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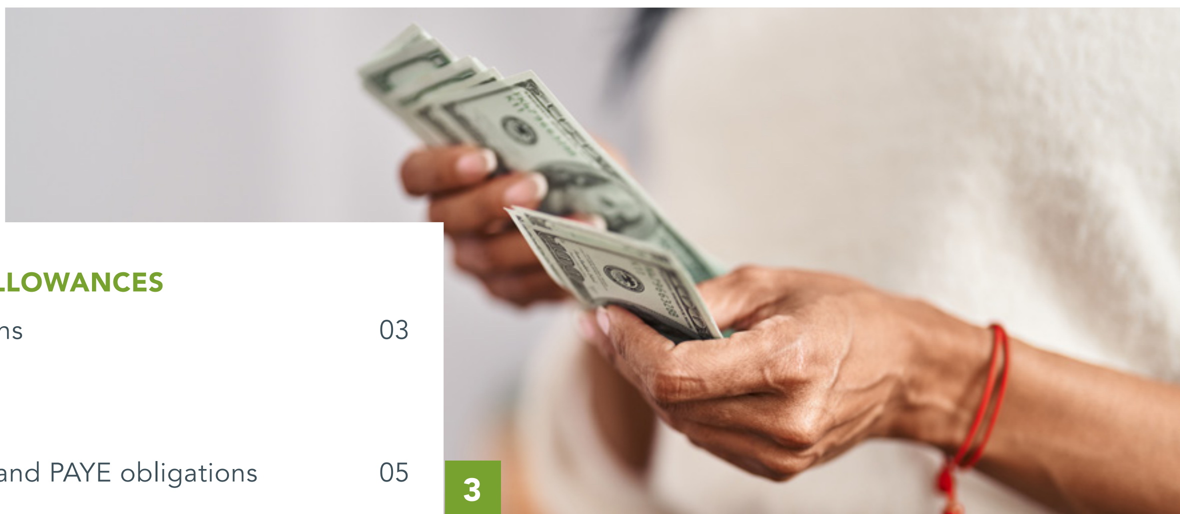
DEDUCTIONS AND ALLOWANCES
INTEREST DEDUCTIONS

TAX ADMINISTRATION
HIGH COURT'S JURISDICTION IN TAX DISPUTES

TRUSTS
SPECIAL TRUSTS



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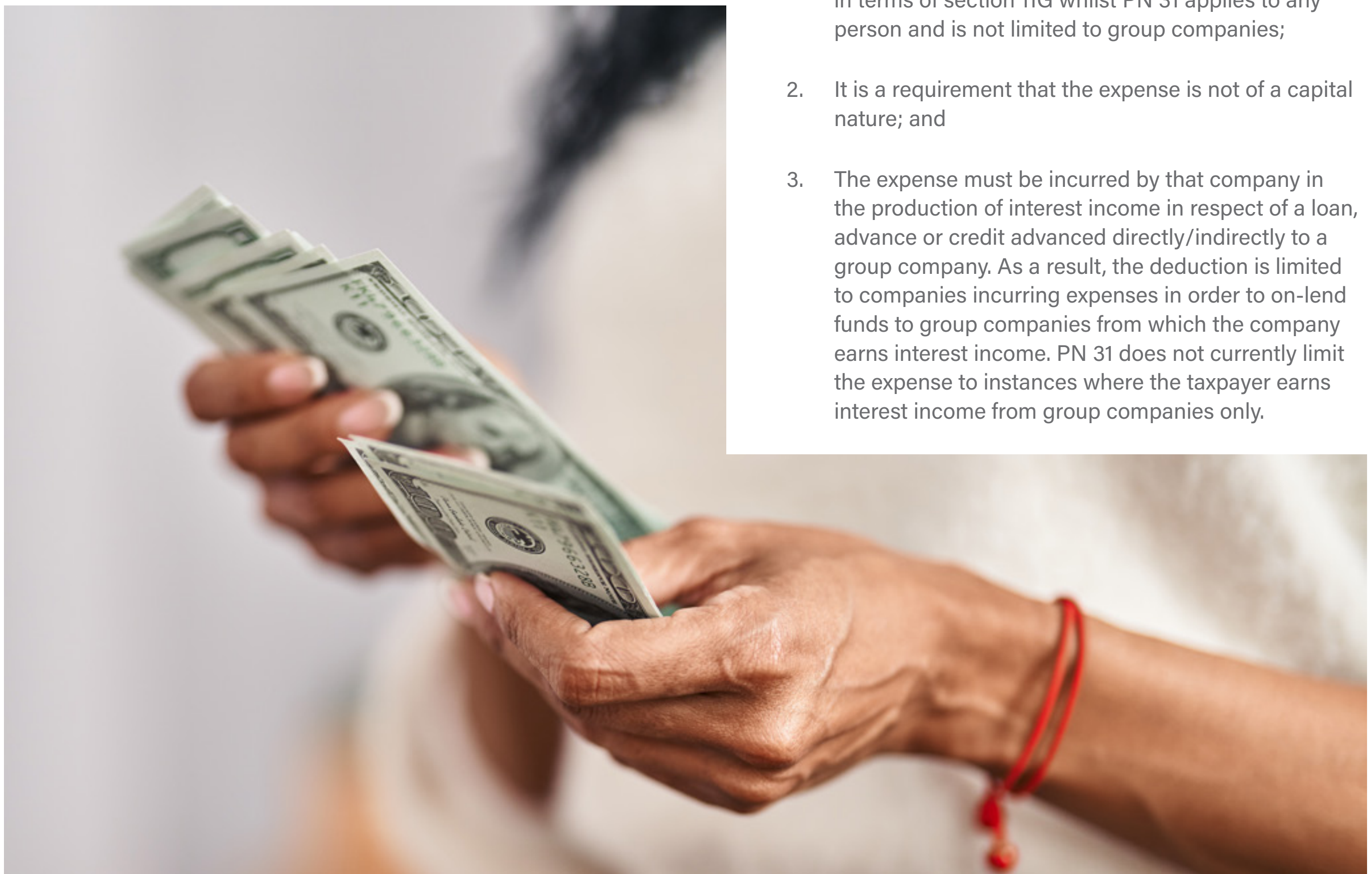
INTEREST DEDUCTIONS

Currently, a taxpayer is entitled to deduct interest calculated in terms of section 24J(2) of the Income Tax Act, 1962 (the Act) if –

- the taxpayer derived income from carrying on a trade; and
- the amount of the interest is incurred in the production of income.

Many taxpayers who do not carry on a trade have until now relied on Practice Note 31 of 1994 (PN 31) to claim a deduction for interest incurred on funds borrowed where such funds were invested in interest-bearing instruments or on-lent, resulting in the taxpayer earning interest income. In particular, PN 31 states as follows:

> "While it is evident that a person (not being a moneylender) earning interest on capital or surplus funds invested does not carry on a trade and that any expenditure incurred in the production of such interest cannot be allowed as a deduction, it is nevertheless the practice of Inland Revenue to allow expenditure incurred in the production of the interest to the extent that it does not exceed such income. This practice will also be applied in cases where funds are borrowed at a certain rate of interest and invested at a lower rate. Although, strictly in terms of the law, there is no justification for the deduction, this practice has developed over the years and will be followed by Inland Revenue."



In 2022, the South African Revenue Service (SARS) indicated that it intends to withdraw PN 31.

However, after public consultation, taxpayers were given an opportunity to make representations regarding the withdrawal. As a result, during the 2023 Budget Speech, it was announced that the proposed withdrawal of PN 31 would be delayed. This was to give time for government to review the impact of the proposed withdrawal and to consider whether changes could be made in tax legislation to accommodate legitimate transactions affected by the withdrawal. It was stated that the withdrawal of PN 31 will be aligned with the effective date of any legislation arising from the proposed considerations.

The 2023 draft Taxation Laws Amendment Bill (the Draft TLAB) containing the proposed amendments to the Act was released on 31 July 2023 and one of the proposed changes was the insertion of a new section 11G into the Act. The proposed section 11G was to provide a deduction for expenditure incurred and is effectively the concession as a result of the withdrawal of PN 31. In terms of the Draft TLAB it was scheduled to come into operation on 1 January 2024.

However, section 11G under the Draft TLAB differed significantly from PN 31 in the following respects:

1. It is limited to a company claiming a deduction of expenses incurred by that company. Taxpayers such as individuals and trusts cannot claim a deduction in terms of section 11G whilst PN 31 applies to any person and is not limited to group companies;
2. It is a requirement that the expense is not of a capital nature; and
3. The expense must be incurred by that company in the production of interest income in respect of a loan, advance or credit advanced directly/indirectly to a group company. As a result, the deduction is limited to companies incurring expenses in order to on-lend funds to group companies from which the company earns interest income. PN 31 does not currently limit the expense to instances where the taxpayer earns interest income from group companies only.

The proposed section 11G also contains a proviso that the amount allowed to be deducted under this section must not exceed the amount of that interest income. This is similar to the current requirement under PN 31.

The draft Explanatory Memorandum on the Draft Bill provides:

> ". . . these requirements are aimed at ensuring that where funding is raised by one group company for purposes of another group company for productive purposes, no tax leakage arises. Where the funds are used within the group for non-income producing purposes, a deduction will not be allowed, and other specific provisions must be considered (ie, section 24O of the Act)."

All taxpayers that are claiming interest deductions but not carrying on a trade would be affected by the withdrawal of PN 31 if they do not qualify for the deduction in terms of the proposed section 11G.

The proposed section 11G is significantly more restrictive than the current position. As a result, once the changes enter into force, certain taxpayers will not be able to claim interest deductions where funds were borrowed to invest in interest-bearing instruments. Such taxpayers will be taxed on the gross amount of their interest income.

Following the public comments on the proposed section 11G, National Treasury (NT) accepted that the proposal is too restrictive and stated that it is not their intention to adversely affect business funding by the proposed withdrawal of PN 31 and that section 11G will be expanded. NT further noted that natural persons should not be excluded from entering into back-to-back arrangements to fund personal expenditure. In order to enable further consultation on the proposed section 11G, NT proposed that section 11G should only come into effect on 1 January 2025 (and no longer 1 January 2024, as stipulated in the Draft TLAB) in respect of years of assessments commencing on or after that date. PN 31 will remain effective until 1 January 2025.

Following the comments, the Taxation Laws Amendment Bill, 2023 (the 2023 TLAB), was published on 1 November 2023; in terms of the 2023 TLAB, the scope of section 11G is much wider. In particular, section 11G will apply to any person to the extent that the interest –

- is incurred in the production of interest that is included in the income of that person; and
- is not incurred in carrying on a trade.

Accordingly, the application of section 11G is not limited to companies, it does not have any capital requirements and it does not require a shareholding threshold to be met.

The proviso to section 11G proposed in the Draft TLAB (as noted above) still forms part of the 2023 TLAB, in terms of which unproductive interest cannot be deducted in terms of this section. This is in line with PN 31.

