Issue 80 | 2025
MARCH

South African Institute of Taxation

Unstructured CPD 150mins

TAX CHRONICLES MONTHLY

Official Journal for the South African Tax Professional

TAX ADMINISTRATION
HIGH COURT DECISION ON THE MEANING OF "BULK" IN THE MINERAL ROYALTY ACT

TAX ADMINISTRATION
PRESCRIPTION AND SETTLEMENT AGREEMENTS

DEDUCTIONS AND ALLOWANCES
INTEREST AND SIMILAR FINANCE CHARGES

CONTENTS

DEDUCTIONS AND ALLOWANCES

0785. Interest and similar finance charges 03

0786. Section 24O deduction of interest on share purchases 06

ESTATE DUTY

0787. The basics of situs assets 09

GENERAL

0788. Can SARS limit access to a taxpayer's premises when carrying out an inspection? 11

0789. SARS interest rates 14

TAX ADMINISTRATION

0790. Dispute procedures 16

0791. High Court decision on the meaning of "bulk" in the Mineral 18

ROYALTY ACT

0792. Prescription and settlement agreements 20

0793. SARS' rights to your retirement savings 24

VALUE-ADDED TAX

0794. Will expanding the list of zero-rated foodstuffs really benefit the poor? 27

INTEREST AND SIMILAR FINANCE CHARGES

In September 2024, SARS provided some long-awaited guidance on the meaning of the term "similar finance charges", in the form of a draft Interpretation Note (Draft IN). In this article, the Draft IN is unpacked to assist taxpayers in understanding how SARS is likely to interpret this definition going forward.

Commentary is also provided on a key tax court case (*ITC 76795* – judgment delivered on 13 January 2025), which dealt directly with this element of the "interest" definition, and which went in the taxpayer's favour. This judgment may be the source of some confusion, given that it directly contradicts significant elements of the SARS guidance set out in the Draft IN.

A BRIEF HISTORY OF THE "INTEREST'" DEFINITION

"Interest", for tax purposes, is deductible or taxable in terms of the rules set out in section 24J of the Income Tax Act, 1962 (the Act), generally on a yield-to-maturity basis over the period of the relevant financial instrument, such as a loan. Prior to 19 January 2017, "interest" was defined in section 24J(1) of the Act to include

> "...the gross amount of any interest or **related finance charges**, discount or premium payable or receivable in terms of or in respect of a financial arrangement ..." *(our emphasis)*.

While not a defined term, some clarity was provided on the term "related finance charges" in *Commissioner, South African Revenue Service v South African Custodial Services (Pty) Ltd* [2012] (SACS). [*Note*: Clarity was provided in the context of section 11(*b*A) of the Act (repealed wef 1 January 2012), and not section 24J – nonetheless, the same term was used in both of these sections and, in practice, the SCA's interpretation in this case was generally applied by taxpayers to "related finance charges" in the context of section 24J as well.] In this case, SACS (the taxpayer) had borrowed monies for the construction of a prison, and had sought to deduct as "interest" (in the form of "related finance charges") a number of additional fees incurred in relation to the borrowed monies:

- **Guarantee fees:** Paid to another company and to SACS' financial advisor during the bid phase for guarantees provided over and above the bank loans obtained;
- **Introduction fees:** Paid to a joint venture partner for a loan advanced to SACS;
- **Financial advisory fees:** Paid to SACS' financial advisor;

"An entire section of the Draft IN is dedicated to an analysis of raising fees (also called originating fees or front-end fees), generally paid to the lender or the person arranging the loan for the provision of the debt funding."

- **Margin fees:** Paid to SACS' financial advisor in respect of its negotiations for bank loans obtained;
- **Commitment fees:** Paid to the banks for the loans advanced;
- **Initial fees:** Paid to the banks for the loans advanced;
- **Administration fees:** Paid to the banks for the loans advanced; and
- **Legal fees:** Paid to SACS' attorneys.

In essence, these fees were all incurred by the taxpayer in order to obtain or maintain access to the debt advanced. "Related" in this instance was interpreted to mean bearing a "close connection to the obtaining of the loans". SACS was permitted by the judge to deduct these fees as "interest" for tax purposes, in that they constituted "related finance charges".

This list of fees in the above case also provided useful examples of the various types of fees incurred by taxpayers when obtaining project or business funding, which do not constitute pure interest. Another common fee is a raising or originating fee, often paid by the borrower to the lender in order to obtain access to the borrowed funds. This is dealt with in more detail below.

THE 2017 AMENDMENT – "SIMILAR FINANCE CHARGES"

With effect from 19 January 2017 [per section 45 of the Taxation Laws Amendment Act, 2016], the "interest" definition in section 24J of the Act was amended to replace the term "related finance charges" with the term "similar finance charges". While this may have seemed an innocuous amendment, in reality it had significant consequences. Taxpayers could no longer place reliance on the very helpful laundry list of fees seen to be included in the "interest" definition in terms of the SACS case.

Given the limited commentary from National Treasury that accompanied this amendment [clause 45 at page 90 of the Explanatory Memorandum on the Taxation Laws Amendment Bill 17B of , 2016, simply stated that this amendment was to clarify "… the policy position that this applies to finance charges of the same kind or nature."], taxpayers were essentially left to their own devices in interpreting the meaning of the word "similar" in this context. The Merriam-Webster dictionary defines "similar" to include "having characteristics in common", and "alike in substance or essentials". This definition, along with National Treasury's cursory comments, gave the impression that this was a very intentional ***narrowing*** of the definition of "interest" for tax purposes.

Due to the lack of guidance on the meaning of this new definition prior to *ITC 76795*, there has been little to no consistency in the treatment by taxpayers of these types of costs and fees.

THE DRAFT INTERPRETATION NOTE

On 27 September 2024, SARS broke its seven-year silence and published the Draft IN on "Meaning of 'similar finance charges'". The Draft IN is quite thorough in defining in detail various terms relating to financing and interest, and provides an illustrative example. Selected key elements have been ***highlighted*** below:

- In order for "similar finance charges" to fall within the "interest" definition for tax purposes, SARS makes it clear on page 7 of the Draft IN that these charges –

  > "…must have ***analogous or matching characteristics*** to that of 'interest'… there must be ***almost no difference in character*** between the finance charges and the interest incurred… the phrase 'similar finance charges' does not include all forms of costs associated with acquiring and executing a loan and ***should not be interpreted and applied too widely***" (our emphasis).

- An entire section of the Draft IN is dedicated to an analysis of raising fees (also called originating fees or front-end fees), generally paid to the lender or the person arranging the loan for the provision of the debt funding. SARS makes a very important distinction here between costs incurred in ***raising, obtaining, or gaining access to capital*** (funding), and costs incurred as ***payment for the use of that capital***. In SARS' view, costs incurred to raise, obtain, or gain access to capital ***cannot*** be seen to be similar to interest, the latter being incurred for the use of borrowed funds. The court in ITC 76795 did not agree with this line of reasoning (see below).

- If these types of fees do not fall within the definition of "interest" set out in section 24J, one is left to determine whether they may still be deductible in terms of section 11*(a)* of the Act, read with section 23*(g)*. A key challenge here, given that these fees are generally incurred in relation to establishing the "income-earning structure" of a taxpayer's business, is that they are more often than not seen to be capital in nature. Therefore, these fees might not be deductible in terms of section 11*(a)*. This means that the costs cannot be deducted at all for tax purposes.

While the Draft IN could not be expected to address every conceivable type of finance charge, it interestingly does not provide any meaningful examples of what, in SARS' view, would constitute "similar finance charges". That being said, it does provide some useful guidance and insights into how SARS may seek to determine the nature of such charges.

While each case will be determined on its own merits, facts and circumstances, SARS provides some useful questions to consider when determining whether a finance charge could be seen as being "similar" to interest are:

- Is the charge incurred in raising, obtaining, or gaining access to capital, or is it incurred for the ***use*** of that capital?
- Is the charge a once-off payment, or a recurring payment?
- Is the charge calculated with reference to the time value of money?
- Is the charge calculated on the total available capital, or the outstanding balance of capital actually owing to the lender?
- Is the charge a fixed amount or is it determined with reference to a percentage?

THE COURT CASE – *ITC 76795*

In a nutshell, the taxpayer in this case (a resident trust) incurred a significant amount of upfront raising fees on various loans used to refinance and improve commercial properties which it owned, which it sought to deduct as constituting "similar finance charges", and therefore "interest" in terms of section 24J(1) of the Act.

SARS argued, as it set out in the Draft IN, that these raising fees were not deductible, for reasons which included the following:

- Raising fees were incurred prior to the commencement of the loans, and interest can only be incurred once the loan facilities become effective. The court held that any timing differences between the incurral of interest and that of raising fees do not change the nature of the charges, and therefore this was not a "relevant dissimilarity".
- Raising fees were paid before the taxpayer had received the benefit of the loan, and therefore did not constitute compensation for the use of the monies borrowed. The court dismissed this argument, and held that the raising fees are "part and parcel of the compensation for the loan", and that, if the taxpayer had not paid the raising fees, there would be no loan at all.
- While the raising fees were determined as a percentage of the loan amount, they were not determined with reference to the time value of money, or to the outstanding loan balance. The court acknowledged that this was a dissimilarity, but held that it was not a relevant one, and that SARS was "elevating 'similarity' to 'sameness'". This is an important distinction which the court made throughout the judgment, making clear its view that "similar" does not amount to "sameness", or to being identical in every conceivable aspect.
- Raising fees amount to "consideration for arranging the loan and not for the use of the loan". The court held that raising fees did indeed amount to consideration for arrangement of the loan, and that without the raising fees, the loan itself would not exist. Rather than amounting to a dissimilarity, the court viewed this aspect as underlining "the close proximity or association between the raising fees and the loans and is indicative of a relevant similarity between the two".
- Finally, the raising fees were once-off payments, while the interest on the loans was paid periodically. The court dismissed this as being an irrelevant dissimilarity.

CONCLUSION

While the Draft IN and the guiding principles provided therein are certainly welcomed, the judgment in *ITC 76795* has thrown the proverbial cat among the pigeons, with the tax court ruling in direct opposition to a number of these guiding principles. It remains to be seen whether SARS will appeal the tax court's decision in *ITC 76795*. If nothing else, the publication of the Draft IN may indicate a renewed focus and scrutiny from SARS on the types of charges that taxpayers may seek to deduct under the guise of "interest".

Per the Draft IN, "similar finance charges" must display the same nature and characteristics as interest, and in SARS' words in paragraph 4.3 of the Draft IN, "there must be almost no difference in character between the finance charges and the interest incurred". This is certainly a narrow interpretation, and it is submitted that other finance charges incurred on financing arrangements are very rarely almost identical to pure interest in every aspect. The court in *ITC 76795* also disagreed with this interpretation, making it clear that "similar" does not mean "same" or "identical".

Given the potential plethora of fees involved in financing arrangements and the lack of consistency in the naming conventions of these fees, it is crucial that taxpayers apply their minds to each of these charges to determine their true nature. This will require reviewing the terms and conditions of financing agreements, and ensuring that adequate evidence is on hand to support the view that these charges are at least "similar" to interest. This task is made even more complex by the subjective nature of the tests provided in the Draft IN – it is a question of degree (how close, how similar), rather than being black and white. In light of *ITC 76795*, the message for now is to exercise caution in the treatment of non-interest finance charges.

