REPUBLIC OF SOUTH AFRICA

IN THE TAX COURT OF SOUTH AFRICA
HELD AT JOHANNESBURG

(1) REPORTABLE: YES / NO
(2) OF INTEREST TO OTHER JUDGES: YES/NO
(3) REVISED.

…………………….. ………………………..
DATE SIGNATURE

CASE NO: 13686

ABC TRADING (PTY) LTD **APPELLANT**

and

THE COMMISSIONER, SOUTH AFRICAN REVENUE SERVICE **RESPONDENT**

J U D G M E N T

CORUM: SUTHERLAND J, WITH KRAUSE et HARTZENBURG, Assessors

INTRODUCTION

[1] The crisp question that arises in this appeal is whether or not the appellant taxpayer is eligible to deduct its capital expenditure in terms of section 15(1)(*a*) of the Income Tax Act 58 of 1962 (the Act) on the grounds that its income is 'derived from mining operations'.[1] CSARS disallowed deductions for the FY 08, 09, 10 and 11, and imposed interest on the unpaid tax in terms of section 89*quat*(2) of the Act and penalty charges on the premise of understatements of income as contemplated in sections 222 and 223 of the Tax Administration Act 28 of 2011 (TAA). The propriety of these impositions is also in dispute.

[2] The nub of the controversy relates to the business model of the taxpayer. It carries on business as a 'contract miner'. The pertinent generic characteristics of a contract miner are these:

2.1. It has the skilled personnel and technological capacity to extract material from the Earth through open cast mining techniques.

2.2. It concludes agreements, as an independent contractor, with other persons, typically mining right holders, to extract material from the Earth for reward payable to it by the mining right holder.

2.3. The remuneration earned for such activity is paid by the mining right holder in several ways, including a fixed regular fee, a fixed rate for

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[1] Section 15 of the Act provides:

Deductions from income derived from mining operations.—There shall be allowed to be deducted from the income derived by the taxpayer from mining operations—

(*a*) an amount to be ascertained under the provisions of section 36, *in lieu* of the allowances in sections 11(*e*), (*f*), (*g*A), (*g*C), (*o*), 12D, 12DA, 12F and 13*quin*;

[Para. (*a*) substituted by s. 20 of Act 55 of 1966, by s. 18 of Act 129 of 1991, by s. 24 of Act 31 of 2005 and by s. 29 of Act 35 of 2007.]

volume of material extracted, and a fixed rate by weight of the material extracted, including the identifiable mineral, the pursuit of which is *the raison d'etre* of the entire enterprise of the mining right holder.

2.4. Payment falls due upon delivery, in a prescribed form, of the mineral or the ore bearing the mineral to the mining right holder. Depending on the mineral being mined, the delivered ore may require further refinement prior to sale or, as in the case of coal, is at once capable of being sold.

2.5. In addition, in respect of the ancillary activities such as 'site establishment' to set up the work- process a fixed fee is payable and in respect of rehabilitation of the pit, a fixed fee is payable.

2.6. It purchases and owns all the equipment required to meet its contractual obligations to the mining right holder and bears the full cost of maintenance thereof itself.

2.7. When one pit is exhausted, the contractor moves on with all of its equipment to the next pit and works that pit for the same client or moves on to the next client. It may be operational on many pits contemporaneously and might move its equipment around as the need arises from one pit to another and from one client to another and back again.

2.8. It is never the owner of the land upon which the pit is located, nor the holder of the mining right, nor is it involved in any way in the marketing and sale of the minerals extracted by its efforts.

2.9. The agreement with the client typically reserves to the mining right holder the right to suspend, or contract the scale of, operations to take account of

market demand for the mineral. This category of risk is, thus, one shared by both contracting parties.

[3] The essential view articulated by CSARS is that the income of such a taxpayer is derived from 'services rendered' to its client, the mining right holder, and is not income derived from 'mining operations' as defined. Insofar as the taxpayer indeed physically extracts ore and minerals from the Earth, and, in this sense, is engaged in 'mining', CSARS is content to recognise that some of the taxpayer's activities could, in a limited sense, 'be regarded' as being engaged in part of the mining operations, but even that modest concession[2] is not really important. The reason for that is because the true locus of the controversy is whether the income derived by the taxpayer from payments made to it by the mining right holder can, upon a proper interpretation of section 15, which has to be read with section 36 of the Act, be understood to be 'income derived from mining operations,' even if it is so that, in ordinary parlance, such a taxpayer is, somehow or other, perceived as being implicated in 'mining operations'. Moreover, CSARS emphasises that what, in its view, needs to be established is that a taxpayer who is properly eligible for the section 15 benefit, must be able show a direct connection to mining operations as the source of its income and in that context, the question of whether or not such a taxpayer undertakes any commercial risks is pertinent.

[4] It is well established that, in law, that mere extraction of a mineral from its natural state does not result in the production of income[3] even though self-evidently,

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[2] Made in the audit letter of 9 November 2012. [bundle 42] see paras 8-11.

[3] ITC 1572 56 SATC 175.

expenditure, including capital expenditure must have been incurred to achieve that result. What is required is an engagement in the 'trade' of mining.[4] This trade, typically, would include the selling of the minerals so extracted, with the logical risks attendant on such a business. In this context, it is CSARS's perspective is that the inter-positioning of an external contractor to extract minerals for a mining right holder against a fixed rate of pay, breaks the critical 'connection' between the fee disbursed to the contractor and the 'mining' source of that income. The mining right holder, having got a contractor to perform the actual extraction of material for it, is more properly to be regarded as the person or entity engaged in mining operations, and the contractor is, in law, too remote from the income derived from the mining operations, (i.e. the income the mining right holder receives from the sale of the minerals and with which it is enabled to pay the contractor) to be able to say that the contractor's income, i.e. the payment from the mining right holder, is derived from 'mining operations' as defined.

[5] There is no point is denying the paradox inherent in this perspective: it means that, in law, the person who actually digs the stuff out of the ground is more remote from the source of the income derived from his physical efforts than the client, who is never physically present at the pit, yet the latter derives its income from mining operations, but the person who actually dug it out of the ground does not.

[6] The issue at stake in these proceedings is whether a proper interpretation of the legislation supports this view.

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[4] *Western Platinum Ltd v CSARS* [2004] 4 All SA 611 at [6].

THE TAXPAYER'S BUSINESS MODEL

[7] The evidence adduced, and the undisputed facts alleged in the taxpayer's appeal grounds shows that the taxpayer's activities fall squarely into the generic concept of a 'contract miner' model. It is common cause that the taxpayer's work activities and remuneration structure are thus:

7.1. The work undertaken included:

7.1.1. Dewatering of opencast pits by means of pumping water to a suitable approved area;

7.1.2. Blasting of rocks, excavation and transportation of topsoil, parting and overburden;

7.1.3. Separate blasting and removal of different categories of chromitite and chromite ore to prevent contamination;

7.1.4. Separate delivery and stockpiling of different categories of chromitite and chromite ore to prevent contamination;

7.1.5. Crushing and screening of ore into three different size fractions to facilitate the next process of mineral extraction; liability and risk of the imposition of a penalty was imposed upon the taxpayer in the event the delivered product failed to meet a prescribed 'clean' threshold; i.e. too much ore and not enough mineral.

