PROFESSIONAL

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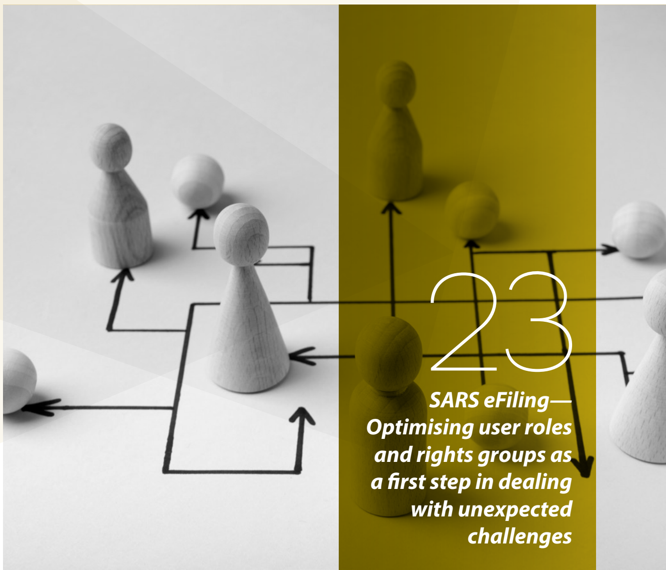

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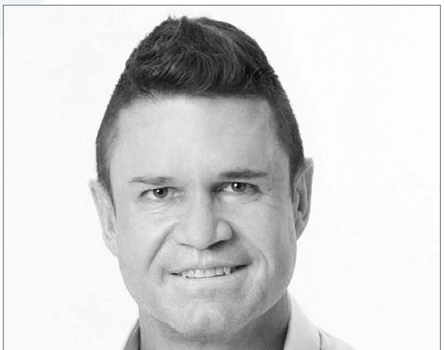

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15 minutes CPD

KIESWETTER MAKES NO EMPTY PROMISES:
NO ONE IS ABOVE THE LAW!

ANDRÉ DANIELS, Head of Tax Controversy and Dispute Resolution at Tax Consulting South Africa

The South African Revenue Service (SARS) released Interpretation Note 129 (IN 129) on 24 May 2023; it provides clarity on the imposition of penalties when the taxpayer has understated their income. SARS Commissioner, Edward Kieswetter, has continually stated that he aims to make non-compliance difficult and costly, and we now see this coming to fruition in IN 129.

The main purpose of IN 129 is to refine the understatement penalty regime, which aims to ensure consistent and equal treatment of taxpayers in comparable circumstances and to deter behaviours that result in non-compliance and under-declarations.

The IN 129 has perhaps shown, more so than many of the other changes SARS has implemented in recent years, that no one is above the law. However, there is a light at the end of the tunnel for non-compliant taxpayers in the shape of the Voluntary Disclosure Programme (VDP).

An overview of the applicable law

As IN 129 clarifies how understatement penalties are imposed, SARS intends to use this practice to penalise non-compliant taxpayers. Section 222(1) of the Tax Administration Act (the TAA) explains exactly how these penalties will be imposed.

In accordance with section 222(2) of the TAA, the understatement penalty is determined by applying the highest applicable understatement penalty percentage to each under-declaration.

Section 222(5) of the TAA states that the "*maximum tax rate applicable to the taxpayer*" must be applied to determine the shortfall in tax; it is determined by ignoring an assessed loss or any other benefit brought forward from a preceding tax period to the tax period in which the understatement has occurred.

Certain taxpayers are taxed either at a flat rate or at a progressive rate of tax. The tax rate applicable to taxpayers subject to a flat rate of tax represents the *"maximum rate applicable to that taxpayer"* for purposes of section 222(5).

For taxpayers that are taxed at a progressive rate of tax, the maximum tax rate applicable to the shortfall envisaged under section 222(3)(c) is the marginal tax rate applicable to the taxable income or taxable turnover that is established by, ignoring the assessed losses or any other benefit brought forward from a preceding tax period to the tax period in question.

No empty promises

With the law being made clear, SARS and Kieswetter are continuing to crack down on non-compliance. They have done so in recent weeks by issuing a statement on 11 May 2023, informing the public that they would be imposing stricter requirements on VAT registrations.

Further, SARS went as far as providing clarity in respect of the tax status of President Cyril Ramaphosa on 7 March 2023. SARS stated that through staff and advisors, the President has always cooperated fully with SARS during audits and there has been no interference or resistance from him, his staff or any other party.

Kieswetter confirmed that *"At no stage was I approached by President Ramaphosa, or anyone on his behalf, with any request related to his personal and/or the business entities in question.".*

The Commissioner further stated: "*In taking this exceptional step to disclose the tax status of the President, with his written consent, SARS would also encourage other high-profile political office bearers and leaders in society to consider taking this proactive step as part of their commitment to transparency. This would go a long way towards building confidence in our country's institutions.*"

This announcement of the President's audit, his clear cooperation, and the press release regarding VAT registrations, along with the issuance of IN 129, clearly indicate that Kieswetter makes no empty promises.

Taxpayers—heed the warning!

We are now seeing this crackdown on non-compliance truly come to fruition. Regardless of one's station in society, SARS will audit you, and where applicable, penalties will be levied at the applicable rate, of which the maximum is 200% in certain circumstances.
It is clear to see from the prior statements made by Commissioner Kieswetter, and further, that even the State President goes through audits and bears the onus of proving properly declared income. It stands to reason that SARS is now, more than ever, pursuing non-compliant taxpayers regardless of their status, without fear, favour or prejudice.

However, the VDP offers a reprieve for willing non-compliant taxpayers.

"With the law being made clear, SARS and Kieswetter are continuing to crack down on non-compliance. They have done so by issuing a statement informing the public that they would be imposing stricter requirements on VAT registrations"

Light at the end of the tunnel

In order to avoid the harsh penalties as described in section 222, errant taxpayers must, before SARS approaches them, declare previously undeclared income through the ongoing VDP avenue, which is regulated by the TAA.

A major benefit of relief sought through the VDP, is that it encompasses all tax types (income tax, employees' taxes such as Pay-as-You-Earn, Unemployment Insurance Fund contributions and the Skills Development Levy, as well as Value-Added-Tax). The only taxes that are not covered are customs and excise duties.

When a taxpayer is granted relief under the VDP, penalties are waived, and the applicant receives amnesty from criminal prosecution by the Commissioner of SARS. The taxpayer will only be liable for the outstanding tax liability as well as the interest levied thereon. It is therefore advised that errant taxpayers should utilise the ongoing VDP in order to become fully tax compliant and thus avoid SARS' wrath.

30 minutes CPD

AUTO-ASSESSMENT:
ONE YEAR LATER

▶ **YOLISA DYASI,** Tax Technical Consultant at SAIT

SARS introduced the concept of 'auto-assessments' during the 2020 year of assessment by collecting third-party data and the pre-population of personal income tax returns (ITR12s). At the time, the select population of approximately one million taxpayers had the ability to review the pre-populated returns and to choose whether to accept or reject the pre-populated return.

Since then, SARS has become more comfortable with the maturity and accuracy of the third-party data collected from employers and other third-party data providers. As a result, in May 2022, SARS announced that they would be moving away from the pre-population model to the issuance of original estimated assessments. The tax fraternity did not accept SARS' decision lightly; many questioned both the legality and the practicality of this decision. ▶

The issues raised by taxpayers and tax practitioners include legislative amendments, third-party data collection, potential risks, the impact on tax practitioners, submission deadlines and debt collection periods.

Legislative amendments

Following the announcement of the change in the auto-assessment process in May 2022, the tax community questioned the legality of the decision, arguing that section 95 of the Tax Administration Act, No. 28 of 2011 (hereafter the TAA) did not allow for SARS to issue an estimated assessment without affording a taxpayer the opportunity to submit a true and accurate return. At present, section 95(1)(a)) states that: *"SARS may make an original, additional, reduced or jeopardy assessment based in whole or in part on an estimate, if the taxpayer—(a) does not submit a return; . . . "*.

As section 95(1)(a) currently reads, a taxpayer's failure to submit a return is a requirement for SARS to issue the original estimated assessment in terms of section 91 read with section 95 of the TAA. In principle, where a taxpayer has not been afforded the opportunity to furnish a true and accurate return to SARS, it cannot be stated that the taxpayer did not or has failed to do so.

With that said, it was anticipated that National Treasury and SARS would amend the provisions of section 95 of the TAA to allow for the issuance of original estimated assessments in the first instance during the 2022 Annexure C process. However, when the Tax Administration Laws Amendment Act, No. 16 of 2022 was officially released, this was not the case.

Many tax professionals are on the fence; they still question the legality of the new auto-assessment process. However, SARS is committed to forge ahead regardless.

Third-party data collection

Auto-assessments are issued based on third-party data collected from employers and other third-party data providers. Third-party data providers include, among others:

- Banks;
- Financial institutions;
- Medical schemes; and
- JSE listed companies that issue financial products.

On 29 March 2023, SARS published a draft notice to section 26 of the TAA for public comment. The draft notice details persons required to submit third-party returns, returns required to be submitted and the due date for submitting a third-party return.

Three notable additions were made to the list of persons required to submit third-party returns:

1. A person referred to in section 18A(1)(a) to (c) of the Income Tax Act, 1962, that issued a receipt in terms of section 18A(2) of the Act;
2. A 'trust' as defined in section 1 of the Income Tax Act, 1962 that is a 'resident' as defined in that section; and
3. A person who issues a solar installation certificate of compliance.

"Taxpayers and tax practitioners can only hope for the best and prepare for the worst to ensure that they are prepared for whatever challenges may come their way"

Although the final notice has not been promulgated as yet, SARS has communicated its intention to utilise this additional third-party data to populate auto-assessments in future. Only when SARS is comfortable that the abovementioned third-party data providers can provide this information accurately and timeously, then will SARS start pre-populating this information in the ITR12 returns. Realistically, this information will only be used from the 2025 year of assessment or even from 2026.

Potential risks

The modernisation, digitisation and streamlining of the personal income tax return submission does not come without any risks, particularly to the fiscus. For example, many cases reported taxpayers receiving undue refunds in 2022 because additional income had not been included in the original estimated assessments issued by SARS. Many taxpayers opted to keep quiet and not disclose the additional income (commission income, rental income, etc.) because SARS issued the assessment, and no evidence existed to suggest that SARS would issue any additional assessments contrary to the original estimated assessments. .

Additionally, owing to the hard validation rules placed on the ITR12 return, taxpayers are unable to correct the third-party data reflected on the return. For example, where a medical scheme certificate reflects spouse A as the primary member but spouse B pays the actual medical scheme fees, spouse B would be entitled to the medical scheme credits in terms of section 6A of the Income Tax Act, No. 58 of 1962 (the Income Tax Act). Unfortunately, spouse A would be unable to remove the third-party data from their income tax return, which results in the medical scheme credits being unduly granted to the incorrect individual.

- Another risk arises when an employer or third-party provider fails to submit their EMP501 reconciliations or 'Third Party Data Annual Submission' timeously (by 31 May), thus resulting in what SARS considers 'incomplete information' in the auto-assessment process.

Although section 95(4) of the TAA does not detract a taxpayer from their obligation to submit a true and accurate return, it also assumes that a taxpayer will be honest and disclose additional information to SARS. This may, in some cases, put them in a debit position immediately after receiving an undue SARS refund.

Impact on tax practitioners

The general consensus amongst many tax practitioners, especially those who specialise in individual income taxes, has been that SARS may be attempting to cut tax practitioners out of the tax compliance equalisation insofar as it relates to individual taxes. Accordingly, this proposition was also placed before SARS.

SARS has reiterated that it has no intentions of cutting tax practitioners out of the equalisation. However, it would seem that this is an unintended consequence for tax practitioners who traditionally deal with individual taxpayers, who are now part of the auto assessment population. This has therefore resulted in financial losses for tax practitioners because some of their clients no longer require their services to complete and submit their returns.

Some tax practitioners are now required to reinvent themselves by shifting their role from that of a traditional 'tax preparer', who completes and submits returns to 'tax auditor', who performs an audit of information contained in original estimated assessments and who liaises with SARS during audits and disputes.

Submission deadlines and debt collection periods

In July 2022, approximately three million taxpayers were issued with original estimated assessments between 1–7 July 2022. SARS is looking to increase that number to five million individual non-provisional taxpayers in 2023.

As a result, fewer taxpayers actually need to submit an income tax return. Therefore, SARS decided to shorten the income tax filing season from 2022 by one calendar month from 23 November in 2021 to 24 October in 2022 (with specific reference to non provisional taxpayers).

The shortened filing season deadline, combined with other challenges such as unprecedented load-shedding hours, cause great frustration and concern for many tax practitioners. During the 2022 filing season, SARS made it explicitly clear that the filing season deadlines would not be extended despite the aforementioned challenges.

"Many tax professionals are on the fence; they still question the legality of the new auto assessment process. However, SARS is committed to forge ahead regardless"

Following the discussions between SARS and the 'recognised controlling bodies' (RCBs) in May 2023, it was communicated that the filing deadlines for 2023 would be similar to those of 2022; they would run from July to approximately the third week of October 2023.

Previously, the auto-assessments issued by SARS were not actual assessments, which were enforceable in terms of Chapter 8 of the TAA, as taxpayers were still afforded the full filing season to accept the pre-populated return or rejected the auto-assessment and submit a true and accurate return.

