



Initial Assessment of Competence

Professional Paper 2

January 2026

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Part (a) Discuss, with reference to case law principles, the income tax implications for Lexi in respect of the all-expenses-paid trip described in section 3 (Additional income).	Marks
Income tax implications	
<u>Identification of the issue:</u> The issue is if a ‘total amount’ ‘in cash or otherwise’ has been received in terms of the <u>gross income definition</u> .	1
<u>Case law principle:</u> The word ‘amount’ includes any form of property with an <u>ascertainable monetary value</u> , including debt and rights (<i>Lategan, Butcher Bros and Brummeria</i>).	1
<u>Application:</u> The trip with a market value of R20 000 was used by Lexi by Arno for services rendered , which equates to something given in return (a quid pro quo or exchange) transaction (<i>Brummeria Renaissance</i>)	1 1
Para. (c)(ii) to the gross income definition specifically includes any voluntary award, received or accrued in respect of services rendered.	1
<u>Application:</u> Lexi will be taxed on the full market value of R20 000 as she rendered the services , even though all expenses paid for the trip were for her and her partner.	1
<u>Section 102(1)(e)</u> of the TAA determines that the taxpayer (i.e. Lexi in this case) bears the burden of prove that the value is correctly determined at R20 000.	1
<u>Conclusion:</u> Lexi will be taxed on the value of the all-expenses trip valued at R20 000 and must thus include the R20 000 in her ‘gross income’ in the 2025 year of assessment.	1P
Available	8
Maximum	7
Total for part (a)	7

Part (b) Calculate Lexi's normal tax payable for her 2025 year of assessment. <ul style="list-style-type: none"> • Provide reasons for amounts which have a nil effect on the calculation. • For the purposes of answering required (b) assume that – <ul style="list-style-type: none"> ○ with regard to point 3.2 (Foreign income – book talk fee) the fee will be fully taxable in South Africa; and ○ section 6B is nil. 			Marks
Full-time employment	R	R	
Salary (par (c) of the gross income definition – s1(1)) R50 000 x 9 months		450 000	1
Exemption: Secondment to the UK DTA upheld by the UK: not exempt from normal tax as Lexi was not outside South Africa for a period exceeding 183 days (section 10(1)(o)(ii))		NIL	1
Fringe benefit – provident contribution R450 000 x 14,8%		66 600	1P
<u>Fringe Benefit: Laptop</u> nil value as only used for business purposes (para. 6(4)(a) of the 7 th Schedule) OR used mainly for Hebony's business (para. 6(4)(bA) of the 7 th Schedule)		NIL	1
<u>Cell phone allowance</u> (s 8(1)(a)(i) R1000 x 9 months)		9 000	1
<u>Cell phone expenses</u> No deduction for the business as Lexi is not a mainly commission-earning employee (s 23(m)) OR No deduction for private cell phone costs as incurred for domestic purposes (s 23(b)) or no deduction for this allowance		NIL	1
<u>Leave pay</u> (s7B(2) read with para. (d) of the gross income definition)		35 000	1
<u>Free meal credits</u> No inclusion as represents an advance, and Lexi spends the amount on business premises (s8(1)(a)(ii)) OR constitutes a voucher (<u>fringe benefit</u>), value of nil as the canteen is exclusively used by the employees of Hebony (para. 8(3) of 7 th Schedule).		NIL	1
<u>Interest-free loan</u> (7 th Schedule – para 2(f) read with para. 11(4)(b)) nil value as it was given to Lexi to enable her to further her studies		NIL	1
<u>Settlement of loan</u> No deduction for the settlement of the loan from Hebony as it is capital in nature OR not in the production of income (s11(a)) OR Section 23(m) prohibits any deduction.		NIL	1
<u>UIF</u> UIF contributions paid are not deductible , as it relate to amounts that do not constitute income under section 1. Any UIF benefits received are specifically exempt in terms of s10(1)(mB)/ s23(f)		NIL	1

