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National Treasury
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0001

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Dear National Treasury and Ms Collins

SUBMISSION - ANNEXURE C 2020 BUDGET REVIEW

1. We present herewith our written submission on the request for Annexure C 2020 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 amendments to various sections of the Income Tax Act, No 58 of 1962 (the Act), the Value Added Tax Act, No 89 of 1991 (the VAT Act) and the Tax Administration Act, No 28 of 2011 (the TAA), as contained in the Taxation Laws Amendment Bill, 2019 (TLAB2019) and the Taxation Administration Laws Amendment Bill, 2019 (TALAB2019), respectively.

3. We also enclose a copy of our prior year Annexure C submissions for 2018, as Annexure B, for ease of reference. We note specifically that with the exception of a few items, National Treasury (NT) has largely not favourably considered our prior year submissions and we would seek to engage with NT on why it believes the relevant proposals would not be in the interests of the South African fiscal policy.

4. We indicate in each instance in Annexure B, the current status of the prior year's submissions, noting whether the proposals have been implement by NT, and indicating where the proposals were partially accepted by NT.

5. 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.

6. As always, we thank NT and SARS for the on-going opportunity to participate in the development of the SA tax law.

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

Yours sincerely

David Warneke	**Dr Sharon Smulders**
CHAIRPERSON: NATIONAL TAX COMMITTEE	**PROJECT DIRECTOR: TAX ADVOCACY**

The South African Institute of Chartered Accountants

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ANNEXURE A

CATEGORY - INCOME TAX: INDIVIDUALS, EMPLOYMENT AND SAVINGS

Section 1 – "gross income" definition & fringe benefits

Legal Nature

7. In the recent case of *BMW South Africa (Pty) Ltd v The Commissioner for the South African Revenue Service* (1156/18) [2019] ZASCA it was held that the provision of tax consulting services by an employer to its expatriate employees constituted a 'benefit or advantage' as contemplated in the definition of 'gross income' in section 1 of the Act (a taxable fringe benefit) in the hands of such employees in accordance with the Seventh Schedule to the Act.

Factual Description

8. Paragraph 10 of the Fourth Schedule to the Act stipulates that the value of the fringe benefit in the above circumstances is the actual cost incurred by the employer in rendering the service. Determining the cost of this service is problematic as in some cases an employer has agreed to fees which incorporate a number of services, of which only some might be exclusively for the benefit of its employees. The administrative complexity in calculating the abovementioned fringe benefit is burdensome and time consuming for employers.

9. The USA for instance, have recently put rules in place to simplify the process of determining what cost relates to the benefit derived by the employer versus that of the employee. These rules state that the employer will assume the annual cost of preparing one host country, one U.S. federal and one state (if required) tax return and the tax equalization calculation. In accordance with IRS regulations, **income will be imputed** to the expatriate equal to the estimated fringe benefit received for the personal portion of the tax preparation services. A like amount will be taken as a deduction if deductions are itemized and are not limited on the tax return. Any additional tax that results from this imputed income will be assumed by the employer through the tax equalization program.

The nature of businesses impacted

10. Employers that have expatriate employees who are tax equalised or tax protected as the employer is liable to bear the tax cost in the employees' host location.

Proposal

11. It is proposed that an imputed amount to be allowed to be regarded as the estimated fringe benefit amount received by the expatriate employees as is permitted in the USA so as to lessen the administrative burden on employers in calculating the tax on the fringe benefit amount.

12. It is also proposed that the taxation of these fringe benefits be done prospectively, not retrospectively.

Second Schedule – Tax Treatment on Withdrawal of foreign pensions

Legal Nature

13. Paragraph 2C and 6 of the Second Schedule deals with the withdrawal or resignation from a pension fund, pension preservation fund provident fund, provident preservation fund or retirement annuity fund. These funds are generally defined in section 1 of the Act as being local South African funds.

14. According to the 2016 Budget Speech, 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. A review of these issues is necessary taking into account the tax policy for South African retirement funds. NT was supposed to review this as part of the Davis Tax Committee findings, but no clarification has been forthcoming.

Factual Description

15. Tax treatment on withdrawal (by a South African tax resident) from a foreign pension fund appears to be uncertain – contributions made to such a fund would not have been allowed as a deduction. NT was supposed to review this as part of the DTC findings, but no clarification has been forthcoming.

The nature of businesses impacted

16. All taxpayers who wish to withdraw their foreign pensions.

Proposal

17. Clarification is required as to the tax implications in this regard, given that the contributions made to such a fund would not have been allowed as a tax deduction.

Paragraph 11A of the Fourth Schedule - Employees' tax for employee share incentive schemes

Legal Nature

18. Paragraph 11A of the Fourth Schedule to the Act deals with the employees' tax aspects of employee share incentive schemes which fall within the ambit of section 8A, 8B and 8C of the Act, and which are included in the definition of "remuneration", specifically in paragraphs (b), (d) and (e).

19. Paragraph 11A of the Fourth Schedule appears to be a stand-alone provision which operates independently of paragraph 2(1) of the Fourth Schedule to the Act.

20. Paragraph 2(1) prescribes the employees' tax withholding obligation for a resident employer (or a representative employer) who pays or becomes liable to pay remuneration to an employee; whereas paragraph 11A appears to apply to both resident and non-resident employers.

21. Paragraph 11A(2) provides as follows:

> *"(2) Employees' tax in respect of the amount of remuneration contemplated in subparagraph (1) must, unless the Commissioner has granted authority to the contrary, be deducted or withheld by the person …*
>
> *Provided that where that person is an "associated institution", as defined in paragraph 1 of the Seventh Schedule, in relation to **<u>any employer</u>** who pays or is liable to pay to that employee any amount by way of remuneration during the year of assessment during which the gain contemplated in subparagraph (1)(a) or (b) or the amount contemplated in 1(c) or (d) arises; and—…*
>
> *(i) that person is not resident nor has a representative employer;*
> *(ii) that person is unable to deduct or withhold the full amount of employees' tax during the year of assessment during which the gain or the amount arises, by reason of the fact that the amount to be deducted or withheld from that remuneration by way of employees' tax exceeds the amount from which the deduction or withholding can be made; or*
> *(iii) the amount of the dividend referred to in paragraph (c) consists of an equity instrument referred to in section 8C,*
>
> *that person and that employer must deduct or withhold from the remuneration payable by them to that employee during that year of assessment an aggregate amount equal to the employees' tax payable in respect of that gain or that amount and shall be jointly and severally liable for that aggregate amount of employees' tax." (Our emphasis and underlining.)*

22. Paragraph 11A(2) provides that employees' tax must be withheld by the "person" (who granted the right or from whom the equity instrument or qualifying equity share was acquired), unless the Commissioner has granted authority to the contrary.

23. In the first instance, where the "person" is a non-resident entity, that non-resident entity would be liable for the employees' tax withholding. However, in terms of the proviso to paragraph 11A(2) where the "person" who is required to withhold the employees' tax is an associated institution (as defined in paragraph (1) of the Seventh Schedule), in relation to any employer (who pays or is liable to pay to that employee any amount by way of remuneration during the year of assessment during which the gain arises) and certain conditions are satisfied, the "person" and the employer become jointly and severally liable for withholding and paying the employees' tax over to South African Revenue Service ("SARS").

Factual Description

24. In the circumstances described in the proviso to paragraph 11A(2) the employees' tax withholding obligation is placed on the following entities, if they are associated institutions (as defined):

- the "person" by whom that right was granted or from whom that equity instrument or qualifying equity share was acquired; and

- "any employer" who pays or is liable to pay to that employee any amount by way of remuneration during the year of assessment.

25. This may be problematic where both the "person" (who granted the right or from whom the equity instrument or qualifying equity share was acquired) and the employer (who pays or is liable to pay any amount by way of remuneration to the employee during the year of assessment during which the gain arises) are foreign non-resident entities. This may occur where a foreign national on a secondment to South Africa is paid by his/her non-resident home country employer and acquires an equity instrument from a foreign group entity.

26. In these circumstances it is unlikely that either the foreign home country employer (who pays the employee's remuneration) or the foreign entity (from whom the equity instrument was acquired) would be registered with SARS as employers for purposes of employees' tax withholding. Note that in our experience it is extremely difficult to register a non-resident entity as an employer with SARS. This may not even be possible where the non-resident entity does not have a permanent establishment in South Africa.

27. The abovementioned problem is further illustrated in the following scenario:

28. An award is made to a non-resident employee in terms of a Long Term Incentive Plan implemented for employees of the group. The award is made by a non-resident group entity and the employee is subsequently seconded to the South African entity for a period of 2 years. The employee is repatriated at the end of the 2 year secondment period in South Africa. The award vests a year later while the employee is rendering services to his home country employer (who is not the grantor of the award (i.e. the "person" referred to in paragraphs 11A(1) and (2)).

29. In these circumstances neither the "person" referred to in paragraphs 11A(1) and (2) nor the employer who pays the employee's remuneration during the year of assessment in which the gain arises are South African resident entities. These entities are unlikely to be registered with SARS and furthermore, it may be impractical, if not impossible for these entities to register as employers with SARS.

The nature of businesses impacted

30. All foreign employers who pay or are liable to pay to an employee any amount by way of remuneration in respect of employee share incentive schemes which fall within the ambit

of section 8A, 8B and 8C of the Act, and which are included in the definition of "remuneration", specifically in paragraphs (b), (d) and (e).

Proposal

31. It is proposed that the proviso to paragraph 11A(2) should be amended to refer to "any *South African resident* employer who pays or is liable to pay to that employee any amount by way of remuneration during the year of assessment during which the gain contemplated in subparagraph (1)(a) or (b) or the amount contemplated in subparagraph (1)(c) or (d) arises;…"

Section 24 – Credit agreements and debtors allowance – sale of fixed property

Legal Nature

32. Section 24(1) of the Act states the following:

"*Subject to the provisions of section 24J, if any taxpayer has entered into any agreement with any other person in respect of any property the effect of which is that, in the case of movable property, the ownership shall pass or, in the case of immovable property, transfer shall be passed from the taxpayer to that other person, upon or after the receipt by the taxpayer of the whole or a certain portion of the amount payable to the taxpayer under the agreement, the whole of that amount shall for the purposes of this Act be deemed to have accrued to the taxpayer on the day on which the agreement was entered into*."

Factual Description

33. For individuals and smaller businesses, the impact of the above section may be significant as the tax on the transaction needs to be paid before the funds have actually been received. This causes severe cash-flow issues for these taxpayers.

The nature of businesses impacted

34. All individuals and small businesses who sell property as set out in section 24.

Proposal

35. It is proposed that consideration should be given to introducing a "cash basis" for the payment of the tax due in respect of the sale of immovable property by individuals and small businesses so as to alleviate any cash-flow difficulties that may arise from the tax having to be paid before the money for the sale has been received.

CATEGORY – DOMESTIC BUSINESS TAXES

Section 1 – "gross income" definition - Tenant installation allowances

Legal Nature

36. Certain landlords provide tenants with an allowance to cover the cost of refurbishing leased property.

Factual Description

37. Case law (Heron Investments (Pty) Ltd vs Secretary for Inland Revenue 33 SATC 181) seems to indicate that these allowances should be treated as capital in nature, but in practice, the treatment appears to vary. In most instances these allowances are provided in respect of short term leases that are concluded.

The nature of businesses impacted

38. All taxpayers who receive refurbishment allowances.

Proposal

39. Clarity is required as to whether these allowances are capital or revenue in nature as the property market has changed substantially since the time of the Heron's decision and furthermore the case dealt with a set of particular circumstances where the lease period approximated ten years.

Section 1 – Definition of "equity share"

Legal Nature

40. The definition of "equity share" in section 1 of the Act is defined as '*any share in a company, excluding any share that, neither as respects dividends nor as respects returns of capital, carries any right to participate beyond a specified amount in a distribution'*.

41. The second proviso to section 10B(2) also refers to an equity share. This section provides for an exemption for foreign dividends received or dividends received from a head quarter company and the proviso reads as follows: '*Provided further that paragraph (a) must not apply to any foreign dividend received by or accrued to that person in respect of a share other than an equity share*.

Factual Description

42. The definition of "equity share" in section 1 of the Act currently does not refer to "foreign dividends" and "foreign returns of capital". It is clear from, for example, the second proviso to section 10B(2), that shares in non-South African tax resident companies may also qualify as "equity shares", however, the definition "equity share" in section 1 of the Act refers to dividends" and "returns of capital", which are concepts that are only defined

in relation to South African tax resident companies and not “foreign dividends” and “foreign returns of capital”, which are the corresponding concepts that refer to shares in non-South African tax resident companies.

The nature of businesses impacted

43. All taxpayers who wish to claim an exemption for foreign dividends or dividends declared or paid by headquarter companies.

Proposal

44. It is proposed that the definition of “equity share” in section 1 of the Act be amended to also refer to “*foreign dividends*” and “*foreign returns of capital*”.

Section 1 – Definition of “portfolio of a collective investment scheme”

Legal Nature

45. A “portfolio of a collective investment scheme: is defined as “*any* –

(a) portfolio of a collective investment scheme in participation bonds;

(b) portfolio of a collective investment scheme in property;

(c) portfolio of a collective investment scheme in securities; or

(d) portfolio of a declared collective investment scheme”.

Factual Description

46. The non-inclusion of a portfolio of a *hedge fund* collective investment scheme in the above definition creates uncertainty in the interpretation of section 25BA of the Act as well as paragraph 61 of the Eighth Schedule to the Act. It is thus uncertain whether a portfolio of a hedge fund collective investment scheme falls within the ambit of section 25BA(1) and paragraph 61 of the Eighth Schedule.

The nature of businesses impacted

47. Any portfolio of a hedge fund collective investment schemes.

Proposal

48. It is proposed that the definition of ‘portfolio of a collective investment scheme’ in section 1 of the Act should be amended to include any ‘portfolio of a hedge fund collective investment scheme’.

<u>Section 8E – Dividends deemed to be income</u>

<u>Legal Nature</u>

49. The Explanatory Memorandum (EM) proposed amendments to the definition of "hybrid equity instrument" in paragraphs (*a*), (*b*) and (*e*) to clarify the scope of the definition of hybrid equity instrument by clarifying that any part redemption of a share refers to a distribution of an amount constituting a return of capital or a foreign return of capital in respect of that share as it is impossible to otherwise redeem a portion of a share.

50. The TLAB2019 refers to the obligation to "distribute an amount determined with reference to the issue price of that share".

51. The proposed amendments to this section are deemed to have come into operation on 21 July 2019 and applies in respect of years of assessment ending on or after that date.

<u>Factual Description</u>

52. The EM seems to target "distributions constituting return of capital or foreign return of capital" but the updated TLAB2019 refers to the obligation to "distribute an amount determined with reference to the issue price of that share".

53. This change is much wider than what the EM proposed, and thus would cover a normal dividend. It would thus seem as if an obligation to distribute a normal dividend would render a share a hybrid equity instrument.

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

54. All taxpayers who receive any dividend or foreign dividend in respect of a share or equity instrument.

<u>Proposal</u>

55. The section needs to be amended to limit the application of the section to at least that proposed in the EM as it clearly cannot be NT's intention that an obligation to distribute a normal dividend would render a share a hybrid equity instrument.

56. The effective date of the amendment (21 July 2019) should not applied retrospectively, but prospectively.

57. The lack of consultation on the additional amendments from the original bills to the promulgated bills is concerning and undermines the credibility and transparency of the legislative process and does not foster a trusting relationship with the public.

<u>Section 12P and the Eleventh Schedule – List of exempt government grants</u>

<u>Legal Nature</u>

58. Section 12P deals with the exemption of amounts received or accrued in respect of government grants. The government grants referred to in the section are those that are listed in the Eleventh Schedule or identified by the Minister by notice in the *Gazette*.

<u>Factual Description</u>

59. The list of grants exempt from income tax under the Eleventh Schedule currently includes government grants which have been terminated/suspended. Examples of these are, *inter alia*, the Enterprise Investment Programme and Manufacturing Competitiveness Enhancement Programme.

60. Additional grants, such as the Critical Infrastructure Programme and Aquaculture Development and Enhancement Programme, have been introduced by the Department of Trade and Industry, however, these are not reflected in the list of grants exempt from income tax under the Eleventh Schedule.

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

61. All businesses that receive government grants as contemplated in section 12P and the Eleventh Schedule.

<u>Proposal</u>

62. An update of the available government grants exempt from income tax should be provided in the Eleventh Schedule to reflect the grants which have been introduced and to delete those which have been terminated/suspended.

<u>Section 22 – Trading stock valuation</u>

<u>Legal Nature</u>

63. The proposed amendments to the TLAB2019 provide that in determining any diminution in the value of trading stock, no account must be taken of the fact that the value of some items of trading stock held and not disposed of by the taxpayer may exceed their cost price.

<u>Factual Description</u>

64. Although the removal of the initial requirement that any diminution in the value of trading stock must be done on an item-by-time basis is welcomed and the new proposed amendment is accepted, the fact that there is still no alignment with the valuation of trading stock for IFRS/GAAP purposes still creates a huge administrative burden for taxpayers in that they need to two separate records for the valuation of trading stock – one for accounting purposes and one for tax purposes.

The nature of businesses impacted

65. All taxpayers who have trading stock.

Proposal

66. It is proposed that the valuation of trading stock for taxation purposes be aligned with the accounting treatment thereof as having to keep two separate records is burdensome for businesses and costly from an audit perspective for both SARS and taxpayers.