In addition, to allow for further dialogue with industry before the provision comes into force, the effective date for the introduction of section 11G has been pushed out to 1 January 2025 and it will apply in respect of years of assessment commencing on or after that date. Until such time, the proposed withdrawal of PN 31 will remain delayed.

The amendments to section 11G and the delayed implementation date are a welcomed respite for the taxpayer. However, it remains to be seen if any further changes are made to section 11G in the 2024 legislative cycle to restrict or widen the current proposed scope of section 11G.

"The 2023 draft Taxation Laws Amendment Bill (the Draft TLAB) containing the proposed amendments to the Act was released on 31 July 2023 and one of the proposed changes was the insertion of a new section 11G into the Act."

Magda Snyckers

ENSafrica

Acts and Bills

- Income Tax Act 58 of 1962: Sections 11G (proposed new section, to come into operation on 1 January 2025), 24J (emphasis on subsection (2)) & 24O;
- Taxation Laws Amendment Bill 36 of 2023 (introduced on 1 November 2023);
- Draft Taxation Laws Amendment Bill, 2023 (released on 31 July 2023).

Other documents

- Practice Note 31 of 1994 (*"Income Tax: Interest paid on moneys borrowed"* – 3 October 1994) (to remain effective until 1 January 2025);
- 2023 Budget Speech;
- Draft Explanatory Memorandum on the Draft Taxation Laws Amendment Bill, 2023 (published on 31 July 2023).

Tags: interest-bearing instruments; deduction of expenses; unproductive interest.

REMOTE WORKING AND PAYE OBLIGATIONS

It is no secret that the COVID-19 pandemic has radically changed our thinking towards how and where we work. Since 2020, many companies have adjusted and sometimes overhauled their working models to fit into the "new way of working" and meet the global demand for remote and hybrid work arrangements in order to stay competitive and retain the best talent.

One may be wondering how this new way of working will affect the collection of taxes by revenue authorities in various countries. In this article, a tax amendment that is being proposed by National Treasury and the South African Revenue Service (SARS) is briefly considered. It may have been inspired by this very question.

On 31 July 2023, National Treasury and SARS published the 2023 draft Taxation Laws Amendment Bill and draft Tax Administration Laws Amendment Bill (2023 Draft TALAB) (collectively referred to as the 2023 Draft Tax Bills) for comment, which was due on 31 August 2023. The 2023 Draft Tax Bills included some of the amendments proposed by the Minister in his Budget Speech in February 2023.

Among the main tax administration amendments that found their way from the Budget into the 2023 Draft TALAB was the proposal relating to the registration of non-resident employers for employees' tax. The proposal was to amend various provisions in the Income Tax Act, 1962 (the Act), to ensure that non-resident employers who pay remuneration to employees who render services in South Africa register as such in South Africa, notwithstanding the fact that they may not have a representative or agent in South Africa.

Since the 2023 Budget, SARS has not only issued the 2023 Draft Tax Bills for comment but has also held workshops with stakeholders to discuss any written comments that were submitted in response to the issue of the 2023 Draft Tax Bills. The workshops were held between 6 and 8 September 2023.

On 25 October 2023, National Treasury and SARS presented the draft response document on the 2023 Draft Tax Bills to the Standing Committee on Finance in Parliament. The draft response document (the 2023 Draft Response Document) contains a summary of the responses from National Treasury and SARS to the public comments received and proposed steps to be taken in addressing any key issues that may have been raised during the consultation process.

PROPOSED CHANGE

Paragraph 2 of the Fourth Schedule to the Act currently reads as follows:

> "(1) Every—
>
> *(a)* employer who is a resident; or
>
> *(b)* representative employer in the case of any employer who is not a resident...",

In the 2023 Draft TALAB, National Treasury proposed (amongst other things) that it be amended to read as follows:

> "(1) Every employer or representative employer..."

The draft memorandum on the objects of the 2023 Draft TALAB notes that the proposed change seeks to, amongst other things, remove the distinction between resident and non-resident employers by requiring any employer (resident or foreign) to deduct employees' tax (PAYE).

LEVELLING THE PLAYING FIELD

According to this draft memorandum, the proposed amendment has been inserted to level the playing field between resident and non-resident employers and ensure alignment with skills development levies and unemployment insurance contributions that are required to be paid by registered employers and which ultimately benefit South African employees.

If the amendment were to become effective in the form proposed in the 2023 Draft TALAB, the registration obligation in paragraph 15 of the Fourth Schedule to the Act could potentially also have applied to non-resident employers notwithstanding the fact that they may not be conducting any business in South Africa.

A question on everyone's mind is how this proposed amendment will affect remote workers, specifically people who reside in South Africa and render employment services (for which they earn remuneration) to employers situated outside of South Africa.

As a point of departure, it will be necessary to determine whether an employer-employee relationship exists between the remote worker and the person compensating the worker for services rendered.

In this context, an *employer* is defined in paragraph 1 of the Fourth Schedule as:

> "any person … who pays or is liable to pay to any person any amount by way of remuneration".

In turn, an *employee* is defined as:

> "*(a)* any person (other than a company) who receives any remuneration or to whom any remuneration accrues;
>
> *(b)* any person who receives any remuneration or to whom any remuneration accrues by reason of any services rendered by such person to or on behalf of a labour broker;
>
> *(c)* any labour broker;
>
> *(d)* any person or class or category of person whom the Minister of Finance by notice in the *Gazette* declares to be an employee for the purposes of this definition; or
>
> *(e)* any personal service provider."

From these definitions, it is clear that the compensation received for services rendered must constitute remuneration in order for the amount to be subject to employees' tax.

The term *"remuneration"* is widely defined in paragraph 1 of the Fourth Schedule to include any amount of income which is paid or is payable to any person by way of any salary, leave pay, wage, overtime pay, bonus, gratuity, commission, fee, emolument, pension, superannuation allowance, retiring allowance or stipend, whether in cash or otherwise and whether or not in respect of services rendered.

The definition in the Fourth Schedule further specifically includes items such as annuities, restraint of trade payments, fringe benefits, allowances and advances, amounts received from the vesting of equity instruments, dividends, etc.

The only amounts that are specifically excluded from the definition of "remuneration" are amounts paid or payable for services rendered or to be rendered by a person in the course of a trade carried on by them independently of the person by whom the amount is paid or payable and of the person to whom the services have been or are to be rendered. Therefore, independent contractors (including freelancers) should not be affected by the proposed amendment. Notwithstanding this, it may be prudent for independent contractors (including freelancers) to review their contractual agreements to ensure that the wording and substance is consistent with what is required for an independent contractor relationship.

Given the wide definition attributable to the term "remuneration" it will be important for individuals rendering services to non-resident persons to interrogate their working relationships and ensure compliance with the Act.

> "Among the main tax administration amendments that found their way from the Budget into the 2023 Draft TALAB was the proposal relating to the registration of non-resident employers for employees' tax."

CONSULTATIONS WITH SARS AND NATIONAL TREASURY

As noted above, on 8 September 2023 SARS and National Treasury held a workshop with stakeholders and other interested parties on the proposed amendment. Some of the relevant comments that were made during the workshop (and noted in the 2023 Draft Response Document) include:

a) the proposed amendment fails to include a "trigger clause" that would activate the obligation to withhold employees' tax;

b) the proposed amendment fails to indicate what the link to South Africa needs to be for a non-resident employer to be subject to the registration and withholding requirement in South Africa;

c) the proposed amendment is going to cause significant administrative costs for foreign employers where South Africa already has a provisional tax system that enables the collection of any taxes due from the relevant "employees"; and

d) SARS has no authority over offshore employers who may not have any business activity or presence in South Africa.

In response to the comments raised, SARS and National Treasury have, in the 2023 Draft Response Document, noted that changes will be made to the proposed amendment to require only non-resident employers conducting business through a permanent establishment in South Africa to withhold employees' tax. The trigger, as well as the link to South Africa, will therefore be a permanent establishment in South Africa. This proposed change should not only limit the obligation to register for PAYE for those non-resident employers that have business activities in South Africa, but it should also alleviate the administrative burden that comes with registering as an employer for PAYE purposes.

POTENTIAL IMPACT

The impact that this proposed amendment will have on the "new way of working" will only be revealed over time. However, it could discourage foreign employers from employing the services of South African residents, bearing in mind the administrative burden that is likely to accompany this proposed amendment. Notwithstanding this, National Treasury and SARS' proposed changes to the amendment, as found in the Taxation Laws Amendment Bill, 2023, are welcomed as they do alleviate this burden to a large extent. Whether SARS will be able to effectively administer the proposed amendment is also something that will become clearer over time.

Although the obligation to deduct PAYE rests on the employer, it is important to note that the income tax liability is ultimately for the account of the employee. If the proposed amendment comes into effect, it would thus be prudent for employees earning remuneration in South Africa to ensure compliance by their non-resident employers and payment of the correct amount of PAYE to SARS, to avoid the employees and employers from being prejudiced. Alternatively, employees should make use of the provisional tax system to ensure that they are complying with their tax obligations in South Africa.

Puleng Mothabeng

Cliffe Dekker Hofmeyr

Acts and Bills

- Income Tax Act 58 of 1962: Fourth Schedule: Paragraphs 1 (definitions of "employee", "employer" and "remuneration"), 2 & 15;
- Draft Taxation Laws Amendment Bill, 2023;
- Draft Tax Administration Laws Amendment Bill, 2023;
- Taxation Laws Amendment Bill 36 of 2023.

Other documents

- 2023 Draft Response Document (issued by National Treasury and SARS in response to comments by interested parties on the Draft Tax Administration Laws Amendment Bill, 2023);
- Draft Memorandum on the Objects of the Draft Tax Administration Laws Amendment Bill, 2023.

Tags: non-resident employers; unemployment insurance contributions; registered employers; remote workers; independent contractors.

CFCS WITH FOREIGN BUSINESS ESTABLISHMENTS

Proposed amendments to the tax laws, following the Coronation *SCA judgment would have made it very difficult for controlled foreign companies with foreign business establishments to outsource functions.*

National Treasury (NT) and SARS published the draft Taxation Laws Amendment Bill, 2023, for comment on 31 July 2023. The draft Bill proposed to amend the foreign business establishment (FBE) exemption for controlled foreign companies (CFCs) in section 9D of the Income Tax Act, 1962.

Section 9D contains certain anti-avoidance rules for CFCs which may result in a notional amount of a CFC's foreign income being taxed in the hands of its South African tax resident shareholders. A foreign company will be a CFC if, for example, more than 50% of the rights to participate in the shares of the company or voting rights in that company are directly or indirectly held by South African tax residents. The net income of a CFC is calculated as if the CFC were tax resident in South Africa, and such income is attributed to and taxed in the hands of its resident shareholders holding more than 10% of the CFC.

