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The explanation provided is not convincing, we have suggested that when a stopper is placed, the taxpayer and practitioner be immediately informed instead of SARS waiting until an enquiry is made. We have further engaged SARS at the highest levels to get this matter resolved. We have also furnished them with specific examples and are expecting some positive feedback to resolve this.

We wish to re-iterate the importance of being more vigilant during this time, as chancers and fraudsters attempt to take chances and come up with various scams that might cause undue stress for you and your clients. Thus, the responsibility of ensuring that the interest of your clients is well-protected including the integrity of your profession lies with you. At the SAIPA Centre of Tax Excellence we will continue to be available by ensuring that all tax queries or challenges are resolved timeously, thus averting unnecessary stress and frustration.

It is worth noting that the 2016 Tax Indaba was a great success and added much value to the profession. The event was well-attended and we were encouraged by the cooperation between the RCB in making this annual event the success that it was. The presentations, panel discussions and plenary sessions were of a high calibre and brought a wealth of knowledge to the attendees.

It is also interesting to note that the new King IV, to be launched in November this year, has recognised the importance of tax governance. This is a step in the right direction and benefit to all tax professionals.

Lastly we wish to congratulate the Tax Ombud for the extension of his term for a further three years. This contributes to the stability of the office hence a positive benefit for the taxpayers.

We encourage all members to ensure that your CPD hours are up to date. All members are required to accumulate a minimum of 20 verifiable and 20 non-verifiable CPD hours per year. For tax practitioners, of the 20 verifiable hours, at least 12 of these must be on tax, at least 4 must be on accounting and at least 2 hours must be on ethics. All hours must be updated on your member profile by 31 December 2016. Should you be short of hours to date please check the upcoming workshops, webinars and also check the products available that count towards continuous professional development.

Enjoy this latest issue of the Tax Professional magazine with the new look and feel as we evolve to meet the needs of our members and taxpayers. The Centre of Tax Excellence (CoTE) is aware of the challenges that members and taxpayers (your clients) are experiencing when it comes to refunds and SARS’ failure to communicate about the stopper placed on refunds.

The assessment reflects a refund and after audit finalisation, the taxpayer awaits the deposit of this refund into their bank account, which they have been using for a number of years. The expected refund is not forthcoming until the tax practitioner or taxpayer queries this with SARS, only to be informed that there is a stopper on their account, and that the taxpayer must present themselves at a SARS branch and comply with the requirements; the refund still remains unpaid.

There have been reported incidents where the taxpayer has been asked by SARS for a second verification. When SAIPA raised the matter with SARS, the explanation given was that the cases with a stopper have been identified as high risk for fraud and that verification is required. Whilst
Tax evasion is by no means a new phenomenon, but as economic pressures exert an ever-growing burden on businesses, individuals, large corporations and multinationals continue to find sophisticated methods of securing extra revenue by making use of tax havens to lower their tax obligations. Leaks such as the infamous Panama Papers and HSBC Swiss leak have served to heighten awareness of what is widely known as Base Erosion and Profit Shifting (BEPS). However, what’s becoming increasingly clear is that more needs to be done to make offshore tax havens less murky.

According to the Organisation for Economic Co-operation and Development (OECD), BEPS refers to tax planning strategies to exploit gaps and mismatches in tax rules to shift profits to low or no-tax jurisdictions. Most schemes are not, in fact, illegal – the problem is that this kind of activity undermines the integrity of tax systems, since businesses that operate across borders can make use of BEPS to gain a competitive and economic advantage. The OECD contends that it challenges voluntary compliance by all taxpayers.

BEPS is defined as the negative effect of multinational companies’ tax avoidance strategies on national tax bases. “Profit shifting is generally done by means of transfer pricing, such as a management fee of royalty charge, while base erosion is usually achieved by creating or trapping profits or gains in another jurisdiction,” says Retief.

Using a very simple illustration as an example, a South African distributor sets up a company in another country, such as Mauritius, and channels the imported goods via this other company, at a
A product that costs R100 in China – which sells for R160 in South Africa – is then purchased by the Mauritian company and sold to the South African company at R130. The South African company will only recognise R30 profit on the sale of the product, through which the Mauritian company merely acted as a conduit. The profit realised in Mauritius will therefore be subject to a lesser tax liability.

**Shifting profits offshore**

A reason base erosion and profit shifting is particularly fascinating is that the world’s biggest and most successful corporations participate in the practice: Google, Apple, Starbucks and Microsoft have all come under the hammer for their tax activities.

Earlier this year, for instance, Google came under scrutiny in the UK for describing it as ‘difficult’ to calculate what tax the tech giant should be contributing in the UK. The company has been known to route foreign profits to Bermuda through subsidiaries in Ireland and the Netherlands. Most estimates, writes Mark Ritson, Adjunct Professor at Melbourne Business School, put Google’s tax payments at £200 million over the last 10 years – when, if it had been worked out according to the corporation tax rate, which is 20% of all UK profits, would have amounted to £1.44 billion.

Apple, too, employs offshoring practices when it comes to its international tax concerns. Recent estimates indicate the company has saved $59 billion in tax payments in the United States as a result of these practices. The company is a classic example of profit shifting, says Retief, as it is registered in more than one jurisdiction – Holland and Ireland – to take advantage of the difference in tax treatment of royalties and lower (even negotiated) tax rates in Ireland.

American pharmaceutical company Pfizer merged with Ireland-based Allergan recently, and plans to shift its headquarters to Ireland, a move which is calculated to potentially save the company up to $148 million in profits. A number of Fortune 500 companies, including Google, have established subsidiaries in Ireland to take advantage of the tax benefits it provides.

 Starbucks is another example of an organisation employing profit-shifting practices to enjoy greater tax benefits. “Beans are sold to the UK via a Swiss company, which means the profit is shifted there, even though the Swiss company doesn’t touch the beans at all or add any value to the transaction,” Retief explains. Switzerland is a popular option for large corporates because of its combination of low taxes and a banking system aimed at protecting its account holders’ privacy.

Closer to home, MTN made headlines last year for the billions of rand earned in African countries that it moved to offshore tax havens, most notably Mauritius. The company said the money was ‘management fees’ but authorities in South Africa, Ghana, Nigeria and Uganda questioned the organisation’s complex and muddy tax payments system; as a result, it had to reverse R2.5 billion in payments in Nigeria, while Ugandan tax authorities demanded over R100 million in repayments. However, there remains no evidence that any of MTN’s offshore activities are in fact illegal.

Major global corporations JPMorgan Chase, Citigroup and Pepsi, too, have subsidiaries in Mauritius, according to the Wall Street Journal, because although the island imposes a 15% corporate tax rate, companies are able to take advantage of tax breaks obtainable as a result of double tax treaties – in addition, capital gains and interest aren’t taxed in Mauritius.

South African mining company Lonmin was found to have moved millions of rand in platinum revenue from South Africa to tax-free Bermuda. Bermuda is a popular profit-shifting destination for large businesses because it does not levy any corporate tax. Other effective tax haven destinations include Luxembourg – where Amazon has its European headquarters – the Cayman Islands, Isle of Man, Jersey, Monaco and the Bahamas.

**The OECD BEPS Package to tackle evasion**

Due to the prevalence of large corporations exploiting gaps in tax rules, the OECD established the BEPS Package in an effort to combat unethical activity. The package is an inclusive international tax framework that has brought together over 100 countries and jurisdictions – it provides 15 actions and tools that enable governments to ensure that profits are taxed where they are generated.

The BEPS Package serves to standardise tax compliance requirements, as well as reduce disputes over international tax rules. Monitoring mechanisms are in the process of being developed in order to ensure that all members of the package and framework comply with its requirements.

“Profit shifting is generally done by means of transfer pricing, such as a management fee of royalty charge, while base erosion is usually achieved by creating or trapping profits or gains in another jurisdiction.”
However, says Retief, there are still widespread challenges associated with profit shifting and tax evasion, and for many the OECD intervention is seen as a political shopping expedition.

What makes these tax matters ‘difficult’ to calculate, however, is that these organisations have built structures that enable them to funnel revenues through offshore tax havens in order to maximise profits. “What these companies have done is not technically illegal as they have negotiated favourable tax terms and are acting within the letter of the law, but their activities have highlighted two major problems: complexity and secrecy,” explains Retief.

