

DRAFT INTERPRETATION NOTE

DATE:

ACT : INCOME TAX ACT 58 OF 1962
SECTION : SECTION 30B(2)(b)(ix)
SUBJECT : ASSOCIATIONS: FUNDING REQUIREMENT

Please note: This Note was released as a draft in 2020. It has been updated to provide further clarity in response to some of the comments submitted, and is being released for a second round of public comment.

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Preamble

In this Note unless the context indicates otherwise –

- “**Commissioner**” means the Commissioner for the South African Revenue Service appointed under section 6 of the South African Revenue Service Act 34 of 1997, or the Acting Commissioner designated under section 7 of that Act;
- “**Companies Act**” means the Companies Act 71 of 2008;
- “**entity**” means an “entity” referred to in paragraphs (a) and (b) of the definition of “entity” in section 30B(1), namely, any mutual loan association, fidelity or indemnity fund, trade union, chamber of commerce or industry (or an association of such chambers), local publicity association, or professional body (see 3) approved by the Commissioner under section 30B(2);
- “**founding document**” means the written instrument such as the constitution or memorandum of incorporation under which an entity is established and governed;
- “**government**” means the government of South Africa in the national, provincial or local sphere contemplated in section 10(1)(a);
- “**mutual loan association**” means an “entity” referred to in paragraph (a) of the definition of “entity” and defined in section 30B(1) as an association of which the sole or principal object is to function as a voluntary savings association where participants make regular contributions into a common pool managed by the members for the mutual financial benefit of those members;
- “**NPC**” means a non-profit company as defined in the Companies Act;
- “**prescribed requirements**” mean the formal conditions and requirements set out in section 30B(2)(b), which an entity must provide for in its founding document and comply with in order to qualify for approval as an entity;
- “**section**” means a section of the Act;
- “**TA Act**” means the Tax Administration Act 28 of 2011;
- “**the Act**” means the Income Tax Act 58 of 1962;
- “**the Constitution**” means the Constitution of the Republic of South Africa, 1996; and
- any other word or expression bears the meaning ascribed to it in the Act.

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

1. Purpose

This Note provides guidance on the interpretation and application of the “funding” requirement contemplated in section 30B(2)(b)(ix), requiring that substantially the whole of an entity’s funding must be derived from its annual or other long-term members or from an appropriation by the government.

2. Background

The entities referred to in section 30B¹ fall outside the scope and income tax rules for public benefit organisations (PBOs)² and recreational clubs.³

The definition of “entity” in section 30B(1) provides for two distinct categories of entities, comprising –⁴

- mutual loan associations, fidelity or indemnity funds, trade unions, chambers of commerce or industry and local publicity associations;⁵ and
- professional bodies (see 3).⁶

The respective entities are diverse in nature but have in common that they usually do not have a profit motive nor do they provide any monetary gain or material advantage for their individual members.⁷ The entities are membership based and exist for the benefit of their members. Although these entities are established to conduct their activities with and for the benefit of their members, they are not prohibited from dealing with non-members within prescribed parameters (see 5.4).

The approval under section 30B(2) is limited to those entities that can demonstrate that substantially the whole (see 5.4) of their funding (see 5.1) is derived from their annual or other long-term members (see 5.2.1) or from an appropriation by the government (see 5.2.2).

Entities approved by the Commissioner under section 30B currently have the advantage of an absolute exemption on their receipts and accruals under section 10(1)(d)(iii) and (iv) (see 7).

3. General description of certain terminology in the context of section 30B(1)

The entities referred to in the definition of “entity” in section 30B(1) are not defined in the Act, with the exception of a mutual loan association (see *Preamble*). SARS has formulated descriptions based on literature reviewed which, amongst other things, includes research documents, reports and other web sources. The following entities are therefore described as follows:

- **“Chamber of commerce or industry (or an association of such chambers)”** means an “entity” referred to in paragraph (a) of the definition of “entity” in section 30B(1), which has as its sole or principal object the promotion, regulation and protection of the interests of the local business community and whose members comprise local business persons.

¹ Section 30B was inserted by section 55(1) of the Taxation Laws Amendment Act 7 of 2010 with effect from 2 November 2010, the date of promulgation of that Act.

² Section 30 provides for the approval of an organisation as a PBO. For more information, see *Tax Exemption Guide for Public Benefit Organisations in South Africa*.

³ Section 30A provides for the approval of an organisation as a recreational club. For more information, see *Tax Exemption Guide for Recreational Clubs*.

⁴ See *Explanatory Memorandum on the Taxation Laws Amendment Bill, 2010*, in paragraph 3.4.

⁵ Paragraph (a) of the definition of “entity” in section 30B(1).

⁶ Paragraph (b) of the definition of “entity” in section 30B(1).

⁷ No member under section 30B(2)(b)(v) may directly or indirectly have any personal or private interest in that entity.

- **“Fidelity or indemnity fund”** means an “entity” referred to in paragraph (a) of the definition of “entity” in section 30B(1), which has as its sole or principal object to indemnify or compensate any third party that suffers a loss or damages in consequence of any act or omission of a member of that fund in the rendering of a particular service by that member to that third party.
- **“Local publicity association”** means an “entity” referred to in paragraph (a) of the definition of “entity” in section 30B(1), which has as its sole or principal object to advertise and promote a particular local city, town, district or area to attract trade, tourism, visitors or industry.
- **“Trade union”** means an “entity” referred to in paragraph (a) of the definition of “entity” in section 30B(1), which functions as a representative body of workers in a certain sector, industry or commerce whose sole or principal object is to promote, protect and advance workers’ interests, rights and working conditions in the workplace whether individually or collectively.⁸
- **“Any NPC, society⁹ or other association of persons¹⁰ established to promote the common interests of persons, being members of such NPC, society or association of persons, carrying on any particular kind of business, profession or occupation”** means an “entity” referred to in paragraph (b) of the definition of “entity” in section 30B(1), which is normally a representative or regulatory body of members of a particular kind of business, profession or occupation, for example, a body for accountants, architects, engineers, lawyers, medical practitioners or scientists. Such a representative or regulatory body sets professional standards and qualifications for that particular business, profession or occupation, encourages sustainability, promotes the protection of the public from malpractice relating to the professional duties and responsibilities of representative or regulatory bodies and their members, encourages international leading practice, and raises the esteem for all businesses, professions or occupations in South Africa.¹¹ These representative or regulatory bodies are referred to in this Note as professional bodies.