Two of the common exemptions relied on by CFCs to avoid attributing "net income" to their tax resident shareholders are the high-tax exemption and the FBE exemption.

- The high-tax exemption applies when, broadly, the CFC is subject to a total foreign tax of at least 67.5% of the normal tax that would have been payable had the CFC been a South African tax resident.

- The FBE exemption applies when, among other requirements, the CFC has a fixed place of business of sufficient substance, carries on business for at least a year, is suitably staffed, and has the necessary equipment and facilities to carry on the primary operations of the business.

THE PROPOSED AMENDMENT

The proposed amendment in the draft Bill requires CFCs of South African multinationals to, among others, be suitably staffed with employees and suitably equipped, and to have suitable facilities to "perform all the important functions of that business for which the controlled foreign company is compensated" to qualify as an FBE. (The current wording of the FBE exemption refers to "conduct the primary operations of that business").

PRACTICAL DIFFICULTIES ARISING FROM THE PROPOSED AMENDMENT

To understand how onerous the FBE exemption will become if the amendment were to be implemented as proposed, it is necessary to analyse the meaning of the phrase "important functions" in the context of the objective of the proposal in the draft explanatory memorandum (the draft EM) on the draft Bill. The draft EM provides background and reasons for the proposed change and examples when necessary.

The draft EM on the proposed amendment states:

> "It has come to the Government's attention that some taxpayers are retaining certain management functions but outsourcing other important functions for which the CFC is also being compensated by its clients."

As there is no definition of "important functions", the ordinary dictionary meaning of these words would apply. The functions of a business are the activities carried out by an enterprise and can be the core revenue-generating activities or support activities. The word "important" means of significance or value. The proposal means that no important functions of a CFC's business, which are revenue-generating (ie, compensated) may be outsourced to third parties, with the CFC employing people to manage the outsourcing. Alternatively, the CFC can still rely on the FBE exemption, but only if it outsources to a group entity located and tax resident in the same country as the CFC's fixed place of business.

"As the investment management functions were outsourced to group entities which were not tax resident in Ireland (where the CFC was tax resident), the taxpayer did not meet the requirements of the FBE exemption."

Here are some examples where the proposed amendments to the FBE exemption could be problematic.

- It is common for businesses to outsource their call centre needs. Is a call centre of a CFC, which is a selling, marketing and distribution subsidiary in the region, an important function for which the CFC is compensated? A call centre for enquiries on sales may be an important function, but what about a help desk? Does a help desk fall within the "all important functions …"? It is submitted that it does.
- What about the entire logistics chain of shipping and

customs clearance of goods to customers in the same country and also internationally? Without delivery of goods to customers, there is no completion of the sale. Therefore, delivery of goods is a vital function. Will a CFC need to have employees, equipment and suitable facilities to carry out the international logistics functions of its business in its entirety? Taken to the extreme, will CFCs now have to employ their own shipping and logistics staff if they intend to continue relying on the FBE exemption?

- What about an online retailer with a website and an app for sales? Can the retailer outsource the development and maintenance of its website and app to the best and most cost-efficient programmers globally? The proposed amendment compels the retailer to employ its own developers or contract with developers employed by another group entity living in the same country as the CFC's fixed place of business. This is contrary to the growing trend for developers and programmers to consult as remote workers globally.

- What if a CFC's sales and marketing strategy is to use social media influencers in multiple countries to generate interest and sales for its products? Is sales and marketing "an important function …"? The sales and marketing function is usually the core activity for which a business generates revenue. At what point can a CFC use services of a third party without such usage being seen to be "managing" an important function?

There are many commercial reasons why South African businesses may wish to outsource their business requirements to a foreign country rather than grow the business organically. Outsourcing to an experienced service provider with an existing network of local relationships will almost always be more cost-effective and time-efficient and less risky. Establishing and maintaining a footprint in foreign markets can be a very costly exercise for South African multinationals. Some businesses may also lend themselves more easily to outsourcing and this would be the norm in the industry globally.

PROBLEMATIC EFFECTIVE DATE OF PROPOSAL

The effective date of the proposal was also problematic and left no time for an SA multi-national group with CFCs to meet the new requirements if it wanted to continue to rely on the FBE exemption to avoid attributing income of the CFC to its South African tax resident shareholders.

The proposed amendment was to have come into operation on **1 January 2024** and would have applied to foreign tax years of CFCs ending on or after that date. This means that the proposal would have applied to all CFCs with financial years ending on or after 1 January 2024. CFCs with a financial year ending on 29 February 2024, 31 March 2024 or 30 June 2024 (which are common financial year-end dates) would already have been caught in the proposals.

WITHDRAWAL OF PROPOSAL BY NT PENDING CONSTITUTIONAL COURT JUDGMENT

In the 25 October 2023 presentation by NT and SARS to the Standing Committee on Finance in Parliament on the draft Bill it was explained that the above proposal would be postponed pending the Constitutional Court (Concourt) appeal of *Commissioner, South African Revenue Service v Coronation Investment Management SA (Pty) Ltd,* [2023] (the *Coronation* judgment). (The proposal therefore does not form part of the Taxation Laws Amendment Bill, 2023, introduced in the National Assembly on 1 November 2023.) In February 2023 the Supreme Court of Appeal (SCA) held in favour of SARS in the *Coronation* judgment that the primary operations of the CFC fund manager included investment management, administration and marketing. The taxpayer had argued that the CFC's primary operations were "the managed outsourcing of the investment management functions in accordance with the terms of the licence." As the investment management functions were outsourced to group entities which were not tax resident in Ireland (where the CFC was tax resident), the taxpayer did not meet the requirements of the FBE exemption.

It will be interesting to see what SARS and NT plan to do after the Concourt appeal decision. When courts have found in favour of the taxpayer in the past, SARS and NT have often changed the relevant tax rules in order not to reduce the tax base. Although the SCA had already found in favour of SARS in the *Coronation* judgment, NT and SARS still proposed changing the FBE exemption to make it overly broad. This is unfortunate as any uncertainty in tax rules adversely affects the competitiveness of South African multinationals operating outside South Africa.

Joon Chong

Webber Wentzel

Acts and Bills

- Income Tax Act 58 of 1962: Section 9D;
- Taxation Laws Amendment Bill 36 of 2023 (introduced on 1 November 2023);
- Draft Taxation Laws Amendment Bill, 2023 (published on 31 July 2023).

Other documents

- Draft Explanatory Memorandum on the Draft Taxation Laws Amendment Bill, 2023 (published on 31 July 2023).

Cases

- *Commissioner, South African Revenue Service v Coronation Investment Management SA (Pty) Ltd* (1269/2021) [2023] ZASCA 10 (7 Feb 2023); [2023] (3) SA 404 (SCA).

Tags: foreign business establishment (FBE); controlled foreign companies (CFCs); anti-avoidance rules; resident shareholders.

FOREIGN BUSINESS ESTABLISHMENTS

The current international tax hot topic is: does your controlled foreign company (CFC) have a foreign business establishment (FBE)?

To recap, if South African residents own more than 50% of a foreign company, then such foreign company is a CFC. In terms of our CFC rules the starting point is that the income from such CFC is taxed in the SA shareholders' hands even if no income/dividend/interest, etc, is paid by the CFC to the SA shareholder.

Fortunately, the above rule is not applicable if the CFC pays tax that is at least 67.5% of the tax that would have been paid had the CFC been an SA tax resident – the so-called high-tax exemption. Alternatively, it is also not applicable if all the income of the CFC is attributable to its FBE (there are of course exceptions to the FBE rule).

The reason for these two exemptions is clear: National Treasury (NT) would like South African companies to expand their business offshore and tax should not prohibit such expansion, provided such expansion is not a sham.

This article focuses on the issue of whether there is an FBE, or whether there can be more than one FBE.

Most times it is clear whether the requirements for an FBE have been met, but there are circumstances where the issues are not clear.

In essence, for there to be an FBE, there must be a fixed place of business in a country (not South Africa) that will be used for the carrying on of the business of the CFC where –

- that business is conducted through one or more structures;
- that fixed place of business is suitably staffed with employees of the CFC who conduct the primary operations of that business;
- that fixed place of business is suitably equipped for conducting the primary operations of that business;
- that fixed place of business has suitable facilities for conducting the primary operations of that business; and
- that fixed place of business is located outside South Africa, mainly for non-tax reasons.

The last point will be ignored and it is assumed that the fixed place of business is outside South Africa for non-tax reasons.

In determining whether there is a fixed place of business, a CFC (CFC1) may use the above-mentioned facilities, employees, and equipment of another group CFC, if that other group CFC is in the same country as CFC1.

CURRENT PROBLEMS

An issue which requires clarity is what happens if one outsources part of one's operations or, alternatively. if one has two FBEs in two different countries.

In February 2023, the first issue was dealt with in *Commissioner, South African Revenue Service v Coronation Investment Management SA (Pty) Ltd,* [2023] (*Coronation*), in which the Supreme Court of Appeal, per the facts, said the company, (CGFM, which was a CFC of Coronation) in Ireland, did not have an FBE as it had outsourced its primary operations.

Per the facts of the case, CGFM had outsourced its investment activities to another company in another country.

The court stated that on the facts:

> "I conclude that the primary operations of CGFM's business (and, therefore the business of the controlled foreign company as defined) is that of fund management which includes investment management. These are not conducted in Ireland."

Due to the above, CGFM did not have an FBE.

One can find sympathy for SARS in that, by all accounts, CGFM earned a significant amount of income and CGFM did not employ the staff or have the facilities to earn such income – arguably the intent of the FBE legislation.

It is said that tax of over R700m may be due to the fiscus by Coronation.

Not surprisingly, it is understood that the matter has been taken on appeal to the Constitutional Court.

In view of the ruling and ignoring the appeal, the rules seem clear that one cannot outsource the CFC's primary operations unless to another group CFC in the same country.

However, what happens if one has one's own staff, equipment, etc, in two different countries – can one then have two or more FBEs? The envisaged scenario is one where there are two (or more) different businesses of the company. Many examples come to mind, eg, a CFC may buy and then sell (two primary operations of that business), or it may buy, sell and deliver (three primary operations of that business), etc.

The above is not that unusual for a company and there are numerous examples of companies having branches in different countries performing different business operations.

From a policy perspective one would expect that if a CFC had, say, 100 people working at the head office in one country and another 80 at a branch in another country, SARS would not be concerned as legitimate operations are clearly being undertaken.

In terms of the high-tax exemption one would probably be fine, but what about the FBE exemption?

At face value the law seems to cater for two different FBEs. If one uses the buy / sell company and assumes that each business is equally important, then there could be a fixed place of business in two different countries.

Further, each fixed place of business would be suitably staffed and equipped to conduct the primary operation of that business (which is either buying or selling).

In terms of the law, arguably, the issue is not whether the fixed place of business is suitably staffed to conduct the primary operations of the CFC but whether it is suitably staffed to conduct the primary operations of that business.

