



VAT 409

Guide for Fixed Property and Construction for Vendors

Value-Added Tax



South African Revenue Service

Preface

This guide is a general guide concerning the application of the VAT Act in connection with fixed property and construction transactions in South Africa. Although fairly comprehensive, the guide does not deal with all the legal detail associated with VAT and is not intended for legal reference. Technical and legal terminology has also been avoided wherever possible. For details in respect of the general operation of VAT, see the *VAT 404 – Guide for Vendors* which is available on the South African Revenue Service (SARS) website (www.sars.gov.za).

All references to “the VAT Act” or “the Act” are to the Value-Added Tax Act 89 of 1991, and references to “sections” are to sections of the VAT Act, unless the context otherwise indicates. Similarly, all references to “TA Act” are to the Tax Administration Act 28 of 2011. The terms “Republic”, “South Africa” or the abbreviation “RSA”, are used interchangeably in this document as a reference to the sovereign territory of the Republic of South Africa, as set out in the definition of “Republic” in section 1(1) of the VAT Act. The terms “Commissioner” and “Minister” refer to the Commissioner for SARS and the Minister of Finance respectively, unless otherwise indicated. A number of specific terms used throughout this guide are defined in the VAT Act. The term “open market value” is used frequently in this guide and is abbreviated where appropriate as “OMV”. These terms and others are listed in the **Glossary** in a simplified form to make the guide more user-friendly.

The information in this guide is based on the VAT and Tax Administration legislation (as amended) as at the time of publishing and includes the amendments contained in the Taxation Laws Amendment Act 16 of 2022, the Tax Administration Laws Amendment Act 20 of 2022 and the Rates and Monetary Amounts and Amendment of Revenue Laws Act 19 of 2022. These Acts were all promulgated on 5 January 2023 as per *Government Gazettes* 47825, 47827 and 47826 respectively.

The VAT rate was increased from 14% to 15% with effect from 1 April 2018. Although rate specific rules apply to certain fixed property transactions, the examples in this guide are not affected by, and do not illustrate these rules. For information on how the VAT rate increase affects specific fixed property transactions, see *Frequently Asked Questions (FAQs): Increase in the VAT rate from 1 April 2018* on the **SARS website**.

The information in this guide is issued for guidance only. This guide is not an “official publication” as defined in section 1 of the TA Act and accordingly does not create a practice generally prevailing under section 5 of that Act. It is also not a binding general ruling under section 89 of Chapter 7 of the TA Act or a ruling under section 41B of the VAT Act unless otherwise indicated.

The previous edition of this guide has been withdrawn with effect from 5 October 2023.

There are various other guides available on the **SARS website** which may be referred to for more information relating to the specific VAT topics. See the *VAT 404 – Guide for Vendors* for a list of the various guides published.

All guides, interpretation notes, rulings, forms, returns and tables referred to in this guide are the latest versions available on the **SARS website**, unless the context indicates otherwise, or available on request via eFiling at www.sarsefiling.co.za, whichever is applicable.

For more information, you may –

- visit the **SARS website**;
- contact the SARS National Contact Centre –
 - if calling locally, on 0800 00 7277; or
 - if calling from abroad, on +27 11 602 2093 (only between 8am and 4:30pm South African time);
- have a virtual consultation with a SARS consultant by making an appointment via the **SARS website**;
- visit your local SARS branch, preferably after making an appointment via the **SARS website**;
- submit legal interpretative queries on the TA Act by e-mail to **TAAInfo@sars.gov.za**;
- submit a ruling application to SARS headed “Application for a VAT Class Ruling” or “Application for a VAT Ruling” together with the VAT301 form by e-mail to **VATRulings@sars.gov.za**, .or
- contact your own tax advisors.

Operational information contained in this guide is up to date as at 5 October 2023. However, always refer to the **SARS website** and any external guides specifically issued on such operational matters, which may be updated from time-to-time.

Comments regarding this guide may be e-mailed to **policycomments@sars.gov.za**.

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Chapter 1

Introduction

1.1 Focus of the guide

The fixed property industry consists of many role-players, including architects, builders, developers, property speculators, quantity surveyors, engineers, plumbers, electricians, municipalities, public entities, financial institutions, estate agents etc. Although these role-players are mentioned in this guide, the content deals primarily with vendors that are involved in transactions concerning the development, construction and selling of fixed property.

1.2 Scope of transactions

VAT is an indirect tax which is levied on the supply of any “goods” or “services” supplied by a “vendor” in the course or furtherance of any enterprise carried on by that vendor. “Goods” is defined to include “fixed property” and any real right in any such fixed property but excluding any right under a mortgage bond or pledge of any fixed property. The scope of transactions with which this guide is concerned with is therefore those described in the definition of “fixed property”, which means –

- land (together with improvements affixed thereto);
- any unit as defined in section 1 of the Sectional Titles Act 95 of 1986;
- any share in a share block company which confers a right to or interest in the use of immovable property under the Share Blocks Control Act 59 of 1980;¹
- in relation to a property time-sharing scheme, any time-sharing interest as defined in section 1 of the Property Time-sharing Control Act 75 of 1983; and
- any real right in any such land, unit, share or time-sharing interest.

It will therefore be found that most transactions which have some connection with the acquisition of rights to fixed property (excluding rights under a mortgage bond or pledge of fixed property) will fall within the ambit of the definition and will be subject to VAT if the supplier is a vendor.

Other examples of rights falling within the definition include:

- Certain rights of use such as usufructs, *usus* or *habitatio*
- Bare dominium rights of ownership
- Servitudes, encroachments and other encumbrances
- Exclusive use areas in sectional title developments
- Rights to minerals or rights to mine for minerals
- Leases or sub-leases of rights to minerals, or to mine for minerals.

Although most supplies of fixed property by a vendor will be subject to VAT, there are certain instances when such supplies will not be. In these cases, the transactions will be subject to transfer duty. It is therefore important that vendors can distinguish between the different types of supplies to establish whether VAT or transfer duty applies. The VAT Act and the Transfer

¹ For more details in this regard, see the VAT 412 – Guide for Share Block Schemes.

Duty Act 40 of 1949 (the Transfer Duty Act) therefore both contain special rules to deal with these situations. (See the *Transfer Duty Guide*.)

1.3 Approach of the guide

The approach of this guide in dealing with the topics mentioned in **1.2** is set out below:

Chapter 1 – This chapter sets out the scope of the most common transactions falling within the definition of “fixed property”.

Chapter 2 – Introduces the reader to the most important concepts, terms and definitions mentioned in the guide so that the VAT treatment of supplies which are explained in later chapters can be understood. A key point addressed in this chapter is the concept of an “enterprise” and the different circumstances under which certain activities conducted will render a person liable to register for VAT.

Chapter 3 – Deals with the interaction between VAT, transfer duty and securities transfer tax. This chapter explains which types of transactions are subject to VAT and when the other taxes will apply.

Chapter 4 – Explains the VAT treatment of the different types of supplies and the VAT accounting in respect thereof. The chapter includes a discussion on the application of the special time and value of supply rules with regard to the declaration of output tax and input tax. It also explains the rules which apply for deducting notional input tax on the acquisition of second-hand goods constituting fixed property.

Chapter 5 – Deals with a number of adjustments which apply in connection with fixed property based on the extent of taxable use. These include annual adjustments in regard to the use of capital goods and services as well as situations which give rise to a change in use or application or change of intention with regard to the taxable use of the fixed property after the initial acquisition.

Chapter 6 – Explains the specific application of the VAT law which has been set out in previous chapters to transactions in the construction industry. The focus is specifically on those vendors that supply construction services only and deals mainly with quoting of prices, costing of projects, invoicing, agent and principal relationships, and certain other aspects such as penalties and retentions which are unique to the construction industry.

Chapter 7 – Deals mainly with the issues faced by developers and property speculators. The focus is therefore on supplies of newly constructed properties and second-hand properties that have been renovated before being sold, or properties that are bought and sold on a speculative basis. Included is a discussion on the consequences of temporarily applying residential properties for exempt supplies whilst they are being marketed for sale (taxable supplies). Other topics include the sale of shares and members’ interests in fixed property, fractional ownership-type developments and land restitution transactions.

Chapter 8 – Deals with the VAT treatment of rental pools. The chapter contains a detailed explanation of the special rules set out in section 52 and how these apply in practice to override what would otherwise be viewed as supplies made by an agent as set out in **2.11**.

Chapter 9 – Discusses some other aspects regarding the supply of fixed property which are not dealt with in the other chapters.

Chapter 2

Definitions and concepts

2.1 Enterprise

The term “enterprise” is the starting point in determining whether a person is liable to be registered for VAT purposes in the Republic. A person is generally considered to be carrying on an enterprise if all of the following requirements are met:

- An enterprise or activity is carried on continuously or regularly by a person in the Republic or partly in the Republic.
- In the course of the enterprise or activity, goods or services are supplied to another person.
- There is a consideration payable for the goods or services supplied.

2.1.1 “Continuously or regularly”

The definition also contemplates that the enterprise activity is carried on all the time (continuously), or it must be carried on at reasonably short intervals (regularly). “Continuously” is generally interpreted as ongoing, that is the duration of the activity has neither ceased in a permanent sense, nor has it been interrupted in a substantial way. The term “regular” refers to an activity that takes place repeatedly. Therefore, an activity can be “regular” if it is repeated at reasonably fixed intervals taking into consideration the type of supply and the time taken to complete the activities associated with making the supply.

Whilst it is relatively easy to identify when construction services culminate in the carrying on of an enterprise, it is not as easy to determine whether the subdivision of land and the resultant sales of the subdivided portions give rise to the carrying on of an enterprise.

It is important to note that a person can be regarded as conducting an enterprise when making only one supply, for example, the construction of a house and the sale thereof. In the context of the property and construction industry, it is therefore critical to ascertain whether an enterprise activity is carried on and whether the supply will be subject to VAT or if the supply is exempt (for example, the rental of a dwelling (see 9.7)).

Example 1 – Carrying on an enterprise: Continuous or regular activity

Facts:

Development Company ABC was formed with the sole and specific purpose of acquiring a piece of land on which it would construct a block of flats. After completion of the project, the block of flats would be sold to Company XYZ for R10 million. After the sale of the flats and the winding up of the project, Development Company ABC will cease trading. Company XYZ will open a sectional title register in respect of the units and sell them individually. This is Company XYZ's first project.

Are Development Company ABC and Company XYZ carrying on enterprises?

Result:

Although Development Company ABC will only realise one sale, it will be engaged in a continuous activity, being the acquisition of the land and the construction of the building that will result in the supply of goods constituting “fixed property”. Development Company ABC will therefore be carrying on an enterprise. Company XYZ also carries on an enterprise as it will be engaged in a number of continuous or regular activities, which will culminate in selling individual units. The fact that it is Company XYZ’s first project is irrelevant.

Example 2 – Mere subdivision and sale of land*Facts:*

Mrs C inherits a property from her deceased mother on which there is a house and some stables. Mrs C decides to subdivide the smallholding into two parts. She retains the portion on which the house is situated and sells off the remaining portion with the stables for a total selling price of R2 million.

Does Mrs C carry on an enterprise by subdividing and selling part of the smallholding?

Result:

The mere subdivision and sale of the subdivided portion of the smallholding by Mrs C is to realise part of the property which she has inherited to her best advantage. As Mrs C is merely disposing of part of the inherited property, she is not regarded as carrying on an enterprise.

Example 3 – Subdivision and sale of land involving various steps and activities*Facts:*

Mr A (non-vendor) inherits a small farm from his deceased father (non-vendor). As Mr A does not want to continue the farming operation, he decides to turn it into a high-security housing estate and sell off the individual subdivisions for R2 million each. This involves subdividing the land into 20 plots which includes –

- the installation of service points for water and electricity; and
- the building of access roads, other common facilities and amenities.

Does Mr A carry on an enterprise?

Result:

The development of the estate which includes the installation of service points and building of access roads to get the subdivided properties into a saleable state is an activity that will be carried on by Mr A on a continuous and regular basis. Mr A will therefore be carrying on an enterprise.

Example 4 – Employee conducts an enterprise outside of an employment arrangement*Facts:*

Mr P is a salaried employee of XYZ Estate Agents. He buys houses, renovates them in his spare time, and then sells them in order to supplement his income. On average, Mr P manages to sell one house per year at an average selling price of R1,5 million.

Does Mr P carry on an enterprise?

Result:

Although on average, Mr P only sells one house per year, he is continuously carrying on activities which are necessary to sell the houses. This constitutes an enterprise activity. Mr P's enterprise activities are separate and distinct from the activities of XYZ Estate Agents, as well as those which he carries out in his capacity as an employee of the agency.

2.1.2 Commercial accommodation

A person that supplies “commercial accommodation”² can only be regarded as carrying on an enterprise if the value of taxable supplies of commercial accommodation is in excess of R120 000 in a 12-month period.³ This is the only activity which has to exceed a threshold to constitute an enterprise activity. See 2.9 for a detailed discussion on the meaning of the term “commercial accommodation”.

2.1.3 Non-enterprise activities (exempt and out of scope supplies)

Specifically excluded from the definition of “enterprise” is any activity that involves the making of exempt supplies, for example, the letting of a dwelling (see 9.7). A person that only makes exempt supplies will not be able to register for VAT. Similarly, if a person is registered for VAT in respect of a taxable activity, and also conducts an exempt activity, output tax cannot be charged on the supplies made in the course of carrying on the exempt activity. Input tax cannot be deducted on expenses incurred in conducting the exempt activity.

If the person sells fixed property in the course of winding down the exempt activity, or the property was not used in the course of conducting an enterprise activity (for example, the vendor's private residence), the subsequent sale of the property will not be subject to VAT. Instead, transfer duty will be payable by the purchaser, subject to the exemptions contained in the Transfer Duty Act. (See 7.6 for an exception regarding the temporary use or application for exempt supplies.)

Example 5 – Supply of a dwelling used as a residence before the sale*Facts:*

Mr G (non-vendor) decides to invest in fixed property and purchases two residential units in a sectional title scheme with the objective of leasing the units out under indefinite lease agreements to earn rental income. After letting the units for a few years, he decides that market conditions are such that he will realise a very good profit if he sells the units.

² Paragraph (a) of the definition of “commercial accommodation” in section 1(1).

³ Proviso (ix) to the definition of “enterprise” was amended with effect from 1 April 2016 to increase the minimum threshold for commercial accommodation from R60 000 to R120 000 in a period of 12 months.

Is Mr G carrying on an enterprise with regard to the letting and subsequent sale of the units?

Result:

Mr G is not carrying on an enterprise as the letting of the units constitutes the supply of a dwelling under a lease agreement which is an exempt supply.

The subsequent sale of the units will not attract VAT as they would have been used for making exempt supplies before selling the units. In other words, the supply is out-of-scope for VAT purposes and the purchasers will be required to pay transfer duty (subject to any exemptions which may be applicable).

2.2 Registration

A person that conducts an enterprise and makes taxable supplies in excess of R1 million in any consecutive 12-month period or will exceed that amount in terms of a contractual obligation in writing, is liable to register. A person may also choose to register voluntarily provided the minimum threshold of R50 000 has been exceeded in the past 12-month period.

Although the voluntary registration rules refer to a minimum threshold of taxable supplies of R50 000, a person that supplies commercial accommodation can only qualify as an enterprise if the value of taxable supplies made is more than R120 000. If the value of the commercial accommodation supplied exceeds R50 000 but does not exceed R120 000, the person will not be entitled to register as a vendor since such person will not be deemed to conduct an enterprise. There are also certain other exceptional cases which are dealt with in the Registration Regulation⁴, which prescribes other conditions which must be met if the applicant has not met the minimum threshold of R50 000 at the time of applying for voluntary registration.

Example 6 – Property investment company conducting an enterprise required to register for VAT

Facts:

ABC Company, a newly formed property investment company, acquires a newly constructed complex consisting of 10 units. ABC Company markets the units individually for R1,2 million per unit. On average, ABC Company manages to sell one unit per month.

Must ABC Company register for VAT?

Result:

ABC Company will be engaged in several continuous or regular activities, which will culminate in selling individual units. This constitutes an enterprise activity and as the value of its taxable supplies exceeds the current registration threshold of R1 million once the first unit is sold, ABC Company must register for VAT at the end of the month in which the first unit is sold and charge VAT on the sale of the units.

⁴ See Government Notices R. 446 and R. 447 as published in *Government Gazette* 38836 dated 29 May 2015 which set out the requirements that must be met by a person applying for registration as a vendor under section 23(3)(a) and 23(3)(b)(ii), respectively.

Example 7 – Voluntary registration as an independent estate agent*Facts:*

After many years of working as an estate agent for a large national estate agency company, Mr A decides to resign and starts his own independent estate agency business. Mr A sells three properties on behalf of his clients and earns a total commission amounting to R100 000 in a 12-month period.

Can Mr A register for VAT voluntarily?

Result:

Mr A is engaged in a continuous activity of arranging the selling of property on a continuous or regular basis. Mr A qualifies to register for VAT voluntarily at the end of the month during which the value of taxable supplies over a period of 12 months exceeds the minimum voluntary registration threshold of R50 000.

Example 8 – Voluntary registration as a business supplying commercial accommodation*Facts:*

During April 2022 Ms S bought a house in La Lucia which she converted into a guesthouse to take advantage of the accommodation needs of tourists in the Durban North area. Ms S earns R100 000 during the first 12 months of running the guesthouse.

Can Ms S register for VAT voluntarily?

Result:

Ms S is engaged in the supply of commercial accommodation to guests on a continuous or regular basis. The value of taxable supplies (commercial accommodation) is, however, less than the threshold of R120 000 in a 12-month period. Ms S is therefore not conducting an enterprise and does not qualify to register for VAT.

Example 9 – Voluntary registration as a business supplying commercial accommodation*Facts:*

Assume the same facts in **Example 8** above, except that Ms S earns R800 000 instead of R100 000 during the first 12 months of running the guesthouse.

Is Ms S required to register for VAT?

Result:

Ms S is engaged in the supply of commercial accommodation to guests on a continuous or regular basis. Ms S qualifies to register for VAT voluntarily at the end of the month that the value of taxable supplies (commercial accommodation) exceeds the minimum threshold of R120 000 in a 12-month period.

2.3 Goods, fixed property and second-hand goods

The term “goods” includes corporeal movable things, fixed property and any real right in such thing or fixed property. The definition basically refers to any tangible property and any real right in such tangible property.

“Fixed property”, in turn, is defined to mean –

- land, including any improvements permanently affixed thereto;
- any sectional title unit;
- any share in a share block company which confers a right to or an interest in the use of immovable property;
- any time-sharing interest as defined in section 1 of the Property Time-sharing Control Act 75 of 1983; and
- any real right in any of the above.

A real right is a right which may be enforced against the world at large. To constitute a real right in fixed property, the right must be registered or capable of being registered in the Deeds Registry. Examples of real rights in fixed property include freehold property ownership rights, property rights held under a sectional title scheme, mineral rights and limited real rights such as bare dominium and servitude.

The classification of a right as a real right is important for VAT purposes, as a real right is regarded as “goods”, whereas a non-registrable personal right constitutes a service. As such, there could, for example, be a different treatment for VAT purposes in respect of –

- the time of supply; or
- whether or not the zero rate applies; or
- whether notional input tax may be deducted (see 2.7).

The term “second-hand goods” includes goods which were previously owned and used. It is necessary to determine whether the property acquired from a non-vendor qualifies as second-hand as the VAT Act allows the deduction of notional input tax even though no VAT was charged on the sale of the property (see 2.7).

2.4 Services

The term “services” is defined to mean anything done or to be done, resulting in a definition of wide inclusion. Therefore, anything that does not constitute “goods” or “money” will usually be a “service”.

Example 10 – Right to purchase acquired from a non-vendor

Facts:

A vendor obtains a right to purchase fixed property from a non-vendor and pays a non-refundable amount to the supplier in respect thereof.

Is the vendor entitled to a notional input tax deduction in respect of the acquisition of the right?

Result:

A notional input tax deduction is only available in respect of second-hand goods acquired from a non-vendor for the purposes of making taxable supplies. As the right to purchase is not second-hand goods acquired from a non-vendor, but rather, the supply of a service, the vendor is not entitled to the notional input tax deduction.

2.5 Supplies

The term “supply” is widely defined to include performance under any sale, rental agreement and instalment credit agreement whether voluntary, compulsory or by operation of law. Apart from supplies that fall within this definition, the VAT Act also provides for certain events (so-called “deemed supplies”) to be regarded as supplies.

The term “taxable supply” includes all supplies of goods or services made by a vendor in the course or furtherance of an enterprise. VAT must be levied on the taxable supply at either the standard or the zero rate.

On the other hand, an exempt supply is a supply that is not subject to VAT. No output tax must be levied on exempt supplies and input tax may not be deducted on any expenses incurred to make those supplies.

Example 11 – Mixed taxable and exempt supplies

Facts:

XYZ Construction (a vendor) carries on the following activities:

- (i) Supply of construction services;
- (ii) Letting of flats for residential purposes; and
- (iii) Provision of housing to employees for a nominal rental.

What are the VAT implications of the activities carried on by XYZ Construction?

Result:

- (i) Construction services – XYZ Construction must levy VAT at the standard rate on the taxable supply and as such is entitled to deduct input tax on the expenses related to this activity (subject to certain exceptions and limitations).
- (ii) Letting of flats – XYZ Construction must not levy VAT on the rental income received in relation to this exempt activity and will not be entitled to deduct any input tax on the related expenses.
- (iii) Supply of employee housing – the VAT implications are the same as in (ii) above.