	R	R	
<u>Savings component</u> (para (eD) to the gross income definition - s1(1))		39 596	1
RUMENARATION		600 196	
<u>Endorsements</u> (para (eD) to the gross income definition - s1(1))		10 000	1
<u>Home expenditure</u> No deduction is allowed for the portion of the apartment, as Lexi cannot provide supporting documents. (unable to meet the burden of proof required under s 102 of the TAA. OR Deduction disallowed as relates to domestic in nature (s23(b))		NIL	1
<u>MC event</u> (follow through from part (a) - par (c) of the gross income definition		20 000	1P
<u>Book talk fee</u> (s1(1) gross income definition read with s 25D(3)) £3 000 x 23,43		<u>70 290</u>	1
TI before s 11F		700 486	
Section 11F(2) deduction		(66 600)	1P
Contribution	66 600		
<i>Limited to the lesser of:</i>			
- R350 000; or			1
- The higher of 27.5% of:			
<i>Remuneration (R450 000 + R66 600 + R9 000 + R35 000 + R39596) = R600 196</i>			1P
<i>Taxable income (R600 196 + R10 000 + R20 000 + R70 290) = R700 486</i>			1P
Higher of 27.5% of R700 486 or R560 600 = R192 633			1
- Taxable income = R700 486			
The applicable limit amount is R192 633, however the limit is more than the amount contributed of R66 600.			
Taxable income		633 886	
Normal tax calculation			
R121 475 + 36% (R633 886 - R512 800)		165 066	1P
Primary rebate: (section 6(2)(a))		(17 235)	1
Section 6A rebate (s 6A(2)(b)(i)(bb))	R728 x 12	(8 736)	1
<u>Section 6quat rebate</u> The UK did not apply any withholding tax and there were therefore no foreign taxes paid by Lexi.		NIL	1
Income Tax payable		139 095	
Retirement amounts			
Withdrawal from vested pot (s 1(1) special inclusion (e) to the gross income definition): subject to the tax tables under the Second Schedule	331 036		1
Transfer to preservation fund (qualifying transfer in terms of para. 4(b) of the Second Schedule)	NIL		1
Normal tax payable from withdrawal (R331 036 - R27 500) x 18%	54 636	54 636	1P
Normal tax payable (R139 095 + 54 636)		193 731	
		Available	28
		Maximum	27
		Total for part (b)	27

Part (c) Discuss whether Hebony should withhold employees' tax on the R121 500 payable to CreativeLexi for January 2025.	Marks
In terms of the Fourth Schedule Hebony (a resident employer) needs to withhold employee's tax if CreativeLexi is a personal service provider (PSP), thus and employee. To test the requirements of a PSP:	1
CreativeLexi (Pty) Ltd is a private company ;	1
Lexis is the sole shareholder of CreativeLexi; (she thus holds more than 20% equity interest), thus a connected person to CreativeLexi:	1
Lexi renders the services personally by promoting brands through content creation and	1
CreativeLexi receives > 80% of income from Hebony (R121 500/R150 000 = 81%) in January 2025.	1
CreativeLexi also do not meet the requirement to exclude it from a personal service provider as: CreativeLexi <u>only employs Arno</u> as a part-time CFO, thus not three or > full-time employees who are unconnected persons to CreativeLexi throughout the year of assessment.	1
Conclusion: Therefore, CreativeLexi is a personal services provider and Hebony must withhold employee's tax (PAYE) on the fees payable to CreativeLexi at 27%.	1P
Employees' tax should have been paid to SARS by 7 February 2025 .	1B
Available	8
Maximum	6
<i>Y1: Critical thinking</i> <i>(Mark awarded for recognition of PSP in the Fourth Schedule and application to the scenario – not merely repetition of theory)</i>	1
Total for part (c)	7

Part (d) Discuss the income tax implications for Holdings in respect of the R68,1 million interest paid to Africa Holdings (Pty) Ltd in its 2025 tax return.	Marks
Holdings pays interest of R68,1 million to Africa Holdings (Pty) Ltd on loans provided by Africa Holdings (Pty). This loan is an instrument in terms of <i>section 24J(1) and Holdings is the issuer of an instrument</i> (loan) in terms of <i>section 24J</i> of the Income Tax Act.	1 1
For interest to be deductible under <i>section 24J(2)</i> , the interest must be incurred in the production of income and for purposes of trade. For expenses to be deductible in the production of income , it must be an inevitable concomitant or closely connected to that expense (<i>PE Tramways</i>)	1
The interest income from loans to subsidiaries (R34.9m) were lower than the interest paid by Holdings on borrowed funds (68.1m), indicating that the purpose of the company was to benefit the subsidiaries rather than to generate 'income' . In addition Holdings is not involved in the management of its subsidiaries.	1
As Holdings received both interest and dividend income, the interest expenses are also linked to the production of exempt dividend income (<i>s 23(f)</i>), which does not qualify for a deduction under <i>s24J(2)</i> and apportionment of the interest expense may be needed.	1
Trade is given a wide meaning (<i>Burgess</i>). Passive income from interest earned from lending at below market terms with no real return is not considered a trade .	1 1
SARS practice is to allow a deduction of interest to the extent that interest has been earned in respect of companies that do not carry on any trade . (<i>SARS Practice Note 31</i>) or <i>The principles contained in PN31 is legislated in section 11G. Section 11G came into effect for years of assessment ending on or after 1 January 2025/2026.</i>	1
Conclusion: Holdings deduction of the interest incurred of R68.1 million is limited to the interest of income earned of R34.9 thus a limited interest deduction of R34,9 million is allowed by SARS.	1P
	Available 9
	Maximum 8
<i>Y1: Critical thinking</i> <i>(Mark awarded for application of complex sections (s24J), thus an analysis and application of s24J considering court case principles and other legislation)</i>	1
	Total for part (d) 9
	TOTAL FOR PART I 50