7.1.6. Constructions and maintenance of roads and access roads;

7.1.7. Rehabilitation of mined out areas during and immediately after completion of operations;

7.1.8. Site establishment and disestablishment in the district in which operations were conducted;

7.1.9. Operation and maintenance of a quartz mine, crushing and screening plant as well as maintenance of access roads and surfaces;

7.1.10. Extraction of chromite ore, not for the taxpayer's own account, but on behalf of and for the benefit of the taxpayer's client in whom the ownership of the chromite ore vested throughout.

7.2. The fees earned by the taxpayer for the services rendered to its clients were calculated to include:

7.2.1. Fixed monthly fee;

7.2.2. Site disestablishment fee at a rate per site;

7.2.3. Removal of overburden fee at a rate per cubic metre;

7.2.4. Removal of waste fee at a rate per cubic metre;

7.2.5. Extraction and delivery of ore fee at a rate per cubic metre;

7.2.6. Crushing and screening of ore fee at a rate per ton;

7.2.7. Rehabilitation – filling of final void fee at a rate per cubic metre;

7.2.8. Rehabilitation, backfill, topsoil and planting at a rate per square metre.

[8] Furthermore, these features were present:

8.1. In terms of some of the agreements with mining right holders, the taxpayer used the electricity and diesel provided by its clients.

8.2. The Taxpayer did not hold any mining license in respect of the mining areas on which it performed the services.

8.3. The mining right holders, and not the taxpayer, were responsible for working the ore to extract chrome after taking delivery of the product from the taxpayer.

8.4. The mining right holders operated their smelter to extract chromium to produce ferrochrome.

8.5. The taxpayer extracted the raw ore (in a condition where chromium is unseparated from the host rock). At the stage of extraction and stockpiling by the taxpayer the chromium is not isolated (won) from the soil or host rock. The taxpayer is never involved in the process of separation of final separation of the mineral from the host rock.

8.6. The mining right holders derived their income from the sale of ferrochrome and chrome alloy extracted from the ore, which includes some of the ore delivered by the taxpayer.

[9] The fact that the taxpayer indeed expended the sums declared on capital expenditure in the several fiscal years is common cause.

THE MEANING OF 'MINING OPERATIONS'

[10] The phrase 'mining operations is defined broadly. Section 1 of the Act provides:

> mining operations' and 'mining' include every method or process by which any mineral is won from the soil or from any substance or constituent thereof… .

[11] This text is a term of art. First, the quaint, and pleasingly anachronistic, phrase 'won from the soil' has been the subject of much of the judicial interpretation. There are two main themes in the case law on its interpretation; first, a gloss on what it means to 'win' minerals and secondly, the need to be involved in the

'trade' of mining which incorporates the unavoidable 'commercial' dimension of dealing in minerals after having been 'won'.

[12] It seems to me that care must be taken not to select only the first part of phrase; i.e. 'won from the soil' for scrutiny.[5] To do so would be to overlook the disjunctive dimension of the whole phrase '….*won from the soil OR from any substance of constituent thereof…*' This construction, in my view, articulates the notion of two distinct, albeit related 'operations' and perhaps, at the level of pedantry, even three distinct potential 'operations' all of which singly or collectively, must be related to the verb 'won from'. 'Won from the soil' suggests that the operations to dig out the earth beneath our feet is contemplated. Won from 'any substance' and won from a 'constituent' of soil suggests the inclusion of processes that might be quite distinct and physically separate from the actual digging of stuff out of the ground, but nevertheless remain 'mining operations'. The obvious examples are smelting or any other process of refinement, aimed at getting at the metal, carried out in plants or laboratories not necessarily anywhere near to a pit or ore stockpile.

[13] These distinctions in the text, *could*, on grammatical grounds, lend support for the proposition that a person who is not engaged in the *whole chain* of possible mining operations from sinking the shaft or digging the pit to the ultimate disposal of the mineral for commercial gain, is nevertheless still engaged in 'mining operations' albeit only a *part of that chain* of operations. Similarly, it can be posited that a person engaged only in the highly technical refinement processes

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[5] See: *Natal Joint Municipal Pension Fund v Endumeni Municipality* 2012 (4) SA 313 (SCA) at [18]–[19] where the holistic approach to statutory interpretation is exhorted.

is involved in a 'mining operation', or indeed, the person who, clad in suit and tie, who sells the minerals but who has never trod upon a sod, in this sense, is engaged in a 'part' of 'mining operations'.

[14] Over and above those considerations, the whole text contains more than this phrase and the impact of another phrase '….include *every* method or process by which ….' needs also to be assessed. Why is the term 'every' and not 'any' used? If the notion that a person might only need to be engaged in a 'part' of 'mining operations' to fall into the defined category requires interrogation, then the purpose of phrase '*every* method or process' must be discerned and reconciled with that proposition. It seems to me that the choice of the term 'every', in this context, is not compatible with a notion of segmented eligibility. Moreover, although this term is not the focus of any of the authorities, a traverse of the cases reveals a rejection of the idea that a taxpayer can fall into the defined category by reason of an 'involvement' in a 'part' of 'mining operations'.

[15] In *Union Government v Nourse Mines 1912 TPD 924* it was held (in relation to a text not identical to the current definition of 'mining operations') at 930 -931:

> What does the Act mean when it speaks of the cost of winning the gold? Does it mean *prima facie* the cost incurred in reaching the ore and then putting it in such condition that it may be worked continuously in the ordinary way, or does it mean *prima facie* the cost incurred in mining and in converting the ore into the metal gold?
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> In the case of *Lewis v Fothergill* (5 Ch. 106), in a mining lease providing for a royalty on every ton of coal won and worked, to win the coal was considered to mean to place the coal in such a position that it could be worked continuously in

> the ordinary way. I do not think, however, that this is what the Legislature intended when it said that the working expenditure of winning the gold should be deducted from the revenue. It never was the intention of the Legislature that the cost of stoping, tramming and hauling, for instance, should be excluded. The ordinary meaning of the words "to win gold" is to obtain or get the gold in the form of metal. To win gold includes all the operations necessary, not only to reach and extract the ore, but also to convert it into metal. There is no reason why we should give to winning gold the technical meaning given to winning coal in *Lewis v Fothergill*. It might be different if the Legislature had spoken of winning ore. Nor does the fact that the word "treating" is used in addition to "winning" make any difference, because the words are manifestly used merely to supplement each other's meaning, and "treating" is not here used in contradistinction to "winning." This seems quite clear from the fact that the word "treating" is omitted in sec. 4, sub-sec. 1, where the word "winning" must include "treating," for we cannot suppose that the Legislature intended different operations, seeing that the profits depend upon the working expenditure of sec. 4, sub-sec. 3. All expenditure, therefore, connected with winning the ore, treating the ore and winning the gold from the ore after treatment until the gold is in a position to be disposed of seems to have been included by the Legislature under the category of working expenditure, unless expressly placed under the head of capital expenditure."

