MONTHLY TAX UPDATE

LATEST DEVELOPMENTS IN TAX LAW – JANUARY 2020

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The Tax Faculty

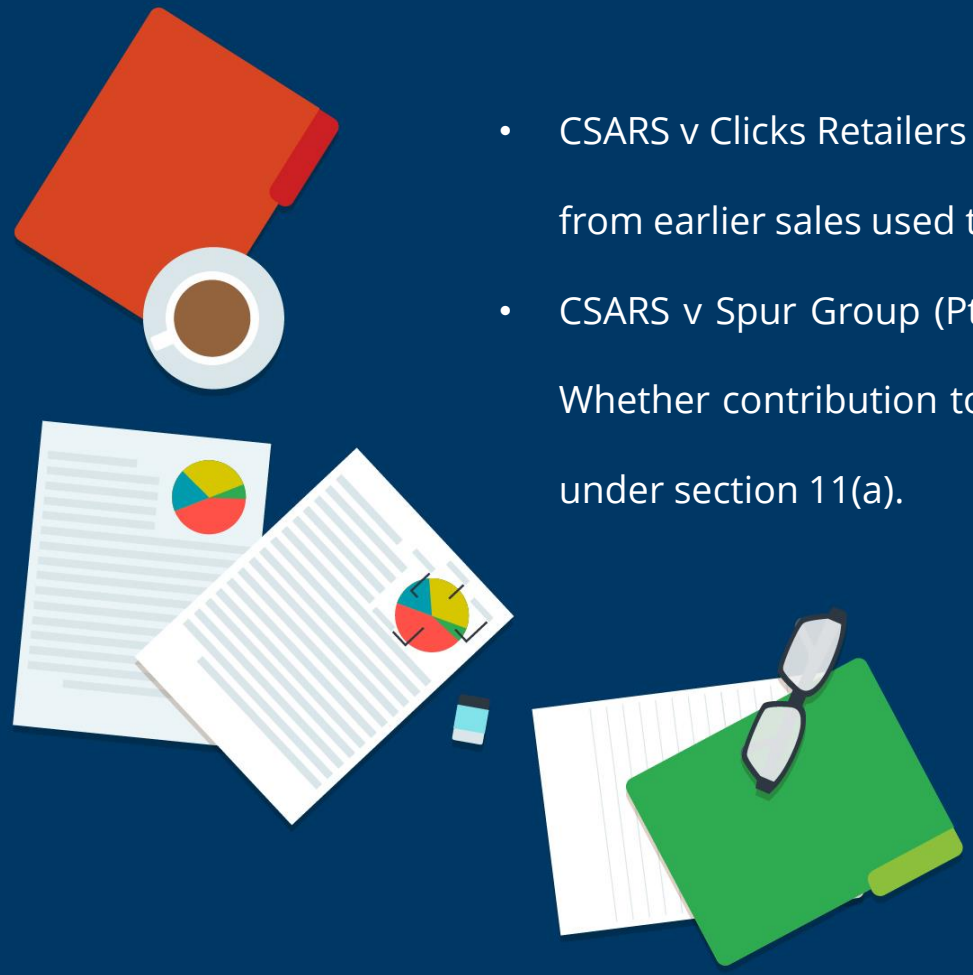
OUTLINE

- Monthly tax update (Income tax, VAT and TAA – excluding customs).
- 21 January 2020 – 25 February 2020.
- https://www.unicustax.co.za/monthly-tax-update-signup/
- Cannot cover everything in detail.
- Relevance of topics.
- Missed anything?

OVERVIEW

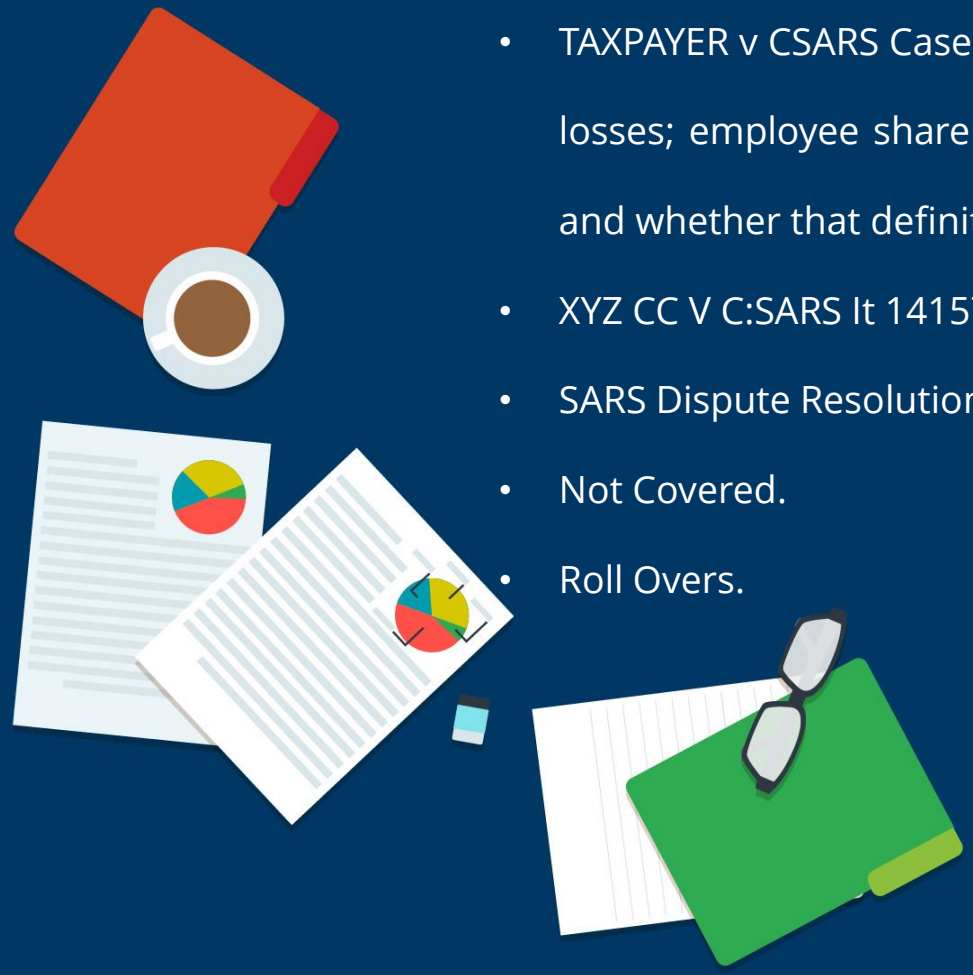
- Tax News Flash.
- General Developments.
- Practical issues (email me).
- Africa Cash & Carry (Pty) Ltd v CSARS (783/18) [2019] ZASCA 148 (21 November 2019) - Whether SARS proved that the methods of assessment used were reasonable; whether the tax court ought to have remitted the assessment; section 89quat interest.

OVERVIEW



- CSARS v Clicks Retailers (Pty) Ltd (58/2019) [2019] ZASCA 187 (3 December 2019) - Whether amount received from earlier sales used to finance future expenditure on same contract.
- CSARS v Spur Group (Pty) Ltd (A285/2019; A285/2018) ZAWCHC (26 November 2019; 12 November 2019) - Whether contribution to employee share incentive trust in the production of income and hence deductible under section 11(a).

OVERVIEW



- TAXPAYER v CSARS Case numbers: 13798; 13931 & 14294 (17 September 2019) Capital gains tax and capital losses; employee share incentive scheme and trust; meaning of "asset" as defined in the Eighth Schedule and whether that definition includes a personal right.
- XYZ CC V C:SARS It 14157
- SARS Dispute Resolution & Judgments 2019 – 2013.
- Not Covered.
- Roll Overs.

Tax News Flash

- SARS CUSTOMS DESTROYS ILLEGALLY IMPORTED GOODS VALUED AT OVER R7-MILLION
  - "Over 13 000 bales of illegally imported clothing, valued at R6,75-million, as well as 15 vehicles, valued at a total of R450 000.00, will be destroyed."
    - 29 November 2019
- Expat tax: Countdown to implementation kicks off
  - "It must be understood that expats' entire remuneration will be taken into account. What this means is that, if they remain tax resident, they will be taxed fully on any allowances and benefits, as if they were just a normal employee working in South Africa."
    - 07 January 2020

The Tax Faculty

General Developments

National Legislation

The following Amendment Acts were promulgated on 15 January 2020:

- Taxation Laws Amendment Act 34 of 2019;
- Tax Administration Laws Amendment Act 33 of 2019; and;
- Rates and Monetary Amounts and Amendment of Revenue Laws Act 32 of 2019.

General Developments

Publications

- List of qualifying physical impairment or disability expenditure – effective from 1 March 2020; and;
  - (See also the Confirmation of Diagnosis of Disability Form (ITR-DD).
- VAT 404 – Guide for vendors.
  - 12 December 2019.

Preparation of Legislation

- Draft guide to building allowances (Issue 2).
  - Due date for comments: 28 February 2020.

PRACTICAL ISSUES

Email me -
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AFRICA CASH & CARRY (PTY) LTD V CSARS

(783/18) [2019] ZASCA 148 (21 November 2019)

Issue(s)

- Powers of the Tax Court to either "*alter*" assessments under the TAA/ to remit assessments back to SARS.
- Onus on SARS to prove that its methods of assessment were reasonable.

AFRICA CASH & CARRY (PTY) LTD V CSARS

(783/18) [2019] ZASCA 148 (21 November 2019)

Background

- The taxpayer operates a “cash and carry” business which generates large amounts of cash.
- The taxpayer manipulated its financial records to reflect lower amounts received in respect of sales than what was truly the case. Sales were under-declared for the 2003 – 2009 years of assessment.
- Certain information came to SARS’ attention, on the basis of which SARS launched investigations into the taxpayer’s financial affairs.