“Complexity arises since it is difficult to know where the substance of the transactions of these organisations has taken place and, therefore, where tax should be paid, and leaks such as the Panama Papers have exposed secrecy through the use of shell companies. This is where the process of profit shifting becomes murky and where it is necessary to talk ethics.”

From a business point of view, tax is a cost, so it’s natural for business leaders to look for ways to minimise that cost – it may not be right, says Retief, but it’s a motivation. There are also circumstances where there are legitimate reasons for companies to use complex off-shore structures.

An unfavourable exchange rate, for instance, is a risk for a business, and if international operations are held in a location such as Mauritius to manage forex risks and allow for operational efficiency, there is no problem if the organisation is legitimate and applies appropriate transfer pricing. “It is only problematic if the business is a front and there is no substance there,” says Retief.

What it essentially boils down to is the need to look beyond the legal to the true economic substance of the practice. The benefit of the Panama Papers leak is that it brings to light the need for the sharing of information on the real beneficiary of cross-border transactions. The Panama Papers have made it easier to break down transactions by jurisdictions and question different authorities. There is more of a focus on understanding the real beneficiary, rather than simply the holding company, which will make interventions to tackle nefarious activities associated with BEPS more effective.

Retief predicts that there will be no end to tax havens in this generation, in spite of the fact that many are linked to criminal and terrorist activities. “Tax havens might be widely criticised, but they play, and will continue to play, a critical role in doing business as a result of increasing economic pressures and the need for the wealthy to preserve their wealth. Where the big shift is happening is that there is growing pressure on companies to illustrate that they are paying corporate tax and much of the future success in dealing with wrongdoing is going to be based on the sharing of information,” he says.

Looking ahead, companies are going to have to start thinking of tax risk in the longer term – companies currently coming under scrutiny for their tax practices are being examined on decisions made years ago. “Businesses need to make decisions now and realise the future implications of those decisions – risk is forward moving, so organisations cannot make decisions based on today’s needs, but rather the impact those decisions might have in years to come,” he concludes.
Tax practitioners are often requested by taxpayers (individuals and businesses) to act as tax representatives. In fact, many tax practitioners accept such requests as it represents a lucrative stream of income. Often tax practitioners believe that once the tax assignment is completed, then their responsibilities as the tax representative ceases. However, when the tax practitioner is called upon by SARS to cough up the cash to settle the taxpayer’s debt, there is shock and disbelief!

The Tax Administration Act and the Public Officer

The Tax Administration Act\(^1\) requires that every company that has an office in South Africa must appoint a Public Officer – also a resident of South Africa – within one month after the company begins to carry on business or acquires an office in the Republic. Of course, the company is expected to inform SARS of the individual appointed as its Public Officer.

The individual must be appointed by the company or by an authorised attorney or agent. If no appointment is made, SARS could appoint either the managing director, company secretary or a director of the company to perform the duties of a Public Officer. A Public Officer is appointed by a company resolution.

The question is: should the tax practitioner also perform and act as a Public Officer for its clients?

Who is the taxpayer?

Before the central question of this brief may be answered, an understanding of the following is required:

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\(^1\) Section 246 of the Tax Administration Act 28 of 2011.
Representative taxpayer\(^2\), Liability of a representative taxpayer, and Personal liability of representative taxpayer.

A distinction must be made between a person chargeable to tax and a taxpayer. A person chargeable to tax is the person upon whom the liability for the tax is imposed and is the person who is personally liable for the tax. But the term ‘taxpayer’\(^3\) as defined by the Tax Administration Act is a very broad term.

A taxpayer includes the following:
- A person chargeable to tax
- A representative taxpayer;
- A withholding agent;
- A responsible third party; or
- A person who is the subject of a request to provide assistance under an international tax agreement.

However, the only relevant concept for the purpose of this brief is the concept of a ‘representative taxpayer’.

### Duties and functions of a Public Officer

The Public Officer is responsible for all matters relating to a tax act. The Public Officer is the ‘face’ of the entity – the Public Officer is, in essence, a representative of the entity in all aspects including tax. In other words, the Public Officer has full representative authority and accountability for the entity.

Generally, the office of the Public Officer is the place for delivery of SARS notices. Alternatively, the company must appoint a place for service or delivery of notices and any other documents. A document will be regarded as properly delivered if handed to the public officer. The Public Officer is the main correspondent between SARS and the taxpayer, to such an extent that SARS never communicates directly with the taxpayer. SARS deems the Public Officer as a taxpayer. Therefore, all actions taken by the Public Officer with respect to tax matters is regarded as having been taken directly by the taxpayer. Consequently, any allegation by a company (the taxpayer) that a particular action by a Public Officer is unauthorised will no longer have any merit. It is the responsibility of the Public Officer to pay the tax from the client’s bank account.

Based on the duties and functions of a Public Officer, it is clear that the Public Officer is also the representative taxpayer of a company or a close corporation. This is the gist of this article and herein located the solution to our primary concern.

### Should Tax Practitioners be Public Officers as well for their clients?

The representative taxpayer, which includes a Public Officer, is a person who is responsible for paying tax on behalf of the taxpayer. Moreover, a representative taxpayer may be held liable for the tax liability of the taxpayer in a personal capacity. If the taxpayer cannot settle the liability, the Public Officer will be held responsible for the tax debt.

The Tax Administrative Act\(^4\) is explicit that a Public Officer, although in a representative capacity, is personally liable for the tax payable while it remains unpaid. If the tax liability remains unpaid, and the public officer (a representative taxpayer) alienates or disposes of amounts from which the tax could legally have been paid to SARS but instead the funds were used to pay another person on behalf of the taxpayer, then SARS may institute civil claims against the Public Officer. Therefore, why should a tax practitioner also perform the duties of a Public Officer for its clients? Legislatively, a tax practitioner could be personally and legally liable for a tax debt of a client and this liability depends on the facts and circumstances of the client (a company, in this situation).

A tax practitioner must consider the risks associated with a client before agreeing to act as its Public Officer. When a client is declared insolvent, a liquidator may undertake the functions and duties of a Public Officer, but the Public Officer is still liable for the unpaid tax debts.

### The way forward

The tax practitioner, therefore, should efficiently manage the tax affairs of a client but should not act in a ‘representative’ capacity for the client as the Public Officer. Therefore, a tax practitioner should perform its duties ‘for and on behalf of a client’ but should not perform its duties in a ‘representative’ capacity. The engagement letter concluded between tax practitioner and client (the taxpayer) should be mindful of these nuances.

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\(^2\) Sections 153, 154 and 156 of the Tax Administration Act 28 of 2011.
\(^3\) Section 151 of the Tax Administration Act 28 of 2011
\(^4\) Section 155
Very often a taxpayer (usually a parent) – a connected party - and who may not be a beneficiary, donates or sells an asset to a family trust. The sale of the asset to a family trust is often via a loan account. This article focuses on the sale of an asset to the trust via loan account at less than market-related interest rates.

**Donation or outright loan?**

When an asset is sold to a trust, it does not imply that the sale will give rise to donation tax – the deciding criteria is the selling price in relation to the market value at the date of sale.

If the sale of the asset is at full market value to a trust, and in this situation, then the sale would not constitute a donation for donation tax purposes. However, if the asset is sold at a price below the market value, then the sale will attract donations tax.

The fact that the asset is sold via a loan account, no transfer of cash has taken place, therefore, donation tax implications are not forthcoming.

In an important tax case law, SARS v Woulidge (2002) (1) (SA 68 SCA), the shares were sold to a trust at their market value, but were in the form of an outstanding loan account. It is given that the loan account was non-interest-bearing and the court held a view that such disposal of the shares had both sizable elements of gratuitousness (interest-free loan account), and proper consideration - that is, the sale of shares at market value. In other words, the purchase price constituted due consideration even though it was an outstanding loan account. The court held the view that the sale constituted a donation as the trust benefited from not paying interest.

With reference to another widely known tax case (Relier (Pty) Ltd v CIR 1997 (S) JTLR 119 (SCA), the
court argued that parties cannot arrange their affairs with the aid of simulated transaction (the disguise sale), but tax affairs must assessed based on the substance (not form) of the transaction that is the intention and spirit in which the transaction was concluded.

