Monthly Tax Update: MAY 2021

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What we are covering this month

- Recent case law judgments
  - Tax Court case: ITC 24918
- SARS matters
  - 2021 filing season and EMP501 reconciliations
  - Tax type transfers
  - Changes to tax directives
  - Recent publications
  - New Interpretation Notes
  - Draft Interpretation Note: Deduction of medical aid lump sum payments

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SARS TC ITC 24918 (IT) [2021] (Johannesburg) (18 March 2021)

- SARS raised additional assessments on ABC Trust for CGT, understatement penalties and interest for 2014, 2015 & 2016.
- The trustees of ABC objected the assessments, and these objections were disallowed apart from one aspect.
- ABC appealed the disallowance of the objection on the basis that the trust was merely a conduit that allowed proceeds from other trusts to flow to their beneficiaries and the CGT ought to be taxed in the hands of the beneficiaries of the trust
- Held that the ABC Trust was not liable to for tax on the capital gain (the appeal was upheld).

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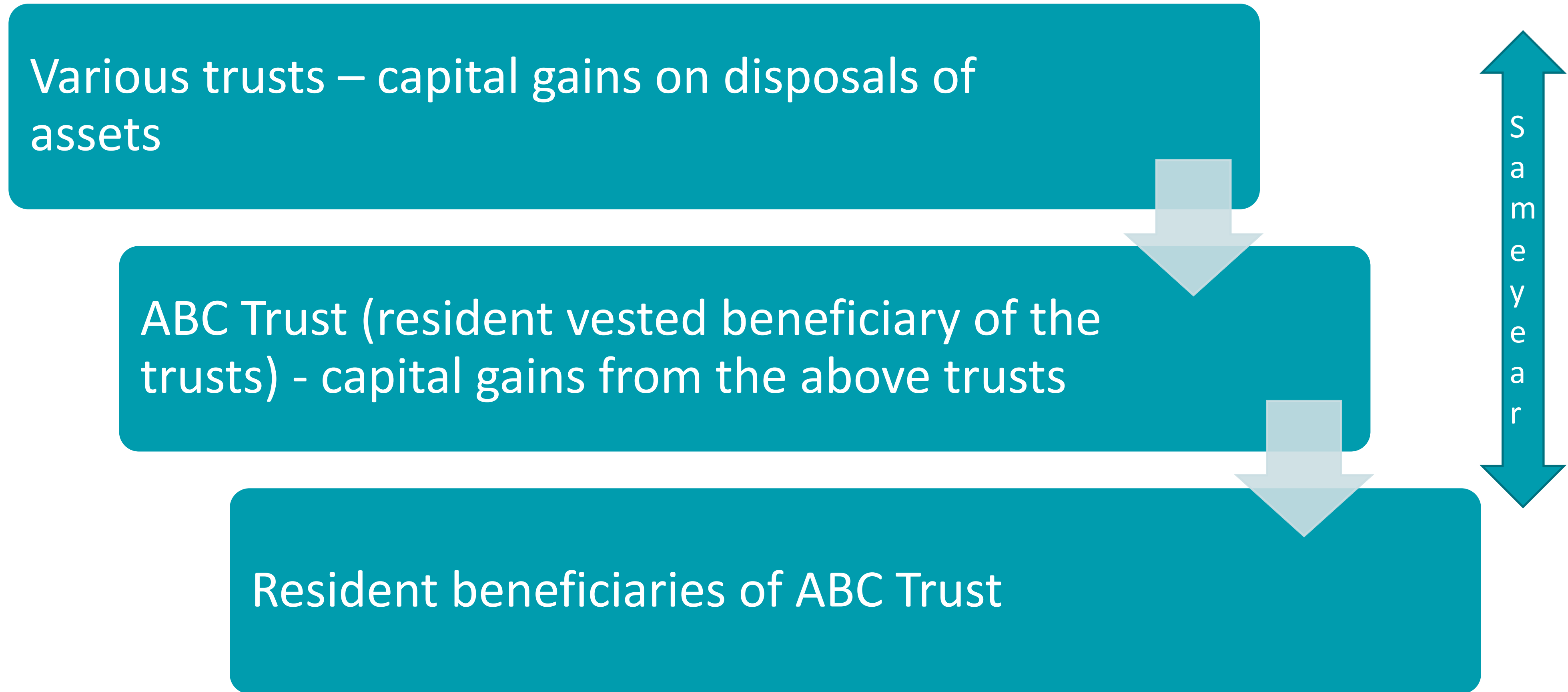
ITC 24918



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Tax law pertaining to trusts

- S 1 definition "person" includes a trust
  - Taxable income taxed at 45%; capital gains effective rate = 80% x 45% = 36% unless s25B or para 80 applies.
- Section 25B
  - Conduit principle – *Armstrong v CIR* 1938 AD 343, 10 SATC 1: income retains its nature
  - Subject to s 7.
- Eighth Schedule paragraph 80

  (1) asset of a trust vesting in a beneficiary

  (2) capital gain vesting in a beneficiary.

