IN THE TAX COURT OF SOUTH AFRICA
BLOEMFONTEIN

Case No. : VAT867

In the matter between:-

MR. X Appellant

and

THE COMMISSIONER FOR THE SOUTH AFRICAN REVENUE SERVICE Respondent

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CORAM: DAFFUE, J

ASSESSORS: MR J. LIEBENBERG and MR B. MATHIBELA

HEARD ON: 17 FEBRUARY 2015

DELIVERED ON: 26 June 2015

I INTRODUCTION

[1] This is an appeal by the taxpayer, Mr X ("the taxpayer") against an assessment by the Commissioner for the South African Revenue Services ("SARS") dated as long ago as 21 May 2008 in respect of value added tax ("VAT") for the tax period ending December 2007.

[2] The taxpayer was assessed for payment of VAT in the amount of R228 258.87. Interest and penalties were added and the total amount claimed was R258 978,91.

[3] The appeal is opposed by SARS.

[4] Adv Y appeared for the taxpayer and Adv Z represented SARS.

II PRELIMINERY MATTERS

[5] SARS took a point *in limine* based on the taxpayer's alleged non-compliance with rule 32(2)(a) and (c) pertaining to his statement of grounds of appeal. It was submitted that the grounds upon which the taxpayer appeals and the material facts and legal grounds upon which the taxpayer relies were not properly stated. SARS knew all the time what was the case it had to meet and it could not show any disadvantage. Having considered the history of the matter and submissions by the parties, we ruled that insofar as an amended statement was filed, albeit late, the taxpayer's non-compliance be condoned.

[6] Hereafter, and for the reasons shown later, Adv Z placed on record that SARS conceded that the taxpayer should not have been assessed in respect of output tax and that the only issue in dispute and to be addressed in the appeal was the computation of input tax and the taxpayer's entitlement to claim such tax.

III MATERIAL FACTUAL MATRIX WITH REFERENCE TO THE BUNDLE PRESENTED AS EXHIBIT "A"

[7] It is deemed necessary to set out the background to the appeal in some detail in order also for the reader to understand the amazing set of circumstances leading to this appeal and our conclusion that so much unnecessary energy and money were spent eventually in order to finalise a dispute that should have been settled six years earlier.

[8] On 27 August 2003 the taxpayer filled out VAT 101 in order to register as a vendor in terms of the Value Added Tax Act, 89 of 1991, as amended ("the VAT Act"). SARS received his application in September 2003 and registered him accordingly. *Ex facie* the application for registration the taxpayer stated his main activity as "Telecommunication Community Services Phones".

[9] Some two years later the taxpayer arranged for the formation and registration of a Close Corporation, to wit AS CC ("the CC"). There is no indication from the documentation before us whether the CC was ever registered for income tax purposes. It was not registered as a vendor for VAT.

[10] The CC, represented by the taxpayer, tendered for two construction contracts. Tenders were awarded which led to construction contracts being entered into. The tender in respect of the one contract relating to the J Local Municipality ("local Municipality") was clearly prepared by the CC and *inter alia* provided for VAT at a rate of 14% to be charged on

the contract price. In the construction contract the contractor was described as X (the name of the taxpayer) and the name of the applicable "legal body" was stated as K Construction without reference to its corporate status, to wit that of close corporation. We are not in possession of the full contract documents pertaining to the second construction contract entered into with government ("the Department"). However we gather from the documentation presented to us that the taxpayer confirmed that he was authorised to sign the contract in his capacity as managing director of the entity referred to as K Construction without reference to it as a close corporation. When one looks at the progress payments and invoices of suppliers in respect of the particular building contract; the contractor's name is shown as K Construction in the one case and on the invoices as K Construction CC. Having considered documentation and also the evidence to which we shall return, it is apparent that the taxpayer in his personal capacity was not the contractor in respect of these two contracts.

