South African Institute of Taxation

Legislative Interpretation

SAIT Webinar
14 April 2022

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Agenda

In this webinar, we will cover the following topics:

- Legislation and policy
  - Reactive submissions
    - SARS draft documents for public comment
- Court cases of interest and tax importance
  - *F Taxpayer v Commissioner for the South African Revenue Service (IT 45842) [2022] ZATC 1*
  - *L'Avenir Wine Estate (Pty) Ltd v Commissioner for the South African Revenue Service (16112/2021) [2022] ZAWCHC 28 (11 March 2022)*
  - *Barnard Labuschagne Incorporated v South African Revenue Service and Another (CCT 60/21) [2022] ZACC 8 (11 March 2022)*

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Presenters

- Jean du Toit: (Head of Tax Technical at Tax Consulting SA)

- Keitumetse Sesana: (Tax Technical Specialist at SAIT)
- Guest:
- Thomas Lobban: (Tax Legal Manager at Tax Consulting SA)

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Recent activity

Draft document for comments:

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

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

Submission date: 31 March 2022

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.

Background

- 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.

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

Background (continued)

- Section 8E deems a dividend or foreign dividend on a hybrid equity instrument to be an amount of income accrued to the recipient and will not be exempt from normal tax. The payer is also not offered a deduction for the payment of affected dividends or foreign dividends.
- The date of issue is important to determine whether a share qualifies as a hybrid equity instrument because that is the date from which the "three-year period" within which the presence of certain redemption rights or obligations for purposes of section 8E must be assessed.
- Section 8E also addresses the enquiry of when redemption features are added to a share or changed after the original issue of the share.

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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.

- ## Background

- *CIR v Conhage (Pty) Ltd* gave birth to Sections 23D and 23G target sale and leaseback arrangements.

- Section 23D is aimed at arrangements in which an asset, which has substantially increased in value owing to currency depreciation or inflation, is sold at market value to another party, such as a financial institution, which then in turn lets or licences the asset back to the seller. In this way, the seller is able to claim a deduction for the lease rentals determined on the increased value of the asset.

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

Background (continued)

- Section 23D is aimed at restricting the allowance which the lessor may claim on the leased asset.
- Section 23G treats targeted sale and leaseback transactions as financial arrangements.
- The objective of section 23G is to prevent one entity from using the tax base of another to obtain a tax benefit.

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SAIT comments on the Draft Interpretation Notes

- **Effect on the Date of Issue of a Share arising from a Change in the Redemption Features**

  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.

- **Sale and Leaseback Arrangements and Related Simulated Transactions**

  "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".

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Recent court cases

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Recent court cases:

- *F Taxpayer v Commissioner for the South African Revenue Service (IT 45842) [2022] ZATC 1*
- *L'Avenir Wine Estate (Pty) Ltd v Commissioner for the South African Revenue Service (16112/2021) [2022] ZAWCHC 28 (11 March 2022)*
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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.

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

<u>CC's approach</u>

- 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)

<u>CC's approach</u>

- 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

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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.

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

<u>CC's findings</u>

- The CC considered the body of case law on the matter and found that the High Court should have found that these judgments can be rescinded.
- The High Court should have considered if the taxpayer made out a case for recission at common law.
- The CC found that the dispute was not covered by the conclusive evidence provisions of section 170, nor was it excluded by section 105.
- The taxpayer was not challenging the correctness of the assessments but whether they had been paid

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

<u>CC's decision</u>

- Having wrongly found that a tax judgment was not rescindable, the High Court was required to revisit the constitutional challenge dismissed in the Court's previous decision in *Metcash Trading*.
- The Court set aside the order of the High Court, and the taxpayer's application for rescission was remitted to the High Court for hearing before a different Judge in order to determine the merits of the application.

L'Avenir Wine Estate (Pty) Ltd v Commissioner for the South African Revenue Service (16112/2021) [2022] ZAWCHC 28 (11 March 2022)

Background

- The taxpayer in this case was a wine producer that approached the HC on an urgent basis for orders permitting it to submit an income tax return for the period from 1 April 2009 to 31 December 2009 and for SARS to assess it for that period ("the disputed period").
- The taxpayer underwent a name change and applied to have the end of its financial year changed to December, which was approved on 25 March 2010. The taxpayer maintains that this took effect for the 2009 tax year, whereas SARS maintains that it applies only from the 2010 tax year.
- This gave rise to the anomaly that there was no return submitted for the disputed period. SARS was not prepared to allow the taxpayer to submit a separate return for this interim period and it refused to issue a reduced assessment for the 2009 and 2010 tax years.