Greg Boy & Graham Molyneux

Forvis Mazars in South Africa

Acts and Bills

- Income Tax Act 58 of 1962: Sections 11*(a)* & (*b*A) [paragraph (*b*A) was deleted wef 1 January 2012], 23*(g)* & 24J (more specifically subsection (1) – definition of "interest" (as amended by section 45 of Act 15 of 2016));
- Taxation Laws Amendment Act 15 of 2016: Section 45 (amending the definition of "interest" in section 24J of the Act to replace the term "related finance charges" with the term "similar finance charges");
- Taxation Laws Amendment Bill 17B of 2016: Clause 45.

Other documents:

- Draft Interpretation Note ("Meaning of 'similar finance charges'") issued on 27 September 2024: Paragraph 4.3;
- Explanatory Memorandum to the Taxation Laws Amendment Bill 17B of 2016 (Clause 45 at page 90).

Cases

- *Commissioner, South African Revenue Service v South African Custodial Services (Pty) Ltd* [2012] (1) SA 522 (SCA) (30 November 2011).

Tags: similar finance charges; income-earning structure; once-off payment; recurring payment; financing agreements.

SECTION 24O DEDUCTION OF INTEREST ON SHARE PURCHASES

INTRODUCTION

For interest expenditure to be deductible, whether in terms of section 11*(a)* or section 24J of the Income Tax Act, 1962 (the Act), the interest expenditure has to be incurred "in the production of income". That means that there must be a close connection between the expenditure and the income-earning operations of the taxpayer considering both the purpose of the expenditure and what it actually effects. It is also trite that shares produce dividend income for the shareholder. This means that, as dividend income is exempt from normal tax, interest incurred in financing share acquisitions is generally not deductible for taxpayers who do not hold shares as "trading stock".

INTRODUCTION OF SECTIONS 23K, 23N AND 24O

After various complex stratagems had been devised by taxpayers under the corporate rollover provisions, to nonetheless enable deductions of interest, sections 23K, 23N and 24O of the Act were introduced to discourage the use of multiple-step debt push-down structures. As will be pointed out below with a specific focus on section 24O, there is, however, still a modicum of uncertainty in certain instances on how these provisions are to be applied.

PURPOSE OF SECTION 24O

The aim of section 24O is to grant the purchaser company a deduction of interest incurred for the purpose of acquiring equity shares in a target "operating company" (or equity shares in the "controlling group company" (defined in section 1(1) of the Act) in relation to a target "operating company") without the purchaser having to use section 45 or 47 interest deduction strategies to acquire the underlying assets out of the target company.

THE EFFECT OF SECTION 24O

In essence, the application of section 24O(2) allows a purchaser company to deduct interest incurred for purposes of acquiring shares in an "operating company" (or "controlling group company" in relation to an "operating company") by deeming such interest on "qualifying debt" to be in the production of income and expended for the purposes of trade. However, the interest deduction limitations, such as section 23N, apply directly to section 24O in that the allowable deduction is limited to an amount calculated by applying the specific formula to the "adjusted taxable income" of the purchaser.

"It would be interesting to see whether an amendment will be made to section 24O going forward to address this anomaly and what form such amendment may take to close the unintended loophole without simultaneously producing unbusinesslike results."

DEFINITION OF AN "OPERATING COMPANY"

Section 24O(1) defines an "operating company" as a company of which at least 80% of the aggregate amounts received by or accrued to that company during a year of assessment constitutes income which is derived from a business carried on continuously by that company and in the course or furtherance of which goods or services are provided or rendered by that company for consideration.

CONDITIONS FOR DEEMING PROVISION IN SECTION 24O(2) TO APPLY

In order for the deeming provision in section 24O(2) to apply, the financing which gives rise to the interest in question must relate to an "acquisition transaction" as defined in subsection (1). An "acquisition transaction" is defined to mean any transaction in terms of which a purchaser company acquires an equity share in another company from a person that does not form part of the same group of companies as that purchaser company if that other company is an operating company on the date of acquisition of that share, and as a result of which, at the end of the day of that transaction, (i) that purchaser company is a controlling group company in relation to that other company, and (ii) both companies form part of the same "group of companies" as defined in section 41(1). (Similarly, acquiring the shares in a "controlling group company" which holds the requisite shares in an operating company also qualifies.) It should be noted that, after the acquisition, there must be a change in control in order to rely on section 24O of the Act. In other words, the section is not applicable to companies that already form part of the same group of companies.

INTEREST DEEMED IN THE PRODUCTION OF INCOME

Section 24O(2), however, provides that interest is deemed to be in the production of income where during any year of assessment the interest is incurred in respect of a debt used for financing an acquisition in terms of an "acquisition transaction" to the extent that (i) the purchaser held the equity shares in the operating company and (ii) the equity shares constituted a "qualifying interest" in an operating company at the end of the *purchaser's* year of assessment. Subsection (3), on the other hand, defines an equity share in a company to constitute a "qualifying interest" in an operating company where the equity share, on the date referred to in subsection (2), namely the purchaser's year-end, is held in a company that qualifies as an operating company "in its latest year of assessment" that ended prior to or on the date of the purchaser's year-end.

POSSIBLE LOOPHOLE IN SECTION 24O

This means that technically, on the wording of the section, it may be possible to incorporate a start-up company which commences operations and qualifies as an operating company on the acquisition date and at its own year-end, and ensure that the start-up company's year of assessment ends before or on the date of the purchaser company's year-end, thereby resulting in the shares held in the start-up "operating company" constituting a "qualifying interest" acquired in terms of an "acquisition transaction" at the date of the purchaser's year-end. All the requirements having been met, the interest so incurred would then be deductible. It follows that the wording used possibly creates an opportunity for schemes where section 24O is used to obtain interest deductions in the funding of start-ups.

EXPLANATORY MEMORANDUM

This loophole was pointed out in the Explanatory Memorandum on the Taxation Laws Amendment Bill, 2019, which states that the "special interest deduction is meant to provide for a deduction where interest-bearing debt is used to acquire shares in established companies with income-producing assets that already generate high levels of income", proposing that the loophole be closed in that "further clarification will be made in the definition of an 'acquisition transaction' in order to ensure that the company must have traded for at least one year prior to the date of acquisition." To date, however, no such amendment has been made.

COMMENTS AND RESPONSES

In the Final Response Document on the Taxation Laws Amendment Bill, 2018 and Tax Administration Laws Amendment Bill, 2018, National Treasury and SARS stated that "[i]t was never intended to grant a deduction for all share acquisitions and particularly, not start-ups." Although Government is not of the view that the current provisions allow for the special interest deduction in respect of "newly established companies that later qualify as operating companies", it is submitted that an argument can be made that the correct interpretation of section 24O nonetheless allows for the deduction provided that the requirements of the section are complied with in the manner outlined above, which accords with the Government's remark that "the practical application of these provisions will be further reviewed in the following legislative cycle to ensure that they are not abused." However, any such scheme will still be subject to the substance over form and general anti-avoidance rules.

POSSIBLE UNBUSINESSLIKE RESULTS AND EXAMPLE SCENARIO

The above notwithstanding, and if one accepts that the special interest deduction should indeed be disallowed in relation to the funding of start-ups, there are certain scenarios wherein amending the definition of an "operating company" to require it to have been in operation for more than one year (as proposed by the above Explanatory Memorandum) would have unbusinesslike results. This may explain why no amendment has been made to date to address the shortcoming identified. Consider the following example:

Company C is a holding company which holds the shares of both Company A and Company B, which are both operating companies and which are interdependent on each other for manufacturing their products. Both are large operating companies which have been successfully operating for many years. Company X wishes to acquire both Company A and Company B from Company C and wishes to consolidate their operations. For commercial reasons, Company X makes it a precondition for the acquisition that Company A and Company B are amalgamated into Company D under the guidance of the current shareholders, after which Company D will be acquired by Company X. In this scenario, the provision as it currently stands should allow for the special interest deduction in relation to the acquisition of Company D (as long as its year-end falls on or before that of Company X). However, amending the definition of "operating company" to require at least one year of operation would preclude Company X from claiming the special interest deduction for the first year. As there is essentially no practical difference from the perspective of the fiscus between the abovementioned approach and an approach where Company X purchases both Company A and Company B separately, it would not make sense for the special interest deduction to be allowed in one instance and not the other, and a disallowance in the prior instance would arguably go against the policy rationale underlying section 24O, as it would force Company X to revert to the very structuring mechanisms that section 24O was enacted to discourage.

FUTURE AMENDMENTS AND CONCLUSION

It would be interesting to see whether an amendment will be made to section 24O going forward to address this anomaly and what form such amendment may take to close the unintended loophole without simultaneously producing unbusinesslike results. For now, taxpayers should take note that, according to Government, the intention behind section 24O is not to allow for interest deductibility for the funding of start-ups, although a taxpayer could be forgiven for coming to the opposite conclusion on the ordinary meaning of the wording of section 24O.

In conclusion, while the current wording of section 24O does provide an opportunity for interest deductions in the acquisition of start-ups, it is clear that the legislative intent was to facilitate such deductions primarily for established, income-generating companies. The potential for misuse of this provision remains a concern, and it is incumbent upon the lawmakers to consider refining the statute both to clarify the intention and to prevent abuse. Taxpayers are advised to obtain professional tax advice in order to make efficient structuring decisions which do not fall foul of section 24O or the anti-avoidance provisions. As possible amendments are awaited, it is crucial for taxpayers to stay informed of the evolving developments of section 24O to ensure compliance and optimal tax planning.

Dewald Pieterse & Dr Hendri Herbst

WTS Renmere

Acts and Bills

- Income Tax Act 58 of 1962: Sections 1(1) (definition of "controlling group company"), 11*(a)*, 23K, 23N, 24J, 24O(1) (definitions of "acquisition transaction" & "operating company"), (2) & (3), 41(1) (definition of "group of companies"), 45 & 47.

Other documents:

- Explanatory Memorandum on the Taxation Laws Amendment Bill, 2019;
- Final Response Document on the Taxation Laws Amendment Bill, 2018 and Tax Administration Laws Amendment Bill, 2018.

Tags: in the production of income; trading stock; deduction of interest; operating company; controlling group company; qualifying debt; acquisition transaction; qualifying interest; special interest deduction.

THE BASICS OF SITUS ASSETS

As the saying goes, the only certain things in life are death and taxes... or in this case, death taxes (also known as estate duty or inheritance tax).

To minimise these types of tax, it is crucial that one has a plan in place. This article looks at how the situs rules play into death taxes, with a focus on South Africa.

WHAT ARE SITUS ASSETS?

"Situs" is a Latin word meaning "site" or "position". The situs of an asset is considered the place where the asset is located. For assets which have their "situs" in certain jurisdictions, estate duty or inheritance taxes are levied on such assets, in those jurisdictions, irrespective of whether the owner of the assets was a tax resident of that jurisdiction.

What does this mean in practice? It means that the country in which the asset is situated as well as the country in which one is tax resident could levy taxes on the same asset, resulting in double taxation.

THE SOUTH AFRICAN SITUS ASSET RULE

For South African estate duty purposes, estate duty is levied on all property of a person who is a South African tax resident, wherever it is situated. South Africa will therefore levy estate duty on its tax residents on a worldwide basis. But, that is not all, South Africa will also levy estate duty on the estates of non-residents on their South African-based assets at a rate of 20% or 25%, depending on the value of the assets. Moreover, other countries may also levy inheritance tax on one's assets even though one is a South African tax resident because those assets are situated in that country, for instance in the United Kingdom (the UK).

