Monthly Tax Update: OCTOBER 2021

Presented by: Professor Jackie Arendse PhD MTP(SA) CA(SA)

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What we are covering this month

- Recent tax judgments:
  - Mukuru Africa (Pty) Ltd v CSARS (ZASCA)
  - CSARS v Spur Group (Pty) Ltd (ZASCA)
  - IT 24888: understatement penalty
- Recent SARS documents and noticesincluding
  - Employers' interim reconciliation filing season
  - Enhanced application process for deferred payment arrangements
  - Amended income tax returns for trusts and companies
  - Updated guide on VAT and non-executive directors

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Mukuru Africa (Pty) Ltd v CSARS
[2021] ZASCA 116 (16 September 2021)

- Appeal from the Tax Court
- Apportionment of VAT under s 17(1) of the VAT Act

- Mukuru, a registered vendor, commenced business on 1/2/2014
- Provides money-transfer and *bureau de change* services, as well as mobile phone credits.
- makes both taxable and exempt supplies and incurs expenditure in acquiring goods and services for the purpose of use, consumption or supply in the making of those supplies.
- the input VAT incurred must therefore be apportioned in terms of s 17(1) of the VAT Act.

Section 17(1)

Where goods or services are acquired or imported by a vendor

partly for consumption, use or supply in the course of making taxable supplies and partly for another intended use,

the extent to which any tax which has become payable in respect of the supply to the vendor or the importation by the vendor… of such goods or services … is input tax,

shall be an amount which bears to the full amount of such tax …, the same ratio (as determined by the Commissioner in accordance with a ruling as contemplated in Chapter 7 of the Tax Administration Act or s 41B)

as the intended use of such goods or services in the course of making taxable supplies bears to the total intended use of such goods or services…

Method of apportionment

- BGR 16 prescribes the standard turnover-based method (STB method) of apportionment as the default method of apportionment, which applies to all vendors who have not obtained an alternative ruling from SARS.
- On 20 February 2017, Mukuru applied to SARS for a ruling under s 41B of the VAT Act to permit the use of a 'transaction count (TC)' ratio to apportion its mixed-purpose input VAT deductions for the tax periods commencing 1 February 2014.
  - On 24 July 2018, SARS approved the TC method for use by Mukuru (the July 2018 ruling) - for the period commencing 1 March 2016, but not in respect of the earlier period from 1 March 2014 to 29 February 2016.
  - SARS took the view that proviso (iii) precluded it from approving the TC ratio for use in any period prior to 1 March 2016. Mukuru objected against SARS decision.

- [10] The primary issue in the appeal is whether SARS (as it contends and the Tax Court held) was precluded by proviso (iii) from granting approval for use of the TC ratio by Mukuru in respect of the period 1 March 2014 to 29 February 2016.

- [13] Relying on what was styled a 'condition' in BGR16, Mukuru argues that, given the nature of its business, it was not 'fair and reasonable' for it to use BGR16.

The ‘condition’ in BGR 16 reads

‘The vendor may only use this method if it is fair and reasonable. Where the method is not fair and reasonable or inappropriate, the vendor must apply to SARS to use an alternative method.’

- Mukuru argued that because BGR16 did not apply to it, the July 2018 ruling did not constitute a change to an existing apportionment method and therefore, proviso (iii) does not apply, to preclude the retrospective operation of the July 2018 ruling.

VAT Guide for Vendors (VAT 404) reads:

- ‘The only approved method which may be used to apportion VAT incurred for mixed purposes without specific prior written approval from the Commissioner, is the turnover-based method.
- This method applies by default in the absence of a specific ruling obtained by the vendor to use another method as there is usually a fairly good correlation between the turnover of a business and the resources (or inputs) which are employed to produce that turnover.’

[17] In any event, it is not open to a vendor to simply ignore a SARS' ruling or to unilaterally apply its own method of apportionment.

What is more, in terms of BGR16, if the method prescribed is not fair and reasonable or appropriate, the vendor must apply to SARS for a fair, reasonable and appropriate ruling.

It does not provide, as Mukuru appears to suggest, that from the commencement of its operations, no approved apportionment method applied to it.

Nor did it provide for Mukuru to simply unilaterally assume its own apportionment; one not sanctioned by SARS.

The remedy for any unfairness and unreasonableness or inappropriateness is for a vendor to apply to the SARS for an alternative method of apportionment, not to regard BGR16 as *pro non scripto*.