Now that SARS has changed its strategy, the original estimated assessments are fully enforceable. SARS may collect any debts arising from these assessments unless the taxpayer submits a revised return disputing the original estimated assessment. This is particularly important for the 2023 year of assessment because SARS has communicated with RCBs that the 'grace period' for payment on debit assessments will no longer be 30 days after the provisional taxpayer deadline; however, it will be moved forward by three months to only 30 days after the non-provisional taxpayer deadline ending in October 2023. This will allow SARS a longer period to collect outstanding tax debts in time to meet their revenue targets by 31 March 2024.

Lastly, and in addition to the shortened deadline and shortened payment grace period, SARS alluded to reserving the first week of July 2023 for auto-assessment taxpayers. This would mean all other provisional and non-provisional taxpayers must wait until the second week of July to start submitting returns. This will assist in avoiding the immense traffic on the eFiling system, which also saw the system crash in 2022.

With Filing Season 2023 well upon us, taxpayers and tax practitioners can only hope for the best and prepare for the worst to ensure that they are prepared for whatever challenges may come their way.

15 minutes CPD

SOUTH AFRICA'S PUSH FOR TRANSPARENCY: UBOs and third-party data disclosure

MATHYS BRIERS-LOUW, CEO of Twenty2 Services & **HUGO VAN ZYL,** CEO of Taxforum

South Africa recently gained global attention when it was placed on the grey list by the Financial Action Task Force (FATF) in 2023. As a result, the country is now required to implement mandatory regulations that demand companies and trusts to disclose their ultimate beneficial ownership (UBO). This move positions South Africa at the forefront of international efforts to combat financial crimes and promote transparency in corporate governance. In addition to UBO disclosure, the country has taken significant steps to increase accountability in financial transactions by designating trusts and companies as third-party data providers.

Enhancing reliability and transparency

To strengthen reliability, transparency and combat illicit activities, South Africa has introduced regulatory changes that place new reporting obligations on trusts and companies. These entities are now required to report UBO details separately to both the Master of the High Court and the Companies and Intellectual Property Commission (CIPC), depending on the nature of the entity. By compelling these organisations to disclose their UBO information, South Africa aims to promote transparency and curb illicit activities. Non-compliance with these regulations can result in substantial penalties, fines, imprisonment and reputational damage.

"The introduction of new compliance obligations following South Africa's greylisting and concerns about state capture is not the end of the story. SARS has expanded its registration process for income tax to ensure tax compliance"

Expanding accountable institutions

In anticipation of being placed on the greylist or potentially avoiding it, the Financial Intelligence Centre (FIC), established under the Financial Intelligence Centre Act (FICA), has expanded the list of accountable institutions. Accountants providing bookkeeping, trust services, trust administration and company formation services are now required to register at the FIC. They must also implement strict procedures to ensure that all staff members report any suspicious transactions, not only those linked to South African trusts. This additional compliance requirement, combined with existing obligations under the FICA, has led small and medium audit and accounting firms to evaluate the risk and cost of providing free or discounted trust and company support.

Significant milestone in combating illicit activities

The implementation of UBO and FIC reporting requirements represents a significant milestone in South Africa's ongoing efforts to combat money laundering, tax evasion and other illicit activities. By collecting and cross-referencing UBO information with data from various stakeholders, the authorities aim to identify individuals who may be using complex ownership structures to conceal their true interests. The FIC intends to collect data on any transaction that may appear suspicious and raise questions about why this measure was not implemented sooner, particularly when suspicions of state capture arose.

Continued compliance obligations

The introduction of new compliance obligations following South Africa's greylisting and concerns about state capture is not the end of the story. SARS has expanded its registration process for income tax to ensure tax compliance. Trusts seeking registration must now provide UBO details to SARS, which will soon be cross-checked with data obtained from other regulatory bodies. This measure aims to uncover potential tax evaders and individuals employing convoluted structures for illicit financial practices. SARS will soon call on all trusts, regardless of size, to provide transactional reporting on all beneficiary transactions.

Instilling confidence in the financial system

By involving third-party data providers in the reporting process, SARS and other regulatory bodies aim to instil confidence in South Africa's financial system and to deter individuals from engaging in illicit activities. By aligning the information provided by trusts and companies with the data accessible to the authorities, discrepancies and non-compliance are more likely to be identified and addressed promptly.

South Africa's regulatory shift aligns with global trends in combating financial crimes and promoting transparency; countries worldwide tighten regulations and increase scrutiny of financial transactions to prevent money laundering, tax evasion and terrorist financing.

Creating a secure and trustworthy financial environment

South Africa's decision to designate trusts and companies as third-party data providers and to require the reporting of UBO details is a significant step towards enhancing transparency and combating illicit activities. By aligning with global trends in financial accountability, the country aims to strengthen its financial system, deter tax evasion and eliminate the misuse of complex ownership structures. As South Africa moves forward, it is poised to create a more secure and trustworthy financial environment, fostering both local and international confidence in its economy.

Conclusion

South Africa's inclusion in the grey list by the FATF has prompted the implementation of mandatory regulations demanding the disclosure of UBO details by companies and trusts. The country's efforts to combat financial crimes and promote transparency in corporate governance have positioned it at the forefront of international endeavours in this regard. By involving third-party data providers and expanding reporting obligations, South Africa aims to strengthen its financial system, deter illicit activities and foster a more compliant and trustworthy financial ecosystem. Continuous monitoring, collaboration among stakeholders and adaptation to emerging challenges will be crucial to the success of these measures.

15 minutes CPD

Tax practitioners be warned: Remain compliant!

ADRIAN MODIKWE, Legal and Compliance Officer at SAIT

The relationship between SARS and recognised controlling bodies (RCBs) in regulating the tax profession is aimed at safeguarding uniform standardisation and enforcement of professional rules and standards to enhance professionalism within the field of taxation. In recent years, there has been more robust engagement between relevant RCBs and SARS.

Section 240A of the Tax Administration Act 28 of 2011 (the TAA) requires all tax professionals in practice to register with an RCB and SARS. Without RCB and SARS registration, an individual has no legal and regulatory authority to act as a tax practitioner or render tax services for a fee. Failure to comply with the above provision may result in criminal prosecution against the offending individual. Furthermore, default in the proper maintenance of compliance with RCB standards, including tax practitioner compliance requirements, may lead to disciplinary measures, including revocation of professional membership and registration with SARS.

Operating as a tax practitioner without the necessary registration constitutes a criminal offence. Consequently, if convicted, the tax practitioner may be liable for substantial financial penalties and/or imprisonment in terms of section 234(2)(c) of the TAA.

The utility in RCB membership is glaring as they play multiple roles in the professions under their exclusive regulation. Apart from regulation and professional recognition, a tax professional gains access to services such as compliance and technical support services. A value-added support benefit for members of the South African Institute of Taxation (SAIT) lies in this institute's exceptional ability to foster proper representation, facilitate relevant education and deliver unprecedented access to SARS through direct escalation networks.

Compliance with professional and ethical standards

In terms of professional regulation, a member gets to understand their role and obligations in the larger professional community. SAIT maintains professional and compliance standards by setting membership eligibility and retention criteria, tailor-made codes of conduct that incorporate SARS regulations and relevant statutory requirements. Additionally, SAIT members are provided with useful guidelines on diverse ethical standards to apply when confronting professional/ethical dilemmas.

Below, we briefly examine two prominent areas of non-compliance with relevant codes, rules and standards of professional conduct, namely disciplinary records and contingency fees.

a) *Disciplinary records - General*

Although listing all potential reasons for disciplinary action or deregistration is challenging, disciplinary history is worth noting. Members who fail to abide by RCB codes and SARS standards may be found to be negligent or otherwise guilty of unprofessional conduct (e.g. failing to timeously and properly file tax returns). Depending on the merits of each case, sanctions range from formal reprimands, financial fines and membership suspension to termination of membership. Operating within prescribed professional and ethical standards is a foolproof way to ensure an immaculate disciplinary record which inevitably affects a tax practitioner's standing, as RCB disciplinary records are distributed to SARS annually.

b) *Contingency fees*

Another example is raising contingency fees against taxpayer refunds which creates a '*perverse incentive*' resulting in a conflict of interest affecting a practitioner's integrity and objectivity; this may eventually obstruct the administration and collection of tax revenue. The return itself cannot give rise to any contingency fee, the extent of any refund or 'saving' can be determined only once SARS raises the assessment. It is only then that the contingency fee might arise and the amount thereof be reasonably quantifiable. Therefore, at face value, contingency fees can allow a tax practitioner to charge fees that are not commensurate with the work done.

Compliance with regulatory requirements

SAIT evaluates and monitors member compliance with industry-specific regulations and statutory requirements enforced by SARS. The main focus areas in terms of regulatory compliance requirements are:

a) *Individual/personal tax compliance*

Tax practitioners should be aware that SARS has the power to deregister tax practitioners under the Tax Administration Act, 2011 due to:

a) non-compliance with tax (Section 240(3)(d)) or
b) existing criminal record and conviction for crimes involving dishonesty and/or fraud (Section 240(4)).

Tax practitioners are expected to lead by example by ensuring that their personal tax affairs are always in good standing. Default in preserving personal tax compliance (i.e. tax debt or general tax non-compliance) raises doubts within SARS and SAIT about the quality and standards of a defaulting tax practitioner's professional work.

Tax practitioners are regularly deregistered for non-compliance with personal tax. According to SARS rules, a mandatory six-month suspension period is applied and deregistered tax practitioners are excluded from registration with any other RCB during this suspension period.

Deregistered tax practitioners are then liable to demonstrate tax compliance for a cumulative period of six months in the preceding twelve-month period before SARS will consider lifting the deregistration and authorise the particular tax practitioner to re-enter practice.

To avoid failing this unique application of the fit and proper person test and to prevent deregistration, all tax practitioners must ensure that they remain tax compliant.

b) *Criminal-free status*

A criminal and/or professional disciplinary history bearing features of criminal fraud/ misrepresentation and other forms of dishonesty deprive an individual of the right to hold an office of trust. Accordingly, all tax practitioners are required to submit a criminal clearance declaration annually. A sworn affidavit must be submitted every five years confirming that their criminal-free status and disciplinary records have remained unblemished.

c) *Continued professional development (CPD)*

Members are required to meet certain professional membership obligations to remain registered with SARS as a tax practitioner. Compliance with the minimum prescribed CPD hours requires a member to complete eighteen hours of verifiable CPD annually.

These hours comprise:

- Ten hours of tax-related learning.
- Six hours of profession-related learning (i.e. accounting, finance, law).
- Two hours of ethics.

Failure to complete these minimum prescribed CPD hours may lead to a fine for each year of default, should a member be referred to the disciplinary board.

Other areas of non-compliance

Non-compliance can be established in other instances of consistent breaches of membership terms and conditions or professional rules and regulations:

- Failure to provide updated membership compliance documentation upon request;
- Poor payment habits/history of annual membership fees;
- Failure to abide by the findings of the disciplinary board;
- Failure to respond to and comply with the annual SARS Compliance Audit; and
- Failure to adhere to SAIT policies.

"Operating as a tax practitioner without the necessary registration constitutes a criminal offence. Consequently, if convicted, the tax practitioner may be liable for substantial financial penalties and/or imprisonment"

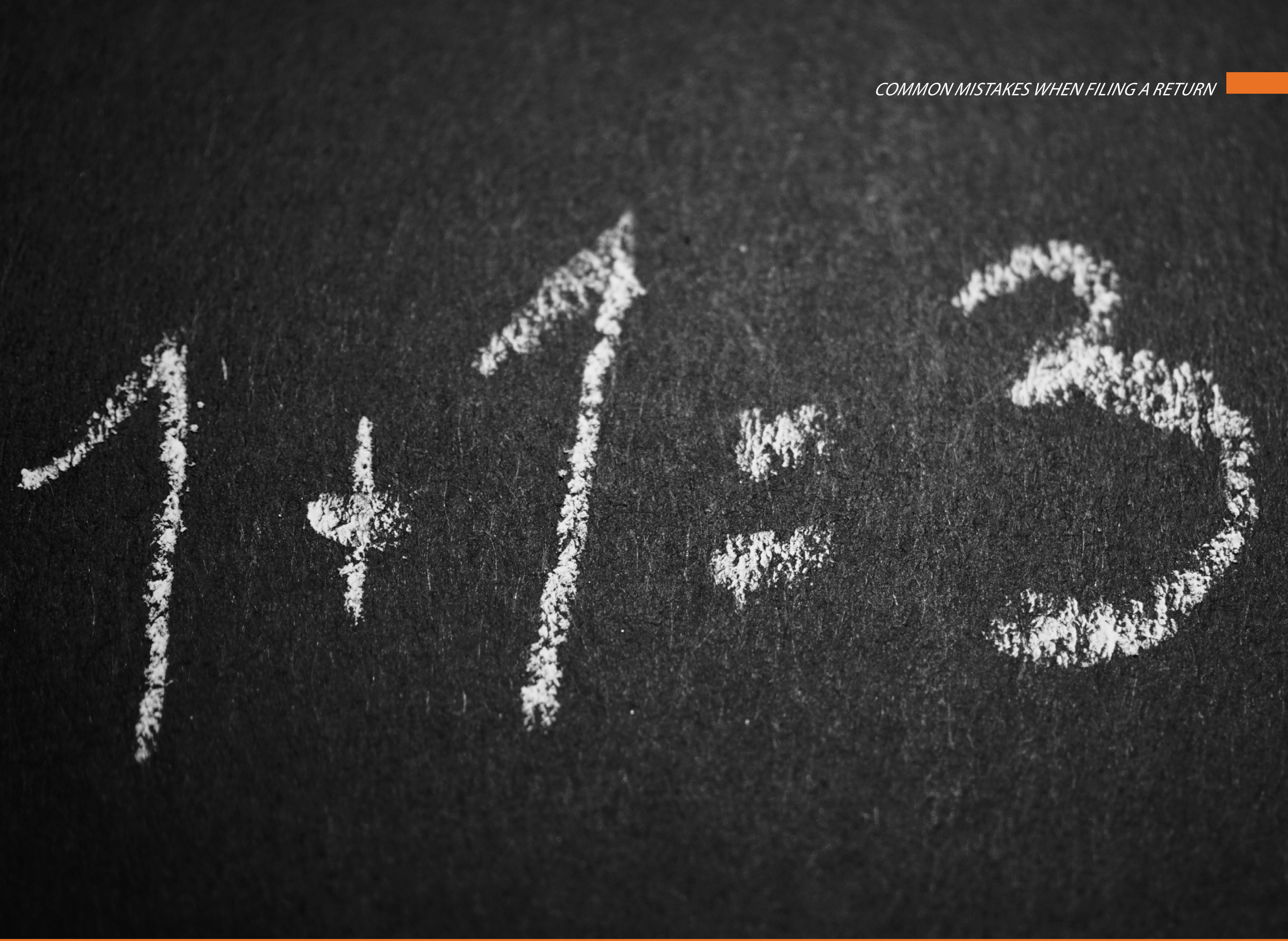
Penalties for non-compliance

Meeting the above key membership and tax practitioner compliance requirements can ensure that a member avoids one or any combination of the following penalties:

- Temporary suspension of membership and registration;
- SARS deregistration (expulsion for six months);
- Entry into non-compliant list published online and distributed to SARS and relevant RCBs;
- Exclusion from any RCB membership or registration; and
- Permanent termination of membership and registration.