If there is a loan account arising as a result of a sale of an asset, and there is clearly no intention that the loan account be repaid, then the legal effect should be given to the true intention of this transaction (the substance and not the form), the transaction should be taxed as a donation viz. the intention to donate the asset.

For a transaction to be classified as a loan it must consist of components for future repayment of the capital amount and components for the future repayment of the interest component. If there is a loan account arising as a result of a sale of an asset, and there is clearly no intention that the loan account be repaid, then the legal effect should be given to the true intention of this transaction (the substance and not the form), the transaction should be taxed as a donation viz. the intention to donate the asset.

The real intention of the taxpayer must be established. Was it to donate the assets to the trust and not to disguise the transaction as a sale? If the transaction is a donation and has all the ingredients of a donation then it is obvious that such transaction must be subject to donation tax, the substance of the transaction.

The use of the R100 000 donation tax exemption

Quite understandably, individual taxpayers are tempted to use the donation tax exemption rule that prohibits the payment of donation tax if the sum value of all property disposed of under donation, donated during any year of assessment, does not exceed R100 000. There is a view that this exemption rule can be used to surrender or waive a portion of the trust loan account in the trust. The donation tax exemption cannot be applied in this situation because section 19 of the Income Tax Act applies to allowance asset only (it is given that the fixed property is not an allowance asset) and it does not apply to donation. It is given that allowance asset refers to a capital asset in respect of which is a deduction or allowance. This refers to deduction in respect of plant and utensil (section 12B), deduction in respect of assets used by manufacturers (section 12C), deduction in respect of Small Business Corporation (section 12E) and the building allowances (section 13).

The relevance of Section 7 of the Income Tax Act (income is deemed to have been accrued or to have been received)

This section refers to the income earned from the asset that is sold to a trust via a loan account and ensures that if an amount accrues to a trust or to a beneficiary as a result of some donation or gratuitous disposition, the person who receives that amount or to whom the amount accrues will not be taxed on the receipt or accrual. Another person, in this situation, the donor will be taxed on the amount. For example, if a property earning rental income is donated to a trust, the rental income would be deemed to be the income of the donor.

Another illustrative example (and similar to the situation under review), would be the sale of an asset to a trust in terms of which the selling price is left owing, either as an interest-free loan or as a loan at an interest rate below a commercial rate of interest. The tax practitioner is reminded that to the extent that the loan is interest-free or below a commercial rate, the loan would be a gratuitous disposition, and any income that accrues to another person as a result of this gratuitous disposition would fall under the deeming provision of section 7 of the Income Tax Act.

Capital gains tax implication

It is given that when an asset is sold to a trust via loan account there will be both income tax implication and capital gain tax implication. This section makes reference to the capital gain tax implication of the asset sold to a trust via loan account with interest rates at either below market rate or at nil interest rates.
If a taxpayer intends to reduce the amount of the loan owing by the trust, that is, to donate a portion of the loan account in a trust each year, then this would amount to a waiver or a reduction of a debt for no or insufficient consideration and such donation would be regarded as a deemed disposal for CGT purposes in terms of paragraph 12 (5) of the Eight Schedule. Illustrative example 1 is also relevant in this situation.

With reference to the question of CGT implication and the annual R100 000 donation tax exemption, please be advised that there are no annual capital gain arising from the R100 000 donation. It used to be the case under para 12(5) but that provision has been deleted and now there is an exemption under paragraph 12A(6) (b)\(^1\).

Instead, the attribution rules (paragraph 67 – 72 of the Eight Schedule) would apply – that is, the capital gain would accrue to the donor of the asset arising on disposal of an asset funded by an interest-free loan. Paragraph 70 and paragraph 73 will be crucial in understanding the ensuing discussion. These paragraph refer to the capital gain, but the mechanics works in the same way as section 7 of the Income Tax Act. Section 7 refers to income tax only while paragraphs 67 to 72 of the Eight Schedule refers to capital gains.

If the capital loss arises from the waiver of a loan to a trust, and the capital gain in the trust is attributed back to the ‘donor’ under (say) paragraph 70, the creditor will not be able to claim the capital loss, since the capital gain will have been removed from the trust.

Paragraph 73 of the Eight Schedule is crucial in this regard. It limits the total amount of the income and capital gain that can be taxed in the hands of the seller (the donor), to the amount of the benefit derived from that donation, to the trust to whom it was made. More simply stated, this implies that the donor’s income is limited to the derived

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\(^1\) 12A. Reduction of debt
(a) This paragraph must not apply to any debt owed by a person-
(b) to the extent that the debt is reduced by way of-
(i) donation as defined in section 55(1); or
(ii) any transaction to which section 58 applies;
benefit of the trust. The quantified benefit to the trust, that is, when an asset is sold to a trust on loan account, and not at market-related interest rate, the difference between the an interest-free or low-interest loan, and the full market value, will therefore determine the extent to which any resulting income and capital gain can be attributed to the donor. An Illustrative example is provided below to demonstrate the application of paragraph 73 of the Eight Schedule and section 7 of the Income Tax Act.

**ILLUSTRATIVE EXAMPLE – Attribution of exempt income and capital gain**

**Background**

At the beginning of year one, Dirk lent R100 000 interest-free to his family trust. Had the trust borrowed the funds from a bank it would have paid interest at the rate of 12% a year. The trust used the funds to purchase South African-listed shares. During the year dividends of R3 000 were received. On the last day of the year of assessment the shares were sold for R110 000. Assume that the disposal is on capital account and that the Trust did not distribute the income of the trust or the capital gain to any beneficiary.

**Question:**

What are the tax consequences of this transaction?

**Answer:**

The interest benefit derived by the trust from the loan is R100 000 × 12% = R12 000.

First, R3 000 of the benefit is deemed back to Dirk under s 7(5) as it represents the ‘profit’ of the trust.

<table>
<thead>
<tr>
<th>Tax Year</th>
<th>Trust Income</th>
<th>Trust Capital Gain</th>
<th>Total Income of Trust</th>
<th>Trust Benefit</th>
</tr>
</thead>
<tbody>
<tr>
<td>1</td>
<td>R3000</td>
<td>R10 000</td>
<td>R13 000</td>
<td>R12 000</td>
</tr>
</tbody>
</table>

It must be borne in mind that the trust income arises by the use of the asset and does not arise as a result of the below market-rate interest-rate loan. The result is that the remaining benefit of R12 000 – R3 000 = R9 000 is used to attribute R9 000 of the capital gain to Dirk. The remaining portion of the capital gain (R1 000) is taxed in the trust. From Dirk’s perspective the R3 000 will be included in his gross income and the R9 000 of the capital gains will be included in his taxable income.

**Conclusion**

The tax practitioner is reminded that to the extent that the loan is interest-free or below a commercial rate, the loan would be a gratuitous disposition, and any income that accrues to another person as a result of this gratuitous disposition would fall under the deeming provision of section 7 of the Income Tax Act.

The quantified benefit to the trust, that is, when an asset is sold to a trust on loan account, and not at market-related interest rate, the difference between an interest-free or low-interest loan, and the full market value, will therefore determine the extent to which any resulting income and capital gain can be attributed to the donor – the donor in the aforementioned example will account for the R3 000 in his gross income while the R9 000 of the capital gains will be included in his taxable income. The capital gains will be included at the appropriate inclusion rate 33.3% (wef 1 March 2016: 40%).

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2 Reproduced from SARS comprehensive guide on CGT (issue 5). December 2015 page 575
3 The interest benefit derived by the trust from the loan is $100,000 \times 12\% = $12,000.
Although the rules for calculating the estimate of taxable income have been with us for little less than three years, the rules still present tax practitioners with difficulties, and which, as a result, give rise to an understatement-of-estimates penalties. This article focuses on the method required for the calculation of the estimates of taxable income. This requires a calculation of the basic amount when estimating taxable income for payment of provisional taxes.

Generally, provisional taxpayers are required to make two estimates of taxable income in a tax-year. Individual taxpayers must calculate the estimates of taxable income by the end of August (first period) each year and an estimate of taxable income in February of each year (the second-period) which is the last day of the tax year of assessment.

