

Part (a) Calculate Emily's taxable income for the 2020 year of assessment. Clearly indicate all items that have a nil effect and provide a brief reason for these items only.				Marks
Note		R		
3.1	<b>Salary</b> (R80 000 pm x 12) <i>[s1(1), gross income, par (c)]</i>	<b>960 000</b>	1	
3.2	Employer contributions to <b>provident fund</b> R960 000 x 7,5% = R72 000 <i>[s1(1), gross income, par (i); 7th Schedule, par 2(l)/12D]</i>	<b>72 000</b>	1	
3.3	Devoted <b>service award</b> <i>[s1(1), gross income, par (c)]</i>	<b>50 000</b>	1	
3.4	Cash inheritance <b>Reason: Capital in nature or capital receipt excluded from gross income</b> <i>[s1, definition///n]</i>	0	1	
3.5	Distribution received on 22% shareholding in <u>Redesign</u> : Return of capital <b>on shares held as trading stock</b> <i>[s1, gross income]</i>	<b>200 000</b>	1	
4.1	<u>Local dividends received</u> on 80% holding in Mega Baby R700 000 x 80% = R560 000 <i>[gross income, par (k)] [married out of community of property]</i>	<b>560 000</b>	1	
4.3	Interest received on debentures <i>[s24J(3)]</i> <b>is deemed to be a dividend in specie</b> , only accrues to Emily <b>on 31 March 2020</b> (last day of Mega Baby's year of assessment <i>[s8F(2)(a)]</i> ). No impact on her 2020 year of assessment. <i>or a interest in terms of section 24J interest (R9.2 million x 7,0292 x 60/365) – R106 305 – days must be used</i>	0	1	
2.2	Donation of 11% interest in Redesign ( <u>held as trading stock</u> ) to a spouse (Thato) (resident at the date of disposal). <b>Deemed disposal at cost</b> (s22(2)). R1 300 000 x 50% = R650 000	<b>650 000</b>	1	
2.2	<b>Closing stock</b> (11% holding in Redesign) R1 300 000 ÷ 2 = R650 000 <i>Share dealer must carry closing stock at cost and included in gross income (not taxable income)</i> <i>[Proviso (i) and (ii) under s22(1)(a)]</i>	<b>650 000</b>	1P	
2.1	<b>Local interest received</b> on Investco investment <b>[s7(8)(a)]</b> , <i>Thato is a non-resident until 1 October</i> thus will be taxed in the hands of Emily (donor) – s7(8)(a) <i>If s 24J was applied, interest will be limited to R23 800</i>	<b>15 000</b>	1	
3.6	<b>Insurance policy premiums paid by employer</b> (Mega Baby) on behalf of employee (Emily): <b>Reason: No fringe benefit as it is an event arising solely out of and in the course of employment of the employee</b> <i>Alternative: Seventh Schedule, proviso to par 2(k)</i>	0	1	
	<b>GROSS INCOME</b>	3 157 000		
	<b>Less: Exempt income</b>			
4.1	<b>Local dividend</b> (on 29/02/2020) <i>[s10(1)(k)]</i>	<b>(560 000)</b>	1P	
2.1	<b>Local interest received</b> on Investco <i>Exemption, s10(1)(i) [younger than 65 years]</i> <i>If s 24J was used limit to R23 800</i> <i>No mark if R25 000 was added</i>	<b>(15 000)</b>	1P	
	<b>Income</b>	2 582 000		

	<b>Less: deductions</b>			
2.2	<b>Opening stock</b> (22% in Redesign [s 22(2)])		<b>(1 300 000)</b>	1
3.3	<b>Devoted service award:</b> R5 000 adjustment under par 2(a) read with par 5 of the Seventh Schedule is only allowed if the long service award is <b>given in a form other than in cash.</b>		0	1
4.3	<b>Debentures issued</b> by Mega Baby Reason: <b>Expense of a capital nature</b>		0	1
	<b>Taxable income before s26A</b> [subtotal 1]		1 282 000	
2.1	Plus: <u>Taxable capital gain</u> [s26A] • <u>Cash donated to trust</u> – <b>no CGT / Rnil</b> Reason: <b>Cash is not an asset as defined.</b> [definition of 'asset', par 1, Eighth Schedule] • <u>Shares donated: Roll-over relief</u> between spouses [s9HB]:		0	1
	<b>Taxable income before s11F</b> [subtotal 2]		1 282 000	
3.2	<b>Provident fund contributions:</b> Emily's contribution                   72 000 Mega Baby's contribution               72 000 <b>144 000</b>			1P
	<b>S11F limited to the lesser of:</b> 1. R350 000; or 2. 27,5% x <u>the higher of:</u>			1
	• Remuneration ( <i>given</i> ): R1 082 000; or			
	• Subtotal 2: R1 282 000 ( <i>before s18A</i> )			
	<u>The higher is:</u> <b>R1 282 000 (P) x 27,5% = R352 550; or</b>			1
	3. Subtotal 1: R1 282 000 ( <i>before s 26A &amp; s18A</i> )			
	Therefore, <b>lowest amount of R350 000, limited to R144 000.</b>		(144 000)	1P
	No donations will receive a s18A deduction, as <b>no s18A certificate and not to a public benefit organisation</b>		0	1
	<b>TAXABLE INCOME</b>		1 138 000	
			<b>Available</b>	<b>23</b>
			<b>Maximum</b>	<b>20</b>
			<b>Total for part (a)</b>	<b>20</b>