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s 25B – Income of trusts and beneficiaries of trusts As it applied in 2014-2016

(1) Any amount received by or accrued to or in favour of any person during any year of assessment in his or her capacity as the trustee of a trust, shall, subject to the provisions of section 7, to the extent to which that amount has been derived for the immediate or future benefit of any ascertained beneficiary who has a vested right to that amount during that year, be deemed to be an amount which has accrued to that beneficiary, and to the extent to which that amount is not so derived, be deemed to be an amount which has accrued to that trust.

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s 25B – Taxation* of trusts and beneficiaries of trusts (as amended)

(1) Any amount (*other than an amount of a capital nature which is not included in gross income or an amount contemplated in paragraph 3B of the Second Schedule**) received by or accrued to or in favour of any person during any year of assessment in his or her capacity as the trustee of a trust, shall, subject to the provisions of section 7, to the extent to which that amount has been derived for the immediate or future benefit of any ascertained beneficiary who has a vested right to that amount during that year, be deemed to be an amount which has accrued to that beneficiary, and to the extent to which that amount is not so derived, be deemed to be an amount which has accrued to that trust.

*1 Amended by s 28(b) of TLA Act 23 of 2020 with effect from 20 January 2021 (previously referred to 'Income of trusts and beneficiaries of trusts').

*2 Inserted by s 28(b) of TLA Act 23 of 2020.

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Eighth Schedule paragraph 80(1)

… where a trust **vests an asset** in a beneficiary of that trust (…) who is a resident, and determines a capital gain in respect of that disposal or, if that trust is not a resident, would have determined a capital gain in respect of that disposal had it been a resident —

(a) that capital gain must be disregarded for the purpose of calculating the aggregate capital gain or aggregate capital loss of the trust; and

(b) that capital gain or the amount that would have been determined as a capital gain must be taken into account as a capital gain for the purpose of calculating the aggregate capital gain or aggregate capital loss of the beneficiary to whom that asset was so disposed of.

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Eighth Schedule paragraph 80(2)

as applied in 2014 - 2016

Subject to paragraphs 68, 69, 71 and 72, where a capital gain is determined in respect of the disposal of an asset by a trust in a year of assessment during which a trust beneficiary (...) who is a resident has a vested interest or acquires a vested interest (including an interest caused by the exercise of a discretion) in that capital gain but not in the asset, the disposal of which gave rise to the capital gain, the whole or the portion of the capital gain so vested-

(a) must be disregarded for the purpose of calculating the aggregate capital gain or aggregate capital loss of the trust; and

(b) must be taken into account for the purpose of calculating the aggregate capital gain or aggregate capital loss of the beneficiary in whom the gain vests.

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Eighth Schedule paragraph 80(2) as amended by the TLAA, 2020

Subject to paragraphs 64E, 68, 69 and 71, where a trust determines a capital gain in respect of the disposal of an asset in a year of assessment during which a beneficiary of that trust (...) who is a resident has a vested right or acquires a vested right (including a right created by the exercise of a discretion) to an amount derived from that capital gain but not to the asset disposed of, an amount that is equal to so much of the amount to which that beneficiary of that trust is entitled in terms of that right —

(a) must be disregarded for the purpose of calculating the aggregate capital gain or aggregate capital loss of the trust; and

(b) must be taken into account as a capital gain for the purpose of calculating the aggregate capital gain or aggregate capital loss of that beneficiary.

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ITC 24918

- ABC Trust argued that it had no liability for tax as no capital gain accrued to it due to the vesting in the beneficiary in the same year – it had merely acted as a 'conduit pipe'.
- Judgment (Wright J)

  [15] In my view, the words "Any amount " which open section 25B(1) include capital gains as:

  [15.1] The words themselves are as wide as they could be when considered literally.