67. Aligning the accounting and tax treatment would align with the President's drive to reduce regulatory burdens and improve economic growth for businesses in South Africa as mentioned by him at the Jobs Summit and the Financial Times Africa Summit in 2019.

Section 30 – "Retrospective approval"

Legal Nature

68. The current section 30 and 30A allows for CSARS to retrospectively approve these organisations, and for PBO's to the extent that they have complied with the requirements of a PBO, in essence an entity that conducted PBA's.

69. This submission will only address PBO's as we believe they require special attention given their service to society.

70. As noted to SCoF, this provision was extended in scope in 2009 beyond the initial limitations periods in 2001 and 2006 in acknowledgement by NT that this sector seldom understands the complexity of their obligations and especially for PBO's, the burden of this complexity should not be an added burden where these entities are helping society and government.

71. Government seeks compliance which we support but it must be fair given the circumstances of the taxpayer group.

72. The proposals in TLAB B18B 2019 proposes to limit the retrospectivity to 3 years and only after all returns are submitted. Though this is an improvement from the draft bill it remains problematic especially for PBO's.

Factual Description

73. Mr and Mrs X looks after AIDS orphans and started as a couple making their house available. Initially it was self-funded and then they received local cash, clothes and food donations. They also sell some of the food donated where it would spoil for not being used in time.

74. After 5 years the burden is too great and they seek more external funding, but the 'external funder' requires them to be a registered PBO.

75. They thus approach SARS for registration.

76. By law, they must register as a company (section 1 definition of company ITA), submit 5 years of income tax returns as a company and pay any taxes due. The latter is required as even though they want to apply as PBO, the process takes months and SARS debt management will in practice seek to recover as the “stops” are seldom effective.

77. They will now have to engage the services of a professional to draft a founding instrument which must also be in compliance with the tax legislation, sign on as fiduciary responsible persons, pay the professional to analyse their cash flows/accruals for the last 5 years to submit returns and pay the corporate tax and any penalties / interest.

78. Only then will SARS TEU register them and if successful, they will get a refund a year or more later.

79. Under the TLAB2019 they will now be penalised for 2 years to pay corporate taxes and penalties/interest.

80. This debt is in our view a “false debt” and so is the refund as it never should have occurred in the first instance, thus the practical problem is self-created due to the application of the law and practice by SARS.

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

81. All taxpayers who are PBO’s.

<u>Proposal</u>

82. The proposed legislation creates a disincentive to register or conduct PBA’s given the risks which are both not in the public interest or that of government.

83. It also remains unclear for unincorporated entities, who exactly SARS intended holding responsible, as no one will incur such responsibility after the fact as fiduciary.

84. It is proposed that the proposal in section 30(3A) be reconsidered and returned to its original wording.

85. It is further proposed that the law be amended to remove the dual application procedure in law which creates this problem so that a PBO can directly apply to TEU rather than first as a normal company. In such instance no refund will be necessary as there will be no debt raised on application, only if the application is rejected by TEU.

<u>Section 30B – Meaning of “funding”</u>

<u>Legal Nature</u>

86. In order for a section 30B association to qualifying for exemption under section 10(1)(d)(iii) or (iv) certain criteria need to be met.

87. Section 10(1)(d) will exempt all "**receipts and accruals"** if the criteria in section 30B is met, which includes two criteria referring to "**funding**".

88. The "funding" requirement is used in section 30B and a threshold requirement is therefore critical.

89. We accept that these types of entities funding models may out of necessity have been expanded and that the policy of what was intended, namely a simple compliance approached but with a restricted funding model, may not be realistic anymore. In such case NT may want to reconsider the current policy, especially where compliance has become a concern.

90. Receipts and accruals include both capital and revenue amounts and also will include passive amounts like interest and dividends, but also trading income, which will be fully exempt should these requirements be met.

91. As the rules of interpretation require all words to be given a meaning, "funding" invariably means something different to "receipts and accruals", hence the use of a different word.

Factual Description

92. One of the requirements is that "*substantially the whole*" of the entity's **funding** must be derived from its annual or other **long-term members** or from an **appropriation by the government** of the Republic in the national, provincial or local sphere.

93. When calculating this threshold, the question then arises what is in "funding" that is not in receipts and accruals and what is "total funding" (base of calculation) as opposed to "*member funding*".

94. For example, below is two approaches, though more exist, to this classification:

EXAMPLE A - STRICT		**EXAMPLE B - BROAD**	
Member income	R100	**Member income**	R100
Interest on cash	R 10	**Interest on cash**	**R 10**
Dividends from subsidiary	R 10	**Dividends from** subsidiary	R 10
Trading income from		**Trading income from**	
Members	R 10	**Members**	R 10
Trading income from others	R 10	Trading income from others	R 10
Receipts from assets		**Receipts from assets**	

disposed of	R 5	**disposed of**	**R5**
Receipts and accruals Total funding “Funding” from members	R145 R140 R110	Receipts and accruals Total funding “Funding” from members	R145 R145 R135

95. In example A there is contravention and in example B compliance, though both revenue streams are the same.

96. This uncertainty in the law creates much disparity in the market depending on which interpretation is followed. It also means that on the broader interpretation, corporate structures are now created with “dividends” seen as member funding (as it was originally funded with member money) and whether NT intended group structures under these section 30B organisations is unclear.

97. As it is also unclear what “funding” means, for example, does it exclude exempt amounts and capital gains, it remains unclear what “total funding” would be in relation to member funding. It is clear that in practice it is wider than just member affiliation fees.

98. We have engaged the SARS TEU to clarify and have provided the following examples of “funding” for them to consider:

Income types which are derived from non-members to consider for **interpretation of “funding”** for section 30B(2)(ix) purposes or funding from members that are non-member fees:

98.1. **Donations** members and non-members

98.2. Sponsorships for events / projects

98.3. Contributions by or fees paid by “related” international industry organisations which promote common interests of their members in similar professions, business, industries outside SA to support SA specific projects and/or to provide support services to their members in SA.

98.4. Bequests from estates of members and non-members

98.5. Project contributions from international organisations like World Bank, OECD and IFAC to produce industry products like accounting standards to be used globally

98.6. Other capital receipts including profits on the sale of assets and intellectual property

98.7. Interest income (passive investment)

98.8. Dividend income (passive investment)

98.9. Royalty income and licensing fees for use of IP

98.10. Rental income from third parties for excess office space – eg. Association rents out excess office space in its building to non-member to ensure that under-utilised part of the building does not stand vacant.

98.11. Training attendance fees charge to firms or employers (non-members) where individual members and non-members work

98.12. Amounts received to Fund the Association's public benefit project activities (eg bursary schemes, education and academic support, community development projects etc)

98.13. Entrance, participation or exhibition fees to occasional events open to public to promote the industry (e.g entrance fees to industry shows)

98.14. Attendance fees for occasional technical events or forums open to public

98.15. Advertising income

98.16. Sale of technical books, journals, magazines to non-members (for example sale of medical journals to exempt entities like libraries, universities).

98.17. Cost recovery charges (no mark-up) to non-members to recover expenses incurred for their benefit (shared facilities, resources)

98.18. Admin and/or management fees charged to other (exempt) industry organisations (eg shared services or facilities of "related" industry organisations that are not members of each other)

98.19. Commission income or similar rewards from third parties for member participation or utilization of their services/ products

98.20. Levies raised by Law on third parties (eg employers) for non-member participation in collective bargaining / negotiations (Trade Unions).

The nature of businesses impacted

99. All taxpayers to whom section 30B applies, which include trade unions and member bodies.

Proposal

100. It is proposed that the wording of section 10(1)(d) and section 30B be harmonised to clarify what the difference is between “funding” and “receipts and accruals”, if any was intended.

101. It is proposed that the concept of “funding” be clarified so that it is clear what is “total funding” as the base of the calculation and what is “member funding” as the threshold. This is especially important to income sources, both passive and active, created from member fees.

Section 30B – Meaning of “substantially the whole”

Legal Nature

102. Section 30B requires “substantially the whole” of as a requirement in relation to funding income, spending and activities. This term is also used in many other sections.

103. SARS have issued BGR20 to clarify its interpretation of the clause as meaning 90% in the strict sense, but will allow 85% as a pragmatic approach.

104. It also then affirms that the taxpayer must use an appropriate method to determine the percentage as relates to the relevant circumstances.

105. Though this pragmatic approach is welcomed, the legislative uncertainty is not.

Factual Description

106. “Substantially the whole” is used for the determination of the threshold in 3 instances in section 30B. Together with the uncertainty of “funding” it makes for a very unclear legal position to implement practically.

107. For example, if a taxpayer uses 85% of the broader or narrow view on section 30B and is involved in a dispute with SARS, is the 85% tenable under law?

108. A concern is also expressed that SARS cannot take a formal interpretation such as 90% and then issue a legally binding BGR that is against its own clear interpretation.

The nature of businesses impacted

109. All taxpayers to whom the term “substantially the whole” applies.

Proposal

110. It is proposed that the term “substantially the whole” be replaced with 85% given that the latter is what SARS gives effect to.

111. It makes no sense to have uncertainty in the tax exempt space which could be resolved with a clear percentage.

Section 31 – Arm's length principle in relation to withholding taxes

Legal Nature

112. Section 31(1) of the Act is broad and extends to any transaction, arrangement, scheme, agreement or understanding and would apply to the advancement of funds from an offshore resident to a South African resident. An interest-free inbound loan therefore appears to fall into the ambit of section 31(1).

113. For section 31(2) to apply to an interest-free inbound loan, not only do the terms of the transaction have to fail the arm's length test, but there must also be a tax benefit as a result of the terms of the agreement. "Tax benefit" is defined as any avoidance, postponement or reduction of any liability to tax.

Factual Description

114. It is uncertain whether section 31(2) would be applicable to an inbound interest-free loan as from the perspective of the borrower, there is arguably no tax benefit as there is no deductible interest to claim.

115. If section 31(2) were invoked this would result in an imputed interest charge which would arguably reduce the taxable income of the borrower and therefore go against the tax benefit requirement in section 31(2). It is our understanding that the tax benefit requirement was to limit the application of section 31 to only provide for adjustments which resulted in an increased tax liability not a reduced liability. So from the borrower's perspective, SARS would not be able to apply section 31(2) to make an adjustment.

116. However, from the perspective of the lender, which is a separate legal entity but also potentially subject to tax in South Africa on any interest, it may derive a tax benefit as a result of the 'avoidance' of the withholding tax (WHT) on interest. The DTA provisions would, however, also need to be taken into consideration. Arguably section 31(2) allows SARS to impute a notional interest accrual for the lender and subject this to the WHT on interest. As the lender would not be subject to tax on the interest in its home country there is no double taxation so there is an argument the DTA would not apply, giving SARS the taxing rights with no DTA relief.

117. We note the findings in the BPR192 issued by SARS on 28 May 2015 that appears to provide SARS' view that in such cases SARS will not seek to apply the WHT on interest to an inbound interest free loan. However, taxpayers do not have full details of the facts under which the ruling was applied for.

The nature of businesses impacted

118. All taxpayers who have and provide inbound interest free loans.

Proposal

119. Clarity should be provided on whether section 31(2) would apply to inbound interest-free loans and whether the WHT on interest will be imposed on the non-resident lender.

Section 41 and 44 – Exclusions to application of the corporate rules

Legal Nature

120. The following words appear in a number places in the corporate rules (Section 41(1) definition of group of companies; section 44(14)(e)):

"*any amount constituting gross income of whatever nature would be exempt from tax in terms of section 10 were it to be received by or to accrue to that company*"

Factual Description

121. If this provision were to be applied literally, a number of the corporate rules would not apply and there would furthermore be no 'groups of companies' as most companies will at some stage receive dividends which are exempt from tax in terms of s10(1)(k).

122. In order for this legislation to make sense it needs to be interpreted to say if all income would be exempt.

The nature of businesses impacted

123. All taxpayers to whom the corporate rules apply.

Proposal

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

"*all amounts* constituting gross income of whatever nature would be exempt from tax in terms of section 10 were they to be received by or to accrue to that company"

Section 42(1)(a)(ii) – Asset for share transactions

Legal Nature

125. Section 42(1)(a)(ii) states in relation to the transfer of assets to a transferee:

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

…or

(cc) as trading stock, 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"

Factual Description

126. It is submitted that this provision lacks clarity as it could be interpreted as:

a) If the two parties are not part of the same group, it **must** be treated as trading stock; or

b) If the two parties are not part of the same group, it **may** be treated as trading stock

127. The EM explains that b) is the correct interpretation.

The nature of businesses impacted

128. All taxpayers to whom section 42 applies.

Proposal

129. 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(8)(b) – Asset for share transaction

Legal Nature

130. Section 42(8) provides that any debt that is transferred along with an equity share in exchange for an asset in terms of section 42 will not give rise to any immediate tax implication if it arose:

“ *Where a person disposes of …..*

(b) any business undertaking as a going concern to a company in terms of an asset-for-share transaction and that disposal includes any amount of debt that is attributable to, and arose in the normal course of that business undertaking, ….”

Factual Description

131. The question that arises in this regard is whether, if a business undertaking is disposed of as a going concern but the rollover aspects of section 42 are applied to only some of the assets the provision still applies in respect of all the debt. It is understood that it does.

The nature of businesses impacted

132. All taxpayers to whom section 42 applies.

Proposal

133. It is suggested that the wording be amended to state (changes in italics):

"(b) any business undertaking as a going concern to a company *and some of the assets are disposed* of in terms of an asset-for-share transaction and that disposal includes any amount of debt that is attributable to, and arose in the normal course of that business undertaking, …."

Section 45 – Intra-group transactions

Legal Nature

134. The current legislation contained in section 45(1)(b)(i) limits the compensation format payable by the transferee company to either be in the form of a loan (issue of debt) or for an exchange of shares (other than equity shares). No other payment format is contemplated based on the wording of this section.

135. In instances where the transferor company and the transferee company agree to settle the consideration by cash, for example, the relief sought in terms of section 45 is not available due to the current wording of the legislation. Generally, in terms of section 45(1)(b), an "intra-group transaction" includes, inter alia, any transaction where a transferor company disposes of equity shares held in foreign company to a transferee company **in exchange for the issue of debt or shares** other than equity shares by that transferee company.

136. The result is companies who may have the cash resources to settle the payment consideration and who may wish to do so by means of using cash resources – are excluded from using the relief that is provided by section 45(1)(b)(i). We have observed in practice that in these instances, the parties have had to first resort to entering into a loan agreement with its attendant essential (determining an arm's length interest rate, period of the loan, repayment terms, etc.) in order to fall within the parameters of the 45(1)(b)(i) group relief provisions. It is also noted that these loan agreements are often shortly thereafter settled using cash resources of the transferee company.

Factual Description

137. The historic EMs have not provided any reasoning as to why a cash settlement mechanism was excluded from the legislation introduced effective 1 Jan 2013. This may have been an oversight when the debt limitation rules were also introduced at the same time as there is no anti-avoidance that may arise by providing a cash settlement mechanism for utilising section 45(1)(b)(i) group relief transactions.

The nature of businesses impacted

138. All transferor and transferee companies that agree to settle the consideration for an intra-group transaction by cash.

Proposal

139. We submit that section 45(1)(b)(i) should be extended to include a cash settlement, as this will provide certainty for taxpayers wanting to use this manner of settlement without having to first enter into a loan agreement.

140. The availability of the option to use cash as a payment format for settlement of the consideration (in section 45(1)(b)(i)) will provide relief to taxpayers from both an administrative and legal perspective and will be more cost efficient as well for both parties.

Eighth Schedule: Paragraph 56 – Disposal by creditor of debt owed by connected person

Legal Nature

141. Paragraph 56(2)(a)(ii) allows a capital loss, determined in consequence of the disposal by a creditor of a debt owed by a debtor (who are connected persons), to be taken into account by the creditor to the extent that the amount of the debt so disposed of represents an amount which is applied to reduce any assessed capital loss of the debtor in terms of paragraph 12A.

Factual Description

142. Paragraph 12A was amended during the 2017 legislative cycle and it now requires a taxpayer to recalculate a gain or loss in these circumstances. Thus paragraph 56(2)(a)(ii) will no longer apply.

The nature of businesses impacted

143. Where a creditor disposes of a debt owed by a debtor, who is a connected person in relation to that creditor.

Proposal

144. Paragraph 56(2)(a)(ii) should be amended to align with the changes to paragraph 12A.

CATEGORY – VALUED ADDED TAX & CUSTOMS

Section 1 – "Electronic services"

Legal Nature

145. Section 1 of the VAT Act defines "electronic services" as those electronic services prescribed by the Minister by regulation in terms of the VAT Act.

146. On 18 March 2019, the revised ‘final’ regulations were published in the Government Gazette (by Government Notice No R221 of 28 March 2014, as amended by Government Notice No 429 of 18 March 2019) prescribing what constitutes ‘electronic services’ as contemplated in the VAT Act. The revised regulations come into effect on 1 April 2019.

Factual Description

147. The final regulations published contain a definition of “telecommunication services” to mean telecommunication services as defined in section 1 of the Electronic Communications and Transactions Act. However, there is no such definition in that Act.

