Preface

This guide provides a basic introduction to capital gains tax (CGT) and should not be used as a legal reference.

For more information about CGT you may –

- visit the SARS website at www.sars.gov.za;
- visit your nearest SARS branch;
- contact your own tax advisor or tax practitioner;
- contact the SARS National Contact Centre –
  - if calling locally, on 0800 00 7277;
  - if calling from abroad, on +27 11 602 2093 (only between 8am and 4pm South African time); or
- consult the Comprehensive Guide to Capital Gains Tax or the Tax Guide for Share Owners, both of which are available on the SARS website.

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## Contents

Preface ................................................................................................................................... i

1. Introduction .................................................................................................................... 1

2. Overview of the core provisions of capital gains tax .................................................. 1

3. Determining a capital gain or loss ............................................................................... 2

3.1 Asset .......................................................................................................................... 2

3.2 Disposal ..................................................................................................................... 3

3.3 Proceeds .................................................................................................................... 3

3.4 Base cost ................................................................................................................... 3

4. Base cost of assets acquired before 1 October 2001 ................................................. 4

4.1 “20% of proceeds” method ......................................................................................... 4

4.2 Market-value method .................................................................................................. 5

4.3 Time-apportionment base cost method ....................................................................... 7

5. Examples ..................................................................................................................... 8

6. Aggregate capital gain or loss ...................................................................................... 9

7. Net capital gain or assessed capital loss ....................................................................... 10

8. Inclusion rate and taxable capital gain ......................................................................... 10

9. Effective rates of CGT ............................................................................................... 11
1. Introduction

Capital gains tax (CGT) was introduced in South Africa with effect from 1 October 2001 and applies to the disposal of an asset on or after that date. Internationally, the idea of such a tax is not uncommon, with many of South Africa’s trading partners having implemented CGT decades ago.

All capital gains and losses made on the disposal of assets are subject to CGT unless specifically excluded.

The CGT provisions are mostly contained in the Eighth Schedule to the Income Tax Act 58 of 1962 (the Act), although some are in the main body of the Act, such as those dealing with change of residence, ceasing to be a controlled foreign company or becoming a headquarter company (section 9H), government grants (section 12P), international shipping (section 12Q) and the corporate restructuring rules (sections 41 to 47). The Eighth Schedule determines a taxable capital gain or assessed capital loss and section 26A of the Act provides that the taxable capital gain must be included in taxable income.

2. Overview of the core provisions of capital gains tax

The CGT Flowchart below sets out the core steps in determining a taxable capital gain to be included in taxable income or an assessed capital loss to be carried forward to a subsequent year of assessment.
3. Determining a capital gain or loss

The Eighth Schedule contains four key definitions (Asset, Disposal, Proceeds and Base Cost) which form the basic building blocks in determining a capital gain or loss.

3.1 Asset

An asset is widely defined and includes property of whatever nature and any right to, or interest in, such property. CGT applies to all assets disposed of on or after 1 October 2001 (valuation date), regardless of whether the asset was acquired before, on, or after that date.

Nevertheless, only the capital gain or capital loss attributable to the period on or after 1 October 2001 must be brought to account for CGT purposes.
3.2 Disposal
A disposal covers any event, act, forbearance or operation of law which results in the creation, variation, transfer or extinction of an asset. It also includes specified events treated as disposals, such as the change in the use of an asset, the commencement or cessation of residence, a company ceasing to be a controlled foreign company and a company becoming a headquarter company.

3.3 Proceeds
The amount received by or accrued to the seller on disposal of the asset constitutes the proceeds. Assets disposed of by donation, for a consideration not measurable in money, or to a connected person at a non-arm’s-length price are treated as being disposed of for an amount received or accrued equal to the market value of the asset. Proceeds will also be treated as being at market value when specified deemed disposal events occur, such as cessation of residence, company ceasing to be a controlled foreign company, company becoming a headquarter company and conversion of a capital asset to trading stock or distribution of an asset in specie. Amounts included in income such as a recoupment of capital allowances are excluded from proceeds.

3.4 Base cost
Broadly the determination of the base cost of an asset depends on whether it was acquired –

- on or after 1 October 2001;
- before 1 October 2001;
- by donation, for a consideration not measurable in money or from a connected person at a non-arm’s length price; or
- in consequence of a deemed disposal event such as a distribution in specie, cessation of residence, company ceasing to be a controlled foreign company, company becoming a headquarter company or conversion of a capital asset to trading stock.