(Underlining supplied)

[16] The recognition that the idea of 'mining' implicates more than one process is critical. 'Mining' means the efforts to reach, to extract and to access metal in turn, and is thus what 'winning' the mineral is about. The notion of 'winning' was again addressed in *ITC 1455 (1988) 51 SATC 111 (T)*. After considering whether

different kinds of minerals might be 'won' differently, it was held that 'winning' should be understood to mean the 'isolation' of the mineral that is already present in the ground. (By contrast, some metals which do not exist in nature are 'produced' after applying a chemical process or other process such as heating or mixing one mineral with another; eg iron, the 'production' of which, it was held, for that reason, fell outside of 'mining'.)

[17] Notably, the Court in *Nourse Mines* approached the enquiry by addressing the *cost* of undertaking the enterprise rather than the mere physical activity, and stressed the complexity of 'operations' needed to 'win' the mineral in the sense that term was employed. The paramountcy of this perspective was made plain in *ITC 1572 56 SATC 175*. In that case, it was stated:

> I am in agreement with Mr *Du Plooy's* proposition to the effect that the mere physical act of extracting minerals considered apart from the other steps necessary to bring income into existence, is, to use his phrase, 'a barren act that is not in itself capable of being an income source'. That physical act cannot, so it was argued, be what is contemplated by the legislature when it uses the words 'mining' or 'mining operations'. I accordingly agree with the submission that when the Act refers to 'income derived from mining/mining operations', this is a reference to income derived from a business of mining and not merely a physical act.
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> It is also true that although 'trade' is defined in s 1 of the Act so as to include a business, that there is no definition in the Act of what a business is. In this regard, some assistance is to be obtained from the following remarks of Sweet DJ in the Canadian case of *Falconbridge Nikkel Mines v MNR* 72 DTC 6337(FCA) at 6341:

> ‘The operation of the mine within the meaning of the relevant legislation can only mean the conducting of a viable, practical undertaking for that purpose. For this it is necessarily, and I would think obviously, required that there be an organisation, a business enterprise, so structured and set up that the multiplicity of requirements to that end will be available. The extracting of the ore, the conversion of it into metal and the sale are parts, and important parts, but only parts, of those requirements. For realistic achievement of the result to be accomplished, and accomplished in a practical and effective sense, they must be supported and accompanied by other activities. It is the totality of that organization, of that enterprise and the totality of the conduct of the business which is “the operation of a mine” within the meaning of the legislation.

(Underlining supplied)

[18] Plainly, it seems that to be a ‘digger’ is not enough to be a ‘miner,’ in the sense contemplated by these authorities.

[19] The decision in *Western Platinum Ltd v CSARS [2004] 4 All SA 611*addressed the question thus at [6], where Conradie JA held:

> [6] Mining operations by themselves cannot produce income. However, the definition of 'mining' and 'mining operations', being context dependent, is capable of accommodating commercial transactions. Since there can be no derivation of income without commercial activity we are entitled to read that into the definition. In the case of minerals or metals from a mine such an income producing transaction would commonly be a sale. One would therefore, at least, have to interpose a sale (and the associated delivery and payment) between the extraction of the minerals and the income, thus postulating a business. I am nevertheless unable to accept the argument for the appellant that the Act

> contemplates as the source of the income the mining trade carried on by the appellant. In order to derive income a taxpayer must generally carry on a trade, but that is not to say that the trade, although it is a *sine qua non* of the trading income, is its *source*.

(Underlining supplied)

[20] In my view, what these authorities imply is that the forensic enquiry about 'income' and its source, is an exercise in which one begins by first identifying *exactly what* constitutes the 'income'. If, as in the example postulated in *Western Platinum*, it is money obtained from a sale, then one goes to ask: what was sold? In that example, it is the mineral that is sold and the 'connection' to the mining as the source of the payment is established. On the other hand, if *what* constitutes the 'income' is a fee, one would ask what was the *quid pro quo*. Obviously, the fee is the reward for services rendered. But to say that is to give voice to a neutral generic fact. What *work justified* the fee may be more useful question to ask. If the answer to that question is that the creditor dug minerals out of the earth, that description, in my view, is incomplete. The full answer would include the significant fact that *in fulfilment of a contract* to extract minerals from the earth, for the benefit of the debtor, the creditor becomes *entitled to the agreed fee*.

[21] In this context, the taxpayer whose undertaking it is to extract topsoil, overburden, and chrome bearing ore is undoubtedly a digger, but is not a miner, as defined, for what its enterprise comprises is merely the physical activity of extraction, but not the broader enterprise of 'mining operations'. CSARS is right to lay emphasis, first, on the critical fact that what is delivered by the taxpayer is

crushed ore which is not in a state to be marketed, and awaits further processing by the client mining right holder to turn it into a commodity that can command interest from potential customers, and second, on the contractual entitlement to a reward as the source of the 'income' it earns.

[22] The poverty of the notion that 'mining operations' can be constituted merely by 'extractive operations' has long been exposed. The oft cited passage from *Federal Commissioner of Taxation v Broken Hill Proprietary Co Ltd 1 ATR 40* was invoked by Harms J in *ITC 1455 (1988) 51 SATC 111 (T*) at pp120-121:

> …... The gold and diamond is already in the earth. One merely isolates it. In the case of iron production the iron is not in the ore. Iron oxide is. The iron is produced by an industrial process and not a mining process. A similar conclusion was reached by the High Court of Australia sitting on appeal in *Federal Commissioner of Taxation* v *Broken Hill Proprietary Co Ltd* 1 ATR 40. The operative paragraph of the judgment deserves quoting:
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> > 'Kitto, J, took a very broad view of what falls within the description of "mining operations". His Honour said:
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> > > "This expression is wider than the working of a mining property. It embraces not only the extraction of mineral from the soil, but also all operations pertaining to mining: Parker v Federal Commissioner of Taxation(1953), 5 AITR 614; 90 CLR 489, at p 494. Thus it comprehends more than_mining in the narrow sense which imports the detaching of lumps of material from the position in which in a state of nature they form part of the soil. It extends to any work done on a mineral-bearing property in preparation for or as ancillary to the actual winning of the mineral (as distinguished from work for the purpose of ascertaining whether it is worth while to undertake mining at all):_*Federal*

> *Commissioner of Taxation* v *Broken Hill South Ltd*(1941), 2 AITR 257; 65 CLR 150, at pp 153, 156, 159, 161. Likewise, it extends to any work done on the property subsequently to the winning of the mineral (eg transporting, crushing, sluicing and screening) for the purpose of completing the recovery of the desired end product of the whole activity: *Federal Commissioner of Taxation* v *Henderson*(1943) 2 AITR 440; 68 CLR 29, at pp 45, 50. In each case it is the close association of the work with the mining proper that gives it the character of operations pertaining to mining" (10 AITR at p 486).