Engagement between SARS and RCBs has created a new space for meaningful dialogue. Still, with increased enforcement and deregistration of tax practitioners for non-compliance with membership obligations, various applicable codes and laws, including proper maintenance of personal tax obligations, SAIT members and the collective tax professional community are strongly encouraged to consider their respective compliance as an integral part of their professional careers as opposed to a mere grudge purchase. In essence, the potential adverse repercussions for non-compliance do not outweigh the efforts it may require to maintain healthy compliance.

As the famous quote by Miguel de Cervantes goes: "*Forewarned is forearmed . . .*"



30 minutes CPD

COMMON MISTAKES
WHEN FILING A RETURN

▶ **NYASHA MUSVIBA,** Tax Director at SA Tax Guide

Before submitting your ITR12, check your tax return against this list of common errors and save yourself the time and hassle of setting things right.

Completing the tax return without obtaining supporting documents

Many individuals wrongly believe that an IRP5 tax certificate is the only supporting document they need when completing the ITR12 for individual tax returns. Not only are there several other supporting documents you will probably need, depending on your tax affairs, but you are also required to keep them safely in your possession for at least five years. This is in case SARS needs access to them in future.

Below is a list of some of the documents you may need:

- IRP5/IT3(a) certificate from your employer (if you had more than one employer in the tax year, you need an IRP5 from each employer)
- Medical aid certificate as well as documents reflecting amounts claimed in addition to those covered by your medical aid
- Pension and retirement annuity certificates
- Proof of your banking details (see below)
- Travel logbook if you have received a travel allowance and an accurate record of all vehicle expenses during the year, including fuel, maintenance, lease and insurance costs
- Tax certificates (IT3(b)) which you received in respect of investment income
- Completed confirmation of the diagnosis of disability form (ITRDD) for taxpayers or dependants with a disability
- Taxpayers who receive foreign employment income must keep a schedule of days spent outside South Africa with copies of passport pages showing exit and entry into South Africa
- Financial statements for individuals who conduct a business as a sole proprietor, if applicable
- Information relating to capital gain transactions, if applicable
- Any other documentation relating to income you received or deductions you want to claim

As proof of banking details, you need a bank statement not more than three months old, which must also be stamped by the bank. If you cannot provide a bank statement, you must provide an original letter, on a letterhead from the bank, reflecting the bank account details and the date the account was opened. The bank statement or the bank letter should clearly show the name of the bank, the name of the account holder, the type of account, the account number, the branch code and the date.

An individual who incurred medical expenses that were not covered by the medical aid can deduct an additional rebate which reduces the normal tax payable to SARS. However, you must ensure that you have the prescription or diagnosis or received services and medicines supplied by any duly registered medical practitioner, dentist, optometrist, homoeopath, naturopath, osteopath, herbalist, physiotherapist, chiropractor or orthopaedist. You must also have actual proof of payment for the out-of-pocket medical expenses; medical expense invoices or statements only will not meet the requirements of SARS. (Note that a qualified medical practitioner must diagnose disability to confirm the physical disability status of a taxpayer or dependants with a disability.)

Ensure that you have all the supporting documents before you file your tax return, including the ones prepopulated by SARS on your tax return. Should SARS require supporting documents, you must be able to provide them within the set time limits. If you fail to submit supporting documents requested by SARS, you may receive an adverse assessment and this might leave you owing money to SARS. Individuals must ensure that they have the supporting documents before they complete and submit the ITR12 tax return.

Assuming you will automatically get a refund

Most people are motivated to file their tax returns when they believe that they will get a refund from SARS. On the contrary, taxpayers are required to file an ITR12 if they exceed a certain income threshold or if they have more than one employer. For 2023, it is R500 000 for employees who received income from a single employer and did not receive an allowance such as a travel, subsistence or office-bearer allowance and employees' tax must have been deducted by the employer in terms of the deduction tables prescribed by SARS.

Taxpayers should avoid using the services of people who guarantee a refund from SARS. An even worse situation is a taxpayer who understates or overstates income in their pursuit of a refund. This is a criminal offence.

Using the wrong source codes

Many adverse assessments are the result of the use of wrong source codes. You should take extra care when completing an ITR12 tax return because each source code has a different tax implication. For instance, certain income might be exempt from tax. However, if you use a source code for taxable income, you will be assessed for tax on this income.

If the wrong source codes are used, it will leave you with the burden of submitting a notice of objection. This process is technical in nature and, as a result, you might have to pay for the services of a tax practitioner.

Some employers issue employees with IRP5 tax certificates generated by the payroll systems instead of the ones exported from the SARS e@syFile system. However, there is a danger that the payroll system might have a discontinued source code. An IRP5 with a discontinued or incorrect source code is not a valid supporting document when submitted as part of a SARS review or audit. It is particularly important to ensure that the IRP5 tax certificate contains current source codes applicable to the 2022 filing season.

Source codes can be found on the SARS website by following this link: https://www.sars.gov.za/types-of-tax/personal-income-tax/tax-season/find-a-source-code/

Not understanding the ITR12 return fields on eFiling

Taxpayers often complain that the online ITR12 has too few fields to complete all the information compared to the manual ITR12 tax return. It is important to note that the ITR12 tax return is generated on eFiling when starting a return on the return wizard. To generate a correct return, you must correctly answer the applicable questions on the first page. For example, the first page will ask if a taxpayer has incurred medical expenses. If you select "no" to this question, the relevant medical expenses field will not be created.

Some common questions asked on eFiling include:

- How many certificates did you receive?
- Do you want to claim expenditure against a travel allowance? (Select "Yes" or "No")
- Did you receive remuneration for foreign services rendered? (Select "Yes" or "No")
- Were there any transactions on any tax-free accounts held by you? (Select "Yes" or "No")
- Do you want to claim donations made to an approved organisation? (Select "Yes" or "No")
- Did you make any retirement annuity fund contributions? (Select "Yes" or "No")

Not declaring other income received during the year of assessment

You must declare all the income received during a specific tax year on the ITR12 tax return. Employees usually declare income reflected on IRP5 tax certificates only and ignore income received from other sources, such as rental income.

If, in fact, you did earn other income not reflected in your IRP5 and do not declare it on the ITR12, you will be faced with a dilemma when SARS asks for bank statements as part of supporting documents. Your bank statements will show that you have received other income which was not declared to SARS, which will issue you with an adverse assessment. The adverse consequences of such an assessment include severe penalties for understating income.

Taxpayers have a tax obligation to ensure that full and accurate disclosure is made of all their relevant information as required in the income tax return, including all income received. Misrepresentation, neglect or omission to submit a return or supplying false information is liable to penalties, additional assessments and, in some cases, criminal prosecution.

"Many individuals wrongly believe that an IRP5 tax certificate is the only supporting document they need when completing the ITR12 for individual tax returns"

Provisional taxpayers failing to file provisional tax returns

Some taxpayers are automatically registered as provisional taxpayers. This, in turn, creates an obligation for them to file provisional tax returns as well as the final ITR12 tax return. Failing to file the provisional tax return when it becomes due will make the taxpayers liable for interest and penalties.

There is no formal registration needed to be a provisional taxpayer. A provisional taxpayer is any person who derives income other than from employment or any person who is notified by SARS that they are a provisional taxpayer.

Directors of private companies and members of close corporations are regarded as employees. Therefore they are not automatically registered as provisional taxpayers unless they have income that falls within the scope of provisional income.

Provisional tax is a method of paying the income tax liability in advance to ensure that the taxpayer does not remain with a large tax debt on assessment. A provisional taxpayer is required to submit two provisional tax returns (IRP6) in a year of assessment based on estimated taxable income. The first return is due by 31 August and the second by 28 or 29 February. A provisional taxpayer can make an optional third provisional tax payment after the end of the tax year but before SARS issues the assessment.

Choosing to submit manually

When you are completing an ITR12 return, you should use an electronic submission through eFiling. The easiest and quickest way to file ITR12 tax returns is online by using SARS eFiling. However, you must first register for eFiling on the SARS eFiling website.

There are a number of advantages to eFiling. For instance, you are given the opportunity to save your return and file it later when you are ready to do so. You also have the opportunity to use the tax calculator function to receive a pre-assessment, which is based on your submission, before a final assessment is done. Furthermore, a return filed via eFiling makes it easier to respond to a SARS audit or verification. Submitting a return through eFiling also gives taxpayers a full history of all submissions, payments and electronic correspondence available at the click of a button. In addition, submission via eFiling saves taxpayers time as they will no longer have to wait in long queues at a SARS office when the tax filing season commences.

Not checking the SARS auto-assessment returns

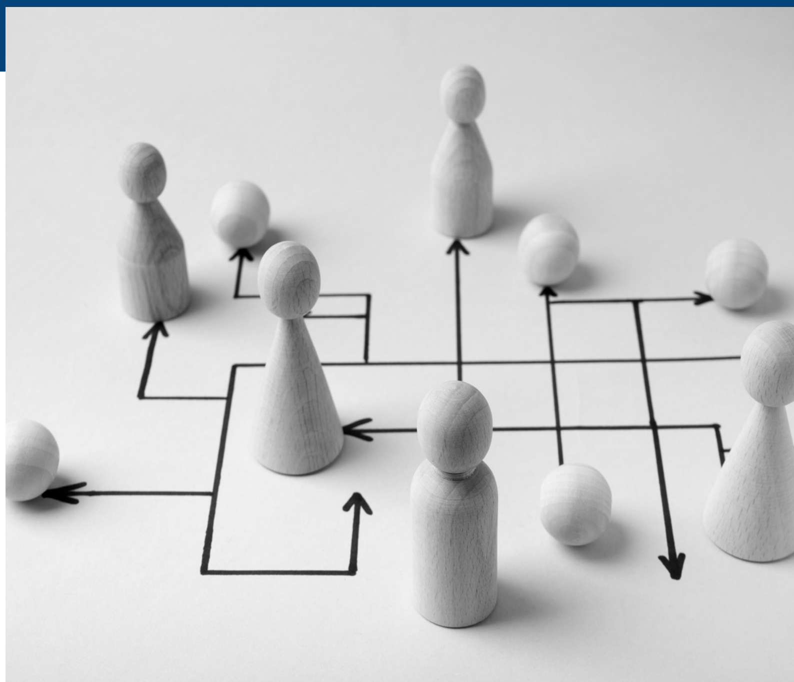
This year, SARS will again issue auto-assessments to taxpayers whose tax affairs are less complicated. SARS receives data from employers, medical schemes, banks, retirement annuity funds and other entities. SARS uses that data to calculate your personal tax assessment. We have noted that if the medical schemes and retirement annuity funds do not have your correct income tax number, the contributions done by the taxpayer will not be prepopulated by SARS. This has caused many taxpayers to owe SARS. You must check SARS' auto-assessments before accepting them.

The previous timeframe of 40 business days from the date of your auto-assessment within which such a return must be filed has been extended to coincide with the normal due date for non-provisional taxpayers. The due date for filing income tax returns for non-provisional taxpayers is 23 October 2023. If an auto-assessment has been issued after 23 October 2023, then the 40 business days will start on the date of the notice of the assessment. Taxpayers who amend or request corrections to be done to the auto-assessed return after the filing due date will be issued with administrative penalties by SARS, which treats amendments or corrections to the income tax return after the due date as late filing of the tax return.

15 minutes CPD

SARS eFILING—
Optimising user roles and rights groups as a first step in dealing with unexpected challenges

▶ **ARIVAN SATHASIVAN,** Associate Director: Indirect Tax Services at EY, **JOHANNAH RACHIDI,** Manager: Indirect Tax Services at EY, & **YOLISA DYASI,** Tax Technical Consultant at SAIT



The years since July 2019 have seen some significant and exciting improvements to SARS eFiling, which have often left taxpayers and tax practitioners having to adjust to keep up quickly.

