IN THE TAX COURT OF SOUTH AFRICA

(WESTERN CAPE DIVISION, CAPE TOWN)

CASE NO: 13935

In the matter between:

M FAMILY TRUST Appellant

and

THE COMMISSIONER FOR THE SOUTH AFRICAN REVENUE SERVICE Respondent

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JUDGMENT: 14 DECEMBER 2016

ALLIE, J:

1. This is an appeal against the decision of the Commissioner of the South African Revenue Service to assess the taxpayer to tax in the following manner:

   1.1 Assessed loss of R14 261 875,00 disregarded

   1.2 Alleged bad debt that arose from alleged embezzlement disregarded

   1.3 All other expenses disregarded because the trust is deemed not to carry on any trading.

   1.4 Understatement Penalty of 75% imposed because it was found that “no reasonable grounds for tax position” was taken.

2. The issues in dispute according to the respondent are:

   The capital losses claimed by Appellant for:

   2.1 The disposal of D Ltd shares held by the taxpayer;

   2.2 The alleged forfeiture of the options to acquire D Ltd shares;

2.3 The legal costs incurred by taxpayer in attempting to compel Mr JK to sign for the release to the taxpayer of the proceeds of received for the disposal of shares;

2.4 The understatement penalty of 25%;

2.5 The legal costs of this appeal.

The factual background

3. Prior to the assessment, M was a shareholder in a mining company, X Trading (Pty) Limited ("*X"*).

M held 50% of the issued shares in X.

During 2008, D Ltd (*"D")* (which was registered as an external company in South Africa) acquired a substantial shareholding in X, through its indirectly wholly-owned subsidiary H (Pty) Limited ("*H"*).

4. Consequently, during April 2008, a share sale agreement was concluded for the sale by shareholders of X (including M) of 74% of their share to H ("*share sale agreement"*). In terms of the share sale agreement –

4.1 H purchased from I and M (in equal shares) 74% of the shares in X.

4.2 The consideration payable to I and M was 26 million shares in D and 25 million options to acquire shares in D.

5. Consequently, the purchase price received by M as consideration for the sale by him of 37% of the shares which he held in X was:

   5.1. 13 million D shares; and

   5.2. 12,5 million options to purchase shares in D.

6. The share sale agreement also required D to procure that I, who held 50% of the 74% shares (i.e. 37%), in X and M who held the remaining 50%, be invited to become directors of both D and H.

7. The value of the transaction, independently reflected in the Annual Financial Statements of D as at 28 February 2009, insofar as it involved M was –

   7.1 in respect of the D shares, R7 627 984,00; and

   7.2 in respect of the D options, R2 750 666,00.

8. Subsequent to the share sale agreement, M (in his capacity as director of D) was issued with further shares in D. He testified that he received further shares of 250 000 and 43 452 on 30 September 2008 and July 2009 respectively.

9. On 30 November 2009, and as a result of a reverse takeover of D by WW Ltd. ("*W*"), the D shares held by the Trust, amounted to 16 152 142 (M, personally held 1 000 000 D Shares). In addition, the Trust held 12 100 000 D share options.

10. The Trust acquired its D Shares and D Options from M.

11. On 30 November 2009, M and the Trust concluded an oral agreement in terms of which the D shares and D options held by M were transferred to the Trust against a total consideration of R19 450 994,00. The Trust did not have the funds to pay for the D shares and D options which it so acquired from M and consequently the parties agreed that M would make a loan to the Trust in that amount.

12. The transaction was subsequently recorded in writing in a Loan Agreement which was concluded on 16 November 2012 with an effective date of 30 November 2009.

13. The amount of R19 450 994,00 was apportioned as follows:

    13.1 R10 965 156,00 in respect of the D shares; and

    13.2 R8 485 838,00 in respect of the D options.

14. On 10 August 2010, the Trust disposed of all of its shares in D (17 362 142) on the open market at Australian $ (A$) 0,12 per share. The prevailing exchange rate on that day was R6,60 per Australian Dollar. In the same transaction M disposed of his 1 000 000 D shares.