If one argues that part of the business is to buy goods, then one simply needs to check if that fixed place of business meets the above requirements to conduct the primary operations of that business (the buying of goods).

A similar point is then raised for the other requirements of the FBE, ie, whether that fixed place of business (for the buying of goods) has the staff and is suitably equipped / has suitable facilities to conduct the primary operations of that business (the buying of goods). If the answer is yes, then, arguably, there is an FBE at that location.

In further support of the above, the specific section which prevents the income from the CFC from being attributed back to the shareholder asks: is the income attributable to any FBE of the CFC?

Such reference clearly takes into account the fact that there could be more than one FBE. There is a counterargument that one could have more than one FBE in the same country. Nevertheless, it would seem in terms of the Income Tax Act, 1962 (the Act), and one would think from a policy perspective, that such operations would be acceptable.

Unfortunately, if one returns to *Coronation*, the judge states (per the above comment) that the primary operations of CGFM's business is the business of the CFC as defined. From this statement it would seem that the full bench of the SCA, on the facts, is stating that the primary operations of the CFC (which is arguably not what the Act says as it says primary operations of **that** business) are the primary operations of the business.

From this comment it would not seem possible to argue that one can have two (or more) primary operations; this could not have been the original intention of the law – at least from a policy perspective.

THE UPDATED POLICY

Per the draft amendments which were released at the end of July 2023 in the draft Taxation Laws Amendment Bill, 2023, NT seems to be obsessed with taxpayers trying to dodge the rules and is losing the bigger picture of South Africans genuinely investing offshore and being competitive.

In essence the draft Bill sought to introduce legislation that in order for an FBE to exist the fixed place of business must be suitable equipped/staffed, etc, to perform all the important functions. It is submitted that such definition was too wide – the words "all the important functions" left too much uncertainty and would be too restrictive. Many "legitimate" CFCs would not have an FBE in terms of the draft Bill.

Fortunately, per the Taxation Laws Amendment Bill, 2023, introduced on 1 November 2023, that amendment has been removed. Unfortunately, the open caveat by NT is that the amendment is withdrawn pending the Constitutional Court judgment in the *Coronation* case.

One hopes the *Coronation* matter, which is said to have been set down to be heard in the Constitutional Court for December 2023, will be finalised as soon as possible – with a more favourable outcome than the initial draft Bill, or at least a ruling that may/may not directly assist the case but would not apply such a narrow interpretation as the draft Bill.

Hylton Cameron

BDO

Acts and Bills

- Taxation Laws Amendment Bill 36 of 2023 (introduced on 1 November 2023);
- Draft Taxation Laws Amendment Bill, 2023 (published on 31 July 2023);
- Income Tax Act 58 of 1962.

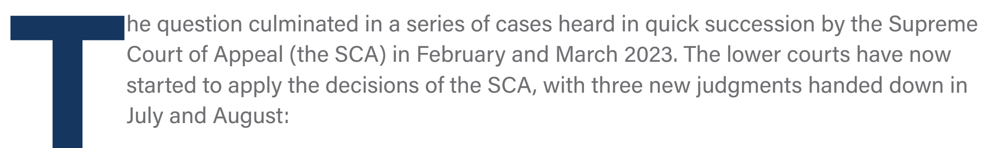
Cases

- *Commissioner, South African Revenue Service v Coronation Investment Management SA (Pty) Ltd* (1269/2021) [2023] ZASCA 10 (7 Feb 2023); [2023] (3) SA 404 (SCA).

Tags: controlled foreign company (CFC); foreign business establishment (FBE); high-tax exemption.

HIGH COURT'S JURISDICTION IN TAX DISPUTES

The interpretation of section 105 of the Tax Administration Act, 2011 (the TAA), and the role of the High Court in adjudicating disputes with SARS have become a matter of intense legal scrutiny.



The question culminated in a series of cases heard in quick succession by the Supreme Court of Appeal (the SCA) in February and March 2023. The lower courts have now started to apply the decisions of the SCA, with three new judgments handed down in July and August:

- *Trustees of the CC Share trust v Commissioner for the South African Revenue Service,* [2023] (*CC Share Trust*);
- *Erasmus v Commissioner for the South African Revenue Service,* [2023] (*Erasmus*);
- *Agenbach NO v Commissioner for the South African Revenue Service,* [2023] (*Agenbach*).

In all three cases, the taxpayer's application to engage the High Court's jurisdiction to review SARS' actions was dismissed, illustrating that the High Court's mantle in tax-related matters has all but dissipated. Unless, of course, the Constitutional Court intervenes.

BACKGROUND

Section 105 of the TAA compels taxpayers to use the framework under Chapter 9 of the TAA to dispute an assessment or a "decision" under section 104 "unless a High Court otherwise directs". Essentially, taxpayers must follow the appeal process that leads to the tax court, which serves as the default forum of first instance to hear tax disputes. Where a taxpayer wishes to engage a different forum (the High Court), it may only do so with a directive from that court under section 105.

Section 105 is cast in limited terms, which raises uncertainty as to its scope and substantive application:

- In terms of scope, it may be clear that a taxpayer must obtain a directive where they seek to challenge the merits of an assessment or a decision as defined under section 104 (a decision that is subject to objection and appeal). But it is not clear if this barrier applies where the taxpayer approaches the High Court to review SARS' exercise of public power as an organ of state, ie, the myriad of decisions taken by SARS that are not subject to an objection or appeal, which may lead to the **making** of an assessment.

- On substantive application, section 105 does not stipulate the criteria that must be satisfied to obtain a directive where the section applies.

Broadly, in the cases in question, the taxpayers argued that the scope of section 105 does not apply where the challenge is directed at the **making** of an assessment or a decision that is not subject to an objection or appeal. This will typically be the case where the taxpayer seeks to review a decision taken by SARS in its engagement with the taxpayer (be it in terms of the Promotion of Administrative Justice Act, 2000 (PAJA) or legality).

SARS' argument in the cases under consideration is that section 105 is absolute. According to SARS, the appeal process under Chapter 9 of the TAA constitutes a complete revision and rehearing of the dispute, including issues of an administrative nature. Implicitly, so SARS argues, the tax court is equipped to deal with judicial reviews; this means that the taxpayer **always** requires permission under section 105 to engage the High Court's jurisdiction directly.

To illustrate why the interpretation of section 105 warrants the attention of the Constitutional Court, it serves to first summarise the judgments handed down to date. This will be followed by an explanation of the issues that remain unanswered.

> "If it is accepted that the High Court must play second fiddle to the tax court, it implies that section 105 trumps the provisions of the Constitution that confer upon the High Court its inherent jurisdiction, not to mention the taxpayer's right to just administrative action and the right of access to courts."

SUMMARY OF CASES

Three of the cases heard by the SCA dealt specifically with the High Court's jurisdiction in the context of section 105 when a taxpayer seeks to review the making of an assessment. These cases are as follows, with the judgment in *ABSA* still pending:

- *United Manganese of Kalahari (Pty) Ltd v Commissioner for the South African Revenue Service,* [2023] (*UMK*);

- *Commissioner for the South African Revenue Service v Rappa Resources (Pty) Ltd,* [2023], (*Rappa*); and

- *ABSA Bank v Commissioner, SARS,* [2023] (*ABSA*).

A fourth case, *Commissioner for the South African Revenue Service and Another v Richards Bay Coal Terminal (Pty) Ltd,* [2023] (*RBCT*), addressed substantially the same question in the context of the tailor-made dispute process under the Customs and Excise Act, 1964.

In *Rappa* and *UMK*, the SCA upheld SARS' argument that a tax appeal under Chapter 9 is sufficiently wide to deal with each and every aspect of a dispute, meaning that a section 105 directive is mandatory even if the making of an assessment is at issue. At this point, it serves to note that the SCA took a different approach in *RBCT*, where the court relied on the Constitutional Court's decision in *Metcash Trading Limited v Commissioner, South African Revenue Service and Another,* [2000] (*Metcash*), to hold that the fact that a taxpayer has an internal appeal against a decision of SARS does not preclude the taxpayer from engaging the High Court's jurisdiction to review that decision. Compellingly, SARS' argument was dismissed as being at odds with the rule of law and various provisions of the Constitution.

In terms of substantive application, it was held in *Rappa* (and confirmed in *UMK*) that a directive under section 105 will only be issued in exceptional circumstances. The court in *Rappa* held that this standard emanates from the wording, context and purpose of section 105 and the historic amendments to this provision. The SCA referred to the High Court judgment in *ABSA* for further support in this regard, where Sutherland J (now DJP) too adopted this threshold.

Rappa's endorsement of the High Court judgment in *ABSA*, however, was selective. The High Court in *ABSA* qualified that exceptionality need not be exotic or rare or bizarre; it simply requires circumstances which sensibly justify an alternative route. Against this qualifier, it was held that a dispute on a point of law would satisfy the threshold of exceptionality. *Rappa* did not engage with this aspect of the High Court judgment in *ABSA*. Instead, it agreed that exceptionality must be shown and endorsed the exceptional circumstances test in *MV Ais Mamas Seatrans Maritime v Owners, MV Ais Mamas & another,* [2002] (*MV Ais*), which requires circumstances that are so out of the ordinary, unusual or uncommon, that they justify the court's intervention.

The latest string of judgments in the High Court accepted the SCA's decision in *Rappa* as being correct. Thus, in terms of scope, it was accepted that a section 105 directive is an absolute requirement. But these cases gain more prominence in the context of the substantive application of section 105, specifically in their rebuke of the High Court judgment in *ABSA*.

The judgments in *CC Share Trust, Erasmus* and *Agenbach* criticised the finding of the High Court in *ABSA* that a dispute on a point of law meets the exceptionality threshold. *CC Share Trust* held that Rappa effectively overturned the High Court's view in *ABSA* on this score, even though such dissent is not readily apparent upon reading the *Rappa* judgment.

Erasmus shed light on this question, as Sher J considered it prudent to comment extensively on the High Court judgment in *ABSA*:

- The High Court in *ABSA* referred to *Metcash* as a precedent for the position that the High Court has a discretion on whether it will compel taxpayers to exhaust their internal remedies where the dispute turns on a point of law.
- Sher J explained that the High Court in *ABSA* seemingly failed to appreciate that *Metcash* was expressed in relation to the power of the High Court to grant **declaratory** relief in tax-related matters and, crucially, *Metcash* was decided before the enactment of the TAA.
- It was further held that *Rappa's* endorsement of the exceptional circumstances test in *MV Ais* effectively overturned the High Court's finding that a point of law would suffice, since a point of law is not in itself extraordinary, uncommon or unusual.