Old registrations need careful attention as upgrades sometimes require eFiling users to go into legacy settings to make adjustments there. Such adjustments may require updates to entity names, types and entity registration numbers, which could even require a meeting with SARS so that updates and mergers are approved.

An often-overlooked item that could create some unforeseen limitations on profiles that have been migrated from legacy systems relates to user roles and rights groups.

As a starting point, it is important to understand the function of user roles and the use of rights groups. Understanding these functions will be the first step in dealing with unexpected challenges.

What are user roles and rights groups?

Frequently, the main eFiling profile owner in smaller tax firms would be the tax director or main tax practitioner in practice. The tax director or tax practitioner would add their clients to this profile to execute their tax mandate. Typically, however, the client's day-to-day compliance work would be done by the junior staff working under the supervision of the tax practitioner. Because the sharing of eFiling usernames and passwords is frowned upon by SARS, the tax practitioner would then have the option to add 'users' to their eFiling profile. This would then allow the junior staff to carry out their day-to-day compliance work by logging into their own eFiling profiles while still having access to the client base.

'User groups' is the grouping of similar users who would be assigned similar roles. For example, where all the office administrators are granted 'view only' rights to ensure that they can see which returns have been submitted but they would not necessarily be able to submit returns themselves.

What types of user rights and user groups exist?

When adding a user to an eFiling profile, there are 14 different user roles that can be assigned to a user, five of which specifically relate to customs. Among others and most importantly, these roles include:

- 'Manage Users', which allows users to add and change users and assign them to groups;
- 'Manage Taxpayers' which allows users to add and change taxpayers;
- 'Manage Groups' which allows users to create and change groups and assign users and taxpayers to groups;
- 'Directives' which allows users to access the tax directives functionality; and
- 'Perform Bulk and Additional Payments' which allows users without full admin rights access to perform bulk and additional payments.

Any user who has not been assigned specific roles will not be able to perform that specific function.

Rights groups further allow the profile owner to assign more specific roles to each user. For example, a Corporate Income Tax specialist may be granted 'submission' rights to the "Organisation Income Tax", "Provisional Tax" and "IT Admin Penalty", thus ensuring that they do not do any work on the value-added tax (VAT) and pay as you earn (PAYE) tax types, as this may not be their areas of expertise.

Why are these functions important?

The segregation of duties (SoD) is an essential element of system control. Auditors often look for duty segregation as part of their analysis of an entity's system of internal controls. SoD serves two key purposes:

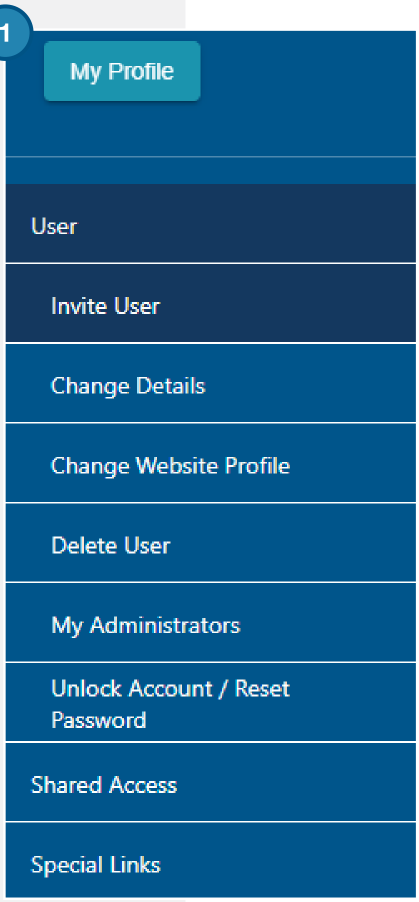
1) It ensures that there is oversight and review to catch errors; and
2) It helps prevent fraud or theft.

In 2021, SARS received an extremely high number of fraud cases, where unauthorised access and unauthorised usage of eFiling profiles were reported. Therefore, it is unsurprising that these stricter measures were put in place to ensure that anyone working on eFiling is authorised to perform those functions.

How to assign user rights (with screenshots from eFiling)

As a first step, confirming the user roles on the portfolio is a good idea. This can be done by simply logging into the portfolio by clicking on "User" at the top, then again on the side and then by selecting "Change Details".

1



2 Once in the "Change Details" section, ensure all required user groups and roles are assigned. Remember to double-check that all required groups are selected.

3

Once this has been done, proceed to "Organisations", then "Rights Groups" and then select the "Manage Groups" section.

- [x] System Default

USER ROLES

- [x] Manage Transfer Duty Financial Account
This role allows users to maintain all financial detail against the Transfer Duty account
- [x] SARS Registration
Can register taxpayers with SARS to get tax reference numbers
- [ ] RLA - View Customs Product information
RLA â€" View Customs Product information
- [ ] RLA - View Client Type
RLA - View Client Type
- [ ] RLA - Manage Customs Product information
RLA â€" Manage Customs Product information
- [x] RLA - Manage Client Type
With this profile, users can only view and change information relating to their specific client type(s)
- [x] Manage Users
Can create & change users and assign them to groups
- [x] Manage Taxpayers
Can create & change taxpayers and assign them to groups
- [x] Manage Groups
Can create & change groups and assign users and payers to groups
- [x] Manage Excise Financial Account
This role allows users to maintain all financial detail against an Excise Account
- [x] Manage Deferment Account
- [x] ISV Activation
This role allows users access to the ISV activation screen
- [x] Directives
- [x] Perform Bulk and Additional Payments
This role allows a user without full admin rights to perform bulk and additional payments.

Note: If no groups or roles are assigned to a user, the user will have limited access once logged into eFiling.

Continue | Back

- Organisation
- SARS Registered Details
- Employee Registration
- Admin Reports
- Rights Groups
  - Manage Groups
  - Organisation Setup
- Customs Registration
- Special Links

UPDATE GROUP DETAILS

Group Name	System Default
Authorisation Level	Submissions (Submissions / Completions / View Only)
Access To Payments	
Tax Types	Provisional Tax (IRP6) Value Added Tax (VAT201) Organisation Income Tax (ITR14/IT12EI/ITR12T) Individual Income Tax (ITR12) Employee's Tax (EMP201) IT56 - Secondary Tax On Companies (STC) EMP501 - Submission Customs Agent Excise Agent VAT Admin Penalty PAYE Admin Penalty IT Admin Penalty Transfer Duty Third Party Appointment Banks Dividends Withholding Tax (DWT) Third Party Appointment Employers Third Party Appointment Other Tax Compliance Status Tax Compliance Status Verification IT3 Medical Scheme Contribution Insurance Payment Withholding Tax on Interest(WTI) Foreign Tax Information (FTI) Mineral Royalties (MPR3) CBC TRN (Tax Reference Number) Directives ITR12 Cancelled Foreign Tax Information (FTI) DELETED
Do you want to import taxpayers from an existing group?	( ) Yes (•) No

Update | Delete Group | Back | Check All | Uncheck All

4

The above simple steps will ensure that the user has the required access and ability to perform their mandate on the client's profiles.

For older profiles, it is not uncommon to find that some user rights have not been selected, particularly relating to "Tax Compliance status and verification" and you will need to select and then update them.

What happens when the rights are revoked or the user is deleted? Once the user rights are revoked on eFiling, that user will no longer be able to perform the functions previously assigned. Similarly, if the user is deleted from the main tax practitioner profile, the user will no longer have access to the client's records.

OPPORTUNITY OR RISK: THE NEW SARS AIT TAX CLEARANCE STATUS PROCESS

15 minutes CPD

▶ **THOMAS LOBBAN,** Head of Cross-Border Tax at Tax Consulting SA

On 24 April 2023, SARS announced the 'new enhanced' Tax Compliance Status (TCS) processes that were applicable with immediate effect. The changes that SARS announced included the discontinuation of the Tender TCS application, as well as the consolidation of the Foreign Investment Allowance (FIA) and Emigration TCS application types into one; these were dubbed 'Approval International Transfer' (AIT).

In the media statement issued on 3 May 2023, SARS confirmed that the enhanced TCS system would aim to make the process easier for compliant taxpayers and to improve turnaround times in these cases; however, this system would also aim to make it 'harder for taxpayers who are unwilling to comply'. Put differently, where the AIT process is concerned, SARS is tightening the compliance screws for those with skeletons in the closet.

The new compliance standard—SARS' gambit

In the past, SARS has sometimes been criticised for lack of enforcement in the face of tax non-compliance. There is perhaps a portion of South African taxpayers who have a nonchalant approach to tax compliance.

They may have been lulled into a false sense of security in the belief that SARS does not take notice of discrepancies or take umbrage with inaccurate or absent disclosures.

According to SARS, as the previous TCS process had been operational since April 2016, it had processed substantial and growing volumes of taxpayers requesting third-party verification, including verification for FIA and Emigration. Given the removal of the separate South African Reserve Bank emigration application requirements, the changes to SARS' processes and forms were necessary.

However, one should also consider the impact of the greylisting of South Africa by the Financial Action Task Force in February 2023 which was prompted by South Africa's failure to adequately tackle illicit financial flows. It was thus inevitable that significant changes in SARS policies were on the horizon.

Confirming the focus on compliance enforcement, SARS has further mentioned in its media statement that the additional information requested "*allows SARS to ensure that all required tax payable has been accounted for and, if required, address any non-compliance that is detected through a verification and/or an audit*".

Opportunity or risk?

The AIT process requires a much deeper level of disclosure on behalf of the taxpayer concerned compared to its previous iterations. The taxpayer is expected to make full disclosure of the sources of the amount to be remitted abroad, with an expansive list of supporting documentation required. This is in addition to full disclosure of local and foreign assets and liabilities (at cost), as well as other strict requirements by SARS. This could be simple in some cases—in others, however, not that much.

In a poll from a training session held for SAIT members and hosted by Jerry Botha, Managing Partner at Tax Consulting South Africa, 71% of the attendees believed that the enhanced AIT process was implemented to audit wealthy taxpayers to uncover potential non-compliance.

Regarding the additional documentary requirements for the AIT application, 82% of the attendees were of the view that, given the level and risk of criminal sanction, the assistance of a tax practitioner and/or an accountant is now an essential element in this process. Overall, 82% of attendees believed that the new AIT process would involve significantly and materially more work.

Compared with the poll results from a previous session on the same topic, hosted for members of the Financial Planning Institute, 88% of the financial advisors believed the AIT process to be significantly different and materially more work. Therefore, the advisory market appears aligned that the new AIT process is not something to be ignored. Notably, 70% of financial advisors believed that both a financial advisor and a tax practitioner are required for the new AIT process. They are probably required because assets and liabilities, both local and foreign, are required to be disclosed on a cost price and market value basis. The cost price disclosure is requested at the submission of the AIT, whereas the market value for three years is requested at the supporting documents stage. It is unclear whether SARS will retain this request for all AIT applicants or if this is limited to certain higher value or higher risk segments only.

This presents an opportunity for tax practitioners to add more value and to expand their practices. However, it also presents new potential risks for both practitioners and their clients because the AIT is a permanent record created; they will effectively remain visible on eFiling for an indefinite time.

Unchecked, check, checkmate

Anyone who has practically worked through the entire new AIT process can attest to the stringent level of taxpayer scrutiny. As one delves deeper into the process, one may be left with more questions than answers about the required disclosures. At the same time, any missteps made may be met with further verification requests by SARS, a rejection of the application or a stringent audit of the taxpayer's affairs.

Presumably, tax practitioners, who are keenly aware of the risks presented by this level of scrutiny by SARS are uniquely poised to tackle this new challenge. However, it is important to ensure that a consistent approach is taken. Where a client does not make full disclosure of their interests to the tax practitioner, this can quickly backfire and result in tax practitioners having to face difficult questions from SARS and/or their client.

"There is perhaps a portion of South African taxpayers who have a nonchalant approach to tax compliance. They may have been lulled into a false sense of security in the belief that SARS does not take notice of discrepancies or take umbrage with inaccurate or absent disclosures"

Further, the AIT process invokes a necessary tactical change to one's approach in practice where it is required, such as section 235(2) of the Tax Administration Act, which places the onus on a practitioner to prove that a false statement made (e.g. the disclosure of incorrect amounts in an AIT application) was not negligent, and that there was a reasonable possibility that they were not aware of the falsity.

Follow the money

Any taxpayer who emigrates or resident who seeks to transfer more than R1 million from South Africa within a year would first be required to confront any historic non-compliance. Where the taxpayer does not directly deal with this, their children or legatees may otherwise have to do so at a later stage. It should suffice to say that this is now an essential element to factor into one's tax planning.

SARS questions will arise where, for example, it is determined that the taxpayer has undisclosed wealth beyond their means based on a mismatch between their AIT disclosures and the disclosures made in their previous tax returns. This new reality thus requires that tax practitioners measure twice and cut once when completing an AIT application for their client.

A focus on the historic compliance of a taxpayer and a proper understanding of the disclosures to be made in the AIT application has moved beyond being a mere tool in one's arsenal as a tax practitioner. Rather, we foresee this becoming a very important component of a holistic services offering.

The AIT process is no mere exercise in filling in a form—these disclosures will add up in a world where eFiling and evolving electronic data capabilities will never forget. The more sophisticated the taxpayer's affairs are, the higher the level of scrutiny will be and the more important it becomes to ensure that the correct expertise is engaged to ensure success.

When embarking down this road, it is important to remember that a careful, strategic and consistent approach to the AIT application process is essential to avoid becoming the canary in the coal mine for others to follow. When in doubt, especially when it comes to tax, conservatism is always the best approach.

