INTERpretation note no. 19 (issue 2)

DATE: 18 January 2006

act: income tax act, no 58 of 1962 (the act)
section: sections 1, definition of “year of assessment”, 5, 66(13A), 89quat and paragraph 21 of the Fourth Schedule to the act
subject: year of assessment: accounts accepted to a date other than the last day of february

1. purpose
the purpose of this interpretation note is to provide guidance regarding the application of the relevant amendments to the definition of “year of assessment” as well as the discretionary power to grant permission to accept financial accounts for a period which differs from the February year-end (referred to as the substituted period) with reference to natural persons and trusts. the relevant sections are not discussed in detail, but an overview of the changes is provided.

2. background
various amendments to the act during 2002 gave effect to the announcement in the 2002 budget review that all taxpayers who elected to have a june year-end would be brought into the standard arrangement with a February year-end with effect from the 2003 year of assessment.

the following amendments were made:

(i) since 1962, when the current act came into force, certain farmers, fishermen and diamond diggers remained outside the provisional tax system with a june year-end, instead of the general February year-end. sections 1, definition of “year of assessment” and 5 of the act were amended to make provision for a February year-end for all taxpayers.

(ii) section 66(13) was replaced and subsection (13)bis was deleted.

(iii) paragraphs 18(2) to (5) of the Fourth Schedule were deleted.

(iv) Paragraph 22 of the Fourth Schedule was deleted.

(v) Section 66(13)ter was deleted and replaced by section 66(13A). Section 66(13A) provides for financial accounts to be drawn up in respect of a period...
ending on dates other than the last day of February. No new principle was introduced as a result of this amendment – the amendment was consequential upon the replacement of section 66(13) and deletion of section (13)bis.

**Note**: Paragraph (i) above was amended by the Taxation Laws Amendment Act No. 30 of 2002, and paragraphs (ii) to (v) above by the Revenue Laws Amendment Act No. 74 of 2002.

Section 3(1) of the Act provides that the powers conferred and duties imposed upon the Commissioner by or under the provisions of the Act may be exercised or performed by him/her personally or by an employee engaged in carrying out those provisions under his/her control, direction or supervision. SARS’ employees, therefore, perform these powers and duties in order to carry out their daily tasks relating to the collection of taxes. The reference to the Commissioner in this Note, therefore, includes an employee of SARS to the extent that the employee has the delegated power to perform the functions.

This Note focuses on natural persons and trusts.

3. **The law and its application**

3.1 **Definition of “year of assessment” in section 1 read together with section 5**

“Year of assessment” is defined as a year or other period in respect of which any tax or duty leviable under the Act is chargeable. The changes to the definition of “year of assessment” can be summarised as follows:

(i) Period up to and including the 2002 year of assessment (prior to the amendment)

   For this period a year of assessment is -

   - the period of 12 months which runs from 1 March of one year to the last day of February of the succeeding year in respect of natural persons and trusts (excluding farmers, fishermen and diamond diggers who have elected not to be provisional taxpayers); or

   - in respect of farmers, fishermen and diamond diggers who have elected not to be provisional taxpayers, the period of 12 months which runs from 1 July 2001 to 30 June 2002.

(ii) Period from 1 July 2002 to 28 February 2003 (change over period)
Amendments were introduced to the definition of “year of assessment” and section 5. These amendments came into operation on 1 March 2002 and are applicable in respect of any year of assessment commencing on or after 1 March 2002. The effect of the amendment is that all farmers, fishermen and diamond diggers with a June year of assessment will change in respect of the 2003 year of assessment to the last day of February 2003. The 2003 year of assessment for all these taxpayers will, therefore, begin on 1 July 2002 and end on 28 February 2003.

This change was compulsory and was be done programmatically by SARS. The taxpayer may not elect to remain on the old system and does not have to apply for a change of year-end to February to accommodate the changes. Financial statements must, however, be drawn up for an eight month period (from July to February), unless approval has been obtained in terms of section 66(13A) (see paragraph 3.2).

The change-over year will be the 2003 year of assessment and will therefore only consist of an eight month period. This period will be regarded as a year of assessment. The effect will, inter alia, be that:

- Any rebate applicable to the change-over year of assessment will be proportionately reduced in terms of section 6(4) of the Act.
- Allowances in terms of sections 12B and 12C of the Act will not be proportionately reduced.
- Depreciation allowance in terms of section 11(e) of the Act must be calculated for the eight month period.