L'Avenir Wine Estate (Pty) Ltd v Commissioner for the South African Revenue Service (16112/2021) [2022] ZAWCHC 28 (11 March 2022)

Background

- The applicant contended that that SARS had to issue a reduced assessment in terms of section 93 of the TAA based on the existence of a “readily apparent undisputed error in the assessment”. SARS rejected this argument.
- The crux of the application is SARS’ refusal to assess the taxpayer for the disputed period. The taxpayer asked for mandatory relief that SARS receive its return and assess it accordingly.

L'Avenir Wine Estate (Pty) Ltd v Commissioner for the South African Revenue Service (16112/2021) [2022] ZAWCHC 28 (11 March 2022)

<u>Court’s approach</u>

- The court noted that the taxpayer overlooked the aspect of PAJA and the interpretation of section 105 of the TAA in *Absa Bank Limited and Another v CSARS 2021 (3) SA 513 (GP)* where it was found that there may be a deviation from the dispute resolution process under Chapter 9 if the HC so directs. Such a departure is justified in “exceptional circumstances”.
- In this case there may be exceptional circumstances but the taxpayer should have approached the court under a review application as opposed to final mandatory relief. The taxpayer conceded on this point.
- The parties were requested to file supplementary papers on if the papers can be amended to constitute a basis for a review application (“conversion”).

L'Avenir Wine Estate (Pty) Ltd v Commissioner for the South African Revenue Service (16112/2021) [2022] ZAWCHC 28 (11 March 2022)

Court's decision

- The taxpayer argued that it would be possible whereas SARS pointed out that it is not possible. The parties are obliged to define the nature of the dispute in their papers and SARS was not called to meet a case based on a review.

- The court agreed with SARS and noted further that if the taxpayer was permitted to make out a case under PAJA, there was a further problem which is the procedural requirements prescribed by PAJA itself.

- In the same vein, if the taxpayer adopted the course of a legality review, it would have to demonstrate that it was brought within a reasonable time.

- A review under PAJA or legality will mean it must raise specific grounds to which SARS must respond. In essence, the taxpayer would then seek to introduce fundamentally different relief.

- On this basis the application was dismissed.

F Taxpayer v Commissioner for the South African Revenue Service (IT 45842) [2022] ZATC 1

Background

- Following an audit performed by SARS in respect of the taxpayer's 2016 to 2018 years of assessment, additional assessments were raised by SARS. The taxpayer requested that SARS provide reasons for the assessments, to enable the taxpayer to properly object to the assessments. The taxpayer duly requested reasons within the 30-day period as allowed by the Rules.

- SARS had 45 business days from the delivery of the taxpayer's request to deliver its reasons, which it failed to do so, and unilaterally extended the time period for delivery of the reasons as per the Rules.

- Upon eventual receipt of the reasons and within the prescribed 30-day time period, the taxpayer delivered its objection against the assessments. Once again, SARS failed to meet the 60-day time period prescribed for providing a notice of outcome of objection. SARS issued a notice of partial disallowance after being served with a Rule 56 notice by the taxpayer.

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F Taxpayer v Commissioner for the South African Revenue Service (IT 45842) [2022] ZATC 1

Background

- The taxpayer delivered a notice of appeal and did not select alternative dispute resolution. SARS was then required to deliver its Rule 31 statement within 45 days thereafter, which it failed to do.

- The taxpayer put SARS on terms for the delivery of the Rule 31 statement, failing which the taxpayer would apply for a final order under section 129(2) of the TAA. SARS advised the taxpayer that only the 2018 tax period had been allocated to her, despite the dispute spanning the 2016 to 2018 years.

- The taxpayer again agreed to allow SARS an extension until 30 July 2021, which SARS agreed to and confirmed that a Rule 31 statement covering all three tax periods would be provided on 30 July 2021. SARS failed to meet this deadline, with the matter allocated to another official and a further extension requested (which was again not met). The taxpayer eventually refused this request. SARS delivered its Rule 31 statement 36 days after expiry of the deadline unilaterally imposed by SARS.

F Taxpayer v Commissioner for the South African Revenue Service (IT 45842) [2022] ZATC 1

Court's decision

- The Court found SARS to have displayed a persistent disregard for the time limits prescribed in the Rules, specifically its failure to seek extension required in respect of providing the reasons, failure to request an extension to file its Rule 31 statement and a failure to provide any explanation to the taxpayer for the delays.

- The taxpayer submitted that the most recent series of delays were simply the perpetuation of a pattern of disregard for the Rules and what is required of administrative functionaries such as the SARS officials in the present matter, which the court agreed with.

- The court ruled that whatever gloss SARS seeks to put on it, the facts of the matter demonstrate that the delays experienced by the taxpayer were egregious, there had been no explanation for the delay and the resultant prejudice to the taxpayer, which prejudice SARS admits (since attempting to mitigate it) is severe.