A VERY SIMPLE EXAMPLE:

Mr Xomolo is an unmarried ordinary resident in South Africa for tax purposes and his only asset is a fixed property situated in the UK, valued at R24 million (±GBP1 million). Mr Xomolo passes away and his asset is bequeathed to his only son (a South African tax resident individual) in terms of his will.

The UK will levy inheritance tax at a rate of 40% on the inheritance of the UK property because of its UK "situs", with an exemption of the first GBP 325 000, resulting in UK inheritance tax in the amount of GBP1 000 000 – GBP325 000 = GBP675 000 x 40% = GBP270 000.

Converted to ZAR = ±R6,48m. The South African Revenue Service (SARS) will also levy estate duty on the property because Mr Xomolo was ordinarily resident in South Africa (as required by the Estate Duty Act) at the date of his death as follows: R24m – R3,5m deduction = R20,5m x 20% = R4,1m.

In total, the death duties on the property would amount to a whopping R6,48m + R4,1m = R10,58m, which is almost half the value of the property. Mr Xomolo's heir might therefore have to sell the property in order to pay the tax on Mr Xomolo's death!

RELIEF: DOUBLE TAX AGREEMENTS

South Africa has entered into estate duty agreements (EDA) with Canada, Botswana, Lesotho, Eswatini, Sweden, the UK, the United States of America (the USA) and Zimbabwe to alleviate the double tax upon death.

In terms of the SA/UK EDA, immovable property may also be taxed in the country in which the property is situated. The EDA therefore does not provide relief from inheritance tax in the UK, so in essence, both countries have taxing rights to the same asset.

DOMESTIC RELIEF

Luckily, the Estate Duty Act, 1955, in South Africa provides for a credit for any foreign taxes paid up to the tax payable in South Africa. Therefore, as per the example, should Mr Xomolo's estate be liable for inheritance tax in the UK at a rate of 40%, the South African relief will allow for a credit of up to 20% from the South African estate duty. This means that the total death taxes on the property would be 40%, or looking at the numbers R6,48m, being the full 40% tax in the UK, with a credit for the full 20% in South Africa. At least the total tax is reduced from R10,58m to R6,48m.

One will note from the example that SARS will limit the deduction of foreign tax paid to the tax that would have been paid in South Africa. Since the tax in the UK is higher, the estate will be liable for the full 40% tax in the UK and receive a full credit for tax in South Africa. Even though the estate will be liable for the higher 40% inheritance tax rate, at least this mechanism prohibits double tax on the same asset.

WHO CLAIMS THE RELIEF?

It should be noted that the executor is the person responsible for claiming the foreign tax credit from SARS, thus it is imperative that the executor is aware of all the foreign assets that one owns, and of how they are taxed abroad on one's death. In this regard, double taxation agreements and other international tax treaties play an important role.

NON-RESIDENTS

It is important to note that if one has emigrated from South Africa, it does not mean that one will fall outside the ambit of South African estate duty, as one will still be subject to South African estate duty on one's South African movable and immovable assets as per the local legislation. It is crucial to understand that non-residents may be subject to estate duty on their South African situs assets even although the country where they are tax resident does not levy estate duty or inheritance taxes in terms of its local legislation.

Mauritius, for one, does not have estate duty or inheritance tax but should a Mauritian tax resident own assets in for instance the USA, the UK or even South Africa, they could be subject to estate duty or inheritance tax on these assets (assets located within these jurisdictions) when they die. For South African situs assets, this could result in non-resident estates being liable for estate duty in South Africa at a rate of 20% or 25% (on the value of the estate exceeding R30m), in the USA at a rate of 40% and in the UK at a rate of 40% (subject to the various primary abatements), with no tax credit available to them in terms of the local Mauritian legislation.

CONCLUSION

One should always ensure that one consults with a professional and keep one's executor in the loop about one's foreign assets. It is vital to include provisions for foreign situs assets in one's will because estate planning is key.

"South Africa has entered into estate duty agreements (EDA) with Canada, Botswana, Lesotho, Eswatini, Sweden, the UK, the United States of America (the USA) and Zimbabwe to alleviate the double tax upon death."

Regan van Rooy

Acts and Bills

- Estate Duty Act 45 of 1955.

Tags: inheritance tax; estate duty agreements (EDA); situs assets.

CAN SARS LIMIT ACCESS TO A TAXPAYER'S PREMISES WHEN CARRYING OUT AN INSPECTION?

Judgment was handed down in the case of Alliance Fuel (Pty) Ltd and Another v Commissioner for the South African Revenue Service *[2024] in the Johannesburg High Court on 15 October 2024.*

In this case the High Court had to determine if the South African Revenue Service (SARS) legally restricted access to the applicants' premises during an inspection.

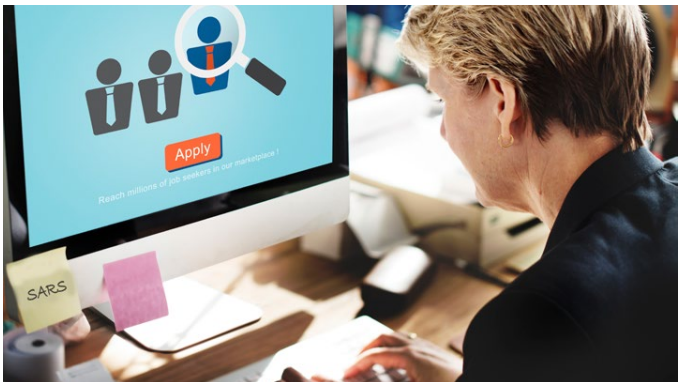
BACKGROUND

The applicants operated fuel facilities in Gauteng and Limpopo. SARS suspected the applicants of engaging in illegal fuel-blending activities involving the mixing of kerosene with diesel, and the sale thereof to the public. In principle, this practice is considered illegal because kerosene effectively attracts less tax than diesel, and by blending it with diesel and selling the mixture as "diesel", businesses profit while not properly accounting for the taxes.

SARS obtained search warrants to search the premises under section 88 of the Customs and Excise Act, 1964 (the C&E Act). These warrants allowed SARS officials to inspect the sites, seize records and equipment, and test fuel samples to confirm the alleged mixing. During the inspections, SARS detained multiple fuel storage tanks, tanker vehicles, laboratory equipment and electronic devices.

The search revealed several indications of illegal fuel blending, including the following:

"Females have longer life expectancies, for example, a female aged one has a life expectancy of 72,74, which is 7,37 years longer than her male counterpart of the same age."



- Laboratory equipment, including test kits for detecting chemical markers added to kerosene. The presence of these kits suggested that the applicants were removing the chemical markers from kerosene to disguise it as diesel.
- A filtration system using sand and activated charcoal, commonly used to remove markers from kerosene. The system also included pumps and flow meters, indicating large-scale blending operations. Field and laboratory tests showed that samples taken from storage tanks contained kerosene without its regulatory chemical markers, suggesting that blending and adulteration had occurred.
- Tests on fuel samples from tanks and tanker vehicles revealed the presence of kerosene mixed with diesel but without the expected chemical markers, a clear indication of tampering to avoid detection and evade fuel taxes.

During the investigation, access to these locations became a major point of contention.

SARS placed security personnel at the entrances of the facilities, restricting entry to essential personnel only. This measure prevented unrestricted access by the applicants' employees and representatives, particularly concerning the storage tanks and processing areas.

While SARS did not entirely prevent the applicants' employees from entering, they limited access strictly to instances deemed necessary. SARS argued that unrestricted entry would allow tampering with evidence or interference with the detained items, such as the adulterated fuel tanks and laboratory equipment.

The applicants applied to the High Court to have access restored.

ISSUES BEFORE THE COURT

Preliminary/Procedural issue

SARS argued that the applicants failed to comply with section 96 of the C&E Act, which requires advance notice before initiating legal proceedings. The applicants had sent notice only one hour before seeking court action, which SARS deemed inadequate.

Main issue

The applicants sought a court order on the grounds of spoliation, claiming that SARS had unlawfully deprived them of their peaceful possession of the premises. They argued that Inspacial Properties (Pty) Ltd, as the owner of the premises, had a lawful right to access, and Alliance Fuel claimed a right to access based on its operational presence at the sites.

The applicants argued that section 88 of the C&E Act only permits SARS to detain movable goods – such as the fuel tanks, laboratory equipment, and vehicles – but does not authorise it to effectively detain immovable property by restricting access to the entire premises.

The applicants contended that the warrants did not expressly authorise SARS to block access to the premises. They insisted that SARS was only entitled to remove detained goods from the premises and that the blocking of general access was both beyond the scope of the warrants and unauthorised by law.

COURT'S FINDINGS

The court ruled that the applicants' notice under section 96 was invalid, as it failed to provide the one-month advance period required, or sufficient justification for shorter notice. This failure undermined their legal standing to challenge SARS' actions. The court nevertheless proceeded to deal with the merits.

The court upheld SARS' authority to restrict access to the premises. Given the scale of the alleged illegal activities and the interconnected layout of the fuel tanks, restricting access was necessary to prevent tampering with evidence and interference with the detained items.

The court accepted SARS' argument that, due to the layout and complexity of the operations, detaining only the tanks and equipment without restricting access to the entire premises would have been ineffective. The court found that SARS' actions aligned with its duty to enforce customs and excise laws and prevent tax evasion.

The court found that the applicants failed to establish a clear right to unrestricted access. The contention that SARS was required to allow complete access was deemed unfounded given the evidence of extensive tampering and adulteration of fuel on-site.

The court therefore dismissed the spoliation application, validating SARS' right to control access under the circumstances. The applicants were denied unrestricted access, and the controlled access implemented by SARS remained in effect. Costs were reserved pending further considerations.

COMMENT

Section 88 of the C&E Act provides that:

- A SARS official, magistrate or member of the police force may detain any ship, vehicle, plant, material or goods at any place for the purpose of establishing whether it is liable to forfeiture under the Act.
- Any ship, vehicle, plant, material or goods may be detained where it is found or shall be removed and stored at a place of security determined by the official, magistrate or member of the police force, at the cost, risk and expense of the owner, importer, exporter, manufacturer or the person in whose possession or on whose premises they are found, as the case may be.
- No person shall remove any ship, vehicle, plant, material or goods from any place where it was detained or from the place of security.

If any ship, vehicle, plant, material or goods are liable to forfeiture under the Act, the SARS Commissioner may seize it.