Proviso (iii) to s 17(1) limits the extent to which SARS may determine a ratio with retrospective effect in certain circumstances

where a method for determining the ratio referred to in this subsection has been approved by the Commissioner,

that method may only be changed with effect from a future tax period, or from such other date as the Commissioner may consider equitable and such other date must fall –

(aa) in the case of a vendor who is a taxpayer as defined in s1 of the Income Tax Act, within the year of assessment as defined in that Act; or

(bb) in the case of a vendor who is not a taxpayer as defined in s 1 of the Income Tax Act, within the period of 12 months ending on the last day of February, or if such vendor draws up annual financial statements in respect of a year ending other than on the last day of February, within that year, during which the application for the aforementioned method was made by the vendor.

[19] The legislature contemplates that the apportionment method for the purposes of s 17 of the VAT Act must relate to a time in the future or, if it is to be retrospective, for a period not exceeding the income tax year during which the application is made for a change in the apportionment method.

Mukuru's application for the July 2018 ruling was an application to change from the STB method to the TC method.

When SARS approved the change of method in response to Mukuru's application, it had no power to do so retrospectively, to a date earlier than 1 March 2016. It follows that the Tax Court was correct in its conclusion that:

'. . . The STB method set out in BGR16 was the only ratio applicable to the appellant until its private binding ruling had been issued in 2017 and proviso (iii) to s 17(1) expressly precluded SARS from issuing a ruling that had effect from a date earlier than 1 March 2016.'

What can we learn from the Mukuru case?

- Mukuru had to apply the standard apportionment method for the period prior to 1 March 2016, even though it did not produce a fair and reasonable result and bore had no resemblance to its business or the extent of its taxable supplies, because it did not apply for a ruling when it commenced trading.
- Ensure that a ruling is obtained timeously to use an alternative method of apportionment if the standard method does not produce a fair result.
- Ensure that a new ruling is obtained when the ruling expires.

CSARS v Spur Group (Pty) Ltd
[2021] ZASCA 145 (15 October 2021)

Payment of a contribution to an employees' share incentive scheme trust:

i. whether there was a sufficiently close connection between the contribution and the taxpayer's income producing operations so as to qualify for a deduction under s 11*(a)* of the Income Tax Act; and

ii. if the connection between the contribution and the taxpayer's production not close or immediate enough to justify the deduction, was SARS precluded from raising additional assessments in respect of the taxpayer's 2005-2009 years of assessment by operation of the period of limitations provided in s 99(1) of the Tax Administration Act.

Background

- Spur is the main operating entity in the Spur Group of companies. It is a wholly owned subsidiary of Spur Corporation Limited (Spur HoldCo).
- On 30 November 2004, Spur HoldCo established the Spur Management Share Trust (the trust), a discretionary trust of which, Spur HoldCo was the sole capital and income beneficiary.
- The Trust Deed was amended on 13 December 2010 to permit the participants to benefit from dividends received by the trust. However, Spur HoldCo remained the sole capital beneficiary.
- On 7 December 2004, Spur concluded a contribution agreement with the trust in terms of which an amount of R48 million was contributed to the trust.
- The trust acquired 1 000 preference shares in NewCo, which were redeemed five years later in December 2009. The R48million was returned to the trust and remained in the trust.

- Spur claimed a contribution of R48 million it made to the trust as a deduction against its income under the general deduction formula (s 11(a)).
- The deduction was spread over the period of the anticipated benefit to be derived from the payment, from 2005 to 2012, in terms of s 23H as follows:
  - R3 462 265 in 2005;
  - R6 924 531 for the years 2006 to 2011;
  - and R3 462 265 in 2012.

The Commissioner's argument

- Spur made the contribution to the trust, of which Spur HoldCo was the sole beneficiary.
- Spur HoldCo was the only party to have benefited directly from the contribution as the trust distributed the preference share capital and the preference share dividends to its beneficiary, Spur HoldCo.
- The participants were thus not the beneficiaries of the contribution.
- The causal link referred to at the end of the preceding paragraph was thus lacking.
- The contribution was therefore not expenditure incurred in the production of Spur's income as required by s 11*(a)*, and there was only an indirect and insufficient link between the expenditure and any benefit arising from the incentivisation of Spur's key staff.

- [31] The contribution of R48 million was used, wholly, to subscribe for preference shares in NewCo.
- Only the trust held the NewCo preference shares, and only *it* was entitled to the return of the R48 million contribution, plus the preference dividend on those shares.
- The participants had no right to any part of the contribution, nor to the preference dividends that flowed from the investment thereof.

- [32] Importantly, in terms of the trust Deed, only Spur HoldCo would, as capital beneficiary, have any right to the ultimate delivery of the R48 million contribution and any yield therefrom.
- The participants were neither capital nor income beneficiaries of the trust at that stage
  - they might have become entitled to dividends accruing to the trust from 2010 onwards, following upon an amendment to the trust deed to this effect, but this fact was irrelevant as the concern was in relation to what was done when the contribution of R48 million was made in 2004.