4. The law

The relevant sections of the Act are quoted in **Annexure A**.

⁸ Trade unions are registered with the Department of Labour under section 95(7) of the Labour Relations Act 66 of 1995. This registration is voluntary.

⁹ The word “society” is described in *The Free Dictionary* as “a group of people broadly distinguished from other groups by mutual interests, participation in characteristic relationships, shared institutions, and a common culture” and “an organisation or association of persons engaged in a common profession, activity or interest”. See www.thefreedictionary.com/society [Accessed 16 September 2021].

¹⁰ An association of persons is generally established or formed by adopting a legal founding document. See GJ Pienaar “Formation” 2 (Third Edition Volume) *LAWSA* [online] (My LexisNexis: 28 February 2015) in paragraph 155.

¹¹ The National Qualifications Framework Act 67 of 2008 requires the South African Qualifications Authority (SAQA) to recognise professional bodies and register their professional designations on the national qualifications framework, which is a comprehensive system approved by the Minister of Higher Education and Training for the classification, registration, publication and articulation of quality-assured national qualifications.

5. Application of the law

The Commissioner must approve an entity for purposes of the exemption from income tax under section 10(1)(d)(iii) or (iv) if –¹²

- that entity has submitted to the Commissioner a copy of its founding document;¹³ and
- the founding document provides for all the prescribed requirements.¹⁴

The “funding” requirement is one of a number of prescribed requirements, for purposes of section 30B, which must be included in the founding document in order for an entity to be approved by the Commissioner, and to retain such approval for its receipts and accruals to qualify for exemption from income tax under section 10(1)(d)(iii) or (iv) (see 7). The other prescribed requirements are not addressed in this Note.

If the founding document of an entity does not provide for the prescribed requirements, the entity will be deemed to comply if the person who has accepted fiduciary responsibility for the funds and assets of the entity, furnishes the Commissioner with a written undertaking¹⁵ that the entity will be administered in compliance with the prescribed requirements.¹⁶

5.1 Meaning of “funding”

The word “funding” is not defined in the Act. The method of attributing meaning to the words used in legislation involves, as a point of departure, examining the language of the provision at issue, the language and design of the statute as a whole and its statutory purpose.¹⁷ In *C: SARS v Dunblane (Transkei) (Pty) Ltd*¹⁸ the court held that words in a section of an Act of Parliament must not be looked at in isolation but in the context in which they are found, both in the immediate context of the sub-section in which they occur and in the general context of the Act.

The word “fund” is described in the *Dictionary.com* as –¹⁹

“funds, money immediately available; pecuniary resources”.

The *Business Encyclopedia* explains “funding” as follows:²⁰

“The term funding refers simply to money the organization designates (budgets) for specific purposes, such as capital spending or an organization's operating budget.”

¹² Section 30B(2).

¹³ Section 30B(2)(a).

¹⁴ Section 30B(2)(b).

¹⁵ A specimen written undertaking form EI 2A is available to assist persons accepting fiduciary responsibility to administer an entity in accordance with the prescribed requirements.

¹⁶ Section 30B(4).

¹⁷ See *Chetty t/a Nationwide Electrical v Hart & another* 2015 (6) SA 424 (SCA).

¹⁸ 2002 (1) SA 38 (SCA), 64 SATC 51 at 57.

¹⁹ www.dictionary.com/browse/funding [Accessed 16 September 2021].

²⁰ www.business-case-analysis.com/funds-funding.html [Accessed 16 September 2021].

The word “funding” is described in *The Free Dictionary* as follows:²¹

“Funding is the act of providing financial resources, usually in the form of money, or other values such as effort or time, to finance a need, program, and project, usually by an organisation or government. Generally, this word is used when a firm uses its internal reserves to satisfy its necessity for cash, while the term financing is used when the firm acquires capital from external sources. Sources of funding include credit, venture capital, donations, grants, savings, subsidies and taxes. Funds can be allocated for either short-term or long-term purposes.”

Having regard to the above, the word “funding” in section 30B(2)(b)(ix) refers to the monetary resources an entity requires to finance its activities in the furtherance of its sole or principal object for which it has been established²² as set out in its founding document and under which it has obtained approval from the Commissioner. The word “funding” is a broader concept than income and is not interpreted to mean gross income.²³ In the context of section 30B(2)(b)(ix), “funding” therefore refers to all the sources of funding derived by an entity.

5.2 Prescribed sources of funding

Section 30B(2)(b)(ix) prescribes that substantially the whole (see 5.4) of an entity’s funding must be derived from –

- its annual members or other long-term members (see 5.2.1); or
- an appropriation by the government (see 5.2.2).

The use of the disjunctive word “or” means that substantially the whole of an entity’s funding must be derived from either one or a combination of the above prescribed sources of funding (see **Example 3**).

5.2.1 Funding derived from annual or other long-term members

The relief under section 10(1)(d)(iii) and (iv) is aimed at entities having members and who derive substantially the whole of their funding from either their annual or other long-term members.

The Act does not define “member” with the exception of defining the term “member” for purposes only of a fidelity or indemnity fund.²⁴ This definition also does not define a member as such but merely states that a member includes a contributor to that fund.

The word “member” is described in the *Oxford Dictionary, Thesaurus and Wordpower Guide* as –²⁵

“a person or organisation belonging to a group or society”.

²¹ <https://encyclopedia.thefreedictionary.com/funding> [Accessed 16 September 2021].

²² An entity is required under section 30B(2)(b)(iv) to use substantially the whole of its funds for the sole or principal object for which the entity has been established.

²³ The term “gross income” is defined in section 1(1).

²⁴ Section 30B(1).