In the case of mixed expenses that relate to both taxable and exempt supplies, for example, office administrative expenses, audit fees and other general overheads, XYZ Construction is only entitled to deduct input tax to the extent that goods or services were acquired to make taxable supplies. In other words, XYZ may only claim a portion of the input tax on those mixed expenses. (See 2.7 for a discussion on input tax and apportionment.)

No VAT must be levied on the sale of flats which were previously leased, or which were used for employee housing as these flats would have been used for making exempt supplies.

An issue which is often overlooked, especially in the case of sole proprietors and small businesses, is that the supply of fixed property used partly as a private residence and partly for taxable purposes constitutes a taxable supply. This typically occurs when the type of business allows the vendor to conduct the enterprise either partially or wholly from home. For example, if a spare bedroom, outbuilding or garage is used as a home office.

A vendor is entitled to deduct a fair and reasonable proportion of the VAT incurred on the acquisition of fixed property used for both taxable and non-taxable purposes as well as any allowable expenditure incurred on the general upkeep of the property. When such a property is subsequently supplied, the supply will be taxable at the standard rate and output tax must be accounted for on the full consideration received (see **2.6** and **5.4.6**). However, the portion of tax which was previously denied upon acquisition of the property is allowed as an input tax deduction when the property is subsequently sold.

Example 12 – Taxable supply of property used partly for enterprise purposes

Facts:

Mr D (a vendor) provides construction services to his clients. He uses the study in his home as his office for conducting business and one of his garages for storing construction material. Mr D bought the house in July 2018 from CBA (Pty) Ltd (a vendor) for a VAT-inclusive price of R1 million and deducted input tax on the basis that 20% of the total area of his home, consisting of one garage and the study, is applied for business purposes (taxable supplies). In January 2023, Mr D decides to relocate to Australia and sells his house for R1,3 million.

What are the VAT implications of the sale of the house for Mr D?

Result:

The sale of the property is regarded as a supply made in the course or furtherance of the enterprise carried on by Mr D because part of the house was used for enterprise purposes. The full selling price is subject to VAT at the standard rate and therefore no transfer duty will be payable. Mr D will be entitled to deduct the portion of input tax which he was previously unable to deduct in the tax period in which the sale of the property is declared. This is sometimes referred to as a “claw-back” input tax deduction.

The VAT implications of the transactions in 2018 and 2023 are illustrated below:

2018:

Mr D paid VAT of R130 434,78 ($R1\,000\,000 \times 15 / 115$), which was declared as output tax by CBA (Pty) Ltd, on the acquisition of the house. Based on the floor space method of apportionment, which was considered appropriate (and confirmed by way of a ruling issued by SARS), it was determined that Mr D used 20% of the house for enterprise purposes. Input tax was deducted to that extent as follows:

Input tax = $R1\,000\,000 \times 20\% \times 15 / 115$
 = **R26 086,96**

2023:

In the tax period covering January 2020, Mr D declared output tax on the sale of the property and claimed a “claw-back” input tax deduction (based on the original price) as follows:

$$\begin{aligned}\text{Output tax} &= \text{R1 300 000} \times 15 / 115 \\ &= \text{R169 565,22}\end{aligned}$$

$$\begin{aligned}\text{Input tax} &= \text{R1 000 000} \times 80\% \times 15 / 115 \\ &= \text{R104 347,83}\end{aligned}$$

2.6 Output tax

Output tax refers to the tax levied by a vendor on the taxable supply of goods or services. The output tax is determined by applying the VAT rate to the value of a supply of goods or services. When the amount charged for the supply of goods or services includes VAT (consideration), the output tax is determined by applying the tax fraction to the consideration.⁵ However, this method cannot be used if the special value of supply rule for commercial accommodation, as discussed in 4.4.3, applies.

Example 13 – Property not part of an enterprise*Facts:*

Mrs T is a sole proprietor who is registered for VAT in respect of the tax consulting business which she conducts. She sells her shares in a share block company for R1 900 000 on 25 June 2023. The shares confer a right to use the share block company's property as a place of residence.

Is Mrs T required to levy VAT on the sale of the share block shares (fixed property)?

Result:

Although the shares in a share block company constitute the supply of “fixed property” as defined, the sale thereof by Mrs T falls outside the scope of her enterprise activity. This is because Mrs T used the property concerned as her private residence and not for any enterprise purposes. The sale of the shares in the share block company is therefore not a taxable supply which is subject to VAT. Mrs T must not levy VAT on the sale of the shares. Instead, the purchaser would be liable for transfer duty on the acquisition of the shares in the share block company as these shares constitute “property” as defined in section 1(1) of the Transfer Duty Act.

⁵ If the property is supplied as part of a going concern or as part of a land reform transaction, the value of the supply and the consideration for the supply will be the same amount. Since such transactions do not include VAT at the standard rate, the tax fraction does not apply.

2.7 Input tax

Input tax refers, amongst others, to the VAT paid by a vendor on the acquisition of goods or services that are to be utilised by that vendor either wholly or partly in the course of making taxable supplies. If goods or services are acquired partly for purposes of making taxable supplies, input tax is limited to the extent that the goods or services are acquired for purposes of making taxable supplies.⁶ The VAT incurred in the course of making exempt or other non-taxable supplies does not fall within the definition of input tax.

A vendor may deduct notional input tax on second-hand goods (including fixed property) acquired under a non-taxable supply and applied in an enterprise.⁷ In the case of fixed property, the deduction may only be made once the time of supply, that is the earlier of the date of registration of transfer of the goods or the date any payment in respect of the consideration is made, occurs. In the case of vendors registered on the invoice basis, the deduction may be made once the fixed property is registered in the name of the vendor and is limited to the extent of payment of any consideration made during that tax period.⁸ The deduction in the case of vendors registered on the payments basis, may be made to the extent of payment of any consideration.⁹

A vendor may only deduct input tax in respect of a share in a share block company (which confers a right to or an interest in the use of immovable property) after a signed use agreement has been entered into between the company that operates the share block scheme and the vendor who becomes a member of that share block company.

Input tax may be deducted by a vendor on the acquisition of goods or services for the purpose of making taxable supplies in the circumstances illustrated in **Examples 14 to 18**.

Example 14 – Land acquired wholly for taxable purposes

Facts:

Company A and Company B (both vendors), enter into a sale agreement in terms of which Company A sells land to Company B for R570 000 (including VAT). Company B makes payment of the full purchase price to Company A on 15 April 2022 and the land is registered in Company B's name on the same day. Company B intends to supply this property to Company C.

Determine the amount of input tax that Company B is entitled to deduct and the tax period in which it can be deducted.

Result:

Input tax = R570 000 × 15 / 115
= R74 347,83

⁶ See Binding General Ruling (VAT) 16 "Standard apportionment method" and the *VAT 404 – Guide for Vendors* for more details on apportionment.

⁷ Before 10 January 2012, the notional input tax deduction was limited to the transfer duty paid by the vendor.

⁸ Section 16(3)(a)(ii)(aa) and (bb)(A).

⁹ Section 16(3)(b)(i).

Company B is entitled to deduct input tax of R74 347.830 as the land is acquired in the course of its enterprise. The input tax can be deducted in the tax period covering the month of April 2022 on condition that Company B is in possession of a valid tax invoice. Had Company B made a part-payment instead of the full purchase price, the input tax would be limited to the tax fraction of the part-payment made.

Example 15 – Importation of goods

Facts:

Company A (vendor) leases an office block to Company B and levies VAT at the standard rate. Company A purchases an air conditioner unit from Company C (based in England) which is to be installed in the office block. Company C dispatches the unit to South Africa and Company A pays VAT of R5 000 to SARS Customs upon entry of the goods into South Africa.

What is the amount of input tax that Company A would be entitled to deduct?

Result:

Company A is entitled to deduct input tax of R5 000 as the air conditioner unit is acquired wholly for use in the course of an enterprise. The input tax can be deducted provided that Company A is in possession of the bill of entry (or other prescribed Customs document), the EDI customs release notification together with a receipt for the payment of the VAT issued on eFiling.

Example 16 – Second-hand goods (not being fixed property) acquired from a non-vendor

Facts:

Company A (vendor) supplies office space to tenants in terms of rental agreements. The rentals payable are subject to VAT at the standard rate.

Company A acquired a bakkie from Mr C (a South African resident and non-vendor), for R175 000 on 25 July 2022. The bakkie is acquired exclusively for purposes of maintaining the office blocks. The full amount of R175 000 was paid to Mr C on 25 July 2022.

Determine the amount of input tax that Company A is entitled to deduct and the tax period in which it can be deducted.

Result:

$$\begin{aligned}\text{Input tax} &= \text{R}175\,000 \times 15 / 115 \\ &= \text{R}22\,826,09\end{aligned}$$

As the bakkie was acquired under a non-taxable supply from Mr C for enterprise purposes, Company A will be entitled to a notional input tax deduction to the extent that payment has been made. As payment was made in full, the full amount of input tax can be deducted in the tax period covering the month of July 2022 on condition that Company A is in possession of the relevant documents (VAT 264 etc).

Example 17 – Input tax on fixed property acquired from a non-vendor*Facts:*

Company A (vendor) acquired an office block from Mr C (non-vendor) for R3 million by way of a sale agreement entered into on 11 March 2020. The property is to be used exclusively for making taxable supplies. Company A paid transfer duty of R146 000¹⁰ to SARS on 12 April 2020. On 1 May 2020, the full purchase price was paid to the transferring attorney and registration of the transfer was effected in the Deeds Registry.

Determine the amount of input tax to which Company A is entitled, and the tax period in which input tax can be deducted.

Result:

The input tax deduction is based on the lesser of the consideration given in money or the OMV of the property. This is an anti-avoidance measure to discourage the artificial over-inflation of prices.

$$\begin{aligned}\text{Input tax} &= \text{R3 000 000}^{11} \times 15 / 115 \\ &= \text{R391 304,35}\end{aligned}$$

Company A would be entitled to deduct input tax of R391 304,35 as the office block is acquired for use in the course of making taxable supplies. The deduction of notional input tax can only be made once the time of supply has occurred and is limited to the extent that the consideration has been paid. The time of supply for fixed property is the earlier of the date the transfer of the property is effected in the deeds registry or the date on which any payment is made in respect of the consideration for the property.

Even though payment of the transfer duty was made on 12 April 2020, the input tax deduction will only be permitted –

- in the tax period covering the month of May 2020 as the time of supply only occurred on 1 May 2020 and not in March 2020 when the agreement was entered into; and
- after the property is registered in Company A's name in the Deeds Registry on condition that Company A is in possession of the relevant documents (VAT 264 etc).

Example 18 – Expenses incurred partly for taxable purposes*Facts:*

Company Z owns a building consisting of 20 equally sized apartments. 10 apartments are rented out as residential accommodation, and the other 10 apartments are leased out as office space. The mixed expenses relate to administration cost and maintenance of the building. Each apartment measures 60 m², with the total m² of the building being 1 200 m².

What portion of the mixed expenses is Company Z entitled to deduct as input tax?

¹⁰ $\text{R88 250} + [(\text{R3 m} - \text{R2,475 m}) \times 11\%] = \text{R146 000}.$

¹¹ Note that the transfer duty does not form part of the purchase price of the property. For further explanation in this regard, see Binding General Ruling (VAT) 57 "Whether the term 'Consideration' Includes an Amount of Transfer Duty for the Purposes of Calculating a Notional Input Tax Deduction on the Acquisition of Second-hand Fixed Property".

Result:

Company Z may, provided that the method is appropriate and approved by SARS, be permitted to use a special method of apportionment based on the floor space as follows:

$$\begin{aligned}
 &= \frac{\text{Square metres (m}^2\text{) used for taxable supplies}}{\text{Total floorspace (m}^2\text{)}} \times \frac{100}{1} \\
 &= \frac{600 \text{ m}^2}{1\,200 \text{ m}^2} \times \frac{100}{1} \\
 &= 50\%
 \end{aligned}$$

Based on the above, Company Z will be entitled to deduct 50% of the VAT incurred on the mixed expenses.

2.8 Going concerns

Fixed property which is sold by a vendor will usually attract VAT at the standard rate. However, it is also possible for the fixed property concerned to form part of the supply of a going concern where an entire enterprise and all the necessary assets (including the fixed property) are sold to the purchaser. In such cases, the supply of the whole business, including the fixed property, may qualify as a zero-rated supply. (See Interpretation Note 57 “Sale of an Enterprise or Part Thereof as a Going Concern” which deals with this topic in more detail.)

Example 19 – Sale of business premises and private dwellings

Facts:

Mrs L (a vendor) is a sole proprietor and a successful furniture manufacturer. She realises the potential for her business to grow, but for this to happen, she must move to bigger premises. She therefore decides to sell her factory premises for R4 million and her private residence for R1 million so that she can buy a new home and new business premises in an area where she will be closer to her customers.

Will the sale of Mrs L's business premises and private home be subject to VAT?

Result:

Mrs L carries on an enterprise in relation to the furniture manufacturing business. The supply of the factory premises is subject to VAT at the standard rate as it is supplied in the course or furtherance of her enterprise. As she is selling only her factory premises and not her entire manufacturing business together with the property, the sale does not qualify as a zero-rated going concern. As Mrs L's private residence does not form part of her enterprise, the sale of this property is not a taxable supply and no VAT will be charged. The purchaser will have to pay transfer duty on acquisition of the property, subject to any exemptions or exceptions which may be applicable.

2.9 Commercial accommodation and domestic goods and services

The term “commercial accommodation”¹² includes lodging, or board and lodging supplied together with domestic goods and services in any house, flat, apartment, room, hotel, guest house etc. The total receipts for the supply of such commercial accommodation must exceed or be likely to exceed R120 000 in any consecutive period of 12 months before the activity can qualify as an “enterprise” as defined.¹³ Commercial accommodation also includes lodging, or board and lodging in a home for children, the aged, physically or mentally handicapped persons, or in a hospice. The R120 000 threshold does not apply to these types of accommodation. The supply of office accommodation or residential accommodation in a dwelling under a rental agreement does not constitute commercial accommodation.

“Domestic goods and services” means goods and services provided in any enterprise supplying commercial accommodation, including –

- cleaning services and maintenance;
- electricity, water,¹⁴ gas, air conditioning or heating;
- a telephone, television set, radio or similar article;
- furniture and other fittings;
- meals;
- laundry services; and
- nursing services.

2.10 Person¹⁵

The following entities (amongst others) are regarded as persons for VAT purposes:

- Individuals (sole proprietors, natural persons)
- Public authorities (although these entities are not usually regarded as enterprises)
- Municipalities
- Companies and close corporations
- Deceased and insolvent estates
- Trust funds
- Incorporated body of persons, for example, an entity established under its own enabling Act of Parliament
- Unincorporated body of persons, for example, a partnership, joint venture, club, society or association with its own constitution

¹² See the VAT 411 – *Guide for Entertainment, Accommodation and Catering* and 4.4.3 of this guide for more information about commercial accommodation.

¹³ The threshold before 1 April 2016 was R60 000.

¹⁴ Water was specifically included in the definition of “domestic goods and services” with effect from 1 April 2016.

¹⁵ The definition of “person” excludes a “foreign donor funded project” from 1 April 2020.

2.11 Agency

An agency is a contract under which one person (the agent) is authorised and required by another person (the principal) to contract or to negotiate a contract with a third person, on the latter's behalf. The agent in representing the principal, creates, alters or discharges legal obligations of a contractual nature between the principal and the third party.¹⁶ The agent therefore provides a service to the principal and normally charges a fee (generally referred to as "commission" or an "agency fee") and does not acquire ownership of the goods and/or services supplied to or by the principal.

This agent/principal relationship may be expressly construed from the wording of a written agreement or contract concluded between the parties. If there is no written agreement or contract, the onus of proof is on the agent who seeks to bind the principal in a contract to demonstrate that an agency agreement exists between the agent and another person who is the principal for the purposes of the supply.

In essence, if an agent/principal relationship exists, the principal is ultimately responsible for the commercial risks associated with a transaction, and the agent is trading for the principal's account. The agent is appointed by, and takes instruction from, the principal regarding the facilitation of transactions as per the principal's requirements and generally charges a fee or earns a commission for that service. A person may also act in a dual capacity, for example, if the person acting as project manager (agent for the landowner) is also the civil engineer or architect on that project (no agency arrangement).

Before determining the VAT consequences of a transaction, it is necessary to establish the relationship between the parties. This is to determine if the vendor is acting as an agent on behalf of another person or as principal. Section 54 contains special provisions to deal with the VAT consequences arising from an agency relationship.

If an agent makes a supply on behalf of the principal, it is the principal who must account for VAT on the supply.¹⁷ Likewise, if a supply is made to an agent on behalf of the principal, it is the principal who must deduct the input tax.¹⁸

A common example of a person that acts as an agent in fixed property transactions is an estate agent. The role and function of estate agents is therefore used in the examples below to illustrate the agency principles discussed.

Example 20 – Goods supplied on behalf of a principal

Facts:

ATZ Real Estate Agents (a vendor) acted on behalf of ABC Properties (a vendor) to sell its commercial property. The property was sold to XYZ Retailers for R1 150 000 (including VAT). XYZ Retailers will operate its retail clothing enterprise from the property. ATZ issued a tax invoice to XYZ Retailers reflecting its details and not those of the principal ABC. ATZ also issued a tax invoice for the commission of R115 000 (including VAT) to ABC.

What are the VAT implications for the parties to the transaction?

¹⁶ Also see the Alienation of Land Act 68 of 1981 on the legal formalities concerning the sale of land.

¹⁷ Section 54(1).

¹⁸ Section 54(2).

Result:

ATZ Real Estate

ATZ Real Estate acted as the legal agent of ABC Properties (principal) for the sale of ABC Properties' property. ATZ Real Estate may issue a tax invoice to the purchaser on behalf of ABC Properties for the taxable supply of ABC Properties' property, as if it was a supply made by ATZ Real Estate. ATZ Real Estate is not liable to account for output tax on the sale, as ATZ Real Estate is not the principal in respect of the supply. ATZ Real Estate must maintain sufficient records¹⁹ and submit the required statement in writing to ABC Properties within 21 days of the calendar month in which the supply took place, so that ABC Properties can correctly account for VAT. Furthermore, ATZ Real Estate is required to issue a tax invoice to ABC Properties in relation to agency services supplied to ABC Properties. ATZ Real Estate's output tax liability is R15 000 ($R115\,000 \times 15 / 115$).

ABC Properties

ABC Properties must not issue a tax invoice to the purchaser in relation to the supply of the property as ATZ Real Estate has already issued the tax invoice on ABC Properties' behalf. ABC Properties' output tax liability is R150 000 ($R1\,150\,000 \times 15 / 115$) on the sale of the property. ATZ Real Estate must issue a statement as set out in section 54(3)(a) to ABC Properties. ABC Properties is entitled to an input tax deduction of R15 000 ($R115\,000 \times 15 / 115$) on the commission charged by ATZ Real Estate.

XYZ Retailers

XYZ Retailers is entitled to an input tax deduction of R150 000 ($R1\,150\,000 \times 15 / 115$) in respect of the VAT incurred on the acquisition of the property, being an expense incurred in the course or furtherance of the enterprise provided that the relevant tax invoice is obtained and retained by XYZ Retailers.

Example 21 – Services supplied on behalf of a principal

Facts:

AM Real Estate Agency (a vendor) engages the services of Vendor C to sell property on behalf of the agency. Vendor C is a property broker and a vendor in her own right. In terms of Vendor C's contract, she is an independent service provider (not an employee of AM Real Estate Agency earning "remuneration") and is entitled to a commission of 40% (including VAT) of the VAT-inclusive fee charged by AM Real Estate Agency to its clients.

Vendor C sold the following properties in July 2022 on behalf of AM Estate Agency's clients:

- (a) A commercial property owned by Vendor X was sold for R2,28 million (including VAT) – AM charged a commission of R80 000 (including VAT).
- (b) A residential property owned by Non-vendor Y was sold for R1 million – AM charged a commission of R57 000 (including VAT).

What are the VAT implications for the parties in respect of the sale of the properties?

¹⁹ See 4.2.1.

Result:

Vendor C

As Vendor C is a vendor in her own right and not an employee of AM Estate Agency, she must issue a tax invoice to AM Estate Agency for the commission that she charges on the sale of the two properties amounting to R 54 800 (including VAT) $[(R80\,000 + R57\,000) \times 40\%]$. Vendor C must therefore declare output tax of R7 147,83 $(R54\,800 \times 15 / 115)$ on the commission earned.

AM Estate Agency

AM Estate Agency must issue a tax invoice to each of the sellers on whose behalf the properties were sold as follows:

- (a) Commission of R80 000 (including VAT) for the sale of Vendor X's commercial property.
- (b) Commission of R57 000 (including VAT) for the sale of the residential property of Non-vendor Y.

AM Estate Agency's output tax liability is R17 869,57 $[(R80\,000 + R57\,000) \times 15 / 115]$ in respect of commission earned on the two properties sold by Vendor C. AM Estate Agency may deduct input tax on the commission paid to Vendor C of R7 147,83 $(R54\,800 \times 15 / 115)$ being an expense incurred in the course or furtherance of its enterprise. The input tax may be deducted in the tax period in which Vendor C's tax invoice is received.

Vendor X

The property was sold by AM Estate Agency of behalf of Vendor X. Therefore, Vendor X must account for output tax of R297 391,30 $(R2\,280\,000 \times 15 / 115)$. Vendor X may deduct input tax of R10 434,78 $(R80\,000 \times 15 / 115)$ on the fee paid to AM Estate Agency as it was an expense incurred in the course or furtherance of the enterprise. A tax invoice must be issued to the purchaser either by Vendor X or by AM Estate Agency (acting as agent) for R2 280 000 (including VAT). In this case, AM Estate Agency issued the tax invoice in respect of the sale.