148. It seems that electronic services supplied to an SEZ operator is subject to VAT at the standard rate. This seems to be an oversight as all services rendered to an SEZ operator should be subject to VAT at the rate of zero per cent.

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

150. It is also noted that the FAQ document does not address the fact that intermediaries can’t act or pay for VAT registered persons and that they can’t pay for VAT on the payment basis.

The nature of businesses impacted

151. All taxpayers conducting electronic services.

Proposal

152. More clarity should be provided in respect of the terms mentioned above.

153. The FAQ document should have the status of a binding ruling in order to clarify and confirm NT and SARS’ policy intention so as to avoid any future disputes in this regard.

Section 2 – Financial Services

Legal Nature

154. Section 2(1)(d) deems the issue, allotment or transfer of ownership of an equity security or a participatory security to be a financial service.

Factual Description

155. Section 2(1)(d) does not cater for the cancellation of an equity security and share buy-backs.

The nature of businesses impacted

156. Taxpayers cancelling shares and undertaking share buy-backs.

Proposal

157. Section 2(1)(d) should include the cancellation of an equity security and share buy-backs.

Section 8(25) – Deemed supplies and corporate rules

Legal Nature

158. Section 8(25) of the VAT Act provides that:

"*For the purposes of this Act, where any goods or services are supplied by a vendor to another vendor, those vendors must for the purposes of that supply or subsequent supplies of those goods or services, be deemed to be one and the same person provided the provisions of section 42, 44, 45 or 47 of the Income Tax Act are complied with…..*"

Factual Description

159. Based on the wording of the section, it would appear that if a transfer is made which complies with the requirements of the relevant corporate rule and is not excluded per the exclusion provisions, but an election is made (also in compliance with the section) not to apply the deferral provisions, section 8(25) of the Act still applies. However, this is not absolutely clear.

160. Furthermore, section 8(25) applies automatically but only to the extent that the relevant Income Tax provision applies. Where certain assets and liabilities are excluded, they do not qualify for section 8(25) relief and the VAT treatment must be considered separately.

161. In the absence of section 8(25), the transaction as a whole could have qualified for zero rating under section 11(1)(e) as the sale of an enterprise as a going concern. This may disadvantage vendors in a group of companies.

The nature of businesses impacted

162. Taxpayers to whom section 42 of the Income Tax Act applies, and specifically where not all the liabilities are a qualifying debt.

Proposal

163. It is suggested that the automatic application of section 8(25) be clarified in situations where the election is made not to apply the deferral provisions.

164. To treat vendors equally, we propose that a vendor should be able to elect whether or not section 8(25) should apply.

Section 8A(2)(c) – Sharia compliant financing arrangements

Legal Nature

165. This is a technical correction.

Factual Description

166. Section 8A(2)(c) of the VAT Act refers to section 24JA(5)(d) of the Income Tax Act but there is no such section in the Income Tax Act. Section 24JA was first included in the 2010 TLAB but since the insertion of this section there has not been a section 24JA(5)(d) and section 8A has also, since inception, noted this apparent incorrect cross reference.

The nature of businesses impacted

167. All taxpayers to whom these sections apply.

Proposal

168. The reference to section 24JA(5)(d) should be deleted and the reference to the correct sub-section should be inserted (perhaps section 24JA(3)(d).

Section 20(8) – Tax invoices

Legal Nature

169. Section 20(8) refers to an identity document as contemplated in section 1 of the Identification Act, 1997.

Factual Description

170. The Identification Act, 1997 does not contain a definition of an “identity document”. It does have a definition of an “identity card”.

The nature of businesses impacted

171. All businesses purchasing second-hand goods or repossesses goods where the supply to the recipient is not a taxable supply.

Proposal

172. The above mentioned reference should be corrected.

Section 21 – Credit and debit notes

Legal Nature

173. Section 21 of the VAT Act stipulates certain requirements for a valid credit/debit note. Any document which does not contain the particulars as envisaged in section 21(3)(a) or 21(3)(b) of the VAT Act, does not constitute a valid credit/debit note and as such a vendor is not entitled to claim an input tax deduction or an adjustment to output tax based on such document. One of the requirements in terms of section 21(3) is that the words “credit note” or “debit note” must be stipulated on the document. However, section 21(5) gives the Commissioner a discretion to accept a credit/debit note if one or more of the particulars are not contained on the document and if there are sufficient records available, or will be available, to establish the particulars of the supply and if it would be impractical to require a full credit/debit note.

Factual Description

174. SARS is currently regarding as invalid, any credit/debit notes that do not have the specific words "credit note" or "debit note" on the face of it. Disallowing valid credit/debit notes because of the specific wording on the document does not seem reasonable especially in light of the discretion given to the Commissioner in terms of section 21(5) and the *South Atlantic Jazz Festival (Pty) Ltd v Commissioner for the South African Revenue Service* [2015] ZAWCHC 8 court case ruling.

175. Furthermore, in 2015 changes were made to section 20 relaxing the particulars required for a tax invoice - that is, the words "tax invoice", "VAT invoice" or "invoice" were subsequently allowed to be stipulated on an invoice not just the words "tax invoice". This reason provided for this amendment was because it did not compromise the audit trail or policy intent for the requirements of the section.

The nature of businesses impacted

176. All vendors who issue credit/debit notes.

Proposal

177. It is recommended that section 21 be relaxed as was done for section 20 in cases were the only missing information from a credit/debit note is the words "credit note" or "debit note" and there are sufficient records available, or will be available, to establish the particulars of the supply.

Section 23 – Registration for VAT

Legal Nature

178. The proviso to section 23(1), provides as follows:

"*Provided that the total value of the taxable supplies of the vendor within the period of 12 months referred to in paragraph (a) or the period of 12 months referred to in paragraph (b) shall not be deemed to have exceeded or be likely to exceed the amount contemplated in paragraph (a), where the Commissioner is satisfied that the said total value will exceed or is likely to exceed such amount solely as a consequence of –*

(i) any cessation of, or any substantial and permanent reduction in the size or scale of, any enterprise carried on by that person; or

(ii) the replacement of any plant or other capital asset used in any enterprise carried on by that person; or

(iii) abnormal circumstances of a temporary nature".

179. Section 23(1A) reads as follows:

"*Every person who carries on any enterprise as contemplated in paragraph (b)(vi) or (vii) of the definition of ''enterprise'' in section 1 and is not registered becomes liable to be registered at the end of any month where the total value of taxable supplies made by that person has exceeded R1 million in any consecutive 12-month period*".

Factual Description

180. The proviso to section 23(1), in particular par (iii) of the proviso to section 23(1), does not currently apply to section 23(1A).

The nature of businesses impacted

181. A person supplying electronic services from a place in an export country as defined in paragraph (b)(vi) and the activities of an intermediary as defined in paragraph (vii) of the definition of ''enterprise'' in section 1.

Proposal

182. The proviso to section 23(1), in particular par (iii) of the proviso to section 23(1), should also apply to section 23(1A).

Section 52 – Pooling arrangements

Legal Nature

183. In terms of section 52 of the VAT Act, any pool managed by any body for the sale of agricultural, pastoral or other farming products and any rental pool managed or operated by a person for the benefit of its members is regarded as a separate enterprise carried on by the operator/manager separately from the members and shall be registered separately for VAT, provided certain requirements are met.

Factual Description

184. Since the implementation of section 52, vendors have been applying and receiving VAT rulings in terms of section 72 allowing them to register the Pool as a separate enterprise, resulting in the Pool accounting for VAT for all supplies made by the Pool members and deducting all the VAT incurred by the Pool members. With a pooling arrangement, the members will not be required to register, thus reducing the administration of the registration of various entities managed and operated by an Operator.

185. On 21 July 2019, National Treasury proposed amendments to section 72 of the VAT Act which will result in the Commissioner being unable to continue to provide the dispensation previously provided (see comments on this section below).

186. The proposed amendments to section 72 of the VAT Act will have a negative impact on various vendors that have been granted a dispensation for section 52 of the VAT Act as it would mean that all vendors who have been granted a section 72 ruling will no longer have that dispensation and the Pool would have to deregister as a VAT vendor and all

the members of the Pool would have to register for VAT individually. The members would have to account for the VAT and deduct the VAT incurred by each individual member.

187. The above process would be an administrative and costly exercise for the Pool, its members and SARS. In this regard, all the members of the Pool would have to go through the registration process without any benefit to the fiscus despite them operating like rental schemes and agricultural pools.

188. As early as 2013, there have been submissions to NT and SARS to amend section 52 of the VAT Act to include other vendors that operate pooling arrangements similar to those defined in section 52 of the VAT to be included in that section.

The nature of businesses impacted

189. Various vendors that have been granted relief in terms of section 72 for a dispensation for section 52 of the VAT Act.

Proposal

190. It is proposed that section 52 of the VAT Act should be amended to include all vendors that have pooling arrangements similar to those currently contained in section 52 of the VAT Act.

Section 67(1) – Contract price or consideration may be varied according to the rate of VAT

Legal Nature

191. The second proviso to section 67(3) of the VAT Act provides as follows:

"… Provided further that this subsection shall not be construed so as to permit any further increase or require a further decrease, as the case may be, in a fee, charge or other amount referred to in this subsection, where such fee, charge or other amount is calculated as a percentage or fraction of another amount which represents the consideration in money for a taxable supply of goods or services, other than a taxable supply charged with tax at the rate or zero per cent or a supply which is an exempt supply."

192. Section 67(1) reads as follows:

"Whenever the value-added tax is imposed for the first time in terms of this Act or the rate of tax applicable under section 7(1) is increased in respect of any supply of goods or services in relation to which any agreement was entered into by the acceptance of an offer made before the tax was imposed for the first time in terms of this Act or the rate of tax applicable under section 7(1) was increased, as the case may be, the vendor may, unless agreed to the contrary in any agreement in writing and notwithstanding anything to the contrary contained in any law, recover from the recipient, as an addition to the amounts payable by the recipient to the vendor, a sum equal to any amount payable by

the vendor by way of the said tax or increase, as the case may be, and any amount so recoverable by the vendor shall, whether it is recovered or not, be accounted for by the vendor under the provisions of this Act as part of the consideration in respect of the said supply."

Factual description

193. The second proviso to section 67(3) does not currently apply to section 67(1). Where section 67(1) applies, a vendor may currently increase its fees with the VAT rate (currently 15%) notwithstanding that its fees may already have been calculated with reference to another VAT inclusive amount.

The nature of businesses impacted

194. Taxpayers whose fees or commissions are calculated as a percentage of another VAT inclusive amount, most recently, foreign suppliers of electronic services who first became liable to register for VAT on 1 April 2019.

Proposal

195. To ensure all vendors are treated equally, it is suggested that the wording of the second proviso to section 67(3) should also apply to section 67(1).

Interpretation Note 92

Legal Nature

196. Interpretation Note 92 prescribes the documentary proof required under section 16(2)(f) that must be obtained and retained by a vendor to substantiate the vendor's entitlement to a deduction as contemplated in section 16(3)(c) to (n).

Factual Description

197. In Interpretation Note 92, in the table under point 3. and under Item H, the documentary proof required is reflected as "proof that the underlying supply of goods or services was taxable at 14%".

The nature of businesses impacted

198. All taxpayers who are VAT registered and who redeem tokens, vouchers or stamps (section 16(3)(i)).

Proposal

199. The VAT rate must be changed to 15% as it still makes reference to 14% instead of 15%.

CATEGORY – TAX ADMINISTRATION ACT (TAA)

Section 1 – Definition of "Official Publication"

Legal Nature

200. Section 1 of the TAA defines "Official Publication" as follows: "*a binding general ruling, interpretation note, practice note or public notice issued by a senior SARS official or the Commissioner*".

Factual Description

201. Currently the Business Requirement Specification (BRS) documents are not included in the section 1 definition of 'Official Publication' and these also do not form part of the section 5 TAA Practice Generally Prevailing and are listed and treated as 'Guides' or 'External Publications' by SARS.

The nature of businesses impacted

202. All taxpayers who are required to use the numerous BRS documents.

Proposal

203. Given that BRS documents contain instructions on the form and content of various different topics and are not guides (i.e SARS informal view) as taxpayer must follow them, they should be included in the definition of "official publication".

Section 11 – Definition of the word "week"

Legal Nature

204. Section 11 of the TAA Act deals with legal proceedings involving the Commissioner. Section 11(4) reads as follows: "*Unless the court otherwise directs, no legal proceedings may be instituted in the High Court against the Commissioner unless the applicant has given the Commissioner written notice of at least one week of the applicant's intention to institute the legal proceedings.*"

Factual Description

205. The word "week" is not defined in the TAA. It is thus unclear what constitutes a week – whether its business days or calendar days.

The nature of businesses impacted

206. All taxpayers who wish to institute legal proceedings at the High Court against the Commissioner.

Proposal

207. The TAA must either contain a definition of a week or change section 11(4) of the TAA to reflect either 7 business days, 5 business days or 7 calendar days, whichever is applicable.

208. The issue is that the taxpayer might understand a week to mean something different from the intended time period by SARS, which could result in the taxpayer providing a written notice in a time period less than what is required. This can delay the instituting of legal proceedings.

Section 16 & 20 – Office of the Tax Ombud: Mandate & Resolution and recommendations

Legal Nature

209. The Tax Ombud must attempt to resolve all issues within the Tax Ombud's mandate at the level at which they can most efficiently and effectively be resolved and must, in doing so, communicate with SARS officials identified by SARS.

Factual Description

210. No time frames are provided in section 20 for SARS to respond to the Tax Ombud's queries raised with it. Neither is there a time frame in section 16 for the Tax Ombud to provide feedback to a taxpayer on its review of the complaint lodged by the taxpayer.

The nature of businesses impacted

211. All taxpayers who have lodged a complaint with the Tax Ombud.

Proposal

212. SARS should have a compelled timeframe (30 days) within which it needs to provide feedback to the Tax Ombud. The Tax Ombud in turn, should have compelled timeframes (30 days) in which it has to provide feedback to a taxpayer in respect of a complaint lodged by a taxpayer.

Section 34 – Reportable arrangements

Legal Nature

213. The term "reportable arrangement" is defined in section 34 of the TAA. Persons who enter into these arrangements must report the details of those transactions to SARS. A "reportable arrangement" does not in itself give rise to a tax liability, but may give rise to a report which is required to be submitted to SARS – the failure of which could give rise to significant penalties.

214. Section 35(1) sets out the legislative circumstances in terms of which an arrangement may be reportable. In addition, section 35(2) provides that an arrangement will be a reportable arrangement if it is listed by the Commissioner in a public notice.

215. Sections 36-39 deal with the excluded arrangements, disclosure obligations, information to be submitted by taxpayers to SARS when reporting these arrangements and the reference numbers required to be issued by SARS.

Factual Description

216. These provisions, and inclusion of public notices listing additional reportable arrangements, currently create a lot of uncertainty for both SARS and taxpayers. One example of this is when does the clock for the 45-day period in terms of section 37(5) start ticking, especially in the case of agreements that are void due to non-fulfilment of conditions that should be reported.

The nature of businesses impacted

217. All taxpayers who have fall within the provisions of reportable arrangements.

Proposal

218. These provisions should be rewritten in their entirety; alternatively, clear guidance should be provided on how these provisions are to be applied in relation to various practical scenarios.

Section 93 and 104 – Reduced assessments and objection against assessment or decision

Legal Nature

219. Both section 93(1)(d) and section 104 of the TAA provide a remedy where a taxpayer is not in agreement with an assessment and wishes to dispute it.

220. Section 93(1)(d) merely provides for a less formal remedy based on a much narrower circumstance; namely a readily apparent undisputed error in the assessment.

Factual Description

221. The law does not regulate the procedure or timelines in respect of section 104 when a remedy is sought under section 93. It is thus uncertain whether the one remedy delays the other or if the one remedy is subject to the other.

222. This results in taxpayers either losing the section 104 remedy should SARS not respond to the section 93 request within 30 days from the date of assessment, or it compels the taxpayer to make two separate submissions to two separate SARS channels (one to request a section 93 correction and the second one is the lodgement of an objection in terms of section 104). A withdrawal of the objection is then necessary if the section 93 remedy is successful.

223. Having to run two separate procedures is both time consuming and a waste of resources for both taxpayers and SARS.

The nature of businesses impacted

224. All taxpayers requesting a reduced assessment in terms of section 93 of the TAA.

Proposal

225. It is proposed that taxpayers be allowed to submit an objection within 14 days after the receipt of a response from SARS on the section 93 application. Given the narrow circumstance in which section 93 applies, this time period should not unduly delay the objection process or provide much opportunity to abuse it to “win” time.

Section 104 – Objection against an assessment or decision (diesel rebates)

Legal Nature

226. Section 4 of the TAA states that the TAA is applicable to the provisions of a “tax Act”. “Tax Act” is defined in section 1 but it specifically excludes customs and excise legislation.

227. Administration of the diesel refund system is done through both the Customs and Excise Act, 1964 (C&E Act), and the VAT Act. Part 3 of Schedule No. 6 of the C&E Act regulates the administration of the diesel refund system by SARS, while actual claims and refunds are administered through the VAT system.

Factual Description

228. It is unclear as to how one may object against the disallowance of diesel rebates where no assessment is issued, as the customs and excise legislation is specifically excluded from the provisions of the TAA.

The nature of businesses impacted

229. All taxpayers wanting to object against the disallowance of a diesel rebate.

Proposal

230. Clarity should be provided in the customs and excise legislation on how to object against the disallowance of a diesel rebate.