15. Consequently, the total consideration of A$2 160 252 must be apportioned as between M personally and the Trust. The apportionment is: 17 361 142 shares sold by the Trust and 1 000 000 sold by M.

16. Following this sale of D Shares, M resigned as a director of D.

17. The total proceeds from the sale of the D shares was transferred into an account held at the Dutch Bank International in the Netherlands ("*the Dutch Bank account"*). The Trust's portion thereof was A$2 042 605. In applying the R6,60 exchange rate, the SA Rand value is R13 481 19,00. The amount was received on behalf of both the Trust and M by the stockbroker, and on M's instruction was transferred to the Dutch Bank account.

18. The Dutch Bank account was held in the name of N Trading Ltd. There were two signatories to the Dutch Bank account, namely M and one Mr JK. Transfers from that account could only be made by both Mr JK and M signing the relevant documents. The account opening form for the Dutch Bank account also reflects that ownership of N Trading Ltd ("*N*") vested in Mr. JK and M. The documents illustrate that N was a corporate entity.

19. On the evidence, the amount of A$ 2 042 605 was transferred out of the Dutch Bank account allegedly, fraudulently without the consent of M. Those funds were meant to have been paid over to the Trust. Mr M testified that:

    19.1 He attempted to have the funds repatriated to South Africa into his personal bank account for the benefit of the Trust, but he was unsuccessful because he could not secure the signature of Mr JK.

    19.2 SARS obtained documentary evidence which was placed before the Court that through a signature purporting to be that of M, Dutch Bank

acting on a joint instruction did transferred the funds to the account of OP Jewellers based in the UAE.

20. M adduced evidence that he kept the funds temporarily in N Trading's account until D Ltd could obtain the requisite S.A Reserve Bank authorisation for him to bring it into the country. Respondent's counsel did not challenge him on this aspect.

21. The pending application with S.A. Reserve Bank is not reconcilable with an intention to conceal the funds from SARS.

22. On the evidence, it was clearly not M's intention that ownership of the funds would pass to N Trading as the Trust remained the beneficial owner and N Trading simply held it on behalf of the Trust.

23. Respondent alleged that the settlement agreement entered into between the taxpayer and various entities including Mr. V and his younger brother, Mr JK, all claims that the taxpayer had against the remaining parties were settled and extinguished upon the fulfilment of the terms of the settlement agreement.

24. Mr M alleged that he couldn't take further steps against the brothers because South African courts don't have jurisdiction over theft or fraud committed in the Netherlands. He stated further that he didn't have money available to pursue an appeal against the North Gauteng High Court's decision to dismiss his application to compel Mr JK to sign so that the funds in Dutch Bank could be

transferred to the taxpayer in South Africa because he alleged that he was involved in several legal disputes and cases that were instigated by Mr V.

25. In *State President of RSA v SARFU*[1] the court explained the procedure of cross examination as follows:

> "*The institution of cross-examination not only constitutes a right, it also imposes certain obligations. As a general rule it is essential, when it is intended to suggest that a witness is not speaking the truth on a particular point, to direct the witness's attention to the fact by questions put in cross-examination showing that the imputation is intended to be made and to afford the witness an opportunity, while still in the witness box, of giving any explanation open to the witness and of defending his or her character. If a point in dispute is left unchallenged in cross-examination, the party calling the witness is entitled to assume that the unchallenged witness's testimony is accepted as correct. This rule was enunciated by the House of Lords in Browne v Dunn and has been adopted and consistently followed by our courts."*

26. The court went on to elucidate the function of cross examination in the broader scheme of the conduct of a trial as follows:[2]

> *"The precise nature of the imputation should be made clear to the witness so that it can be met and destroyed,particularly where the imputation relies upon inferences to be drawn from other evidence in the proceedings. It should be made clear not only that the evidence is to be challenged but also how it is to be challenged.*[4][4] *This is so because the witness must be given an*

[1] President of the RSA v SARFU 2000(1) SA 1 (CC) at para 61
[2] SARFU *supra* at para 63

opportunity to deny the challenge, to call corroborative evidence, to qualify the evidence given by the witness or others and to explain contradictions on which reliance is to be placed."

