South African Institute of Taxation

LEGISLATIVE INTERPRETATION: A RECAP OF 2022

Tax Practice on the Move Series

YOUR KEY TO THE TAX COMMUNITY

About The Presenters

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A RECAP OF KEY 2022 INTERPRETATION NOTES

Draft Interpretation Note – Effect on the Date of Issue of a Share arising from a Change in the Redemption Features

- Purpose
  - The draft interpretation note (draft IN) deals with whether adding redemption features or making a change to the existing redemption features of a share constitutes a new date of issue for purposes of section 8E.
  - The draft IN explains and defines what hybrid equity instrument is, date of issue etc.
  - The critical question as to when a variation of the redemption features of a share will result in a new date of issue under section 8E is considered in this draft IN.
  - Section 8E is an anti-avoidance provision that targets shares and equity instruments with substantial debt features. The treatment of these shares as hybrid financial instruments ensures that debt is not disguised as short-term redeemable preference shares or any other redeemable share containing certain dividend preferences.
- SAIT Comments
  - On an overall basis the contents of the draft interpretation note are welcomed. As such, the comments contained in SAIT's submission were largely contextual in nature

Draft Interpretation Note – Sale and Leaseback Arrangements and Related Simulated Transactions

Purpose

- This draft interpretation note (draft IN 2) provides guidance on the application of sections 23D and 23G to certain sale and leaseback arrangements.

What is a sale and leaseback arrangement?

- A sale and leaseback arrangement is a transaction in which the owner of an asset sells the asset to the financier and then enters into a use agreement whereby the hires the asset back from the financier. In this way the taxpayer raises the required funding through the proceeds on the sale of the asset and the repayment of the financing takes the form of rent.
- *CIR v Conhage (Pty) Ltd* gave birth to Sections 23D and 23G target sale and leaseback arrangements.

SAIT Comments

- On an overall basis the contents of the draft interpretation note are welcomed.

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Draft Interpretation Note – Sale and Leaseback Arrangements and Related Simulated Transactions

- SAIT Comments

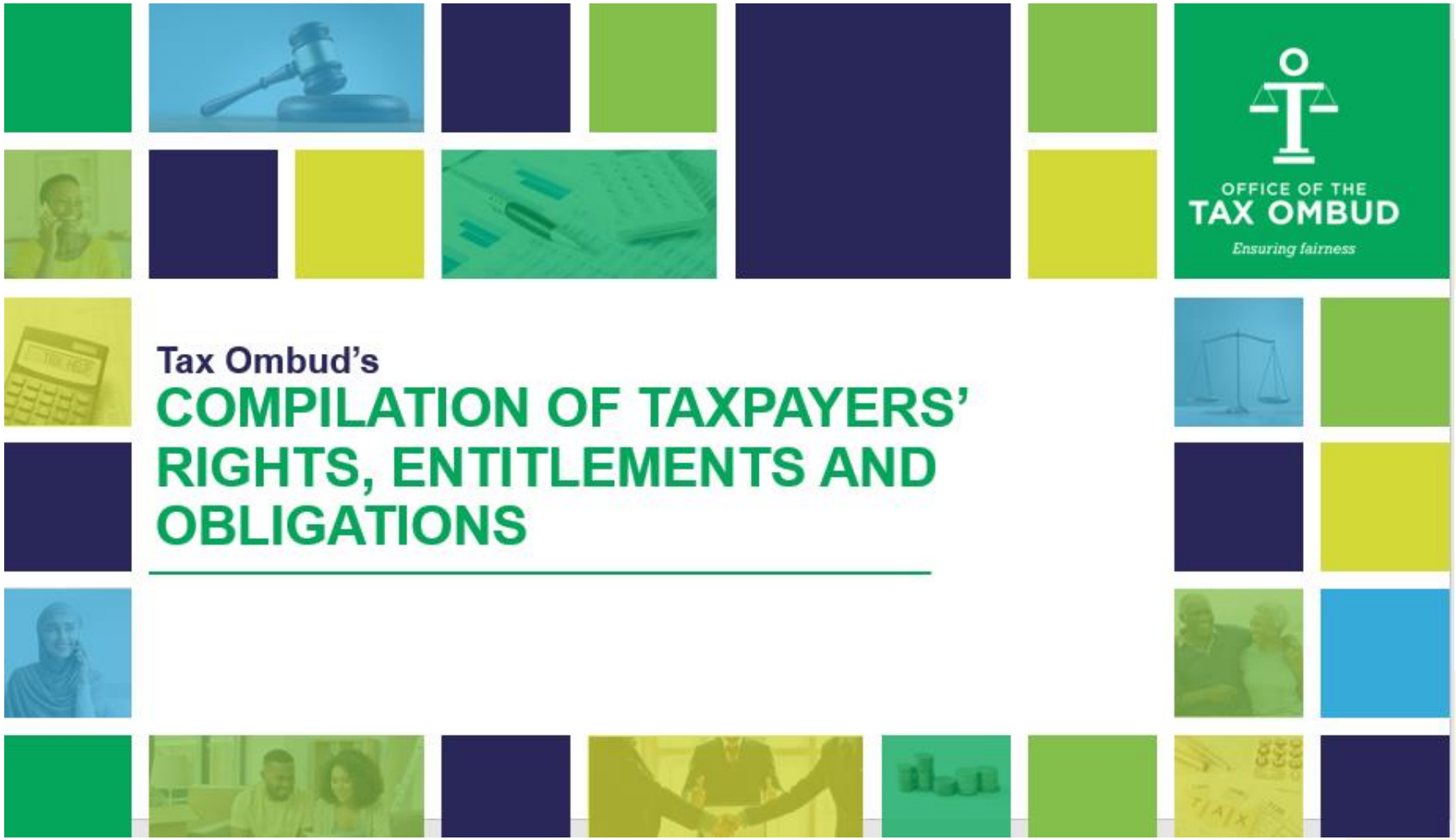
"It appears that SARS has opted to apply the provisions and application of section 23G(3) of the Act, in a narrow manner.