The SCA's judgment in *ABSA* was delivered on 29 September 2023. The SCA briefly dealt with the scope of section 105, where it cited *Rappa* as the authority for the interpretation and application of this provision. The SCA then simply stated that the High Court recognised that it could only exercise its jurisdiction in exceptional circumstances, and it was noted that this approach was endorsed by the SCA in *Rappa.*

The SCA, however, did not address the issues raised in *CC Share Trust, Erasmus* and *Agenbach* regarding the High Court's views in *ABSA* on exceptionality, ie, that a point of law is sufficient. The SCA focused on the question whether the High Court correctly characterised the dispute as one involving a point of law only. The SCA held that the dispute did not turn solely on a question of law, and accordingly, no exceptional circumstances existed to justify a deviation from the default route. Based on this conclusion, it appears that a point of law would thus meet the exceptionality standard. But the SCA did not expressly state whether a question of law would <u>always</u> be sufficient.

In sum, based on the lower courts' application of *Rappa*, which was seemingly endorsed again in *ABSA*, a taxpayer always requires permission under the umbrella of section 105 to launch a review in the High Court. In doing so, it must make out a case of exceptionality, where a point of law may (but would not necessarily) pass muster.

ANALYSIS

On the scope of section 105, the implication of *Rappa* is that the tax court ousts the High Court's jurisdiction to deal with judicial reviews, which is problematic for several reasons:

- The SCA's finding that the tax court's wide powers of revision extend to the determination of the legality of an assessment is based on the decision in *Kommissaris van Binnelandse Inkomste v Transvaalse Suikerkorporasie,* [1987], which predates the Constitution and the TAA.
- The tax court is not clothed with similar status as the High Court. The latter draws its status from the Constitution and is affirmed in the Superior Courts Act, 2013. The tax court's omission from the ranks of the divisions of the High Court is not inadvertent:
    - Initially, the draft Tax Administration Bill, 2010 (the TAB), provided that a taxpayer may dispute an assessment under Chapter 9 in the tax court or in terms of a review application to the High Court.
    - On 21 May 2010, the Constitution Amendment Bill, 2010, and the Superior Courts Bill, 2010, were published. These Bills proposed that the tax court would become a Special Division of the High Court.
    - Based on the proposal contained in these Bills, the draft TAB was published for public comment. In terms of the amended draft of the TAB, clause 105 was changed to expressly provide that taxpayers may dispute an assessment under Chapter 9 in the tax court or by way of review application to the tax court. The accompanying Draft Memorandum on the Objects of the Tax Administration Bill, 2010, confirmed that this change is a product of the proposed elevated status of the tax court.

  - But when the Superior Courts Bill, 2011, was published, the tax court was excluded as a Division of the High Court.
  - In keeping with this change, when the TAA was promulgated, section 105 reverted to its original wording where review applications were reserved for the High Court only.

- The tax court's apparent lack of jurisdiction to adjudicate reviews in terms of PAJA and legality can be gleaned from the TAA itself. The tax court's jurisdiction to hear applications on procedural matters is circumscribed by section 117(3), which is confined to procedural matters provided for in the "rules". The Rules promulgated under the TAA do not cater for review applications. Similarly, the powers of the tax court under section 129 of the TAA do not extend to reviews either.
- Section 6(1) of PAJA requires that reviews under the said Act be brought in a "court" or "tribunal". The definitions of these terms under section 1 of PAJA do not include the tax court. Invariably it must follow that the tax court cannot hear reviews brought in terms of PAJA.
- If it is accepted that the High Court must play second fiddle to the tax court, it implies that section 105 trumps the provisions of the Constitution that confer upon the High Court its inherent jurisdiction, not to mention the taxpayer's right to just administrative action and the right of access to courts.
- It is difficult to accept that the legislature intended to upend these constitutional provisions purely by implication, as opposed to explicit enactment.

As to substantive application, it is unclear on what basis the exceptionality standard was adopted. This does not emanate from the wording of section 105. Apparently, according to *Rappa*, this is implicit in the language and purpose of section 105. But it serves to note that where the "exceptional circumstances" standard applies elsewhere in the TAA, it is imposed expressly, not implicitly. This threshold is confined to sections 104(5)*(a)*, 107(2)*(b)*, 113(13), 124(2), 145*(a)*(ii) and 218.

As a matter of course, this interpretation repudiates section 39(2) of the Constitution as it again curtails the taxpayer's right to just administrative action and the right of access to courts.

CONSTITUTIONAL CLARITY

Against these questions, it cannot be said that *Rappa* settled the law on section 105. And this is perhaps best revealed by the fact that the litigants in several of the cases in question clearly have their own reservations on the SCA's findings. The taxpayers in *Rappa* and *UMK* have filed applications for leave in the Constitutional Court to appeal their SCA judgments. These are in addition to the application filed in the same court by the taxpayer in *Forge Packaging (Pty) Ltd v Commissioner for the South African Revenue Service,* [2022], for leave to appeal the High Court's judgment on the same issue. SARS has also since filed its application to appeal the judgment in *RBCT*.

The proliferation of cases with the same jurisdictional question illustrates the imperative that the Constitutional Court speaks on the underlying issues. The taxpayer's right to just administrative action, the right of access to courts and the High Court's jurisdiction are invariably constitutional issues that engage the Constitutional Court's jurisdiction. The non-constitutional grounds are equally compelling. The substantive application of section 105 (which is now less certain) raises a question of law of general public importance; one which implicates the entire tax base.

"The SCA, however, did not address the issues raised in *CC Share Trust, Erasmus* and *Agenbach* regarding the High Court's views in *ABSA* on exceptionality, ie, that a point of law is sufficient."

Jean du Toit (reviewed by **Andries Myburgh**)

ENSafrica

Acts and Bills

- Tax Administration Act 28 of 2011: Chapter 9 (sections 101–150); Sections 104 (emphasis on subsection (5)*(a)*), 105, 107(2)*(b)*, 113(13), 117(3), 124(2), 129, 145*(a)*(ii) & 218;
- Constitution of the Republic of South Africa, 1996: Section 39(2);
- Promotion of Administrative Justice Act 3 of 2000: Sections 1 (definitions of "court" & "tribunal") & 6(1);
- Customs and Excise Act 91 of 1964;
- Superior Courts Bill 7 of 2011;
- Constitution Seventeenth Amendment Act of 2012;
- Superior Courts Act 10 of 2013;
- Draft Tax Administration Bill, 2010.

Other documents

- Draft Memorandum on the Objects of the Draft Tax Administration Bill, 2010;

Cases

- *Absa Bank Limited and Another v Commissioner for the South African Revenue Service* (2019/21825) [2021] ZAGPPHC 127; 2021 (3) SA 513 (GP) (11 March 2021);
- *Trustees of the CC Share Trust and Others v Commissioner for the South African Revenue Service* (38211/21) [2023] ZAGPPHC 597 (24 July 2023);
- *Erasmus v Commissioner for the South African Revenue Service* (9706/21) [2023] ZAWCHC 215 (18 August 2023);
- *Agenbach NO v Commissioner for the South African Revenue Service,* [2023];
- *United Manganese of Kalahari (Pty) Ltd v Commissioner for the South African Revenue Service* [2023] JDR 0863 (SCA); (1231/2021) [2023] ZASCA 29 (24 March 2023);
- *Commissioner for the South African Revenue Service v Rappa Resources (Pty) Ltd* (1205/2021) [2023] ZASCA 28; 2023 (4) SA 488 (SCA) (24 March 2023);
- *Commissioner for the South African Revenue Service v Absa Bank Limited and Another* (596/2021) [2023] ZASCA 125 (29 September 2023);
- *Commissioner for the South African Revenue Service and Another v Richards Bay Coal Terminal (Pty) Ltd* (1299/2021) [2023] ZASCA 39 (31 March 2023);
- *Metcash Trading Ltd v Commissioner, South African Revenue Service and Another* (CCT3/00) [2000] ZACC 21; [2001] (1) SA 1109 (CC);
- *MV Ais Mamas Seatrans Maritime v Owners, MV Ais Mamas, & Another* [2002] (6) SA 150 (C);
- *Kommissaris van Binnelandse Inkomste v Transvaalse Suikerkorporasie Bpk* [1987] (2) SA 123 (A);
- *Forge Packaging (Pty) Ltd v Commissioner for the South African Revenue Service* (21634/2021) [2022] ZAWCHC 119; 85 SATC 357 (13 June 2022).

Tags: High Court's jurisdiction; declaratory relief; exceptional circumstances.

REPATRIATION OF FOREIGN ASSETS TO SETTLE SA TAX DEBTS

On 24 July 2023 Angelo Agrizzi obtained a favourable judgment from the High Court in Pretoria in a unique tax dispute with the South African Revenue Service (SARS).

Following Agrizzi's evidence before the Zondo Commission ("Judicial Commission of Inquiry into Allegations of State Capture, Corruption and Fraud in the Public Sector including Organs of State"), SARS launched a tax inquiry into the whistle-blower's tax affairs following suspicions of fraud, money laundering, racketeering and tax evasion. Agrizzi was subsequently slapped with a tax bill of about R230 million, which SARS wanted to collect.

The court in *Commissioner for the South African Revenue Service v Angelo Agrizzi and Another,* [2023], had to decide on two applications that were brought before it.

The first was an application (the repatriation application) brought by SARS for the compulsory repatriation of foreign assets held by Agrizzi in Italy as contemplated in section 186(2) of the Tax Administration Act, 2011 (the TAA). In terms of the repatriation application, the Commissioner sought an order compelling the respondent to repatriate all his assets located outside of South Africa, specifically in Italy, in order to satisfy his outstanding tax debts.

The second application (the review application) was a counter-application to the repatriation application. The application was brought by Agrizzi in terms of which he sought an order reviewing SARS' decision to refuse his request for the suspension of his assessed outstanding tax liability in terms of section 164 of the TAA.

Given that this is potentially the first reported judgment dealing with the application of section 186 (repatriation applications), the discussion here has been limited to the court's interpretation and application of this provision.

BACKGROUND AND FACTS

Following the Zondo Commission, SARS launched a tax inquiry into the finances of the African Global Group of Companies (previously known as Bosasa) and various related individuals and companies. As a result of evidence that was led before the Zondo Commission, SARS was made aware of a large scheme of fraud, money laundering, racketeering and tax evasion involving Bosasa at a time when Agrizzi was the group's chief operating officer.

In terms of the tax inquiry held by SARS, SARS formed the view that Agrizzi had received "gross income" as defined in section 1(1) of the Income Tax Act, 1962, which he had failed to declare in his annual income tax returns.

As such, on 7 December 2020 SARS issued a letter of audit findings to Agrizzi and on 11 March 2021 SARS raised additional income tax assessments for the tax years 2006 to 2019. In terms of the assessments, it was determined that Agrizzi had underdeclared an amount of around R196 million in his taxable income and was liable to tax for an amount of about R230 million, which included normal income tax, understatement penalties (USP), provisional tax penalties and interest.