27. Respondent's counsel failed to challenge the veracity of Mr M's allegation that the funds were embezzled nor did respondent adduce evidence that could gainsay the assertion that the funds were illegally transferred to an account over which the taxpayer had no control.

28. The settlement agreement's terms could be construed as being wide enough to encompass the illicit withdrawal of the funds in N Trading's account.

29. This court doesn't need to decide whether the embezzlement did in fact occur nor is it obliged to decide that the settlement agreement applied to the alleged embezzlement.

30. The issue of embezzlement may become the subject of a dispute in another forum and this court will not pronounce upon it at this stage.

31. A far more crucial decision has to be made concerning whether paragraph 35(3)(*c*) of the Eight Schedule to the Income Tax Act applies to the removal of the funds from the control of the taxpayer.

The Applicability of paragraph 35(3)(*c*) of the Eighth Schedule

32. Paragraph 35 provides as follows:

> *"Proceeds from disposal.—(1) Subject to subparagraphs (2), (3), and (4), the proceeds from the disposal of an asset by a person are equal to the amount received by or accrued to, or which is treated as having been received by, or accrued to or in favour of, that person in respect of that disposal, and includes—*
>
> *(a)…*
>
> *(b)…*
>
> *(3) The proceeds from the disposal, during a year of assessment, of an asset by a person, as contemplated in subparagraph (1) must be reduced by—*
>
> *(c) any reduction, as the result of the cancellation, termination or variation of an agreement or due to the prescription or waiver of a claim or release from an obligation or any other event during that year, of an accrued amount forming part of the proceeds of that disposal."*

33. Unlike paragraph 35(1) which refers specifically to money "*received or accrued to,*" a plain reading of paragraph 35(3) reveals that it applies to money that accrued to the taxpayer.

34. Accordingly, it must be inferred that the legislature intended to exclude from the ambit of paragraph 35(3), money that was "*received*" and not accrued.

35. The agreement in terms of which the taxpayer disposed of the shares it held in D Ltd on 10 August 2010 was a sales agreement. The shares were disposed of

on the stock exchange and their price was paid in full and received on behalf of the taxpayer by its stockbrokers.

36. On 7 October 2010 the proceeds were paid into a bank account held in the name of N Trading Ltd.

37. On 21 October 2010 the taxpayer attempted to transfer the monies from the N Trading Ltd bank account held at Dutch Bank, Amsterdam, Netherlands to Mr Q. The bank in Amsterdam refused to effect the transfer, as it required both the signatures of the signatories to the bank account.

38. On 7 December 2010 the money was transferred from the N Trading Ltd account at the bank in Amsterdam, Netherlands to OP Jewellers in Emirates UAE.

39. Mr M's testimony is that he consider the funds to have been received by the stockbroker on behalf of the Trust.

40. In *casu*, it is therefore common cause that the Trust received payment and arranged for it to be held by N Trading temporarily. The funds had accordingly gone beyond mere accrual.

41. Accordingly, section 35(3)(*c*) can't apply to the transaction.

42. In the course of giving meaning to words, a purposive approach[3] is the favoured method used in interpretation of documents, including legislation. In the context of this case, more specifically to give the correct meaning to the words in the Act: "*or any other event during that year*".

43. In *Endumeni Municipality's case***,** the Supreme Court of Appeal confirmed the approach to be adopted in interpretation as follows:

> *"[18] Over the last century there have been significant developments in the law relating to the interpretation of documents, both in this country and in others that follow similar rules to our own. It is unnecessary to add unduly to the burden of annotations by trawling through the case law on the construction of documents in order to trace those developments. The relevant authorities are collected and summarised in Bastian Financial Services (Pty) Ltd v General Hendrik Schoeman Primary School. The present state of the law can be expressed as follows. Interpretation is the process of attributing meaning to the words used in a document, be it legislation, some other statutory instrument, or contract, having regard to the context provided by reading the particular provision or provisions in the light of the document as a whole and the circumstances attendant upon its coming into existence. Whatever the nature of the document, consideration must be given to the language used in the light of the ordinary rules of grammar and syntax; the context in which the provision appears; the apparent purpose to which it is directed and the material known to those responsible for its production. Where more than one meaning is possible each possibility must be weighed in the light of all these factors. The process is objective not subjective. A*