The prescription issue

SARS raised additional assessments on 28 July 2015 in respect of Spur's 2005-2009 years of assessment.

The original assessments were raised on

31 May 2007 (2005),

7 August 2007 (2006),

12 May 2009 (2007),

24 February 2010 (2008) and

16 January 2010 (2009).

Section 99(1) of the TAA

Provides that the Commissioner may not make an assessment more than three years after the date of the original assessment by SARS, but

except where (s 99 (2)*(a)*) in the case of assessment by SARS the fact that the full amount of tax chargeable was not assessed, was due to –

(i) Fraud;

(ii) Misrepresentation; or

(iii) Non-disclosore of material facts.

- SARS alleged that the amount of tax chargeable in terms of the additional assessments were not so assessed by SARS in the 2005- 2009 years of assessments due to misrepresentation and non- disclosure of material facts by Spur.
- In its 2005 income tax return (IT14), Spur had answered 'no' to the following questions:
  - Were any deductions limited in terms of s 23H?
  - Did the company make a contribution to a trust?
  - Was the company party to the formation of a trust during the year?
- In the 2006 income tax return, Spur answered 'no' to the question:
  - Were any deductions limited in terms of s 23H?

Furthermore, in each of the 2005-2008 income tax returns, the amount of deductions claimed in respect of the contribution, which were limited by s 23H of the ITA, were disclosed by Spur under the category ‘other deductible items’ and not under the line item ‘prepaid expenditure (as limited by s 23H)’.

- [46] Spur's defence to the allegation of misrepresentation and non- disclosure of material facts was that the aforesaid statements were negligently and inadvertently made.
- Spur also asserted that the Commissioner failed to establish the requisite *causal nexus*, in that it is unclear how Spur's inadvertent and incorrect disclosures would have altered the basis of the Commissioner's assessment in the affected years.
- Spur submitted that as the onus to establish a *causal nexus* to displace the statutory immunity conferred by the TAA has not been met, the additional assessments issued in respect of Spur's 2005-2009 years of assessment were unlawful, invalid and cannot be confirmed.

- Conclusion: Spur had made false statements in the returns
  - [63] I should also add that as a matter of policy, a court would be loath to come to the assistance of a taxpayer that has made improper or untruthful disclosures in a return. Clearly, this would offend against the statutory imperative of having to make a full and proper disclosure in a tax return.
  - [64] In light of what I have stated above, I therefore find that the misrepresentations and non-disclosures by Spur caused the Commissioner not to assess Spur correctly within the three-year period after the original statements.
- Thus, the appeal was upheld and the assessments raised by SARS for 2005 – 2012 were confirmed.

IT 24888 (Western Cape Tax Court, 18 June 2021)

- The appellant ("Z CC") trading in properties and building work, concluded contract with a purchaser ("ABC") in terms of which it sold to ABC an immovable property for the sum of R25.2 million including VAT.
- The agreement provided that the purchase price was payable in tranches of R350 000 '…on transfer of each erf to the end user purchaser' from ABC. Registration of transfer to ABC was subsequently effected on 27 October 2016.
- The agreement was thus concluded, and transfer effected, during the appellant's 2017 year of assessment.
- Z did not declare the capital gain on the disposal in its 2017 income tax return, as it was of the view that the capital gain on the sale would only accrue to it on transfer of the individual erven to third party end users.

Time of disposal: para 13(1) of the Eighth Schedule

The time of disposal of an asset by means of -

(a) a change of ownership effected or to be effected from one person to another because of an event, act, forbearance or by the operation of law is, in the case of -

(i) an agreement subject to a suspensive condition, the date on which the condition is satisfied;

(ii) any agreement which is not subject to a suspensive condition, the date on which the agreement is concluded.

Time of disposal: suspensive condition

In *CSARS v Bosch* [2014] ZASCA, Wallis, J stated:

"A suspensive condition is one that suspends the exigible content of a contract, either in whole or in part, pending the occurrence of an uncertain future event."

If the "certain conditions" constituted a suspensive condition in a sale contract and these were met before the end of the year of assessment, the time of the disposal will be in that year.

Note: The registration in the deeds office is not a suspensive condition.

- SARS issued an additional assessment on 29 March 2018 in which *inter alia* it imposed a 25% understatement penalty of R798 372.
- Paragraph 4.3 of the SARS rule 31 statement read as follows:
  - The omission of the proceeds of R22 105 263 (VAT excl.) from the disposal of an asset in the Appellant's income tax return for the 2017 year of assessment for capital gains purposes, resulted in a loss to the prejudice of the *fiscus*, rendering the Appellant liable for the payment of an understatement penalty at the rate of 25% for a behaviour category of "reasonable care not taken in completing a return" on a standard case imposed in terms of s 222 read with s 223 of the TAA.