Non-vendor Y

Non-vendor Y is not liable to account for any output tax and may not deduct any VAT incurred to sell the property. The VAT charged by AM Estate Agency is therefore a cost to non-vendor Y. The purchaser will pay transfer duty on the property acquired, subject to any exemption which may be applicable.

Example 22 – Acting in a dual capacity

Facts:

Vendor F (a property development company) engages the services of WEP Engineering to source subcontractors such as builders and electricians for a new property development. WEP Engineering is appointed to carry out the civil engineering work on the project and will also oversee the work of the subcontractors as project manager. WEP Engineering will therefore act as the agent of Vendor F in managing and administering the project in addition to carrying out the civil engineering work as principal. All parties are registered VAT vendors that account for VAT on the invoice basis. During the tax period ending July 2022, WEP Engineering received the following tax invoices on behalf of Vendor F:

- S Electrical – R57 000 (initial circuitry analysis).
- G Landscaping – R22 800 (landscape plans).

WEP Engineering also issued tax invoices for the period to Vendor F in respect of fees for –

- project management – R114 000; and
- engineering work – R456 000.

WEP Engineering was paid for the project management for the period, but only received payment of 50% of the fees relating to the engineering work, as some of the items included in the tax invoice were still being verified by Vendor F.

What are the VAT implications for the parties?

Result:

Subcontractors

S Electrical and G Landscaping must account for output tax of R7 434,78 ($R57\,000 \times 15 / 115$) and R2 973.91 ($R22\,800 \times 15 / 115$) respectively.

WEP Engineering

WEP Engineering must account for output tax of R14 869,57 ($R114\,000 \times 15 / 115$) on the project management fee charged and R59 478,26 ($R456\,000 \times 15 / 115$) on the engineering work invoiced, even though full payment has not yet been received.

As WEP Engineering acted as agent on behalf of Vendor F in managing the project, it is not entitled to an input tax deduction on the fees charged by the subcontractors. It does, however, need to notify Vendor F in writing as required under section 54(3),²⁰ of the details of any supplies received on its behalf from the subcontractors within 21 days of receiving the supplies. WEP Engineering can deduct input tax on the goods or services it acquired as principal in order to provide both the project management and the engineering services to Vendor F.

WEP Engineering must be careful to distinguish between –

- tax invoices for goods or services which WEP Engineering acquired to render services to Vendor F; and
- tax invoices for goods or services acquired for Vendor F where WEP Engineering acted in the capacity of agent for Vendor F.

Vendor F

Vendor F can deduct input tax in respect of the subcontracting fees, the project management fees, and the engineering fees provided the required supporting documents are retained (that is tax invoices and a statement from WEP Engineering).

²⁰ See 4.2.1.

The following amounts will therefore be deductible as input tax:

	R
Electricity circuitry analysis	7 434,78
Landscape plans	2 973,91
Project management fee	14 869,57
Engineering fee	<u>59 478,26</u>
	<u>84 756,52</u>

Since Vendor F is registered to account for VAT on the invoice basis, the full amount of input tax is allowed on the engineering fee even though only 50% of the amount invoiced has been paid (this is subject to Vendor F making full payment within 12 months of the end of the tax period within which the deduction was made).

2.12 Open market value

The “OMV” is defined with reference to section 3 of the VAT Act which sets out the process of determining the OMV of a supply in different circumstances. The OMV is a VAT-inclusive concept and usually needs to be determined with reference to transactions between “connected persons” in certain circumstances, or where there are rules regarding the limitation of input tax. In simple terms, and in the context of supplies of “fixed property”, the OMV is the price (consideration) which could be obtained on the sale of the property between a willing buyer and a willing seller dealing at arm’s length in an open market.

Chapter 3

Interaction between value-added tax and other indirect taxes

3.1 Introduction

This chapter deals with the interaction between VAT and other indirect taxes which could potentially be applicable on a transaction involving fixed property. The other taxes discussed in this chapter include transfer duty, and securities transfer tax (introduced on 1 July 2008).

3.2 Value-added tax vs transfer duty

Transfer duty is an indirect tax imposed on the value of fixed property obtained by any person by means of a transaction as defined in the Transfer Duty Act. A “transaction” is defined to include, amongst other things, transactions under a sale, donation or waiver.

“Property” is defined in section 1(1) of the Transfer Duty Act to mean land in the Republic and any fixtures thereon and includes –

- real rights in land;
- rights to minerals or rights to mine for minerals (including leases or sub-leases pertaining to those rights);
- an interest in a “residential property company”²¹;
- an interest in a holding company (including a close corporation) where that company and all of its subsidiaries would together be regarded as a “residential property company” if it were a single entity;
- certain contingent rights or shares or member’s interests which relate to the use or acquisition of “residential property”²² held in a discretionary trust under certain circumstances; and
- a share in a share block company acquired on or after 1 September 2009.²³

The following rates applied between **1 March 2018 and 28 February 2020**:

All persons	On the first R900 000	0%
	On the value between R900 000 and R1,25 million	3%
	On the value between R1,25 million and R1,75 million	6%
	On the value between R1,75 million and R2,25 million	8%
	On the value between R2,25 million and R10 million	11%
	On the value exceeding R10 million	13%

The following rates apply between **1 March 2020 and 28 February 2023**:

All persons	On the first R1 million	0%
	On the value between R1 million and R1,375 million	3%
	On the value between R1,375 million and R1,925 million	6%
	On the value between R1,925 million and R2,475 million	8%
	On the value between R2,475 million and R11 million	11%
	On the value exceeding R11 million	13%

²¹ As defined in section 1(1) of the Transfer Duty Act.

²² *Ibid.*

²³ For more details in this regard, see the VAT 412 – Guide for Share Block Schemes.

The following rates apply from **1 March 2023**:

All persons	On the first R1,1 million	0%
	On the value between R1,1 million and R1,512 500	3%
	On the value between R1,512 500 and R2,117 500	6%
	On the value between R2,117 500 and R2,722 500	8%
	On the value between R2,722 500 and R12,100 000	11%
	On the value exceeding R12,100 000	13%

For a practical explanation on how to apply the above rates, see the *Transfer Duty Guide* and **Example 23** in this guide.

To ensure that the sale of fixed property is not subject to both VAT and transfer duty, the Transfer Duty Act contains an exemption from transfer duty to the extent that the supply is subject to VAT, irrespective of whether it is subject to VAT at the standard rate or zero-rate. The payment of VAT will therefore normally take precedence over the payment of transfer duty if the supplier is a vendor. However, as mentioned earlier, sometimes the supply of fixed property may be subject to transfer duty even if the seller is a vendor. For example, the sale of a vendor's private residence, or the sale of property used by a vendor for the purposes of employee housing will be subject to transfer duty as these supplies are not made in the course or furtherance of the enterprise carried on by the vendor.

Generally, the sale of a share, or a member's interest in a company or close corporation that happens to own fixed property does not constitute a supply of "fixed property" as defined for VAT purposes, but rather a financial service which is exempt from VAT. The sale of shares in a "residential property company" is, however, subject to transfer duty as such supplies are included in the definition of "property" as defined in section 1(1) of the Transfer Duty Act (see 7.6.2). Similarly, the sale of shares in a share block company on or after 1 September 2009 is subject to transfer duty unless the supply concerned is a taxable supply for VAT purposes.

The sale of any timeshare interest in fixed property or fractional ownership in such property is not regarded as the supply of "shares" and can therefore not be regarded as a financial service for VAT purposes. As timeshare interests and fractional ownership interests fall within the definitions of "fixed property" and "property" as defined in sections 1(1) of the VAT Act and Transfer Duty Act respectively, such supplies will usually be subject to VAT if the supplier is a vendor. If the supplier is not a vendor, or the supply is not in the course or furtherance of the vendor's enterprise, then transfer duty will be payable (subject to any exemptions or exceptions which may apply).

Example 23 – VAT vs transfer duty payable on a transaction

Facts:

Mr P (a vendor) decides to move his business and residence from Pretoria to Cape Town. He therefore sells the property from where his business is conducted for R3,42 million and his private residence for R1,8 million. Both properties were sold on 1 April 2023.

Which taxes apply on the sale of the properties?

Result:

The sale of the business property is subject to VAT at the standard rate as it is supplied in the course or furtherance of Mr P's enterprise ($R3\,420\,000 \times 15 / 115 = R446\,086,96$ output tax). However, as Mr P's private residence was not part of the enterprise, the purchaser will pay transfer duty calculated as follows:

		R
On the first R1,1 million	$0\% \times R1,1 \text{ million} =$	nil
On the value between R1,1 million and R1,512 500	$3\% \times R412\,500 =$	12 375
On the value between R1,512 500 and R1,8 million	$6\% \times R287\,500 =$	<u>17 250</u>
	Total transfer duty =	<u>29 625</u>

Note that Mr P is liable to declare VAT of R446 086,96 as output tax on his VAT 201 return for the tax period covering 1 April 2023 for the sale of the business property, whereas the purchaser is liable to pay transfer duty of R29 625 to SARS in respect of the private residence acquired.

3.3 Value-added tax and securities transfer tax

Share transactions that do not constitute a supply of fixed property and as a result are not subject to either VAT or transfer duty as set out in **3.2**, may be subject to securities transfer tax (STT).

See the **SARS website** for more details on transfer duty, share blocks and STT.

3.4 Contract prices

Section 64 of the VAT Act deems the price charged by a vendor to include VAT, and under of section 65 the price advertised or quoted must include VAT. It is therefore very important that when parties conclude a contract to purchase fixed property, the price should be clearly stated and it should be clear whether VAT or transfer duty is payable.

This is especially important when the transaction is a taxable supply for VAT purposes as any price stated in the contract will be deemed to include VAT if it is silent on the matter.

It is therefore advisable to include a clause in the agreement which deals with the taxes which may be payable, based on the understanding of the parties to the agreement. This will ensure that the agreement is clear on what happens if the parties have agreed on a certain price based on an incorrect assumption as to whether VAT or transfer duty is payable.

In the event that a contractual dispute arises between the parties regarding the purchase price of the property, SARS can merely confirm whether the supply is a taxable supply or not, and the general principle that any price advertised, quoted, stated or charged by a vendor is deemed to include VAT.

Failure to clearly state prices and to deal adequately with VAT and other taxes which may be payable in the contract for the sale of fixed property can often lead to court action.

This is illustrated in the following cases:

- In the case of *Strydom vs Duvenhage NO en 'n Ander*,²⁴ the sale agreement was silent on VAT as it was assumed that the purchaser was liable to pay transfer duty. However, the sale was found to be a taxable supply which was subject to VAT. It was therefore concluded that the stated price in the contract was VAT-inclusive.

The court held that it could not be implied that if the purchaser agreed to pay transfer duty as a separate tax amount over and above the purchase price, that this means that the stated price could be increased by an amount equivalent to the VAT which was payable on the transaction.

- In *Van Aardt vs Galway*,²⁵ the seller leased his farm to the buyer with an option to purchase for a stated price of R700 000. The buyer exercised the option and held the seller to the price of R700 000 inclusive of VAT. The seller tried to withdraw from the contract, arguing that the option was invalid; that the option price implied that it was exclusive of VAT; and that in any event, any VAT liability would be for the buyer's account.

The court held that the option was valid, but did not rule on whether the option price was inclusive or exclusive of VAT. The court took a view similar to the one expressed in *Strydom v Duvenhage* and pointed out that the imputation of an intention to the parties was not necessary to lend business efficacy to the contract. In so doing, the court took the view that it was not able to rule on the matter as it did not have the specific facts relating to VAT. The result being that it was left in the hands of the parties to determine the agreed price and for the VAT legislation to be interpreted within the context of the facts in that regard.

If the sale of a going concern does not meet the requirements of section 11(1)(e), which zero-rates the transaction, the parties often contest whether the purchase price is VAT inclusive or not. It may be found that such contracts describe the sale as a supply of fixed property (subject to VAT at the standard rate) rather than the sale of an enterprise, which happens to have fixed property as part of its assets which are necessary for conducting the enterprise, as a going concern (subject to VAT at the zero rate). For more information on going concerns, see Interpretation Note 57 “Sale of an Enterprise or Part Thereof as a Going Concern” which deals with this topic in more detail.

²⁴ (569/96) [1998] ZASCA 70; 1998 (4) SA 1037 (SCA); [1998] 4 All SA 492 (A) (18 September 1998).

²⁵ (923/10) [2011] ZASCA 201 (24 November 2011).

Chapter 4

Accounting for value-added tax

4.1 Introduction

This chapter is aimed at assisting vendors to correctly account for VAT and deals with situations in which a vendor must issue a tax invoice, as well as the requirements for a valid tax invoice. The terms “output tax” and “input tax” are discussed, as well as time and value of supply rules which determine when and how much output tax and input tax must be accounted for in any particular tax period.

4.2 Tax invoices

Every vendor making taxable supplies of goods or services must, within 21 days of making the supply, issue a tax invoice to the recipient of the supply. To constitute a valid tax invoice, the relevant document must contain the details prescribed in section 20. A vendor may only deduct input tax incurred in the making of taxable supplies if a valid tax invoice or, in certain prescribed circumstances, alternative documentary proof²⁶ containing such information as is acceptable to the Commissioner is obtained and retained to substantiate the deduction. The details on a tax invoice will vary, depending on whether the consideration for the taxable supply (the total amount including VAT) exceeds R5 000 or not.

Since most transactions involving fixed property will be for a consideration exceeding R5 000, a full tax invoice must be issued by the supplier to the recipient containing the following particulars:

- The words ‘tax invoice’, ‘VAT invoice’ or ‘invoice’²⁷
- The name, address and VAT registration number of the supplier
- The name, address and, where the recipient is a registered VAT vendor, the VAT registration number of the recipient
- An individual serialised number and the date on which the tax invoice is issued
- A full and proper description of the goods or services supplied
- The quantity or volume of the goods or services supplied
- Either the value of the supply, the total amount of tax charged and the consideration for the supply; or where the amount of tax charged is calculated by applying the tax fraction to the consideration, the consideration for the supply and either the amount of tax charged or a statement to the effect that it includes a charge for the tax and the rate at which the tax was charged
- The value and consideration denominated in South African Rands (except in relation to a zero-rated supply)

²⁶ Section 16(2)(g).

²⁷ With effect from 1 April 2016, section 20(4)(a) and section 20(5)(a) have been amended to include the words ‘VAT invoice’ or ‘invoice’ and to remove the requirement that these words must appear in a prominent place.

An abridged tax invoice may be issued if the consideration for the supply of goods or services exceeds R50, but does not exceed R5 000. An abridged tax invoice has the same requirements as above, except that the name, address and VAT registration number of the recipient and the quantity or volume need not be specified.

If a vendor is unable to obtain the prescribed documentation under section 16(2)(a) to (f), that vendor may, under section 16(2)(g), apply to SARS for a VAT ruling requesting that alternative documentary proof held by the vendor may be used to substantiate a deduction. The request for the ruling must be made at least two months before the expiry of the five-year prescription period within which a deduction may be made by that vendor. SARS will only issue the ruling if satisfied that –

- the vendor has taken all reasonable steps to obtain the prescribed documentary evidence and is now applying for the ruling as a last resort to resolve the issue;
- the inability of the vendor to obtain and maintain the prescribed documentation was due to circumstances beyond that vendor's control; and
- no other provision of the VAT Act allows for a deduction based on the particular document in the vendor's possession.

4.2.1 Agency

The normal rule is that any tax invoice relating to a supply by, or to the agent, on the principal's behalf should contain the principal's particulars. The VAT Act, however, allows an agent to issue a tax invoice in respect of a supply made on behalf of the principal. In such a case, the agent's details may be reflected on the tax invoice and the principal may not also issue a tax invoice in respect of that same supply. The VAT Act also allows for the agent to be provided with a tax invoice as if the supply is made to the agent.

Should a tax invoice have been issued by or to an agent in the circumstances described above, the agent must maintain sufficient records so that the name, address and VAT registration number of the principal can be ascertained. In addition, the agent must issue a statement to the principal, in writing, within 21 days of the end of each calendar month, notifying the principal of –

- a full and proper description of the goods or services supplied or received;
- the quantity or volume of the goods supplied or received; and
- either –
 - the value of the supply, the amount of tax charged and the consideration for that supply; or
 - where the amount of tax charged is calculated by applying the tax fraction to the consideration, the consideration for the supply and either the amount of tax charged, or a statement that it includes a charge in respect of the tax and the rate at which the tax was charged.

In these circumstances, the agent is required to retain the original tax invoices (if these documents are to be retained on the principal's behalf).²⁸

²⁸ Section 54(3).

Similarly, when an agent imports any goods into the Republic on behalf of a principal, the agent must issue a statement notifying the principal of –

- a full and proper description of the goods imported;
- the quantity or volume of the goods imported; and
- the value of the goods imported and the amount of tax paid on importation of the goods; and
- the receipt number for the payment of such tax issued on eFiling.

4.3 Time of supply

The purpose of determining the time of supply for goods or services is to establish the date that a supply is made for VAT purposes. This is the date that determines the tax period during which the supplier is required to declare the output tax and the tax period that the recipient may be entitled to deduct input tax on goods or services acquired. The output tax and input tax are declared and deducted by a vendor on a VAT 201 return for the tax period which covers the time of supply.

The general rule for time of supply is the earlier of an invoice being issued or payment of the consideration being made. However, the supply of fixed property has a special time of supply rule, which is the earlier of –

- the date of registration of transfer of the property in the Deeds Registry, or
- the date on which any payment in respect of the consideration for the supply is made.

Notwithstanding the special time of supply rule, the supplier of the fixed property will only be required to account for output tax on the supply in the tax period in which payment is received. The term “payment” in this context means any amount received that has the effect of reducing or discharging the obligation relating to the purchase price. In other words, the payment received by the supplier must reduce the amount ultimately owed by the purchaser in respect of the purchase price of the property. Similarly, input tax can be deducted by the recipient to the extent that payment has been made which has the effect of reducing or discharging the obligation relating to the purchase price. This means that vendors account for the VAT on fixed property supplies only to the extent that payment is made. However, this rule does not apply if the supply is between “connected persons” if the recipient is not entitled to a full input tax deduction in respect of the property. (For a discussion on connected persons see **4.4.2.**)

Any payment made into the trust account of an attorney or third party (for example, an estate agent) in respect of a property sale, pending registration of transfer of the property in the name of the purchaser, will not trigger the time of supply. Unless and until the funds are actually at the disposal of the seller and applied as consideration received which reduces or discharges the obligation under the contract of sale for the property, no “payment” has occurred. Consequently, there is no liability to declare output tax, or right to deduct input tax until the funds have been released as “payment” to the seller.

Example 24 – Application of the special time of supply rule*Facts:*

ABC Properties is a vendor that carries on an enterprise as a property developer. It accounts for VAT monthly under the Category C tax period. Mr V signs an agreement to purchase a bachelor flat in one of ABC Properties' newly completed sectional title developments for R570 000 (including VAT) on 25 January 2022. Mr V made a "deposit" payment of R200 000 in cash which was held in Conveyancer C's trust account until Bank S had approved and paid the balance of the purchase price to ABC Properties. The transfer of the property is registered in the Deeds Registry on 29 April 2022. On 30 April 2022, Conveyancer C is advised by Bank S that R370 000 has been paid to ABC Properties. On the same day, Conveyancer C pays the R200 000 "deposit" which was held in trust into ABC Properties' bank account.

What is the time of supply for ABC Properties in respect of the bachelor flat sold to Mr V and how should ABC Properties account for VAT?

Result:

As the transfer of the unit was registered in the Deeds Registry on 29 April 2022 and the full purchase price was paid into ABC Properties' bank account on 30 April 2022, the time of supply is 29 April 2022, being the earlier date. Since ABC Properties has received full payment before the end of the April 2022 tax period, it will be required to account for the full output tax of R74 347,83 ($R570\,000 \times 15 / 115$) in the tax period covering the month of April 2022.

Notes:

1. The date on which the agreement was signed (25 January 2022) is not relevant for VAT purposes. This date would only be relevant if the transaction was subject to transfer duty.
2. Although R200 000 was paid as a "deposit" to Conveyancer C prior to the date of transfer in the Deeds Registry, ABC Properties does not have access to those funds as they are held in trust. The receipt is therefore not regarded as "payment" received by ABC Properties at that stage, as it cannot be applied as consideration towards the reduction or discharge of the purchase price at that time.

Example 25 – Accounting for VAT on partial payment*Facts:*

Assume that in **Example 24** above, Conveyancer C only managed to transfer the R200 000 "deposit" which was held in trust into ABC Properties' bank account on 4 May 2022.

What would the time of supply be for ABC Properties in respect of the bachelor flat sold to Mr V and how should ABC Properties account for VAT?

Result:

As the transfer of the unit was registered in the Deeds Registry on 29 April 2022 which was before the date of the first part payment of R370 000 from Bank S, the time of supply remains 29 April 2022. ABC Properties will, however, only account for VAT on the actual payments received as follows:

Tax period ending April 2020 – Output tax = $R370\,000 \times 15 / 115 = R48\,260,87$
Tax period ending May 2020 – Output tax = $R200\,000 \times 15 / 115 = R26\,086,96$

4.4 Value of supply

4.4.1 General rule

The value of supply of goods or services is the amount on which VAT is charged. Therefore, the value of the supply of goods or services is an amount that excludes VAT. The amount that includes VAT is defined as “consideration”.

This can be illustrated in the formula –

VALUE + VAT = CONSIDERATION <i>therefore</i> CONSIDERATION – VAT = VALUE
--

The VAT Act also contains special value of supply rules which will apply in certain instances instead of the general value of supply rule which has been discussed above. The two most important special rules which require further discussion in this guide are those concerning supplies between connected persons, and certain supplies of accommodation. These rules are discussed in 4.4.2 and 4.4.3 respectively.

