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24 November 2023

National Treasury
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Dear National Treasury and Ms Collins

SUBMISSION - ANNEXURE C 2024 BUDGET REVIEW

1. We present herewith our written submission on the request for Annexure C 2023 issues on behalf of the South African Institute of Chartered Accountants' (SAICA) National Tax Committee (NTC), as set out in Annexure A.

2. Our submission includes a combination of representations, ranging from serious concerns about the impact or effect of certain provisions to simple clarification or suggestions for potentially ambiguous provisions, in relation to either existing sections or the latest proposed amendments to various sections of the Income Tax Act, No. 58 of 1962 (the ITA), the Value Added Tax Act, No 89 of 1991 (the VAT Act), the Employment Tax Incentive Act, No. 26 of 2013 (the ETI Act) and the Tax Administration Act, No. 28 of 2011 (the TAA), as contained in the Taxation Laws Amendment Bill, 2023 (TLAB2023) and the Taxation Administration Laws Amendment Bill, 2023 (TALAB2023), respectively.

3. We have noted and considered National Treasury's responses on certain matters of our prior year submissions. Where the consideration was still unclear or we still believe it to be in the public interest, we would seek to engage with National Treasury on why it believes the relevant proposals would not be in the interests of South African fiscal policy or in creating alignment between tax policy and legislation. There are however numerous matters previously raised that were not addressed at the 3 November 2022 engagement.

4. We have deliberately tried to keep the discussion of our submissions as concise as possible, which does mean that you might require further clarification. In this respect, you are more than welcome to contact us in this regard.

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5. We have also highlighted in yellow, the areas that we feel require priority considering the impact that it would have on taxpayers/the fiscus.

6. We would like to encourage National Treasury and propose, as Parliament did in 2022, to maybe expand its engagement on the Annex C submissions and policy matters not considered for a particular fiscal year to an annual and regular process.

7. As always, we thank National Treasury and SARS for the on-going opportunity to participate in the development of the South African tax law.

Should you require any further clarification on any of the matters raised please do not hesitate to contact us.

Yours sincerely

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CHAIRPERSON: NATIONAL TAX COMMITTEE	**PROJECT DIRECTOR: TAX ADVOCACY**

The South African Institute of Chartered Accountants

ANNEXURE A

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CATEGORY - INCOME TAX: INDIVIDUALS, EMPLOYMENT AND SAVINGS

Section 23(m) & 23(b) – Home office allowances and disallowance of interest paid *(submission originally made in 2022)*

Legal Nature

1. Interpretation Note 28 (Issue 3) issued by SARS deals with deductions of home office expenses incurred by persons in employment or persons holding an office. This Interpretation Note states that, for years of assessment commencing on or after 1 March 2022, if the interest expense (interest incurred on a home bond) meets the requirements in section 24J, the portion of interest incurred in connection with the part of the premises used for purposes of trade (the home office) will be prohibited by section 23(*m*) and is not deductible.

2. The reason for disallowing this deduction, according to SARS, is that section 23(m) – a section that prohibits the deduction of certain expenses for salary earners (other than a few expenses, such as those allowed in terms of **section 11(a)**, for example, the rent, repairs or other expenses incurred in respect of a home office that are allowed under section 23(b)) – does not allow the deduction of interest on a bond on a home office because the interest is deductible under **section 24J** and not section 11(a) as required in terms of section 23(m).

3. Section 23(m) only applies to expenditure, losses or allowances ***contemplated in section 11*** and which relate to any employment in respect of which the taxpayer derives any remuneration. This begs the question whether section 24J is a section 'contemplated' under section 11. If it is, then section 24J interest will be prohibited by section 23(m) as section 23(m) only allows interest deductible in terms of section 11(a) as a deduction (section 23(m)(iv)). If it is not, then section 24J interest will remain deductible as it is not prohibited by section 23(m)(iv) as it is not an expense contemplated in section 11 and thus the section 11(a) argument no longer applies.

4. SARS argues that section 24J is '**contemplated in section 11'** by means of section 11(x). Section 11(x) states that there shall be allowed as a deduction from the income of a person '*any amounts which in terms of any other provision in this Part (encompassing section 5 to 37G), are allowed to be deducted from the income of the taxpayer'*. This section, according to SARS thus includes section 24J, as it is 'contemplated in section 11', even though it is not deductible under section 11.

5. However, it is our understanding that section 24J is a standalone deduction provision under Part I of Chapter II. Section 24J(2) reads as follows: *Where any person is the issuer in relation to an instrument….deemed to have incurred such interest…….which must be* ***<u>deducted from the income</u>*** *of that person….*

6. As we understand it, section 24J is not reliant on section 11(x) as the 'deduction' section (see the 2009 Explanatory Memorandum on the Taxation laws Amendment Bill) which stated the following in relation to the changes to section 11A:

7. "*Section 11A allows taxpayers to claim their pre-start up expenses even though a trade has not yet commenced. All deductions under section 11A are ring-fenced so as to be useable only against present and future income from the same trade. The deductions … cover all items listed in section 11 (other than section 11(x) which refers to deductions outside section 11(x)). When enacted in 2003, these deductions included all interest deductions relating to section 24J instruments because section 24J was previously only a timing provision (the deduction being granted by virtue of section 11(a) or (bA). Late in 2004, amendments were made so that section 24J shifted from a mere timing provision to a stand-alone deduction and income provision. A corresponding amendment to section 11A, however, was inadvertently omitted, thereby excluding section 24J from section 11A start-up relief. The cross-references to section 24J will accordingly be included section so as to restore the intent of the initial legislation*."

8. Thus, interest was no longer deductible in terms of section 11(a), but in terms of section 24J and it fundamentally also changed the nature of section 24J. Should section 24J be contemplated as being included in section 11(x), then interest would be deductible under both section 24J and section 11(x), which clearly cannot be.

9. So, the question is whether section 24J is covered under section 11(x) and therefore a deduction under section 11 and consequently prohibited by section 23(m). Or does it rank as a separate deduction from section 11?

10. In this regard, we refer to section 8(4)(a) which stipulates the following:

(4)

(a) There shall be included in the taxpayer's income all amounts allowed to be deducted or set off under the provisions of sections 11 to 20, inclusive, section 24D, section 24F, section 24G, section 24I, section 24J, section 27(2)(b) and section 37B(2) of this Act, except section 11(k), 11(n), 11(p) and (q), section 11F, section 12(2) or section 12(2) as applied by section 12(3), section 12A(3), section 13(5), or section 13(5), as applied by section 13(8), or section 13*bis*(7), section 15(a) or section 15A, or under the corresponding provisions of any previous Income Tax Act, whether in the current or any previous year of assessment which have been recovered or recouped during the current year of assessment:

11. This section specifically includes in a taxpayer's income a recoupment of amounts allowed as a deduction under, inter alia, section 11 to 20 and separately incorporates the various other sections separately listed.

12. One of these separately listed sections is section 24J.

13. The legislator had to specifically list the deductions allowed that must be recouped to ensure the proper operation of the provision, but as section 24J is separately listed from the deductions allowed under section 11 to 20, it is evident that the legislator did not contemplate or intend section 24J as being included under section 11.

14. It would have been superfluous to list section 24J separately if it was in any event included under section 11(x) and therefore section 11. The context also clearly indicates and aligns to the scheme of the Act to allow for deductions and match recoupments accordingly.

15. In persuasive support of this conclusion the court IT 25042 (14 July 2022) at [38] states:

> *"I agree with the Councillor for the Appellants in the Heads of Argument that section 24J constitutes a standalone deduction provision in relation to interest as defined".*

16. Other than the overtly technical argument presented above, SARS has not raised any policy matter as to why it would object to the continuing deduction of interest incurred in the production of income and in the course of trade. They also accept that it in principle creates arbitrage between those who rent the property from which a home office is conducted and those that purchase such property.

17. Furthermore, should such a taxpayer dispose of such property, they will now be subjected to pro rata CGT that the primary residence exclusion also does not apply to, even though the largest expense in relation to the property, namely interest, was denied.

Factual Description

18. SARS has in practice, since the inception of section 23(b), taken the interpretation that pro rata interest expenditure incurred on a bond over premises, used partially for trade, is a cost of such premises and is deductible.

19. Factually, interest expenditure incurred on a bond to purchase premises is directly connected to carrying on such trade and is no different from a cost such as rental to enable the use of premises.

20. In addition to the above, it seems inequitable from a policy perspective, that a person renting a house with a home office, would be entitled to deduct the rental paid (allowed in terms of section 23(m)(iv)), yet a person who owns the house would not be able to deduct the interest on the bond.

The nature of taxpayers impacted

21. All taxpayers required to work from home or conducting services/trade from home and have a bond on their home.

Proposal

22. In addition to our recommendations made in our 2021 Annexure C submission on section 23(m) and section 23(b) – see Annexure A- we recommend that legislative clarity is urgently provided in this regard as the legislative interpretation concerns would impact various other sections of the Income Tax Act as well.

23. We are of the view that section 11(x) does not include section 24J and thus that interest expenditure incurred in respect of a home office should be allowed as a deduction and not be prohibited by section 23(m)(iv).

24. Even if SARS' argument is correct, there seems no legitimate policy reason to prevent the pro rata deduction of interest incurred in the production of income and in the course of trade in respect of home offices. The law should be amended to explicitly allow for the deduction.

Section 23(m) & 23(b) – Home office allowances *(submission originally made in 2021)*

Factual description

25. We have addressed the policy and technical alignment of the provision as pertains to interest above. The below addresses the technical arguments on interest but also the broader policy concerns as pertains to home offices allowances and the changing reality.

26. Section 23(b) provides for a limitation of deduction for home office expenses that an individual can claim.

27. In May 2021 SARS issued an updated Draft Interpretation Note 28 for public comment and in November 2021 it issued a revised version of this draft interpretation note. The revised version provides further clarity in response to the public comments submitted and addresses the deductibility of interest incurred in connection with a home office.

28. It stipulates that the consequence of bond interest being deductible under section 24J(2) and not under section 11(a), is that bond interest incurred in respect of a home office premise is prohibited from deduction by section 23(m).

29. The Draft Briefing Note to the revised interpretation note states the following: "*The interpretation discussed above represents a significant change, and, accordingly, the updated draft IN 28 is being released for a second round of comment.*"

30. Furthermore section 23(b) requires that "such part" of a premise must be "*regularly and exclusively used*" for the purposes of such trade.

31. The reason for inserting this limitation was explained in the 1991 Income Tax Act Explanatory Memorandum as:

CLAUSE 23

Deductions not allowed in the determination of taxable income: Amendment of section 23 of the principal Act

Section 23(b) of the principal Act prohibits the deduction of domestic and private costs as well as expenditure incurred in connection with premises not occupied for the purposes of trade. However, if any part thereof is used for the purposes of trade, a deduction is nevertheless allowed. The test as to whether any premises are used for the purposes of trade, is a question of fact and often very difficult to establish. In the past, various disputes have arisen in this connection, especially with regard to expenses relating to the maintenance of a study at home. The amendment introduced by this clause now requires that in order to qualify for a deduction, the relevant part—

(*a*) must be specifically equipped for purposes of the person's trade; and

(*b*) must be used regularly and exclusively for purposes of trade.

32. In this regard it should be noted that it was particularly "a study at home" and not home offices *per se* that was problematic to SARS as the former rather than the latter was actually the practice.

Factual Description

33. SARS has in practice, since the inception of section 23(b) taken the interpretation that pro rata interest on a bond of a premises, used partially for trade, is a cost of such premises and is deductible.

34. Factually interest on a bond to purchase a premise is directly connected to carrying on such a trade and is no different from a cost such as rental to enable use of a premises.

35. Section 23(b) was created in circumstances when a "home study" was for a few and something that was not that common as it was commonly used for ancillary work (self-study) or after hour work.

36. Today our reality is a lot different. Our work, clients and homes are digitally connected and many people can now perform their full and primary work from their "home office".

37. It is highly unlikely that many employers will require all employees to return to the offices or on a full-week basis, meaning that the home office will become a permanent location of work for many employees regardless of the lockdown restrictions.

38. This applies across job levels and sectors in the economy which means that it also applies to those who do not have the luxury of large suburban homes and a stand-alone "home study". These new "work from home" taxpayers mostly only have shared family space.

39. This "home office" migration is not only COVID driven but is a result of changes brought about the digital economy and how people work. However, as the digital and "gig economy" expanded more, especially younger taxpayers have moved away from the traditional employment model and now have multiple "gigs" that vary from Uber services to part time employment and multiple short term contractor work. Even their payment model has migrated away from cash and money. This has resulted in exponentially more "individual small business taxpayers" conducting business that not only share personal and business moveable assets such as cars and cell phones but also their place of home and work.

40. This needs to be considered when contemplating amendments to section 23(b) and/or 23(m) in order to enable an equitable tax regime relating to the future working environment. Section 23(b) has an extremely narrow application and should be expanded to accommodate the "new normal".

41. We strongly suggest that there should have been a certain degree of relaxation in the legislation especially in relation to the requirement in section 23(b) that the home office be "exclusively" used for the purposes of trade. Furthermore, the prohibition of the bond interest which will be effective for years of assessment commencing on or after 1 March 2022 will further prejudice those employees forced to work from home.

The nature of taxpayers impacted

42. All taxpayers required to work from home or conducting services/trade from home, which has significantly expanded since COVID 19 and we believe will remain significant even after the pandemic.

Proposal

43. Consideration needs to be given to amending the definition of "exclusively used" to "used mainly as a home office". It is submitted that by increasing the requirement from "regularly and exclusively" to "mainly", the deductions scope is limited to persons who use the space more than 50% for trade purposes but not exclusively as opposed to used less than 50% but in regular intervals of the time but exclusively when in such use.

44. Consequently, the requirement for remunerated taxpayers to receive commission or variable income in section 23(m) should be deleted. There seems to be no policy rationale to distinguish between commission and other remuneration earners when in both instances they are required to work from home. This seems a historically factually limitation when most persons who factually worked from home were earning such types of income. That is not true anymore.

45. Furthermore, we believe SARS' interpretation of "such part" in section 23(b), that this relates to a specific room, does not correctly reflect the law. Where the same part is exclusively used for carrying on a trade by more than one taxpayer it should be allowed as a deduction for both in equal parts and this should be clarified in the legislation. This, however, is only an interpretative challenge under the current "exclusive use" requirement.

46. In addition to the above, the scope of qualifying expenses for purposes of section 23(b) should be expanded to align to the changing factual reality that employees now have to incur necessary and not convenience business expenses for the purposes of conducting their trades.

47. An example of items that should be included in the section and allowed as a deduction, would be a salaried employee meeting all the other requirements of sections 23(m) and 23(b), having to incur costs such as printing paper, cartridges, stationery, fast/stable internet (such as fibre), security costs, UPS etc. relating to working from home. These costs would be subject to the same normal apportionment rules if not exclusively used for trade purposes.

48. In respect of the bond interest, section 23(b) should refer to interest which is deductible under section 11(a) and section 24J(2).

49. Regarding internet costs and telephone costs, taxpayers have had to use their internet and telecommunications systems in order to carry out their employment duties effectively, including participating in virtual meetings/video conferences and being available on their cell phones (sometimes requiring the installation of boosters etc). Currently a disparity exists between those whose employers are willing to pay these costs versus those who are already disadvantage by not having this benefit as paragraph 6(4)(bA) and 10(2)(bA) of the Seventh Schedule **correctly in our view** already places a zero value on these costs for employees. We submit that section 23(m) should mirror these provisions.

50. Thus, the interpretation of the provision "expenses in connection with premises" in section 23(b) should be extended to include the costs of equipping the home office with the necessary consumables (stationery, insurance etc) and running costs (e.g. monthly charges in respect of communication services).

51. It is submitted that legislation should be amended to accommodate the deduction of these costs, considering the "new normal".

52. Furthermore, relief should be provided from the pro-rata capital gains tax that will arise on the subsequent sale of the house due to the section 23(b) claims that were allowed, for at least the period covered by the lockdown.

Section 30B(2)(b)(ix) – Associations and Trade Unions *(submission originally made in 2022)*

Legal Nature

53. Section 30B(2)(b)(ix) of the ITA requires that substantially the whole of any association's funding must be derived from its annual or other long-term members or from an appropriation by the government.

54. “Funds” are referred to in section 30B(2)(b)(iv). This sub-section states that the entity is required to utilise substantially the whole of its funds for the sole or principal object for which it has been established.

55. SARS’ interpretation of ‘funding’ creates a legal anomaly as it implies that the extent of the receipt of non-taxable amounts (such as donations, grants etc) could put the exemption of the entity at risk when the exemption in context was not created for such purpose.

56. Thus, the exemption provision would not integrate with the administrative provision in the legislation in terms of SARS’ interpretation as section 30B seems to supersede section 10(1)(d)(iii) and (iv) instead of section 30B being read in the context of section 10(1)(d)(iii) and (iv), the latter being the actual exemption provision as relates to amounts of income received and accrued.

57. The section 30B concept of “funding” is interpreted to go beyond the confines of section 10(1)(d)(iv) which is the actual exemption.

Factual Description

58. Funding: SARS recently issued the final version of Interpretation Note 125 (IN 125) on “Associations: Funding Requirements” that provided guidance on the interpretation and application of the “funding” requirement.

59. IN 125 contains various concerns that might jeopardise many associations’ tax-exempt status. SAICA raised these concerns in its submission on the draft version of IN 125, dated 5 November 2021. One of the concerns relates to SARS’ interpretation of the term “funding”.

60. SARS’ interpretation of “funding” includes items such as loan capital and overdrafts received, other capital amounts and donations received – none of which would be included in ‘gross income’ as defined in section 1 of the ITA i.e. amounts that would ordinarily not be taxable and would ordinarily not require an exemption are now jeopardising an entity’s tax exemption status.

61. Appropriations from government: SARS’ interpretation is that the exemption should be interpreted narrowly and therefore “sphere of government” should also be interpreted narrowly. For the legal reasons set out in our submission we do not agree with SARS’ interpretation or that the case law they cite is applicable.

62. The absurdity created is for example, an entity that receives a significant donation that is capital in nature and not subject to tax, can now be at risk of losing its exemption status. Furthermore, receiving funds from government that are appropriated by national or provincial government but indirectly through a scheduled entity such as SARS or a SETA is now interpreted as being non-qualifying funding and again exposing the entity to its exemption being withdrawn by CSARS.

63. This mismatch would cause situations where entities would have to consider refusing to receive indirect government grants or capital receipts so as not to jeopardise their exemption status when the receipt of such amounts should not raise concern as it does not create trading or competition and it still must be aligned to the objectives of the entity. It also does not impinged on the organisations objective of not being for profit as it is not receiving these amounts in a scheme of profit making. This would purely be driven by the fact that the three spheres of government habitually use agencies and entities to disperse funds for service delivery.

64. It could never have been the intention of the legislature, in the context of the legislation as drafted, to prevent bodies from receiving funds that are not income and would not require an income exemption to start with whether from a sphere of government to perform a public good just because a sphere of government decided to appropriate the monies in a particular way through a particular state-controlled organ. Such an interpretation would result in a glaring absurdity.

65. Substantially the whole: Reference is made in the draft IN to Binding General Ruling (BGR) 20 and SARS notes that it will interpret "substantially the whole" as 90% or more but will accept 85% or more as meeting the criteria.

66. As mentioned in our previous submission, dated 30 April 2020, in our view the law does not allow SARS to take a position contrary to the promulgated law and SARS' own express interpretation of it and thus we consider the BGR position to be unlawful.

67. SAICA does, however, support the 85% threshold as a better interpretation of the law but is of the view that it should be included in law to avoid uncertainty and debate, especially should a dispute arise where SARS will invariably argue that 90% is its formal position on the interpretation.

68. Withdrawal of approval: SARS takes the position that if the non-compliance is not corrected after notice was given, the exemption is withdrawn from the year of first non-compliance and not from the current year of assessment.

69. The legislation is, however, not clear on this, and SARS' view would seem impracticable because if, for example, the entity failed the funding test 3 years ago, it would never be able to correct it and would at best be able to correct it from the current year when the notice was received.

70. It also would mean that, if the exemption is withdrawn retrospectively, there upon following years would be taxable and would have to be reassessed as a company with resubmission of an ITR14 from the first year of contravention which could be decades.

71. The law provides no leeway or discretion to the CSARS to resolve this impossibility to instruct the exempt body to correct its non-compliance going forward.

72. Exiting the regime: Many entities find themselves in a position where membership funding alone just can't sustain them financially. However the "exit charge" in s30B(9) is

based on the market value of all the assets less liabilities as being included in taxable income. In most instances this would require the entity to sell off a material part of its assets and would not be a viable option either thus keeping them trapped. Many of these entities acquired their assets long before section 30B and its current administrative requirements came into being.

The nature of taxpayers impacted

73. Associations and trade unions wanting to or that have already applied for exemption under section 10(1)(d)(iii) & (iv) read with section 30B.

Proposal

74. Funding: The purpose of section 30B is to regulate the operations of entities for the exemption of taxable amounts under section 10(1)(d)(iii) & (iv) and it should integrate with and be interpreted in context with section 10(1)(d). "Funding" should thus not include all amounts received.

75. Section 30B should deal only with taxable amounts that need to be exempted, like member fees and other incidental trading income. All other receipts (such as investment income (defined), donations, capital amounts etc) should be excluded from "funding". Therefore, amounts that are not included in gross income should not be seen as a source of funding.

76. The definition of "funding" should thus be amended and it is proposed that the requirement should rather be that the income from trading with non-members should be limited to a certain percentage.

77. Appropriations from government: The legislation should be amended to clarify and properly reflect the expanded interpretation of "sphere of government" that includes other government entities or organs of state as this would still be in line with the purpose and intention of the ITA.

78. Substantially the whole: The legislation should be amended to reflect 85% as the threshold.

79. Withdrawal of approval: We accept that if the withdrawal is applicable only after notice provided by SARS, compliant taxpayers are at a disadvantage as many taxpayers will now "ride the system" till caught, but similarly if SARS is compelled by the current legislation to compel the association or union to correct historical positions that they cannot, that is also impractical. The legislation should thus be amended to make it clear from what date the withdrawal of approval is effective – preferably from the period after the notice is provided by SARS.

80. It is also suggested that the legislation is amended so that the sanction for non-compliance is not only withdrawal (not retrospective), but that other sanctions such as penalties based on a percentage of impermissible trading income be introduced. This

would ensure a balance between SARS's ability to regulate the industry and also sanction historical non-compliance without creating an incentive for non-compliance.

81. Exiting the regime: Where an organisation finds itself unable to suitably fund itself from membership fees not exit the regime, it is proposed that a mechanism be introduced to enable such an exit. This can be achieved by either reducing the exit charge to a more reasonable fixed % and/or introducing a temporary measure similar to par 51A Eighth Schedule to enable exits.

Section 89*quat* – Interest on under/overpayment of provisional tax *(submission originally made in 2022)*

Legal Nature

82. Section 89*quat* makes provision for the imposition of interest on underpayments and overpayments of provisional tax. Interest in terms of this section is either levied on an underpayment of tax or paid on an overpayment of tax from the 'effective date'.

83. In terms of section 89*quat*(4), interest is payable to a *provisional taxpayer* if the 'credit amount' exceeds the normal tax payable for that year of assessment and:

- The amount exceeds R10 000; or
- The taxable income for the year exceeds R20 000 (company); or
- The taxable income for the year of assessment exceeds R50 000 (for any other person).

Factual description

84. There is no provision in the ITA or the TAA that grants individuals who are *not provisional taxpayers*, interest on PAYE withheld in excess of the tax due for the year. Once SARS has assessed such a taxpayer, SARS can keep the taxpayer's money for a lengthy period without having to pay any interest.

85. This is clearly unfair and a questionable practice.

86. An example of how this can (and has) occurred is where a DTA applies to an individual in respect of tax on a provident fund lumpsum, where South Africa has no taxing rights but PAYE was incorrectly paid over to SARS on this amount. Despite a lengthy dispute process to which SARS eventually conceded, SARS did not have to pay interest.

The nature of taxpayers impacted

87. Individuals that are not provisional taxpayers and that have had excessive PAYE deducted from their remuneration by their employers.

Proposal

Provision should be made in the Act for the payment by SARS of interest to individuals when PAYE has been over-deducted by their employers, from the date of assessment to the date of eventual payment of the refund by SARS, with the interest accruing from date of assessment till date of payment of the refund by SARS.

Paragraph 13 of the First Schedule – Farming *(submission originally made in 2022)*

Legal Nature

88. Paragraph 13 of the First Schedule of the Act deals with farmers who purchased livestock to replace livestock previously sold on account of drought, stock disease or damage to grazing by fire or plague.

89. It allows such farmers to elect a deduction of the purchase expenditure of said 'replacement livestock' in the year of assessment in which the aforementioned sale took place. The deduction must, however, be claimed within five years of the end of the year of assessment in which the sale took place.

90. Paragraph 13(2) then disallows the deduction of the cost of the 'replacement livestock' in the year of assessment in which it was purchased.

Factual Description

91. The amounts received from the livestock sold on account of drought, disease, etc. qualify as gross income and are subject to income tax. The resultant tax burden thus creates a cash flow problem for the farmer as it impedes on his ability to replace as much livestock as possible. The farmer could have purchased more replacement livestock had he not had to pay tax from the sale.

92. Though paragraph 13 allows him to 're-open' the previous assessment (in which the sale took place), he will have already paid the tax (cash) in respect of that year and suffered a reduction in his cash flow. Re-submitting that prior tax return will also likely result in an audit, thereby delaying whatever refund he may be due, which he would use to purchase more replacement livestock.

The nature of taxpayers impacted

93. Farmers of livestock.

Proposal

94. The gross income resulting from the livestock sold on account of drought, stock disease, etc. ought to be disregarded in the year of assessment in which the sale took place, and instead be included in (rolled over to) the year of assessment in which the replacement livestock is purchased, thus matching the gross income from the sale to the deduction on the expenditure incurred on the replacement livestock.

95. Paragraph 13(2) should therefore be deleted.

Fourth Schedule: Paragraph 1 and 9(1) – Standard Employment *(submission originally made in 2022)*

Legal Nature

96. Paragraph 9(1) of the Fourth Schedules states that the Commissioner may, *inter alia*, prescribe the amount of employees' tax to be deducted from any amount of remuneration.

97. According to the SARS Guide for Employers in respect of Employees' Tax for 2022, the weekly, fortnightly and monthly tables, as published each year after the Budget Speech, must be used to determine the amount of employees' tax to be withheld from the balance of remuneration for each pay period. The annual table must be used at the end of the tax period or year of assessment to determine the final amount of employees' tax payable for the full year or period of assessment.

