BOWMAN TAX UPDATE **PREPARED BY: JOHAN KOTZE**

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1. INTRODUCTION

The purpose of this update is to summarise the developments that occurred during the second quarter of 2014 (i.e. 1 April 2014 to 30 June 2014) specifically in relation to Income Tax and 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 and to consider areas that may be applicable to their situation. 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.

This update contains aspects dealing with tax reforms of the retirement industry, which comes into operation on 1 March 2015.

It is worth noting the draft regulations pertaining to VAT registrations.

The reader is referred to ITC 1870, which the writer has been involved in, and is welcome to contact the writer if more insight in the case are required.

Interpretation notes, rulings and guides are all important aspects of the developments that took place, as they give taxpayers an insight into SARS' application of specific provisions. It is however important to note that these publications are not law, but may bind SARS. Taxpayers should nonetheless consider these publications carefully to determine whether, and how, they are actually applicable to their own circumstances.

Enjoy reading on!

2. MEDIA STATEMENT – 2014 RATES & MONETARY AMOUNTS AND AMENDMENT OF REVENUE LAWS BILL AND FIRST BATCH OF THE DRAFT TAXATION LAWS AMENDMENT BILL

National Treasury on 10 June 2014 published the 2014 Rates and Monetary Amounts and Amendment of Revenue Laws Bill ('Rates Bill'), First Batch of the 2014 draft Taxation Laws Amendment Bill and Regulations ('TLAB').

The Rates Bill gives effect to the rates and monetary threshold changes announced in the 2014 Budget, and will be tabled in Parliament shortly. It is published for public information. The Rates Bill deals with numerical adjustments. It does not deal with new and substantive changes in law, which is normally dealt with in the annual TLAB. The 2014 draft TLAB will be published for public comment in July 2014.

The First Batch of the 2014 TLAB is not the full bill, but is intended to solicit comments on two specific amendments to inform the full draft TLAB to be published in July. Draft regulations on one of the specific amendments dealing with defined benefit funds are also published for comment, and provide taxpayers with an early indication of some of the proposed reporting requirements.

This First Batch of the 2014 draft TLAB and Regulations deals with the following two amendments:

1. <u>The tax treatment of the risk businesses of long-term insurers</u>

   The current taxation of long term insurers does not distinguish between the investment and risk businesses. However, from a tax policy point of view the two types of businesses cannot be taxed by applying the same principles. From the perspective of a long-term insurer, profits or losses arising in respect of risk business should be fully taxed and should therefore not form part of the tax calculation of a policyholder fund that focusses on the taxation of the return on assets invested for the benefit of policyholders on the trustee basis.

It proposed that as from 1 January 2016 a clear distinction be drawn in the taxation of investment and risk business conducted by long term insures. Profits or losses that result from such new risk business will be taxed in the corporate fund.

2. <u>Retirement reforms and in particular rules with regards to defined benefit funds</u>

Changes to the rules and thresholds that apply to the tax deductible contributions to retirement savings will become effective on 1 March 2015. Defined benefit funds offer retirement benefits that are calculated according to the rules of the pension fund where the value of the contributions to the fund may not be an accurate reflection of the benefits that may be received by the retirement fund member. For example, if the pension fund is in financial difficulty and the employer needs to make additional contributions to meet the expected liabilities, it may be unfair to tax members of the fund on those contributions as if they were a fringe benefit if there is no associated increase in benefits.

In order to avoid any discrepancies, align the tax treatment of contributions to defined contributions pension funds and defined benefit pension funds and to improve fairness in relation to the receipt of retirement benefits within defined benefit funds, a prescribed methodology is proposed to determine a notional employer contribution for members of defined benefit pension funds. The notional employer contribution will be a fringe benefit that is taxable in the hands of the employee and will be included in the total pension contribution amount to calculate whether the individual is still below the allowable annual and monthly deductible limits.

The proposal is based on the concept of a ‘fund member category’. A ‘fund member category’ is a group of members of a fund whose entitlement to receive benefits and the value of those benefits when they are received are determined by the same rules, and in respect of whom the same contributions are paid as a proportion of pensionable salary by them and by their employer. The fringe benefit should be calculated separately for each fund member category of a fund. This is to ensure that the fringe benefits are calculated across groups of members in the same way as the fund pools contributions and the costs of paying benefits across members.

To calculate the fringe benefit, the employer would need to multiply the pensionable salary by the 'fund member category factor' that is provided in the 'contribution certificate' and subtract the value of any contributions made by the employee.

The pension fund would be required to calculate the 'fund member category factor' by following the calculation method specified in regulations. This requires the fund to separate benefits for which members of the fund are eligible into defined benefit, defined contribution, underpin and risk benefit components. A separate calculation method is specified for each type of component. If the fund offers more than one benefit component of a particular type, a calculation would need to be performed for each benefit component separately, and the results aggregated.

3. RETIREMENT REFORMS – DRAFT TAXATION LAWS AMENDMENT BILL, 2014

3.1 Amendment of par. 14 of Fourth Schedule

Paragraph 14 of the Fourth Schedule to the Income Tax Act is hereby proposed to be amended by the insertion after subparagraph (1) of the following subparagraph:

'(1A) In addition to the records required in accordance with Part A of Chapter 4 of the Tax Administration Act and subparagraph (1), every employer shall retain the contribution certificates as contemplated in paragraph 12D(4) of the Seventh Schedule and those contribution certificates shall be available for scrutiny be the Commissioner.'.

Subsection (1) comes into operation on 1 March 2015.

3.2 Amendment of par. 1 of Seventh Schedule

Paragraph 1 of the Seventh Schedule to the Income Tax Act is hereby proposed to be amended by the deletion of the definitions of 'defined benefit component', 'defined contribution component' and 'retirement funding income'.

Subsection (1) comes into operation on 1 March 2015.

3.3 Sustitution of par. 12D

The Seventh Schedule to the Income Tax Act is hereby proposed to be amended by the substitution for paragraph 12D of the following paragraph:

'12D. (1) For the purposes of this paragraph—

'benefit' in relation to an employee that is a member of a pension fund, provident fund or retirement annuity fund, means any amount payable to that member or a dependant or nominee of that member by that fund in terms of the rules of the fund;

'contribution certificate' means the certificate contemplated in subparagraph (4);

'defined benefit component' means a benefit or part of a benefit receivable from a pension fund, provident fund or retirement annuity fund by a member of that fund or a dependant or nominee of that member other than a defined contribution component or underpin component of a fund;

'defined contribution component' means a benefit or part of a benefit receivable from a pension fund, provident fund or retirement annuity fund—

(a) where the interest of each member in the fund in respect of that benefit has a value equal to the value of—

(i) the contributions paid by the member and by the employer in terms of the rules of the fund that determine the rates of both their contributions at a fixed rate;

(ii) less such expenses as the board of that fund determines should be deducted from the contributions paid;

(iii) plus any amount credited to the member's individual account upon—

(A) the commencement of the member's membership of the fund;

(B) the conversion of the component of the fund to which the member belongs from a defined benefit component to a defined contribution component; or

(C) the amalgamation of that fund with any other fund, if any,

other than amounts taken into account in terms of subparagraph (iv);

(iv) plus any other amounts lawfully permitted , credited to or debited from the member's individual account, if any, as increased or decreased by fund return; or

(b) which consists of a risk benefit provided by the fund directly or indirectly for the benefit of a member of the fund;

'fund member category' in relation to members of a pension fund, provident fund or retirement annuity fund, means any group of members in respect of whom, in terms of the rules of the fund—

(a) the employers of those members and those members must respectively make a contribution to that fund in an amount in respect of retirement funding employment income in the same specified proportion;

(b) the determination of the value of the benefits of the members referred to in paragraph *(a)* and the determination of the entitlement of those members to those benefits are made according to the same method;

'fund member category factor' means the fund member category factor contemplated in subparagraph (4);

'member' means in relation to a pension, provident or retirement annuity fund, any member or former member of that fund but does not include any member or former member or person who has received all the benefits which may be due to them from the fund and whose membership has thereafter been terminated in accordance with rules of the fund;

'retirement-funding income' means—

(a) in relation to any employee or the holder of an office (including a member of a body of persons whether or not established by or in terms of any law) who in respect of his or her employment derives any income constituting remuneration as defined in paragraph 1 of the Fourth Schedule and who is a member of or, as an employee, contributes to a pension fund or provident fund established for the benefit of employees of the employer from whom such income is derived, that part of the employee's said income as is taken into account in the determination of the contributions made by the employer for the benefit of the employee to such pension fund or provident fund in terms of the rules of the fund; or

(b) in relation to a partner in a partnership (other than a partner contemplated in paragraph *(a)*) that part of the partner's income from the partnership in the form of the partner's share of profits as is taken into account in the determination of the contributions made by the partnership for the benefit of the partner to a pension fund or provident fund in terms of the rules of the fund: Provided that for the purposes of this definition a partner in a partnership must be deemed to be an employee of the partnership and a partnership must be deemed to be the employer of the partners in that partnership;

'underpin component' means a benefit receivable from a pension fund, provident fund or retirement annuity fund the value of which benefit, in terms of the rules of the fund, is the greater of the amount of a defined contribution component or a defined benefit component other than a risk benefit;

'valuator' means valuator as defined in section 1 of the Pension Funds Act;

(2) The cash equivalent of the value of the benefit contemplated in paragraph 2*(l)* , where a pension, provident or retirement annuity fund consists solely of defined contribution components, is the value of the

amount contributed by the employer for the benefit of an employee that is a member of that fund.

(3) Where a pension, provident or retirement annuity fund consists of components other than only defined contribution components, the cash equivalent of the value of the benefit contemplated in paragraph 2*(l)* is an amount that must be determined in accordance with the formula

$$X = (A \times B) - C$$

in which formula—

(a) 'X' represents the amount to be determined;

(b) 'A' represents the fund member category factor in respect of the employee;

(c) 'B' represents the amount of the retirement funding employment income of the employee;

(d) 'C' represents the sum of the amounts contributed by the employee to the fund in terms of the rules of the fund,

in respect of that year of assessment.

(4) The board of a fund, as defined in section 1 of the Pension Funds Act, must provide to the employer of the employees which are members of a fund a contribution certificate—

(i) no later than one month before the commencement of the year of assessment in respect of which the contribution certificate is issued;

(ii) where the rules of the fund are amended and those amendments affect the value of or entitlement to any benefit payable to a member of that fund or a dependant or nominee of that member, the contribution certificate must be supplied to the employer no later than one month prior to the day on which those amendments become effective; and

(iii) where the rules of the fund are amended retrospectively and those retrospective amendments affect the value of or entitlement to any benefit payable to a member of that fund or a dependant or nominee of that member, a contribution certificate reflecting the value of or entitlement to any benefit payable must be supplied to the employer no later than one month after the day on which those amendments become effective.

(5) The Minister must make regulations prescribing—

(a) the manner in which a fund must determine the fund member category factor; and

(b) the information that the contribution certificate contemplated in subparagraph (4) must contain.

(6) No value must be placed in terms of this paragraph on the taxable benefit derived from any contribution made by an employer to a fund—

(a) for the benefit of a member of that fund who has retired from that fund; or

(b) in respect of the dependants or nominees of a deceased member of that fund.'.

Subsection (1) comes into operation on 1 March 2015.

