REPUBLIC OF SOUTH AFRICA

IN THE TAX COURT OF SOUTH AFRICA

GAUTENG LOCAL DIVISION, JOHANNESBURG

Case No.: **14302**

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

14/02/2024
DATE ______________________ SIGNATURE

In the matter between:

ABD Limited **Appellant**

and

THE COMMISSIONER FOR THE SOUTH AFRICAN REVENUE SERVICE **Respondent**

J U D G M E N T

This judgment was prepared and authored by the Judge whose name is reflected and is handed down electronically by circulation to the Parties / their legal representatives by email and by uploading it to the electronic file of this matter on CaseLines. The date of the judgment is deemed to be 14 February 2024.

MANOIM, J

[1] In this case ABD Limited appeals against an increased assessment imposed on it by the Commissioner for South African Revenue Service (SARS) (the respondent). The case raises certain unique questions about a practice known as transfer pricing.

[2] ABD is a South African telecommunications company with subsidiaries worldwide. These subsidiaries are operating companies, with local shareholders, but having ABD as a significant shareholder. ABD licences its intellectual property to these operating companies (from now on referred to as Opcos) in return for which they pay ABD a royalty.

[3] The present case involves the royalty payments made by fourteen of the Opcos to ABD during the periods 2009 to 2012. ABD charged all of them the same royalty rate of 1% for the right to use its intellectual property. The extent of what that right represented is in dispute. The calculation of the royalty rate is based on two factors. The size of the profit earned by the Opco from the use of the IP and then how that profit is divided between the Opco and ABD. ABD's counsel came up with a useful metaphor to describe this exercise. He said the first determination is about the size of the pie and the second about how to divide the pie.

[4] What emerges in this litigation is that there are different methodologies that experts may use in performing these calculations. Nevertheless, there is at least an agreement on the principle to be applied. The royalty must be at arms-length – i.e., what would it be if it was between two independent enterprises as opposed to a company taxed in one jurisdiction and its subsidiary taxed in another.

[5] In 2011 ABD retained the services of a consultancy known as Company A to advise it on what royalty it should charge its various Opcos. Company A procured research on the subject and then, informed by that, came up with the recommendation that a royalty of 1% could be justified.

[6] SARS contends that the 1% is not an arms-length royalty. On various occasions it issued an additional assessment to increase the royalty. SARS relied on the Commissioner's powers in terms of section 31(2) of the Income Tax Act 58 of 1962 (Income Tax Act) to do so.

[7] That section in its then formulation provided that:

> "31(2) Where any supply of goods or services has been effected—
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> (*a*) between—
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> (i) (aa) a resident; and
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> (bb) any other person who is not a resident; or
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> (ii) …
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> (*b*) at price which is either—
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> (i) less than the price which such goods or services might have been expected to fetch if the parties to the transaction had been independent persons dealing at arm's length (such price being the arm's length price); or
>
> (ii) …
>
> the Commissioner may...in the determination of the taxable income of either the acquirer or supplier, adjust the consideration in respect of the transaction to reflect an arm's length price for the goods or services."

[8] Put more succinctly the Commissioner had the power to adjust the consideration to reflect an arm's length price if he considered the price received was less than it would have been in an arm's length transaction between independent persons. That begs the question central to this case; how does one determine an arm's length price?

[9] For that purpose, SARS first relied on the expertise of a Mr David. His report led to an additional assessment being levied by SARS that ABD considered excessive and has formed the basis of this appeal. However, during the course of these appeal proceedings, in October 2020, SARS retained the services of a new expert, an economist, Dr Slate. Based on his recommendation SARS seeks to adjust the royalty rate further to conform with what he calculates should have been the arms-length royalty rates payable in the tax years from 2009 to 2012.

[10] The difference between the David and Slate calculations is over how they calculated the size and division of the pie. Mr David relied on ABD's consultant's figures for the size of the pie as 3% of turnover, but then made his own determination on its division. He said that ABD was liable for the full 3%. ABD whilst agreeing with his determination of the size of the pie disagrees with his determination of its division. (He considered that ABD should be considered to have 100% of the pie. ABD disputes this.) By contrast Dr Slate recalculated the size of the pie (leading to a much larger pie; on average 47% as opposed to Slate's 3%); but divided the pie between ABD

and the OPCO's, thus reducing ABD's share of the pie to 6% from David's 100%.[1] ABD disagrees with Slate's calculation of the size of the pie but agrees with his division of the pie.

[11] Since in this appeal SARS relies on Dr Slate's approach and no longer that of Mr David, it is to his conclusions about the size of the pie I concern myself.

[12] In contrast to ABD's flat royalty rate of 1% for all the Opcos over the entire four-year period, SARS, advised by Dr Slate, now contends ABD should have charged a variable royalty rate depending on the country and the year it was earned. The fluctuations created by adopting his approach are considerable. Thus, in one instance the royalty rate he considers to be appropriate has been below 1% (Sudan in 2011) while in another he contends it should have been charged at 9,2% (Syria in 2010).

[13] I set out below the table of the royalties that Dr Slate, and now SARS acting on his advice, contends should have been charged by ABD to these fourteen Opcos during the period 2009 to 2012. This royalty rate is not yet the subject of a further increased assessment, but SARS seeks an order from the court in terms of section 129(2)(*b*) of the Tax Administration Act (TAA) that this additional assessment be adjusted to reflect these rates as set out in the table.