[11] The taxpayer's books were apparently in a mess. Ms. B, the auditor who was involved with the audit of the taxpayer's VAT returns, stated on 19 March 2008 in an email that she had by then already handed her findings to the taxpayer on 17 March 2008, that is two days earlier, and that he had 14 days to respond before she would raise her assessments. This caused a Mr C to respond thereto on 6 April 2008 indicating that the taxpayer completed the VAT returns on his own, that his bookkeeping was in a mess and that he had

been instructed to "sort this mess out". He needed an extension of 45 days, "…taking into account the registration of VAT that needs to be done. He (the taxpayer) has combined the account records of his public phone's business with the accounting records of his CC." This letter was received by MS B on 11 April 2008 and she responded thereto, stating that Mr C was not the authorised accountant according to SARS' information and that any corrections could be done from the 02/08 tax period onwards, meaning that if the taxpayer wanted to "….split the two types of business ventures (telephones and constructions) this must also be done from the periods following the periods of the audit. No backdated changes can be done."

[12] *Ex facie* the assessment letter of 21 May 2008 SARS made adjustments to both the VAT outputs and inputs of the taxpayer for the period ending December 2007. The taxpayer apparently did not declare any outputs on income received and as a result of the audit SARS included the amounts received from the Local Municipality, a government department and a telecommunication company as income and calculated the output tax accordingly. SARS accepted the income from the public phones to be in accordance with the summary provided by the taxpayer. Pertaining to the adjustments regarding input tax, several amounts were not accepted as input tax for various reasons, *inter alia* due to non-compliance with the provisions of the VAT Act, invoices were not made out to the taxpayer and others were clearly in respect of personal expenses.

[13] On 23 June 2008 the taxpayer on behalf of the CC and on a letterhead of the CC objected to the audit and assessment. He indicated clearly in this letter the following: "We are an emerging small construction company…" (emphasis added.) He challenged the assessment in respect of the payments received from the Department on the basis that the amounts received did not qualify as income, but loans paid out to the contractor to assist it in completing the construction contract. SARS was not satisfied with the manner in which the objection was raised and on 25 July 2008 informed the taxpayer of the proper procedure to be followed. This caused a delay of a year and a formal objection in the form required by SARS was received on 25 August 2009 only. In this further objection the taxpayer again set out his objections referred to earlier, but amplified those as well. He also referred to the fact that some of the payments received from the Local Municipality were paid without the municipality allowing for any VAT. In respect of the telecommunication phone business it was stated that the amount of R246 373,32 relied upon by SARS was the total airtime sales for that year, but the taxpayer was only entitled to 33% commission thereon. As the telecommunication system does not allow for VAT it was not possible to charge output tax. Notwithstanding this the taxpayer claimed input tax. Not a word was said in this objection pertaining to the CC or the fact that the two construction contracts were entered into with the CC. Fact of the matter is that SARS was informed of this more than a year earlier.

[14] The taxpayer's objection was dismissed on 4 March 2010 whereupon the taxpayer filed a notice of appeal. The matter was eventually heard by the Tax Board on 14 June 2010. Two small amounts in respect of input tax were allowed, but otherwise the assessment was not interfered with at all. We have reason to accept, although we are not in possession of a copy of the decision of the Tax Board, that the matter was not argued based on the taxation of the wrong entity.

[15] Nothing further transpired and this caused SARS to take steps to apply for civil judgment for recovery of the outstanding tax debt. The matter was set down and the file was allocated to D. At the last minute the taxpayer instructed legal representatives and by agreement SARS did not proceed with its application on the allocated date.

[16] On 30 October 2014 the following orders were made:

> "It is ordered (by agreement):
>
> 1. The matter be postponed and set down for trial on 17 and 18 February 2015;
> 2. Shortened time limits shall apply;
> 3. The respondent shall file his notice of intention to oppose on or before 13 November 2014;
> 4. The respondent shall within 15 days from serving his notice of intention to oppose file his answering affidavit stating reasons why the application is opposed;
> 5. The respondent shall file his statement of grounds of appeal in terms of rule 32 on or before 28 November 2014;
> 6. E Attorneys of Bloemfontein have been instructed as respondent's attorneys of record and that all documents to be

served on the respondent may be served on this firm of attorneys.