[3] Natal Joint Municipal Pension Fund v Endumeni Municipality 2012 (4) SA 593 (SCA) at para 18; Bothma-Batho Transport 9Edmd) Bpk v S Botha & Seun Transport 9Edms) Bpk 2014 (2) SA 494 (SCA) at para 12

> *sensible meaning is to be preferred to one that leads to insensible or unbusinesslike results or undermines the apparent purpose of the document. Judges must be alert to, and guard against, the temptation to substitute what they regard as reasonable, sensible or businesslike for the words actually used. To do so in regard to a statute or statutory instrument is to cross the divide between interpretation and legislation. In a contractual context it is to make a contract for the parties other than the one they in fact made.* ***The 'inevitable point of departure is the language of the provision itself', read in context and having regard to the purpose of the provision*** *and the background to the preparation and production of the document*."

(My emphasis.)

44. In IT case no. 1880[4] a narrow interpretation was given to the words: *"or any other event*" by finding that the words were meant to denote similar categories as those expressed by the preceding words in the paragraph.

45. Appellant's counsel sought to distinguish the current case from case no 1880 on the basis that case no 1880 involved an unrelated damages claim against the taxpayer. *In casu*, the taxpayer is also seeking to deduct a loss sustained by the alleged misconduct of a person completely unrelated to the agreements to sell the shares. I am not convinced that the facts cause the two cases to be distinguishable from one another.

46. Although appellant's counsel argued that the words would be tautologous if the *eiusdem generis* rule were to be applied to them, it is not for a court to identify

[4] 78 SATC 103

possible scenarios where the words would find application. Having regard to the context in which the words are used and their clear purpose, it is sufficient to establish that the words apply to situations where the purchaser of an asset is partially or wholly released from the obligation to pay for the asset disposed of. Ultimately, the words were not intended to apply to an embezzlement of the nature alleged in this case, for the reasons stated herein.

47. The set–off or deduction contemplated is one which flows as a consequence of extinguishing the taxpayer's right to receive payment and the payee's obligation to pay.

48. The relevant *nexus* is to the event that causes such extinguishing not to a subsequent unrelated event caused by a person who held no obligation to pay for the asset disposed of and who acted outside the agreement to dispose of the asset.

49. The *nexus* cannot be a broad and vague one between the accrual and the deduction's event, irrespective of how remotely it is connected to the failure to actually retain/receive the funds.

50. If the legislature intended a deduction to be available for any unrelated reason, that would have the consequence of a reduced payment, it would have expressed itself in words conveying that meaning.

51. The purpose of paragraph 35(3) is to provide relief in the form of a deduction from the proceeds of a disposal of an asset in certain circumscribed instances

where the proceeds had as yet not been paid but had already accrued to the taxpayer and where provision for payment of the funds are varied, extinguished, waived or cancelled.

52. In summary, the alleged fraud and embezzlement that caused the funds to be removed from the control and beneficial use of the taxpayer is an event that is not covered by paragraph 35(3)(*c*) of the Eighth Schedule for the following reasons:

    52.1 The funds were already received by the taxpayer and didn't accrue to it and accordingly didn't fall within the protection provided by paragraph 35(3);

    52.2 The alleged embezzlement was committed by a party that was unrelated to the transaction for the disposal of the shares.

53. The appellant cannot claim the amount of the alleged embezzlement as a deduction in terms of paragraph 35(3)(*c*).

Should the cost of 12,100,000 share options that was converted into 1,210,000 shares be included in the base cost of the D Ltd shares or alternatively be allowed as a capital loss?

54. Although the Appellant's tax practitioner stated that only 1,210,000 share options were converted into 1,210,000 shares and therefore he wanted to claim a capital loss for the forfeiture of the remaining share options, Mr M testified that he and his accountant laboured under the misapprehension that the

options were converted to shares on a 1:1 ratio and that he had forfeited some options when he resigned as a director of D. He only recently found documents on the internet that shows that 12,100,000 share options were converted to 1,210,000 shares. The Appellant accordingly now seeks to include the cost of the 12,100,000 share options in the total capital loss that the Appellant sustained.