Section 125 – Appearance at a hearing of the tax court

Legal Nature

231. The right of appearance in a tax court is currently regulated by section 12 and section 125 of the TAA. These sections set out when a senior SARS official may appear on behalf of SARS or the Commissioner in proceedings in any matter before the Tax Court or High Court.

Factual Description

232. Section 125(1) of the TAA provides that a senior SARS official, referred to in section 12 of the TTA, may appear at the hearing of an appeal in support of an 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*".[1]

233. It is, therefore clear that the TAA originally envisaged clients of tax practitioners to be represented by tax practitioners at a hearing of an appeal, but this right of appearance has since been removed from the TAA.

The nature of businesses impacted

234. All taxpayers using a tax practitioner to assist them with their tax affairs.

Proposal

235. Given the importance of these matters within the Chartered Accountancy profession and specifically within the tax industry, right of appearance for tax practitioners is sought in respect of the process and proceedings involving a dispute between the taxpayer and SARS that is before the courts – that is, the right to appeal against an assessment/decision made by SARS in the Tax Court.

236. Section 125(2) should thus be reinstated into the TAA.

Section 164 – Payment of tax pending objection and appeal

Legal Nature

237. Section 164(5) provides for a SARS official to deny a request to suspend a payment of tax due. It also provides for a SARS official to revoke a decision to suspend payment with immediate effect if certain criteria are met.

Factual Description

238. Other than relying on the provisions of the Promotion of Administrative Justice Act (PAJA) on the basis that these decisions/actions constitute unreasonable administrative action, there seems to be no remedy for taxpayers should SARS decide to deny a request for suspension of payment or should it decide to revoke a decision to suspend payment in terms of subsection (3).

The nature of businesses impacted

239. All taxpayers who request a suspension of payment of tax due and whose requests are denied or decisions to allow the suspension are revoked.

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1 The sub-section used to read as follows: "The 'appellant' or the 'appellant's' representative may appear at the hearing of an appeal in support of the appeal". It was deleted by s. 26 of Act, No. 13 of 2017.

Proposal

240. Taxpayers should be provided with an option to object to such decisions if they believe that the position taken by the senior SARS official is not justified. This would prevent taxpayers from having to rely solely on the provisions of the PAJA which is often a long and costly option of dispute resolution.

Section 210 (read with section 208) – Definition of "preceding year"

Legal Nature

241. In terms of 210 of the TAA, where the SARS is satisfied that non-compliance by a person (as detailed in section 210(2)) exists, SARS must impose the appropriate penalty in accordance with the table in section 211 (Fixed Amount Penalty Table).

Factual Description

242. Non-compliance in terms of section 210(2) includes the failure to comply with an obligation that is imposed by or under a tax Act, subject to certain exclusions. For example, the failure by a company to submit a tax return would constitute non-compliance, subject to which a penalty may be imposed.

243. The Fixed Amount Penalty Table prescribes that the penalty should be calculated with reference to the assessed loss or taxable income for the 'preceding year'. The term 'preceding year' is defined in section 208 to mean "the year of assessment immediately prior to the year of assessment during which a 'penalty' is assessed".

Problem statement

244. As an example, a company has a December year-end, and both its 2016 and 2017 returns are outstanding, SARS now levies the fixed amount penalty in the 2019 calendar year. From the existing definition of 'preceding year', because the penalty is assessed in 2019, 2018 is the year immediately prior the year in which the penalty is assessed. However, as this year has not yet been assessed, SARS would not know what the assessed loss / taxable income is and can therefore not determine the penalty. Where it was the intention of the legislator to mean the last assessed year of assessment, it is submitted that this may be more appropriate.

Proposal

245. It is proposed that the definition of the term 'preceding year' be amended to clarify that "the year of assessment immediately prior to the year of assessment during which a 'penalty' is assessed" is in fact intended to refer to the last assessed year of assessment.

Section 223 – Understatement penalty percentage table

Legal Nature

246. Section 223 of the TAA imposes penalties for an "understatement" made by a taxpayer in certain circumstances. Column 5 and 6 of the penalty table reduces the penalty

depending on whether there was a voluntary disclosure by the taxpayer before or after a notification of an audit or criminal investigations.

Factual Description

247. Section 223 does, however, not refer to "Voluntary Disclosure Programme" as contained in Part B of Chapter 16 of the TAA and uncertainty remains as to whether the words "voluntary disclosure" in section 223 means "Voluntary Disclosure Programme" as contained in Part B of Chapter 16 of the TAA or if it is just the normal grammatical meaning of term "voluntary disclosure" should be applied.

248. From SARS' website it seems that the SARS' position is that the taxpayer must have applied under Part B of Chapter 16 of the TAA. However, in practice it seems that there are differing approaches followed by SARS and taxpayers – those ranging from the normal grammatical meaning of the term, to those *applied* under Part B, to those *qualifying* under Part B and even to the extreme of having a signed contract under Part B.

249. This difference in interpretation and practice by SARS and taxpayers makes it very difficult for taxpayers to understand and know their obligation in order to qualify for the relief.

The nature of businesses impacted

250. All taxpayers who are subject to an understatement penalty in terms of section 223 and to whom columns 5 and 6 of the understatement penalty percentage table apply.

Proposal

251. It is requested that SARS clarify what is meant by "voluntary disclosure" in section 223 and we submit that at most it should involve having made an application as envisaged in section 226(1) of the TAA.

Section 240 – Registration of tax practitioners

Legal Nature

252. Section 240(3) lists the circumstances under which a person cannot register as a tax practitioner.

Factual Description

253. Section 240(3) does not mention a person that is insolvent meaning that an insolvent person can register as a tax practitioner.

The nature of businesses impacted

254. All insolvent or rehabilitated insolvents.

Proposal

255. SARS and NT should clarify what their position is with regard to the registration of a person who is insolvent or a rehabilitated insolvent as a tax practitioner.

Annexure B

2018 ANNEXURE C SUBMISSION

1. We note that, with the exception, as noted below, most of the proposals made in terms of the SAICA Annexure C submission made on 26 November 2018 were not accepted or implemented by NT.

2. The exception, which have been implemented or partially implemented by NT, is the following:

    - NT undertook in Parliament to host a residency workshop to discuss the proposed amendments to section 10(1)(o) of the Act which it did hold in April 2019.

CATEGORY - INCOME TAX: INDIVIDUALS, EMPLOYMENT AND SAVINGS

NOT IMPLEMENTED - Section 7C – "Unpaid" distributions to beneficiaries of a Trust

Legal Nature

3. Section 7C of the Act promulgated on 19 January 2017 came into effect on 1 March 2017 and applies to any amount owed by a trust in respect of a loan, advance or credit provided to that trust by a connected person (including a beneficiary) before, on or after that date.

Factual Description

4. Historically trustees of discretionary trusts have exercised their discretion and vested amounts in the hands of beneficiaries in terms of section 25B of the Act and paragraph 80 of the Eighth Schedule to the Act. However, as allowed in terms of discretion provided to the trustees by the trust deeds, these amounts were not "paid" to the beneficiaries. Typically, these amounts have been disclosed on the financial statements of the trust as "amounts owed to beneficiaries".

5. The question arises whether these amounts that have been vested in the hands of the beneficiaries are considered to be "any loan, advance or credit" as contemplated in section 7C as an unpaid vested amount would arguably be "any loan, advance or credit".

6. Since the introduction of section 7C various commentators and tax specialists in South Africa have expressed different and contrasting views on this. In the Explanatory Memorandum to the Taxation Laws Amendment Bill 2016, the following comments have been expressed by NT:

    "The proposed rules will apply only in respect of loans advanced or provided by a natural person or, at that person's instance, by a connected company. An amount that is vested irrevocably by a trustee in a trust beneficiary and that is used or administered for the

benefit of that beneficiary without distributing or paying it to that beneficiary will not qualify as a loan or credit provided by that beneficiary to that trust if:

- *The vested amount may in terms of the trust deed governing that trust not be distributed to that beneficiary, e.g. before that beneficiary reach a specific age; or*
- *That trustee has the sole discretion in terms of that trust deed regarding the timing of and the extent of any distribution to that beneficiary of such vested amount.*

An amount vested by a trust in a trust beneficiary that is not distributed to that beneficiary will, however, qualify as a loan or credit provided by that beneficiary to that trust if that non-distribution results from an election exercised by that beneficiary or a request by that beneficiary that the amount not be distributed or paid over, e.g. if the beneficiary has reached the age which a vested amount must be paid over or distributed to him or her".

7. In the first instance it is noted that the above view was expressed in relation to an example that did not directly deal with unpaid trust distributions but indirect loans. It is submitted that based on above, it appears that NT and SARS may not have intended to regard the amounts that have been vested in the hands of the beneficiaries without actually paying it as "loan, advance or credit" for the purpose of section 7C.

8. However, it remains unclear what the relevance is of the above statement "*unless the beneficiary elected or requested that the amount should not be paid to him/her*", as without the trust deed providing for such discretion it cannot be unilaterally withheld. Where such discretion is exercised in terms of the trust deed, i.e. payment is also subject to a discretion, it may impact on the actual vesting of the amount (i.e. vesting creates a right to demand immediate payment for the benefits to flow).

9. The lack of clarity in this regard leaves taxpayers in an uncertain position where the wording of the legislation (section 7C) and the Explanatory Memorandum may not be completely aligned and reflective of NT intention.

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

10. All beneficiaries of discretionary trusts, where the amounts have been vested in the hands of the beneficiaries, but not yet paid.

<u>*Proposal*</u>

11. It is requested that the legislation be amended to expressly clarify under which circumstances unpaid distributions from a discretionary trust constitute a loan, advance or credit for section 7C purposes, or less ideally, that a Binding General Ruling be issued in this regard.

NOT IMPLEMENTED – Section 25(5) and section 7C of the Act – application of section 7C in relation to a deceased estate

Legal Nature

12. Section 25(5) of the Act, effectively deems a deceased estate to be a natural person for income tax purposes. Currently section 7C of the Act is not excluded from the application of section 25(5) of the Act.

Factual Description

13. As the main purpose behind section 7C of the Act is to discourage the use of trusts for estate planning purposes, section 7C should no longer apply after a person's date of death (being the relevant date as at which the liability for estate duty is determined).

14. In the absence of the exclusion of section 7C from section 25(5), these sections when read together could have the unintended consequence of a loan, advance or credit owing to a deceased estate giving rise to an application of section 7C in relation to the estate i.e. resulting in a deemed donation by that estate, which is contrary to the rationale of section 7C.

15. A further anomaly that arises in relation to section 25(5) is that, despite being treated as a natural person, a deceased estate could never be a "resident" as defined in section 1 of the Act as after death one can no longer be said to be ordinarily present or physically present in the Republic (even if that was the case before death).

The nature of the business impacted

16. All deceased estates, where a loan was granted by the deceased (to which section 7C applies).

Proposal

17. Section 25(5) of the Act, which has the effect of deeming a deceased estate to be a natural person other than for the application of certain sections, should not apply to section 7C effective 1 March 2017.

18. Clarity is also needed as to how the residency status of a deceased estate should be determined for income tax purposes.

NOT IMPLEMENTED – Section 7C(1A) of the Act – clarification of loan rights

Legal Nature

19. We note that the inclusion in section 7C(1A) of the Act is aimed at covering instances where a loan is granted by a person and thereafter the loan is bequeathed or donated to another person.

Factual Description

20. The phrase "person acquires a claim" is used, without including a definition of "a claim", which leaves this broad term open to interpretation. For example, in the case of a deceased estate of a person who advanced a loan to a trust, upon death, the deceased estate is considered to be a person for purposes of the Act, but the provisions of section 7C are not intended to apply to a deceased estate. The executor of the estate is appointed to wind up the deceased estate and if there are distributions thereafter, these will be distributed to the heirs/legatees of the deceased.

21. In this scenario, it is unclear whether the executor would be treated as having acquired the claim of the loan to the trust. However, that the executor is not a connected person in relation to the trust, in terms of the definition of connected person in relation to a trust. It is not clear whether the application of section 7C would then be switched off at death as the claim of the loan is treated as having been acquired by the executor who is not a connected person in relation to the trust.

22. Alternatively, if the executor is not treated as having acquired a claim to the loan, the heirs/ legatees (on the assumption that they are connected persons to the trust) would then be treated as having acquired the claim in relation to the loan. If this is the case, the date of the acquisition of such claim is not clear from the legislation. This claim could either be acquired on death of the funder of the loan or only on the date on which the estate is wound up and the loan remains for the inheritance of the heirs/legatees.

23. Furthermore, it is seemingly not required that the loan be acquired (i.e. loan ceded), but merely that a claim to an amount owing is acquired. This also raises concern as to whether debt security cessions or other security arrangements fall within the ambit of section 7C.

The nature of the business impacted

24. All deceased estates and heirs/legatees, where a loan was granted by the deceased (to which section 7C applies) and subsequently inherited by the heirs/legatees.

Proposal

25. We request that the word "claim" be defined in the Act. To eliminate the scope for differing interpretations, we submit that clarity be provided on the term "acquisition of a claim", specifically in the context of deceased estates.

26. We further request clarity on how a claim for purposes of this provision is regarded as having been acquired and how it is validated and effected. Clarification is sought in the legislation as to whether the acquisition of a claim is a lesser or broader right than a ceded loan.

<u>NOT IMPLEMENTED – Section 7C of the Act – extension to company loans</u>

<u>Legal Nature</u>

27. In the 2017 amendments the legislator widened the scope of section 7C by also including loans to companies where 20% or more of the shares of the company are held directly or indirectly by a trust or a beneficiary of the trust.

28. The insertion of section 7C(1)(ii) in 2017, as amended in terms of the Taxation Laws Amendment Bill of 2018, makes the application of section 7C overly broad so as to apply to transactions that were not intended to be subject to section 7C.

29. The amended section 7C(1)(ii) reads as follows:

"(ii) a company if at least 20 per cent of—

(aa) the equity shares in that company are held, directly or indirectly; or

(bb) the voting rights in that company can be exercised,

by a trust referred to in subparagraph (i) whether alone or together with any person who is a beneficiary of that trust or the spouse of a beneficiary of that trust or any person related to that beneficiary or that spouse within the second degree of consanguinity."

<u>Factual Description</u>

30. The reason for the introduction of section 7C of the Act was stated in the Explanatory Memorandum to the Taxation Laws Amendment Bill 2016 as introducing measures to combat the avoidance of donations tax and estate duty by taxpayers who utilised interest-free loans to transfer assets/wealth:

"At issue is the avoidance of estate duty and donations tax when a person transfers wealth through the use of an interest free loan or a loan with interest below market rates. These loans are either used to facilitate the transfer of assets or assist the trust to acquire an asset. This is done in order to avoid donations tax as no donation arises on the sale of an asset or on advancing loan funding to a trust."

31. Although the legislator had a specific mischief/avoidance in mind with this amendment (taxpayers transferring wealth to companies where the shares of the companies are being held by trusts where such wealth would grow outside the "estate" of the taxpayer) these amendments appear to have a number of unintended consequences.

32. Firstly, the use of a company the shares of which are held by a trust as a structure for the avoidance of Estate Duty is not the only reason why interest-free or low interest loans are provided to companies. Normal trading companies receiving working capital loans from the owners of these companies are now also affected by section 7C.

33. These loans are provided to the companies in question as part of the normal trading operations and to provide for the cash flow needs of the companies in question and are not for the purposes of transferring wealth to trusts or for the purpose of future reduction of estate duty. Also, in some instances the shareholding in the companies are held in trusts to provide protection to the natural person beneficiaries from potential claims that might arise from other risky trading ventures also conducted by the natural person and not for the purpose of avoiding Estate Duty.

34. Secondly, as section 7C applies to loans made by both natural persons or companies at the instance of a natural person, the impact of section 7C(1)(ii) is that even goods or services provided on credit by one company to another company through normal trading transactions the shares of which are already under a trust structure may potentially, at least on the literal wording of the provision, invoke the application of section 7C if the transaction was done at the instance of the specified natural person.

35. Thirdly, section 7C(1)(ii) could in certain instances result in section 7C being applied to funding derived from the same amount of a loan more than once, for example, where Mr A provides a loan to Company A (shares of which are held by Trust B) and Company A then on-advances the same funds to Company C (the shares of which are also held by Trust B). Section 7C will then potentially apply to both loans, which seems absurd.

36. The impact of section 7C appears to be much wider than the stated purpose as per the original Explanatory Memorandum released in 2016, as loans in the above circumstances have either nothing to do with the trust or else were not advanced for purposes of avoiding estate duty.

The nature of the business impacted

37. Any company that has been provided with a loan by a natural person who holds at least 20% of equity shares or voting rights in that company, while such natural person is also a beneficiary in relation to a trust.

Proposal

38. It is submitted that at the very least there should be a requirement of a direct or indirect shareholding by the trust in the company in excess of 50% alone or together with any other connected persons, since no trust beneficiary would dispose of the debt and assets to an independent majority shareholder to merely avoid estate duty. The current threshold in section 7C(1)(b)(ii) is too low.

39. The importance of the overly broad application of section 7C of the Act was also raised in our 2017 Annexure C submission.

NOT IMPLEMENTED – Section 7C of the Act – interpretation of the phrase "at the instance of"

Legal Nature

40. In relation to section 7C of the Act, there is very little precedent regarding the interpretation of the phrase "at the instance of" a natural person.