AFRICA CASH & CARRY (PTY) LTD V CSARS

(783/18) [2019] ZASCA 148 (21 November 2019)

Background

- Not all documentation was available to SARS for purposes of its investigations.
- In the premises SARS used an estimation of under-declared sales, based on the limited reliable data at its disposal, in terms of section 95 of the TAA.
- SARS applied the "*gross profit percentage methodology*" in its estimation of under-disclosed sales:
  - SARS had at its disposal "raw data" in respect of a 7-month period, which reflected a gross profit percentage of 3,6%; and
  - SARS applied this percentage in order to estimate the under-declared sales for the 2003 – 2009 years of assessment.

AFRICA CASH & CARRY (PTY) LTD V CSARS

(783/18) [2019] ZASCA 148 (21 November 2019)

Background

- SARS issued a letter of its preliminary audit findings based on this methodology, followed by a Letter of Findings and the issuance of estimated assessments.
- The taxpayer objected to the assessments, which objection was disallowed.
- It later appeared that SARS' calculations had been incorrect and that a percentage of 2,04% rather than 3,6% should have been used by SARS in applying its methodology.
- The taxpayer launched an appeal to the Tax Court.

AFRICA CASH & CARRY (PTY) LTD V CSARS

(783/18) [2019] ZASCA 148 (21 November 2019)

Background

- SARS did not withdraw its assessments but communicated to the taxpayer's attorneys that the Tax Court would be asked to confirm the 2,04% reduced calculated margin as well as the reasonableness of SARS' methodology.

AFRICA CASH & CARRY (PTY) LTD V CSARS

(783/18) [2019] ZASCA 148 (21 November 2019)

Background

- The Tax Court:
  - approved of the gross profit percentage methodology used by SARS;
  - altered the estimated assessments of income tax and VAT liability under section 129(2) of the TAA;
  - reduced the liability for section 89 *quat* interest; and
  - ultimately dismissed the taxpayer's appeal.

AFRICA CASH & CARRY (PTY) LTD V CSARS

(783/18) [2019] ZASCA 148 (21 November 2019)

Background

- This matter is the taxpayer's appeal against the judgment of the Tax Court, specifically in that the Tax Court:
- (a) dismissed the taxpayer's first point that SARS was bound by the assessments;
- (b) found that the assessments were reasonable;
- (c) concluded that the Tax Court had jurisdiction in terms of s 129(2)*(b)* of the Act to alter the assessments and grant the order it did; and
- (d) concluded that the section 89*quat* interest should not be remitted altogether.

AFRICA CASH & CARRY (PTY) LTD V CSARS

(783/18) [2019] ZASCA 148 (21 November 2019)

Arguments for the taxpayer

- The taxpayer argued that:
  - (1) SARS was not allowed to contend for a materially different tax liability to that reflected in its assessments, and should have issued revised assessments or there should have been a valid concession.
  - (2) the Tax Court's alteration of the assessments encroached on SARS' functions and was *ultra vires*.
  - (3) SARS has not proven the reasonableness of its assessments.
  - (4) the section 89*quat* interest should have been remitted.
- The *audi alteram partem* principle had not been adhered to by the Tax Court.

AFRICA CASH & CARRY (PTY) LTD V CSARS

(783/18) [2019] ZASCA 148 (21 November 2019)

Arguments for SARS

- SARS' stance was that:
  - SARS was not obliged to withdraw assessments;
  - it was within the Tax Court's powers to "alter" SARS' assessments – the methodology employed by SARS remained the same, even if the percentage was different;
  - the methodology used by SARS was reasonable.

AFRICA CASH & CARRY (PTY) LTD V CSARS

(783/18) [2019] ZASCA 148 (21 November 2019)

Judgment

- Was SARS bound by the assessments?
  - In terms of the definition in section 1, an "assessment" is:

    "*the determination of the amount of tax liability or refund, by was of self-assessment by the taxpayer or assessment by SARS*". (Own emphasis.)
  - The taxpayer claims that SARS did not issue additional assessments, withdraw the assessments, or make a valid concession.
  - SARS maintains that it did make a concession.
  - The question, then, is whether there was a valid concession.
  - This question need not be determined, because the assessments were already altered by the Tax Court under section 129(2).

AFRICA CASH & CARRY (PTY) LTD V CSARS

(783/18) [2019] ZASCA 148 (21 November 2019)

Judgment

- Tax Court's powers to "alter" an assessment in terms of section 192(2)(b) of the TAA
  - The change to the assessments was the result of an "obvious error".
  - The changes did not completely change the assessment so that it became "an entirely new entity".
  - Section 127(2)(b) allows the Tax Court to "alter" an assessment in these circumstances.
  - The Tax Court must remit the matter to SARS only if the change in the assessment is such as to necessitate further investigation by SARS/ to require further evidence, and is not due to an obvious error.

AFRICA CASH & CARRY (PTY) LTD V CSARS

(783/18) [2019] ZASCA 148 (21 November 2019)

Judgment

- The reasonableness of SARS' "gross profit percentage" methodology
  - In order for SARS to discharge the onus of proof that its methods were "reasonable", SARS must show that its decision was "a rational decision taken lawfully and directed to a proper purpose":

    Bel Porto School Governing Body & Others v Premier, Western Cape & Another [2002] ZACC 2; 2002 (3) SA 265 (CC).
  - SARS must strike a balance based on the facts and context of the matter:

    Bato Star Fishing (Pty) Ltd v Minister of Environmental Affairs and Tourism & Others [2004] ZACC 15; 2004 (4) SA 490 (CC).
  - In this case SARS' methodology was shown to be reasonable and there was no reason for the Court to interfere with it.

AFRICA CASH & CARRY (PTY) LTD V CSARS

(783/18) [2019] ZASCA 148 (21 November 2019)

Judgment

- Section 89*quat* interest
  - The Tax Court altered the section 89quat interest to be in line with the amended quantum of the tax levied.
  - There is no basis on which to criticize the Tax Court's approach in this regard.

AFRICA CASH & CARRY (PTY) LTD V CSARS

(783/18) [2019] ZASCA 148 (21 November 2019)

Judgment

- In the result:
  - there is no basis for the Court to interfere with the order of the Tax Court.
  - the appeal involved complex issues – costs including the costs of two counsel should be allowed.

AFRICA CASH & CARRY (PTY) LTD V CSARS

(783/18) [2019] ZASCA 148 (21 November 2019)

Judgment

- The court ordered that:
  - The taxpayer's appeal is dismissed with costs, including the costs of two counsel.

AFRICA CASH & CARRY (PTY) LTD V CSARS (783/18) [2019] ZASCA 148 (21 NOVEMBER 2019)

Whether SARS could prove that its methods of assessment used were reasonable; whether Tax Court should have remitted the assessment & s 89quat interest

Relevance/ comments

- The Tax Court has the power to alter SARS' additional assessments:
  - If the change was due to an "obvious error".
  - If there is still need for further examination and investigation, the matter should be referred back to SARS.

CSARS V CLICKS RETAILERS (PTY) LTD

(58/2019) [2019] ZASCA 187 (3 December 2019)

Issue(s)

- Whether amounts received from earlier sales, used to finance future expenditure are on the same contract for purposes of section 24C of the ITA.

CSARS V CLICKS RETAILERS (PTY) LTD

(58/2019) [2019] ZASCA 187 (3 December 2019)

Background

- The taxpayer owns and operates the Clicks retail business.
- The taxpayer instituted a loyalty programme for which customers can subscribe.
- The customer can the earn loyalty points when using their ClubCard to make purchases.
- The loyalty points can later be redeemed in full or partial payment i.r.o. future purchases (the goods are effectively acquired at a discount).

CSARS V CLICKS RETAILERS (PTY) LTD

(58/2019) [2019] ZASCA 187 (3 December 2019)

Background

- Clicks claimed an allowance in terms of section 24C of the ITA, for the 2009 year of assessment.
- The allowance was calculated on the basis of the cost of sales to the taxpayer in honouring vouchers that customers were expected to redeem during the next year.
- The section 24C claim was disallowed and the dispute was eventually heard by the Tax Court.

CSARS V CLICKS RETAILERS (PTY) LTD

(58/2019) [2019] ZASCA 187 (3 December 2019)

Background

- The Tax Court ruled in the taxpayer's favour on the basis that:
  - (a) it was artificial and factually incorrect to regard the expenditure that the taxpayer would incur when a customer redeemed a voucher, as arising under a "different contract" to the 1st purchase and sale;
  - (b) the 1st purchase and sale agreement incorporated the terms of the ClubCard agreement, but despite this the 1st purchase and sale remains the contract that triggers both the earning of income by the taxpayer and the obligation by the taxpayer to incur future expenditure;
  - (c) the obligation to incur future expenditure was incurred under the same contract from which the income was earned, and the taxpayer qualified for the 24C claim.
- This is SARS' appeal against the Tax Court's decision.

CSARS V CLICKS RETAILERS (PTY) LTD

(58/2019) [2019] ZASCA 187 (3 December 2019)

Arguments for SARS

- SARS argued that it had correctly disallowed the deduction:
  - the 1st purchase and sale agreement was separate from the ClubCard agreement;
  - the ClubCard agreement itself did not give rise to any income in the taxpayer's hands because it was issued free of charge;
  - the taxpayer's obligation to award points arose under the ClubCard agreement; and
  - the taxpayer was likely to incur future expenditure when vouchers are redeemed, at no cost to the customer – this obligation formed part of the ClubCard contract and not the 1st purchase and sale (in terms of which income was received).

CSARS V CLICKS RETAILERS (PTY) LTD

(58/2019) [2019] ZASCA 187 (3 December 2019)

Arguments for the taxpayer

- The taxpayer argued that:
  - the ClubCard agreement did not give rise to an obligation on the taxpayer to issue rewards;
  - the taxpayer's obligation only arose with the 1st purchase and sale;
  - qualifying purchases by the customer not only brought into existence, but determined the extent of, the taxpayer's obligations;
  - as a result, each time the taxpayer issued rewards, there was "a direct and immediate connection" between the obligation and the qualifying purchase – this meant that every qualifying purchase was income-earning and obligation-imposing;
  - the "same contract" requirement was therefore met.