Companies are expected to calculate the estimate of taxable income (first-period) on or before the last day of the six-month after the commencement of the tax year which coincides with the commencement of the financial year. The second estimate of taxable income for a company must be done on or before the last day of the financial year. So if a company financial year begins on 1 January, then the first-period estimate must be done on or before 30 June of each year. The second-period estimates of taxable income must be done on or before 31 December each year – the last day of the year of assessment.

Calculation of the basic amount for the first period

With reference to the first period, the provisional tax
must be paid on or before the last business day of the period, that is, 31 August for individual taxpayers. For companies, the provisional tax must be paid on or before the last day of the six-month after the commencement of the tax year which coincides with the commencement of the financial year.

For the first period, a provisional taxpayer is required to submit a return stipulating the estimate of taxable income that a provisional taxpayer is expected to earn in the year of assessment under review. The amount of provisional tax for the first period is based on this estimate. The provisional taxpayer is required to pay half of the total estimated liability for normal tax, less payment already made if the provisional taxpayer is an individual.

Moreover, the estimated taxable income must include taxable capital gains made, or that are anticipated to be made, during the relevant year of assessment. If in the first period, there is a reasonable expectation that a taxable capital gain will be made during the second period, then the expected capital gain must be included in the estimate of the taxable income. For individual provisional taxpayers the estimate must exclude the taxable portion of lump sum benefits and severance benefits received by or accrued to (or to be received by or accrue to) the taxpayer during the year of assessment.

The ‘basic amount’ is the taxable income assessed for the latest preceding year of assessment, less any taxable capital gain included therein and, for individual provisional taxpayers, any taxable portion of a lump sum benefit or severance benefit, but includes the two-thirds of the fund benefit paid in the form of annuity. The basic amounts also includes amount received by an individual in respect of voluntary awards and lump sum from an employer (as per paragraph (d) of the definition of ‘gross income’).

The two dilemmas

There are two dilemmas confronting a provisional taxpayer when calculating the provisional tax for the first period. These are:

i) Which year of assessment must a provisional taxpayer use in order to determine the ‘basic amount’ for income tax purposes, and

ii) By what percentage should the basic amount increase by 8%, 16%, 24%?

First dilemma

With reference to the dilemma in (i) above, the basic amount applicable to an estimate (for the first period and the second period if the taxable income is R1 million or less) is ‘the taxpayer's taxable income as assessed by SARS for the latest preceding year of assessment’ and for which a notice of assessment was issued by SARS 14 calendar days or more before the date on which the estimate was submitted to SARS.

ILLUSTRATIVE EXAMPLE 1

Background information

Taxpayer A’s year of assessment ends on 28 February each year. Taxpayer A submitted a first period provisional tax estimate for the 2017 year of assessment on 30 August 2016. A notice of assessment was issued to Taxpayer A for the 2017 year of assessment on 30 August 2016. A notice of assessment was issued to Taxpayer A for the 2016 year of assessment on 31 July 2016. A notice of assessment was issued to Taxpayer A for the 2015 year of assessment on 31 July 2015. A notice of assessment was issued to Taxpayer A for the 2016 year of assessment on 30 August 2016. A notice of assessment was issued to Taxpayer A for the 2015 year of assessment on 31 July 2015. Taxpayer A’s taxable income as assessed in 2015 was R150 000. Taxpayer A did not have any taxable capital gains or retirement or severance related lump sums in 2015.

Question: Which year of assessment should Taxpayer A use to calculate the basic amount?

Answer: Taxpayer A’s latest preceding year of assessment is 2015 because it is the latest year of assessment for which Taxpayer A was issued a notice of assessment 14 days or more from the date on which the first provisional tax estimate of taxable income was submitted. Taxpayer A’s 2016 assessment is not the latest year of assessment and cannot be used to calculate the basic amount as the notice of assessment was issued less than 14 days (August 30 less 14 days = 16 August is the cut-off date) before the date on which the first provisional tax estimate of taxable income was submitted. It is given that the 2016 assessment was issued on 18 August 2016 which is only 12 days difference and is within the 14 day period.
Second Dilemma

With reference to the second dilemma in (ii) above, this section of the brief considers what the percentage increase of the basic amount should be when estimating the taxable income. The amount of the estimate for the first period cannot be less than the ‘basic amount’ unless the circumstances of the case justify the submission of a lower amount.

There is no tax legislation that prevents a taxpayer from using a lower amount as the basic amount. The taxpayer, however, can be called to justify the lower amount used to determine the basic amount. The reason for using a lower amount must not be frivolous. SARS has the legislative right to call upon a provisional taxpayer to justify any estimate made by the taxpayer to furnish particulars of income and expenditure (or any other information). If SARS is not pleased with the estimate, SARS could increase the amount that it considers reasonable. This increase in estimate is not subject to objection and appeal according to the Fourth Schedule of the Income Tax Act.

The basic amount in relation to an estimate of taxable income (for the first period and the second period) is calculated as follows:

- The taxable income as assessed by SARS for the latest preceding year (as discussed above under item (i)) of assessment in relation to the estimate,
- LESS: Taxable gain included in that taxable income, taxable portion of any retirement fund lump sum benefit, and lump sum amounts received from the employer.

It is understood that the basic amount used as an estimate should include only regular income. The Fourth Schedule of the Income Tax Act informs the taxpayers that the basic amount should be increased by 8% a year if the basic amount is based on assessment issued more than 18 months after the end of the latest year of assessment.

The first illustrative example can be used again to demonstrate how percentage increase of the basic amount can be applied. It is concluded that latest year of assessment is 2015 and its taxable income is R150 000. The ‘basic amount’ for the first period of provisional tax estimate for 2017 is required. It is given that the estimate is made on 30 August 2016.

But paragraph 19(d) of the Fourth Schedule to the Income Tax Act prescribes that the estimate ‘must be made more than 18 months after the end of the latest preceding year of assessment in relation to such estimate’. The first provisional tax estimate is not made ‘more than 18 months’ after the end of the 2015 year of assessment, and therefore, the basic amount should not be increased by 8% per year.

With reference to the illustrative example 2 cited above, the Taxpayer A submitted the first provisional tax estimates for the 2017 tax year on 30 August 2016. It was concluded that the latest preceding year of assessment is 2016 tax-year. The taxable income given for the 2016 tax year is R210 000 and can be used as the basic amount without an additional 8% increase! The last preceding year of assessment (2016) is less than 18 months. The same amount of R210 000 can be used to calculate the basic amount for the first provisional tax payments for the 2018 year of assessment if the 2016 assessment is still the latest year of assessment and does not exceed 18 months period. Under these circumstances, the basic amount must not be increased by 8%.

In the aforementioned example, the 2016 assessment has been assessed in time for the first 2017 provisional tax estimation; the basic amount is equal to the 2016 taxable income. If the last year of assessment for the first 2017 provisional tax estimation was 2015, then the basic amount must be increase by 16%. If the last year of assessment for the first 2017 provisional tax estimation was 2014, then the basic amount must be increase by 24%.
FURTHER WELCOME TAX INCENTIVES ANNOUNCED FOR RENEWABLE ENERGY SECTOR

Renewable energy is seen as the long-term future to the planet’s energy demands as a result of the increasing effects of climate change due to the long-term use of fossil fuels. South Africa, in particular, has certain obligations as a party to the United Nations Framework Convention on Climate Change (UNFCCC) to ensure the reduction of greenhouse gas emissions and to incentivise investments in low carbon, clean energy. In addition to the environmental factors, South Africa’s load shedding and insufficient power supply has resulted in a further demand for the greater procurement and use of renewable energy.

However, renewable energy projects and initial set-up costs are expensive. As a result, government has introduced many tax incentives in the renewable energy sector. Some of the incentives or mechanisms which have been introduced are focused on reducing carbon emissions, including the still to be introduced carbon tax. Other incentives are focused on energy efficiency such as the industrial policy projects’ additional allowance contained in s12I of the Income Tax Act, No 58 of 1962 (Act), the energy efficiency savings’ allowance contained in s12L, as well as the production of renewable energy and fuels’ allowance contained in s12B.