*However, it appears that the result put forward by SARS in Example 3, that the interpretation of section 23G(3) is being read as "…. lessee **and** sublessee …".*

As a result an unwarranted double "hit" occurs wherein the sub-lessee is "hit" with a limitation on deduction whilst the lessee (also the sublessor) is taxed on the full amount(s) and then is also subject to a limitation.

We believe that that the policy underpinning the legislation will be adequately fulfilled where either the lessee or sublessee is subject to the limitation in deduction, not both".

Tax Ombud



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Tax Ombuds Compilation of Taxpayers Rights, Entitlements and Obligations

YOUR RIGHTS AS A TAXPAYER

- You have the right of access to information
- You are entitled to receive quality and timely service from SARS
- You have the right to a fair, unbiased and just tax system

YOUR ENTITLEMENTS AS A TAXPAYER

- You are entitled to finality
- You are entitled to make certain requests/proposals/applications to SARS
- You are entitled to complain without fear of victimisation

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Draft Interpretation Note – Determination of the Taxable Income of Certain Persons from International Transactions: Intra-Group Loans

Background and purpose

- Taxpayers are broadly financed in two ways, namely using equity and debt. The returns on equity capital and debt capital are treated differently for tax purposes
- This Note provides taxpayers with guidance on the application of the arm's length principle in the context of the pricing of intra-group loans. The pricing of intra-group loans includes a consideration of both the amount of debt and the cost of the debt.

SAIT Comments

- Identifying the commercial or financial relations (paragraph 5.3)
  - Analysis of various factors, inter alia the performance of the business in the industry as well as the differences in industry sectors needs to be taken into account.
  - Concerning – non-conformance of factors such as business or product cycle by some companies in a particular industry but non-conformance may be purely for business reasons such as bad management in the MNE group or other factors.

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Draft Interpretation Note – Determination of the Taxable Income of Certain Persons from International Transactions: Intra-Group Loans

SAIT Comments

- Identifying the commercial or financial relations (paragraph 5.3)
  - Requested that acknowledgement be in the draft IN in some detail so as to ensure that transfer pricing adjustments are not made on entities that have a legitimate basis for not conforming to the industry norms - some level of comfort to taxpayers if it could be indicated that exceptions do exist.

- De-minimis threshold – safe harbour

  - SARS has previously provided a safe harbour or risk harbour to create some degree of certainty for taxpayers when looking at thin capitalisation and the associated arm's length rate of interest to be applied on loan transactions

  - Furthermore, the Davis Tax Committee made recommendations that a safe harbour should be considered for loan transactions. The OECD has also warned against adopting a pure arm's length test for loan transactions.