CSARS V CLICKS RETAILERS (PTY) LTD

(58/2019) [2019] ZASCA 187 (3 December 2019)

Judgment

- The Court held that:
  - the ClubCard contract created rights for the customer as well as obligations on the taxpayer.
  - the idea that the 1st purchase and sale is so inextricably linked to the ClubCard agreement that the two form part of the same contract is problematic:
    - *CSARS v Big G Restaurants (Pty) Ltd* (157/18) [2018] ZASCA 179 (03 December 2018): rejected the idea that two "inextricably linked" agreements can be part of the same contract for purposes of section 24C.
  - the right to income by the taxpayer is only created by the 1st purchase and sale agreement; the obligation to issue rewards vouchers is imposed by the ClubCard agreement.
  - to view the contracts as one and the same ignores the reality of the situation.
  - the appeal is therefore upheld with costs.

CSARS V CLICKS RETAILERS (PTY) LTD

(58/2019) [2019] ZASCA 187 (3 December 2019)

Judgment

- The Court ordered that:
  - SARS' appeal is upheld with costs including costs of two counsel.
  - The order of the Tax Court is set aside and replaced with the following:

  "The appeal is dismissed."

CSARS V CLICKS RETAILERS (PTY) LTD

(58/2019) [2019] ZASCA 187 (3 December 2019)

Relevance/ comments

- It is confirmed that two “inextricably linked” agreements are not one and the same agreement for purposes of section 24C.

C:SARS V SPUR GROUP (PTY) LTD

(A285/2019; A285/2018 ZAWCHC (26 November 2019; 12 November 2019)

Issue

- Whether contributions made by an employer to an employee share incentive trust are made "*in the production of income*" (section 11(a) of the Income Tax Act 58 of 1962 ("the ITA")).

C:SARS V SPUR GROUP (PTY) LTD

(A285/2019; A285/2018 ZAWCHC (26 November 2019; 12 November 2019)

Background

- During 2004, the Spur Group of Companies decided to implement a Share Incentive Scheme (“the Scheme”) for qualifying employees (“participants”).

C:SARS V SPUR GROUP (PTY) LTD

(A285/2019; A285/2018 ZAWCHC (26 November 2019; 12 November 2019)

Background

- The Scheme was set up as follows:
  - the Spur Management Share Trust ("the Trust") was established with Spur HoldCo as beneficiary;
  - the Trust acquired a shelf company, NewCo;
  - participants were offered ordinary shares in NewCo in proportions determined by Spur HoldCo; and
  - participants were not entitled to deal with the shares within the first 7 year from date of purchase; otherwise the shares would be forfeited.

C:SARS V SPUR GROUP (PTY) LTD

(A285/2019; A285/2018 ZAWCHC (26 November 2019; 12 November 2019)

Background

- Spur Group made a contribution of ± R48 million to the Trust (of which Spur HoldCo was the beneficiary).
- The ± R48 million contribution was to be used by the Trust in order to obtain shares in NewCo.
- NewCo in turn, used the proceeds of the contribution to obtain shares in Spur HoldCo.

C:SARS V SPUR GROUP (PTY) LTD

(A285/2019; A285/2018 ZAWCHC (26 November 2019; 12 November 2019)

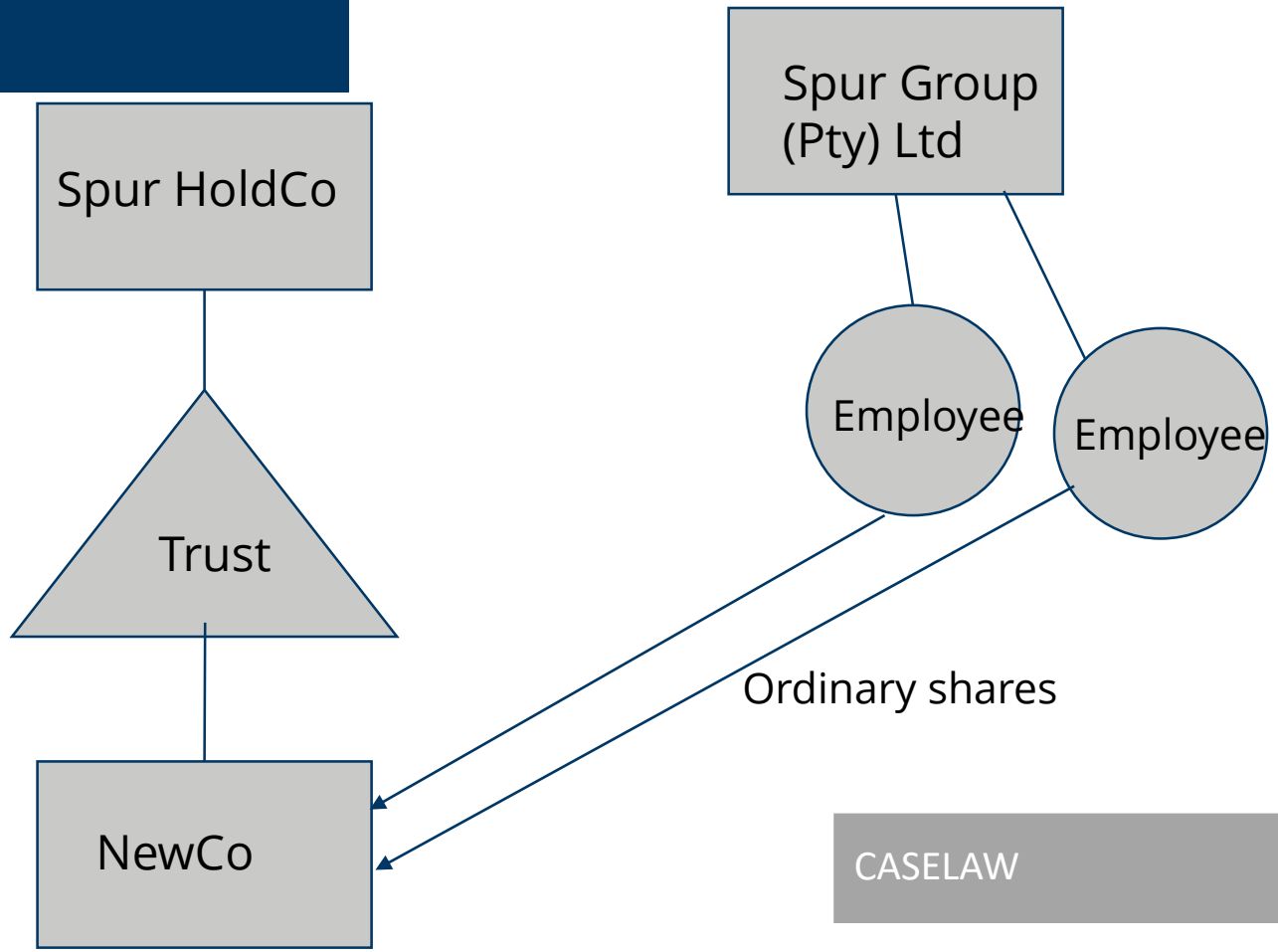
Background

- The Scheme terminated early during 2010.
- NewCo was deregistered and participants became beneficiaries of the Trust – only to extent of the dividends.
- Spur Group's ± R48 million contribution was not repaid to it, but instead vested in Spur HoldCo.
- Dividends were paid to participants in accordance with the Scheme.

C:SARS V SPUR GROUP (PTY) LTD

(A285/2019; A285/2018 ZAWCHC (26 November 2019; 12 November 2019)

Background



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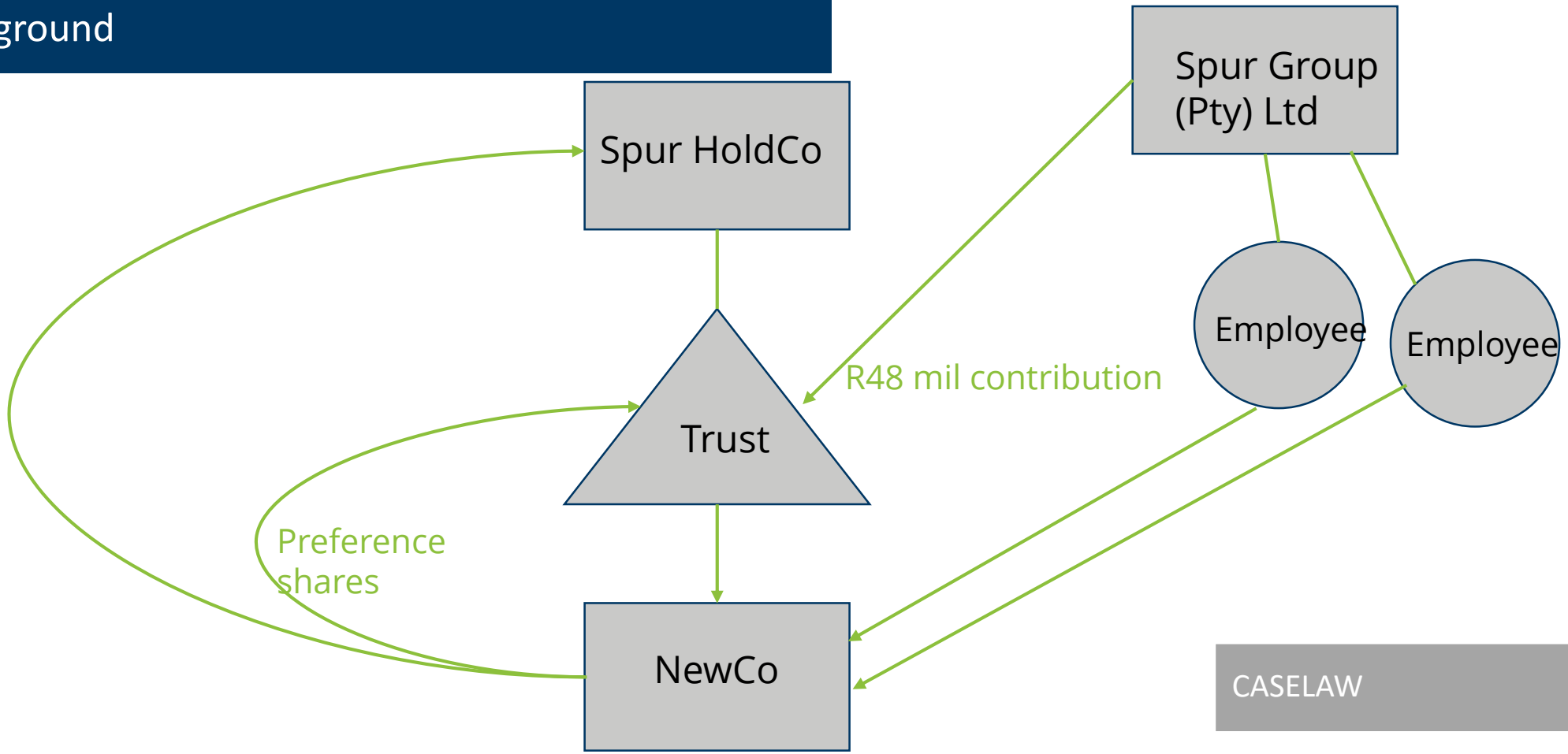
(A285/2019; A285/2018 ZAWCHC (26 November 2019; 12 November 2019)