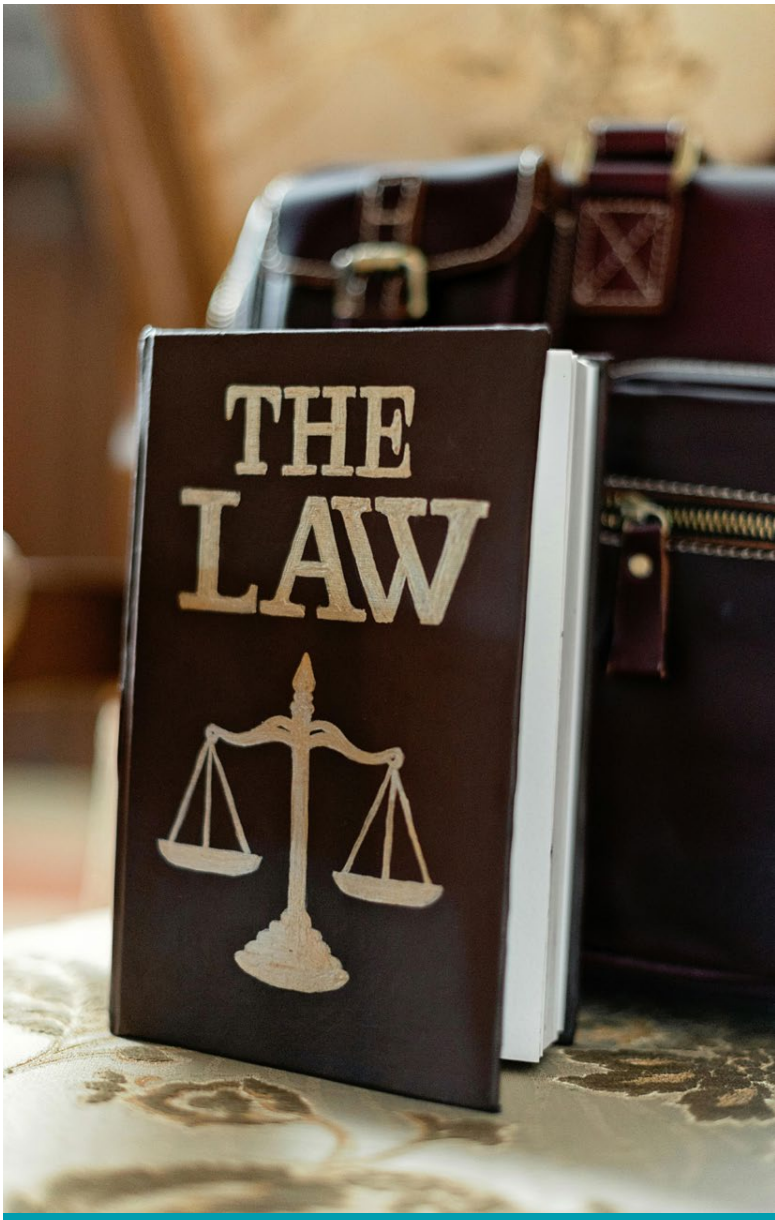
From the above, it appears that the section may only be relevant to movable goods as

- only ships, vehicles, plants, materials or goods are included;
- the common theme appears to be goods that can be removed (illegally) by any person or to a place of security by SARS; and
- the relevant goods are differentiated from the premises/ place.

However, section 4(12) of the C&E Act provides that an official may lock up, seal, mark, fasten or otherwise secure any warehouse, store, room, cabin, place, vessel, appliance, utensil, fitting, vehicle or goods if they have reason to believe that any contravention under the C&E Act has been or is likely to be committed in respect thereof or in connection therewith.

Whether section 88 is relevant or not, it appears that section 4 gives SARS the powers to lock up and/or seal any place in any event.

What could be interesting is whether a government institution in writing advises a subject of acts taken or to be taken, but using the incorrect section of the relevant legislation, whether administrative justice has been served or complied with in accordance with the Promotion of Administrative Justice Act 3 of 2000. It may be found that use of incorrect legislation can potentially not properly advise the subject of the criteria they are required to meet.



Heinrich Louw & Petr Erasmus

Cliffe Dekker Hofmeyr

Acts and Bills

- Customs and Excise Act 91 of 1964: Sections 4(12), 88 & 96;
- Promotion of Administrative Justice Act 3 of 2000.

Cases

- *Alliance Fuel (Pty) Ltd and Another v Commissioner for the South African Revenue Service* (2024/084746); [2024] ZAGPJHC 1044; 2024 JDR 4443 (GJ) (15 October 2024).

Tags: fuel-blending activities; illegal fuel blending; tax evasion.

SARS INTEREST RATES

TAX, VAT, FRINGE BENEFITS, LOANS, DONATIONS TAX AND DIVIDENDS TAX

It is important to remember that interest and penalties paid to SARS are not deductible expenses for income tax purposes. On the other hand, interest received from SARS is fully taxable (after deducting the current initial exemption of R23 800 per annum (R34 500 if you are 65 or older) for all local interest income earned by natural persons).

- **Income tax, provisional tax, dividends tax, etc**

  Payable to SARS on short payments of all such taxes (other than VAT): 11.25% per annum with effect from 1 March 2025 (was 11.5% per annum with effect from 1 January 2025).

  Payable by SARS on refunds of tax (where interest is applicable): 7.25% per annum with effect from 1 March 2025 (was 7.5% per annum with effect from 1 January 2025).

  If the refund is made after a successful tax appeal or where the appeal is conceded by SARS, the interest rate is 11.25% per annum with effect from 1 March 2025 (was 11.5% per annum with effect from 1 January 2025).

- **VAT**

  Payable to SARS on late payments: 11.25% per annum with effect from 1 March 2025 (was 11.5% per annum with effect from 1 January 2025).

  Payable by SARS on VAT refunds after prescribed period: 11.25% per annum with effect from 1 March 2025 (was 11.5% per annum with effect from 1 January 2025).

- **Fringe benefits**

  Official interest rate for loans to employees below which a deemed fringe benefit arises: 8.5% per annum with effect from 1 February 2025 (was 8.75% per annum with effect from 1 December 2024). See below for details of historical changes.

- **Dividends tax**

  Official interest rate for loans (designated in rands) to shareholders below which the interest on such loans can be deemed to be dividends on which dividends tax is payable: 8.5% per annum with effect from 1 February 2025 (was 8.75% per annum with effect from 1 December 2024). See below for details of historical changes.

- **Donations tax**

  Loans to trusts by connected natural persons with interest charged at rates below the official rate create a deemed donation subject to donations tax at 20% on the interest forgone each year.

- **Penalties**

  The amount of penalties for late payments (where applicable) are substantial (at least 10%) and are in addition to interest charged.

FRINGE BENEFITS, LOANS, DONATIONS TAX AND DIVIDENDS TAX – INTEREST RATES

- If inadequate interest is charged to an employee (including working directors) on loans (other than for the purpose of furthering their own studies) in excess of R3 000 from their employer (or associated institution), tax on the fringe benefit may be payable.

  Unless interest is charged at the "official" rate or greater, the employee is deemed to have received a taxable fringe benefit calculated as being the difference between the interest actually charged and the interest calculated at the "official" rate.

  For employees' tax purposes, the amount of the tax benefit must be calculated as accruing to the employee with reference to whenever interest is payable; if not regularly, then on a monthly basis for monthly paid employees, weekly for weekly paid employees, etc.

- Subject to a number of exceptions, distributions of income and capital gains from a company / close corporation are normally subject to dividends tax at the flat rate of 20%. Loans or advances to or for the benefit of a shareholder / member will be deemed to be dividends but only to the extent that interest is not charged on the loan at the "official" rate (or market-related rate in the case of foreign currency loans) and to the extent that fringe benefits tax is not payable on an interest-free (or subsidised-interest) loan where the shareholder is an employee.

  It is not the amount of the loan but the interest not charged which is deemed to be a dividend. Relevant low-interest loans are accordingly subject to dividends tax payable by the company and only in respect of the interest benefit.

"For employees' tax purposes, the amount of the tax benefit must be calculated as accruing to the employee with reference to whenever interest is payable."

- Loans to trusts by connected natural persons with interest charged below the official rate create a donation subject to donations tax at 20% (25% if cumulative lifetime donations of the donor amount to more than R30m) on the interest forgone each year.
- With effect from 1 March 2011, the official rate has been defined as the rate of interest equal to the South African "repo rate" plus 1%. For foreign currency loans, the rate is the equivalent of the foreign "repo rate" plus 1%. The South African repo rate currently stands at 7.5% per annum (with effect from 1 February 2025).

THE "OFFICIAL" RATE OF INTEREST OVER THE PAST FIVE YEARS

With effect from		*Rate per annum*
1 February 2020	–	7.25%
1 April 2020	–	6.25%
1 May 2020	–	5.25%
1 June 2020	–	4.75%
1 August 2020	–	4.50%
1 December 2021	–	4.75%
1 February 2022	–	5.00%
1 April 2022	–	5.25%
1 June 2022	–	5.75%
1 August 2022	–	6.50%
1 October 2022	–	7.25%
1 December 2022	–	8.00%
1 February 2023	–	8.25%
1 April 2023	–	8.75%
1 June 2023	–	9.25%
1 October 2024	–	9.00%
1 December 2024	–	8.75%
1 February 2025	–	8.50%

Kent Karro

Crowe

Tags: deductible expenses; connected natural persons; official rate; donations tax; taxable fringe benefit; low-interest loans; repo rate.

DISPUTE PROCEDURES

If any taxpayer has received a tax assessment (Assessment) from the South African Revenue Service (SARS) that did not align with the factual tax position or interpretation of the tax Acts, they are not alone. Many South Africans find themselves in this situation, facing what appears to be an impossible tax bill.

The Tax Administration Act, 2011 (the TAA), read together with the rules promulgated in terms of section 103 of the TAA (the Rules), govern the administration of tax laws in South Africa.

The good news? Options are available. If one disagrees with a SARS Assessment, one has the right to challenge it. It is easy to forget that the tax Acts protect the rights of taxpayers and that SARS does not hold all the power. Here is how an Assessment can be disputed:

REQUEST A SUSPENSION OF PAYMENT:

SARS has a "pay now, argue later" policy. This means SARS expects to be paid, notwithstanding that the tax liability is disputed. If one does not pay one's tax liability, even if one is going to object to the Assessment, SARS can take judgment and start execution proceedings. The "pay now, argue later" policy stems from the statutory obligation to pay tax. In order to make sure that SARS does not take judgment and execute against one's property, one needs to request a suspension of payment. This request, if accepted by SARS, suspends one's obligation to pay the assessed tax until one's dispute has been finalised.

SARS' debt collection arm and its audit arm do not necessarily liaise with each other. It follows that the suspension of payment and the dispute steps set out below need to occur simultaneously.

Ask for an explanation regarding the merits of the matter, if there is any uncertainty as to how SARS came to its Assessment:

- One can request SARS to provide reasons for its Assessment before an objection (dispute) is lodged.
- One has 30 business days after receiving the assessment to request reasons from SARS.
- SARS must respond and provide reasons within 45 business days, unless an extension is granted due to exceptional circumstances

OBJECT TO THE ASSESSMENT:

- After getting SARS' explanation (or if no reasons were requested), one has 80 business days to object to the Assessment. The objection is the most important dispute document as it sets out the grounds on which a taxpayer disagrees with SARS and generally the grounds cannot be changed. Taxpayers are strongly urged to approach tax practitioners to assist them in drafting the objection. The objection ought to be detailed, have evidence attached where applicable and set out the amounts which are in dispute. More importantly, it should also address penalties and interest, which in many cases is the biggest challenge.

- SARS must notify the taxpayer of an allowance (whether whole or partial) or a disallowance of the objection together with its reasons within 60 business days of the objection, unless it has asked for further information or documents. Should SARS not respond timeously, there are various avenues within which to finalise the matter at that stage.