41. There is considerable uncertainty as to the ambit of the provision in relation to low interest loans provided by companies i.e. subsection 7C(1)(b) of the Act.

Factual Description

42. For example, in the case of a company the shares of which are held by a discretionary family trust, is a loan "at the instance of" a natural person if the natural person is a director of the company and is also a member of the family? In the latter situation such an outcome would be absurd, since there is no estate duty benefit to such a person by the provision of the loan (the shares in the company are outside the estate of the natural person, since they are already held by the trust).

The nature of the business impacted

43. Low-interest loans between companies that are already under a discretionary family trust structure appear to be hit by the provision.

Proposal

44. It is submitted that the ambit of the provision would be better clarified in line with policy intent by the inclusion of an estate duty benefit trigger as a requirement and the deletion of the phrase "at the instance of that person" in subsection 7C(1)(b) of the Act.

45. The trigger could be worded *"[and] in the case of any loan, advance or credit contemplated in subsection (1)(b), any share in the company would have directly or indirectly formed part of the estate, as defined in section 1 of the Estate Duty Act No. 45 of 1955, of the natural person at any time during the year of assessment, had the natural person died at such time"*.

NOT IMPLEMENTED – Section 7C(3) of the Act – calculation of deemed donation on last day of year of assessment

Legal Nature

46. In terms of section 7C(3) of the Act a deemed donation is made on the last day of the year of assessment of the trust. The issue is that the loan balance is not necessarily determinable on year-end date.

Factual Description

47. Example: If one assumes the trust's year of assessment ends on 28 February, the deemed donation must be calculated on 28 February. The loan balance is not

necessarily determinable on 28 February. The financial statements of the trust are the only accurate indication of what the loan amount should be. As the financial year only ends on 28 February, the financial statements will not yet be available and will only be available a few months after that (tax certificates are required, etc.).

The nature of the business impacted

48. Applicable to all trust and/or companies having an outstanding loan, advance or credit provided by a connected person in terms of which section 7C of the Act would be applicable.

Proposal

49. We propose that the Act needs to provide additional time for the calculation of the deemed donation in terms of section 7C of the Act.

NOT IMPLEMENTED – Section 7C and section 60 of the Act – payment of donations tax by the end of the following month

Legal Nature

50. In terms of section 60 of the Act, donations tax is payable by the end of the month following the month during which a donation takes effect. The Commissioner can allow for a longer period in terms of section 60(1) of the Act.

Factual Description

51. As the donations tax return cannot be submitted via e-filing, an IT144 form needs to be completed manually and submitted to SARS along with proof of payment.

52. The problem is firstly that the payment of this donations tax needs to be loaded onto eFiling and processed as a “credit push” transaction. Because the system does not provide for it, the payment has to be made as an overpayment of income tax that SARS then later has to allocate to donations tax.

53. Secondly, the time period of 31 days (end of March) is not enough time to allow for the calculation and payment, as well as the allocation of the payment in this instance.

The nature of the business impact

54. Section 59 of the Act provides that the donor will be liable for donations tax. Hence all natural persons that provided interest free loans or low interest rate loans to the trust would be impacted.

Proposal

55. It is submitted that SARS will have to adjust the eFiling system to provide for the submission of donations tax returns and the payment of the donations tax via eFiling. It

appears that the period of 30 days has to be extended in the case of section 7C deemed donations.

NOT IMPLEMENTED – Section 7C(5)(h) of the Act – exclusion of employer share trusts from section 7C

Legal Nature

56. Section 7C(5)(h) of the Act excludes employee share schemes from the application of section 7C to ensure that such schemes are not negatively affected. Certain requirements must, however, be met for the exclusion to apply.

Factual Description

57. Whilst the amendment to exclude employee share scheme trusts is welcomed, we respectfully remind NT that it was proposed in the 2017 Budget Review that an exclusion for business trusts and therefore business companies held by trusts, would also be introduced.

58. In many instances, trusts are used to conduct active trades (business trusts) and the interest-free loans made are representative of the equity or capital introduced by the entrepreneur into the business.

59. The latter is similar to interest-free loans made by a shareholder to a company (with which no objection can be found). It is therefore submitted that the ambit of the provisions of section 7C of the Act have been cast too widely in this regard.

60. An exclusion should be provided for trusts that conduct an active trade as these trusts and the concomitant interest-free loans have not been set up with the sole or main purpose of avoiding Estate Duty or Donations Tax.

61. The trusts pay tax on their taxable income derived from an active trade and retained by the trust at the rate of 45%.

62. While hypothetically interest could be levied on such loans in order to avoid the penal consequences of section 7C(3) of the Act, in many instances it will not be practically possible to do so. For example, the trust may have external borrowings in respect of which the levying of interest may result in a breach of any covenants, bearing in mind that the interest-free loan is effectively equity.

The nature of the business impacted

63. All business trusts carrying on an active trade as well business companies held by trusts, which have a loan that will fall within the ambit of section 7C of the Act.

Proposal

64. The exclusion of *bona fide* employer share incentive trusts is welcomed and must be extended to business trusts carrying on an active trade as well business companies held by trusts.

NOT IMPLEMENTED – Incidental impact of section 7C – Charged interest and the National Credit Act No 34 of 2005 (the NCA)

Legal Nature

65. We have noted that loans that were previously interest free but that have been made interest bearing to minimise the impact of section 7C, may have an unintended impact in relation to the NCA.

Factual Description

66. Simplistically, any loan granted to a trust will generally be termed a credit agreement as defined in the NCA under the provisions of section 8(4)(f)[2] of the NCA. Alternatively, such loan granted to a trust may fall within the ambit of section 8(3)[3] of the NCA being a credit facility or section 8(5)[4] of the NCA being a credit guarantee.

67. This means that most loans, if interest bearing, are legally required to be registered with the National Credit Regulator.

68. Per the definitions in section 1 of the NCA, a trust is considered to be a juristic person if it has three or more trustees.

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[2] Section 8(4)(*f*) reads as follows: "An agreement, irrespective of its form but not including an agreement contemplated in subsection (2), constitutes a credit transaction if it is –…

(*f*) any other agreement, other than a credit facility or credit guarantee, in terms of which payment of an amount owed by one person to another is deferred, and any charge, fee or interest is payable to the credit provider in respect of –
- (i) the agreement; or
- (ii) the amount that has been deferred."

[3] Section 8(3) reads as follows: "An agreement, irrespective of its form but not including an agreement contemplated in subsection (2) or section 4(6)(6), constitutes a credit facility if, in terms of that agreement-

(a) a credit provider undertakes-
- (i) to supply goods or services or to pay an amount or amounts, as 40 determined by the consumer from time to time, to the consumer or on behalf of, or at the direction of, the consumer; and
- (ii) either to-
  - (aa) defer the consumer's obligation to pay any part of the cost of goods or services, or to repay to the credit provider any part of 45 an amount contemplated in subparagraph (i); or
  - (bb) bill the consumer periodically for any part of the cost of goods or services, or any part of an amount, contemplated in subparagraph (i); and

(b) any charge, fee or interest is payable to the credit provider in respect of- (i) any amount deferred as contemplated in paragraph (a)(ii)(aa); or (ii) any amount billed as contemplated in paragraph (a)(ii)(bb) and not paid within the time provided in the agreement.

[4] Section 8(5) reads as follows: "An agreement, irrespective of its form but not including an agreement contemplated in subsection (2), constitutes a credit guarantee if, in terms of that agreement, a person undertakes or promises to satisfy upon demand any obligation of another consumer in terms of a credit facility or a credit transaction to which this Act 20 applies."

69. The scope of the NCA is to protect individuals and small businesses. There are exceptions contained in section 4(1)(a) of the NCA, however these tend to mainly apply to relationships between natural persons and juristic persons with an asset threshold above R1 million or where such loans do not exceed R250 000.

70. However, the determination of such amounts is made at the time the loan was advanced. No transitional rules have seemingly been inserted in the NCA for pre-existing loans to value these asset thresholds at the time when the loan was made and not on the commencement of the NCA.

71. It would therefore seem that if, for example, Mr A sold his holiday house to the trust (the trust's only asset) on loan account for R200 000 in 1965 (MV R3m 2017) interest free, then by applying an interest rate after 1 March 2017 to avoid section 7C, the NCA would apply as the value of the trust's assets at the time the credit transaction was made was below R1m and also the loan amount was below R250 000.

72. Furthermore, such an arrangement between beneficiary and trust or beneficiary and company held by the trust is not excluded by section 4(2) NCA as they are not deemed to be acting at arms-length.

73. The charging of interest due to section 7C also affects the actual existence of the loan.

74. Section 89(2)(d) read with section 89(5)(a) of the NCA provides that a credit agreement is void from the date the agreement was entered into, where the credit provider was unregistered, but required to do so in terms of the NCA at the time the agreement was made. Such null and void credit agreement trumps any provision of common law, any other legislation or any provision of an agreement to the contrary, per section 89(5) of the NCA.

75. In a Supreme Court of Appeal (SCA) case[5], the appeal turned on whether an agreement of purchase and sale, which provided for interest to be payable on deferred payments, amounted to a credit transaction under s 8(4)(f) of the NCA. Such agreement would be unlawful unless the party extending the credit was registered as a credit provider in terms of section 40 of the NCA. The court in this case declared the agreement null and void *ab initio*.

76. The legalities of charging interest must be considered by all parties to the agreement when considering whether or not to charge interest on a loan, advance or credit. These include the application of the *in duplum* rule as proposed in section 7D which effectively means that the NCA prohibits interest from being charged in excess of the amount of the loan capital, while section 7D read with section 7C may nevertheless effectively impose donations tax on such interest.

[5] *Visagie NO and Others v Erwee NO and Another (unreported case no 734/2013)* (judgement delivered on 19 September 2014)

Proposal

77. NT and SARS should also therefore consider the possible anomalous impact that the NCA has on loans that will now be interest bearing due to section 7C of the ITA. The effect of the loan possibly being null and void/illegal in terms of the NCA should also be considered where such loan is possibly disposed of by operation of law.

NOT IMPLEMENTED – Section 7C(5) of the Act – loan subject to secondary tax on companies (STC)

Legal Nature

78. Section 7C(5)(g) of the Act currently excludes loans that were subject to section 64E(4) of the Act.

79. Section 64E(4) of the Act essentially provides for a deemed dividend where any loan provided by a company to a non-company tax resident that is either a connected person in relation to that company, or a connected person of the first mentioned person.

Factual Description

80. Section 7C(5), however, does not address loans that were subject historically to section 64C of the Act which loans are excluded from section 64E(4) to avoid double taxation.

81. Section 64C of the Act deemed certain amounts to be a dividend for STC purposes.

Proposal

82. It is submitted that section 7C(5)(g) should be extended to include loans that were historically subject to section 64C of the Act.

NOT IMPLEMENTED – Section 10(1)(q) of the Act - bursaries awarded to employees and relatives of employees and nature of payment

Legal Nature

83. Section 10(1)(q) of the Act provides that no taxable benefit arises when an employer provides a bursary or study loan to assist employees or relatives of employees to study and become skilled.

84. The nil value benefit will only apply should the bursary be provided for the purpose of studying at a recognised educational/research institution, and in the event that assistance is provided to employees, an agreement has to be concluded whereby the employee agrees to refund the employer for the bursary in the event of failing to continue with the studies (for any reason other than death, ill-health or disability).

Factual Description

85. In terms of section 10(1)(q) the payment of fees directly to an institution does not trigger tax, however, payment to the employee to reimburse for expenses paid to the same institution does create a taxable event.

86. Many employers do not have the resources to manage full bursary schemes or to fund payments upfront to institutions or to manage approval processes in time for registration dates to be met.

87. For many employers, the award of bursaries is an *ad hoc* function and the reimbursement mechanism gives the employer some flexibility in payment options.

88. It is noted that NT has indicated before that they do not favour a reimbursive structure for education. However, given the dire need for education in South Africa, the policy rationale behind this stance is unclear.

89. It is unclear what NTs concerns are as we perceive little in the way of abuse as the payment would be directly associated to a study outcome and this approach merely addresses employer risk.

90. A reimbursement substantially reduces the employer's risk in having to manage debt for non-completion, which the Department of Higher Education has in its 2016 report on fees indicated, can apply to as much as 60% of first year students.

Proposal

91. If the true nature of the payment, in whatever form, is for the purpose of enabling an employee or relative of an employee to study further then the section 10(1)(q) exemption should apply. Section 8 of the Act should therefore be amended to specifically allow for the reimbursement of study fees to be a non-taxable reimbursement. Further the Interpretation Note should therefore be amended to include the other forms of funding.

92. In our view NT should be encouraging employers to fund these studies as it eases the burden on the state in terms of education, as well as for future social grants as more individuals will be qualified to earn a living wage.

NOT IMPLEMENTED – Section 10(1)(q) of the Act - bursaries awarded to employees and relatives of employees and recovery of debt

Legal Nature

93. Section 10(1)(q) of the Act provides that no taxable benefit arises when an employer provides a bursary or study loan to assist employees or relatives of employees to study and become skilled.

94. The nil value benefit will only apply should the bursary be provided for the purpose of studying at a recognised educational/research institution, and in the event that

assistance is provided to employees, an agreement has to be concluded whereby the employee agrees to refund the employer for the bursary in the event of failing to continue with the studies (for any reason other than death, ill-health or disability).

95. Paragraph 13 of the Seventh Schedule to the Act provides for a taxable benefit to arise on the waiver or release of an employee from a debt. However, there are certain nil value provisions under paragraph 13(2) that are not relevant for the further discussion below.

Factual Description

96. In terms of section 10(1)(q) the employee must be obligated to repay the bursary, i.e. a debt to the employer arises, should the employee fail to complete the studies for reasons other than death, ill-health or disability.

97. There is currently no provision in law that would allow for the debt/loan to be regarded as interest free or at a low interest rate without triggering a fringe benefit. NT and SARS are of the view that the provisions for a low or interest free debt provided for under paragraph 11(4)(b) of the Seventh Schedule to the Act only apply to loans given for purposes of study (and not debts that arise as a result of section 10(1)(q) not being fulfilled). As a result, the employer must either charge interest on the debt or must account for a fringe benefit in relation to the interest benefit being provided.

98. Further, if the employee is unable to repay the debt and the employer opts to write off the debt, a benefit under paragraph 13 of the Seventh Schedule to the Act will arise.

99. Bursaries awarded to lower income earners in order to up-skill and enhance their qualifications are usually significant in value when compared with the salaries of the employees. If the employee is unable to complete his/her studies and a debt arises, he/she is then burdened not only having to repay the debt but also the interest on the debt. If the employer, realising that the debt is burdensome for the employee and/or that it will take the employee a long time to repay the debt then chooses to waive the debt, a further benefit becomes taxable.

Proposal

100. In order to assist employees and to encourage employers to implement broad-based bursary schemes, we recommend the following:

- Paragraph 11(4) of the Seventh Schedule to the Act be amended to allow for low interest or no interest to be levied on a debt that arises from a section 10(1)(q) bursary without triggering a taxable fringe benefit; and

- Paragraph 13(2) of the Seventh Schedule to the Act be amended to allow an employer to waive a debt that arises by virtue of a section 10(1)(q) bursary where the employee's remuneration proxy is less than R250,000.

<u>NOT IMPLEMENTED – Section 58 of the Act – deemed donations</u>

Legal nature

101. Section 58 of the Act gives rise to a deemed donation where property is disposed of for a consideration which, in the opinion of the Commissioner, is not adequate consideration. This section gives rise to interpretational issues.

102. Although SARS has in the past issued binding private rulings indicating that section 58 presupposes an element of gratuitousness, academic writers have in the past opined that this section may be applied regardless of the motive behind the disposal.

103. Clarity is needed as to the scope of the section. In particular, it is not clear what is meant by the term "adequate consideration" included in the section, which is not defined.

Factual description

104. Based on the literal wording of section 58, the deemed donation potentially applies to any disposal of property at less than what the Commissioner may regard as adequate consideration. It is presumed that what is meant by "adequate consideration" is the current market value of the property although this is unclear. Examples of where property may be disposed of at less than market value include instances where BBBEE partners are introduced into a business for a discounted consideration with long term BBBEE objectives in mind.

The nature of business impacted

105. The impact of this section is very broad. It potentially applies to any disposal of property at less than market value, despite having an underlying commercial rationale.

106. In particular, the potential of suffering donations tax at 20% discourages the introduction of BBBEE partners into a business at less than market value (which is often how these transactions are structured).

Proposal

107. Clarity is needed with regard to the interpretation of section 58, particularly as to whether at least a partial motive of gratuitousness is required for the provision to be invoked and in relation to the meaning of the term "adequate consideration". A Binding General Ruling or Interpretation Note would be welcomed.

CATEGORY – DOMESTIC BUSINESS TAXES

NOT IMPLEMENTED – Section 24C(2) of the Act – Amounts received in terms of contracts and future expenditure

Legal Nature

108. Section 24C(2) of the Act provides for an allowance where the income of any taxpayer in any year of assessment includes or consists of an amount received by or accrued to him in terms of any contract and the Commissioner is satisfied that such amount will be utilised in whole or in part to finance future expenditure which will be incurred by the taxpayer in the performance of his obligations under such contract.

