if they wish to claim these reductions, this is generally done in the form of a logbook. Special rules apply to an employee who has the right of use of more than one company car, and potentially, if the company car is a pool vehicle available to employees in general, or if the employee is regularly required to perform duties outside of normal office hours.

Employers are required to calculate and withhold employees' tax on a monthly basis. With effect from 1 March 2011 when calculating the monthly employees' tax withholdings, employers must include 80% of the cash equivalent of the taxable benefit as remuneration. This reduced withholding (previously 100% was included) takes into account potential reductions which may take place on assessment, for example, the business reduction. However, in the event that an employer is satisfied that at least 80% of the use of the motor vehicle during a year of assessment will be for business purposes, then only 20% of the cash equivalent of the taxable benefit is included as remuneration and is subject to employees' tax.

7.2 Income Tax – Long service awards – No. 71

This Note provides guidance and clarity on the income tax consequences for an employee when the employer gives an employee an asset as a long service award.

Employers give employees a wide range of awards. The reasons for the awards are varied; often it is a gesture of appreciation for services rendered, recognition for outstanding performance or recognition for the length of the employee's service (commonly referred to as a 'long service award'). These awards are, with a few exceptions, subject to taxation.

The award could be in a number of forms including money, an asset, a service, the right of use of an asset or residential accommodation.

This Note focuses on the income tax treatment for an employee when an employer gives the employee an asset as a long service award. The income tax consequences will be different if an employer gives an employee a long service award in a form other than an asset.

The awarding of an asset by an employer to an employee in recognition of the employee's long service is a taxable benefit. Gift vouchers are assets, but a gift voucher for a meal is specifically excluded from paragraph 2(*a*) because it is dealt with in paragraph 2(*c*) or (*d*) (the latter paragraphs are not covered in this Note).

The cash equivalent of the value of the taxable benefit arising from the acquisition of an asset is equal to the *value of the asset* less any consideration paid by the employee for the asset.

In the context of long service awards, the value of the asset is generally equal to the cost of the asset to the employer. In addition, in the case of qualifying long service awards the value of the asset may be reduced by the lesser of:

(a) the cost to the employer of all assets given to the employee for long service during the year of assessment; or

(b) R5 000.

For an award to qualify as a long service award, the asset must have been given to the employee for being in employment with the same employer for:

(i) an initial unbroken period of service of at least 15 years; or

(ii) a subsequent unbroken period of service of not less than 10 years.

7.3 VAT – Supplies made for no consideration – No. 70

This Note serves to:

- set out the legal framework for the VAT treatment of supplies of goods or services which are made by vendors for no consideration in certain circumstances; and
- provide guidance to vendors, on whether:
    - input tax may be deducted in respect of any VAT incurred on goods or services acquired to make supplies for no consideration; and
    - output tax must be declared on any goods or services supplied for no consideration.

The definition of 'enterprise' in section 1(1) is one of the most important definitions in the VAT Act. Its main purpose is to set out as clearly as possible, the type of persons, activities and supplies which are intended to form part of the tax base, as well as those that are meant to be excluded. In terms of paragraph (*a*) of this definition, there is a general requirement that enterprises participating in the VAT system must charge a consideration (price) for the goods or services they supply.

The implication of not meeting this requirement is that supplies made for no consideration are not made in the course or furtherance of an enterprise, and hence, will not be a taxable supply. However, there are many different circumstances under which enterprises will, for purely commercial reasons, make a supply without charging a consideration.

This raises the question as to whether there are certain circumstances under which a supply for no consideration may be regarded as a taxable supply, and consequently, whether it will be possible for the supplier to deduct input tax on any expenses incurred for the purpose of making those supplies.

The ability to correctly characterise a particular supply as being taxable or not is important because the vendor will generally have a right to deduct the VAT incurred on any goods or services acquired for the purposes of making taxable supplies, but will not be able to do so if the supplies are exempt, out-of-scope, or in connection with any other non-taxable activities conducted by the vendor.

To fully understand the VAT treatment of supplies made for no consideration under the South African VAT system, it is necessary to understand the underlying policy framework which influences the design of the VAT system, as well as the general international characteristics and principles upon which a VAT system of taxation is based. This is important because although the different countries that have VAT (or goods and services tax (GST) as it is known in some other countries) have very similar core features, there are often a number of differences in the detail of how the features and designs of those systems apply.

7.4 Income Tax – Amalgamation of amateur and professional sporting bodies – No. 46 (Issue 4)

This Note provides information and guidance on the amalgamation of amateur and professional sporting bodies carried out under section 125 of the RLAA 2007.

Before its deletion, section 10(1)(*c*D) provided an exemption from income tax for:

> ‘the receipts and accruals of any amateur sporting association’.

The above provision was deleted with effect from 15 July 2001 with the introduction of a new tax dispensation for exempt organisations. Under the new dispensation, a concept of a PBO conducting an approved PBA was introduced. Both these terms are defined in section 30. The PBAs approved by the Minister of Finance are set out in Part I of the Ninth Schedule to the Act. A PBA under the heading ‘Sport’ is described in paragraph 9 as follows:

> ‘The administration, development, co-ordination or promotion of sport or recreation in which the participants take part on a non-professional basis as a pastime.’

Provided an amateur sporting organisation complied with the requirements and conditions of section 30 and conducted the approved PBA, the organisation could be approved as a PBO and was fully exempt from income tax on its receipts and accruals. One of the requirements contained in section 30 was that an approved PBO was not permitted to engage in any trading or business activities.

As a result of the professional sport conducted by some national or provincial sporting organisations, they no longer qualified as amateur sporting associations and thus failed to comply with the requirements for approval as PBOs. This was because they did not conduct the approved PBA described above and consequently their income was regarded as being derived from trading activities or a business undertaking. Certain sporting bodies therefore separ.ted their professional and amateur activities in order for the amateur body to qualify as a PBO.

The professional arm of any sporting body is always seen as the ‘income provider’ or ‘promoter’ of the amateur sporting activities.

The total income of the professional arm derived from sponsorships, media rights and the like is fully taxable, while money expended by the professional arm in supporting amateur sport is not deductible under section 11(*a*) as it is not in the production of income.

In 2006 the provisions of the Act relating to PBOs were amended to provide a partial-taxation system for approved PBOs conducting trading or business activities. This meant that PBOs were permitted to retain their trading activities while being taxed on their trading income without losing their tax-exempt status.

The separation of a sporting body into two separate entities proved to be to the disadvantage of certain sporting bodies and consequently the 2007 Budget Review proposed measures to be introduced to assist in the re-integration of the separate sporting entities, so that expenditure incurred by

the professional body to develop amateur sport could be deducted by the unified body, a taxable entity.

7.5 Income Tax – Wear and tear or depreciation allowances – No. 47(3)

This Note provides guidance on the application and interpretation of section 11(*e*) in relation to the determination of:

- the ‘value’ of a qualifying asset on which the allowance is based; and
- acceptable write-off periods of such assets.

This Note is a binding general ruling made under section 89 of the Tax Administration Act on section 11(*e*) in so far as it relates to the determination –

- of the value of an asset for purposes of section 11(*e*); and
- the amount that will qualify as an allowance.

This ruling applies to any qualifying asset brought into use during any year of assessment commencing on or after 1 March 2009.3

This Note provides guidance on the circumstances under which the wear-and-tear or depreciation allowance provided for in section 11(*e*) may be claimed as a deduction.

It also contains an annexure which provides the different write-off periods for qualifying assets.

7.6 VAT – Documentary proof required in terms of section 16(2) to substantiate a vendor's entitlement to 'input tax' or a deduction as contemplated in section 16(3) – No. 49 (Issue 2)

This Note provides guidelines on the documentary proof that must be obtained and retained under section 16(2) to substantiate a vendor's entitlement to 'input tax' as defined in section 1(1), or a deduction as contemplated in section 16(3)(*c*) to (*n*).

Value-added tax (VAT) is aimed at taxing final consumption. As a result, where a vendor acquires goods or services for purposes of consumption, use or supply in the course of making taxable supplies, that vendor is entitled, subject to the provisions of sections 16(2), 16(3), 17(1), 17(2) and 20 to deduct from the amount of output tax:

- the VAT paid in respect of a taxable supply made to that vendor;
- an amount equal to the tax fraction of any payment made by the vendor in respect of second-hand goods. For the period prior to 10 January 2012, the deduction of input tax was, in respect of second-hand goods which consist of 'fixed property' as defined, limited to the amount of transfer duty or stamp duty paid;
- an amount equal to the tax fraction of the outstanding cash value in respect of goods repossessed by the vendor under an instalment credit agreement; or
- a deduction as contemplated in sections 16(3)(*c*) to (*n*).

7.7 Income Tax – Farming operations: Equalised rates of tax – No 29 (Issue 2)

This Note provides guidelines with regard to the method applied in the calculation of the rating amount applicable to farmers who elected that their tax be calculated at equalised rates of tax under paragraph 19(5) of the First Schedule to the Act.

Issue 1 of this Note, issued on 30 March 2005, is hereby replaced.

A person, deriving income from farming operations may, under paragraph 19(5), elect to be subject to tax according to the rating formula set out in section 5(10). The rating concession is applied due to the abnormal accrual of income occurring in one year of assessment in comparison with another year. Farming income may fluctuate on an annual basis because of, for example, an extended period between sowing and eventual crop yields – in other words, periods of little or no income followed by periods of inflated income.

This rating concession applies only to individuals (natural persons), executors of deceased estates and trustees of insolvent estates. Once the option has been exercised to adopt the equalised rates, this election will be binding on the taxpayer for the current year as well as all future years of assessment, irrespective of the fact that farming operations may be terminated. No provision is made in the Act for a variation either by the farmer or by SARS.

7.8 No. 69 – Game farming

This Note:

- provides guidance on the application of selected sections of the Act and paragraphs of the First Schedule to persons carrying on game-farming operations, with its primary focus being the provisions applicable to livestock;
- is not intended to deal with farming in general; and

- replaces Practice Note No. 6 dated 30 July 1999.

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

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

The First Schedule applies regardless of whether a taxpayer derives an assessed loss or a taxable income from farming operations. The Schedule may further apply even after farming operations have been discontinued [section 26(2)].

Section 26 and the First Schedule are applicable to game farming since it comprises farming operations.

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

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

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

A farmer is required to bring to account the value of game livestock in opening and closing stock. No standard values have been prescribed by regulation for game livestock, but SARS accepts that game livestock may

be allocated a standard value of nil. Game livestock which is acquired by donation or inheritance is included in opening stock in the year of acquisition at market value under paragraph 4.

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

A farmer who ceases to carry on game-farming operations must generally continue to deal with any game livestock under the First Schedule.

Special rules apply for income tax and CGT purposes upon the death or sequestration of a farmer.

7.9 Provisions of the Tax Administration Act that did not commence on 1 October 2012 – No. 68 (Issue 2)

On 1 October 2012 the Act came into operation except for certain provisions relating to interest. This Note provides guidance on the identification of those interest provisions which have not come into operation.

Issue 1 of this Note omitted to include sections 64B(9) and 64K(6) of the Income Tax Act No. 58 of 1962 in Annexure B. This oversight has been corrected in this issue.

Under section 272 the President must by proclamation in the *Gazette* determine the date on which the Act comes into operation and may determine different effective dates for different provisions.

The proclamation (Annexure A) was published on 14 September 2012 and provides that the Act shall come into operation on 1 October 2012 except for:

- sections 187(2), (3)(*a*) to (*e*) and (4), 188(2) and (3) and 189(2) and (5); and

- a provision of Schedule 1 to the Act that amends or repeals a provision of a tax Act relating to interest under that tax Act, to the extent of that amendment or repeal.