We agree entirely with his Honour's view that "mining operations" covers "work done on a mineral-bearing property in preparation for, or as ancillary to, the actual winning of the mineral", but with regard to the statement, that "it extends to any work done on the property subsequently to the winning of the mineral (eg transporting, crushing, sluicing and screening) for the purpose of completing the recovery of the desired end product of the whole activity", we have a reservation. We do not doubt that to separate what is sought to obtain by mining from that which is mined with it, eg the separation of gold from quartz by crushing etc or the separation of tin from dirt by sluicing, is part of a "mining operation", but we would not extend the conception to what is merely the treatment of the mineral recovered for the purpose of the better utilization of that mineral. Thus to crush bluestone in a stone crushing plant so that it can be used for road making, or to fashion sandstone so that it becomes suitable for building a wall or a town hall is not, as we see it, a mining operation. Nor would the cutting of diamonds or opals which have been recovered by mining operations fall within the description of mining operations. In *Federal Commissioner of Taxation* v *Henderson, supra*, it was decided

that to obtain gold from gold-bearing material, i.e. slum dumps, by sluicing, screening, filtering and chemical treatment, was a mining operation and this, of course, we accept. The reason for so deciding, however, has no application to a process that does no more than either reduce in size lumps of iron stone of manageable size taken from the earth, or, to increase the size of small fragments of ore taken from the earth in order that the ore which has been mined can be conveniently carried away from the mine and utilized in steel making. In *Henderson's* case the object of the taxpayer's mining operations was to obtain gold and those operations comprehended all the steps in the recovery of gold from the slum dumps; here the object of the taxpayer's mining operations is to obtain iron ore – the end product – and those operations comprehend all the steps taken to do so, but once the iron ore is obtained in manageable lumps then its further treatment, either to reduce or increase its size so that it can be conveniently transported from the mine and better utilized in industry, forms no part of the mining operation. In the same way we would not regard the converting of brown coal into briquettes as part of a mining operation; nor would we regard the treatment in a refinery of naturally occurring hydro-carbons in a free state as part of the operation of mining for petroleum. The mining operation in the last-mentioned instance would finish with what is referred to in s 122AA as the "obtaining" of petroleum as defined. Accordingly, we would not treat "the whole activity" referred to in the passage from his Honour's judgment just quoted as extending to the disposal of the product mined, and because we think "the end product" of the mining activity in this case is iron ore to be taken away from the mining property, we consider that "mining operations" ends when the iron ore is in a state

> suitable for this. The taking away from the mining property of ore which has been mined, whether that be done by the mining company or by someone else, is a step subsequent to the conclusion of the mining operations.

(Underlining supplied)

[23] Accordingly, in the chain of activity which constitutes 'mining operations' it seems plain that the mere activity of extraction is a necessary *but not sufficient* attribute for the taxpayer to fall into the class of persons involved in 'mining operations' and at the other end of the process spectrum, once the mineral is 'isolated' any further activity to convert the mineral into a substance that does not exist in a natural state, cannot be 'mining operations' as defined.

[24] The problem of how to deal with the generic 'contract miner' and the anomaly already alluded to is not novel. I was referred to the writings of M C Van Blerck, *Mining Tax in South Africa* (1990) TAXFAX, at p35 where the author offers a view, which is a somewhat semantic and rhetorical contention, that as the state owns all mineral rights and, as at the time of his writing, mining rights were all in terms of leases from the state, all mining is therefore 'in truth' undertaken on a contract 'basis'. The comparison is self-evidently inapposite, but in any event, is unhelpful.

[25] In addressing the fee-earning independent contractor, his opinion is expressed thus:

> Can it be said that the same principles apply when the contractor operates on the basis of a charge which relates to his inputs and efforts rather than receiving a share of profits? To put it differently, is a contractor undertaking mining

> operations where he effectively conducts such operations for the benefit of another, and receives no share in the resultant profits other than a negotiated fee related to his efforts and costs? It is considered that this must be so as the contractor is conducting a process by which a mineral is won from the earth; as a consequence the income which he derives will be taxed in accordance with mining tax rates and the expenditures will be deductible in accordance with the special mining tax provisions.

[26] This is the heart of the taxpayer's case. However, the opinion is unsustainable. One reason why it cannot stand is that it ignores the authorities to the contrary. Mere extraction is not enough to render a contractor who earns a fee for extraction as a person eligible to fall into the class of persons who are engaged in 'mining operations' as defined. The contractor is not in the 'trade' of mining; rather the contractor is in the trade of servicing a miner's requirements by the extraction of material. The paradox has already been mentioned.

[27] The flaw in Van Blerck's contention is usefully illustrated by comparison with the circumstances examined in *Gloucester Manganese Mines (Postmasburg) Ltd CIR 12 SATC 229*. The mining right holder conferred on the contractor the right to mine the mineral in return for a percentage of the profits on the sale of the mineral. This relationship is joint venture. The contractor in this example was held to be, indeed, engaged in 'mining operations'. The 'trade' of the contractor was not mere extraction, and moreover, its income was dependent upon the dynamics of the market for the sale of the mineral and therefore that taxpayer shared in those risks with the owner of the mining rights and was no independent contractor insulated from the trade of extracting and selling minerals.

The distinction is manifest; i.e. the contract miner is, in effect, an outsourced service, remunerated by the risk-taker, whereas in a joint venture the 'non-owner' of the mining right shares the risk in the whole venture.

[28] The submission was made that since 2002 most mining is undertaken through contract miners; I presume the contention is confined to open cast mining. No evidence was adduced to establish this as a fact. However, even on such a premise, the ubiquity of such a practice contributes nothing to the forensic enquiry. The passage in *Western Platinum*, cited above continues thus at [6] – [7]:

> [6] ….Section 36(7C) of the Act speaks not of 'mining' or 'mining operations' but of '… income derived from the working of any producing mine'. This expression (arguably more focused than the expressions 'mining' and 'mining operations') leaves no doubt that to be mining income its source must be minerals taken from the earth. This was the view correctly taken by the Full Court in *Commissioner for Inland Revenue v BP Southern Africa* (*Pty*) *Ltd* 1997 (1) SA 375 (C) when it said that' Properly construed, in the context of the Act and the Schedule, the phrase "income derived from mining operations" means income derived from the business of extracting minerals from the soil . . .' (at 379CD).
>
> The court used this formulation to point the difference between the derivation of income from working a mine and the derivation of deemed income that accrued to the respondent from the sale of its interest in a mine.
>
> [7] The appellant did not challenge the finding of the court *a quo* that in order to qualify as mining income, the income had to be directly connected to the mining source. 'Directly connected' is an expression from the judgment of the lower court adopted by this court in *D & N Promotions* (at 306CD):

> '. . . the income and the source from which the income arises, namely farming operations, which of course embraces numerous agricultural activities, must be directly connected. An indirect connection or a remote one will not suffice.'