109. Section 24C was introduced into tax legislation by section 18(1) of the Income Tax Act No. 104 of 1980. The explanatory memorandum on the Income Tax Bill, 1980 explains the reason for the insertion of section 24C as follows:

"The new section caters for the situation which often arises in the construction industry and sometimes in manufacturing concerns, where a large advance payment is made to a contractor before the commencement of the contract work, to enable the contractor to purchase materials, equipment etc. In a number of instances such advance payments are not matched by deductible expenditure, resulting in the full amounts of the advance payments being subject to tax." (own emphasis)

110. It is submitted that the wording of section 24C does not always achieve the outcome envisaged in the Explanatory Memorandum.

Factual Description

111. Taxpayers engaged in the distribution of high value machinery, equipment or motor vehicles often enter into agreements with customers in terms of which the customer has to pay a significant portion of the consideration as a deposit before the taxpayer orders the trading stock which is the subject matter of the agreement. The deposit becomes taxable in the year of assessment in which it is received.

112. Taxpayers also enter into agreements in terms of which the customer pays the full consideration in terms of the agreement towards the end of a year of assessment but delivery of the machinery, equipment or motor vehicle only occurs after year end for a variety of reasons. The full consideration becomes taxable upon receipt.

113. In both scenarios, the taxpayer has ordered and paid for the machinery, equipment or vehicle but has not yet delivered the machinery, equipment or vehicle to the customer and transfer of ownership has therefore not yet taken place. The stock is therefore on hand and has not been disposed of.

114. While the expense has been incurred for purposes of section 11(a), the expense does not qualify for deduction in arriving at taxable income as the machinery, equipment or

vehicle will be included in closing stock for tax purposes. The expense in relation to the acquisition of the machinery, equipment or vehicle will only be deductible in the subsequent year of assessment through its inclusion in the opening balance of trading stock.

115. This is confirmed in Interpretation note 78 (IN 78) which states at paragraph 4.2.3 on page 12: *"A similar issue arises with trading stock when a taxpayer has incurred expenditure in acquiring items of trading stock. Once the expenditure has been incurred it does not constitute future expenditure even if the trading stock is included in the taxpayer's closing stock."*

116. This means that the taxpayer is taxed on the full receipt which is <u>not matched by deductible expenditure</u>.

<u>The nature of the business impacted</u>

117. Taxpayers engaged in the distribution of high value machinery, equipment or motor vehicles often enter into agreements with customers in terms of which:

- the customer has to pay a significant portion of the consideration as a deposit before the taxpayer orders the trading stock which is the subject matter of the agreement; or

- the customer pays the full consideration in terms of the agreement towards the end of a year of assessment but delivery of the machinery, equipment or motor vehicle only occurs after year end for a variety of reasons.

<u>Proposal</u>

118. It is recommended that section 24C be reworded to achieve its intended purpose in relation to all taxpayers. This can be achieved by amending the definition of "future expenditure" in section 24C(1) as follows:

"For the purposes of this section, "future expenditure" in relation to any year of assessment means an amount of expenditure which the Commissioner is satisfied <u>has been incurred during the current or</u> any preceding year of assessment or will be incurred after the end of such year:

a. *in such manner that such amount will be allowed as a deduction from income in a subsequent year of assessment; or*

b. *in respect of the acquisition of any asset in respect of which any deduction will be admissible under the provisions of this Act."*

NOT IMPLEMENTED – Paragraph 64E of the Eighth Schedule to the Act – exclusion of capital gains when section 8C applies

Legal Nature

119. Paragraph 64E of the Eighth Schedule to the Act was inserted into the Act by section 74(1) of the Taxation Law Amendment Act of 2017. The Explanatory Memorandum to the 2017 Taxation Laws Amendment Bill noted that paragraph 64 was inserted to clarify that amounts included in the employee's income in terms of section 8C of the Act will be disregarded by the share incentive scheme for capital gains tax (CGT) purposes.

120. Paragraph 64E of the Eighth Schedule to the Act, effective 1 March 2017, reads as follows:

"Where a capital gain is determined in respect of the disposal of an asset by a trust and a trust beneficiary has a vested right to an amount derived from that capital gain, that trust must disregard so much of that capital gain as is equal to that amount if that amount must in terms of section 8C be:

a. *included in the income of that trust beneficiary as an amount received or accrued in respect of a restricted equity instrument; or*

b. *taken into account in determining the gain or loss in the hands of that trust beneficiary in respect of the vesting of a restricted equity instrument."*

121. It is submitted that the wording of paragraph 64E does not achieve the outcome envisaged in the Explanatory Memorandum.

Factual Description

122. Employers often introduce share based incentives schemes that utilise trusts.

123. These schemes are often implemented as follows:

- The employer establishes a trust with its employees being the beneficiaries of the trust;
- The employer makes a contribution to the Trust;
- The Trust uses the contribution to acquire equity shares. The shares may vest in the beneficiaries immediately in the sense that the employees are entitled to dividends and voting rights attached to the shares, but the shares will only be distributed to the employees by the trust after a lock-in period. Alternatively, the shares only vest in the employees after expiry of the lock-in period;
- After a lock-in period, the shares held by the Trust are distributed to the employees and all restrictions are lifted.

124. The tax implications are as follows:

- The contribution made by the employers may or may not be deductible under section 11(a) of the Act depending on the purposes with which the contribution was made;

- The contribution will be of a capital nature in the hands of the Trust;

- The acquisition of the shares by the Trust will constitute an asset in the hands of the Trust with a base cost equal to the expenditure incurred in acquiring the shares. Having said that, since the base cost of the shares was funded by the employer company it is arguable that as a result of paragraph 20(1)(a) read with paragraph 20(3)(b), the base cost of the shares in the hands of the Trust is Rnil;

- Paragraph 11(1)(d) of the Eighth Schedule includes in the definition of disposal, the vesting of an interest in an asset of a trust in a beneficiary. Paragraph 13(1)(iiB) of the Eighth Schedule determines that the time of disposal of an asset by means of the granting by a trust to a beneficiary of an equity instrument contemplated in section 8C is the time that that equity instrument vests in that beneficiary as contemplated in that section;

- For purposes of section 8C, the shares vest in the hands of the employees after the lock-in period when all the restrictions are lifted;

- The employees, being beneficiaries of the trust, are connected persons in relation to the Trust. The disposal of the shares to the beneficiaries at the time of vesting will therefore be deemed to take place at market value (paragraph 38);

- To the extent that the market value of the shares at the time of vesting exceeds the base cost of the shares, a capital gain will arise in the hands of the Trust. The same gain will also be taxed in the hands of the employees in terms of section 8C;

- Paragraph 64E exempts the gain arising from the disposal of an asset (the shares) in the hands of the Trust where a trust beneficiary has a vested right to an amount derived from that capital gain to the extent that the gain is taxed in terms of section 8C; and

- It is submitted that the employees in the scenario described, have a vested right to the asset and do not have a vested right to an amount derived from that capital gain.

The nature of the businesses impacted

125. All employers operating share based incentive schemes housed in trusts.

Proposal

126. It is recommended that paragraph 64E be reworded to achieve its intended purpose.

127. The suggested wording is to set the phrase *"a trust beneficiary has a vested right to an amount derived from that capital gain"* as an alternative, as noted below:

"Where a capital gain is determined in respect of the disposal of an asset by a trust as a result of the vesting of an equity instrument as contemplated in section 8C or a trust beneficiary has a vested right to an amount derived from that capital gain ~~and a trust beneficiary has a vested right to an amount derived from that capital gain~~ that trust must disregard so much of that capital gain as is equal to that amount if that amount must in terms of section 8C be:

a. included in the income of that trust beneficiary as an amount received or accrued in respect of a restricted equity instrument; or

b. taken into account in determining the gain or loss in the hands of that trust beneficiary in respect of the vesting of a restricted equity instrument."

CATEGORY – VALUED ADDED TAX & CUSTOMS

NOT IMPLEMENTED - Section 8(25) of the VAT Act - Relief in respect of group reorganisation

Section 1(1) of the VAT Act – definition of 'surrender of goods'

Legal Nature

128. Section 1(1) of the VAT Act defines the term "surrender of goods" as meaning the termination of any instalment credit agreement by the debtor and subsequent obligation on the creditor, to that agreement, to take possession of any goods previously supplied under that agreement.

129. Section 8(10) of the VAT Act provides that where there is a surrender of goods under an instalment credit agreement, a supply of such goods shall be deemed to be made by the debtor under such instalment credit agreement to the person exercising the person's right or obligation of possession under such instalment credit agreement.

130. The Explanatory Memorandum that amended section 8(10) of the VAT Act and inserted the definition of "surrender of goods" in the VAT Act, stated the following:

"It is proposed that the current deemed supply pertaining to the repossession of goods be expanded to cater for a surrender of goods by a vendor to a financier (creditor) in terms of any instalment credit agreement covered in terms of the National Credit Act, 2005."

131. Section 127 of the National Credit Act, No 34 of 2005 (the NCA) sets out the provisions regarding the surrender of goods. Without quoting the section, the purpose of this section is to set out the procedures to be followed by a debtor when he/she wants to surrender the goods outside the pre-agreed terms of the financing arrangement. It involves giving notice to the financier, delivery of the goods, a waiting period where the debtor can again change his/her mind, how the financier can sell the goods and set-off against the creditor, etc.

Factual Description

132. Some instalment credit agreements (ICA) provide that at the end of the agreement the debtor has to return the goods or alternatively pay a lump sum or re-finance the outstanding balance.

133. This return of the goods is a contractual obligation of the debtor and not the termination of the ICA by the debtor as a result of the surrendering of the goods as envisaged in the NCA and the definition of "surrender of goods" in the VAT Act.

134. As a result, the return of the goods in terms of these ICA's do not fall within the provisions of section 8(10) of the VAT Act and the financier will consequently not have an input tax deduction as there is no deemed supply.

The nature of businesses impacted

135. Financiers of goods in terms of ICA's.

Proposal

136. It is proposed that the definition of "surrender of goods" be amended to include scenarios where it is a contractual obligation of the debtor to return the goods.

NOT IMPLEMENTED – Sections 8(20) and 20(4) of the VAT Act – consideration to be included on tax invoices pursuant to a deemed supply by an agent

Legal Nature

137. Section 8(20) of the VAT Act provides that where an importation of goods is deemed to be made by an agent, as contemplated in section 54(2A)(b) of the VAT Act, such agent shall be deemed to make a supply of goods to the recipient of the supply by the principal as contemplated in subparagraph (iii) of that section.

138. Section 10(22B) of the VAT Act states that the consideration for the deemed supply contemplated in section 8(20) of the VAT Act will be deemed to be the total amount of the value placed on the importation of the goods in terms of section 13(2) of the VAT Act (i.e. the customs value, the duty levied plus 10 per cent of the said value) and the amount of tax levied on the importation.

Factual Description

139. As a result of section 8(20) of the VAT, the agent will be required to issue a tax invoice, in terms of section 20(4) of the VAT Act, to the recipient for the full consideration due on the supply in terms of section 10(22B) of the VAT Act. However, the recipient will only be liable to pay the import VAT (and potentially the customs duty depending of the agreement with the supplier) to the agent as the consideration (i.e. the sale price) will be due and payable to the foreign supplier. Therefore, if the agent includes the full consideration on the invoice it may have (depending on the manner in which it issues this invoice and its accounting system) an outstanding debtor in its accounting records, as only the import VAT will be payable by the recipient to the agent.

The nature of businesses impacted

140. Any agent importing goods on behalf of a non-resident, non-registered VAT vendor subject to section 54(2A) of the VAT Act.

Proposal

141. It is recommended that section 20 of the VAT Act be amended to allow the agent to invoice for the import VAT amount only on the tax invoice. If required the full consideration could still be included on the tax invoice, but as part of for example the details/description.

142. Alternatively, we recommend that a provision is included in section 20 of the VAT Act that would allow the Commissioner to prescribe the particulars to be included in a tax invoice issued for deemed supplies under section 8(20) of the VAT Act in a regulation.

NOT IMPLEMENTED – Section 8(29) of the VAT Act – leasehold improvements

Legal Nature

143. Section 8(29) of the VAT Act states that where a (vendor) lessee makes leasehold improvements for no consideration, in circumstances where the lessee will use the property and improvements for taxable supplies or mixed supplies, there will be a deemed taxable supply by the lessee to the lessor.

Factual Description

144. Based on previous submissions made it is again submitted that section 8(29) of the VAT Act is not necessary, since it is extremely uncommon and unlikely that a lessee will make leasehold improvements for no consideration, other than in cases where the lease agreement provides that upon termination of the lease, the premises should be returned to the lessor in the same state in which the lessee received it.

145. Furthermore, there is an actual supply of goods by the lessee to the lessor, in respect of leasehold improvements affected, on the basis of accession. The introduction of the section introduces unnecessary ambiguity.

The nature of businesses impacted

146. Parties to property leases where leasehold improvements are made.

Proposal

147. To overcome the potential difficulties with the application of section 8(29) of the VAT Act, we recommend that the section should be deleted from the VAT Act along with sections 9(12) and 10(28) of the VAT Act.

NOT IMPLEMENTED – Section 8A(1) of the VAT Act - Sharia compliant financing arrangements: Murabaha agreements

Legal Nature

148. Murabaha agreements are mark-up financing transactions. These agreements are generally offered by financial institutions, such as a bank, to clients in order for clients to obtain financing for various assets such as vehicles.

149. For example, the bank will purchase a vehicle from a third party on instruction from the client and sell it to the client at a pre-agreed price. The mark-up on the resale by the bank creates a profit for the bank which is calculated with reference to the time value of money. The client then pays the marked-up price on a deferred basis similar to an instalment sale agreement, i.e. an ICA.

150. A material term of these agreements will usually include that should the client default in terms of the obligations stated in the agreement that the bank may institute action to repossess the vehicle. Normally, when dealing with ICA's and when motor cars are repossessed the provisions in section 8(10) of the VAT Act relating to repossessions apply.

151. However, Murabaha agreements as contemplated in section 8A(1) of the VAT Act do not constitute ICA's as defined in section 1(1) of the VAT Act. It follows that the provisions in section 8(10) of the VAT Act relating to repossessions can therefore not apply.

152. This does not mean that there isn't a supply when the bank repossesses the vehicle. There is in fact a supply which takes the form of a sale and should the bank be able to claim input tax where it acquires, by way of repossession, the vehicle from a resident client the amount of input tax claimed will be limited to the tax fraction of the lesser of the amount paid (i.e. realised by the Bank and set off against the debt) or the open market value.

Factual Description

153. Financial institutions that provide finance to debtors, based on Murabaha agreements, are affected by the fact that the repossession provisions, contemplated in section 8(10) of the VAT Act do not apply to such transactions. Such institutions include banks and collective investment schemes in shares.

The nature of businesses impacted

154. Sharia financial institutions entering into finance arrangement as contemplated in section 8A(1) of the VAT Act.

Proposal

155. It is proposed that the VAT Act be amended to state that, in the case of Murabaha agreements as contemplated in the VAT Act, the amount fetched when the asset is disposed of in order to recover the debt (for example where the asset is sold on auction) should be deemed to be the market value of the supply under repossessions. This proposal is based on the fact that the amount fetched at auction is the amount that is set-off against the debtor's account.

NOT IMPLEMENTED – Section 8A(2)(c) of the VAT Act - Sharia compliant financing arrangements

Legal Nature

156. Section 8A(2)(c) of the VAT Act provides that, in the case of any diminishing Musharaka as defined in section 24JA(1) of the Act, any amount contemplated in section 24JA(5)(d) of the Act paid or payable to the bank by the client shall be deemed to be consideration in respect of an exempt financial service supplied by the bank as contemplated in section 2(1)(f): Provided that this paragraph shall not apply to the extent to which the consideration constitutes any fee, commission or similar charge.

Factual Description

157. The Act does not contain a section 24JA(5)(d). Instead, section 24JA(6)(b) of the Act provides the formula that must be used to determine the financing charge.

The nature of businesses impacted

158. Any parties to a Sharia compliant financing arrangement in terms of section 24JA(1) of the Act.

Proposal

159. It is recommended that the VAT Act be amended to delete the reference to section 24JA(5)(d) of the Act and to replace it with a reference to section 24JA(6)(b) of the Act.

NOT IMPLEMENTED – Section 15(2A) - Accounting for VAT on the payments basis – the R100 000 rule

Legal nature

160. Section 15(2A) of the VAT Act allows certain categories of vendors registered on the payments basis to account for output tax on the payment basis notwithstanding the fact that the value of the consideration for a supply exceeds R100 000.

161. The exclusion applies to, amongst others, a public authority.

162. "Public authority" is defined in paragraph (ii) of the definition of "public authority" in section 1(1) of the VAT Act as "*any public entity listed in Part A or C of Schedule 3 to the Public Finance Management Act*."

163. Water Boards are currently listed under Part B of the Public Finance Management Act; hence these entities do not constitute "public authorities" for VAT purposes.

Factual description

164. It thus follows from the above that Water Boards are currently required to account for output tax on the invoice basis on all sales in excess of R100 000. In the case of Water Boards this will include virtually all supplies made as most supplies relate to the supply of bulk water to municipalities.

165. Most municipalities are currently under financial strain resulting in payments to Water Boards being outstanding for protracted periods of time.

