South African Revenue Service

DRAFT INTERPRETATION NOTE

DATE:

ACT : EMPLOYMENT TAX INCENTIVE ACT 26 OF 2013

SECTION : SECTION 1(1) DEFINITION OF "EMPLOYEE", THE PROVISO TO THE DEFINITION OF "MONTHLY REMUNERATION" AND PROVISO TO SECTION 6

SUBJECT : MEANING OF "EMPLOYEE" FOR PURPOSES OF THE EMPLOYMENT TAX INCENTIVE ACT

This draft Note, which was previously published as a draft for comment, has been updated with the latest amendments introduced by the Taxation Laws Amendment Act 20 of 2021.

Contents

Preamble

In this Note unless the context indicates otherwise –

- **"Basic Conditions of Employment Act"** means the Basic Conditions of Employment Act 75 of 1997;
- **"definition of employee"** means the definition of "employee" under section 1(1) of the ETI Act;
- **"ETI"** means employment tax incentive;
- **"ETI Act"** means the Employment Tax Incentive Act 26 of 2013;
- **"Fourth Schedule"** means the Fourth Schedule to the Income Tax Act;
- **"Income Tax Act"** means the Income Tax Act 58 of 1962;
- **"person"** means a natural person;
- **"section"** means a section of the ETI Act;
- **"SETA"** means a sector education and training authority established under section 9(1) of the Skills Development Act;
- **"Skills Development Act"** means the Skills Development Act 97 of 1998;
- **"TA Act"** means the Tax Administration Act 28 of 2011; and
- any other word or expression bears the meaning ascribed to it in the ETI Act.

All guides and interpretation notes referred to in this Note are available on the SARS website at **www.sars.gov.za**. Unless indicated otherwise, the latest issues of these documents should be consulted.

1. Purpose

This Note provides clarity on the interpretation and application of the definition of "employee" read together with the proviso to section 6. The scope of this Note is restricted to arrangements entered into by parties, typically as part of a composite arrangement, in an attempt to claim the ETI for persons not meeting the definition of "employee", specifically arrangements involving learning institutions. The Note therefore does not consider other scenarios in which the definition of "employee" is critical for purposes of claiming the ETI.

No income tax or employees' tax implications such as fringe benefits are considered in this Note.

2. Background

The ETI Act has been introduced to provide an incentive in order to encourage employment creation.[1] The *Explanatory Memorandum on the Employment Tax Incentive Bill, 2013*, states that –

> "In response to the high rate of youth unemployment, Government wishes to implement an incentive mainly aimed at encouraging employers to hire young and less experienced work seekers.
>
> …
>
> Government's aim is that the incentive should assist in the generation of sustainable employment opportunities that enjoy protection under labour law legislation."

The aim of the incentive is to encourage employers to generate sustainable employment opportunities for young persons between the ages of 18 and 29, as well as for persons of any age in special economic zones, and in any industry identified by the Minister by notice in the *Government Gazette*. Government's aim is the generation of sustainable employment opportunities that enjoy protection under labour law legislation.[2]

The incentive provided for under the ETI Act is fundamentally based on an employer-employee relationship. The ETI Act does not define "employer". Section 3 is, however, unambiguous as to who are eligible employers. An employer is eligible to receive the ETI only if the employer is registered for purposes of withholding and paying over to SARS the employees' tax under paragraph 15 of the Fourth Schedule . The ETI Act, however, defines "employee".[3] Besides the requirements contained in this definition, a number of criteria must be met before a person will be considered to be an employee for purposes of the ETI Act.[4]

In some instances, taxpayers become party to composite arrangements which are arguably aimed at abusing the incentive. These composite arrangements typically involve a learning institution, an organisation, and a person for a limited period of either 12 or 24 months. Under the arrangement, the organisation is responsible for paying an agreed-upon training fee to the learning institution, on behalf of that person. Contractually the parties refer to this training fee as the person's basic remuneration. The learning institution is responsible for providing the person with training, mostly in the form of an accredited SETA training course, as well as all the lectures, and training facilities for the duration of the arrangement. In some cases, practical field training is included. Notwithstanding that an employment contract may have been entered into under this composite arrangement, no work is carried out by the person for the organisation.