[29] Accordingly, the critical enquiry is into the 'connection' between 'income' and 'source' and whether the connection between the mining operations and the income is broken by an intervening happening. This is the reason why it is not appropriate to try to disaggregate bits and pieces of overall mining operations, as if they could constitute self-standing trades or businesses of 'mining operations.'[6] Accordingly, in my view, the taxpayer is not, in the defined sense, involved in 'mining operations'

THE SPECIAL CAPITAL DEDUCTION BENEFIT IN SECTION 15

[30] It is appropriate to contextualise the controversy both as to the legal environment and as to the actual circumstances of the business environment of the taxpayer. Taxation legislation is a special type of law-making. Its content consists of a plethora of levies on taxpayers, complicated by the invention of different classes of taxpayers, and by the conferring of benefits to some classes of taxpayers and not to others, on innumerable grounds. The appearance of capriciousness in the course of such a web of obligations and benefits is apparent, yet such a rebuke would be out of place because the context in which such a regime operates renders it indeed rational. The foremost characteristic of taxation is that it is an instrument of economic and social policy, by its very nature variable, pragmatic

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[6] Reference was made in argument to the remarks about contract miners by the Davis Tax Committee in paragraph 11.8 of its December 2014 interim report to the Minister of Finance on Mining Taxation. In my view, these remarks are not germane to the present controversy. Other than acknowledging the practice of contract miners and alluding to problematic policy considerations about how to accommodate that business model into the mining tax system, in the future, the burden of the report does not address itself to the interpretation of current legislation.

and responsive to changing circumstances in society. In that role, its very purpose is to engineer various economic and social outcomes by the conferring of benefits or the exclusion of some taxpayers from benefits widely conferred. By such means the fiscal health of the state is sought to be secured so that it may more readily meet the demands made upon it by society. Accordingly, it is no criticism of the legislation that some taxpayers are favoured and others are not. Moreover, as a result, it is not imperative to squeeze the language employed in the legislation to broaden the ambit of special privileges conferred on a particular class of taxpayer on grounds of equity or in pursuit of 'tax neutrality.' The decision to favour some and not others is firmly within the legislative sphere. It is for this reason that where a special benefit is conferred, the provisions are to be strictly construed.[7]

[31] Accordingly, the revelation of an anomaly or a paradox in the effect of a special benefit is no licence to read into the text of such a provision a 'solution' to the anomaly because the conferment is always to be understood to be a concrete choice intended to benefit the given class by way of incentivising that class only in its particular role in the economy, with no sense of entitlement by other taxpayers, who fall outside of the circumscribed class.

[32] Ordinarily, a taxpayer who incurs capital expenditure cannot deduct it all in the fiscal year in which it was disbursed but must amortise it over a number of years,

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7 See: *Western Platinum Ltd v CIR* [2004[4 All SA 611 (SCA) at [1].
"The *fiscus* favours miners and farmers. Miners are permitted to deduct certain categories of capital expenditure from income derived from mining operations. Farmers are permitted to deduct certain defined items of capital expenditure from income derived from farming operations. These are class privileges. In determining their extent, one adopts a strict construction of the empowering legislation. That is the golden rule laid down in *Ernst v Commissioner for Inland Revenue* 1954 (1) SA 318 (A) at 323CE and approved in *Commissioner for Inland Revenue v D & N Promotions* (*Pty*) *Ltd* 1995 (2) SA 296 (A) at 305AB.

as prescribed, the periods thus determined being the notional lifetime of the assets depreciated by wear and tear, or some other expressly articulated formula. Section 11(*e*) of the Act regulates, in general, that calculation. Only in two classes of taxpayer is capital expenditure, in whole, in the year of disbursement, allowed: farmers and miners.

[32] Section 15(*a*) of the Act provides:

> There shall be allowed to be deducted from *the income derived by the taxpayer from mining operations*—
>
> (*a*) an amount to be ascertained under the provisions of section 36, *in lieu* of the allowances in sections 11(*e*), (*f*), (*g*A), (*g*C), (*o*), 12D, 12DA, 12F and 13*quin*;

[33] Self-evidently, section 15 cannot stand alone. Indeed, to read that section alone does not inform the reader what may be deducted. Section 36, to which reference is made, is integral to the coherence of section 15. The portions of section 36 relevant to this controversy are sub-sections (7C), (7E), (7F), (7G), and (10). The identification of *what* 'capital expenditure' in terms of section 15, may be deducted occurs in sub-section (7C).

[35] In that sub-section, the first of two critical dimensions of the deduction of capital expenditure is addressed, i.e. the section 15 deduction is available only in respect of a 'producing mine.' Sub-section (7C) provides that:

> Subject to the provisions of subsections (7E), (7F) and (7G), the amounts to be deducted under section 15(*a*) from income derived from <u>the working of any producing mine</u> shall be the amount of capital expenditure incurred.

[36] The introduction of the concept of a 'producing mine' is plainly a serious constriction of the scope of the deduction benefit; i.e. not every mine can qualify. What needs to be produced is minerals. A worked out mine cannot be 'producing.' Axiomatically, a mine that produces minerals shall also produce revenue, whether or not a profit is achieved. But a mine that fails to 'win' any minerals cannot be a 'producing mine'. From this provision it must be inferred that the benefit is aimed at a limited class of miners.

[37] The second crucial theme about deducting capital expenditure that is addressed is the principle of ring-fencing the entitlement to deduct capital expenditure to a specific mine, rather than availing a deduction to the taxpayer in relation to its entire operations. This appears in sub-section (10) which provides in the plainest terms:

> Where separate and distinct mining operations are carried on in mines that are not contiguous, the allowance for redemption of capital expenditure shall be computed separately.

[38] Each of the three sub-sections referred to by sub-section (7C) address the *implementation of the deduction* in ways that again emphasise the restriction of the scope of the benefit.

[39] The provisions of sub-section (7E) read:

> The aggregate of the amounts of capital expenditure determined under subsection (7C) in respect of any year of assessment in relation to <u>any mine or mines</u> shall not exceed the taxable income (as determined before the deduction of any amount allowable under section 15(*a*), but after the set-off of any balance of assessed loss incurred by the taxpayer <u>in relation to such mine or mines</u> in

> any previous year which has been carried forward from the preceding year of assessment) derived by the taxpayer from mining, and any amount by which the said aggregate would, but for the provisions of this subsection, have exceeded such taxable income as so determined, shall be carried forward and be deemed to be an amount of capital expenditure incurred during the next succeeding year of assessment in respect of the mine or mines to which such capital expenditure relates.