Table of Royalty rates now contended for by SARS based on Dr Slate

Opco	**2009**	**2010**	**2011**	**2012**
Afghanistan	1.7%	3.2%	1.9%	1.7%
Benin	3.5%	4.9%	2.0%	2.3%
Cameroon	2.7%	3.6%	1.5%	1.7%
Congo	2.2%	4.0%	1.8%	1.7%
Cyprus	1.9%	4.1%	1.5%	1.5%
Ghana	2.2%	4.2%	1.5%	1.4%
Guinea-Bissau	4.6%	4.3%	2.3%	1.5%
Ivory Coast	1.7%	2.6%	1.4%	0.9%
Rwanda	9.2%	6.5%	1.8%	5.3%

[1] Despite this reduction in the division of the pie, ABD's tax liability remains far higher on the Slate approach than on the David approach.

Opco	2009	2010	2011	2012
Sudan	1.3%	1.8%	0.8%	0.9%
Syria	4.9%	9.2%	6.7%	5.8%
Uganda	1.9%	2.7%	1.3%	1.2%
Yemen	1.9%	3.6%	4.5%	1.5%
Zambia	1.3%	1.8%	0.7%	1.0%

Relief sought

[14] ABD's principal relief is for the court to uphold its appeal and for the court to set aside the additional assessments for the 2009-2012 tax years. SARS relief is for the court to alter the additional assessments in terms of section 129(2)(*b*) of the Tax Administration Act, 28 of 2011, to reflect the quantifications done by Dr Slate set out in the table above.

Transfer pricing

[15] The Corporate Finance Institute (CFI) gives a useful definition of transfer pricing:

> "Transfer pricing refers to the prices of goods and services that are exchanged between companies under common control. For example, if a subsidiary company sells goods or renders services to its holding company or a sister company, the price charged is referred to as the transfer price."[2] Entities under common control refer to those that are ultimately controlled by a single parent corporation."

[16] The CFI goes on to explain why companies may use transfer pricing:

> "Multinational corporations use transfer pricing as a method of allocating profits (earnings before interest and taxes) among their various subsidiaries within the organization. Transfer pricing strategies offer many advantages for a company from a taxation perspective, although regulatory authorities often frown upon the manipulation of transfer prices to avoid taxes. Effective but legal transfer pricing takes advantage of different tax regimes in different countries by raising transfer prices for goods and services produced in countries with lower tax rates. <u>In some cases, companies even lower their expenditure on interrelated transactions by avoiding tariffs on goods and services exchanged internationally</u>."

(My emphasis)

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[2] Corporate Finance Institute – accessed on 3 October 2023.

[17] This last observation has salience for the present case. ABD makes the point that ABD has no incentive to charge its Opcos a lower royalty to avoid paying higher taxes in South Africa. A table in the record sets out the marginal tax rates in both South Africa and the jurisdictions. This shows that for most of them the tax rates in the jurisdictions where the Opcos were located, were equal to or higher than the South African tax rate. But it was argued that there was a further disincentive to under charge on the royalty. ABD has minority shareholders in most of the Opcos. If it were to undercharge the Opcos through the royalty this would mean it inflated its profits in the Opcos. The result of this is that the minority shareholders would be rewarded with profits that exceeded their shareholdings.

[18] SARS did not place these facts in dispute. Rather it said this consideration was irrelevant to the assessment of the current matter. That may be so. But it is relevant to the genesis of the rate that ABD has adopted. It starts, as I noted earlier, with ABD commissioning Company A, a consultancy, to advise it on the value of its intellectual property.

[19] Company A compared royalty rates in 18 territories where ABD Opcos were located and came to the following conclusion:

> "The ABD Group Royalty Rates were found to be in a range from 0.7% to 1.3%, depending on the financial performance, market share and brand health of the ABD brand in each territory. The average ABD Group Royalty Rate was found to be 1%, which would be a suitable rate if ABD preferred to have a uniform approach across all licensees. This approach also acknowledges the 'halo' effect of the ABD brand across the various territories."[3]

[20] ABD followed the advice Company A gave it. It had two aspects to it; that ABD should apply a rate that was an average of the rates of the territories considered. This led to an adoption of a rate of 1% (The range of the rates was between 0.7% and 1.3% thus much flatter than the rate range calculated by Slate); and second that applying a uniform rate had practical implications for both ABD and the Opcos. Company A explained why:

> "An average rate will mean that both ABD Group and the licensees will have some confidence about the likely levels of payment and so can plan accordingly. By averaging the rate across a number of years, both ABD Group and the licensees benefit from smoothing the effect of fluctuations in performance."[4]

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[3] Company A Sampson's ABD Royalty Analysis March 2011., Caselines 02-10.

[4] Ibid, Caselines 02-6.

SARS additional assessments

[21] The dispute between ABD and SARS had its origins with ABD's 2009 assessment. SARS initially accepted ABD's royalty calculations in 2009. But in 2014, SARS undertook a transfer pricing audit. The outcome was that in March 2014 SARS issued an additional assessment for ABD's 2009 tax year. Several more adjustments followed.

[22] According to ABD's rule 32 statement for the 2009 year, the chronology of SARS's changes was:

> "SARS based its determination of arm's length royalties, initially on a 2009 expert report of Brand Finance on ABD Brand Strength Analysis but later in part on a 2011 report of Company A Sampson on ABD Royalty Rate Analysis; and on 2015 and 2016 reports of Mr David".[5]

[23] But now, as noted, SARS seeks to rely on the work of Dr Slate in 2020 for the additional assessments which lead to a much greater liability for ABD than would have been the case under the earlier David based assessments. This has led to ABD to accuse SARS of a 'flip flop', a charge SARS vehemently denies. But ABD argues, as one of its grounds of appeal, that SARS could only issue an additional assessment in terms of section 92 of the Tax Administration Act 28 of 2011 (TAA), if it is satisfied that "….an assessment does not reflect the correct application of a tax Act to the prejudice of SARS or the fiscus". SARS, it argues, could not rationally have been satisfied that the original assessment did not reflect the correct application of the Act. What ABD is arguing here is that even if the Commissioner has the power to act in terms of section 31(2) of the Income Tax Act to adjust a price to reflect an arm's length price, this does not give SARS the power to act in terms of section 92 of the TAA, to make an additional assessment, because even if the price was not an arm's length price that is not a correct application of the TAA, because there is no obligation for a taxpayer to charge an arm's length price. Subtle as this argument is, its determination can wait for another day. I will proceed on the premise that SARS has such a power to act in terms of section 92 of the Tax Administration Act read with section 31(2) of the Income Tax Act.