The Act introduces a new regime for purposes of the accrual of interest on tax debts or refunds owed by SARS. Most of the interest provisions are contained in Chapter 12 which comprises:

- section 187 – General interest rules;
- section 188 – Period over which interest accrues; and
- section 189 – Rate at which interest is charged.

Schedule 1 of the Act sets out the provisions of various Acts administered by SARS that have been or will be amended by the Act. The Acts affected and the paragraphs of Schedule 1 that apply include the Transfer Duty Act, 1949 (paragraphs 1 to 11), Estate Duty Act, 1955 (paragraphs 12 to 22), Income Tax Act, 1962 (paragraphs 23 to 107), Value-Added Tax Act, 1991 (paragraphs 108 to 146), South African Revenue Service Act, 1997 (paragraph 147), Skills Development Levies Act, 1999 (paragraphs 148 to 156), Unemployment Insurance Contributions Act, 2002 (paragraphs 157 to 166), Diamond Export Levy (Administration) Act, 2007 (paragraphs 167 to 171), Securities Transfer Tax Administration Act, 2007 (paragraphs 172 to 179), Mineral and Petroleum Resources Royalty (Administration) Act, 2008 (paragraphs 183 to 192) and a number of amending Acts.

The new interest regime necessitated substantial changes to SARS' existing systems which were not finalised by 1 October 2012. As a result, most of the provisions of Chapter 12 of the Act that relate to the accrual of interest on tax debts or refunds, did not commence on that date. Consequently, until the commencement of the provisions contained in Chapter 12, the provisions of Schedule 1 to the Act that repeal, delete or amend the interest provisions of the other tax Acts regulating the accrual and calculation of interest, will not commence and these provisions of the other tax Acts remain in force.

7.10 VAT - Treatment of public authorities, grants – No. 39 (Issue 2)

This Note:

- sets out the VAT treatment of public authorities, grants and transfer payments and deals with the impact of the amendments in this regard which came into effect on 1 April 2005; and
- withdraws the first issue of Interpretation Note No. 39 dated 4 December 2007, as from 8 February 2013.

This Note intends to provide a clear framework for the application of the law, so that vendors who transact with government departments, public entities and municipalities will have clarity on the application of the Act before and after 1 April 2005 in respect of the following:

(a) The application of the zero rate in terms of section 11(2)(*p*) as it read before being deleted, as well as sections 11(2)(*n*), 11(2)(*s*), 11(2)(*t*) and 11(2)(*u*) which deal with certain payments made by or to public authorities, constitutional institutions and municipalities.

(b) The application of the deeming provisions in terms of sections 8(5), 8(5A) and 8(23) in respect of certain supplies and payments made by or to public authorities, designated entities and municipalities.

(c) The difficulties associated with the meaning of the term 'transfer payment' as it read before being deleted and the rationale for introducing the definition of a 'grant'.

(d) Determining whether or not an entity is a 'public authority', and consequently, whether that entity must register and account for VAT or not.

(e) Determining whether certain input tax and output tax adjustments are allowed to, or required by, public authorities.

8. DRAFT INTERPRETATION NOTES

8.1 Income Tax - Taxable benefit – use of employer-provided telephone or computer equipment or employer-funded telecommunication services

This Note provides clarity regarding:

- the determination of the value of the taxable benefit arising from the private or domestic use by an employee of employer-provided or employer-owned telephone or computer equipment (including cellular telephones, smartphones, laptops, tablets, modems, removable storage devices, printers and software) or telecommunication services; and
- the taxability of any allowance or reimbursement granted by the employer to the employee for the employee's privately-owned equipment or service contract which is used by the employee for purposes of the employer's business.

Employers often provide employees with telephones or computer equipment. The intention is that the employee will use the assets for work purposes, however given that the assets are often used outside of the office, some private or domestic use is inevitable.

Previously, the Seventh Schedule to the Act treated almost all private or domestic use by employees of employer-owned telephones and computer equipment and employer-provided telecommunication services as a taxable benefit under paragraphs 2(*b*) or 2(*e*).

The associated compliance and enforcement costs were potentially prohibitive and in 2008 the legislation was amended to provide that in certain circumstances an employee's private or domestic use will not be taxed. This Note discusses the circumstances when an employee's private or domestic use of these benefits will not be subject to taxation.

The Note focuses primarily on the following scenarios:

- Employer-owned (or leased) equipment and related services

  In this scenario the employer provides the employee with equipment or related services and incurs the associated cost. Two potentially taxable benefits arise, namely:

  - the private or domestic use of an employer-owned or provided asset [paragraph 2(*b*)]; and
  - access to and use of a telecommunication network (for example, line rental, call charges, data downloads) for private or domestic purposes at the employer's cost [which constitutes the provision of free or cheap services under paragraph 2(*e*)].

- Employee-owned (or leased) equipment and related services

  In this scenario the employee would typically have entered into a contract with a service provider for which the employee (and not the employer) has acquired the right to, for example, a cellular telephone (cell phone) or laptop and access to a telecommunication network. The contract with the service provider could take the form of a standard 24-month (or similar) contract between the employee and the service provider or a 'prepaid' (or similar) contract.

  The employer may require the employee to use his or her private contract or equipment during the course of the employee's employment for work purposes. Typically the employer would grant the employee an allowance or a reimbursement in order to defray the expenditure incurred for business purposes.

8.2 VAT – Vouchers supplied at a discount

This Note sets out the VAT implications of vouchers supplied at a discount.

It is common for vouchers to be supplied to customers for a consideration less than the monetary value stated on the voucher. In other words, the voucher is supplied at a discount.

The issue under consideration is whether VAT must be accounted for on the:

- discounted amount paid for the voucher; or
- the stated monetary value of the voucher,

when the voucher is used as payment for a supply of goods or services.

8.3 VAT – The supply of movable goods as contemplated in section 11(1)(a)(i), read with par. (a) of the definition of 'exported' and the corresponding documentary proof

The purpose of this Note is to:

- explain the requirements that need to be adhered to with regard to the direct export of movable goods; and
- prescribe the documentary proof, acceptable to SARS, that must be obtained and retained by a vendor;

in order to levy VAT at the zero rate on a supply of movable goods in terms of a sale or instalment credit agreement where those goods are consigned or delivered to a recipient at an address in an export country.

Interpretation Note No. 30 (Issue 2) 'Documentary Proof Required on Consignment or Delivery of Movable Goods to a Recipient at an Address in an Export Country' dated 15 March 2006 is hereby withdrawn. The effective date of Issue 3 is to be announced.

However, the following must be noted: All rulings issued taking into account the provisions of Interpretation Note No. 30 (Issue 2) dated 15 March 2006 remain in force until such rulings expire or are specifically withdrawn.

The South African VAT system is destination based, which means that only the consumption of goods and services in South Africa is taxed. VAT is therefore levied at the standard rate on the supply of goods or services in

South Africa as well as on the importation of goods into South Africa. Subject to certain requirements, VAT may be levied by a vendor at the zero rate where movable goods are exported from South Africa.

The term 'exported' as referred to in section 11(1)(*a*) is defined in section 1(1) of the VAT Act, amongst others, as follows:

> ' **'[E]xported'**, in relation to any movable goods supplied by any vendor under a sale or an instalment credit agreement, means –
>
> (*a*) consigned or delivered by the vendor to the recipient at an address in an export country as evidenced by documentary proof acceptable to SARS.'

In order for a vendor to supply movable goods (excluding second-hand movable goods where notional input tax was deducted on the acquisition of such goods) in terms of a sale or instalment credit agreement and levy VAT at the zero rate, the vendor must:

- consign or deliver the movable goods to the recipient at an address in an export country; and
- obtain and retain the required documentary proof as is acceptable to SARS.

This export is classified as a 'direct export' as the supplying vendor is in control of the export and ensures that the movable goods are exported from South Africa.

In instances where the movable goods are not exported by the vendor by means of a direct export, the provisions of the VAT Export Incentive Scheme (the Scheme) will find application.

This Note is only applicable to the direct export of movable goods. Under no circumstances will a vendor be able to levy VAT at the zero rate as contemplated in this Note on a supply of services.

8.4 Income Tax – Determination of the taxable income of certain persons from international transactions: Thin Capitalisation

This Note provides taxpayers with guidance on the application of the arm's length basis in the context of determining whether a taxpayer is thinly capitalised under section 31 and, if so, calculating taxable income without claiming a deduction for the expenditure incurred on the excessive portion of finance.

The guidance and examples provided are not an exhaustive discussion of every thin capitalisation issue that might arise. Each case will be decided on its own merits taking into account its specific facts and circumstances.

The application of the arms' length basis is inherently of a detailed factual nature and takes into account a wide range of factors particular to the specific taxpayer concerned. SARS has provided what it considers to be indicators of risk, acknowledging that the risk indicator may not constitute an arm's length position for a particular taxpayer or industry. SARS welcomes comments regarding this aspect as well as suggestions of areas for further guidance (including views on what that guidance may be) and indeed any aspect of this Note. Comments should be submitted by 30 June 2013.

Practice Note No. 2 of 14 May 1996 'Income Tax: Determination of Taxable Income where Financial Assistance has been Granted by a Non-resident of South Africa to a Resident of South Africa' and its Addendum of 17 May 2002 are withdrawn by this Note for years of assessment commencing on or after 1 April 2012. The practice note remains applicable to transactions that fall within the ambit of section 31(3) for years of assessment commencing before 1 April 2012.

Taxpayers are broadly financed in two ways, namely through the use of equity and debt. The returns on equity capital and debt capital are treated differently for tax purposes. Interest payments incurred in the production of income by a person carrying on a trade are, subject to certain conditions

and restrictions, deductible in determining taxable income while distributions of profits (whether in the form of dividends or returns of capital) are not deductible.

The way in which a taxpayer is financed has an impact on the calculation of the taxpayer's taxable income. This raises tax concerns regarding the balance between the amount of equity capital and debt capital. A taxpayer which is considered to have too little equity when considered against the amount of its debt is said to be thinly capitalised for tax purposes.

Thin capitalisation typically becomes an issue in cases where a South African taxpayer is funded either directly or indirectly by non-resident connected persons. The funding of a South African taxpayer with excessive intra-group, back-to-back or intra-group-guaranteed debt may result in excessive interest deductions thereby depleting the South African tax base.

South Africa introduced thin capitalisation rules in 1995. Under these rules, which were contained in section 31(3), SARS was empowered to have regard to the international financial assistance rendered and if it was considered excessive in proportion to the particular lender's fixed capital in the borrower, the interest, finance charges or other consideration relating to the excessive financial assistance was disallowed. SARS' views on what constituted excessive international financial assistance were documented in Practice Note No. 2 of 14 May 1996. These rules and Practice Note No. 2 have been repealed and are only applicable to years of assessment commencing before 1 April 2012.

For years of assessment commencing on or after 1 April 2012, thin capitalisation is no longer dealt with by a separate subsection of section 31 and is instead governed by the general transfer pricing provisions of subsection 31(2).

One of the most significant changes is that taxpayers must determine the acceptable amount of debt on an arm's length basis. The arm's length basis will be discussed further in this Note.

This Note deals with the provisions of section 31 which, as noted above, are applicable for years of assessment commencing on or after 1 April

2012. For example, in the case of a year of assessment ending on 31 December, the first year of assessment to which the new legislation will apply is the year of assessment commencing on 1 January 2013 and ending on 31 December 2013.