The assets described in the last two bullet points are generally treated as having been acquired at a cost equal to their market value.

Assets acquired on or after 1 October 2001
The base cost of an asset acquired on or after 1 October 2001 generally comprises the actual expenditure incurred on the asset. In order to qualify for inclusion in base cost, such expenditure must appear on the list of qualifying expenditure in paragraph 20 of the Eighth Schedule. Some of the main costs that qualify to be part of the base cost of an asset include –

- the costs of acquisition or creation of the asset;
- the cost of valuing the asset for the purpose of determining a capital gain or loss;
- the following amounts actually incurred as expenditure directly related to the acquisition or disposal of the asset, namely—
  - the remuneration of a surveyor, valuer, auctioneer, accountant, broker, agent, consultant or legal advisor, for services rendered;
  - transfer costs;
- securities transfer tax, transfer duty or similar tax or duty;
- advertising costs to find a seller or to find a buyer;
- moving costs;
- installation costs including foundations and supporting structures;
- donations tax limited by a formula;
- cost of an option used to acquire or dispose of the asset;

- cost of establishing, maintaining or defending a legal title to or right in the asset;
- cost of effecting an improvement to or enhancement of the value of the asset; and
- value-added tax incurred on an asset and not claimed as an input tax credit for value-added tax purposes.

**Holding costs**

Holding costs generally do not form part of the base cost of an asset. Expenditure on repairs, maintenance, protection, insurance, rates and taxes, or similar expenditure is specifically excluded. Borrowing costs (including bond registration costs, bond cancellation costs and raising fees) are also generally excluded with one exception. Under that exception a person is entitled to add to base cost one-third of the interest incurred on borrowings used to acquire listed shares and participatory interests in collective investment schemes. One-third of the interest incurred on borrowings used to refinance such investments may also be included. However, interest on borrowings used to finance the acquisition of shares in an operating company contemplated in section 24O may not be included in the base cost of those shares since such interest would be deductible against the borrowing company’s income under that section.

**Reduction of base cost**

Any expenditure referred to above which is allowable against a company’s income must be reduced in arriving at the base cost of an asset. For example, capital allowances will reduce the expenditure incurred in acquiring an asset.

**4. Base cost of assets acquired before 1 October 2001**

In order to exclude the portion of the capital gain relating to the period before 1 October 2001, the base cost of the asset as at that date must be determined according to any one of the following methods:

- “20% of proceeds”
- Market value on 1 October 2001
- Time-apportionment base cost

**4.1 “20% of proceeds” method**

Under this method the valuation date value of the asset is equal to 20% of the proceeds after first deducting from the proceeds any allowable expenditure incurred on or after 1 October 2001. This method would typically be used when no record of pre-valuation date expenditure exists and no valuation was obtained at 1 October 2001.
4.2 Market-value method

Under the market-value method, the market value of the asset on 1 October 2001 must be determined. Various requirements apply before the market-value method can be used.

Time limit for performing valuations

All valuations must have been completed by 30 September 2004. If a company failed to perform a valuation by this date, it will not be permitted to use the market-value method. Valuations must be performed as if done on 1 October 2001. The prices on 1 October 2001 of specified financial instruments such as South African-listed shares and participatory interests in South African collective investment schemes were determined by SARS and published in the Government Gazette. A company is required to use these prices and therefore does not need to determine its own values for these assets. The prices are also available on the SARS website.

Who may perform valuations?

The Act does not prescribe who may perform a valuation. This task was the responsibility of the company and the onus of substantiating a valuation rests with the company. A company was, however, entitled to appoint a professional person to assist with the valuation.

Methods to be adopted in valuing specified assets

In general the Act does not specify the methods to be used in performing valuations, though there are some exceptions which are summarised in the table below.

Table 1 – Market value on 1 October 2001

<table>
<thead>
<tr>
<th>Type of asset</th>
<th>Valuation method</th>
</tr>
</thead>
<tbody>
<tr>
<td>General rule</td>
<td>Market value = price based on willing buyer, willing seller acting at arm’s length in an open market</td>
</tr>
<tr>
<td>South African-listed securities</td>
<td>Volume weighted average price for the five business days preceding 1 October 2001</td>
</tr>
<tr>
<td>Foreign listed securities</td>
<td>The ruling price (usually the last sell price) on the last business day before 1 October 2001</td>
</tr>
<tr>
<td>Participation rights and “property shares” in South African collective investment schemes</td>
<td>Average &quot;sell to management company&quot; price for the last five trading days before 1 October 2001</td>
</tr>
<tr>
<td>Participation rights in foreign collective investment schemes</td>
<td>Same as for South African collective investment schemes, except based on last trading day before 1 October 2001</td>
</tr>
</tbody>
</table>

1 Prices supplied in Government Gazette 23037 of 25 January 2002 and on SARS website under Types of Tax / Capital Gains Tax / Market Values.