(Underlining supplied)

[40] The phrases emphasised in the cited passage make clear that the claimed deduction must dance and remain in hold with a specified revenue stream, which like the capital expenditure itself, has to be linked to a particular mine, and not to the taxpayer's broader business operations. The cardinal significance of this stricture is neatly illustrated in the controversy addressed in *Armgold/Harmony Freegold joint Venture (Pty) Ltd v CSARS 2013 (1) SA 353 (SCA) at [23] – [24*] about the notion that each mine of a single taxpayer could be a different trade of business of the taxpayer; rejecting that view, Leach JA held:

> [22] The appellant argued that all of this showed that it was impermissible to allow the St Helena loss, incurred by deducting its operating expenses from its gross income, to be deducted from the taxable income of the Joel and Freegold mines as, to do so, would amount to setting off of St Helena's operating expenses against the other two mines' incomes to determine their taxable incomes before making their capex deductions.
>
> [23] Compelling though this argument is in certain respects, I do not see how the mining activities conducted by the appellant at each one of its three mines can be said to be a separate 'trade' defined in s 1 of the Act as including, *inter alia*,

'every profession, trade, business, employment, calling, occupation or venture . . .' from that conducted at the other mines. A company which carries on mining operations certainly carries on the 'trade' of mining, but it would be both fanciful and artificial to regard its mining operations at the St Helena mine as being a different trade from the operations it conducts at its other two mines. Had the legislature intended each mine's operations to be regarded as a separate trade, it could easily have said so. Not only did it not, but the provisions of s 36(7E) in which reference is made to the 'aggregate of the amounts of capital expenditure . . . in relation to any mine or mines,' clearly exclude different mining operations being regarded as different trades. The appellant's argument based upon the necessity to regard its operations at its different mines as different trades must therefore fail.

[24] On the other hand, however, much of the appellant's criticism of SARS's method of assessment has merit. Section 36(7F) envisages the capex deduction of each mine to be determined by having regard to the taxable income derived from that mine, an objective that will be defeated if the operating expenses incurred of one mine are to be taken into account in respect of another. In addition, in *ITC 1420* Kriegler J held in regard to the variable tax rate levied against different mines, that the effect of the formula 'is to tax richer mines at a higher rate than poorer mines'. That effect would be nullified if the operating expenses of a poor mine could be used to reduce the tax liability of a rich mine, and it is not surprising that it was stated in the *Explanatory Memorandum on the Income Tax Bill*, 1990 'that the profitability of each mine must determine the tax rates of the relevant mine and that it should not be influenced by losses and expenditure of other mines or from other sources'. Finally, but most importantly, s 36(7C) provides for the amount to be deducted under s 15(*a*) to be the capital expenditure on a particular mine, determined by the income derived from working

that mine. Violence would be done to this if the operating expenses of one mine were setoff against the income of another, and I have therefore concluded that it is impermissible to do so.

[41] Sub-section (7F) is even more emphatic. That sub-section provides:

> The aggregate of the amounts of capital expenditure determined under subsection (7C) in respect of any year of assessment in relation to any one mine shall, unless the Minister, after consultation with the Cabinet member responsible for mineral resources and having regard to any relevant fiscal, financial or technical implications, otherwise directs, not exceed the taxable income (as determined before the deduction of any amount allowable under section 15(*a*), but after the set-off of any balance of assessed loss incurred by the taxpayer in relation to that mine in any previous year which has been carried forward from the preceding year of assessment) derived by the taxpayer from mining on that mine, and any amount by which the said aggregate would, but for the provisions of this subsection, have exceeded such taxable income as so determined, shall be carried forward and be deemed to be an amount of capital expenditure incurred during the next succeeding year of assessment in respect of that mine: Provided that where the taxpayer was on 5 December 1984 carrying on mining operations on two or more mines, the said mines shall for the purposes of this subsection be deemed to be one mine.

(Underlining supplied)

[42] The upshot of these provisions, in my view, is that the section 15 deduction entitlement can be available only to taxpayers whose 'mining operations' involve capital expenditure of the nature described which is capable of computation by these formulae. Taxpayers whose 'mining operations' involve 'capital expenditure' that cannot fit into this straitjacket are not taxpayers who fall into the

class intended to be beneficiaries of the special up-front capital deduction benefit.

[43] The insurmountable problem that the taxpayer faces is claiming the deduction within the context of the ring-fencing structure inherent in the benefit. It is significant that at no time did the taxpayer in its returns submit the annexures A, B and C of schedule 4 which serve to document the matching revenue and capital expenditure per 'mining operation'. The reason it did not so is that its business model does not lend itself to apportioning capital expenditure in that manner. Only after the returns had been submitted, did the taxpayer compute the revenue streams from each pit. Even then it did not venture to apportion capital expenditure to each revenue source.

[44] There was an objection to CSARS raising this omission of filing the schedule 4 forms during the hearing on the footing that filing incomplete returns was not a pleaded issue. That point is correct, but the objection is misconceived. The relevance of the evidence was not to establish a culpable failure, but rather to illustrate the inability of the taxpayer to bring itself within the ambit of the class of persons who are entitled to the benefit.

[45] Allied to this question, was the evidence about proximity of the several pits and mines upon which the taxpayer was engaged. Because it is common cause that the localities were not contiguous, and indeed the revenue stream analysis prepared by the taxpayer indicated several operations, some arguably with more than one pit, it is plain that the capital deduction claimed was for the entire spectrum of operations, disregarding the geographic sources of revenue.

The upshot is that the taxpayer is eligible to fall into the category of taxpayer intended to enjoy the section 15 benefits.

[46] The historical context in which the benefit has existed serves to illustrate that the benefit is not, was not and cannot have been envisaged as one which a taxpayer who operates as a contract miner could be entitled to enjoy. The special deduction was the subject of consideration by the 1986 Margo commission on the Tax Structure of the Republic of South Africa.[8] In Chapter 14 the Commission addressed the taxation of mining. It noted the notorious fact that the mining industry had dominated the economy since the discovery of diamonds in 1871. In the 20th century it was gold that was the colossus of the economy. The fiscal dependence on mining tax resulted in the decision to treat the taxation of mining differently to the rest of the economy. (And so it remains to this day; in December 2014, the Davis Tax Committee submitted an interim report to the Minister of Finance on the taxation of mining in which it addressed the special case of mining taxation, addressing section 15 and 36 in particular, and the special circumstances of the mining industry in fiscal policy.)

[47] The historical evolution of the special deduction was recounted in the Margo Commission Report of 1986. The purpose and scope of the section 15 deduction regime is described thus:

> 14.17. The mining industry is granted a special allowance, known as the *redemption allowance,* for the redemption of capital expenditure. It is not granted the wear-and-tear, scrapping or obsolescence allowances on plant and machinery granted to traders, manufactures and others. It is in this respect that

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8 RP 34/1987, presented on 20 November 1986, Government Printer, Pretoria.

tax assessment of a mining concern differs radically from that of any other industry or trade, although it is similar in certain respects of farming. The redemption allowance is granted for both tax and lease purposes. It is not to be confused with the *capital allowance,* granted mainly for lease purposes (but extended to a handful of gold mines for tax purposes). This will be discussed later in the chapter.

14.20. The capital expenditure ranking for redemption is deducted from income in accordance with special rules, which have been changed twice since the beginning of 1984 by the addition of s36(7E) and 36(7F) to the Income Tax Act. The deduction itself is, of course, what is referred to as the redemption allowance.