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30 minutes CPD

CLAIMING YOUR SOLAR REBATE: BE CAREFUL

PROFESSOR HERMAN VIVIERS, Associate Professor, School of Accounting Sciences, North-West University

We all know the saying that "*If something sounds too good to be true, usually it is*". This raises the question of whether the recent 2023 National Budget announcement regarding the proposed tax incentive for individuals who choose to invest in solar panels will be that beneficial. Hence, will this really constitute a light in the dark South African power crisis tunnel for taxpayers or not?

The objective behind the proposed tax incentive is held to encourage private investment by individuals in solar electricity generating systems that will aid in addressing South Africa's power supply crisis.

The purpose of this article is to take a closer look at, and to critically evaluate, the recently announced renewable energy tax incentive proposed for individuals. Also, this article explains how this proposed tax incentive will impact an individual's normal tax calculation. Although the proposed tax incentive for individuals is currently subject to public comments for consideration by National Treasury, it is aimed to be formally introduced into the Income Tax Act as part of the 2023 legislative amendment cycle. It is important to note that a renewable energy tax incentive has also been newly announced for businesses; however, this incentive falls outside the scope and purpose of this article.

"Taxpayers subject to employees' tax will only be able to claim the solar panel rebate for the first time during the 2023/24 tax filing season. However, cognisance should be taken of the fact that the rebate will be allowed to be considered when determining and submitting provisional tax payments regarding the individual's 2024 year of assessment"

What is the proposed tax incentive for individuals?

Individuals (natural persons) will be able to claim a solar rebate to the value of: 25% based on the cost of new and unused solar photovoltaic (PV) panels but limited to a maximum rebate amount of R15 000 per individual.

The reason why it is a requirement that the solar panels must be "*new and unused*" is to ensure that additional capacity will be generated than what is already available as part of the attempt to curb the current power supply crisis. However, it is not that simple and straightforward. The solar panels must also adhere to the following additional requirements to qualify for the solar panel tax rebate:

- The minimum capacity/design output must be 275 watts (W) per solar panel;
- Panels must be installed, as portable solar panels will not qualify for the solar panel tax rebate; and
- Panels can either be installed as part of a new system or as an extension of an existing system at a residence that is mainly used by an individual for domestic purposes.

Evaluating the feasibility and reasonableness of the solar panel tax incentive for individuals

Although the prices for solar panels in South Africa will vary based on the region, the panels' watt (W) capacity and the type of panel manufacturer and/or supplier, solar panel prices range, on average, between R1 800 for a 360W solar panel and R4 200 for a 550W solar panel (inclusive of VAT). The average household uses between six and fourteen 455W capacity solar panels and up to approximately 23 panels for bigger homes.

In evaluating the former statistics to those of the tax incentive proposed for individuals, where a rebate of 25% based on the cost of the solar panels only, will be allowed but limited to a maximum rebate amount of R15 000, the following could be deduced:

- A maximum rebate of R15 000 means that the maximum expense amount allowed to be incurred by a single individual in the acquisition of solar panels that will rank for the solar panel tax rebate is R60 000 (i.e. R15 000 ÷ 25%). As most individuals are not registered value-added tax (VAT) vendors, it means that this maximum expense amount of R60 000 represents the cost for solar panels inclusive of VAT.
- This means that the solar panel tax rebate enables a single individual, on average, to purchase (in a worst-case scenario where 550W panels are required) up to 14 solar panels for a single household (i.e. R60 000 ÷ R4 200 per 550W solar panel = 14 solar panels in total).
- For spouses or couples living together, each spouse or partner will qualify for its own maximum rebate amount of R15 000, given that each spouse or partner should separately incur and pay for the acquisition of solar panels for their joint home. This means that for bigger households, the solar panel tax rebate, on average, enables the installation of up to 28 solar panels at a single home (based on a total solar panel cost of R120 000 paid by two spouses or partners in equal parts).

"The risk prevails that there is room for manipulating profit margins on the supply of solar system equipment and labour costs to enable an individual taxpayer to claim the maximum allowed rebate of R15 000 in full"

However, the risk prevails that there is room for manipulating profit margins on the supply of solar system equipment and labour costs to enable an individual taxpayer to claim the maximum allowed rebate of R15 000 in full. The latter applies despite instances where the actual total cost of an individual's solar panels is far below the maximum expenditure limit of R60 000. This room for manipulation is illustrated by way of the following example:

Mr A (individual taxpayer) wants to install a solar panel system at his private residence during June 2023. The system that matches his power needs will require the installation of ten 550W solar panels at the cost of R4 200 (inclusive of VAT) each. Hence, his total solar panel expense will amount to R42 000 (inclusive of VAT), making him eligible to qualify for a solar panel tax rebate of R10 500 (calculated as 25% x R42 000). However, to claim the maximum allowed rebate of R15 000 (as opposed to R10 500) instead, Mr A and a contractor arrange that the profit margin on the solar panels will be inflated to a total cost of R60 000 (inclusive of VAT), while the profit margins on the other equipment (an inverter, batteries, etc.) and labour needed for the installation, which the same contractor will also supply, are to be reduced. In return for the favour granted by the contractor to balance out (manipulate) the profit margins on the various goods and services to be supplied, which will enable his client to claim the maximum allowed solar tax rebate of R15 000, Mr A will elect the contractor and make use of their services as his preferred supplier.

To combat the risk of possible profit-margin manipulation, the tax regulator needs to consider additional measures to be put in place that will require a valuation of solar panels' fair market value that would apply between independent persons dealing at arm's length prices before the solar panel tax rebate is granted.

Furthermore, the fact that the announced tax incentive for individuals is only available for a limited time period raises uncertainty regarding its effectiveness and the actual reasons and/or true intentions behind its introduction. For individuals, it has been indicated that the tax incentive will only apply for one year. Moreover, to qualify for the rebate, the individual taxpayer must furnish a valid Certificate of Compliance (COC) as issued in terms of the Electrical Installation Regulations (2009), evidencing that the solar photovoltaic (PV) panels were brought into use for the first time during the period between 1 March 2023 and 29 February 2024. This time-period limitation was motivated by National Treasury as a measure to encourage individual taxpayers to invest in renewable energy systems as soon as possible. However, this motivation is regarded as non-plausible when evaluated against the current weak South African economy in which cash-strapped consumers need to operate and which is associated with quarterly increases in the interest rate. In reality, the cost to acquire and install a solar panel system is expensive; so is the cost of financing.

- According to media reports published during 2022, ESKOM tried, through its tariff application to the National Energy Regulator of South Africa (NERSA), to continue charging on-grid solar users a standard fee per month, despite the fact that they have discontinued using grid electricity. Attempts such as the latter are perceived as a concern in evaluating the true rationale behind the time-period limitation placed upon the announced solar panel tax rebate. The possibility exists that the proposed solar panel tax rebate might only be a smoke screen for SARS to take stock of who have solar panel systems and for this information to be shared with ESKOM for possible future penalties to be imposed on taxpayers for leaving the ESKOM grid (either permanently, or temporarily when applying a hybrid solar panel system). The latter might also be perceived as a possible violation of taxpayers' and/or consumers' rights.

"Solar panels installed at one's private residence for domestic use will qualify as personal-use assets (in terms of paragraph 53 of the Eighth Schedule to the Income Tax Act), meaning that any possible capital gain or loss that might realise upon disposal will need to be disregarded for normal tax purposes"

In addition to the COC document requirement, an individual must also be able to furnish a valid VAT invoice (with supporting proof of payment) which indicates the cost of the solar panels. However, it is not a requirement to have a separate invoice for the cost of the solar panels only. A single invoice containing the supply of numerous goods and services will be accepted as long as the cost of the solar panels is indicated separately from the other items on the invoice. Hence, it is important to note that the cost of solar panels only will qualify for the tax rebate. The latter is held to be unfair towards the taxpayer because the installation and operation of an effective solar generating system does not only require solar panels but also other equipment (a converter, batteries etc.) that will not qualify for any type of tax relief in the hands of the individual taxpayer deciding to invest in a solar panel system.

The final aspect to consider is the high risk of being selected upon assessment by SARS for audit and verification purposes when you are trying to claim your solar panel rebate. SARS might take the same aggressive audit and verification approach as it has applied to taxpayers who wanted to claim home office expenditure for working from home during the COVID-19 Pandemic period. If so, this might place an additional administrative burden and even an additional compliance cost upon individual taxpayers.

Impact of the solar panel tax rebate on an individual's normal tax calculation

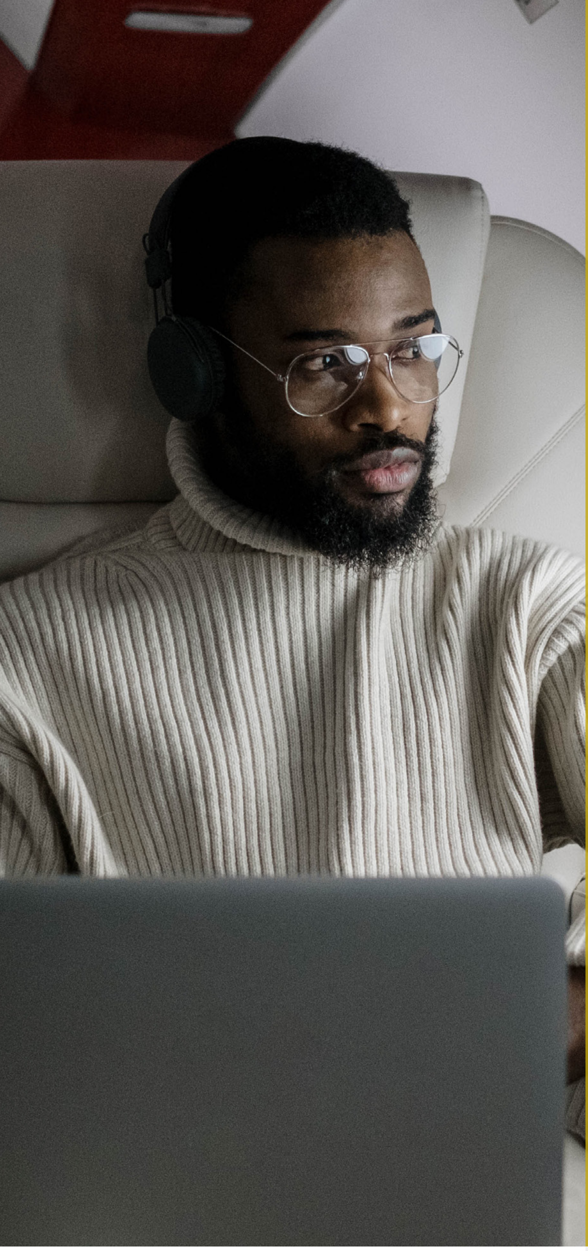
Since the tax incentive is granted in the form of a rebate against one's normal tax liability and not as a deduction against income (or taxable income), it means that a natural person must first be liable for normal tax before they are able to benefit from this tax incentive. Like other normal tax rebates available to natural persons, it is submitted that this solar panel tax rebate will also not be allowed to create or increase an assessed loss position in the hands of a natural person taxpayer.

The benefit of the tax incentive being granted in the form of a rebate rather than that of a deduction or a capital allowance is that a rebate can never be recouped. Hence, in the event that the solar panels are sold as part of a residence or damaged and indemnified by way of an insurance pay-out, the individual will not have to recoup any amount, meaning that no normal tax effect will be triggered upon the subsequent actual or deemed disposal of the solar panels. Solar panels installed at one's private residence for domestic use will qualify as personal-use assets (in terms of paragraph 53 of the Eighth Schedule to the Income Tax Act), meaning that any possible capital gain or loss that might realise upon disposal will need to be disregarded for normal tax purposes. However, as an anti-avoidance measure to prevent potential abuse, it was indicated that there might be a clawback of the rebate in the event that the individual sells their solar panels within one year after it was first brought into use.

Taxpayers subject to employees' tax will only be able to claim the solar panel rebate for the first time during the 2023/24 tax filing season. However, cognisance should be taken of the fact that the rebate will be allowed to be considered when determining and submitting provisional tax payments regarding the individual's 2024 year of assessment.

Take away

In conclusion, it is therefore clear that there are numerous aspects to be considered by individual taxpayers before the decision is taken to invest in a solar panel generating system. One of these considerations is the decision to claim the proposed solar panel tax rebate and its impact on, and related consequences for, such taxpayers' normal tax calculation.



15 minutes CPD

Working abroad but South Africa is still my real home: The impact of section 10(1)(o)(ii)

▶ **NIKKI KENNEDY,** Founder and co-owner of NK Accounting Services and Lecturer at Akademia

Many South Africans jump at the opportunity to work abroad, earning those lovely dollars, pounds or euros.

However, while working abroad, some of these South Africans are working for an employer who would likely deduct employees' tax from their foreign remuneration; what are the implications to consider in South Africa?

Ordinarily resident of South Africa

Section 1(1) of the Income Tax Act No. 58 of 1962 (hereafter referred to as the Act), provides the definition of a 'resident'. In terms of a natural person (a living, breathing individual), there are two potential types of residents to be considered. The one would be a natural person who is ordinarily resident in the Republic of South Africa. The other would be a natural person who is physically present in South Africa, based on the number of days per year of assessment and looking at this over the prior five-year period, as well as the current year of assessment. It is important to note that the physical presence test is applicable to a natural person who is not ordinarily resident. Therefore, if a natural person qualifies as ordinarily resident, the physical presence test would not influence such a person's tax residency status in South Africa. Furthermore, there is a difference between citizenship and residency status. This article deals with tax residency; it specifically looks at a taxpayer who is ordinarily resident of the Republic of South Africa. Citizenship will typically be determined by place of birth or by applying to become a citizen of a country due to fulfilment of the requirements of the government of that specific country through a formal process after a stipulated number of years residing within the country's borders.