2 Same as footnote 1.
Type of asset | Valuation method
--- | ---
Controlling interest in listed company | The listed price at 1 October 2001 must be adjusted by the control premium or discount at the time of sale
South African second-hand endowment policies | Greater of –
- Surrender value
- Insurer's market value (assume policy runs to maturity)
Farm land | Market value less 30% or market value based on what a willing buyer would pay a willing seller dealing at arm’s length in an open market.

Submission requirements

Generally, proof of any valuation performed within the prescribed period must be retained for five years after the date of submission of the return reflecting the disposal of the asset. However, with the high-value assets described in the table below, the valuation forms were required to be lodged with the first return of income submitted after 30 September 2004. If the return was not thus submitted, the person disposing of the asset will not be permitted to use the market-value method for these assets.

Table 2 – Assets subject to early valuation submission requirements

<table>
<thead>
<tr>
<th>Type of asset</th>
<th>Applies</th>
<th>If market value exceeds</th>
</tr>
</thead>
<tbody>
<tr>
<td>Intangible assets (such as goodwill and trade marks)</td>
<td>Per asset</td>
<td>R1 million</td>
</tr>
<tr>
<td>Unlisted shares</td>
<td>All shares held by the person in the company</td>
<td>R10 million</td>
</tr>
<tr>
<td>All other assets</td>
<td>Per asset</td>
<td>R10 million</td>
</tr>
</tbody>
</table>

Limitation of losses

The Eighth Schedule contains loss-limitation rules which apply when the market value of an asset on 1 October 2001 has been determined, or has been published in the Government Gazette (the latter would apply, for example, to South African-listed shares). Under specified circumstances a person’s ability to choose a method for determining the valuation date value of an asset will be restricted by these rules which are beyond the scope of this guide.

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3 Section 29(3)(a) of the Tax Administration Act 28 of 2011 read with paragraph 29(6) of the Eighth Schedule.
## 4.3 Time-apportionment base cost method

The time-apportionment base cost method may be used when a company has a record of the date of acquisition and cost of an asset. The following formula is used to determine the time-apportionment base cost of an asset:

\[ Y = B + [(P - B) \times N / (N + T)] \]

In which –

- **Y** = The amount to be determined
- **B** = Allowable expenditure incurred before 1 October 2001
- **P** = Proceeds on disposal of asset
- **N** = Number of years or part of a year before 1 October 2001
- **T** = Number of years or part of a year on or after 1 October 2001

For purposes of this formula the following should be borne in mind:

- Improvements or additions made before 1 October 2001 are assumed to have taken place when the asset was acquired.
- A part of a year is treated as a full year.
- The period before 1 October 2001 is limited to 20 years when –
  - improvements have been made to an asset in more than one year of assessment before 1 October 2001; and
  - the asset was acquired before 1 October 1981.
- When no additions or improvements have taken place before valuation date, the 20-year limit does not apply.
- When capital allowances have been claimed on an asset for normal tax purposes –
  - the proceeds must be reduced by the amount of any recoupments; and
  - the expenditure must be reduced by the amount of any capital allowances that the company was entitled to claim as a deduction.

The following additional formula must be used to determine the value of “P” (proceeds) when improvements to an asset occur on or after 1 October 2001:

\[ P = R \times B / (A + B) \]

In which –

- **R** = Amount received or accrued from disposal of asset
- **B** = Allowable expenditure incurred before 1 October 2001
- **A** = Allowable expenditure incurred on or after 1 October 2001

A special “depreciable assets” formula applies when –

- capital allowances have been claimed on an asset;
- additions to the asset have occurred on or after 1 October 2001; and
• the proceeds from the disposal of the asset exceed all the allowable expenditure on the asset.

The use of the special depreciable assets formula is illustrated in Example 2.