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[5] CaseLines 003-243 paragraph 34.

Overview

[24] The case is unusual in that neither side, despite lengthy heads of argument has produced a single case on the central topic of the case – the approach a court should adopt to the subject of transfer pricing. Instead, both sides have relied on a document produced by the Organisation for Economic Cooperation and Development (OECD) titled "OECD Transfer Pricing Guidelines for Multinational Enterprises and Tax Administrations" (Guidelines). During the course of this litigation reliance was placed on two version of the Guidelines; one dated 2017 and the other 2022. While there are differences between the two, insofar as the relevant paragraphs in the Guidelines concern the present case, these are not material, and I will reference the 2022 Guidelines. It is a detailed document extending to more than 600 pages if one includes the annexures. The natural question to be asked is why if there is such detail in the Guidelines would disputes over its application still arise? The answer is that in many pertinent areas the Guidelines are expressed either in equivocal terms or create exceptions to more general suggested principles. It is in these interstices that the roots of the present dispute emerge.

Terminology

[25] The Guidelines contain useful definitions of the key terms used in the case. We start with the concept of an arm's length transaction which is defined as one where:

> "conditions are made or imposed between the two enterprises in their commercial or financial relations which differ from those which would be made between independent enterprises, then any profits which would, but for those conditions, have accrued to one of the enterprises, but, by reason of those conditions, have not so accrued, may be included in the profits of that enterprise and taxed accordingly".[6]

[26] But it is important not to pay mere lip service to the concept of the arm's length principle. Its rationale for trade consequences and for fairness must be appreciated. The Guidelines in the foreword explain:

> "A major reason is that the arm's length principle provides broad parity of tax treatment for members of MNE groups and independent enterprises. Because the arm's length principle puts associated and independent enterprises on a more equal footing for tax purposes, it avoids the creation of tax advantages or disadvantages that would otherwise distort the relative competitive positions of either type of entity. In so removing these tax considerations from economic decisions, the arm's length principle promotes the growth of international trade and investment.[7]

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[6] See Guidelines, definition section.

[7] Guidelines paragraph 1.8.

[27] First, we begin with the relationship between ABD and its Opcos. This relationship is described as one between 'associated enterprises'. They are considered 'associated' because ABD exercises control over the Opcos. As the Guidelines note, when independent enterprises transact with one another, market forces will govern their relationship. Thus, if ABD were to licence an independent entity and not one it controlled, and they agreed on a royalty, the assumption is that the amount of the royalty was a product of market forces. Where the enterprises are not independent viz. ABD and the Opcos, the lingering question is whether ABD's ability to control the Opco or market forces determined the royalty. But as the Guidelines caution:

> "Tax administrations should not automatically assume that associated enterprises have sought to manipulate their profits." [8]

[28] Nevertheless, in the even-handed manner the Guidelines are drafted, they go on to state:

> "When transfer pricing does not reflect market forces and the arm' length principle, the tax liabilities of the associated enterprises and the tax revenues of the host jurisdictions could be distorted." [9]

[29] This then leads on to the central problem faced in this case. How does one assess whether a transaction between associated enterprises, referred to in the language as a "controlled transaction", is one at arm's length and hence from a tax perspective of the jurisdiction in question, benign? The solution in the guidelines is to adopt one of the various methodologies it recommends be followed. They serve as the litmus test to a transaction – is it or is it not the equivalent of an arm's length transaction - one between independent enterprises shaped by the operation of market forces.

[30] Four experts testified about what the appropriate methodology to be used was, and conversely, what was not. Testifying for ABD were three experts but they relied on different methodologies. Two of them Mr Brine and Ms Sana testified that the royalty represented that of an arm's length transaction using a method known as the Transactional Profit Split Method or TPSM. I explain later what this method means. However, a third expert for ABD, Dr John, employed what is known as the Comparable Uncontrolled Price Method, or CUP. Ms Sana gave supporting evidence for Dr John on the CUP application as well.

[31] Thus, what ABD sought to do is to justify its royalty as one that is arm's length based on two distinct methodologies. SARS relied in the hearing on a single expert, Dr Slate who also used the TPSM method but relied on a different data set to that used by Mr Brine and Ms Sana.

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[8] Guidelines paragraph 1.2.
[9] Guidelines paragraph 1.3.

What are the methods

[32] The two methods of relevance in this case are the TPSM and the CUP

(i) Transactional Profit Split Method (TPSM)

[33] In the Guidelines the definition is broken up into two. First it defines a transactional profit method as:

> "A transfer pricing method that examines the profits that arise from particular controlled transactions of one or more of the associated enterprises participating in those transactions."

[34] In a further definition TPSM is then defined as:

> "A transactional profit split method that identifies the relevant profits to be split for the associated enterprises from a controlled transaction …and then splits those profits between the associated enterprises on an economically valid basis that approximates the division of profits that would have been agreed at arm's length."

(Emphasis provided)

(ii) Comparable uncontrolled price method (CUP)

[35] In the Guidelines a CUP is defined as:

> "A transfer pricing method that compares the price for property or services transferred in a controlled transaction to the price charged for property or services transferred in a comparable uncontrolled transaction in comparable circumstances."

(Emphasis provided)

[36] As is evident from the underlined portions of these definitions there is a wide margin for interpretation on their application. For this reason, the Guidelines attempt to put some more flesh on these definitions in sections that discuss them in further detail.