8.5 Income tax – Deductibility of expenditure and losses arising from embezzlement or theft of money

This Note provides guidance on:

- the deductibility of expenditure and losses incurred in a taxpayer's trade as a result of the embezzlement or theft of money, including expenditure incurred on legal and forensic services to investigate such losses; and
- the taxation of stolen money in the hands of the thief.

Taxpayers may incur expenditure and losses during the course of their business activities as a result of embezzlement or theft of money by, for example, employees, directors, shareholders, partners, burglars or armed robbers. As a consequence, these taxpayers may also incur expenditure pertaining to legal and forensic services to investigate such losses.

The embezzlement or theft of money has income tax implications for both the victim and the thief.

Expenditure and losses incurred by a taxpayer in carrying on a trade as a result of embezzlement or theft of money and any legal and forensic expenditure incurred in investigating the crime will qualify as a deduction in determining taxable income provided it meets the requirements of section 11(*a*) or in the case of legal expenses, section 11(*c*). An important factor in determining the deductibility of the expense or loss will be whether the risk of its incurral was a necessary incident of the taxpayer's trade.

A person who derives funds illegally, whether by embezzlement or theft, is regarded as having 'received' those funds for the purposes of the definition

of the term ‘gross income’ in section 1(1) and will be subject to income tax on those funds.

8.6 Determining a ‘group of companies’ for purposes of the Corporate Rules contained in Part III of Chapter II of the Act

This Note provides guidance on the interaction of the definitions of a ‘group of companies’ contained in sections 1(1) and 41(1).

The corporate rules contain, amongst other things, special provisions relating to the income tax consequences (including capital gains tax consequences) of transactions between companies forming part of a ‘group of companies’. Under qualifying circumstances, the corporate rules make it possible for companies in such a group of companies to transfer assets between each other without adverse tax consequences.

The Act contains two definitions of a ‘group of companies’, namely, a general definition in section 1(1) which generally applies to the Act as a whole and a narrower definition in section 41(1) which applies to the corporate rules and a limited number of other provisions in the Act. The definition in section 41(1) excludes certain companies which might otherwise have qualified for relief under the corporate rules.

8.7 Deduction of expenditure incurred on repairs

This Note provides guidance on the interpretation and application of section 11(*d*) which allows a deduction for expenditure incurred on repairs for the purposes of trade.

Expenditure on repairs to an asset not comprising trading stock is likely to be of a capital nature, particularly when it is not incurred at regular intervals. This is because the expenditure relates to the protection of a capital asset.

Expenditure of a capital nature does not qualify as a general deduction under section 11(*a*). Nevertheless, section 11(*d*) makes provision for the deduction of expenditure incurred on repairs for the purposes of trade provided the requirements are met.

For purposes of section 11(*d*) it is important to distinguish between a 'repair' and an 'improvement' since only expenditure incurred on repairs is deductible under section 11(*d*). No hard and fast rules can be provided for this distinction. Each case must be decided on its own facts.

In order for an asset to be repaired, there must be damage or deterioration to a part of the original asset or structure and the intention of the taxpayer must be to restore the asset or structure to its original condition. Because there are no set criteria as to what constitutes a repair and only principles derived from case law, each case will have to be determined on its merits.

8.8 Tax treatment of tips for recipients, employers and patrons

This Note discusses and clarifies the potential income tax, SDL and UIF implications in respect of the receipt of tips encountered in (but not limited to) the service industry. The Note will focus on a 'tripartite' tipping relationship between the following three parties:

- The patron
- The recipient
- The owner

For example, a customer (the patron) pays a waitron (the recipient) a tip for excellent service in a restaurant owned and operated by the owner. In some circumstances, the owner may also pay the recipient a tip in his own capacity.

The Note considers an employee's potential obligation to include the receipt of tips in gross income and his related provisional tax and UIF responsibilities. It also considers the owner and a patron's possible

obligations to withhold employees' tax on such tips and to account for SDL and UIF.

The Note does not deal with compulsory service charges which are added by the owner to a patron's bill (for example, adding a 10% service fee to a restaurant bill for tables of greater than eight guests). Service charges are generally received by the owner for his own benefit and included in that owner's gross income.

9. BINDING PRIVATE RULINGS

9.1 BPR 130 – Sale of mining rights and the respective base cost of each mining right

This ruling deals with the capital gains tax consequences arising from the sale of mining rights.

In this ruling references to sections and paragraphs are to sections of the Act and paragraphs of the Eighth Schedule to the Act applicable as at 9 March 2012 and unless the context indicates otherwise, any word or expression in this ruling bears the meaning ascribed to it in the Act.

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

- section 1(1), definition of 'gross income'; and
- paragraphs 1, 3, 4, 11, 20, 33, 35 and 38 of the Eighth Schedule.

Parties to the proposed transaction

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

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

Description of the proposed transaction

The Applicant is in the business of mining and selling of minerals.

The Applicant initially obtained mining rights from a 'connected person' as defined in section 1(1) and accordingly treated the transaction under paragraph 38 of the Eighth Schedule. The result of applying paragraph 38 was that the connected person included the market value of the assets as proceeds and the Applicant acquired the mining rights at the same market value.

The Applicant intends to sell the mining rights which it initially acquired from the connected person (mining right no's. 1 and 2), as well as other prospecting and mining rights awarded to it by the Department of Mineral Affairs (mining right no's. 3, 4 and 5).

In terms of the proposed sale agreement the Applicant will dispose of mining right no's. 1, 2, 4 and 5, and a portion of mining right no. 3, under section 11 of the Mineral and Petroleum Resources Development Act No. 28 of 2002.

The Applicant proposes to apportion the proceeds of the sale in accordance with the surface area linked to each mining right, as it relates to the total hectares of all surface areas included in the transaction (the 'surface area apportion method').

The proposed transaction will only relate to the mining rights and not the surface area or land itself. The Applicant will retain ownership of the land and will merely allow the purchaser access to the land in order to exploit the mining rights so acquired.

Conditions and assumptions

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

Ruling

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

- The proceeds which will arise from the proposed transaction will be of a capital nature and subject to the provisions of the Eighth Schedule.
- Each mining right to be disposed of in the proposed transaction will be regarded as an individual 'asset', as defined in paragraph 1 of the Eighth Schedule.

- The ‘surface area apportionment method’ will not be regarded as an appropriate method for allocating the proceeds of the sale to the individual mining rights disposed of.
- The base cost of mining right no’s. 1 and 2, initially acquired from the connected person, will be the respective market value as established under paragraph 38 of the Eighth Schedule on the acquisition date thereof.
- The base cost of mining right no. 3, relating to the sale of a portion of that mining right, will be the proportionate market value thereof established under paragraphs 38 and 33 of the Eighth Schedule.
- The base cost of mining right no’s. 4 and 5 will be the amount incurred in creating these mining rights, as provided for in paragraph 20 of the Eighth Schedule.

9.2 BPR 131 – Vesting date of a restricted equity instrument

This ruling deals with the vesting date of a restricted equity instrument acquired by employees in respect of their employment.

In this ruling references to sections and paragraphs are to sections of the Act and paragraphs of the Fourth Schedule to the Act applicable as at 18 September 2012 and unless the context indicates otherwise, any word or expression in this ruling bears the meaning ascribed to it in the Act.

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

- section 8C; and
- paragraphs 2 and 11(A) of the Fourth Schedule.

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

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

The Holding Corporation: A company incorporated in Jersey which is the holding company for a group of companies including the Applicant (the Group)

Qualifying employees: Eligible directors and employees within the Group

Description of the proposed transaction

The Holding Corporation (the Corporation) is a company incorporated in Jersey, and listed on the Alternative Investment Market of the London Stock Exchange.

The Corporation has a Share Option Scheme (the Scheme) in place which has been adopted by the Board of Directors.

In terms of the rules of the Scheme, options are granted to eligible directors and employees within the Group.2

An option entitles a Qualifying employee to acquire shares in the Corporation upon exercise of the option.

An option is personal to a Qualifying employee and cannot be transferred, changed or otherwise disposed of by him/her and shall lapse immediately if the Qualifying employee purports to transfer, change or otherwise dispose of the option.

Subject to the rules of the Scheme, an option may not be exercised earlier than the latest of

- three years after the date granted; or
- the date on which a committee determines that the required performance conditions have been satisfied.

An option is exercised by a Qualifying employee upon delivery of a duly completed notice of exercise to the company, accompanied by the full payment of the exercise price for the shares for which the option is being exercised.

Conditions and assumptions

This ruling is subject to the additional condition that it only applies to instances where a Qualifying employee exercises his/her option and does

not deal with any eventuality which may occur thereafter during the existence of the Scheme.

Ruling

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

- The options granted under the Scheme rules will each constitute a ‘restricted equity instrument’, as defined in section 8C(7).
- The options will terminate as a result of their exercise and will not vest.
- Any shares acquired in the Corporation by a Qualifying employee will be unrestricted equity instruments. The aforementioned shares will vest at the time of acquisition, as contemplated in section 8C(3)*(a)*, when all the terms and conditions of the scheme have been fulfilled.
- A gain will only be included in the income of a Qualifying employee when an event contemplated in the aforementioned paragraph occurs. No obligation to withhold employees’ tax will exist prior to such an event.

9.3 BPR 132 – Disposal of a business as a going concern by a trust to a company in exchange for shares in the company

This ruling deals with the disposal of a business as a going concern by a trust to a company, in exchange for shares in the company, and whether the transaction will qualify for the relief provided for under section 42 of the Act.

In this ruling references to sections and paragraphs are to sections of the Act and paragraphs of the Eighth Schedule to the Act applicable as at 1 October 2012 and unless the context indicates otherwise, any word or expression in this ruling bears the meaning ascribed to it in the Act.

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

- section 41(2);
- section 42; and
- paragraphs 11(*g*) and 12(5) of the Eighth Schedule.

Parties to the proposed transaction

The Applicant: A trust established in and a resident of South Africa

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

Description of the proposed transaction

The Applicant (the Trust) operates a game farming business (the Business) on land co-owned by the beneficiaries of the Trust, the Co-Applicant and another company also incorporated in and a resident of South Africa.

The Business has become very successful since being established, far exceeding the original expectations of the founders of the Trust. The everyday management of the Business within the Trust's environment has, however, become cumbersome and complex.

The Trustees agreed that the existing structure of the Business should be transferred to a company, and the Co-Applicant was identified as the preferred vehicle for this transaction.

Ruling

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

- The disposal of the Business as a going concern, by the Applicant to the Co-Applicant, will constitute an asset-for-share transaction as envisaged in section 42.
- The provisions of paragraphs 11(1)(*g*) and 12(5) of the Eighth Schedule will not apply as a result of the provisions of section 41(2).
- No ruling is issued on the application of *Part V* of Chapter II of the Act.

9.4 BPR 133 – Transfer of a residence out of a company to a natural person

This ruling deals with the capital gains tax and transfer duty consequences, for both the transferor and transferee, in respect of a residence to be transferred out of a company to a natural person who is a qualified transferee for purposes of the relief measures provided for under the relevant legislation.

In this ruling references to sections and paragraphs are to sections of the Act and paragraphs of the Eighth Schedule to the Act applicable as at 4 October 2012 and unless the context indicates otherwise, any word or expression in this ruling bears the meaning ascribed to it in the relevant Act.