²⁵ M Wait, S Hawker and C Soanes *Oxford Dictionary, Thesaurus and Wordpower Guide* (2001) Oxford University Press [Accessed 16 September 2021].

For purposes of the “funding” requirement, a member is not limited to only a natural person but may also include a juristic person, which is a legal entity separate and distinct from its members such as a company or close corporation.²⁶

Section 30B does not prescribe a minimum or maximum number of members that should belong to an entity since this may prejudice smaller entities. Section 30B also does not prescribe a minimum membership period but does require that an entity must at least have annual or other long-term members.

The word “annual” is described in the *Oxford Dictionary, Thesaurus and Wordpower Guide* as –²⁷

“occurring or recurring once in each year; continuing for the period of a year”.

The word “annual” referred to in the “funding” requirement therefore means lasting for a year, that is, a period of 12 months. The annual period is not required to coincide with a calendar year, the financial year or year of assessment of an entity.

If a member signs up for an annual membership in the middle of a year, that membership fee is regarded as derived from an annual member and will be included in the “substantially the whole” (see 5.4) calculation even though it is not in relation to a period of 12 months.

The word “long-term” is described in the *Lexico.com* as –²⁸

“occurring over or relating to a long period of time”.

Since section 30B distinguishes between annual and long-term members it can be inferred that long-term membership must run for a period longer than a year and that membership in general must not run for a period of less than 12 months.

The *BusinessDictionary.com* describes “membership” as follows:²⁹

“Belonging, either individually or collectively, to a group. Some memberships may require a fee to join or participate while some do not. Others, as in the case of MENSA, have specific skill requirements that must be reached prior to be accepted into the group. Special privileges or benefits are entitled to members although not all members may have the same rights and privileges. For example, a leader might have special rights that allow the individual to preside over meetings or create rules and guidelines for the group.”

An entity incorporated as an NPC electing to have members must set out in its memorandum of incorporation the –³⁰

- qualifications for membership;
- process for applying for membership;
- cost of membership in any class;

²⁶ The definition of “person” does not exclude companies, other incorporated entities, associations of persons, or statutory bodies. Also see, definition of “person” in section 2 of the Interpretation Act 33 of 1957.

²⁷ M Wait, S Hawker and C Soanes *Oxford Dictionary, Thesaurus and Wordpower Guide* (2001) Oxford University Press [Accessed 16 September 2021].

²⁸ www.lexico.com/definition/long-term [Accessed 16 September 2021].

²⁹ www.businessdictionary.com/definition/membership.html [Accessed 19 November 2020x].

³⁰ See item 4 of Schedule 1 to the Companies Act.

- rights and obligations of membership in any class; and
- grounds on which the membership may be suspended or terminated.

The membership of associations is explained by *LAWSA* as follows:³¹

“The rules of an association determine in the first instance which persons are eligible for membership of the association,

The rules of an association will usually set out the procedure which must be followed before prospective members are admitted. This could take the form of a written application coupled with formal notification of acceptance from the management committee, the payment of the prescribed membership fee and the placing of a new member’s name on the membership list.

The rights and duties which stem from membership depend on the provisions of the constitution. Generally speaking, members are, *inter alia*, entitled to enjoy the amenities and other privileges provided by the organisation. In turn, they must pay entrance and subscription fees or levies which may be called for under the constitution.”

(Footnotes omitted.)

It is clear from the above that an entity irrespective of whether it is constituted as an NPC, association of persons or society should set out the requirements and conditions for that entity’s membership in its founding document. The validity of membership of an entity is therefore evidenced by the presence of formal procedures for membership eligibility, acceptance and admittance as well as membership rights obtained after being accepted as a member. A non-member is therefore a person or organisation, which has not officially joined an entity.³²

Membership is usually granted if the particular qualifying criteria and requirements relating to membership of a particular entity as set out in their founding documents are complied with (see **Example 4** in **Annexure B**). The qualifying criteria and requirements as well as the membership categories a member may qualify for will differ from entity to entity. The personal particulars of qualifying members together with their privileges and rights are generally recorded in a membership register of an entity.

A member may or may not be required to pay a registration, joining or entrance fee, a membership fee, or a subscription to belong to an entity. The membership fees or subscriptions applicable to a particular membership category may vary from entity to entity (see **Example 4** in **Annexure B**).

³¹ GJ Pienaar “Associations” 2 (Third Edition Volume) *LAWSA* [online] (My LexisNexis: 28 February 2015) in paragraphs 162 to 164.

³² See the description of the word “non-member” in the *Cambridge English Dictionary* available online at <https://dictionary.cambridge.org/dictionary/english/non-member> [Accessed 16 September 2021].

In order to obtain the right to access various activities³³ provided by an entity or to enjoy various benefits associated with the membership of a particular entity a member may or may not be required to pay a fee in addition to the membership fee or subscription for such activities or benefits. For example –

- a local businessperson may become a member of a local publicity association to enjoy the benefit of being listed on the local business directory available on the internet, enabling access to advertising opportunities, and to establish and maintain contacts through networking opportunities beneficial to that businessperson;
- a local businessperson may become a member of a chamber of commerce or industry to obtain business, trade, legal, labour and taxation information, advice and assistance, and network with other local business stakeholders and foreign delegates and dignitaries to enhance the person's business performance and profile;
- an employee may become a member of a trade union to gain access to legal advice and assistance should a dispute arise with that member's employer;
- a professional person may become a member of a professional body to participate in seminars, webinars, workshops and other training activities aimed at enhancing the particular skills and expertise required in that particular profession or industry thus ensuring development and enabling the person to remain up-to-date with policies and practices within that particular profession or industry. A professional person may also become a member of a professional body to obtain professional indemnity insurance to protect the member against any potential claims by clients deeming work produced or professional advice provided by that member as being inadequate.

Any funding derived by an entity from its members will meet the "funding" requirement provided it aligns with the entity's funding model. This does not limit funding derived by an entity to only membership fees or subscriptions and may therefore include, for example, donations, rental income, conference or examination fees from members (see **Annexure B**).