The Draft Taxation Laws Amendment Bill, 2016 (Draft TLAB 2016) intends introducing the latest renewable energy incentive. The Explanatory Memorandum to the Draft TLAB 2016 states that large-scale renewable energy projects are currently not sufficiently catered for ‘due to the capital intensive nature of the supporting infrastructure whose tax treatment would need to be specifically targeted’. In particular, ancillary capital expenditures that indirectly support renewable energy production, such as the construction of necessary fences and roads close to renewable energy farms do not qualify for any deductions under the Act. The lack of sufficient tax deductions for such auxiliary outlays is, according to the industry, one of the major restrictions on the feasibility of such projects.

Government, therefore, proposes that provision is made for further specific tax deductions to encompass the supporting capital infrastructure for large renewable energy projects. The proposal is limited to renewable energy projects exceeding 5MW and above. The reason for this appears twofold. First, projects within the 5MW to 50MW band are barely economically viable and this will, hopefully, boost such projects’ viability. Secondly, all renewable energy projects approved under the Renewable Energy Independent Power Producers Procurement Programme of the Department of Energy exceed at least 5MW.

The proposal includes provision for a deduction of pretrade expenditure in much the same way as s11A of the Act to the extent that the capital expense is actually incurred prior to the commencement of, and in preparation of, carrying on that trade, and where it has not been allowed as a deduction previously in the current or any previous year of assessment. The new intended s12U of the Act also provides for an antiavoidance mechanism, in that any supporting infrastructure capital expenditure that exceeds the income in any year of assessment be ring-fenced to the specific trade of the production of renewable energy. The proposed amendment is due to apply to large renewable energy projects undertaken during any year of assessment commencing on or after 1 April 2016.

While the increase of renewable energy tax incentives is most certainly welcome, it remains to be seen whether the recent round of proposed amendments will have a positive effect on the uptake of large renewable energy projects. An additional tax deduction in a similar form as the additional 50% research and development tax deduction has, despite calls from the industry, not been forthcoming. Nevertheless such an amendment may have a much larger impact on the feasibility of sorely needed large-scale renewable energy projects.

“The lack of sufficient tax deductions for such auxiliary outlays is, according to the industry, one of the major restrictions on the feasibility of such projects.”
The worlds of tax law and labour law are complex, ever-changing and closely intertwined. That means that South African organisations need to consider what legislation in each of these fields says about concepts such as remuneration, employees, and bonuses. In other words, your finance team needs to know something about labour law as it handles your taxes, while your human resources team needs to understand where labour and tax regulation intersect.

We see this interaction at work when we determine who exactly should be treated as an employee by your organisation rather than as a contractor or an independent service provider. For its part, SARS has expanded the definition of an employee over the years in an effort to cast the PAYE (personal income tax) net wider. This has some important implications for how you manage your payroll.

With that in mind, I’d like to break down how you should handle your relationships with personal service providers — Small & Medium Businesses that SARS effectively sees as disguised employees of your business — and labour brokers, who have come under more and more scrutiny in recent years.

**Defining Personal Service Providers**

In days gone by, employees would resign and then continue to do the same job as before — except they would bill for their services through a company. Employees, especially those in higher tax brackets, could thus pay a lower company tax rate on their gross income and reduce their personal income tax bills.

SARS clamped down on this practice through an amendment to the Income Tax Act in 2000 that essentially turned the company into an employee for PAYE purposes. If you have someone working for your company as a service provider, you must withhold PAYE tax at a rate of 28% if it is registered as a company, and 41% of it is registered as a trust. The following cannot be personal service providers:

- Natural persons – in other words, an employee trading as a sole proprietor or a partnership.
- Labour brokers.
- Service providers that provide all services.
to you through their employees other than directors and their spouses and relatives.

- Service providers which throughout the tax year of assessment have three or more full-time employees (other than shareholders, trust beneficiaries and their spouses and relatives).

If the service provider is not excluded by these rules, they will be classified as a personal service provider, as long as any of the following applies:

- You would regard the person as an employee if he or she rendered the service directly rather than through a company or trust.
- The worker does most of his or her duties on your premises and under your supervision.
- The service provider earns 80%-plus of its annual income from any one of its clients.

To overcome this last test, you should ask your service providers who may qualify as personal service providers to provide you with an annual affidavit or solemn declaration that they do not receive 80% of their service income from your business. You may rely on this declaration in good faith.

In addition to withholding PAYE for a personal service provider, you must also produce a tax certificate using the same tax certificate reporting codes as used for normal employees. If the vehicle charges VAT, the remuneration will be the service fee value excluding VAT. You can, of course, can claim the input VAT back.

**Tighter laws on labour brokers**

SARS has also put labour brokers under increasing scrutiny. Now, it defines a labour broker as any natural person who provides clients with employees to render a service or procures other persons and provides them to a client. In each case, the client controls and supervises the workers provided by the labour broker.

You pay a fee to the labour broker, who in turn pays the workers and makes all statutory payments on their behalf, including PAYE and SDL. If the labour broker is not in possession of an IRP30 tax exemption certificate, you must withhold PAYE and the Skills Development levy from the total fee you pay the labour broker.

SARS will issue an IRP30 exemption certificate to a labour broker if:

- Carries on an independent trade.
- Is registered as a provisional taxpayer.
- Is registered as an employer for PAYE purposes.
- Is up to date with all its tax returns.

SARS will not issue an IRP30 exemption certificate to a labour broker if:

- More than 80% of its gross income is likely to consist of amounts received from any one client or associated institution, and there are less than four employees who are not connected persons in relation to the labour broker.
- The labour broker provides the services of any other labour broker to any of its clients.
- The labour broker is contractually obliged to provide a specified employee to render services to any client.

Companies, close corporations or trusts that, prior to March 2009, were labour brokers are no longer labour brokers in terms of tax law, but remain Temporary Employment Services in terms of labour law. They must be paid through the creditors system rather than the payroll. For labour brokers, the PAYE you withhold should be calculated on the total fee according to the statutory tax table.

Be careful that you carefully distinguish between labour brokers and personal service providers for tax reporting purposes.

**Closing words**

In general, SARS is trying to capture PAYE tax at the source from as many people your business works with as possible, including some labour brokers, personal service providers and some contractors. Its philosophy is to capture tax now and refund later if necessary. Be aware that people not regarded as employees in labour law, such as some independent contractors, are not necessarily independent contractors in terms of tax law.

As the global market leader of integrated accounting, payroll and payment systems, we have become an indispensable business partner to the country’s Small & Medium Businesses. For us, this isn’t just about providing use the smartest technology to reinvent and simplify business accounting and payroll, but also helping clients to navigate the tax and legal environment. That’s why we present our labour and tax law seminars to help entrepreneurs make sense of an increasingly complex landscape.
The Draft Taxation Laws Amendment Bill of 2016 was released for public comment on Friday 8 July (the ‘2016 TLAB’). It proposes certain amendments to the rules currently contained in the Income Tax Act No. 58 of 1962 (the ‘Act’) dealing with employee-based incentive plans.

Some of these proposed changes were foreshadowed by announcements made by the Minister of Finance in the 2016 Budget Speech, namely that:

- Section 8C of the Act will be reviewed to address schemes where restricted shares held by employees are liquidated in return for an amount qualifying as a dividend
- Certain dividends in respect of restricted equity instruments are subject to income tax. These taxable dividends will be specifically included in the definition of ‘remuneration’ for employees’ tax purposes
- The Act will be amended to avoid possible double taxation on the acquisition of a restricted equity instrument under both the definition of ‘gross income’ and under section 8C of the Act

Specifically, a substitution of paragraph (ii) of the proviso to section 10(1)(k)(i) has also been proposed. This paragraph of the proviso currently provides that any dividends received or accrued to a taxpayer in respect of services rendered or to be rendered, or in respect of/by virtue of employment or the holding of any office, will not be exempt from income tax, unless that dividend was received or accrued in respect of a restricted equity instrument held by that person, or in respect of a share held by that person.