Factual Description

98. The SARS Guide for Employers in respect of Employees' Tax for 2022 also includes the following:

Employees' tax

- **Standard Employment income**
  - The weekly, fortnightly and monthly tables, as published each year after the Budget Speech must be used to determine the amount of employees' tax to be withheld from the balance of remuneration for each pay period. The annual table must be used at the end of the tax period or year of assessment to determine the final amount of employees' tax payable for the full year or period of assessment,.
- **Non-standard employment income**
  - The Commissioner prescribes tax deduction tables for such classes of employees as the Commissioner may determine and also prescribe the manner in which they may be applied.
  - Employees' tax must be calculated and deducted at 25% on the balance of remuneration.
- **Tax Directive**
  - Where the employer is in possession of a tax directive in respect of an employee who is in non-standard employment, employees' tax must be deducted in accordance with the directive.

Summary

Scenario	Employees' tax
Employee is required to work at least 22 hours a week (standard employment) and earns remuneration which exceeds the annual tax threshold (R87 300 if less than 65 years old / R135 150 if 65 years or older /R151 100 if 75 years or older)	Use tax deduction tables
Employee is required to work at least 22 hours a week (standard employment) and earns remuneration which does <u>not</u> exceed the annual tax threshold (R87 300 if less than 65 years old / R135 150 if 65 years or older / R151 100 if 75 years or older)	No employees' tax to be deducted
Employee is in non-standard employment, required to work at least 5 hours per day and earns less than R349 for that day	No employees' tax to be deducted
Employee is in non-standard employment, required to work at least 5 hours per day and earns more than R349 for that day	25% deduction
Employee is in non-standard employment, required to work less than 5 hours per day and earns less than R349 for that day	25% deduction

99. The SARS Guide for Employers in respect of Employees' Tax for 2022 uses deleted concepts such as "standard employment". This term was relevant when SITE was still applicable.

100. Individuals who are in single employment and who only work for a few hours a day, according to the above table, should be taxed at 25%. The actual normal tax payable on

assessment, will generally be less than the 25% required to be withheld by employers in terms of the table above.

101. This 25% is however not in the law anymore nor the relief under the repealed clause (b) of para 11B Fourth Schedule, definition of Standard Employment.

The nature of taxpayers impacted

102. All taxpayers who have single employment and who only work for a few hours a day and any employee, who derives the daily amounts from more than one employer, but the aggregate is below the upper limit where the 18% rate no longer applies.

Proposal

103. It is proposed that a regime similar to the repealed para 11B Fourth Schedule be reinserted.

104. This should enable (a) that the Commissioner can direct that 25% PAYE be withheld where the employee receives remuneration from more than one employer as is the current practice and as was enabled in the repealed para 11B and (b) that the employer is entitled to apply the tax tables where the employee submits a written declaration similar to what was contained in the repealed definition of Standard Employment.

Fourth Schedule: Paragraph 13(2)(b) – Issuing of employees' tax certificates *(submission originally made in 2022)*

Legal Nature

105. Paragraph 13(2)(b) of the Fourth Schedule provides that where an employer has ceased to be an employer in relation to an employee but has continued to be an employer in relation to other employees, then the employer must issue an employees' tax certificate to the former employee within 14 days of the date on which the employer ceased to be an employer to that employee.

Factual Description

106. The SARS guide and legislation requires the IRP5 certificates to be issued 14 days after an employee resigns, dies or retires. Although this provision makes sense for manual IRP5 processes, as were in effect at the time this paragraph was inserted into the legislation, these processes are now automated and the provision does not take into account the changes in the IRP5 process or the technological advances made in the submission process.

107. However, payroll systems require periodical close off and are not open to close out and issue IRP 5 outside these cycles to protect the integrity of the data.

108. It is not feasible for employers to issue IRP5 certificates during the year for each employee to which one of these events relates. It is further not clear what the purpose is of issuing these mid-cycle IRP5 certificates, except in the case of death.

109. There are also now 2 PAYE reporting cycles in a year which did not exist historically and taxpayers are not dependent on their “tax info” from employers as it is now on SARS efiling.

The nature of taxpayers impacted

110. Employees who resign or retire during a year of assessment.

Proposal

111. The requirement to issue IRP5 certificates on resignation or retrenchment within 14 days should be removed as it is unclear why this is necessary, but it is also not practically feasible to issue these certificates within this time period.

112. It is proposed that this requirement be aligned to the current SARS biannual reporting cycles.

Paragraph 14(6) - Penalty for late submission on the EMP501 reconciliation *(submission originally made in 2022)*

Legal Nature

113. Paragraph 14(6) of the Fourth Schedule of the Act imposes a percentage-based penalty under Chapter 15 of the TAA for each month that the employer fails to submit a complete return (i.e. an EMP501 reconciliation). Such penalty may not exceed 10 per cent of the total amount of employees’ tax deducted or withheld, or which should have been deducted or withheld by the employer from the remuneration of employees for the period described in that subparagraph.

Factual Description

114. On review of the administrative non-compliance penalties in Chapter 15, it appears that the penalty referred to is in terms of section 213 of the TAA, which provides for the imposition of a percentage-based penalty, as is envisaged by paragraph 14(6).

115. Section 213 does not empower SARS to impose a penalty on the late submission of the EMP501 reconciliation unless there is simultaneous late payment or ‘underpayment’ by the due date. The penalty referred to in paragraph 14(6) is thus not applicable in the circumstances and cannot be construed to be applicable.

116. The more appropriate penalty section would, in our view, be section 210 of the TAA which provides for a fixed amount penalty for the late or non-submission of returns.

The nature of taxpayers impacted

117. All employers

Proposal

118. An amendment to paragraph 14(6) to refer to a fixed amount penalty for the late or non-submission of returns per section 210 of the TAA, instead of a percentage-based penalty as is currently the case.

119. SARS can furthermore then amend this notice to prescribe a fair penalty for this administrative non-compliance that applies per month which matches the degree of non-compliance with the penalty, as envisaged by the legislature.

Fourth Schedule: Paragraph 17(5) – First provisional tax payment (expatriates) *(submission originally made in 2020)*

Legal Nature

120. The first provisional tax liability is based on a full year's taxable income of a taxpayer that is then halved to take into account the first six-month period of the year to which this payment relates. From this amount, the PAYE withheld during the period of six months can be deducted as well as any foreign taxes proved to be payable in terms of section 6*quat*.

121. The SARS Frequently Asked Questions on "Foreign Employment Income Exemption (Section 10(1)(o)(ii) of the Income Tax Act, 1962)" explains, in question 34, how the PAYE should be treated in these circumstances. It stipulates that:

"*The R1,25 million should be accumulated on a monthly basis in respect of all qualifying remuneration items. As soon as the R1,25 million limit is reached, the income in excess of R1,25 million becomes subject to normal tax. The R1,25 million cannot be smoothed or averaged over the year of assessment. It must be calculated by adding up all remuneration items received from the beginning of the year of assessment or applicable start date of an assignment until the R1,25 million limitation is reached*."

122. For South African expatriate employees this means that for PAYE purposes, employers are allowed to deduct the entire exemption in the first few months, resulting in no or little PAYE claimable in the first provisional tax period. However, for provisional tax purposes it appears that only one half of the capped exemption (R1.25m) can be claimed in respect of the first provisional tax period.

Factual Description

123. Thus, despite using the basic amount for their first provisional tax payment, taxpayers may only claim actual PAYE paid in the first six months. It therefore appears that an unintended artificial mismatch between the provisional tax due and PAYE available for the deduction is created as the accumulation of section 6quat rebate as set out in the FAQ 34, has not been extended to para17(5) (Fourth Schedule) provisional tax adjustment.

124. Paragraph 17(5) of the Fourth Schedule to the Income Tax Act provides that SARS may after 'taking into account any… factors having a bearing upon the probable liability of

taxpayers for normal tax, prescribe tables for optional use by provisional taxpayers falling within any category specified by the Commissioner'.

125. Unfortunately, the factors mentioned above for South African expatriates have not been taken into account for the purposes of the first provisional tax payment, resulting in an artificial first provisional tax payment that the taxpayer will only be refunded 19 months later on assessment.

126. An example[1] to illustrate the point is set out below:

127. A South African tax resident is seconded from South Africa by a local employer to a foreign country where he pays 10% tax (flat rate) deducted from the foreign payroll. Not having worked a single day in South Africa, his March to December 2020 foreign employment income totals R2 million. During January to February 2021, he works in SA earning another R400 000 − that is, his gross annual employment income equals R2,4 million. All his foreign employment income meets the physical days outside SA test − that is, the March to December 2020 days in South Africa were limited to annual leave. His annual balance of remuneration may therefore be reduced by the R1,25 million exemption in terms of section 10(1)(o)(ii), and an IRP3(q) was issued to his employer.

128. The PAYE will be calculated as follows:

PAYE HISTORY - recreated	2020/21	1st Prov	2nd Prov
Foreign employment income - including 7th Schedule Benefits	R 2 000 000	R 1 200 000	R 800 000
Local employment income - including 7th Schedule Benefits	400 000		400 000
Gross employment income - including 7th Schedule Benefits	2 400 000	1 200 000	1 200 000
Less: FEIE capped at R1.25m	(1 250 000)	(1 200 000)	(50 000)
Balance of remuneration - 4th Schedule Para 2	R 1 150 000	R -	R 1 150 000
PAYE as per PAYE Table (annual) on balance of remuneration	R 369 257	R -	R 369 257
Foreign tax credit - section 6quat - IRP3(q) directive	(75 000)	-	(75 000)
Foreign taxes paid	200 000	120 000	80 000
Foreign tax disregarded	(125 000)	(120 000)	(5 000)
PAYE as per FAQ No 34's answer applied to PAYE Table (annual)	R 294 257	R -	R 294 257

129. The provisional tax returns will be completed as follows:

[1] Source: Accountancy SA, August edition, article written by Mr H. van Zyl

FIRST PROVISIONAL TAX	2020/21	1st Prov	2nd Prov
SECOND PROVISIONAL TAX PAYMENT			
Estimated taxable income for 2021 tax year		R 1 150 000	R 1 150 000
Normal Tax on estimated taxable income		R 384 271	R 384 271
Less: primary rebates section 6		(14 958)	(14 958)
Less: Tax credit for medical scheme fee s6A		369 313	369 313
Less: Additional Medical Expenses credit s6B			
Total tax Payable (A)	(both Ptax)	369 313	369 313
Half the normal tax payable on taxable income (A/2)	(1st Ptax)	184 657	
Tax Payable for the year on taxable income (A)	(2nd Ptax)		369 313
Less: Employees' Tax Deducted during the period	this period!	-	(294 257)
Less: Foreign tax credits (s6quat and treaty rules)	allowable this period!		(75 000)
FIRST PROVISIONAL TAX (Should have been R56/2 ONLY)		R 184 657	
Less: First Provisional Tax actually paid	(2nd Ptax)		(184 657)
SECOND PROVISIONAL TAX PAYMENT (Should be R56)	R 56		(R184 601)

130. It is evident from the above, that the taxpayer has made an overpayment of R184 601 and this will only be refunded on assessment.

The nature of businesses impacted

131. All South African resident expatriates.

Proposal

132. Paragraph 17(5) should be amended to cater for this situation.

Fourth Schedule: Paragraph 30(1)(b) – Criminal offence in respect of the use of funds *(submission originally made in 2021)*

Legal Nature

133. In terms of paragraph 30(1)(b) of the Fourth Schedule a person who wilfully and without just cause uses or applies any amount deducted or withheld as employees' tax for a purpose other than paying such amount to SARS commits an offence rendering that person liable on conviction to a fine or to imprisonment for a period not exceeding 12 months.

Factual Description

134. In the *Peri Formwork Scaffolding Engineering (Pty) Ltd v CSARS* ((A67/2020) [2021] ZAWCHC 165 (23 August 2021)) case, the core of SARS's argument was that the relationship between the taxpayer and SARS is "akin to a fiduciary relationship in that the taxpayer is required to act for the benefit of SARS". It further argued that the taxpayer had failed in its fiduciary duty, which required the taxpayer to "observe the highest degree of care" in relation to the employees' tax (PAYE) deducted, insulate this amount, not mix it with other business income, and not subject this money to "risks associated with non-

payments by third parties”. Further, SARS contended that the taxpayer shouldn’t have to borrow money from third parties to pay SARS.

135. Thus, SARS argued that the money collected on behalf of SARS cannot be utilised as cash flow, and that such money should be ring-fenced from all other money.

136. The Judge, however, held that she was not in agreement that the relationship between an employer and SARS is akin to a fiduciary relationship which would elevate the obligation by an employer to pay over monies that is collected on behalf of it to SARS, to that of, for example, a principal and agent relationship.

137. Taxpayers are thus not precluded from utilising the PAYE money, mixing it with other monies or paying it into a credit or overdraft facility i.e. are not legally obliged to ring-fence the money by putting it into a separate account for instance as the legal relationship between SARS and taxpayer is one of a debtor/creditor and not a fiduciary.

138. Despite the above judgment, it is still a criminal offence to **use or apply** any amount deducted or withheld as employees' tax for a purpose other than paying such amount to SARS.

139. By law, even though there is no fiduciary relationship, it is thus still a criminal offence to use the money that has been withheld for PAYE for any other purpose. The scope of this criminal offence is, however, uncertain.

140. For example, would a taxpayer be guilty if it used one bank account to collect its trade income and pay all its debts i.e. they are mixing their funds even though the available balance remains more that the taxes due? A further uncertainty is where such money is paid into an overdraft or credit facility and then used to pay any PAYE liabilities, as legally the overdraft money does not belong to the taxpayer, it belongs to the bank and any the taxpayer would be using the money incidentally to reduce his or her interest exposure. Would this sort of payment be considered as using the PAYE money for another purpose?

The nature of taxpayers impacted

141. All employers.

Proposal

142. Further clarity on the scope of this criminal offence should be provided but in light of the Peri Scaffolding case again affirming that the relationship between SARS and taxpayers being debtor/creditor and not fiduciary, it is proposed that the criminal offence in paragraph 30 should be removed as it seems ill conceived and impractical under the current law.

Seventh Schedule: Paragraph 2(d) – Residential accommodation fringe benefit *(submission originally made in 2020)*

Legal Nature

143. Paragraph 2(d) of the Seventh Schedule to the ITA states that a taxable benefit is deemed to have been granted where the employer has provided the employee with residential accommodation either free of charge or for a rental consideration which is less than the value of such accommodation.

144. The value of the fringe benefit is the rental value of such accommodation (generally calculated using a formula as set out in paragraph 9(3)) less any rental consideration given by the employee for such accommodation in respect of such year.

145. Furthermore, paragraph 9(9) of the Seventh Schedule provides that where the employee has been provided with residential accommodation by his employer or any associated institution in relation to the employer and such employee has an interest in the accommodation in question and the accommodation has been let to the employer or to any associated institution in relation to the employer, the rental shall for the purposes of this Act (excluding this subparagraph) be deemed not to have been received by or to have accrued to the employee or any connected person in relation to the employee.

Factual Description

146. Many individuals rent their private houses to their employers who in turn provide the use of the house back to these individual employees. The employee is taxed on this fringe benefit using the formula, however, the rental payments received by the employee are not subject to income tax in the employee's hands.

147. In many instances, the fringe benefit value as calculated in terms of the Seventh Schedule, is lower than the rental amount received by the employee from his/her employer. In addition to this, the rental received by the employee is not taxable in his/her hands, creating a tax avoidance situation.

148. To illustrate this point by way of an example, let's assume that an employee owns a four-bedroom house that is then rented to the employee's employer for R20 000 per month. The use of the house is then provided back to the employee by the employer. A fringe benefit would thus arise and it should be calculated in terms of the formula included in paragraph 9(3) of the Seventh Schedule. The employee's remuneration proxy is R800 000 for the purpose of this example and it is assumed that the employer does not pay for the power or fuel.

149. In terms of the formula in paragraph 9(3), the monthly taxable fringe benefit would be R10 753,50. This is amount calculated as follows:

(R800 000 – R83 100) x 18% x 1/12 = R10 754.

150. The tax that the person would pay on this amount would be R4 839 (R10 754 x 45%).

151. From a cash flow perspective, the employee would have received a cash flow benefit of R15 161, being the rental income received of R20 000 (which is not taxable) less the tax payable on the fringe benefit of R4 839. This amounts to a yearly cash flow benefit of R181 932.

The nature of taxpayers impacted

152. All employees who lease their private houses out to their employers, who in turn provide the use of the house back to these employees, where the value calculated in terms of paragraph 9(3) is lower than the rental received by the employee.

Proposal

153. This tax avoidance gap should be addressed in paragraph 9(9) by taking into consideration the market value of the property and by ensuring that there is a correlation between the value of the fringe benefit calculated and the rental income received by the employee.

Seventh Schedule: Paragraph 2(e) – Employee wellness programmes *(submission originally made in 2022)*

Legal Nature

154. Paragraph 2(e) of the Seventh Schedule to the Income Tax Act prescribes that a taxable benefit shall be deemed to have been granted to an employee, if any service has at the expense of the employer been rendered to the employee and that service has been utilised by the employee for private or domestic purposes and no payment, or an inadequate payment, has been given by the employee for the service.

155. This benefit is valued as the cost to the employer in rendering the service or having such service rendered, less any amount paid by the employee for the service (paragraph 10(1)(b) of the Seventh Schedule).

156. Subparagraph (2) provides that no value is placed on certain types of services provided by an employer. Item (c) of subparagraph (2) provides that any service rendered to all employees, in general, for the better performance of their duties at their place of work, or a place of recreation provided by the employer, will have no value for tax purposes. Accordingly, benefits falling within this provision may be provided tax-free.

157. Many employers offer participation in “employee wellness programmes” to their employees to provide them with support and to ensure that they are better equipped to overcome challenges they may face including, for example, financial and mental health issues.

158. The service is offered to all employees in general but for practical reasons, including confidentiality as well as the nature of the service that may be required (for example, after hours trauma counselling), cannot be rendered at the employee’s place of work. Some of the services are telephonic, and others are face-to-face and often provided at the premises of the service-provider for that particular service.

159. Employee wellness programmes are operated on the basis that confidentiality will be guaranteed for the employee and accordingly, the employer is not provided with the names of employees who utilise the service. The employer is only aware of the number of employees who utilised the service in a particular month. The employer usually pays the service provider a fixed amount per month for the service, which is based on the number of individuals employed by the company, and not by the number of employees who utilise the service.

160. In view of the above, to the extent that it is determined that there should be a taxable benefit, as a result of the fact that the service is not offered at the premises of the employer, and would not be defined as "recreation" as intended by subparagraph (2) above, the employer is unable to include the value of a taxable benefit in the taxable income of employees who utilise the service and report this on their IRP5/IT3(a) Employees' Tax Certificates. It is important to note that the cost to the employer of having the service available to employees is typically as low as R20 per month, per employee.

Factual Description

161. Employee wellness programmes include the services of skilled professionals who are able to offer telephonic assistance, face-to-face and telephonic counselling services, legal and financial advice, trauma support as well as managerial support to employees. The services are generally available 24 hours a day, 365 days per year.

162. The support provided through these programmes results in healthier and happier employees, which translates into reduced absenteeism and higher levels of productivity.

163. Due to the confidential nature of the issues that employees wishing to utilise this service may want to discuss with a professional service provider, as well as the fact that after-hours support may be required by an employee, it is not feasible for the services to be provided at the employee's place of work. In addition, as the services cannot be said to be recreational in nature, the requirements of paragraph 10(2)(c) are difficult to meet, resulting in a potential taxable fringe benefit in the hands of the employees.

164. As mentioned above, this creates practical problems for the employer, as the employee wellness programme is set up in such a way as to guarantee confidentiality to the employee. The employer is therefore not provided with the names of the employees who utilised the service and is therefore unable to determine who has utilised the potentially taxable benefit and to include the value of the service in the employee's taxable income.

The nature of taxpayers impacted

165. Employees of any employer that offers an employee wellness programme.

Proposal

166. Paragraph 10(2)(c) of the Seventh Schedule should be amended to accommodate employee wellness programmes by expanding item (c) to include such services utilised by employees while they are away from their place of work but generally available to all employees.

Seventh Schedule: Paragraph 2(*l*) – Employer contributions to foreign retirement funds
(submission originally made in 2020)

Legal Nature

167. Paragraph 2(l) of the Seventh Schedule to the ITA states that any employer contribution to an approved pension fund or provident fund is treated as a taxable benefit in the hands of the employee. However, this change in legislation had no impact on contributions made to foreign funds and the previous tax treatment relating to foreign funds still applies – that is, employer contributions to foreign pension/provident funds do not result in a taxable fringe benefit. This is confirmed in SARS' Guide for foreigners working in South Africa, where it is stated that:

168. "*Employer contributions to a foreign pension fund that is similar to an approved South African fund or social security systems are not subject to tax in South Africa. Contributions by an employer to a pension fund are made by the employer as a result of an obligation that rests on the employer under rules of the fund, and therefore do not accrue to the employee*."

169. It is, however, unclear what is regarded as a foreign pension fund that is similar to an approved South African fund. SARS has not provided further clarity on this but confirmation of SARS following the practice stipulated in the Guide can be found in BPR 247, issued on 8 September 2016, where it was ruled that employer contributions to a foreign private pension fund do not constitute a taxable benefit in the hands of the employee.

170. Further to the above, National Treasury and SARS have on numerous occasions advised that they will review the tax treatment of foreign pension funds but to date no changes in legislation have been introduced. Below are the instances where it was mentioned in the National Budget Speech that the tax treatment of foreign pensions would be revisited:

170.1 **2013 Annexure C proposals**: Cross-border pensions: South African residents working abroad and foreign residents working in South Africa regularly contribute to local and foreign pension funds, which gives rise to a variety of tax issues. While certain limited rules have long been in place, these rules are largely *ad hoc*. With overall retirement reform now in effect, cross-border pension issues need to be fully reconsidered. The main issue is whether the tax focus should rely solely on the national source of the services provided or the national origin of the pension fund serving as the savings vehicle. Given the complexity of the issues involved, extensive consultation is required. Possible legislative action may occur if consensus is easily achieved (such as neutralising any unintended differences between cross-border lump sum pay-outs and annuities).

170.2 **2014 Annexure C proposals:** Cross-border retirement saving: South African residents working abroad and foreign residents working in South Africa regularly contribute to local and foreign pension funds. With overall retirement reform now in effect, cross-border pension issues need to be reconsidered. Given the complexity of the issues involved, it is proposed that the review take place over two years, with extensive consultation. On a related matter, certain provisions in the Income Tax Act refer to "pension" or to "pensions or an annuity". The wording excludes lump sum retirement fund benefit pay-outs. It is proposed that the provisions be amended to apply equally to annuities and lump sums.

170.3 **2016 Annexure C proposals:** Foreign pension contributions, annuities and pay-outs: When the residence-based taxation system was introduced in 2001, section 10(1)(gC) was added to the Income Tax Act to exempt foreign pensions derived from past employment in a foreign jurisdiction (i.e. from a source outside of South Africa). The question of how contributions to foreign pension funds and the taxation of payments from foreign funds should be dealt with raises a number of issues, which require a review. Sufficient time would be required to determine how to deal with contributions to foreign funds and the taxation of payments from foreign funds, taking into account the tax policy for South African retirement funds.

170.4 **2018 Annexure C proposals:** Tax treatment of contributions to retirement funds situated outside South Africa: The Income Tax Act currently exempts all retirement benefits from a foreign source for employment rendered outside of South Africa from taxation. The interaction of this exemption with double taxation agreements and other provisions of the Income Tax Act will be reviewed to ensure that the principle of allowing deductible contributions only in cases where benefits are taxable is upheld.

Factual Description

171. Based on the above it is evident that the tax treatment of employer contributions to foreign pension funds is unclear, and it appears that SARS is no longer applying the principles that applied prior to the introduction of the retirement reforms in 2013.

The nature of taxpayers impacted

172. Employers making contributions to foreign retirement funds.

Proposal

173. Clarity is required on what the requirements are for a foreign fund to be regarded as similar to an "approved South African fund" and to confirm the taxation treatment of employer contributions to foreign funds.

Seventh Schedule: Paragraph 5 – Acquisition of assets at less than actual value *(submission originally made in 2021)*

Legal Nature

174. Paragraph 5(2)(*b*) of the Seventh Schedule to the ITA makes provision for the granting of a long service award (which can be provided as an asset or now also in the form of a cash benefit) to an employee as a no value fringe benefit, provided that the value of such long service award does not exceed R5 000.

Factual Description

175. We are very thankful for the recent amendment that long service awards are not only limited to non-cash assets but now also apply to other reasonable awards granted for long service.

176. Despite the above positive amendment, the requirement that the value of the long service award should not exceed R5 000 still applies. This limit has not been changed since 2002 (20 years ago).

The nature of taxpayers impacted

177. All employees receiving long-service awards.

Proposal

178. The amount R5 000 should be increased to R10 000 to allow employees to be more realistically rewarded without suffering taxation, for remaining in service to their employers. This is a benefit not only to the employers but also to the economy as a whole.

179. A similar amendment as that mentioned above for long service awards, should be enacted for bravery awards as well.

Seventh Schedule: Paragraph 5 and 10 – Acquisition of assets at less than actual value and free or cheap services *(submission originally made in 2021)*

Legal Nature

180. Paragraph 5 of the Seventh Schedule stipulates that where an asset has been acquired by an employee, the value of the taxable benefit shall be the difference between the value of the asset less any consideration given by the employee.

181. Paragraph 10(1) stipulates the value that needs to be placed on any taxable benefit derived from the rendering of a service to any employee and paragraph 10(2) the services for which have no value for employees' tax purposes.

Factual Description

182. Although there are certain instances where no value is placed on the fringe benefit mentioned above, these don't cater for situations where an employer gives a small gift or 'assistance' to an employee, especially as relates to the recent unrest and resultant looting for instance.

183. Companies with staff members in the affected areas (especially KZN) provided basic necessities and other support (e.g. ambulance service for staff in distress, food parcels, security support, evacuation, temporary accommodation, clothes etc.) to their employees that were affected by the recent unrest. Of concern are the fringe benefits tax implications of this support and the administrative burden related to it.

184. Other jurisdictions also have similar provisions in their legislation, such as the UK that provides exemption for “trivial benefits”, (Tax on trivial benefits - GOV.UK (www.gov.uk):

Tax on trivial benefits

You don't have to pay tax on a benefit for your employee if all of the followi apply:

- it cost you £50 or less to provide
- it isn't cash or a cash voucher
- it isn't a reward for their work or performance
- it isn't in the terms of their contract

This is known as a 'trivial benefit'. You don't need to pay tax or National Insurance or let HM Revenue and Customs (HMRC) know.

You have to pay tax on any benefits that don't meet all these criteria.

If you're not sure whether a benefit counts as a trivial benefit call the employer helpline.

185. Similarly, Lesotho also has a provision exempting small benefits to employees (FBT Public Ruling (lra.org.ls):

What Fringe Benefits are Exempted or Excluded?