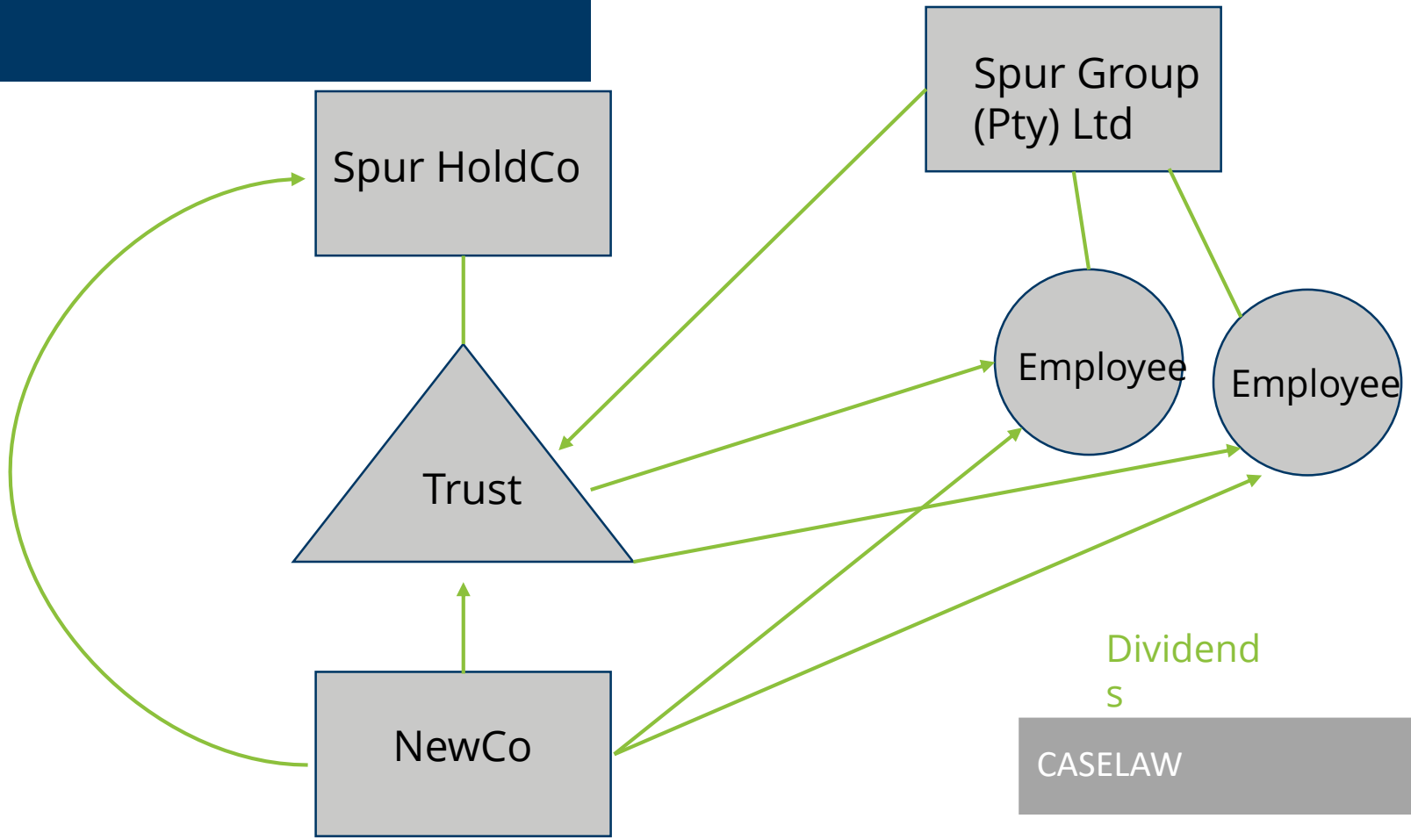
Background



C:SARS V SPUR GROUP (PTY) LTD

(A285/2019; A285/2018 ZAWCHC (26 November 2019; 12 November 2019)

Background



C:SARS V SPUR GROUP (PTY) LTD

(A285/2019; A285/2018 ZAWCHC (26 November 2019; 12 November 2019)

Background

- Spur Group then proceeded to claim the ± R48 million contribution as a deduction against its taxable income in terms of section 11(a) of the ITA, during each of the 2005 – 2012 years of assessment.
- These deductions were disallowed by SARS.
- The matter was heard by the Western Cape Tax Court, and decided in Spur Group's favour.
- This is an appeal against the judgment of the court a quo.

C:SARS V SPUR GROUP (PTY) LTD

(A285/2019; A285/2018 ZAWCHC (26 November 2019; 12 November 2019)

Arguments for the taxpayer

- It must be considered:
  - Why the contribution was made; and
  - Whether this purpose was achieved.
- The contribution was a *conditio sine qua non* for the existence of the Scheme and the subsequent (albeit indirect) benefit to participants.

C:SARS V SPUR GROUP (PTY) LTD

(A285/2019; A285/2018 ZAWCHC (26 November 2019; 12 November 2019)

Arguments for the taxpayer

- Participants did benefit, albeit not directly.
- The purpose of the Scheme was to incentivise staff. There is a close causal link between the contribution and the "*production of income*".

C:SARS V SPUR GROUP (PTY) LTD

(A285/2019; A285/2018 ZAWCHC (26 November 2019; 12 November 2019)

Arguments for SARS

- It was argued for SARS that:
  - If the contribution was made solely in order to incentivise participants in the Scheme, then the contribution should have been made directly to the participants (and not the Trust). (In other words, Spur Group would have to part with the contribution in favour of the participants which it did not do.)
  - There is no connection between the participants and the Trust.
  - There is, therefore, no direct causal link between the contribution and the production of income.

C:SARS V SPUR GROUP (PTY) LTD

(A285/2019; A285/2018 ZAWCHC (26 November 2019; 12 November 2019)

Arguments for SARS

- In summary, the argument for SARS was that the ± R48 million did not constitute an expense incurred in the production of income, on the basis that it was not directly given to participating employees.

⇨ SARS relied only on the "positive test" contained in section 11(a) of the ITA, and not the "negative test" in section 23(g) of the ITA.

C:SARS V SPUR GROUP (PTY) LTD

(A285/2019; A285/2018 ZAWCHC (26 November 2019; 12 November 2019)

Judgment

- It must be determined whether the contribution made in respect of the Scheme, is sufficiently closely linked to Spur Group's production of income for the 2005 – 2012 years of assessment:
  - if a direct enough causal link is not found, then prescription would become relevant in respect of the 2005 – 2009 years of assessment; and
  - if a causal link/ nexus existed, then the contribution would have been an expense incurred in the production of income.

C:SARS V SPUR GROUP (PTY) LTD

(A285/2019; A285/2018 ZAWCHC (26 November 2019; 12 November 2019)

Judgment

- Of relevance are sections 11(a) and 23(g) of the ITA, which must be read together to determine whether an amount is deductible or not.
- It must be taken into account:
  - whether there has been “expenditure” or “loss”;
  - actually incurred;
  - during the year of assessment;
  - in the production of income;
  - not capital in nature; and
  - if claimed as a deduction against income derived from trade, the amount must have been expended for purposes of trade.

C:SARS V SPUR GROUP (PTY) LTD

(A285/2019; A285/2018 ZAWCHC (26 November 2019; 12 November 2019)

Judgment

- In the production of income:
- *PE Electric Tramway* case:
  - (a) whether the act to which the expenditure is attached is performed in the production of income; and
  - (b) whether the expenditure is linked closely enough to the taxpayer's income earning operations.

C:SARS V SPUR GROUP (PTY) LTD

(A285/2019; A285/2018 ZAWCHC (26 November 2019; 12 November 2019)

Judgment

- Also:
- *CIR v Genn & Co*

C:SARS V SPUR GROUP (PTY) LTD

(A285/2019; A285/2018 ZAWCHC (26 November 2019; 12 November 2019)

Judgment

- The purpose of the expenditure was "…*to incentivise the taxpayer's key staff through a scheme which facilitated the acquisition of an indirect investment in the shares of HoldCo for scheme participants*…"

C:SARS V SPUR GROUP (PTY) LTD

(A285/2019; A285/2018 ZAWCHC (26 November 2019; 12 November 2019)

Judgment

"...it must be acknowledged that indeed the bulk of the benefit inures to the Spur Group, but that, in my view, does not detract from the actual purpose of the expenditure... As rightly found by the Tax Court, it has not been suggested in these proceedings that the Spur Group, by making the R48 million contribution was shamming or that the transaction was dressed or disguised to make it appear to be something that it was not, especially with the purpose of evading tax or avoiding a peremptory rule of law. In fact it is quire clear that maintaining a content and motivated workforce forms part of the costs of performing the income producing operations and is crucial to the Spur Group's commercial success and profitability...