4. RETIREMENT REFORMS – DRAFT EXPLANATORY MEMORANDUM – FIRST BATCH OF THE TLAB 2014

VALUATION OF FRINGE BENEFIT FOR DEFINED BENEFIT CONTRIBUTIONS

[Applicable provision: Paragraph 1 and 12D of the Seventh Schedule and the introduction of specific regulations]

I. Background

In 2013 changes were made in the Taxation Laws Amendment Act of 2013 regarding the valuation of defined benefit contributions by an employer as a fringe benefit in the hands of the employee.

Defined benefit funds have retirement benefits that are calculated according to the rules of the pension fund where the value of the contributions to the fund may not be an accurate reflection of the benefits that may be received by the retirement fund member. For example, if the pension fund is in financial difficulty and the employer needs to make additional contributions to meet the expected liabilities, it may be unfair to tax the individual on those contributions as if they were a fringe benefit if there is no associated increase in benefits.

In order to avoid these discrepancies, align the tax treatment of contributions to defined contributions pension funds and defined benefit pension funds and to improve fairness in relation to the receipt of retirement benefits within defined benefit funds, a formula was introduced to approximate the increase in retirement benefits within a defined benefit fund.

The formula calculates a notional employer contribution to the defined benefit fund based on the estimated increase in retirement benefits. The notional amount is deemed a fringe benefit to the employee.

II. Reasons for change

The formula that was included in the Taxation Laws Amendment Act of 2013 requires the use of a factor to determine the value of the notional employer contribution. The amendments provide the methodology that should be used by the pension fund actuaries to calculate the factor that is used by the employer as an input in the final formula. The amendments also describe the processes required to ensure that the factor and additional relevant information is provided on a timely basis to employers and has been verified by the appropriate personnel.

With regard to hybrid pension funds which have an ‘underpin’ component, the amendments also provide additional details on the calculation of the notional employer contributions. These funds have retirement benefits which consist of both a defined contribution element and a defined benefit element, but where the retirement benefit is based on whichever element is greater.

III. Proposal

A. Fund member category

The amended proposal relies on the concept of a ‘fund member category’. A ‘fund member category’ is a group of members of a fund whose entitlement to receive benefits and the value of those benefits when they are received are determined by the same rules, and in respect of whom the same contributions are paid as a proportion of pensionable salary by them and by their employer. The notional employer contribution should be calculated separately for each fund member category of a fund.

This refinement is introduced to ensure that the notional employer contributions are calculated across groups of members in the same way as the fund pools contributions and the costs of paying benefits across members. The calculation of notional employer contribution, which is used to calculate the total pension contributions and is assessed as a percentage of taxable income to determine deductibility, thus introduces no additional unfairness between different individual members beyond that which is already captured in the fund rules.

<u>Example A:</u>

A retirement fund has an accrual rate of 1/55 for all members in respect of service less than ten years, rising to 1/40 in respect of service greater than ten years. The employer pays a contribution rate of 16% of pensionable salary in respect of all members of the fund, and all members pay contributions at a rate of 7.5% of pensionable salary.

Although the fund has two accrual rates, all members are eligible to receive the additional accrual under the same circumstances, and the employer and employee contribution rates are the same for all members. The fund therefore pools costs across members with less than ten years’ service and members with more than ten years’ service. There is thus only one fund member category.

Example B:

A retirement fund has an accrual rate of 1/55 for staff and 1/30 for executives. The employer pays contributions of 20% of pensionable salary for staff and 30% of pensionable salary for executives. Since a different contribution rate is paid by the employer, there are two fund member categories and separate notional employer contribution amounts should be calculated for each.

B. Contribution certificate

It is proposed that a separate 'contribution certificate' be provided by the Fund for each fund member category, to the employer and SARS. The 'contribution certificate' must contain various pieces of information, including:

- Details of the pension fund and year of assessment to which the certificate applies;
- Details of the employer; the different components of the fund – whether they be defined benefit components, defined contribution components; risk benefit components or hybrid elements; and
- The fund member category factor for the applicable fund member category.

Requirements for the contribution certificate are laid out in a regulation.

C. Calculation of the value of the fringe benefit

To calculate the notional employer contribution to a defined benefit fund, the employer would need to multiply the pensionable salary by the 'fund member category factor' that is provided in the 'contribution certificate' and subtract the value of any contributions made by the employee.

The pension fund would be required to calculate the 'fund member category factor' by following the calculation method specified in the regulation. This requires the fund to separate benefits for which members of the fund are eligible into defined benefit, defined contribution, underpin and risk benefit components. A separate calculation method is specified for each type of component. If the fund offers more than one benefit component of a particular type, a calculation would need to be performed for each benefit component separately, and the results aggregated.

D. Defined benefit component factor

A formula is prescribed for the calculation of this factor. The formula assumes that the defined benefit on retirement is a combination of an annuity and a lump sum.

The value of the annuity accrual is determined by multiplying the annuity accrual rate by a number intended to reflect the value of the benefits, which depends on the pension increase policy of the pension fund in terms of section 14B(3) of the Pension Funds Act and the average age at which members of that fund member category retire from the fund with benefits that are unreduced or un-augmented in terms of the fund rules as a consequence of the age at which they retire. The number is read off a table provided in the regulation.

This table has been calculated taking the following factors into consideration:

- Average expected levels of post-retirement mortality
- Average expected levels of pre-retirement mortality
- Expected investment returns pre- and post-retirement on a portfolio of assets whose term, nature and security broadly matches the lump-sum and annuity liabilities promised by defined benefit pension funds
- The average level of spousal benefits provided by pension funds
- The prices of annuities available in the private market.

Consistent with the overall methodology, the intention of the factors is to approximately reflect some estimate of the long-run cost of providing a benefit to a particular group of members, rather than the pace at which particular employers may choose to fund for those benefits.

The annuity accrual rate is defined as the average increase (over all members of the fund member category) in the annuity benefit expressed as a proportion of final salary occurring as a result of membership of the fund over the year of assessment, assuming that individual members remain in the fund until retirement. Valuators should first calculate the improvement in annuity benefits expressed as a proportion of final salary for each individual member over the year of assessment, and then take the average across all members of the fund member category. For funds without split accrual this should be a simple exercise.

If the fund pays a lump sum benefit on retirement, the lump sum accrual rate would be multiplied by 0.9 to estimate the increase in the lump sum retirement benefit. These amounts are added together to obtain the defined benefit component factor.

Lump sum and annuity accrual rates should be calculated after any commutation to which members may be entitled, based on the average rate at which members have exercised this option in the recent past, and the terms upon which that commutation is exercised.

E. Underpin component factor

Retirement funds that have an ‘underpin’ would use a revised formula which takes the maximum of either the defined benefit sub-component factor calculated using the method specified above or the defined contribution sub-component factor and adds 10 per cent of whichever component factor is smaller. Adding the 10 per cent is intended to represent the additional benefit to the member of having the protection offered by the underpin.

F. Risk benefit component factor

The risk benefit component factor is calculated by multiplying the average risk benefit that members of the fund member category are entitled to should they die in the year of assessment, expressed as a proportion of pensionable salary, by 0.01. (Disability benefits are not valued by the formula, but are expected to be broadly proportional to the value of the death benefits). As before, the valuator should first calculate the risk benefits payable to each individual member or their dependents as a proportion of pensionable salary, and then take an average of members of the fund member category. Any defined contribution account values paid to the member's dependents on their deaths should be excluded from this calculation.

The 'fund member category factor' (that the employer will use to value the notional employer contribution) is the sum of the defined benefit component factor and the risk benefit component factor.

G. Defined contribution component factor

The defined contribution component factor is equal to the contribution rate in respect of the defined contribution benefit component.

The fund member category factor is the aggregate of all the factors calculated in respect of the benefit components of the fund.

The contribution certificate must be compiled by the board of the pension fund in consultation with the valuator of the fund and must be provided to the employer at least a month before the year of assessment.

Example A:

An employer offers a defined benefit pension to their employees, which has an annuity accrual rate of 1/55 for those who have less than ten years' service and 1/40 for those who have more than ten years' service. The fund also pays a lump sum at retirement of 0.067 of final salary per year of service. The fund reports that the average increase in pension benefits over the previous five years has been 100% of CPI. Members of this fund are able to retire from age 60 with unreduced benefits in terms of the rules, but their actual average retirement age is 63.

There are no differences in contribution rates or rules determining the eligibility for and value of the benefits paid to members of the fund so there is only one fund member category. The pension fund is required to complete a 'contribution certificate' for that fund member category that needs to be passed on to the employer one month before the start of the individuals' tax year.

The pension fund would need to calculate the expected actual accrual rate for members. This value is calculated by averaging the increase in the annuity accrual across all members during the year of assessment. Since the fund has increased benefits for those who have served longer than ten years, the average annuity accrual rate is 1/50. The pension fund then needs to read off the value in the table of numbers provided in the annexure that is associated with the average retirement age of fund members – 63 – and the actual average pension increases granted over the last five years – 100% of CPI. The number to be used in the defined benefit component factor calculation is therefore 9.9.

The defined benefit component factor is calculated according to the formula in the regulations and equals (1/50 * 9.9) + (0.067 * 0.9) which is 0.2583.

The pension fund would also calculate the average risk benefit that members (or their dependents or nominees) would be entitled to upon death should they die during the year of assessment, expressed as a proportion of their pensionable salary. If this amount is two times pensionable salary the risk benefit component factor would equal (2 * 0.01) which is 0.02.

Since there are no other benefit components for which calculation methodologies are supplied, the defined benefit component factor and the risk benefit component factor are added together in the 'contribution certificate' to get a fund member category factor of 0.2783.

The employer, or the payroll company, would receive this number from the pension fund in the 'contribution certificate' and use it in the formula provided in the legislation to calculate the value of the notional employer contribution (which would be a fringe benefit). An employee who had a gross annual salary of R500 000 and a pensionable salary of R350 000, with employee contributions of 7.5% of pensionable salary, would have a notional employer contribution of (0.2783 * 350 000) – (0.075 * 350 000) = 97 405 – 26 250 = R71 115 for the year of assessment.

To check whether the employee is within the allowable deductible limits of either 27.5% of total remuneration or the R350 000 deductibility cap, the employer would need to add the notional employer contribution onto gross salary to obtain total remuneration. In this example total remuneration would be (500 000 + 71 115) = R571 115 and the total contributions to a retirement fund would be (71 115 + 26 250) = R97 405. The percentage contribution to the retirement fund is thus (97 405 / 571 115) which is 17.06%. The individual could make further retirement contributions (say to a retirement annuity) of up to (0.275 – 0.1706) * 571 115 = R59 629 while still receiving a tax deduction.

Example B:

An employer offers a hybrid pension scheme to their employees. On retirement, the employees get a benefit which is the greater of 1/40 of their final salary per year of service and an annuity which can be purchased by a contribution rate of 15% of pensionable salary to a defined contribution account. The fund allows retirement from age 63 and the pension benefits granted over the previous five years has averaged 100% of CPI. Death benefits are 3 times pensionable salary plus the value of the defined contribution account on death.

The fund therefore has one fund member category, who are eligible for two benefit components – a risk benefit and an underpin benefit.

The value of the underpin benefit is the greater of the factor in respect of the defined benefit sub-component and the factor in respect of the defined contribution sub-component plus 10% of the lesser of the two.