Under these arrangements, the person generally does not render any services to the organisation and does not obtain practical work experience. The person receives accredited education in the form of training courses through an accredited learning institution. Under some arrangements, the person may be exposed to work-based exercises and activities by another organisation (not the primary organisation) which pays only a fixed monthly fee. These fees are paid to the learning institution and not to

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1 Section 2(1).
2 *Explanatory Memorandum on the Draft Employment Tax Incentive Bill, 2013*.
3 Section 1(1).
4 Section 6.

the person.[5] The number of persons contracted are often more than what is reasonably necessary to conduct the organisation's business.

In an attempt to curb the apparent abuse of the ETI a number of amendments were introduced to the ETI Act,[6] namely –

- an amendment to the definition of "employee" by inserting additional requirements;
- the inclusion of the proviso to the definition of "monthly remuneration"; and
- the inclusion of the proviso to section 6.

3. The law

Section 1(1)

1. Definitions.—(1) In this Act, unless the context indicates otherwise—

"employee" means a natural person—

(*a*) who works for another person and in any other manner directly or indirectly assists in carrying on or conducting the business of that other person;

(*b*) who receives, or is entitled to receive remuneration, from that other person; and

(*c*) who is documented in the records of that other person as envisaged in the record keeping provisions in section 31 of the Basic Conditions of Employment Act, 1997 (Act No. 75 of 1997),

but does not include an independent contractor;

"monthly remuneration"—

(*a*) where an employer employs and pays remuneration to a qualifying employee for at least 160 hours in a month, means the amount paid or payable to the qualifying employee by the employer in respect of a month; or;

(*b*) where the employer employs a qualifying employee and pays remuneration to that employee for less than 160 hours in a month, means an amount calculated in terms of section 7(5):

Provided that in determining the remuneration paid or payable, an amount other than a cash payment that is due and payable to the employee after having accounted for deductions in terms of section 34(1)(*b*) of the Basic Conditions of Employment Act, 1997 (Act No. 75 of 1997), must be disregarded;

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5 See *Explanatory Memorandum on the Taxation Laws Amendment Bill, 2021.*

6 The Taxation Laws Amendment Act 20 of 2021 effective from 1 March 2022 and applicable in respect of years of assessment commencing on or after that date.

Section 6

> **6. Qualifying employees.**—An employee is a qualifying employee if the employee—
>
> …
>
> : Provided that the employee is not, in fulfilling the conditions of their employment contract during any month, mainly involved in the activity of studying, unless the employer and employee have entered into a learning programme as defined in section 1 of the Skills Development Act, 1998 (Act No. 97 of 1998), and, in determining the time spent studying in proportion to the total time for which the employee is employed, the time must be based on actual hours spent studying and employed.

4. Application of the law

4.1 Definition of "employee"

The purpose of definitions in a statute is to define the meaning of key words and phrases used in that statute. Words and phrases included in a definition clause therefore acquire, for purposes of that specific statute, technical meanings that may deviate from their ordinary meaning. Such words and phrases must be understood in accordance with the meaning ascribed by the definition clause.

In *Minister of Defence and Military Veterans v Thomas*,[7] the Constitutional Court held that it is, as a general rule, not permissible to use the meanings attributed to words in other statutes as determinative in the interpretation of a different statute. If Parliament has defined a word used in a statute, it is taken as an indication that Parliament contemplated a special meaning assigned to the word for that statute and not an ordinary meaning.

In *Independent Institute of Education (Pty) Limited v Kwazulu-Natal Law Society and Others*,[8] the Constitutional Court considered the interpretation of words in one Act with reference to words used in another Act. In this case it was stated that there is no principle of interpretation that requires a Court without more to interpret one piece of legislation with reference to another and that a special meaning given to a word or expression in one statute may not be assigned to the same word or expression in another statute which does not define that same word either at all or in the same terms.

The term "employee" is defined in and for purposes of the ETI Act. Therefore, the definition of "employee" in paragraph 1 of the Fourth Schedule or in any other Act will not apply for purposes of the ETI.

Under the definition of "employee", the person must –

- be a natural person (see **4.1.1**);
- work for another person [see **4.1.2(a)**] and in any other manner directly or indirectly assist in carrying on or conducting the business of that other person [see **4.1.2(b)**];
- receive or be entitled to receive remuneration from that person (see **4.1.3**);

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7 2016 (1) SA 103 (CC).

8 2020 (2) SA 325 (CC).