4.4.2 Connected persons

The general value of supply rule, discussed in 4.4.1, does not apply if –

- the taxable supply of fixed property (or other goods or services) is made between connected persons;
- the supply is made for no consideration or for a consideration which is less than the OMV;²⁹ and
- the purchaser is either not a vendor, or if registered for VAT, would not be entitled to deduct the full input tax credit in respect of that supply.

In such cases, VAT must be accounted for by the supplier on the OMV of the supply.

Example 26 – Value of supply

Facts:

DEF Properties (a vendor) sells a newly developed residential property to its sole member Mr V for R570 000 (including VAT). Mr V acquired this property to be used exclusively as his primary residence. On the date of sale, the OMV of the property was R1 368 000.

What is the value of supply of the residential property for VAT purposes?

²⁹ Note that the term “open market value” is a VAT-inclusive concept which is dealt with in section 3 of the VAT Act.

Result:

As Mr V (not a vendor) and DEF Properties are “connected persons” in relation to each other, and the property will be used exclusively for residential purposes which is not in the course or furtherance of any enterprise conducted by Mr V, the purchase price cannot be used to calculate the VAT payable as it is less than the OMV.

The value of supply and the VAT are calculated as follows:

$$\begin{aligned}
 \text{Value} &= \text{OMV} - \text{VAT} \\
 &= \text{R1 368 000} - (\text{R1 368 000} \times 15 / 115) \\
 &= \text{R1 368 000} - \text{R178 434,78} \\
 &= \text{R1 189 565,22}
 \end{aligned}$$

Even though the selling price is R570 000, the value of the supply is R1 189 565,22 and the output tax liability to be accounted for by DEF Properties amounts to R178 343,78.

4.4.3 Commercial accommodation

The supply of commercial accommodation means the supply of lodging, or board and lodging together with domestic goods and services which are supplied as part of the accommodation.³⁰ The normal value of supply rules will generally apply for the supply of any commercial accommodation. However, a special valuation rule will apply if the commercial accommodation is supplied for a continuous period exceeding 28 days at an all-inclusive charge, in which case, only 60% of the all-inclusive charge is subject to VAT at the standard rate. See the *VAT 411 – Guide for Entertainment, Accommodation and Catering* for more information on the VAT treatment of commercial accommodation.

Example 27 – Value of supply for commercial accommodation

Facts:

On 1 March 2020, Vendor G (vendor) supplies commercial accommodation in a guesthouse to a customer for an unbroken period of 50 days at a daily all-inclusive charge of R600 (excluding VAT which amounts to R90). The commercial accommodation includes the charge for accommodation, meals and laundry.

What is the value of supply and how much VAT must be charged on the supply?

Result:

$$\begin{aligned}
 \text{Value} &= (\text{All-inclusive charge} \times \text{number of days}) \times 60\% \\
 &= (\text{R600} \times 50 \text{ days}) \times 60\% \\
 &= \text{R18 000}
 \end{aligned}$$

$$\begin{aligned}
 \text{VAT} &= \text{R18 000} \times 15\% \\
 &= \text{R2 700}
 \end{aligned}$$

³⁰ Paragraph (a) of the definition of “commercial accommodation” in section 1(1).

Chapter 5

Adjustments

5.1 Introduction

This chapter deals with situations where a vendor will be required to make an adjustment to input tax or output tax. It explains when adjustments should be made and how the taxable value and the VAT to be declared in respect of the adjustments should be calculated.

Adjustments to input tax or output tax will arise in respect of taxable supplies if, for example –

- an irrecoverable debt is written off by a vendor;
- a debit or credit note is issued or received by a vendor;
- early payment of an account gives rise to a settlement discount;
- a customer returns faulty goods to the supplier; or
- a change in the extent of taxable use or application of goods or services occurs.

5.2 Irrecoverable debts

A vendor that accounts for VAT on the invoice basis may make an input tax adjustment when debts relating to taxable supplies have become irrecoverable, subject to two conditions. Firstly, the debts must relate to taxable supplies made for a consideration in money at the standard rate. Secondly, the vendor must have accounted for the VAT on those supplies in a previous VAT return (that is, the vendor must be accounting for VAT on the invoice basis and not on the payments basis). Once the above requirements are met, the vendor may be entitled to effect an input tax adjustment by applying the tax fraction to the consideration actually written off.

A debt will be considered as irrecoverable if both the following requirements have been complied with:

- The vendor must have done all the necessary entries in the accounting system to record that the amount has actually been written off.³¹
- The vendor must have ceased active recovery action on the debt or handed the debt over to an attorney or debt collector.

The input tax may be deducted in the tax period in which both the abovementioned requirements have been met. If payment in respect of a debt which has previously been written off as irrecoverable is subsequently received, the vendor must declare output tax thereon in the tax period in which the payment is received.

³¹ Note that this does not include any accounting provisions for bad debts. Input tax may only be deducted in respect of those bad debts which the enterprise properly regards as irrecoverable and has actually written them off as such.

Example 28 – Calculation of input tax deduction*Facts:*

Company A (a vendor) leases an office to Mr X for R11 150 (including VAT) per month. Mr X vacated the premises after not paying his rent for three months and being threatened with legal action. Company A has accounted for output tax in its monthly VAT return despite not receiving payment because it is registered on the invoice basis. As a tracing agency confirmed that Mr X had left the country and since the collection costs would be excessive, Company A decides on 1 December 2022 to cease all efforts to recover the outstanding amount and writes the amount off in its accounting records.

Can Company A make an input tax adjustment, and if so, in which tax period can the deduction be made?

Result:

$$\begin{aligned}\text{Adjustment} &= R11\,150 \times 15 / 115 \times 3 \text{ months} \\ &= R4\,363,04\end{aligned}$$

Company A has written the debt off as irrecoverable in December 2022 and may therefore deduct input tax on the irrecoverable debt in the tax period covering that month.

5.3 Debit and credit notes

Situations often arise that necessitate an adjustment to the consideration charged for a supply. The first of these situations is when the adjustment results in the consideration being reduced. This may arise, for example, if a discount is granted or when faulty goods are returned to a supplier and a credit is granted or a refund is made. In these situations the supplier is required to issue a credit note and make an adjustment to output tax, while the recipient of the credit note must make an adjustment to input tax.

The supplier is permitted to account for the adjustment by either deducting the excess amount (deemed to be input tax) or reducing the output tax declared by the amount of the excess. On the other hand, the recipient vendor will be required to repay the amount of the excess. This can be attained in one of two ways. Firstly, the excess amount can be deemed to be tax charged by the recipient in respect of a taxable supply made in the tax period in which the credit note was issued. Secondly, the input tax deducted by the recipient may be reduced by the excess amount.

These adjustments must be accounted for in the VAT return for the tax period in which the decrease in consideration occurs; that is, in the tax period in which the credit note should be issued by the vendor. It should be noted that these adjustments are required, whether or not the credit note or debit note is issued, if it becomes apparent that an incorrect amount of tax has been accounted for.

It is also important to note that if the recipient of the credit note is not a vendor for VAT purposes, the vendor issuing the credit note will only be able to deduct the input tax in the tax period in which the refund is made, or it is applied as a credit for the benefit of that person against any other debts owed.

Example 29 – Decrease in consideration (credit note event)

Facts:

Company A leased an office to Mr X for a monthly rental of R11 500 (including VAT). A tax invoice for the March 2022 rental was issued on 15 March 2022. On 1 April 2022, Company A realised that due to a computer error, it had charged Mr X two months' rent instead of one month. Company A immediately issued a credit note for the amount of R11 500.

In which tax period must Company A make an adjustment in respect of the credit note issued?

Result:

In the tax period covering the month of April 2022 Company A may either:

Deduct input tax = R11 500 × 15 / 115 **Or** Reduce output tax = R11 500 × 15 / 115
= R1 500 = R1 500

Debit notes are issued if, for example, the supplier has undercharged for a supply. When a debit note is issued, the supplier will be required to make an adjustment to output tax and the recipient must make an adjustment to input tax. The amount of the excess is deemed to be tax charged by the supplier in the tax period in which the adjustment is to be made. These adjustments must be accounted for in the VAT return for the tax period in which the debit note is issued by the supplier.

Example 30 – Increase in consideration (debit note event)

Facts:

Company A leases an office for a monthly rental of R11 500 (including VAT). On 1 April 2022, Company A realised that it had not charged the tenant the 10% annual increase in the March 2022 rental and proceeded to issue a debit note for the increase.

In which tax period must Company A declare output tax on the debit note issued?

Result:

$$\begin{aligned}\text{Output tax} &= (\text{R}11\,500 \times 10\%) \times (15 / 115) \\ &= \text{R}150 \text{ in the tax period covering the month of April 2022.}\end{aligned}$$

Remember that the rules discussed above apply to vendors in accordance with the accounting basis which they use to account for VAT. For example, a vendor that is registered on the payments basis will only make the necessary adjustments when payment in respect of the debit or credit note is made or received. Vendors on the invoice basis will account for the debit or credit note upon the issue or receipt of that document.

5.4 Change in use or application

5.4.1 General

A vendor that increases or decreases the use of capital goods or services to make taxable supplies must make an adjustment to output tax or input tax (as the case may be). Similarly, if stock items or capital assets are taken from the business for own use, or applied for exempt or other non-taxable purposes, an adjustment event will arise. An adjustment to output tax will be required when –

- goods or services acquired wholly or partly for making taxable supplies are subsequently applied wholly for private, exempt or other non-taxable purposes; or
- there is a decrease of more than 10% in the extent of taxable use or application by the vendor of capital goods or services which have an adjusted cost of R40 000 or more.

An adjustment to input tax may be permitted when –

- goods or services applied wholly or partly for exempt or private purposes are subsequently applied wholly or partly for making taxable supplies; or
- there is an increase of more than 10% in the extent of taxable use or application by the vendor of capital goods or services which have an adjusted cost of R40 000 or more.

The definition of “adjusted cost” is used for purposes of calculating certain input and output tax adjustments required by, or allowed to, a vendor on any change of taxable use of assets. The effect is that any costs incurred in acquiring the assets which are not VAT inclusive (or deemed to include VAT) are excluded from the formula used to calculate the adjustment. Examples include finance charges (exempt) or labour charges by a non-vendor (no VAT chargeable), and salary and wages incurred in the manufacture, assembly, construction or production of those goods or services.

5.4.2 Change in use from taxable to private or exempt purposes

A vendor that purchases or imports any goods or services (including capital goods or services) for enterprise purposes is required to declare output tax if those goods or services are subsequently used for personal purposes, exempt or out of scope supplies.³² The output tax is calculated on the OMV of the goods or services concerned. An exception to this rule may apply when the property developer temporarily lets newly developed dwellings as exempt residential accommodation whilst continuing with the intention to sell those properties. (See 7.6 for further information in this regard.)

Example 31 – Change in use from taxable to private (non-taxable) purposes

Facts:

Mr A decides to erect four sectional title townhouses on a piece of vacant land which he owns. Since the activity which Mr A intends to conduct is a taxable activity, he may register for VAT voluntarily under section 23(3) at the outset of the project to charge VAT on the sale of the units. Once constructed, three of the units are sold for a VAT inclusive price of R570 000 each, but Mr A decides that he wants to live in the fourth unit instead of selling it.

Calculate the adjustment that should be made.

³² Section 18(1).

Result:

$$\begin{aligned}\text{Output tax adjustment} &= \text{R}570\,000 \text{ (OMV)} \times 15 / 115 \\ &= \text{R}74\,347,83\end{aligned}$$

As Mr A now lives in the unit permanently, he has changed his intention for which the unit is held from a wholly taxable purpose to a wholly non-taxable purpose. If he subsequently sells the unit, the supply will not be in the course or furtherance of his enterprise and will be subject to transfer duty (if any) and not VAT.

5.4.3 Decrease in extent of taxable use of capital goods or services

An adjustment is required to a vendor's output tax if there is a decrease of 10% or more in the extent to which capital goods or services are used or applied in the course of making taxable supplies.³³ This adjustment is made on an annual basis and as a practical arrangement, the adjustment should be done within six months after the financial year-end.³⁴ No adjustment is required if the adjusted cost is less than R40 000 (excluding VAT).

Example 32 – Decrease in extent of taxable use of capital goods

Facts:

Ms S (a vendor) owns several commercial and residential properties which she rents to tenants. She therefore makes both taxable and exempt supplies. In March 2022, she purchased a computer system for R115 000 (inclusive of VAT) which she uses in her business. At the time of purchasing the computer, Ms S derived 80% of her rental income from taxable supplies and 20% from exempt supplies. Ms S elected to use the standard turnover-based method of apportionment and deducted input tax of R12 000 ($15 / 115 \times \text{R}115\,000 \times 80\%$) in the April 2022 tax period, in respect of the computer system acquired.

As at the end of her financial year being February 2023, Ms S determined that her exempt supplies have increased significantly as she has bought and sold several buildings over the past year. As a result, her rental income is now 60% taxable and 40% exempt respectively. At the end of that month the computer system had an OMV of R92 340.

Calculate the output tax adjustment that Ms S is required to make.

Result:

Under section 18(2), Ms S is required to make an adjustment taking into account the decrease in the extent of taxable use of the computer which is determined as follows:

$$A \times (B - C)$$

where –

A represents the lesser of –

- (i) the adjusted cost of the computer, namely R115 000; or
- (ii) the OMV of the computer, namely R92 340;

B represents the extent of taxable use of the computer at the time of the acquisition or in the prior 12-month period, namely, 80%; and

³³ Section 18(2).

³⁴ See paragraph 8.4.3 of the VAT 404 – Guide for Vendors

C represents the extent of the taxable use of the computer during the current 12-month period, namely, 60%.

$$\begin{aligned}\text{Adjustment} &= \text{R}92\,340 \times (80\% - 60\%) \text{ or } \text{R}92\,340 \times 20\% \\ &= \text{R}18\,468\end{aligned}$$

$$\begin{aligned}\text{Output} &= \text{R}18\,468 \times 15 / 115 \\ &= \text{R}2\,408,87\end{aligned}$$

Ms S must therefore declare output tax of R2 408,87 in block 12 of her VAT 201 return within a period of six months after the financial year-end.

5.4.4 Change in use from non-taxable to taxable purposes

A vendor will be permitted an input tax deduction when goods or services are held for exempt or private purposes, and subsequently applied by the vendor for consumption, use or supply in the course of making taxable supplies.³⁵ However, no deduction is allowed if an input tax deduction is specifically denied. The deduction may be made in the tax period in which the goods or services are applied by the vendor for taxable purposes. The input tax is calculated by applying the tax fraction to the lower of the adjusted cost (including VAT) or the OMV of the goods or services and is limited to the extent that the goods or services are intended for taxable use. The full adjustment is made in the tax period in which the change in use occurs, whether the vendor accounts for VAT on the invoice or payments basis.

Example 33 – Change in use from private to taxable purposes

Facts:

Mr Q, a building contractor and vendor, purchases a single cab bakkie for private purposes on 1 March 2022. The bakkie costs R228 000 (including VAT) and excludes finance charges. A year later, on 1 April 2023, Mr Q decides to use the bakkie exclusively in his business for purposes of transporting his building equipment to the various building sites. At the time of introducing the bakkie into the business, it had an OMV of R205 200.

How much input tax will Mr Q be entitled to deduct?

Result:

$$\begin{aligned}\text{Input tax:} &= \text{R}205\,200 \times 15 / 115 \\ &= \text{R}26\,765,22 \text{ in the April 2023 tax period.}\end{aligned}$$

³⁵ Section 18(4).

5.4.5 Increase in extent of taxable use or application of capital goods or services

An input tax adjustment may be made by a vendor if there is an increase of 10% or more in the extent to which capital goods or services are used or applied in the course of making taxable supplies.³⁶ This adjustment is made on an annual basis and as a practical arrangement, the adjustment should be done within six months after the financial year-end.³⁷ The adjustment is not required if the adjusted cost is less than R40 000 (excluding VAT).

Example 34 – Increase in extent of taxable use of capital goods

Facts:

Assume the same facts in **Example 32** regarding Ms S whose financial year-end is February, except that:

- She initially derived 60% of her income from taxable supplies and 40% from exempt supplies at the time that she purchased the computer system; and
- As a result of the buildings that she had bought and sold over the past year, her rental income is now 80% taxable and 20% exempt.

Calculate the input tax adjustment that Ms S may make in the February 2020 tax period.

Result:

The adjustment which may be made to take into account the increase in the extent of taxable use of the computer is determined by the formula:

$$A \times B \times (C - D)$$

where –

- A represents the tax fraction 15 / 115;
- B represents the lesser of –
 - (i) the adjusted cost of the computer, namely, R115 000; or
 - (ii) the OMV of the computer, namely R92 340;
- C represents the extent of taxable use of the computer during the current 12-month period (80%)
- D represents the extent of the taxable use of the computer at the time of acquisition or in the prior 12-month period (60%).

$$\begin{aligned} \text{Adjustment} &= 15 / 115 \times R92\,340 \times (80\% - 60\%) \\ &= 15 / 115 \times R92\,340 \times 20\% \\ &= R2\,408,87 \end{aligned}$$

Ms S may deduct an additional R2 408,87 as input tax in block 18 of her VAT 201 return for within six months after the financial year-end.

³⁶ Section 18(5).

³⁷ Section 18(6) deems the supply to take place on the last day of the vendor's "year of assessment" as defined in section 1(1) of the Income Tax Act 58 of 1962 or the last day of February if the vendor is not a taxpayer. Note, however, the practical arrangement that applies here.

5.4.6 Subsequent sale or disposal of goods or services partly applied for taxable supplies

The vendor is required to account for output tax on the full consideration for the supply when a vendor acquires goods or services which are used partly for making taxable supplies and subsequently supplies those same goods or services. The vendor is entitled, in these circumstances, to deduct the VAT paid on the acquisition of the goods or services that was previously disallowed.³⁸ The adjustment must be made in the tax period in which the goods or services are supplied, regardless of whether the vendor is on the invoice or payments basis. This is generally referred to as a “claw-back” of input tax. If the vendor sold fixed property before 10 January 2012, the deduction would be limited to the transfer duty paid if the fixed property was acquired from a non-vendor.³⁹

Example 35 – “Claw-back” input tax adjustment

Facts:

Mr Z purchases a building on 10 June 2018 consisting of an office and a residential flat for a consideration of R1,15 million (including VAT). The building is used 60% for exempt supplies (rental of residential flat) and 40% for taxable supplies (rental of office). On 15 July 2022, Mr Z sells the building for R1,71 million (including VAT).

What is the VAT treatment of the above transactions?

Result:

10 June 2018

The apportionment percentage was determined by using the turnover-based method at the time of acquisition. The vendor deducted input tax of R60 000 ($[(15 / 115 \times R1\ 150\ 000) \times 40\%]$).

15 July 2022

Mr Z is required to account for output tax of R223 043,48 ($R1\ 710\ 000 \times 15 / 115$) on this transaction.

An input tax credit for the portion of VAT previously disallowed (60% used for exempt supplies) may be deducted in the same VAT return.

The adjustment is determined by the formula:

$$A \times B \times C$$

where –

A represents the tax fraction, namely $15 / 115$;

B represents the lesser of –

(i) the adjusted cost of the building, namely R1 150 000; or

(ii) the OMV of the building, namely R1 710 000; and

³⁸ Section 16(3)(h).

³⁹ Section 16(3)(h) proviso (i) was deleted with effect from 10 January 2012.

C represents the extent of the exempt use of the building before its sale by the vendor (that is, 60%).

$$\begin{aligned}\text{Input tax adjustment} &= [\text{R}1\,150\,000 \times 15 / 115] \times 60\% \\ &= \text{R}90\,000\end{aligned}$$

5.4.7 Change in use upon acquisition of a going concern

An adjustment must be made if a recipient acquires a going concern at the zero rate and the enterprise or part thereof is subsequently used for non-taxable purposes.⁴⁰ The value of the supply is the cost to the recipient, to the extent that it is acquired for non-taxable purposes. The recipient of the zero-rated going concern must therefore declare output tax on this non-taxable part of the going concern.

No adjustment is required if part of the going concern that will be used for taxable supplies is equal to not less than 95% of the total intended use.

Example 36 – Change in use adjustment by the recipient

Facts:

Vendor A (an individual) acquires a small guesthouse enterprise for R4 million from Vendor B as a going concern during May 2022. The sale includes all the assets which are necessary for conducting the business, including the property on which the guesthouse is situated. The guesthouse has 10 identical units and all the requirements of a going concern have been complied with to allow the transaction to be zero-rated under s 11(1)(e). However, Vendor A will live in one of the units and it will therefore no longer be made available to guests.

Calculate the output tax adjustment which must be made by Vendor A.

Result:

$$\begin{aligned}\text{Output tax} &= ((\text{R}4\,000\,000 \times 1 / 10) \times 15\%) \\ &= \text{R}60\,000\end{aligned}$$

⁴⁰ Section 18A.

Chapter 6 Construction

6.1 Introduction

As mentioned in **Chapter 1**, there are various role-players in the construction industry. These persons include, for example, the landowner of the fixed property, estate agents, contractors (main and subcontractors) that carry out the building works, as well as architects, engineers and qualified professionals that certify payment certificates (hereinafter referred to as “third party quantity surveyors”). This chapter focuses on the various services in respect of the construction of buildings on fixed property and the VAT implications thereof.