As indicated above meals and medical fringe benefits provided on an equal basis are exempt from FBT. The following are some of the benefits that, for practical and policy considerations, are not subject to fringe benefit tax.

- Private use of motor vehicle by an employee provided on special occasional hardship circumstances, for example, to take care of funeral or bereavement and emergency situations.
- Common transportation operated by or on behalf of the employer to transport employees outside the normal 8 am to 5 pm working hours, to remote places where the employer's business is conducted.
- Small common benefits that are difficult to quantify and place value received by each individual employee, for example, use of an employer's recreational and sporting facilities. Staff parties and functions are typical examples.
- Accommodation provided on a remote employer camp site.
- Uniform and similar employer branded attire or clothing.
- Passage granted to an employee at the commencement or termination of employment if such passage is the actual expenditure incurred for transportation by the employer or represents a reimbursement of actual expenditure. A cash allowance in lieu of passage is taxable.

The nature of taxpayers impacted

186. Employers providing assistance or small gifts to employees.

Proposal

187. A *de minimus* threshold of R1 000 should be inserted into paragraph 5 and 10 to provide relief from the fringe benefit arising from the provision of services or goods to employees, especially in emergency situations such as the recent unrest in KZN and Gauteng.

Seventh Schedule: Paragraph 7 – Right of use of motor vehicle *(submission originally made in 2021)*

Legal Nature

188. Where an employer provides an employee with the right of use of a motor vehicle, a taxable fringe benefit arises in the hands of the employee and is included in gross income in terms of paragraph (i) of the gross income definition in the ITA).

189. The taxable benefit is quantified in terms of paragraph 2(b) and 7 of the Seventh Schedule to the ITA.

190. Paragraph 7 of the Seventh Schedule stipulates that where an asset has been acquired by an employee, the value of the taxable benefit shall be the difference between the value of the asset less any consideration given by the employee.

Factual Description

191. As a cost saving measure it is fairly common practice for an employer to provide the use of a company motor vehicle to a group of expatriate employees working temporarily in South Africa, rather than providing a different motor vehicle to each employee.

192. In terms of paragraph 2(b) of the Seventh Schedule to the ITA, a taxable benefit will be deemed to have been granted to an employee where the employer has provided the employee with the right of use of any motor vehicle for private or domestic purposes, either free of charge or for a consideration which is less than the value of such use.

193. Paragraph 7(2) of the Seventh Schedule to the ITA provides that the cash equivalent of the value of the taxable benefit, is the value of the private use of the vehicle, less any consideration given by the employee for the use thereof.

194. The legislation does not currently provide for the apportionment of the taxable benefit arising from the private use of the vehicle in the hands of each employee who has the use of the vehicle.

195. Consequently, the full value of the taxable benefit is taxed in the hands of each employee. Tax is therefore collected by SARS from each employee on the private use of the same vehicle, regardless of the fact that the access that each employee has to the vehicle for private use is limited to its availability of the vehicle at the time.

196. The taxable benefit for each month that the motor vehicle is used by the employee (other than a vehicle acquired in terms of an operating lease) is calculated by multiplying the determined value of the motor vehicle, as determined by the Minister by Regulation by a percentage (3.5% or 3.25%) depending upon whether or not the vehicle was acquired with a maintenance plan.

197. The legislation appears to assume that the use of a motor vehicle will be allocated by an employer to a single employee, rather than to a group of employees to use collectively. Consequently, the legislation does not provide for the apportionment of the taxable benefit where the use of a company motor vehicle is provided to a group of employees and to ensure that the full value of the vehicle is only taxed in full as a taxable benefit once in total.

The nature of taxpayers impacted

198. Employees receiving the collective right to use a company vehicle including employees of multinationals seconded to render services in South Africa temporarily.

Proposal

199. A paragraph, similar to paragraph 9(5) should be included under paragraph 7 allowing the Commissioner to make an equitable determination in this regard.

Seventh Schedule: Paragraph 9(3) – Remuneration proxy *(submission originally made in 2021)*

Legal Nature

200. Employees who receive residential accommodation from their employer are taxed on this benefit as a fringe benefit. The cash equivalent of the fringe benefit is referred to as the "rental value" and is determined in accordance with paragraph 9 of the Seventh Schedule to the Income Tax Act less any consideration given by the employee for the benefit.

201. Where the employer secures the residential accommodation through an arms' length lease agreement, the "rental value" for the employee is the lower of the cost to the employer in providing the accommodation and the value as determined in accordance with a formula set out in paragraph 9(3) of the Seventh Schedule ("the formula value"). In circumstances where the employer (or an associated institution to the employer) owns the accommodation, it is mandatory to use the formula value as the "rental value", unless a tax directive is applied for in terms of paragraph 9(5) of the Seventh Schedule.

202. The formula value is a function of "remuneration proxy" which is defined in section 1 of the Act as follows:

 …*in relation to a year of assessment, means <u>the remuneration</u>, as defined in paragraph 1 of the Fourth Schedule, derived by an employee from an employer during the year of assessment immediately preceding that year of assessment, other than the cash equivalent of the value of a taxable benefit derived from the occupation of residential accommodation as contemplated in subparagraph (3) of paragraph 9 of the Seventh Schedule in the application of that subparagraph*…

Factual Description

203. With effect from 1 March 2016, paragraph 2(l) of the Seventh Schedule was introduced which included employer contributions to retirement funds as a taxable fringe benefit, therefore increasing employees' overall "remuneration" by the value of these contributions. The ultimate tax effect of this change was largely described as tax neutral because employees would be allowed an equal amount as a tax deduction. It was only if the employee's actual and deemed retirement fund contributions exceeded R350,000 per year or 27.5% of remuneration (or taxable income) that there would be an impact on net take home pay, as the allowable tax deduction for retirement fund contributions would be limited in these circumstances. This limitation was justified by the Treasury because it only impacted the higher earners and that it was in line with one of the aims of the retirement fund reform to prevent wealthy individuals from claiming excessive tax deductions and therefore promoting equity amongst taxpayers.

204. However, as "remuneration proxy" is defined with reference to "remuneration" and not the balance of remuneration (i.e., the amount remaining after allowable tax deductions), employees whose accommodation fringe benefits were determined with reference to the formula in paragraph 9(3) of the Seventh Schedule arbitrarily had their accommodation fringe benefit value increased without there being any relevant change in their

circumstances. This could not have been the intention of the Legislature as the accommodation fringe benefit was completely unrelated to the retirement fund tax reform. In fact, this would have been contrary to the intention of promoting equity amongst taxpayers.

205. Although we note the remedy provided by the paragraph 9(5) (obtaining a tax directive if the rental value is lower than the formula value) is available, this is an administratively burdensome process as a new tax directive per year, per employee is required. These directive applications must also be supported by two independent valuations which are extremely costly for an employer with large numbers of employees residing in employer owned accommodation.

The nature of taxpayers impacted

206. Employees who are provided with employer provided accommodation (e.g. in the agriculture, hospitality, education, mining etc sectors as well as at various state-owned entities).

Proposal

207. The remuneration proxy in the formula value in paragraph 9(3) should exclude the employer contributions to retirement funds that are taxed as a fringe benefit.

Seventh Schedule – Relocation Costs (NEW)

Legal Nature

208. Paragraph 2 of the Seventh Schedule read with paragraph (I) of the definition of “gross income” in section 1 of the Act stipulate the various instances in which a taxable benefit shall be deemed to have been granted by an employer to his employee in respect of the employee’s employment with said employer.

209. Paragraph 3(1) then stipulates that the cash equivalent of the value that needs to be placed on any taxable benefit shall be determined by the employer, in accordance with the provisions of the Seventh Schedule.

210. Paragraph 3(2) provides that the Commissioner may, if the amount determined seems to him/her to be incorrect, re-determine the cash equivalent and issue the employer with a notice of the assessment in terms of section 96 of the TAA for the unpaid amount of employees’ tax that is required to be deducted or withheld from such cash equivalent.

211. Section 10(1)(*n*B) exempts, from a taxpayer’s income, *any benefit or advantage accruing to any employee by virtue of an employer bearing certain expenses relating to the employee’s (a) taking up employment, (b) transferring from one place of employment to another or (c) termination of employment*.

212. The exempt expenses include:

- The transportation of the employee, members of his/her household and their personal goods and possessions from his/her previous place of residence to his/her new place of residence;

- Costs incurred by the employee in respect of sale of his/her previous residence and in settling-in permanent residential accommodation at his/her new place of residence;

- The cost of renting temporary residential accommodation for the employee and members of his/her household during a period which ends 183 days after his/her transfer took place or after his/her date of appointment.

213. The Guide for Employers in respect of Employees Tax (2024) ("the Guide") further outlines items exempt from tax if reimbursed by the employer for actual expenditure incurred by the employee:

- Bond registration and legal fees paid in respect of a new residence that has been purchased;
- Transfer duty paid in respect of the new residence;
- Cancellation fees paid for bond cancellation on previous residence;
- An agent's commission paid on the sale of the previous residence;
- New school uniforms;
- Replacement of curtains;
- Motor vehicle registration fees;
- Telephone, water and electricity connection.

Factual Description

214. As outlined in the legislation, should an expense be reimbursed and the reimbursement falls within any of the categories of expenses listed in section 10(1)(*n*B), the reimbursement will be exempt from the employee's tax.

215. Neither the legislation nor the Guide define the documentation that will be deemed as sufficient proof of expenditure provided by the employee to the employer upon reimbursement of relocation expenditure incurred.

216. Upon relocation, employees also incur the following settling-in costs based on their relocation. These are however not specifically listed in the Guide:

- broadband internet connection for the new residence;

- appliances and other household items (e.g. curtains) that need to be purchased by a single person who previously lived with parents;

- fees incurred for the early termination of a lease, as well as the deposit needed for the new apartment they are relocating to;

- expenses for items needed in the new apartment, which were not needed in the previous residence, e.g. carpets for the tiled floor of the new apartment where the previous residence had wall-to-wall carpeting;

- board and lodging for pets until the owner is settled in the new residence,
- restocking the new residence with cleaning products and damage to items in the process of relocating.

217. The application of the expense categories outlined in section 10(1)(*n*B) to the actual expenses listed in the Guide leads to ambiguity.

218. Furthermore, the list of expenses noted in the Guide is often interpreted by SARS officials as being a complete and final list of expenses for which a reimbursement is allowable for purposes of the section 10(1)(*n*B) exemption. Expenses not listed in the Guide are thus not considered for reimbursement purposes by SARS officials, despite there not being an exhaustive list of expenses. Furthermore there is also no legislative provision stipulating the format or type of documentation that should be accepted by employers from employees upon reimbursement of relocation expenses.

219. As a result, the employer is issued an assessment for under-declaration of employees' tax (PAYE).

220. The additional assessments issued by SARS, which include penalties and interest, create more costs to the employer over and above the establishment of business premises in a new location.

221. This creates an unnecessary burden for employers and disincentivises employers to reimburse relocation costs; thus adversely affecting the impacted employees.

The nature of taxpayers impacted

222. Employees relocating for employment purposes, who are also reimbursed by their employers for relocation costs incurred.

Proposal

223. To avoid ambiguity, the first two categories of section 10(1)(*n*B) should be redefined with clear requirements as to acceptable proof of expenditure[2] for SARS that should be provided by the employee to an employer for purposes of the reimbursement of relocation costs.

224. The Guide for Employers should then be aligned to the 'current realities' of relocation costs and properly note that the SARS list in the guide is not exhaustive.

225. We submit that consideration may need to be given to potentially re-introduce a cash relocation allowance, (subject to a limit/cap), for which proof of expenditure is not required (deemed expended). Although this was removed as an administrative arrangement due to abuse concerns, it will ease employers' administrative burden for purposes of SARS' Vision 2024, which will require the reporting of data in real-time. This

[2] Taking into account that the way goods are purchased has now changed due to business practices and technological advancement.

reporting will be less complicated as there will not be any delayed submissions by employees of the necessary proof of expenses for reimbursement purposes.

226. Should employers decide to rather reimburse the employee expenses an amount exceeding the aforementioned cash relocation allowance limit, those employers can then use a reimbursement process in relation to relocation costs.

Employment Tax Incentive Act – Section 6 *(submission originally made in 2021)*

Legal Nature

227. Section 6 of the ETI Act contains the following proviso inserted in terms of section 59 of the Taxation Laws Amendment Bill (TLAB), 2021:

> "*Provided that the employee is not, in fulfilling the conditions of their employment contract during any month, mainly involved in the activity of studying, unless the employer and employee have entered into a learning programme as defined in section 1 of the Skills Development Act, 1998 (Act No. 97 of 1998), and,* ***in determining the time spent studying in proportion to the total time for which the employee is employed, the time must be based on actual hours spent studying and employed*****.**" [our emphasis]

Factual Description

228. The wording in bold may give the impression that if the employer and employee have entered into such a learning programme, even if in fulfilling the conditions of the employment contract during any month, as long as they are not mainly involved in the activity of studying, this proviso would not apply.

229. However, we are not certain that this is the intention of National Treasury or that addresses the potential tax avoidance schemes that resulted in these amendments. We note below the comments made by the public in relation to the proposed changes to the ETI Act contained in the first batch of the TLAB as well as National Treasury's response in relation to this:

Comment: The proposed amendments to section 6 of the ETI Act result in what are actually legitimate ETI claims no longer qualifying for the incentive. As a result, instances where the employer provides on the job training, where the employer and employee have entered into a learnership or apprenticeship programme, or where the employee is on a secondment may no longer qualify for the incentive. Consideration should rather be given to clarifying that the employee should be given a cash payment in lieu of services rendered.

Response: Accepted. The incentive is intended to apply to all legitimate arrangements where the employee is not only engaged in the activity of studying, but rather gaining valuable work experience. In the event that some of the employee's duties involve some sort of training or studying, the costs of said training or studying should ideally be borne by the employer. To ensure that the employee's remuneration package is not solely allocated to costs associated with any required training or studying, qualification for the incentive shall further be based on the employee receiving a cash payment in lieu of services rendered. Changes will be made in the 2021 Draft TLAB to reflect this intention.

230. In our view, based on the above comment and response, it seems that where the employee is registered for a learning programme as defined in section 1 of the Skills Development Act, 1998 (Act No. 97 of 1998), any costs incurred for such programme must be borne by the employer and should not in any way impact the cash wage that the employee is entitled to in terms of the employment contract and in line with the Basic Conditions of Employment Act.

231. This is to prevent schemes whereby the employees do not/will not receive payment from the employer, since the employer must pay such remuneration to, for example, a consulting firm or training college under the relevant agreement, on a monthly basis. In some instances, the agreement will provide that the employees ‘cede’ or “forfeit” their remuneration to the consulting firm or training college.

232. In such circumstances, it is envisaged that the employees will have a right or entitlement to remuneration from the employer and then cede such right or entitlement. So, whilst the requirement that remuneration is ‘paid or payable’ will be met, there needs to be consideration of whether or not the requirement of the minimum wage being paid to the employee, in terms of section 4, has been met. If not, the employer will not be entitled to claim the ETI.

The nature of taxpayers impacted

233. All employers wanting to claim the ETI.

Proposal

234. The wording in bold requires clarification to correctly reflect the principle to be applied. Specifically, the waiver or cession of the wage or salary in favour of the fees **after accrual** for the learning programme should result in a disqualification of the arrangement for receiving the ETI.

235. Furthermore, the term “wage” as defined in section 1 of the ETI Act should be clarified to provide that this must be a cash payment received from the employer by the employee (although this can be inferred from the definition in the BCEA, it’s not clear as the BCEA also has separate references to remuneration).

CATEGORY – DOMESTIC BUSINESS TAXES

Sections 7C and 56 – Loans to a trust by a connected person and donations tax *(submission originally made in 2020)*

Legal Nature

236. Section 7C generally applies where a natural person makes an interest-free loan to a trust. The non-charging of interest is regarded as a donation subject to donations tax at the rate of 20%. The donation is regarded as having been made to the trust by the natural person on the last day of the year of assessment of the trust and donations tax is payable by the end of the month following the month during which the donation takes effect.

Factual Description

237. The financial accounts of most trusts are only prepared a while after the year end and thus the actual levels of the loan and corresponding interest can only be determined then. The reason for this is that it is often uneconomical for the trust to have a full-time accounting function, as the limited transactions will not financially justify such an expense.

The nature of businesses impacted

238. All natural persons or companies who are subject to section 7C.

Proposal

239. A grace period of a minimum of 3 months, preferably 7 months, should be granted in respect of payment of the donations tax. 7 months would align with the top-up payment of provisional tax. This will assist in ensuring more accurate calculations of the donations tax payable.

Section 7C and section 31 – Clarity on interaction *(submission originally made in 2020)*

Legal Nature

240. Section 7C(5)(e) states that the sections 7C(2) and (3) will not apply to a loan "where that loan advance or credit constitutes an affected transaction as defined in section 31(1) that is subject to the provisions of that section."

241. For the exemption to apply the loan must be subject to section 31 i.e. be a cross border connected party transaction which is not at arm's length i.e. an 'affected transaction' and be subject to the provisions of section 31. That is, an adjustment needs to be made. The law is not clear on what this means if the arm's length interest rate is less than the official rate.

Factual Description

242. Where a person has made, for example, a non-interest-bearing loan to a connected offshore trust and a tax benefit is derived, section 31 will require that an amount be included in the South African resident's taxable income to the extent of the arm's length

interest is not charged. It will also require a ‘secondary adjustment’ to be made which, where the lender is an individual, amounts to the deeming of the amount of the section 31 interest included in the taxable income to be a donation for donations tax purposes.

243. If the arm’s length interest rate is say 4% and this amount is included in the South African taxpayer’s income, it could be argued that the loan has been “subject to the provisions of section 31” even though the official rate is 4.5%, with the result that section 7C would not apply to the loan at all. On the other hand, had actual interest of 4% (the arm’s length rate) been charged, section 7C(5)(e) would have applied and the taxpayer would need to pay donations tax on the interest represented by the additional 0.5% in terms of section 7C. Such difference in treatment can clearly not be the intention.

<u>The nature of businesses impacted</u>

244. All persons who have made a loan to an offshore trust and are potentially subject to section 7C.

<u>Proposal</u>

245. Section 7C(5)(e) should be amended to rather state (additional words in bold italics) “‘where that loan advance or credit constitutes an affected transaction as defined in s31(1) ***to the extent*** that is subject to the provisions of that section.”

Section 8EA – Dividends on third-party backed shares deemed to be income (NEW)

<u>Legal Nature</u>

246. The recent revised 2023 Draft Taxation Laws Amendment Bill proposal seeks to exclude dividends from certain equity shares from the application of section 8EA by introducing an ownership requirement in the ultimate target operating company when a holder receives a local or foreign dividend in respect of an equity share as defined.

247. We refer to an extract of the proposed amendment to section 8EA below:

> *“Provided that where an equity share in an operating company is acquired by any person as contemplated in paragraph (a) or (b) of the definition of “qualifying purpose” and the share so acquired is no longer held directly or indirectly by that person at the time of the receipt or accrual of that dividend or foreign dividend in respect of the preference share, this subsection **<u>must not apply</u>**, unless—*
>
> *(a) that equity share in the operating company was disposed of and the funds derived from that disposal are used by the issuer of the preference share for the redemption of that preference share within 90 days of that disposal; or*
>
> *(b) that equity share in the operating company was a listed share and substituted for a listed share in terms of an arrangement that is announced and released as a corporate action …”*

Factual Description

248. The inclusion of the above proviso in welcomed as it caters specific for commercially driven transactions which do not intend to undermine the fiscus.

249. It does however not cater for disposals where the proceeds from a disposal is used for the full or partial settlement by any person of any dividend or foreign dividend in respect of a preference share which was issued for a qualifying purpose, as is currently catered for in terms paragraph(d) of the definition of "qualifying purpose".

The nature of taxpayers impacted

250. Taxpayers who are subject to s8EA and need to dispose of the relevant equity shares in order to obtain proceeds required for the full or partial settlement of dividends in respect of a preference share which was issued for a qualifying purpose

Proposal

251. We recommend that the exclusion to the ownership requirement be extended to include commercial transactions where there has been a disposal or part disposal of underlying operating company's equity shares to meet dividend payments of the preference shares which shares were issued for a qualifying purpose.

Section 8EA – Dividends on third-party backed shares deemed to be income *(submission originally made in 2022)*

Legal Nature

252. Section 8EA deems any dividend or foreign dividend received by or accrued to a person during any year of assessment in respect of a share to be an amount of income received by or accrued to that person if that share constitutes a third-party backed share at any time during that year of assessment.

253. A third-party backed share means any preference share in respect of which an enforcement right is exercisable by the holder of that preference share or an enforcement obligation is enforceable as a result of any amount of any specified dividend, foreign dividend, return of capital or foreign return of capital attributable to that share not being received by, or accruing to the person entitled thereto.

254. An "enforcement right" is any right, whether fixed or contingent, of the holder of that share or of any person that is a connected person in relation to that holder to require any person other than the issuer of that share to: acquire that share from the holder of the share, or make any payment in respect of that share in terms of a guarantee, indemnity or similar arrangement or procure, facilitate or assist with any acquisition contemplated in paragraph (a) of this definition in section 8EA or the making of any payment contemplated in paragraph (b) of this definition in section 8EA; and the enforcement right is exercisable or enforcement obligation is enforceable as a result of any amount of any specified dividend, foreign dividend, return of capital or foreign return of capital attributable to that share not being received by or accruing to the person holding that share.

Factual Description

255. An "enforcement right" is defined such that it gives the right contemplated therein to the holder of a share or to any connected person in relation to the holder. So, for example, a company might hold the shares but its holding company might hold the enforcement right.

256. The definition of "third-party backed share", however, refers to the relevant share "in respect of which an enforcement right is exercisable by the holder" - it does not refer to the situation where the right is exercisable by a connected person. There is clearly a disconnect here.

The nature of taxpayers impacted

257. Persons holding a "third-party backed share" where the enforcement right is exercisable by a connected person.

Proposal

258. The definition of "third-party backed share" should include the situation where the enforcement right is exercisable by a connected person.

Section 8F – Interest on hybrid debt instruments deemed to be dividend *in specie* (NEW)

Legal Nature

259. Section 8F the Income Tax Act deems interest in respect of a hybrid debt instrument or hybrid interest to be treated in a similar manner to the yields of an equity instrument. These rules disallow the deduction of interest paid and deem this interest to be an *in specie* dividend for the issuer of the instrument and an *in specie* dividend for the recipient.

260. Section 8F(3)(f) stipulates that an exclusion is triggered to the deeming rule when a registered auditor has certified the payment by a company of an amount owed in respect of that instrument that had been or was to be deferred by reason of the market value of assets being less than the amount of the liabilities.

Factual Description

261. In a prior submission, we requested that National Treasury engage with IRBA on the proposed wording of the exclusion so that it aligns with the auditing standards framework and also as to what a registered auditor can do in such capacity as opposed to what is expected from management to do and verify which remains exclusive to them.

262. Our basis for this was as follows:

263. The work to be performed by an auditor in section 8F(3)(f) does not in our view currently fall within the Auditing Standards and Procedures. Though registered auditors commonly use Agreed Upon Procedures (AUP), these do not technically accommodate the legislative requirement. The reasons for this are discussed next.

264. The purpose of an audit is to enhance the degree of confidence of intended users in the financial statements. This is achieved by the expression of an opinion by the auditor on whether the financial statements are prepared, in all material respects, in accordance with an applicable financial reporting framework. In the case of most general purpose frameworks, that opinion is on whether the financial statements are presented fairly, in all material respects, or give a true and fair view in accordance with the framework. An audit conducted in accordance with ISAs and relevant ethical requirements enables the auditor to form that opinion. (Ref: Para. A1) (ISA 200. 3.)

265. The financial statements subject to audit are those of the entity, prepared by management of the entity with oversight from those charged with governance. ISAs do not impose responsibilities on management or those charged with governance and do not override laws and regulations that govern their responsibilities. However, an audit in accordance with ISAs is conducted on the premise that management and, where appropriate, those charged with governance have acknowledged certain responsibilities that are fundamental to the conduct of the audit. **The audit of the financial statements does not relieve management or those charged with governance of their responsibilities.** (Ref: Para. A2–A11) (ISA 200.4.)

266. We also further refer to paragraph R950.6 of the IRBA Code of Professional Conduct which states that following:

> "***A firm shall not assume a management responsibility related to the subject matter or subject matter information of an assurance engagement provided by the firm***. *If the firm assumes a management responsibility as part of any other service provided to the assurance client, the firm shall ensure that the responsibility is not related to the subject matter or subject matter information of the assurance engagement provided by the firm*."

267. Based on the information above, it is clear that obtaining a subordination agreement would be the responsibility of management and not at the instance of the auditor.

268. In accordance with the terms of engagement, the auditor has a responsibility to express an audit opinion on the clients' financial statements. This responsibility does not extend to any other third parties unless agreed otherwise or required by law/regulation.

269. With this in mind, from an auditing point of view, management would generally only enter into a subordination agreement in the event of factual insolvency; an action that needs to be taken to, among other things, satisfy the auditor in his/her assessment of going concern (a requirement contained in ISA 570, Going Concern). Furthermore, these subordination agreements are generally entered into between related parties, for example loans from group companies or loans from shareholders.

270. IRBA has thus indicated that the process was outside of the auditing standard processes (certification was well beyond an agreed upon procedure) and had requested that the legislation be worded within the existing auditing standards framework.

271. We also note that the “carve-out” in terms of section 8F(3)(f) is not only applicable to entities that are subject to an audit hence the carve-out should apply to ALL taxpayers in the event that a subordination agreement is entered into for the purposes of satisfying the going concern requirement as mentioned above.

The nature of taxpayers impacted

272. Taxpayers entering into subordination agreements.

Proposal

273. Unfortunately, there has been no progress in this regard with regards to our submission.

274. Given the challenges of using a Registered Auditor to perform this function and at the same time providing SARS with sufficient comfort by an independent person, we make the below proposal.

275. Our proposal inserts an “Independent Registered Tax Practitioner” (as envisaged in section 223(3)(b) TAA) as the functionary to affirm the proposed objective criteria and who SARS are able to exercise regulatory control over.

276. The legislation be reworded as follows:

276.1 Insertion of a definition under section 8F(1) for “subordination agreement” as follows:

276.1.1 **‘subordination agreement’** means an agreement that is entered into in relation to an instrument which agreement defers the obligation to pay an amount so owed by a company on a date or dates falling within that year of assessment by reason of, inter alia but including, that obligation being conditional upon the market value of the assets of that company not being less than the amount of the liabilities of that company.