Selling expenses (for example, estate agent’s commission) are treated as a reduction in proceeds for the purpose of determining the time-apportionment base cost. This aspect is not illustrated in the examples which follow.

To assist taxpayers, SARS has made available a time-apportionment base cost calculator (“TAB calculator”) on its website which uses an Excel spreadsheet. The TAB calculator does not apply when the special depreciable assets formulae are applicable. More advanced examples can be found in the Comprehensive Guide to Capital Gains Tax.

5. Examples

Example 1 – Time-apportionment base cost: All expenditure incurred before valuation date

Facts:
ABC (Pty) Ltd has a financial year ending on the last day of February. It purchased a machine for R100 000 on 1 September 1996 and sold it for R150 000 on 29 February 2020. At the date of sale, capital allowances of R100 000 had been claimed on the machine.

Result:
(a) Exclude recoupment from amount received or accrued and capital allowances from cost

<table>
<thead>
<tr>
<th>Consideration received or accrued</th>
<th>R 150 000</th>
</tr>
</thead>
<tbody>
<tr>
<td>Less: Recoupment</td>
<td>(100 000)</td>
</tr>
<tr>
<td>Proceeds for CGT purposes</td>
<td>50 000</td>
</tr>
<tr>
<td>Cost</td>
<td>100 000</td>
</tr>
<tr>
<td>Less: Capital allowances</td>
<td>(100 000)</td>
</tr>
<tr>
<td>Cost for CGT purposes</td>
<td>0</td>
</tr>
</tbody>
</table>

(b) Determine time-apportionment base cost

\[ Y = B + \left( P - B \right) \times \frac{N}{N + T} \]
\[ = R0 + \left( R50 000 - R0 \right) \times \frac{6}{25} \]
\[ = R0 + R12 000 \]
\[ = R12 000 \]

(c) Determine capital gain or loss

<table>
<thead>
<tr>
<th>Proceeds</th>
<th>R 50 000</th>
</tr>
</thead>
<tbody>
<tr>
<td>Less: Base cost</td>
<td>(12 000)</td>
</tr>
<tr>
<td>Capital gain</td>
<td>38 000</td>
</tr>
</tbody>
</table>
Example 2 – Time-apportionment base cost: Expenditure incurred after valuation date

**Facts:**

XYZ (Pty) Ltd has a financial year ending on the last day of February. It purchased a machine for R100 000 on 1 September 1996. The machine was upgraded on 1 July 2018 at a cost of R10 000.

The machine was sold for R150 000 on 29 February 2020. At the date of sale, capital allowances of R100 000 had been claimed on the original cost of the machine while allowances of R4 000 had been claimed on the cost of improvements.

**Result:**

(a) Exclude recoupments from proceeds

\[
\begin{array}{c|c|c}
\text{Consideration received or accrued} & 150 000 \\
\text{Less: Recoupment} & (104 000) \\
\text{Proceeds for CGT purposes} & 46 000 \\
\end{array}
\]

(b) Exclude capital allowances from cost

<table>
<thead>
<tr>
<th>Before</th>
<th>After</th>
<th>Total</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>1 October 2001</td>
<td>1 October 2001</td>
<td></td>
</tr>
<tr>
<td>Cost</td>
<td>100 000 (B1)</td>
<td>10 000 (A1)</td>
</tr>
<tr>
<td>Less: Capital allowances</td>
<td>(100 000)</td>
<td>(4 000)</td>
</tr>
<tr>
<td>Cost for CGT purposes</td>
<td>0 (B)</td>
<td>6 000 (A)</td>
</tr>
</tbody>
</table>

(c) Determine portion of proceeds relating to period before valuation date

\[P_1 = \frac{R_1 \times B_1}{A_1 + B_1}\]

\[= \frac{R150 000 \times R100 000}{R110 000} \]

\[= R136 364\]

(d) Determine time-apportionment base cost

\[Y = B + [(P_1 - B_1) \times N / (N + T)]\]

\[= R0 + [(R136 364 - R100 000) \times 6 / 25]\]

\[= R8 727\]

(e) Determine capital gain or loss

\[
\begin{array}{c|c|c}
\text{Proceeds} & 46 000 \\
\text{Less: Valuation date value} & (8 727) \\
\text{Cost after valuation date} & (6 000) \\
\text{Capital gain} & 31 273 \\
\end{array}
\]

6. **Aggregate capital gain or loss**

A company’s aggregate capital gain or loss is determined by adding the capital gains and losses on individual assets together for a specific year of assessment.
7. **Net capital gain or assessed capital loss**

A company’s net capital gain or assessed capital loss is determined by deducting any assessed capital loss brought forward from the previous year of assessment from the aggregate capital gain or loss. An assessed capital loss may be deducted only from capital gains and added to capital losses. It may not reduce taxable income.