C:SARS V SPUR GROUP (PTY) LTD

(A285/2019; A285/2018 ZAWCHC (26 November 2019; 12 November 2019)

Judgment

... Stated differently, the money was disbursed in order indirectly to facilitate the carrying on of the taxpayer's trade. Even if the contribution did not directly benefit the employees, the overwhelming evidence supports the fact that it incentivised and motivated the participating employees, as I have said, albeit indirectly. I also do not understand it to be a requirement that employees benefit directly from the contribution. What seems paramount, at least in my view, is the purpose of the expenditure and what it affects." (Own emphasis.)

C:SARS V SPUR GROUP (PTY) LTD

(A285/2019; A285/2018 ZAWCHC (26 November 2019; 12 November 2019)

Judgment

- The Court ruled in the taxpayer's favour.
- The appeal was dismissed with costs.

C:SARS V SPUR GROUP (PTY) LTD

(A285/2019; A285/2018 ZAWCHC (26 November 2019; 12 November 2019)

Minority judgment

- In a minority judgment, Salie-Hlope J states that:
  - The idea was always that the contribution would return to the Spur family.
  - The control exercised by Spur HoldCo over the Trust is of significance.
- It is stated that: “”
- *The share scheme was designed in such a manner that Spur HoldCo would be the ultimate recipient of the investment in the NewCo preference shares resulting from Spur’s contribution. The participants (employees) are not the beneficiaries of the contribution.*

C:SARS V SPUR GROUP (PTY) LTD

(A285/2019; A285/2018 ZAWCHC (26 November 2019; 12 November 2019)

Minority judgment

- The accounting treatment of the contribution supports the above view – the contribution made by the Spur to the Trust was from a group perspective, recognised as not representing an expense to the group.
- The Trust was controlled by Spur HoldCo – the trustees of the Trust had no discretion.
- The contribution was only for the benefit of the group.

"*The distance created by the various legal instruments in the formation of the trust, the contribution, the incentive scheme et al is a masquerade to appear as a section 11(a) expenditure*."

C:SARS V SPUR GROUP (PTY) LTD

(A285/2019; A285/2018 ZAWCHC (26 November 2019; 12 November 2019)

Minority judgment

- Prescription: incorrect information was provided in respect of years of assessment which would otherwise have prescribed, which constitute misrepresentations.
- SARS would have been entitled to lift the veil of prescription.

C:SARS V SPUR GROUP (PTY) LTD

(A285/2019; A285/2018 ZAWCHC (26 November 2019; 12 November 2019)

Minority judgment

- The judgment should have provided that:
  - The appeal be upheld with costs, including costs of two counsel;
  - The order of the Tax Court to read that the appeal is dismissed and the additional assessments raised by SARS for the 2005 – 2012 years of assessment are confirmed.

TAXPAYER V CSARS

Case numbers: 13798; 13931 & 14294 (17 September 2019)

Issue

- The meaning of a “right” and “asset” for purposes of the Eighth Schedule to the ITA (CGT).

TAXPAYER V CSARS

Case numbers: 13798; 13931 & 14294 (17 September 2019)

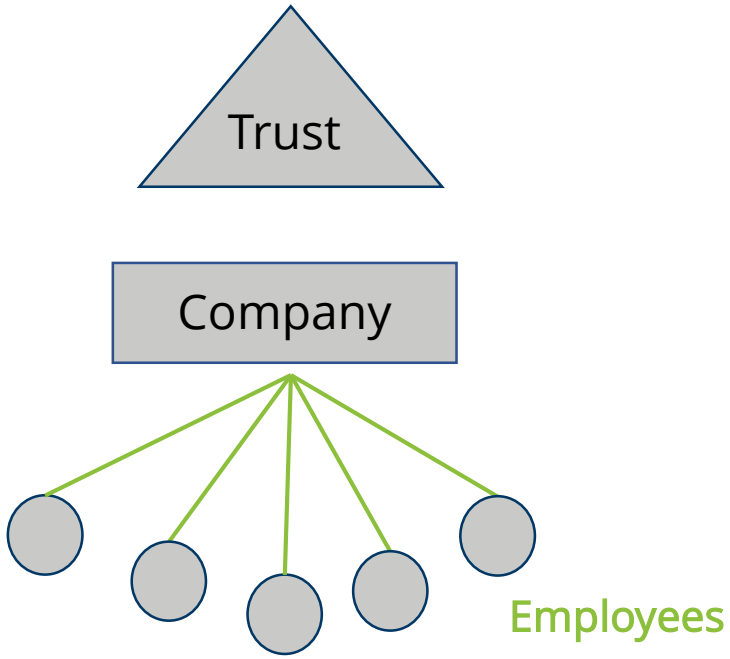
Background

- The taxpayer implemented an Employee Share Incentive Scheme ("the Scheme") incentivise and retain its employees.
- A Trust was used in the implementation of the Scheme:
  - The taxpayer established a discretionary trust.
  - The Trust acquired shares in the taxpayer.
  - The purchase price of the shares were reflected in a loan account in the taxpayer's books.
  - The Trust was obliged to grant share options to the taxpayer's employees at a specific "strike price" when instructed to do so by the taxpayer.
  - When the employees exercised their share options and paid the "strike price", the Trust disposed of the shares to the taxpayer's employees, at less than base cost.
  - In consequence of the above the Trust suffered losses for the 2007 – 2013 years of assessment.
  - The "strike price" for the shares was paid directly to the taxpayer in part settlement of the loan account.
  - The taxpayer agreed to "make good" the Trust's losses (by writing off the balance of the loan/ crediting the loan account).

TAXPAYER V CSARS

Case numbers: 13798; 13931 & 14294 (17 September 2019)

Background



TAXPAYER V CSARS

Case numbers: 13798; 13931 & 14294 (17 September 2019)

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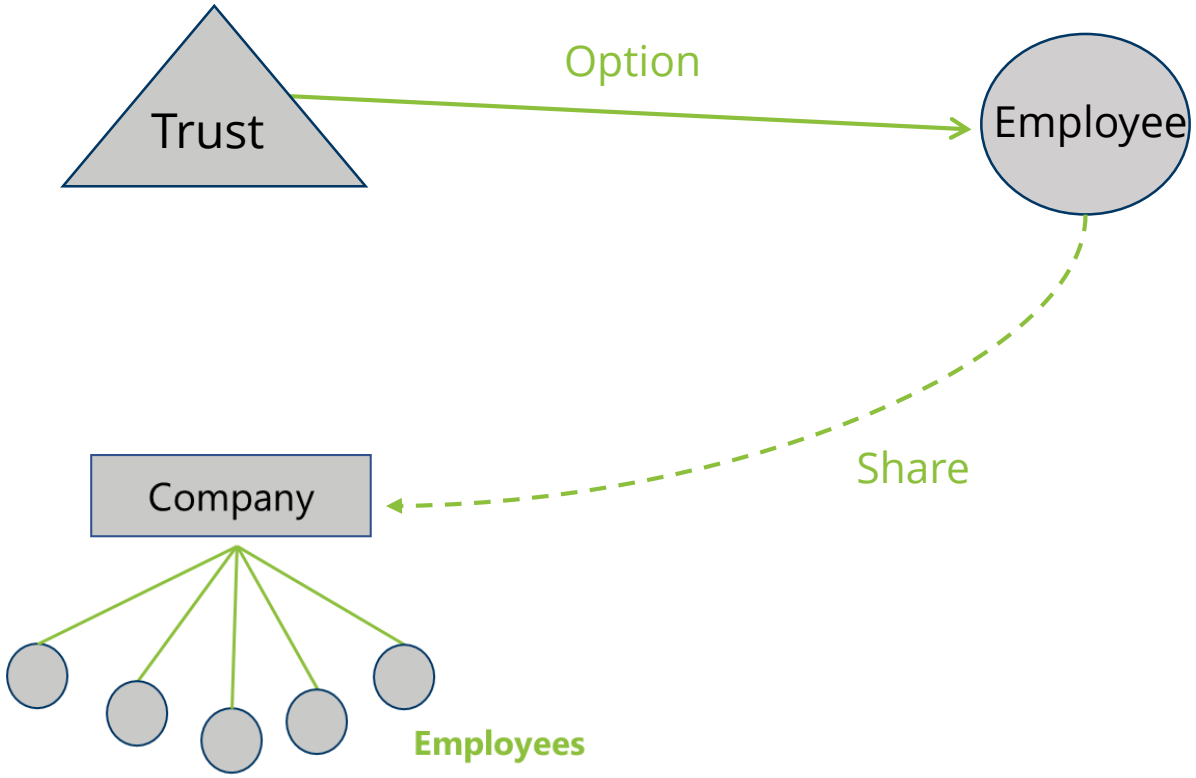