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

- section 64FA(1)(*c*);
- paragraph 51A of the Eighth Schedule; and
- section 9(20) of the Transfer Duty Act

Parties to the proposed transaction

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

Co-Applicant 1 A company incorporated in a foreign country, and not a resident of South Africa, that holds 100% of the share capital of the Applicant 2

Co-Applicant 2 A natural person who is a resident of South Africa, but who lives abroad, and holds 100% of the share capital of Co-Applicant 1

Description of the proposed transaction

Co-Applicant 2 purchased the property in December 1996 in the name of the Applicant. The purchase price was funded by way of shares that had been issued to Co-Applicant 1 to an amount of R599 401. The only asset held by the Applicant is the property and the only asset held by Co-Applicant 1 is the share capital of the Applicant.

Co-Applicant 2 has had the right to use the property since acquisition and at all material times he incurred the expenditure required for the property's maintenance. At times he let the property at arms' length as holiday accommodation to generate funds to enable him to defray expenses in relation to the property. Between 11 February 2009 and 31 May 2012, the property was so rented out for a total of 483 days, that is, for 40% of that time period. Accordingly, Co-Applicant 2 used the property for domestic purposes during the same period for 60% of the time.

No holding costs (as contemplated in paragraph 20 of the Eighth Schedule) or selling expenditure have been incurred by the Applicant in respect of the property after 1 October 2001 for purposes of adding such costs to the Applicant's base cost (as determined under Part V of the Eighth Schedule) of the property. A market value of R 900 000 was determined as valuation date value as at 1 October 2001. A decision was made, however, (under paragraph 26 of the Eighth Schedule) to determine the base cost of the property by using the time-apportionment method (as provided for in paragraph 30 of the Eighth Schedule), as this method yielded the more favourable result for the parties to the proposed transaction.

The present market value of the property is R2 750 000. The time-apportioned base cost is calculated as follows:

The initial purchase price = 599 401

Add: Portion of the accounting profit relating to the pre-valuation and post valuation date period (Present market value – base cost = accounting profit

R 2 750 000 – R 599 401 = R 2 150 599)

5/16 x R2 150 299 = 672 062

Base cost = 1 271 463

It is proposed that the Applicant dispose of the property to Co-Applicant 1 by way of a dividend *in specie*. The property will then be disposed of by Co-Applicant 1 to Co-Applicant 2 by way of a further dividend *in specie*. In terms of the proposal both distributions are to take place before 31 December 2012.

Conditions and assumptions

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

- Once the distribution of the property has taken place, the respective companies making the distribution will be wound up and deregistered. The steps to do so, as contemplated in section 41(4) of the Act, must be taken by each of them respectively within a period of less than six months of the proposed distribution.
- The distributions referred to in the rulings must both take place before 31 December 2012.

Ruling

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

- The proposed distribution of the property by way of a dividend *in specie* from the Applicant to Co-Applicant 1, and from Co-Applicant 1 to Co-Applicant 2 also by way of a dividend *in specie,* will be a disposal as contemplated in paragraph 51A of the Eighth Schedule to the Act.
- The Applicant and Co-Applicant 1 must be treated as if each of them disposed of the property at its base cost at the time of the disposal, being R1 271 463.
- Co-Applicant 2, the Applicant and Co-Applicant 1 must be treated as one and the same person with regard to:
    - the date of acquisition of the property own by the Applicant;
    - the amount and date of incurral by the Applicant of any expenditure in respect of the property allowable under paragraph 20 of the Eighth Schedule to the Act; and
    - any valuation of the property effected by the Applicant under paragraph 29(4) of the Eighth Schedule to the Act to determine the market value of the property on valuation date (1 October 2001).
- Neither distribution of the property will attract transfer duty.

- Neither distribution of the property will attract dividends tax.

9.5 BPR 134 – Exemption under section 10B(2)(a) in relation to a foreign dividend that is deemed to be received by a person who is a resident

This ruling deals with the income tax consequences with regard to an election made by a person under section 4(1) of the Amnesty Act that deemed the person to be the holder of any foreign asset which was held on 28 February 2003 by a discretionary trust which is not a resident of South Africa.

In this ruling references to sections are to sections of the relevant Act applicable as at 20 September 2012 and unless the context indicates otherwise, any word or expression in this ruling bears the meaning ascribed to it in that Act.

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

- section 10B(2)(*a*) of the Act; and
- section 4 of the Amnesty Act.

Parties to the proposed transactions

The Applicant: An individual who is a resident of South Africa

The Trust: A discretionary trust that is not a resident of South Africa, established by the Applicant for the benefit of the Applicant and his family

Foreign Co: A company that is not a resident of South Africa that holds various investments outside South Africa

Description of the proposed transactions

The Applicant was the donor in relation to the Trust. The Trust owns 100% of the shares in Foreign Co. The trustee of the Trust intends to simplify the investment holding structure of the assets held by the Trust through Foreign Co by removing Foreign Co from the structure. To this end the trustee

intends ensuring that Foreign Co will distribute all of its assets to the Trust as a dividend *in specie*.

The Applicant applied for amnesty previously and made the election contemplated in section 4(1) of the Amnesty Act. As a result, for the purposes of the Act, the shares in Foreign Co are deemed to be held by the Applicant. Dividends will be deemed to be received by the Applicant.

Conditions and assumptions

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

- The proposed transaction is not part of or connected with any other transaction, operation or scheme, other than as set out in the application for the ruling.
- The distribution by Foreign Co of all of its assets as a dividend *in specie* to the Trust will be a 'foreign dividend' as defined in section 10B(1) of the Act.

Ruling

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

- The distribution by Foreign Co of all of its assets as a dividend *in specie* to the Trust will result in a foreign dividend being deemed to be received by the Applicant.
- This foreign dividend will be exempt from normal tax in the hands of the Applicant under section 10B(2)(*a*) of the Act.

9.6 BPR 135 – Improvements effected on land in terms of a long term lease

This ruling deals with the income tax consequences, for both the lessor and the lessee, resulting from a long term lease agreement in terms of which the lessee will be obliged to effect improvements on immovable property

without any claim for either compensation for the improvements or for the removal thereof upon termination of the lease.

In this ruling references to sections are to sections of the Act applicable as at 30 August 2012 and unless the context indicates otherwise, any word or expression in this ruling bears the meaning ascribed to it in the Act.

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

- section 1(1), definition of the term 'gross income' paragraph (*h*);
- section 11(*g*); and
- section 11(*h*).

Parties to the proposed transaction

The Applicant: A subsidiary company incorporated in and a resident of South Africa that will acquire land from a fellow subsidiary company

The Co-Applicant: A company incorporated in and a resident of South Africa, that will lease the land from the Applicant and effect improvements thereon in accordance with contractual terms that will be embodied in a long term lease agreement

Description of the proposed transaction

The Applicant intends to acquire a portion of a farm which has already been subdivided. The farm is owned by a fellow subsidiary company in relation to the Applicant, but it is subject to a perpetual lease in favour of a religious and charitable institution. The institution is approved by SARS for the South African Revenue Service as a public benefit organization under section 30.

The subdivision will be sold to the Applicant at a nominal price because of the burden of the perpetual lease. The perpetual lease in respect of this portion is to be cancelled thereafter which will facilitate the conclusion of a long-term lease agreement between the Applicant and the Co-Applicant. The reason for this transaction is that the parties consider it inappropriate, on religious grounds, for the institution to undertake the development itself. The salient terms of the lease agreement will be as follows:

- The Applicant will lease the portion to the Co-Applicant for a 99 year period, but the Co-Applicant may (because of a provision of religious law which the parties consider would govern this transaction), terminate the lease at its option, though not for a period of 63 years from the date when the lease takes effect. Thereafter this option may be exercised at any time during subsequent three year cycles.
- The Co-Applicant will be obliged to effect improvements on the portion of land to a minimum specified value, by not later than a specified date. These improvements will be at the Co-Applicants own cost and comprise a commercial property.
- Neither the total value of the improvements, nor the date at which all improvements must be completed, is specified. The Co-Applicant is, therefore, entitled to effect improvements beyond the specified date and agreed minimum amount.
- The Co-Applicant will not be obliged to secure the Applicant's prior approval of the plans for the improvements. The Applicant must, however, approve a master development plan and the Co-Applicant must adhere to it. The Applicant must also consent to the commencement of construction, but may not withhold its consent unreasonably.
- The Co-Applicant must complete the construction within a construction period to be indicated in a time table to be submitted in terms of the lease agreement, which further provides that in submitting plans and specifications to the Applicant and Property Association (if any) for approval, the Co-Applicant must include an indication of the construction period required to complete the improvements and time table of material target dates for commencement of construction to practical completion of the improvements.
- The Co-Applicant will lease the improvements, once effected, to tenants for the duration of the lease.

- The Co-Applicant will not be entitled to any compensation for the improvements upon the lapsing, cancellation or expiry of the lease agreement.

<u>Ruling</u>

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

- The Applicant must include the fair and reasonable value of all improvements effected by the Co-Applicant in its gross income, as contemplated in paragraph (*h*)(ii) of the definition of 'gross income' in section 1(1).
- The Applicant will be entitled to an allowance under section 11(*h*), determined by using the present value of the actual development costs arising out of the performance of the Co-Applicant's obligations under the lease agreement, discounted at the rate of 6% over the 99 year period of the lease.
- The Co-Applicant will be entitled to an allowance over a 25 year term in respect of any expenditure actually incurred, as contemplated in section 11(*g*), if the improvements are occupied for the production of the Co-Applicant's income or the Co-Applicant derives income there from.
- In the event that the lease agreement is terminated before the expiry of the full 25 year term during which the section 11(*g*) allowance may be claimed, the unredeemed balance of the allowance at the termination date may be deducted by the Co-Applicant from its

9.7 BPR 136 – Taxation of subsistence allowances paid to employees

This ruling deals with subsistence allowances paid by an employer to its employees and the amount of the allowance that will be deemed to have been expended under section 8(1)(*a*)(i)(*bb*) read with section 8(1)(*c*) of the Act.

In this ruling references to sections are to sections of the Act applicable as at 14 January 2013 and unless the context indicates otherwise, any word or expression in this ruling bears the meaning ascribed to it in the Act.

This is a ruling on the interpretation and application of the provisions of section 8(1)*(a)*(i)(*bb*) read with section 8(1)*(c)*.

Parties to the proposed transaction

The Applicant: An employer providing subsistence and travel benefits to its employees in respect of local travel for business purposes

The Employees: Employees of the Applicant

Description of the proposed transaction

The Applicant has a subsistence and travel policy (the policy), in terms of which the Applicant will pay employees, who are required to spend at least one night away from their usual place of residence on local travel for business purposes, an allowance for each night away to cover personal expenses such as meals, refreshments, laundry and room service. The allowance is equal to 80 percent of the Gazetted amount contemplated in section 8(1)(*c*), regardless of whether the cost for accommodation includes breakfast or not.

'Subsistence' is defined in the policy as an allowance that the Applicant will pay to employees in order to cover their meals and incidental costs while away from their usual place of residence for business purposes. The allowance is specifically not for accommodation, since the Applicant will arrange and pay for the accommodation separately. Some of the accommodation establishments include breakfast whilst others do not.

The policy does not apply to employees who are constantly away from their usual place of residence because they are required to render services on the Applicant's offsite facilities situated far from their usual place of residence.

In terms of the policy, when an employee is away for a day but not a night, no subsistence allowance is payable.