- be documented in the records of that other person as envisaged in the record keeping provisions in section 31 of the Basic Conditions of Employment Act (see **4.1.4**); and
- not be an independent contractor (see **4.1.5**).

All the abovementioned requirements must be met for the person to be considered an "employee" as defined in section 1(1).

It is important to note that the ETI is an incentive and thus when dealing with provisions creating tax privileges a strict interpretation of the provisions should be applied.

4.1.1 Must be a natural person

The definition of "employee" requires that an employee is a natural person. The phrase "natural person" is not defined in the ETI Act, and must therefore be given its ordinary legal meaning. A natural person is a human being and distinguished from a juristic person created by operation of law. *LAWSA*[9] states the following in this regard:

> "Modern law distinguishes between two classes of persons: (a) natural persons; and (b) juristic or artificial persons…All human beings, irrespective of their age, mental condition or intellectual ability, are recognised as legal subjects. Every human being therefore can have rights, duties and capacities although the content of these rights, duties and capacities may vary depending on factors such as the person's mental condition and age. To distinguish them from other juristic persons humans are referred to as 'natural persons'."

Accordingly, a natural person is a human being, and does not include a juristic or artificial person.

4.1.2 Must work for another person and in any other manner directly or indirectly assist in carrying on or conducting the business of that other person

An "employee" must work for another person and in any other manner directly or indirectly assist in carrying on or conducting the business of that other person. These requirements are considered in more detail below.

(a) Meaning of "works for another person"

The word "work" is not defined in the ETI Act and should thus be interpreted according to its ordinary meaning as applied to the subject matter with regard to which it is used.[10]

Dictionary.com defines "work" as a –[11]

> "**1** physical or mental effort directed towards doing or making something".

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9 DSP Cronje (updated by M Carnelley) "Different Kinds of Person" 20(1) (Second Edition Volume) *LAWSA* [online] (My LexisNexis: 30 November 2009) in paragraph 439.

10 EA Kellaway *Principles of Legal Interpretation of Statutes, Contracts and Wills* (1995) Butterworth's at 224.

11 **www.dictionary.com/browse/work** [Accessed 30 March 2023].

In *C: SARS v Terraplas South Africa (Pty) Ltd*[12] it was held that a dictionary meaning of a word cannot govern the interpretation. It can only afford a guide. The question arises as to what is the meaning applicable in the context of the particular document under consideration. The word "work" in the context of the definition of "employee" envisages more than just a contractual relationship between two parties involving the payment of an amount by one party to the other.

In order to obtain a greater understanding of the intention or purpose of a section or definition, it is sometimes useful to refer to the Explanatory Memorandum of an Act.[13]

Under the consideration of the definition of "employee", the *Explanatory Memorandum on the Employment Tax Incentive Bill, 2013* states that it is –

> "necessary to ensure that the employee referred to in the Legislation, not only provides services to the qualifying employer, but is also remunerated by that self same employer."

The *Explanatory Memorandum* states further that –

> "A "working day" will be any day that the qualifying employee would be required to work in the ordinary course of his or her employment."

By the use of the word "work", it was envisaged that the person must provide services to the employer and must regularly assist the employer in carrying on or conducting the business of the employer for which the person is remunerated.

Legally, the essential features required to make a specific contract one of employment are, amongst others, as follows: [14]

- The intention of the parties to conclude a contract of employment (true nature of relationship), also referred to as the reality test
- The existence of a relationship of authority
- The remuneration of the employee
- The rendering of personal services by the employee
- The employee being an integral part of the employer's organisation

In *State Information Technology Agency (SITA) (Pty) Ltd v CCMA and others*[15] the Labour Appeal Court confirmed that the focus has finally shifted from the formal contract of employment to the existence of an employment relationship. The Labour Appeal Court identified the following as the primary criteria for the employment relationship:[16]

- An employer's right to supervision and control
- Whether the employee forms an integral part of the organisation with the employer

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12 [2014] 3 All SA 11 (SCA); 76 SATC 377 at 385.

13 *C:SARS v United Manganese of Kalahari* 2020 (4) SA 428 (SCA).

14 F van Jaarsveld "Criteria to Distinguish Contracts of Employment from Related Contracts" 24(1) (Third Edition Volume) *LAWSA* [online] (My LexisNexis: 30 November 2017) in paragraph 121.

15 [2008] 7 BLLR 611 (LAC).