276.2 The proposed reword of the carve out for section 8F(3)(f) is as follows:

276.2.1 **(f)** that constitutes a hybrid debt instrument –

(i) solely in terms of paragraph (b) of the definition of hybrid debt instrument;

(ii) is subject to or will be subject to a subordination agreement; and

(iii) the taxpayer was in possession of a confirmation issued by an independent registered tax practitioner as envisaged in section 223(3)(b) of the Tax Administration Act 2011, that –

(aa) was issued by no later than the date the annual financial statements in respect of that year of assessment were signed;

(bb) confirms the existence of the subordination agreement in relation to that year of assessment; and

(cc) confirms that the subordination agreement came into existence subsequent to the end of that year of assessment or the end of any prior year of assessment.

Section 9D – Controlled foreign companies (NEW)

Factual Description

277. As part of our submission to National Treasury concerning the proposed amendment to the meaning of "foreign business establishment" per the 2023 draft Taxation Laws Amendment Bill, SAICA and other stakeholders called for the withdrawal of the amendment pending the Constitutional Court's judgment in the case between the CSARS and Coronation Investment Management SA (Pty) Ltd.

278. This was duly accepted by National treasury (NT) and the proposed amendment has been withdrawn.

279. We also suggested in our submission that NT should review South Africa's CFC legislation against similar regimes in other jurisdictions in order to align our legislation to international best practice, including considering the recommendations of the OECD's BEPS Action Plan 3, the impact of the pending OECD Pillar 2 Global Minimum tax, and the extent that the current legislation is administratively burdensome for most taxpayers.

The nature of taxpayers impacted

280. South African taxpayers subject to section 9D of the Act.

Proposal

281. Notwithstanding the withdrawal of the proposed amendment to section 9D, we assert that a review of South Africa's CFC legislation by NT is still warranted and request same.

Section 10 – Home-owners association exemption *(submission originally made in 2022)*

Legal Nature

Section 10(1)(e)(i) exempts any *levy received by or accrued to an association of persons from its members, where the Commissioner is satisfied that such association of persons has been formed solely for purposes of managing the collective interests common to all its members, which includes expenditure applicable to the common immovable property of such members and the collection of levies for which such members are liable.*

Factual Description

282. Many associations which are not Share Blocks or Body Corporates are still not aware of the fact that the exemption in s10(1)(e) only becomes available on approval/registration with SARS. When this is picked up, there is no legislative option for retrospective registration.

283. SARS is insisting that these entities submit "normal" income tax returns to get up-to-date and will not consider registration requests before this is done. This leaves many entities open to a large tax liability, particularly where the entity still has to build up reserves to comply with the new Ombud's requirements.

284. This is extremely punitive for what is merely administrative non-compliance due to a change in law and it was not the intention to be a revenue collection mechanism as there is no leakage, rather just regulation.

The nature of taxpayers impacted

285. Home-owners associations.

Proposal

286. We therefore propose that the ability to backdate registrations be provided for in the legislation. Additionally, a more "user friendly" approach by SARS should be adopted by SARS for associations attempting to correct their tax affairs, particularly where the potential taxable income is significant.

287. A similar concession is made in section 30(3B) ITA for PBO's due to similar concerns regarding lack of awareness and impracticalities of penalising taxpayers for regulatory administrative non-compliance rather than tax evasion or avoidance.

288. A similar concession was also previously provided a certain class of taxpayer facing comparably unique circumstances, i.e. Bargaining Councils[3].

289. This reason for the this tax relief, articulated in the Explanatory Memorandum on the 2017 Taxation Laws Amendment Bill, was that since the Bargaining Councils *would be at risk of closure or would suffer severe financial distress if high penalties and interest are imposed for non-compliance, and given the unique circumstances of this case, specific set of provisions is required to address the situation*.

290. Since home-owners associations face similar financial risks, we believe they should be given an opportunity to backdate their "exemption" registration with SARS to ensure their compliance.

Section 10(1)(cA)(i) – Exemptions for Institutions, Boards or Bodies *(submission originally made in 2021)*

Legal Nature

291. Section 10(1)(cA)(i) and (ii) respectively provide an absolute exemption from income tax of the receipts and accruals of any –

- institution, board or body established by or under any law engaged in specified prescribed activities; and

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[3] "Bargaining Council tax relief" in Part II of the 2017 Taxation Laws Amendment Act.

- association, corporation or company all the shares of which are held by any such institution, board or body.

292. The exemption under section 10(1)(cA)(i) will, however, apply only to the extent that such institution, board or body –

- has been approved by the Commissioner subject to any conditions deemed necessary to ensure that the activities of that institution, board or body are wholly or mainly directed to the furtherance of its sole or principal object; and
- complies by law or under its constitution with the prescribed requirements.

Factual Description

293. Section 10(1)(cA)(i) states that Commissioner may withdraw the exemption of any institution, board or body if satisfied that such institution, board or body has during any year of assessment failed to comply with section 10(1)(*c*A)(i). The exemption will be withdrawn with effect from the commencement of the year of assessment in which non-compliance or failure by an institution, board or body occurred.

294. Section 10(1)(cA)(i) does, however, not require SARS to provide the institute, board or body with adequate reasons relating to its withdrawal, before the exemption is withdrawn.

The nature of taxpayers impacted

295. All institutes, boards or bodies that are tax exempt in terms of section 10(1)(cA)(i).

Proposal

296. Given that the spirit of the law in regards to tax exempt entities is to provide such entities an opportunity to correct, given their public interest mandate, rather than just withdraw the exemption status (e.g. section 30(5), 30A(5), 30B(5) & 30C(2) of the ITA), it is recommended that this be incorporated into this section as well, aligning the law and policy.

297. This will ensure that the relevant taxpayer receives a notice explaining what it has done wrong, what the Commissioner expects them to do to correct and by when. Following it not complying with such a request it would then be administratively fair to withdraw its exemption.

Section 10(1)(e) – Exemptions for Body Corporates *(submission originally made in 2021)*

Legal Nature

298. Section 10(1)(e)(i) exempts *any levy* received by or accrued to a body corporate established in terms of the Sectional Titles Act, No. 95 of 1986 from its members.

299. Section 10(1)(e)(ii) exempts any receipts or accruals, *other than levies*, derived by a body corporate to the extent that the aggregate of those receipts and accruals do not exceed R50 000.

300. The Sectional Titles Schemes Management Act No. 8 of 2011 requires the body corporate to maintain a 10-year plan for maintenance, repair and replacement of capital items. This must be supported with a reserve fund sufficient to cover the cost of future maintenance and repair of common property.

301. The minimum level for this reserve fund has been set at 25% of the previous financial year's "administrative fund" (the fund for operating costs) levies.

Factual Description

302. In light of the requirement to keep a large reserve fund, body corporates will now earn additional interest income that will no longer be exempt in terms of section 10(1)(e)(ii).

The nature of taxpayers impacted

303. All institutes, boards or bodies that are tax exempt in terms of section 10(1)(e).

Proposal

304. In order to mitigate the additional interest income that the body corporates are likely to earn from the above statutory requirement, we suggest that the s10(1)(e) exemption limit of R50,000 should be based on the amount of the available reserves at the end of the year multiplied by the repo rate.

Section 11(e) – Wear and tear allowance *(submission originally made in 2021)*

Legal nature of problem

305. Section 11(e) provides for the wear and tear allowances on assets and SARS' Interpretation Note 47 and Binding General Ruling 7 (BGR 7) contain the considerations and write-off periods for determining the useful life of a qualifying asset and therefore the annual value of the allowance available to a taxpayer.

306. An amendment was made to section 11(e) in 2018 that provided that the amount of the wear and tear allowance must be determined on the basis of the periods of use listed for this purpose in a public notice issued by the Commissioner, or a shorter period of use approved by the Commissioner on application in the prescribed form and manner by the taxpayer.

307. This amendment comes into effect from a date determined by the Minister of Finance in the Gazette. This date has not yet been determined.

Factual description

308. The proposed amendments to section 11(e) have removed the Commissioner's discretion to determine the just and reasonable amount by which qualifying assets have depreciated in a given year and therefore the amount of the allowance. This amount is now to be determined on the basis of the periods of use listed for this purpose in a public notice issued by the Commissioner, or a shorter period of use approved by the Commissioner on application in the prescribed form and manner by the taxpayer.

309. Although Interpretation Note 47 was updated in February 2021 to include an Annexure with the write-off periods that are acceptable to SARS and the formalised process for applying to the Commissioner for a shortened write-off period, the Minister of Finance has not made the law effective to implement the proposed solution set out in the amendment to section 11(e) – that is, no public notice has as yet been issued or published in the Gazette.

310. Interpretation Note 47 refers to "small" items (cost of less than R7 000) that may be written off in full in the year of assessment in which they are acquired and brought into use. This amount has applied since 2009 and has not been increased since.

The nature of taxpayers impacted

311. All taxpayers that own qualifying capital assets.

Proposal

312. Other than requiring the Minister of Finance to issue the Gazette to make the proposed amendment to section 11(e) effective, we request that the amount considered to be a "small" item for the purposes of section 11(e) as mentioned in Interpretation Note 47 should be increased to R25 000 considering inflation and the unprecedented increase in the purchase price of goods over the years.

Section 12H – Learnership Allowances

Legal Nature

313. The sunset clause for section 12H is 31 March 2024.

Factual Description

314. No extension was noted in this year's draft tax bills, even though no announcement was made in the Budget Review that this incentive would be discontinued.

315. NT has previously noted that it was reviewing all incentives including the learnership allowance (particularly as relates NQF 6 and above) and would reconsider various incentives after public engagement with its finding. Accordingly it was expected that NT would do public engagements before any allowances were discontinued.

The nature of taxpayers impacted

316. Taxpayers providing registered learnerships to employees.

Proposal

317. We submit that it should be extended for 12-24 months to enable NT sufficient time to finish its review of the effectiveness of the allowance and to publicly engage stakeholders impacted.

318. SAICA has conducted independent research on the impact of the section 12H allowance and we would welcome an engagement with NT to discuss possible changes to the incentive that would make it more effective in achieving its intended policy outcome.

Section 12S, 12N – SEZ and other building allowances *(submission originally made in 2022)*

Legal Nature

319. The objective of the SEZ regime is to "(i) promote industrial agglomeration, (ii) build the required industrial infrastructure, (iii) promote coordinated planning among key government agencies and the private sector, and (iv) guide the deployment of other necessary development tools" (Department: Trade and Industry, 2018).

320. Thus, the object of an SEZ is to promote industrial development both inside and outside the SEZ. The Act grants a number of incentive allowances for operators within an SEZ. Specific to SEZs are section 12R of the Act which defines an SEZ and a qualifying company that may be granted special allowances. Section 12S of the Act grants a 10% per annum allowance to a qualifying company in respect of new and unused buildings and improvements owned by that company.

321. To ensure, *inter alia*, that the letting of land from the government remains attractive from a tax perspective, section 12N was introduced in the Act in 2010. This section finds application where a lessee undertakes improvements on leased property in terms of a Public Private Partnership or where the property is owned by the government in the national, provincial or local sphere or certain government-owned exempt entities.

322. Section 12N of the Act deems the qualifying company to be the owner where the buildings and improvements are not owned, but only in specific circumstances as set out in that section. Section 12N of the Act does not extend to sublessees, other than to companies in the same group of companies as defined in the Act. Section 12N of the Act refers to a number of sections of the Act, including sections granting building allowances.

323. This section therefore permits for an allowance on improvements to be calculated as if the lessee owned the property with one of the conditions being that the taxpayer must use the property to produce income. In such case, the expenditure incurred by the lessee to complete improvements shall be deemed to be the cost for the purposes of the allowance.

324. Section 13 of the Act envisages improvements by lessees, but the other sections require that improvements be owned for the allowances to apply. Section 11(g) of the Act grants an allowance for leasehold improvements but does not apply to improvements in an SEZ because the lessor is a tax-exempt entity.

325. In South Africa, buildings and improvements that adhere to the land are owned by the land-owner. Leasing, no matter the length of the lease, does not confer ownership rights.

The rights granted under ownership and lease are fundamentally different. This difference is confirmed by the provisions of sections 12N and 12NA of the Act.

Factual Description

326. Sections 12S, 13*quat*, 13*quin*, 13*sex* of the Act require that a building or improvement be "owned" by the taxpayer for the building allowance to apply. "Owned" and/or "ownership" is not defined in the Act and must therefore take on the meaning under common law.

327. Leasehold is not ownership, even if it is a 99-year lease that is renewable in perpetuity. Leasehold grants a limited real right. A lease longer than 10 years is accepted as a long-term lease and this creates a limited real right and is registrable in the Deeds Office.

328. It is clear that in South African Law, ownership grants a real right to the owner over the property in question. Leases grant limited rights real rights to the lessee. Even though a lease may diminish the rights of an owner, the rights granted under ownership and lease are fundamentally different.

329. The implications of long-term leases and building capital allowances, especially relevant to Special Economic Zones ('SEZs'), were researched and it was confirmed that a lease contract, no matter how long or how often it is renewed or renewable, even if in perpetuity, is not akin to ownership in South African law.

330. One of the issues investigated is the receipt of the section 12S capital allowance in respect of buildings built by the taxpayer who does not (and will not) own it since it is often owned by government, which has an arrangement in terms of which a private sector entity will build while government provides and owns the land.

331. It seems that the ownership of land and therefore improvements in SEZs remain with a government entity (Government Gazette, 2012) the commercial entity operating in the zone cannot own the improvements under South African Law.

The nature of taxpayers impacted

332. Taxpayers undertaking improvements to land that is not owned by them, especially those in SEZs.

Proposal

333. Although we acknowledge National Treasury's willingness, as expressed in the Annexure C meeting held on 7 November 2022, to consider allowing a deduction for companies wholly owned by the State and who undertake improvements on land in an SEZ, we are of the view that this is not wide enough and does not align with the intention of an SEZ.

334. It is recommended that, in order to prevent anomalies as discussed above and to meet the goal of encouraging businesses to invest in SEZ's and to encourage wider economic activity, either the **ownership requirement** of the building allowance sections mentioned

above should **be removed** and the wording altered to work in the same way as section 13 of the Income Tax Act; or a **definition of ownership** should be **added** to the Act to **include long term leases** of 10 years or more, even if only for the purposes of the SEZ allowances. Alternatively, the term “owned” as used in section 12S of the Act should be defined as including leases of ten or more years.

335. With regard to leasehold improvements, we submit that by removing the “ownership” requirement from sections 13*quin* and 13*sex,* the income tax treatment of improvements on leased property, whether used for the purposes of manufacture or for other commercial purposes would be on a par and would more closely align with the sentiment expressed in Final Response Document from National Treasury and SARS on the Taxation Laws Amendment Bill of 2010 (National Treasury, 2010), namely that the lessee should be put in the same place as the owner, but not in a better place.

336. Acknowledging a possible concern that section 13 allowances might be granted to both parties, we note that the section 13 building allowances are granted on the cost to the taxpayer of the improvements as long as the building in question is used for the purposes mentioned in that section. The cost to the taxpayer is the limiting factor.

337. So too, acquiring a never-before-used building (from a developer for example), results in a cost to the new owner who then uses the building for the purposes mentioned and deducts the section 13 allowance based on that cost. If then on-leased, the lessee will not have incurred the costs and therefore is not entitled to the allowance.

338. Section 13(3) contains the recoupment provision allowing the recoupment of allowances to reduce a replacement building‘s cost. Again, no double deduction arises, since the allowances dictate the recoupment amount.

339. A tax-exempt lessor that incurs the cost of the improvements would not be entitled to deduct the allowance since that entity will not have an ‘income’ as defined against which to deduct the allowance. The allowances are only “allowed to be deducted from the income of the taxpayer”[4].

340. Thus, even if in the unlikely event of the cost being shared between lessor and lessee, the allowance will still be limited to that cost and the proof of that cost would be required.

341. In summary, by removing the ownership requirement as recommended, the other allowances simply fall in line with section 13. There is no additional advantage either way if the ownership requirement is removed from section 13*quin* of the Income Tax Act. The effects would be the same as those of section 13 of the Income Tax Act. Please refer to our examples below.

342. The above proposal may make section 11(*g*) of the Income Tax Act partly obsolete.

[4] Opening paragraph of s13(1), *13quin*, 13*sex* and of s12S(2)

343. Presently section 11(*g*) allows a lessee to write-off over the period of the lease the cost of improvements carried out under an obligation to do so in the lease agreement. The write-off period is limited to the lease period but with a maximum of 25 years. The lessee gets no allowance where the improvements are not the product of a contractual obligation that results in an inclusion in the lessor's gross income or where the lessor is a tax-exempt entity – i.e. the leasehold improvements are not included in the lessor's income in terms of the gross income definition paragraph (*h*)[5].

344. If the ownership requirement of section 13*quin* is removed, clauses obligating lessees to effect improvements may more frequently be omitted from lease agreements in order to avoid an inclusion in the lessor's gross income in terms of para (*h*), since this would no longer be achieved at the expense of capital allowances for the lessee. The extent to which such clauses might continue to be incorporated in lease agreements in order to provide the lessor with an enforceable right to have improvements affected is unclear.

345. Section 11(*g*) will still be advantageous where a lease period exceeds 20 years (the period for building allowances), but still limited to 25 years.

346. If the tax-exempt entity is one of those listed in section12N, the improvements are deemed to be owned by the lessee for the purposes of the sections listed.[6]

347. Examples of changes to ownership requirement in capital allowance sections

Example 1:
Entity A (tax-exempt entity) leases a piece of land to Entity B. According to the 20-year lease agreement, Entity B is obligated to effect leasehold improvements (the erection of a building on the piece of land) to the value of R3 million within one year of entering into the lease agreement. Entity B then sub-leases the building to Entity C who uses the building for the distribution of goods (thus, not a process of manufacture).

Entity B	**Current legislation**	**Recommendation to remove 'owner' requirement**
Deductions		
- Improvements	(-)* *section 11(*g*) not applicable, as the lessor did not include the amount in gross income (tax-exempt entity); section 12N not applicable as sub-leasing; section 13*quin* not applicable as not owner of building.	(150 000)* *R3 000 000 x 5% (section 13*quin*), "owner of building" requirement removed, costs incurred by Entity B Note: No costs incurred by Entity C, hence no deduction available to Entity C

[5] Section 11(*g*)(vi)
[6] See paragraph 4 of the first submission.

End of the lease agreement (disposal of *bare dominium* in the improvement):

Entity B	**Current legislation**	**Recommendation to remove 'owner' requirement**
Proceeds	-	-
Less: Base cost	R3 000 000* *(R3 000 000 less Rnil)	Rnil* *(R3 000 00 less R3 000 000 claimed under s 13*quin*, par 20(3)(*a*) of the Eighth Schedule)
Capital gain or (loss)	(R3 000 000)	-

Eventual disposal of the land and building for R10 million by Entity A:

Entity A	**Current legislation**	**Recommendation to remove 'owner' requirement**
Proceeds	R10 000 000	R10 000 000
Less: Base cost	Rnil* *par 20(1)(*h*)(ii)(*cc*) of the Eighth Schedule – no amount was included in the gross income of Entity A under par (*h*) of the gross income definition	Rnil *par 20(1)(*h*)(ii)(*cc*) of the Eighth Schedule – no amount was included in the gross income of Entity A under par (*h*) of the gross income definition
Capital gain or (loss)	R10 000 000 Entity A will not be taxed on the capital gain of R10 000 000 as Entity A is a tax-exempt entity.	R10 000 000 Entity A will not be taxed on the capital gain of R10 000 000 as Entity A is a tax-exempt entity.

Example 2:

Entity A (a taxable entity) leases a piece of land to Entity B. According to the 25-year lease agreement, Entity B is obligated to effect leasehold improvements (the erection of a building on the piece of land) to the value of R3 million within one year of entering into the lease agreement. The improvements were completed within one year of entering into the lease agreement. Entity B uses the building for the distribution of goods (thus, not process of manufacture). No allowance under section 11(*h*) was granted to Entity A.

Entity A	**Current legislation**	**Recommendation to remove 'owner' requirement**
Gross income inclusion	R3 000 000 (gross income paragraph (*h*))	R3 000 000 (gross income paragraph (*h*))

Entity B	Current legislation	Recommendation to remove ‘owner’ requirement
Deductions		
- Improvements	(125 000)* *R3 000 000 / (25y less 1y) (section 11(*g*))	(125 000)* *R3 000 000 / (25y less 1y) (section 11(*g*)) OR (150 000)* *R3 000 000 x 5% (section 13*quin*), “owner of building” requirement removed, costs incurred by Entity B

End of the lease agreement (disposal of *bare dominium* in the improvement):

Entity B	Current legislation	Recommendation to remove ‘owner’ requirement
Proceeds	-	-
Less: Base cost	Rnil* *(R3 000 000 less R3 000 000 claimed under section 11(*g*), par 20(3)(a) of the Eighth Schedule)	Rnil* *(R3 000 00 less R3 000 000 claimed under section 13*quin*, par 20(3)(a) of the Eighth Schedule)
Capital gain or (loss)	-	-

Eventual disposal of the land and building for R10 million by Entity A:

Entity A	Current legislation	Recommendation to remove ‘owner’ requirement
Proceeds	R10 000 000	R10 000 000
Less: Base cost	R3 000 000* (R3 000 000 less Rnil) *par 20(1)(*h*)(ii)(*cc*) of the Eighth Schedule – amount included in the gross income of Entity A under par (h) of the gross income definition less any allowance granted under s 11(*h*)	R3 000 000* (R3 000 000 less Rnil) *par 20(1)(*h*)(ii)(*cc*) of the Eighth Schedule – amount included in the gross income of Entity A under par (h) of the gross income definition less any allowance granted under s 11(*h*)

Capital gain or (loss)	R7 000 000	R7 000 000

Example 3:
Entity A (a taxable entity) leases a piece of land to Entity B. Entity B is entitled but not obligated to effect leasehold improvements in terms of the lease agreement. Entity B in fact erects a building at a cost of R3 million within one year of entering into the lease agreement. Entity B uses the building for the distribution of goods (thus, not process of manufacture).

Entity A	**Current legislation**	**Recommendation to remove 'owner' requirement**
Gross income inclusion	-* *gross income paragraph (*h)* not applicable as no obligation in terms of lease	-* *gross income paragraph (*h)* not applicable as no obligation in terms of lease

Entity B	**Current legislation**	**Recommendation to remove 'owner' requirement**
Deductions		
- Improvements	(-)* *section 11(*g*) not applicable, as no obligation in terms of lease; section 13*quin* not applicable as not owner of building.	(150 000)* *R3 000 000 x 5% (section 13*quin*), "owner of building" requirement removed, costs incurred by Entity B

End of the lease agreement (disposal of *bare dominium* in the improvement):

Entity B	**Current legislation**	**Recommendation to remove 'owner' requirement**
Proceeds	-	-
Less: Base cost	R3 000 000* *(R3 000 000 less Rnil)	Rnil* *(R3 000 00 less R3 000 000 claimed under s 13*quin*, par 20(3)(*a*) of the Eighth Schedule)
Capital gain or (loss)	(R3 000 000)	-

Eventual disposal of the land and building for R10 million by Entity A:

Entity A	**Current legislation**	**Recommendation to remove 'owner' requirement**
Proceeds	R10 000 000	R10 000 000

Less: Base cost	Rnil* *par 20(1)(*h*)(ii)(*cc*) of the Eighth Schedule – no amount was included in the gross income of Entity A under par (*h*) of the gross income definition	Rnil* *par 20(1)(*h*)(ii)(*cc*) of the Eighth Schedule – no amount was included in the gross income of Entity A under par (*h*) of the gross income definition
Capital gain or (loss)	R10 000 000	R10 000 000

Sections 12R – Special Economic Zones (SEZs): Reduced corporate tax rate *(submission originally made in 2020)*

Legal Nature

348. Section 12R provides for reduced corporate tax rate of 15% for qualifying companies situated in SEZs.

Factual Description

349. Section 12R no longer specifies the reduced corporate tax rate of 15% within the section (this has been moved to section 3 of Schedule 1 of the Rates and Monetary Amounts and Amendment of Revenue Laws Bill, 2017).

The nature of businesses impacted

350. All qualifying companies operating in SEZs.

Proposal

351. We recommend that section 12R either make reference to where the reduced corporate tax rate percentage can be found, or such rate should be specified within the section itself.

Sections 12R – SEZs: Qualifying companies *(submission originally made in 2020)*

Legal Nature

352. Section 12R(1) defines a "qualifying company" that will be entitled to the tax benefits of operating in a SEZ.

Factual Description

353. "Qualifying companies" as defined in section 12R(1) do not require pre-approval in order to benefit from the reduced corporate tax rate of 15% (other than meeting the required qualifying criteria).

354. As such, should a company meet the definition of a "qualifying company", the question is whether the reduced corporate tax rate will automatically be applied to qualifying companies when completing their tax returns, or whether qualifying companies must specifically elect to be taxed at the reduced rates.

355. In addition, when utilising the SEZ tax benefits, it is unclear whether companies will require a letter from the SEZ operator as proof of meeting the “qualifying company” requirements, or if the onus of proof is on the individual company in this regard.

The nature of businesses impacted

356. All companies operating in an SEZ that potentially qualify as a “qualifying company”.

Proposal

357. Clarification on the above issues is kindly requested and if necessary, section 12R should be amended accordingly.

Sections 12R – SEZs: Monitoring of the Department of Trade and Industry (DTI) *(submission originally made in 2020)*

Legal Nature

358. One of the requirements of a “qualifying company” as defined in section 12R(1) is that the company must carry on a trade in a special economic zone designated by the Minister of Trade and Industry in terms of the Special Economic Zones Act and approved by the Minister of Finance after consultation with the Minister of Trade and Industry for the purposes of this section by notice in the Gazette.

359. The SEZ Act in section 7 sets out the functions of the Advisory Board, of which the DTI is a member.

Factual Description

360. While the SEZ Act sets out the duties of the DTI in relation to SEZs (in terms of acting on the Advisory Board and reporting to Parliament), clarification is required as to whether the DTI has any further involvement in terms of monitoring the performance of the individual companies located within the SEZ, or whether this performance will be monitored on an individual basis solely by the SEZ operators, with a consolidated performance/progress report being provided to the Advisory Board.

The nature of businesses impacted

361. All businesses operating in an SEZ.

Proposal

362. Clarification on the above issue is kindly requested.

Sections 12R – SEZs: Interaction of Income Tax Act and SEZ Act *(submission originally made in 2020)*

Legal Nature

363. The SEZ Act requires that a company obtain approval from the SEZ operator to locate itself in a SEZ. The Income Tax Act does not require any such approval.

Factual Description

364. It is therefore our understanding that it is only a requirement of the SEZ Act that companies should obtain approval if they are currently not located within a SEZ but wish to start operating in a SEZ. No further approvals or pre-approvals should have to be obtained in order for companies to access the SEZ tax benefits once they are operating within the SEZ.