It is further ordered that:

7. The respondent shall co-operate immediately when called upon by the applicant for a pre-trial to be conducted well in advance of trial dates given;
8. This is a final postponement;
9. Respondent shall be liable for the costs of the day including all other wasted costs incurred as a result of the postponement of this matter."

[17] It should immediately be said that D was not privy to all the documents now contained in exhibit "A" at the stage when he considered the aforesaid application.

[18] The matter eventually went on trial on 17 February 2015 based on the appellant's appeal to this court and evidence was led.

[19] During the preparation for the hearing it was established that the CC was in actual fact the contractor and recipient of income in terms of the contracts with the Local Municipality and the Department . When the matter was called the issue was immediately raised with the legal representatives of the parties.

[20] The effect of such discovery is that, bearing in mind the authorities referred to later, the appeal has to succeed, albeit partially, and the assessment has to be set aside, or altered, or referred back to SARS for the reasons advanced below.

[21] SARS's legal representatives considered the issue and its counsel conceded eventually that the output tax relating to income received in respect of the Local Municipality and the Department contracts had to be ignored and/or written back. On the other hand, all input tax claimed in respect of expenses allegedly incurred relating to these two contracts and/or the CC as well as all personal expenses unrelated to the Telecommunication phone business had to be disallowed.

IV THE EVIDENCE

[22] The taxpayer testified and thereafter closed his case. Ms B, the auditor whose team was responsible for the audit and made the assessment, testified on behalf of SARS.

[23] The taxpayer explained that it was impossible to present his case properly as all his tax invoices and other supporting documents were given to SARS during the audit process and were never returned to him. Ms B disputed this and stated that SARS does not keep such documents and return these to taxpayers after they have served their purpose. SARS simply does not have sufficient storage facilities to keep unnecessary documents. It is common cause that the taxpayer prepared a spread sheet during SARS' audit, which document is contained in Exhibit "A", *inter alia* at pages 99 to 134. He added all the information contained in columns A to G, whilst Me B added columns H, I and J and the summary at the bottom. Column H contains the amounts found by SARS at the time to be the correct VAT amounts claimed.

The figures in column I reflect the difference between the amounts claimed and allowed and the reasons for disallowance are tabulated in column J. The taxpayer was requested to indicate which of the expenses tabulated in the spread sheet related to his Telecommunication phone business, but he was not prepared to do so. It is evident from his evidence that the only expenses incurred by him in respect of this business were for fuel and electricity and the purchase of air time from M. It was thus really an easy task to establish from the spread sheet which amounts qualified for input tax.

[24] The taxpayer maintained his stance as set out in his objections and grounds of appeal and testified that SARS erred in accepting that he earned the income reflected in the documents relied upon. He stated that he was only entitled to 33% of the on sale of Telecommunication airtime to customers and not the full turnover relied upon by SARS. Furthermore there was no way that he could charge VAT from customers as the price charged was fixed by Telecommunication. SARS's stance is based on the provisions of the VAT Act to which we shall return. It claims that the taxpayer is liable for payment of output tax and entitled to deduct relevant input tax in respect of the Telecommunication phone business. However Mr Z conceded in his final argument that SARS was prepared to remit payment of output tax in this regard. This was actually conceded from the onset as indicated above.

[25] Ms B conceded that she received the letter from Mr C, the person who alleged that he had been appointed by the taxpayer to take over his bookkeeping and tax matters. She testified that she believed at the time that whatever needed to be rectified should be done from the period following the period applicable to her assessment. It is evident from her evidence that she never appreciated at the time that two different entities, the individual taxpayer and his CC, were involved and that their tax matters became entangled.