(iii) Period from 1 March 2003

With effect from 1 March 2003 all natural persons and trusts will have a year of assessment for a period of 12 months which runs from 1 March of one year to the last day of February of the succeeding year.

With reference to trusts it must be emphasised that the year of assessment has always been the last day of February. However, it is realised that certain trusts were permitted to render their accounts to dates other than the end of February. With effect from the 2003 year of assessment these trusts will also have a year of assessment of February. Trusts with an accounting period that differs from a February year-end, will also have a change over period as described in (ii) above.
3.2 Financial statements drawn up for periods that differ from the year of assessment (substituted periods)

3.2.1 Introduction

Section 66(13)ter has been deleted and substituted by section 66(13A). Section 66(13A) came into operation on 1 July 2002 and applies in respect of years of assessment commencing on or after that date.

The purpose of the section is to provide relief in circumstances where it is not convenient for a taxpayer to render accounts in respect of his/her business income ending on the last day of February.

Section 66(13A) provides for financial accounts to be drawn up in respect of a period ending on dates other than the last day of February. It is important to distinguish between a “year of assessment” as defined, and the period for which financial accounts are drawn up. As explained in paragraph 3.1 above, the “year of assessment” of all natural persons and trusts will run from 1 March of one year to the last day of February of the succeeding year. This will not necessarily coincide with the financial year of a business.

In terms of section 66(13A) a taxpayer may apply to the Commissioner to draw up the financial accounts to a date other than the last day of February where the Commissioner is satisfied that the whole or some portion of the taxpayer's income cannot be conveniently returned for any year of assessment. The Commissioner may approve such a request, subject to such conditions as he/she may impose.

Taxpayers who were allowed to submit substituted accounts in terms of the deleted section 66(13)ter and who wish to continue to do so, must re-apply.

Section 66(13A) deems the income for the substituted period to be the income for the year of assessment ending on the last day of February. It is not required to apportio any income to fall into the year of assessment.
Example (A)

H, a general dealer, whose year of assessment ends the last day of February, was always permitted to render financial accounts in respect of his trading income to 31 July. He re-applied in terms of section 66(13A) and his application was approved. During the period 1 August 2002 to 31 July 2003 he earned taxable income of R100 000 in respect of the business and also received a salary of R80 000 for the year of assessment 1 March 2002 to 28 February 2003.

His taxable income for the 2003 year of assessment will be:

- Trading income: R100 000
- Salary income: R80 000
- Taxable income: R180 000

3.2.2 Conditions imposed by the Commissioner

(i) While financial accounts for a business or professional may be submitted to a date different from the year of assessment, the last day of February will be the operative date for all other purposes of the Act, for example, the rebates and rates of tax will be governed by the statutory year of assessment.

(ii) Approval to submit financial accounts to a date other than the last day of February is limited to income derived from a business or profession. The Commissioner will not permit taxpayers to make up their returns in respect of any other income such as remuneration, interest, rentals, royalties, dividends, etc. for a period other than the statutory year of assessment ending on the last day of February.

In the case of remuneration, the employer must comply with the provisions of the Fourth Schedule, for instance, an employees' tax certificate must be issued –

- for the year of assessment ending the last day of February; and
- within 14 days after the end of the year of assessment, i.e. last day of February.

The IT3 returns regarding remuneration not subject to PAYE, interest, rentals, royalties, etc. must also be compiled up to the last day in February of
the year of assessment, notwithstanding that accounts of business are made up to some other date.

Example (B)

| A trader who is also in receipt of a salary may be permitted to render accounts in respect of his trade to, say 30 June, but his salary must be returned to the end of February (using the same statutory year of assessment for both sources of income). |

(iii) Application to render accounts to a date other than the last day of February may involve negative tax implications for the fiscus. The early closing off of financial statements may lead to the manipulation of the income and/or expenditure of a person, for example, the deferral of income derived during peak seasons. Approval will only be allowed if the Commissioner is satisfied that the purpose of such a request is not the obtaining of a tax benefit.