The nature of businesses impacted

365. All businesses wishing to locate their operations in a SEZ as well as those currently operating in a SEZ.

Proposal

366. We would appreciate clarity on whether our understanding of the legislation currently in place is correct.

Section 20 – Assessed losses *(submission originally made in 2021)*

Legal nature of problem

367. Section 20 allows for the set-off of the balance of assessed losses.

Factual description

368. In countries that operate on a worldwide/residence-based tax system, foreign losses are capable of being offset against local income. Sometimes foreign capital losses are quarantined or ring-fenced, but revenue losses are allowed to be deducted.

369. When South Africa moved to a worldwide tax system in 2001, foreign revenue losses were quarantined and could not be offset against local income. Tax practitioners who were involved in 2000 and 2001 and were engaging with SARS were told that this was being done because SARS did not know the extent of foreign losses, and they needed to protect the tax base until they got a handle of "what was out there", as it was put.

370. It is now 20 years later and the provision is still in section 20.

Business/Persons impacted

371. Companies with assessed and foreign losses.

Proposal

372. An update should be provided on whether the quarantining of foreign revenue losses is still necessary and if not, then the ring-fencing proviso should be removed.

Section 23M – Limitation of interest deduction – related interest *(submission already made in 2021)*

Legal nature of problem

373. Section 23 restricts the interest deduction for a debtor and will apply if a "controlling relationship" exists between the debtor and the creditor and the creditor is not subject to tax in South Africa in respect of such interest or when a creditor, not subject to tax, sources the funding from a person who is in a controlling relationship with the debtor.

Factual description

374. While the Taxation Laws Amendment Act expands the definition of "interest" for purposes of section 23M, the new definition does not include the wording **"related interest**". However, the wording "related interest" is used three times in the amended section 23M without any clarification as to its meaning. Presumably it refers to the new additions to the definition of interest. However, introducing undefined concepts will make interpretation and application exceedingly difficult and unintended non-compliance likely.

Business/Persons impacted

375. Taxpayers subject to section 23M.

Proposal

376. Clarification in the legislation on the meaning of "related interest" is required.

Section 23M(3) – Limitation of interest deductions (NEW)

Legal Nature

377. We refer to an extract of section 23M(3) below:

> *3) The amount of interest allowed to be deducted in respect of all debts owed as contemplated in subsection (2), in respect of any year of assessment must not exceed the sum of—*
>
> *(a) the amount of interest received by or accrued to the debtor; and*
>
> *(b) an amount determined by multiplying the adjusted taxable income of that debtor for that year of assessment by 0,3,*
>
> *reduced by so much of any amount of interest incurred by the debtor in respect of debts other than debts contemplated in subsection (2) as exceeds any amount not allowed to be deducted in terms of section 23N.*
>
> (our emphasis underlined)

Factual Description

378. Section 23M(3) requires that the amounts calculated in subsections 3(a) and (b) must be reduced by so much of any interest incurred in respect of debts (other than interest on debts disallowed in terms of section 23N).

379. To the extent that the interest incurred includes interest that is not deductible for income tax purposes (for example interest not incurred in the production of income) the reduction of the interest allowed as a deduction by the non-deductible interest would result in a double disadvantage to the taxpayer (the non-deductible interest would be added to taxable income and the interest allowable as a deduction in in terms of 23M would also be reduced.

The nature of taxpayers impacted

380. Businesses applying section 23M Interest limitation rules that also incur non-deductible interest.

Proposal

381. We recommend that the word "deductible" be inserted to clarify the intention; such that the provision will read as follows:

3) The amount of interest allowed to be deducted in respect of all debts owed as contemplated in subsection (2), in respect of any year of assessment must not exceed the sum of—

(a) the amount of interest received by or accrued to the debtor; and

(b) an amount determined by multiplying the adjusted taxable income of that debtor for that year of assessment by 0,3,

*reduced by so much of any amount of [**deductible]** interest incurred by the debtor in respect of debts other than debts contemplated in subsection (2) as exceeds any amount not allowed to be deducted in terms of section 23N.*

Section 23M(3) – Limitation of interest deductions – IFRS 16 Finance Leases (NEW)

Legal Nature

382. The definition of "interest" noted in section 23M(1) *includes any finance cost element recognised for purposes of IFRS in respect of any lease arrangement that constitutes a finance lease as defined in IFRS16.*

Factual Description

383. In calculating the section 23M(3) limitation, the finance cost element in respect of IFRS16 will form part of "*interest incurred by the debtor in respect of debts other than debts contemplated in subsection (2)*" and will therefore be subtracted in calculating the s23M(3) limit, thereby lowering the limitation, given that the finance cost element must

be subtracted irrespective of whether or not it was allowed as a deduction from income (it won't have been allowed as a deduction from income, since it is purely an accounting concept).

384. For example, if a farming company requires financing for its farming equipment and enters into finance leases for this purpose with a completely independent South African bank, the required subtraction of the finance cost element of the finance leases in terms of section 23M(3) will have the effect of reducing the s23M limitation.

385. This must surely be unintended, given that such finance cost element will also not be added back in the calculation of "adjusted taxable income", because the finance cost element of finance leases is purely an accounting concept and will not have been allowed as a deduction from income.

The nature of taxpayers impacted

386. Taxpayers who have entered into a finance lease in terms of IFRS16 and are subject to section 23M.

Proposal

387. The s23M(3) should be amended by the insertion of the word 'deductible' before the words "interest incurred by the debtor" as noted in our paragraph 84 above.

Section 23M(4) – Limitation of interest deductions – the succeeding year of assessment (NEW)

Legal Nature

388. Section 23M(4) deems the interest incurred, that is in excess of the s23M(3) limitation, to be carried forward to the following year of assessment and be an amount of interest that is incurred in that succeeding year of assessment.

Factual Description

389. It is unclear whether the interest is deemed to be incurred in the succeeding year of assessment for purposes of the entire Act, or merely for purposes of section 23M only.

390. Although we assume that it is for purposes of Part I of the Act, it would be better if this were expressly clarified in the subsection.

The nature of taxpayers impacted

391. Those taxpayers subject to section 23M(4).

Proposal

392. The words "for purposes of this Part" should be inserted into s23M(4) to clarify this point.

Sections 23M(6)(b), 8F(3)(d) and 8FA(3)(d) – Infrastructure investment and social impact funds held and/or funded by long term insurers, pension funds, provident funds (NEW)

Legal Nature

393. Whilst National Treasury through Regulation 28 of the Pension Funds Act in respect of infrastructure investments seeks to encourage investments in infrastructure as contemplated in the Regulation, the interest limitation provisions of sections 23M, 8F and 8FA negatively impacts investments by Pension fund, Long-term insurers and retirement funds.

394. A similar negative impacts arises in respect of investments in social impact funds.

Factual Description

Infrastructure investments

395. SA's infrastructure needs are significant and span all major infrastructure sectors (energy/electricity, transport & logistics, bulk water supply & wastewater management, telecommunications & data infrastructure, amongst others). Per Government's own analysis, more than R6 trillion is required for SA's infrastructure between 2016 and 2040[7].

396. The Just Energy Transition Investment Plan announced by Government estimates that R1.5 trillion is required between 2023 and 2027 for new energy/electricity infrastructure alone[8]. To fund this amount, at least R500 billion is needed to be raised from the private sector.

397. The investment into new power generation capacity has become even more urgent recently, with 2023 experiencing unprecedented load shedding and Eskom announcing that there is a high probability of Stage 8 loadshedding[9], resulting in consumers being without power for up to 12 hours a day.

398. Furthermore "to encourage rapid private investment to alleviate this energy crisis, in the 2023 Budget Review, Government proposed to temporarily enhance the current renewable energy tax incentive available in section 12B of the Act".

399. To achieve this, Government also recently amended Regulation 28 of the Pension Funds Act to encourage infrastructure investments by retirement funds[10] and long-term insurers. However, certain sections in the Income Tax Act will have a negative impact on the mobilisation of such funding.

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[7] National Infrastructure Plan 2050 (NIP 2050) Phase 1, Government Gazette No. 46033 of 11 March 2022
[8] https://www.thepresidency.gov.za/content/south-africa%27s-just-energy-transition-investment-plan-jet-ip-2023-2027
[9] https://www.eskom.co.za/power-system-is-severely-constrained-with-a-high-risk-of-increased-stages-of-loadshedding-in-winter/
[10] Government Gazette No. 46649 of 1 July 2022

400. Given the conflict in legislation and resulting impact on available funding, it is recommended to exclude infrastructure investments (as defined in the amended Regulation 28 of the Pension Funds Act) from the application of sections 23M, 8F, 8FA of the Income Tax Act, so that the country can mobilise the required funding for much needed infrastructure development[11].

Social Impact funds

401. The current wording of sections 23M, 8F and 8FA constrain and restrict financing and investment into social infrastructure as well as other positively impactful areas due to reduced returns. Institutional investors are significant investors into such funds, which ordinarily struggle to attract lenders and investors that are willing to provide the necessary funding/funding on the required terms that meet the developmental needs of the target sector or market segment, which includes:

- ➢ Renewable energy initiatives;
- ➢ student accommodation,
- ➢ rental housing & housing developments,
- ➢ financial inclusion e.g. SMME and consumer finance as well as education e.g. schools, tertiary education and other education.

<u>*The nature of taxpayers impacted*</u>

402. Infrastructure and social impact investments that take the legal form of companies and that are wholly or jointly owned and funded by retirement funds and life insurers or a combination of these regulated institutions.

[11] Mobilising Long-Term Capital in SA
It is commonly known that the most suitable source of long-dated capital for infrastructure investment is the retirement industry, specifically regulated pension funds. The benefits, for both pension funds and infrastructure development, are as follows:
➢ Pension funds have long-term investment horizons that match the duration of infrastructure investments (typically 15-25 years).
➢ Investments are often linked to CPI and have predictable cash flows, which is beneficial for pension funds that manage long-term inflation risks.
➢ Pension funds represent a large source of capital (according to the FSCA, ca. R4.3 trillion of assets in 2020), with very little of this capital currently invested in SA infrastructure. This is particularly relevant given the sheer size of the total investment requirement.
➢ Investment can be funded using local sources of capital from pension funds, rather than 'tapping' international funding sources. This encourages ownership by local entities, enabling local capacity building and beneficiation, retaining and reinvesting profits in-country (rather than being transferred offshore), in addition to reducing the dependency on international capital flows and associated risks.

Proposal

403. Consideration should be given to extending the exclusions to funding for infrastructure investments and social impact investments provided by retirement funds and long-term insurers.

Section 23M and section 31 – The ordering of these sections *(submission originally made in 2022)*

Legal Nature

404. Section 31 and section 23M both seek to disallow interest deductions. The interaction between these two sections, as to which one takes priority, has caused many debates.

405. National Treasury and SARS have noted that in their view, section 31 should be applied prior to section 23M, i.e. "*Government proposes that companies first apply the arm's length test to financial transactions, followed by the interest limitation rules, i.e. the interest limitation rules should apply to net interest expense that has already passed the arm's length test*."

406. "*Section 23M and section 23N contain certain limitations on the amount of interest which may be deducted. Section 31 applies prior to considering the impact, if any, of section 23M and section 23N. Accordingly, when these sections refer to taxable income in the definition of ' adjusted taxable income' and to the amount of interest which is allowed to be deducted in section 23M(3) and section 23N(2), the reference is to the amount of taxable income and the amount of interest which may be deducted, after section 31 has been applied*."

407. Unfortunately, neither SARS nor National Treasury have provided any reasoning to support this view.

Factual Description

408. National Treasury and SARS have noted that in their view, section 31 should be applied prior to section 23M. No reasons were provided for this view. Certain commentators have, however, stated that they feel section 23M should apply before section 31. Despite National Treasury's views on this matter, the legislation is not clear on the ordering of these sections.

The nature of taxpayers impacted

409. Those taxpayers meeting the requirements of sections 23M and 31.

Proposal

410. The legislation should clearly stipulate the order in which these two sections should be applied given that the legislation is lacking in this regard and to avoid unnecessary disputes on the matter.

Section 24 – Lay-by agreements (NEW)

Legal nature

411. Sections 24(2A) and (2B) of the Act were amended to specify that section 24 relief is applicable to lay-by agreements.

412. It is argued, however, section 24(1) does not in fact apply to lay-by agreements.

Factual description

413. There are two issues that must be evaluated when considering lay-by sales, (a) the deposit received and (b) the accrual of the outstanding debtors' amount.

Deposit received

414. Section 24(2A) refers to *a lay-by agreement as contemplated in section 62 of the Consumer Protection Act, 2008 (Act No. 68 of 2008).*

415. Section 62 of that Act reads as follows:

(1) If a supplier agrees to sell particular goods to a consumer, to accept payment for those goods in periodic instalments, and to hold those goods until the consumer has paid the full price for the goods—

(a) *each amount paid by the consumer to the supplier remains the property of the consumer*, and is subject to section 65, until the goods have been delivered to the consumer; and

(b) the particular *goods remain at the risk of the supplier until the goods have been delivered* to the consumer.

(emphasis added)

416. In *Geldenhuys v CIR (1974) (3) SA 256 (C); 14 SATC 419* it was held that the words "received by … the taxpayer" in the definition of "gross income" in section 1 of the Act mean 'received by the taxpayer on his own behalf for his own benefit'.

417. It is clear then that lay-by cash deposits received by the supplier are not "received" by the supplier, even if the funds are intermingled with the supplier's other cash takings (see ITC 24510, 2019, SATC).

418. Lay-by sales deposits are not "gross income" because taxpayers do not receive them for their own benefit. In law, the seller is effectively holding the cash deposit in trust and the cash deposit is, therefore, not a receipt in the income tax sense.

Accrual of the outstanding debtors' amount

419. In *Mooi v SIR, 1972 (1) SA 674, 34 SATC 1* it was held that the phrase “accrued to” in the definition of “gross income” means a person must be unconditionally entitled to the amount. As the goods sold in terms of a lay-by agreement are still in the supplier’s possession, the taxpayer is not unconditionally entitled to the outstanding lay-by amount.

420. Therefore, the amount of outstanding debtors does not accrue to the taxpayer.

421. Section 24(1) therefore does not specifically apply to lay-by agreements (see Hassan & Van Heerden, 2023; Haupt, 2023; Louw, 2022; Nel, 2023). There should consequently be no concern in relation to the relief.

422. There is international support for the arguments presented.

International comparison

423. The Australian Tax Office issued a ruling (TR 95/7) titled “Income tax: lay-by sales”.

424. In accordance with the decision (Australian Tax Office, 1995: p 4):

> When are amounts received under a lay-by sale earned?
>
> 6. With one exception, *amounts received* (e.g., initial deposit and instalments) by the seller from the buyer while goods are held by the seller *under a lay-by sale are not earned by the seller, and therefore are not derived for the purposes of subsection 25(1) of the ITAA [Australian Income Tax Act],* until the buyer pays the final instalment of the purchase price and the goods are delivered to the buyer.
>
> 7. *The exception is any initial deposit which*, by the terms or conditions of the lay-by sale, *is a non-refundable deposit that a buyer is required to pay to a seller*. A non-refundable deposit is earned and is derived by a seller when it is due to be paid by the buyer.
>
> (emphasis added)

425. The Australian Tax Office consequently does not tax amounts received by or owed as a result of a lay-by sale under the Australian Income Tax Act. The only exception to this rule is for deposits that are non-refundable.

<u>*The nature of taxpayers impacted*</u>

426. Taxpayers selling goods in terms of lay-by agreements.

<u>*Proposal*</u>

427. It is proposed that section 24 must exclude the phrase “*a lay-by agreement as contemplated in section 62 of the Consumer Protection Act, 2008 (Act No. 68 of 2008)*”.

Section 24BA – Transactions where assets are acquired as consideration for shares issued *(submission originally made in 2021)*

Legal nature of problem

428. Section 24BA is an anti-avoidance provision to address potential value shifting arrangements arising in the context of asset for share transactions. In essence, this section provides for the event where there is a mismatch in the value of the asset received and the value of the shares issued as consideration.

Factual description

429. The test to ensure whether there is a mismatch is if the consideration is different from what would have been the case between independent persons dealing at arm's length.

430. This formulation is understood where the parties are not at arm's length, as then the best indication would be whether the values are the same. But where the parties are independent persons dealing at arm's length, the application of section 24BA does not seem reasonable.

431. There can be many reasons why arm's length parties will agree to different values. But then to apply the test of what would independent parties acting at arm's length do to a scenario where the parties that are dealing with each other are independent parties at arm's length, and yet still come out with a different number to the agreed number and subject the company to tax, does not seem to make sense. However, this is what happens as can be seen from BPR254 – Consequences of cross border and domestic asset for share transactions).

432. SARS justifies its approach because of the words "before taking into account any other transaction, operation, scheme, agreement or understanding that directly or indirectly affects that consideration".

433. In other words, SARS seems to ignore the true facts and taxes the transaction based on hypothetical facts.

Business/Persons impacted

434. Independent parties dealing at arm's length entering into an asset for share transaction.

Proposal

435. If the legislature wishes to have a blanket rule that there must always be the "correct" exchange ratio between the value of the shares issued and the value of the assets, otherwise tax will be payable, then this must be clearly stipulated in the legislation. However, if the true purpose is only to attack non-arm's length parties who do not transact at arm's length and accept the outcome of actual arm's length dealings, then the legislation needs to be amended to prevent SARS from applying it in the way that they currently do.

Section 24I – Exchange differences and assessed losses (NEW)

Legal Nature

436. Section 24I(3) of the Act provides that in determining the taxable income of a person subject to section 24I, the exchange differences (foreign exchange gains or losses) must be added to, or deducted from, the income of the taxpayer.

437. Section 24I(2) applies a company, whether or not such company carries on a trade. This may be inferred from the fact that although section 24I(2)(b) states that s24I only applies to trusts that carry on a trade, section 24I(2)(a) makes the section apply to any company without stipulating that the company must be carrying on a trade. This stance also finds support in SARS IN 101 at 4.2.1, which states: “Section 24I applies to any company irrespective of whether it carries on a trade.”

Factual Description

438. Due to currency fluctuations, it often occurs that a company that does not carry on a trade incurs a s24I foreign exchange loss in a given year of assessment but a foreign currency gain in the following year of assessment.

439. However, if a company does not carry on a trade and incurs a deductible s24I foreign exchange loss during a year of assessment which causes it to have an assessed loss during the year of assessment, section 20(1)(a) prevents the company from carrying forward and utilising the balance of assessed loss against the foreign currency gain in the following year of assessment, unless it embarks on a trade in such following year of assessment. This creates an inequitable mismatch for a non-trading company in that it is taxed on the foreign exchange gains without being allowed to set off the previous year’s foreign exchange losses.

440. This often occurs in group structures, which often involve investment or intermediary holding companies that do little more than act as shareholder or as a conduit for funding. Where the funding is denominated in a foreign currency, the holding company will realise foreign exchange gains and/or losses.

441. The general absence of other income in the hands of the holding company would result in the section 24I loss creating a current year assessed loss for the company.

442. The absence of trade would preclude the company from carrying forward the assessed loss under section 20 of the Income Tax Act.

443. The trade requirement in relation to the recognition and carry forward of losses resulting from exchange differences creates an inequitable result for these companies as the companies are required to include foreign exchange gains in income in any given year, while not being able to set off prior year foreign exchange losses against such income.

The nature of taxpayers impacted

444. Non-trading South African resident taxpayers with foreign exchange gains/losses in respect of exchange items.

Proposal

445. We submit that over the term of any exchange item, the net tax position for the company should align with the net foreign exchange gain or loss on the exchange item.

446. We recommend that companies be expressly allowed to carry forward an assessed loss to the extent that the assessed loss arises from s24I foreign exchange losses. This loss would then be offset against future foreign exchange gains (i.e. ring-fence the assessed loss carried forward to be off set only against section 24I gains).

Section 25B – Taxation of trusts and beneficiaries of trusts *(submission originally made in 2021)*

Legal nature of problem

447. Section 25B sets out rules for distributions of income by trusts. It does so by deeming the receipt to be awarded to the beneficiary and deeming the related expenses to be incurred by the beneficiary, but it does not allow a loss. If the expenses exceed the income then the beneficiary is treated as 'breaking even', and the excess expenses are carried forward and deemed to be expenses in the following year.

Factual description

448. The effect of this is that current year's losses may be offset against future years' income. But the same principle is not applied to section 7(8) and paragraphs 72, 80(1) and 80(2) of the Eighth Schedule.

449. In the case of section 7(8), while the approach is initially the same as section 25B, a loss cannot be offset against the next year's income for the purpose of determining the amount to be attributed to the donor.

450. Similarly, under paragraph 72 capital losses cannot be offset against capital gains, and only the latter are attributed.

451. For example, the same applies under paragraph 80(1) of the Eighth Schedule – if two assets are vested in a beneficiary, one with a capital gain of R100 and the other with a capital loss of R80, the beneficiary is taxed on the R100 gain and not on the R20; and the loss of R80 cannot be carried forward as a loss in the trust.

452. Similarly, under paragraph 80(2) if there is a realised gain of R100 and a loss of R80, only the gain vests in the case of a vesting trust, and not the net gain. In a discretionary trust the trustees can manage the position by vesting only R20 and leaving the R80 gain behind to be offset by the R80 loss. However, if there is a loss of R100 in year one and a gain of R120 in year 2 and there is a vesting trust, the beneficiary will pay tax on the gain of R120 in year two and get no benefit from the loss of R100 in year one. And in a

discretionary trust if the trustees award only R20 in year two, the trust will be taxed on the R100 gain without being able to offset the loss of R100 in year one.

Business/Persons impacted

453. All taxpayers that are subject to section 7(8) and paragraphs 72, 80(1) and 80(2) of the Eighth Schedule.

Proposal

454. To prevent the inequality that arises, section 7(8) and paragraphs 72, 80(1) and 80(2) of the Eighth Schedule should be amended to align with the treatment in section 25B.

Section 31(6) and 31(7) – Exemptions: application unclear *(submission already made in 2022)*

Legal Nature

455. Section 31 contains two specific exemptions which are included in section 31(6) and section 31(7).

456. Section 31(6) applies where the transaction is the granting of financial assistance or the use of intellectual property to a controlled foreign company (CFC) which has a foreign business establishment ("FBE") and the tax payable by that CFC amounts to 67.5% of the tax that would be paid in South Africa if that CFC were subject to tax in South Africa.

457. Section 31(7) provides an exemption for loan funding made to a foreign group company where the loan is interest free and for a minimum period of 30 years and certain other conditions are met. The purpose of this exemption is to allow resident companies to extend loan funding which is in economic substance equity to group companies without risk of an adjustment.

Factual Description

458. Both the above sub sections only relate to transactions between separate legal entities where one is a South African resident entity and the other is a non-resident entity. The sections do not seem to cater for similar transactions between a South African resident and a foreign permanent establishment (PE) of another South African resident.

459. The application of section 31(6) and section 31(7) between two resident taxpayers where one has a PE offshore and the transaction is with the PE is not clear. A question was raised whether there is an anomaly in the application of these exemptions and whether the sections should be broadened.

The nature of taxpayers impacted

460. Transactions between a South African resident and a foreign permanent establishment (PE) of another South African resident

Proposal

461. The sections should be amended to clarify that these two exemptions apply to all potentially affected transactions listed in section 31(1)(a).

Section 41(10) – Contingent Liabilities (NEW)

Legal nature

462. A provision that was added in 2017 is section 41(10) of the Act, which states that, for the purposes of the corporate rules, a contingent liability will be treated as a debt actually incurred.

463. This is not in line with the corporate rules that serve to defer the taxation that would ordinarily arise when assets are transferred from one party to another as set out in the relevant rules.

Factual description

464. The objective of section 41(10) is to make it clear that the specified liabilities include contingent liabilities which also satisfy the specified criteria (e.g. arose as part of the going concern or more than 18 months prior to the relevant transaction etc.). The 2017 Explanatory Memorandum states that because contingent liabilities are not yet real obligations they would not be considered as "debts" for purposes of corporate restructures.

465. Reference to Interpretation Note 94 ("IN 94") and the "Ackerman" Supreme Court of Appeal judgment, issued in 2010 make it clear that the seller cannot allege that the contingent liability has been incurred (and deduct it for tax purposes) and the purchaser may only consider the amount incurred when the obligation ceases to be contingent (if it ever does).

466. IN 94 then explains that, generally, until a continent liability becomes a real liability, the purchaser, which has used the contingent liability as part of the consideration for an asset, may not treat the cost of such asset, to the extent it is paid for with the contingent liability, as incurred.

467. The purchaser must wait until the liability becomes 'real' to be able to deduct the cost or portion thereof of the asset (or related allowances).

468. Since section 41(10) states that the deemed incurral only applies for purposes of the corporate rules and therefore it seems to mean that it cannot be used for other purposes; i.e., (a) to facilitate additional amounts to be deducted for purposes of the general deduction formula (trading stock), (b) capital allowances or (c) base cost for capital assets.

469. However, the corporate rules generally allow the transferee to "step into the shoes of the transferor" insofar as the transferred assets and the claiming of the cost of trading stock or allowances/base cost are concerned.

470. A question that arises is what becomes of the contingent liability when it materializes? Is the transferee allowed to claim deductions, allowances or a base cost related to this loan?

471. IN 94, specifically in relation to the corporate rules (part 7), states that the rest of the IN must be taken into account, but *"In making such an evaluation no regard must be had to the fact that the assumption of the contingent liabilities by the transferee was part of the consideration for the acquisition of the assets"*.

472. Thus, despite the fact that it does not refer to section 41(10), because IN 94 was issued in December 2016 (before section 41(10) was introduced) and has not been updated, and there was thus, at the time of its issue, no legal support for the tax position taken at the time, the IN aligns with s41(10) in determining that the contingent liabilities may, essentially, be considered incurred when used as part of the consideration and, thus, the transferee may continue to claim the allowances for the assets purchased in the same manner as the transferor would have.

473. What happens to the contingent liabilities, however, when they become actual liabilities in the transferee's hands when the corporate rules have been used?

474. IN 94 states that once the contingent liability transferred becomes unconditional, the transferee may claim the expense on the same basis as the transferor would have. The example given is that if the transferor would have claimed a revenue deduction e.g. for a bonus, then the transferee must, when actually incurred, claim it as such, even though the assumption of the liability was used to buy a capital asset.

475. This is the opposite approach to the rest of IN 94.

476. This approach also brings into question, despite it stating that it only applies for the corporate rules, the intended extent of s41(10).

477. Nowhere in sections 41 to 47 does it state that the transferee must step into the shoes of the transferor insofar as contingent liabilities are concerned. Thus, though the outcome is favourable to taxpayers (and one which would be preferred for non-corporate rule asset transfers), it is not supported by the legislation (an IN is not legislation). Nor is it consistent with the treatment of transactions outside the corporate rules which involve contingent liabilities.