14.21. In years of assessment ending before 1 January 1984 redemption was allowed in full against income from mining operations. Any balance represented an assessed loss which qualified as a deduction against income from any other source. There was, in short, no ring fence.

14.22. For the years of assessment ending on or after 1 January 1984 the deduction of the redemption allowance is limited to taxable income from mining. Any excess is carries forward to the next year. In short, a ring fence, impenetrable to capital expenditure, but not to revenue losses. Is placed around the company's *mining operations.* This is the effect of s 36(7E) of the Act.

14.23. On 5 December 1984 it was announced that, except in those cases where, on that date, more than one *mine* was already being operated by the same person, the capital expenditure incurred by any mine was rank for deduction from the income of that mine only. That is to say, each individual mine was surrounded by a ring fence, impenetrable to capital expenditure, but through which current losses would be allowed to pass. A new s 36(7F) imposed this

restriction. Provision was made for the Minister to grant exemption in special cases. The Commission feels that such exemption should have been made automatic for mines that fail, and **recommends** accordingly.

14.25. The preceding paragraphs have set out the rules relating to what, in ordinary language, may be described as the immediate write-off, or 'expensing', of capital expenditure against a mine's income. Submissions to the Commission related mainly to the lifting of the two ring fences that have been erected in recent years, restricting this write-off, first, to mining income generally, and then to the income of a specific mine. Other submissions emphasized the desirability of retaining the immediate write-off as a central feature of our system of mining taxation.

14.26. The justification for allowing the immediate write-off of capital expenditure in mining is grounded on one point of principle and two practical considerations. The point of principle is that, mining being an exceptionally risky venture, no lease consideration or tax should be payable until capital expenditure has been recouped in full. It is argued that, were any other policy to be followed, there would soon be fewer mines and smaller tax base. The practical considerations are that immediate write-off is simpler, especially in a mining environment; and that the alternative would be to write assets off over their useful lives, which in many cases would entail highly contentious estimates of the life of the mine.

[48] The perception that investors in mining who invest huge sums and wait long periods for a return need relief through special tax benefits is at the heart of the special capital deduction provisions. The *Davis Committee (Supra)* observed in 2014:

In addition to the general income tax provisions, the mining sector is also eligible for various deductions, capital and other tax incentives as described below.

2.1. Evolution of special mining tax incentives

The life cycle of a mine is shaped by various factors which differentiate it from manufacturing concerns. These factors need to be understood in order to have some appreciation for those drivers giving rise to the provision of special tax incentives to the mining industry.

Mining is a cyclical industry and investments in the different stages of the mining industry lifecycle (exploration, development, production and mine closure) tend to follow these cycles. In general, as already noted, mining is a long-term activity requiring significant upfront capital investment and expertise to develop large ore-deposits to the mining production stage. The steps of moving from greenfields exploration through to the development of operating mines (when income is finally generated) may involve multiple decades and many billion rands to bring a project to fruition. Over this period the project will be exposed to fluctuating commodity cycles, changing technology and risks on the geology and technical side of a project, as well as other extraneous potential risks. Mining is also a geographically situated activity which is subject to significant risk from sudden changes describes earlier. Other industries are far more mobile and will relocate to different jurisdictions should the political or legislative environment change significantly.

In an effort to ameliorate the risk posed to mines during their production life cycle, special tax allowances have been provided over the years (discussed more fully below). These incentives provide for the following allowances:

a) To cater for the large upfront investments made by mines

b) The costs of decommissioning mines (mostly environmental rehabilitation costs)

c) In the case of gold mines (for many years gold was the mainstay of South African mining), providing certain additional allowances (mainly intended as a proxy for the cost of money involved in financing the capital outlays involved in commissioning a mine)

d) Also, specifically in the case of gold mining, tax relief for those taxpayers mining marginal ore bodies.

2.3. Deductions

23.1……

2.3.2. Depreciation

Normally taxpayers are allowed to write off assets acquired and used for purposes of trade over the useful life of such assets. Special write-off allowances are granted for manufacturing operations, owners of commercial property, owners of hotels, pipelines, and so forth, but for purposes of this report this is not elaborated on. To the extent that part of a mining taxpayer's operations do not constitute mining operations as defined, it therefore has to avail itself of these general write-off allowances.

The abovementioned is of importance in that these general provisions are only overridden as far as they pertain to a mining taxpayer carrying on mining operations. Furthermore, mining taxpayers are entitled to a 100% capital redemption allowance (discussed below) in lieu of the allowances that would otherwise be grated (not in addition) to non-mining taxpayers.

It is important to bear in mind that the 100% capital redemption allowance is not elective; once a taxpayer satisfies the requirements of the definition of mining

> operations and mining, such a taxpayer is compelled to claim the 100% capital redemption allowance as envisaged in section 15 read with 36 of the income Tax Act.

(Underlining supplied)

CONCLUSIONS ON ELIGIBILITY OF TAXPAYER TO CLAIM A DEDUCTION

[49] To sum up:

49.1. Within the parameters of the definition of 'mining operations' the taxpayer is not engaged into a business which falls into that category of business.

49.2. Independently of that finding, the taxpayer's capital expenditure is not of the kind that the capital expenditure of the taxpayer is eligible for the deduction provided for in sections 15 and 36.

LIABILITY OF THE TAXPAYER TO PAY INTEREST AND PENALITIES ON THE UNDERSTATEMENT OF INCOME

[50] The bare fact of the understatement is not in dispute, once the ineligibility to claim the capital expenditure deduction is established. The issue that remains is whether culpability attaches to that understatement warranting the imposition of penalties and interest.

[51] In terms of section 222 and 223 of the TAA, a penalty of 25% was imposed, invoking (ii) of the table of penalties in section 223, i.e. for 'reasonable care not being taken in completing return'. An objection was duly lodged in terms of section 224 read with section 270(6D).

[52] The controversy relates to whether there are grounds to remit the penalty, as contemplated in section 223(3). That subsection provides:

> (3) SARS must remit a 'penalty' imposed for a 'substantial understatement' if SARS is satisfied that the taxpayer—
>
> (*a*) made <u>full disclosure</u> 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 <u>based upon full disclosure of the specific facts and circumstances of the arrangement</u> 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.
>
> [Para. (*b*) substituted by s. 73 of Act 21 of 2012 (wef 1 October 2012) and amended by s. 76(1)(*b*) of Act 39 of 2013 (wef 16 January 2014).]

(Underlining supplied)

[53] The provisions of section 270(6D)(*a*) also apply, and provide:

> If an understatement penalty is imposed as a result of an understatement, as defined in section 221, made in a return submitted before the commencement date of this Act, a taxpayer may object against the penalty under Chapter 9 (whether or not the taxpayer has previously objected against the assessment imposing the penalty) and if the return was required under—
>
> (*a*) the Income Tax Act, excluding returns required under the Fourth Schedule to that Act, a senior SARS official must, in considering the objection, reduce the penalty in whole or in part if satisfied that there were extenuating circumstances; or…."
>
> [Para. (*a*) substituted by s. 65(*a*) of Act 44 of 2014 (wef 1 October 2012).]