8. **Inclusion rate and taxable capital gain**

The taxable capital gain of a company is determined by multiplying the net capital gain by the inclusion rate. For years of assessment commencing on or after 1 March 2016 the inclusion rate of a company or close corporation is 80%. For years of assessment commencing on or after 1 March 2012 it was 66.6% and before that 50%.

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**Example 3 – Determination of a taxable capital gain**

**Facts:**

XYZ (Pty) Ltd realized the following capital gains and losses during its financial year ended 29 February 2020:

<table>
<thead>
<tr>
<th>Description</th>
<th>Value</th>
</tr>
</thead>
<tbody>
<tr>
<td>Vacant land</td>
<td>R 50 000</td>
</tr>
<tr>
<td>Trade mark</td>
<td>R 25 000</td>
</tr>
<tr>
<td>Loan (debtor insolvent)</td>
<td>(R 5 000)</td>
</tr>
<tr>
<td>Shares</td>
<td>(R 10 000)</td>
</tr>
<tr>
<td>Aggregate capital gain</td>
<td>R 60 000</td>
</tr>
</tbody>
</table>

XYZ (Pty) Ltd does not have an assessed capital loss from the previous year of assessment.

**Result:**

<table>
<thead>
<tr>
<th>Description</th>
<th>Value</th>
</tr>
</thead>
<tbody>
<tr>
<td>Aggregate capital gain</td>
<td>R 60 000</td>
</tr>
<tr>
<td>Less: Assessed capital loss brought forward</td>
<td>(0)</td>
</tr>
<tr>
<td>Net capital gain</td>
<td>R 60 000</td>
</tr>
<tr>
<td>Taxable capital gain 60 000 × 80%</td>
<td>R 48 000</td>
</tr>
</tbody>
</table>

The taxable capital gain will be included in the company’s taxable income and taxed at the rate of 28%, that is, R48 000 × 28% = R13 440,00. The effective rate of tax on the sum of all the gains and losses is R13 440,00 / R60 000 × 100 = 22.4%.
9. Effective rates of CGT

Table 3 – Statutory, inclusion and effective rates of tax (1 April 2019 to 31 March 2020)

<table>
<thead>
<tr>
<th>Type of company</th>
<th>Inclusion rate</th>
<th>Statutory rate</th>
<th>Effective rate</th>
</tr>
</thead>
<tbody>
<tr>
<td>Company &amp; Close corporation</td>
<td>80</td>
<td>28</td>
<td>22.4</td>
</tr>
<tr>
<td>Small business corporation</td>
<td>80</td>
<td>0 – 7 – 21 – 28</td>
<td>0 – 5.6 – 16.8 – 22.4</td>
</tr>
<tr>
<td>Micro business&lt;sup&gt;4&lt;/sup&gt;</td>
<td>50</td>
<td>0 – 1 – 2 – 3</td>
<td>0 – 0.5 – 1 – 1.5</td>
</tr>
<tr>
<td>Taxable income derived by company in special economic zone</td>
<td>80</td>
<td>15</td>
<td>12</td>
</tr>
<tr>
<td>Life Assurer – individual policyholder fund</td>
<td>40</td>
<td>30</td>
<td>12</td>
</tr>
<tr>
<td>Life Assurer – company policyholder fund</td>
<td>80</td>
<td>28</td>
<td>22.4</td>
</tr>
<tr>
<td>Life Assurer – untaxed policyholder fund</td>
<td>0</td>
<td>0</td>
<td>0</td>
</tr>
<tr>
<td>Life Assurer – corporate fund</td>
<td>80</td>
<td>28</td>
<td>22.4</td>
</tr>
<tr>
<td>Life Assurer – Risk policy fund</td>
<td>80</td>
<td>28</td>
<td>22.4</td>
</tr>
</tbody>
</table>

<sup>4</sup> Under paragraph 57A a micro business’s assets are not subject to CGT. However, under paragraph 6 of the Sixth Schedule 50% of the receipts of a capital nature from the disposal of micro business assets are included in taxable turnover.