55. Appellant's counsel contended that the correct calculation of the capital loss consequent upon the conversion is as follows:

55.1 D shares and options were purchased for a total price of R19 450 994.00;

55.2 17 362 142 D shares were disposed of and an amount of A$ 2 042 605 accrued to the Trust. The South African rand exchange of R6,60 to 1 A$ results in the amount accrued being equal to R13 483 235,00.

55.3 When the R13 483 235,00 is deducted from the R19 450 994,00 acquisition cost then there is a capital loss of R5 967 759,00.

56. It was further contended that the capital loss would have remained the same on the Trust's initially misunderstood calculation of the conversion of options to shares and there would have been no advantage to the Trust to have deliberately misrepresented the conversion calculation.

57. Paragraph 20(1)(*c*)(ix) of the Eighth Schedule states that the base cost of an asset acquired by a person is the sum of —

> *"the following amounts actually incurred as expenditure directly related to the acquisition or disposal of that asset, namely—*
>
> (ix) *if that asset was acquired or disposed of by the exercise of an option (other than the exercise of an option contemplated in item (f)), the expenditure actually incurred in respect of the acquisition of the option."*

58. On Respondent's behalf it was argued that there was a cancellation of shares and that Paragraph 18 of the Eighth Schedule applies.

59. Paragraph 18 provides as follows:

> "(1) *Where a person who is entitled to exercise an option—*
>
> *(a) to acquire an asset not intended for use wholly and exclusively for business purposes; or*
>
> *(b) …*
>
> *has abandoned that option, allowed that option to expire, or in any other manner disposed of that option other than by way of the exercise thereof, any capital loss of that person determined in respect of that expiry shall be disregarded*."

60. As the documentary evidence provided by both the Appellant and the Respondent and the testimony of the Appellant demonstrate that there was a conversion of 12,100,000 share options to 1,210,000 shares in a 10:1 ratio, it is

patently clear that paragraph 20 rather than paragraph 18 of the Eighth Schedule finds application.

61. In our view, the cost of 12,100,000 share options should therefore be included in the base cost of the D Ltd shares that were disposed of.

Does an Understatement Penalty Find Application and if, so in which category does the Appellant's alleged failure to declare fall?

62. SARS assessed the Appellant with an understatement penalty of 75% on the basis of "*no reasonable grounds for tax position taken*".

63. Respondent, now seeks an understatement penalty of 150% on the basis of "*intentional tax evasion*" without having initially raised it in its Notice of Assessment and Statement of Grounds of Assessment.

64. A trial by ambush cannot be countenanced and SARS is not entitled to increase its claim for understatement penalty without due notice.

65. Sections 221 to 223 of the Tax Administration Act 28 of 2011 defines the circumstances which justify the imposition of an understatement penalty as follows:

> *"**UNDERSTATEMENT PENALTY (ss 221-233)***
>
> ***Imposition of understatement penalty** (ss 221-224)*
>
> ***221. Definitions.**—In this Chapter, unless the context indicates otherwise, the following terms, if in single quotation marks, have the following meanings:*
>
> ***'repeat case'** means a second or further case of any of the behaviours listed under items (i) to (v) of the understatement penalty percentage table reflected in section 223 within five years of the previous case;*
>
> ***'substantial understatement'** means a case where the prejudice to SARS or the fiscus exceeds the greater of five per cent of the amount of 'tax' properly chargeable or refundable under a tax Act for the relevant tax period, or R1 000 000;*
>
> ***'tax'** means tax as defined in section 1, excluding a penalty and interest;*
>
> ***'tax position'** means an assumption underlying one or more aspects of a tax return, including whether or not—*
>
> *(a) an amount, transaction, event or item is taxable;*
>
> *(b) an amount or item is deductible or may be set-off;*
>
> *(c) a lower rate of tax than the maximum applicable to that class of taxpayer, transaction, event or item applies; or*
>
> *(d) an amount qualifies as a reduction of tax payable; and*
>
> ***'understatement'** means any prejudice to SARS or the fiscus as a result of—*
>
> *(a) a default in rendering a return;*
>
> *(b) an omission from a return;*

(c) an incorrect statement in a return; or

(d) if no return is required, the failure to pay the correct amount of ‘tax’.