Draft Interpretation Note – Determination of the Taxable Income of Certain Persons from International Transactions: Intra-Group Loans

SAIT Comments

- De-minimis threshold – safe harbour
  - The move away from this practice and these recommendations places an increased onus on taxpayers to prove that loan transactions are arm's length both in terms of their quantum (thin capitalisation) and price (interest rate). We therefore believe that a provision of a “de minimis’ rule will be appreciated by taxpayers as typically taxpayers tend to object to having full debt capacity and pricing studies performed especially for relatively small loans.
  - SARS should consider allowing small loan transactions to be entered into without testing and a safe harbour for loan transactions where the quantum of the loan is below a certain amount.

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Draft Interpretation Note – SAIT response to call for comment on draft interpretation note – Section 37A

SAIT Comments on Rehabilitation and timing

- Should there be a total impasse in interpreting section 37A in line with the provisions of the MPRDA and the provisions of the NEMA, National Treasury should consider amendments to section 37A to make the section practically enforceable.
- The necessity of ensuring that the facilitation of the rehabilitation expenditure through the tax regime is effective, is critically important in a period where any non-qualifying expenditure have to come out of day-to-day cashflow and operating expenses, in cases where mines are undertaking their very real rehabilitation obligations due to shaft and pit closures, etc.
- It does not appear to be in anyone's interest to have a punitive interpretation that hinges on a timing requirement that does not follow from the legislation creating the initial obligations.

Legislative Cycle

- The draft Tax Amendment Bills that were issued for public comment on 29 July 2022.
- The briefing of the Parliamentary Finance Committees by National Treasury and SARS took place on 23 August 2022. For greater detail, members may access National Treasury's presentation here.
- The SAIT Tax Technical Work Groups, consisting of industry specialists, compiled detailed and comprehensive submissions in response to the proposals contained therein. Members may access the submissions here.
- National Treasury and SARS scheduled public workshops with interested stakeholders to discuss issues that were raised in the written submissions made regarding the 2022 Draft Tax Bills. These workshops were held virtually over 3 days.
- Public hearings were scheduled as follows:

- 13 September 2022: Draft Rates Bill
- 14 September 2022: Draft TLAB and Draft TALAB

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Legislative Cycle

- National Treasury and SARS presented their response document to the public submissions at the Parliamentary Finance Committees hearings on the 2022 Draft Rates and Monetary Amounts and Amendment of Revenue Laws Bill and 2022 Draft Revenue Laws Amendment Bill on 20 and 21 September 2022. For feedback on the parliamentary hearings, members can access the following documents:

- National Treasury and SARS Presentations to the Standing Committee on Finance on 20 September 2022 and on 21 September 2022; and

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A RECAP OF KEY 2022 CASES

Court cases of interest and tax importance

Barnard Labuschagne Incorporated v South African Revenue Service and Another (CCT 60/21) [2022] ZACC 8 (11 March 2022)

Commissioner, South African Revenue Service v Sasol Chevron Holdings Limited (Case no 1044/2020) [2022] ZASCA 56 (22 April 2022)

Commissioner for the South African Revenue Service v Capitec Bank Limited (Case No: 94/2021) (21 June 2022)

Barnard Labuschagne Incorporated v South African Revenue Service and Another (CCT 60/21) [2022] ZACC 8 (11 March 2022)

Background

- The taxpayer is a law firm that applied for leave to appeal against a decision of the High Court that a certified statement in terms of section 172(1) of the TAA is not rescindable.
- SARS filed a certified statement that the taxpayer owed SARS an amount of R804 747.
- Taxpayer brought an application to rescind the judgment, in the alternative that section 172 and 174 are unconstitutional.
- The High Court held that the judgment cannot be rescinded and dismissed the alternative constitutional challenge. The High Court refused an application for leave to appeal with costs, as did the Supreme Court of Appeal.
- Matter taken to the Constitutional Court.

Barnard Labuschagne Incorporated v South African Revenue Service and Another (CCT 60/21) [2022] ZACC 8 (11 March 2022)

CC's approach

- The CC explained that section 172 provides that if a person has an outstanding tax debt, SARS may after 10 business days' notice, file a certified statement setting out the tax payable.