Part (b) Advise Emily, purely from a tax perspective, what the – (i) advantages will be if she decides to invest the inheritance from her late father (see note 3.4) in local tax-free investments. No calculations are required.	Marks
<b><u>Return on tax-free investment is not subject too normal tax</u></b> All (100% of) the income and capital growth as returns on a tax-free investment will be tax free. All ' <b>income</b> ' growth (such as dividends, interest, etc.) will be <b>exempt</b> [s12T(2)] and <b>any capital gain</b> upon a tax-free investment's subsequent disposal will be <b>disregarded</b> [s12T(3)] for normal tax purposes.	1 1
<b><u>Dividend income as a return on investment is exempt from dividends tax</u></b> All <b>dividend distributions</b> to a natural person on a tax-free investment will be <b>exempt from dividends tax</b> [s64F(1)(o)].	1
<b><u>Re-capitalisation/re-investment of savings are not limited</u></b> Any income arising from the tax-free investment that is <b>capitalised</b> (re-invested as a contribution to the same underlying tax-free investment) will <b>not be part of the annual contribution limitation</b> of R33 000 <b>nor the lifetime contribution limit</b> of R500 000 [s12T(5) & (6)]. <i>(The R36 000 limitation applicable since 1 March 2020 does not form part of the SAICA Examinable Pronouncements for ITC 2021 and will not be marked).</i>	1
<b>Available</b>	<b>4</b>
<b>Maximum</b>	<b>2</b>
<b>Total for part (b)(i)</b>	<b>2</b>

Part (b) Advise Emily, purely from a tax perspective, what the – (ii) disadvantages will be if she decides to invest the inheritance from her late father (see note 3.4) in local tax-free investments. No calculations are required.	Marks
<b><u>Forfeit tax benefit if capital loss is realised</u></b> In the instance that the tax-free investment realised a <b>capital loss</b> upon its disposal (due to for example a drop in share prices/weak economy at the time of death, etc.), the capital loss will also <b>need to be disregarded</b> . In such a case the taxpayer will lose the tax benefit of utilising such capital loss against other capital gains [s12T(3)].	1
<b><u>Ownership limitation / limited transferability</u></b> <b>Only natural persons (or their estates) are allowed to hold (be the owner of) a tax-free investment</b> and no other 'person' as defined in s1. Hence, such investment <b>cannot be transferred to a legal entity</b> , such as a family-owned trust or company [s12T(1)(b)].	1
<b><u>Contribution limitations</u></b> • <b>Contributions</b> to a tax-free investment are <b>only allowed to be made in cash</b> , and not in forms other than in cash [s12T(4)(b)]; and	1
• <b>Any income arising from the tax-free investment that is transferred to a new tax-free investment held by the same person) will be regarded as forming part of the annual contribution limitation</b> of R33 000 <b>and the lifetime contribution limit</b> of R500 000 [s12T(5) & (6)].	1
• The <b>total contributions</b> to be made to <b>all tax-free investments held</b> by a single taxpayer are <b>in aggregate limited to R33 000 per year of assessment and in aggregate limited to R500 000 during the lifetime of the natural person</b> [s12T(5)]. <i>(The R36 000 annual limitation that is applicable since 1 March 2020 does not form part of the SAICA Examinable Pronouncements for ITC 2021)</i>	1