  [15.2] The word "any" has been held to be "a word of wide and unqualified generality. It may be restricted by the subject-matter or the context, but prima facie it is unlimited". (Per Innes CJ in *R v Hugo* 1926 AD 268 at 271.) "In its natural and ordinary sense, any – unless restricted by the context – is an indefinite term which includes all of the things to which it relates." (*Per* Innes JA in *Hayne & Co v K Steam Mill Co Ltd* 1914 AD 363 at 371)". See *Commissioner for Inland Revenue v Ocean Manufacturing Ltd* 1990 (3) SA 610 (A) at 618 G – H.

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ITC 24918

[20] In my view, what passed from the vesting trusts to ABC and then to ABC's beneficiaries were capital gains "determined in respect of the disposal of an asset" and which constituted "capital gain but not an asset" within the meaning of these words in the main body of paragraph 80(2) rather than "an asset" as these words were used in the main body of paragraph 80(1).

This finding flows from the agreed facts set out above.

On these facts, the vesting trusts disposed of certain capital assets and in consequence thereof made capital gains.

What the trustees of the vesting trusts awarded to ABC were the realised proceeds of these capital gains. These proceeds are in my view accurately described by the parties as "amounts" in the agreed facts. What was awarded from vesting trust to ABC and then on to ABC's beneficiaries were amounts being the proceeds of and representing capital gains.

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[[21] In short, the capital gains in question fall within the purview of section 25B(1), section 25B(2) and paragraph 80(2) but not within paragraph 80(1) at least as these sub-sections and sub-paragraphs read for the years under consideration.

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- Wright J:
  - Held that the words "*any amount*" in s 25B should be interpreted widely to include the realised proceeds of capital gains, irrespective of the fact that the vesting of capital gains in trust beneficiaries is specifically dealt with in para 80(2).
  - Held that para 80(2) had to be read with other applicable laws, being s 25B and the conduit principle.
  - Relied on the remarks of Trollip JA in the *Rosen* case that the *Armstrong* case "*... authoritatively established the conduit principle for general application in our system of taxation in appropriate circumstances*".

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- Wright J:
  - Noted that s 25B(1) had been amended by TLAA 23 of 2020 with effect from 20 January 2021 to include the words ‘other than an amount of a capital nature which is not included in gross income ...’ and concluded that this was evidence that the prior wording allowed the gains to flow rather than become trapped.
  - Thus, held that the capital gains flowed through to the beneficiaries of the ABC Trust as a result of the application of s 25B (as opposed to paragraph 80(2)) and the beneficiaries, and not the ABC Trust, were required to include the capital gains in their taxable income calculations.

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Order:

1. The appeal is upheld.
2. The additional assessments for the appellant for the 2014, 2015 and 2016 years of assessment are set aside.
3. There is no order as to costs.

Update: SARS appealing directly to the SCA

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ITC 24918
SARS view

- A capital gain is "determined" by **the trust which actually disposes** of the asset, not by the beneficiary in whom the asset or capital gain is vested.
- A beneficiary only "takes into account" the capital gain "determined" by the trust.
- It is not, therefore, possible for a capital gain to be "conduited" through multiple trusts as it is only the first trust in the chain which "determines" the capital gain.

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Explanatory Memorandum on the Taxation Laws Amendment Bill, 2020 (at 58)

Amendment to s 25B

"… some commentators have contended that s 25B(1) also applies to amounts of a capital nature (for example, proceeds on disposal of a capital asset).

There is no substance in this contention because the Eighth Schedule contains specific provisions dealing with such amounts, but for the purposes of clarity it is proposed to exclude amounts of a capital nature that are not deemed to be included in gross income from the ambit of s 25B(1)."

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SARS view

CGT Guide p 606

- Section 25B deals with income and has no relevance to capital gains and losses. This fact can be seen from the heading (Income of trusts and beneficiaries) and from the history of the provision.
- Section 25B applies to both resident and non-resident trusts.
- Before it was amended by the in 2004, the opening words of s 25B(1) referred to 'any income' but this was changed to 'any amount' as a result of uncertainty whether the word 'income' was being used in its defined sense of gross income less exempt income, or in the more general sense of the word.
  - If it meant the former, many types of income derived by non-resident trusts would have been excluded because the definition of 'gross income' includes in the gross income of a non-resident only amounts from a SA source.
  - Even if it were contended that the word 'amount' could include an amount of a capital nature, under the maxim *generalia specialibus non derogant* [General things do not derogate from specific things] the Eighth Schedule must take precedence over s 25B, since it is the more specific provision.