Following the method described above, the value of the defined benefit sub-component factor is 9.9 / 40 = 0.2475. The defined contribution sub-component factor has a value of 0.15. The underpin component factor is therefore equal to 0.2475 + 0.1 x 0.15 = 0.2625.

The risk benefit component is valued at 0.01 x 3 = 0.03 (the value of any defined contribution account paid out on death is excluded from the calculation of risk benefit factors).

The fund member category factor is therefore 0.2625 + 0.03 = 0.2925.

IV. Effective date

The proposed amendments are effective as from 01 March 2015 and will be applicable in respect of years of assessment commencing on or after that date.

5. RETIREMENT REFORMS – DRAFT REGULATIONS – DETERMINATION OF THE FUND MEMBER CATEGORY FACTOR

Definitions

1. In these Regulations, any word or expression to which a meaning has been assigned in Income Tax Act, 1962 (Act No. 58 of 1962), bears the meaning so assigned, and—

'annuity accrual rate' means, in relation to a period for which a certificate is issued, the increase in the annuity benefit of a defined benefit component —

(a) occurring as a result of fund membership during the period in respect of which the certificate is issued; and

(b) expressed as the average of a proportion of final salary (as defined in the rules of the fund) in respect of all members of a fund member category;

as if all those members would have remained members of the fund until those members may retire from employment with unreduced benefits in terms of the rules of fund.

'annuity benefit' means an annuity—

(a) payable by a fund on retirement in consequence of membership or past membership of that fund;

(b) in respect of which a portion of the final salary (as defined in the rules of the fund) is utilised to calculate the amount of the benefit of the fund member; and

(c) in respect of a lump sum commuted for a payment in the form of an annuity;

'lump sum' means an amount—

(a) payable by the fund on retirement in consequence of membership or past membership of that fund to a member of that fund or to a dependant or nominee of that member;

(b) of which the value is calculated as constituting a portion of the final salary (as defined in the rules of the fund) of the fund member; and

(c) any amount in respect of an annuity commuted for a payment in the form of a lump sum;

'lump sum accrual rate' means in relation to a period for which a certificate is issued, the increase in the lump sum of a defined benefit component—

(a) occurring as a result of fund membership during the period in respect of which the certificate is issued; and

(b) expressed as the average of a proportion of final salary in respect of all members of a fund member category;

'risk benefit' means a benefit payable in respect of the death or permanent disablement of a member to that member or to a dependant or nominee of that member.

Fund member category factor is aggregate

2. The fund member category factor must, for the purposes of paragraph 12D(2) of the Seventh Schedule to the Income Tax Act, 1962, be calculated by aggregating—

(a) the defined contribution component factor determined as prescribed by regulation 3;

(b) the defined benefit component factor determined as prescribed by regulation 4;

(c) the underpin component factor determined as prescribed by regulation 5, and

(d) the risk benefit component factor determined as prescribed by regulation 6,

for that fund member category.

Determination of defined contribution component factor

3. (1) The defined contribution component factor is the contribution rate (as specified in the rules of the fund) in respect of the total of the contributions to the fund by the employee and the employer in respect of each defined contribution component.

(2) Any contribution in respect of a risk benefit provided by the fund directly or indirectly for the benefit of a member of the fund or a dependant or nominee of that

member must not be taken into account in determining the fund member category factor as contemplated in subregulation (1).

(3) If a fund member is entitled to receive more than one contribution component in respect of a fund member category—

(a) the fund must calculate a defined contribution factor in respect of each defined contribution component; and

(b) the defined contribution component factor for the purposes of this regulation is the sum of the amounts calculated in terms of paragraph *(a).*

Determination of defined benefit component factor

4. (1) The defined benefit component factor in respect of a defined benefit component must be determined in accordance with the formula—

$$X = (A \times B) + (C \times D)$$

in which formula—

(a) **'X'** represents the defined benefit component factor to be determined;

(b) **'A'** represents the annuity accrual rate;

(c) **'B'** represents the number that must be obtained—

(i) by establishing the percentage in respect of the amount of the annual pension increase as contemplated in section 14B(3)*(a)* of the Pension Funds Act in terms of the rules of the fund based on the consumer price index for members of that fund member category;

(ii) by establishing the number of the average age at which members of that fund member category retire without any retirement benefit being reduced or increased as a result of that retirement in terms of the rules of the fund; and

(iii) where the column and line intersect when—

(A) the percentage in subparagraph (i) is matched with the corresponding percentage in the 'Consumer Price Index' line in Schedule I; and

(B) the number of the age contemplated in subparagraph (ii) is matched with the corresponding number in the 'Youngest Age of Retirement' column Schedule I:

Provided that if any percentage contemplated in subparagraph (i) or any number contemplated in subparagraph (ii) does not correspond with any percentage or number in Schedule 1, the percentage to be taken into account is the lesser of the nearest percentage in Schedule 1 to the established percentage and the number to be taken into account is the lower of the nearest number in Schedule 1 to the established number.

(d) **'C'** represents the lump sum accrual rate; and

(e) **'D'** represents the number 0.9.

(2) If a fund member is entitled to receive more than one defined benefit component in respect of a fund member category—

(a) the fund must calculate a defined benefit component factor in respect of each defined benefit component; and

(b) the defined benefit component factor for the purposes of this regulation is the sum of the factors calculated in terms of paragraph *(a).*

Determination of underpin component factor

5. (1) The underpin component factor must be determined in accordance with the formula—

$$X = A + B \times C$$

in which formula—

(a) **'X'** represents the underpin component factor to be determined;

(b) **'A'** represents the greater factor of—

(i) the defined contribution component factor calculated utilising the formula in regulation 3(1) for the defined contribution component used for the purposes of determining the underpin component; or

(ii) the defined benefit component factor calculated by utilising the formula in regulation 4(1) for the defined benefit component used for the purposes of determining the underpin component.

(c) **'B'** represents the number 0.10; and

(d) **'C'** represents the smaller factor of—

(i) the defined contribution component factor calculated utilising the formula in regulation 3(1) for the defined contribution component used for the purposes of determining the underpin component; or

(ii) the defined benefit component factor calculated by utilising the formula in regulation 4(1) for the defined benefit component used for the purposes of determining the underpin component.

(2) If a fund member is entitled to receive more than one underpin component in respect of a fund member category —

(a) the fund must calculate an underpin component factor in respect of each defined underpin component; and

(b) the underpin component factor for the purposes of this regulation is the sum of the factors in terms of paragraph *(a).*

Determination of risk benefit component factor

6. (1) The risk benefit component factor must be determined in respect of all risk benefits provided by the fund directly or indirectly for the benefit of a member of the fund or a dependant or nominee of that member

(2) The risk benefit component factor must be determined in accordance with the formula

$$X = A \times B$$

in which formula—

'X' represents the risk benefit component factor to be determined;

'A' represents the number 0.01; and

'B' represents the average of a proportion of retirement funding income in respect of all members of the fund member category in respect of risk benefits to which the member or his or her dependants or nominees would have become entitled if the member had died during the year of assessment in respect of which the certificate is issued.

(2) If a fund member is entitled to receive more than one risk benefit component in respect of a fund member category—

(a) the fund must calculate a risk benefit component factor in respect of each risk benefit; and

(b) the risk component factor for the purposes of this regulation is the sum of the factors calculated in terms of paragraph *(a).*

Short title and commencement

7. These Regulations are called the Regulations in terms of paragraph 12D(5)*(a)* of the Seventh Schedule to the Income Tax Act, 1962, on the determination of the fund member category factor and come into operation on 1 March 2015.

6. RETIREMENT REFORMS – DRAFT REGULATIONS – INFORMATION TO BE CONTAINED IN CONTRIBUTION CERTIFICATES

SCHEDULE

Definitions

1. In these Regulations, any word or expression to which a meaning has been assigned in Income Tax Act, 1962 (Act No. 58 of 1962) or the Regulations in terms of paragraph 12D(5)(*a*) of the Seventh schedule to the Income Tax Act, 1962, on the determination of the fund member category factor bears the meaning so assigned.

Persons that must prepare contribution certificate

2. The contribution certificate must be prepared by the board, as defined in section 1 of the Pension Funds Act, in consultation with the valuator of that fund.

Signing of contribution certificate

3. The contribution certificate must be signed by the valuator of the fund and two board members of the board of the fund, as contemplated in section 7A of the Pension Funds Act, and the principal officer of the fund as contemplated in section 8 of the Pension Funds Act;

Preparation of contribution certificate in respect of each fund member category

4. A contribution certificate must be prepared in respect of each fund member category in respect of each year of assessment

Content of contribution certificate

5. A contribution certificate must contain—

(a) the year of assessment in respect of which the contribution certificate is issued;

(b) the name and such details as are necessary to identify the fund that issues the certificate;

(c) the name and such details as are necessary to identify the employer in respect of whose employees the contribution certificate is issued;

(d) the fund member category in respect of which the certificate is issued;

(e) the defined contribution, defined benefit and underpin components for which members of that fund member category may become eligible in terms of the rules of the fund;

(f) the fund member category factor for the fund member category in respect of which the contribution certificate is issued;

(g) an analysis of the fund member category factor in a manner indicative of the composition of the fund member category factor in respect of the defined contribution component factor, defined benefit component factor, underpin component factor and risk benefit factor of which that fund member category factor is comprised;

(h) an analysis of the actual contribution rate to the fund in respect of members of the fund member category a manner indicative of the composition of the

contributions in respect of employer and employee contributions and the defined benefit, defined contribution and underpin components;

(i) an analysis of how the retirement funding employment income of members of the fund member category to which the contribution certificate applies relates to the final salary used for benefit calculations for those members in terms of the rules of the fund;

(j) a setting out of the pension increase policy of the fund and to what extent the pension increases actually granted to the members of a fund member category in respect of the previous five years accords with that pension increase policy;

(k) an analysis of the actual retirement ages of members of the fund in respect of the previous five years and the adjustments which were applied to benefits of those members who retired earlier or later during those five years than the retirement age stipulated in the fund rules;

(l) an analysis of any benefit increases in respect of past service, granted over the year of assessment in respect of which the contribution certificate is issued (including changes in retirement age, pension increase policy and the definition of pensionable salary); and

(m) an description and detailed explanation of any matter which may have an effect on the difference between the value of benefits for tax purposes in terms of these Regulations and the current or future cost of paying for these benefits.

Short title and commencement

6. These Regulations are called Regulations in terms of paragraph 12D(5)*(b)* of the Seventh Schedule to the Income Tax Act, 1962, on the information to be contained in contribution certificates and come into operation on 1 March 2015.

7. DRAFT REGULATIONS

7.1 Registration for VAT vendors – Briefing Note on the draft registration regulations

BRIEFING NOTE ON THE DRAFT REGISTRATION REGULATIONS

Following the 2013 Budget announcement that VAT registration would be streamlined to ease the compliance-burden while guarding against fraud, certain amendments have been made to voluntary registration for VAT purposes and include the following:

- The scope of section 23(3)(*b*) has been broadened to allow a person to voluntarily register as a vendor where that person has not yet made any taxable supplies or has made taxable supplies which do not exceed R50 000 and there is a reasonable expectation that the person would make taxable supplies exceeding R50 000 within the following 12-month period commencing from the date of registration.
- The ambit of the application of section 23(3)(*d*) is clarified. In order to register under this section, a person must demonstrate that such person conducts a continuous and regular activity and that due to the nature of the activity, taxable supplies are likely to be made only after a period of time.