TAXPAYER V CSARS

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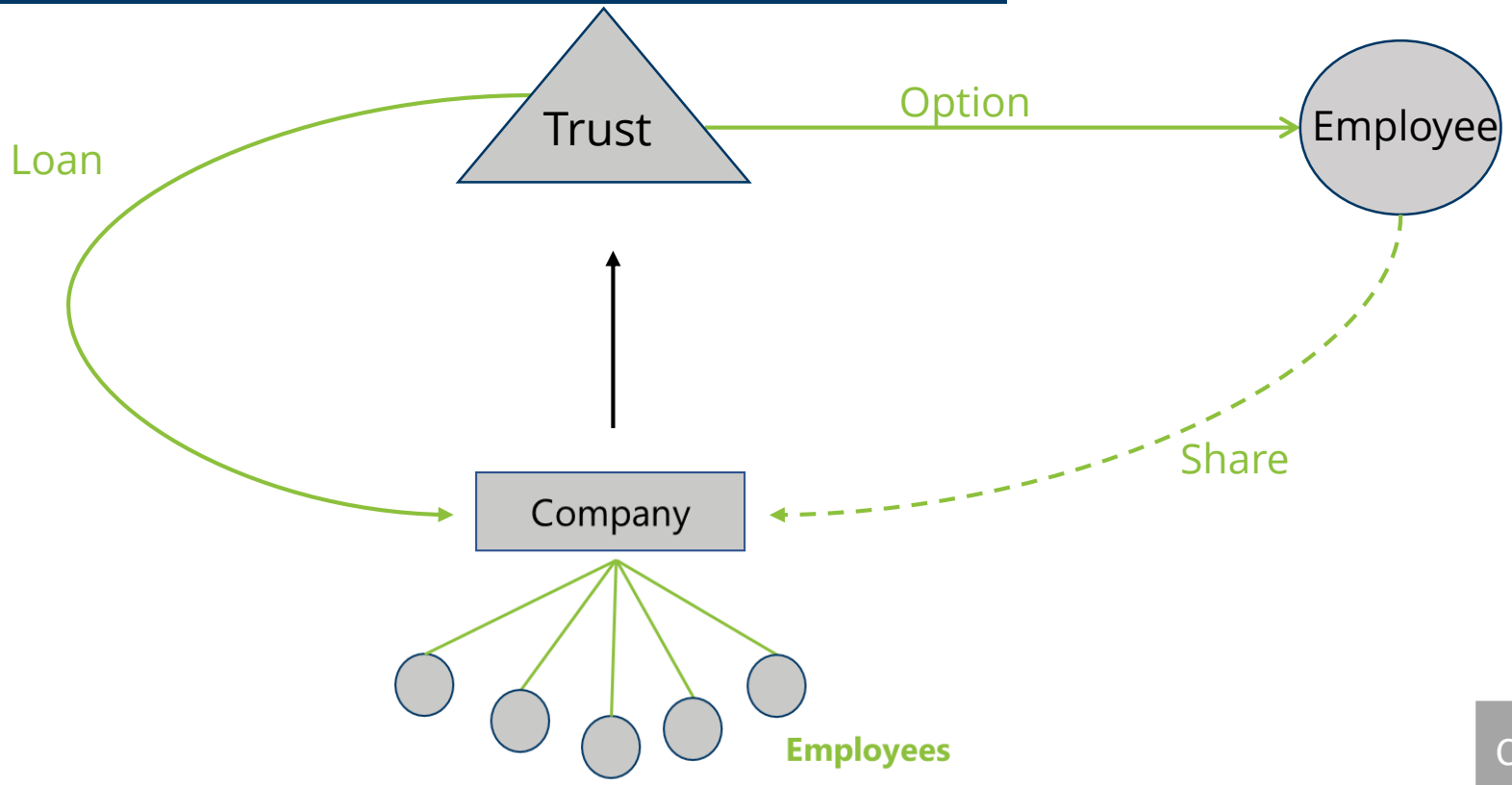


TAXPAYER V CSARS

Case numbers: 13798; 13931 & 14294 (17 September 2019)

Arguments for the taxpayer

- The taxpayer claimed that it was entitled to claim capital losses for CGT purposes in the 2007 – 2013 years of assessment on the following basis:
  - The taxpayer acquired the right to incentivise its employees (the right to have share options made available to its employees at specific strike prices once it gave instruction to the trustees);
  - This right is an "*asset*" for CGT purposes;
  - The "*base cost*" of the "*asset*" (the right) was the amount of the losses made good by the taxpayer (the same amount as the Trust's losses);
  - The "*asset*" was "*disposed of*" when the shares were offered to the employees by the Trust – this extinguished the taxpayer's right; and
  - There were no "*proceeds*" arising from the "*disposal*", and the taxpayer therefore suffered a capital loss.

TAXPAYER V CSARS

Case numbers: 13798; 13931 & 14294 (17 September 2019)

Arguments for the taxpayer

- The taxpayer's right was a right to claim performance or an act *(ius in personam ad faciendum).*
- The matter, so the taxpayer contended, was simple and logical.

TAXPAYER V CSARS

Case numbers: 13798; 13931 & 14294 (17 September 2019)

Arguments for SARS

- The nature of the taxpayer's right is not clear: no rights can arise from a mere instruction by the taxpayer to the trustees of the Trust.
- If a right does exist, then for purposes of the definition of "*asset*" in paragraph 1 of the Eighth Schedule to the ITA:
  - It is not a right to or interest in property as contemplated in paragraph (b) of the definition of "*asset*"; and
  - it is also not corporeal property, an intellectual property right or a contractual right for purposes of paragraph (a) of the the definition of "*asset*".
- Construing the right as an "asset" for purposes of the Eighth Schedule to the ITA also goes against common sense, because the right will never be reflected as an asset in the taxpayer's financial statements.

TAXPAYER V CSARS

Case numbers: 13798; 13931 & 14294 (17 September 2019)

Arguments for SARS

- The appeal amounts to "*sophistry*" and "*strains the definition of 'asset'…*".

TAXPAYER V CSARS

Case numbers: 13798; 13931 & 14294 (17 September 2019)

Judgment

- The issue for adjudication was the meaning of a "*right*" in context of the definition of an "*asset*" as contained in Paragraph 1 of the Eighth Schedule to the ITA.
- An "*asset*":

"***'asset'*** *includes-*

(a) property of whatever nature, whether movable or immovable, corporeal or incorporeal, excluding any currency, but including any coin made mainly from gold or platinum; and

(b) a right or interest of whatever nature to or in such property."

TAXPAYER V CSARS

Case numbers: 13798; 13931 & 14294 (17 September 2019)

Judgment

- The definition of an "*asset*" for CGT purposes should be interpreted in such a manner as to yield a "*sensible and business-like result*" rather than an "*absurd an uncommercial result*".
- "*...any **right** referred to in the context of capital gains tax is a right in or to property, whether movable or immovable, corporeal or incorporeal...*" (Own emphasis.)

- The term "*right*" is not defined in the Eighth Schedule.
- Regard must be had to the common law when interpreting the meaning of the word "*right*" in this context.
- It must then be determined which rights are also assets for purposes of CGT.

TAXPAYER V CSARS

Case numbers: 13798; 13931 & 14294 (17 September 2019)

Judgment

- Under common law, "*rights*" include:
  - Real rights/ *ius in rem* (rights in or to a thing or property), including:
    - ownership; and
    - limited real rights, such as a servitude or a real security right (such as a pledge or mortgage bond).
  - Personal rights/ *ius in personam* (rights against another person/ group of persons):
    - the right to claim delivery of a thing/ *ius in personam ad rem acquirandam*; and
    - the right to claim performance or an act/ *ius in personam ad faciendum*.

TAXPAYER V CSARS

Case numbers: 13798; 13931 & 14294 (17 September 2019)

Judgment

- A right, whether it is a real right or a personal right, is an asset in terms of common law.
- However, for CGT purposes a personal right is not an asset as defined in the Eighth Schedule. It is based on contract and is not in any way attached to or related to property (it is "unrelated to any proprietary rights vesting in the taxpayer").
- On this basis alone, the taxpayer's appeal should fail.

TAXPAYER V CSARS

Case numbers: 13798; 13931 & 14294 (17 September 2019)

Judgment

- Moreover, in order to claim a loss, the taxpayer must prove that in terms of the Eighth Schedule:
  - it had disposed of its asset;
  - the asset was owned by it;
  - the disposal resulted in a capital loss; and
  - the loss occurred during the year of assessment.
- The taxpayer failed to prove that these substantive requirements had been met.

TAXPAYER V CSARS

Case numbers: 13798; 13931 & 14294 (17 September 2019)

Judgment

- It is not clear that the extinction of the taxpayer's right once the trustees perform their contractual obligations, is in fact a "*disposal*" for CGT purposes. No evidence was led to this effect.

- There was no expenditure to the taxpayer, as alleged, even if there was a disposal, because no loss was suffered by the Trust upon the extinction of the taxpayer's right.

- As regards "base cost", the taxpayer failed to state what expenditure was actually incurred in respect of the cost of acquisition or creation of its asset. This point raises further questions regarding when the right/ asset was acquired or created, what the price of acquisition was, what value was disposed of, and exactly when did the disposal occur?

TAXPAYER V CSARS

Case numbers: 13798; 13931 & 14294 (17 September 2019)

Judgment

- If the value of the right was the continued commitment and loyalty of the taxpayer's employees (as it contends), then the taxpayer contradicts itself by stating that it received no consideration in exchange for the disposal of its rights. (Also, what amount should be attached to the consideration?)

TAXPAYER V CSARS

Case numbers: 13798; 13931 & 14294 (17 September 2019)

Judgment

- The taxpayer's arguments as to why the base cost of the asset is the expenditure incurred by it which is equal to the loss made by the Trust on delivery of the shares.
- Once again, the taxpayer's arguments regarding base cost and proceeds are unclear.

TAXPAYER V CSARS

Case numbers: 13798; 13931 & 14294 (17 September 2019)

- Ultimately:
  - the taxpayer's right, even if it was an "asset", is not an "asset" for CGT purposes;
  - the taxpayer failed to establish the base cost of its asset;
  - the taxpayer failed to demonstrate that the asset was disposed of; and
  - the taxpayer failed to show that the proceeds from such disposal was nil.

  - The appeal must be dismissed and the additional assessments confirmed.

TAXPAYER V CSARS

Case numbers: 13798; 13931 & 14294 (17 September 2019)

Judgment

- The court ordered that:
- (1) the USP imposed by SARS for the 2013 year of assessment is waived/ remitted;
- (2) save for (1) above, the appeals for the 2007 – 2013 years of assessment are dismissed;
- (3) save for (1) above, the additional assessments raised by SARS for the 2007 – 2013 years of assessment are confirmed; and
- (4) no order as to costs (including costs of the interlocutory application).