5.2.2 Funding derived from an appropriation by government

Government is understood as the governing body of a state³⁴ and is the exclusive power in which the administration of a state is vested. The government is according to the Constitution³⁵ constituted as national,³⁶ provincial³⁷ and local³⁸ spheres of government,³⁹ which are distinctive, interdependent and interrelated. The different levels of government therefore all have legislative and executive authority in their own spheres. The Constitutional Court held in *Minister of Defence and Military Veterans v*

³³ An entity must under section 30B(2)(b)(vi) direct substantially the whole of its activities to the furtherance of its sole or principal object and not for the specific benefit of an individual member or minority group.

³⁴ www.lexico.com/en/definition/government [Accessed 16 September 2021].

³⁵ Section 40(1) of the Constitution.

³⁶ Chapter 5 of the Constitution.

³⁷ Chapter 6 of the Constitution.

³⁸ Chapter 7 of the Constitution.

³⁹ The receipts and accruals of the government are exempt from income tax under section 10(1)(a).

*Thomas*⁴⁰ that within its constitutional sphere of competence each sphere of government reigns supreme.

The national sphere of government is the central government administration and consists of the national parliament and the different state departments as determined by the President.⁴¹ The provincial sphere of government consists of the nine provincial legislatures and the respective provincial departments.⁴² The local sphere of government consists of municipalities.⁴³

Entities granted approval by the Commissioner under section 30B(2) are placed in a favourable position because their receipts and accruals are exempt under section 10(1)(d)(iii) or (iv) (see 7). The courts have tended to reject a construction of a statutory provision, which implies the extension of a class privilege and to interpret it strictly.⁴⁴ It is for this reason that the word “government” referred to in section 30B(2)(b)(ix) must be interpreted strictly so as not to include any other state entities, for example, entities established as agents of the government or organs of state.⁴⁵ This is supported by section 10(1)(a), which clearly separates the three spheres of government from their controlled agencies and other independent bodies.

The word “appropriation” referred to in the “funding” requirement is not defined in the Act. It is described in the *Dictionary.com* as –⁴⁶

- “1 the act of appropriating.
- 2 anything appropriated for a special purpose, especially money.
- 3 an act of a legislature authorizing money to be paid from the treasury for a specified use”.

Any funds specifically allocated to an entity by any sphere of government will be regarded as an appropriation by the government as contemplated in the “funding” requirement.

Example 1 – Example of funding derived by an entity, which is not from an appropriation by the government

Facts:

A professional body provides educational activities to future recruits, which is partially funded by FASSET, which is the sector education and training authority (SETA) established by the Minister of Higher Education and Training under the Skills Development Act 97 of 1998 for the finance, accounting, management consulting and other financial services sector.

⁴⁰ 2016 (1) SA 103 (CC).

⁴¹ For a list of National Departments, see Schedule 1 to the Public Service Act 103 of 1994.

⁴² For a list of Provincial Departments, see Schedule 2 to the Public Service Act 103 of 1994.

⁴³ The Local Government: Municipal Structures Act 117 of 1998 regulates the establishment of municipalities.

⁴⁴ This rule was laid down in *Ernst v CIR* 1954 (1) SA 318 (A), 19 SATC 1 and approved in *CIR v D & N Promotions (Pty) Ltd* 1995 (2) SA 296 (A), 57 SATC 178 at 182 and *Western Platinum Ltd v C: SARS* [2004] 4 All SA 611 (SCA), 67 SATC 1 at 6.

⁴⁵ See paragraph (b) of the definition of “organ of state” in section 239 of the Constitution.

⁴⁶ www.dictionary.com/browse/appropriation [Accessed 16 September 2021].

Typically 90% of the professional body's funding is derived from FASSET to cover the costs relating to training, exams, transcripts and overall related administration.

Result:

FASSET is not within the national, provincial or local sphere of government. FASSET is regarded as an institution, board or body established under the Skills Development Act, 1998, as contemplated in section 10(1)(cA)(i).

The professional body therefore does not meet the funding requirement of section 30B(2)(b)(ix) since substantially the whole of its funding is not derived from an appropriation by government.

5.3 Funding derived from sources other than from members or an appropriation by government

This Note does not discuss in detail all the sources of funding, which an entity may derive. Other sources of funding will include funding derived by an entity, which is not from that entity's annual or long-term members or from an appropriation by the government. This may include funding derived from non-members, for example, foreign capital grants, foreign donor funding, and donations from non-members (see **Examples 2, 4 and 5** in **Annexure B**). The facts and circumstances of each case will determine whether an entity's funding was derived from the prescribed sources (see **5.2**).

Employers sometimes pay an employee's annual membership fee to a professional body, especially if such membership is a prerequisite of the employee's employment, such as a medical practitioner's membership of the Health Professions Council of South Africa. In such an instance, the entity's funding is derived from the member notwithstanding payment by the employer.

Investment income⁴⁷ earned on funds or capital is not related to an entity's annual or long-term members or from an appropriation by the government regardless of whether the funds invested were originally derived from members or from an appropriation by the government.⁴⁸ If funds invested are derived from a mixture of sources, for example, from members, an appropriation by government and non-members it becomes onerous and cumbersome to determine the source of member's and government funds and could be subject to abuse. Investment income is therefore regarded as funding derived from a source other than the prescribed sources of funding (see **5.2**).

The sum of all the other sources of funding, excluding funding derived from the prescribed sources of funding, may not exceed 15% of the total funding derived by an entity (see **5.4**). The facts and circumstances of each case will determine whether the "funding" requirement is met.

⁴⁷ An entity must in accordance with section 30B(2)(b)(iv) use substantially the whole of its funds for the sole or principal object for which that entity has been established.

⁴⁸ See *Western Platinum Ltd v C: SARS* [2004] 4 All SA 611 (SCA), 67 SATC 1.

5.4 Substantially the whole of an entity's funding

The expression “substantially the whole” is not defined in the Act. In Binding General Ruling (Income Tax) 20 “Interpretation of the Expression ‘Substantially the Whole’ ” it is stated that in the strict sense the expression “substantially the whole” is regarded by SARS to mean 90% or more. However, since the entities contemplated in section 30B operate in an uncertain environment making proper planning difficult, SARS will accept a percentage of not less than 85%. This is to ensure that entities approved by the Commissioner do not enjoy an unfair advantage over other taxable entities conducting similar income-generating activities and to permit small-scale self-sustainability.