V APPLICABLE LEGISLATION

[26] The following definitions contained in the VAT Act apply in *casu:*

> "'Vendor' means any person who is required to be registered under this Act: provided that where the Commissioner has under section 23 or 50A determined the date from which a person is a vendor that person shall be deemed to be a vendor from that date."
>
> "'Services', means anything done or to be done, including the granting, assignment, cession or surrender of any right or the making available of any facility or advantage, but excluding a supply of good, money or any stamp, form or card contemplated in paragraph (c) of the definition of 'goods'".
>
> "'Supplier' in relation to any supply of goods or services, means the person supplying the goods or services."

Section 9(3)(b)(ii) of the VAT Act provides:

> "(3) Notwithstanding anything in subsection (1) or (2) of this section – (a)……;
> (b) where and to the extent that –
> (ii) goods or services supplied directly in the construction, repair, improvement, erection, manufacture, assembly or alteration of goods are supplied under any agreement or law which provides for the consideration for that supply to become due and payable in instalments or periodically in relation to the progressive nature of the work,
> those goods or services shall be deemed to be successively supplied, and each such successive supply shall be deemed to take place whenever any payment in respect of any supply becomes due, is received, or any invoice relating only to that payment is issued, whichever is the earliest."

[27] Section 64(1) of the VAT Act stipulates:

> "Any price charged by any vendor in respect of any taxable supply of goods or services shall for the purposes of this Act be deemed to include any tax payable in terms of section 7(1)(a) in respect of such supply; whether or not the vendor has included tax in such price."

[28] "Input tax" is defined in section 1 of the VAT Act. In relation to a vendor it is *inter alia* the tax charged under section 7 and payable in terms of that section by the supplier on the supply of goods or services made by that supplier to the vendor where the goods or services concerned are acquired by the vendor wholly for the purpose of consumption, use or supply in the course of making taxable supplies or, where the goods

or services are acquired by the vendor partly for such purpose, to the extent that the goods or services concerned are acquired by the vendor for such purpose. VAT levied on private expenses contrary to the above definition is excluded from VAT input claims.

[29] Tax invoices shall comply with the requirements of section 20(4) of the VAT Act. It is unnecessary to deal with these requirements.

[30] In terms of section 16(2) of the VAT Act an input tax deduction can only be allowed when a vendor is in possession of a tax invoice which complies with the requirements of section 20(4) of the VAT Act.

[31] Section 102(1) of the Tax Administration Act, 28 of 2011, deals with the burden of proof and stipulates as follows:

> "1) A taxpayer bears the burden of proving—
> (a) that an amount, transaction, event or item is exempt or otherwise not taxable;
> (b) that an amount or item is deductible or may be set-off;
> (c) the rate of tax applicable to a transaction, event, item or class of taxpayer;
> (d) that an amount qualifies as a reduction of tax payable;
> (e) that a valuation is correct; or
> (f) whether a 'decision' that is subject to objection and appeal under a tax Act, is incorrect."

VI RELIANCE ON LEGAL PRINCIPLES: RELEVANT AUTHORITIES

[32] In terms of section 129(2) of the Tax Administration Act the Tax Court may (a) confirm the assessment of SARS, (b) order the assessment to be altered or (c) refer the assessment back to SARS for further examination and assessment. The Tax Court is also entitled in terms of section 129(3) to reduce, confirm or increase an understatement penalty imposed by SARS.

[33] No court may close its eyes for established legal principles and a court may *mero motu* rely on such principles. See **Nedbank v Mendelow NO** 2013 (6) SA 130 (SCA) at paras [17] – [22]. If the facts to which the legal principles apply are squarely raised in the papers or in evidence, a court should not allow the continuation of a wrong because the legal representatives of the parties did not appreciate the correct legal principles. See **Cunningham v First Reddy Development 249** 2010 (5) 325 (SCA) para [29] and [30]; **Thompson v SABC** 2001 (3) SA 746 (SCA) para [7] and **Cusa v Tao Ying** Metal Industries 2009 (2) SA 204 (CC) at para [68] where the CC found as follows: "Where a point of law is apparent on the papers, but the common approach of the parties proceeds on a wrong perception of what the law is, a court is not only entitled, but in fact also obliged, *mero motu,* to raise the point of law and require the parties to deal therewith. Otherwise, the result would be a decision premised on an incorrect application of the law. That would infringe the principle of legality." See also **Meintjies NO v Coetzer** 2010 (5) SA 186 (SCA) para [15].