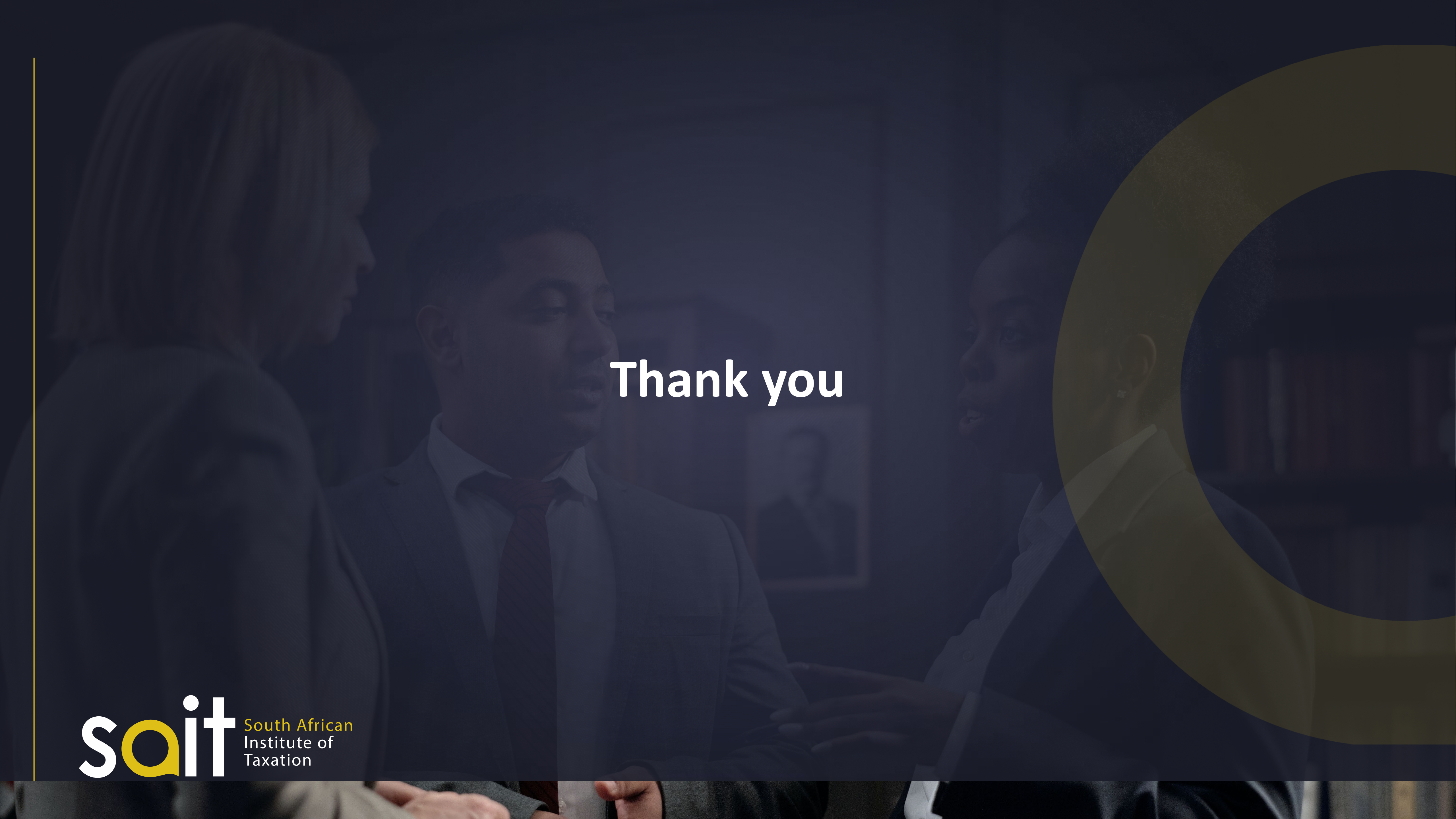
F Taxpayer v Commissioner for the South African Revenue Service (IT 45842) [2022] ZATC 1

Court's decision

- The court went further to state that SARS had dismally failed to fulfil its obligations, both under the constitutionally entrenched right to fair administrative action, the TAA and the Rules.
- SARS' application for condonation in respect of non-adherence to the time-frames imposed in terms of the Rules was dismissed by the court, and the taxpayer's appeals in respect of the 2016 – 2018 years of assessment were upheld.
- The court awarded costs to the taxpayer, but did not award costs on a punitive scale, despite the lambasting judgment.

Thomas Lobban biography

Thomas is a SARS-registered tax practitioner, and a co-author of the LexisNexis Expatriate Tax textbook. Thomas holds an LLB and LLM Tax Law degree and specializes in tax technical matters, with a focus on cross-border taxation and fin-tech matters.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