Provision is made for Regulations to be issued:

(i) specifying the proof that a person must provide in order to be successfully registered;

(ii) setting out the requirements that must be met by a person applying for voluntary registration as a vendor under section 23(3)(*b*)(ii) [the person applying for registration only has to meet the requirements for one of the listed categories]; and

(iii) prescribing the activities that would constitute an activity for which a long lead time is normally experienced before any taxable supplies can be made.

The requirements referred to in (ii) require a person to provide proof that:

- the average value of taxable supplies made in the months preceding their application for registration, exceeded R4 200;
- taxable supplies made for one month exceeded R4 200, if the enterprise has only made taxable supplies for one month;
- the vendor has entered into a written contracts evidencing the contractual liability to make taxable supplies exceeding R50 000 in the following 12 months;
- the vendor has entered into a finance agreement and the total annual repayments under that agreement is in excess of R50 000; and
- expenditure has been incurred or will be incurred for purposes of the enterprise and the annual repayments of such expenditure will exceed R50 000.

The activities referred to in (iii) are:

- Agriculture
- Forestry
- Aquaculture
- Mining
- Construction
- Property development
- Infrastructure development

7.2 VAT Registration section 23(3)(b)(ii) regulation

DEFINITIONS

1. In this regulation, unless the context indicates otherwise, any word or expression to which a meaning has been assigned in the Act, has the meaning so assigned, and the following terms have the following meaning:

'Banks Act' means the Banks Act, 1990 (Act No. 94 of 1990);

'National Credit Act' means the National Credit Act, 2005 (Act No. 34 of 2005);

'Tax Administration Act' means the Tax Administration Act, 2011 (Act No. 28 of 2011); and

'the Act' means the Value-Added Tax Act, 1991 (Act No. 89 of 1991).

REQUIREMENTS TO BE MET

2. (1) A person carrying on any enterprise and the total value of taxable supplies made or to be made has not exceeded R50 000, but can reasonably be expected to exceed that amount within 12 months from the date of registration qualifies to register as a vendor. That person must in addition to the information required in terms of Chapter 3 of the Tax Administration Act, provide the Commissioner with the following to substantiate that such enterprise is reasonably expected to make taxable supplies in excess of R50 000 in the following 12 months reckoned from the date of registration:

(2) Taxable supplies made for more than two months:

(a) Proof that the average value of taxable supplies made by the person in the preceding months, prior to the date of application for registration, exceeded R4 200 per month;

(b) For purposes of determining the average value of taxable supplies, the person must use the value of taxable supplies made for a minimum of two and a maximum of eleven months immediately preceding the date of application.

(3) Taxable supplies made for one month: In the case where the person's enterprise has only made taxable supplies for one month, proof that the total value of taxable supplies made by the person in that month has exceeded R4 200;

(4) Written Contracts: A written contract in terms of which the person is required to make taxable supplies in excess of R50 000 in the following 12 months reckoned from the date of registration.

(5) Finance Agreements: A copy of the relevant agreement where the person has entered into—

(a) a financial agreement with a bank registered in terms of the Banks Act;

(b) a 'credit agreement' with a 'credit provider' as defined in the National Credit Act; or

(c) an agreement with a designated entity, public authority or any other person who continuously or regularly provides finance;

wherein the person mentioned in *(a)*, *(b)* or *(c)* above has agreed to fund the expenditure incurred or to be incurred in the commencement or furtherance of the enterprise and the total annual repayments in terms of that financial, credit or other agreement will exceed the amounts contemplated in sub-paragraph (6)(*b*) below; or

(6) Expenditure:

(a) Proof of—

(i) expenditure incurred or to be incurred in connection with the commencement or furtherance of the enterprise, as set out in any written agreement entered into by such person; or

(ii) capital goods acquired in connection with the commencement of the enterprise, together with proof of payment or any extended payment agreement entered into; and

(b) the total annual repayment of items contemplated in sub-paragraph (6)*(a)*(i) and (ii), where applicable, will in the following 12 months reckoned from the date of registration exceed R50 000.

7.3 VAT Registration section 23(3)(d) regulation

DEFINITIONS

1. In this regulation, unless the context indicates otherwise, any word or expression to which a meaning has been assigned in the Act, bears the meaning so assigned and the following terms have the following meaning:

'the Act' means the Value-Added Tax Act, 1991 (Act No. 89 of 1991).

NATURE OF ACTIVITIES

2. (1) A person may register as a vendor at the time that any goods or services are acquired directly in respect of the commencement of a continuous and regular activity set out below:

(a) Agriculture:

(i) The cultivating of land for purposes of producing crops; or

(ii) The breeding and raising of livestock or wild animals;

(b) Forestry: The planting, maintaining and harvesting of tree plantations;

(c) Aquaculture: The cultivating of freshwater or saltwater aquatic organisms;

(d) Mining: The exploring and/or extracting of any mineral, metal and/or natural gas resource;

(e) Construction: The construction of ships, yachts, other floating vessels, aircrafts, locomotives or similar structures;

(f) Property Development (including Township Development): The construction of residential or commercial buildings for purposes of selling or leasing, provided the activity is not an exempt activity contemplated in section 12 of the Act.

(g) Infrastructure Development: Infrastructure development in the form of buildings or similar permanent installations and structures, for purposes of carrying on that person's enterprise, where the—

(i) total value of such acquisition, under any contractual obligation, exceeds R1 million; and

(ii) completion phase of such infrastructure will exceed 12 months from date of commencement of that development.

(2) A person conducting any activity listed in paragraphs (*a*) to (*g*) must, where required in terms of any legislation, have applied for or be in possession of the relevant permit, licence or similar document, issued or to be issued by the appropriate regulatory authority, authorising that person to conduct that activity.

7.4 Draft public notice listing reportable arrangements for purposes of section 35(2) and 36(4) of the Tax Administration Act

This draft notice proposes the list of reportable arrangements that have certain characteristics that may lead to an undue tax benefit as well as the list of reportable arrangements that are not likely to lead to an undue tax benefit.

This notice replaces, with effect from the date of publication thereof, all previous notices issued under sections 80M(2)*(c)* and 80N(4) of the Income Tax Act, 1962 (Act No. 58 of 1962), and section 35(2) of the Tax Administration Act, 2011.

1. General

In this notice, unless the context indicates otherwise, any word or expression to which a meaning has been assigned in the Income Tax Act, 1962 (Act No. 58 of 1962), or section 1 or section 34 of the Tax Administration Act, 2011 (Act No. 28 of 2011), has the meaning so assigned.

2. Reportable arrangements

2.1. Subject to the provisions of paragraph 3, the following arrangements have been identified to have certain characteristics that may lead to an undue tax benefit:

2.1.1. Any arrangement in terms of which fees that are payable or may become payable, on or after the date of publication of this notice, by a person that is a resident to a person that is not a resident with regard to services rendered to that resident in the Republic, exceed or are reasonably expected to exceed R5 million;

2.1.2. Any arrangement in terms of which a company buys back shares, on or after the date of publication of this notice, from one or more shareholders for an aggregate amount of at least R10 million, if that company issued or is required to issue any shares within 12 months of entering into that arrangement or of the date of any buy-back in terms of that arrangement;

2.1.3. Any arrangement that is expected to give rise, on or after the date of publication of this notice, to any rebate in respect of foreign taxes if the amount of the rebates to be taken or that have been taken into account in determining normal tax payable by any person or persons that is or are party to that arrangement, exceeds or is reasonably expected to exceed an aggregate amount of R5 million;

2.1.4. Any arrangement in terms of which a person that is a resident makes contributions or payments, on or after the date of publication of this notice, to a trust that is not a resident and acquires a beneficial interest in that trust, where the amount of all contributions or payments or the value of the interest exceeds or is reasonably expected to exceed R10 million, excluding any contributions or payments made, or beneficial interest acquired in any:

(a) portfolio comprised in any investment scheme contemplated in paragraph *(e)*(ii) of the definition of 'company' in section 1(1) of the Income Tax Act; or

(b) foreign investment entity as defined in section 1(1) of the Income Tax Act;

2.1.5. Any arrangement in terms of which a person or persons, by means of acquiring shares or voting rights on or after the date of publication of this notice, acquire the controlling interest in a company that—

(a) has carried forward or expects to carry forward a balance of assessed loss exceeding R20 million from the year of assessment immediately preceding the year of assessment in which the controlling interest is acquired; or

(b) expects to have an assessed loss exceeding R20 million in the year of assessment during which the controlling interest is acquired;

2.1.6. Any arrangement in terms of which an amount that exceeds or is reasonably expected to exceed R5 million is or becomes payable by a person that is a resident to a person that qualifies as an insurer in terms of any law of any country other than the Republic (hereinafter referred to as the insurer) if any amount or amounts payable, on or after the date of publication of this notice, in cash or otherwise, to any beneficiary in terms of that arrangement are to be determined mainly by reference to the value of particular assets or categories of assets that are held by or on behalf of the insurer or by another person for purposes of that arrangement.

2.2. If a person becomes a participant in an arrangement referred to in paragraph 2.1 before the date of publication of this notice and that arrangement qualifies as a reportable arrangement on that date, the date upon which the 45 days reporting obligation period referred to in section 37(4) of the Tax Administration Act commences is regarded as the date of this publication.

3. Excluded arrangements

3.1. The following has been identified as an arrangement which is not likely to lead to an undue tax benefit: Any arrangement where the tax benefit which is or will be derived or is assumed to be derived from that arrangement does not exceed R5 million.

8. TAX CASES

8.1 C:SARS v Miles Plant Hire (Pty) Ltd

Applicant, being the Commissioner for SARS, had filed an urgent application in which it sought *inter alia* an order to set aside a resolution adopted by Respondent, being Miles Plant Hire (Pty) Ltd to file for voluntary business rescue and for the final winding-up of Miles Plant Hire.

Subsequent thereto, the business rescue practitioner, whose appointment was in part the subject of the application, had filed a notice in terms of section 132(2)(*b*) of the Companies Act 71 of 2008 terminating the business rescue proceedings, with the result that the only remaining issue for adjudication was the winding-up.

Miles Plant Hire had filed a notice of its intention to argue a question of law concerning the interpretation of section 177(3) of the Tax Administration Act 28 of 2011 in that it contended that the section in question required SARS to seek leave to institute the present application for winding-up since there was a disputed tax debt in respect of which an appeal was pending.

Section 177(1) provided that SARS may institute proceedings for the sequestration, liquidation or winding-up of a person for a tax debt and s 177(3) provided that if the tax debt was subject to an objection or appeal or a further appeal against a decision by the tax court, the proceedings may only be instituted with leave of the court before which the proceedings were brought.

SARS, after the filing of the notice of intention to argue a point of law, had filed a notice to amend its notice of motion by adding a prayer in terms of which it sought leave to institute the winding-up proceedings.

Miles Plant Hire did not oppose the amendment and, shortly before the hearing of the application, the parties had agreed that if the question of law was decided in favour of SARS, then Miles Plant Hire would concede the merits of the application and if Miles Plant Hire succeeded, the Application stood to be dismissed.