APPEAL THE DECISION:

- If SARS does not agree with one's objection, its decision can be appealed. A notice of appeal must be submitted within **30 business days** of receiving the notice of disallowance of the objection.
- If one does want to appeal a disallowance, one first needs to determine to which forum one will be appealing. If the amount in dispute does not exceed R1 million, then one may appeal to the tax board. There is talk about increasing this amount to R5 million; however, at present any amount in dispute which exceeds R1 million may be appealed to the tax court.
- In the notice of appeal one may indicate that one is willing to participate in alternative dispute resolution (ADR) proceedings. If SARS is of the view that the matter is capable of being resolved through ADR, the matter will be referred to ADR and the appeal process will be pended.
- If the matter is not resolved through ADR or not capable of being resolved through ADR, it will be referred to either the tax board or tax court, depending on the amount in dispute.
- If one is unhappy with the outcome of the appeal to the tax board or tax court, one may appeal to the full bench of the High Court, or directly to the Supreme Court of Appeal.

WHAT IF A DEADLINE IS MISSED?

It may happen that a deadline is missed. One should not panic! In some cases, SARS may grant extensions if it is satisfied that there are reasonable grounds for such a request:

For requesting reasons: up to 45 business days. After that, a SARS official does not have any discretion to provide any further extensions.

For filing an objection: up to 30 business days (or for a longer period in special cases where there are exceptional circumstances which are beyond the control of the taxpayer). A SARS official cannot extend the objection period if three years have elapsed since the date of the Assessment.

For appealing a decision: up to 21 business days (or up to 45 business days in exceptional circumstances).

One must remember that these extensions are not guaranteed. It is always best to act within the original deadlines if possible.

WHY THIS MATTERS

Understanding these timelines is crucial for protecting one's rights as a taxpayer. By acting promptly and within these deadlines, the taxpayer has the best chance of resolving any disputes with SARS fairly.

Dealing with tax matters can be complicated and qualified tax practitioners should be in a position to provide taxpayers with the right assistance to help ensure that the right steps are being taken within the correct time frames.

"The Tax Administration Act, 2011 (the TAA), read together with the rules promulgated in terms of section 103 of the TAA (the Rules), govern the administration of tax laws in South Africa."

Daniel Robb

Shepstone & Wylie

Acts and Bills

- Tax Administration Act 28 of 2011: Section 103.

Other documents

- Rules for dispute resolution in terms of section 103 of the Tax Administration Act.

Tags: tax assessment; "pay now, argue later" policy; tax liability; notice of appeal; alternative dispute resolution (ADR) proceedings; deadline; correct time frames.

HIGH COURT DECISION ON THE MEANING OF "BULK" IN THE MINERAL ROYALTY ACT

In the landmark decision of *ASPASA NPC and Others v Commissioner for the South African Revenue Service* [2024] (ASPASA) the Pretoria High Court, on 6 December 2024, addressed a variety of procedural challenges raised by the Commissioner for the South African Revenue Service (SARS) but also provided essential clarifications on two key legal issues: the High Court's directive under section 105 of the Tax Administration Act, 2011 (the TAA), and the interpretation of the specified condition "bulk" in respect of aggregates in Schedule 2 to the Mineral and Petroleum Resources Royalty Act, 2008 (the Mineral Royalty Act). These aspects have far-reaching implications for taxpayers in general and the aggregates industry specifically.

HIGH COURT REJECTS SARS' PROCEDURAL TACTICS

SARS employed a multifaceted procedural strategy (no less than six preliminary and procedural grounds of defence) to obstruct the applicants from approaching the High Court on the merits of the case, namely a statutory interpretation matter in order to ensure their compliance with the Mineral Royalty Act. Despite these tactics, SARS itself had requested a special allocation from the Deputy Judge President of the Gauteng High Court, emphasising the urgent need for clarity on the interpretation of "bulk" to address the industry-wide concerns under the Mineral Royalty Act. The High Court categorically refuted SARS' procedural objections as deemed disingenuous, noting that its arguments focused on procedural barriers, despite its acknowledgement of the broader significance of resolving the legal standoff between it and the aggregates industry.

JURISDICTION

One of those procedural barriers raised by SARS was section 105 of the TAA, which generally restricts tax disputes to the tax court unless the High Court directs otherwise. The provision aims to streamline tax litigation and ensure that disputes primarily follow the administrative remedies established in the TAA. However, the court identified appropriate or exceptional circumstances in this case that warranted deviation from the default position. These included:

- The purely legal nature of the issue;
- The widespread implications for the aggregates industry; and
- The inability of the tax court to issue an industry-binding declaratory order.

The court highlighted the efficiency and certainty provided by a single High Court decision rather than a series of tax court decisions, each binding the immediate parties. By granting the section 105 directive, the court reinforced the role of the High Court in addressing legal questions in "tax matters" of significant public interest and industry-wide relevance.

This sets an important precedent for taxpayers seeking declaratory relief from the High Court in order to obtain clarity and certainty on statutory interpretation issues. The court's decision comes amidst a growing body of cases challenging the scope of section 105 of the TAA. Taxpayers should not be dismayed by the recent string of Supreme Court of Appeal cases barring the High Court from considering pure legal issues, as this judgment reaffirms the High Court's vital role in addressing legal issues in tax matters. Several pending judgments in the Constitutional Court are poised to be seminal in shaping taxpayer rights and the boundaries of the High Court's inherent jurisdiction in tax matters.

INTERPRETATION OF THE CONDITION "BULK" AND THE PURPOSE OF THE MINERAL ROYALTY ACT

The interpretation and the meaning of the condition of "bulk" in Schedule 2 to the Mineral Royalty Act as it relates to aggregates was the crux of the dispute. SARS argued that "bulk" referred to aggregates at any stage, including post-beneficiation. In contrast, the applicants contended that "bulk" should be interpreted as the state of aggregates in their unprocessed form, at the "muck pile" (ie, the unprocessed condition immediately after extraction).

The court adopted a purposive approach, analysing the text, context, and purpose of the Mineral Royalty Act. The court noted that "bulk" in the context of the Mineral Royalty Act carries a technical meaning aligned with the industry's understanding, rather than the meaning in common parlance. In upholding the applicants' interpretation, the court concluded that the condition "bulk" in Schedule 2 means the shot rock (ie, blasted rock) at the quarry face prior to any beneficiation. Thus, aggregates at the muck pile are in the condition stipulated by Schedule 2 as it is commercially viable at the mine mouth, reinforcing that royalties must be levied at the condition of the first saleable point.

The Mineral Royalty Act, as the court observed, serves two fundamental purposes, firstly, promoting beneficiation rather than penalising it and, secondly, ensuring fair compensation to the State for the extraction of mineral resources. These dual objectives underscore the critical role of mineral royalties in balancing economic activity with national interests. The court rejected SARS' interpretation as it effectively nullified section 6(2)*(b)* of the Mineral Royalty Act, which accounts for changes in mineral condition post-beneficiation. The SARS approach, the court reasoned, would discourage beneficiation, impose disproportionate royalties through the increased value through the process of beneficiation, and is inherently discriminatory because, to determine a royalty based on an increased value, would be to penalise aggregates in a manner in which mineral bearing ore is not penalised. This results in absurd outcomes detrimental to the aggregates industry and the broader economy.

The court's analysis resonates beyond the aggregates industry, as the interpretational principles outlined could influence disputes in other mining royalty matters. Mining taxpayers, even those outside the aggregates industry, should take heed of the court's emphasis on the purpose of the Mineral Royalty Act not to penalise but rather promote beneficiation and its implications for tax obligations in the mining sector.

STRIKE-OUT APPLICATION AGAINST SARS' ALLEGATIONS AND TREATMENT OF TAXPAYERS

The High Court's judgment also granted the applicants' strike-out application against SARS where the judgment was particularly scathing, addressing SARS' conduct in the litigation. The court noted with regret that the statements made by SARS in its answering affidavit were intemperate, disproportionate, and reflective of an inappropriate hostility toward taxpayers. These included baseless accusations that the applicants were abusing court processes, involved in a stratagem, lacked *bona fides* and were engaged in conduct described as "at best opportunistic and at worst trying to mislead the court". This is especially troubling given SARS' role as an "important and powerful organ of state", expected to uphold fairness and impartiality in its dealings with taxpayers.

The court highlighted that the applicants had approached it not to undermine SARS, but to ensure compliance with the Mineral Royalty Act and clarify statutory ambiguities that directly impacted their mineral royalty obligations. The court further reasoned that allowing SARS to use such an intemperate tone against taxpayers, who are compelled to maintain ongoing interactions with SARS by submitting to assessments, would unfairly tip the scales and necessitate intervention to "level" "the playing fields". The court's disapproval was heightened by the fact that SARS had previously issued a non-binding written opinion to the fourth to eleventh applicants, explicitly agreeing with their interpretation of the Mineral Royalty Act, as adopted by the applicants in this case. Despite this, SARS adopted a hostile and contradictory stance, opposing the applicants' reasonable and lawful application. Such conduct, the court emphasised, is not befitting of a public authority tasked with administering the tax law fairly and respectfully.

In granting the strike-out application with costs on a punitive scale, the court sent a clear message that taxpayers are entitled to be treated with respect and professionalism, particularly in matters of pure statutory interpretation. SARS' regrettable approach in this case stands as a cautionary tale, reminding all state organs of their obligation to act with decorum and fairness in all interactions with taxpayers.

SIGNIFICANCE OF DECLARATORY ORDERS BEYOND THIS CASE

The court emphasised that declaratory orders in the High Court provide faster resolutions than the tax court and carry binding authority, promoting legal certainty. Rather than fostering litigation, declaratory orders in the High Court avert a multitude of tax court litigation by clarifying legal interpretations, thereby reducing the volume of cases reaching the tax court. The court noted that it is more appropriate for the High Court to adjudicate such cases, as its binding authority prevents inconsistent rulings and unnecessary tax court disputes, ultimately serving the interests of justice and ensuring efficient resolution of legal interpretational issues. This approach benefits not only taxpayers but also SARS by streamlining the interpretation of contentious legal provisions. In doing so, declaratory orders advance judicial efficiency while protecting the integrity of tax administration.

CONCLUSION

The High Court's decision in *ASPASA* is a landmark judgment with profound implications for tax administration and statutory interpretation. By addressing the procedural barriers raised by SARS, granting the section 105 directive, and providing a well-reasoned interpretation of "bulk", the court not only clarified critical aspects of the Mineral Royalty Act but also reaffirmed the High Court judiciary's role in ensuring fairness and legal certainty. For taxpayers, this judgment is a reminder of the power of the High Court to resolve complex legal disputes and the importance of holding administrative authorities to account. Mining taxpayers, in particular, should note the broader interpretational principles established by this case, which could significantly impact their tax obligations in future disputes.

**ENS represented ASPASA and the other applicants in this matter.*

Andries Myburgh & Emilé Cronje

ENS

Acts and Bills

- Tax Administration Act 28 of 2011: Section 105;
- Mineral and Petroleum Resources Royalty Act 28 of 2008: Section 6(2)*(b)*; Schedule 2 ("Unrefined Condition of Mineral Resources").

Cases

- *ASPASA NPC and Others v Commissioner for the South African Revenue Service* (2023/099811) [2024] ZAGPPHC 1286; 2025 JDR 0350 (GP) (6 December 2024).

Tags: tax disputes; meaning of the condition of "bulk"; extraction of mineral resources; non-binding written opinion; declaratory orders.