[37] Before I do so there is another definition that is relevant to the issues. Given that the asset in this case is a set of IP rights it is an intangible. The Guidelines define intangibles as:

> "…something which is not a physical asset or a financial asset, which is capable of being owned or controlled for use in commercial activities, and whose use or transfer would be compensated had it occurred in a transaction between independent parties in comparable circumstances. Rather than focusing on accounting or legal definitions, the thrust of a transfer pricing analysis in a case

> involving intangibles should be the determination of the conditions that would be agreed upon between independent parties for a comparable transaction."[10]

[38] As part of its treatment of what an intangible is the Guidelines go on to discuss what a brand means for the purpose of a transfer pricing analysis.

> "The term 'brand' is sometimes used interchangeably with the term 'trademark' and 'trade name'. In other contexts, a brand is thought of as a trademark or trade name imbued with social and commercial significance. A brand may, in fact, represent a combination of intangibles and/or other items, including among others, trademarks, trade names, customer relationships, reputational characteristics, and goodwill. It may sometimes be difficult or impossible to segregate or separately transfer the various items contributing to brand value. A brand may consist of a single intangible, or a collection of intangibles,…."

[39] One of the central issues of criticism that ABD have with Dr Slate is the notion that he has valued the wrong brand. Use of the term "wrong" brand is a misnomer. What the criticism of Dr Slate is, is that he has valued the ABD brand based on an extended notion of what has been transferred to the Opcos. As I go into in more detail later ABD contends that the licences to the Opcos are limited to the use of tradenames and trademarks not goodwill. Dr Slate has assumed it includes all rights to a brand, including goodwill, thus making these intangibles appear more valuable than they in fact are. Thus, if they are more valuable a higher royalty than the 1% would appear justified. ABD disputes this premise.

ABD's case

[40] As I mentioned earlier ABD's case rested on the testimony of three experts. Two experts (Mr Brine and Ms Sana) relied on TPSM method, and one, Dr John, relied on a CUP, although supported by Sana on some aspects of this.

ABD on TPSM

[41] Mr Brine is a London based professional employed by Company A. He leads Company A' s brand valuation practice and has eighteen years' experience in this area. He has a background as a chartered accountant as well as in marketing. He relied for his expert report on an earlier Company A report prepared by colleagues and this in turn was based on survey evidence conducted by a company called Company B. Brine conceded he was not involved in the preparation of either. Key to the Company A analysis is a technique used to value a brand known

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[10] Ibid 6.6.

as the Role of Brand Index or ROBI. This technique seeks to measure the degree to which a brand plays a role in driving customer choice and then expressing that as a percentage.

[42] SARS challenged the fundamental legal basis for Brine's testimony on the basis that it constituted inadmissible hearsay. ABD argued that survey evidence has been held admissible as an exception to the hearsay rule in certain circumstances. I provisionally admitted this testimony and deferred argument on this issue until the end of the case.

[43] In the interim, prior to my making a ruling on this issue, ABD sought to deal with the hearsay criticism by leading a witness, a Mr Coat, whose firm was involved in some of the data calculations that formed the data used in the Company A report. But at the end of the case, SARS argued that Mr Coat could not close the gap that remained in the chain of this evidence, to rescue it from a hearsay objection as it was Mr Coat' partner, not him, who had performed the data analysis. SARS conceded that survey evidence can be admitted as an exception to the hearsay rule in terms of Hearsay Act,[11] and that in the leading case on the point, *McDonalds,* the court had stated that a properly conducted survey could be admitted in evidence without requiring affidavits from the respondents. But SARS went on to argue that the court in *McDonalds* has also held that this was subject to the proviso that the opposing party (in this case SARS) is given an opportunity to check the results of the survey. SARS contended that it had not been given access to such results. [12]

[44] ABD argued at the end of the case that Mr Brine's testimony was not hearsay as SARS had earlier admitted the Company A report and hence ABD could rely on this admission. It also sought to argue that if it was hearsay the evidence for the same reason ought to be admitted. As I have not ended up relying on ABD's TPSM evidence I do not need to decide this point.

[45] Separately from this hearsay legal challenge, Dr Slate addressed what he said were eight main flaws with the Company A's methodology. I do not need to consider if any of these criticisms, legal or economic are valid. What it does illustrate is the vulnerability of the TPSM technique in disputes about intangibles when based on evidence from surveys. Nevertheless, ABD does not need to succeed on both methodologies it seeks to rely on. It only needs to succeed on one. I for this reason go on to discuss the case ABD made on the application of the CUP method.

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[11] Section 3 of the Law of Evidence Amendment Act, 45 of 1988.

[12] *McDonalds Corporation v Joburgers Drive-In-Restaurant* 1997(1) SA 1 (A) at pages 26-27.

ABD on the CUP method

[46] This aspect of the case was a departure from what ABD had relied on previously in the Company A reports, where the TPSM was applied. The case largely relied on the testimony of Dr John although his testimony was bolstered in certain aspects by Ms Sana.

[47] The Guidelines make it clear that where a CUP is applicable it is the preferred method to be used.

> "Where it is possible to locate the comparable cup, it is the preferred method for the determination of arm's length price."

[48] The reasons for this go back to the original analysis of the transfer pricing problem. It is the one method that seeks to replicate how market forces would work for a transaction between independent entities. However, the criteria for selecting an appropriate CUP are strict. Put differently, whilst a CUP, if it works, is considered the best method to apply, it also has the most hoops for the party relying on it to pass through.