16 At 615.

- The extent to which the employee was economically dependent upon the employer

Having regard to the definition of "employee", it does not suffice that there is a contract between the parties creating an employer-employee relationship. The factual question is whether the employee works for the employer. The facts and circumstances of each case must be considered to determine the latter. The substance over legal form will be considered when assessing an employer's eligibility to claim the ETI.[17]

A person will generally not be considered to be an employee for purposes of the ETI Act if, despite having concluded a contract of employment with an organisation –

- the person performs no work for the organisation;
- the nature and extent of any work that is performed by the person is such that it does not assist the organisation in carrying on or conducting its business or is not an integral part of the organisation;
- the organisation has no or very limited supervision or control over the person;
- the person does not receive any remuneration from the organisation for the work performed; or
- the person is not entitled to the leave provisions provided under the Basic Conditions of Employment Act.

The above list is not exhaustive but does assist in determining whether a person meets the definition of "employee" for purposes of the ETI Act. Each case will be considered having regard to its specific facts.

If taxpayers are party to composite arrangements which typically involve a learning institution, an organisation, and a person for a limited period of either 12 or 24 months under which the person undergoes training, mostly in the form of an accredited SETA training course, as well as all the lectures and no work is carried out by the person for the organisation, may not meet the requirement "work for". Each case will be considered having regard to its specific facts.

The qualifying learnership agreements envisaged under section 12H of the Income Tax Act[18] must be distinguished from arrangements under which a learning institution is responsible for providing the person with training in the form of an accredited SETA training course by means of lectures, training facilities for the duration of the skills and training agreement together with practical field training. The learnership agreements and apprenticeships envisaged under section 12H are registered with a SETA, and require the person to work for the employer in a regulated environment in order to encourage skills development. Employees undergoing these types of learnerships could qualify for the ETI if all the requirements of the definition of "employee" and the other provisions in the ETI Act are complied with.[19]

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17 See *Explanatory Memorandum on the Taxation Laws Amendment Bill, 2021.*

18 For more information on this section, see Interpretation Note 20 "Additional Deduction for Learnership Agreements".

19 For more information on the ETI, see the *Draft Guide to the Employment Tax Incentive* (Issue 5).

(b) Must in any other manner directly or indirectly assist in carrying on or conducting the business of that other person

The recent amendment[20] to the definition of "employee" included the requirement that an employee must *in any other manner directly or indirectly assists in carrying on or conducting the business of that other person*.

The words "directly" and "indirectly" are not defined in the ETI Act. *Dictionary.com* defines "directly" as "in a direct line, way, or manner; straight"[21] and defines "indirectly" as "by a connection that is not immediate".[22] The words "directly or indirectly" should, however, not be interpreted in isolation in its application, but regard must be had to the context and purpose of the provision.[23] The requirement is that the employee must assist "directly or indirectly" in carrying on or conducting the business of "that other person", in other words the person for whom the employee works [see **4.1.2(a)**] and who must remunerate the employee (see **4.1.3**).

According to its ordinary dictionary meaning, the word "assist" means "If you assist someone, you help them to do a job or task by doing part of the work for them.".[24]

Although the phrase "carrying on or conducting the business" is not defined in the ETI Act, the courts have provided useful guidelines in clarifying its meaning.

In *Estate G v COT*, Beadle CJ made the following comments on what constitutes "carrying on business":[25]

> "The sensible approach, I think, is to look at the activities concerned as a whole, and then to ask the question: Are these the sort of activities which, in commercial life, would be regarded as 'carrying on business'? The principal features of the activities which might be examined in order to determine this are their nature, their scope and magnitude, their object (whether to make a profit or not), the continuity of the activities concerned, if the acquisition of property is involved, the intention with which the property was acquired. This list of features does not purport to be exhaustive, nor are any one of these features necessarily decisive, nor is it possible to generalize and state which feature should carry most weight in determining the problem. Each case must depend on its own particular circumstances."

The question whether an employee assists in carrying on or conducting the business of the employer is a factual question. In this regard one can, amongst others, consider the activities undertaken as a whole. The question is whether these activities are regarded in commercial life as assisting in the carrying on of business. The principal features of the activities must thus be examined in order to determine whether they are in nature, scope and magnitude, contributing to the object and the continuity of the activities concerned.[26]

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20 The Taxation Laws Amendment Act 20 of 2021 effective from 1 March 2022 and applicable in respect of years of assessment commencing on or after that date.