222. Understatement penalty.—*(1) In the event of an 'understatement' by a taxpayer, the taxpayer must pay, in addition to the 'tax' payable for the relevant tax period, the understatement penalty determined under subsection (2) unless the 'understatement' results from a bona fide inadvertent error.*

(2) The understatement penalty is the amount resulting from applying the highest applicable understatement penalty percentage in accordance with the table in section 223 to each shortfall determined under subsections (3) and (4) in relation to each understatement in a return.

(3) The shortfall is the sum of—

(a) the difference between the amount of 'tax' properly chargeable for the tax period and the amount of 'tax' that would have been chargeable for the tax period if the 'understatement' were accepted;

(b) the difference between the amount properly refundable for the tax period and the amount that would have been refundable if the ‘understatement’ were accepted; and

(c) the difference between the amount of an assessed loss or any other benefit to the taxpayer properly carried forward from the tax period to a succeeding tax period and the amount that would have been carried forward if the 'understatement' were accepted, multiplied by the tax rate determined under sub section (5).

(4) If there is a difference under both paragraphs (a) and (b) of sub section (3), the shortfall must be reduced by the amount of any duplication between the paragraphs.

(5) The tax rate applicable to the shortfall determined under subsections (3) and (4) is the maximum tax rate applicable to the taxpayer, ignoring an assessed loss or any other benefit brought forward from a preceding tax period to the tax period.

223 Understatement penalty percentage table.—

(1) …

(2) An understatement penalty for which provision is made under this Chapter is also chargeable in cases where—

(a) an assessment based on an estimation under section 95 is made; or

(b) an assessment agreed upon with the taxpayer under section 95(3) is issued.

(3) SARS must remit a 'penalty' imposed for a 'substantial understatement' if SARS is satisfied that the taxpayer—

(a) made full disclosure of the arrangement, as defined in section 34, that gave rise to the prejudice to SARS or the fiscus by no later than the date that the relevant return was due; and

(b) was in possession of an opinion by an independent registered tax practitioner that—

(i) was issued by no later than the date that the relevant return was due;

(ii) was based upon full disclosure of the specific facts and circumstances of the arrangement and, in the case of any opinion regarding the applicability of the substance over form doctrine or the anti-avoidance provisions of a tax Act, this requirement cannot be met unless the taxpayer is able to demonstrate that all of the steps in or parts of the arrangement were fully disclosed to the tax

practitioner, whether or not the taxpayer was a direct party to the steps or parts in question; and

(iii) confirmed that the taxpayer's position is more likely than not to be upheld if the matter proceeds to court."

66. There is a discernible prejudice to the *fiscus* in the following respects:

66.1 by including the total amount of the alleged embezzlement as a bad debt, the taxpayer, incorrectly defined and overstated the loss it allegedly incurred without considering the applicability of paragraph 35(3)(*c*).

66.2 by stating that the options were forfeited in its tax return, the taxpayer created the impression that the capital loss that was suffered on the forfeiture of the share options was larger.

67. Mr M testified that it was never his intention to evade taxation, and that he at the time was involved with a number of business interests and litigation against him and his businesses. This had caused certain tax and Reserve Bank matters not to be up to date.

68. Mr M also testified that he has limited financial and tax knowledge and that he relied on his accountant.

69. His accountant confirmed that when the tax returns were submitted there were time constraints and that he was under a lot of pressure. These factors resulted in certain errors being made on the tax returns. His accountant testified very

candidly that the bad debts were incorrectly claimed on the tax return in error when he replied to SARS' audit findings.

70. The accountant testified that the returns, were submitted on the best information available at the time. When he submitted the returns, he hoped for the best.

71. The tax practitioner made an error in the way he apportioned the share options to a conversion into shares.

72. The tax practitioner made a further error in claiming the alleged embezzled funds as a bad debt.

73. A taxpayer cannot disavow himself/herself of tax responsibilities by relying on an accountant or tax practitioner as the tax practitioner is only obliged declare information on tax returns as provided by the taxpayer.