The due date for the payment of the full amount assessed, in terms of the notice of assessment issued, was 18 March 2021. Notwithstanding this, the parties agreed that the assessed amount could be paid in two instalments, with the first due date for payment being 1 April 2021 and the second 30 April 2021.

On 28 April 2021, Agrizzi delivered a request for extension for the delivery of his objection to the assessment. On the same day, Agrizzi also submitted a request for the suspension of payment of the debt as contemplated in section 164 of the TAA (two days prior to the second due date for payment).

The request for an extension was granted by SARS, including a subsequent request for extension that was made by Agrizzi.

However, SARS declined the request for the suspension of payment of the assessed amount and directed that payment be made within 10 business days from the date of the refusal.

"The court highlighted SARS' failure to join the NPA and the South African Reserve Bank to the proceedings as an impediment to granting the order sought by SARS."

Notwithstanding the refusal, on 13 August 2021, Agrizzi submitted his objection against the assessments. The objection was partially allowed by SARS on 9 February 2022, reducing the assessed amount from R230 million to R174 million.

In the midst of Agrizzi's tax woes, on 14 October 2020 he was arrested and charged with fraud and corruption. He applied for bail, which was granted on 30 October 2020. His bail was set to an amount equal to the value of his fixed property situated in Italy. As part of the bail conditions, Agrizzi was required to hand over the original title deed of the relevant property to the National Prosecuting Authority (NPA). Further, Agrizzi had to provide the NPA with a signed guarantee secured by the relevant property in terms of which Agrizzi would cede to the state all of his rights, title and interest in the property to be held as security pending the discharge of his obligations in terms of the bail conditions.

LEGAL CONSIDERATIONS: SECTION 186 OF THE TAA

Chapter 11 (sections 169 to 186) of the TAA deals with the recovery of tax. More specifically, Part F (section 186) deals with remedies in regard to foreign assets, and sets out the jurisdictional ambit within which an order for the repatriation of foreign assets may be sought.

In this context, section 186(2) allows a senior SARS official to apply to the High Court for an order compelling the taxpayer to repatriate assets located outside of South Africa in order to satisfy a tax debt owing to SARS.

The jurisdictional requirements that must be met before a senior SARS official may bring such an application are contained in subsection (1) of section 186, which states that –

- the taxpayer concerned must not have sufficient assets located in South Africa to satisfy the tax debt in full;

- the senior SARS official must believe that the taxpayer has assets outside of South Africa or has transferred assets outside of South Africa for no consideration or for a consideration less than the fair market value; and
- the assets outside South Africa may fully or partly satisfy the tax debt.

COURT'S FINDING

In relation to the repatriation application, it was SARS' submission that it had met the jurisdictional requirements for an order to be granted as contemplated in section 186(2). SARS noted that it was aware of assets situated in Italy which belonged to Agrizzi and which could be used to settle the outstanding tax debt or a portion thereof. Alternatively, SARS submitted that Agrizzi transferred assets outside of South Africa for no consideration or for a consideration less than market value.

In response to SARS' submissions Agrizzi raised three objections, namely:

1. There is no "tax debt" as defined. It was submitted on behalf of Agrizzi that a "tax debt" is "an amount of tax due or payable in terms of a tax Act" as contemplated in section 169(1) of the TAA. It was further submitted that an assessment is not "due and payable" until it is final. In this regard, it was noted that an assessment becomes "final" only if, among other things, no objection has been made.

   Agrizzi submitted that an objection to the assessments had been submitted, which was partially upheld by SARS. Agrizzi had also made his intention clear to appeal those parts of the objection that were not upheld. As such, Agrizzi was of the view that because he had not yet exhausted his internal right to appeal, the assessments could not be considered final and therefore no outstanding tax debt can be said to exist.

2. The application was not brought by a senior SARS official. The authority of the SARS official who deposed to the founding affidavit in the repatriation application was challenged by Agrizzi. It was submitted that SARS did not place sufficient evidence before the court of the relevant official's authority or seniority as required by the TAA.

3. The order sought in the repatriation application was legally impermissible as it would be contrary to Agrizzi's bail conditions. One of the assets specifically noted in SARS' notice of motion in the repatriation application was the property in Italy, which had already been ceded to the NPA as part of the bail conditions in the criminal proceedings.

The court did not agree with the first two objections raised by Agrizzi. In respect of the first ground of objection the court noted that as a point of departure, section 186(1) must be considered in the context of Chapter 11, which deals with the recovery of tax. The court also cautioned against ignoring the express wording used in section 186(1). In this regard, the court noted that section 186(1) expressly refers to an "outstanding tax debt" and not a "tax debt" as defined in section 169(1) of the TAA. The court, therefore, held that Agrizzi's reliance on the definition of a "tax debt" as contemplated in section 169(1) was misplaced in the circumstances.

The court held that the adjusted amount assessed was an outstanding tax debt required to be paid by the date noted in the notice of assessment (IT34) issued to Agrizzi (being 18 March 2021 before the partial allowance of the objection).

Notwithstanding the aforementioned, the court did agree that having regard to the bail conditions set in the criminal matter, the order sought by SARS was legally impermissible. The court highlighted SARS' failure to join the NPA and the South African Reserve Bank to the proceedings as an impediment to granting the order sought by SARS. In this context, the court noted that granting the compulsory repatriation order would significantly interfere

with the terms set for Agrizzi's bail. SARS' response in this regard was that Agrizzi should renegotiate his bail conditions with the NPA to allow for the order to be granted.

The court found this submission to be untenable and noted that the NPA's non-joinder to the proceedings had left the court to speculate as to what the attitude of the NPA might be to a request from Agrizzi to renegotiate his bail conditions should the repatriation order be granted. The court therefore held that having regard to the fact that Agrizzi's bail conditions precluded him from selling his property in Italy, the relief sought by SARS in the repatriation application was legally impossible. It was noted that not only would the order result in a variation of a material bail condition, it would also result in the arrest and incarceration of Agrizzi.

The court held that its finding in this regard was dispositive of the repatriation application and ultimately dismissed the application with costs.

CONCLUDING REMARKS

The court's judgment seems to draw a sharp distinction between what constitutes a "tax debt" and what constitutes an "outstanding tax debt", notwithstanding that the definition of an "outstanding tax debt" in section 1 of the TAA makes reference to a tax debt.

It is also interesting to note that even though the court found that SARS had met the jurisdictional requirements contained in section 186(2), the repatriation application was still refused on the basis that it would be legally impossible to repatriate one of the assets listed in SARS' notice of motion, namely the property situated in Italy. Other assets that were identified by SARS for repatriation included –

(i) a vehicle to the estimated value of R1,767,660;

(ii) funds held in a bank account in Italy with a value of R398,018.11;

(iii) cryptocurrency; and

(iv) funds held in Agrizzi's wife's bank account (who was joined as a second respondent) to the value of R10,968,696.30.

Puleng Mothabeng

Cliffe Dekker Hofmeyr

Acts and Bills

- Income Tax Act 58 of 1962: Section 1(1) (definition of "gross income");
- Tax Administration Act 28 of 2011: Sections 1 (definitions of "tax debt" & "outstanding tax debt") & 164 (review application); Chapter 11 (sections 169 to 186) (with emphasis on sections 169(1) & 186(2) (repatriation application).

Other documents

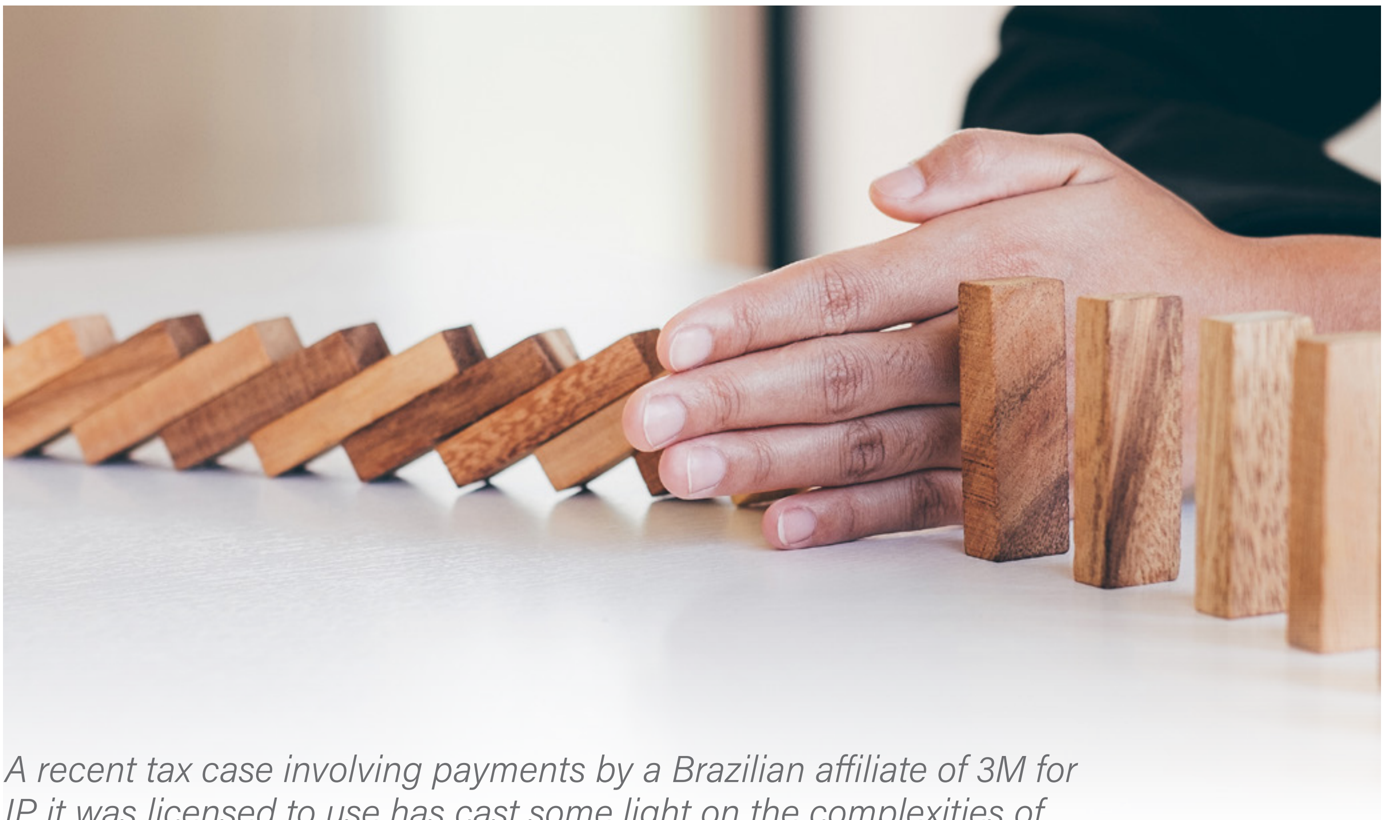
- Notice of assessment (IT34).