[34] The assessment relied upon by SARS is clearly incorrect relating to the output tax attributed to the taxpayer pertaining to income received from the Local Municipality and the Department. This was from the onset readily conceded by SARS' legal representative. On the other hand the taxpayer was also not entitled to claim input tax which had to be claimed by his CC if that CC was in fact registered as a vendor in terms of the VAT Act which is apparently not the case.

VII EVALUATION OF THE EVIDENCE AND FINAL CONCLUSIONS

[35] Although the taxpayer claimed to be at a disadvantage as he was not in possession of relevant invoices, vouchers and other supporting documents to show that his claim in respect of input tax was correct and should not be interfered with, we are of the view that, with reference to the documentation prepared by the taxpayer and supplemented by Ms B – the spread sheet referred to above - the taxpayer has not convinced us that any of those tax inputs which were initially accepted as correct based on the assumptions made by SARS, are indeed valid claims, save in respect of the supplier, M. We bear in mind that the burden of proof rests on the taxpayer.

[36] We are prepared to accept Ms B's calculations. She testified that the information was obtained from the taxpayer and from documentation such as bank statements supplied by him.

These documents were returned to him after the audit. The amount of R87 854,43 in column H was found to be the VAT amount that could be claimed validly, based on SARS' assumptions that the taxpayer incurred the expenses personally. This amount included the amount of R28 897,16 in respect of M. However as became apparent from the documentation and the evidence, the difference between the above amounts was regarded as input tax which the taxpayer could claim, but for the fact that he was not the contracting party in respect of the two construction contracts. Therefore he could not in his personal capacity claim the input tax in respect of expenses incurred relating to the two construction contracts. The total amount claimed in respect of input tax as calculated in the spread sheet is R135 272,50. This amount, excluding the amount of R28 897,16, is an invalid input. Consequently, R28 897,16 shall be deducted from the total input of R135 272,50 claimed to arrive at the correct amount payable by the taxpayer, to wit R106 375,34, being the total of invalid input claimed.

[37] In the light of the uncertainty, the lack of further detail and the taxpayer's version that SARS relied on his turnover figures in respect of the Telecommunication phone business, instead of 33% on turnover, being his income in the form of commission, Mr Z conceded that the claim in respect of output tax relating to this issue should be remitted. Therefore all output tax taken into consideration in the assessment has to be remitted.

[38] In conclusion the appeal should succeed, albeit partially. The assessment should be altered to reflect in addition input tax previously allowed in the total amount of R106 375,34, the effect being that this amount is due and payable by the taxpayer to SARS.

[39] In view of the history of this matter and the success obtained by the taxpayer, bearing in mind the wrong point of departure by SARS, we are of the view that penalties and interest charged for any period prior to this judgment should be remitted.

[40] Having considered all aspects and notwithstanding the taxpayer's partial success, we are of the opinion that this is a suitable case where each party should take responsibility for payment of his/its own costs.

VIII THE ORDERS

[41] Consequently we make the following orders:

1. The appeal succeeds partially;
2. The assessment of 21 May 2008 in respect of the tax period ending December 2007 is to be altered as follows:
   2.1 In remitting all VAT amounts claimed to be output tax not declared;
   2.2 By remitting all amounts relating to invalid input tax and substituting same with the amount of R106 375,34, being in respect of invalid input tax.
3. Each party shall pay his/its own costs.

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J. P. DAFFUE, J

I concur.

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J. LIEBENBERG (Assessor)

In concur.

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B. MATHIBELA (Assessor)

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