21 **www.dictionary.com/browse/directly** [Accessed 30 March 2023]

22 **www.dictionary.com/browse/indirectly** [Accessed 30 March 2023].

23 *Chisuse and others v Director-General, Department of Home Affairs and another* 2020 (6) SA 14 (CC).

24 **www.collinsdictionary.com/dictionary/english/assist** [Accessed 30 March 2023].

25 1964 (2) SA 701 (SR), 26 SATC 168 at 173 and 174.

26 *Estate G v COT* (above). See also *CIR v Stott* 1928 AD 252, 3 SATC 253 at 257 and ITC 1283 (1978) 41 SATC 36 (SW) at 43.

Example 1 – Definition of "employee" not met

Facts:

On 1 March 2022, Company Z concluded an employment contract with V, aged 20 years, for a limited period of 12 months. Company Z and V agreed to a monthly remuneration of R3 500. The employment contract provides that V receives full time training at a learning institution, College A, from 1 March 2022 for a period of 12 months at a monthly training fee of R3 500. V's monthly remuneration of R3 500 is paid directly to College A to cover the training fee. Company Z complied with payroll-related statutory requirements, namely, payments of employees' tax, unemployment insurance fund contributions and skills development levies.

Company Z, V and College A entered into a composite arrangement under which College A is responsible for providing V with training in the form of an accredited training course, all the lectures and training facilities for the duration of the skills, and training agreement together with practical field training. V did not work for Company Z which was paying V's remuneration.

Result:

Notwithstanding the fact that an employment contract was entered into between Company Z and V, no work (as required by the ETI Act) was carried on by V for Company Z. V received only accredited education in the form of training courses through College A. V did not work for Company Z for the 12-month period and did not contribute in any direct or indirect manner in carrying on the business of Company Z. V therefore does not meet the requirement of the definition of "employee" for purposes of the ETI Act.

Company Z was therefore not entitled to claim the ETI for V.

Example 2 – Definition of "employee" met

Facts:

Company B operates in the building construction industry. On 1 January 2023, Company B, X and College Q concluded a learnership agreement registered with the Construction Education and Training Authority, for a duration of 12 months. Company B then concluded an employment contract with X, aged 22 years, for the duration of the learnership agreement of 12 months.

Company B agreed to pay X a learnership allowance of R3 500 per month. Company B complied with payroll-related statutory requirements, namely, payments of employees' tax, unemployment insurance fund contributions and skills development levies.

X was employed to assist the civil engineers already employed by Company B and was assigned to be part of a specific project. X worked for Company B from Monday to Friday, 8am to 5pm, with an hour lunch break each day. X was entitled to 15 days annual leave, and the other statutory leave provisions as per the Basic Conditions of Employment Act.

Company B was responsible for providing X with supervision, mentoring and coaching at work, and on the job training to enable X to competently perform the specified workplace experience required under the learnership agreement.

College Q was responsible for providing X with the necessary training resources, and course lectures for the duration of the learnership agreement. X was expected to attend lectures outside normal working hours.

Result:

X worked for Company B by assisting the civil engineers on a specific project while under the learnership agreement, and received a learnership allowance from Company B. The learnership allowance meets the definition of "remuneration" as considered under **4.1.3**. X, therefore, meets the requirement of the definition of "employee" for purposes of the ETI Act.

Company B may claim the ETI for X, provided that all of the other requirements under the ETI Act are met.[27]

4.1.3 Requirement to receive or is entitled to receive remuneration

The third requirement of the definition of "employee" is that the person should receive or be entitled to receive remuneration from the employer for which work is performed and for assisting in carrying on or conducting the business of that employer. If the person works for a person, but receives remuneration from another person for the work performed, the person will not meet the requirement of the definition of "employee".

The term "remuneration" is not separately defined in the ETI Act. Having regard to section 1(2), and read together with the definition of "monthly remuneration",[28] the term bears the meaning ascribed to it in paragraph 1 of the Fourth Schedule.[29]

The word "remuneration" is defined in the Fourth Schedule as any amount of income which is *paid or is payable* to any person by way of any salary, leave pay, wage, overtime pay, bonus, gratuity, commission, fee, emolument, pension, superannuation allowance, retiring allowance or stipend, paid in cash or otherwise, and is not dependent on whether the amount is paid or payable for services rendered. The definition is subject to a number of inclusions and exclusions.