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SARS view
CGT Guide p 606

- Further evidence that s 25B applies only to income can be seen from the fact that it is 'subject to the provisions of section 7'. Section 7 deals largely with the attribution of income to a donor. Had it been intended that s 25B also apply to capital gains, s 25B would have been made subject to the special attribution rules in paras 68, 69 and 71.
- A capital gain cannot be attributed under s 25B(1) because it does not constitute an amount received or accrued. It is comprised of proceeds less base cost.
  - Could it be argued that proceeds fall to be dealt with under s 25B(1) while base cost is addressed in s 25B(3)? For the reasons already explained, the amount contemplated in s 25B(1) does not include amounts of a capital nature.
  - Secondly, s 25B(3) refers to a 'deduction or allowance'. These words are typically used to refer to amounts deducted from income, and when the legislature refers to the base cost of an asset in the main body of the Act, it tends to do so explicitly as in s 9HA(2) and s 12P.
  - In addition, s 25B(4) limits the deductions or allowances attributed to a beneficiary under s 25B(3) to the income of the beneficiary. It would make no sense to limit the base cost of an asset to the income of a beneficiary.

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SARS view
CGT Guide p 607

- The Eighth Schedule contains self-contained provisions for dealing with trusts and their beneficiaries. There is therefore no conflict between s 25B and the Eighth Schedule, and the specific provisions of the Eighth Schedule must prevail.
- For the sake of clarity, it is proposed in the Taxation Laws Amendment Bill, 2020 to exclude from s 25B(1) 'an amount of a capital nature which is not included in gross income'.

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SARS view
CGT Guide p 611-612

- There is a vast difference between the legislative provisions that prevailed at the time of the *Armstrong* and *Rosen* cases and the provisions that are currently enacted. A trustee of a discretionary trust is no longer merely an 'administrative conduit pipe' for tax purposes. The trust has been clothed with its own separate legal *persona* and is a taxable entity in its own right. …
- The conduit-pipe principle cannot, therefore, be applied to override the legislative intent. Paragraph 80 remains the sole mechanism for attributing a capital gain arising in a trust to a beneficiary.
- If a capital gain has not been attributed out of a trust to a specific person, the core rules must be applied and the trust must bear the CGT consequences. In other words, attribution is something that cannot be read in; it can be applied only when it is provided for.

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CGT Guide p 621: Capital gain flowing through multiple discretionary trusts

Can a capital gain flow through multiple resident discretionary trusts when it is vested by each consecutive trustee in the same year of assessment?

- The words 'the trust' in para 80(2)(*a*) refer to the same trust mentioned in the opening words of the subparagraph, namely, the trust that has determined a capital gain in respect of the disposal of an asset. A beneficiary that happens to be a trust does not determine a capital gain in respect of the disposal of an asset – it must simply account for the capital gain attributed to it under para 80(2)(*b*). Such an attributed capital gain cannot be further attributed.
- Thus, a capital gain of a discretionary trust can be attributed only once and cannot flow through multiple resident discretionary trusts in the same year of assessment. Any subsequent on-distribution of an amount equal to the attributed capital gain simply represents a disposal which does not give rise to a capital gain or loss, usually just a part-disposal of the on-distributing trust's bank account.

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2021 filing season and EMP501 reconciliations

- Filing season expected to open from 1 July 2021.
- The auto assessment process initiated in 2020 will progress in 2021, with a focus on ensuring that third parties submit data timeously and accuracy.

- *Provisional* deadlines:
  23 November 2021: non-provisional taxpayers(eFiling or branch)
  31 January 2022: provisional taxpayers
- Draft ITR12 released to RCBs for input.

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2021 filing season and EMP501 reconciliations

- Due date for submission of the EMP501 covering the full tax year from 1 March 2020 to 28 February 2021 is **31 May 2021**.
  - Penalty for late submission (or incomplete submission): up to 10% of PAYE (para 14(6) of the Fourth Schedule) will be levied at 1% per month that the reconciliation is outstanding.
  - An employer who wilfully or negligently fails to submit a (EMP201 or EMP501) return to SARS is guilty of an offence and is liable, upon conviction, to a fine or imprisonment for up to 2 years.