TAXPAYER V CSARS

Case numbers: 13798; 13931 & 14294 (17 September 2019)

Relevance/ comments

- In order to qualify for reduced tax liability, a taxpayer must show that losses incurred by it are capital losses in that the losses:
  - are related to an asset (a personal right is not an asset for purposes of CGT);
  - the asset was disposed of;
  - the disposal was at a loss; and
  - the losses relate to a right in or to property owned by the taxpayer or anyone else.

XYZ CC V C:SARS

IT 14157

Issue

- Evidence – onus of proving that SARS' factual findings during audit and reasons for rejecting an objection were faulty;
- The common law test to qualify as "*independent contractor*".

XYZ CC V C:SARS

IT 14157

Background

- The taxpayer, in conducting its business, enlisted the services of two entities:
  - IOP (represented by its sole proprietor, Mr C); and
  - VWX Construction (represented by its sole proprietor, Mr D).
- Mr C also held the title of General Manager with the taxpayer, and Mr D worked as Tecnhical Advisor.
- The taxpayer treated amounts paid to IOP and VWX in respect of services rendered by Mr C and Mr D as amounts paid to independent contractors, and did not withhold employees' tax under the Fourth Schedule to the ITA.
- Following an audit, SARS contended that Mr C and Mr D were both employees of the taxpayer and that payments made to IOP and VWX for services rendered would be subject to employees' tax.

XYZ CC V C:SARS

IT 14157

Background

- This is an appeal to the Tax Court which follows a SARS audit and subsequent dispute between SARS and the taxpayer.

XYZ CC V C:SARS

IT 14157

Arguments for the taxpayer

- The taxpayer contended that:
  - Mr C t/a IOP was an independent contractor for purposes of work done under IOP's name;
  - Mr D t/a VWX was also an independent contractor when he rendered services under the name of VWX.
  - Amounts paid to IOP and VWX did not constitute remuneration for purposes of the Eighth Schedule, because they were paid to independent contractors and not to employees of the taxpayer.
  - Neither Messrs. C and D's positions with the taxpayer, nor the fact that they were the sole proprietors of IOP and VWX respectively, detracted from IOP and VWX's status as independent contractors.

XYZ CC V C:SARS

IT 14157

Arguments for SARS

- SARS argued that:
  - For the 2011 year of assessment, IOP was not an independent contractor and amounts paid to it for services rendered by Mr C were subject to employees' tax on the basis that:
    - Mr C performed work at the taxpayer's premises and made use of the taxpayer's employees;
    - IOP did not conduct trade independently for this year of assessment and did not have 3 or more employees of its own.

XYZ CC V C:SARS

IT 14157

Arguments for SARS

- For all periods in dispute, VWX was not an independent contractor and payments made to it for services rendered by Mr D were subject to employees' tax on the basis that:
  - Mr D performed work at sites allocated by the taxpayer and made use of the taxpayer's employees;
  - VWX did not have its own employees and did not conduct trade independently; and
- Regard should be had to the facts of the matter – the fact was that the taxpayer, in order to conduct its business, would have had to have a General Manager as well as a Technical Advisor in its employ.

XYZ CC V C:SARS

IT 14157

Judgment

- The appeal was dismissed with costs.

XYZ CC V C:SARS

IT 14157

Judgment

- The taxpayer's case was "*...as confused as it was confusing.*"
- Documentation presented as evidence were incoherent and witnesses' testimony was contradictory and at times evasive.
- The evidence failed to show that VWX was an independent and fully operational construction entity, or whether it was even an operating construction entity at all.
- VWX existed only in name and Mr D was therefore an employee of the taxpayer only, and not of VWX.

XYZ CC V C:SARS

IT 14157

Judgment

- Based on the evidence alone, the taxpayer failed to show that SARS' audit findings and reasons for rejecting the taxpayer's objection were wrong.
- It must follow that the appeal fails on this basis.
- For the sake of completeness, the Court pointed out that, despite the taxpayer having failed to discharge its onus of proof, VWX would in any event not have met the common law test to qualify as "*independent contractor*":
  - VWX did not have more than 3 employees; and
  - VWX did not operate at any premises other than those of the taxpayer.

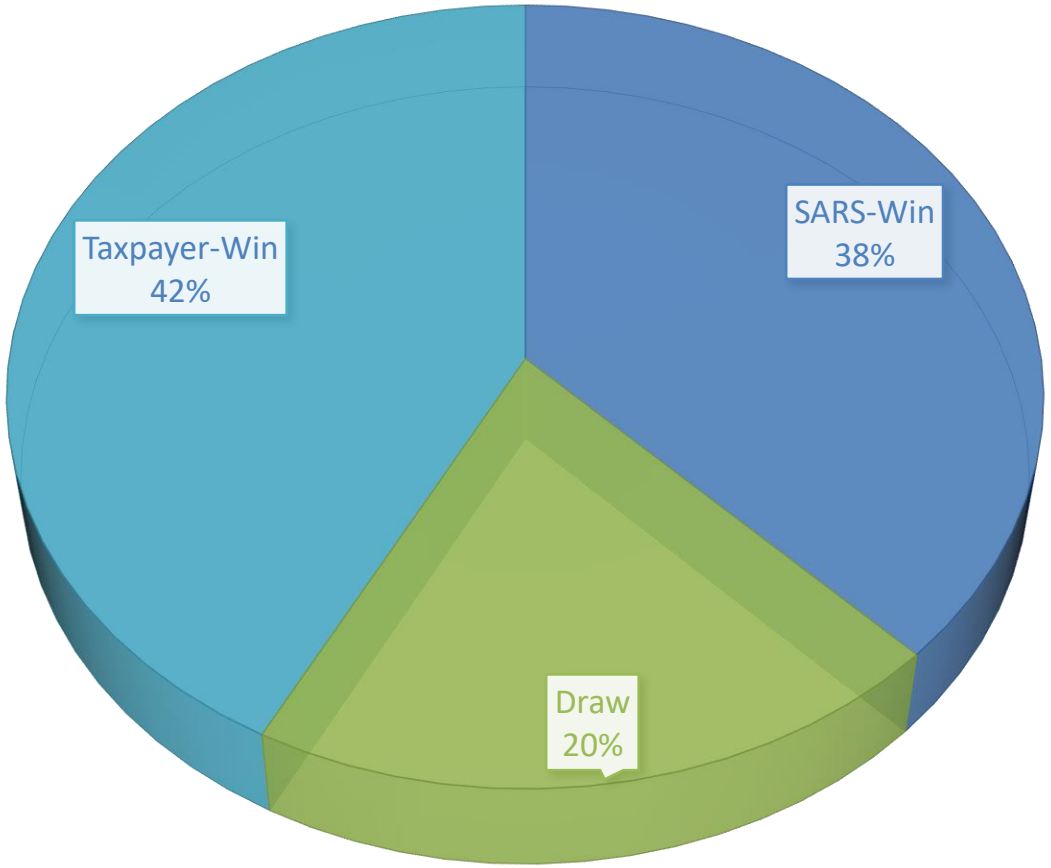
XYZ CC V C:SARS

IT 14157

Comments/ relevance

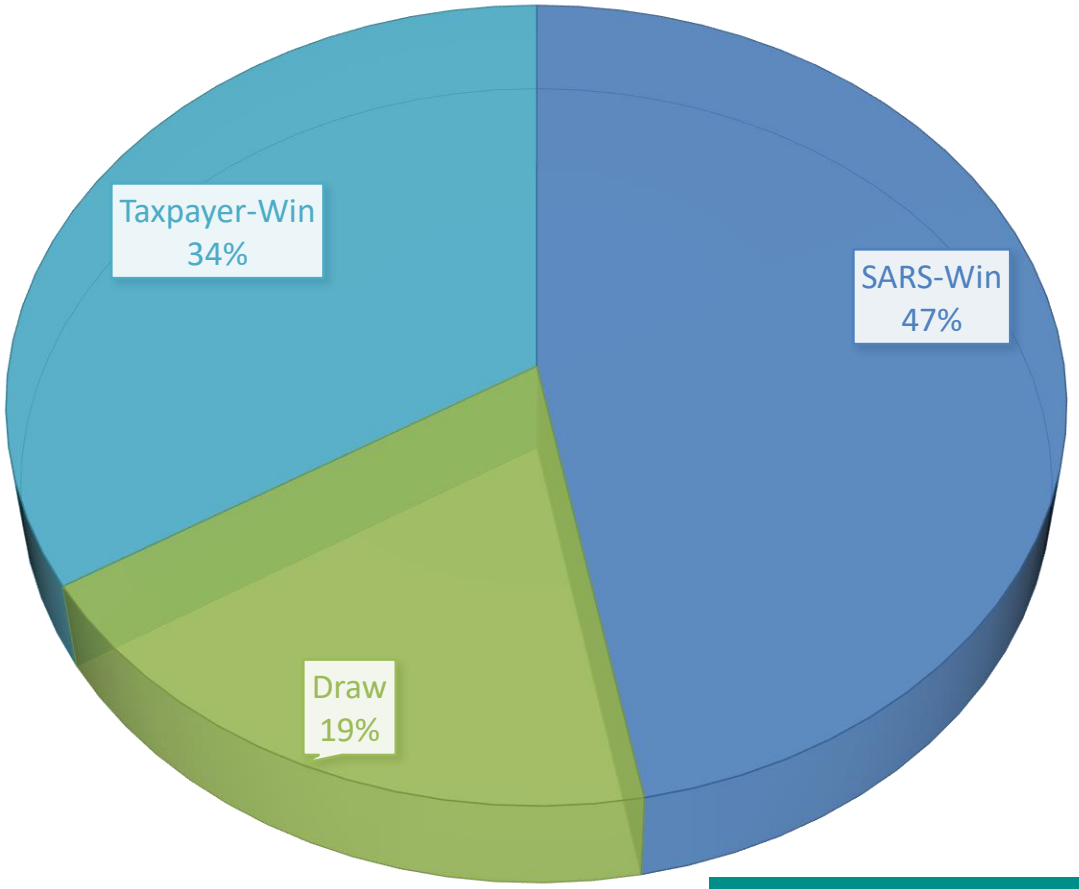
- The taxpayer bears the onus of proving that SARS' factual findings during audit and reasons for rejecting an objection, were faulty or misdirected.
- The taxpayer's case will fail on the basis of insufficient evidence alone.
- The common law test to qualify as "independent contractor" is confirmed.