- Section 172(2) provides that the statement may be filed even if the tax debt is subject to a dispute.

- Section 174 provides that the statement "must be treated as a civil judgment lawfully given in the relevant court in favour of SARS for a liquid debt for the amount specified in the statement".

Barnard Labuschagne Incorporated v South African Revenue Service and Another (CCT 60/21) [2022] ZACC 8 (11 March 2022)

CC's approach

- The CC highlighted other features of the TAA:
  - Section 164 – "pay now argue later"
  - Section 170 – the production of a document issued by SARS purporting to be a copy or extract of an assessment is conclusive evidence of the making of that assessment and the correctness thereof
  - Section 175 and 176 – SARS can amend or withdraw a certified statement

Barnard Labuschagne Incorporated v South African Revenue Service and Another (CCT 60/21) [2022] ZACC 8 (11 March 2022)

CC's approach

- The CC highlighted the antecedents of these provisions in the ITA and VAT Act
- ITA: Section 91(1)(b) – filing of certified statement; Section 88 – pay now argue later; section 92 – correctness of a certified statement may not be disputed; section 94 – conclusive evidence provision; section 91(1)(bA) – withdrawal of certified statement
- VAT: Sections 40(2)(a), 40(2)(b), 40(5) and 42 of the repealed VAT Act
- These essential features of the repealed provisions are replicated in the TAA.

Commissioner, South African Revenue Service v Sasol Chevron Holdings Limited (Case no 1044/2020) [2022] ZASCA 56 (22 April 2022)

Background

- This case was an appeal by SARS against a judgment by the High Court in Pretoria, in favour of Sasol Chevron Holdings Limited ("the taxpayer").

- A division of Sasol (A Co) sold goods to another Sasol division (B Co), which immediately on-sold them to an unrelated third party for export to Nigeria. Regulation 15(1) of the Export Regulations requires that goods sold for exportation purposes must be exported within 90 days of the sale. However, B Co failed to do so.

- As such, A Co requested SARS to issue a ruling extending the prescribed 90-day period and SARS declined the application for extension. The taxpayer then instituted a review application under the Promotion of Administrative Justice Act, 2000 ("PAJA") seeking an order to review and set aside SARS' decision albeit more than 180 days after SARS' decision was given.

Commissioner, South African Revenue Service v Sasol Chevron Holdings Limited (Case no 1044/2020) [2022] ZASCA 56 (22 April 2022)

Arguments before the Court

- SARS asserted that section 7(1) of PAJA requires such a review application to have been instituted within 180 days from the date of the decision, or within such an extended period as has been agreed between the parties or as has been granted by a court in terms of section 9 of PAJA.

- However, since there was no agreement between the parties, and the Respondent had not brought such an application for extension of the 180-day period, this period stands and cannot be extended. Therefore, SARS argued that the review application must be dismissed on that ground alone without consideration of the merits of the review.

- The taxpayer contended that SARS' reasons for the decision were only provided at a later date, and therefore the 180-day period had only begun to run from 27 March 2018. Accordingly, the taxpayer's review application (which was submitted on 21 September 2018) was within the 180-day period.

Commissioner, South African Revenue Service v Sasol Chevron Holdings Limited (Case no 1044/2020) [2022] ZASCA 56 (22 April 2022)

Findings of the Court

- The High Court had agreed with the taxpayer and considered the merits of the review application. However, the Supreme Court of Appeal (SCA) found that the fact that the parties continued to exchange further correspondence beyond the date of SARS' decision (6 December 2017) cannot detract from the fact that SARS' impugned decision was taken on 6 December 2017.

- The Court went further to state that the decision taken on 6 December 2017 is the decision that the taxpayer referred to in its application and sought to set aside. Because the decision was made on 6 December 2017, the taxpayer had submitted its review application outside of the 180-day period.

- The Court noted that where no application for the extension of the 180-day period has been made, it has no authority to enter into the substantive merits of a review application. It therefore held that, in favour of SARS, the High Court's decision should be overturned and the merits of the review application need not be considered.

Commissioner for the South African Revenue Service v Capitec Bank Limited (Case No: 94/2021) (21 June 2022)

Background

- The facts concerned the unsecured lending business of Capitec Bank Limited (Capitec), in terms of which Capitec advanced credit in the form of personal loans to customers under term loan contracts.