If implemented as currently proposed, the substitution of paragraph (ii) to this proviso will exclude from the 10(1)(k) exemption, any dividend received or accrued to a person in respect of services rendered or to be rendered, or in respect of/by virtue of employment or the holding of any office, other than dividends accrued to that person in respect of:

1. An equity instrument, after that equity instrument has vested in that person as contemplated in section 8C; or
2. A marketable security, contemplated in section 8A, held by that person.
In addition, the 2016 TLAB proposes that section 8C(1A) be substituted. This section currently provides that a return of capital other than a distribution of an equity instrument received by a taxpayer in respect of a restricted equity instrument must be included in that taxpayer's income. The suggested substitution provides that any amount received by or accrued to a taxpayer in respect of a restricted equity instrument must be included in his/her income during the relevant year of assessment, with the exception of amounts that are:

- distributed as a return of capital or foreign return of capital to that taxpayer by way of a distribution of a restricted equity instrument;
- subject to the provisions of the Act dealing with dividends received in respect of restricted equity instruments; or
- taken into account in terms of section 8C in determining the gain or loss in respect of that restricted equity instrument.

These amounts will constitute 'remuneration' in terms of paragraph (e) of the definition contained in paragraph 1 of the Fourth Schedule to the Act, being amounts required to be included in the income of a taxpayer in terms of section 8C of the Act. As such, employees’ tax will be required to be withheld in respect of these amounts.

It is anticipated that the abovementioned changes will come into operation on 1 March 2017, and apply in respect of any amount received or accrued to a taxpayer on or after that date. It therefore appears that this proposed change would apply to existing, unvested restricted equity instruments.

A further proposed change, which was not announced in the 2016 Budget Speech, is the introduction of a new section 8CA of the Act. This section would deal with expenditure incurred in respect of ‘restricted equity instrument schemes’. A ‘restricted equity instrument scheme’ is defined for these purposes, in relation to an employer, as a scheme in terms of which an equity instrument (as defined in section 8C), the value of which is determined directly or indirectly with reference to an equity share in that employer (or an associated institution in relation to that employer), can be acquired by an employee or director of that employer, where that equity instrument will qualify as a restricted equity instrument (as defined in section 8C) at the time of its acquisition by an employee or director, and which will be subject to the provisions of section 8C(1) upon vesting.

The proposed section 8CA(2) goes on to provide that any expenditure actually incurred and paid by an employer in respect of a restricted equity instrument scheme must be treated as expenditure incurred evenly over the longest period during which an equity instrument can qualify as a restricted equity instrument in terms of the relevant scheme. Unless it is treasury’s intention that this reference is limited to issued equity instruments only, this proposed amendment may have a significant impact on schemes that are to operate for long periods of time. The amendment does not cross refer to the existing ‘timing’ provision in section 23H of the Act.

Section 8CA(3) also permits a deduction for an employer in respect of much of the expenditure it has actually incurred and paid in respect of that scheme, as is treated as having been incurred in terms of section 8CA(2) during the relevant year of assessment. It is currently unclear whether this proposed amendment is intended to permit a deduction in respect of amounts paid by employers as dividends and redemption proceeds, in addition to the amounts incurred by employers to facilitate the acquisition of instruments in terms of the scheme.

This insertion is also proposed to come into operation on 1 March 2017 and, if section 8CA is introduced as proposed, it will apply in respect of any amount that is paid, or becomes payable by the relevant employer, on or after that date.

In addition to the above, the Draft Tax Administration Laws Amendment Bill of 2016 (the ‘2016 TALAB’) proposes that the definition of ‘remuneration’ be updated to include the amount of any dividend received or accrued:
in respect of a restricted equity instrument as defined in section 8C to the extent contemplated in paragraph (dd) of the proviso to section 10(1)(k)(i) of the Act; and

to a person in respect of services rendered or to be rendered, or in respect of/by virtue of employment or the holding of any office contemplated in paragraph (ii) of the proviso to section 10(1)(k)(i) of the Act.

As such, employees’ tax will be required to be withheld in respect of these amounts as well.

Lastly, the 2016 TLAB proposes that paragraph (c) of the definition of ‘gross income’ contained in section 1 of the Act be amended to exclude amounts referred to in sections 8B and 8C. It is anticipated that this welcome change will come into operation on 1 March 2017, and apply in respect of years of assessment ending on or after that date.

It follows that, if the abovementioned proposals are implemented in their present form, taxpayers should carefully re-evaluate their tax position in relation to any amounts, including dividends, received or accrued to them in respect of instruments that are subject to the provisions of section 8C of the Act. Employers should also carefully consider their employees’ tax withholding obligations, as well as the timing and amount of deductions to which they may be entitled in respect of expenditure incurred by them in connection with their employee incentive arrangements.

It may even be prudent for the structure of their existing employee incentive arrangements to be re-considered to ensure that these continue to meet the commercial purposes for which they were established, without resulting in an unnecessarily complex position for the various parties concerned.
TAX NEWS

MIXING PULP DOES NOT MAKE IT A FICTION – FARMERS NEED TO ACCOUNT FOR ‘WORK IN PROGRESS’ ON THEIR TAX RETURNS

Esther van Schalkwyk, Senior Tax Consultant, BDO SA

A wine farmer recently discovered that ‘produce held and not disposed of’ includes the pulp of grapes that were harvested and delivered to a wine co-operative, where it was mixed with the pulp of other members. The farmer had retained an undivided share in the pooled pulp held by the co-operative which was to be sold as wine on behalf of its members.

The farmer under discussion was the appellant in Avenant vs SARS, in which the Supreme Court of Appeal (SCA) handed down judgement on 1 June 2016 in favour of SARS. When submitting their annual income tax returns, farmers are required to include in their income the value of all livestock or produce held and not disposed of at the beginning and end of each year of assessment. Where traders are allowed to deduct the cost of purchasing trading stock, they are also required to include the value of closing stock held and not disposed of at the end of the year of assessment in calculating their taxable income. It is now settled law that trading stock also includes partly manufactured goods or so-called ‘work-in-progress’ which need not be in a saleable form.

In the case of Avenant vs SARS, the SCA held that the meaning attributed to ‘livestock and produce held and not disposed of’ should accord with the meaning attributed to ‘trading stock held and not disposed of’ in terms of the ordinary rules of the Income Tax Act relating to trading stock. Farmers should therefore also be mindful of including work-in-progress (which does not need to be in a saleable form) as part of their produce held and not disposed of at the beginning and end of each year of assessment.

Avenant had delivered all of his harvested grapes to a wine co-operative as at the end of his 2009 year of assessment. At year-end the harvested grapes had already been pressed into pulp and were mixed with the pulp of other members of the co-operative. The cooperative was responsible for making, packaging, marketing and selling the wine. Each farmer who contributed to the pool would share in the net proceeds of the sale of the wine, pro rata to that farmer’s contribution and after the co-operative had deducted its expenditure. The co-operative did not hold the pulp on its own behalf but rather on behalf of its members who retained joint ownership, each in an undivided share of the pooled pulp and later of the pooled wine, pro rata to their contributions of grapes.

The SCA held that the processing of the grapes by being pressed into a pulp and starting the natural fermentation process (even if chemicals had been added) did not transform the grapes into something essentially different from the produce of the harvest. Avenant’s main argument before the SCA was that the pulp which he had delivered to the co-operative did not constitute ‘produce held and not disposed of’ by him at the end of the year of assessment. The SCA however agreed with SARS that where a trader retains ownership of produce without necessarily retaining possession, that produce is considered to be held and not disposed of for purposes of calculating the farmer’s taxable income.

Although the pulp did not have a market value, SARS is allowed to fix any fair and reasonable value on produce to be included in a farmer’s return. The SCA reiterated that the difficulty (whether perceived or real) in determining a value for work-in-progress does not permit a court to deviate from the plain language of the Income Tax Act. The SCA was satisfied that the distilling wine price would place a fair and reasonable value on Avenant’s closing stock because the distilling wine price had an ascertainable value and favoured the taxpayer as most wines would fetch a higher price than distilling wine.

There are a few important points to take from this judgement. Farmers should be mindful to include in their taxable income their work-in-progress as ‘produce held and not disposed of’ at the end of each tax year - work-in-progress need not be in a saleable form. SARS may fix any fair and reasonable value for ‘produce held and not disposed of’ (which need not be market value). Even though a farmer may have given up possession and mixed his produce with other produce not owned by him, he will still be required to account for his pro-rata share of the produce as closing stock if he retains ownership of the produce.
It is common practice for suppliers to deliver the goods that they supply at the premises of their customers on the customer’s request. The suppliers then either deliver the goods themselves or they contract the services of third parties to deliver the goods on their behalf, for which they charge a delivery fee.