SARS DISPUTE RESOLUTION & JUDGMENTS 2019 – 2013



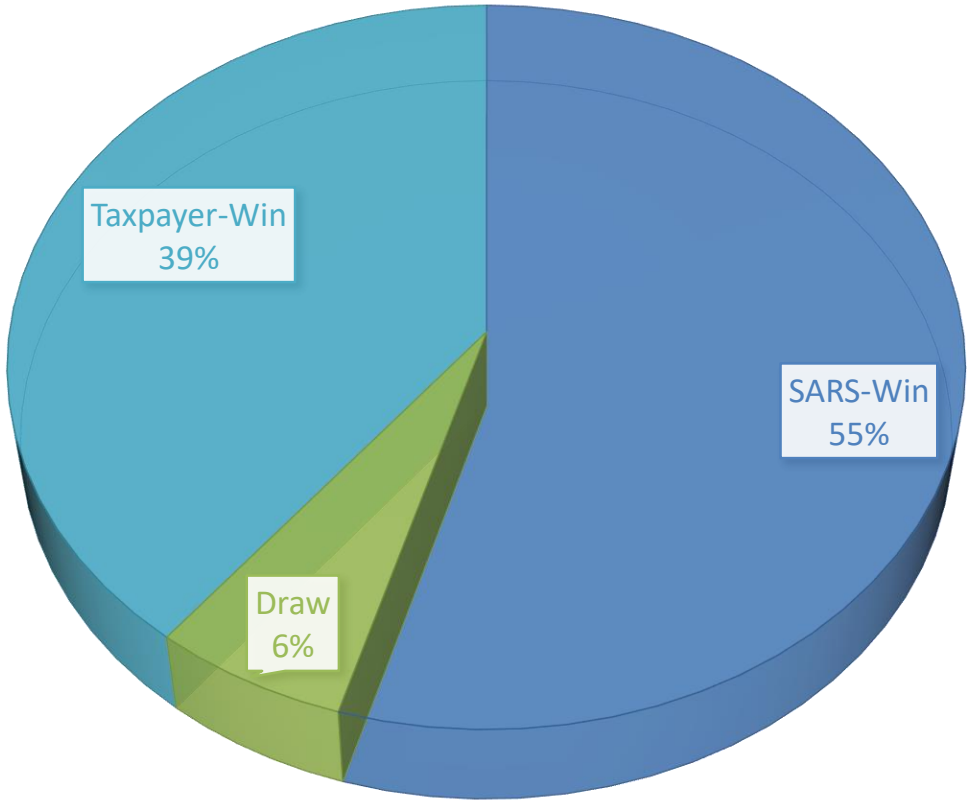
ALL COURTS

SARS DISPUTE RESOLUTION & JUDGMENTS 2019 – 2013



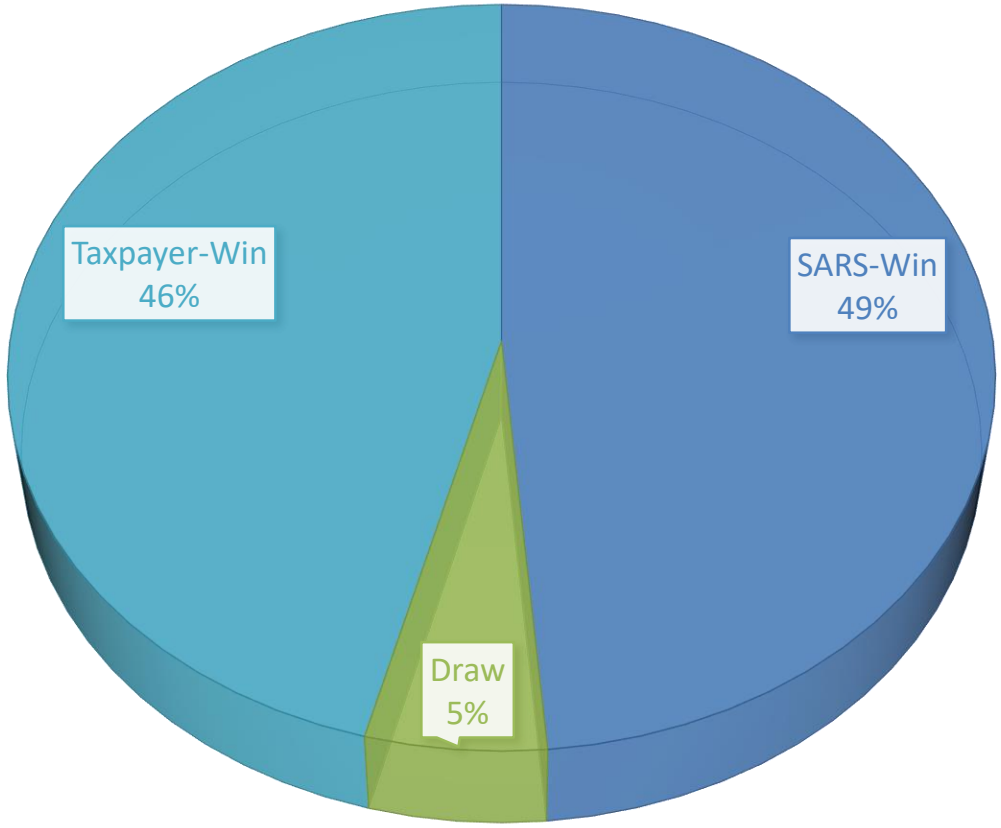
TAX COURT

SARS DISPUTE RESOLUTION & JUDGMENTS 2019 – 2013

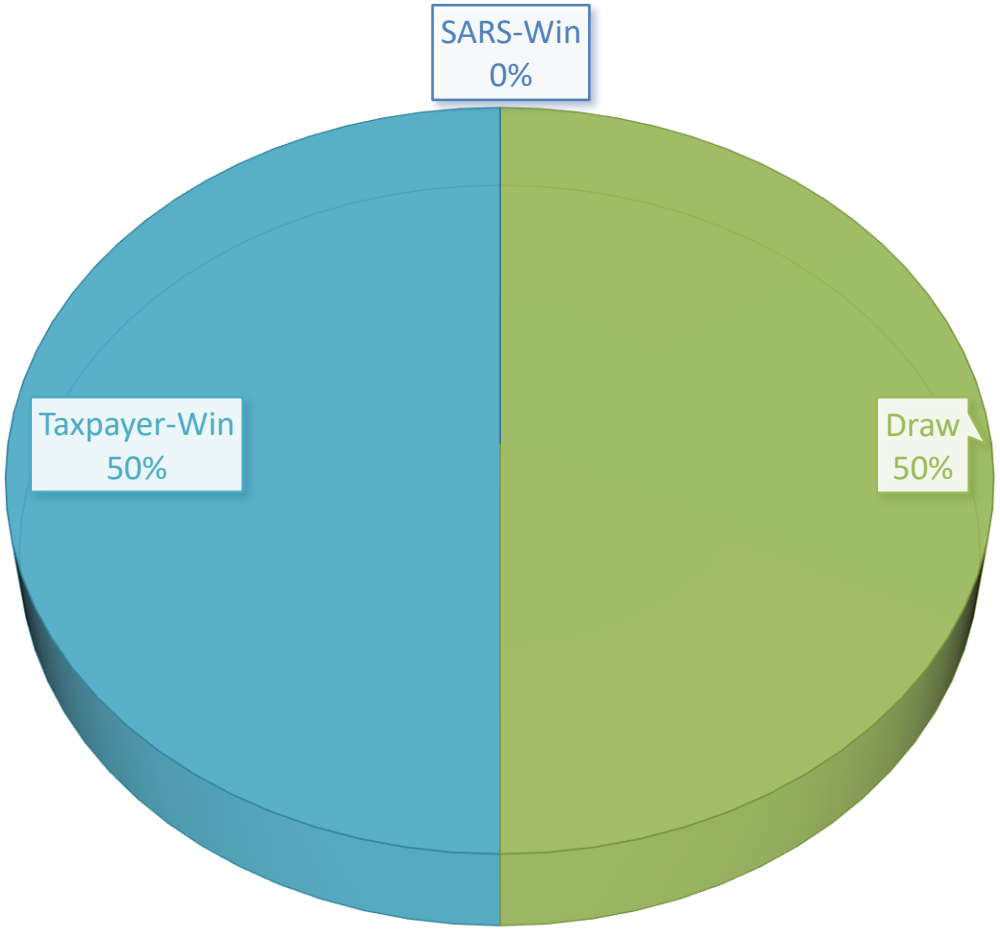


HIGH COURT

SARS DISPUTE RESOLUTION & JUDGMENTS 2019 – 2013



SARS DISPUTE RESOLUTION & JUDGMENTS 2019 – 2013



NOT COVERED

- BPR 335 - STT exemption for foreign governments

ROLL OVERS

- BPR 334 - Waiver of loan claims by the settlor of a trust;
- BPR 336 - Liquidation Distribution;
- BPR 337 - Amalgamation transactions involving the assumption of liabilities only; and;
- BPR 338 - Donations of money made to a public benefit organisation at a fundraising event.

Any Questions

- Please use the Question Portal on iLearn to post any questions.

THANK YOU

You are welcome to send any other questions to ntheron@unicustax.co.za

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