The total funding of an entity, that is, the total of all income irrespective of whether such income is of a revenue or capital nature received by or accrued to an entity for a particular year of assessment⁴⁹ before the deduction of any expenses or allowable deductions must be used to calculate whether an entity complies with the “substantially the whole” of the “funding” requirement. See **Annexure B** for examples providing a step-by-step approach for calculating “substantially the whole” of an entity's funding to determine compliance with the “funding” requirement.

Example 2 – “Substantially the whole” of an entity's funding

An entity, which derives –

- 55% of its funding from foreign capital grants, will not meet the “substantially the whole” of the “funding requirement;
- 30% of its funding from donations from non-members, will not meet the “substantially the whole” of the “funding requirement;
- 35% of its funding from levies imposed from non-members, will not meet the “substantially the whole” of the “funding requirement;
- 65% of its funding from membership fees and 20% of its funding from foreign donor funding, will not meet the “substantially the whole” of the “funding requirement; and
- 45% of its funding from membership fees, 20% of its funding from rental income from its members, 15% from the use of a canteen by its members and 5% of its funding from donations from its members, will meet the “substantially the whole” of the “funding” requirement.

An entity will meet the “funding” requirement even though substantially the whole of its funding is not derived from its annual or other long-term members, but substantially the whole is derived from an appropriation by the government.

The “funding” requirement will also be met if at least 85% of an entity's funding is derived from a combination of its annual or long-term members and from an appropriation by the government.

⁴⁹ The term “year of assessment” is defined in section 1(1). See Interpretation Note 90 “Year of Assessment of a Company: Accounts Accepted to a Date Other Than the Last Day of a Company's Financial Year” and Interpretation Note 19 “Year of Assessment of Natural Persons and Trusts: Accounts Accepted to a Date Other Than the Last Day of February”.

Example 3 – Funding derived by an entity from a combination of an appropriation by the local sphere of government and from its members

Facts:

A local publicity association has been formed to promote, advertise and develop a small town in the Eastern Cape to attract trade, tourism, and commerce or industry within that particular town.

Municipality X has an interest in attracting investment to the town that is under its jurisdiction. Furthermore, Municipality X has a responsibility to support the growth of local enterprises through small business coalitions and also to develop and attract tourism to that particular town. Municipality X has made funds available to the local publicity association to achieve these objectives.

The local publicity association used the funds to develop a website, brochure and a guide listing and advertising the local businesses, artists and crafters as well as promoting the local attractions in the area such as the wildlife, birds, plants and the Karoo landscape in general as well as the local attractions and museums.

The local publicity association derives 95% of its funding from the municipality and 5% from contributions from its annual or other long-term members comprising interested individuals and businesses who have a direct interest in the town.

Result:

The local publicity association qualifies as an “entity” under paragraph (a) of the definition of that term in section 30B(1). It will meet the “funding” requirement under section 30B(2)(b)(ix), since substantially the whole of its funding is derived from a combination of an appropriation from the local sphere of government (95%) and from its members (5%).

Non-compliance with the “substantially the whole” of the “funding” requirement will result in an entity not being approved under section 30B(2) or may result in an entity, which has been approved by the Commissioner losing its tax-exempt status and being regarded as a taxable entity subject to income tax (see **Example 5** in **Annexure B**).

6. Withdrawal of approval

The Commissioner may withdraw the approval of an entity if that entity has, in any year of assessment in any material respect or on a continuous or repetitive basis, failed to comply with section 30B or with its founding document as it relates to that section.⁵⁰

The Act does not specify what constitutes a “material, continuous, or repetitive” failure by an entity. The *CollinsDictionary.com* provides the following descriptions:

- “Material” as “material evidence or information is directly relevant and important in a legal or academic argument.”⁵¹

⁵⁰ Section 30B(5).

⁵¹ www.collinsdictionary.com/dictionary/english/material [Accessed 16 September 2021].

- “Continuous” as “a continuous process or event continues for a period of time without stopping.”⁵²
- “Repetition” as “a thing, word, action, etc. that is repeated.”⁵³

A failure by an entity to comply with section 30B in any material respect may therefore include a significant, relevant, and important failure. A failure on a continuous basis may be prolonged without interruption, while a failure on a repetitive basis may be done many times in the same manner by the entity.

The Commissioner may withdraw the approval in any of the above circumstances but must decide each case on its own facts and circumstances. Notice must be given to the transgressing entity of the intention to withdraw the approval and also specify a period within which corrective steps must be taken.

If no corrective steps are taken by the entity within the period stated in the notice, the approval will be withdrawn from the beginning of the year of assessment in which the non-compliance or failure by the entity occurred.⁵⁴ The decision to withdraw the approval is subject to objection and appeal (see 8).

On withdrawal of its approval, the affected entity must transfer or take reasonable steps to transfer its remaining assets within six months or a longer period allowed by the Commissioner to specified entities.⁵⁵ Failure to do so will result in the inclusion of an amount in its taxable income.⁵⁶ A detailed discussion of the consequences of the withdrawal of an entity’s approval does not form part of the scope of this Note.

7. Receipts and accruals exempt from income tax

The receipts and accruals of any entity approved by the Commissioner under section 30B are exempt from the payment of income tax under section 10(1)(d)(iii) or (iv), respectively. The exemption granted under section 10(1)(d)(iii) and (iv) is an absolute exemption. All receipts and accruals falling within gross income,⁵⁷ being the total amount, in cash or otherwise, received by or accrued to or in favour of an entity, will be exempt from income tax under section 10(1)(d)(iii) and (iv).

An amount will be “received” by a person as envisaged in the Act only if the person receives it on his or her own behalf and for his or her own benefit.⁵⁸ An amount “accrues” to a person when the person is entitled to it and when the person’s right to the amount is unconditional.⁵⁹ An amount is included in a person’s gross income in the year of assessment in, which that person receives it or the year of assessment in, which it accrues to that person, whichever comes first.⁶⁰

⁵² www.collinsdictionary.com/dictionary/english/continuous [Accessed 16 September 2021].