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NB: EMP501s and SDL tax holiday

- SDL exemption for the months of May to August 2020 under the Disaster Management Tax Relief Measures: must show SDL as zero for these months.
- If the SDL for these 4 months is overstated on the February 2021 EMP501 and/or 2021 IRP5/IT3(a) certificates (effectively ignoring the SDL exemption), the SARS reconciliation process will automatically increase the SDL payable for February 2021, resulting in an outstanding SDL liability together with penalties and interest.
- This must be corrected on the EMP501 and/or IRP5/IT3(a) certificates.

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Tax type transfers

- In 2020, SARS implemented changes to the eFiling tax type transfer process for all personal income tax products. The change impacted individual taxpayers and representative taxpayers of deceased and insolvent estates of individuals.
- Reasons for the change:
  - Taxpayers will have full control of their eFiling profiles; and
  - The relationship between taxpayers and their representatives can be authenticated.
- New process for all other entities and tax products was rolled out 23 April 2021.
- SAIT Notice https://cdn.ymaws.com/www.thesait.org.za/resource/resmgr/2021_technical/0415_mailer/Rollout_of_Tax_Type_Transfer.pdf
- SARS Guide pm managing your user profile: https://www.sars.gov.za/gen-elec-18-g01-how-to-register-for-efiling-and-manage-your-user-profile-external-guide/

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2021 filing season SARS website

Enhancements to the SARS MobiApp	26 April 2021 – The taxpayers will now receive estimated assessment via MobiApp. Taxpayers will have an option to either view the return or edit the return. Once editing, the return option is selected, the taxpayers original return will be filed / submitted to SARS. For more information, see the updated Guide to the SARS MobiApp.

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Guide on tax directives

- The **Completion Guide for IRP3(a) & IRP3(s) Forms** was updated on 26/4/21.
  - The purpose of this guide is to assist Fund Administrators / Long-term Insurers and / or employers with the completion of a Tax Directive Application form to obtain a Tax Directive (IRP3) before a lump sum can be paid to an employee.
  - The Guide was updated to include an Arbitration / CCMA Award filed; and the *'Year of assessment'* on a directive and tax certificate was clarified.
  - The Guide was also updated with the Provident and Provident Preservation funds compulsory annuitisation and with the following new reasons on the tax directive application forms:
    - Par (*e*A) Living Annuity Commutation Termination of a Trust (Form E);
    - Cessation of SA Residence (Form B and Form C)
    - Unclaimed death benefits (Form A&D)
- See the [Completion guide for IRP3(a) & IRP3(s) forms.]()

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Changes to guides on directives (26 April 2021)

- **Guide on Tax Directive for emigration, cease to be resident and expiry of visas** was updated to include the definitions of 'provident fund' and 'provident preservation fund' were amended for the annuitisation of benefits on retirement. The purpose of this guide is to provide basic information relating to the tax directive applications for emigration withdrawals and withdrawals due to the expiry of a visa. Guide on Tax Directive for emigration, cease to be resident and expiry of visas.
- **Guide to the Tax Directive functionality on eFiling** was updated with the Tax Directive functionality to request previous years' tax directives. This guide is designed to assist Fund Administrators / Long-term Insurers / Employers / Tax Practitioners and/or Individuals with the Tax Directive administrative functions on eFiling. Guide to the Tax Directive functionality on eFiling.

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Changes to guides on tax directives (cont.)

Transfers between Funds and preservation funds

- The Guide on how to complete, submit and cancel a recognition of transfer was updated with additional fields for the annuitisation of Provident and Provident preservation Funds and with the additional fields for the second transfers of public sector benefits to another approved fund.
- The purpose of this guide is to provide guidance on the use and submission of the recognition of transfer form (ROT01) for transfers between Funds and preservation funds; and the recognition of the purchase of an annuity form (ROT02) when annuities are purchased on retirement, the beneficiary purchase an annuity upon the death of the member or annuitant or transfer to / between Long-term Insurers.
- Guide on how to complete, submit and cancel a recognition of transfer.

10 May 2021 – Tax Directives: Updated IBIR-006 Specification

- SARS will implement changes to the Tax Directives interface between now and 21 May. Please refer to the updated IBIR-006 revision 6.105 Interface Specification to familiarise yourself with the coming enhancements.