For a more detailed explanation of the inclusions and exclusions contained in the definition of "remuneration" as defined in the Fourth Schedule, see Annexure B of the *Draft Guide to the Employment Tax Incentive* (Issue 5).

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27 For more information on the ETI, see the *Draft Guide to the Employment Tax Incentive* (Issue 5).

28 For more information on the definition of "monthly remuneration", see the *Draft Guide to the Employment Tax Incentive* (Issue 5).

29 See section 1(2) stating that for the purposes of the definition of "monthly remuneration" in subsection (1), "remuneration" has the meaning ascribed to it in paragraph 1 of the Fourth Schedule.

The amendment[30] to the definition of "monthly remuneration" introduced a proviso to curb the abuse of the ETI.[31] The proviso aims to exclude non-cash payments and salary sacrifices made by an employee. Monthly remuneration is therefore limited to cash amounts paid to the employee plus any amount that the employer has legally deducted under section 34(1)(*b*) of the Basic Conditions of Employment Act.

Section 34(1)(*b*) of the Basic Conditions of Employment Act provides for deductions required or permitted in terms of a law, collective agreement, court order or arbitration award. Examples of such deductions are employees' tax,[32] unemployment insurance fund contributions,[33] garnishee orders[34] and union membership fees[35].

4.1.4 Must be documented

A further measure to curb the abuse of the ETI is the requirement that with effect from years of assessment commencing on or after 1 March 2022, the natural person who works for another person must be documented in the records of that other person as envisaged in the record keeping provisions in section 31 of the Basic Conditions of Employment Act.[36]

Section 31 of the Basic Conditions of Employment Act provides that every employer must keep a record containing at least the following information:

- the employee's name and occupation;
- the time worked by each employee;
- the remuneration paid to each employee;
- the date of birth of an employee under 18 years of age; and
- any other prescribed information.

These records must be kept by the employer for a period of three years from the date of the last entry in the record.[37] No person may make a false entry in these records.[38] An employer that keeps a record as prescribed in section 31 of the Basic Conditions of Employment Act is not required to keep any other record of time worked and remuneration paid as required by any other employment law.[39]

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30 Taxation Laws Amendment Act 20 of 2021 effective from 1 March 2022 and applicable in respect of assessments on or after that date.

31 *Explanatory Memorandum on the Taxation Laws Amendment Bill*, 2021.

32 A deduction in terms of a law, specifically the Income Tax Act.

33 A deduction in terms of a law, specifically the Unemployment Insurance Contributions Act 4 of 2002.

34 A deduction in terms of a court order.

35 A deduction in terms of a collective agreement.

36 Section 58(1)(*a*) of the Taxation Laws Amendment Act 20 of 2021.

37 Section 31(2) of the Basic Conditions of Employment Act.

38 Section 31(3) of the Basic Conditions of Employment Act.

39 Section 31(4) of the Basic Conditions of Employment Act.

4.1.5 Exclusion of independent contractors

An independent contractor is specifically excluded from the definition of "employee" for purposes of the ETI. The ETI Act does not contain a definition of "independent contractor".

The word "independent" is defined in *Dictionary.com* as:[40]

> "not influenced or controlled by others in matters of opinion, conduct, etc.; thinking or acting for oneself:".

The word "contractor" in turn is defined in *Dictionary.com* as:[41]

> "a person who contracts to furnish supplies or perform work at a certain price or rate."

An independent contractor is therefore not under the control of an employer, and contracts in an independent way with persons to perform a job.

The current South African common law uses a "dominant impression test" to determine whether a person is considered an independent contractor or an employee. The following factors are usually considered in determining whether a person is an employee or independent contractor:

- The company controls the manner that work is done either by detailed instructions, by training, by requesting that prior approval be sought, or by instituting disciplinary steps for unacceptable performance by the person. This type of control is indicative of an employer-employee relationship.
- The company controls the work done, the environment in which the work is done by giving instructions as to the location, when to begin or stop, pace, order or sequence of work. The greater the degree of supervision, the greater the indication in favour of employee status.
- An employment contract is one of personal service (that is, the employee is at the "beck and call" of the employer). Where the company has a contractual right to insist on the personal service of a person or to object to substitution (for example, the worker substitutes his or her own employee for him or herself), or if the person may not freely hire, fire, pay or supervise his or her own assistants, an employer-employee relationship is usually prevalent.
- A reporting regime indicates that a measure of supervision exists, albeit indirect and historic in nature. The existence of a reporting regime, depending on factors such as content, detail, regularity, and obligation, can be persuasive in favour of an employer-employee relationship.
- Should the person contract away his or her right to control his or her time, even for only a portion of his or her productive hours, there is at least a persuasive indicator in favour of an employee status.
- If the company provides the office equipment or tools, stationery etc it tends to indicate a degree of dependence and lack of investment, and hence the existence of an employer-employee relationship.