6.2 Relationship between landowner and contractor

Architects and engineers are involved in the drawing up of plans, surveying the property and other activities in preparation for the construction of buildings on fixed property. They may also act as project managers and be involved in the preparation of the contract documentation, issuing instructions, overseeing that the construction is carried out according to specifications, and certifying payments due to the contractors. Project managers may also act in different capacities. For example, a vendor who is an engineer may render engineering services and project management services to a landowner in respect of the same project. Further, the project manager might also be given the power to act as the landowner’s agent in concluding contracts with subcontractors, or this may be done by the main contractor as an implicit part of the responsibilities of the job. Sometimes the main contractor may also take on the role of the project manager and in other cases, these tasks are carried out by separate parties. It is therefore very important to establish the contractual relationship between the parties and the role that each party plays in executing the construction contract as this will determine whether input tax may be deducted, or if output tax must be declared by any of the parties in any given situation.

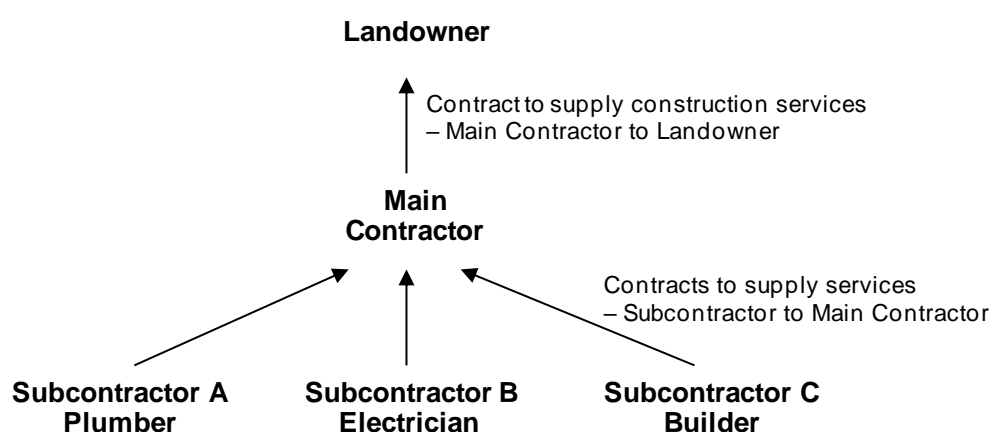
Sometimes, a joint bid is submitted encompassing a variety of contractors that will attend to specified components of the work which is to be performed. For example, one contractor could erect the building and another could carry out the electrical installation. Such a bid may be made by the parties through a joint venture company or partnership which has been formed for the purpose of carrying out the project. In such a case, the joint venture company or partnership, which is a separate person from the participants in the project, must be separately registered for VAT purposes if the requirements for registration are met. One of the factors in deciding if the entities concerned are liable to register as a body of persons will be whether they co-operate with each other in respect of the building operations and share in profits and expenses of the joint operations. If the entities share in profits, it is likely that the contractors will be regarded as a body of persons which is liable to register for VAT separately from the entities participating in the arrangement. If the project is to be carried out under a “Public Private Partnership Agreement” as defined in Regulation 16 of the Treasury Regulations (issued under section 76 of the Public Finance Management Act 1 of 1999), each party to that agreement will be a “designated entity” as defined in section 1(1). There are special rules in the VAT Act which apply to vendors that fall within the definition of “designated entity”.

It is essential that the relationship between the landowner and the various contractors be established to ensure that each party correctly accounts for VAT. Although there are many different possibilities and scenarios in the construction industry which will determine the relationship between the applicable parties, two common arrangements are discussed in **6.2.1** and **6.2.2** to illustrate the VAT implications of the activities carried on.

6.2.1 Landowner contracts only with main contractor

In this situation, the landowner enters into a building contract with the main contractor and each of the subcontractors has a contractual relationship with the main contractor. The landowner looks to the main contractor for due compliance with the building contract and there is no contractual relationship between the landowner and the subcontractors. The main contractor therefore acts as a principal, and not as agent, in supplying construction services to the landowner.

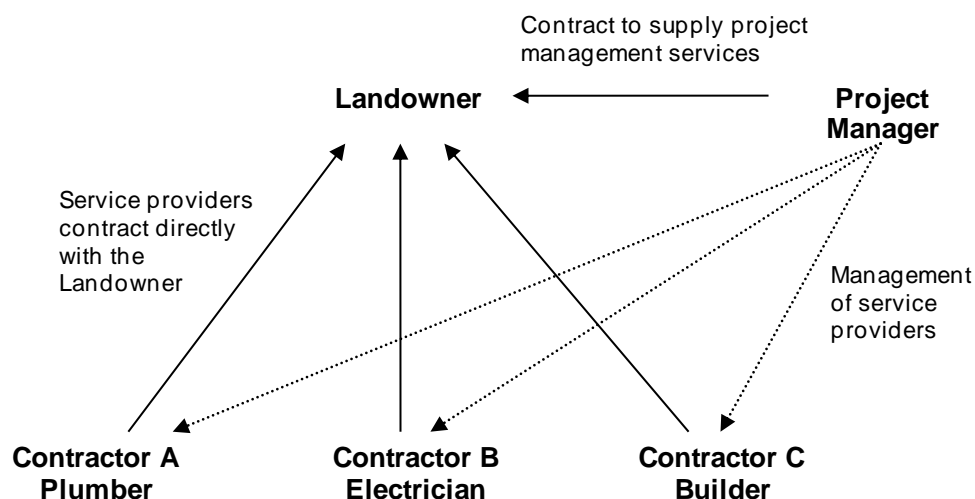
The various subcontractors issue tax invoices to the main contractor for goods or services supplied to the main contractor. The main contractor, in turn, deducts input tax on these acquisitions and issues a tax invoice to the landowner for any goods or services that have been supplied to the landowner under the building contract for the period concerned and accounts for output tax thereon. This type of arrangement is illustrated below.



6.2.2 Landowner contracts directly with various contractors

Under this arrangement, the landowner contracts directly with the various contractors. There is accordingly no main contractor as the services of the individual contractors are supplied directly to the landowner. The various contractors must issue tax invoices directly to the landowner for the landowner to deduct the input tax.

The landowner may also appoint a project manager to manage the project but will still contract with the individual contractors directly to supply goods and services. In such a case, the contractors and the project manager must issue tax invoices directly to the landowner for the landowner to deduct the input tax. This type of arrangement is illustrated on the next page:



Once the construction is completed, the landowner may employ the services of an estate agent to market the units and conclude the sale contracts on the landowner's behalf. In return, the estate agent will receive a commission (see **Example 20**).

6.3 Construction services

This paragraph examines the VAT implications that contractors and subcontractors will have to observe when preparing their bids, as well as the requirements that must be met once the bid has been awarded. In the rest of this chapter, the VAT implications of certain events arising at the various stages in the construction process are discussed. Ancillary services, such as the services supplied by estate agents, are also briefly discussed.

6.3.1 Pre-tender stage

Registration as a vendor

As indicated in **2.2**, if a person makes taxable supplies in excess of R1 million in any consecutive 12-month period or will exceed that amount in terms of a contractual obligation in writing, that person is required to register for VAT.

Tendering for work with government departments, public entities and municipalities, often requires that a bidder must submit a tax clearance certificate. As a result, there has been a tendency for bidders to register for VAT solely in anticipation of being awarded a contract. In these circumstances, the bidder (if not already registered for VAT) in anticipation of being awarded the contract, may only apply for voluntary registration if the requirements under section 23(3) are met. The bidder will be required to register once the contract is awarded, and the value of taxable supplies in terms of the contract will exceed R1 million in a consecutive 12-month period. (See **2.2**). It is thus important to ensure that the possible VAT registration liability of the bidder be adequately considered when agreeing on the contract price, and that both parties are aware of, and agree to, the impact of a VAT registration on the contract price.

Setting prices

Once the contractor, that is already a vendor, has elected to submit a tender, the next issue to consider is the pricing of the goods or services to be supplied in line with the tender requirements.

In setting the price, the contractor has an option to either –

- include the VAT amount in the contract price, in which case the quote must include a statement that the price includes VAT at the standard rate; or
- state separately, and with equal prominence, the contract price excluding VAT, the VAT amount and the contract price including VAT.

Example 37 – Quoting of prices in tender documents*Facts:*

X Plumbers CC (vendor) is invited to tender for the supply and installation of toilets, baths and washbasins in a block of flats.

How should X Plumbers CC show the costing on the tender?

Result:

The costing for the tender (including the mark-up on costs) could read as follows:

<u>Tender: X Plumbers CC</u>	<u>R</u>
Materials (excl. VAT)	50 000
Labour	<u>15 000</u>
Sub-total:	65 000
Add VAT @ 15%	<u>9 750</u>
TOTAL (including VAT):	<u>74 750</u>

If the quoted price by a vendor does not contain a statement to the effect that the price is inclusive of VAT, the price will be deemed to include VAT. If a person is not a vendor at the time that the bid or quote is submitted, but later applies to be voluntarily⁴¹ registered as a vendor, the person may quote the price inclusive of VAT, with a statement that such price is subject to the bidder becoming a VAT vendor. (See 3.4.).

Example 38 – Prices quoted are deemed to include VAT*Facts:*

In terms of a written contract entered into on 1 January 2022, a contractor (vendor) accepts a job to carry out renovations to a factory for the sum of R100 000. The contract is silent on whether VAT is included in the quoted price.

On what amount must the contractor account for output tax?

⁴¹ Generally, a person can only register as a vendor once a tender has been awarded. However, a person can register voluntarily under section 23(3) subject to certain requirements being met.

Result:

$$\begin{aligned}\text{Output tax} &= \text{R}100\,000 \times 15 / 115 \\ &= \text{R}13\,043,48\end{aligned}$$

This is because the contract price of R100 000 is deemed to be inclusive of VAT.

It is also important for vendors to note that when calculating prices to be included in a bid or tender document, the VAT paid or payable on goods or services which are acquired in the course of performing the work is not a “cost” from an accounting or economic point of view. This is because the VAT may be deducted as input tax if the goods and services are acquired for taxable purposes and the documentary requirements are met, for example a valid tax invoice is retained.

6.3.2 Contract stage

Once the bid has been accepted and the contract awarded, a building contract between the landowner and the contractor comes into existence. However, the nature of building contracts will usually necessitate the appointment of subcontractors. (See **6.2** for a discussion on the relationship between the landowner and a contractor.) Once the appointments are made, work commences and the contractors are paid for work done, usually based on the progress made in relation to the completion of the building.

Time of supply

The general time of supply rule as discussed in **4.3** is the earlier of the date of the invoice or the date of payment of any part of the price. Construction services are, however, subject to a special time of supply rule under section 9(3)(b). In terms of this rule, the goods or services are treated as being supplied periodically or successively in relation to the progressive nature of the work that has to be carried out in terms of a construction contract.

What this means is that construction services or progressive supplies in relation to the construction of a building which are invoiced on a periodic basis, are deemed to be supplied successively. Each progressive or successive supply is deemed to take place whenever any payment in respect of that supply becomes due, is received, or any invoice relating only to a specific payment is issued, whichever is the earlier. This allows for VAT to be collected and accounted for periodically during the term of the contract in respect of each portion of the work completed. This special rule also overrides the special time of supply rule which applies for certain supplies between connected persons.

Generally, the way in which the construction industry works is that the contractor first drafts a certificate of payment which is submitted to a third party, for example, the project manager, engineer or architect, for certification. The obligation to pay for the work invoiced only becomes unconditional upon certification of the amount due. In view of this, the time of supply is only regarded as having occurred once the claim is certified by the third party. It should, however, be noted that the contractual terms regarding payments will inform the time of supply.

Escalations

Increases in the cost of materials or labour during the contract or variations to the original contract will be included in the certificate of payment and the VAT in respect thereof will become payable at the same time as the other completed work on the contract.

Retentions

The building contract will normally make provision for retentions, which means that some part of the contract price may be withheld by the recipient of the goods or services from until certain conditions are met. Retentions are usually employed as a means of ensuring that the construction work is done according to agreed timeframes, specifications, and standards. Retentions are normally payable at a later stage once the recipient is satisfied with the quality of the completed work and the timeframe within which it was completed.

The contractor will only be required to account for output tax on the retention amount at the earlier of the date that –

- an invoice is issued for the retention amount; or
- the retention amount becomes due for payment; or
- the retention amount is recovered by the contractor from the recipient.

Bonuses

The contract may provide for the payment of bonuses upon early completion of the project or at any stage thereof. The payment of bonuses attracts VAT in the same way as any other component of the contract price. If the contract is silent, the bonus will be deemed to include VAT. (See 7.4.)

Penalties

A building contract could make provision for the payment of so-called “penalties” if the contractor fails to adhere to the scheduled building timelines. The wording of the contract could stipulate that the penalty may either be a lump sum or a set amount per day or other period of time. The effect hereof is the reduction of the contract sum agreed upon between the landowner and contractor, and consequently, a reduction of the value upon which VAT must be levied. (See 6.4.2.)

The landowner may reduce the contract fee with such penalties during the course of the building work. The penalty amount is usually determined with reference to the retention amount which the recipient withholds upon completion of the project. Other penalties as agreed in the contract may also be applicable, but it should be noted that the set-off of the penalties against the agreed contract price does not necessarily indicate a reduction in the taxable contract fee. Depending on the terms of the contract the penalty could represent a reduction of the agreed contract fee, in which case the value of the supply is reduced and VAT must be accounted for on the reduced amount. Alternatively, the penalty could be a payment which is not in relation to a taxable supply of goods or services and as such not subject to VAT.

Example 39 – Penalty for late completion

Facts:

The agreed contract price for construction services is R115 000 (including VAT). A late completion penalty of R10 000 (including VAT) was incurred by the builder and as per the agreement, is regarded as a reduction in the contract price.

How much output tax must be declared?

Result:

The VAT payable on the contract is as follows:

	R
Original contract price	115 000,00
Less: Penalty	<u>10 000,00</u>
	<u>105 000,00</u>
VAT (R105 000 × 15 / 115)	<u>13 695,65</u>

A credit note must be issued and an input tax adjustment should be made for the difference in VAT on the amount of R10 000 in the next VAT return, if the builder has already issued an invoice and accounted for the full amount of VAT on the original price.

6.4 Tax invoices, debit notes and credit notes

6.4.1 Tax invoices

Generally, a vendor is only entitled to deduct input tax if a valid tax invoice is retained. (See the *VAT 404 – Guide for Vendors*.) As stated in **6.3**, the building contract generally makes provision for the certification of the work to be undertaken before payments will be made. The contractor will, therefore, submit a progress payment to a third party such as a quantity surveyor or architect, and the latter would certify the work done. The third party can certify these items on the contractor's invoice for a progress payment or issue a certificate stating the amount to which the vendor is entitled. In order for the documents referred to above to constitute valid tax invoices that the recipient can use in order to deduct input tax, the requirements of section 20(4) must be met. Amongst others, the document must contain the words "tax invoice", "VAT invoice" or "invoice". Furthermore, it must contain the name, address and VAT registration number of the contractor and either the name and address of the recipient (for example, the landowner, or the main contractor) or the name and address of the third party acting as agent on behalf of the recipient. In the latter case, the third party will be required to maintain sufficient records to enable the name, address and VAT number of the recipient to be ascertained (see **Chapter 4**).

Should the documents concerned fail to comply with the requirements of section 20(4), the supplier is obliged to issue a valid tax invoice by means of a separate document. It should be noted that a supplier must issue a tax invoice to the recipient of the supply within 21 days of the time of the supply.

The subcontractor and the main contractor can agree that the main contractor may use self-invoicing. For the requirements to adopt a self-invoicing procedure, see BGR 15.

Whether or not a document constitutes a valid "tax invoice" or not, does not influence the period in which the supplier must account for output tax on a supply. Special time of supply rules apply to construction if the consideration becomes due and payable in instalments or periodically (successive or progressive supplies). Each successive or progressive supply is deemed to take place when payment is due, received or an invoice (a document notifying an obligation to make payment) relating to that payment is issued, whichever is earlier.⁴²

⁴² Refer to section 9(3)(b).

6.4.2 Debit and credit notes

If a tax invoice was issued in respect of a supply and there is a subsequent adjustment to the consideration, an incorrect amount of VAT would have been accounted for by the parties. A debit or credit note (as the case may be) will therefore have to be issued to correct the position. (See 5.3.)

If the contractor has accounted for a greater amount of output tax than the actual tax due, the contractor will have to issue a credit note to the landowner. In accounting for these adjustments, the contractor can either increase the input tax deduction by the excess amount or reduce the output tax for such tax period by the amount of the excess. On the other hand, the landowner will have to either increase output tax or reduce the input tax deduction in the period in which the credit note is issued.

Example 40 – Over-payment of output tax

Facts:

ABC Contractors submitted a progress payment claim for R100 000 and accounted for the output tax of R13 043,48 $[(R100\,000 \times 15 / 115)]$ in the tax period ending April 2022. However, the architect was not available at the time to certify the amount. The client agreed to pay the full amount subject to the architect's certification at a later stage. The architect later determined that payment of only R70 000 was due, based on the work completed at that stage and that the balance of R30 000 was to be refunded.

How should the difference be dealt with?

Result:

$$\begin{aligned}\text{Adjustment} &= R30\,000 \times 15 / 115 \\ &= R3\,913,04\end{aligned}$$

ABC Contractors is entitled to make the necessary adjustment as too much output tax would have been declared. This adjustment is made by increasing its input tax deduction by R3 913,04 (R13 043,48 less R9 130,43) in the period the architect certified the work completed. ABC Contractors will further be obliged to issue a credit note to the client who is required to declare output tax on the same amount.

6.5 Professional Services

The fees invoiced by project managers, architects and estate agents (if they are VAT vendors), are subject to VAT at the standard rate. VAT charged on goods or services acquired from these vendors may be deducted as input tax, provided the relevant tax invoices are held. The deduction is, however, limited to the extent the goods or services are acquired for taxable purposes, and the amount and period in which the deduction can be made depend on whether the vendor is registered on the payments or invoice basis of accounting for VAT.

The time of supply in respect of goods or services supplied progressively or periodically to contractors is deemed to take place at the earlier of the date that –

- each progress payment becomes due in terms of the agreement;
- each progress payment is received; or
- any invoice relating to that payment is issued.

The general time and value of supply rules will apply when goods or services are not supplied by third party suppliers on a progressive basis. For example, if a vendor is contracted to supply a geological surveying service these supplies take place at the earlier of the time that an invoice is issued, or the time that any payment of consideration is received by the supplier of the service. (See **4.3**).

Chapter 7

Developers and speculators

7.1 Registration

Developers and speculators continuously or regularly develop and sell fixed property in the normal course of conducting business. It follows, that these activities fall within the ambit of an enterprise (see 2.1 for a discussion on the carrying on of an “enterprise”). When the income from conducting such a business exceeds the compulsory VAT registration threshold⁴³ or will exceed that amount in terms of a contractual obligation in writing, the developer or speculator will be required to register as a vendor. The developer or speculator may also choose to voluntarily register for VAT.⁴⁴ Developers and speculators in fixed property that are registered for VAT will therefore charge VAT on all taxable supplies made and will be entitled to input tax on the VAT-inclusive costs incurred in the course of developing and selling fixed property. Taxable supplies in such cases may also include, for example, the rental of office space, the sale of scrap or excess building materials, or the supply of labour.

All references to the terms “property developer” or “developer” in this chapter apply equally to property speculators, except for 7.6 where the term “developer” is specifically defined for VAT purposes in the context of temporary letting and excludes property speculators.

7.2 Input tax

A developer is entitled to deduct input tax in respect of the acquisition of goods or services for the purpose of making taxable supplies, provided that the required documentation is held. A vendor may also deduct notional input tax if second-hand goods (which were not subject to VAT) are acquired for taxable purposes, for example, when property is bought from a non-vendor (see 2.7). Typically, a property developer in fixed property may, amongst others, deduct input tax in relation to the following types of supplies:

- Acquisition of fixed property
- Development (building) costs
- Professional services, for example, payments made to architects and engineers
- Marketing costs, including estate agency fees, advertising expenses, and so on

7.3 Output tax

Once the fixed property is developed and advertised for sale, the developer must make sure that any prices quoted or advertised, are inclusive of VAT. The developer must account for output tax on each sale.

Example 41 – Accounting for VAT

Facts:

ABC Properties Limited is a vendor and its main activity is the development and sale of sectional title residential units. It acquired a piece of vacant land from a private person for R1 million and paid transfer duty of R12 000 on 15 January 2022.

⁴³ Currently the compulsory VAT registration threshold is R1 million in any consecutive period of 12 months.

⁴⁴ Section 23(3)(b).

The transfer was registered on 1 March 2022 at which point the purchase price was settled with the seller.

ABC Properties Ltd's intention was to develop 100 sectional title units on the vacant land and to sell each unit individually for R570 000 (including VAT). To complete the project, it appointed CB Builders to build the units at a cost price per unit of R342 000 (including VAT). ATZ Real Estate was appointed as the estate agents who will market and sell the units.

On 1 April 2022, CB Builders issued a tax invoice for R34,2 million (including VAT) to ABC Properties Ltd for the completion of the development. On 1 June 2022, ATZ Real Estate sold the entire development for R57 million (including VAT) to a property investment company XYZ Investments that intends letting out the units as dwellings. On 2 June 2022, ATZ Real Estate issued a tax invoice to ABC Properties Ltd for R5,7 million, being a commission of 10% (including VAT) on the VAT exclusive selling price of R50 million.

What is the VAT liability of each party involved in the above transactions?