Miles Plant Hire had a disputed tax debt of R37 441 091.55 in respect of which an appeal was pending and it was common cause that it had submitted objections against certain assessments raised by SARS and that the objections had been disallowed, hence the pending appeal which was to be heard in the Tax Court during November 2013.

Miles Plant Hire, in its challenge to the assessments under appeal, did not directly challenge the *quantum* of the tax debt which was the subject of a certificate filed in terms of section 172 of the Tax Administration Act as outstanding, and therefore a civil judgment in favour of SARS for a liquid debt.

Furthermore, Miles Plant Hire's sole shareholder had entered a plea of guilty to fraud and tax evasion, being income tax and VAT for the 2007 and 2008 tax years, and that returns for the 2010, 2011 and 2012 tax years remained outstanding.

Miles Plant Hire's primary basis for its objection was that the penalty in the circumstances was 'inordinate and harsh' and that it had 'never been the intention of [Miles Plant Hire's sole shareholder] to avoid her tax obligations or to defraud SARS in any manner' and Miles Plant Hire's notice of appeal blamed its internal accountant for the state of its financial affairs.

Miles Plant Hire contended that the provisions of section 177(3), properly construed, required SARS to seek the court's leave to institute the winding-up proceedings prior to the winding-up proceedings being instituted by way of notice of motion and since SARS had omitted to do so, Miles Plant Hire contended that the winding-up application was premature and that it stood to be dismissed on that basis.

Miles Plant Hire contended further that the intention of the legislature is to be divined by reference to the ordinary grammatical meaning of the words used and these envisaged that an application for winding-up may 'only be instituted' with the leave of the court before which the proceedings are to be brought, i.e. that an application for winding-up may be instituted if and only if prior leave has been granted by the court before which any winding-up proceedings are ultimately brought.

SARS contended that it was open to it, in those instances where an appeal against a tax debt is pending, to bring winding-up proceedings before a court and to seek leave from that court to pursue the application.

Acting Judge van Niekerk held the following:

(i) That what was undisputed was that section 177(3) of the Tax Administration Act conferred a discretion on the court, when there was a pending tax dispute, to permit a tax debt to be recovered in sequestration, liquidation or winding-up proceedings and what was in issue was when that discretion had to be exercised.

(ii) That the principles of interpretation to be applied were recently affirmed in *Natal Joint Municipal Pension Fund* v *Edumeni Municipality* per Wallis JA and what the judgment underscored was that the exercise of interpretation did not require a court to discern the intention of the legislature only by reference to plain meaning of words with a deferential nod, if so required, in the direction of the *Oxford English Dictionary*.

(iii) That, starting with the language of the subsection, to 'institute' a proceeding is not necessarily limited to the act of service of a notice of motion; proceedings were equally capable of being instituted in the sense of 'initiated' or 'started' or 'commenced' once a matter served before a court and after any required preliminary matters had been dealt with.

(iv) That, in other words, the limitation in the language was one which precluded a court, when sequestration, liquidation or winding-up was sought in the face of a pending objection or appeal, from exercising its discretion in relation to the merits of the application unless and until all of the facts and circumstances relevant to the pending tax appeal are considered. This did not require the court to determine the appeal; what was required was a consideration of the grounds of appeal and a consideration of whether they might reasonably disclose any merit.

(iv) That if leave to institute the proceedings was refused, the proceedings are discontinued, whether by way of postponement pending the outcome of the appeal or some other appropriate outcome and this meaning is sustained by the words ' . . . with leave of the court before which the proceedings are brought.' The 'proceedings' in this context can only mean the proceedings referred to in subsection (1), i.e. the sequestration, liquidation or winding-up proceedings and the tense employed ('are brought') in section 177(3) indicated that it is the court before which the proceedings serve that is enjoined to grant or refuse leave, not a court before which at some future date the proceedings are to be brought.

(v) That the interpretation contended for by Miles Plant Hire would require SARS first to apply to court to obtain permission to institute sequestration, liquidation and winding-up proceedings, as the case may be and at that stage the issue before the court would be limited to whether SARS ought to be afforded leave to commence winding-up proceedings by way of notice of motion, notwithstanding the fact of a pending objection or appeal. It might be assumed that a Miles Plant Hire in such proceedings would seek to make out a case to the effect that the assessments in question are incorrect, to the extent that once corrected, the entity concerned would not be insolvent.

(vi) That should leave to institute the proceedings be granted, a further application would then have to be prepared and brought before a different judge. There was nothing in the subsection, on Miles Plant Hire's interpretation, that would preclude a Miles Plant Hire from again raising, in relation to the merits of the application, the fact of a pending objection or appeal, the merits of the appeal or, for example, from seeking a postponement of the winding-up proceedings pending the outcome of the ruling by the Commissioner or the Tax Court as the case may be.

(vii) That this would lead to an absurd result, where the discretion exercised in the first application potentially fetters the court before which the subsequent, substantive application is served and a discretion is best exercised once, with full knowledge of all of the relevant facts and circumstances.

(viii) That the words 'the proceedings may only be instituted with the leave of the court before which the proceedings are brought' mean that the disputed tax debt is not recoverable under the 'pay now, argue later' rule during winding-up proceedings, unless the court before which those proceedings serve, permits it.

(ix) Such an interpretation affirms the court's inherent discretion in winding-up proceedings, and empowers the court to evaluate all of the appropriate facts and circumstances including the merits of any objection and pending appeal and to make an appropriate order.

(ix) That there was nothing in the papers that persuaded the court that there were any grounds in terms of which the court should be inclined to refuse leave to institute winding-up proceedings on account of the pending appeal but, on the contrary, the grounds for appeal were clearly intended only to further delay the inevitable.

(x) That it was accordingly just and equitable that Miles Plant Hire's affairs be wound up and that an independent liquidator be appointed to conduct an investigation into Miles Plant Hire's financial affairs and SARS had made out a case for a final winding-up order.

SARS granted leave to institute the winding-up proceedings and Miles Plant Hire was placed under a final order of winding-up.

8.2 ITC 1870

The taxpayer had concluded a private/public partnership with the State Department of Correctional Services to build a prison on State owned land and its brief was to design, construct, operate and maintain a maximum security prison for twenty-five years.

SARS had disallowed the expenditure incurred by the taxpayer and the dispute came before the presiding judge in the Tax Court *a quo* (see *ITC 1845* 73 SATC 80) who had to determine whether the expenditure relating to the construction and various financial expenditures for this project was of a capital or of a revenue nature.

The Tax Court *a quo* found that all the expenditure of some R464 376 824 was of a revenue nature and consequently all the expenditure was deductible in terms of section 22(2A) of the Income Tax Act and the whole amount of some R464 376 824 was treated as trading stock and was deductible.

SARS appealed the decision of the Tax Court *a quo* to the Supreme Court of Appeal and its judgment was reported as *C: SARS* v *South African Custodial Services* (*Pty*) *Ltd* 2012 (1) SA 522 (SCA), 74 SATC 61.

In the Supreme Court of Appeal, Plasket AJA, who delivered the judgment of the court, raised three issues for determination and for reasons relevant to the interpretation of the judgment these were:

- the validity of the taxpayer's objection to the assessment for the 2002 year of assessment,
- the deductibility of the cost of constructing and equipping the prison and
- the deductibility of interest and other costs.

The first of the three issues was essentially a prescription point and the taxpayer succeeded on that point. The second of the three issues was the deductibility of the expenditure of the entire project as being of a revenue nature and the appeal against the Tax Court *a quo*'s decision was upheld and SARS succeeded on that point. The taxpayer succeeded on the third issue being the deductibility of interest and other costs.

Plasket AJA found that expenditure by the taxpayer did not fall within the parameters of section 22(2A) read with section 11(*a*) of the Act as it never carried on any construction or brought building materials onto the site or other trade in the course of which improvements were effected by it to the land which was State owned.

The Supreme Court of Appeal disallowed the deduction of the expenditure of R228 821 436 incurred in respect of the construction of the prison and R95 558 256 in respect of provisioning it and the total amount disallowed was R324 379 692 but since the total amount in issue was R464 376 824, this meant that the Supreme Court of Appeal was left to deal with the balance of the amount claimed which comprised deductibility of interest and other costs.

In order to bid for the tender and raise loans, the taxpayer had to finance the construction of the prison and it incurred a number of fees to various parties and it also incurred interest on its loans and claimed in the alternative to be entitled to a deduction in respect of the various fees and the interest in terms of section 11(*b*A) of the Act.

In order to make sure that the expenses in issue had in fact been incurred in the relevant tax year, the matter was referred back to the Commissioner and this is referred to as the timing issue.

The order issued by the Supreme Court of Appeal stated that '*the assessment is referred back to the Commissioner for him to determine the amount that is deductible from the taxpayer's income in terms of section 11(bA) of the Income Tax Act*.'

Upon being referred back to the Commissioner, he had disallowed the 'further costs' category of R64 346 528 and the only amount and category in issue for interpretation in the Tax Court was whether the 'further costs' of R64 346 528 ought to be deductible in accordance with the judgment of the Supreme Court of Appeal.

This category of 'further costs' comprised for example bid expenses, developer fees, legal fees, insurance, start-up costs, specialist advocate costs and lenders technical advisors costs and the taxpayer submitted that these items had the character of related finance charges.

the taxpayer contended that once the matter had been referred back, the Commissioner was not at large to disallow the deduction of R64 346 528 as his role was limited to the timing issue of whether the expenses had been incurred in the relevant year as per the principle enunciated in *Caltex Oil* (*SA*) *Ltd* v *SIR* 37 SATC 1.

The taxpayer contended, in regard to the question of whether the issue of 'further costs' was properly raised as a justiciable issue in the Supreme Court of Appeal, that this was a factual issue which could properly be determined by the members of the Tax Court.

SARS contended that the 'further costs' was a new issue and not raised during the various appropriate stages in terms of section 81 of the Act and, in addition, it was not raised as a separate issue before the Supreme Court of Appeal where at all times the 'further costs' category was a trading stock issue.

Judge Victor held the following:

<u>As to the further costs category</u>

(i) That the grounds of appeal raised the 'guarantee fee, the introduction fee and finance charges' as a section 11(*b*A) issue and also raised other issues *re* costs such as the costs of outside consultants, legal fees, administration fees and related finance charges under different sections of the Act. While there is no express reference to 'further costs category', costs are referred to generally and a very clear picture emerged in the statement of grounds of appeal where the taxpayer placed specific reliance on section 11(*b*A) in the alternative should the section 22(2A) and (3A) interpretation fail.

(ii) That the 'further costs' category was a category of expenditure in the alternative before the Supreme Court of Appeal and it had not been abandoned. However, the nomenclature of the category 'further costs' for this range of expenditure was not ideal as it covered various categories of costs such as legal fees and developer fees and start-up costs which could so easily have been dealt with when the other fees were categorised and dealt with; moreover, in the absence of a line by line scrutiny by the Supreme Court of Appeal, it is accepted that the categorisation of 'further costs' is not a rigid category and it is nomenclature used as a tool of convenience by auditors. The label of this category does not place a rigid limitation on the legal interpretation of tax principles when considering the various items within it.

(iii) That having established factually that it was an issue before the Supreme Court of Appeal, it becomes necessary to interpret the judgment to determine whether it was fairly placed as a justiciable issue before the Supreme Court of Appeal and it therefore became necessary to interpret the judgment.