74. In my view, respondent's counsel didn't vigorously challenge Mr R, the tax practitioner's *bona fides* concerning what he entered on the tax return. Neither did he put it to Mr M that he deliberately gave incorrect information to the tax practitioner with a view to evading tax. The credibility of Messrs M and R was not impugned during cross examination, specifically in relation to their disavowal of an attempt to deliberately conceal the true tax position of the taxpayer.

75. I conclude therefore, that there was no intentional tax evasion in the manner in which the 2011 return was completed.

76. I am however convinced that the taxpayer failed to take reasonable care in having the returns completed and submitted and it is therefore liable for understatement penalty.

77. Consequently, an understatement penalty of 50% should, in my view, apply.

Considerations for a cost order against the Appellant.

78. In terms of section 130 of the Tax Administration Act, the Tax Court may, in dealing with an appeal, on application by an aggrieved party, grant an order for costs if:

> *"The appellant's grounds of appeal are held to be unreasonable".*

79. Respondent's counsel argued that the Appellant's grounds of appeal are unreasonable for the following reasons:

    79.1 The taxpayer deliberately contended that the share options were forfeited when M resigned as director of D Ltd, whilst the options were in fact converted to shares, as set out above.

    79.2 The evidence demonstrates that the contention that the proceeds from the disposal of the D shares were embezzled or stolen is factually incorrect. The settlement agreement entered into by *inter alia* the taxpayer and Mr JK had the effect that if any money was in fact embezzled, it was recovered in terms of the settlement agreement.

79.3 The contention that the funds received from disposing of the D shares were embezzled and that constitutes “any other event” as envisaged in section 35(3)(*c*), is without any merit and unreasonable. The proceeds from the sale of the D shares were in fact, on the taxpayer’s own admission, received by its stockbrokers, kept by the stockbrokers for two months and then transferred to a bank account in the Netherlands, which was nominated by the taxpayer.

80. The accountant, in his response to the audit findings, requested that SARS make available to appellant documentation that it had acquired through the co-operation of D Ltd concerning the 10:1 conversion of the D Ltd shares. He also requested a meeting to clear up this dispute. SARS failed to respond to this request. In view of how quickly appellant made concessions concerning the erroneous claim of a bad debt and the correct amount of share options that were converted to shares, a substantial part of this court case could have been avoided, thereby narrowing the issues at an earlier stage and considerable costs and time could have been saved.

81. Paragraph 35(3)(*c*) is widely and vaguely constructed and stands to be interpreted more broadly by a litigant before a court has pronounced on its interpretation in the context of the facts of this case. I am unable to conclude that the Appellant ought to have known that its objection would not fall within the ambit of paragraph 35(3)(*c*).

82. The appellant has been partially successful in as much as the exchange rate that it contended applied to the shares disposed is upheld, the share valuation that it contends ought to have applied to the reverse takeover will apply, the cost of the 12,100,000 share options will be included in the calculation of the base cost of the shares disposed of and the grading of its conduct when completing the tax return will now be altered, thereby reducing the amount of the understatement penalty.

83. I am not persuaded that appellant had no reasonable grounds for its objection in its entirety.

84. I make no cost order.

IT IS ORDERED THAT:

1. The assessment is referred back to SARS, in terms of section 129(2), for reassessment, and SARS shall take into consideration the following:

    1.1 The proceeds from the sale of the D Ltd shares shall not be reduced by any amount relating to any possible embezzled funds as the proceeds have been received by the tax payer.

    1.2 The cost of the 12,100,000 share options converted into 1,210,000 D Ltd shares shall be included in the base cost of the shares disposed of.

    1.3 Legal cost of R427 538, 00 incurred by the taxpayer in litigation to recover the funds, shall be excluded from the base cost of the shares, bearing in mind that the Appellant abandoned reliance on

those costs.

2. The foreign exchange conversion of the shares disposed of shall be in accordance with the exchange rates relied on by the Appellant in its calculations on the papers.

3. The share valuation for the reverse take-over shall be calculated in compliance with the Appellant's calculations set out in the papers.

4. An understatement penalty of 50% shall apply.

5. No costs order is made.

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R. ALLIE