Ruling

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

For the purposes of section 8(1)*(a)*(i)*(bb)*:

- An allowance paid by the Applicant in terms of the policy, which amount is less than the *Gazetted* amount contemplated in section 8(1)*(c)*(ii), will fall within the deeming provisions of section 8(1)*(c)*(ii) only when the Applicant has not borne any of the expenses in respect of which the allowance is paid.
- If the Applicant bears any of the expenses in respect of which the allowance is payable, the maximum amount deemed to be expended under section 8(1)*(c)*(ii) will be the *Gazetted* amount, reduced by the amount of expenses borne by the Applicant. For example, in determining the maximum amount that will be deemed to be expended under section 8(1)*(c)*(ii), the *Gazetted* amount must be reduced by the breakfast charge when the accommodation paid for by the Applicant includes breakfast as a separate charge.
- This ruling is not applicable to subsistence allowance paid in respect of employees that are constantly away from their usual place of residence due to the nature of the business of the Applicant, such as employees at the Applicant's offsite facilities.
- This ruling is also not applicable to subsistence allowance paid in respect of travel outside South Africa for business purposes.

9.8 BPR 137 – Sale of business in terms of an intra-group transaction

This ruling concerns the sale of a business in terms of an intra-group transaction and whether:

- the sale can be seen as a transaction relating to a liquidation, winding-up and deregistration as envisaged under section 47 of the Act; and

- certain assets may be excluded from the ambit of section 45 of the Act where a business is sold.

In this ruling references to sections are to sections of the Act applicable as at 16 January 2013 and unless the context indicates otherwise, any word or expression in this ruling bears the meaning ascribed to it in the Act.

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

- section 45(6)(*e*) and (*g*); and
- section 47.

Parties to the proposed transaction

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

The Co–Applicant: A company incorporated in and a resident of South Africa that holds 100% of the shareholding in the Applicant

Description of the proposed transaction

The Co-Applicant purchases and distributes goods manufactured by the Applicant. The Applicant has long-term loan financing from offshore companies (who are shareholders in the Co-Applicant). This loan financing was obtained for the purpose of financing the construction of the Applicant's manufacturing plant and funding the working capital of its operations. The interest on this loan is currently deducted in terms of section 24J. This loan will be assumed by the Co-Applicant as part of a restructure, set out below.

The shareholders have agreed to combine the Co-Applicant and the Applicant. As part of the combination of the Co-Applicant and the Applicant, the shareholders intend to move the Applicant's business to the Co-Applicant in order to improve the current supply chain.

Both the Co-Applicant and the Applicant have incurred significant tax losses since inception – for the Applicant it is due largely to the accelerated depreciation allowances on its manufacturing assets, and for the Co-applicant it is due largely to the high cost of the procurement of the Applicant's products.

It has been proposed that the supply chain between the Applicant and the Co-Applicant be removed by transferring the Applicant's business to the Co-Applicant.

The Applicant and the Co-Applicant will enter into a sale of business agreement, wherein the Applicant agrees to sell its business as a going concern to the Co-Applicant. Accordingly, all assets are purchased and liabilities are delegated to the Co-Applicant in terms of this agreement (some minor assets may remain to settle debts). It is envisaged that the sale of business qualifies as an intra-group transaction, as contemplated in section 45.

At the time that the proposed transaction, which is the subject of this ruling, will take place, the Applicant will be 100% held by the Co-Applicant.

As it is likely that section 45 will automatically apply to the transfer of the assets, an agreement envisaged in section 45(6)(*g*) will be included in the sale of business agreement that will provide for the 'election' out of the operation of section 45 in respect of certain assets, to be identified at a later date, but such date to be before the completion date of the contract.

The net purchase consideration for the business will be left outstanding on loan account, although this may be repaid in due course.

<u>Conditions and assumptions</u>

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

- A directors' resolution will be passed to approve the transfer of the assets through a sale of the assets.
- The Co-Applicant and the Applicant will form part of the same group of companies at the time of the sale of the business.
- Capital assets to be disposed of by Applicant will be held as capital assets by Co-Applicant.
- Trading stock to be disposed of by Applicant will be held as trading stock by Co-Applicant.

- The Applicant will not take steps to liquidate, deregister or unwind within a period of 36 months from the time the sale of business agreement is implemented.
- The Applicant and Co-Applicant will elect, in terms of section 45(6)(*g*), that section 45 will not apply to certain assets to be sold in terms of this transaction.
- To the extent that section 23K applies to the shareholder loans, it is assumed that a directive, as envisaged in that section, will be sought and obtained from SARS for SARS. This binding private ruling does not constitute a directive under section 23K.
- The interest deduction claimed by the Applicant in the past was fully deductible under section 24J or 11(*a*), taking into account the provisions of section 31.
- The loans will be transferred at face value which will equal the then market value.
- The provisions of section 31 have not been considered.

<u>Ruling</u>

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

- To the extent that assets are not elected out of section 45 under section 45(6)(*g*), the sale of these assets and liabilities by the Applicant to the Co-Applicant will constitute an intra-group transaction as contemplated in section 45.
- Section 47 will not apply to the sale of assets to the Co-Applicant, as it is not the intention of the parties to liquidate, wind up or deregister the Applicant. The assets are accordingly not disposed of in terms of a liquidation distribution referred to in section 47, hence section 45(6)(*e*) will apply to this disposal.
- To the extent that loans are transferred from the Applicant to the Co-Applicant, and where interest paid was deductible by the Applicant on

these loans, interest paid by the Co-Applicant, going forward, will be deductible on these loans.

9.9 BPR 138 – Subscription for shares at nominal values coupled to a repurchase agreement at

This ruling deals with the income tax consequences relating to a subscription for shares at nominal values and the repurchasing of those shares in the future for the same nominal values.

In this ruling references to sections and paragraphs are to sections of the Act and paragraphs of the Eighth Schedule to the Act applicable as at 20 December 2012 and unless the context indicates otherwise, any word or expression in this ruling bears the meaning ascribed to it in the Act.

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

- section 24J;
- section 42;
- section 58; and
- paragraph 38 of the Eighth Schedule.

Parties to the proposed transaction

The Applicant: A company that is the controlling group company, the shares of which are listed on the Johannesburg Stock exchange

The Co-Applicants: Empowerco, a controlled group company to be used as a special purpose vehicle to hold empowerment shares in the Applicant

Employee Trust, an employee share ownership scheme trust, the beneficiaries of which are black employees of the Applicant's group of companies 2

Description of the proposed transaction

The Applicant proposes to enter into a Broad Based Black Economic Empowerment (BBBEE) transaction in terms of which it will transfer

ownership of shares in itself, representing a portion of its South African (SA) operations, to its black employees through the Employee Trust.

A summary of the proposed transaction is set out in the steps below:

- The Applicant will issue a new class of shares (class B shares) to Empowerco under section 42, representing 20% of its SA operations.
- Empowerco and the Employee Trust will enter into a 'share issue and repurchase agreement' in terms of which Empowerco will issue shares to the Employee Trust, equalling 50.1% of its ordinary shares, at a nominal value. It will be a term of issue of these shares that Empowerco will have an option to repurchase some of the shares at the end of a 10 year lock-in period at the same nominal value. The number of shares to be repurchased will be based on a compound growth formula.
- The remaining Empowerco shares held by the Employee Trust after execution of the repurchase agreement will be distributed by the Employee Trust to its beneficiaries, subject to a disposal restriction for a period of 7 days.
- During the 7 day restriction period the Empowerco shares will be exchanged under section 42 for listed shares in the Applicant.

Ruling

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

- The subscription of shares in Empowerco by the Employee Trust will not be deemed to have been disposed of under a donation by Empowerco, as envisaged in section 58(1).
- Section 24J will not be applicable to the share issue and repurchase agreement to be entered into by Empowerco and the Employee Trust and thus no interest will have to be accounted for by the parties.
- When Empowerco repurchases the shares from the Employee Trust in terms of the repurchase agreement, no capital gain will arise from the disposal of these shares by the Employee Trust as the proceeds from the disposal will equal the acquisition cost of the shares.

Paragraph 38 of the Eighth Schedule will not be applicable to the disposal of these shares by the Employee Trust.

9.10 BPR 139 – Disposal of assets by a recreational club

This ruling deals with the capital gains tax consequences and the roll over relief provided for under paragraph 65B of the Eighth Schedule in respect of the disposal of some of the assets held by a recreational club and the utilisation of the total proceeds to acquire replacement assets.

In this ruling references to paragraphs are to paragraphs of the Eighth Schedule to the Act applicable as at 12 February 2013 and unless the context indicates otherwise, any word or expression in this ruling bears the meaning ascribed to it in the Act.

This is a ruling on the interpretation and application of the provisions of paragraph 65B of the Eighth Schedule.

Parties to the proposed transaction

The Applicant: A recreational club approved under section 30A of the Act.

Description of the proposed transaction

The Applicant owns various properties which are utilised for social and recreational purposes.

The Applicant is embarking on an upgrade of its facilities and intends to dispose of certain portions of its properties (the properties) currently housing certain facilities which are mainly used by the members of the Applicant.

The proceeds derived from the sale of the properties will be utilised for purposes of developing new facilities on the remainder of its properties which will also be used mainly by the members of the Applicant.

Conditions and assumptions

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

- The Applicant will elect that paragraph 65B of the Eighth Schedule applies.
- The properties to be disposed of (and the relevant buildings situated thereon) were used mainly for purposes of providing social and recreational amenities to the members of the Applicant.
- The assets to be acquired will constitute replacement assets as envisaged by paragraph 65B of the Eighth Schedule.
- The proceeds from the disposal of the properties will be equal to or exceed the base cost of the respective properties and an amount at least equal to the proceeds on the disposal will be expended to acquire one or more replacement assets.
- The contracts for the acquisition of the replacement assets will be concluded within a period of 12 months after the date of the disposal of the properties.
- The replacement assets will be brought into use within a period of 3 years from the date of disposal of the properties.
- The replacement assets will be used mainly by members of the Applicant for social and recreational activities.

Ruling

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

- Any capital gain determined in respect of the disposal of the properties must be disregarded when determining the Applicant's aggregate capital gain or aggregate capital loss

9.11 BPR 140 – Unbundling Transactions

This ruling deals with an unbundling transaction with specific reference to the application of section 46(1), (7) and (8) of the Act.

In this ruling references to sections are to sections of the Act applicable as at 08 February 2013 and unless the context indicates otherwise, any word or expression in this ruling bears the meaning ascribed to it in the Act.

This is a ruling on the interpretation and application of the provisions of section 46.

Parties to the proposed transaction

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

The Co-Applicant: An investment holding company incorporated in and a resident of South Africa

The Unbundled Companies: Nine companies that are wholly owned subsidiaries of the Applicant, one of which is not a resident of South Africa

Description of the proposed transaction

The Applicant and Co-Applicant form part of the same group of companies. The Co-Applicant is a wholly owned subsidiary of an investment holding company that is not a resident of South Africa (non-resident shareholder).

The non-resident shareholder wishes to establish a headquarter company for its African investments. As a result of the Applicant and Co-Applicant's presence in South Africa as well as South Africa's headquarter holding company regime, the parties intend to establish a headquarter company in South Africa.

In order to establish such a headquarter company in South Africa the following steps are envisaged for the proposed transaction:

- In year one the Applicant will distribute all the shares held in the Unbundled Companies to the Co-Applicant in terms of an unbundling transaction.
- In year two the Co-Applicant will elect under section 9I to be a 'headquarter company' as defined in section 1(1).

Conditions and assumptions

This ruling is subject to the additional condition and assumption that, at the time of the unbundling transaction, the Co-Applicant is not a ‘disqualified person’ as defined in section 46(7)(*b*).

Ruling

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

- The proposed distribution by the Applicant of the shares held in the Unbundled Companies to the Co-Applicant will be an ‘unbundling transaction’ as defined in section 46(1).
- Section 46 will apply to the proposed distribution, provided that an election contemplated in section 46(8) is not made by the Applicant and the Co-Applicant.