The term 'ordinarily resident' is not defined in the Act and we therefore need to refer to case law for clarification. In *Cohen v CIR* 1946 AD 174, 13 SATC 362, the court found that a taxpayer's ordinary residence would refer to the taxpayer's most 'fixed or settled residence' and that the country where the taxpayer would be ordinarily resident would be the country to which such a taxpayer would return after the taxpayer's worldwide wanderings and thus the taxpayer's 'real home'.

Even though the SARS Interpretation Notes are not binding on SARS and taxpayers, it still provides insights into SARS' likely treatment and the reasoning that SARS will follow when evaluating certain situations. SARS Interpretation Note 3 provides a natural person with some guidance in terms of the ordinarily resident component about the definition of 'resident' contained in section 1(1) of the Act. This interpretation note lists a few factors to consider when determining whether a natural person is ordinarily resident in South Africa. Specific mention is made that the list is by no means exhaustive; rather, it is a guideline of aspects to be considered. These are, among others, the natural person's intention to be ordinarily resident in South Africa; nationality; the most fixed and settled place of residence; the place where that person stays most of the time; the status in South Africa and in other countries; the place where the person's personal belongings are; the place where family and social, cultural and other activities are; and reasons for visits and how regular these visits are. If it has been established that a person is ordinarily resident in South Africa, such a person will be a 'resident' and will be taxed in South Africa on such a person's worldwide income, further to paragraph (i) of the definition of 'gross income' in section 1(1) of the Act.

It is, therefore, critically important to ensure that the taxpayer who is working abroad, understands this and can provide documentary proof to substantiate foreign residency, as it will have an impact on the normal tax payable in South Africa.

R1.25 million exemption on foreign employment income

Section 10(1)(o)(ii) of the Act provides for an exemption of remuneration up to a maximum of R1.25 million per year of assessment. This remuneration includes all forms of foreign employment income, including *"by way of any salary, leave pay, wage, overtime pay, bonus, gratuity, commission, fee, emolument or allowance . . . in respect of services rendered outside the Republic by that employee for or on behalf of any employer".*

An important point to note is that the exemption relates to remuneration. This means that there has to be an employee/ employer relationship from which the income was earned. Therefore, this excludes business income earned abroad because it will not form part of foreign employment income.

There are other requirements to be fulfilled in order to qualify for the exemption. These relate to the number of days that the taxpayer was outside the Republic and thus outside South Africa. These days out of the Republic need to be during the period or periods when the services were rendered. Therefore, the taxpayer was outside the Republic during the same period or periods when the services were rendered for which foreign employment income was earned.

"Taxpayers wanting to work abroad should carefully consider the potential tax consequences of such a decision, especially if they have not yet decided to return to their beloved South Africa"

The days to note here have two requirements and both of these need to be met:

1) Over any 12-month period, the taxpayer was outside of the Republic for more than 183 full days in total. Therefore, any 12-month period may be considered and not only specifically a year of assessment.
2) Over the same 12-month period as mentioned above, there needs to be a continuous period of at least 60 full days outside of the Republic. This means that within the 12-month period in which the taxpayer was outside of the Republic for more than 183 full days for foreign employment, of these 183 full days in total, there would have been a period of at least one consecutive 60 full days out of the Republic.

If both of these two requirements have been met and the income relates to foreign employment income, then the taxpayer, who is ordinarily resident in the Republic (South Africa), may receive the maximum of R1.25 million exemption on that foreign employment income.

The balance of the foreign employment income will then be taxable in the taxpayer's South African income tax return. For this, consideration could be given to the section 6quat rebate in respect of foreign taxes on income.

Conclusion

Taxpayers wanting to work abroad should carefully consider the potential tax consequences of such a decision, especially if they have not yet decided to return to their beloved South Africa only for short visits with family and friends. Furthermore, such a taxpayer might very well be falling within the realm of being ordinarily resident of South Africa even though living and working abroad; therefore, this taxpayer has to account for worldwide income in South Africa and pay tax on foreign employment income in South Africa.

15 minutes CPD

CHANGING TAX RESIDENCE: HEADING FOR THE HILLS

MICHAEL MCKINON, Director of Michael J. McKinon Incorporated

SECTION 1

The changed process

The process of emigrating from South Africa (SA) has undergone significant changes over the past 24 months. The process has moved from a well-understood, regimented, document intensive and fairly lengthy process (i.e. the old MP336(b) process) through the South African Reserve Bank (SARB) to a process that is now administered by SARS. The handover to SARS by the SARB was framed as being part of a wider modernisation of the SARB; however, it seems that it may rather have been part of an ongoing delegation of duties to Authorised Dealers (ADs) by the SARB.

The process is now administered in its entirety by SARS and ends by notifying a local bank, where a bank account is still maintained in SA, of the change in a person's status from tax resident to non-resident so that local remaining bank accounts can be designated as 'non-resident' (there are no more 'blocked accounts'). The process was supposed to have become simpler and less document intensive but we have come full circle. Although the process has now reached a point where it is fairly certain and structured, it has been a rocky road getting here.

At the time of the handover by SARB to SARS, it seemed that SARS was perhaps not completely ready for the handover. Although a process was set out by SARS, the taxpayers, ADs and financial institutions all seemed to have had different views as to what exactly the process was and what documentation was required. This led to much frustration, unnecessary delays and, in some cases, loss of value as the rate of exchange continued to worsen.

In the beginning, we were able to notify SARS of the change in status by disclosing the change on an IT12 tax return and funds were able to be excited out of SA using an 'Emigration' tax clearance. Until recently, some institutions would accept these emigration tax clearances and some would only accept the old Foreign Investment Allowance (FIA) clearance. Some would only accept one of the above clearances and the final confirmation of non-residence from SARS. Some, with the final confirmation letter and the new clearance, the Application for International Transfer (AIT) in hand, as is now the case, require further documentation, which is as extensive, if not more extensive, than what SARB required under the old MP336(b) system.

Approximately six weeks ago, SARS finally changed the system to what seems to be the final and, in our opinion, the correct change. SARS has changed the tax clearance system by simplifying the available clearances to either a 'Good Standing' (a local clearance) or an 'AIT' (an international transfer clearance). The questions that SARS ask in an application for AIT clearance are extensive; yes, it asks many questions but these are, in reality, no more extensive than what the old MP336(b) process asked when the SARB had administered the process. The questions are clear and concise for the moment; it seems that the confusion that existed before has been removed. There are now two documents required, namely the confirmation of non-residence and, if funds are being removed from SA, the AIT tax clearance. We still see some banks calling for tax clearances on emigration even though no funds are leaving SA. We see many taxpayers that have been outside SA for many years who are now notifying SARS of their non-residence status. In these situations, no funds are leaving SA and, in our opinion, to be asking for a tax clearance is a flawed approach. The confirmation of non-residence would just have been issued by SARS and probably by the same department; therefore, this document should be sufficient.

It seems that the ADs have been tasked with taking their own risk-based approach to the handling of changes in tax residence status; this is the cause of differences in the documentation still required after confirmation by SARS. These differences in documentation requirements are, in some instances, still causes for concern and in our opinion, SARS should address these in order to make the process universal, irrespective of which AD or institution is used.

Since the recent changes introduced by SARS, despite some negative views, the system and process seem to have stabilised; it is now more clearly structured.

SECTION 2

Who is leaving SA?

There is a wide range of people who are changing their tax residence from that of South Africa to other tax jurisdictions. The major groups of people whom we consult, include: new graduates leaving university who know they will struggle to find work in SA and who have decided to start their careers offshore; young married couples with newborn or small children who are leaving SA to find safer countries with more certain futures for their children; more mature wealthy families and individuals who are in their mid-to-late careers and who have either made their fortunes or who are well established in their careers; and many who have been factually non-resident, living in other countries permanently for decades and who are now 'cleaning up' their affairs by formalising their changed status with SARS.

"We still see some banks calling for tax clearances on emigration even though no funds are leaving SA. We see many taxpayers that have been outside SA for many years who are now notifying SARS of their non-residence status"

Can you 'emigrate'?

If you are working or living offshore, you fall into one of two camps; you are either a non-resident or you are an expatriate, an 'expat', i.e. a person who is a tax resident in SA but who is temporarily abroad (from an exchange control perspective). The tax consequences of these two statuses are vastly different and very often misunderstood by taxpayers.

Expatriates

Expats are tax residents of South Africa, i.e. they are taxed in SA on their worldwide income and persons who are not tax resident in SA, are taxed only on income that is sourced or deemed to be sourced in SA. Expatriates have a limited exemption available to them; section 10(1)(o)(ii), exempts the first R1 25 million from SA tax provided that certain conditions are met.

Non-residents

Persons who are not tax resident in SA are not taxed on their worldwide income in SA; rather, they are taxed only on income that is sourced or deemed to be sourced in SA and in situations where a Double Tax Treaty (DTA) applies and designates that an amount of income must or may be taxed in SA.

Common misunderstandings

To be on the right side of the law, taxpayers should ensure that they understand their factual residential status. The days of falling through the cracks, not being tax resident anywhere, or being so-called 'citizens of the world', are long gone. Upon scrutiny by SARS, all taxpayers will fall to be either resident or non-resident and, if you have misunderstood your status, you could be facing large tax penalty and interest assessments from SARS. You may also find that you are on the wrong side of SA exchange controls and you will also be on the wrong side of the tax laws in your foreign country, having underpaid tax or worse.

WATCH YOUR **RENTALS**

15 minutes CPD

BERRY EVERITT, CEO of Chas Everitt International

If you own one or more residential properties that you let out to tenants or even if you are using part of your home as an Airbnb, it is important to note that any rent you receive forms part of your personal income and must be declared to the South African Revenue Service (SARS) on your annual tax return.

Deliberately not declaring it is effectively tax evasion, which is a crime in terms of the Tax Administration Act 28 of 2011; it could lead to you having to pay a hefty penalty at the very least—on top of the outstanding tax owed—or even result in a jail sentence of up to five years.

What is more, as SARS continues to hone the efficiency of tax collection, it is increasingly unlikely that any such non-declaration and/ or under-declaration will remain undetected. It is also important to note that holiday homes, bed-and-breakfast establishments, guesthouses, garden flats and even rooms that are let in your own home, fall into the same rental property net as separate apartments and houses that you may have bought specifically to rent out.

Expenses can be deducted

However, it is not all doom and tax gloom for landlords; they are allowed to deduct certain expenses that are related to the letting of the property from the gross rental received* when calculating the taxable amount of income received from a rental property, provided that they are able to show SARS that they are carrying on a *bona fide* trade through the rental of one or more properties.

According to SARS, permissible expenses include:

- Any interest paid on a bond during the relevant tax year;
- The municipal property rates paid for the year;
- The premiums paid for structural (HOC) insurance;
- Amounts paid to repair and maintain the property, including garden and pool services;
- Security costs such as a monthly fee paid to a security company; and
- Monthly levies paid if the property is in a Sectional Title complex or gated estate.

Landlords may also deduct the cost of any advertisements placed to attract tenants to the rental property and any fees or commissions paid to estate agents in regard to the letting of the property.

What is not allowed

They may not, though, claim any VAT that may be incurred on any of the above expenses, as the "*supply of accommodation in a dwelling*" is a VAT exempt supply. They must also be careful to make a distinction between expenses incurred in the production of their rental income and those that are not, such as the costs of any improvements made to the property.

The latter are defined by SARS as capital in nature and distinct from the costs of repairs and maintenance in that they would generally result in an increase in the value of the property asset. (And though the improvements are not permitted as a deduction from rental income, owners should still keep a record of these, as they could come in useful to legitimately reduce CGT liability if and when a rental property is sold.)

"Landlords must be careful to add any rent received to their taxable income and to deduct only permissible expenses"

In the event that the permissible expenses incurred in the production of rental income exceed the actual income, SARS will, in most cases, allow the loss to be set off against any other income earned by the taxpayer.

In addition, if you are retired and/ or not earning any other income, it is possible that your rental income could fall below the tax threshold for your age-group and that you will have no tax liability. According to SARS, the tax thresholds for the 2023/ 24 tax year are R95 750 for individuals under 65; R148 217 for people aged 65 to 75 and R165 689 a year for those over 75.

Make matters right

But as a landlord, you will in either case still need to submit a tax return or risk paying an administrative penalty for non-submission.

On this point, it is worth noting that the Tax Act also empowers SARS to issue tax assessments based on estimates to people who regularly fail to submit returns—and to charge cumulative penalties and interest on any amounts that are unpaid in terms of those assessments.

So our advice to any landlord who has not previously declared their rental income, for whatever reason or who has mistakenly failed to submit a tax return at all, is to urgently seek the help of an accountant or tax consultant to approach SARS and voluntarily rectify the situation as soon as possible.

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*Any deposit paid by a tenant does not need to be declared as part of the landlord's gross income for the relevant tax year, provided that there is a lease in place that provides for the deposit to be refunded at a later stage. Any deposit amount will usually only be regarded as income if and when it is retained by the landlord for some reason, such as to repair damages caused by the tenant.

15 minutes CPD

An overview of changing South African tax residency: The Double Taxation Agreement route

▶ **DELANO ABDOLL,** Admitted Attorney and Team Leader: Cross-Border Taxation at Tax Consulting South Africa

Over time, the residence-based taxation system in South Africa has become more pivotal to internationally mobile persons, especially high-net-worth individuals and expatriates in general. In terms of this system, South African residents are taxed on their worldwide income and non residents are taxed only on income sourced within the borders of South Africa. Viewed from the perspective of South African expatriates abroad, this often makes the transition from resident to non-resident (even temporarily) a relatively easy decision to make.