⁵³ www.collinsdictionary.com/dictionary/english/repetition [Accessed 16 September 2021].

⁵⁴ Section 30B(6).

⁵⁵ Section 30B(7).

⁵⁶ Section 30B(9).

⁵⁷ Section 1(1).

⁵⁸ *Geldenhuys v CIR* 1974 (3) SA 256 (C), 14 SATC 419.

⁵⁹ *Lategan v CIR* 1926 CPD 203, 2 SATC 16; *Ochberg v CIR* 1933 CPD, 6 SATC 1.

⁶⁰ *SIR v Silverglen Investments (Pty) Ltd* 1969 (1) SA 365 (A), 30 SATC 199.

Receipts or accruals of a capital nature that are not specifically included in gross income would not be included in the receipts and accruals referred to in the opening words of section 10(1)(d) since they do not require exemption. Receipts or accruals of a capital nature are taken into account in determining a taxable capital gain, which is included directly in paragraph (b) of the definition of “taxable income” in section 1(1). While a taxable capital gain is potentially subject to income tax, the exemptions in section 10 do not apply to it because a taxable capital gain is included directly in taxable income and does not comprise “income” (gross income less exempt income).⁶¹ Any capital gain or capital loss determined on an asset donated or bequeathed to a professional body exempt under section 10(1)(d)(iv) must be disregarded by the donor.⁶² A person must disregard any capital gain or capital loss on the disposal of an asset when any amount constituting gross income of whatever nature would be exempt from tax under section 10(1)(d) were it to be received by or to accrue to that person.⁶³

8. Objection and appeal

Any decision of SARS in the exercise of its discretion under section 30B is subject to objection and appeal in accordance with Chapter 9 of the TA Act.⁶⁴

An entity may object within 30 days from the date of a decision by the Commissioner under section 30B, for example, not to approve an entity.

The objection must be made on the prescribed form and specify in detail the grounds on which it is made.⁶⁵ SARS will consider the objection and may disallow the objection or allow the objection completely or in part.

If on disallowance of the objection the entity is dissatisfied with the decision by SARS, it may appeal against the disallowance. Such appeal must be in writing and lodged with SARS within the prescribed period.

9. Record-keeping

An entity must adhere to all applicable compliance obligations under the TA Act, for example, record-keeping, returns, assessments, dispute resolution (see **8**), interest, refunds and anti-avoidance.

All entities are required to keep records for five years⁶⁶ from the date of the submission of a return⁶⁷ under the TA Act.

⁶¹ For more information, see *Comprehensive Guide to Capital Gains Tax*.

⁶² Paragraph 62(c) of the Eighth Schedule to the Act.

⁶³ Paragraph 63 of the Eighth Schedule to the Act.

⁶⁴ Section 3(4)(b).

⁶⁵ The rules for objections and appeals are formulated under section 103 of the TA Act and published in Government Notice 550 in *Government Gazette* 37819 of 11 July 2014. For more information on the resolution of tax disputes, see *Dispute Resolution Guide: Guide on the Rules Promulgated in terms of Section 103 of the Tax Administration Act, 2011* and *Alternative Dispute Resolution: Quick Guide*.

⁶⁶ Section 29(3) of the TA Act.

⁶⁷ The term “return” is defined in section 1 of the TA Act and includes any form, declaration, document or other manner of submitting information to SARS that incorporates a self-assessment or is the basis on which an assessment is to be made by SARS.

A person must keep the records, books of account or documents that –⁶⁸

- enable the person to observe the requirements of a tax Act;
- are specifically required under a tax Act or by the Commissioner by public notice; and
- enable SARS to be satisfied that the person has observed these requirements.

The records must be kept or retained in –⁶⁹

- their original form in an orderly fashion and in a safe place;
- the form, including electronic form,⁷⁰ as may be prescribed by the Commissioner in a public notice;⁷¹ or
- a form specifically authorised by a senior SARS official.

These records should be available for inspection purposes by a SARS official to verify compliance with the requirements as explained above, or for purposes of an inspection, audit or investigation.⁷²

Records that are relevant to an audit, investigation, an objection, or appeal must be retained until the audit or investigation is concluded or until the assessment or the decision becomes final in the event of an objection or appeal (in case the five-year retention period is exceeded).⁷³

Books of account should at least be compiled in a manner that indicates compliance with the “funding” and spending requirements of section 30B.

An entity is not exempted from the obligation to deduct or withhold employees’ tax if the entity qualifies as an employer.⁷⁴ The entity must register as an employer for employees’ tax purposes within 21 business days of becoming an employer and submit monthly EMP201s.

10. Conclusion

In order to be approved under section 30B(2), an entity must satisfy the Commissioner that, amongst other things, substantially the whole of its funding is derived from its annual or other long-term members or from an appropriation by the government.

An entity bears the onus of proving that it complies with the requirements relative to the approval as discussed in this Note⁷⁵ and must retain the necessary evidence to support the view taken.⁷⁶ The burden may be discharged by way of supporting evidence submitted by the entity, provided such evidence is reasonable.

⁶⁸ Section 29(1) of the TA Act.

⁶⁹ Section 30(1) of the TA Act.

⁷⁰ For more information, see *Electronic Communications Guide*.

⁷¹ See Government Notice 787 in *Government Gazette* 35733 of 1 October 2012.

⁷² Section 31 of the TA Act.

⁷³ Section 32 of the TA Act.

⁷⁴ See definition of “employer” in paragraph 1 of the Fourth Schedule to the Act.

⁷⁵ Section 102 of the TA Act.

⁷⁶ Section 29 of that Act.

It is a factual enquiry whether an entity complies with the “funding” requirement and since the facts and circumstances pertaining to each entity differ, each case will be considered on its own merits.