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Recent SARS publications

Information on the tax obligations relating to Small, Micro, and Medium Enterprises (SMMEs):

Small business leaflet

Turnover Tax leaflet

Customs trader leaflet

Traveller's leaflet

New interpretation notes

23 April 2021 – Income Tax Act, 1962: Two interpretation notes were published:

- Interpretation Note 115 – Withholding tax on interest

  https://www.sars.gov.za/wp-content/uploads/Legal/Notes/IntR-IN-2021-02-IN-115-Withholding-tax-on-interest.pdf

- Interpretation Note 116 – Withholding tax on royalties

  https://www.sars.gov.za/intr-in-2021-03-in-116-withholding-tax-on-royalties/

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Interpretation Note 115 – Withholding tax on interest (23 April 2021)

- Deals with the interpretation and application of ss 50A to 50H.
- Section 10(1)(*h*) provides a blanket income tax exemption for interest payable to non-residents subject to two exceptions relating to physical presence in SA.
- WHT is a final tax at a rate of 15%, which may be reduced by the application of a DTA.
- Applies to SA source interest (see s 9(2)(b)) paid to or for the benefit of a foreign person, subject to exemptions.

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Example – exemption from WHT

On 1 March of the year of assessment under review, B, a resident, donated R1 million to the B Family Trust, a non-resident trust formed and effectively managed in Country G. The trust immediately on-lent the funds to C, a resident, at a rate of 8% a year. During the year of assessment under review the trust earned interest of R80 000 on the loan to C which was attributed to B under s 7(8).

Result:

The interest paid by C to the trust is exempt from withholding tax on interest (under s 50D(1)(*e*)) because it was attributed in full to a resident donor (B) under s 7(8).

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Example – exemption from WHT

On 1 March of the year of assessment under review, B, a resident, lent R1 million to the B Family Trust, a non-resident trust formed and effectively managed in Country G. The loan bore interest at a rate of 2% a year. Had the trust borrowed the money from a commercial bank, it would have paid interest at the rate of 8% a year. The trust immediately on-lent the funds to C, a resident, at a rate of 8% a year.

During the year of assessment under review the trust earned interest of R80 000 on the loan to C of which R60 000 was attributed to B under s 7(8) [R1 million × (8% − 2%)].

Result:

Of the interest paid by C to the trust, R60 000 is exempt from withholding tax on interest because that amount was attributed to a resident donor (B) under s 7(8).

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Example – reduced rate under a DTA

T, a resident of Country S, advanced a loan to Company F, a resident.

According to the loan agreement entered into by T and Company F, T is entitled to interest at 9% a year on the loan amount of R600 000. The interest became due and payable on 31 August 2021.

Article 11(2) of the South Africa – Country S Tax Treaty provides that interest received by a resident of a Contracting State [Country S], from a source within the other Contracting State [South Africa], may be taxed in that other Contracting State [South Africa] but at a rate not exceeding 5% of the interest paid.

T duly completed and submitted the declaration and undertaking to Company F before payment of the interest.

Result:

Since T submitted the declaration and undertaking before payment of the interest by Company F, withholding tax on interest must be deducted at the reduced tax rate

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Example – reduced rate under a DTA

Result:

Since T submitted the declaration and undertaking before payment of the interest by Company F, withholding tax on interest must be deducted at the reduced tax rate of 5%:

	R
Loan advanced by T	600 000
Interest received (R600 000 × 9%)	54 000
Withholding tax on interest (5% × R54 000)	2 700

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Interpretation Note 116 – Withholding tax on royalties (23 April 2021)

- Deals with the interpretation and application of ss 49A to 49H which relate to withholding tax on royalties.
- WHT on royalties applies to royalties from a source within SA (see s 9(2)(c) – (f)) paid by any person (whether a resident or not) to a foreign person for the use of intellectual property belonging to that person or for the imparting of or the undertaking to impart any scientific, technical, industrial or commercial knowledge or information, or the rendering of or the undertaking to render any assistance or service in connection with the application or utilisation of such knowledge or information.
- WHT on royalties is a final tax at the rate of 15%; can potentially be reduced or eliminated by a tax treaty.
- Various exemptions (s 49D).

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Example – WHT on royalties

X, a resident of Country Z, entered into an agreement with Y, a South African resident, allowing Y to make use of X's invention.

According to the agreement, X is entitled to royalties from Y for the use of the patent rights relating to the invention.

The royalties are payable on 31 January each year and are calculated at 5% of Y's turnover for each financial year ending on 31 December.