PRESCRIPTION AND SETTLEMENT AGREEMENTS

In November 2023, SAICA made an Annexure C submission on the problem of the prescription of assessments which are the subject of follow-on adjustments involving a dispute in an earlier year of assessment.

References in this article to sections are to sections of the Tax Administration Act, 2011 (TAA), unless the context otherwise indicates.

The SAICA feedback summary dated 7 December 2023, in paragraph 34 (edited to remove cross-references and duplication), provided as follows:

> "Suppose there is a dispute between SARS and a taxpayer for a particular year (year 1) and the final outcome thereof results in an adjustment of amounts which will be carried forward to subsequent years (ie, balance of assessed losses, etc). While SARS will be able to issue a revised assessment in respect of the relevant amount (ie, a loss to be carried forward) for year 1, if the subsequent years have prescribed in terms of section 99, SARS will not be able to adjust subsequent years' amounts affected by year 1's dispute, which were carried over from the previous year."

National Treasury's reported response was that this was a fair point and that it would be considered.

However, when there is a settlement involving, say, year 1, an opportunity presents itself to bring the prescribed years within the settlement in order to overcome the three-year prescription limit in section 99(1) by using section 99(2)*(d)*.

Besides an assessed loss, there are a number of situations in which this issue arises, including the carry-forward of an assessed capital loss, closing stock which becomes opening stock in the next year of assessment, prepayments claimed in a year of assessment which need to be added back in the next year of assessment and adjustments involving the section 24C allowance for future expenditure, amongst others.

The rules for settlement of disputes are contained in Part F of Chapter 9 of the TAA in sections 142 to 150.

Section 142 defines "dispute" to mean:

> "a disagreement on the interpretation of either the relevant facts involved or the law applicable thereto, or of both the facts and the law, which arises pursuant to the issue of an assessment or the making of a 'decision'".

The procedure for lodging an objection and appeal against an assessment is set out in section 104 and in the dispute resolution rules provided for in section 103 and set out in GN 3146 in GG 48188 of 10 March 2023. It might therefore be expected that a dispute would have to be given expression by way of an objection and appeal, although this is not stated in the above definition.

"The Constitutional Court then cited various authorities to support its view that settlement agreements expedite an end to litigation which was in the parties' interests and promote the administration of justice."

Section 99(2)*(d)* provides that the three-year prescription period in section 99(1) does not apply to the extent that –

"(d) it is necessary to give effect to—

(i) the resolution of a dispute under Chapter 9; or

(ii) an assessment referred to in section 93(1)(d) if SARS becomes aware of the error referred to in that subsection before expiry of the period for the assessment under subsection (1);"

Chapter 9 deals with dispute resolution and includes sections 101 to 150. Section 93(1)*(d)* provides that SARS may make a reduced assessment if –

"(d) SARS is satisfied that there is a readily apparent undisputed error in the assessment by—

(i) SARS; or

(ii) the taxpayer in a return;"

It may well happen that by the time the dispute is settled, the error in the assessments should, viewed objectively, have been readily apparent to SARS. In addition, SARS in most cases should have been aware of the issue during the three years following the relevant assessment, since it would have been aware of it in the first year which was under dispute. But even if section 99(2)*(d)*(iii) cannot be applied, it still leaves section 99(2)*(d)*(i) to be explored.

Section 146 provides:

"146. Circumstances where settlement is appropriate

The Commissioner may, if it is to the best advantage of the state, 'settle' a 'dispute', in whole or in part, on a basis that is fair and equitable to both the person concerned and to SARS, having regard to—

(a) whether the 'settlement' would be in the interest of good management of the tax system, overall fairness, and the best use of SARS' resources; ..."

Section 147(3) of the TAA provides that any settlement agreement must include details on:

"(c) treatment of the issue in future years;"

I-CAT International Consulting (Pty) Ltd v Commissioner, South African Revenue Service [2023] dealt with the issue whether the assessment in the year following the year in dispute had prescribed despite being brought within the settlement agreement.

In the 2014 year of assessment, the taxpayer claimed a deduction of R17 171 433 for compensation for royalties under section 11*(a)* of the Income Tax Act, 1962 (the Act). SARS disallowed the deduction on the grounds that it was of a capital nature, representing a cancellation fee on a distribution agreement and issued an additional 2014 assessment. Its objection having been disallowed, the taxpayer lodged an appeal to the tax court. SARS then raised an alternative argument that only R7 997 663 was paid in 2014 with the balance of R10 154 940 having been paid in 2015. One should note at this point that the balance is actually R9 173 770, a substantial shortfall of R981 170. As so often happens in tax judgments, one is left guessing whether this was simply a calculation error or whether the taxpayer incurred additional expenditure over and above the sum originally claimed in 2014.

Why SARS changed its grounds of appeal to concede that the deduction was of an income nature but not all incurred in 2014 is not explained. On the date of the tax court hearing (28 October 2019), the taxpayer and SARS settled the appeal on the basis that R7 997 663 was deductible in 2014. The settlement, which was made an order of court, stated in clause 6 that while the amount relating to the 2015 year of assessment of R10 154 940 fell outside the tax appeal, the taxpayer could endeavour to apply to SARS under section 93(1)*(d)* for a reduced 2015 assessment.

The 2015 assessment had been assessed on 26 February 2016 and the taxpayer's application under section 93(1)*(d)* was lodged on 13 December 2019. In order to be within the three-year prescription limit, the application should have been lodged by 25 February 2019. SARS refused the request on 26 January 2021 on the basis that the 2015 assessment had prescribed, which resulted in the present High Court application.

Before the High Court, the taxpayer argued that the 2015 assessment had not prescribed by virtue of section 99(2)*(d)*(i) and (iii). SARS, on the other hand, argued that no objection had been lodged against the 2015 assessment and therefore it was not under dispute. It also did not form part of the appeal against the 2014 assessment and the tax court had no jurisdiction to deal with the 2015 assessment. SARS, so the argument went, was not obliged to accept the taxpayer's application under section 93(1)*(d)*. This was quite a startling about-face on the part of SARS. It had agreed in the settlement agreement that the taxpayer could approach it under section 93(1)*(d)*. Why would it insert such a clause, no doubt being fully aware of the deductibility of the amount and the fact that it was readily apparent that it qualified as a deduction, only to renege on its undertaking when the taxpayer lodged its application? In the absence of an explanation, this sort of behaviour does not advance SARS' reputation.

Vermeulen AJ, however, disagreed with SARS and held that the matter indeed fell within section 99(2)*(d)*(i) .

The court stated the following:

> "[89] It is also not a strange occurrence that parties agree to include something in a settlement and consent order that is only indirectly linked to the issues. In *Eke v Parsons* [2016 (3) SA 37 (CC).] the Constitutional Court inter alia stated as follows:
>
> > '[19] ... In certain instances, agreement – or lack of it – on certain terms may mean the difference between an end to litigation and a protracted trial. Negotiations with a view to settlement may be so wide-ranging as to deal with issues that, although not strictly at issue in the suit, are related to it – whether directly or indirectly – and are of importance to the litigants and require resolution. Short of mere formalism, it does not seem to serve any practical purpose to suggest that these issues should be excised from an agreement that a court sanctions as an order of court.'"

The Constitutional Court then cited various authorities to support its view that settlement agreements expedite an end to litigation which was in the parties' interests and promote the administration of justice.

Vermeulen AJ observed that at the time SARS included clause 6 in the settlement agreement, it was aware that the 2015 assessment had prescribed. Nevertheless, it still included the clause even though it served no purpose, was superfluous and insignificant. Citing *Commissioner for Inland Revenue v Golden Dumps (Pty) Ltd* [1993], the court noted that to disregard the words of a statute *per incuriam* (without due regard to the law or the facts) is contrary to the firmly established canon of construction that a meaning must be given to every word. This principle applies equally to private documents. [See *Craies on Statute Law* 7 ed at 103-4.] The court thus saw no reason why this principle should not apply to clause 6 of the settlement agreement.

The court concluded that the inclusion of clause 6 in the settlement agreement was "part and parcel of their resolution of the dispute which they dealt with under ch 9" and therefore SARS' finding that the 2015 assessment had prescribed fell to be reviewed and set aside.

It is submitted that the taxpayer, instead of agreeing to the insertion of clause 6, should have insisted on SARS agreeing to reduce the 2015 assessment as part of the settlement agreement. After all, what is the purpose of section 99(2)*(d)*(i) if not to deal with undisputed assessments that are more than three years old? If it related only to disputed assessments, they would not have prescribed because the taxpayer would have lodged an objection against them in time, thus rendering the provision purposeless.

Clause 6 unnecessarily forced the taxpayer to jump through another hoop (the undisputed readily apparent error hoop) without any guarantee that it would succeed. It is submitted and the understanding is that SARS will, in appropriate circumstances, include so-called prescribed assessments in a settlement agreement in order to resolve a dispute in a fair and equitable manner, particularly when the adjustments to the subsequent years are causally linked to the year in dispute.

Example – Subsequent "prescribed" assessment brought within settlement

Facts:

In year 1 Company X claimed a deduction of R1 million for prepaid rent for the hire of a facility for a conference to be held early in year 2. For accounting purposes, the prepayment was shown on the balance sheet in year 1 and expensed through the income statement in year 2. In year 2 the company added back the rent paid in year 1 of R1 million in order to reverse the accounting deduction and claimed a similar prepayment of R1,2 million in respect of a conference facility to be used early in year 3. SARS added back the deduction in year 1, contending that section 23H of the Act applied. The taxpayer lodged an objection, on the basis that under the proviso to section 23H, the section did not apply because the facility would be used within the first six months of year 2. In year 2 SARS reversed the add-back of R1 million and added back the prepayment of R1,2 million, resulting in increased taxable income of R200 000. The company, however, owing to an oversight, failed to lodge an objection against the year 2 additional assessment. Section 23H did not apply for the same reason. The year 1 assessment was also the subject of a number of other issues which the company negotiated to resolve with SARS. By the time the settlement was negotiated, more than three years had elapsed after the date of the year 2 assessment.

Result:

The issues in year 2 are causally related to the year 1 assessment. It is in SARS' interest to add back the year 1 prepayment and in the company's interest to have the year 2 prepayment allowed as a deduction. In order to settle the dispute, both parties agree to bring the year 2 assessment into the settlement, even though no objection was lodged against it. Under section 99(2)*(d)*(i) the year 2 assessment has not prescribed, thus enabling SARS to issue the reduced assessment.

Note: Had SARS refused to bring the year 2 assessment into the settlement, the company would have had good grounds for requesting the assessment to be reduced under section 93(1)(d), read with section 99(2)*(d)*(iii).

CONCLUSION

Section 99(2)*(d)*(i) offers a valuable lifeline to taxpayers when their assessments are out of time and causally linked to a dispute in a prior tax year for which a settlement agreement is negotiated. When the error in the "prescribed" assessment is undisputed and readily apparent, section 99(2)*(d)*(iii) offers a possible alternative route to a reduced assessment.

This article was first published in ASA April 2024

Duncan McAllister

Acts and Bills

- Income Tax Act 58 of 1962: Sections 11*(a)* & 23H;
- Tax Administration Act 28 of 2011: Sections 24C, 93(1)*(d)*, 99 (specific reference to subsections (1) & (2)*(d)*(i) & (iii)), 103, 104, 142 (definition of "dispute"), 146 & 147(3); Chapter 9 ("Dispute resolution" (sections 101 to 150) – specific emphasis on Part F of Chapter 9 (sections 142 to 150)).