166. The above situation places undue strain on the finances of Water Boards.

The nature of the businesses impacted

167. All Water Boards.

Proposal

168. We recommended that Water Boards listed in Part B of the Public Finance Management Act listed be excluded from the R100 000 threshold contained in section 15(2A) of the VAT Act.

NOT IMPLEMENTED – Sections 16(2)(d) of the VAT Act – documentary requirements for purposes of claiming input tax on retrospective adjustments to the value of goods imported

Legal Nature

169. Section 1 of the VAT Act defines the term "input tax", *inter alia*, to mean the VAT incurred by a vendor on the importation of goods by that vendor, provided that the goods or services concerned are acquired by the vendor wholly for the purpose of consumption, use or supply in the course of making taxable supplies or, where the goods or services are acquired by the vendor partly for such purpose, to the extent that the goods or services concerned are acquired by the vendor for such purpose.

170. Section 16(2)(d) of the VAT Act disallows the deduction of input tax in respect of the importation of goods into the Republic, unless a bill of entry or other document prescribed in terms of the Customs and Excise Act, No 91 of 1964 (Customs and Excise Act), together with the receipt for the payment of the tax in relation to the said importation,

have been delivered (including by means of an electronic delivery mechanism) in accordance with that Act and are held by the vendor making that deduction, at the time that any return in respect of that importation is furnished.

171. Section 40(1)(c) of the Customs and Excise Act provides that no entry shall be valid unless the true value of the goods on which duty is leviable or which is required to be declared under the provisions of this Act and the true territory of origin, territory of export and means of carriage have been declared.

172. Section 40(3)(a)(i) of the Customs and Excise Act provides that subject to the provisions of sections 76 and 77 and on such conditions as the Commissioner may impose and on payment of such fees as he may prescribe by rule –

(i) an importer or exporter or a manufacturer of goods shall on discovering that a bill of entry delivered by him or her –

(aa) does not in every respect comply with section 39; or

(bb) is invalid in terms of subsection (1) of this section, adjust that bill of entry without delay by means of –

(A) a voucher of correction; or

(B) cancellation of such bill of entry and substitution of a fresh bill of entry; or

<u>in such other manner as the Commissioner may prescribe</u> (own emphasis).

<u>Factual Description</u>

173. In terms of section 16(2)(d) of the VAT Act, a vendor claiming the VAT paid on the importation of goods as input tax must, at the time of making the deduction, hold a bill of entry or other prescribed document in terms of the Customs and Excise Act together with receipt of payment.

174. In this regard, section 40(3)(a)(i)(bb)(C) of the Customs and Excise Act provides that a bill of entry may be adjusted in a manner as prescribed by the Commissioner. The aforementioned adjustments result for a number of reasons, for example retrospective transfer pricing adjustments, and may include a significant number of bills of entry over a period. In certain instances, and to curb the costs and effort involved in retrospective adjustments where various bills of entry are involved, vendors often make such subsequent adjustment to the original bill of entry by making disclosure to SARS, followed by SARS issuing a Letter of Demand and the vendor completing and submitting a CEB01.

175. It seems that most SARS branch offices accept the Letter of Demand issued by SARS together with the completed CEB01 form and proof of payment of the VAT to SARS as the “other document prescribed in terms of the Customs and Excise Act” as envisaged in section 16(2)(d) of the VAT Act. However, we understand that this may not be the interpretation of all SARS officials.

The nature of businesses impacted

176. All importers, especially importers importing from related parties where annual transfer pricing adjustments are required to be made.

Proposal

177. It is recommended that SARS provides clarity on the above by issuing an Interpretation Note or Binding General Ruling which describes what it considers *"other prescribed document in terms of the Customs and Excise Act"* to be.

NOT IMPLEMENTED – Section 18A(2) of the VAT Act – adjustment in consequence of acquisition of going concern wholly or partly for purpose other than making table supplies

Legal Nature

178. Section 18A(2) of the VAT Act provides *inter alia*, that the value of the supply deemed by subsection 18A(1) to have been made by the vendor, shall be the full cost to such vendor of acquiring such enterprise, part, goods or services, as the case may be, reduced by an amount which bears to the amount of such full cost the same ratio as the intended use or application of the enterprise, part, goods or services in the course of making taxable supplies bears to the total intended use or application of the enterprise, part, goods or services: Provided that—

(i) the cost to such vendor of acquiring such enterprise, part, goods or services may be reduced by any amount which represents an appropriate allocation of such full cost to the acquisition of any goods or services which form part of such enterprise or part of an enterprise and in respect of the acquisition of which by the vendor a deduction of input tax would be denied in terms of section 17(2); or

(ii) where such enterprise, part, goods or services were acquired—

(*aa*) by means of a supply made by a vendor for no consideration or for a consideration in money which is less than the open market value of the supply; and

(*bb*) in circumstances where the supplier and the recipient are connected persons,

the cost of such enterprise, part, goods or services shall be deemed to be the open market value of the supply of such enterprise, part, goods or services. (own emphasis).

Factual Description

179. The purpose of this section is to place the acquiring vendor in the same position as he would have been had he paid VAT on the acquisition of goods or services acquired in respect of the exempt activities of the enterprise acquired.

180. The value of an enterprise is generally determined to include the following, where applicable:

Seller, discretionary earnings (SDE) + Tangible assets (i.e. the value of properties and buildings + other assets) + Estimated value of intangible (i.e. the value of brand, reputation, trademarks) + Value of debtors) less value of business liabilities.

181. It follows that the cost of acquiring an enterprise (actual cost paid for the enterprise or the open market value of such enterprise) includes an amount appropriated to the value of non-taxable supplies (i.e. the book value of debtors and liabilities the estimated value of future income associated with trademarks and reputation of the enterprise, etc.).

182. Based on a strict reading of the section, it seems that the acquiring vendor is required to also account for output tax on the cost of the non-taxable assets appropriated to the cost of the enterprise. Given that this section intends to place SARS in the same position had the enterprise not been disposed of and the fact that the section is not a charging section, the effects, based on a strict interpretation, are that SARS will collect output VAT on items that are otherwise not subject to VAT.

The nature of businesses impacted

183. Vendors that acquire an enterprise partly for a purpose other than making taxable supplies are required to account output tax on the value of taxable goods or services (excluding goods or services in respect of which input tax would be denied in terms of section 17(2) of the VAT Act), to the extent to which such goods or services are acquired for purposes of consumption, use or supply otherwise than in the course of making taxable supplies.

Proposal

184. It is recommended that the below is inserted as a further provision to provide clarity on the exclusion of non-taxable items appropriated to the value of an enterprise:

"Provided further that the cost to such vendor shall further be reduced by the cost of any goods or services which would, if supplied by a vendor in the course of its enterprise, will not be subject to VAT in terms of section 7(1) of the VAT Act."

NOT IMPLEMENTED – Section 18C of the VAT Act - leasehold improvements rules for the Lessor

Legal Nature

185. Section 8(29) of the VAT Act states that where a (vendor) lessee makes leasehold improvements for no consideration, in circumstances where the lessee will use the property and improvements for taxable supplies or mixed supplies there will be a deemed taxable supply by the lessee to the lessor.

Factual Description

186. Following on section 8(29), section 18C of the VAT Act provides that vendor (lessee) making mixed supplies will get the full input tax deduction whilst the lessor is liable for output tax which it cannot recover with the result that it may not have the funds to pay the VAT.

The nature of businesses impacted

187. Any lessor where a lessee performs leasehold improvements for no consideration in terms of section 8(29) of the VAT Act.

Proposal

188. It is proposed that section 18C of the VAT Act should be deleted from the VAT Act.

NOT IMPLEMENTED – Section 20 of the VAT Act – tax invoices

Legal Nature

189. Section 20 of the VAT Act places a statutory obligation on all vendors to issue tax invoices within a prescribed time, form and manner. Any document which does not contain the particulars as envisaged in section 20(4) of the VAT Act, does not constitute a tax invoice and as such a vendor is not entitled in terms of section 16(2) of the VAT Act to claim an input tax deduction based on such document.

190. Further, in terms of section 20(1) of the VAT Act, where a supply of goods and/or services has been made from a vendor (i.e. supplier) to another vendor (i.e. recipient) the supplier must issue a tax invoice within 21 days from making the taxable supply.

191. Section 54(3) of the VAT Act requires that where tax invoices are issued to an agent as contemplated in section 54(2) of the VAT Act, the agent must notify its principal in a written statement within 21 days of the end of the calendar month during which the supply was made.

192. Section 16(2)(g) of the VAT Act, provides that SARS may issue a ruling to a recipient for the use of alternative documentation, where the recipient has despite taking reasonable steps, *inter alia*, been unable to obtain a tax invoice as a result of the supplier having failed to issue the tax invoice.

Factual Description

193. Where a supplier refuses to issue a tax invoice in terms of section 20 of the VAT Act to the recipient, the recipient is not able to claim the input tax (where applicable) since it is not in possession of a tax invoice in relation to that supply as required in terms of section 16(2)(a) of the VAT Act. This means that the recipient is left “out of pocket” until it obtains a tax invoice.

194. It is a criminal offence in terms of section 234 of the TAA not to issue a document as required under the VAT Act, including a tax invoice. Similarly, in terms of section 58 of the VAT Act it is a criminal offence where the agent fails to issue the statement in terms of section 54(3) of the VAT Act to its principal. SARS, however, rarely if ever takes legal proceedings as a result of the non-issue of tax invoices by suppliers or statements by agents. The lack of SARS action in the case of the non-issue of tax invoices was also commented on in the Jazz Festival case[6] by the taxpayer:

> *"It was furthermore contended by the appellant that the Commissioner is responsible, in terms of section 4(1) of the VAT Act, to carry out the provisions of the Act and that he took no action against the sponsors to ensure compliance with section 20, nor did he impose punitive measures on them."*

195. Notwithstanding section 16(2)(g) of the VAT Act, which is a timeous and costly solution to assist the recipient and which is subject to SARS discretion and therefore not guaranteed, and section 234 of the TAA which is unlikely to be imposed due to timing and cost factors for SARS, there are no other provisions in the VAT Act or the TAA that would allow SARS to provide assistance to vendors who request suppliers to issue tax invoices, where such suppliers refuse to do so.

The nature of businesses impacted

196. All vendors where suppliers refuse to issue tax invoices, after having received written requests to do so, in relation to taxable supplies made as required by section 20 of the VAT Act.

Proposal

197. It is recommended that SARS be given powers to ensure that the obligations under sections 20(1) and 54(3) of the VAT Act are enforced where supplier vendors/agents refuse to be compliant. It is recommended that SARS be given authority to impose an administrative non-compliance penalty, in cases where vendors have requested these documents without success. Supplying vendors and agents may then be given the opportunity to object if they believe the penalty was wrongfully imposed, since they had no liability to issue such documents.

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[6] *South Atlantic Jazz Festival (Pty) Ltd v Commissioner for the South African Revenue Service* [2015] ZAWCHC 8 (judgment delivered on 6 February 2015)

NOT IMPLEMENTED – Section 41B of the VAT Act – provisions to allow backdated rulings for 5 years to allow for equity and fairness – section 17(1) proviso (iii) read with section 16(3) proviso (i)

Legal nature

198. A taxpayer's liability for VAT is calculated as the sum of output tax attributable to a tax period, less the amounts of input tax to which the taxpayer is entitled, as supported by documentary evidence. This is the basic premise of a VAT system.

199. Section 1 of the VAT Act defines the term "input tax" to mean the VAT incurred by a vendor in respect of goods or services acquired, where the goods or services concerned are acquired for the purpose of consumption, use or supply in the course of making taxable supplies.

200. Where goods or services are acquired for another purpose, no deduction of input tax is allowed and in terms of section 17(1) of the VAT Act, where the goods or services are acquired for a dual purpose, the deduction of input tax is allowed proportionally (apportioned) based on the intended taxable use, usually expressed as a percentage of total "intended use".

201. There is generally a five- year period within which input tax may be deducted (see the proviso to section 16(3) of the VAT Act). This balances fairness and the necessity for efficient tax administration.

202. In terms of section 17(1) proviso (iii) of the VAT Act, where SARS has previously issued a ruling as to the method by which the "intended taxable use" should be determined (i.e. an apportionment ruling), the method may subsequently only be changed from a future date. This provides for certainty. It is noted from the Explanatory Memorandum when the said limitation was introduced, that the purpose was to prohibit vendors from claiming refunds in respect of prior years, albeit that they failed to apply timeously for a special method of apportionment.

Factual description

203. Input tax apportionment occurs throughout the year with every VAT return which is submitted, calculated by applying the ratio calculated in respect of the previous financial year. At the end of the current financial year, the apportionment ratio is recalculated and any over- or under recoveries of input tax is corrected in one adjustment. Should it be determined that the method is inequitable, whether in favour of the taxpayer or SARS, SARS is only permitted to issue a ruling on an alternative method to be applied from a future date. This leaves the year in which the inequality prevailed, unaltered.

204. Although SARS may acknowledge that the turnover based method of apportionment yields a grossly unfair and obscure result, where a taxpayer, for whatever reason, did not apply the standard turnover based method of apportionment in the absence of an apportionment ruling, and although the amendment does not appear to have been

intended that SARS can assess for prior years, SARS now has no discretion but to assess using the standard turnover basis.

The nature of the businesses impacted

205. This matter influences all vendors who receive non-taxable revenue who apply for a ruling to use an alternative apportionment method, where the turnover-based methods yields inequitable results.

Proposal

206. For the reasons above we recommend that SARS be granted discretion to issue rulings retrospectively from the time that SARS deems equitable. Furthermore, we recommend that section 44 of the VAT Act be amended to include a section which would prohibit vendors to claim VAT refunds in respect of retrospective tax periods prior to the first day of the financial year in which the ruling application was duly submitted to SARS.

NOT IMPLEMENTED – Section 41B of the VAT Act and Chapter 7 of the TAA – provisions dealing with the re-application of existing rulings, subject to expiration dates

Legal nature

207. The provisions in section 41B of the VAT Act stipulates that the Commissioner may issue a VAT class ruling or a VAT ruling and the specifics in relation to such rulings.

208. Chapter 7 of the TAA includes the provisions dealing with the application and issuing of advance rulings.

Factual description

209. Neither section 41B of the VAT Act, nor Chapter 7 of the TAA make provision for the time frame within which a person must re-apply for rulings subject to an expiration date.

210. Although in practice SARS in some cases allow the existing ruling to remain in force after the expiration date, provided the person has timeously submitted a re-application, no legislative provisions exist in this regard.

The nature of the businesses impacted

211. Persons relying on rulings granted subject to expiration dates.

Proposal

212. We recommend that a provision is introduced to section 41B of the VAT Act and Chapter 7 of the TAA that the re-application of rulings subject to expiration dates must be made within a particular timeframe prior to the expiration date.

213. Further, we recommend that a provision be included that if the person submitted the re-application within the required timeframe that the existing ruling will remain in force until the re-application has been confirmed, amended or declined by SARS.

NOT IMPLEMENTED – Section 50 of the VAT Act – inequitable apportionment/non-deductibility of input tax as a result of VAT registrations in terms of section 50

Legal nature

214. Section 50 of the VAT Act provides that a vendor (e.g. a company who is liable to be registered as a VAT vendor, hereinafter referred to as "the Vendor") may apply to the Commissioner to register branches or divisions of the Vendor as separate vendors. Where the Commissioner has approved such application and the branches and divisions are registered separately (hereinafter referred to as the Branches) section 50(2) of the VAT Act provides that the Branches shall be deemed to be carried on by a person separate from the Vendor.

215. Section 17(1) of the VAT Act read with the definition of "input tax" provides that the tax incurred by the vendor on the acquisition or importation of goods or services, constitute "input tax" only to the extent to which the goods or services are acquired/imported for purposes of consumption, use or supply in the course of making taxable supplies. The extent of taxable application, use or supply is to be determined in accordance with a method prescribed by the Commissioner, which is the standard turnover basis, envisaged in Binding General Ruling 16 Issue 2 (BGR 16).

216. Section 10(23) of the VAT Act provides that where a supply is made for no consideration, the value of the supply is deemed to be nil. In this regard the Court held in the *KCM* case[7] that section 10(23) of the VAT Act only functions in respect of taxable supplies. It was further held that since taxable supplies are, in terms of section 7(1) of the VAT Act required to be made in the course or furtherance of the vendor's "enterprise", it is necessary to have regard to the definition of "enterprise" to determine whether the supply can be said to be made in the course or furtherance of an enterprise. The definition of "enterprise" specifically requires that supplies need to be made to another person for a consideration and specifically excludes exempt supplies. Also refer to Interpretation Note 70 (IN 70) issued by SARS which deals with the VAT treatment of supplies made for no consideration.

217. The provision which deems the Branches or divisions to be persons separate from the Vendor, has the effect that goods or services made available by one Branch to another constitutes a "supply" of "goods" or "services" by one vendor to another vendor and that such a supply may be taxable as if the Branches are separate legal persons from one another. Consequently, where such a supply is taxable, the supplying vendor is liable for VAT at either the standard or the zero rate of VAT and is required to issue a tax invoice in the ordinary course as if the supplies were made to a separate legal person, whereas the recipient vendor is entitled to claim such VAT charged to it as input tax subject to the general rules for input tax, including apportionment where relevant. Equally, where any

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[7] *KCM v Commissioner South African Revenue Service* (VAT 711) [2009] ZATC 2 (judgement delivered on 14 August 2009)

exempt supplies are made by one Branch to another, such exempt supplies need to be reflected on the supplying vendor's VAT return.