For the year ended 31 December 2020, Y's turnover was R600 000. The royalty was paid on 31 January 2021 and Y withheld the withholding tax on royalties as required.

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Example – WHT on royalties

Result:

	R
Turnover for 2020	600 000
Royalties (R600 000 × 5%)	30 000
Withholding tax (15% × R30 000)	4 500

- On 31 January 2021 when the royalty was paid, X is liable for withholding tax on royalties of R4 500.
- Y was therefore obliged to withhold this amount and pay it to the Commissioner by 28 February 2021.
- Y withheld the amount of R4 500 and therefore paid X R25 500 (R30 000 royalty − R4 500 withholding tax on royalty).
- If X pays over the amount of withholding tax on royalties as required to the Commissioner, the amount will be regarded as an amount paid by Y in respect of Y's liability under the Act.

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Draft Interpretation Note: Deduction of medical aid lump sum payments

- Provides guidance on the interpretation and application of s 12M which relates to the deductibility of a lump sum amount paid by a taxpayer to or in respect of a former employee or dependants of that former employee for purposes of covering post-retirement medical benefits.
- The income tax implications of this benefit to the former employee are not considered in this Note.

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Section 12M

- Section 12M allows a taxpayer to claim an immediate deduction of a lump sum payment made for purposes of covering the post-retirement medical aid contributions of a specified former employee or dependant if it meets the requirements below:
  - an amount is **paid** by the taxpayer (see **4.2.1**);
  - by way of a **lump sum** (see **4.2.2**);
  - during the taxpayer's **year of assessment** (**4.2.3**);
  - in the **course of the taxpayer's trade** (**4.2.4**);
  - to –
    - any **former employee** who retired from the taxpayer's employment on the grounds of **old age, ill-health or infirmity** or to any **dependant** of such former employee (see **4.2.5**), or
    - an insurer under a **policy of insurance** taken out solely in respect of one or more of the above-mentioned former employees or their dependants (see **4.2.5**); and
  - the purpose of making the lump sum payment is to enable the former employee or his or her dependants to make a contribution to a **medical scheme or a medical scheme fund.**

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Section 12M

- The deduction is limited to the extent that the lump sum payment is for the purpose of making a contribution to a specified medical scheme or medical scheme fund in respect of the above-mentioned former employee or dependant.
- No deduction is allowed if the taxpayer or any connected person in relation to the taxpayer retains or has a future obligation as relates to the mortality risk of the above-mentioned former employee or dependant.
- Section 23(*e*) does not prohibit a deduction under s 12M.

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Example - Amount paid to an insurer

- Company W enter into a policy of insurance with GE Insurers, an insurer as defined in s 29A.
- According to the policy of insurance if an employee retires on the ground of ill-health, Company W will make a lump-sum payment of R1 000 000 to GE Insurers.
- GEInsurers will assume the responsibility for all future medical aid scheme contributions of the former employee, or a dependant of such a former employee. **In addition**, GE Insurers will also contribute to a separate wellness product sold and administered by a separate company in the same group of companies as the medical scheme, which provides certain benefits to a former employee or a dependant of such former employee.

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Result

- The proviso to s 12M prohibits a deduction where the amount paid by a taxpayer is not for purposes of making contributions in respect of a former employee or dependant of such former employee to a medical aid scheme.
- Therefore, the amount deductible under s 12M will be limited to the portion of the lump sum related to the medical aid scheme contributions.
- The portion related to the contributions to the loyalty programme will not be deductible by the taxpayer under s 12M.

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Example - Amount paid to an insurer

- Company Z makes a payment of R900 000 on 15 April 2020 to DEF Insurers, an insurer as defined in s 29A, in respect of the medical aid contributions of former Employee X.
- Employee X retired from Company Z on the grounds of ill-health.
- According to the policy of insurance Employee X's medical aid coverage is for a period equal to the shorter of the earlier of Employee X either reaching the age of 75 years or his death. In the event that Employee X survives beyond the age of 75 years, Company Z will be responsible for further medical aid contributions.

Result:

- The proviso to a 12M prohibits a deduction where a taxpayer retains an obligation, whether actual or contingent, in respect of the mortality risk of a former employee or dependant of such a former employee. Should Employee X survive beyond the age of 75 years, the mortality risk will be assumed by Company Z.
- In retaining the mortality risk of Employee X after the age of 75 years it has retained a contingent obligation and will be precluded from deducting the lump sum payment under s 12M.

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QUESTIONS?

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