Result:

ABC PROPERTIES LTD			
Description	Output tax / input tax	Tax Period	Output / input
Acquisition of vacant land for R1 million	Input tax must be in possession of a tax invoice or in certain prescribed circumstances, alternative documentation acceptable to the Commissioner $(R1\,000\,000 \times 15 / 115) = R130\,434,78$	March 2022	(R130 434,78)
CB Builders development costs	Input tax must be in possession of a tax invoice or in certain prescribed circumstances, alternative documentation acceptable to the Commissioner $(R34\,200\,000 \times 15 / 115)$	April 2022	(R4 460 869,57)
Sale of sectional title units to XYZ Investments	Output tax $(R57\,000\,000 \times 15 / 115)$	June 2022 (as the date of payment is the earlier of date of invoice or registration)	R7 434 782,61

Commission paid to ATZ Real Estate	Input tax must be in possession of a tax invoice or in certain prescribed circumstances, alternative documentation acceptable to the Commissioner (R57 000 000 × 15 / 115)	June 2022	(R743 478,26)
CB BUILDERS			
Description	Input / output tax	Tax Period	VAT output / (input)
Development / building services supplied to ABC Properties Ltd	Output tax (R34 200 000 × 15 / 115)	April 2022	R4 460 869,57
ATZ REAL ESTATE			
Description	Input / output tax	Tax Period	VAT output / (input)
Commission charged for services rendered to ABC Properties Ltd	Output tax (R5 700 000 × 15 / 115)	June 2022	R743 478,26
XYZ INVESTMENTS			
Description	Input / output tax	Tax Period	VAT output / (input)
Purchase of sectional title residential units from ABC Properties Ltd	Input tax Nil (not entitled to deduct input tax as the sectional title units are acquired to make exempt supplies that is residential letting)	Not applicable	Nil

7.4 Advertising or quoting prices

Any price advertised or quoted in respect of the taxable supply of fixed property by a vendor, must include VAT and must be shown as follows:

- A statement in the advertisement or quotation that the price includes VAT; or
- Indicating or quoting the price excluding VAT whilst also disclosing the amount of VAT and the price including VAT with equal prominence. (See 3.4.)

It is an offence, punishable by law, to advertise VAT-exclusive prices. A vendor may also not state or imply that any form of trade, cash or any other form of discount or refund is in lieu of the VAT that is chargeable on a supply. Apart from being illegal, such statements mislead the public into believing that it is possible to escape paying the VAT on a transaction.

7.5 Land reform and land restitution

The government's Land Reform Programme is made up of the following principal focus areas:

- *Land Redistribution* – to provide the landless indigent, labour tenants, farm workers, women, and emerging farmers with access to purchase land for residential and productive uses.
- *Land Restitution* – to restore land and provide other restitution remedies to people dispossessed of land rights by racially discriminatory legislation passed since 19 June 1913.
- *Land Tenure Reform* – to provide for secure forms of land tenure, to help resolve tenure disputes and to make awards to provide people with secure tenure.

Within these focus areas, government [via the Department of Agriculture, Land Reform and Rural Development (DALRRD)] has established the following Programmes through which financial assistance is provided to qualifying beneficiaries, or fixed property is acquired by the DALRRD for use by qualifying beneficiaries:

- *Commonage* – land is set aside for communal agricultural usage but owned by a municipality, and as the demand is from the municipality, the municipality is viewed as the beneficiary.
- *Land Redistribution for Agricultural Development (LRAD)* – the DALRRD provides financial assistance (referred to as an LRAD grant).
- *Proactive Land Acquisition Strategy (PLAS)* – the DALRRD will acquire agricultural land within an Integrated Development Plan and will hold the land for a period (normally between one year and three years), after which it will sell the land to the beneficiaries. Qualifying beneficiaries will be entitled to LRAD grants in respect of the acquisition of the land.
- *General (Land Claims and Restitution)* – the DALRRD provides a grant to assist successful beneficiaries of a negotiated land restitution settlement to manage or secure their restored or compensatory land.

If fixed property is acquired by the Cabinet member, responsible for land reform, under the Provision of Land and Assistance Act 126 of 1993 or section 42E of the Restitution of Land Rights Act 22 of 1994, for use by qualifying beneficiaries, the supply of such fixed property is zero-rated.⁴⁵

If financial assistance is provided directly to qualifying beneficiaries, the zero-rating⁴⁶ only applies to the extent that the transactions are financed from grants or subsidies to which beneficiaries are entitled from the DALRRD under the Provision of Land and Assistance Act 126 of 1993. The zero-rating does not apply to any additional consideration which may be payable by the beneficiary to the vendor supplying the fixed property. The zero rate will also not apply if any movable property such as farming implements and other equipment is supplied together with the fixed property, unless the transaction qualifies as the supply of a going

⁴⁵ See section 11(1)(s).

⁴⁶ See section 11(1)(t).

concern (see Interpretation Note 57 “Sale of an Enterprise or Part Thereof as a Going Concern”). If the transaction is not the supply of a going concern, the movables are treated as a separate supply from the fixed property, and the consideration attributable to the movables must be charged with VAT at the standard rate.

7.6 Temporary rental of units (dwellings)

Property developers acquire and develop fixed property for the purpose of making taxable supplies. However, sometimes due to market conditions or other factors, newly constructed units are temporarily rented out to earn rental income, whilst the properties are still ultimately held for taxable supplies. In this scenario, rental operations are intended to provide the developer with temporary cash inflows to cover the carrying cost associated with the extended period of time that the property may be held.

7.6.1 Temporary relief under section 18B

Special relief was introduced under section 18B to deal with developers who entered into rental agreements with tenants on or after 10 January 2012. Under this provision, temporary relief from the onerous effect of the deemed supply was granted for a maximum period of 36 months to developers that temporarily rent residential fixed properties which continue to be held for sale. The 36-month period is calculated from the date that the dwelling is first let and applied per dwelling and not per agreement.

The relief period was initially granted until 31 December 2014, but was subsequently extended until 31 December 2017.⁴⁷ The relief was in the form of a suspension of the output tax which was payable on such a change in use adjustment, until one of the following events occurs:

- The temporary letting period for the dwelling concerned has exceeded 36 months.
- The developer permanently changes the intention for which the dwellings are held from taxable purposes to non-taxable purposes.⁴⁸
- The developer permanently applies the dwellings concerned for non-taxable purposes.⁴⁹

To qualify for this relief –

- the vendor concerned had to have been a “developer” (as defined);
- the developed units concerned must have been temporarily rented as dwellings for the first time between 10 January 2012 and 31 December 2017;
- the developer was required to continue marketing and holding the property for taxable purposes during the temporary lease period; and
- the developer had to keep a proper record of the temporary rentals.

For purposes of the dispensation, a “developer” was defined as a vendor that continuously or regularly constructs, extends or substantially improves fixed property consisting of any dwelling or parts thereof with the intention to subsequently sell that property. To access the relief, the developer had to show that the initial intention was to develop the dwellings for sale,

⁴⁷ See Binding General Ruling 48 “The Temporary Letting of Dwellings by Developers and the expiry of section 18B” (BGR 48).

⁴⁸ For example, the developer no longer intends to sell the properties, and therefore only advertises for letting purposes.

⁴⁹ For example, the developer applies one of the properties as a private residence.

and that there was a continuation of that intention during the relief period to sell the dwellings concerned.

If the change in application from taxable to exempt supplies (or private non-taxable use) was matched by a permanent change in the taxable purpose for which the property was held, the relief from the adjustment as provided in section 18B does not apply.

This means that an output tax adjustment under section 18(1) must be made, based on the OMV of the unit. This occurs, for example, when the taxable purpose of resale is permanently abandoned in favour of earning rental income from the lease of the property as a dwelling, or if the developer decides to use the property as a residence. The facts and circumstances of the case dictate whether there has been a permanent change in the taxable purpose or not.

Any subsequent supply of that property after the adjustment date under section 18(1) would not have been a taxable supply for VAT purposes. The transaction would instead have been subject to transfer duty, subject to any exemptions or exceptions which may have applied. This rule also applied to the subsequent sale of a property in respect of which the developer was required to declare output tax on the deemed supply under section 18B(3)⁵⁰ before selling the property.

As section 18B ceased to apply with effect from 1 January 2018, any temporary letting of such newly developed dwellings for the first time, on or that date, are required to account for the output tax adjustment under section 18(1).⁵¹

Example 42 – Temporary rentals and own use – Section 18B

Facts:

On 1 December 2015, Developer A bought a block of six old townhouses for R2 million as stock-in-trade. The townhouses were refurbished and subsequently advertised for sale on 18 May 2016. The units were all of equal size and value. The OMV of each unit was R570 000. However, because of a downturn in the property market, the developer was unable to find a buyer for any of the units. Five of the dwellings were therefore temporarily let to tenants for a period of nine months (1 September 2017 to 31 May 2018) to cover some of the costs of development, as well as interest on the bond over the property. (The remaining unit was not occupied at all until it was later used as a private residence.) Developer A continued to market all the properties for sale whilst some of the townhouses were temporarily let as dwellings.

Developer A subsequently sold four of the dwellings that were temporarily let, following the initial temporary letting period of nine months. In addition, the lease period for one of the units was extended until 30 September 2020. The director of Developer A also decided to permanently occupy the remaining unit as his own residence from 1 May 2017 and therefore did not continue to market that particular unit for sale.

What are the VAT consequences for Developer A?

⁵⁰ See Binding General Ruling 55 “Sale of Dwellings by Fixed Property Developers” (BGR 55).

⁵¹ See 7.6.2 for the new regime on temporary letting by developers that was introduced with effect from 1 April 2022.

Result:

Developer A qualified for the temporary relief as provided in section 18B for five of the units as lease agreements were entered into for the first time between 10 January 2012 and 31 December 2017 for short periods and those dwellings continued to be held for sale (taxable supplies). To qualify for the relief, Developer A was required keep proper records of the temporary rentals. Since the four units were temporarily let for a period of less than 36 months, Developer A did not need to make an output tax adjustment under section 18B. The subsequent sale of those units are subject to VAT at the standard rate.

As the rental period for the one unit expired after 31 December 2017, Developer A was required to account for output tax in the return for the tax period in which the 36-month period allowed for temporary letting ends (that is, the August 2020 tax period). As there are no transitional rules for a VAT rate increase or decrease in respect of change-in-use adjustments, the VAT rate used to calculate the adjustment is the one that applied at the time the adjustment was required to be made. In this example, the adjustment had to be made using a VAT rate of 15%. The subsequent sale of the unit will be subject to transfer duty and not VAT.

With regard to the remaining unit which is used as a residence by the director of Developer A, there was no relief available under section 18B. This is because there was a permanent change in use to non-taxable purposes (personal use) and the unit was no longer held for taxable supplies. Developer A would therefore have been required to declare output tax of R70 000 ($R570\,000 \times 14 / 114$ ⁵²) in block 12 of the VAT 201 return for the tax period covering 1 May 2017, which is the date that the permanent change in use occurred. The subsequent sale of the unit would have been subject to transfer duty and not VAT.

7.6.2 Temporary relief under section 18D

As indicated in 7.6.1, section 18B ceased to apply with effect from 1 January 2018. However, a similar relief mechanism was introduced in respect of temporary letting by developers under section 18D with effect from 1 April 2022. This means that, between 1 January 2018 and 31 March 2022, any newly developed dwelling that has been temporarily let the first time will not be subject to any relief provisions like that previously provided under section 18B or that which is currently available under section 18D.⁵³

For a detailed explanation on the background to section 18D and the similarities and differences between sections 18B and 18D, see Binding General Ruling 64 “Temporary Application of New Dwellings for Exempt Supplies Simultaneously held by Developers for Taxable Purposes” (BGR 64).

To qualify for the relief under section 18D, the following conditions must be met:

- The vendor concerned must be a “developer” as defined.⁵⁴
- The developed units concerned must have been temporarily applied⁵⁵ as residential accommodation (exempt supplies) for the first time on or after 1 April 2022.

⁵² The VAT rate was increased from 14% to 15% with effect from 1 April 2018.

⁵³ Consequently, any temporary letting of dwellings by developers during that period will mean that an output tax adjustment must be made by the developer under section 18(1) based on the OMV of the fixed property at the time the property is let (whether temporarily or not).

⁵⁴ See section 18D(1)(a).

⁵⁵ Section 18D(1)(b).

- The developer is required to continue marketing and holding the properties for taxable purposes during the 12-month period that they were temporarily applied for exempt supplies.
- The “temporarily applied” letting period must not exceed a period of 12 months, whether as a fixed or continuous period, or in aggregate. (This rule applies per dwelling unit.)
- The developer must keep a proper record of the temporary lettings including proof that each unit concerned has been let for no longer than 12 months in aggregate.

If the above requirements are met and the developer decides to temporarily let one or more of the dwelling units as residential accommodation, the law will apply as follows:

- The developer must make an output tax adjustment⁵⁶ based on the adjusted cost of the construction, extension or improvement of the fixed property concerned.⁵⁷ The time of supply for the adjustment is the date that the agreement for the letting and hiring of the accommodation in a dwelling comes into effect.⁵⁸
- Upon expiry of the 12-month period (or lesser period if the temporary letting ceases completely at an earlier date), the developer may make an input tax deduction⁵⁹ equal to the output tax that was previously declared when the temporary letting commenced. The same will apply if the property is sold during the period in which it was temporarily let.
- If the property concerned is sold during the time that it is temporarily applied for exempt supplies, the sale will be a taxable supply at the standard rate under section 7(1)(a). However, if the letting of the property continues beyond the 12-month period allowed, or there is a permanent change in use to exempt supplies (or own use) then the developer must make an output tax adjustment on the adjusted cost (the input tax previously claimed on the fixed property) in the month the fixed property is temporarily applied.
- Any sale of the property by the developer after the property has been subjected to an output tax adjustment under section 18(1) will not be a taxable supply under section 7(1)(a). Instead, the purchaser will be liable to pay transfer duty on the transaction.

Example 43 – Temporary rentals and own use – Section 18D

Facts:

On 1 December 2021, Developer B completed a development consisting of 30 units of identical size and cost to develop. After selling 26 of the 30 units, Developer B decided to cover some of the holding costs of the property by letting out the four remaining unsold units as residential accommodation from 1 May 2022 whilst continuing to market those units for sale.

⁵⁶ Section 18D(2).

⁵⁷ Section 10(29). Note that the current wording of section 10(29) does not include the adjusted cost of the land itself. In the 2023 Draft Taxation Laws Amendment Bill it is proposed that changes to the VAT law will be made to include the cost of the land in the adjusted cost.

⁵⁸ Section 9(13).

⁵⁹ Section 16(3)(o).

The four remaining unsold dwellings were let as follows:

- Unit 11 was let for a fixed period of 18 months.
- Unit 13 was let on a month-to-month basis (indefinite period lease). The tenant eventually ended up staying in the unit for more than 12 months.
- Unit 29 was let for a fixed period of six months and during that period, the unit was sold to another person.
- Unit 30 was initially let for a fixed period of four months and thereafter the developer decided to use the unit as his permanent residence.

What are the VAT consequences for Developer B?

Result:

- All of the 26 units sold so far would be subject to the standard rate of VAT under section 7(1)(a). (That is, normal VAT rules would have applied to the sale of those units.)
- Unit 11 was let for a fixed period of 18 months, so it does not fall within the provisions of section 18D. Consequently, Developer B must make an output tax adjustment under section 18(1) based on the OMV of Unit 11 when entering into the lease. Any subsequent sale of Unit 11 will be subject to transfer duty and not VAT.
- Unit 13 would have initially qualified for the relief under section 18D when the temporary letting commenced. At that time, Developer B would have had to declare output tax under section 18D(2) based on the cost of the construction, extension or improvement of the fixed property. However, the tenant eventually ended up staying in the unit for more than 12 months, so on the first day of the thirteenth month, Developer B must declare output tax based on the OMV of Unit 13 under section 18(1). At the same time, an input tax deduction would be allowed under section 16(3)(o) to recover the output tax previously declared under section 18D(2). Any subsequent sale of Unit 13 will be subject to transfer duty and not VAT.
- Unit 29 would have qualified under section 18D. Developer B would have to declare output tax under section 18D(2) based on the cost of the construction, extension or improvement of the fixed property when the leasing commenced. However, when the property was later sold, an input tax deduction would be allowed under section 16(3)(o) to recover the output tax previously declared under section 18D(2). As the property was sold during the period in which it was temporarily let, the sale of the property is a taxable supply at the standard rate under section 7(1)(a).
- Unit 30 would have initially qualified for the relief under section 18D. When the temporary letting commenced, Developer B would have had to declare output tax under section 18D(2) based on the cost of the construction, extension or improvement of the fixed property. However, at the time when Developer B decided to use the property as his/her own dwelling, he/she would have had to declare output tax based on the OMV of Unit 13 under section 18(1). An input tax deduction would be allowed under section 16(3)(o) to recover the output tax previously declared under section 18D(2). Any subsequent sale of Unit 13 will be subject to transfer duty and not VAT.

See BGR 64 for more details about how the law applies in respect of temporary letting by developers of newly developed dwelling units that are held as trading stock for sale.

7.7 Sale of a share or member's interest

The supply of an “equity security” such as shares in a company or a member's interest in a close corporation is a “financial service” which is exempt from VAT. However, when a vendor disposes of shares in a company or the member's interest in a close corporation which has a residential property as its sole or main asset, the transaction will be subject to transfer duty if the property concerned constitutes “residential property” as defined in section 1(1) of the Transfer Duty Act.

It follows that a developer does not carry on an enterprise to the extent that dwelling units are constructed if the ultimate supply is the sale of the shares or member's interest in the property owning entity⁶⁰ instead of the supply of the fixed property itself. In such cases, the developer may not register for VAT nor deduct any input tax on the acquisition of the fixed property or maintenance and general expenditure incurred. (See the *Transfer Duty Guide* for a discussion on residential property companies.)

Furthermore, a developer does not carry on an enterprise to the extent that dwellings are developed –

- as rental stock to earn residential rental income (exempt); or
- as the place of residence of the developer or any connected person in relation to that developer.

There are also special rules which apply to the sale of shares in a share block company. The sale of such shares will be subject to VAT at the standard rate if the supply is made in the course or furtherance of a vendor's enterprise. In any other case, the supply will be subject to transfer duty (if applicable).

7.8 Fractional ownership

Fractional ownership refers to the collective ownership of an asset. The asset concerned could be anything from an aircraft to a yacht, but typically the underlying asset is a luxury home, holiday apartment, or hotel suite of high monetary value (often with managed hospitality and support services) which is used by the fractional owners for leisure purposes. The costs of administering the scheme are divided among the fractional owners in accordance with their shareholding in the entity (normally a company) which owns the asset. Through the use of an ownership usage roster, the fractional owners are each allocated a number of days or weeks during the year within which they may enjoy the exclusive use of the property's amenities, and the related common areas of the applicable resort, or other property of similar size and type. Some fractional projects also participate in exchange programmes, which allow purchasers access to other properties located abroad which are of comparable quality and value.

In short, the purchase of a fractional interest normally involves the sale of shares in a company which goes hand-in-hand with a use agreement which regulates how the underlying property or any part thereof is to be used by the fractional owners. The issue which normally arises in

⁶⁰ This will not apply to the sale of any time-sharing interest which is specifically included in the definition of “fixed property”.

this regard is whether the supply of a fractional ownership interest in a company (which has as its underlying asset a fixed property) constitutes –

- the sale of an equity security (share) – which is exempt from VAT and therefore treated the same as the normal purchase of shares in a juristic person;⁶¹ or
- the supply of shares in a share block company or the supply of a time-sharing interest – both of which constitute the supply of “fixed property” and “goods” (as defined) and are subject to VAT at the standard rate of 15% if the supplier is registered for VAT (or required to be registered); or
- a supply which is subject to transfer duty.

From a VAT perspective, the determining factor of the taxable nature or otherwise of the supply of these fractional interests is based on whether the supply of the rights and interests under the fractional ownership scheme constitutes the supply of “fixed property” and “goods” as defined in section 1(1) (regardless of whether the fractional ownership scheme itself complies with the provisions of the Share Blocks Control Act 59 of 1980 or the Property Time-Sharing Control Act 75 of 1983). The characteristics of the fractional ownership schemes described above which involve the underlying use of fixed property are very similar to share block and time-sharing schemes. This is because included in the supply is a right to, or an interest in, the use of immovable property or a part thereof.

The view is that the supply of fractional ownership interests in a scheme where the objective is for the shareholders to acquire the use of fixed property does not merely constitute the supply of equity shares, but rather, interests in share block or time-sharing schemes which confer a right of use or occupation upon the owners. Since the supply of such rights and interests constitutes fixed property, it follows that a property developer, a property agent or any other vendor supplying fractional ownership interests in fixed property is liable to levy and collect the VAT from the purchaser if the seller is a vendor.

Fractional ownership interests in fixed property are therefore subject to VAT at the standard rate when supplied by a person that is, or should be, registered as a VAT vendor. Failure to charge VAT will result in the price charged for the supply being deemed to include VAT at the standard rate. The supply of a fractional ownership interest in fixed property by any person that is not liable to register for VAT is subject to transfer duty.

7.9 Low-cost housing

The supply of any low-cost housing to beneficiaries by a developer (including a municipality that acts as a developer) which is paid for by the Department of Human Settlements (DOHS) as part of a national housing programme contemplated in the Housing Act 107 of 1997 is zero-rated under section 8(23) read with section 11(2)(s).

Some important points to note in this regard:

- Only the payment by the DOHS to the developer that is responsible for delivering the completed houses to the beneficiaries is zero-rated. The zero-rating does not extend to any subcontractors that may be engaged by the developer in the course of constructing the houses.

⁶¹ For legal authority on this topic, see the Supreme Court of Appeal judgment in the case of *TCT Leisure v The Commissioner for the South African Revenue Service* (59/09) [2010] ZASCA 10 (12 March 2010).