[54] The view of SARS is that that the taxpayer, by reason of wrongly claiming capital expenditure as addressed above, understated its proper tax liability by a sum exceeding R1 million and thus committed a 'substantial understatement' as contemplated by section 222. Moreover, the taxpayer, so argues CSARS, despite claiming to have relied on a tax opinion, never disclosed that allegation until discovery in these proceedings, nor did it act on the advice which was to make full disclosure, and, in consequence, did not take reasonable care in the preparation of the return.

[55] When an appeal is lodged against the discretionary imposition of a penalty, the court does not defer to the exercise of such a discretion but conducts a re-hearing and exercises 'its own original discretion'. (*Commissioner of Inland Revenue v Da Costa* 1985 (3) SA 768 (AD) at 774 H – J.)

[56] There are no material disputes of fact about the case put forward by the taxpayer. However, there are substantial differences in the contentions about what inferences may properly be drawn from the facts. The key premise is that the taxpayer acted under advice and was thus bona fide and reasonable within the meaning of section 223, thus deserving of amelioration of the penalties.

[57] The taxpayer at the relevant time was the wholly owned subsidiary of a holding company (the holding company). The holding company obtained advice, not the taxpayer *per se.* Ordinarily, nothing would turn on this distinction if the advice sought was to advise about the operations of the taxpayer. That is not the case in this matter. The advice sought was in respect of other subsidiaries.

[58] This fact provoked CSARS to challenge the legitimacy of the argument invoking the procurement of advice. Although the taxpayer was never mentioned in the details given by the holding company when seeking the advice nor in the advice give, the advice addressed generically, the issue of section 15 deductions in respect of contract miners. Save for some quibbles, the business model of the taxpayer was, for the purpose of the advice sought, indistinguishable from the entities in respect of whom the advice was given. If the holding company could say that it directed its subsidiary to conduct itself in accordance with advice procured for other subsidiaries, there could be no sensible objection to its stance. The sole risk run would be that, as a fact, there might be a material difference between the taxpayer and the other subsidiaries. In this case, for present purposes, I find that there are none.

[59] However, the evidence that, as a fact, this advice was truly relied on by the executive decision makers of the taxpayer is thin. The fact of the existence of the advice was revealed very late in the progress of this appeal. No explanation has been offered why that is so. More important (given the significance of the existence of the advice, and the alleged reliance thereon when the tax returns were filed from FY 08 onwards) is the absence of its disclosure when the appeal against the imposition of interest and penalties was lodged. If indeed, as a fact, the advice was truly relied on, how conceivably could that information not have been put to the CSARS as the central pillar of the appeal? Most damningly, there is no evidence that the taxpayer's executives (as distinct from the holding company's executives) knew the advice existed when the returns were submitted. However, I shall pass over these considerations and assume, for the purposes of this judgment, that the allegations of knowledge have been established.

[60] An examination of the advice itself discloses that the holding company was informed unequivocally that CSARS had already taken a stand that contract miners could not claim the section 15 deduction. The advice was that the holding company had to accept that acting in accordance with a contrary viewpoint to that of CSARS would almost guarantee contestation. Moreover, and critically, in my view, advice was given to prepare for the inevitable debate by garnering all relevant evidential support and having it in coherent form on hand to meet the challenge that awaited the holding company, and, even more significantly, to *make full disclosure* to CSARS. The evidence does not disclose whether, in respect of the two subsidiaries mentioned in the advice, the deduction was

claimed, and if such contestation occurred in respect of them. I shall, for the purposes of this judgment, draw no inference from the absence of any mention by CSARS of the tax affairs of those entities.

[61] What is manifestly obvious from the evidence adduced is that the taxpayer did not heed the advice, especially the critical advice to make 'full disclosure' to CSARS. In my view, that injunction implied that, upon making the returns, that the status of the taxpayer as a contract miner be expressly stated, and that a motivation be advanced as to why it was appropriate to claim the deduction. The taxpayer did nothing of the sort. Indeed, albeit not clandestinely, the taxpayer simply claimed a globular sum and did not file the prescribed schedules A, B and C of income and capital expenditure for each of the mines at which had been employed. As alluded to earlier, in another context, the only reason for not filing such schedules was that the capital expenditure could not be attributed to localities ring-fenced from one another.

[62] However, even if the matter is approached on the assumption that the advice was relied on, the contentions of the taxpayer that the decision to impose the penalties is inappropriate is ill founded. The advice, at its highest, suggests a 'strong argument' can be advanced to support the taxpayer's preferred view. However, what is *that* argument? Is it the argument advanced to this court? The advice, initially from a firm of public accountants and then endorsed by counsel, at best, is advice to resist SARS's view, if it dared, on the premise that a case could made for eligibility. The substance of the advice is superficial, does not deal meaningfully with the well-known authorities, and most strikingly does not set out a thesis to present in defence of the taxpayers' case. The impression

made by the documents is that the ‘advice’ was preliminary in nature, rather than the rendering of a firm opinion.

[63] The advice in short says little more than the taxpayer should give CSARS a run for its money. The price of that gamble is that if you lose, you pay. And so it ought to be. No case is made out that the taxpayer, in terms of this advice, had any reasonable basis to conclude that it was acting in accordance with a well-considered view of the application of the law that could trump the CSARS view.

[64] As regards the interest liability, (levied in terms of section 89*quat*(2) of the Act) it is plain that the taxpayer has had the financial benefit of the unpaid tax, whether in the form of actual money to be used to its advantage, or the absence of having to pay interest to a lender of that sum of money. *Prima facie*, having had the utility of the money, interest should be paid.

[65] The taxpayer contends that it should be afforded relief pursuant to section 89*quat*(3) of the Act. That subsection provides:

> (3) Where the Commissioner having regard to the circumstances of the case is satisfied that the interest payable in terms of subsection (2) is a result of circumstances beyond the control of the taxpayer, the Commissioner may direct that interest shall not be paid in whole or in part by the taxpayer.
>
> [Sub-s. (3) substituted by s. 24 (1) of Act 36 of 1996, by s. 29 of Act 5 of 2001 and by s. 17 (1) of Act 8 of 2010.]

[66] It must follow that as the taxpayer relies on the same premises as that in respect of the penalties, no grounds exist to do so. The chief criterion of circumstances beyond the taxpayers control are plainly absent.

[67] I am unable to conceive of any reasons, in the exercise of my discretion, why a decision different to that of the decision the CSARS, would be appropriate.

CONCLUSIONS ON THE LIABILITY TO BEAR INTEREST AND PENALITIES

[68] In my view, there are no grounds upon which to conclude the impositions in terms of section 223 of the TAA or the imposition of interest in terms of section89*quat*(2) of the Act, ought to be different.

THE ORDER

[69] The order is as follows:

69.1. The appeal is dismissed.

ROLAND SUTHERLAND
JUDGE

Hearing: 20, 21 and 23 February 2017
Delivered: 30 March 2017