Leveraged Legal Products
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Annexure A – The law

Section 10(1)(d)(iii) and (iv)

10. Exemptions.—(1) There shall be exempt from normal tax—

- (d) the receipts and accruals of any—
 - (i)
 - (ii)
 - (iii) mutual loan association, fidelity or indemnity fund, trade union, chamber of commerce or industries (or an association of such chambers) or local publicity association approved by the Commissioner in terms of section 30B; or
 - (iv) company, society or other association of persons established to—
 - (aa)
 - (bb) promote the common interests of persons (being members of such company, society or association of persons) carrying on any particular kind of business, profession or occupation,
approved by the Commissioner in terms of section 30B;

Section 30B

30B. Associations.—(1) For the purposes of this section—

“**entity**” means—

- (a) any mutual loan association, fidelity or indemnity fund, trade union, chamber of commerce or industry (or an association of such chambers) or local publicity association; or
- (b) any—
 - (i) non-profit company as defined in section 1 of the Companies Act;
 - (ii) society; or
 - (iii) other association of persons,
established to promote the common interests of persons (being members of the company, society or association of persons) carrying on any particular kind of business, profession or occupation,

approved by the Commissioner in accordance with subsection (2);

“**member**” in the case of a fidelity or indemnity fund includes a contributor to that fund;

“**mutual loan association**” means an association of which the sole or principal object is to function as a voluntary savings association where participants make regular contributions into a common pool managed by the members for the mutual financial benefit of those members.

(2) Subject to subsections (3) and (4), the Commissioner must approve an entity for the purposes of section 10(1)(d)(iii) or (iv) if—

- (a) that entity has submitted to the Commissioner a copy of the constitution or written instrument under which it has been established;
- (b) the constitution or written instrument contemplated in paragraph (a) provides that—
 - (i) the entity must have a committee, board of management or similar governing body consisting of at least three persons, who are not connected persons in relation to each other, to accept the fiduciary responsibility of that entity;
 - (ii) no single person may directly or indirectly control the decision-making powers relating to that entity;

- (iii) the entity may not directly or indirectly distribute any of its funds or assets to any person other than in the course of furthering its objectives;
- (iv) the entity is required to utilise substantially the whole of its funds for the sole or principal object for which it has been established;
- (v) no member may directly or indirectly have any personal or private interest in that entity;
- (vi) substantially the whole of the activities of the entity must be directed to the furtherance of its sole or principal object and not for the specific benefit of an individual member or minority group;
- (vii) the entity may not have a share or other interest in any business, profession or occupation which is carried on by its members;
- (viii) the entity must not pay to any employee, office bearer, member or other person any remuneration, as defined in the Fourth Schedule, which is excessive, having regard to what is generally considered reasonable in the sector and in relation to the service rendered;
- (ix) substantially the whole of the entity's funding must be derived from its annual or other long-term members or from an appropriation by the government of the Republic in the national, provincial or local sphere;
- (x) the entity must as part of its dissolution transfer its assets to—
 - (aa) another entity approved by the Commissioner in terms of this section;
 - (bb) a public benefit organisation approved in terms of section 30;
 - (cc) an institution, board or body which is exempt from tax under section 10(1)(cA)(i); or
 - (dd) the government of the Republic in the national, provincial or local sphere;
- (xi) the persons contemplated in paragraph (b)(i) will submit any amendment of the constitution or written instrument of the entity to the Commissioner within 30 days of its amendment;
- (xii) the entity will comply with such reporting requirements as may be determined by the Commissioner from time to time; and
- (xiii) the entity is not knowingly and will not knowingly become a party to, and does not knowingly and will not knowingly permit itself to be used as part of, an impermissible avoidance arrangement contemplated in Part IIA of Chapter III, or a transaction, operation or scheme contemplated in section 103(5).

(3) The requirements contained in subsection (2)(b)(iii) and (v) do not apply in respect of a mutual loan association.

(4) Where the constitution or written instrument of an entity does not comply with subsection (2)(b), the Commissioner may deem it to so comply if the person who has accepted fiduciary responsibility for the funds and assets of that entity furnishes the Commissioner with a written undertaking that the entity will be administered in compliance with that subsection.

(5) Where the Commissioner is—

- (a) satisfied that any entity approved in terms of subsection (2) has during any year of assessment in any material respect; or
- (b) during any year of assessment satisfied that any such entity has on a continuous or repetitive basis,

failed to comply with this section, or the constitution or written instrument under which it was established to the extent that it relates to this section, the Commissioner must notify the entity that he or she intends to withdraw approval of the entity if corrective steps are not taken by the entity within the period stated in the notice.

(6) If no corrective steps are taken by the entity contemplated in subsection (5), the Commissioner must withdraw approval of that entity with effect from the commencement of the year of assessment contemplated in subsection (5).

(7) If the Commissioner has withdrawn the approval of an entity as contemplated in subsection (6) the entity must within six months after the date of the withdrawal of approval (or such longer period as the Commissioner may allow) transfer, or take reasonable steps to transfer, its remaining assets to any entity, public benefit organisation, institution, board or body or the government of the Republic, contemplated in subsection (2)(b)(x).

(8) If an entity is wound up or liquidated, the entity must, as part of the winding-up or liquidation, transfer its assets remaining after the satisfaction of its liabilities to any entity, public benefit organisation, institution, board or body or the government of the Republic, contemplated in subsection (2)(b)(x).

(9) If an entity fails to transfer, or to take reasonable steps to transfer, its assets as contemplated in subsection (7) or (8), an amount equal to the market value of those assets which have not been transferred less an amount equal to the bona fide liabilities of that entity must for the purposes of this Act be deemed to be an amount of taxable income which accrued to that entity during the year of assessment in which the withdrawal of approval in terms of subsection (6) or the winding-up or liquidation contemplated in subsection (8) took place.

(10) Any person who is in a fiduciary capacity responsible for the management or control of the income and assets of any approved association and who intentionally fails to comply with any provision of this section or of the constitution, or other written instrument under which such association is established to the extent that it relates to the provisions of this section, shall be guilty of an offence and liable on conviction to a fine or to imprisonment for a period not exceeding 24 months.

Annexure B – Calculation of “substantially the whole” of the “funding” requirement

The following examples provide a step-by-step approach to calculate “substantially the whole” to determine compliance with the “funding” requirement.