9.12 BPR 141 – Transaction of securities from an untaxed policyholder fund or another long-term insurer

This ruling deals with the question as to whether the transfer of securities from an untaxed policyholder fund (UPF) of one long-term insurer to a UPF of another long-term insurer will be exempt from securities transfer tax.

In this ruling references to sections are to sections of the relevant Act applicable as at 18 December 2012 and unless the context indicates otherwise, any word or expression in this ruling bears the meaning ascribed to it in that Act.

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

- sections 41 and 45 of the Act; and
- section 8(1)(*a*)(iii) of the STT Act.

Parties to the proposed transaction

The Applicant: A registered long-term insurance company that is a resident of South Africa

The Co-Applicant: Another registered long-term insurance company that is a resident of South Africa

Description of the proposed transaction

The Applicant and Co-Applicant are wholly owned subsidiaries of Holdco. As part of restructuring of the group, Holdco proposes to transfer the business of the Applicant to the Co-Applicant in terms of section 38 of the Long-Term Insurance Act No. 52 of 1998 on the following basis:

- The business of the Applicant will be transferred at net asset value, on loan account, to the Co-applicant under section 45 of the Act.
- The transfer will include the transfer of securities from the UPF of the Applicant to the UPF of the Co-applicant.
- Section 45 of the Act will not be applicable to the transfer of assets from the UPF of the Applicant to the UPF of the Co-applicant by virtue of section 41(3) of the Act.

Ruling

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

- The transfer of securities from the UPF of the Applicant to the UPF of the Co-applicant will qualify for exemption from STT, as contemplated in section 8(1)(*a*)(iii) of the STT Act, irrespective of the fact that section 45 of the Act will not be applicable to the transfer by virtue of section 41(3) of the Act.

10. BINDING GENERAL RULING

10.1 BGR 9 (Issue 2)

This BGR:

- identifies the taxes administered by SARS, which in its opinion constitute taxes on income or substantially similar taxes for purposes of South Africa's tax treaties;
- provides specific commentary on the nature of the now-repealed STC and its replacement, dividends tax; and
- reflects SARS' view of the recognition of dividends tax as a covered tax under South Africa's tax treaties when it has been imposed after signature of a tax treaty.

A tax treaty generally provides for relief for:

- specified taxes, usually listed under Article 2 of a tax treaty, that are in existence at the time the tax treaty is entered into; and
- any identical or substantially similar taxes on income that are imposed after the date of signature of the tax treaty in addition to, or in place of, existing specified taxes.

10.2 BGR 12 – VAT – Input tax on the acquisition of a non-taxable supply of second-hand motor vehicles by motor dealers

This BGR reproduces the statement in paragraph 7.3 of the *Value Added Guide for Motor Dealers (VAT 420)* under the heading 'Over-allowances: Notional Input Tax and Open Market Value', which comprises a BGR under section 89 of the TA Act.

The Guide, issued during March 2009, deals with the VAT implications arising from the supply by motor dealers being vendors, of motor cars and other vehicles. This BGR updates references to section 76P of the Income

Tax Act No. 58 of 1962 with references to the TA Act and incorporates subsequent amendments to sections of the VAT Act.

10.3 BGR 13 – Calculation of VAT for certain betting transactions

This BGR reproduces paragraph 4.2.1 of Interpretation Note No. 41 (Issue 2) 'Application of VAT to the Gambling Industry' dated 31 March 2008, which comprises a BGR under section 89 of the TA Act.

The Note deals with the VAT implications of specific transactions in the gambling industry. This BGR updates references to section 76P of the Income Tax Act, No. 58 of 1962 with references to the TA Act and incorporates subsequent amendments to sections of the VAT Act.

10.4 BGR 14 – VAT treatment of specific supplies in the short-term industry

This BGR sets out the VAT treatment of the issues listed below which have been highlighted during discussions with the short-term insurance industry:

- The time of supply in relation to the supply of short-term insurance and the related intermediary services
- Alternative documents to be used as a tax invoice in respect of the supply of short-term insurance and the related intermediary services
- Approval to issue recipient-created tax invoices, debit or credit notes
- International transport policies including stock through-put, goods in transit, marine insurance policies and travel coupons
- Hull and associated liability insurance
- Insurance cover provided to South African residents in respect of fixed property and movable property

- Excess payments
- Indemnity payments
- Third party payments
- Recoveries
- Group accident claims
- Reinsurance

10.5 BGR 15 – Recipient-created tax invoices, credit and debit notes

This BGR reproduces paragraph 5 of Interpretation Note No. 56 'Recipient-Created Tax Invoices; Credit and Debit Notes' dated 31 March 2010, which comprises a BGR under section 89 of the TA Act.

The Note provides the necessary approval by SARS for the issuing of recipient-created tax invoices, credit and debit notes. This BGR updates references to section 76P of the Income Tax Act No. 58 of 1962 with references to the TA Act and incorporates subsequent amendments to sections of the VAT Act.

10.6 BGR 16 – VAT – Standard apportionment

This BGR reproduces the statement in paragraph 8.4.3 of the *Value-Added Tax Guide for Vendors (VAT 404)* under the heading 'Formula: Turnover-based method of apportionment', which comprises a BGR under section 89 of the TA Act.

The Guide, which is updated annually, sets out the apportionment method which must be used to calculate the amount of VAT to be deducted as input tax in respect of the acquisition of goods or services for a mixed purpose. This BGR updates references to section 76P of the Income Tax Act, No. 58

of 1962 with references to the TA Act and incorporates subsequent amendments to sections of the VAT Act.

10.7 BGR 17 – VAT – Cancellation of registration of separate enterprises, branches and divisions

This BGR sets out the application of section 50(3) regarding the cancellation of the registration of a separate enterprise, branch or division of the main enterprise (hereinafter collectively referred to as the branch enterprise) and whether such cancellation constitutes a deemed supply in terms of section 8(2).

10.8 BGR 18 – VAT – The zero-rating of various types of dates

This BGR sets out the VAT treatment of dates in its various forms in order to determine if the supply of such dates will be subject to VAT at the zero rate as envisaged in section 11(1)(*j*) read with Item 13.

Suppliers and importers of dates have approached SARS requesting confirmation that the supply of dates in its various forms will be subject to VAT at the zero rate, and that the importation thereof would be exempt from VAT.

11. BINDING CLASS RULING

11.1 BCR36 – Reserves of a collective investment scheme in securities and the distribution thereof to unitholders

This ruling deals with the tax treatment that will be applicable in respect of reserves held by a collective investment scheme in securities that will be distributed to unitholders in the scheme.

In this ruling references to sections are to sections of the Act applicable as at 16 October 2012 and unless the context indicates otherwise, any word or expression in this ruling bears the meaning ascribed to it in the Act.

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

- section 10(1)(*i*B);
- section 10(1)(*k*)(i)(*ee*); and
- section 25BA.

Class

The class members to whom this ruling will apply will be the unitholders as described below.

Parties to the proposed transaction

The Applicant: A collective investment scheme in securities as contemplated in the Collective Investment Schemes Control Act No. 45 of 2002

Unitholders: Unitholders of a participatory interest in the Applicant

Description of the proposed transaction

In terms of an arrangement entered into prior to January 2005, dividends were received by the Applicant up to 31 December 2010 and were included in the 'gross income' of the Applicant as these dividends were not distributed within the 12 month period as required by section 25BA. These dividends were exempt in the hands of the Applicant under section 10(1)(*k*)

and they remained on the balance sheet of the Applicant as undistributed reserves.

In order to unwind the Applicant, these reserves must be distributed. The reserves can, however, only be unlocked if the counter party to the arrangement receives the revenue stream originally agreed upon.

The Applicant, therefore, wishes to sell participatory interests in itself to members of the public. The proceeds of the sales to members of the public will be used to increase the Applicant's interest in an underlying collective investment scheme in securities. The distributions received by the Applicant from the underlying collective investment scheme in securities will be paid into a bank account. The payments received will be used to unlock the Applicant's reserves, *viz* dividends which accrued but which could not be accessed because of inadequate payments received from the underlying collective investment scheme in securities.

<u>Ruling</u>

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

- The Applicant's reserves will not be subject to the provisions of section 10(1)(*k*)(i)(*ee*) as the dividends had accrued to the Applicant prior to the date on which these provisions became effective.
- As these amounts were not distributed within the applicable 12 month period (that is 1 January 2011 to 31 December 2011) they will be exempt from normal tax in the Applicant's hands as the non-distribution took place prior to the effective date of the amendment to the provisions of section 25BA, which came into effect 1 January 2012.
- The distribution of the reserves by the Applicant to Unitholders will be exempt from normal tax in the hands of the Unitholders under the provisions of section 10(1)(*i*B).
- The ruling applies only to the distribution of the undistributed reserves of the Applicant as at 31 December 2011.

11.2 BCR37 – Distribution of shares in an unbundling transaction

This ruling deals with the question as to whether the transfer of equity shares held by a company to the shareholders of that company, in an unbundling transaction, will be exempt from dividends tax and securities transfer tax.

In this ruling references to sections are to sections of the relevant Act applicable as at 19 November 2012 and unless the context indicates otherwise, any word or expression in this ruling bears the meaning ascribed to it in that Act.

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

- section 46 of the Act; and
- section 8(1)(*a*)(iv) of the STT Act.

Class

The class members to whom this ruling will apply will be the Shareholders as described below.

Parties to the proposed transaction

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

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

Shareholders: Shareholders of the Applicant

Description of the proposed transaction

The Applicant owns 100% of the equity shares in the Co-Applicant. The Applicant would like to unbundle its equity shareholding in the Co-Applicant through a pro-rata distribution of the Co-Applicant shareholding. The intention is to establish a primary listing for the Co-Applicant on the Johannesburg Stock Exchange (JSE) and a secondary listing of the American Depositary Receipts on the New York Stock Exchange (NYSE).

Both the Applicant and Co-Applicant will remain a resident of South Africa for tax purposes.

In order to comply with the US federal securities laws, the Co-Applicant will be required to register with the Securities and Exchange Commission (SEC) for purposes of the distribution of its shares, unless a dispensation is agreed with the SEC. The replication of the JSE and NYSE listing structure for the Co-Applicant will enable shareholders to trade in the Applicant's shares on the same basis as they do currently.

Ruling

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

- The distribution of the Co-Applicant's shares by the Applicant to its shareholders will constitute an 'unbundling transaction', as defined in section 46(1) of the Act.
- The distribution of the Co-Applicant's shares by the Applicant through an unbundling transaction will be deemed not to be an amount transferred by the Applicant for purposes of Part VIII of Chapter II, as contemplated in section 46(5) of the Act.
- The transfer of the Co-Applicant's shares pursuant to the Applicant's unbundling distribution will be exempt from securities transfer tax under section 8(1)(*a*)(iv) of the STT Act.

11.3 BCR 38 – Exchange of one restricted equity instrument for another

This ruling deals with the tax consequences under sections 8C and 42 of the Act in respect of the exchange of one restricted equity instrument for another.

In this ruling references to sections are to are to sections of the relevant Acts applicable as at 20 December 2012 and unless the context indicates otherwise, any word or expression in this ruling bears the meaning ascribed to it in the Act.

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

- section 8C of the Act;
- section 42 of the Act; and
- section 8 of the STT Act.

Class

The class members to whom this ruling will apply will be the beneficiaries as described below.