[49] What Dr John did was to go through the history of the Opcos and in doing so he identified a transaction that he considered met the requirement for a CUP and more specifically an 'internal CUP'.(I explain what this term means later) The transaction is known as the Cyprus transaction as it involved ABD's sale of a subsidiary based in Cyprus to a third party, Company C Telecoms International (Company C). The sale took place on 15 July 2018. However, it did not at the time include a brand licence agreement. But on 3 September 2018 the parties concluded a brand licence agreement. What is significant is that this licence agreement took place at a time when the Cyprus entity was now independently owned. Thus, argues ABD, the parties were at arm's length at the time the agreement to licence the brand was concluded. The material terms of the licence were that the brand was licenced for a period of three years to Company C, but the latter was given the right to terminate the brand agreement at any time with immediate effect.

[50] Dr John makes the point that not only is the Cyprus agreement a suitable candidate for a CUP, but it is also what the Guidelines term an 'internal CUP'. An internal CUP is described as a transaction between one party to the controlled agreement (in this case ABD) and an independent party (Company C). Dr John's evidence is that not only is a CUP superior to other methods, but also that an internal CUP, if available, is superior to an external CUP (one where neither party is party to the controlled transaction).

[51] Dr John here is not relying on his own opinion but the OECD Guidelines as this extract from his report explains:

> "To corroborate using an internal CUP as the most reliable information available, OECD TPG 3.27 states that '[i]nternal comparables may have a more direct and closer relationship to the transaction under review than external comparables.' OECD TPG 3.29 follows that 'whenever reliable internal comparables exist, it may not be necessary to search for external ones.' "[13]

[52] The Guidelines go on to explain the advantage of an internal CUP:

> "The financial analysis may be easier and more reliable as it will presumably rely on identical accounting standards and practices for the internal comparable and the controlled transaction. In addition, access to information on internal comparables may be both more complete and less costly."

[53] When the original David report was done Dr John looked at an external CUP as a basis for comparison. This proved unsuitable as it was not possible to conclude without further facts that it was reliable. But in contrast when the Cyprus transaction became known its utility as an internal CUP became clear to him.

Criticism of Dr John

[54] SARS did not contest the idea that if a suitable internal CUP was available, it was the most reliable method to use. It could hardly do so given that SARS accepts the authority of the Guidelines. Rather, SARS questioned whether the Cyprus transaction was a reliable comparable based again on what it said the Guidelines required. The Guidelines lay out certain requirements which are common to all methodologies. These requirements as summarised are:

> "§1.36 The economically relevant characteristics or comparability factors that need to be identified in the commercial or financial relations between the associated enterprises in order to accurately delineate the actual transaction can be broadly categorised as follows:
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> - The contractual terms of the transaction (D.1.1).
> - The functions performed by each of the parties to the transaction, taking into account assets used and risks assumed, including how those functions relate to the wider generation of value by the MNE group to which the parties belong, the circumstances surrounding the transaction, and industry practices (D.1.2).
> - The characteristics of property transferred or services provided (D.1.3).

[13] John expert report paragraph 51. ¶

- The economic circumstances of the parties and of the market in which the parties operate (D.1.4).
- The business strategies pursued by the parties (D.1.5)."

[55] What the Guidelines state in relation to the CUP method is where there are differences in comparables the CUP method is still recommended, provided that these differences can be measured and hence accounted for.

[56] The line of cross examination was to ask Dr John if he had considered certain factors that the Guidelines indicate are relevant to all methodologies i.e. would apply both to the CUP and the TPSM methods. Whilst acknowledging that they did, Dr John conceded he had not, but said not all these factors were relevant in all situations. He eschewed he said a mechanistic approach to their application.

[57] He was also pressed on whether there were differences. He acknowledged that there were. The Guidelines also state that in using the CUP method if there are differences these should be measured and taken into account if the method is to be used. Dr John was asked if he had measured the differences in his analysis. He said he was unable to measure them and hence had not. It was put to him that on this basis the CUP method which he had espoused was not a useful comparable in these circumstances. There were differences which he had conceded existed, but he had not measured.

[58] Dr John insisted however that notwithstanding this criticism the Cyprus agreement was still an appropriate candidate as an internal CUP. Most of the differences were not relevant on his assessment whilst others which might be were not material. To the obvious criticism that if he could not measure them how could he be so sure that they were not material he had two responses. First, he stressed the distinction between the asset value of an intangible asset and the royalty rate as this passage in his cross-examination illustrates:

> "[COUNSEL FOR SARS]: The question was whether economic circumstances and we referred specifically the size of market, the extent of competition, the availability of substitute goods and services, the nature and extent of government regulation of the market is a relevant comparability factor to the CUP Method."

[59] "MR JOHN: Well, here there are several factors and I have conveyed that these factors are not relevant for the determination of royalty rates. They may be relevant for the determination of the asset value of the property but not the rate of the income."

[60] In relation to the measurability challenge Dr John relied on his own resource that he keeps of royalty values for his company known as Royalty Stat. He describes Royalty Stat as a company that inter alia provides:

> "Comparable royalty rates (in the form of a commercial online database) drawn from proprietary compilations of publicly available license or similar. (such as asset purchase) agreements within the meaning of the OECD Transfer Pricing Guidelines…"

[61] Based on his experience of this database, first set up in 1999, he said that the differences were never material in royalty agreements. Thus, what Dr John does is to give both a theoretical and an empirical (based on his own research) response to the criticism that the Cyprus CUP was not a true comparable.

[62] Ms Sana dealt with two of the issues about comparability – exclusivity and duration. The Cyprus agreement unlike some of the other Opco agreements gave Company C exclusivity. The Cyprus agreement was for 3 years but other Opco agreements varied in duration – some for 10 years some indefinite.

[63] She testified that normally exclusivity would command a higher price since it allows a greater degree of market power and influence. But like Dr John her view was that in practical terms exclusivity does not have a material impact on price. She also testified that duration does not have a material influence on the value of the brand and hence the royalty. This she based on her many years of encountering such agreements. But she also offered a rationale. She said a longer agreement meant less risk for the licensor and hence it might agree to a lower royalty i.e. even less than 1%. She supported Dr John's view that the Cyrus CUP as an internal CUP, provided an appropriate benchmark for an arm's length royalty.