Cases

- *Commissioner for the South African Revenue Service v Angelo Agrizzi and Another* (45008/2021) [2023] ZAGPPHC 604; [2023] JDR 2844 (GP).

Tags: money laundering; tax evasion; understatement penalties (USP); provisional tax penalties; recovery of tax.

IMPACT OF GOVERNMENT INTERVENTIONS



A recent tax case involving payments by a Brazilian affiliate of 3M for IP it was licensed to use has cast some light on the complexities of determining an arm's length price for intra-group services.

Many companies operating in Africa are continually faced with both tax and non-tax restrictions which prohibit tax deductions for and payment of certain fees for services rendered and intellectual property (IP) licensed. Historically, ways to manage these restrictions have involved combining such payments into franchise-style arrangements, which fit into the non-tax regulations and allow a certain percentage of revenue to be extracted through the charge.

As African revenue authorities have become more sophisticated, these arrangements have been challenged. The authorities are challenging service arrangements which are typically priced using a cost-plus approach, even though the non-tax regulators continue to limit the payments that should be made to a specific percentage of revenue.

The OECD Transfer Pricing Guidelines for Multinational Enterprises and Tax Administrations – OECD 2022 recognise this challenge. Paragraph 1.152 states:

> "There are some circumstances in which a taxpayer will consider that an arm's length price must be adjusted to account for government interventions such as price controls (even price cuts), interest rate controls, controls over payments for services or management fees, controls over the payment of royalties, subsidies to particular sectors, exchange control, antidumping duties, or exchange rate policy."

"It is interesting that the Brazilian legal restrictions include both limits on technology-transfer payments and limits on patent royalties. The restrictions are not detailed enough to determine whether the specific restriction applying to 3M was publicly promulgated."

The question is how these adjustments should be considered when applying an arm's length test to a charge for services or IP made to a recipient based in a country which has such regulations. The key test should be whether payments of fees to a third party rendering the same services, or providing the same or similar IP, would be subject to the same restrictions. The OECD Transfer Pricing Guidelines endorse this view at paragraph 1.154:

> "As a general rule, where the government intervention applies equally to transactions between associated enterprises and transactions between independent enterprises (both in law and in fact), the approach to this problem where it occurs between associated enterprises should be the same for tax purposes as that adopted for transactions between independent enterprises."

Thus, if the restrictions apply equally to third-party transactions as well as to transactions between related parties, the restricted amount should be viewed as the arm's length position. This was tested in the case of *3M Company and Subsidiaries, Petitioner v. Commissioner of Internal Revenues, Respondent* 160 T.C. No 3 (9 February 2023); Docket No 5816-13 (*3M*) in the United States Tax Court.

This article examines the case and its impact on similar challenges found in Africa.

CASE SUMMARY AND COMMENTARY

3M owned IP and provided this through a licence arrangement to a Brazilian affiliate. The provision of the IP was governed by three trademark licences executed in 1998. Each licence concerned a separate set of trademarks. In accordance with the licences, the Brazilian affiliate paid a royalty to 3M equal to 1% of its sales of the trademarked products.

The Commissioner of the Internal Revenue Service (IRS) determined that the income of 3M should be increased under Internal Revenue Code (I.R.C.) section 482 (s 482) to an arm's-length rate of 6% of the sales, which arguably corresponded to the maximum amount that the Brazilian affiliate could have paid for the intellectual property in question under the laws of Brazil, less related expenses.

3M argued that this adjustment did not consider the effect of Brazil's legal restrictions, which limited the amount that the Brazilian affiliate could pay. The IRS maintained that the restrictions did not comply with I.R.C. s 482, which specifies the conditions to be met before such restrictions could be considered.

Unlike the OECD Transfer Pricing Guidelines, the rules in I.R.C. s 482 allow a foreign legal restriction to be taken into account in making allocations under s 482, if it meets the following seven requirements:

1. The restriction affected uncontrolled taxpayers under comparable circumstances for a comparable period of time;
2. the restriction was publicly promulgated;
3. the restriction was generally applicable to all similarly situated persons (both controlled and uncontrolled);
4. the restriction was not imposed as part of a commercial transaction between the taxpayer and the foreign government;
5. the taxpayer exhausted all remedies prescribed by foreign law or practice for obtaining a waiver of the restriction (other than remedies that would have a negligible prospect of success);
6. the restriction expressly prevented the payment or receipt, in any form, of all or part of the arm's-length amount; and
7. the taxpayer and related parties did not engage in any arrangement with controlled or uncontrolled parties that circumvented the restriction and did not materially violate it.

Both parties agreed that the fixed ceilings on the amounts payable as royalties for the licensing of patents, unpatented technology, and trademarks are Brazilian legal restrictions that apply only to payments made by a Brazilian company to a controlling foreign company. There was no evidence put forward to support the idea that the legal restrictions affected "an uncontrolled taxpayer under comparable circumstances for a comparable period of time." That meant the first and third requirements listed above were not met. This supports the guidance provided by the OECD, that in considering whether a restricted amount represents the arm's length amount, the restriction should apply equally to similar transactions between third parties and related parties.

Interestingly, the matter did not stop there. The parties also disagreed on the meaning of the term "publicly promulgated". The IRS maintained that to be publicly promulgated, a foreign legal restriction must be in writing. 3M disagreed and contended that a foreign legal restriction need not be in writing to be publicly promulgated. The court held that a foreign legal restriction is "publicly promulgated" only if the restriction is in writing. It stated the following:

> "Taking unwritten restrictions into account in determining section 482 allocations would foster disputes between taxpayers and the Internal Revenue Service as to the substance of unwritten rules made by foreign governments."

It is interesting that the Brazilian legal restrictions include both limits on technology-transfer payments and limits on patent royalties. The restrictions are not detailed enough to determine whether the specific restriction applying to 3M was publicly promulgated. The OECD Transfer Pricing Guidelines do not contain a similar requirement, but a taxpayer would need to prove that the restrictions apply equally to related-party and third-party arrangements, making some degree of general publication implicit.

This suggests that restrictions specific to the transaction need to be made public to meet the requirements. This could be an important precedent for dealing with non-tax regulators in Africa, where there are widely known general limitations affecting the amounts of cross-border payments of service fees or licence fees that can be made. The limitations also affect applications that need to be made for specific arrangements which would be available to the applicant but not necessarily available as comparable third-party evidence.

IMPACT OF THE CASE ON AFRICAN COUNTRIES

Within a group, there are usually certain centralised functions. These functions typically provide support activities for the benefit of all members of the group and, if they provide a commercial benefit to the recipient entities, they are charged for.

The OECD member countries have grappled with determining an arm's length position for the recovery of fees relating to such activities for years. The activities are far from the main operational activities of the group but require significant time and effort, often disproportionate to the charges levied. For instance, a group may provide several centralised activities, eg, finance, human resources, IT support, etc, all of which arguably require a separate benchmark to be undertaken to support that any charge for the service provided is at arm's length. This issue led to the OECD member countries adopting a simplified approach for supporting the arm's length charge for such non-core back-office support services without the need for comprehensive documentation support and benchmarking through comparable analyses. This simplified approach has been a welcome development for multinationals; however, most African revenue authorities have chosen not to adopt it. Why not?

Most African countries rely heavily on withholding taxes to protect their tax base. Services fees, which are often not subject to a withholding tax, present a significant risk to African revenue authorities and are generally perceived to be a profit-shifting practice. Comprehensive documentation and support are important to satisfy the tax authority that any such charge is commensurate with the benefit received from the service. Non-tax regulations also provide a layer of protection for the country, ensuring that the funds charged cannot flow freely. Sadly, many of the African countries have not aligned the tax treatment with the non-tax regulation. Even when a multinational can show evidence that the charge is at arm's length, the payment is still blocked by non-tax restrictions. This poses a real problem for a multinational.

To comply with home country transfer pricing rules, the service-providing entity is often faced with making a unilateral transfer pricing adjustment or accruing for an amount which will probably never be received.

From a tax perspective, this could be alleviated either through raising a bad debt provision against the charge levied but not received or by applying to have the matter resolved through the Mutual Agreement Procedure (MAP), to try and eradicate any risk of double taxation.

The *3M* case has helped to give some clarity on the application of the OECD Transfer Pricing Guidelines where regulatory restrictions impede the payment of certain fees. Such restrictions need to be public and apply consistently to both related-party arrangements as well as third-party arrangements.

The challenge arises when such restrictions only apply to transactions between related parties, which is the case in many African countries. How should multinationals deal with the risk of non-deductibility and/or non-payment? While using the MAP could resolve the double taxation issue that arises from non-deductibility, it is onerous, time-consuming and the outcome is not guaranteed. Nor does it resolve the non-payment issue.

Can the multinational entity providing the service build an argument that not charging the recipient entity for the service is arm's length? Could reliance be placed on the core subsidiary versus non-core subsidiary concept aired in both the *Chevron* case (*Chevron Australia Holdings Pty Ltd v Commissioner of Taxation* (No 4) [2015] FCA 1092) and the earlier *GE Electric* case (*General Electric Capital Canada Inc v The Queen,* 2009 TCC 563)? The fact that a subsidiary is strategically important and requires the support of the multinational's services, irrespective of whether the subsidiary can secure a tax deduction for a fee, or remit a fee, should not drive the commercial decision of whether or not to support that business. Commercially, the business, which is a core activity, will be fully supported, irrespective of whether a charge is made for such support.

The OECD Transfer Pricing Guidelines also offer some degree of support for this argument at Paragraph 1.155:

> ". . . it seems unlikely that an independent enterprise would willingly subject itself to a substantial risk of non-payment for products or services rendered by entering into an arrangement when severe government interventions already existed unless the profit projections or anticipated return from the independent enterprise's proposed business strategy are sufficient to yield it an acceptable rate of return notwithstanding the existence of the government intervention that may affect payment."

This suggests that an argument could be made that not charging service fees where support is rendered to a strategically important subsidiary is an arm's length arrangement. Provided that there are wider commercial reasons for supporting that entity and a return is generated from that entity to benefit the provider of the services (often the parent entity), the non-charging of the fees should be viewed as arm's length, both according to international precedent and the OECD Transfer Pricing Guidelines.

CONCLUSION

The *3M* case has provided some endorsement for the application of the OECD Transfer Pricing Guidelines when government restrictions impact the ability of an entity within a multinational enterprise to pay for certain group charges. Whether this assists multinational enterprises facing similar restrictions across Africa, remains to be seen. In many cases, such restrictions only apply in the context of a group. A more creative approach may be needed to protect both the recipient entity and the service-providing entity from double taxation as a result of restrictions on the tax deductibility of such payments as well as on the actual making of the payment.