(iv) Approval to render financial accounts up to the end of September will be granted on condition that the income is taxable in the year of assessment ending in February of the same year. Approval to render financial accounts ending after September of a year will be granted allowing the income to be taxed in the year of assessment ending on the last day of February following the closing date of the financial accounts.

In other words, by choosing an accounting date that falls within the period from March to September, the income accruing after the last day of February up to the date the accounting records are drawn up, will be taxed at the rates of tax and rebates that are applicable to the year ending February.

Example (C)

| B was permitted to render financial accounts for the 2004 year of assessment in respect of his farming income to 30 September 2004. The income from farming will be taxable at the rate of tax applicable to the year of assessment ending on the last day of February 2004. Rebates will... |
also be those applicable to the 2004 year of assessment. Other income such as remuneration, interest, etc. should be returned for the 12 months ending the last day of February 2004.

Example (D)

C was permitted to render financial accounts for the 2005 year of assessment in respect of his trading income for the period 1 January 2004 to 31 December 2004. The income from trading will be taxable for the year of assessment ending on the last day of February 2005. The rate of tax chargeable and rebates will be those applicable to the 2005 year of assessment. Other income for the period 1 March 2004 to 28 February 2005 must be reflected in the annual return of income for the 2005 year of assessment. Provisional tax payments will be in line with the February year of assessment (see paragraph 3.4).

(v) Where a beneficiary of a trust has acquired a vested right to any income distributed by a trust, the income will be taxable in the hands of the beneficiary in the same year of assessment as that of the trust.

Example (E)

The Super Trust is permitted to render financial accounts in respect of its trading income to 30 June of each year. Its profits from trading during the period 1 July 2003 to 30 June 2004 were R100 000. An amount of R80 000 was distributed to beneficiary D.

The trust will be taxable on R20 000 for the year of assessment ending on the last day of February 2004, while D will be taxable on R80 000 for the year of assessment ending on the last day of February 2004.

(vi) Requests received from taxpayers will be considered individually, taking the specific circumstances of the taxpayer into account. In the case of a partnership, it must be established that all the partners are in agreement with the request to submit accounts to a date other than the last day of February.

(vii) Application for a substituted period must be in writing and reasons detailing the special circumstances to be taken into account must be furnished. Taxpayers must provide sufficient information and documentation in order for the Commissioner to make an informed decision.
3.2.3 Public Benefit Organisations (PBOs)

The receipts and accruals of any PBO approved by the Commissioner are exempt from tax. All PBOs are obliged to render annual income tax returns, notwithstanding that they are exempt from income tax. A PBO which is a trust may apply for permission to draw up financial accounts for periods ending on dates other than the last of day of February.

Income earned on the investment of funds by a PBO (which is a trust) must be returned to the date approved for submitting the financial accounts of the PBO as such income is inherently part of its funds to be utilised in the ordinary course of its activities.

3.2.4 Share-purchase schemes

Trusts created by employers as vehicles for share-purchase schemes designed to benefit employees normally have the same year end as the company. Permission may be granted to the trust to submit financial accounts in accordance with the year end of the company. In most of these types of trusts, the main source of taxable income will consists of passive income such as interest.

All income received by or accrued to the share-purchase trust may be returned to the date approved for submitting financial accounts of the share-purchase trust.

3.2.5 General

(i) A taxpayer with more than one source of “business” income may apply to have different accounting dates for each source of income. A separate application must be submitted in respect of each business.

Example (F)

A taxpayer applies to submit his substituted accounts as follows:

<table>
<thead>
<tr>
<th>Income Type</th>
<th>Accounting Date</th>
</tr>
</thead>
<tbody>
<tr>
<td>Partnership income (business)</td>
<td>End of March</td>
</tr>
<tr>
<td>Farming income</td>
<td>End of June</td>
</tr>
</tbody>
</table>

(ii) A capital gain or capital loss on the disposal of an asset is determined on the date that the asset is disposed of. Such a gain or loss must be accounted for in the year of assessment in which it was realised. Section 66(13B) provides that the word ‘income’ in section 66(13A) includes any aggregate capital gain or aggregate capital loss. If a farmer, for example, has a year-end of
30 June 2005, any capital gain/loss realised during the period 1 July to 30 June 2005 in respect of the farming activities must be accounted for in the farming accounts ending on 30 June 2005. A capital gain/loss that is not related to the farming business (such as a profit on a holiday home) will form part of the other income and must be returned to February.