Example 4 – Calculation to determine whether “substantially the whole” of the entity’s funding is derived from the prescribed sources of funding*Facts:*

According to its founding document, ABC’s object is to promote the interests of its members who are engineers. This object is achieved by providing research affecting the engineering profession, publishing journals, books, pamphlets or other publications, providing learning including examinations, regular conferences and workshops and other professional development, promoting and ensuring a high standard of professional behaviour by members in order to preserve and maintain the integrity and status of the profession.

Membership of ABC is open to all individuals and bodies that have an interest in the goals of ABC. The Executive Committee of ABC considers applications for membership. Membership lasts from 1 January to 31 December. Membership is automatically renewed by payment of membership fees before 31 March of each year except for student membership, which is granted on an annual basis (proof of student registration is a requirement for annual membership).

ABC has the following five membership categories:

1. Honorary membership

ABC’s Executive Committee may bestow such membership on a person who in its opinion has made a valuable contribution to the advancement of engineering. A member will retain such membership for life. Membership fees will be 50% of the annual ordinary membership fee.

2. Ordinary membership

Any individual who has an interest in the mission and goals of ABC.

3. Affiliated membership

Open to companies, societies or other organisations having an interest in the aims of ABC.

4. Senior membership

Any member who has reached the age of 65 and who was a member for 10 years before turning 65 may apply for senior membership of the entity.

5. Student membership

A person will qualify for student membership only if the person is a full-time registered engineering student up to and including Masters studies at a South African higher educational institution. Doctoral students will be registered as ordinary members.

The membership fees for the relevant membership categories are as follows:

| | R |
|------------------|-------|
| Honorary member | 1 150 |
| Ordinary member | 2 300 |
| Affiliate member | 4 600 |
| Senior member | 600 |
| Student member | 200 |

The current membership of ABC and membership fees derived from its annual or other long-term members amounting to R1 567 200 is constituted as follows:

| | R |
|--|------------------|
| 350 Student members | <u>70 000</u> |
| Total membership fees derived from annual members | <u>70 000</u> |
| 28 Honorary members | 32 200 |
| 320 Ordinary members | 736 000 |
| 150 Affiliate members | 690 000 |
| 65 Senior members | <u>39 000</u> |
| Total membership fees derived from other long-term members | <u>1 497 200</u> |

The total amount received or accrued for the year of assessment is R3 217 200 and comprises the following:

| | R |
|--|------------------|
| Membership fees | 1 567 200 |
| Seminars and courses | 700 000 |
| Registration and entrance fees | 200 000 |
| Training and examination fees | <u>350 000</u> |
| Total funding derived from annual or other long-term members | <u>2 817 200</u> |
| Investment income | 300 000 |
| Seminar and course fees derived from non-members | <u>100 000</u> |
| Total funding derived from sources other than from members | <u>400 000</u> |

ABC applied to the Commissioner for approval under section 30B(2) for its receipts and accruals to be exempt from income tax under section 10(1)(d)(iv).

Result:

Total funding derived from members / Total funding × 100% must not be less than 85%.

$$R2\,817\,200 / (R3\,217\,200) \times 100\% = 88\%$$

ABC derives 88% of its funding from its annual or other long-term members. ABC therefore complies with the “substantially the whole” of the “funding” requirement under section 30B(2)(b)(ix).

The Commissioner may approve ABC for purposes of section 10(1)(d)(iv) if all the prescribed requirements of section 30B(2) have been met.

Example 5 – Calculation to determine whether “substantially the whole” of the entity’s funding is derived from the prescribed sources of funding

Facts:

XYZ is an employee organisation registered as a trade union under the Labour Relations Act 66 of 1995. The aims and objects of XYZ include, amongst other things, to promote the interests of its members, to improve wage and workplace conditions, to contest arbitrary and unfair dismissal of its members, and to provide legal assistance in matters relating to members’ employment. XYZ has been approved by the Commissioner under section 30B(2), as XYZ is a trade union and qualifies as an “entity” under paragraph (a) of the definition of “entity” in section 30B(1). The receipts and accruals of XYZ are therefore exempt from income tax under section 10(1)(d)(iii).

The following receipts and accruals are reflected for a year of assessment:

| | R |
|--|--------------------|
| Annual members | 20 000 000 |
| Other long-term members | <u>100 000 000</u> |
| Total membership fees | 120 000 000 |
| Agency fees (see Note 1) | 30 000 000 |
| Commission received (see Note 2) | 10 000 000 |
| Rental income (see Note 3) | 15 000 000 |
| Sale of branded merchandise to members | 3 000 000 |
| Donations received from members | 800 000 |
| Investment income | 400 000 |
| Advertisements | <u>200 000</u> |
| Total receipts and accruals | <u>179 400 000</u> |

Notes:

1. An agency shop agreement with the employer has been concluded. Agency fees are therefore deducted by the employer from the wages of employees who are non-members of XYZ.
2. XYZ, in addition to its core business as a trade union as set out in its founding document, also offers its members a range of benefits through various service providers at discounted rates. Such benefits include, for example, insurance products, funeral schemes and services, personal loans, financing for studies and healthcare-related products. XYZ receives commission from the various service providers when members invest in or purchase such any such services or products.
3. Rental income is derived from the letting of various holiday apartments to members.

Result:

Step 1: Identify receipts and accruals derived from members

| | R |
|--|--------------------|
| Membership fees | 120 000 000 |
| Rental income (see Note 3) | 15 000 000 |
| Sale of branded merchandise to members | 3 000 000 |
| Donations received from members | <u>400 000</u> |
| Total receipts and accruals from members | <u>138 400 000</u> |

Step 2: Calculate whether substantially the whole of XYZ's funding is derived from its members

Total funding derived from members / Total funding × 100% must not be less than 85%.

$$R138\,400\,000 / R179\,400\,000 \times 100\% = 77\%$$

XYZ derives 77% of its funding from its annual or other long-term members. XYZ therefore does not comply with the "substantially the whole" funding requirement for this particular year of assessment.