(iv) That the interpretation of a judgment can only be done by a judge and not the full Tax Court – as was stated by Harms DP in *KPMG Chartered Accountants* (*SA*) v *Securefin Ltd and Another* 2009 (4) SA 399 (SCA), '…interpretation is a matter of law and not of fact and, accordingly, interpretation is a matter for the court and not for witnesses…'

<u>As to the interpretation of the judgment</u>

(v) That the taxpayer contended that one should not apply a superficial nuance or impression of the words and categories used by the Supreme Court of Appeal but one ought to consider the rationales and the reasoning of the Supreme Court of Appeal otherwise one arrived at too slender a basis for arriving at a conclusion that the Supreme Court of Appeal did not deal with an amount as large as R64 346 528 and it contended further that the Supreme Court of Appeal did not undertake line item security but dealt with principles, hence the absence of the express words 'further costs.'

(vi) That the taxpayer contended that there were limitations to be read into the order – the Commissioner only had to attend to deductions under section 11(*b*A) based on the timing issue and did not have the discretion to decide whether there should be a deduction of any item. The taxpayer therefore relied on the order as it was worded and submitted that it was to be interpreted as it stood and in the light of the disputed interpretation of the order it was clearly necessary to look at the judgment itself and this was done in great detail by both parties.

(vii) That if the order is unclear then the first extrinsic source would be the judgment itself and the taxpayer referred to various words and phrases in the judgment to support their case that the 'further costs' were considered in the overall picture before the Supreme Court of Appeal but obviously these phrases must be read within the context of where they are found in the judgment. The words 'other costs', 'financial costs', 'in order to bid for the tender', 'raise the loans', 'various fees' and 'furtherance of the SACS' project' does extend the deductibility principle beyond a very limited interpretation and hence a broad approach was adopted by the Supreme Court of Appeal in interpreting the deductibility principle as the touchstone used by the Supreme Court of Appeal to extend the principle was to incorporate all the costs as a related finance charge that was closely connected with the furtherance of the project.

(viii) That the Commissioner's contention that the various fees referred to in the structure of the judgment did not encompass the 'further costs' category had to fail in the light of the broader approach by the Supreme Court of Appeal to the various categories of costs. If the only section 11(*b*A) category was the guarantee fees, introduction fee and other finance charges, as alleged by the Commissioner, then the allowable deductions would have been limited to those categories only but, instead, the Supreme Court of Appeal went much wider in allowing raising fees (margin fee, financial advisory fee, commitment fee, bid guarantee fee) to be deductible because of 'the close connection to the obtaining of loans and the furtherance of the taxpayer's project.' The Supreme Court of Appeal had characterised the various fees as a related finance charge for the purpose of section 11(*b*A).

(ix) That it was correct that nowhere in the judgment was reference expressly made to the category of 'further costs' but the judgment went much wider than guarantee fees, introduction and other finance charges and referred to a range of other fees which were not highlighted in the disallowance document and the grounds of appeal document and the Supreme Court of Appeal with respect must have had in mind a broader approach to the proper application of section 11(*b*A) of the Act.

(ix) That from the documents and submission made in the Tax Court it seemed that the 'further costs' category was not pursued with the usual adversarial vigour and thus resulted in the Supreme Court of Appeal not dealing with it as a separate category but at the same time the issue was not abandoned.

(x) That the concession by the Commissioner on the eve of the hearing in this court on a wide range of fee categories also went way beyond the guarantee fee, introduction fee and deductible finance charges on which the Commissioner relied for his interpretation of the judgment and this was relevant. Implicit in the judgment of the Supreme Court of Appeal was the application of the principle to a wide range of costs and this meant that the 'further costs' category fell to be interpreted within the ambit of section 11(*b*A) albeit that it was obliquely canvassed in the Supreme Court of Appeal.

(xi) That some of the items in the 'further costs' category were the same as those which the Supreme Court of Appeal had ruled deductible and the interpretation and application of the principle could not be limited because of an absence of an express reference to a category known as 'further costs' in the Supreme Court of Appeal judgment. Principles emanating from judgments are meant to be applied to different facts otherwise the law would be a static process.

(xii) That a sensible objective observer looking at the judgment in its entire context would note the import of the principles of allowing the deductions of a wide variety of fees and the like; the category 'further costs' is but a descriptive outline or a convenient label perhaps for accountants and on the whole the items listed in 'further costs' are a 'close connection' to the furtherance of the project.

(xiii) That once this is the case, in the absence of an express reference to disallowing 'further costs', the judgment had to be interpreted to include 'further costs' and the Commissioner was accordingly directed to allow the deduction in terms of section 11(*b*A) of the category of costs labelled as 'further costs'.

(xv) That in determining the question of costs of the matter in the Tax Court, the Commissioner's opposition was not unreasonable and therefore no costs order was made.

8.3 ITC 1871

The taxpayer and its sponsors were at all material times registered vendors in terms of the Value-Added Tax Act.

The taxpayer, at all material times, carried on business as the owners and organisers of a world acclaimed festival, the latter being an annual international festival and in the course of organising such events the taxpayer had obtained sponsorships for the festival from various sponsors and they essentially bartered services.

In terms of the sponsorship agreements the sponsors agreed to contribute and did contribute to the organisation by providing the taxpayer with certain services and cash payments and the services provided by the sponsors to the taxpayer included flight tickets, airtime to broadcast the festival promotions and advertisements on certain radio stations and television channels and certain city or municipal services.

In return for the sponsorships, the taxpayer agreed to provide and did provide the sponsors with certain services, these being festival stage branding, which entailed the sponsors' logos being displayed on the backdrop of the stage; festival venue branding, which entailed the sponsors' logos being displayed on the venue; the sponsors' logos to be displayed in all promotions, advertisements and events associated with the festival in all mediums of communication used; and corporate hospitality marquees, accommodation and festival tickets.

The sponsors did not charge VAT on the supply of goods and services made or rendered to the taxpayer and no VAT was paid by the taxpayer on the sponsorships so received. The sponsors did not issue tax invoices to the taxpayer in respect of the services they provided to the taxpayer.

The taxpayer, in turn, did not issue the sponsors with tax invoices in respect of the services it provided to the sponsors in terms of the sponsorship agreements.

The taxpayer did not declare output tax on the value of the services supplied to it by the sponsors in its VAT returns for the relevant periods of assessment nor did it claim input tax on the value of the services supplied to it by the sponsors in any of its VAT returns. It was on the basis of an audit conducted into the tax affairs of the taxpayer that SARS had raised the assessments and levied taxes and interest on the assessment so raised.

The amount in dispute in the appeal, comprising as it did of the assessments raised for the 2006 and the 2007 VAT periods of assessment, together with interest levied thereon, was in an amount of R1,020,659-80.

The taxpayer admitted that it was obliged to account for output tax on the aforementioned amount for the relevant periods of assessment and had failed to do so, but, on the other hand, the taxpayer submitted that it was, in principle, also entitled to deduct, from that output tax, input tax in respect of the supply of goods and services supplied to it by the sponsors during the relevant periods of assessment.

The taxpayer lodged an objection against SARS' assessment and SARS, in turn, disallowed the taxpayer's objection to the assessment and the taxpayer then filed an appeal against SARS' disallowance of its objection.

SARS contended that the amounts sought to be deducted as input tax deduction did not qualify for input tax deduction under the Value-Added Tax Act as the taxpayer did not comply with the substantive and procedural requirements to claim and to deduct input tax on those supplies and that the taxpayer's appeal, based as it was to the asserted principled entitlement to deduct input tax, could not succeed.

SARS contended that as the sponsors did not charge VAT on the supply of the sponsorship to the taxpayer, and no VAT was payable or paid by the taxpayer on those sponsorships, the amounts sought to be deducted by the taxpayer as input tax in respect of the sponsorships did not fall within the ambit of par. (*a*) of the definition of 'input tax.'

SARS contended further that the amounts the taxpayer sought to have deducted as input tax did not qualify as input tax in as much as no input tax had actually been charged and, accordingly, no input tax was paid or became payable for the supply of goods or services rendered to the taxpayer.

The taxpayer stated that it repeatedly demanded from the sponsors that it be provided with tax invoices to enable it to claim input tax deduction. When the sponsors failed to issue the taxpayer with the required tax invoices, the taxpayer informed SARS of the failure by the sponsors to provide it with the required tax invoices, coupled with a demand that SARS, consistent with its responsibility to carry out the provisions of the Value-Added Tax Act, forces the sponsors to issue the the taxpayer with the required tax invoices.

The main issue in dispute in this appeal is whether the taxpayer should be allowed to deduct input tax in respect of supplies made to it by the sponsors during the relevant periods of assessment despite the fact that the sponsors have not issued it with tax invoices in respect of those supplies and the dispute, as formulated by SARS, revolves around the question as to whether the amounts sought to be deducted by the taxpayer, as an input tax deduction, qualify for such deduction in terms of the Value-Added Tax Act.

Judge Yekiso held the following:

(i) That the taxpayer had not suggested that it paid input tax in respect of the goods supplied and services rendered to it by the sponsors. As a matter of fact, the taxpayer had not asserted that it was charged tax in terms of section 7 of the Act in respect of supplies made to it by the sponsors or, that the amount sought to be deducted was payable in terms of that section. All that the the taxpayer asserted was that, in principle, it was entitled to deduct input tax which otherwise would have been charged for the supply of goods and services rendered to it by the sponsors.

(ii) That the reason why the taxpayer could not deduct input tax on the sponsorships received from the sponsors was because the sponsors did not provide the taxpayer with tax invoices on such sponsorships to enable it to claim input tax deduction based on such sponsorships and it was for this reason that the taxpayer sought what appeared to be an order that SARS should force the sponsors to issue it with such tax invoices.

(iii) That section 16(2) of the Act provided that no deduction of input tax in respect of any supply of goods or services should be made unless the prescribed document in relation to that supply had been provided and was held by the vendor making that deduction at the time that the relevant return was submitted.

(iv) That section 16(3) of the Act provided that where a vendor was entitled to claim a deduction in terms of section 16(3) such vendor may claim that deduction against output tax attributable to a later tax period which ended no later than five years from the tax period during which the tax invoice for that supply should have been issued.

(iv) That the taxpayer had complained that it could not deduct input tax on the VAT output as the sponsors refused to issue the taxpayer with tax invoices despite repeated demands that they issue it with such tax invoices but the fact that the sponsors failed to issue such tax invoices did not leave the taxpayer without a remedy as it could have, in terms of section 20(2) of the Act, created a document deemed to be a tax invoice under those circumstances contemplated in paras (*a*), (*b*) and (*c*) of section 20(2) of the Act.

(v) That the taxpayer was entitled to claim input tax for the period of assessment in which it was in possession of a valid tax invoice but it was not in possession of a valid tax invoice during any one of the VAT periods of assessment and it was on that basis that the taxpayer could not deduct input tax from the amount assessed as output tax; moreover, refusal by the sponsors to issue the taxpayer with the required tax invoices could very well have been met by an appropriate court order compelling the sponsors to issue it with the required tax invoices and all these options were and probably are still open to the taxpayer.