(iii) Foreign income

- Foreign interest - where a taxpayer receives an annual certificate from a foreign financial institution which reflects interest earned during the tax year of the foreign country, an equitable apportionment of the income and tax over the tax year would be acceptable. The appropriate portions can then be allocated to the relevant South African year of assessment, taking into account the provisions of section 24J of the Act.

- Remuneration normally accrues on a monthly basis and may be easily accounted for in a year of assessment.

- Dividends accrued on the date of declaration and should not pose any problems.

- Residents (natural persons and trusts) conducting a business offshore may apply for permission to draw up financial accounts according to the offshore year end.

Example (G):

X is a partner in a partnership conducting business in Lesotho. X is the only partner resident in South Africa. The partnership draws up its financial accounts to the end of June. X will be permitted to render financial accounts in respect of the partnership accounts to the end of June.

(iv) The discretionary powers of the Commissioner contained in section 66(13A) are not subject to objection and appeal (see section 3(4) of the Act).

(v) If the circumstances of the taxpayer change, a new application must be submitted.
3.3 **Provisional tax**

Taxpayers who carried on farming, fishing or diamond digging operations on or before 30 June 1965 –

- either elected not to pay provisional tax and had a June year of assessment; 
  or
- had a year of assessment ending on the last day of February and paid provisional tax only once a year.

With effect from the 2003 year of assessment all taxpayers will have a –

- year of assessment ending on the last day of February; and
- liability to make provisional tax payments in terms of paragraph 21 of the Fourth Schedule. [Paragraph 22 of the Fourth Schedule was repealed with effect from years of assessment commencing on or after 1 July 2002]

Paragraphs 18(2) to (5) of the Fourth Schedule were deleted with effect from the commencement of years of assessment ending on or after 1 January 2003. Any election not to be a provisional taxpayer, which was still in force for the 2002 year of assessment, is no longer applicable from the 2003 year of assessment.

The effect of the amendments is that all taxpayers who fall into the definition of “provisional taxpayer” as defined in paragraph (1) of the Fourth Schedule are liable for provisional tax payments (payable twice a year and a third payment where applicable) as follows:

- 1st payment – 31 August
- 2nd payment – End of the year of assessment (February)
- 3rd payment – 30 September (if applicable – 7 months after the year of assessment).

3.4 **Provisional tax and substituted periods**

If approval has been granted to a taxpayer to submit financial accounts to a date other than the last day of February, the taxpayer may apply to make provisional tax payments in line with the closing date of such accounts, as approved by the Commissioner (paragraph 21(2) of the Fourth Schedule).

Paragraph 21(2) refers to accounts drawn to a date falling after the end of the year of assessment. Where accounts are drawn up in respect of dates ending after September but before the last day of February following the closing date of the
financial accounts paragraph 21(2) will not be applicable. Provisional tax payments will, therefore, be payable as indicated in paragraph 3.3.

Taxpayers must apply in writing detailing the special circumstances to be taken into account. Partners in a partnership must apply individually, as the circumstances of each partner must be taken into account. The Commissioner may, having regard to the circumstances of the case, approve provisional tax payments to fall in line with the dates as approved for the substituted periods. This discretion is subject to objection and appeal (see section 3(4) of the Act).

If approval has been granted in terms of section 66(13A) to submit substituted accounts, approval to pay provisional tax according to the dates as approved for the substituted accounts will not automatically be approved. This approval will be conditional on the income from the business or trading activities for which the substituted period is allowed being the main source of income giving rise to a provisional tax liability. In other words, in exercising the discretion in paragraph 21(2) of the Fourth Schedule, the Commissioner will approve payments for provisional tax in accordance with the main source of income.

**Example (H)**

<table>
<thead>
<tr>
<th>A taxpayer receives the following income:</th>
</tr>
</thead>
<tbody>
<tr>
<td>Business income (main source of income) with a February year of assessment.</td>
</tr>
<tr>
<td>Farming income – approval has been granted to submit substituted accounts with a June year-end.</td>
</tr>
</tbody>
</table>

In this case the taxpayer will not receive approval to make provisional tax payments on dates other than 31 August and the last day of February.