<b>Penalty for exceeding contribution thresholds</b> If, upon assessment, it is found that Emily invested in various tax-free investments with various financial service providers and that <b>the aggregate of all contributions exceeds the limitations of</b> either R33 000 (for the year of assessment) or R500 000 (for her lifetime up to date), any excess contributions above any one of these two limitation amounts will be <b>taxed at 40%</b> and will be deemed to be an amount of normal tax payable by Emily in the current year of assessment.	1
<b>Available</b>	<b>6</b>
<b>Maximum</b>	<b>4</b>
<b>Total for part (b)(ii)</b>	<b>4</b>
<b>Total for part (b)</b>	<b>6</b>

Part (c) Briefly explain, with respect to note 4.2, and with supporting calculations, the implications for Mega Baby with regard to – (i) VAT for the tax period ended 31 March 2020	Marks
As candidates are required to 'explain' the tax implications, they must provide reasons (i.e. explanations) to substantiate their answers. <i>No mark if stated that input tax needs to be 'paid/levied/charged' (e.g. if correct input tax terminology was not used) or if stated that 'notional input tax' needs to be claimed.</i>	
<b>Payment of night shift and overtime allowances</b> There will be <b>no VAT consequences</b> (alternative: <b>no input tax can be claimed</b> ) as it represents ' <b>remuneration</b> ' which is <b>excluded from the definition of an 'enterprise'</b> [proviso (iii)(aa) of the definition of 'enterprise' in s1].	1
<b>Purchase of delivery vehicles</b> <b>Claim input tax</b> on the vehicles as it represents delivery vehicles that are <b>not 'motor cars'</b> ( <b>single-cab delivery vehicle</b> , therefore not wholly or mainly for the carriage of passengers) as defined that will be used wholly/100% in the making of taxable supplies. The transport of goods by road in SA is a standard-rated/taxable supply: R400 000 x 15% x 20 vehicles = <b>R1 200 000</b> . <i>[definition of a 'motor car' in s1, read with s17(1)]</i>	1  1
<b>Supply of a right of use of a vehicle</b> is a <b>fringe benefit</b> to drivers is a <b>deemed supply</b> in terms of s 18(3) on which <b>output tax</b> needs to be <b>levied/paid/charged</b> : R400 000 x 0,6% x 15/115 x 2 months x 20 employees/vehicles = R12 522 <i>[s18(3) read with Government Notice 2835, section 10(13) of the VAT Act]</i> <i>Please note the time of supply rules are not applied as only the VAT is to be accounted for in the tax period ended 31 March 2020 (i.e. Feb/March 2020) is required.</i>	1  2P
<b>Available</b>	<b>6</b>
<b>Maximum</b>	<b>3</b>
<b>Total for part (c)(i)</b>	<b>3</b>

Part (c) Briefly explain, with respect to note 4.2, and with supporting calculations, the implications for Mega Baby with regard to – (ii) normal tax for the 2020 year of assessment.	Marks
<i>As candidates are required to 'explain' the tax implications, they must provide reasons (i.e. explanations) to substantiate their answers.</i>	
<b>Payment of night shift allowances: February 2020</b> R190 000 will be deductible in terms of s11(a)/general deduction formula as it was both incurred and paid during Mega Baby's 2020 year of assessment. <i>[Night shift allowances before 1 March 2020 are not 'variable remuneration' as defined in terms of s7B.]</i>	1
<b>Payment of night shift allowances: March 2020</b> R220 000 will <u>not</u> be deductible in terms of s11(a)/general deduction formula in Mega Baby's 2020 year of assessment because it represents ' <b>variable remuneration</b> ' as defined in terms of para (d) of that definition in s7B(1), which is <b>only deemed to be incurred once actually paid</b> by Mega Baby (the employer) to the drivers (the employees), namely on 5 April 2020 / <i>during Mega Baby's 2021 year of assessment.</i> <i>[Night shift allowances classified as 'variable remuneration' since 1 March 2020.]</i>	1
<b>Payment of overtime allowances: February 2020 and March 2020</b> R615 000 (i.e. R285 000 + R330 000) will be deductible in terms of s11(a)/general deduction formula as it was both incurred and paid during Mega Baby's 2020 year of assessment. <i>[Overtime pay had been classified as 'variable remuneration' since 1 March 2013.]</i>	1 1
<b>Purchase of delivery vehicles</b> As the purchase of the delivery vehicles is capital in nature, there is no s11(a) deduction. Therefore, claim s11(e) capital allowances from 1 February 2020 (date brought into use) to 31 March 2020 on the amount exclusive of VAT/input tax [s23C(1)]: R400 000 x 20 vehicles x 25% (Alt: ÷ 4) x 2/12 = R333 333 <b>Alternative:</b> R8 million x 25% (Alt: ÷ 4) x 60/366 days = R327 869	1 1
<b>Supply of right of use of vehicles (fringe benefits) to drivers</b> A s11(a)/general deduction formula deduction will be allowed equal to the amount of output tax paid on the deemed supply of the fringe benefit, namely (R12 522).	1P
<b>Available</b>	<b>7</b>
<b>Maximum</b>	<b>3</b>
<b>Total for part (c)(ii)</b>	<b>3</b>
<i>Communication skills – presentation</i>	<b>1</b>
<b>Total for part (c)</b>	<b>7</b>