(vi) That if the taxpayer had genuinely believed that it was entitled to the input tax deduction on the merits, but for the sponsors' refusal to issue the taxpayer with the required tax invoices, the taxpayer's appropriate remedy would have been to approach the sponsors to agree to it issuing the recipient-issued invoices and to make an application to the Commissioner in terms of section 20(2) of the Value-Added Tax Act and upon such agreement with the sponsors and the approval by the Commissioner, the taxpayer would then issue the recipient-issued invoices and use them to support its input tax deduction as contemplated in section 16(3)(*g*) of the Act.

(vii) That there was an obligation on registered vendors, which included the taxpayer, to comply with the provisions of the Value-Added Tax Act and the taxpayer cannot, now that it failed to comply with the provisions of the Act in the first place, contemplate any form of relief in terms of which SARS is ordered to force the sponsors to issue the taxpayer with the required invoices.

(ix) That the relief provided for in section 20(7)(*b*) of the Act did not assist the taxpayer either as the relief contemplated in section 20(7) specifically states that there had to be sufficient records available to establish the 'category of supplies' before the Commissioner may disregard the requirement that a tax invoice be issued.

(xi) That the transactions which formed the basis of the assessments raised were barter transactions: the taxpayer supplied the sponsors with services on which it was liable for VAT output and the details of the services supplied were clear from the contracts and other documentary evidence. In exchange for the services supplied or rendered to the sponsors, the taxpayer received certain supplies from the sponsors including cash. This was a contentious mix of supplies and the 'category of supplies' received was uncertain. In as much as one can make a determination of the category of supplies constituting the basis of liability for output tax, one could not make a similar determination on the category of supplies constituting a basis of liability for input tax.

(xii) That, therefore, the taxpayer had failed to make out a case for the relief it sought and the appeal was dismissed and the assessments, as raised by the SARS, were confirmed and the taxpayer was ordered to pay SARS' costs of the appeal.

9. INTERPRETATION NOTES

9.1 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 – No. 30(3)

This Note:

- explains the requirements that need to be adhered to; and
- prescribes the documentary proof, acceptable to the Commissioner, that must be obtained and retained by a vendor;

in order to levy VAT at the zero rate on a supply of movable goods under 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) dated 15 March 2006 'Documentary Proof Required on Consignment or Delivery of Movable Goods to a Recipient at an Address in an Export Country' is hereby withdrawn. This Note (Issue 3) is effective from 2 May 2014.

With regard to export transactions:

- for which the time of supply occurred before the effective date of Issue 3, the provisions of Interpretation Note No. 30 (Issue 2) dated 15 March 2006 apply; or
- for which the time of supply occurred:
  - on or after the effective date of Issue 3; or
  - in respect of progressive supplies as contemplated in section 9(3)(*b*) where:
    - any payment for the supply becomes due or is received before as well as after the effective date of Issue 3; or
    - any invoice issued in relation to that payment occurs before as well as after the effective date of Issue 3; and
    - the goods are delivered only after the effective date of Issue 3,

the provisions of Issue 3 apply.

The following must be noted: All rulings or decisions 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 the Republic is taxed. VAT is therefore levied at the standard rate on the supply of goods or services in the Republic as well as on the importation of goods into the Republic unless an exemption or exception applies. Subject to certain requirements, VAT may be levied by a vendor at the zero rate if the vendor is responsible for consigning or delivering those goods to an address in an export country.

Paragraph (*a*) of 'exported' as referred to in section 11(1)(*a*) is defined in section 1(1) of the VAT Act 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 the Commissioner.'

In order for a vendor to supply movable goods (excluding second-hand movable goods on which notional input tax was deducted on the acquisition of such goods) under 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 the Commissioner.

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

The provisions of the Regulation will apply to movable goods that are not exported by the vendor by means of a direct export, unless this Note otherwise indicates.

This Note is only applicable to the export of movable goods as contemplated in section 11(1)(*a*)(i) read with paragraph (*a*) of the definition of 'exported' in section 1(1) of the VAT Act.

In order for a vendor to substantiate its entitlement to apply the zero rate to the supply of movable goods to a recipient at an address in an export country, that vendor must be in possession of documentary proof as is acceptable to the Commissioner.

In the event that the Commissioner is not satisfied that there is sufficient proof of export, the supply cannot be zero-rated and, is therefore, subject to VAT at the standard rate.

This Note only applies to direct exports, that is, movable goods supplied by the vendor under a sale or instalment credit agreement and consigned or delivered at an address in an export country; and may not prescribe all possible scenarios.

9.2 VAT – Appplication of the VAT Act to the gambling industry – No. 41(3)

This Note provides clarity on the value-added tax (VAT) implications of specific transactions undertaken in the gambling industry.

This Note sets out the VAT implications of the various supplies made by and to a vendor in the gambling industry. It contains, for ease of reference, an extract from Binding General Ruling No. 13, which allows VAT to be calculated using the net drop method, subject to certain conditions being met.16 or facsimile on 086 540 9390. The application should be headed 'Application for a VAT Class Ruling' or 'Application for a VAT Ruling' and it must meet all the requirements as set out in section 79 of the TA Act. 17

10. DRAFT INTERPRETATION NOTES

10.1 The supply of goods and services by professional hunters and taxidermists to non-residents

This Note explains the VAT treatment of various supplies to foreign hunters including hunting services, taxidermy services, the supply of a trophy as well as the subsequent export of the trophy.

The supply of accommodation, hunting services and other goods or services that are consumed while the foreign hunter is in the Republic will be subject to VAT at the standard rate. The supply of dip and pack services as well as the trophy fee may be zero rated provided the relevant provisions contained in section 11 are met.

11. BINDING PRIVATE RULINGS

11.1 BPR 168 – Income Tax – Corporate rules: Disposal of assets within 18 months of acquisition

This ruling deals with the effect of section 42(7) the Income Tax Act on the disposal of assets in terms of an ‘intra-group transaction’ as defined in section 45(1) when the disposal will take place within 18 months of the assets having been acquired in terms of an ‘asset-for-share transaction’ as defined in section 42(1).

In this ruling references to sections are to sections of the Income Tax Act applicable as at 14 May 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 sections 42(7) and 45(2) and (3).

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

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

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

Subco: A company incorporated in and a resident of South Africa and a subsidiary of the Applicant.

<u>Description of the proposed transaction</u>

The Applicant acquired assets from Company X in exchange for equity shares in the Applicant in terms of an ‘asset-for-share transaction’ as defined in section 42(1). As a result of this ‘asset-for-share transaction’, Company X holds 94% of the equity shares in the Applicant.

The Applicant intends disposing of the assets acquired to Subco in terms of an ‘intra-group transaction’ as defined in section 45(1). This disposal will take place within 18 months of the assets having been originally acquired by the Applicant.

The Applicant holds 74% of the equity shares in Subco. The purchase price will be settled by Subco by means of an interest free loan account.

<u>Conditions and assumptions</u>

This binding private ruling is subject to the additional condition and assumption that:

- The disposal of the assets by Company X to the Applicant in exchange for equity shares in the Applicant does in fact constitute an ‘asset-for-share transaction’ as defined in section 42(1) and will qualify for relief as provided for in section 42(7).

<u>Ruling</u>

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

- The Applicant will not be subject to tax on any recoupment on the disposal of the assets it acquired from Company X disposed to Subco, including the recoupment of any allowances claimed by Company X and the Applicant in respect of such assets.

- Section 42(7) will have a nil effect on the disposal of the assets by the Applicant to Subco under section 45 notwithstanding the fact that the disposal may take place within 18 months of having been acquired by the Applicant *via* an ‘asset-for-share transaction’.

- To the extent that Subco acquires the assets from the Applicant under section 45, the income tax value of such assets will be equal to the income tax value of the assets for the Applicant on the date of disposal to Subco. This being the income tax value of the assets for Company X on the date of the disposal of the assets under section 42 to the Applicant less any subsequent allowances claimed by the Applicant.

11.2 BPR 169 – Commercial building allowances

This ruling deals with the deduction of a commercial building allowance in respect of a unit, as contemplated in the Sectional Titles Act No. 95 of 1986 (the ST Act).

In this ruling references to sections are to sections of the Income Tax Act applicable as at 11 March 2014 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 section 13*quin*.

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

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

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

<u>Description of the proposed transaction</u>

The Applicant and the Property Developer (the Developer) jointly acquired a vacant piece of land. The land is jointly held in undivided shares of 9/16th (57.1%) by the Applicant, and 7/16th (42.9%) by the Developer.

The parties each paid their proportionate share of the purchase consideration on the joint acquisition of the land. The parties propose to register a sectional title development scheme (the scheme) over the property (and its proposed buildings) under the provisions of the ST Act.

It is proposed that the Applicant and the Developer will develop the jointly owned land by each erecting for its respective separate use, and at its own cost, a commercial building thereon, each building comprising a separate tower.

The two buildings will be separated by a greened thoroughfare, as regards the appearance above ground level. Below ground, the underground parking basement will be constructed as a single basement, which will establish a single foundation for the two towers. The basement will be separated into two parts by a wall on each level, with dedicated parking areas for each unit.

In order to give effect to the proposed improvements to the land, the Applicant and the Developer will conclude a development agreement to erect the commercial buildings which will ultimately be the object of the scheme.

The development agreement will govern the terms of the proposed development, including the quality, extent and costing of the Applicant's unit, the construction of which will be project managed by the Developer. It will also regulate the division of development costs between the Applicant and the Developer, ensuring that the Applicant will have the sole financial responsibility for the development of its separate unit (including its proportionate basement parking area). The development costs pertaining to the shared amenities will be shared between the parties proportionate to their joint land ownership ratios, or such other ratio as agreed by them.

The Developer will, by way of a separate construction contract, engage a building contractor for the construction of its own unit as well as the common structures and shared amenities. In addition, the Developer will subcontract the construction of the Applicant's unit, whilst remaining contractually bound to deliver the unit to the Applicant.

<u>Conditions and assumptions</u>

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

<u>Ruling</u>

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

- The Applicant will be entitled to claim a commercial building allowance on its unit, as contemplated in section 13*quin,* on occupying the unit after registration of the sectional plan under the provisions of the ST Act, and prior to the tenants of the Developer occupying the Developer's unit.
- The Applicant will also be entitled to claim a commercial building allowance on its unit, as contemplated in section 13*quin,* on

occupying its unit after registration of the sectional plan under the provisions of the ST Act, should the tenants of the Developer occupy the Developer's 'unit' prior to registration of the sectional plan and prior to the Applicant occupying its unit.

11.3 BPR 170 – Definition of unrestricted equity instrument

This ruling deals with the question whether the condition imposed on an employee to sell back shares over a period of time to his employer (at market value on termination of employment) will result in the shares being regarded as 'restricted equity instrument[s]' as contemplated under section 8C(7).

In this ruling references to sections are to sections of the Income Tax Act applicable as at 17 January 2014 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(7).

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

The Applicant: An individual who is not a resident of South Africa

<u>Description of the proposed transaction</u>

The Applicant intends to sell shares which he acquired in a company (the Employer) in terms of the Employer Group Employee Share Scheme (the Scheme).

The Applicant is a resident of Country X and rendered services in Country X at all relevant times in relation to the proposed transaction.

The Applicant was previously employed by the Employer which is also a resident of Country X. During the course of the Applicant's employment, he acquired shares in the Employer in terms of the Scheme.