The question that arises is whether the supplier should charge value-added tax (“VAT”) on the delivery fee, particularly where the supplier acquires the services of a third party to deliver the goods, and merely recovers the delivery fee from the customer charged by the third party.

The tax court recently considered the VAT status of delivery fees charged by a taxpayer that carries on a fast foods delivery business. The taxpayer contracts with fast food outlets to advertise their menus in a booklet, which it then distributes to households in the area in which the taxpayer operates. Customers order fast foods from the taxpayer by placing a telephonic order. The taxpayer in turn places the order with the relevant fast food outlet, dispatches a driver to the outlet to collect and pay for the food, and to deliver the food to the customer.

The taxpayer charges a fixed percentage of the price of the food purchased by customers as a commission to the fast food outlet, on which it levies and accounts for VAT. The taxpayer charges the price of the food to the customer without any mark-up, and also includes a delivery charge on the tax invoice issued to the customer, which it describes as ‘driver’s petrol money’. The driver, who is required to wear the branded clothing of the taxpayer and to carry hotboxes branded with the taxpayer’s logo, is entitled to retain the ‘driver’s petrol money’ collected from the customer. The issue under
The dispute was whether the ‘driver’s petrol money’ is subject to VAT in the hands of the taxpayer.

In the recent matter, the taxpayer contended that the drivers who collected and delivered the fast food were independent contractors and were not its employees, and that the collection and delivery of the food was not a supply made by the taxpayer. The taxpayer argued that the only service that it supplies is receiving the phone call, placing the order with the outlet and communicating the order to the independent drivers who then collect and deliver the food. It further contended that its only clients are the food outlets from whom it receives a commission, and the callers who placed the orders were not its clients. The ‘river’s petrol money’ was paid to the driver directly, and to the extent that the taxpayer collected the petrol money (for example where the customer paid electronically), the taxpayer argued that it did so as agent on behalf of the driver.

The tax court had to consider whether the ‘driver’s petrol money’ comprised consideration for VAT purposes for any supply made by the taxpayer to its customers, i.e. whether it was a payment made in respect of, in response to, or for the inducement of the supply of any goods or services by the taxpayer.

The tax court considered certain United Kingdom authorities on the issue, and took a pragmatic view based on these authorities in analysing the VAT implications. The tax court disregarded a provision in the driver’s contract that the taxpayer does not remunerate the driver for the delivery of the food because the client pays the delivery fee directly to the driver, as it considered this provision to be contrary to the facts. The facts indicated that the taxpayer outsources its delivery services to the drivers.

By using sub-contracted drivers for which it charges a fee to the customers. It is further irrelevant that the delivery fees did not generate any profit for the taxpayer.

The tax court also considered the economic reality of the taxpayer’s business, which required it to collect the food from the fast food outlets and to deliver it to the customers. Without the delivery service component, the taxpayer’s business cannot function. The drivers wear the branded clothing of the taxpayer and present themselves to the customers as if they are an integral part of the taxpayer’s business. The taxpayer is further only able to generate the commission income from the fast food outlets because it also offers the delivery service, even if the service is characterised as arranging the delivery of the food, rather than an actual delivery service.

Based on this analysis, the tax court held that the ‘driver’s petrol money’ is a payment made by the customer in respect of, or, in response to the service provided by the taxpayer, whether that service comprises the actual supply or the arranging of the supply of the delivery service. The driver’s right to retain the payments received is in terms of their contract with the taxpayer, and not in terms of any agreement with the customer. The ‘driver’s petrol money’ was therefore held to be subject to VAT in the hands of the taxpayer.

The judgment of the tax court provides valuable guidance as to whether any amount charged to a customer, including delivery fees, comprises consideration for a service supplied to the customer which attracts VAT. Delivery fees and similar charges are often considered to be merely a non-taxable reimbursement of costs incurred on behalf of the customer, and their VAT status should be reviewed in view of this judgment. In determining whether such charges are subject to VAT, it is not sufficient to rely only on the agreements between the parties, but the facts and the commercial and economic reality of the taxpayer’s business should also be considered.
The South African Revenue Service (SARS) has released the long-awaited update to its draft notice in terms of section 29 of the Tax Administration Act, 2011 (TA Act). The draft notice outlines key record keeping requirements for transfer pricing transactions. This is the first time that a South African taxpayer will be required to pay attention to a section which outlines what information and records need to be kept. No doubt, there will certainly be an increase in overall compliance costs for taxpayers to consider.

SARS has been very clear that the final draft notice’s purpose is to create a base of information to be retained that will enable the taxpayer to have all the necessary information in place to be able to form an opinion or analysis on whether the cross border related party transaction (potentially affected transactions) can be supported by the arm’s length principle, as required by section 31 of the Income Tax Act no. 58 of 1962 (Income Tax Act).

In future, if taxpayers do not have this information on hand, they will be contravening the TA Act and a non-compliance penalty could be applicable. The non-compliance penalty would be in addition to any primary and secondary transfer pricing adjustments and related penalties and interest for those adjustments.

There are important updates and changes in the amended draft notice. Most important is the amendment which makes the new requirement applicable to a broader scope of taxpayers. While the previous draft notice was only relevant for a taxpayer with a group consolidated South African turnover of R1 billion or more, the new notice requires a much wider spectrum of taxpayers to heed the Transfer Pricing legislation.

In terms of the updated draft notice, it appears that the R1 billion threshold has been seen to be
too burdensome on taxpayers that may not have material related party transactions.

This threshold has been changed and the amended draft notice’s threshold reads as follows:

“A person must keep the records specified in paragraph 3 and 4 if the person –
(a) has entered into a potentially affected transaction; and
(b) the aggregate of the person’s potentially affected transactions for the year of assessment exceeds or is reasonably expected to exceed the higher of –
(i) 5 per cent of the person’s gross income; or
(ii) R50 million.”

The above amendments mean that it will be far more likely for more taxpayers to fall within the new requirement. For example, where a taxpayer has less than R1 billion turnover but potentially affected transactions of over R50 million, this taxpayer will have to meet the requirements as per the amended draft notice.

Paragraphs 3 and 4 which are referred to in the definition above, and which are part of the amended draft notice, provide a list of the information required. Paragraph 3 refers to questions which assist in detailing the overall information about the taxpayer, while Paragraph 4 is only applicable to potentially affected transactions which exceed, or are reasonably expected to exceed R1 million. The Tax Advisory team assumes that this is SARS’ definition referred to above of “material in relation to potentially affected transactions”.

It is important to note, however, that where a transaction falls below R1 million, it would not require information as per that which is set out in section 4, but the transaction would still need to be considered according to “arm’s length” as per section 5 of the notice.

SARS’ draft notice has been published for a final round of public comment which must be submitted on or before 19 August 2016. Grant Thornton’s Transfer Pricing team believes that the majority of comments are expected to focus on the new threshold as this will require many more taxpayers to comply with the amendment and the requirement of how long this documentation must be kept.

It is concerning that the thresholds seem particularly lower than those outlined previously and these new requirements are more than likely going to increase compliance costs for smaller taxpayers. While the R1 billion threshold previously was elected so that small to medium businesses were less affected by the thresholds, the lower thresholds are certainly going to cause greater regulation and red tape for SMEs.

The Grant Thornton Transfer Pricing team believes that the new Transfer Pricing requirements are South Africa’s legislative way of aligning itself to international standards. To date, South Africa has been very lenient when it comes to compulsory transfer pricing documentation retention requirements, yet many countries worldwide, and African countries such as Tanzania, Kenya or Ghana, have already implemented compulsory transfer pricing documentation requirements.

In many ways, SARS is formalising an approach which has been informally in place already. Taxpayers should already have considered the questions under paragraphs 3 and 4 as it is a requirement of section 31 of the Income Tax Act to discharge the onus of being at arm’s length.

It is vital for taxpayers to work closely with skilled advisors in terms of the new requirements because SARS has expressly highlighted that this is a documentation retention requirement and therefore is wider than just a Transfer Pricing document. It will be imperative for multinational companies to work closely with their tax teams to make sure everything is in order, that all elements are documented accordingly and that the right information is in place.