Parties to the proposed transaction

The Applicant: A company that is the controlling group company, the shares of which are listed on the Johannesburg Stock exchange

The Co-Applicants: Empowerco, a controlled group company to be used as a special purpose vehicle to hold empowerment shares in the Applicant

Employee Trust, an employee share ownership scheme trust

The Beneficiaries: The Employee Trust's beneficiaries, a certain group of employees of the Applicant's group of companies

Description of the proposed transaction

The Applicant proposes to enter into a Broad Based Black Economic Empowerment (BBBEE) transaction in terms of which it will transfer ownership of shares in itself, representing a portion of its South African (SA) operations, to a certain group of employees through the Employee Trust.

A summary of the proposed transaction is set out in the steps below:

- The Applicant will issue a new class of shares (class B shares) to Empowerco under section 42 of the Act, representing 20% of its SA operations.
- Empowerco will issue shares to the Employee Trust, equalling 50.1% of its ordinary shares, at a nominal value. It will be a term of issue of these shares that Empowerco will have an option to repurchase some of the shares at the end of a 10 year lock-in period (maturity date) at

the same nominal value. The number of shares to be repurchased will be based on a compound growth formula.

- The remaining Empowerco shares held by the Employee Trust after execution of the repurchase agreement will be distributed by the Employee Trust to its beneficiaries subject to a disposal restriction for a period of 7 days.
- During the 7 day restriction period the Empowerco shares will immediately be exchanged under section 42 of the Act for shares in the Applicant.

Ruling

The ruling made in connection with the proposed transaction, with particular regard to the distribution of the Empowerco shares by the Employee Trust to the Beneficiaries, and the exchange of these shares by the Beneficiaries for shares in the Applicant under section 42 of the Act, is as follows:

- For purposes of sections 8C and 42 of the Act, the date of acquisition of the Empowerco shares by the Beneficiaries will be the distribution date which will be the maturity date.
- The exchange of Empowerco shares by the Beneficiaries for shares in the Applicant will be deemed as fulfilling the requirements of item *(bb)* of paragraph *(a)*(ii) of the definition of 'asset-for-share transaction' in section 42 of the Act.
- The exchange of Empowerco shares by the Beneficiaries for shares in the Applicant will qualify for roll-over relief as contemplated in section 42 of the Act.
- The Beneficiaries will be taxed on the market value of the Applicant's shares under section 8C of the Act.
- No securities transfer tax will be payable on the transfer of the Empowerco shares under section 42 of the Act by virtue of the application of section 8(1)*(a)* of the STT Act.

12. GUIDES

12.1 VAT 404 – Guide for vendors

The VAT 404 is a basic guide where technical and legal terminology has been avoided wherever possible.

Below is a brief synopsis of some of the most important changes affecting the administration of VAT since the previous issue of this Guide:

1. VAT 201 modernisation

   SARS has modernised its current Third Party Data Platform to accommodate the bulk submission of third party data through the new Direct Data Flow channel. It is expected that more modernisation changes will be implemented in phases during 2013, especially in light of the TA Act. Vendors are therefore advised to check the SARS website for the latest information, as well as the VAT Connect.

2. Tax Administration Act

   With effect from 1 October 2012, the general administration of all taxes in South Africa is governed primarily by the TA Act. The TA Act only deals with tax administration, and incorporates into one piece of legislation certain administrative provisions that are generic to all tax Acts administered by SARS. It also seeks to align the various administrative provisions which were previously duplicated in the different tax Acts and to simplify and harmonise the provisions as far as possible. Certain provisions relating to the general administration of VAT have therefore been replaced by provisions in the TA Act.

3. Definition of Instalment Credit Agreements (ICA)

   Two changes have been made to the wording of the definition of 'instalment credit agreement'. The definition now includes any amount determined with reference to the time value of money. The effect being that such amounts should be interpreted to be within the meaning of the term 'finance charges' mentioned in the definition. Changes have also been made concerning the person who is liable to

accept the risk of destruction, loss, maintenance, repair and insurance of the goods or services while the agreement remains in force. The amendments were necessary to ensure that the Islamic financing instrument known as Ijarah, which is regarded as a form of finance lease, can be treated the same as an instalment credit agreement for VAT purposes. The amendment applies from 1 January 2013.

4. Credit or debit notes

The specific conditions for the issuing of credit or debit notes in section 21(1) has been extended to allow for the correction of an error in regard to the statement of the consideration on the original tax invoice issued in respect of a supply. For instance, if a vendor incorrectly states the consideration as being R1 114 on a tax invoice instead of R114, the vendor would previously have been prohibited from issuing a credit note to the recipient to correct the mistake because it did not fall within the specified conditions. The amendment now allows a vendor to make such a correction in cases where the supplies concerned were made on or 1 January 2013.

5. Customs Controlled Area (CCA) rules

Further refinements to the rules in respect of CCAs have been made that will apply to all supplies or imports occurring on or after 1 January 2013. The rules now provide that where goods are imported into a CCA, it will remain outside the VAT net until entered for home consumption. The removal of imported goods (i.e. exempt from VAT on importation) from a CCA must be disclosed on a voucher of correction if not returned within the prescribed period with a result that VAT becomes payable in terms of section 7(1)(b). A deemed supply will occur when locally acquired goods (excluding goods acquired for the purposes of entertainment and motor cars) are removed from the CCA and not returned within the prescribed period.

6. Pre-entry sale of imported goods

When a non-resident supplies goods after they have been imported into South Africa but before they have been entered for home

consumption, the supply is exempt in terms of section 12(k). However, the non-resident may elect to waive the exemption, subject to the approval by SARS. Section 12(k) has now been amended to clarify that it is no longer a requirement for the imported goods to be entered into a licensed Customs and Excise storage warehouse before the sale for the exemption to apply.

7. Exemption for bargaining councils and political parties

Two new exemptions in the form of sections 12(ℓ) and (m) have been introduced for bargaining councils established in terms of section 27 of the Labour Relations Act, 1995 and political parties registered in terms of section 15 of the Electoral Commission Act, 1996 respectively. In terms of these exemptions, any goods or services supplied by the entities concerned to any of their respective members is exempt from VAT to the extent that the consideration for such supply consists of membership contributions. The exemptions apply in respect of any such supplies made on or after 1 January 2013. Other activities conducted by bargaining councils and political parties remain taxable. For example, if a bargaining council or political party conducts an enterprise of renting out office space in a building which it owns to commercial tenants, VAT must be charged on the rent if the value of the taxable supplies exceeds the registration threshold, or if the entity has voluntarily registered for VAT in this regard.

8. Relief for past supplies by bargaining councils and political parties

Section 40C has been introduced to provide bargaining councils and political parties with the opportunity to apply for relief in certain circumstances where SARS has raised an assessment for VAT before 1 January 2013 in respect of supplies that are now exempt in terms of section 12(ℓ) and 12 (m). SARS is also prevented from raising assessments and making refunds in regard to activities of the type envisaged by the new exemptions conducted before 1 January 2013. Bargaining councils and political parties that only make exempt supplies under the new exemptions will be required to deregister for VAT, but section 8(2F) provides additional relief in this regard as the

taxable value of the deemed supply of assets which arises upon deregistration in these cases will be deemed to be nil. This relief applies if the entity ceases to be a vendor solely by reason of the introduction of these new exemptions.

9. Conversion from share block to other forms of property ownership

   Section 8(19) has been amended to provide that a conversion of rights and shares in a share block company to any other form of property ownership is not regarded as a supply made in the course or furtherance of an enterprise. Consequently, when any 'immovable property' (being 'fixed property' as defined in section 1(1)) is supplied to the shareholder by the share block company in return for the surrender by the shareholder of the shares in the share block company, neither of the supplies concerned will be subject to VAT.

10. Abridged tax invoices

   The threshold for issuing an abridged tax invoice has been increased from R3 000 to R5 000. This will apply to all supplies made on or after 20 December 2012.

12.2 VAT 409 – Guide for fixed property and construction

This guide is a general guide concerning the application of the VAT Act in connection with fixed property and construction transactions in South Africa. Although fairly comprehensive, the guide does not deal with all the legal detail associated with VAT and is not intended for legal reference.

The previous edition of this guide has been withdrawn with effect from 26 March 2013.

The approach of this guide in dealing with the topics mentioned in paragraphs 1.1 and 1.2 is set out below:

Chapter 1

This chapter sets out the policy background and scope of transactions falling within the definition of 'fixed property' which are the focus of this guide.

Chapter 2

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

Chapter 3

Provides a brief overview of the legal concepts 'agent' and 'principal'. This is important as the VAT consequences of a transaction cannot be determined until the contractual relationship between the parties is established.

Chapter 4

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

Chapter 5

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

Chapter 6

Deals with a number of adjustments which apply in connection with fixed property based on the extent of taxable use. These include annual adjustments in regard to the use of capital goods and services

as well as situations which give rise to a change in use or application, or change of intention with regard to the taxable use of the fixed property after the initial acquisition.

Chapter 7

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

Chapter 8

Deals mainly with the issues faced by developers and property speculators. The focus is therefore on supplies of newly constructed properties and second-hand properties that have been renovated before being sold, or properties that are bought and sold on a speculative basis. Included is a discussion on the consequences of temporarily applying properties for exempt supplies (residential purposes) whilst being held for taxable purposes. Other topics dealt with include subsidised low cost housing developments, fractional ownership type developments and land restitution transactions. VAT 409 – Guide for Fixed Property and Construction Chapter 1 10

Chapter 9

Discusses the rules concerning fixed property supplied as part of an enterprise which is a going concern. It sets out the circumstances as to when the transaction may be subject to VAT at the zero rate and when the standard rate will apply.

Chapter 10

Deals with the VAT treatment of rental pools. The chapter contains a detailed explanation of the special rules set out in section 52 and how

these apply in practice to override what would otherwise be viewed as supplies made by an agent as contemplated in Chapter 3.

Chapter 11

Discusses other aspects regarding the supply of fixed property which is not dealt with in the other chapters.

12.3 VAT 412 – Guide for Share Block Schemes

This guide is a general guide concerning the application of the Act to share block schemes in South Africa.

This guide deals with the VAT implications of share block schemes in South Africa and the various types of supplies related to these schemes. The intention of this guide is not to cover each and every type of transaction that can take place, but rather to attend to basic principles and their effect from a VAT point of view.

The guide will focus mainly on the following aspects:

- Basic principles relating to share block schemes and how they function

  Before delving into the application of the VAT law in regard to share block schemes, we will first establish the basic principles and functioning of a share block scheme.

- The VAT implications of share block schemes

  We will consider the core VAT implications of share block schemes and the implications for the share block company, the developer and the shareholder.

- The conversion of share block schemes

  We will consider the conversion of companies to share block companies and share block companies to sectional title schemes together with the VAT implications of these conversions.

- The VAT implications of the levy fund

Every share block company is obliged, by the Share Blocks Control Act 59 of 1980, to establish and maintain a levy fund. We will consider the specific VAT consequences of such a levy fund.

- The termination and deregistration of share block schemes

  The share block scheme may be terminated voluntarily by the shareholders. The scheme may also be terminated by the sale in execution or expropriation of the immovable property or by the compulsory liquidation of the share block company. We will consider the VAT implications of the termination of the share block scheme and the VAT deregistration of the share block company.

- Historical development of the VAT Act in relation to share block schemes

  With effect from 9 July 1993, the definition of 'enterprise' was amended to include the activities of a share block scheme where the share block company applied for voluntary registration. We will briefly consider the other important amendments introduced with effect from 9 July 1993 which fundamentally affected the VAT implications of share block schemes.

The approach of this guide in dealing with the topics mentioned in paragraph 1.1 is set out below.

Chapter 1

Describes the scope of topics that will be covered in the guide, as well as the approach adopted.

Chapter 2

Sets out the basic legal principles and explains the functioning of a share block scheme. It is important, for the purposes of this guide, to first understand the nature and operation of a share block scheme before dealing with the VAT consequences of the typical supplies which can be expected in such a scheme.