- The zero-rating does not apply to the extent that the developer (for example, a municipality) receives a payment from the DOHS to build its own rental stock that will be used for exempt supplies of residential accommodation under section 12(c) by the municipality.

Chapter 8

Rental pools

8.1 Introduction

Special rules apply with regard to the VAT treatment of rental pool schemes.⁶²

For convenience and simplicity, in this Chapter –

- the words “owner” or “owners” are used to refer to owners and shareholders in sectional title schemes, time-sharing schemes and share block companies which participate in a rental pool scheme;
- the words “unit” or “units” are used to refer to the units or rights in fixed property which are applied in the rental pool scheme, and with which the enterprise is conducted by the operator; and
- the term “operator” is used to refer to the person that carries on the activities of the rental pool scheme as principal as contemplated in section 52(2).

8.2 What is a rental pool scheme?

8.2.1 Description of a rental pool scheme

The term “rental pool scheme” is not defined in the VAT Act, but may be described as an arrangement whereby the persons referred to in section 52(2) share resources and apply their combined interests or rights of use of fixed property for the purpose of conducting an enterprise⁶³ for the benefit of the members of the rental pool. The persons referred to are –

- the owners of time-sharing interests in a property time-sharing scheme as defined in section 1 of the Property Timesharing Control Act 75 of 1983;
- the owners of sectional title interests in a sectional title scheme as defined in section 1 of the Sectional Title Act. 95 of 1986; and
- the shareholders in a shareblock company as defined in section 1 of the Shareblocks Control Act 59 of 1980.

Once a rental pool scheme has been established, an operator must be appointed to carry on the enterprise activity of the rental pool. The operator could be anyone, for example –

- the time-share body corporate, sectional title body corporate or share block company;
- an estate agent;
- a person who specialises in time-share sales and renting of such units;
- an entity which has been created specifically for the purposes of conducting the rental pool activity;
- any other person appointed to carry on this activity.

⁶² See section 52(2).

⁶³ For the purposes of this chapter, a rental pool scheme is discussed in the context of a commercial accommodation enterprise. However, the principles could apply equally to rental pools which, for example, rent out office space.

Should a time-share body corporate, sectional title body corporate or share block company be appointed to carry out this task, it will be carrying on a dual function for the unit owners concerned in that it will be collecting levies as well as managing the rental pool scheme. In any of these cases, the operator must register the rental pool separately for VAT. For example, if an estate agent is appointed as the operator, the rental pool must be registered as a separate branch of that estate agent's business.

8.2.2 Functions of a rental pool

The operator may carry out the following functions:

- General property management and administration
- Collection of rentals
- Arranging of other specific services required by the pool members
- Payment of service charges on behalf of owners
- Ensuring that the units are cleaned and serviced
- Marketing, advertising and renting out of units

In addition to the above functions, the main purpose of section 52(2) is to create a situation in which the operator is regarded as the principal and not the agent of the owners of the units. This allows the input tax and output tax to be accounted for by the operator under one VAT registration, instead of by each owner under a number of separate VAT registrations.

8.2.3 Participation in a rental pool

There are different ways in which a unit owner may participate in a rental pool, for example:

- The unit owner may be contractually obliged to apply the unit immediately in a rental pool scheme upon purchasing the unit from the developer.
- If the rental pool scheme is voluntary, a unit owner may have an option to apply the unit in an existing pooling arrangement at some time after purchasing the unit.
- If there is initially no pooling arrangement at the time of purchase, a group of unit owners may decide at a later stage to create a rental pool scheme and to apply their units in the pool.

In any of these cases, the owners must elect in writing that the rental pool will be regarded as a separate enterprise from the owners, and that it is treated as the principal for the purposes of supplying commercial accommodation. (See **2.9** for a discussion on commercial accommodation).

8.3 Registration

To understand the requirements for VAT registration of a rental pool scheme, the provisions of sections 52(2), 23 and 50 must be considered. In addition, the exemption in section 12(f) which applies in respect of levies must be considered, as the operator of a rental pool is often the body corporate or share block company of the building, or the managing agent which also collects levies on behalf of the body corporate or share block company. As mentioned in **8.2**, this may lead to the performance of a dual function and the activities of the rental pool (taxable) should be kept separate from the activities of the levy fund (which is exempt if the development is not time-share).

Once the owners have provided the required declaration referred to in section 52, the rental pool scheme is deemed to be an enterprise which is operating separately from the owners, and is regarded as a principal and not as an agent of the owners for VAT purposes.

The VAT registration implications of this are –

- that the operator must be regarded as a separate person from the owners participating in the rental pool;
- that if the operator is the body corporate or another person who is already registered for VAT, it will have to register the pool separately as a branch on a form VAT 102e; and
- that the total amount earned from the use and application of all the units in the pool is deemed to be in respect of an enterprise carried on by the operator.

8.4 Accounting for value-added tax

8.4.1 General administrative issues

The general rules regarding the accounting for VAT by operators of rental pools can be summarised as follows:

- The operator will be liable for the payment of output tax and will be entitled to deduct input tax (provided the operator is in possession of a valid tax invoice, issued in the name of the member or in the name of the operator, and further the tax invoice must bear the VAT registration number belonging to the rental pool).
- The operator will remain responsible for performing the duties imposed under the VAT Act regarding the activities of the rental pool until the unit is withdrawn from the rental pool, or the rental pool ceases to operate.
- On termination of the agreement between the operator and a member, the pool will be deemed to supply the unit (or any other goods or right capable of assignment, cession or surrender in respect of the unit) to that member. The pool will therefore be liable to account for output tax on the supply of the unit to the exiting member.
- The operator is liable for any tax, additional tax, penalty and interest chargeable under the VAT Act or the TA Act on the activities of the rental pool. This applies not only in regard to supplies of commercial accommodation and other incidental supplies made by the operator, but also includes the supply of units in the pool and any adjustments in regard to the taxable use of those units, or any other goods or services previously applied in the pool for enterprise purposes.
- The operator must retain all records (including tax invoices) relevant to the operation and management of the pool.

8.4.2 Supplies of commercial accommodation

Once the owners have elected in writing to conduct their commercial accommodation activities through a rental pool, the operator will become liable to charge VAT on the supply of any commercial accommodation and will be entitled to deduct any input tax which may be allowed if the supplies by the rental pool exceed the compulsory registration threshold for VAT.

The time and value of supply rules for commercial accommodation supplied by a rental pool scheme are as follows:

Time of supply

The general time of supply rule applies in respect of supplies of commercial accommodation, being the earlier of the following dates:

- The date that any invoice is issued to the customer; or
- The date that any payment is received by the person conducting the rental pool scheme.

In the event that the supplier and the recipient are “connected persons” as defined in section 1(1), the time of supply is –

- the time that any services are performed; or
- in the case of goods which are to be removed, the time that the goods are removed; or
- in the case of goods which are not to be removed, the time that the goods are made available to the recipient.

Value of supply

- If the pool supplies commercial accommodation and domestic goods and services for an unbroken period of 28 days or less, VAT will be levied at the standard rate on the full consideration charged for the supplies.
- In the case of commercial accommodation and domestic goods and services supplied at an all-inclusive charge for an unbroken period of more than 28 days, VAT will be levied at the standard rate on only 60% of the all-inclusive charge for the supplies.
- Should the supplier and the recipient be “connected persons” as defined in section 1(1), the consideration for any commercial accommodation and domestic goods and services supplied between the parties will usually be equal to the OMV thereof.⁶⁴

Since the supply of commercial accommodation is the supply of “entertainment” (as defined), the circumstances in which any entertainment expenses are incurred in providing that entertainment must comply with the exceptions set out in the provisos to section 17(2)(a) otherwise those expenses will be specifically disallowed. (See the *VAT 411 – Guide for Entertainment, Accommodation and Catering*.)

8.4.3 Charges for management, administration and other supplies

The operator may also charge a management or administration fee for carrying on the rental pool enterprise, or for other supplies made, for example, if commission is charged for the sale of units on behalf of the rental pool members. The fee could be charged to the individual unit owners directly, or it could be charged to the rental pool scheme (depending on the contractual arrangements).

Should the operator also carry on other taxable activities for which that person is separately registered for VAT, those charges for management, administration or commission will also attract VAT at the standard rate. (For example, if the operator collects levies on behalf of a body corporate and charges a fee for that service.)

⁶⁴ Section 10(4).

Should an owner not participate in the rental pool, but the operator of the rental pool sources tenants or customers through the rental pool scheme on behalf of that owner, the following applies:

- The operator will be acting as the agent of the owner.
- If the owner is a vendor, that owner (and not the operator of the rental pool) will be liable to account for any VAT charged on the supply of commercial accommodation to the customer.
- Any commission or fee charged by the operator to the owner will include VAT, and if the owner is a vendor which supplies commercial accommodation, the VAT incurred on the fee or commission may be deducted as input tax. If the owner is not a vendor, any VAT charged by the person conducting the rental pool will be a cost to the owner.

Example 44 – Accounting for other supplies

Facts:

M Properties is a property management company which also operates and manages a time-share rental pool scheme. The property management activities are registered under the trading name “M Properties Management Services” (Registration 1) and the activities of the rental pool are registered as a branch of M Properties under the name “ABC Rental Pool” (Registration 2). M Properties has received the required declarations from the unit owners participating in the scheme to the effect that the rental pool should be regarded as the principal for VAT purposes.

M Properties charges a monthly management fee of R3 420 to the members of the rental pool for operating and managing the scheme. According to the rules of the scheme, all services in connection with the management of the units in the pool must be regarded as the expenses of the rental pool scheme and not of the individual members of the pool.

M Properties also collects the time-share levies on behalf of XYZ Cottages Body Corporate (Registration 3) and from time-to-time finds tenants for unit owners that do not participate in the rental pool, for which a finder's fee is charged.

What are the VAT implications of these activities?

Result:

M Properties Management Services (Registration 1)

- M Properties (under Registration 1) makes a supply of management services to the rental pool (under Registration 2). Therefore, M Properties must issue a tax invoice and declare output tax of R446,09 ($R3\,420 \times 15 / 115$).
- VAT must be accounted for at the standard rate on any fees charged for collecting the time-share levies in the tax period on behalf of XYZ Cottages Body Corporate, as well as any finder's fees charged to unit owners that do not participate in the rental pool.

ABC Rental Pool (Registration 2)

- M Properties (under Registration 2) will be able to deduct R446,09 as input tax as the expense was incurred wholly in the course or furtherance of the rental pool enterprise. The balance of R2 973,91 will be deducted from the monthly income of the rental pool as an expense before distributing the net amount to the members.
- The VAT collected on the time-share levies by M Properties Management Services (Registration 1) is collected as agent for XYZ Cottages Body Corporate. The VAT collected must therefore be paid over to XYZ Cottages Body Corporate that will account for the output tax on their VAT 201 return. Input tax may be deducted on the agent fees incurred for the collection of the levies.

8.4.4 Supply of units and changes in use**(a) Units acquired from the developer (vendor)**

In the event a unit is acquired from a developer and the unit holder decides to place it in a rental pool scheme, the operator is permitted to deduct the full input tax credit. This is on condition that the unit is intended to be used to make taxable supplies and a valid tax invoice is retained.

(b) Units acquired from a person other than the developer**(i) The seller is a vendor not participating in the rental pool**

Should the owner selling the unit be a vendor that has not participated in the rental pool, for example, if the unit was used to provide commercial accommodation outside of any pooling arrangement in which the other unit owners may be participating, or for example, if the unit was held for speculative purposes as stock for resale, the sale of the unit will be a taxable supply and the purchaser will pay VAT. If the purchaser applies the unit in the rental pool, the operator will be permitted to deduct the full input tax credit provided that the purchaser obtains a tax invoice from the seller. Alternatively, if the new owner decides not to participate in the pool, the normal rules regarding an enterprise will apply as discussed in **Chapter 2**.

In the case of the seller not applying the unit for enterprise purposes, the purchaser will pay transfer duty at the applicable rate (subject to any exemptions which may apply). If the purchaser applies the unit in the rental pool, the operator will be permitted to deduct a notional input tax credit.⁶⁵

(ii) The seller is a participant in the rental pool

The supply is treated as follows in the event a unit has been applied in the rental pool and the owner sells the unit to another person:

- Once the unit is in the rental pool, any subsequent supply by the owner is regarded as being a supply by the operator.
- If the purchaser elects to remain in the rental pool, the supply will not be regarded as a taxable supply for VAT purposes.
- Similarly, if the purchaser elects in writing that the unit must continue to be operated and managed as part of the rental pool, the supply will be exempt from transfer duty under section 9(15B) of the Transfer Duty Act.

⁶⁵ For fixed property acquired on or after 10 January 2012, the input tax deduction is no longer limited to the transfer duty paid or payable.

- Should the purchaser elect not to participate in the rental pool at the time of the sale, the operator will be required to account for output tax at the standard rate on the consideration for the supply. However, if the purchaser is a vendor, the unit may be purchased as a going concern and therefore subject to VAT at the zero rate provided that all the conditions of a going concern transaction are met (as discussed in 2.8). In this situation the purchaser is already registered for VAT because commercial accommodation is supplied in an enterprise carried on by that person outside of the pooling arrangement and the value of the person's taxable supplies exceeds R120 000 in the past 12 months. Alternatively, the purchaser could be a property trader and the unit may be acquired for speculative purposes with the intention of making a profit on the subsequent sale thereof.
- In the case of the purchaser electing at some time after the sale to no longer participate in the rental pool, the operator will be required to make an adjustment for the change in use and account for output tax on the OMV of the unit as at the date of the change in use.
- Should the purchaser initially not participate in the rental pool, but elects at a later date to apply the unit in the pool, the operator will be permitted to make an input tax adjustment based on the lesser of the cost of the unit or the OMV, provided that the purchaser is registered for VAT.

(c) Application of units in the rental pool

The operator will be allowed to deduct input tax on units applied in the rental pool scheme by pool unit owners, provided that –

- the operator has the required statement in writing from the owners that the activities of the rental pool are to be treated separately for VAT, and that the operator is to be regarded as the principal for any goods or services supplied or acquired;
- a valid tax invoice has been issued in the name of the member or in the name of the operator which bears the VAT registration number belonging to the operator (which relates to the rental pool enterprise); and
- the operator is liable to register for VAT, or is entitled to register voluntarily.

The normal rules regarding apportionment and disallowance of input tax will apply to the operator, as for any other vendor. However, the operator is not required to apportion the input tax with regard to units placed in the pool merely because the deed of sale or pooling agreement may allow the owner to use the unit for limited periods during the year. This is because the rental pool is regarded as having “acquired” the units wholly for the purposes of making taxable supplies. The operator will further be permitted to deduct input tax for the furnishing of units by owners that participate in the pooling scheme.

Should the unit owner be a vendor that applied the unit for taxable supplies in a commercial accommodation enterprise, or if for example, the unit was held for speculative purposes before applying that unit in the rental pool, no input tax may be deducted by the operator. The reason for this is that the unit owner (being a vendor at the time) would have been entitled to deduct input tax when the unit was applied for enterprise purposes. The statutory limitation⁶⁶ of five years on any input tax claim in this regard will apply if no input tax was claimed by the owner in respect of any unit which was acquired, constructed, held or applied for taxable purposes during the time that the owner was a vendor.

⁶⁶ Proviso (i) to section 16(3).

In the event that the vendor elects to participate in the rental pool and causes the previous enterprise activity to end, no output tax will be payable under section 8(2) upon deregistration, as the enterprise activity is essentially substituted under the operator's enterprise and VAT registration number. The VAT consequences with regard to any changes in taxable use, or supply of the unit whilst it is in the rental pool will therefore become the liability of the operator.

(d) Withdrawal of units from the rental pool

A change in the taxable use of units in the rental pool scheme will result in the operator being deemed to have applied the unit for purposes other than making taxable supplies and the operator will be required to account for output tax on the OMV of the units concerned.

For example an output tax adjustment must be made when owners permanently withdraw their units –

- for own use or occupation⁶⁷ (see **5.4.2**), or
- for the purpose of conducting an enterprise activity outside of the existing pooling arrangement.

The operator will be required to account for the output tax even if the pooling agreement contains a clause which makes the owner responsible for paying the VAT. This is because the operator is liable for the VAT in the first instance (being the vendor making that adjustment), regardless of whether or not the amount may be recovered from the owner.

Should a unit owner first withdraw a unit from the rental pool before selling the unit, or before the rental pool ceases to conduct an enterprise, the operator must make an output tax adjustment and account for output tax at the standard rate on the OMV of the unit.

In the case that a unit is withdrawn from the rental pool before selling the unit, the subsequent sale of the unit will either –

- be subject to transfer duty because the unit owner is not a vendor; or
- be a taxable supply at the standard rate which must be accounted for by the seller if that unit owner is a vendor that has applied the unit in an enterprise activity outside of the rental pool.

(e) Cessation of the rental pool

If the rental pool ceases and the unit owner is a vendor for reasons other than the supply of commercial accommodation, or the unit owner is not registered (or not required to be registered) for VAT, the supply of accommodation in the unit will not constitute a taxable supply. If at some time after the rental pool activity has ceased, the unit owner applies the unit in a commercial accommodation enterprise, or if for example, the unit is held as stock for speculative purposes (taxable supplies), the owner may at that time⁶⁸ make an input tax adjustment based on the lesser of the cost or OMV of the unit.

⁶⁷ An owner does not “withdraw” the unit if it is occupied or used by the owner or the owner's guests for the period allowed in accordance with the rules of the rental pool scheme.

⁶⁸ After output tax has been paid upon deregistration of the rental pool scheme as required under section 8(2).

(f) Personal use of units

In most instances the rental pool agreement makes provision for the owner to use the unit (or any other available unit in the rental pool) for prescribed periods of time. In such a case, the rental pool makes a taxable supply of commercial accommodation to the unit owner or to the guest of the unit owner (as the case may be). The rental pool will be required to account for output tax at the standard rate on any consideration charged for the supply. Furthermore, if the unit owner and the rental pool are “connected persons” as defined in section 1(1), VAT must be accounted for on the OMV of the supply, if no consideration is charged or the consideration charged is less than the OMV of the supply. (See also **4.4.2** and **8.4.2**.)

(g) Rental distribution to owners

The rental pool will be required to account for output tax when it supplies commercial accommodation and related services in the course of its enterprise. However, when the operator of the rental pool distributes the rental income after offsetting expenses to the owners, this will not be regarded as consideration for the supply of goods or services by the owners to the rental pool. The owners will not be required to register for VAT or declare any output tax on the distribution received.

Chapter 9

Miscellaneous issues

9.1 Introduction

This chapter deals with other issues relevant to fixed property transactions which are either not dealt with in the previous chapters, or where additional information on the topic is useful to clarify the VAT treatment.

9.2 *Bare dominium* and usufruct

The term “*bare dominium*” refers to the real right of ownership of an asset (for example, fixed property), whereas the term “usufruct” refers to a limited real right involving the use of the same asset. The usufruct allows the holder of the right (the usufructuary) to enjoy the use of the property and to benefit from the “fruits” of the asset during the lifetime of the usufructuary, or for a specified period of time, or until the happening of a specified event. As a result, the ownership of the asset could vest in one person (the bare dominium owner) whereas the right to use the asset vests in another person.

The supply of the bare dominium or usufruct in relation to fixed property is subject to VAT at the standard rate if the supplier is a vendor, and if the supply is in the course or furtherance of that vendor’s enterprise. If the parties to the transaction are related (as in the case of connected persons), it may be necessary to use the OMV of the property to determine the value of the supply for the usufruct and/or bare dominium in relation to that property. (See 2.3.2 of the *Transfer Duty Handbook* for more details in this regard.)

In the case of the supply of the bare dominium or usufruct not being in the course or furtherance of the vendor’s enterprise, the transaction will be subject to transfer duty.

9.3 Employee housing

If an employer provides employees with accommodation in a house or hostel, the supply is exempt (whether the employer is the owner of the property or not) subject to certain exceptions. In this instance, a deemed supply⁶⁹ in respect of the benefit or advantage to the employee will not arise, hence the employer will not be required to account for output tax on the supply.

9.4 Expropriation

If fixed property belonging to a vendor is expropriated and the vendor receives any payment, in respect of the land, that payment will be subject to VAT at the standard rate. The vendor will be required to account for VAT at the standard rate, except if the fixed property belonging to the vendor was not used in the course or furtherance of an enterprise. For example, when the property concerned is the vendor’s private dwelling.

⁶⁹ See section 18(3).

9.5 Right of occupation (life rights)

A “right of occupation” in relation to a housing interest, is defined as a right which confers the power to occupy a portion in a housing development scheme for the duration of the lifetime of the purchaser or any other person mentioned in the contract in terms of which the housing interest is acquired, without conferring the power to claim transfer of the ownership of the portion to which the housing interest relates. This is typically found in housing development schemes for retired persons.

The sale and re-sale of the right of occupation under a life right is exempt from VAT.⁷⁰

9.6 Servitudes

A servitude is a limited real right and entitles the holder to limited use or access to another person’s property or to insist that such other person refrains from exercising certain entitlements normally flowing from the right of ownership. “Fixed property” is defined to include any real right in land, a unit, a share or time-sharing interest. Therefore, when a servitude is renounced by a vendor for a consideration and such renunciation is in the course or furtherance of that vendor’s enterprise, the supply will attract VAT at the standard rate. Otherwise, such renunciation may be subject to transfer duty (subject to any exemptions or exceptions contained in the Transfer Duty Act).