The nature of taxpayers impacted

478. All corporate restructures where contingent liabilities will be sold and specifically the transferee in this regard.

Proposal

479. The law thus needs to be clear in order to align with the practice i.e. it should state that the transferee will step into the shoes of the transferor insofar as contingent liabilities are concerned.

Section 42(1)(a)(ii)(cc) – Asset-for-share transactions – nature of asset (NEW)

Legal nature

480. Section 42 requires the recipient company to acquire the assets as capital or revenue assets in line with how the transferor held them.

481. This requirement is however overridden by a third provision that the company must acquire the asset *“as trading stock, where that person holds it as a capital asset and that company and that person do not form part of the same group of companies”*.

Factual description

482. This provision may be read in one of two ways:

   (a) If the transferor and transferee are not a group of companies, the transferee must acquire the asset as trading stock; or

   (b) If the transferor and transferee are not a group of companies, the transferee may acquire the asset as trading stock.

483. These two “options” lead to very different outcomes for the recipient company.

484. The Explanatory Memorandum (“EM”) to the 2015 Taxation Laws Amendment Act, which introduced these provisions, makes it clear that interpretation (b) above is what was intended.

485. Therefore, the legislation and not only the EM must make this scenario clear as to the correct interpretation.

The nature of taxpayers impacted

486. All section 42 restructures, specifically the transferee in this regard.

Proposal

487. Section 42(1)(a)(ii)(cc) should be changed to read:

   “as ***a capital asset or*** *as trading stock, where that person holds it as a capital asset and that company and that person do not form part of the same group of companies”* (suggested changes underlined in bold).

Section 42(6) – Asset-for-share transactions – Equity holding and engagement on a full time basis with the transferee (NEW)

Legal nature

488. Section 42(6) applies when:

- a person's equity holding falls to less than a 10% interest; or
- they cease to form part of the same group of companies (assuming one of those applied when section 42 was entered into), or
- if the person ceases to be engaged on a full-time basis with the company to which the asset was transferred (or a controlled group company of that company).

489. The effect of this provision is that the person is deemed to dispose of all the shares they hold in the company and they must then pay Capital Gains Tax (CGT) thereon, to the extent of the market value of the assets transferred at the time of the section 42 transaction, less the base cost, and to reacquire the shares at that market value.

Factual description

490. The issue arises due to the fact that the anti-avoidance provision is triggered if the individual took up full-time employment with the transferee company but did not rely on that fact to satisfy the requirements of section 42; relying rather on the qualifying interest criteria, or vice versa.

491. If that person ceases that full time employment but nevertheless retains qualifying interest by continuing to hold more than 10% of the equity shares and voting rights or, if applicable, through continuing to hold shares in a transferee that is a listed company, technically, the anti-avoidance provision is still triggered.

492. Similarly, if the person ceases to hold at least 10% of the shares and voting rights or to hold share in the listed company but continues to be fully employed for more than 18 months, the section will be triggered.

493. Despite the wording this cannot have been the intention as had the person have only relied on one of the criteria i.e. employment or qualifying interest, the section would have permitted deferral and the anti-avoidance provision would only have been triggered if that one criteria ceased to be met.

494. In short section 42(6) is triggered, despite the fact that it sets out alternatives, if both the qualifying interest and the employment requirements were satisfied when section 42 was entered into, but one ceases to be satisfied.

The nature of taxpayers impacted

495. All section 42 restructures where section 42(6) applies and specifically the person referred to in section 42(6).

Proposal

496. The law needs to make it clear that the anti-avoidance provision should be triggered only if neither requirement (i.e., qualifying interest and full-time employment) continue to be satisfied.

Section 42(1)(a)(ii)(cc) – Intragroup transactions *(submission originally made in 2020)*

Legal Nature

497. Section 42(1)(a)(ii)(cc) provides that the recipient company of the asset acquired in terms of a qualifying section 42 transaction will acquire it from the transferor "as trading stock, where that person holds it as a capital asset and that company and that person do not form part of the same group of companies".

498. This may be read in two ways:

1) That if the person and the company are not part of the same group of companies and the transferor held it as a capital asset the recipient company must acquire the asset as trading stock; or

2) That if the person and the company are not part of the same group of companies and the transferor held it as a capital asset the recipient company may acquire the asset as trading stock i.e. there is a choice. The explanatory memorandum indicates that the latter is intended.

Factual Description

499. The wording is imprecise and leaves taxpayers without certainty.

The nature of businesses impacted

500. All companies who have entered into a section 42 transaction with a person who is not part of their group of companies.

Proposal

80. It is suggested that the provision be amended to say (changes in italics):

"as a result of which that company acquires that asset from that person:

…or

(cc) where that person holds that asset as a capital asset and that company and that person do not form part of the same group of companies that company may elect to treat it as trading stock".

Section 42(6) – Asset-for-share transactions – further corporate restructures (NEW)

Legal nature

501. Section 42(6) is not triggered if the subsequent transaction is a section 45, 46, 47 or paragraph 65 transaction.

Factual description

502. The exclusions do not cover the position where the qualifying interest is lost due to a further section 42 or section 44.

503. However, Binding Private Rulings ("BPR") 159 and 231 indicate that this is acceptable to SARS where the shareholder of the liquidated company in the amalgamation acquires the shares previously subject to section 42.

504. BPRs cannot be applied by taxpayers who did not apply for the BPR.

The nature of taxpayers impacted

505. All parties to a s42 corporate restructure.

Proposal

506. The legislation needs to be changed to make it clear that section 42(6) will not be triggered if a further section 42 or a 44 transaction is entered into, and the qualifying interest requirement is fulfilled via the new shareholding.

Paragraph 43A of the Eighth Schedule – Dividends treated as proceeds on disposal of certain assets (NEW)

Legal nature of problem

507. During 2017, NT introduced anti-avoidance measures that targeted dividend stripping schemes which included certain share buy-back avoidance schemes. These measures countered the scenario where companies (taxpayers) were applying the exemptions provided in the ITA for corporate income tax when it came to the receipt of a local dividend and the exemption from dividends withholding tax when this dividend was distributed between companies.

508. Effectively Taxpayers took advantage of this opportunity to extract value from subsidiary (target) companies through the receipt of large tax-exempt dividends. The target company shares would then be subsequently sold at a significantly lower value (as the net asset value would be net of the pre-sale dividend), thus reducing the tax applicable to the shareholder on the sale of the target company's shares.

Factual description

509. An unintended consequence of these anti-avoidance measures arises where legitimate business transactions may be caught in the net cast by the definition of an extraordinary dividend (for example, the declaration of dividends to create cashflow for holding companies to service debt repayments or obligations).

510. We noted the following in respect of paragraph 43A:

511. Para (b) of the definition of "extraordinary dividend" is ambiguous as the introductory paragraph reference 'the amount of any dividend received or accrued.

512. Whilst the intention is that the amount of any dividend received or accrued should relate to dividends in respect of the share being disposed of, the wording can be read wider to include all dividends received or accrued from the company. The wording should reference to the dividend received or accrued in respect of "that share" to clearly highlight that the dividend which should be included in the computation of extraordinary dividend relates to a dividend received in respect of the share that is being disposed of.

513. Furthermore, the reference to "within a period of 18 months prior to the disposal of that share" in the paragraph requires clarification, i.e. does the quoted text provide that once a share is disposed of, all associated dividends linked to that share should no longer be considered for the definition of extraordinary dividend in future potential extraordinary dividend transactions.

Business/Persons impacted

514. Companies where dividends are being declared for legitimate business transactions.

Proposal

515. Consideration should be given to:

- Paragraph (b) of the definition should be amended to read as follows " *any other shares, means so much of the amount of any dividend received or accrued in respect of that share...*"

- Introducing exclusionary criteria in the paragraph to prevent legitimate business transactions from being caught in the net of the definition of extraordinary dividend. This can include, reference to funding requirements, where for example, the intention of the dividend was specifically to fund legitimate business transactions such as settling loan funding and related interest; these types of distributions should be excluded from the definition of extraordinary dividend to the extent that all other requirements of the paragraph is met; and furthermore; the reference to "within a period of 18 months prior to the disposal of that share" in the paragraph requires clarification, i.e. does the quoted text provide that once a share is disposed of, all associated dividends linked to that share should no longer be considered for the definition of extraordinary dividend in future potential extraordinary dividend transactions.

Paragraph 43A of the Eighth Schedule – Dividends treated as proceeds on disposal of certain assets *(submission originally made in 2021)*

Legal nature of problem

516. Paragraph 43A of the Eighth Schedule to the Income Tax Act, 1962 is an anti-avoidance provision providing that any exempt extra-ordinary dividend that is received by a corporate shareholder 18 months prior to the disposal of shares, or in regard to or in consequence of a disposal of shares, would be reclassified as income or proceeds for capital gains tax purposes.

Factual description

517. In terms of an amendment to paragraph 43A(2) of the Eighth Schedule to the Income Tax Act which is effective for transactions occurring on or after 20 February 2019, a dilution in the effective interest of a company in another company (target company) may give rise to a capital gain in the hands of the former company.

518. Paragraph 64B of the Eighth Schedule provides for a full exemption from CGT in the case of the disposal of qualifying equity shares in a foreign company to a non-SA resident.

519. To illustrate the interaction between these two sections, the following example is provided:

A South African company (SACo) has a wholly owned Namibian subsidiary (NamSub). As part of an empowerment transaction NamSub issues shares to Namibian residents thereby diluting the effective shareholding of SACo to say, 80%. Should SACo have earned 'extraordinary dividends', the company will be subject to CGT on the capital gain that will need to be accounted for in terms of paragraph 43A(2). Had SACo disposed of 20% of its shares in Namsub to the Namibian residents it would have enjoyed full exemption from CGT in terms of paragraph 64B.

Business/Persons impacted

520. SA Companies issuing shares in their controlled foreign companies to third parties as part of economic empowerment transactions.

Proposal

521. A carve-out should be included in paragraph 43A to provide that the treatment as a disposal set out para 43A(4) will not apply in circumstances where, had there been an actual disposal, the capital gain would have been disregarded in terms of paragraph 64B.

CATEGORY – INTERNATIONAL TAX

Sections 7(5), 7(8) and 31 – Low or interest-free loans to offshore trusts *(submission originally made in 2020)*

Legal Nature

522. Where there has been a low or no interest loan to an offshore trust both section 7(5) or section 7(8) and section 31 potentially apply. In relation to sections 7(5) and 7(8), it is unclear which section applies first if the loan is to a non-resident trust and there is a stipulation in the trust deed that denies any of the beneficiaries the income until the happening of an event, but either way there will be attribution of income received by the trust to the 'donor' to the extent of the interest not charged.

523. However, the effect of applying both sections 7(5) and 7(8) is to include an amount equal to the uncharged interest in the hands of the 'donor' twice. In practice, SARS does not apply both sections and only requires that the income not equal to the 'uncharged interest' be included once. It is left to the taxpayer to decide whether to include the amount of the attributed income or to include the uncharged interest based on the arm's length principle.

Factual Description

524. The law is not clear and should be amended to provide clarity.

The nature of businesses impacted

525. All persons who have made a low or interest-free loan to an offshore trust.

Proposal

526. Sections 7(5) and 7(8) should include a proviso that should a section 31 adjustment have been made the relevant provision will not be applicable.

527. Section 7(5) should be made applicable only to a resident recipient of the donation, settlement or other disposition in order to clarify that this section is not also applicable to donations to non-residents, which is covered by section 7(8).

Section 7(8) – Donation, settlement or other disposition to a non-resident *(submission originally made in 2020)*

Legal Nature

528. Section 7(8) deals with the position where a donation, settlement or other disposition has been made by a 'resident' to a non-resident entity.

Factual Description

529. Where a person made a donation, settlement or other disposition before becoming a South African tax resident the question arises whether the section 7(8) provisions apply to that same person after they become resident.

530. It should be noted that transfer pricing provisions would, in any event require an amount of deemed interest to be included in that person's income if there is a tax benefit, so this point and the point raised in the previous item mentioned above are linked.

The nature of businesses impacted

531. All persons who have made a low or interest-free loan to an offshore trust prior to becoming South African tax resident.

Proposal

532. Section 7(8) should be amended to clarify that it either applies to persons who made a donation, settlement or other disposition before becoming a South African resident or that it does not apply to such persons (as per the intention).

CATEGORY – VALUED ADDED TAX

Section 1 – Definition of "enterprise" *(submission originally made in 2021)*

Legal Nature

533. The exclusion in proviso (xiii) under the definition of "enterprise" in section 1(1) stipulates the circumstances under which a person that is neither a resident of the Republic, nor a registered vendor and that person supplies to a recipient solely the use or right of use of ships, aircraft and rolling stock under any rental agreement, will be deemed not to be the carrying on of an enterprise, despite that those goods are supplied for use in the Republic.

Factual description

534. The exclusion in proviso (xiii) under the definition of "enterprise" in section 1(1) is limited to only the supply of ships, aircraft and rolling stock.

The nature of taxpayers impacted

535. Persons who are neither a resident of the Republic, nor a registered vendor and that supply assets other than ships, aircraft and rolling stock but that otherwise comply with the requirements of the proviso.

Proposal

536. The exclusion in proviso (xiii) under the definition of "enterprise" in section 1(1) should be expanded to include supplies of all types of assets such as cranes, specialised equipment, heavy machinery etc.

537. There does not seem to be any reason as to why the type of asset supplied should determine whether an enterprise is carried on in SA or not.

Sections 8(23) and 11(2)(s) – Deemed supply to a National Housing Programme *(submission originally made in 2020)*

Legal Nature

538. Section 8(23) deems a supply of services to be made by a vendor to any public authority or municipality to the extent of any payment made to or on behalf of that vendor in terms of a national housing programme contemplated in the Housing Act, 1997 (Act No. 107 of 1997). Section 11(2)(s) zero rates these services.

Factual Description

539. Section 8(23) seems to envisage a single grant recipient who will receive the funding and will be able to apply the zero-rating. Therefore, any disbursements of the funding to other entities (excluding non-profit company (NPC) to NPC transactions which need to be considered separately), will not be able to apply the zero-rating.

540. For example, a developer assists a NPC with the construction of social housing units. The NPC's aims and objectives are to provide low cost housing to the needy. With this particular development, the NPC provides low cost renting of units to the needy. To fund the development costs, the NPC obtained a grant from the Social Housing Regulatory Authority and obtained debt funding. As the zero-rating will not extend to the developer, the developer will need to charge VAT on its development services to the NPC. The NPC, however, will not be able to claim the input tax deduction as arguably, these costs have been incurred for the purposes of making exempt supplies (i.e. the rental of housing units).

541. Hence, the grant funding received by the NPC will need to be consumed to pay the VAT or the NPC will have to source additional debt funding to cover these costs. It puts the NPC in a difficult position and in some cases, the unintended VAT cost jeopardizes the viability of the project which in turn has a ripple effect on the persons who are in desperate need of receiving the low cost housing.

542. Sections 8(23) and 11(2)(s) were to be deleted with effect from 1 April 2017. However, it subsequently became evident that both National Treasury and municipalities were not ready to implement the amendments that would have the effect that the national housing programme payments would be standard-rated.

543. National Treasury, therefore, proposed during 2017 that the effective date of the repeal of the zero-rating be postponed for two years until 1 April 2019.

544. However, this proposal to postpone the effective date of the deletion of sections 8(23) and 11(2)(s) was not enacted.

545. Therefore, section 8(23) and s 11(2)(s) were reinserted with effect from 1 April 2017, based on the same wording which came into effect on 1 April 2011, except that the requirement that the national housing programme must have been approved by the Minister by regulation after consultation with the Minister responsible for Human Settlements was not re-enacted.

546. Further, it is worth noting that prior to 1 April 2011, section 8(23) applied only to the extent that taxable supplies would be made, which meant that houses built for letting purposes did not qualify for the zero rate. As the reference to 'taxable supplies' has been deleted, it would appear that houses built for letting purposes also qualify for the zero rate. In the 2019 Budget Speech, an amendment was to be proposed to clarify the VAT treatment of payments relating to rental stock in terms of the National Housing Programme, however, no clarity has yet been provided.

547. The strict application of the provisions of the ITA (including s11(2)(s)) has led to many housing projects not being viable and have in some instances forced local businesses to liquidate. National Treasury has been approached about this concern but there has been no traction. The only remaining option for taxpayers is to go to Court.

The nature of businesses impacted

548. All vendors that supply services to any public authority or municipality to the extent that any payment is made to or on behalf of that vendor in terms of a national housing programme contemplated in the Housing Act.

Proposal

549. We recommend that National Treasury urgently provide clarity on this matter.

550. Should it be decided that these sections are to be deleted, we would recommend that National Treasury provide alternative mechanisms to ensure that projects of this nature are viable for the implementing parties.

Section 14(1) – Timing of VAT on imported services *(submission originally made in 2022)*

Legal Nature

551. In terms of section 14(1) and 14(2), VAT should be accounted for and is payable by the recipient of imported services in terms of s7(1)(c), within 30 days of the earlier of receipt of the invoice issued by the supplier or the time any payment is made by the recipient in respect of that supply.

Factual description

552. In many instances it is practically impossible to comply with the 30-day time period and this has further apportionment implications. Failure to pay the VAT within this timeframe will result in the imposition of penalties and interest at the prescribed rate.

553. The payment and filing/ declaring within 30 days are impractical and extremely short for most organisations to process. The short filing and payment deadlines, combined with the strict penalty regime for not declaring and paying timely returns, creates additional pressure on businesses attempting to comply as they may face challenges collating all the required information for filing accurate returns within the time allowed.

554. Furthermore, stringent controls are put in place by organisations to ensure that VAT on imported services is applicable. Such invoices are analysed on a case-by-case basis to determine firstly whether these services are used and consumed in the Republic. Generally, the business unit procuring such services must be consulted to determine this factual question. Thereafter, the relevant CFO or tax division needs to analyse whether these are being used otherwise than for the purpose of making taxable supplies.

555. Foreign suppliers of services often charge South Africa vendors in a currency (transaction currency) that is different from the taxing jurisdiction i.e., the ZAR currency. However, the VAT return must be submitted and paid for in ZAR and therefore the currency must be converted from the transaction currency to the reporting currency. It is acceptable to the Commissioner of South African Revenue Service to use one of the following options to determine the rand equivalent of the consideration for the supply:

555.1 The daily exchange rate on the date the time of supply occurs.

555.2 The daily exchange rate on the last day of the month preceding the time of supply.
555.3 The monthly average rate for the month preceding the month during which the time of supply occurs.
555.4 This process further adds to the processing time of the transaction.

556. The calculation of the 30 days from the time of supply i.e., the date the invoice is being issued is also unclear. When is an invoice issued? "Issued" means supplied or delivered – does this then mean that the 30 days is calculated from the date of the invoice or when the invoice is received by the relevant party?

557. With so many stringent controls and processes involved the timing rule of within 30 days is challenging and impractical.

558. Many international jurisdictions also face the similar issues, and the filing period varies among countries from monthly (e.g., South Africa), bi-monthly (e.g., Iceland), quarterly (e.g., New Zealand, Norway, European Union), or semi-annually (e.g., Japan).

<u>The nature of taxpayers impacted</u>

559. Vendors that import services.

<u>Proposal</u>

560. In keeping with international best practice and to address this concern, section 14(2) should be revised/amended to extend the 30 days' to 60 days or to allow the VAT on imported services to be accounted for on a payment basis as the appropriate time for vendors to process the necessary payment.

Section 15 – Accounting basis – cash basis for SMEs *(submission originally made in 2022)*

<u>Legal Nature</u>

561. Section 15(1) directs that vendors account for VAT on the invoice basis, while section 15(2) provides for an exception to this rule, allowing specific vendors the option of accounting for VAT on the payments basis. This group of vendors includes natural persons with taxable supplies of less than R2.5 million during the preceding (or coming) 12 months [section 15(2)(*b*)].

<u>Factual Description</u>

562. The below extract from the SARS VAT404 Guide provides some well-known reasons for this concession by government:

A few advantages and disadvantages of the payments basis of accounting are set out in the table below.

563.

Advantages	Disadvantages
• Suitable for small businesses. • Advantageous when the vendor allows lengthy periods of credit. • Facilitates cash flow.	• May deduct VAT only after payments made to suppliers. • More difficult to implement accounting systems to manage, administer and calculate accurately (for example, reconciliation with income tax returns and adjustments).

564. The above shows government's awareness of the cash flow difficulties faced by small businesses, which are partially caused by the fact that they are often paid months after invoicing customers. Some of these customers include government departments, municipalities and state-owned entities[12].

565. These businesses are often placed in the very unfortunate position of having to choose between tax compliance and paying their overhead expenses, which are often "more pressing" as failure to settle these may threaten the very existence of these businesses.

566. With the success rate of small businesses currently being as low as it is, it is incumbent on government to provide the necessary assistance needed to address some of the difficulties faced by the small business sector, since it is well recognized that this sector is crucial to the economic success of any nation.

567. Though some small businesses may choose to trade as sole proprietorships, many others choose to trade as juristic persons.

568. Through the insertion of section 15(2)(*a*)(viiii) into the VAT Act[13], the legislature has previously shown that it is willing and able to aid a business' VAT-related cash flow constraints by extending the payments basis to include the South African Broadcasting Corporation (SABC).

569. The Explanatory Memorandum on the Taxation Laws Amendment Bill, 2015[14] noted the following in this regard:

570. *Under normal VAT rules, the SABC should account for output tax on the earlier of an issued invoice (i.e. on issued TV license notices) or payment made for the supply. However, there is a high level of non-payment of TV license fees by television owners.*

12 https://www.dpme.gov.za/publications/Reports%20and%20Other%20Information%20Products/70008-20200630%20Research%20on%20Late%20Payment%20of%20SMMEs%20V03.pdf

13 Taxation Laws Amendment Act No. 25 of 2015

14 https://www.sars.gov.za/wp-content/uploads/Legal/ExplMemo/LAPD-LPrep-EM-2015-01-Explanatory-Memorandum-on-the-TLA-Bill-29-of-2015.pdf

The VAT requirement to account for output tax on an invoice basis on the revenue it might not be able to collect, <u>places a significant financial constraint on the SABC</u>.

571. If a multi-billion rand corporation can be strained by habitual and known late payments, the impact on SME's is much greater. Extending the payments basis to the rest of the small business sector would be keeping in line with this legislative sentiment.

<u>The nature of taxpayers impacted</u>

572. Small businesses trading as juristic persons.

<u>Proposal</u>

573. Section 15(2) should be amended to include juristic persons with taxable supplies not exceeding R5 million. Extending the payments basis to juristic persons will provide parity with natural persons.

574. A concomitant amendment may also be necessary to s15(2A)(iii) as the continued rationale of the per invoice limit seems to have disappeared as reflected in the removal of various local government and entities from this requirement. There is also already a total annual supply limitation. To add to this challenge, the R100 000 per invoice limit has not been amended **since its insertion in 1997**. It is proposed that it be deleted or at least significantly increased.

<u>Section 23 – VAT registration threshold</u> *(submission originally made in 2020)*

<u>Legal Nature</u>

575. Section 23 currently requires a taxpayer to register for VAT when its taxable supplies exceed R1 million.

<u>Factual Description</u>

576. This threshold was last changed on 1 March 2009 from R300 000 to R1 million. If this amount was changed annually in line with inflation the threshold would have increased to an amount in the region of R1.8 million.

577. For a professional practice with an annual turnover of R1 million, fees would need to be increased by 15% to cater for VAT which in the current economic climate could result in a significant loss of clients who might not be able to pay the fees charged. Alternatively, if fees were maintained at the same level, the professional practice would suffer a direct loss of annual income of R130 434 at a rate of 15/115, less inputs claimable.

578. However, a professional practice is unlikely to have much in the way of VAT inputs to counter the VAT outputs. In addition, there is a significant administrative burden in completing VAT returns for a small business/professional practice.

<u>The nature of businesses impacted</u>

579. All small businesses but specifically businesses rendering services, with taxable supplies above R1 million per annum.

Proposal

580. In the current economic climate where small businesses and professional practices are struggling to survive, it appears that an adjustment to the VAT threshold is urgently needed. It is suggested that the threshold be increased to R1.8m as a minimum.

Section 51 – Bodies of persons, corporate or unincorporated *(submission originally made in 2022)*

Legal Nature

581. This section applies *inter alia* where immovable property is owned by co-owners who are not in partnership, but who nevertheless constitute a "body of persons".

582. The co-ownership is deemed to be a separate person from its members for purposes of the Act, even though legally this is not the case.

Factual Description

583. There are significant anomalies and difficulties with the above treatment, especially where the co-owners are themselves vendors and have claimed input tax on the acquisition or construction of the property, and yet the co-ownership is the VAT vendor letting the property. There are a number of unsatisfactory methods of dealing with these issues to try and mitigate any unnecessary VAT leakage.

584. Moreover, if one of the co-owners is not a VAT vendor and disposes of its interest, despite the fact that the co-ownership is a registered enterprise, the transfer of the undivided interest in the property by the co-owner triggers transfer duty in the hands of the acquirer, and yet there is no mechanism for this transfer duty to be offset against any VAT payable, either by the acquirer or by the co-owners.

The nature of taxpayers impacted

585. Co-owners in a property who are not in partnership, but who nevertheless constitute a "body of persons".

Proposal

586. Given the widespread use of co-ownerships in the property industry, and the complete lack of standardisation as to how they are treated, this matter needs reconsideration either in the form of a redraft of the legislation (which is preferable) or at least by the issue of a binding general ruling which deals with these anomalies and difficulties.

Section 54 – VAT for agents acting on behalf of foreign principals *(submission originally made in 2022)*

Legal Nature

587. Section 54(2A)(b), 8(20), 9(9) and section 10(22B) deal with the VAT implications for agents acting on behalf of foreign principals.

Factual description

588. Section 54(2A)(b) provides that where goods are imported into the Republic by an agent (acting on behalf of a principal who is not a resident and not a registered vendor) and the supply is made to a person in the Republic, the importation is deemed to be made by such agent. This is only the case if, inter alia, the agent paid the import tax and this tax will not be reimbursed to such agent by the principal.

589. Section 8(20) further stipulates that in these circumstances the agent is deemed to make a supply of the goods to the recipient of the supply by the principal.

590. It appears that the agent in these circumstances is out of pocket for the 'new' VAT on the supply to the person in the Republic (not the import VAT). Similar provisions are contained in the Electronic Services Regulations, but these Regulations allow the agent to claim the VAT back. The agent not being able to claim the VAT back in the section 54(2A)(b) import situations could make South Africa less competitive.