Chapter 3

Introduces the reader to the most important VAT concepts, terms and definitions mentioned in the guide so that the VAT treatment of supplies which are explained in later chapters can be understood. Key points addressed in this chapter include an explanation of the terms 'enterprise', 'supply', 'taxable supply' and the meaning of 'fixed property'.

Chapter 4

Provides a brief overview of the legal concepts 'agent' and 'principal'. This is important as the VAT consequences of a transaction cannot be determined until the contractual relationship between the parties is established.

Chapter 5

Deals with how VAT should be accounted for in respect of the different types of supplies made by share block schemes, including the value and timing rules. The chapter sets out the general rules with regard to classifying supplies, record-keeping, invoicing and documentation required. It discusses the VAT treatment of the core transactions of a share block company in terms of the most recent amendments to the Act.

Chapter 6

A company which owns immovable property can be converted to a share block company by means of a special resolution of the company and lodging amended memorandum and articles of association with the Companies and Intellectual Property Commission. We will consider the VAT implications of this conversion. Similarly, we will also consider the VAT implications of a share block company that decides by special resolution to convert the immovable property of the share block company to sectional title units.

Chapter 7

Considers the VAT implications of the levy fund created in terms of legislation which is funded from contributions received from the shareholders to fund the running expenses of the share block company. We will distinguish between the levy fund and loan obligation of a share block scheme and explain the exempt nature of services supplied by a share block company if these services are funded by contributions to the levy fund.

Chapter 8

Provides a brief overview of the termination or deregistration of a share block scheme. This chapter will consider the different ways in which a share block scheme can be terminated or deregistered and the VAT consequences of each. This is important since the termination or deregistration of a share block scheme may create a liability for VAT which is often overlooked.

Annexure A

Provides a brief overview of the historical changes to the Act and other legislation as it relates to share block schemes. This information is included as an annexure to the guide as it provides a detailed analysis of the amendments and their effect on the various parties which may be involved in transactions relating to share block schemes without detracting from the purpose of this guide which is to explain the current VAT treatment.

12.4 VAT 421 – Guide for short-term insurance

This guide is a general guide concerning the application of the VAT Act to short-term insurance transactions in South Africa. Although fairly comprehensive, the guide does not deal with all the legal detail associated with VAT and is not intended for legal reference.

The approach of this guide in dealing with the topics mentioned in paragraph 1.2 is set out below.

Chapter 1

Sets out the policy framework which governs the VAT treatment of insurance in general. It includes a description of the policy background as determined by VATCOM before VAT was introduced in South Africa on 30 September 1991. It also describes the scope of topics concerning short-term insurance transactions that will be covered in the guide and the approach adopted.

Chapter 2

Explores some of the principles which underpin the law of insurance in South Africa and the ordinary meaning of the term 'insurance'. Included, is a description of what insurance is all about and a discussion of some of the differences between short-term and long-term insurance. This chapter is important in coming to terms with the main principles of insurance law so that the VAT implications of certain insurance-related transactions explained later in the guide can be understood.

Chapter 3

Introduces the reader to the most important VAT concepts, terms and definitions mentioned in the guide so that the VAT treatment of supplies which are explained in later chapters can be understood. Key points addressed in this chapter include an explanation of the terms 'enterprise' and 'financial services' in the context of insurance, as well as the meaning of the term 'insurance' which is specifically defined for VAT purposes and is wider than the ordinary meaning. The chapter also explains the difference between taxable and non-taxable supplies which is fundamental in establishing whether output tax must be declared and input tax may be deducted.

Chapter 4

Provides a brief overview of the legal concepts 'agent' and 'principal'. This is important as the VAT consequences of a transaction cannot be determined until the contractual relationship between the parties is established. These concepts are particularly important with regard to

supplies of insurance as agents, brokers and other intermediaries play an important role in the insurance industry in writing and maintaining policies of insurance and providing auxiliary services which are related to the supply of insurance.

Chapter 5

Deals with how VAT should be accounted for in respect of the different types of supplies made by insurers and intermediaries including the timing rules. The chapter sets out the general rules with regard to classifying supplies, record-keeping, invoicing and documentation required. It discusses the VAT treatment of premium income which may be paid directly or collected via intermediaries as well as commissions and some other types of supplies which are typically found in the insurance industry. The effect of the imported services provisions for insurers that make exempt supplies are also dealt with in this chapter. The VAT implication of deemed supplies arising as a result of the making and receiving of indemnity payments is dealt with separately in Chapter 6.

Chapter 6

This chapter focuses on the VAT implications of settling claims and the different ways in which this can be done. The most important aspects include how to deal with input tax from the insurer's perspective when making trade payments and indemnity payments. From the insured's perspective, the most important aspects include the VAT treatment of the deemed supply which may arise as a result of receiving an indemnity payment, as well as the VAT treatment of excess payments.

12.5 Transfer Duty Guide

This document contains a discussion of the application of the Transfer Duty Act 40 of 1949, in respect of transactions involving immovable property

such as land, buildings and other real rights in connection with immovable property situated in South Africa.

The previous edition of this guide has been withdrawn with effect from 13 March 2013.

Some of the main topics discussed in this document include:

- the meaning of various definitions;
- the imposition of transfer duty on acquisitions of property;
- different kinds of transactions which are subject to either VAT or transfer duty;
- calculation of transfer duty;
- exemptions; and
- issues relating to the payment of transfer duty, the submission of returns and supporting documentation and other matters generally related to the administration of the Transfer Duty Act.

The approach of this guide in dealing with the topics mentioned in paragraph 1.3 is set out below.

Chapter 1

> Provides a brief historical perspective and some background information relating to transfer duty. It also describes the scope of topics that will be covered in the guide and the approach adopted.

Chapter 2

> This chapter explores some of the main definitions which underpin the application of the Transfer Duty Act and is important in coming to terms with how the Act is meant to be applied in the context of the law of property, the law of contract and various other legislative acts which govern property transactions in South Africa. Definitions dealt with include: date of acquisition; 'fair value'; 'property'; 'residential property company'; 'residential property'; and 'transaction'. The most fundamental of these is the concept of 'property' which has a particular meaning in the legal context as well as a specific meaning

as defined in section 1(1) of the Act and also links with the definition of the term ‘fixed property’ as defined in section 1(1) of the VAT Act. This definition is therefore explained in some detail as the acquisition of anything falling within the meaning of ‘property’ forms the main part of the tax base of transfer duty.

Chapter 3

Describes the transactions and events which make up the tax base of transfer duty, being acquisitions of ‘property’ either by way of a transaction or in any other manner, as well as renunciations of interests in ‘property’ which has the effect of enhancing the value of property. As most of the important definitions and concepts would have already been explained in Chapter 2, this chapter provides a summary of the meaning of those terms and puts them into context within the meaning of the term ‘acquisition’. Since this term is also fundamental to the application of the law when it comes to different types of property transactions and different modes of acquisition, the term is discussed in some detail. Also dealt with in this chapter is the cancellation of transactions and transactions which are concluded through representatives or agents who act on behalf of, or for the benefit of others.

Chapter 4

Briefly sets out aspects which relate to the date of liability for transfer duty and the period in which the duty must be paid. This chapter focuses on the practical aspects relating to the definition of the term ‘date of acquisition’ and the term ‘acquisition’ which are explained in Chapters 2 and 3.

Chapter 5

Deals with determining who is liable to pay transfer duty in any particular situation. The general rule is that the transferee is liable, but the Act also contains provisions which make other persons liable for the duty in certain types of transactions.

Chapter 6

Focuses on the determination of the dutiable value of the property acquired or the value by which property is enhanced by the renunciation of an interest therein. The applicable valuation rules as set out in the definition of the term 'fair value' are discussed in the context of the different transactions and events. The chapter includes a discussion of different valuation factors that SARS may consider (or which must be considered) when an inadequate consideration is paid between the parties, or where the declared value is less than the fair value of the property. This chapter also sets out what is to be included and excluded from the consideration paid (or payable) which will be subject to duty.

Chapter 7

Sets out the rules for calculating transfer duty and the rates of duty that have applied over the years. Included are a number of different examples of how to calculate duty for past and current transactions as well as the application of the formula in section 2(5) for calculating the duty on an acquisition of an undivided share in property. The examples also demonstrate how to establish whether transfer duty or VAT is payable on a transaction.

Chapter 8

Deals with exemptions from duty. One of the most important of these is section 9(15) which provides for an exemption from transfer duty when a property transaction constitutes a taxable supply of 'fixed property' as defined in section 1(1) of the VAT Act. This exemption and a few others are explained in more detail, mainly as a result of other legislation or legal principles which apply in certain transactions. In some cases, the further explanations are required due to the complexity of the wording of the exemption itself.

Chapter 9 – Deals with matters associated with the payment and recovery of duty. It covers the period for payment, the issuing of receipts and interest payable on late payments.

Chapter 10

> Deals with compliance matters concerning the administration of the Act generally in the context of the TA Act. It includes a discussion on how these aspects impact on the interpretation of definitions, the submission of returns and payments, recovery of unpaid duty, objections, appeals and dispute resolution.

12.6 Basic guide to tax-deductible donations

This guide provides a basic explanation of tax-deductible donations.

The South African Government has recognised that certain organisations are dependent upon the generosity of the public and to encourage that generosity has provided a tax deduction for certain donations made by taxpayers.

A taxpayer making a *bona fide* donation in cash or of property in kind to a section 18A-approved organisation, is entitled to a deduction from taxable income if the donation is supported by the necessary section 18A receipt issued by the organisation or, in certain circumstances, by an employees' tax certificate reflecting the donations made by the employee. The amount of donations which may qualify for a tax deduction is limited.

The eligibility to issue section 18A receipts is restricted to specific approved organisations which use the donations to fund specific approved PBAs.

This guide has been prepared to assist organisations in determining whether they qualify for approval to issue section 18A certificates and to explain the requirements that must be complied with if approved.

12.7 Basic Guide to Income Tax for PBOs

This guide provides basic information on public benefit organisations

An organisation that has a non-profit motive or is established or registered as a non-profit organisation does not automatically qualify for preferential

tax treatment. An organisation will only enjoy preferential tax treatment after it has applied for and been granted approval as a PBO by the TEU. Once approved the PBO must continue to comply with the Act and related legislation throughout its existence.

Approved PBOs have the privilege and responsibility of spending public funds, which they derive from donations or grants, in the public interest on a tax-free basis. The donations or grants may be received from the general public or directly or indirectly from the State. It is therefore important to ensure that exempt organisations use their funds responsibly and solely for their stated objectives, without any personal gain being enjoyed by any person including the founders and the fiduciaries.

The conditions and requirements for an organisation to be approved as a PBO are contained in section 30 while the rules governing the preferential tax treatment of PBOs are contained in section 10(1)(*c*N). Section 10(1)(*c*N) provides for the exemption from normal tax of certain receipts and accruals of approved PBOs. Certain receipts and accruals from trading or business activities will nevertheless be taxable.

This guide has been prepared to assist non-profit organisations in South Africa to understand the basic implications relating to PBOs with particular reference to income tax.

The eligibility to issue valid receipts for tax-deductible donations under section 18A and other tax issues affecting PBOs such as capital gains tax, estate duty, securities transfer tax, transfer duty, customs duty, skills development levy and value-added tax are not discussed in this guide.

13. INDEMNITY

Whilst every care has been taken in the production of this update we cannot accept responsibility for the consequences of any inaccuracies contained herein or for any action undertaken or refrained from taken as a consequence of this update.