“To date, South Africa has been very lenient when it comes to compulsory transfer pricing documentation retention requirements, yet many countries worldwide, and African countries such as Tanzania, Kenya or Ghana, have already implemented compulsory transfer pricing documentation requirements.”
Tax payable by South Africans working abroad is impacted by whether they will remain tax resident of South Africa. A natural person is a ‘resident’ if he or she is either ordinarily resident in the Republic or meets the physical presence test. South African tax residents are taxed on worldwide income in South Africa. A non-resident is subject to tax in South Africa on income from a South African source.

A number of exemptions and deductions may apply to income earned whilst outside South Africa. This article focuses on the exemption relating to foreign employment income (section 10(1)(o)(ii) of the Income Tax Act) earned outside of South Africa. This exemption applies to services rendered outside South Africa for or on behalf of an employer, for an individual who is outside of South Africa for a period/periods exceeding 183 days (calendar days) in aggregate, during any 12-month period starting or ending during a tax year. The exemption only applies if the 183-day period includes a 60-day continuous period of absence from South Africa.

SARS recently issued Draft Interpretation Note 16 (Issue 2) (DIN16) for comment. When compared with the current version of Interpretation Note 16 (IN16), the DIN16 contains a shift in certain aspects of the tax exemption on foreign employment income. In calculating the 183/60 day periods, the DIN16 applies SARS’s previous practice (IN16) and takes into account weekends, public holidays, annual leave days, sick leave days and rest periods spent outside South Africa to determine the exemption. IN16 contains practical examples of the ‘183/60 day approach’ and, based on practice, the determination of the exemption is relatively straightforward. A number of relatively complex issues may arise and employers need to evaluate the impact on its employees that render services offshore. DIN16 highlights that a ‘common misconception is that all remuneration received or accrued during the qualifying 12-month period of 12 months is exempt’ and that only ‘the remuneration received or accrued in respect of services rendered outside the Republic during the qualifying period of 12 months is exempt’. SARS’s view is derived from the wording itself.

Essentially, DIN16 relies on apportionment, which acts as a ‘second step’ to determine the exempt remuneration, if the 183/60 day tests have been met. The first test applies the 183/60 day rules, which take into account weekends, public holidays, annual leave days, sick leave days and rest periods, and the second test applies SARS’s apportionment methodology which excludes any day not regarded as a ‘work day’. A ‘work day’, for DIN16 purposes does not include weekends, public holidays or leave days. Only days of actual services rendered are taken into account. In determining the tax exempt portion, the following apportionment formula should be used for DIN16 purposes:

\[
\text{Exempt portion} = \frac{\text{Work days outside South Africa}}{\text{Total work days for period: 1}} \times \text{Remuneration received during period}
\]

SARS also deals with the common scenario in terms of which employees are required to take rest periods, enforced by the home or host country’s health and safety regulations and states that no ‘actual services are rendered during the rest periods, even though the employees remain in continuous employment during these periods. The services that are rendered to earn the remuneration are the services that are rendered during the work shifts’. SARS is of the view that if ‘those services are rendered offshore and during a qualifying period, all remuneration attributable to those offshore services will qualify for exemption and no apportionment must be done’. This approach is uncertain as it may be that the 183/60 day rules are complied with, but it is not clear whether compulsory health and safety rest periods (which are not annual leave) are then regarded as ‘work days’ outside South Africa. What if those compulsory rest periods are spent in South Africa – does it affect the ‘work day’ driver in the apportionment approach? Practical examples in the final version of the DIN will assist.

In conclusion, it must be remembered that the burden of proof is on the taxpayer to show that an amount is exempt. Employers and individuals rendering services offshore need to take account of SARS’s contemplated approach under the DIN and ensure compliance with the Act.
On July 20 2016, the National Treasury announced its proposed changes to the Special Voluntary Disclosure Programme (SVDP) in respect of offshore assets and income. The proposed changes are an attempt to simplify the process of giving non-compliant taxpayers the opportunity to voluntarily disclose offshore assets and income before the new global standard for automatic exchange of information between tax authorities begins in 2017.

The proposed changes include:

- Instead of calculating two different amounts (i.e. seed capital and investment returns) for inclusion in the taxpayer’s taxable income, only one amount now needs to be calculated. This amount equals 50% of the highest value of the aggregate of all assets situated outside SA between 1 March 2010 and 28 February 2015 that were derived from undeclared income, which will be included in taxable income and subject to tax in SA.
- The above value is the market value determined in the relevant foreign currency translated into rands at the spot rate at the end of the tax period in which the highest value fell.
- The undeclared income that originally gave rise to the abovementioned assets will be exempt from income tax, donations tax and estate duty liabilities arising in the past. That being said, however, future income will be fully taxed and assets declared will remain liable for donations tax and estate duty in the future, should the applicant donate these assets or pass away while still holding them.
- Taxpayers who disposed of any foreign held assets prior to 1 March 2010 may also apply for relief under the SVDP in terms of special deeming provisions.
- Any noncompliance in terms of Value Added Tax, employees’ tax (PAYE), unemployment insurance fund (UIF) contributions and skills development levies (SDL) will not qualify for the SVDP. However, relief for penalties associated with this non-compliance will continue under the existing voluntary disclosure programme in terms of the Tax Administration Act, 2011.

These proposed changes are in line with the new OECD-led Base Erosion and Profit Shifting (BEPS) project and Common Reporting Standards aimed at uncovering non-compliant tax practices.

Prior disclosure programmes in SA, namely those in 2003 and 2010 jointly recovered over R9 billion in taxes from undisclosed foreign assets held by South African citizens.
5 TRUE STORIES OF TOTALLY WEIRD TAX DEDUCTIONS

Tax season is almost upon us, which means someone; somewhere is asking the age-old question: Can I write off my cat food? (The answer: You can’t unless it’s a business expense). What you can do, however, is read this excellent roundup of weird tax deductions, guaranteed to get you jazzed about filling out that tax return. And if you aren’t ready for tax season, what are you waiting for?

1. Bar Mitzvah networking
“I’ve seen my fair share of weddings, bar and bat mitzvahs and other large parties that were ‘100% business deductions,’” says Howard Rosen, a certified public accountant and tax attorney based in St. Louis. “When I asked for the invite list and the business relationship of each person on it, most of the deduction disappeared.” No wonder: If you’re inviting customers, bankers, attorneys and so on, you may be able to deduct the direct costs associated with those people. If it’s your Aunt Martha, 12 cousins on your mom’s side and your sorority sisters, you may be out of luck.

2. Bruno the Guard Dog
“I’ve seen my fair share of weddings, bar and bat mitzvahs and other large parties that were ‘100% business deductions,’” says Howard Rosen, a certified public accountant and tax attorney based in St. Louis. “When I asked for the invite list and the business relationship of each person on it, most of the deduction disappeared.” No wonder: If you’re inviting customers, bankers, attorneys and so on, you may be able to deduct the direct costs associated with those people. If it’s your Aunt Martha, 12 cousins on your mom’s side and your sorority sisters, you may be out of luck.

3. The Paleo Deduction
“Last tax season, a client wanted to deduct the cost of their family eating non-processed foods as a medical expense,” according to John Kane, a CPA with the Cook Martin firm in Salt Lake City. “Their argument was that their diet — gluten-free, vegan, paleo — was expensive. There was no diagnosed medical condition, the taxpayer simply felt that they were able to think more clearly as a result of their ‘clean eating.’ This, unfortunately, is not deductible.”

4. Deductions by Way of Fiji
“Another client insisted his trips abroad were to find buyers for his products,” says Rosen. “What were his products, you ask? He was a residential real estate developer and he had never done any business outside his immediate area. I asked him to document any sales calls, banking relationships, potential buyers or other developers he had talked or met with on these trips. That ended the discussion pretty quickly.”

5. The Company Man
“I had a client that operated a handyman business and he expensed and deducted everything that was put on his company credit card,” says Jared R. Callister, a CPA with Fishman, Larsen & Callister in Fresno, California. “He was adamant that all expenses were business-related. However, when I combed through the receipts and found he was trying to deduct things like toothbrushes, deodorant and even women’s lingerie, it became clear that many of his so-called business expenses were just personal non-deductible purchases.”

Source: www.time.com
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