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40 **www.dictionary.com/browse/independent** [Accessed 30 March 2023].

41 **www.dictionary.com/browse/contractor** [Accessed 30 March 2023].

- If the company provides an office or workshop or the work continually and invariably occurs at the usual place of business of the company, there is an indication of dependence, control, lack of investment, and hence, an employer-employee relationship.

The above list is not exhaustive and should be used only as a guide. For a detailed consideration on these indicators, see Interpretation Note 17 "Employees' Tax: Independent Contractor".

4.2 Proviso to section 6

The proviso[42] to section 6 was also introduced to curb the abuse of the ETI. The proviso must be read with the amendments to the definitions of "employee" and "monthly remuneration". It provides that the employee is not, in fulfilling the conditions of their employment contract during any month, mainly involved in the activity of studying. In determining the time spent studying in proportion to the total time for which the employee is employed, the time must be based on actual hours spent studying and employed. This determination need not be done if an employer and employee have entered into a learning programme as defined in section 1 of the Skills Development Act.

The word "mainly" is interpreted to mean more than 50%.[43] In determining "mainly" regard must thus be had to the time spent studying in proportion to the total time for which the employee is employed. The facts of each case must be considered.

A learning programme as defined in section 1 of the Skills Development Act is, however, excluded from the training envisaged under the proviso to section 6. Section 1 of the Skills Development Act defines a "learning programme" to include –

> "a learnership, an apprenticeship, a skills programme and any other prescribed learning programme which includes a structured work experience component".

Only the learnership programmes within the said definition will qualify for the exclusion stated in the proviso to section 6. In this regard the context, purpose and interpretation of the Skills Development Act must be considered. Section 3 of this Act provides that any person applying this Act must interpret its provisions to give effect to—

a) its purposes; and

b) the objects of the National Qualifications Framework Act 67 of 2008.

Reference to "any other prescribed learning programme" in the said definition must therefore be interpreted in its context. The application of the *ejusdem generis*-rule is sometimes expressed by the maxim *noscitur a sociis*, that is the measuring of a word may be ascertained by reference to those associated with it. In other words, if two or more words which are susceptible of analogous meaning are coupled they are understood to be used in their cognate sense. They take, as it were, their colour from each other. The more general is restricted to a sense analogous to the less general.

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42 Section 59(1) of the Taxation Laws Amendment Act 20 of 2021 with effect from 1 March 2022 and applicable in respect of years of assessment commencing on or after that date.

43 See *SBI v Lourens Erasmus (Edms) Bpk* 1966 (4) SA 434(A), 28 SATC 233.

General words following upon and connected with specific words are more restricted in their operation than if they stood alone. Their meaning is cut down so as to comprehend only things of the same kind as those designed by the specific words unless of course, there is something to show that a wider sense was intended. The words “any other prescribed learning programme” can thus not be interpreted to mean any form of a training programme not meeting the requirements of the relevant legislation.

The facts and circumstances of each case must be considered to determine whether the programme meets the definition of a “learning programme” as defined in section 1 of the Skills Development Act.

5. Recordkeeping

Under section 29(2) and (3) of the TA Act, any records, books of account or other documents relating to the ETI claim, must be retained and carefully preserved for a period of five years from the date of submission of the return.

In order to assist in enforcing the ETI Act, SARS may, under section 46(1) of the TA Act, request the taxpayer orally or in writing to submit relevant information and documents. SARS may, amongst other things, require the taxpayer to provide for inspection any information relating to the person for whom the taxpayer claimed the ETI. The following information may be requested by SARS (the list is not exhaustive but rather a guide):

- Employment contract
- Job description
- Payslips
- Register of leave entitlement and utilisation
- Register of hours worked, including timecards, as well as the nature and outcome of work performed
- Training contract
- Attendance register of training

Under section 47(1) and (2) of the TA Act, SARS may require the employer or employee to meet with the Commissioner’s representative for an interview to clarify issues of concern to SARS and produce for examination any documents relating to the ETI claim.