Karen Miller

Webber Wentzel

Other documents

- The OECD Transfer Pricing Guidelines (*Transfer Pricing Guidelines for Multinational Enterprises and Tax Administrations – OECD* 2022]: Paragraphs 1.152 & 1.154 & 1.155;
- Internal Revenue Code (I.R.C.) section 482.

Cases

- *3M Company and Subsidiaries, Petitioner v. Commissioner of Internal Revenue, Respondent* 160 T.C. No 3; 9 February 2023; Docket No 5816-13;
- *Chevron Australia Holdings Pty Ltd v Commissioner of Taxation* (No 4) [2015] FCA 1092;
- *General Electric Capital Canada Inc v The Queen* [2009] TCC 563.

Tags: Internal Revenue Code (I.R.C.); OECD Transfer Pricing Guidelines; Mutual Agreement Procedure (MAP).

SPECIAL TRUSTS

While the provisions in the Income Tax Act, 1962 (the Act), that apply to ordinary trusts are often the subject of disputes in the tax court or of binding private rulings issued by the South African Revenue Service (SARS), the same cannot be said for special trusts.

The dispensation applicable to special trusts in the Act may apply in instances where a person is unable to look after their own affairs and where the special trust is then created for the benefit of such person. In Binding Private Ruling 384 (BPR 384), questions regarding the special trust dispensation were considered.

FACTS

The applicant in BPR 384 is a resident person with a disability who suffered a traumatic brain injury as a result of which he is unable to work, talk or maintain himself independently, but he is still able to make decisions. His wife takes care of his physical needs and manages his financial affairs under power of attorney. The co-applicant in BPR 384 is a special trust for the sole benefit and maintenance of the applicant for the duration of his lifetime, due to his mental and physical disabilities.

The secondary beneficiaries of the special trust are the applicant's spouse and children, who may only benefit as discretionary beneficiaries from the trust after the death of the applicant. The special trust formerly served as a family trust for the benefit of the applicant, his spouse and children, but it became a special trust pursuant to the trust deed being amended.

The applicant has a loan account against the special trust due to funds made available to the co-applicant. The applicant proposed ceding this loan account to the special trust with the objective of reducing the trust's liabilities and ensuring that more funds are available to take care of the applicant's maintenance needs during his lifetime should something happen to his wife.

RULING

Firstly, it is important to note that SARS' ruling is subject to the additional condition and assumption that the cession of the loan account does not result in an amount being transferred to the special trust which, for purposes of the applicant's maintenance, is excessive.

Pursuant to this, SARS ruled as follows:

- That the cession by the applicant of his loan account to the special trust does not constitute a donation in terms of section 54 of the Act.

- That the proceeds in respect of the cession of the loan account will be equal to the face value of the loan account, under paragraph 38 of the Eighth Schedule to the Act. Consequently, no capital gain or loss will be realised by the applicant from the cession of the loan account and paragraph 39 is not applicable.

ANALYSIS

SARS' finding that the cession of the loan account does not constitute a donation, is unsurprising. In Binding Private Ruling 309, the facts were similar and SARS ruled that where the primary beneficiary (who suffered from early onset dementia) intended to transfer an amount to a special trust to provide for her future upkeep and well-being, it did not constitute a donation in terms of section 54 of the Act. It is possible that SARS' view, in the case of BPR 384, was also that the cession of the loan account was not motivated by "pure liberality or disinterested benevolence" as the cession will only benefit the applicant during his lifetime. In *Estate Welch v Commissioner for the South African Revenue Service,* [2004], it was held that the definition of "donation" in section 55(1) of the Act was not synonymous with the common law concept of a donation, but that the legislature had not by the use of the word "gratuitous" in section 55(1) eliminated the element of "pure liberality or disinterested benevolence". The legislature did not intend to depart from the common law in this particular respect. In the context of BPR 384, it is also possible that the condition to which the ruling was subject, that the cession of the loan account does not result in the transfer of an amount that is excessive for purposes of the applicant's maintenance, played a role in SARS' decision.

In respect of the CGT issue, SARS' ruling on the application of paragraphs 38 and 39 of the Eighth Schedule, is sensible. These paragraphs were likely considered as the applicant, being a beneficiary of the special trust, is a connected person in relation to the trust. The purpose of these provisions is to prevent tax avoidance where assets are disposed of in the context of connected persons, by stating that disposals between connected persons –

- are deemed to take place for a consideration that is arm's length (if the consideration is less than an arm's length price) (see paragraph 38); and
- resulting in a capital loss, must be treated so that the capital loss is ring-fenced and can only be set off against capital gains realised as a result of disposals between the same connected persons.

Given that the consideration for the asset, the applicant's loan account against the trust, was equal to the face value of the loan, it is clear that no capital gain or capital loss arose as a result of the cession.

"Firstly, it is important to note that SARS' ruling is subject to the additional condition and assumption that the cession of the loan account does not result in an amount being transferred to the special trust which, for purposes of the applicant's maintenance, is excessive."

Louis Botha

Cliffe Dekker Hofmeyr

Acts and Bills

- Income Tax Act 58 of 1962: Sections 54 & 55(1) (definition of "donation"); Eighth Schedule: Paragraphs 38 and 39.

Other documents

- Binding Private Rulings 309 (*Disposal of an asset by a public benefit organisation*) (31 August 2018) & 384 (*Cession to special trust of the beneficiary's loan account*) (28 October 2022).

Cases

- *Estate Welch v Commissioner for the South African Revenue Service* [2004] 2 All SA 586 (SCA); 2005 (4) SA 173 (SCA).

Tags: secondary beneficiaries; connected persons; arm's length price; primary beneficiary.

IMPORTED VS ELECTRONIC SERVICES

The supply of most goods or services in South Africa is subject to value-added tax (VAT) at 15%.

Where cross-border services are involved, challenges can arise to establish whether the non-resident supplier is required to register for and charge VAT to the South African resident recipient, or whether the recipient purchaser is required to self-assess (reverse charge) VAT at 15% on imported services. This distinction is particularly relevant in the context of electronic services.

ELECTRONIC SERVICES

South Africa introduced electronic services legislation in June 2014 and significantly expanded the scope thereof with effect from 1 April 2019. In the context of electronic services, a non-resident supplier (who does not have any physical presence in South Africa) is regarded as carrying on a VAT "enterprise" in South Africa if it supplies "electronic services" as prescribed by the Minister of Finance by regulation, and at least two of the following circumstances are present (the "2/3 rule"):

- the recipient of the service is a South African resident;
- the payment for such services originates from a South African bank account; or
- the recipient has a business address, residential address or postal address in South Africa.

Subject to certain limited exclusions, the term "electronic services" is broadly defined in VAT Regulation 429 (published in *Government Gazette* 42316) to mean **any services** supplied by means of an electronic agent, electronic communication or the internet for any consideration. Section 23(1A) of the VAT Act requires that the non-resident supplier must register for VAT at the end of the month where the total value of its taxable supplies of electronic services has exceeded R1 million in any consecutive 12-month period.

Although not always easy to categorise, electronic services typically include services provided via digital marketplaces or other online platforms (eg, virtual transaction management or lead generation services), software licences, software-as-a-service arrangements, information technology services and online subscription services, among other things.

IMPORTED SERVICES

In contrast, any services (including electronic services) acquired by a South African resident recipient from a non-resident supplier are regarded to be "imported services" for VAT purposes to the extent that the services are used or consumed in South Africa for purposes other than for making taxable supplies. Generally, where the non-resident supplier is not registered for VAT, the recipient purchaser must account for and pay VAT at 15% to the South African Revenue Service (SARS) on the value of the imported services acquired for non-taxable use. A self-assessment in terms of section 7(1)*(c)* of the VAT Act is a final cost and no input tax or other deduction or adjustment is available to the recipient in respect thereof.

However, in terms of section 14(5)*(a)* of the VAT Act, the recipient is not required to pay VAT on imported services if the service is subject to VAT in terms of section 7(1)*(a)*, thus if the service is supplied by the non-resident supplier as a "vendor" (being a person who is registered or is required to be registered for VAT) in the course or furtherance of an "enterprise" (including an electronic enterprise) in South Africa. In this case, the non-resident supplier would be liable to declare and pay the VAT to SARS.

In essence, the recipient is left in the same net VAT position, as it would be able to claim an input tax deduction in respect of the taxable use portion of any actual VAT incurred while the non-taxable portion will remain a VAT cost, but the VAT reporting obligations are different. It is therefore critical to establish whether or not the non-resident supplier is required to register for VAT (for example, as an electronic services provider), as well as what the effective date of its VAT registration is.

COMPLEX VAT ANALYSIS

According to SARS' VAT Connect Issue 15 (published in December 2022), the recipient purchaser "may have to ask the supplier a few questions to establish if that person is liable to register for VAT or not". However, in practice, many challenges arise for the recipient purchaser to determine whether the non-resident supplier has a VAT registration obligation in South Africa.

Except for the contractual arrangements that would be known between the parties, the recipient may not be familiar with the supplier's (offshore) business operations and, furthermore, may not have the necessary technical resources to embark on a detailed VAT analysis in this regard. Even if the recipient is able to establish what the supplier's VAT position is, or to outsource such a determination at an additional cost, there is no legislative requirement for the recipient to ensure compliance by the supplier with its South African VAT obligations, nor is there any requirement upon the recipient to enforce such compliance. This could leave the South African recipient vulnerable from a VAT perspective.

ULTIMATE LIABILITY FOR THE VAT

A further important consideration is to determine which party is ultimately responsible for the VAT (and potentially late payment penalties and interest) in the event that the non-resident supplier belatedly registers for VAT on a retrospective basis. Section 67(1) of the VAT Act allows the non-resident supplier to recover the VAT from the South African recipient, unless a written agreement between the parties provides otherwise. This could result in double taxation for the South African recipient on any non-taxable use portion of the imported services where it has previously self-assessed VAT at 15% in this regard.

Given the absence of VAT legislation providing for an input tax or other adjustment to be made by the recipient purchaser, it is not enough for it to simply raise awareness of the South African electronic services legislation. A recipient purchaser of offshore electronic type services should carefully consider the relevant VAT and pricing clauses of its contractual arrangements with the non-resident supplier and ensure that it is satisfied as to which party is to bear the VAT cost.

"A self-assessment in terms of section 7(1)*(c)* of the VAT Act is a final cost and no input tax or other deduction or adjustment is available to the recipient in respect thereof."

Annelie Giles

ENSafrica

Acts and Bills

- Value-Added Tax Act 89 of 1991: Sections 1(1) (definitions of "electronic services" & "enterprise"), 7(1)*(a)* & *(c)*, 14(5)*(a)*, 23(1A) & 67(1).

Other documents

- VAT Regulation 429 (published in *Government Gazette* 42316): definition of "electronic services";
- SARS' VAT Connect Issue 15 (published in December 2022).

Tags: self-assess; electronic services; resident recipient; non-resident supplier; imported services; input tax deduction.

sait South African Institute of Taxation