The nature of taxpayers impacted

591. Agents acting on behalf of foreign principals.

Proposal

592. Agents in these circumstances should be allowed to claim the VAT back.

Electronic Service regulations *(submission originally made in 2020)*

Legal Nature

593. Revised regulations to prescribe and clarify the VAT treatment of electronic services (e-services) supplied by foreign suppliers to South African consumers came into effect in South Africa from 1 April 2019. These regulations require foreign electronic service providers supplying "electronic services" to qualifying South African recipients to register for VAT in South Africa and these regulations significantly broadened the scope of "e-services".

594. The new definition of "electronic services" is extremely wide and leaves many foreign suppliers uncertain whether they are required to register for VAT or not. SARS published an explanatory memorandum and a document setting out answers to frequently asked questions (FAQs) that provide some guidance on how to apply VAT in the case of non-resident suppliers of electronic services in South Africa.

595. Section 54(2B) of the VAT Act, which became effective from 1 April 2019, allows a non-resident supplier of electronic services to appoint an intermediary VAT vendor in South Africa to act on its behalf. That is, the foreign entity would supply the electronic service to the South African intermediary which would be regarded as making the supply to residents and not the foreign entity principal.

Factual Description

596. The electronic services regulations require some clarity especially regarding imported services, compulsory VAT application rules and exceptions to registration for single transactions.

597. Despite SARS issuing a FAQ document, it is still unclear whether information or advice which is communicated via an e-mail transmitted electronically falls within the ambit of the regulation. “Electronic communication” is defined in the Electronic Communications and Transaction Act 25 of 2002 to mean ‘a communication by means of data messages’, and “data messages” is defined to mean ‘data generated, sent, received or stored by electronic means’.

598. On the face of it, it seems that information or advice communicated via e-mail will therefore fall within the scope of e-services. The Explanatory Memorandum stipulates, however, that one of the policy intentions behind the amendments is to subject to VAT those services that are provided using minimal human intervention. It provides as an example that legal advice prepared outside of South Africa by a non-resident and sent to a recipient in South Africa via e-mail will not be subject to the regulations.

599. Notwithstanding the statement made in the Explanatory Memorandum, it has to be borne in mind that the Explanatory Memorandum does not have any legal status and limited interpretative persuasion. National Treasury should preferably clarify and confirm this policy intention by requesting SARS to issue a binding general ruling so as to avoid any future disputes in this regard.

600. Furthermore, section 54(2B) only allows for an intermediary who acts on behalf of a non-resident electronic services supplier, being the principal, who is <u>not a registered vendor</u>, to account for VAT on behalf of that principal. As it is unlikely that non-resident suppliers of electronic services who are not liable to register for VAT in South Africa will require the services of an intermediary to supply their electronic services to recipients in South Africa, as the cost of the intermediary services will render these supplies uneconomical, this requirement makes the provisions regarding intermediaries superfluous.

The nature of businesses impacted

601. All foreign suppliers of electronic services in South Africa.

Proposal

602. The electronic services regulations should provide further clarity on the matters mentioned above and the FAQ document should have the status of a binding ruling.

603. We also recommend that section 54(2B)(ii) of the VAT Act be amended to delete the requirement that an intermediary may only account for VAT on behalf of a <u>non-registered</u> supplier of electronic services, but that it be allowed to account for VAT on behalf of all non-resident suppliers of electronic services.

CATEGORY – TAX ADMINISTRATION ACT (TAA)

Legal Professional Privilege for Tax Practitioners *(submission originally made in 2022)*

Legal Nature

604. In 2019 SAICA made a substantive submission on why legal professional privilege (LPP) should be granted to Registered Tax Practitioners and why the UK *Prudential* case was not good authority to ignore the principle.

605. Currently clients of registered tax practitioners have no LPP including when such clients are represented in legal forums such as the Tax Board and the Tax Court by persons who are not registered legal practitioners.

Factual description

606. At the 3 November 2022 Treasury and SARS engagement this matter was again raised.

607. SARS confirmed that it did note to tax practitioners that it would consider LPP for tax practitioners once regulation was implemented but had envisaged statutory regulation as proposed in the Tax Practitioners Regulation Bill 2008.

608. It must be emphasised that the current regulatory model exceeds what is commonly understood as fully regulated as stated in SARS 2003 Discussion Document referencing the Australian and German models, given that only the SA model puts the revenue authority as the de facto regulator with an open ended discretion of matters to regulate.

609. SARS however also conceded that there were certain valid legal concerns raised as pertains litigation privilege and tax practitioners being unable to represent their taxpayer clients in confidence without their conversations and consultations being privileged. As noted and acknowledged by SARS, even the perception of such lack of confidentially creates the risk that a client will not fully and frankly disclose matters to the tax practitioner and therefore proper advice cannot be provided.

610. Though SARS has clarified that full LPP would be contingent on a statutory regulatory regime, which could happen in future, some intervention was required. SARS has recently proposed that a regime similar to the Australian Tax Authorities Accountants Concession be considered[15] though that only addresses certain advice privilege, rather than taxpayers legally entrenched rights to litigation privilege.

The nature of taxpayers impacted

611. Clients of registered tax practitioners seeking professional advice on disputes and certain other processes such as VDP (Chapter 16 Part B) and compromise applications (Chapter 14 Part D).

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[15] https://www.ato.gov.au/about-ato/commitments-and-reporting/in-detail/privacy-and-information-gathering/our-approach-to-information-gathering/?page=51

Proposal

612. It is proposed that full LPP be provided in respect of all client and tax practitioner consultations and correspondences relating to processes envisaged under Chapter 9 TAA i.e. tax disputes with SARS, VDP applications (Chapter 16 Part B) and Compromise applications (Chapter 14 Part D).

613. It is further proposed that the documents, advice and information set out in the ATO Accountants Concession as "Restricted" and "Non-source" documents be considered and codified in the TAA or some other binding legal instrument (e.g. public notice).

Section 5 &16 – Original law in amendment acts (NEW)

Legal Nature

614. The "consolidated law" of the Tax Acts is the original Act read with each amendment Act issued thereafter.

615. However, from a practical perspective, to enable the public to more easily use the Tax Acts, publishers "amend" the original Act by inserting the amendments to that particular Tax Act into the original Act as replacement or new legislation. Sometimes the original legislation is, for whatever reason, put in the amendment Act and not as an amendment, repeal or insertion into the original Act.

616. This was done with section 1 & 2 of the Taxation Laws Amendment Act, 2012 (TALAA 2012) regarding International Agreements and the Tax Ombud's role in addressing complaints relating to certain customs matters.

Factual Description

617. Where the legislator does not amend or insert the new provisions of the legislation in the original legislation (i.e. the TAA) but as original legislation in the amendment Act, it makes it difficult for publisher to insert it into the consolidated text.

618. This legislative style undermines what the creation of the TAA sought to achieve, namely an easily readable and consolidated Tax Administration Act that follows the logical life cycle of the taxpayer.

The nature of taxpayers impacted

619. All taxpayers, politicians and academics as users of legislation published by publishers.

Proposal

620. Section 1 and 2 of the TALAA 2012 should be amended retrospectively and become insertions of new sections in the TAA.

621. It is proposed that section 1 of the TALAA 2012 be inserted as a new section 5A of the TAA given that it is dealing with a general matter applicable to the whole TAA.

622. It is also proposed that section 2 of the TALAA 2012 be inserted as section 16(2A) of TAA given it relates to the mandate of the Office of the Tax Ombud.

Section 18(6) – Review of complaint received by the OTO *(submission originally made in 2020)*

Legal Nature

623. Section 18(6) of the TAA provides that the Office of the Tax Ombud (OTO) “must inform the requester of the results of the review or any action taken in response to the request, but at the time and in the manner chosen by the Tax Ombud”.

Factual Description

624. Whilst we understand the limitations on the OTO due to capacity issues, from a taxpayer perspective, there is a need for certainty in terms of when the taxpayer can expect feedback on a matter lodged for review with the OTO.

625. Furthermore, where the taxpayer has taken further action on the matter - for example, if the taxpayer chooses to refer the matter to Tax Court - the feedback from the OTO will be important in the considerations of that process.

626. We also understand that where recommendations are made to SARS by the OTO, these first have to be reviewed by SARS before being sent to the taxpayer, resulting in further delays in communication to the taxpayer.

627. It should be noted that at the point a complaint is lodged by the taxpayer with the OTO, SARS would have had 2-3 internal reviews and weeks or even months to have reconsidered the matter. Time for SARS to respond should therefore not be an issue as the matter should have been well ventilated and documented internally at SARS.

The nature of businesses impacted

628. Taxpayer submitting complaints to the OTO.

Proposal

629. The OTO should be required to provide feedback on the outcome on matters submitted by taxpayers for review within 30 days from the date of the complaint. Similarly, notwithstanding the MoU between SARS and the OTO, SARS should be compelled to respond to the OTO within 14 days to enable the OTO to respond.

630. When the OTO submits its recommendations to SARS, the same should be sent to the taxpayer, despite the fact that SARS is not compelled to accept the recommendations. This would assist the taxpayer in determining whether it would be worthwhile to await SARS response or seek further legal recourse.

Section 20(2) – Resolutions and recommendations by the OTO *(submission originally made in 2020)*

Legal Nature

631. In terms of section 20(2) of the TAA, recommendations made by the OTO after reviewing matters lodged by taxpayers, are not binding on the taxpayer or SARS. If SARS, for example, rejects a recommendation, SARS must communicate reasons for this decision to the OTO, within 30 days of the recommendation.

632. Whilst the legislature has already affirmed the policy that there should be more transparency and accountability when it comes to the OTO recommendations, there seems to be a technical oversight that there is no express compulsion/prohibition to supply the SARS reasons to the complainant taxpayer or the taxpayer's rejection of the OTO's recommendation to SARS, though the OTO has a discretion on the latter.

633. It therefore in practice seems that OTO is afforded a discretion as there is no express prohibition to such disclosure though this discretion does not seem intended given the policy on transparency and administrative fairness adopted by the legislature and does not seem to align to the policy.

634. Once the OTO notes that SARS has not accepted a recommendation and provided reasons, those reasons are the basis on which the taxpayer would have to consider whether further actions are justifiable. Withholding such reasons from the complainant who should be the person to whom disclosure is made undermines the transparency and efficiency of the escalation system,

Factual Description

635. Where a taxpayer has lodged a complaint with the OTO and the OTO has made recommendations to SARS which recommendations SARS does not accept, the OTO merely responds to the taxpayer that SARS has not accepted the recommendations and the OTO cannot further assist the taxpayer.

636. The OTO will merely disclose what their recommendations were but we also understand that where recommendations are made to SARS by the OTO, these first have to be reviewed by SARS before being sent to the taxpayer, resulting in further delays in communication to the taxpayer. In many instances this just compounds the injustice suffered by the taxpayer.

637. In this instance, not only is the taxpayer no further in resolving the matter and will have no recourse other than litigation, but the taxpayer also has no understanding as to why, if the OTO made a favourable recommendation, SARS has refused to implement such recommendation to create fair administrative action.

638. The taxpayer as the complainant, is now forced to either compel disclosure by the OTO through a PAIA request or court litigation just to be informed of the reasons why SARS will not take corrective action directly affecting the taxpayer.

639. Whilst the OTO may include SARS' reasons in its report to the Minister of Finance, there is no other recourse for taxpayers to know why these recommendations were not accepted by SARS, nor is the taxpayer afforded the opportunity to reject the OTO's recommendations made to SARS.

640. There also appear to be no timelines contained in the law within which SARS must implement recommendations made by the OTO where these recommendations have been accepted by SARS. In practice such implementation may therefore even take years.

The nature of businesses impacted

641. All taxpayers that have lodged complaints with the OTO.

Proposal

642. Where the recommendation by the OTO relates to a **specific taxpayer**, the OTO should communicate to the taxpayer with 7 days after receipt from SARS, SARS' reasons for not accepting the recommendation.

643. Where the recommendations relate to the outcome of a **systemic investigation**, the OTO should communicate to the public in the OTO's annual report, SARS' reasons for not accepting recommendations made by the OTO in this regard.

644. Where SARS accepts the recommendations made by the OTO, such recommendations must be implemented by SARS within 90 business days (systemic issues) or 30 days (taxpayer specific issues) of receiving the recommendations unless SARS can provide **compelling reasons** why it is unable to do so and must provide the time period in which it believes it will be able to comply to the OTO.

Section 42 – Keeping the taxpayer informed (verifications) *(submission originally made in 2020)*

Legal Nature

645. Where a SARS official is involved in or responsible for an audit, section 42(2)(b) of the TAA requires that SARS, upon conclusion of the audit in the instance where the audit identified potential adjustments of a material nature, must provide the taxpayer with a document containing the outcome of the audit including the grounds for the proposed assessment.

646. Upon receipt of such document, the taxpayer must respond in writing within a period of 21 days from the delivery of the document by SARS to the facts and conclusions set out in SARS' document.

647. Though the heading of Chapter 5 of the TAA refers to a process called "verification" as information gathering process, nowhere in the TAA is there a defined procedure for this process notwithstanding that there is one for all four other stated processes namely audit, request for relevant information, inspection and criminal investigations.

648. Furthermore, a problem is that the term "audit" is defined neither in section 42 nor in section 1 of the TAA with the resultant ambiguity whether the "verification" procedures, which are nearly the same as an audit, performed by SARS in respect of a taxpayer's return, are subject to section 42 of the TAA or not, given the ordinary meaning of the term "audit" being "a systematic review or assessment of something".

Factual Description

649. SARS in numerous instances, particularly with regard to individuals, notifies taxpayers of a "verification" of the taxpayer's return following submission of that return.

650. The "verification" process usually involves the taxpayer having to submit to SARS extensive supporting documentation in respect of the amounts and disclosures contained in the tax return.

651. Following submission of the documentation:

651.1 Where relevant, SARS compares this to information to that which it obtains from external sources (IRP5 submissions by employers, IT3b submissions by financial institutions etc.);

651.2 Where relevant, SARS raises queries or requests for further information particularly in the case of an individual who carries on a trade in his/her personal capacity such as the letting of a property or the carrying on of a business.

652. Following its "verification" procedures, SARS will often raise an additional assessment without providing the reasons for the additional assessment or affording the taxpayer the opportunity to respond to the conclusions reached by SARS upon completion of their procedures. Such an approach is in conflict to the process set out in section 42 of the TAA.

653. The manner in which SARS raises additional assessments without providing the taxpayers with reasons therefore and an opportunity to make a submission to refute the SARS' grounds of additional assessment prior to the assessment being raised by SARS is also in conflict with the Supreme Court of Appeal judgment in SARS v Pretoria East Motors (Pty) Ltd (291/12) [2014] ZASCA 91 delivered on 12 June 2014 where the learned judge at paragraph [11] said as follows:

"As best as can be discerned, [SARS's] approach was that if [it] did not understand something [it] was free to raise an additional assessment and leave it to the taxpayer to prove in due course at the hearing before the Tax Court that she was wrong. [This] approach was fallacious. The raising of an additional assessment must be based on proper grounds for believing that, in the case of VAT, there has been an under declaration of supplies and hence of output tax, or an unjustified deduction of input tax. In the case of income tax it must be based on proper grounds for believing that there is undeclared income or a claim for a deduction or allowance that is unjustified. It is only in this way that SARS can engage the taxpayer in an administratively fair manner, as it is obliged to do. It is also the only basis upon which it can, as it must, provide

grounds for raising the assessment to which the taxpayer must then respond by demonstrating that the assessment is wrong. This erroneous approach led to an inability on [SARS's] part to explain the basis for some of the additional assessments and an inability in some instances to produce the source of some of the figures [it] had used in making the assessments." [our insertions]

654. Furthermore, verifications are also used by SARS to delay refund payments, however, without a similar feedback mechanism with timelines and outcomes as in section 42.

655. If SARS followed due process for verifications similar to section 42 of the TAA, the number of disputed assessments which is a time consuming and expensive process for taxpayers and SARS alike, would reduce dramatically.

656. SARS has now on its website added the following definition of verification[16]:

What is verification?

Verification is a face-value verification of the information declared by the taxpayer on the declaration or in a return. This involves a comparison of this information against third party data gathered by SARS from various sources, the financial and accounting records and/or other supporting documents provided by taxpayers to ensure that the declaration/return is a fair and accurate representation of the taxpayer's tax position. Once you have submitted your declaration/return, your declaration/return could be selected for verification.

The nature of businesses impacted

657. All taxpayers subject to SARS' verification procedures.

Proposal

658. A new section or a sub-section of section 42 should be inserted into the TAA to define what constitutes a "verification" performed by SARS and how it is to be conducted by them and it should also include the checks and balances to ensure that SARS adheres to an administratively fair process during the verification process.

659. Given that SARS has since September 2021 added a definition of verification and seems quite capable of defining and distinguishing verification from audit, it is merely prudent that a definition and corresponding process and procedure is added into the TAA to fill the current legal vacuum.

[16] Being Audited or Selected for Verification – South African Revenue Service (sars.gov.za)

<u>Section 89 – Binding private rulings</u> *(submission originally made in 2020)*

<u>Legal Nature</u>

660. The overall object of a binding private ruling (BPR) is to allow SARS to provide individual taxpayers or "classes" of taxpayers with its views in relation to transactions or facts that are specific to them only.

661. A ruling, therefore, serves to provide guidance as to SARS's views on certain transactions before entering into them and therefore serves to mitigate the risks of proposed transactions.

<u>Factual Description</u>

662. Rulings are generally requested in order to obtain certainty for tax return purposes but also to ensure that the tax implications are not a deal-breaker in relation to a specific transaction/contract. In terms of the SARS Comprehensive Guide to Advance Tax Rulings, "*a binding ruling application can only be accepted if the proposed transaction to which the interpretation is to apply will be concluded in the future. There is no exception to this rule*". It also states that "*there is no express statutory requirement that the proposed transaction may not be entered into before the ruling is issued, but it is arguably the implication*". Thus, these BPRs have to be obtained in advance of any contract being signed or return being submitted.

663. In practice, obtaining a BPR for many transactions is inefficient as it currently takes too long to receive the ruling. In many instances, the BPR application is made and the transaction cannot proceed until the BPR is issued, which is detrimental to transactions and their implementation processes to ensure that they are fulfilled timeously (which often has commercial impacts if delayed).

664. Sometimes the BPR outcome will be a deal-breaker but more often than not the transaction may proceed regardless of the outcome of the ruling. However, the taxpayer wants certainty regarding the tax return treatment so as not to expose the transaction to penalties and interest.

<u>The nature of businesses impacted</u>

665. All businesses applying for BPRs.

<u>Proposal</u>

666. Once SARS has agreed that the matter is accepted for purposes of a BPR, the BPR must be issued within 90 days of the notification to the taxpayer that the matter was accepted for issuing a ruling.

Sections 93(1)(a) & 99(2)(d) TAA – Period of limitations for issuance of assessments (NEW)

Legal Nature

667. SARS can issue an additional or reduced assessments between 3 and 5 years after an assessment or self- assessment, respectively.

668. The TAA sets out in a logical manner that assessments for subsequent years will follow each other in sequence. This sequence can be interrupted should SARS or the taxpayer successfully dispute an assessment, since all amounts that impact an assessment in sequence in the following year are impacted, e.g. the balance of the assessed loss or capital loss or allowances that are deducted in one year and carried back the following year. It can also be that tax returns are submitted out of sequence.

669. Where all the impacted assessments have not prescribed, this can be remedied by SARS reissuing all the impacted assessments in the correct sequence with the correct carry-forward and carry-back amounts.

Factual Description

670. However, where all or some of the assessments have prescribed, the TAA does unfortunately not properly cater for this, as SARS correctly argued in the recent High Court case of ***I-Cat International Consulting (Pty) Ltd v Commissioner for The South African Revenue Service*** (41667/2021) [2023] ZAGPPHC 268; [2023] 3 All SA 154 (GP) (24 April 2023).

671. This is also an issue if, for example, a dispute occurs in year 1, which takes 6 years to resolve, and then impacts the amounts in year 2. In such a case, neither SARS nor the taxpayer can dispute year 2 before the year 1 dispute is resolved.

672. This is neither party's fault, but an inherent problem with the TAA.

673. Following the judgment in I-Cat, a taxpayer or SARS would have to specifically include ALL of the following prescribed years in a compromise or in the heads of argument before a court on appeal, to ensure that SARS is enabled to make the relevant adjustments in the subsequent assessments following the year of assessment in dispute.

The nature of taxpayers impacted

674. SARS and taxpayers in dispute in relation to assessments where the subsequent periods are prescribed or become prescribed while the dispute is being finalized, and the subsequent periods' tax payable/refundable or carry forward of balances will be impacted by the outcome of the prior year's dispute.

Proposal

675. Sections 93(1)(a) and 99(2)(d) of the TAA should be expanded and clarified to confirm and enable SARS' to amend subsequent years of assessments impacted by the amendment of an assessment in a previous year where such subsequent assessments

are not prescribed (s93) or when those assessments are prescribed (s99) even if those assessment were not directly in dispute.

Section 96 – Notice of assessment *(submission originally made in 2021)*

Legal Nature

676. SAICA welcomes initiatives that makes it easier to comply with tax obligations.

677. SARS issues automated assessments to certain taxpayers based on data it receives from employers, financial institutions, medical schemes, retirement annuity fund administrators and other third-party data providers to create auto-assessments.

678. Taxpayers receive an SMS indicating that they have been auto assessed with a link to the e-filing website or SARS Mobi-app. Once taxpayers have clicked on the link, they can review the auto-assessment and choose to accept it or choose to edit the assessment. Should they fail to respond to the auto-assessment, SARS will make an estimated assessment based on the data at SARS' disposal.

Factual Description

679. Not accepting or responding to the auto-assessment, could result in taxpayers missing out on allowable deductions and refunds or could result in taxpayers omitting additional income (such as capital gains, foreign investment income etc) and then being subject to penalties and interest.

680. Chapter 8 of the TAA deals with assessments, however, the issuing of automated assessments is not legislated for in the TAA.

681. Section 96 of the TAA deals with notice of assessments, and section 96(2) states that SARS must give the person assessed in the case of an estimated or an assessment not fully based on a return submitted by the taxpayer, a statement of the ground for the assessment.

682. This does not occur when issuing automated assessments.

The nature of taxpayers impacted

683. Taxpayers receiving auto-assessments.

Proposal

684. Chapter 8 of the TAA should incorporate the issuing of auto-assessments by SARS and stipulate SARS' as well as the taxpayers' responsibilities in this regard.

Section 98 – Withdrawal of assessments *(submission originally made in 2021)*

Legal nature of the problem

685. The withdrawal of assessment provisions in section 98 of the TAA are too narrow in their application.

Detailed factual description

686. Section 98 of the TAA provides very limited circumstances under which SARS may withdraw an assessment despite the fact that no objection or appeal has been lodged by the taxpayer.

687. These include assessment issued to the incorrect taxpayer or in respect of the incorrect tax period or incorrect payment allocation.

688. Circumstances may arise where SARS raises a blatantly incorrect assessment either because it does so based on incorrect facts or a misunderstanding of facts, the incorrect application of law, or because it hasn't followed proper administrative procedure as laid out in the TAA and various court judgments.

Nature of the business / persons impacted

689. All taxpayers issued with blatantly incorrect assessments by SARS.

Proposal

690. A taxpayer should be allowed to request SARS, and SARS should be permitted, to withdraw a blatantly incorrect assessment in any of the aforementioned circumstances as it allows SARS to perform its duties more efficiently without a long and protracted dispute resolution process which absorbs unnecessary time and resources on the part of both SARS and taxpayers.

Section 104 – Grounds to object *(submission originally made in 2020)*

Legal Nature

691. In the *Barnard Labuschagne Inc v South African Revenue Service and Another 2020 ZAWCHC* (15 May 2020) case, the taxpayer (Barnard Labuschagne Inc), sought to rescind a statement filed by SARS under section 172 of the TAA.

692. The reason for SARS filing the statement with the Court in that case was due to the taxpayer having a long-running dispute with SARS on the allocation of payments against an outstanding tax debt.

693. The Court held that the application for a rescission of judgment could not be upheld because the taxpayer should first have used the dispute resolution mechanisms, such as objections against assessments and appeals contained in the TAA, before electing to bring the application to the High Court.

694. However, no right of objection in relation to such matters is provided for in law in section 104 of the TAA.

Factual Description

695. The concern we have is that in the above case the taxpayer had no mechanism to object as was suggested by the judge because, although it is acknowledged that a taxpayer

can object against an assessment, there is no mechanism for a taxpayer to object against a statement of account.

696. Not being able to object against a statement of account is particularly problematic where the balance is incorrect due to a misallocation of a payment by SARS or due to a journal entry made by SARS - the reasons for which are unclear to the taxpayer despite trying to clarify the reasons with SARS.

697. In this regard we refer specifically to the Office of the Tax Ombud's Report on its investigation into systemic issues, released in June 2020, which highlighted the escalating number of complaints received in relation to PAYE Statements of Account changing regularly with no explanation given to the taxpayer. In some instances, these changes resulted in the taxpayer becoming non-compliant - for instance, when SARS raised assessments to absorb the credits, it resulted in EMP501's (reconciliations) reflecting as outstanding which affected the compliance status of the taxpayer. Taxpayers cannot be expected to change the reconciliations as they were correct.

The nature of businesses impacted

698. All businesses where the statement of account contains misallocations of payments by SARS or journal entries processed by SARS that were incorrectly processed as mentioned in the Office of the Tax Ombud's report.

Proposal

699. Section 104(2) of the TAA should be amended to include the right of taxpayers to object against a decision by SARS not to correct entries on a statement of account.

Section 125 – Appearance at a hearing of the tax court *(submission originally made in 2020)*

Legal Nature

700. Section 125(1) of the TAA provides that a senior SARS official, referred to in section 12 of the TAA, may appear at the hearing of an appeal in support of the assessment or 'decision'. It is noteworthy to mention that the - now deleted - section 125(2) of the TAA allowed clients to be represented by tax practitioners "… at the hearing of an appeal in support of the appeal". It is therefore clear that the TAA originally envisaged clients of tax practitioners being represented by tax practitioners at a hearing of an appeal, but this right of appearance has since been removed from the TAA.

701. The right to appear on behalf of taxpayers in the Tax Court is not dealt with expressly in the rules after the deletion of section 125(2) TAA. Consequently, the rules prescribe that any matter not expressly dealt with follow the Superior Courts rules.

702. The Superior Court rules address the right of appearance in the Right of Appearance in Courts Act which, as a standing position, only allows admitted advocates and attorneys to appear in court and consequently then in the Tax Court.

Factual Description

703. The deletion of section 125(2) of the TAA appears to us to have been an oversight as the Explanatory Memorandum notes that this right is implicit.

704. In our view, this right is not implicit and this has significantly altered the legal *status quo.* We accept that SARS never intended to change the right of appearance that has been long-standing in our tax dispute dispensation.