Part (d) Discuss, with respect to note 4.3, the tax consequences for Mega Baby for the 2020 year of assessment. • Ignore VAT. • No calculations are required.	Marks
<i>No marks are to be awarded for theory. Candidates must apply the information of the scenario in their answers to earn marks.</i>	
The debt is an <b>interest-bearing instrument</b> and was issued by Mega Baby (issuer), a SA resident company and <i>section 24J</i> applies.	1
The <b>face value amount</b> of R9,2 million received by Mega Baby on <b>1 January 2020</b> for issuing the debentures will <b>constitute a receipt of a capital nature</b> and will <b>not be included in the company's gross income</b> for normal tax purposes during its 2020 year of assessment or <i>Mega Baby has the obligation for repayment and therefore did not receive it unconditionally/ for its own benefit and on its own behalf. Hence, no inclusion in its gross income.</i>	1
<b>Interest (s 24J(2) is deductible</b> as the interest is incurred <b>in the production of income and trade (funding of delivery vehicles) however,</b>	1
<b>Mega Baby is the issuer of a 'hybrid debt instrument'</b> as defined <i>[par (c) of this definition under s8F(1)];</i>	1
because <b>Mega Baby</b> owes R9,2 million (i.e. 23 000 x R400) in terms of a <b>qualifying arrangement</b> as defined in <i>s80L (given)</i> that was issued to Emily	1
<b>Emily</b> is a <b>connected person</b> in relation to <b>Mega Baby</b> because she <b>holds 80%</b> of the company's equity shares and voting rights <b>which is at least 20%</b> as required in terms of par. (d)(iv) of the definition of a ' <i>connected person</i> ' in s1; and	1
Mega Baby is <b>only obliged to redeem</b> the debentures (instrument) in full <b>after a period of 31 years</b> ( <i>1 January 2020 to 31 December 2051 = 31 years</i> ) which is <b>not within 30 years</b> (and the debentures are also not repayable on demand – this is clearly stated).	1
<b>Implications</b>	
S8F is applicable, which <b>prohibits Mega Baby from deducting the interest</b> incurred in terms of <i>s24J(2)</i> for normal tax purposes <i>[s8F(2)(b)]</i> .	1
The <i>s24J</i> <b>interest</b> amount incurred by Mega Baby during its 2020 year of assessment is deemed to be a <b>dividend in specie declared by Mega Baby to Emily</b> <i>[s8F(2)(a)]</i> .	1
The deemed dividend <i>in specie</i> is <b>deemed to have been declared and paid</b> by Mega Baby on <b>31 March 2020</b> ( <i>the last day of its year of assessment</i> ). <i>Mark only awarded if correct date is applied.</i>	1
As the dividend is deemed to be a dividend in specie, the company ( <b>Mega Baby</b> ) <b>is liable to pay dividends tax</b> at a rate of <b>20%</b> <i>[s64EA(b)]</i> .	1
<b>Mega Baby must have paid</b> the dividends tax to SARS before/on <b>30 April 2020</b> ( <i>the last day of the month following the month in which the dividend was paid</i> ) <i>section 64K</i> .	1
<b>Available</b>	<b>12</b>
<b>Maximum</b>	<b>6</b>
<b>Total for part (d)</b>	<b>6</b>