The common misconception among these expatriates, however, is that departing from South Africa and relocating to a temporary destination will trigger SARS to automatically regard them as non-resident taxpayers. This is incorrect. A formal process must be followed to cease one's South African tax residency status. Failing to do so, SARS may audit the misinformed expatriate, who will still be subject to tax on their worldwide income. It is crucial, then, to understand how the transition to a non-resident tax status operates with reference to the Double Taxation Agreements (DTA) into which South Africa has entered.

Determining the initial tax residency status

Determining a natural person's tax residency status is generally the starting point in understanding their tax liability under the Income Tax Act (the Act). Many perceive the consideration of whether a natural person is a tax resident or not as a simple enquiry when applying the definition of 'resident' under section 1(1) of the Act. However, this is not the case, especially when it is reliant on the impact of a DTA. At the risk of stating the obvious, the 'initial' tax residency of a natural person is triggered, either by them being (a) ordinarily resident in South Africa; or (b) physically present in South Africa for certain prescribed periods.

Notwithstanding these principles, the definition's proviso allows a South African tax resident to become non-resident under the provisions of a DTA. This means, among other things, that those expatriates who are abroad but have the intention to remain ordinarily resident in South Africa can elect to inform SARS of their ceasing to be a tax resident (albeit temporarily). The qualifying criteria, however, will depend on the application of those DTAs that contain a treaty-specific definition of a resident. Again, this does not occur automatically.

▶

"At the risk of stating the obvious, the 'initial' tax residency of a natural person is triggered, either by them being (a) ordinarily resident in South Africa; or (b) physically present in South Africa for certain prescribed periods"

As a quick recap of the basics of whether an expatriate is eligible to become a non-resident in terms of a DTA; they should first confirm whether there is a DTA in place between South Africa and the host country. If so, the following broad requirements may be considered:

- Whether they are also regarded as a tax resident in the host country;
- Whether it is their intention to permanently return to (and remain in) South Africa at some point in the foreseeable future; and
- Based on that intention, whether their personal facts and circumstances would be supportive of the so-called 'tie-breaker test' contained in the applicable DTA.

Tie-breaker test

We all know that the tie-breaker test in a DTA between South Africa and a host country, in the majority of cases, will resolve the conflict of a person who is found to be a tax resident of both contracting states. However, careful guidance necessitates that one only proceeds to the tie-breaker test once a residency 'tie' factually exists. For example, take the wording of Article 4(2) of the DTA between South Africa and the United Arab Emirates in which its treaty-specific definition reads as follows:

> "2. *Where by reason of the provisions of paragraph 1 of this Article an individual is <u>a resident of both Contracting States</u>, then that individual's status shall be determined as follows . . ." <u>(own emphasis)</u>.*

This makes the issuance of a valid certificate of residence from the foreign revenue authority or a letter from the authority indicating tax residency in that foreign country (if available), the gateway document for SARS' recognition that a South African expatriate has ceased tax residence under the tie-breaker test. In the absence of this gateway document to confirm foreign tax residency on a date aligned with the effective date indicated on SARS' Notice of Non-Tax Resident Status records, many South African expatriates may be incorrectly taxed as non residents—days, weeks or even months sooner than a DTA permits.

SARS' request for relevant supporting documents

Recently encountered in practice on a daily basis is the fact that taxpayers who want to update their tax residency status to non-resident, owing to the application of the DTA, will be requested by SARS to submit the following relevant supporting documents:

- The signed declaration indicating the basis on which they qualify.
- A letter of motivation setting out the facts and circumstances in detail to support the disclosure that they have ceased to be a tax resident.
- A copy of their passport and travel diary.

Of importance from a client-risk management perspective is the fact that these documents are required, in addition to the colloquial 'tax residency certificate' from a foreign revenue authority. This, in turn, makes it evident that the cessation of tax residency in South Africa (whether permanently or temporarily) is by no means a box-ticking exercise.

Conclusion

Changing an expatriate's tax resident status through a DTA is complex, knowing that more frequent and detailed enquiries by SARS are focused on those claiming to cease their South African tax residence. Having said that, these individuals should definitely seek assistance from cross-border taxation professionals who are well equipped to manage the entire process.

CASE LAW WRAP-UP

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Commissioner for SARS v Coronation Investment Management SA (Pty) Ltd
(1269/2021) [2023] ZASCA 10 (07 February 2023)

ISSUE

The issue before the Supreme Court of Appeal (SCA) in this matter was whether a controlled foreign company (CFC) constituted a foreign business establishment (FBE) as contemplated in the Income Tax Act, No. 58 of 1962 (the ITA).

FACTS

Coronation Investment Management (Pty) Ltd (the taxpayer) was the sole owner of Coronation Fund Management (CFM), a subsidiary of the taxpayer situated on the Isle of Man. CFM, in turn, was the sole owner of Coronation Global Fund Managers Limited (CGFM), being registered and operating in Ireland.

CGFM had outsourced its investment management functions to Coronation Asset Management (Pty) Ltd (CAM) registered in South Africa, as well as Coronation International Limited (CIL) registered in the United Kingdom.

During the 2011, 2012 and 2013 years of assessment, the taxpayer filed its income tax returns and excluded the net income of CGFM from its taxable income. Subsequently, in April 2015, the South African Revenue Service (SARS) conducted an audit in respect of these years and issued an additional assessment for the 2012 tax year, which included the net income of CGFM and an understatement penalty thereon.

The taxpayer submitted an objection and subsequently appealed the additional assessment, following which SARS issued a reduced assessment. However, a significant portion of the tax debt still remained.

The taxpayer appealed to the Tax Court and argued that CGFM was a foreign business establishment (FBE) in terms of section 9D of the Act. The Tax Court ruled in favour of the taxpayer and set aside SARS' additional assessments. Accordingly, SARS appealed to the Supreme Court of Appeal (the SCA).

THE TAXPAYER'S CASE

The taxpayer's case centred around the licence granted to CGFM by the Central Bank of Ireland to operate as a 'management company' in terms of the European Communities Regulations under Investment Services Directive 93/22/EEC 2125.

The taxpayer contended that CGFM's business plan, which had been attached to its licence application, presented an outsource business model where CGFM would concentrate on being a product provider and that the eventual licence granted by the CBI did not approve investment management functions.

In addition, the taxpayer asserted that since the actual performance of investment trading functions were not envisaged in CGFM's business plan, the performance of such functions could not constitute a part of CGFM's primary functions.

The taxpayer disputed the imposition of the understatement penalty on the basis that it had relied on a tax opinion procured from a leading tax expert. However, the taxpayer did not disclose the contents of the tax opinion.

SARS' CASE

SARS argued that CGFM's primary functions comprised investment management and since these functions were outsourced to CAM in South Africa and CIL in the United Kingdom, CGFM lacked economic substance and was not considered to be an FBE in terms of section 9D of the Act.

While it is permissible for a CFC to outsource locational permanence and economic substance, it must comply with the proviso in subsections *(aa)* to *(cc)* of the definition of FBE in section 9D(1) of the ITA, which CGFM did not do.

Furthermore, SARS imposed the understatement penalty on the imputed net income of the taxpayer's 2012 year of assessment, on the basis that there had been "*a substantial understatement resulting in a penalty of 10% of the tax that would otherwise have been paid*". Whereas the taxpayer had obtained a tax opinion on the matter, it did not disclose the contents hereof. SARS drew a negative inference from this non-disclosure and thus argued that it was entitled to impose the understatement penalty.

OUTCOME

The SCA found in favour of SARS and the appeal was upheld with costs against the taxpayer, including the costs of two counsels. The understatement penalty imposed by SARS was, however, set aside.

CORE REASONING

The Court considered section 9D of the Act which provides the requirements for an FBE exemption.

To be considered an FBE, the CFC must have a fixed place of business in the foreign country, used for the carrying on of business for a period of not less than one year. In addition, the business must be conducted through one or more office or other structures, which are suitably staffed and have on-site managerial and operational employees who conduct the primary operations. In addition, the premises must be suitably equipped, with suitable facilities for its primary operations and the reasons for its location being outside South Africa must not be to facilitate a postponement or reduction of tax in South Africa.

An FBE may utilise the structures, employees, equipment and facilities of another company, albeit provided that the other company is subject to tax in the same jurisdiction, as well as a part of the same group of companies, and is situated in the same country as the FBE.

According to the Court, the core functions of CGFM were indeed investment management, as stated in its Memorandum of Incorporation and as echoed by certain witnesses, i.e., the managing director of CGFM, one of the founders of Coronation Group.

Furthermore, the Court held that "*these functions had to fall within the ambit of its business in order to be outsourced. An agent cannot perform a function which does not form part of the business of the principal. In other words, CGFM could not outsource a function it did not possess in the first place.*" .

The Court concluded that the primary business operations of CGFM were those of fund management, including investment management. Since these functions were not conducted in Ireland and were, in fact, outsourced to CAM in South Africa and CIL in the United Kingdom, the requirements for FBE status exemption were not met, with respect to the proviso contained in section 9D(1)*(aa)* to *(cc)*.

With regards to SARS' claim for understatement penalties, the Court found that SARS was unable to prove that the exclusion of CGFM's profits from CIMSA's taxable income was not due to a bona fide error, and accordingly did not discharge its onus in this regard. As such, the understatement penalties were set aside.

TAKEAWAY

South African resident companies must consider the law carefully when incorporating subsidiaries in foreign jurisdictions. Section 9D of the Act is clear on the requirements for an FBE. Critically, taxpayers must be able to evidence that the primary operations of the controlled foreign company are carried out in accordance with the requirements of the FBE exemption in section 9D.

In the event of the FBE being non-compliant with the relevant requirements in any way, the total profits of the CFC will be included in the taxpayer's taxable income, which will result in a significant tax liability.

Commissioner, South African Revenue Service v The Thistle Trust (Case no 516/2021) [2022] ZASCA 153 (7 November 2022)

ISSUE

The issue before the Supreme Court of Appeal (SCA) whether the Tax Court was correct to uphold an appeal against the additional assessments raised by SARS against the Thistle Trust (the taxpayer). The additional assessments related to the interpretation of section 25B of the Income Tax Act, No. 58 of 1962 ("the ITA") and paragraph 80(2) of the Eighth Schedule thereto, in relation to the distribution of capital gains to beneficiaries of trusts.

FACTS

The taxpayer was a beneficiary of multiple trusts, referred to as 'Tier 1 Trusts', within the Zenprop Group. During the 2014–2016 years of assessment, the Tier 1 Trusts disposed of specific capital assets and realised gains thereon. The capital gains were distributed, *inter alia*, to the taxpayer during the same years of assessment. In turn, the taxpayer distributed these amounts to its beneficiaries in the same years. The proceeds received were treated as taxable in the hands of the taxpayer's beneficiaries.

SARS raised additional assessments for the 2014–2016 years of assessment, in terms of which the capital gains distributed to the taxpayer by the Tier 1 Trusts were treated as taxable in the taxpayer's hands. SARS further imposed an understatement penalty, with interest.

The taxpayer lodged an objection, which SARS disallowed. The taxpayer lodged an appeal in the Tax Court, which court found that the Tier 1 Trusts had disposed of capital assets and the gains distributed to the taxpayer (and thereafter its beneficiaries), were amounts as contemplated in sections 25B(1), 25B(2), and paragraph 90(2) of the Eighth Schedule. As such, per the court, the distribution to the taxpayer's beneficiaries was a distribution of capital gains taxable in the beneficiaries' hands.

The Tax Court accordingly set aside the additional assessments and SARS, with leave of the Tax Court, lodged a further appeal to the SCA.

THE TAXPAYER'S CASE

The taxpayer contended that paragraph 80(1) and 80(2) of the ITA were applicable, and the capital gains were taxable in the hands of the resident beneficiaries of the taxpayer. Counsel for the taxpayer submitted that this was evident upon a reading of paragraph 11(1)*(d)* of the Eighth Schedule, which provides that a disposal for capital gains tax (CGT) purposes includes the vesting of an interest in an asset of a relevant trust in a beneficiary. Furthermore, paragraph 80(2) of the Eighth Schedule must be read with section 25B of the ITA, to the effect that that 'an amount' per the provision included capital gains.

The taxpayer further argued that the 'conduit-pipe' principle was applicable hereto and that the gains distributed by the Tier 1 Trusts to the taxpayer constituted an asset which had vested in the taxpayer's beneficiaries. As such, the taxpayer was merely a conduit for the gain that flowed to its beneficiaries.

SARS' CASE

SARS argued that paragraph 80(2) of the Eighth Schedule applied and section 25B of the ITA did not.

Specifically, the proceeds received on disposal of the assets by the Tier 1 Trusts constituted *capital gains* in their own hands, following which the gains were then distributed to the taxpayer. As such, paragraph 80(2) of the Eighth Schedule was solely applicable.

The taxpayer had acquired a vested right to the capital gains distributed to it but not to the capital assets themselves. The taxpayer then distributed this amount to its beneficiaries and, in doing so, it did not realise a capital gain in respect of the disposal of a capital asset as contemplated in paragraph 80(2) of the Eighth Schedule. As such, the capital gains accrued pursuant to the disposal of the capital assets by the Tier 1 Trusts were taxable in the hands of the taxpayer.