Under section 102(1)(*b*) of the TA Act the burden of proving that an amount is deductible or may be set off, is on the taxpayer.

6. Understatement Penalty

Section 222(1) of the TA Act provides that an understatement penalty is payable in the event of an "understatement" by a taxpayer in addition to the "tax" payable for the relevant period. The understatement penalty is determined under section 222(2) of the TA Act unless the "understatement" results from a bona fide *inadvertent error*.

Section 222(2) of the TA Act provides that the understatement penalty is the amount resulting from applying the highest applicable understatement penalty percentage in accordance with the table in section 223 of the TA Act to each shortfall determined under sections 223(3) and (4) of the TA Act to each "understatement".

The term "understatement" is defined in section 221 of the TA Act as any prejudice to SARS or the *fiscus* as a result of –

- failure to submit a return required under a tax Act or by the Commissioner;
- an omission from a return;
- an incorrect statement in a return;
- the failure to pay the correct amount of tax[44] when a return is not required; or
- an impermissible avoidance arrangement.[45]

The definition of "tax" in section 221 of the TA Act was amended by the Tax Administration Laws Amendment Act 16 of 2022[46] to include an ETI as referred to in section 2(1) for purposes of Part A of Chapter 16 of the TA Act.

This amendment was deemed to have come into operation on 1 September 2022, and applies to any return, for purposes of paragraph 14(2) of the Fourth Schedule, submitted or after that date.

Prior to the amendment the definition referred to the definition of "tax" in section 1(1) of the TA Act but excludes penalties and interest. The term "tax" in section 1(1) of the TA Act includes a tax, duty, levy, royalty, fee, contribution, penalty, interest and any other moneys imposed under a tax Act.

An employer that reduces the employees' tax payable[47] with an ETI amount to which the employer is not legally entitled or wrongly calculated will therefore be subject to an understatement penalty.

Any penalty imposed under section 222(2) of the TA Act must be reduced by any penalty imposed under section 4(2) in respect of the same employment tax incentive amount.[48]

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44 Section 221 of the TA Act defines "tax" as "tax as defined in section 1, excluding a penalty and interest". Section 1 defines "tax" as "for purposes of administration under this Act, includes a tax, duty, levy, royalty, fee, contribution, penalty, interest and any other moneys imposed under a tax Act".

45 Defined in section 221 of the TA Act to mean "an arrangement in respect of which Part IIA of Chapter III of the Income Tax Act is applied and includes, for purposes of this Chapter, any transaction, operation, scheme or agreement in respect of which section 73 of the Value-added Tax Act or any other general anti-avoidance provision under a tax Act is applied".

46 Section 26(1) of the Tax Administration Laws Amendment Act 16 of 2022.

47 Section 2(2) of the ETI Act.

48 Section 27(1) of the Tax Administration Laws Amendment Act 16 of 2022.

For a detailed consideration of the understatement penalty and its implications for ETI see the *Draft Guide to the Employment Tax Incentive* (Issue 5).

7. Objection and appeal

Under section 104 of the TA Act, "a taxpayer who is aggrieved by an assessment made in respect of the taxpayer may object to the assessment". If SARS disallows the objection, the taxpayer may follow the appeal route under section 107 of the TA Act, read with the rules made by the Minister of Finance.[49]

8. Conclusion

Under the definition of "employee", the person must –

- be a natural person;
- work for another person and in any other manner directly or indirectly assist in carrying on or conducting the business of that other person;
- receive or be entitled to receive remuneration from that person;
- be documented in the records of that other person as envisaged in the record keeping provisions in section 31 of the Basic Conditions of Employment Act; and
- not be an independent contractor.

In addition to the abovementioned requirements, the person must not, in fulfilling the conditions of their employment contract during any month, mainly be involved in the activity of studying.

In the context of the ETI Act, a mere contractual relationship between two parties involving the payment of an amount by one party to the other is insufficient to meet the definition of "employee" . The person must also work for the organisation that pays the remuneration for the work performed. The facts and circumstances of each case will be considered to determine whether the nature and extent of any work performed by the person is such that it does assist the organisation in carrying on and conducting its business and is an integral part of the organisation.

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[49] Government Notice 550 in *Government Gazette* 37819 of 11 July 2014.