Where different accounting dates have been approved in respect of income received from different sources, provisional tax payment dates will be approved having regard to the main source of income giving rise to a provisional tax liability.

In most instances, the first day of the accounting year will be regarded as the date from which the period for the first payment will be reckoned. In the year of conversion, the first provisional tax payment will be six months from the commencement of the year of assessment in question.
Example (I) (change from a February year-end to July year-end)

If approval is granted to a taxpayer, who submitted financial accounts up to 28 February 2003, to submit financial accounts, with effect from the 2004 year of assessment, to 31 July, the provisional tax payments for the year of assessment ending on the last day of February 2004 may be approved as follows:

In respect of the 2004 year of assessment:

1\textsuperscript{st} payment - six months after the date of the commencement of the 2004 year of assessment, i.e. 31 August 2003

2\textsuperscript{nd} payment - 31 July 2004

3\textsuperscript{rd} payment - 31 January 2005

In respect of the 2005 and subsequent years of assessment:

1\textsuperscript{st} payment - six months after 31 July, i.e. 31 January

2\textsuperscript{nd} payment - 31 July

3\textsuperscript{rd} payment - 31 January

All other income such as remuneration, interest, rent, etc. must still be accounted for during the 12 months ending the last day of February and taken into account in calculating provisional tax payable for January and July.

Example (J)

G, who always submitted his accounts on the last day of February, has now requested to submit his financial accounts on 30 September, with effect from the 2004 year of assessment. He also requested to pay provisional tax in line with the accounting date. For the 2003 year of assessment G would have submitted accounts for the period 1 March 2002 to 28 February 2003. If approval is granted for the 2004 year of assessment he will submit financial accounts for the period 1 March 2003 to 30 September 2004, i.e. an extended period of 19 months.

Provisional tax for the 2004 year of assessment will be payable as follows:

- 1\textsuperscript{st} payment - 31 August 2003
- 2\textsuperscript{nd} payment - 30 September 2004
In respect of the 2005 and subsequent years of assessment, provisional tax payments will be payable on the following dates:

- 1st payment - 31 March
- 2nd payment - 30 September
- 3rd payment - 31 March

Example (K) (December year-end)

H, who always submitted his accounts on the last day of February, has now requested to submit his financial accounts on 31 December, with effect from the 2004 year of assessment. He also requested to pay provisional tax in line with the accounting date.

For the 2003 year of assessment H would have submitted accounts for the period 1 March 2002 to 28 February 2003. For the 2004 year of assessment he will submit financial accounts for the period 1 March 2003 to 31 December 2003, i.e. a short period of 10 months.

Provisional tax for the 2004 and subsequent years of assessment will be payable as follows (see second paragraph of paragraph 3.4):

- 1st payment - 31 August
- 2nd payment - 28 February
- 3rd payment - 30 September

3.5 Interest on underpayments and overpayments of provisional tax

Whenever a substituted period has been approved for provisional tax payments, the “effective date” (as defined in section 89quat(1) of the Act) in relation to a year of assessment will be six months after the last day of the second provisional tax payment relating to the substituted period approved by the Commissioner.

3.6 Trading stock and livestock

3.6.1 Trading stock

The provisions of section 22 of the Act regarding trading stock held and not disposed of apply at the beginning and end of years of assessment.

The same applies where accounts are accepted on a date agreed to by the Commissioner [section 22(6)]. The reference in section 22 to the beginning or end of the year of assessment will mean, where accounts are accepted in terms of
section 66(13A), a reference to the beginning or end of the period covered by the accounts.

3.6.2 Livestock

Paragraph 1 of the First Schedule to the Act contains a similar provision.

4. Value-Added Tax (VAT)

A vendor whose enterprise consists solely of agricultural, pastoral or other farming activities and the value of whose taxable supplies from such farming activities does not exceed (and is not likely to exceed) R1m per annum, may apply in writing to submit six-monthly returns – so-called Category D returns (section 27(4) of the Value-Added Tax Act, No. 89 of 1991). These tax periods end on the last day of February and August, unless the vendor makes written application for his tax periods to end on such other days as the Commissioner may approve.

Farmers who previously had June year-ends who have now changed to a February year-end may apply to submit VAT returns in line with their new tax year-end.