The essential features of the Scheme, in relation to the shares held by the Applicant, are as follows:

- the Applicant is the beneficial owner of the shares;
- the Applicant may sell the shares at any time to any party subject to the management board of the Employer approving the purchaser of the shares; and
- the Applicant is required in terms of the rules of the Scheme to sell the shares when leaving the Group.

Subsequent to the acquisition of the shares, the Applicant was required to enter into a Put and Call Option Agreement (the Agreement). The Agreement does not require the Applicant to sell the shares to the Employer, but to a company in the same group as the Employer (the Company) should it call on the Applicant to do so. The Agreement gives the Applicant the right to sell the shares to the Company at the time that the Applicant wishes to sell the shares.

The Agreement also provides that, as regards all employees, shares will be sold at market value, to be determined by the employer on termination of employment, but not all the shares can be sold immediately. The sales will be spread over a period of four years after the issuance of the notice fixing the price per share.

The Applicant's employment with the Employer had previously been terminated and the Applicant sold some of his shares to the Company in terms of the Agreement. The remaining shares will, in terms of the Agreement, be sold to the Company over a period of four years at a pre-determined price, that is, the market value which was determined and fixed at the time of termination of the Applicant's employment.

The Applicant is not required to render any further services to the Employer.

The Applicant would like to relocate to South Africa with his family and he will most likely become a resident of South Africa before the remaining shares are sold to the Company.

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 remaining shares held by the Applicant will constitute 'unrestricted equity instrument[s]' as defined in section 8C(7).

11.4 BPR 171 – Amalgamation transaction

This ruling deals with the income tax and securities transfer tax consequences for the parties concerned in a proposed amalgamation transaction intended to extinguish a layer of companies considered unnecessary in a holding structure.

In this ruling references to sections and paragraphs are to sections of the relevant Acts and to paragraphs of the Eighth Schedule to the Act applicable as at 27 May 2014 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 44 of the Act;
- paragraph 11 of the Eighth Schedule to the Act; and
- section 8(1)(*a*)(ii) of the STT Act.

Parties to the proposed transaction

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

The First Co-Applicant: A close corporation incorporated in and a resident of South Africa

The Second Co-Applicant: A close corporation incorporated in and a resident of South Africa

The Third Co-Applicant: A natural person who is a resident of South Africa and the sole member of the First Co-Applicant

The Fourth Co-Applicant: A natural person who is a resident of South Africa and the sole member of the Second Co-Applicant

Description of the proposed transaction

The First and Second Co-Applicant each owns half of the issued share capital of the Applicant. The only liability of each of the First and Second Co-Applicants is a loan account in favour of the Third and Fourth Co-Applicants respectively.

The First and Second Co-Applicants are passive holding entities. The only functions they serve are as proxies for the Third and Fourth Co-Applicants who hold the respective members' interests through which those members indirectly exercise what they consider to be their interests in the Applicant. They had both been active in the manufacturing industry through the First and Second Co-Applicants, but some years ago decided to join forces.

The Applicant then became their business vehicle and was established with the First and Second Co-Applicants as its sole shareholders, the shareholding being their respective sole assets and the loan accounts their respective sole liabilities. For all practical purposes the Third and Fourth Co-Applicants, through their control of the First and Second Co-Applicants, operate as would the shareholders of the Applicant. They therefore consider the First and Second Co-Applicants an unnecessary additional layer between them and the Applicant operating company.

The purpose of the proposed transactions is to eliminate the close corporations. The First Co-Applicant will amalgamate with the Applicant. Upon completion of that amalgamation transaction, the Second Co-Applicant will do the same.

The First Co-Applicant will dispose of all its assets to the Applicant at their base cost, namely its shares in the Applicant and its loan account claim against the Applicant. In exchange, the Applicant will issue equity shares in its authorised capital to the First Co-Applicant with a market value equal to the base cost in the hands of the First Co-Applicant of the assets to be received by the Applicant. The First Co-Applicant will undertake to commence proceedings for its liquidation, winding up or de-registration immediately upon implementation of the transaction, and to distribute as a dividend *in specie* to the Third Co-Applicant as its sole member, the shares to be issued to it by the Applicant.

After the implementation of the foregoing transaction, a transaction in almost identical terms will take place between the Second Co-Applicant and the Applicant. The shares to be issued by the Applicant to the Second Co-Applicant will, however, be distributed to the Fourth Co-Applicant.

Conditions and assumptions

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

- The First and Second Co-Applicants hold the shares in the Applicant as capital assets.
- The First and Second Co-Applicants must, within 36 months after the date the proposed transaction is entered into by the Co-Applicant concerned, or within such further period as the Commissioner may allow, take steps to liquidate, wind up or deregister.
- No such step may, after it has been taken, be withdrawn at any stage or nothing may be done by the Co-Applicant concerned to invalidate any such step with the result that it will not be liquidated, wound up or deregistered.

Ruling

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

- The proposed transactions will qualify as amalgamation transactions as contemplated in section 44(2)(*a*).
- The First and Second Co-Applicants will be deemed to have disposed of the shares they hold in the Applicant for amounts equal to the base cost of those shares on the date of the disposals concerned. The First

and Second Co-Applicants will not realise any capital gains on the shares transferred to the Applicant.

- The cancellation of the shares by the Applicant will not constitute a disposal as contemplated in paragraph 11.
- The contributed tax capital of the Applicant will increase after each proposed transaction by an amount equal to the contributed tax capital of the Co-Applicant concerned at the time of its termination, represented by the shares held in that Co-Applicant by the Third and Fourth Co-Applicants respectively.
- The Third and Fourth Co-Applicants will be deemed to have disposed of their respective members' interests in the First and Second Co-Applicants as a result of the proposed transactions for amounts equal to the expenditure incurred by them in respect of those interests allowable under paragraph 20.
- The Third and Fourth Co-Applicants will also be deemed to have acquired their shares in the Applicant on the date on which they acquired their erstwhile members' interests and for a cost equal to the expenditure incurred, as contemplated in the previous item, on the respective dates those costs were incurred in respect of those members' interests. Those costs must be treated as expenditure actually incurred by the Third and Fourth Co-Applicants in respect of the shares in the Applicant for the purposes of paragraph 20.
- Any valuation done in respect of the members' interests under paragraph 29 will be deemed to have been done in respect of the Third and Fourth Co-Applicants' shares in the Applicant.
- Those shares will not constitute amounts transferred or applied by the First and Second Co-Applicants for the benefit of the Third and Fourth Co-Applicants, respectively.
- The First and Second Co-Applicants must disregard the disposals of shares in the Applicant to the Third and Fourth Co-Applicants

respectively for purposes of determining their respective taxable incomes or assessed losses.

- Securities transfer tax will not be payable in respect of the transfers of the shares and members' interests.

11.5 BPR 172 – Plant used in the production of renewable energy

This ruling deals with the deduction allowed in respect of the cost of machinery, plant, implements, utensils or articles owned and used in the generation of electricity from solar energy.

In this ruling references to sections are to sections of the Income Tax Act applicable as at 10 June 2014 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 12B(1)(*h*), read with section 12B(2).

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

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

<u>Description of the proposed transaction</u>

The Applicant proposes to construct grid-tied solar photovoltaic systems (PV Systems) to be used by the Applicant at many of its business locations within South Africa to generate electricity from solar energy.

The electricity to be produced by the PV Systems will feed directly into the power supply systems of the respective facilities without being stored in batteries.

In some instances the PV Systems will be installed on leased land.

The process of generating electricity from solar energy will be as follows:

- Sunlight will be absorbed by the silicone-based semi-conductors of a PV Panel, generating direct current (DC) electrical energy, which will be conveyed by DC feeder lines to a DC Combiner.
- The DC Combiner electrically combines the multiple strings of solar panels. On the output side of the DC Combiner combined sets of DC feeder lines run to an alternating current inverter (AC Inverter).
- The AC Inverter will convert the DC electrical energy to AC electricity on which electrically powered equipment will operate.
- The AC inverted current will travel from the AC Inverter into the facility's main service panel, from which a further connection will be established for use by equipment.
- The PV System will be affixed or mounted at the various locations, as follows:
- Each PV System will be affixed to a specially designed and constructed concrete foundation having regard to the requirements of each location.
- In accordance with industry standards, a PV System has a useful life of 25 years, which includes the concrete foundation and supporting steel structure.
- The PV Panels are bolted to concrete foundations and can be removed by using appropriate equipment. After removal, the PV Panels could either be scrapped or transported to another location for re-use.

<u>Conditions and assumptions</u>

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

<u>Ruling</u>

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

- The PV Panels situated at the various leased and owned locations, consisting of all their constituent parts, including the concrete foundations and supporting steel structures, will constitute 'plant' used in the ‘generation of electricity’ for purposes of section 12B(1)(*h*), the cost of which is deductible in accordance with the rates and periods contemplated in section 12B(2).

- The DC Combiner and feeder lines situated at the various leased and owned locations will constitute ‘plant’ used in the ‘generation of electricity’ for purposes of section 12B(1)(*h*), the cost of which is deductible in accordance with the rates and periods contemplated in section 12B(2).
- The AC Inverters, including all equipment situated therein, situated at the various leased and owned locations will constitute ‘plant’ used in the ‘generation of electricity’ for purposes of section 12B(1)(*h*), the cost of which is deductible in accordance with the rates and periods contemplated in section 12B(2).

12. BINDING CLASS RULING

12.1 BCR 44 – Repurchase of non-redeemable, non-participating preference shares

This ruling deals with the tax consequences of a repurchase of non-redeemable, non-participating preference shares.

In this ruling references to sections and paragraphs are to sections of the relevant Acts and paragraphs of the Eighth Schedule to the Act, applicable as at 14 November 2013 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 1(1), definition of ‘equity share’, section 8E of the Act,
- paragraph 11(2)(*b*) of the Eighth Schedule; and
- section 2(1) of the STT Act.

<u>Class</u>

The class members to whom this ruling will apply are described in point 4 below.

Parties to the proposed transaction

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

Class Members: Holders of non-redeemable, non-participating preference shares issued by the Applicant

Description of the proposed transaction

The Applicant issued non-redeemable, non-participating preference shares at a par value amount. The preference shares are not redeemable, even though they confer the right to a return of the capital on the winding up of the Applicant in an amount equal to the issue price of the preference shares. A decision was taken to undertake a general and/or specific repurchase of the preference shares at the current market price as traded on the JSE. The repurchase price constitutes a discount to the issue price of the preference shares.

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 preference shares will not constitute ‘equity shares’ for purposes of the definition in section 1(1) of the Act.
- The preference shares will not be recharacterised as hybrid equity instruments merely by reason of their repurchase by the Applicant and dividends paid by the Applicant during the current financial year of assessment will not be recharacterised as income in the hands of the Class Members.
- Any power of the Applicant to repurchase the preference shares in terms of the Takeover Regulation Panel Requirements or section 164

of the Companies Act will not be deemed to be an obligation to do so for purposes of section 8E of the Act.

- The proposed transaction, including the cancellation of the preference shares, will not result in a disposal by the Applicant of an asset, as contemplated in paragraph 11 of the Eighth Schedule to the Act.
- Securities transfer tax will be payable at the rate of 0.25% on the repurchase price payable by the Applicant for the preference shares.
- In the event of any particular repurchase of preference shares, to the extent that there is a dividend element, dividends withholding tax may apply.

13. INDEMNITY

Whilst every reasonable 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.