- In terms of clause 13 of a standard loan contract entered into between Capitec and its customers, Capitec provided its customers with loan cover, the proceeds of which were applied to settle or reduce the outstanding loan amount due to Capitec in the event of death or retrenchment.

- During the period from November 2014 to November 2015, Capitec claimed R71 520 811.85 as a deduction, which constituted the tax fraction of the total insurance payouts (R582 383 753.66) recovered by Capitec from its insurers and which Capitec used to settle the outstanding loans owed by its customers with respect to the loan cover.

Commissioner for the South African Revenue Service v Capitec Bank Limited (Case No: 94/2021) (21 June 2022)

Arguments before the Court

- SARS disallowed the deduction claimed by Capitec and contended that the loan cover payments did not qualify for an input tax deduction in terms of section 16(3)(c) of the VAT Act, because the supply of the loan cover did not constitute a 'taxable supply' in that:
    - Capitec did not charge any consideration for the loan cover; and
    - Because the loan cover was supplied in the course of Capitec's business of providing credit to its customers, it was an 'exempt supply'.

Commissioner for the South African Revenue Service v Capitec Bank Limited (Case No: 94/2021) (21 June 2022)

Arguments before the Court

- Capitec contended that since the borrower had to pay interest and fees, consideration was provided for the loan cover, and alternatively that, even if the loan cover was for no consideration, it still levied a fee, termed a 'taxable supply', in terms of section 10(23) of the VAT Act.

- Capitec further contended although it did not charge a distinct fee for its loan cover, the loan cover was integral to its unsecured lending business, and thus generating both interest income and fee income, and that the cost of providing the loan cover was recovered through that income.

Commissioner for the South African Revenue Service v Capitec Bank Limited (Case No: 94/2021) (21 June 2022)

Findings of the Court

- In considering the applicable provisions the SCA found that, inter alia, the clear and unambiguous terms of the loan contract indicated that the customer was to receive loan cover from Capitec free of charge, i.e., no consideration was received by Capitec in respect of its supply of the loan cover.

- Therefore, in the absence of a consideration, the supply of the loan cover did not qualify as an 'enterprise' as envisaged in section 1 of the VAT Act and it was therefore not chargeable with tax in terms of section 7(1)(a) of the VAT Act – which charges tax on supplies in the course or furtherance of an enterprise.

- The SCA went on to say that Capitec made an exempt supply of credit available to its customers, which was not deductible, and all other activities involved in doing do were incidental to the supply of credit, because the supply of the loan cover was not a taxable supply as required by the first proviso to section 16(3)(c)(i) of the VAT Act.

Commissioner for the South African Revenue Service v Capitec Bank Limited (Case No: 94/2021) (21 June 2022)

Findings of the Court

- The SCA held that the tax fraction of the loan cover payouts did not qualify for deduction. Consequently, the main question in the appeal was answered in favour of SARS.

- The SCA found further that Capitec did not apportion the deduction in its return, nor did it plead apportionment as a ground of objection to SARS' assessment or ground of appeal.

- In view of Capitec's failure to plead apportionment and SARS was correct to disallow Capitec's deduction of the whole amount, on this basis alone. Capitec did not raise the issue of a mixed supply in the tax court. Capitec adopted an all or nothing approach. Capitec bore the onus and did not discharge it. Thus, the SCA held that it could not decide this issue on appeal.

Commissioner for the South African Revenue Service v Capitec Bank Limited (Case No: 94/2021) (21 June 2022)

Findings of the Court

- Lastly, in terms of section 213 of the Tax Administration Act No. 28 of 2011 (TAA) read with section 39(1) of the VAT Act, SARS levied a 10% penalty on Capitec for the underpayment of VAT arising from the deduction of notional input tax in respect of the loan cover payouts.

- The SCA found that the requirements in terms of section 217(3) of the TAA, which provided for the remission of the penalty levied, were met. This was because this was the first time a penalty had been imposed by SARS on Capitec in the three years preceding the relevant VAT return; and there were reasonable grounds for Capitec claiming the deduction: Capitec had obtained a favourable opinion from a senior counsel; and the only way Capitec could reasonably have tested the issue was to claim the deduction in its tax return. The SCA thus held that in such circumstances the penalty should have been remitted, as it could not be said that the contesting of the amount was unreasonable.

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