[64] In addition to being used to put forward his own transfer pricing analysis Dr Slate was also used by SARS to offer a critique of the ABD experts. The broad thrust of this criticism was to suggest that relying on the Cyprus transaction as a proxy for a CUP was misplaced because the agreement did not meet the requirement of comparability. But a number of these criticisms were based on a legal rather than an economic analysis and as ABD has persuasively argued were based on error.

[65] Dr Slate argued that the rights granted in the Cyprus CUP were not the same as those granted to the Opcos. But under cross examination this turned out to be a legal error because he assumed that the rights given by ABD to ABD Dubai which included goodwill had been given to the Opcos – as it happened these rights were more limited and did not include goodwill.

[66] Then he argued that the agreement with Cyprus could not be regarded as one with an independent entity because ABD Cyprus had historically been an ABD Opco. In terms of the Guidelines an entity is not independent of another if it is an associate. An associate is an enterprise that is controlled by the other entity. But when the IP agreement was reached with Company C ABD, the Cyprus Opco was under the latter's control, and no longer ABD's. The IP agreement was, it must be recalled, reached some months after ABD Cyprus had been sold to Company C and the latter had assumed control over the former. The test for when the enterprise is considered independent must be at the time that the IP agreement is concluded because at that time the negotiations take place between independent parties thus replicating a situation where market forces operate to determine the royalty rate.

[67] The next issue was over what the Guidelines term 'unique and valuable' contributions. If both parties in a controlled transaction make unique and valuable contributions to the IP that is being licenced, then this may make comparing transactions more complex because this aspect cannot be measured. Dr Slate argued the Opcos make a unique and valuable contribution to the IP. ABD does not dispute this. The question rather is whether the unique and valuable contributions that the Opcos make in terms of their respective agreements are distinctive from one another. If not, the fact that each separately makes unique and valuable contributions is of no significance unless these contributions are distinct from one Opco to another. ABD argued that none of the agreements was exceptional in the sense they made contributions not made under any of the other Opco agreements. But this was not merely its contention.

[68] Even on SARS own case they are not. Dr Slate stated in one of his reports that "I analysed the OPCOS collectively rather than as separate entities due to their comparable functional profiles."

[69] If this is the case then the fact that the Opcos each make unique and valuable contributions, does not detract from the comparability of the Cyprus CUP, because these contributions were, taken as a whole, similar.

Dr Slate

[70] Dr Slate was the only expert called by SARS to testify. Dr Slate is an economist and a partner in an economic consultancy known as XXX Economics where he heads the Intellectual Property Valuation & Transfer Pricing service. He regularly advises private clients and authorities on transfer pricing issues including in the telecommunications industry.

[71] Dr Slate served two purposes for the SARS case. First, he served as rebuttal witness for the expert testimonies of John, Brine, and Sana respectively. Secondly, he advanced his own theory applying the TPSM to the royalty issue which led him to conclude that the previous assessment had significantly underestimated the size of the pie and using his application of the TPSM he came to size of the pie substantially larger than his predecessor Mr David –from 3% to 47 %. (Note the language size of the pie is that used by counsel in the hearing and is not that of Dr Slate.)

[72] I have dealt with Dr Slate's critique of the application of the CUP method. As I have not considered ABD's TPSM submissions I do not need to consider Dr Slate's critique of them, save to note that he did not accept their analysis as a correct application of the TPSM.

[73] Dr Slate filed two expert reports as well as a set of slides when he testified. But in brief what he set out to do was to make use of a methodology which attempted to calculate the incremental price consumers are willing to pay for a brand. The theoretical basis for this is as follows. Companies develop brands so that consumers will pay more for them than for a rival product. It is this brand, which is licenced, in this case to the Opcos, for which the royalty is then charged.

[74] In order to determine the brand value of the ABD brand and hence the arm's length royalty, he made use of a technique known as the willingness to pay or WTP. He sought to investigate how much more a buyer was willing to pay for a branded product versus an unbranded product. That way he concluded he could calculate the value of the brand. This is how he explains it in his report:

> "A brand relates to a "trademark or trade name imbued with social and commercial significance. ABD customers are willing to pay an incremental price due to the social and commercial significance that the relevant brand has in the market. Such social and commercial significance arises due to branding activities performed by ABD. I denote this incremental price the brand price premium. All else being equal, the OpCos benefit from the use of the relevant brand by earning higher revenues." [14]

[75] As he expressed it elsewhere:

> "A customer segment that prefers one seller's product over another, has a higher willingness to pay ('WTP') for the preferred product, all else being equal."

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[14] Slate report dated 2 October 2020, paragraph 140.

[76] What Dr Slate did to calculate the WTP was very ambitious. He developed a survey with a series of questions in which ABD customers in some of the fourteen jurisdictions under assessment, were asked about their preferences for the ABD brand versus a hypothetical company which was non-existent. Thus, its purpose was to survey ABD's customers' preference for paying a premium or incremental price for its mobile services versus that of a hypothetical company.

[77] As an organisational task and its attention to detail this was a most impressive effort. SARS also had to meet an early warning from ABD that it would challenge the admissibly of the surveys as hearsay. In response SARS procured confirmatory affidavits from a large number of its researchers who had conducted the interviews. It is not clear if it was able to do so for all. Nevertheless, the case started with what appeared to be ABD's acceptance that the hearsay issue had been satisfactorily addressed. It was only at the eleventh hour during final argument, and in response to a question from the court about the hearsay issue, that ABD indicated that it had never made such a concession. I considered that raising the issue at that late stage and then only in response to a question from the bench, was manifestly unfair to SARS. I will accept that even if the affidavits did not cover all the surveys that from a point of fairness, SARS should be allowed to have this evidence admitted. In any event the entire ABD case during the trial was conducted on the basis that it was admitted, thus distinguishing it from the approach of SARS which had challenged the admissibility of ABD's survey evidence from the outset.