<p><b>Part (e) Explain the following regarding the policy to be adopted for the sale of cash gift cards:</b></p> <p><b>(i) How the VAT should be accounted for by Mega Baby when a cash gift card –</b></p> <ul style="list-style-type: none"> <li>○ is sold to one of its customers; and</li> <li>○ is redeemed in full by a customer on the acquisition of napkins and napkin liners for babies within 36 months after its date of issue</li> </ul> <ul style="list-style-type: none"> <li>• Support your answer with reference to the principle(s) of relevant case law. No calculations are required.</li> </ul>	<b>Marks</b>
<p><b><u>VAT treatment when gift card is sold</u></b></p> <p><b>No output tax will be accounted for</b> on the <b>sale</b> of a cash gift card.</p> <p><b>Reason:</b> In terms of s10(18) of the VAT Act, where a right to receive goods or services to the <b>extent of a monetary value stated on any token or voucher (such as a cash gift card)</b> is granted for a <b>consideration in money</b>, the supply of such token or voucher (gift card) is <b>disregarded</b>.</p>	1  1
<p><b><u>VAT treatment when gift card is redeemed within 36 months for nappies</u></b></p> <p>The supply of <b>baby ‘nappies’ (napkins and napkin liners for babies)</b> by Mega Baby will represent a <b>taxable supply of goods</b> at the zero rate/0% and output tax is levied/charged. [effective since 1 April 2019].</p>	1
<p><b><u>Value of supply:</u></b> Mega Baby will need to account for output tax at the zero rate/0% <b>on the full consideration of the baby nappies</b> supplied to the customer [s10(3)(a) and s11(1)(w) in Part C of Schedule 2 to the VAT Act].</p>	1P
<b>Available</b>	<b>4</b>
<b>Maximum</b>	<b>3</b>
<b>Total for part (e)(i)</b>	<b>3</b>

<p>Part (e) Explain the following regarding the policy to be adopted for the sale of cash gift cards:</p> <p>(ii) How Mega Baby's gross income, as defined in the Income Tax Act, will be impacted when a cash gift card –</p> <ul style="list-style-type: none"> <li>○ is sold to one of its customers; and</li> <li>○ expires before it is fully redeemed by a customer.</li> </ul> <p>• Support your answer with reference to the principle(s) of relevant case law. No calculations are required.</p>	<p>Marks</p>
<p><u>Legislative principle:</u> Mega Baby needs to include an amount obtained in its gross income <b>on the earlier that it is received by or accrues to it.</b></p>	<p>1</p>
<p><u>Case law principle:</u> However, the case of <i>Geldenhuys v CIR</i> established the principle that the term '<b>received by</b>' means that Mega Baby (<i>the taxpayer</i>) needs to receive such an amount <b>on its own behalf and for its own benefit.</b></p> <p><i>No mark awarded for case name, only for case law principle applied in the correct context.</i></p>	<p>1</p>
<p><b><u>Impact on gross income when gift card is sold?</u></b></p>	
<p><u>Application:</u> The amount received from the gift card sales, were <b>not for Mega Baby's own benefit, but were to be held for the gift card holder.</b></p>	<p>1</p>
<p>The <b>right to benefit</b> from the monetary amount in the form of a cash discount upon the subsequent acquisition of goods and/or services from Mega Baby <b>remains the property of the gift card holder (and not that of Mega Baby) until it is redeemed</b> (either in full or on part) for up to a period of 36 months after the date of sale. It is thus held in a fiduciary capacity.</p>	<p>1</p>
<p><u>Conclusion:</u> <b>On the date of sale, Mega Baby will not include the cash amount received from the disposal of the gift card in its gross income.</b></p>	<p>1P</p>
<p><b><u>Impact on gross income when gift card expires before fully redeemed?</u></b></p>	
<p><u>Application:</u> Upon the expiry of the gift card Mega Baby will have no further obligations towards the gift card holder, as all rights to and benefits of the cash value of the unredeemed cash amount will be forfeited by the card holder when it expires. Hence, the <b>unredeemed value of the cash amount will become the property of Mega Baby, to be held on its own behalf and for its own benefit from the date that the gift card expires.</b></p>	<p>1</p>
<p><u>Conclusion:</u> <b>On the date of expiry, Mega Baby needs to include the unredeemed portion of the cash amount</b> (which could either be the entire original sales price, or a portion of it) <b>in its gross income.</b></p>	<p>1P</p>
<p style="text-align: right;"><b>Available</b></p>	<p><b>7</b></p>
<p style="text-align: right;"><b>Maximum</b></p>	<p><b>7</b></p>
<p style="text-align: right;"><b>Total for part (e)(ii)</b></p>	<p><b>7</b></p>
<p style="text-align: right;"><i>Communication skills – logical argument</i></p>	<p>1</p>
<p style="text-align: right;"><b>Total for part (e)</b></p>	<p><b>11</b></p>
<p><b>TOTAL FOR THE QUESTION</b></p>	<p><b>50</b></p>