9.7 Levy funds

If a body corporate, share block company, housing development scheme, or homeowners’ association⁷¹ supplies services to its members and the costs for these services are paid from levy fund contributions received from members, the provision of those services is exempt from VAT. However, the body corporate, share block company or housing development scheme may apply to SARS to regard the supply of the services (or some of the services) as being subject to VAT at the standard rate. In such cases, the levies will only attract VAT at the standard rate if SARS has allowed that entity to register for VAT and has directed that the exemption is not applicable to that entity (or is applicable only to a limited extent).

This exemption does not apply to a body corporate or share block company that manages a property time-sharing scheme. In the case of homeowners’ associations, the exemption only applies to associations⁷² formed solely to manage the collective interests of residential property use and ownership of all its members.

9.8 Leasehold improvements

During the period of a lease agreement, a lessee may be required to effect leasehold improvements, or do so on a voluntary basis. This will generally entail improvements that become permanently attached to the leasehold property belonging to the lessor.

In accordance with the common-law principle of *superficies solo cedit*, buildings or attachments which have become permanently attached to land, become the property of the owner of the land on which they have been built or attached. Improvements that are effected under a lease agreement by the lessee and that are permanently attached to the land or

⁷⁰ Section 12(c)(i).

⁷¹ From 1 April 2014 the exemption under section 12(f) was extended by the insertion of paragraph (iv) to include homeowners’ associations.

⁷² The association of persons concerned must be of the type that is not permitted to distribute any of its funds to any person other than a similar association of persons.

buildings therefore become the property of the lessor. Whether this form of accession has taken place or not will depend on the circumstances of each case.

The VAT Act did not previously contain specific provisions dealing with the consequences for the parties when a lessee effects leasehold improvements for no consideration to the lessor's property during the period of the lease. To address this situation, amendments to the VAT Act were made in this regard with effect from 1 April 2018.⁷³

The VAT law now provides that the lessee is deemed to make a supply of goods⁷⁴ at the time of completion of the leasehold improvements.⁷⁵ The time of completion of the leasehold improvements will depend on the specific circumstances or facts but will generally be the date of approval for occupation by the relevant municipality, or the date stipulated in the agreement. In the absence of the aforementioned, third-party confirmation, such as an architect's certificate may indicate the date of completion.

The lessee is not required to account for output tax on effecting the leasehold improvements, as the value is deemed to be nil.⁷⁶ However, the lessor will be required to account for output tax on these improvements to the extent that the lessor, at the time of completion of the leasehold improvements, uses the fixed property otherwise than for purposes of making taxable supplies.⁷⁷

The effect of these provisions is that the lessor is in the same position had the lessor effected the leasehold improvements itself and the use thereof were for purposes other than to make taxable supplies.

The value of the supply is the amount stipulated in the agreement, or if no amount is stipulated, the OMV (both amounts being VAT inclusive). The normal rules in respect of connected persons apply. (For a discussion on connected persons see 4.4.2.)

Example 45 – No obligation to effect improvements and no consideration payable in respect thereof

Facts:

A lessee and a lessor concluded a lease agreement for the use of immovable property, in return for a market related monthly rental. The lessee is under no obligation to effect any improvements, but during the course of the lease, effects certain improvements which become permanently attached to the property. The lessee uses the improved building wholly in the course of making exempt supplies.

What are the VAT consequences of the leasehold improvements for the lessor and the lessee respectively?

⁷³ The deeming provisions in the amendments do not apply if the leasehold improvements have been made (whether compulsory or not) for a consideration, or the lessee (being a vendor) uses the leasehold improvements wholly for non-taxable purposes.

⁷⁴ Section 8(29).

⁷⁵ Section 9(12).

⁷⁶ Section 10(28).

⁷⁷ Section 18C.

Result:

Lessee

As the lessee uses the improved building wholly for the purpose of making exempt supplies, the lessee may not deduct input tax on any goods or services acquired to effect the improvements.

No deemed supply arises under section 8(29) for the lessee, irrespective of whether or not the lessee was obliged to effect the improvements. This is because the improved property is used by the lessee wholly for the purposes of making exempt supplies.

Lessor

Because there is no deemed supply of goods by the lessee to the lessor under section 8(29), the lessor is not required to make any adjustment under section 18C, regardless of the purpose for which the lessor is using the building at the time of completion of the leasehold improvements.

Example 46 – Improvements effected, partially for purpose of making taxable supplies by the lessee, and no consideration payable in respect thereof

Facts:

A lessee and a lessor concluded a lease agreement for the use of immovable property, in return for a market related monthly rental. In addition to the monthly rental, the lessee is obliged to effect improvements to the value of R1,3 million during the period of the lease, for no consideration. The date of approval for occupation by the relevant municipality of the improved property, was on 1 March 2022. The lessee uses the improved property to conduct a passenger transport business by bus (exempt) and a car rental business (taxable). The lessor uses a third of the property to conduct a passenger transport business by bus (exempt).

What are the VAT consequences of the leasehold improvements for the lessor and the lessee respectively?

Result:

Lessee

As the lessee uses the improved building partly in the course of making taxable supplies, and partly for the purpose of making exempt supplies, the lessee must apportion any VAT incurred on goods or services acquired to make the improvements. The extent to which input tax may be deducted is determined by using the prescribed turnover-based method in BGR 16,⁷⁸ or another method approved under section 41B. This deduction is also subject to sections 16 and 20.

A deemed supply also arises under section 8(29) for the lessee, because the improved property is partly used for purposes of making taxable supplies. The deemed supply occurs on 1 March 2022 and the value of the supply is nil. The lessee therefore has no output tax liability.

⁷⁸ Binding General Ruling (VAT) 16 “Standard Apportionment Method” (BGR 16).

Lessor

Because there is a deemed supply of goods by the lessee to the lessor under section 8(29), and the lessor uses the improved property partly to make exempt supplies, the lessor is deemed to make a taxable supply and is required to make an adjustment in the return covering March 2022, calculated as follows:

Adjustment = R56 521,74

Where: A = 15 / 115

B = R1,3 million

C = 33,33%

9.9 Judgment of the Supreme Court of Appeal on the *Respublica* case⁷⁹

9.9.1 Factual background

Respublica (Pty) Ltd (Respublica) (the respondent) concluded an agreement in terms of which it leased immovable property it owned, to a university. Under the agreement, the university was allowed to lease the immovable property to its students, and to use it for holiday accommodation provided to third parties.

The dispute related to whether Respublica was supplying “commercial accommodation” and was therefore entitled to apply the special value of supply rule under section 10(10). Section 10(10) provides that VAT is only payable on 60% of the total consideration received (all-inclusive charge) if the commercial accommodation is supplied for an unbroken period exceeding 28 days. The complete facts of the *Respublica* case and the arguments of both the Commissioner and the Appellant may be found in the reported judgment and are therefore not repeated in this guide.

9.9.2 Principles enunciated

Only a natural person can take up temporary accommodation

The Supreme Court of Appeal (SCA) confirmed that the ordinary meaning of the word, “lodger” refers to a natural person taking up temporary accommodation. Therefore, Respublica’s contention that it supplied lodging to the university, being by its nature incapable of living in such accommodation, is at odds with the ordinary meaning of the word as used in the VAT Act.

The nature of the contractual agreements must be taken into account

Respublica contended that the university’s students were the “true lodgers”, and as a result, its supply to the university complied with the definition of “commercial accommodation”. The SCA found that on the facts of the case, two distinct legal relationships were contemplated. The first being the lease of immovable property, together with specified services and utilities to the property between Respublica and the university, and the second, between the university and its students and holiday visitors for the supply of short-term accommodation. Respublica had no contractual nexus to the latter contractual relationship.

⁷⁹ Judgment handed down by the SCA in *CSARS vs Respublica (Pty) Ltd* (1025/2017) [2018] ZASCA 109 (11 September 2018).

9.9.3 Supreme Court of Appeal decision

The SCA upheld the appeal and found that the relevant contractual rights and obligations are those as between Respublica and the university and not between the university and its students. The supply by Respublica did not meet the first requirement of “commercial accommodation”.

Glossary

Bare dominium	In relation to the rights over immovable property, means bare ownership rights and that the owner of the immovable property does not have the right of use of the property. Typically, another person known as the usufructuary will have the right of use over the property (usufruct) which will be registered as a personal servitude against the title deed of the property.
Body corporate	Means a group of persons, being owners of sectional title units in a sectional title scheme comprising buildings and the land on which such buildings are situated, that are responsible for the management and administration of the sectional title scheme.
Commercial accommodation	<p>Lodging, or board and lodging supplied –</p> <ul style="list-style-type: none"> • together with domestic goods and services, in any house, flat, apartment, room, hotel, motel, inn, guesthouse, boarding house, residential establishment, holiday accommodation unit, chalet, tent, caravan, camping site, houseboat, or similar establishment which is regularly or systematically supplied but excluding a dwelling supplied in terms of an agreement of letting and hiring thereof; • in a home for the aged, children, physically, or mentally handicapped persons; and • in a hospice. <p>A dwelling supplied in terms of an agreement for letting and hiring thereof is not regarded as commercial accommodation.</p> <p>Also see “domestic goods and services” below in respect of values.</p>
Connected person	<p>Describes and identifies the relationships between different persons which includes, but is not limited to: family relatives, partnerships, trust beneficiaries, branches of the same legal entity, companies with the same shareholders etc. If persons are connected in terms of the definition, it may be necessary to apply special time and value of supply rules that require VAT to be charged, based on the OMV of the supply, rather than on the amount of consideration received.</p> <p>Examples include the following (amongst others):</p> <ul style="list-style-type: none"> • Natural persons who are related by blood or marriage • A company and subsidiaries of that company • Any close corporation and its members • A natural person and a company where that natural person is interested in 10% or more of the company’s paid up capital, equity shares or voting rights in that company

Consideration	<p>The total amount of money (including VAT) received for a supply. As such, the value of the supply in addition to the VAT charged would equal the consideration for the supply.</p> <p>For barter transactions where the consideration is not in money, the consideration is the OMV of goods or services (including VAT) received for making the taxable supply. Section 10 determines the value of supply or consideration for VAT purposes for different types of supplies.</p> <p>Any act or forbearance, whether voluntary or not for the inducement of a supply of goods or services will constitute consideration, but it excludes any donation made to an association not for gain. Also excluded is a “deposit” which is lodged to secure a future supply of goods and held in trust until the time of the supply.</p>
Domestic goods and services	<p>Includes –</p> <ul style="list-style-type: none">• cleaning and maintenance;• electricity, gas, air conditioning or heating;• a telephone, television set, radio or other similar article;• furniture and other fittings;• meals;• laundry;• nursing services; or• water, <p>when supplied together with commercial accommodation.</p>
Dwelling	<p>Means, any building, premises, structure or any other place, or any part thereof, used or intended for use predominantly as a place of residence or abode of any natural person (or which is intended for this purpose), including fixtures and fittings belonging thereto and enjoyed therewith. The supply of a dwelling does not include the supply of commercial accommodation.</p>
Enterprise	<p>Any business activity in the broadest sense. It includes any activity carried on –</p> <ul style="list-style-type: none">• continuously or regularly;• by any person;• in or partly in the Republic;• in the course of which goods or services are supplied for a consideration that is some form of payment;• whether or not for profit.

Special inclusions

- Public authorities – certain government departments and provincial authorities.
- Municipalities.
- Welfare organisations and implementing agents in respect of foreign donor funded projects.
- Share block companies.
- Non-residents supplying certain electronic services subject to certain requirements [if at least two of the following circumstances apply: Services are supplied to a South African resident, payment originates from the RSA, or the recipient has an address (that is business, postal or residential) in the RSA].

Examples

- Ordinary businesses – manufacturers, traders, auctioneers, landlords, contractors etc.
- Trades and professions – builders, electricians, plumbers, doctors, lawyers, accountants etc.

Exclusions

- Services rendered by an employee to an employer, for example, salary/wage/remuneration earners. This must, however, be distinguished from a private independent contractor who is not excluded.
- Supplies by a branch or main business permanently located outside the RSA (must be separately identifiable and maintain its own system of accounting).
- Private or recreational pursuits or hobbies (unless carried on like a business).
- Private occasional transactions, for example, occasional sale of domestic/household goods, personal effects or private motor vehicle.
- Any exempt supplies (listed in section 12).
- Supplies by persons that are not vendors.

Exempt supplies Means, a supply on which no VAT may be charged (even if the supplier is registered for VAT). Persons making only exempt supplies may not register for VAT and may not recover input tax on purchases to make exempt supplies.

Section 12 contains a list of exempt supplies.

Examples

- Rental of accommodation in any "*dwelling*" including employee housing.
- Certain services to members of a sectional title, share block or old age scheme funded out of levies (not applicable to timeshare schemes).

Goods	<p>Includes the following:</p> <ul style="list-style-type: none"> • Corporeal (tangible) movable things, goods in the ordinary sense (including any real right in those things) • Fixed property, land and buildings (including any real right in the property for example, servitudes, mineral rights, notarial leases etc) • Sectional title units (including timeshare) • Shares in a share block company • Electricity • Postage stamps • Second-hand goods <p>Excludes the following:</p> <ul style="list-style-type: none"> • Money, that is, notes, coins, cheques, bills of exchange etc. (except when sold as a collector's item) • Value cards, revenue stamps etc. which are used to pay taxes (except when sold as a collector's item) • Any right under a mortgage bond
Housing development scheme	<p>Means any scheme, arrangement or undertaking –</p> <ul style="list-style-type: none"> • in terms of which housing interests are alienated for occupation, whether the scheme, arrangement or undertaking is operated pursuant to or in connection with a development scheme or a share block scheme or membership of or participation in any club, association, organization or other body, or the issuing of shares, or otherwise, but excluding a property time-sharing scheme; or • declared to be a housing development scheme by the Minister by notice in the <i>Gazette</i> for the purposes of the Housing Act 107 of 1997.
Input tax	<p>This is the tax paid by the recipient to the supplier of goods or services. Input tax may only be deducted by the recipient vendor if the goods or services are acquired for making taxable supplies and if the vendor is in possession of the required supporting documents or, in certain prescribed circumstances, such alternative documents containing the information acceptable to the Commissioner. An apportionment of input tax must be made if goods or services are acquired only partly for taxable supplies. In the case of importation, the vendor must be in possession of a bill of entry (or other prescribed Customs document), the EDI release notification together with a receipt for the payment of the VAT issued on eFiling.</p> <p>In certain instances, input tax may also be deducted on supplies of second-hand goods which were not subject to VAT, (for example if goods were acquired from a non-vendor). The recipient vendor must retain a proper record of the details of the transaction as is acceptable by the Commissioner.</p> <p>Input tax may not be deducted if goods or services are acquired for making exempt supplies, other non-taxable activities or for private use.</p>

Open market value (OMV)	The term “open market value” (abbreviated in this guide as “OMV”) is defined with reference to section 3 of the VAT Act which sets out the process of determining the OMV of a supply in different circumstances. The OMV is a VAT-inclusive concept and usually needs to be determined with reference to transactions between “connected persons” in certain circumstances, or where there are rules regarding the limitation of input tax. In simple terms, and in the context of supplies of “fixed property”, the OMV is the price (consideration) which could be obtained on the sale of the property between a willing buyer and a willing seller dealing at arm’s length in an open market. Similar terms such as “fair value” and “fair market value” are defined in section 1(1) of the Transfer Duty Act and section 1 of the TA Act respectively.
Owner	In relation to fixed property means the person in whose name the land is registered in the Deeds Registry concerned (if applicable) and also any successor in title of such person.
Person	Refers to the entity which is liable for VAT registration and includes – <ul style="list-style-type: none"> • sole proprietor, that is, a natural person; • company/close corporation; • partnership; • deceased/insolvent estate; • trust funds; • incorporated body of persons, for example an entity established under its own enabling Act of Parliament; • unincorporated body of persons, for example club, society or association with its own constitution; and • municipality/public authority.
Recipient	In relation to any supply of goods or services, means the person to whom the supply is made.
Rental agreement	Means an agreement entered into for the letting of goods.
Right of occupation	Means the right of a purchaser under a housing interest which confers the power to occupy a portion in a housing development scheme for the duration of the lifetime of the purchaser under the Housing Development Schemes for Retired Persons Act 65 of 1988. This could also include rights acquired by any other person mentioned in the contract in terms of which the housing interest is acquired (subject to the provisions of section 7 of that Act), but without conferring the power to claim transfer of the ownership of the portion to which the housing interest relates.
SARS	South African Revenue Service.
Second-hand goods	Means goods (including fixed property) that have been previously owned and used but excludes animals, gold coins, goods containing gold and certain “old order” mining rights.
Sectional title	This term is not defined in the Sectional Titles Act 95 of 1986, but it refers to a type of ownership in fixed property. An owner has full title to a particular demarcated section of a building which is known as a “unit” and is registered as such in the Deeds Registry concerned.

Services

Broadly defined and includes –

- the granting, assignment, cession, surrender of any right;
- the making available of any facility or advantage; and
- certain acts which are deemed to be services under section 8,

but excludes –

- a supply of “goods”;
- a supply of “money”; and
- any stamp, form or card which falls into the definition of “goods”.

Examples:

- Commercial services – electricians, plumbers, builders
- Professional services – lawyers
- Advertising agencies

Share block scheme

Means any scheme in terms of which a share, in any manner whatsoever confers a right to or an interest in the use of immovable property.

Supply

This definition is very wide and includes all forms of supply (including the expropriation of fixed property), irrespective of where the supply is effected and any derivative of supply is construed accordingly.

Tax invoice

This is a special document which is required to be held by a vendor to deduct input tax. The term is dealt with in section 20 which sets out what is required to be reflected on the document as follows:

Full tax invoice

The following details are required if the consideration is R5 000 or more, or is a zero-rated supply:

- The words “tax invoice”, “VAT invoice” or “invoice”
- Name, address and VAT registration number of the supplier
- Name and address of recipient, VAT registration number of the recipient
- Serial number and date of issue
- Accurate description of goods and/or services
- Quantity or volume of goods or services supplied
- Price and VAT

Abridged tax invoice

Should the amount (including VAT) be less than R5 000, the same requirements as above apply, except that the name, address and VAT registration number of the recipient and the quantity or volume does not need to be specified.

Tax period	<p>There are five different tax periods as follows:</p> <p>Category A - Two-monthly (ending at the end of every odd month), for example, January, March, May, July etc.</p> <p>Category B - Two monthly (ending at the end of every even month), for example, February, April, June etc.</p> <p>Category C - Monthly (taxable supplies greater than R30 million P/A).</p> <p>Category D - Six-monthly (certain farmers only – taxable supplies less than R1,5 million per annum).</p> <p>Category E - Annually (only in exceptional circumstances for connected persons with only one transaction per year).</p>
Taxable supply	<p>This is a supply which is chargeable with tax under the VAT Act. A taxable supply does not include any exempt supply listed in section 12, even if supplied by a registered vendor.</p> <p>There are two types of taxable supplies, namely –</p> <ul style="list-style-type: none">• those that attract the zero rate (listed in section 11); and• those on which the standard rate of 15% must be charged.
Time sharing	<p>Means the right to or interest in the exclusive use or occupation, during determinable periods during the year, of accommodation as envisaged in the Property Time-sharing Control Act 75 of 1983.</p>
VAT	<p>Value-added tax.</p>
Vendor	<p>This includes any person who is registered or is required to be registered for VAT. If the Commissioner has determined the date from which a person is a vendor, a person shall be a vendor from that date.</p>

Contact details

The **SARS website** contains contact details of all SARS branch offices and border posts.

Contact details appearing on the website under “Contact Us” (other than branch offices and border posts) are reproduced below for your convenience.

Digital channels

E-mail

- For tax practitioners: **pcc@sars.gov.za**
- For taxpayers: **contactus@sars.gov.za**

When you send an email to the above mailboxes, you will receive an automated reply with a case number assigned. For ease of use, this number will be quoted in related correspondence on the progress of the case.

SARS Online Query System

Use our Digital Service offerings offered by the SARS Online Query System (SOQS). Go to ‘Contact Us’ on the SARS website sars.gov.za and click on “Send us a Query”.

Online appointments

Use our online booking system to request an online appointment or before going to a SARS branch. Go to ‘Contact Us’ on the SARS website **www.sars.gov.za** and click on “Make an appointment”.

SARS Head Office

Physical Address

South African Revenue Service
Lehae La SARS
299 Bronkhorst Street
Nieuw Muckleneuk
0181
Pretoria

Postal Address

Private Bag X923
Pretoria
0001
South Africa

SARS website

www.sars.gov.za

Telephone

012 422 4000

SARS Fraud and Anti-Corruption hotline

0800 00 28 70

Complaints Management Office

Telephone
0860 12 12 16

SARS Website
www.sars.gov.za

Office
Any SARS Branch

Contact Centre
0800 00 7277

eFiling Website
www.sarsefiling.gov.za

SARS Contact Centres

- You may contact SARS by phone, e-mail or visiting a SARS Branch. Before visiting a branch, remember to “Make an Appointment”. Find the function under “Contact Us” on the **SARS website**.
- Call our SARS Contact Centre on 0800 00 7277
- International Callers may contact our Contact Centre on +27 11 602 2093

Practitioners

Telephone / Contact Centre
0800 00 72 77

E-mail
pcc@sars.gov.za

Business hours
Weekdays 8:00 – 16:00 (except Wednesdays)
Wednesdays 9:00 – 16:00

Before visiting a branch, remember to “Make an Appointment”. Find the function under “Contact Us” on the **SARS website**.

VAT Rulings

Should there be any aspects relating to VAT on which a specific VAT Ruling is required, you may submit a ruling application on a VAT301 to SARS by e-mail to **VATRulings@sars.gov.za**. All applications must comply with section 79 of the TA Act [excluding section 79(4)(f), (k) and (6)].