Other documents:

- SAICA Annexure C 2024 Budget Review (24 November 2023);
- SAICA feedback summary dated 7 December 2023 (edited to remove cross-references and duplication): Paragraph 34;
- Dispute resolution rules provided for in section 103 of the TAA and set out in GN 3146 in GG 48188 of 10 March 2023;
- GN 3146 in *Government Gazette* 48188 of 10 March 2023;
- *Craies on Statute Law* 7 ed at 103-4;
- Settlement agreement in terms of Part F of Chapter 9 of the TAA: Clause 6.

Cases

- *I-CAT International Consulting (Pty) Ltd v Commissioner, South African Revenue Service* [2023] (6) SA 477 (GP), 86 SATC 101;
- *Commissioner for Inland Revenue v Golden Dumps (Pty) Ltd,* [1993] (4) SA 110 (A), 55 SATC 198.

Tags: assessed capital loss; rules for settlement of disputes; dispute; settlement agreement.

SARS' RIGHTS TO YOUR RETIREMENT SAVINGS

The South African retirement fund dispensation has been in the news for several reasons: The two-pot retirement system was implemented on 1 September 2024, which for the first time allowed individuals to withdraw a limited portion of their retirement savings every year from their so-called savings pot.

A media release by the South African Revenue Service (SARS) on 31 January 2025 indicated that individuals had withdrawn a total of approximately R43.42 billion from their savings pots as at that date. Furthermore, the Financial Sector Conduct Authority (FSCA) has indicated its intention to investigate the high transaction fees charged for withdrawals by certain fund administrators. In addition, the FSCA has indicated that according to reports received from several pension funds, more than R5.2 billion in pension fund contributions have not been paid over by employers on behalf of their employees.

Considering this, it is apt to consider the High Court judgment in the Eastern Cape Division (Gqeberha) on 27 August 2024 in *Piet v Commissioner for the South African Revenue Service* [2024] (Piet), where the taxpayer requested that funds paid to SARS from his retirement savings to settle a tax debt, be repaid.

SARS' POWER TO COLLECT TAX

The South African Revenue Service (SARS) wields significant powers under the Tax Administration Act, 2011 (the TAA), to ensure the efficient collection of taxes. This is evident from the specific provisions contained in the TAA that empower SARS to collect or recover tax debts owed by a taxpayer from third parties. These provisions extend SARS' reach beyond the taxpayers themselves, allowing SARS to recover outstanding amounts from individuals or entities with a connection to the taxpayer.

One of the most impactful provisions, which is also the focal point of this article, is section 179 of the TAA, which allows SARS to appoint a third party to satisfy a taxpayer's "outstanding tax debt", by paying money held on behalf of or money owed to the taxpayer, including pensions, directly to SARS.

Before section 179 and the High Court's finding in Piet are discussed, the facts are set out to provide some necessary context.

FACTS

The taxpayer, Sizakele Crosby Piet, sought the repayment of R145,934.99, which was paid by the Allan Gray Retirement Fund (Allan Gray) to SARS on 28 August 2023 in terms of a notice received by Allan Gray under section 179(1) of the TAA, without the taxpayer's knowledge.

The debt in question arose from an additional assessment raised against the taxpayer for the 2015 year of assessment. From the judgment it appears that the taxpayer's objection against the additional assessment was unsuccessful.

The taxpayer contested the section 179 notice on the following grounds:

- The section 179 notice was not written by a senior SARS official as required by legislation – it was rather "a product of artificial intelligence" and was null and void.
- There was non-compliance with section 179(4).
- There was non-compliance with section 179(5).
- There was a violation of section 37A of the Pension Funds Act, 1956 (the PFA).
- There was a violation of section 27 of the Constitution of the Republic of South Africa, 1996.

SARS on the other hand argued the following:

- It had the authority under section 179 of the TAA to appoint a third party, such as Allan Gray, to pay the taxpayer's outstanding tax debt from funds held on behalf of the taxpayer, including pensions.
- Various demands were issued to the applicant for the unpaid tax debt in accordance with section 179(5) of the TAA, and the applicant was put on clear and unequivocal terms to settle his debt.

THE LAW

Section 179(1) of the TAA states the following: –

> "A senior SARS official may authorise the issue of a notice to a person who holds or owes or will hold or owe any money, including a pension, salary, wage or other remuneration, for or to a taxpayer, requiring the person to pay the money to SARS in satisfaction of the taxpayer's outstanding tax debt". (own emphasis)

Section179(2) provides an opportunity for the third party receiving the notice to inform SARS of any inability to comply with the notice, whereas section 179(3) provides for the personal liability of the third party should it part with the money contrary to the notice.

In terms of section 179(4), SARS may, "on request by a party affected by the notice", amend the notice to extend the period over which the tax debt must be paid to SARS to allow the taxpayer to pay basic living expenses of the taxpayer and his or her dependants.

Section 179(5) protects the taxpayer by requiring SARS to issue a final demand to the tax debtor (taxpayer) at least 10 business days before sending the 179(1) notice. This final demand must outline the steps SARS may take to recover the tax debt if it remains unpaid, as well as the debt relief options available to the taxpayer. In the case of a natural person, the demand must inform the taxpayer that they may apply to SARS for a reduction in the amount due within five business days of receiving the demand, based on their and their dependants' basic living expenses.

Section 179(6) provides that the issue of a final demand is not required if SARS is satisfied that to do so would "prejudice the collection of the tax debt".

JUDGMENT

The court's judgment in terms of section 179 of the TAA was based mainly on whether SARS complied with the requirements in section 179(5).

Although not a contested point between the parties, the court pointed out that SARS is, in terms of section 179(1), entitled to issue a notice to a third party (Allan Gray) who holds money on behalf of a taxpayer, requiring Allan Gray to pay that money to SARS to satisfy the taxpayer's tax debt.

Regarding the taxpayer's claim that the section 179 notice was not authored by a senior SARS official as mandated by legislation but was instead "a product of artificial intelligence" and therefore invalid, the court ruled that, under section 179(2), Allan Gray had the opportunity to raise any concerns about the notice or its contents. Had Allan Gray raised such concerns, the appropriate SARS official could have amended the notice as deemed necessary under the circumstances. The court thus held that it is not the taxpayer who has the standing to challenge the validity of the section 179 notice, but rather the third party to whom the notice was issued.

The court further determined that Allan Gray's failure to question or raise concerns about the notice, coupled with its payment of the money to SARS – which the court described as being done "seemingly without difficulty" – is a matter that should not concern SARS. Allan Gray was required, in terms of section 179(3), to pay the money in accordance with the notice.

In respect of the taxpayer's argument that SARS did not comply with section 179(4) of the TAA in that the taxpayer was not afforded an opportunity to request SARS to amend the notice, the court held that, while the applicant is affected by the notice, his recourse in terms of section 179 appears to be limited. The court held that the taxpayer can request SARS to amend the notice to extend the period over which the amounts are to be paid to SARS, as contemplated in section 179(4).

The court determined that for a taxpayer to avail themselves of the remedy provided under section 179(4), it is a prerequisite that the third party notifies the taxpayer of the notice. Without such notification, the taxpayer would be unaware that the third party has received the notice, and consequently, would not have the knowledge required to request that SARS amend the notice.

"The court's judgment in Piet appears to suggest that in terms of section 179(4) a taxpayer should be notified by a third party (in the case Allan Gray) of the fact that SARS has issued the notice, before the funds are paid over to SARS."

The court found that SARS had issued the necessary final demand(s) to the taxpayer before appointing Allan Gray as a third party to pay the tax debt as required by section 179(5). The court held that the final demand correctly included the prescribed details and in each instance the taxpayer "was put on clear and unequivocal terms to settle his debt".

The court furthermore pointed out that it is the third party's obligation to inform the taxpayer, in this case its member, of a notice prior to making payment to SARS. If the third party failed to inform the taxpayer, this cannot be attributed as a fault on the part of SARS.

Interestingly, the taxpayer also argued that if section 179 of the TAA is read with certain provisions of the PFA, SARS' conduct was unconstitutional in that it infringed the taxpayer's right to have access to social security, which is constitutionally protected. The court also rejected this argument.

Ultimately, the court rejected the taxpayer's application as SARS complied with section 179 of the TAA.

COMMENT

There are several interesting and important issues that arise from this judgment, of which the following are highlighted:

While there are several cases dealing with non-compliance by SARS of section 179, in particular the final demand requirement in section 179(5) of the TAA (read with section 179(1)), this appears to be one of the first instances where the court considered other parts of section 179. The High Court has ruled in favour of taxpayers in the context of non-compliance with section 179(5) on several occasions, including in the cases of *WPD Fleetmas CC v Commissioner South African Revenue Service and Another* [2020] (19 August 2020) and *SIP Project Managers (Pty) Ltd v Commissioner for the South African Revenue Service* [2020] (29 April 2020).

The court's judgment in Piet appears to suggest that in terms of section 179(4) a taxpayer should be notified by a third party (in the case Allan Gray) of the fact that SARS has issued the notice, before the funds are paid over to SARS. The challenge, however, is that in terms of section 179(3), a third party receiving a section 179 notice is required to "pay the money in accordance with the notice" and "is personally liable for the money" if it parts with the money contrary to the notice. If a third party notifies the taxpayer of the notice issued to it, there is the risk that the taxpayer may proceed to withdraw its funds, to avoid funds being paid to SARS under the notice. While this risk is remote in the pension fund context, where there are several administrative checks that would have to take place before one can withdraw from the fund, this is a genuine risk where the notice is issued to a bank in which some of the taxpayer's funds are held. If a taxpayer withdrew its funds from its bank account prior to the funds being paid over to SARS, the bank would potentially be personally liable to SARS for the money that was supposed to be paid over in terms of the notice.

Practically, if a final demand is correctly issued and communicated to the taxpayer, the taxpayer will have had an opportunity to decide how to respond to the threat of losing funds held by a third party and prevent this from happening. The taxpayer has at least 10 business days to respond and prevent a third-party notice from being issued and losing funds if SARS complies with the final demand requirement. As such, section 179(4) and the phrase "person affected by the notice" should arguably have been interpreted differently. If one follows the court's interpretation, the third party is at risk of non-compliance with the notice and the taxpayer will also get a second bite at the cherry so to speak.

It is, of course, crucial that a taxpayer is not unfairly prejudiced as it has real life consequences for the taxpayer, such as Mr Piet, who even represented himself in these court proceedings. Finding out years after the fact that one's pension has been reduced without one's knowledge to pay a tax debt, is not something that one would want to happen to any taxpayer.

While the court's finding in favour of SARS is acknowledged and it appears that SARS complied with the requirements of section 179 in the current instance, it is unclear from the judgment how a third party, such as a bank or pension fund, could practically give notice to the taxpayer of the impending loss of funds to SARS, while avoiding the risk of non-compliance under section 179(3).

Danielle Annandale & Louis Botha

WTS Renmere

Acts and Bills

- Tax Administration Act 28 of 2011: Section 179 (specific reference to subsections (1), (2), (3), (4), (5) & (6));
- Constitution of the Republic of South Africa, 1996: Section 27;
- Pension Funds Act 24 of 1956: Section 37A.

Other documents

- Section 179 notice.