The nature of businesses impacted

705. All taxpayers.

Proposal

706. We propose that the deletion of section 125(2) should be repealed retrospectively.

707. Furthermore, in view of the fact that South African registered tax practitioners are subject to a statutorily regulated regime, a SARS' approved professional code of conduct and disciplinary processes that enforce compliance therewith, we believe that National Treasury should seek to amend the legislation so as to provide tax practitioners with 'tax practitioner litigation privilege' as well as a right to appear before the Tax Court.

708. For further details in this regard, please refer to SAICA's submission to National Treasury dated 7 July 2020 entitled "Legal professional privilege and right of appearance in court – Applicability to tax practitioners".

Section 164 – Suspension of payment requests & reduced assessments (NEW)

Legal Nature

709. Section 164(2) of the TAA enables a taxpayer to request for the suspension of the payment of tax (or a portion thereof) due under an assessment if he/she lodges or intends to lodge a dispute.

710. Section 93(1) empowers SARS to issue a reduced assessment despite the fact that no objection was lodged or appeal noted [section 93(2)].

Factual Description

711. While the TAA makes provision for SARS' issuance of a reduced assessment even where a taxpayer has not lodged a dispute, section 164 as it currently reads does not allow taxpayers to request that SARS suspend their payment of tax if they submit a request for a reduced assessment in terms of section 93.

The nature of taxpayers impacted

712. All taxpayers who request SARS for a reduced assessment in terms of section 93 of the TAA.

Proposal

713. Section 164(2) of the TAA should allow a taxpayer to request for the suspension of the payment of tax if that taxpayer requests that SARS issues a reduced assessment in terms of section 93 of the TAA.

714. The provision should read as follows:

"(2) A taxpayer may request a senior SARS official to suspend the payment of tax or a portion thereof due under an assessment if the taxpayer ***[requests that SARS issue a reduced assessment in terms of section 93]****, or intends to dispute or disputes the liability to pay that tax under Chapter 9."*

Section 164(3) – Payment of tax pending appeal *(submission originally made in 2020)*

Legal Nature

715. In terms of section 164(3), a senior SARS official may suspend payment of the disputed tax or a portion thereof having regard to various factors mentioned in the sub-section. There have been some practical challenges with respect to the suspension of payments, for example, there are no timelines to which SARS must adhere in making a decision on whether to grant the suspension or not.

716. Delays in making the decision sometimes lead to collection action being taken by the SARS debt management department and/or this impacts the tax compliance status of taxpayers.

Factual Description

717. Whilst SARS is making a decision regarding the request, in accordance with the legislation and as confirmed by SARS, it is as though a suspension is in place and SARS may not take collection steps. However, this is not the case in practice, due to lack of adequate communication between the various divisions within SARS - for example, if the suspension request is made via the auditor or even on e-Filing, this is not necessarily communicated timeously to the debt management department.

718. It is also not possible to request the suspension via e-Filing in some instances - for example, disputes in relation to trusts. When making the request by calling the Contact Centre or via email, there are often delays in SARS' internal communications conveying this to the relevant departments, and taxpayers are then subjected to third party collections in some instances.

719. To recover the funds after such an agency appointment is an immense challenge in practice.

The nature of businesses impacted

720. All taxpayers requesting suspension of payments.

Proposal

721. SARS should implement a 21 business day turnaround for issuing decisions regarding suspension of payment requests. If SARS does not respond within this timeframe, the suspension should automatically be applied.

722. Section 164(3) should be amended to expressly state that until a decision is made, the tax compliance status of the affected taxpayer should not be impacted by the related payment due, which is subject to the suspension request.

723. Similar to the SARS portal on its website for taxpayers to upload documentation, there should be a similar 'portal' to request suspension of payment where, for whatever reason, the suspension request is not available on e-Filing.

724. Having this within the system will hopefully alleviate the communication issues where the requests are made by teleconference or via email.

Sections 172 – Civil judgments *(submission originally made in 2020)*

Legal Nature

725. Section 172(1) states that if a person has an outstanding tax debt, SARS may, after giving the person at least 10 business days' notice, file with the clerk or registrar of a competent court a statement, certified by SARS as correct, setting out the amount of tax payable.

726. In the *Barnard Labuschagne Inc v South African Revenue Service and Another 2020 ZAWCHC* (15 May 2020) case, the taxpayer (Barnard Labuschagne Inc), sought to rescind such a statement filed by SARS under section 172 of the TAA.

727. The reason for SARS filing the statement with Court in that case was due to the taxpayer having a long-running dispute with SARS on the allocation of payments against an outstanding tax debt.

728. The Court held that the application for a rescission of judgment could not be upheld because the taxpayer should first have used the dispute resolution mechanisms, such as objections against assessments and appeals contained in the TAA, before electing to bring the application to the High Court.

729. This is notwithstanding that SARS and National Treasury have long defended the constitutionality of this extra-judicial process on the grounds that the filing of the certificate with the High Court in fact brought this process under judicial oversight as required by the Constitutional Court[17].

[17] *University of Stellenbosch Legal Aid Clinic and Others v Minister of Justice and Correctional Services and Others*; *Association of Debt Recovery Agents NPC v University of Stellenbosch Legal Aid Clinic and Others*; *Mavava Trading 279 (Pty) Ltd and Others v University of Stellenbosch Legal Aid Clinic and Others* (CCT127/15) [2016] ZACC 32; 2016 (6) SA 596 (CC); (2016) 37 ILJ 2730 (CC); 2016 (12) BCLR 1535 (CC) (13 September 2016)

Factual Description

730. The concern is that SARS and National Treasury have created a legal vacuum as relates to taxpayers' rights to have civil judgments rescinded, by arguing they are both inside the mandate of the High Court when faced with Constitutional objection and also outside the High Court's mandate when faced with an application to rescind.

731. This has removed all of a taxpayer's legal rights to have unilateral SARS debt judgments rescinded.

The nature of businesses impacted

732. All taxpayers against who SARS have taken judgment under section 172 of the TAA.

Proposal

733. It is proposed that National Treasury should propose to bring the conduct of SARS back under principles of constitutionality by subjecting SARS' conduct to judicial scrutiny as required by the Constitutional Court.

734. All section 172 applications should not merely be filed with the clerk but should be a judgment of the court by application brought by SARS. Given that this is an action of last resort and all SARS' other rights under the TAA such as agency appointment and "pay now argue later", there are only few instances where this would apply.

Section 190(2) of the TAA – Refunds of excess payments *(submission originally made in 2021)*

Legal nature of the problem

735. The TAA currently provides that SARS may not authorise a refund until such time that a verification, inspection, audit or "criminal investigation" has been finalised.

Detailed factual description

736. In some cases, these verifications, inspections, audits and "criminal investigations" by SARS take months or years to finalise.

737. However, it remains unclear what the term "criminal investigation" entails and whether it will be applied per taxpayer or include entire industries etc.

738. The legislation must clarify whether "criminal investigation" referred to is in respect of a person against whom there is confirmed evidence of a crime committed and whether this crime was reported to the South African Police Service (SAPS) and a SAPS case number been obtained.

739. As SARS impacts taxpayer rights by withholding refunds, lack of legislative clarity in this regard should not continue. An example is the 2019 investigation of an entire industry, the agriculture sector, followed by a blanket withholding of refunds.

740. The verification, inspection, audit or criminal investigation in the section should refer to the specific refund in question and not any refund.

741. As was evidenced in the Tax Ombud's 2019 report on Systemic Issues at SARS, one of the issues identified was that refunds for one period were being withheld whilst an audit/verification was in progress for another period. Withholding of the refund should be relevant to the period under audit or investigation and not to unrelated periods. This mostly applies to VAT refunds.

742. A taxpayer currently has no recourse against this administrative decision made by SARS and SARS is also not compelled to provide reasons for the decision to withhold the refund.

743. Though not part of this specific matter, we have also previously raised concerns with SARS' involvement in the criminal justice system, how constitutional rights are protected and how powers are given within the constitutional mandate. This ranges from search and seizure, sanction, overlap of civil and criminal investigations, who decides on criminal investigation and prosecution if not SAPS and the NPA and who oversees the legality of all these processes as they are outside of the jurisdiction of the Independent Police Investigative Directorate.

744. In regard to criminal intelligence-gathering, which is part and parcel of criminal investigations, we note in the 2017 OECD report that SARS claims it conducts no criminal intelligence-gathering activities at a covert level. SARS doing investigations and then also paying and sourcing counsel for NPA matters essentially puts SARS on equal footing with the historical Scorpions unit.

Nature of the business / persons impacted

745. All taxpayers subject to verification, inspection, audit or criminal investigation.

Proposal

746. "Criminal investigation" for the purposes of withholding refunds should be defined and limited to a particular taxpayer and a reasonable timeline of 30 days in which SARS must finalise the verification, inspection, audit and criminal investigation relating to the specific refund should be included.

747. The administrative decision made by SARS should be subject to objection and appeal.

748. To ensure that SARS does not turn into a *quasi* Scorpions Unit, it should ensure that its actions do not overlap with those of the NPA and SAPS whose role it is to follow up on criminal matters and who have the prosecution rights in this regard.

Section 234 – Removal of requirement of "wilfulness" from certain statutory offences. *(submission originally made in 2020)*

Legal Nature

749. National Treasury has categorised the criminal offences into those for which intent or negligence is required and those for which intent is required.

750. The maximum penalty of a fine or two years' imprisonment will remain and it will be left to the presiding officer to decide what sentence or sanction is appropriate on conviction, considering all the aspects of a case, though the offence will remain a criminal conviction with significant consequences. These impacts include employment prospects, international travel, business opportunities etc.

Factual Description

751. Whilst SARS may choose not to lay a charge for prosecution for administrative 'mistakes', the legislation gives SARS the power to do so, should it so wish. This in itself leads to another Constitutional concern of arbitrary prosecution.

752. SARS in response to this matter on TALAB19 noted that it doesn't prosecute, whereas the NPA does. This response ignores the fact that without SARS seeking prosecution by laying a charge with the SAPS or NPA under section 234 which, as with section 235, will exclusively be done by SARS, no criminal prosecution would occur. SARS is therefore instrumental in the process of prosecuting criminal offences.

753. This is in stark contrast to legislation such as POCA and FICA where there is a compulsion to report such criminal activities and we fail to understand why SARS would not want to compel complaints that result in prosecutions for criminal actions given its stated strategy.

754. SARS and National Treasury's stance in this matter seems to indicate an inclination that SARS wants to reserve the right who to prosecute for reasons that it feels should not be subject to public scrutiny.

755. This means that where you have 3 taxpayers who have committed the exact same criminal tax offence, a SARS official has a discretion to do nothing, to impose a civil sanction or to lay a compliant for a criminal sanction without any objective legal requirements as to how he/she decided on such sanction.

756. SARS has noted that they would not want to effect a prosecutorial process with all administrative transgressions and would like to have a discretion. This approach is misguided for criminal matters and the solution rather lies in ensuring that only actions that are extremely objectionable to society should be criminalised.

757. The argument of SARS seems to indicate and support our view that the list of offences in section 234 of the TAA have not been appropriately considered.

758. It is a matter we have raised with SCoF before and has become even more important with these amendments.

The nature of businesses impacted

759. All taxpayers.

Proposal

760. The purely administrative instances of non-compliance should merely be subject to civil sanction or only criminalised for repeat offenders who, through their conduct, show a pattern of intent to undermine the *fiscus*.

761. Sections 234 – 237 of the TAA should include the compulsion to lay a charge for prosecution with SAPS and NPA. These entities will then, in their investigative and prosecutorial frameworks, re-evaluate evidence gathered of the alleged crime and measure such evidence against the prescribed standard of proof.

Section 240 – Grounds for disqualification as a registered tax practitioner (violent crime) *(submission originally made in 2020)*

Legal Nature

762. Section 240 of the TAA states that a person may not register a tax practitioner or that SARS may deregister a registered tax practitioner if the person/tax practitioner has during the preceding five years been convicted, whether in the Republic or elsewhere, of theft, fraud, forgery, uttering a forged document, perjury, an offence under the prevention of Corrupt Activities Act, an offence under the Prevention and Combating of Corrupt Activities Act, 2004 (Act No. 12 of 2004) or any other offence involving dishonesty, for which the person has been sentenced to a period of imprisonment exceeding two years without the option of a fine or to a fine exceeding the amount prescribed in the Adjustment of Fines Act, 1991 (Act No. 101 of 1991).

Factual Description

763. Given the state of violent crime in South Africa we propose that violent crimes also be included as a disqualification criterion.

764. SAICA has proposed a similar prohibition for the Audit Professions Amendment Bill 2020 and will also be reconsidering its bylaws in this regard.

The nature of businesses impacted

765. All tax practitioners.

Proposal

766. It is suggested that the following wording be added to section 240(3):

“has been convicted anywhere in the world of a criminal offence in which violence is an element, including but not limited to public violence; murder; rape; sexual assault; trafficking of persons; robbery; kidnapping; assault and/or torture and has been sentenced in respect thereof to imprisonment without the option of a fine. Where any such conviction has led to a sanction of imprisonment with an option of a fine or to a fine being imposed, SARS shall have the discretion to decide whether or not to register the tax practitioner or cancel the registration of the tax practitioner.”

Section 240 – Tax practitioner registration and impact of suspension of membership *(submission originally made in 2020)*

Legal Nature

767. One of the sanctions imposed by SAICA on its members, in addition to fines and termination of SAICA membership, is suspension of membership.

768. Section 240(3)(a) however only allows for deregistration where a member has been **removed** for serious misconduct.

769. Suspension does not legally equate to removal in the strict sense and is also temporary.

770. Furthermore, this section only applies to a “related profession” (e.g. accounting) by a controlling body and not to the tax profession itself.

Factual Description

771. Where a member is subject to disciplinary proceedings, he or she may have committed a breach of the code of professional conduct that does not justify permanent removal as a member but temporary removal through suspension for a fixed period e.g. 6 months.

772. Such person will not enjoy the rights of membership during the period of suspension, but as he or she was not removed as member, it would seem that he or she would still be able to continue to practice as tax practitioner.

773. A similar concern was noted and proposal made in relation to **registered auditors** in the Audit Professions Amendment Bill 2020.

The nature of businesses impacted

774. All tax practitioners.

Proposal

775. It is submitted that the law needs to be amended to introduce a **new ground** under section 240(3) whereby a person whose membership is suspended by a “controlling body” shall on notification by such body to SARS, not qualify to be registered as a tax practitioner or cease to be registered as a tax practitioner for the same period as the suspension of membership.

776. Furthermore, section 240(3)(a) should be amended as follows:

*“(a) during the preceding five years has been removed **by a controlling body as a tax practitioner or** from a related profession by a ‘controlling body’ for serious misconduct;”*

Section 240 – Registration of tax practitioners *(submission originally made in 2022)*

Legal Nature

777. Section 240(1) of the TAA requires natural persons who provide tax advice or assistance with completing a tax return (for consideration) to register with (a) a recognized controlling body and (b) SARS as a tax practitioner.

Factual Description

778. While keeping individuals accountable for the tax advice they provide is important, this has given rise to several practical concerns in the context of incorporated practices and partnerships.

(a) *Legal client relationships versus tax practitioners*

779. When a client signs on with a tax practitioner firm, legal liability as well as “ownership” of the contract with the client rest with the firm and not the individual partners.

780. No one member/shareholder/partner of the firm is therefore the full owner of that contract.

781. To use an example, A and B are both individuals who have incorporated a company called “TP Inc”, a limited liability company. Client C then signs on for tax services to be rendered by TP Inc.

782. A proper interpretation of section 240(1) is that A or B should charge the Client C for tax services rendered in their personal capacities.

783. TP Inc may alternatively adhere to section 240 by providing the tax services, but for no consideration. This is because the requirement to register as a tax practitioner excludes persons who provide tax advice for no consideration.

784. However, neither of the above options are in line with the legal contract signed by Client C, nor is it in line with the working practices of any practice other than sole practitioners.

785. It is the current working practice of SARS to accept that, for example, A will be the named tax practitioner and therefore takes responsibility for all tax services performed by TP Inc.

786. This is, however, only a working practice.

787. Section 240(1) does not recognize and allow non-natural persons to register as tax practitioners. A strict reading of the TAA therefore implies that TP Inc is in breach of

section 240(1) because while it renders tax services for a fee, it does not qualify to register as a tax practitioner because it is not a natural person.

(c) Employees of incorporated firms and their obligation to register as tax practitioners

788. Section 240(2)(d) exempts individuals from registering as tax practitioners if they are working under the direct supervision and authorization of a tax practitioner.

789. Continuing the example provided above, A only has authority to issue instructions to the employees of TP Inc in his capacity as an employee of TP Inc, not in his (personal) capacity as tax practitioner.

SARS E-filing profiles for individuals versus firms

790. The SARS e-Filing platform currently provides for an accounting/tax firm to have its own e-filing profile which contains all its tax clients' e-filing profiles. This firm's e-filing profile is, however, linked to the e-Filing account of any registered tax practitioner who is an owner or employee of the firm.

791. To continue the TP Inc example noted previously, the e-filing profile of A (one of the owners/employees of TP Inc) will now therefore contain access to every single client of TP Inc. It is also on A's e-Filing profile that the user rights for all employees of TP Inc are granted.

792. If A were to ever leave TP Inc, he would retain e-filing access to all of TP Inc's clients. He cannot simply abandon his e-Filing profile to TP Inc, as it is his personal e-filing profile.

793. Additionally, he would still retain legal liability for all tax returns submitted on this profile, since all powers of attorney and authorizations would have been in his personal name, not TP Inc's.

794. TP Inc's employees have access to the clients' e-filing profiles only through A's profile.

795. Although it is possible to transfer these profiles to a new tax practitioner should A leave TP Inc, this is an extraordinarily time-consuming process as it would require a manual transfer request (on e-filing) for every single client and a new Power of Attorney to be signed for every single client of TP Inc.

796. This is not unique to tax hence the Auditing Professions Act recognizes "firms" in section 38.

<u>The nature of taxpayers impacted</u>

797. All firms that run tax practices with registered tax practitioners with profiles on the SARS e-filing platform.

Proposal

798. An amendment be made to section 240 to recognize non-natural persons (including incorporated firms and partnerships) as tax practitioners.

799. The amendment provide that each accounting/tax firm have an individual who takes full responsibility for the function of the tax/accounting practice, similar to how a representative taxpayer take responsibility for all other taxes of incorporated entities.

800. The Act could create personal liability for this representative.

Penalties could be built into the law to ensure that incorporated entities would lose their SARS tax practitioner status if they do not update or maintain the eligibility of the representative taxpayer.

Definition of "date of assessment" & Sections 251 -255 – Electronic delivery *(submission originally made in 2020)*

Legal Nature

801. Section 96 states the notice of assessment must include the "date of assessment". The definition of "date of assessment" has been deleted from the Income Tax Act, but it still remains in section 1 of the TAA.

802. In terms of the TAA, the "date of assessment" is defined as, *inter alia*, in the case of an assessment by SARS, the date of the issue of the notice of assessment.

803. Thus the "date of assessment" is tied to the "issue" of the assessment and it is our understanding that an assessment will only be "issued" if it is delivered to the taxpayer.

804. In terms of a recent court case (*SIP Project Managers (Pty) Ltd v The Commissioner for the South African Revenue Service* (Case Number 11521/2020), it was held that delivered means that the document must be delivered to the taxpayer (via electronic platform or to the last known address of the taxpayer) and a notice generated by the e-Filing system does not satisfy the requirement of delivery unless such notice is uploaded onto the taxpayer's profile.

805. Furthermore, in handing down its decision in the matter of *Singh v Commissioner, South African Revenue Service* 2003 (4) SA 520 (SCA), the Supreme Court of Appeal confirmed that a taxpayer can lawfully receive notice of an assessment only if it is delivered electronically by SARS as prescribed by sections 251 and 252 of the TAA.

806. Sections 251 and 252 state that SARS is regarded as having issued, given, sent or served the communication to the company if -:

…(d) sent to the person's last known electronic address, which includes—
(i) the person's last known email address;
(ii) the person's last known telefax number; or

(iii) the person’s electronic address as defined in the rules issued under section 255(1).

807. The rules issued under section 255(1) state at 3(2) that delivery will occur for electronic filing communications when SARS correctly submits the notice etc on the users electronic system, which the court in SIP case held is when the taxpayer can access it ie. not when it is generated on the SARS system “backend”.

Factual Description

808. A notice of assessment requires disclosure of the “date of assessment”.

809. The date on the assessment is usually the date when the letter is compiled by SARS on the SARS system backend but this may differ from the date on which it is loaded (“issued”) onto the taxpayer’s efling profile allowing the taxpayer to access it.

810. The law is now clear that date of issue for the purpose of section 251-255 of the TAA and the rules is not the “letter date” or even the date that SARS adds something in the back end of the system, but rather the date that the taxpayer can access it on his eFiling profile.

811. Though the law is now clear it remains a problem in practice that SARS’ letters are dated before the taxpayer can access them and that SARS calculates the days from the date of the letter or when the letter is uploaded on the backend of their system and not from date that the taxpayer is able to access it on eFiling.

The nature of businesses impacted

812. All taxpayers.

Proposal

813. It is submitted that the solution lies in the never-implemented draft section 255 of the TAA rules that were issued in 2016 where it was proposed in a new clause 4(2)(a)(iii) that:

> (2) A SARS electronic filing service must—
> (a) provide a registered user with the ability to—
> <u>(iii) nominate an alternative electronic address to which the SARS electronic filing service must deliver a notification of the submission of an electronic filing transaction by SARS to the registered user’s electronic filing page.</u>

814. It will then be easy to align the “date of delivery” as when the date when the email notification entered the communicator’s system, which is again aligned to what the rule already states for other SARS electronic communications.

815. This will also address taxpayers' long-held concern that e-Filing is not a proper or appropriate notification method and will avoid taxpayers being subject to SARS' sporadic "other notifications", like SMS etc. which only work in respect of certain products and services.

Chapter 2 – New Part G: Taxpayer Bill of Rights *(submission originally made in 2021)*

Legal Nature

816. Currently SARS and taxpayers' rights are contained in the TAA. The SARS Service Charter also stipulates a taxpayer's rights and obligations as well as the service time frames that a taxpayer can expect from SARS.

Factual Description

817. Despite the above, SARS does not necessarily always comply with the procedures outlined in the TAA (see the Office of the Tax Ombud's Systemic Investigations Report) or in the SARS Service Charter. Due to the long time periods and exorbitant costs involved in addressing these deficiencies, only a few taxpayers have challenged SARS' non-compliance in court.

818. As many taxpayers are not well acquainted with the TAA, crystallising taxpayers' rights in a document would help raise public awareness of taxpayers' rights as well as SARS' legal obligations.

The nature of taxpayers impacted

819. All taxpayers interacting with SARS.

Proposal

820. A Taxpayers' Bill of Rights that is binding on SARS should be included in a separate chapter (Part G) of the TAA. SAICA's TAA sub-committee is currently doing research on the international best practice to assess what would be the best solution for the South African context and is willing to share the findings with the National Treasury.

Chapter 17 – Criminal offences *(submission originally made in 2021)*

Legal Nature

821. Section 234 contains a list of criminal offences wilfully committed by a person and also includes a list of requirements that if a person wilfully or negligently fails to do these, will be considered a criminal offence.

Factual Description

822. Currently, a SARS official falsely communicating information to the Tax Ombud (lying or misrepresenting facts) does not constitute a criminal offence. Neither is the lying by a SARS official to get a search warrant a criminal offence. The only remedy afforded to the taxpayer is to approach the Public Protector.

823. In terms of section 28(1) of the Criminal Procedure Act 51 of 1977, if a policeman lied to get a search warrant, it would be a criminal offence of perjury.

The nature of taxpayers impacted

824. All taxpayers submitting complaints to the Tax Ombud or subjected to a search warrant where a SARS official has lied or misrepresented facts.

Proposal

825. A similar offence and sanction to that in the Criminal Procedures Act should be included in the TAA or Chapter 17 of the TAA should be amended to include as a criminal offence a SARS official that lies or makes misrepresentations to the Office of the Tax Ombud or to get a search warrant.

826. Consideration should also be given to compulsory publication of SARS disciplinary cases (similar to what SAICA does with its members) on a no name basis which the Office of the Tax Ombud could review.

827. This would certainly improve SARS' public image and build trust with taxpayers that SARS does in fact apply consequence management.

Decisions not subject to objection or appeal *(submission originally made in 2021)*

Legal Nature

828. The ITA and the TAA, in various sections, provide the taxpayer with an opportunity to lodge a dispute against a decision or action taken by SARS.

Factual Description

829. Notwithstanding the above, there are sections in the ITA and the TAA that do not allow a taxpayer the opportunity to dispute a decision or action taken by SARS.

830. These include:

830.1 Section 58(1) of the Income Tax Act – Where any property has been disposed of for a consideration, *which in the opinion of the Commissioner*, is not an adequate consideration, then that property shall be deeded to have been disposed of under a donation.

830.2 *Section 9 of the TAA* – A decision or notice made by a SARS official (excluding a decision giving effect to in an assessment or notice of assessment that is subject to objection and appeal) to a taxpayer, may *in the discretion of a SARS official* be withdrawn or amended by a SARS official.

830.3 Section 93(1)(d) and (e) of the TAA – SARS may make a reduced assessment if *SARS is satisfied* that there is a readily undisputed error in the assessment by either the taxpayer or SARS and *if a senior SARS official is satisfied* that an assessment was based on the failure to submit a return or submission of an incorrect return by a third party under section 26 or by an employer under a tax Act or a processing error by SARS or a return fraudulently submitted by a person not authorised by the taxpayer.

830.4 Section 161(3) of the TAA – If security is required by SARS, the security *must be* of the nature, amount and form *that the senior SARS official directs*.

830.5 Section 164(3)/(5) – *A senior SARS official may suspend* the payment of tax or a portion thereof having regard to various factors set out in section 164(3), one of the factors being whether the taxpayer has tendered adequate security for the payment of the disputed tax and accepting it is in the interest of SARS or the fiscus. A senior SARS official may also deny a request for suspension or revoke a decision to suspend payment with immediate effect *if satisfied* of certain criteria set out in section 164(5).

830.6 Section 167(1)/(4) of the TAA – A senior SARS official may enter into an agreement with a taxpayer under which the taxpayer is allowed to pay a tax debt in one sum or in instalments *if the official is satisfied* of certain criteria stipulated in section 167(1). A senior SARS official may also terminate an instalment payment agreement *if satisfied that* certain requirements are met in section 167(4).

830.7 Section 227 of the TAA – This section describes the requirements for a valid voluntary disclosure, however, a decision taken by SARS regarding the validity of the requirements of a voluntary disclosure application is not subject to objection and appeal.

The nature of taxpayers impacted

831. All taxpayers that are subject to a SARS official's decision or SARS' discretion as mentioned above.

Proposal

832. To avoid expensive court procedures for all concerned, the above sections should be made subject to objection and appeal.