SARS further argued that this section concerns the taxation of income accruing to trusts and their beneficiaries, whereas the amounts herein were of a capital nature. As such, section 25B did not apply.

OUTCOME

The SCA found in favour of SARS and the appeal was partially upheld with no order made as to costs.

CORE REASONING

The SCA held that, in determining what 'any amount' constituted for purposes of sections 25B(1) and 25B(2) of the ITA, the sections were to be read as a whole. Whereas section 25B(2) of the ITA concerns 'any amount' when considering the provisions of section 25B as a whole, it is clearly concerned with amounts of an income nature and not of a capital nature. As such, capital gains are excluded from the meaning of 'any amount' for purposes of section 25B.

The SCA concluded that section 25B applies to the taxation of the income of a trust or its beneficiaries and that the Eighth Schedule deals with capital gains in the hands of trusts or their beneficiaries. Thus, it concluded that the Tax Court had erred in finding that section 25B of the ITA was applicable in this instance. Furthermore, the Court held that the 'conduit-pipe principle' did not find application herein.

In determining whether SARS correctly imposed the understatement penalty, the SCA held that SARS was entitled to levy a penalty where a taxpayer submitted a return understating its taxable income or deemed taxable income. In this instance, however, SARS imposed an understatement penalty of 50%, which relates to circumstances where a taxpayer has no reasonable grounds for the tax position taken.

The taxpayer had, however, obtained a legal opinion to support its position. It was accepted that the understatement by the taxpayer was a *bona fide* and inadvertent error, as it believed that section 25B was applicable. The penalties were thus set aside.

- In addition, on the basis that the CGT assessment resulted in a tax liability due to SARS, the taxpayer would be liable for interest in terms of section 89quat(2) of the ITA.

TAKEAWAY

A trust cannot apply the provisions which deal with distributions of income and capital to beneficiaries simultaneously. Distributions are either classified as income or capital and the treatment thereof for tax purposes will depend on such classification. Furthermore, where a taxpayer makes a *bona fide* and inadvertent error, SARS may not impose an understatement penalty.

Lance Dickson CC V Commissioner for SARS
(A211/2021) [2023] ZAWCHC (31 January 2023)

ISSUE

In this matter, the High Court was seized of the issues whether correct behaviour was applied by SARS as a basis for the understatement penalty imposed or if a different penalty should have been imposed. Furthermore, if the penalty imposed by SARS was incorrect, the further issue was whether a different (higher) penalty might have been imposed instead.

FACTS

Lance Dickson Construction CC (the taxpayer) owned immovable property, and concluded a sale agreement with a related entity (the purchaser), in terms of which the purchaser agreed to purchase the property for R25.2 million. This was calculated on the basis that, once subdivided, the property would comprise 72 individual erven valued at R350 000 each. KMC would pay R350 000 to the taxpayer when each erf was on-sold to a final purchaser. The agreement stated that the capital gains tax (CGT) on the entire transaction would be paid by the taxpayer on an ad hoc basis as and when each erf was on-sold, and the relevant amount had been received by the taxpayer.

When the taxpayer rendered its 2017 return, however, none of the individual erven had been on-sold. As such, the taxpayer did not disclose the sale in the return. SARS picked up on this when it reviewed the 2017 tax return in conjunction with earlier tax assessments and was of the view that the taxpayer was liable for the full CGT amount. SARS thus raised additional tax and an understatement penalty of 25% for reasonable care not taken in completing the return, under s223(1) of the Tax Administration Act, No. 28 of 2011.

Pursuant to a dispute lodged by the taxpayer, the matter was appealed in the Tax Court which upheld SARS' view and the 25% penalty. The taxpayer took the matter on further appeal to the High Court.

THE TAXPAYER'S CASE

The taxpayer conceded that it had made a substantial understatement, following which the issues in dispute narrowed to the understatement penalty imposed.

The taxpayer contended that it had not acted unreasonably in adopting the tax position; nevertheless, the understatement did not arise from its return completion process and, therefore, the basis of the understatement penalty was inappropriate. An understatement in this case would instead have arisen from the tax position taken by the taxpayer.

As any understatement in this case was not causally connected to the process followed by the taxpayer in completing its return, SARS had identified the incorrect behaviour in applying the understatement penalty. In this case, it was a difference in legal interpretation.

The failure to levy a higher understatement penalty thus confirmed that SARS was satisfied that the underestimation was not deliberate or a result of negligence, otherwise it would have been obliged to levy a higher penalty

SARS' CASE

SARS argued that the imposition of the 25% understatement penalty was justified on the basis that the taxpayer had not taken reasonable care in completing its return. Reasonableness would have required the taxpayer to have known that the sale of the property in September 2016 and subsequent registration on 27 October 2016, was a disposal event that triggered proceeds which accrued to the taxpayer during the 2017 year of assessment. As the failure to make this declaration fell below the standard of a reasonable person in similar circumstances, the understatement penalty was correct.

However, during cross-examination in the Tax Court, the SARS official (the witness), who was tasked with investigating the taxpayer's 2017 return, accepted that she had chosen the wrong behavioural category *vis-à-vis* the understatement penalty. The witness conceded that SARS had erred in imposing a 25% penalty but went on to suggest that the taxpayer should be happy with the lesser penalty as its conduct had been unreasonable either way.

OUTCOME

The Court found in favour of the taxpayer and directed SARS to alter the 2017 additional assessment to exclude the understatement penalty imposed with costs awarded in favour of the taxpayer.

CORE REASONING

Section 221, read with section 222 of the Tax Administration Act, allows SARS to impose a penalty where the taxpayer has understated its taxable income (where this does not stem from a *bona fide* inadvertent error). It was common cause that the taxpayer had understated its CGT liability and that this was not due to a *bona fide* inadvertent error.

- The Court found that the witness for SARS was unable to distinguish between the two understatement categories. SARS' case for understatement penalties was made on the basis of the taxpayer not having taken reasonable care in completing its tax return (and nothing else). Despite this, in its own evidence, SARS admitted that the understatement penalty was levied on the basis of the taxpayer having no reasonable grounds for the tax position taken.

The Court also found that the Tax Court had incorrectly relied on the case of *Purlish Holdings (Pty) Ltd v Commissioner of SARS* [2019] ZASCA 04. In that case, the SCA had determined that the Tax Court was unable to unilaterally increase understatement penalties imposed by SARS. It was on this basis that the Tax Court stated that it was not empowered to increase the understatement penalty imposed on a taxpayer to 50%; it was equally unable to allow the taxpayer to escape liability for 25% of the penalty imposed by SARS.

If SARS elected to impose a 25% understatement penalty, it was required to prove the factual basis therefor when its determination was challenged by the taxpayer. SARS did not do so and there is no basis for it to recover that penalty from the taxpayer. The Tax Court was thus wrong in confirming the understatement penalty of 25%. As SARS also did not prove any basis for the 50% penalty, this was not contended by the taxpayer and did not apply.

TAKEAWAY

This case serves as a reminder of the limits on SARS' power. Ironically, through its own lenience in levying a reduced penalty on the taxpayer, SARS undermined its own case with the result that the understatement penalty fell to be remitted. This affirms that SARS is bound by the provisions of the Tax Administration Act and must prove the facts upon which the understatement penalty is based. This case further clarifies the power of the Tax Court to vary an understatement penalty.

BINDING RULINGS

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Binding Private Ruling: BPR 387

Attribution of nett income to a public benefit organisation (09 December 2022)

ISSUE

This ruling determines the tax consequences of a public benefit organisation (PBO) holding a participatory interest in a controlled foreign company, which is a foreign incorporated charity.

FACTS

The applicant was established to administer and control a special fund for the sole purpose of receiving donations to be used exclusively to provide funds, assets, essential services or other resources for the benefit of its beneficiaries. The applicant has embarked on a programme to solicit donations from wealthy South Africans who have emigrated to other countries. It is envisaged that charities will be established in various identified foreign countries or cities and will collect donations. These donations will be used to supplement the annual financial needs of the applicant and to build up funds which can be distributed to its beneficiaries.

This proposed transaction entails the establishment of a so-called 'Association Charitable Incorporated Organisation' or 'Association CIO' in the United Kingdom (UK), being a corporate structure designed specifically and exclusively for charities. It is regulated principally by the Charity Commission of England and Wales. The applicant will be the sole member of the Association CIO.

All or most of the trustees will be UK residents and will be chosen by their willingness and commitment to raise funds for the Association CIO. Although it is the trustees who are responsible for managing and controlling the CIO and who thus constitute its effective management, the member of the CIO would be entitled to vote. Although the CIO will be established to raise funds for the ultimate benefit of the applicant's beneficiaries, it will, nevertheless, have full discretion as to which charity (whether in the UK or not) it will distribute its funds.

The governance of the Association CIO will take place at two levels:

- The board of charity trustees, who will manage the affairs of the CIO and may exercise the powers of the CIO, collectively as a board for this purpose. The trustees must exercise their duties in terms of English charity law and will incur a personal liability where they act in breach of their charitable duties. The board may decide to donate or distribute funds to its members if this is in furtherance of the object of the CIO and if they qualify as beneficiaries of the CIO.

- The members may also be trustees, albeit will act in different capacities when making decisions in different capacities. The following decisions can only be made by a CIO's members passing a resolution (by either a 75% majority in a general meeting or a unanimous written resolution) in accordance with rules set out in the relevant legislation:

    - Amending the CIO's constitution – the UK Charity Commission of the UK will review any amendments that the members may approve from time to time, and will refuse to register any amendments to the constitution which are non-compliant with general principles of UK charity law and CIO legislation;

    - Applying to the Commission to amalgamate the CIO with any number of other CIOs;

    - Transferring the CIO's undertaking to another CIO; and

    - Applying to the Commission for the CIO to be dissolved.

RULING

- The ruling made in connection with the proposed transaction is as follows:

- Section 9D of the Income Tax Act, 58 of 1962 applies to the applicant.

- The amount to be included in the applicant's income under section 9D(2) will be exempt in terms of the provisions of section 10(1)(cN)(i).

- Section 72A of the Income Tax Act (return relating to a controlled foreign company) will apply to the applicant.

Binding Class Ruling: BCR 085

En commandite partnerships investing in photovoltaic solar energy plants

(09 December 2022)

ISSUE

This Ruling determines the deductibility of expenditure to be incurred by en commandite partnerships investing in photovoltaic solar energy systems, which will be installed at the partnerships' clients' premises, in terms of power purchase agreements (PPAs).

FACTS

The applicant is a resident company specialising in renewable energy utilities. It proposed setting up multiple en commandite partnerships with various resident individuals, trusts or companies (limited partners), which partnerships will invest in solar energy generation assets (assets). The partnerships will generate and sell electricity to end users in terms of PPAs concluded with its clients.

Each partnership will be ringfenced in respect of projects to be invested into in a particular year of assessment. They will be closed off once the number of partners have reached 20 persons.

The assets to be procured by the partnership will include solar photovoltaic panels, cables, batteries and inverters.

The acquisition of the assets will be partially funded by the applicant and partially in terms of agreements between the limited partners and third parties, which third parties will provide funding to the limited partners of up to 95% of the value of the assets in terms of ICAs. The material terms of the ICAs will be as follows -

- the finance period will be for a minimum period of 12 months;
- the financed amount will carry finance charges; and
- the financed assets will constitute security for adherence by the partners of their obligations under the ICA. In the event of a default, the financier will become entitled to the income generated by the assets.

PPAs will be concluded between the applicant and its clients, which clients will pay for the use of the electricity generated by the assets which are, or will be, owned by the partnerships and installed at the clients' premises. The partnerships will purchase existing systems installed by the applicant; alternatively, acquire and install the assets for the specific purpose of generating and selling electricity under the signed PPAs.

When a limited partner joins the partnership, they will be required to sign a deed of adherence, setting out the value of assets so to be acquired, which value will represent the capital contribution by the limited partner, and which amount will be used solely for the purpose of acquiring the assets.

The limited partner, as well as the third-party financier, will make payment of the respective amounts into the partnership's bank account, which funds will then be used by the partnership to make payment of the amount required to acquire the assets. If not already installed, the assets so acquired will be installed by a service provider appointed by the applicant, under an outsourcing agreement.

All operations will be outsourced to the applicant, including agreements for insurance and maintenance of the assets. Management fees will be payable to the applicant, as well as the fees payable for the services outsourced to the applicant.

The profits generated in respect of the assets owned by the partnerships will be paid to the limited partners in proportion to their interests therein, and with reference to the value of their capital contributions over the life of the assets.

RULING

The ruling made in connection with the proposed transaction is as follows:

(a) Each limited partner will be considered to hold a proportionate interest in the assets procured by the partnership. Their interest will be determined with reference to the value of their capital contribution to the partnership, in relation to the total capital contribution made to the partnership.

(b) In respect of the acquisition by the partnership of assets not exceeding 1 megawatt (in relation to one or more projects), each limited partner will be entitled to a proportionate share of the capital allowance in terms of section 12B(2)*(b)* of 100% of the cost of such assets, in the year of assessment in which they are brought into use.

(c) In respect of the acquisition by the partnership of assets exceeding 1 megawatt (in relation to one or more projects), each limited partner will be entitled to a proportionate share of a capital allowance in terms of section 12B(2)*(a)* of –

- 50% of the cost of the assets in the year of assessment in which they are brought into use;
- 30% of the cost of the assets in the second year of assessment; and
- 20% of the cost of the assets in the third year of assessment.

(d) In relation to the cost of the foundations and structures designed for the installation of the section 12B(1)*(h)* assets which meet the criteria as contained in the proviso to section 12B(1), the same deductions as the assets to which they relate.