Cases

- *Piet v Commissioner for the South African Revenue Service* (3090/2023) [2024] ZAECQBHC 51 (27 August 2024); 2024 JDR 3710 (ECGq);
- *WPD Fleetmas CC v Commissioner South African Revenue Service and Another* (31339/20) [2020] ZAGPPHC (19 August 2020);
- *SIP Project Managers (Pty) Ltd v Commissioner for the South African Revenue Service* (11521/2020) [2020] ZAGPPHC (29 April 2020); 2020 JDR 1093 (GP).

Tags: two-pot retirement system; pension fund contributions; outstanding tax debt; additional assessment; senior SARS official.

WILL EXPANDING THE LIST OF ZERO-RATED FOODSTUFFS REALLY BENEFIT THE POOR?

In his opening of Parliament address on 18 July 2024, President Cyril Ramaphosa stated that the Government of National Unity will look to expand the basket of essential food items subject to value-added tax (VAT) at the zero rate and undertake a comprehensive review of administered prices. Subsequently, politicians, members of Parliament, trade unions, the South African Poultry Association and the Red Meat Producers Organisation have all called for the expansion of the list of zero-rated foodstuffs.

This is not surprising since the 2024 National Food and Nutrition Security Survey stated that 3,7 million households in South Africa reported inadequate or severely inadequate access to food. The 2024 South African Food Security Index published by Shoprite, in conjunction with Stellenbosch University, indicated that food security in South Africa was at its lowest point in 2023 relative to the period 2010–2023. Furthermore, the number of people in South Africa not meeting the minimum energy requirements increased from 1,8 million in 2001 to 4,7 million in 2021 and by 2023, 23,6% of households were consuming a lower variety of food than usual given economic constraints.

The calls for expansion of the list of zero-rated foodstuffs cite two main reasons. Firstly, it will reduce the cost of food items for poor households in the wake of high food price inflation. Secondly, adding more protein to the zero-rated basket will encourage poor and low-income households to add more protein to their diets to address malnutrition.

The question that arises is whether adding more food items to the basket of zero-rated foodstuffs will indeed reduce the cost of these items, and whether it will address malnutrition.

HISTORY OF ZERO-RATING FOODSTUFFS

Without any zero-rating or exemptions, VAT is inherently a regressive tax. This is because the amount of VAT paid by lower income households on essential goods and services as a percentage of their disposable income is higher than that of high income households, although high income households may spend higher amounts on VAT in absolute terms. The zero-rating of basic foodstuffs is aimed at alleviating the regressivity of the tax.

When VAT was introduced on 30 September 1991 at a rate of 10%, only two food items were initially zero-rated: brown bread and maize meal. The number of zero-rated food items was subsequently temporarily increased from 30 September 1991 to 31 March 1992 with the addition of another eight items. The zero-rating of these additional eight items was extended from 1 April 1992.

With effect from 7 April 1993, when the VAT rate was increased from 10% to 14%, the basket of zero-rated food items was expanded by a further nine items to increase the total number to nineteen. Following the VAT rate increase from 14% to 15% on 1 April 2018, the zero-rated basket was expanded further with the addition of cake wheat flour and white bread wheat flour from 1 April 2019. Sanitary towels were also zero-rated with effect from 1 April 2019.

At the end of 2024, the basket of basic foodstuffs that are zero-rated comprised of 21 food items. In addition, zero-rating also applies to petrol and diesel, illuminating kerosene and sanitary towels. Petrol and diesel are, however, subject to excise duties, the fuel levy, the Road Accident Fund levy. Furthermore, public transport by road and rail, and the provision of residential accommodation are exempt from VAT.

"As confirmed by various global and local studies, the VAT system is not an effective tool to provide relief to poor and low-income households, mainly because the benefit of zero-rating is enjoyed by all consumers, even more by those who can afford the food items and to pay the tax."

PREVIOUS STUDIES

A number of studies, both globally and in South Africa, have been conducted over the years to determine the effect of zero-rating basic foodstuffs on alleviating the regressivity of VAT, and the implications of zero-rating. Some of these studies and their findings are discussed below.

The Katz Commission extensively considered the incidence and benefits of the zero-rating of basic foodstuffs. Its interim report in 1995 stated that zero-rating benefits the poor modestly in absolute rand terms and benefits the non-poor by substantially greater amounts. Moreover, it found that, of the total revenue loss due to zero-rating, only approximately a third of the benefits went to low-income households. The Katz Commission stated that the zero-rating of basic foodstuffs may be considerably less beneficial to consumers than is commonly assumed, and concluded that any further erosion of the VAT base through zero-rating or exemptions should not be considered in view of the limited contributions that such measures make to the relief of poverty.

A study conducted by the Organisation for Economic Cooperation and Development in 2015 found that, despite the progressive effect of reduced rates on food products, reduced VAT rates are a very poor tool for targeting support to poor households. At best, rich households receive as much benefit from the reduced rate as poor households and, at worst, rich households benefit vastly more than poor households. The study indicated that in some cases, the benefit to rich households is so large that the reduced VAT rate actually has a regressive effect in benefiting the rich much more in absolute terms.

The Davis Tax Committee also considered the zero-rating of basic foodstuffs in some detail. In its final report on VAT to the Minister of Finance (29 March 2018) it referred to a study conducted by National Treasury in 2006 which found that the zero-rating of specific foodstuffs provides a larger proportional benefit to the poor, thereby enhancing progressivity, but it provides a larger absolute benefit to the rich, who consume larger quantities. The report also referred to studies conducted by Professor Ingrid Woolard and by Inchauste et al which found that the zero-rating of foodstuffs results in the South African VAT system being essentially neutral or even slightly progressive. It noted that the poor benefit more from certain food items such as brown bread and maize meal, but the wealthy benefit substantially more from zero-rating of items such as milk and fruit and vegetables. Accordingly, the wealthy not only also benefit from the zero-rating of food but for some items they benefit significantly more than the poor. The Davis Tax Committee concluded that zero-rating is a very blunt instrument for the pursuit of equity objectives, and it strongly recommended that no further zero-rated food items should be considered.

When the VAT rate was increased from 14% to 15% on 1 April 2018, the Minister of Finance appointed an independent panel of experts to review the zero-rating of various items, including bread, white bread flour, cake flour, school uniforms, baby formula, individually quick frozen (IQF) poultry parts, sanitary towels and nappies. With regard to IQF poultry parts, the panel could not reach consensus on its zero-rating. Some panel members raised a concern that the definition was not sufficiently clear, which could give rise to abuse. Other concerns raised were the cost of foregone revenue, that zero-rating could encourage imports, and that the benefits would not be passed on to consumers. The panel stated that nutritional programmes would be more efficient to offset the higher cost for low-income households.

Although there is consensus that the zero-rating of basic foodstuffs alleviates the regressivity of VAT, there also seems to be consensus that no further food items should be zero-rated as a means to alleviate the impact of high foods prices on poor and low-income households. There is also no evidence that adding more protein to the zero-rated food items basket will get poor or low-income households to add more protein to their diet.

IMPLICATIONS OF ZERO-RATING

Apart from the concerns raised by these studies, mainly that the zero-rating of basic foodstuffs benefits all consumers, and that it may benefit high income households substantially more than poor or low-income households, the following consequences of zero-rating should also be considered:

- Zero-rating results in forgone revenue for the fiscus. In October 2024, the Deputy Minister of Finance indicated that the zero-rating of the current list of 21 food items costs the fiscus approximately R30 billion annually in lost revenue. This amount does not seem to include the lost revenue resulting from illuminating kerosene and sanitary towels. The panel of experts estimated at the time (in 2018) that the zero-rating of IQF poultry parts would cost the fiscus R2,1 billion per annum in forgone VAT revenue.

- The food items that are zero-rated must be accurately defined to ensure clarity and to avoid interpretational challenges and abuse. If the food items are not clearly identified, then it creates an opportunity for misclassification of other similar products, and potentially increased litigation to obtain clarification.

- Zero-rating distorts consumer preferences. If the demand for the zero-rated food items increases because of the zero-rating, that could in itself give rise to shortages of the product in the market with a resultant increase in the price, which would eliminate any benefit of the zero-rating for poor or low-income households.

- Zero-rating gives rise to administrative complexities for both suppliers and the South African Revenue Service. The items that qualify for zero-rating need to be accurately identified, and systems need to be implemented to ensure the correct and accurate VAT accounting and reporting in relation to these items.

- There is no guarantee that suppliers will pass the benefit of zero-rating on to consumers. Suppliers could keep the selling price of zero-rated food items the same as the current VAT inclusive price, on the pretence of higher costs of production. The benefits of zero-rating are then captured by suppliers in the form of higher margins, as the Davis Tax Committee reported was the case when illumination kerosene was zero-rated.

- If a poor or low-income household cannot afford to purchase a particular food item in the first instance, then the zero-rating of the item is unlikely to make it affordable.

- In terms of section 13(3) and Schedule 1 to the Value-Added Tax Act, 1991, all zero-rated foodstuffs are exempt from any VAT payable on the importation of these goods into South Africa. This may be an incentive for importers, which could give rise to increased imports. The impact of increased imports on local producers must be considered. Furthermore, if the intention is to make these food items more affordable to poor and low-income households and to address malnutrition, any import tariffs on the foods items to be added should be reviewed. However, the removal of import tariffs will negatively affect local producers.

ALTERNATIVES TO ZERO-RATING

There is no doubt that poor and low-income households suffer from high food price inflation and possibly malnutrition. If the zero-rating of basic foodstuffs is not an effective means to alleviate the plight of poor and low-income households, then what is the alternative?

The Katz Commission, the Davis Tax Committee and the panel of experts all stated that it would be substantially more efficient to rather collect the tax revenue on food items and to redistribute the additional income through a targeted transfer to the poor. The panel recommended that as an alternative to zero-rating, the monthly social grants and old age social pension should be increased. The Davis Tax Committee noted that more than 75% of households in the poorest four deciles already receive cash transfers and such cash transfers could be increased. The panel also recommended, as alternatives to zero-rating, the introduction of food vouchers where cash grants are not feasible or practical, and the upscaling of feeding schemes. To address the issue of nutrition, the panel made various recommendations, including the upscaling of high impact nutrition interventions targeting women, infants and children, and the expansion of the national school nutrition programme.

CONCLUSION

As confirmed by various global and local studies, the VAT system is not an effective tool to provide relief to poor and low-income households, mainly because the benefit of zero-rating is enjoyed by all consumers, even more by those who can afford the food items and to pay the tax. There is no clear evidence that VAT causes food price inflation, which is mainly driven by input costs. There is general consensus that specifically targeted relief measures aimed at poor and low-income households, such as increased social grants and old age social pensions, food vouchers and the expansion of the national school nutrition programme, are better suited to address the difficulties faced by these households in relation to high food prices and malnutrition.

Gerhard Badenhorst

Cliffe Dekker Hofmeyr

Acts and Bills

- Value-Added Tax Act 89 of 1991: Section 13(3); Schedule 1.

Other documents:

- Katz Commission of Inquiry into Taxation: Interim report (1995);
- 2024 National Food and Nutrition Security Survey;
- 2024 South African Food Security Index (published by Shoprite, in conjunction with Stellenbosch University);
- Study conducted by the Organisation for Economic Cooperation and Development (2015);
- Davis Tax Committee: Final Report on VAT (29 March 2018).

Tags: the zero rate; zero-rated food items; high food price inflation.

sait South African Institute of Taxation