[78] I now turn to how the survey was used. The WTP technique is not an invention of Dr Slate. He testified that it had been used previously by the United Kingdom's erstwhile Competition Commission.

[79] The primary enquiry of the WTP method is to ascertain the price premium the consumer is willing to pay. But as Dr Slate noted it is "difficult to observe price premiums directly in the market." His solution to this conundrum was to devise a survey whose purpose was to compare the ABD brand with the brand of another product which provided the identical products and services. To do this he developed a hypothetical new entrant to the respective markets which he called Tele Green. Since Tele Green would be unknown to the respondent (the person interviewed) it would serve to compare ABD with an unbranded product and hence test the customer's willingness to pay the premium for ABD.

[80] He designed the survey questions, trained the researchers on how to complete it and then when the results were completed and tabulated, he measured them quantitatively. In order to do a quantitative exercise, the respondent had to give a number in answer to the questions. Thus, one question was "What the price of Tele Green would have to be for you to choose it".

[81] Although fourteen markets are under assessment the WTP study was conducted in only six markets. Three of which he termed legacy markets. These are markets where the operating company had always been part of ABD. These were (Cameroon, Ivory Coast and Uganda). In three other markets the operating companies had been acquired by ABD from another firm, Company D, and were re-branded as ABD companies in 2006-2007 year. These are Benin, Ghana, and Sudan. D Slate used this survey data from the six markets to estimate a WTP for the remaining eight markets. The survey was based on the responses from 2,713 business to consumer and 1,245 business to business customers.

[82] The results of the surveys showed that price premiums customers were willing to pay for ABD branded products varied from 35% to 79% for the business to consumer market and 24% to 52% for the business-to-business market.

[83] What this exhaustive effort in the survey is meant to do, is to bring him to a figure that he can then plug into his further calculations. He goes on to use terminology which is confusing because he speaks of 'brand revenue' and also 'revenue attributed to the brand', which sound similar, but he uses as distinct concepts.

[84] His first step is to isolate brand revenue from non-branded revenue. This is an accounting exercise He says he took these figures from the financial statements and where he did not have them for each year, he used an average, based on the years he had. It was necessary for him to do this as Opcos earn some revenue from selling the ABD branded services and products, but also earn other revenue from selling phones and equipment. Since selling phones and equipment have nothing do with the operational business of the ABD brand, he excluded this revenue which he referred to as non-branded revenue, from the total revenue earned to get a total he refers to as the ABD branded revenue.

[85] At this stage his figure is a pure revenue figure for selling ABD branded products and services. But recall that his object is to reach a figure that reflects the value added by the brand. This figure is not apparent from the mere revenue figure for the sale of brand related products and services.

[86] This is where the WTP exercise comes in. His next step is to calculate the revenue attributable to the brand. What he means here is the price premium earned by selling the ABD brand. This is an economic concept as opposed to an accounting one. The price premium arrived at is the difference between what a consumer would pay for the same service unbranded as opposed the one that is ABD branded. Since unlike the branded revenue figure this cannot be derived from financial statements this is where the WTP figures fit in.

[87] He performs a set of further set of calculations to arrive, using the data obtained from the WTP survey, at a weighted price premium for all the Opcos for all the periods. This application of the method is not criticised, so I have not burdened the decision by going through the calculations. But his approach to considering costs which was his next step was disputed so I detail this.

[88] He sought to determine which costs were attributable to the brand. Dr Slate used this figure to determine the contribution made by each party to the revenue attributable to the brand. He then used this relative contribution to work out the split between the respective Opco and ABD. The final step was then to multiply the revenue attributable to the brand with split factor to arrive at royalty rates expressed as a percentage. He did this for all fourteen Opcos for all the years that were the subject of the assessment viz. 2009 to 2012. This led to a wide variance in rates with the lowest at 1.1% and the highest 6.7%

Criticism of Slate's approach

[89] The most significant critique of Dr Slate's valuation is a legal one, but it has profound implications for his survey on which it is contingent. ABD as noted earlier argue that Dr Slate has valued the wrong brand. As I stated earlier this is a misnomer. He has valued the correct brand which is the ABD brand. Rather the critique is that he has misconstrued the extent of the rights to the brand which the Opcos acquired. Dr Slate has assumed that ABD licensed the Opcos more extensive branding rights than it did. He assumed part of the rights licensed included goodwill. This error then had implications for the survey questions on which the WTP calculations were based. Questions in the survey were based on the goodwill of the ABD brand. This meant the survey was premised on the ABD transferring greater rights to the Opcos and hence a more valuable IP right than they in fact enjoyed.

[90] It is understandable how this error came about. In 2006 ABD acquired a company called Company D which was renamed ABD Dubai. ABD then entered into a Master Licence agreement with ABD Dubai. ABD Dubai was given the right to sublicense these rights. This Master licence gave extensive IP rights including goodwill to ABD Dubai. But the licence agreements with the

Opcos did not follow this wording. They had the right to use the ABD logo, trademarks etc., but this did not include goodwill.

[91] I quote here from the Cameroon agreement which is representative of the language of all the others.

> "The licensor grants to the licensee and the Licensee accepts, a non-assignable non-exclusive right to use and exploit the trademarks in relation to the licensed products in the territory …"

[92] This understanding of the limited rights that were transferred is replicated in the pleadings. Thus, in SARS's rule 31 statement the limited extent of this right is acknowledged.