218. From the said provisions and effects, it follows that the ultimate amount of tax payable to SARS should be identical to the amount that would have been payable, had separate VAT registrations not been effected. However, at least two scenarios exist where the aim is not achieved, i.e. where the ultimate amount of tax payable will increase due to the separate registrations, albeit that all of the Branches only make taxable supplies.

219. These two scenarios occur where:

- One Branch (typically the Branch where the treasury function is housed) borrows funds to be used by another Branch wholly in the course of making taxable supplies (typically an operational Branch). In this instance, for VAT purposes, the borrowing Branch makes an exempt supply to the other Branch by on-lending the funds acquired, and in the ordinary course may or may not elect to account for a notional amount of "interest" for management accounting purposes – notional since a legal entity cannot legally charge itself interest and where it is accounted for, it will accordingly be eliminated in the "consolidated" financial statements of the company. Where the borrowing Branch elects to account for the so-called notional interest, such interest may have the effect that the lending Branch may be required to apportion input tax incurred on overhead/administration costs, on the basis that it receives this non-taxable income. However, where the borrowing Branch elects not to account for this notional amount of interest, section 10(4) of the VAT Act does not find application to deem the value for this notional amount of interest at a market related rate, since firstly, it is arguable whether a notional amount of interest constitutes interest, and secondly, since the receiving Branch is not required to apportion input tax on the basis that it makes only taxable supplies.

- One of the Branches acquires goods or services which are used by another Branch. For VAT purposes, the first-mentioned Branch who acquired the goods or services once again supplies the acquired goods or services to the last-mentioned Branch. As is the case with notional interest, the acquiring Branch may decide, for management accounting purposes, to account for the value of the goods or services supplied or not to account for such a value. Where the decision is not to account for any amounts, SARS' view at the moment is that, instead of regarding the goods or services supplied and deeming it supplied for no consideration (as envisaged in section 10(23) of the VAT Act), SARS deems such supplies made otherwise than in the course of the first-mentioned Branch's enterprise. This has the effect that no input tax is claimable by either of the Branches. Furthermore, should SARS' logic be followed and be extended to any other scenario where one Branch supplies goods or services for no consideration to another Branch in any other circumstance (i.e. not being goods or services acquired expressly with the intention of use by the other Branch), the supplying Branch's deemed non-supply of the goods or services will imply a change-in-use by the supplying Branch which will require an output tax adjustment by the one Branch with no corresponding deduction by the other.

Factual description

220. It thus follows from the above that the current VAT implications effectively depend on the accounting treatment, which is clearly undesired.

The nature of the businesses impacted

221. All vendors who are given approval by SARS to register its branches or divisions as separate vendors and who provide goods or services to one another.

Proposal

222. We recommended that the value of any supply by one person to another person as contemplated in section 50 of the VAT Act, be deemed to be nil. This is not uncommon in other jurisdictions like the European Union.

223. Alternatively, we would recommend that the VAT Act or BGR 16 be amended to exclude fictitious financial service entries or non-supplies from the standard turnover based method of apportionment for purposes of section 50 VAT registrations. This will also limit the number of unnecessary ruling applications, unnecessary disputes and clearly undesirable results for the Vendor.

NOT IMPLEMENTED – Section 52 of the VAT Act – pooling arrangements

Legal Nature

224. Section 52 of the VAT Act finds application to, *inter alia*, *"any pool managed by anybody for the sale of agricultural, pastoral or other farming products, being a pool as contemplated in section 17 of the Marketing of Agricultural Products Act, 1996 (Act No 47 of 1996), may on written application by such body, for the purposes of this Act be deemed to be an enterprise or part of an enterprise carried on by that body separately from the members of such body…"*

Factual Description

225. The pool registration option is only available to bodies that manage pools for the sale of agricultural, pastoral or other farming products, being a pool contemplated in section 17 of the Marketing of Agricultural Products Act, No. 47 of 1996 (Marketing of Agricultural Products Act) and rental pool schemes in respect of time sharing interests, sectional title schemes and shareholders in share block companies.

226. Before an agricultural pool can apply for and be deemed to be an enterprise separate from its members it must firstly be a pool as contemplated in section 17 of the Marketing of Agricultural Products Act.

227. It appears as if there are no pools, as envisaged in section 17 of the said Marketing of Agricultural Products Act, currently approved by the Minister. Hence no pool within the agricultural space is in a position to apply for section 52 of the VAT Act to apply.

228. Consequently, section 52 of the VAT Act can only find application to rental pools as noted in the section.

229. It is unclear on what basis only one industry is effectively singled out to make use of pooling, i.e. rental pools, in circumstances where there are other industries where these pooling arrangements will also find application.

The nature of businesses impacted

230. Agricultural pools for various supplies of produce and any other industry where there may be pooling arrangements.

Proposal

231. It is recommended that this section be amended to provide discretionary powers to the Commissioner to approve of any industry who applies for pooling.

232. In particular regard must be had to the agricultural industry where pooling is common but since these pools are not approved in terms of section 17 of the Marketing of Agricultural Products Act, these pools cannot apply for separate VAT registration.

NOT IMPLEMENTED – Section 54(2A)(a) of the VAT Act – importation of goods by an agent on behalf of its principal

Legal Nature

233. Section 54(2A)(a) of the VAT Act states the following:

"For the purposes of this Act, where any goods are imported into the Republic by an agent who is acting on behalf of another person who is the principal for the purposes of that importation, that importation shall be deemed to be made by that principal and not by such agent: Provided that a bill of entry or other document prescribed in terms of the Customs and Excise Act in relation to that importation may nevertheless be held by such agent." (own emphasis)

Factual Description

234. In practice where an agent imports goods on behalf of a principal, the customs documentation is in some cases issued in the name of the agent.

235. As far as we are aware, no distinction is made for purposes of claiming the import VAT, i.e. regardless of whether the customs documentation is issued in the name of the agent or issued in the name of the principal but merely held by the agent, the principal is allowed to claim the import VAT.

236. For purposes of clarity however, we have included our recommendation below.

The nature of businesses impacted

237. Any importer of goods that utilizes an agent to import goods on its behalf.

Proposal

238. It is recommended that the wording in the proviso to section 54(2A)(a) of the VAT Act be changed from "be held by the agent" to " be issued to the agent".

NOT IMPLEMENTED – Section 54(2A)(b)(ii) of the VAT Act – importation of goods by an agent on behalf of a foreign principal

Legal Nature

239. Section 54(2A)(a) of the VAT Act provides that where any goods are imported into the Republic by an agent acting on behalf of another person, being the principal, such goods shall be deemed to be imported by such principal and not by the agent.

240. Section 54(2A)(b) of the VAT Act provides, *inter alia*, that:

> *"(b) Notwithstanding the provisions of paragraph (a), where any goods are imported into the Republic by an agent who is acting on behalf of another person who is the principal for the purposes of that importation and -*
>
> *(i) The agent is a registered vendor; and*
>
> *(ii) The principal is not a resident of the Republic and is not a registered vendor; and*
>
> *(iii) The goods are imported by the principal for the purposes of a supply made or to be made by him to a person in the Republic; and*
>
> *(iv) The agent obtains and retains documentary proof, as is acceptable to the Commissioner, that -*
>
> *(aa) he paid the tax on importation on behalf of that principal; and*
>
> *(bb) such agent and that principal agree in writing that the said tax has not and will not be reimbursed to such agent by that principal,*
>
> *That importation shall for the purposes of this Act be deemed to be made by such agent and not by that principal."*

241. Section 8(20) of the VAT Act provides that where an importation of goods is deemed to have been made by an agent, as contemplated in section 54(2A)(b) of the VAT Act, such agent shall be deemed to make a supply of goods to the recipient of the supply by the principal as contemplated in subparagraph (iii) of that section.

Factual Description

242. Where a non-resident continuously and regularly imports goods into the Republic, for use or on-supply to any other person, that non-resident is liable to register as a VAT

vendor in the Republic if its taxable turnover in a 12-month period exceeds the R1 million registration threshold.

243. Where such non-resident is duly registered, the VAT incurred on importation will be claimable as input tax only by that vendor and section 54(2A)(b) of the VAT Act does not apply. However, where a non-resident who is liable to register does not register as a vendor, such non-compliance will entitle the non-resident to the relief afforded by the section, by virtue of the fact that the person is not a resident of the Republic and not a registered vendor.

244. It is our understanding that the said sections were introduced to provide relief to vendors who purchase goods from non-residents (who are not liable and not able to register as VAT vendors), so as to avoid cascading.

The nature of businesses impacted

245. Vendors that purchases goods from non-residents that are not liable/able to register as VAT vendors.

Proposal

246. It is recommended that the word “registered” which precedes the word “vendor” in section 54(2A)(b)(ii) of the VAT Act be deleted.

NOT IMPLEMENTED – Schedule 1 to the VAT Act – the meaning of “exported” for purposes of Schedule 1

Legal Nature

247. For purposes of the VAT Act the term “exported” is defined in section 1(1) of the VAT Act and only relates to movable goods supplied by any vendor, under a sale or an instalment credit agreement. Therefore, any goods that are consigned or delivered from a place in the Republic to a place in a foreign jurisdiction where transfer of ownership of the goods does not occur pursuant to a sale or instalment credit agreement will not fall within the definition of “exported” for purposes of the VAT Act.

248. Schedule 1 to the VAT Act stipulates that, subject to certain conditions, goods temporarily exported from the Republic will be exempt from import VAT when the goods are returned to the Republic, where no change of ownership has taken place.

249. Similarly, an exemption from import VAT exists pursuant to Schedule 1 to the VAT Act where, subject to certain conditions, goods are imported, re-exported and thereafter returned to the Republic, where no change of ownership has taken place.

Factual Description

250. The term “exported” as defined in section 1(1) of the VAT Act, is applicable to all sections in the VAT Act, including the schedules thereto.

251. Therefore, the term “exported” as included in Schedule 1 to the VAT Act could cause ambiguity for the reasons detailed below.

252. We acknowledge that the wording, “where no change of ownership has taken place” indicates the intention of the legislature, i.e. that this does not envisage “exported” as defined in section 1(1) of the VAT Act in terms of a sale or instalment credit agreement.

253. With the current wording however, a narrow interpretation could be applied, i.e. the exemptions envisaged in Schedule 1 to the VAT Act would only be applicable where goods are exported under e.g. a sale, but the goods are returned before ownership had transferred for whatever reason.

254. This is clearly not the intention of the legislature as the items included in the exemptions are items that has/will not be sold, to mention a few examples:

- Goods temporarily admitted for processing, repair, cleaning, reconditioning or for the manufacture of goods exclusively for exportation, e.g. goods (including parts therefore) for repair, cleaning or reconditioning;

- Goods temporarily admitted for specific purposes, e.g. goods for display or use at exhibitions, fairs, meetings or similar events or commercial samples owned abroad and imported for the purpose of being shown or demonstrated in the Republic for the soliciting of order for goods to be supplied from abroad;

- Goods temporarily admitted subject to exportation in the same state, e.g. private motor vehicles belonging to a person taking up temporary residence in the Republic or models or prototypes, to be used in the manufacture of goods.

255. In terms of re-imported goods subject to the exemption in Schedule 1 the exemption only applies where section 11(1)(a) of the VAT Act does not apply, i.e. the goods were exported pursuant to a sale or instalment credit agreement, which again strongly indicates that the term as defined in section 1(1) of the VAT Act would not apply to Schedule 1 to the VAT Act.

The nature of businesses impacted

256. Any vendor that temporarily exports or re-imports goods in terms of Schedule 1 to the VAT Act.

Proposal

257. We recommend that a paragraph be included in the pre-amble to Schedule 1 to the VAT Act that states that notwithstanding the definition of “exported” in section 1(1) of the VAT Act, the following exemptions will apply.

258. Alternatively, a definition of “exported” applicable only to Schedule 1 to the VAT Act, could be included that replicates the definition of “exported” in section 1(1) of the VAT Act, excluding the wording “under a sale or an instalment credit agreement”.

CATEGORY - TAX ADMINISTRATION

NOT IMPLEMENTED – Determining days in the TAA

Legal Nature

259. The calculation of time for things to be done or not done in the TAA is fundamental to it being implemented and operating effectively.

260. It is also only administratively fair if taxpayers clearly know when something must be done or not done and how to determine the period or date by which or within it must be done or not done.

261. In the TAA, calculation of time can apply in many different manners, including due to the use of both the undefined word “day” and defined word “business day”.

262. Furthermore, calculation of time is also impacted by:

- “Business day” as defined in section 1 excluding Chapter 9 disputes;
- “Business day” as defined in section 1 including Chapter 9 disputes, thus excluding the period from 16 December – 15 January;
- “Day”, which takes its normal meaning of calendar day;
- A day notified, i.e. a specific day (section 244);
- Months, which by the Interpretation Act means calendar months;
- Section 215(3) where time commences from the first day;
- Where it is a number of days, section 4 of the Interpretation Act applies and the first day is excluded and the last day included;
- If SARS specifies a day for payment, submission or other action, and the period or day specified ends on a Saturday, Sunday or Public holiday, the “day” becomes the last business day before such date;
- In any other instance than the above, section 4 of the Interpretation Act applies and if last day lands on a Saturday, Sunday or Public holiday, that day a becomes the “business day” after such day; and

- Where a time on that day is specified, then that is the end of the "day" and after that is the beginning of the next "business day".

263. Reckoning of days is also subject to other common law methods[8].

Factual Description

264. The determination of something as rudimentary as by when something needs to be done is overly complex in the TAA with various other laws and other provisions in the TAA applying.

265. This complexity is clearly also creating confusion for SARS officials. For example, the standard verification letter requires submission of documents within 21 business days, yet the final demand letter and eFiling system calculates the requirement in calendar days.

The nature of businesses impacted

266. All taxpayers.

Proposal

267. It is proposed that all days in the TAA be "business days" and if SARS requires a shorter period that they specify a specific return date and not a number of business days.

268. Furthermore, consideration should be given to consolidate the various provisions of determining "days" and time periods in the TAA into a single section for taxpayers.

NOT IMPLEMENTED – Chapter 16 Part B and section 104 of the TAA

Legal Nature

269. Chapter 16 Part B of the TAA deals with the Voluntary Disclosure Programme (VDP). In particular section 227 makes provision for the requirements for a valid VDP. Section 231 of the TAA makes provision that SARS may, subsequent to the conclusion of a VDP agreement, withdraw the relief granted under that VDP agreement, if a taxpayer failed to disclose a matter that was material for the purposes of making a valid voluntary disclosure.

270. Section 104 of the TAA deals, *inter alia*, with objections that may be lodged against the following decisions made by SARS:

- A decision not to extend the period for lodging an objection; and

- A decision not to extend the period for lodging an appeal.

[8] http://www.justice.gov.za/sca/judgments%5Csca_2001/2000_440.pdf at [6]

Factual Description

271. It is clear from the above sections that where SARS declines a VDP application for whatever reason, the taxpayer has no right to object to such decision and it thus follows that where SARS declines a VDP application, taxpayers are reliant upon PAJA to bring a review application to the High Court, which is very costly.

The nature of businesses impacted

272. All taxpayers who submit VDP applications are potentially subject to this treatment.

Proposal

273. It is proposed that section 104 of the TAA be amended to include a decision by SARS to decline a VDP application.

NOT IMPLEMENTED – Section 210 and 211 of the TAA – corporate tax administrative penalty applying retroactively

Legal Nature

274. SARS has released a Regulation for incidences of non-compliance by a person in terms of section 210(2) of the TAA that are subject to a fixed amount penalty in accordance with section 210 and 211 of the TAA.

275. It is accepted that though the penalty will apply to non-compliance dating back to 2009, the monthly penalty will only be calculated with reference to the effective date of the penalty notice referencing the notice i.e. monthly penalty will only apply prospectively from the effective date (SARS noted 9 December 2018). This is, however, not expressly stated in the notice.

Factual Description

276. Concern is expressed regarding the wording of section 211(2)(b) of the TAA, in that when SARS does not have the company's most recent address to which to deliver the penalty notice, the monthly penalty will apply from date of non-compliance, which may be from 2009. It may be that this is not an issue as section 210(2) states that non-compliance is failure to comply with an obligation that is imposed under a tax Act and is listed in a public notice. The concern is that it does not expressly require that these two criteria must be present on the date from which the penalty is calculated, but merely on the date when the penalty is imposed.

277. Furthermore, section 252 read together with section 23 of the TAA includes delivery by physical, postal and electronic means. Thus, even if the company is on eFiling, can SARS issue a penalty assessment to the invalid postal address (which practice seems to have increased recently) and apply section 211(2)(b) of the TAA notwithstanding that it could have effectively delivered the assessment by SARS eFiling or email instead.

The nature of businesses impacted

278. All companies that may be liable for the tax administrative penalty with outdated addresses.

Proposal

279. It is submitted that if the penalty is imposed in terms of section 211(2)(b) of the TAA from the date of historical non-compliance where a company's address may be out of date (for whatever reason including SARS eFiling errors), it would be retroactive and in our view not what was intended by the legislature.

280. In this regard we submit that the notice should expressly state that for the purposes of section 211(2)(b) of the TAA, the date of non-compliance is the effective date of the notice. It is further requested that SARS clarify the address update and effective delivery concern expressed above.