Matters in dispute

- Whether there was an understatement, properly classified (in the form of an omission from a return), which caused prejudice to SARS or the *fiscus* as provided in the definition of "understatement" in s 221 of the TAA;
- If so, whether the understatement arose from (a) behaviour on the part of the appellant which may appropriately be described as 'reasonable care not taken in completing a return'; (b) unreasonable actions on the part of the appellant; or (c) a *bona fide* and inadvertent error on its part.

Prejudice to SARS?

- In terms of s 221 “understatement” means **any** prejudice to SARS or the *fiscus.* The word “any” is “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).
  - Income tax would have been recovered earlier from that tax period, had the capital gain been declared. The delay in paying tax when due caused prejudice to SARS or the *fiscus.*
  - Time spent on the audit.

Behaviour category

[45] The question which then arises is whether SARS correctly categorised the understatement as being the result of 'reasonable care not taken in completing a return'.

Although during argument SARS advanced various reasons why it was correctly categorised as such, it is bound by the concession of its own witness Ms X that this was, in hindsight, incorrect and that the penalty should rather have been based on 'no reasonable grounds "for tax position" taken' which would have attracted a penalty of 50%.

Can the Tax Court change the penalty %?

Section 129(3) of the TAA:

'In the case of an appeal against an understatement penalty imposed by SARS under a tax Act, the tax court … may reduce, confirm or increase the understatement penalty.'

But, only if the issue has been properly raised for adjudication before that court (*Purlish* ZASCA [2019]).

Thus, the taxpayer remains liable for the 25% penalty.

Employer reconciliations

SARS website:

The Employer Interim Reconciliation Declaration (EMP501) submission period closes on 31 October 2021.

During this period, employers are required to reconcile the payroll tax liabilities (PAYE, SDL and UIF) declared on their monthly Employer Declarations (EMP201) for the first six months of a reconciliation year (1 March to 31 August 2021).

SARS Guide to Dispute Administrative Penalties

13/9/21: updated with PIT Once-off Penalty information

A once-off administrative penalty will be levied for the late submission of a return by taxpayers that were selected for auto assessment for the 2020 year of assessment, and failed to accept or decline/edit and submit their return before 15 February 2021, if they were required to.

- Taxpayers that did not take any action will be issued with an auto original estimated assessment after 15 February 2021.
- If a return is subsequently submitted by the taxpayer after this assessment is issued and the financial information on the 2020 tax return has been edited, a once off admin penalty may be imposed (if 1 or more other returns are outstanding in addition to the 2020 return).

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- The once-off penalty will also be imposed on all provisional and non-provisional taxpayers that were not auto assessed for 2020 tax year, and submitted the 2020 return after the deadline:
  - Non-provisional taxpayers: 30 November 2020; and
  - Provisional taxpayers: 15 February 2021.
- The taxpayer will be notified of the imposed penalty through the penalty assessment notice (AP34).
- The notice will reflect imposed penalties, outstanding returns, and corrective measure to be followed in order to prevent accumulation of penalties.
- Taxpayers are advised to submit a request for remission (RFR) if they do not agree with the penalty imposed.

Requesting deferred payment arrangements

SARS has made enhancements to e-Filing to enable taxpayers to request Deferral Payment Arrangements.

Allows taxpayers to make payment arrangement requests without having to visit a SARS branch office or contact the SARS Contact Centre.

Applies to: personal income tax, corporate income tax, dividends withholding tax, VAT, PAYE/UIF/SDL and administrative penalties.

Trusts 2021 Filing Season

SARS has amended the ITR12T form and made system changes

SARS website - Trusts Filing Season 2021 changes

Step by step guide to complete your ITR12T

Comprehensive Guide to the Income Tax return for Trusts

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Corporate Income Tax (CIT)

Website notice

SARS recently made system changes and amended the

- Income Tax Return for Companies (ITR14) and
- Notice of Assessment for Companies (ITA34C)
- Guides (https://www.sars.gov.za/types-of-tax/corporate-income-tax/completing-an-itr14/):
  - How to complete the ITR14 on efiling
  - How to complete the ITR14 (General guide)

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Guide on VAT and non-executive directors Updated 28 July 2021

https://www.sars.gov.za/wp-content/uploads/Ops/Guides/LAPD-VAT-G15-VAT-Quick-Reference-Guide-for-Non-Executive-Directors.pdf

BGR 40 - 10 February 2017

BGR 41 - 4 May 2017

QUESTIONS?

Please use the Q&A portal or the Chat box

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