> "<u>MATERIAL FACTS UPON WHICH SARS RELIES IN OPPOSING THE APPEAL</u>
>
> 15. ABD (Pty) Ltd ("ABD SA") and ABD Group Management Services Ltd are the legal owners of the:
>
> 15.1. ABD trademarks; and
>
> 15.2. Copyright subsisting in ABD logos prepared by ABD, excluding know- how, customer data and telecommunication licenses,
>
> (hereinafter individually or collectively referred to as the 'IP')."

[93] In the ABD's rule 32 statement this paragraph 15 is admitted. It is thus common cause on the pleadings what the extent of the rights being licensed to the Opcos was, and this is consistent with the terms of the Opco agreements.

[94] In the Company A report this limitation is recognised in the following paragraph:

> "In this report, the term brand refers to the ABD name, logo and other associated visual and intellectual property brand elements and systems. It focuses on the legally protectable, verbal and visual and IP elements."

[95] It is true that sometimes ABD's experts used the term 'brand' without qualification. But this cannot be regarded as a concession. It is accepted by both parties that the term brand can have both a limited and extended meaning. The guidelines recognise this as well.

> "The term brand is sometimes used interchangeably with the terms trademark and trade name. In other contexts, a brand is sort of as a trademark or trade name imbued with social and commercial significance."

[96] So too did Dr Slate in his report where he states this about brands:

> "As seen from the above, a brand can serve different roles as Maruya and Mishra outlined in their literature review."

[97] But what matters is what was licenced because that is the basis on which the royalty is established, and this, as I mentioned earlier, is the limited right to the use of the trademarks. It does not include goodwill or to phrase it differently, customer perceptions of the service. And there is a good reason that the Opco agreements didn't include goodwill. That is because the goodwill that would redound to their benefit is something that they would develop from their own efforts in their respective markets; it is not something they would need to licence from ABD.

[98] The error in respect of the brand then infected the approach to the survey that Dr Slate conducted. This is clear from several of the questions which clearly contemplate goodwill. For instance, respondents were asked about the reasons why they might use ABD as their mobile service provider. Amongst the pre-determined choices for answers are the following: *"Good customer service*"; and *"ABD has the most accessible refills"* and; *"ABD has the widest coverage"*. But all these answers reflect on the efficiency of the respective Opcos, not the rights that have been licensed. It is hard to see why these answers, whichever is chosen, form a reliable basis for an exercise in valuing an arm's length royalty rate for the right to use trademarks.

[99] But this was not the only criticism that ABD made of the survey. It was, ABD argued, biased from the manner in which the questions were framed. For instance, the survey asked respondents the reasons why they might prefer ABD. But this was not an open-ended question. Respondents were given five choices. The interviewer was prompted with following instruction. *"Please insist until an effective response is achieved. Must be marked as 'Agree' for at least one option to proceed".* Thus, anyone who might choose a reason other than the five designated was excluded from the survey.

[100] It was put to Dr Slate in cross examination that if the reason the respondent preferred ABD was because its prices were lower this was not an option. Thus, if this was the case the interview either ended (skewing the sample) or continued with the respondent giving a false reason thus biasing the sample.

[101] A further criticism of its reliability is that the survey was performed in 2020. Yet respondents had to indicate what they might have done in the period 2009 –2012. They were asked: "What the price for Tele Green would have had to be for you to choose it instead 2009-2012? Please indicate on a scale below."

[102] 40% of the respondents would have been teenagers a decade before. As counsel for ABD put it in cross examination to Dr Slate, some of them may not have been old enough to have a phone in this earlier period let alone pay for it. But even if they weren't teenagers, the reliability of this question asked in 2020 about a willingness to pay for a period that commenced ten years earlier is self-evidently unreliable. Dr Slate was forced to assess the willingness to pay in the years under assessment. But doing so, many years later, was never going to get answers to which one could attach any reliability. This makes the survey despite its exhaustiveness an exercise in futility, built on questions whose answers can make no claim to rigour or reliability. If the WTP is erected on such shaky foundations for its data, then it does not constitute a reliable metric to suppose what an arm's length royalty would have been for this period. But its most fundamental problem is that it tested a willingness to pay for rights that were broader than those the subject of the licence agreement. This false premise infects the entire value of the exercise.

[103] But the content of the survey is not the only question mark that hangs over Dr Slate's efforts. ABD also challenged the way he applied the TPSM. ABD argued that Dr Slate had used revenue, not profits, to calculate his royalty rate. His premise is based on the incremental revenue earned by the Opcos from using the ABD brand. ABD argues that he has not taken into account the increased costs that the Opcos incur to earn the price premium. Challenged on this Dr Slate said this was a distortion of his evidence as he does take costs into account when he does his revenue split, as he did so on the basis, pro rata, of what the respective marketing costs of the Opcos and ABD were. But that argues ABD is to use costs to perform a different exercise. It does not entail an enquiry into the costs the Opcos incur to earn the price premiums.

[104] Here again ABD relies as the source for its approach commentary in the Guidelines:

> "Most commonly, the relevant profits to be split under the transactional profit split method are operating profits. Applying the transactional profit split method in this manner ensures that both income and expenses of the MNE are attributed to the relevant associated enterprise on a consistent basis. However, depending on the accurate delineation of the transaction, it may be appropriate to split a different measure of profits such as gross profits, and then deduct the expenses incurred by or attributable to each relevant enterprise (excluding expenses already taken into account)."[15]

[105] There was a lengthy cross examination on this issue but Dr Slate continued to justify his approach, although when challenged, he could not locate it in the Guidelines, except in paragraphs which referred in the broadest terms to adopting a pragmatic approach. The debate

[15] Guidelines, op cit., paragraph 2.162.

ended inconclusively with Dr Slate reluctant to concede the point. But what it does illustrate is that Dr Slate relies on a methodology that is unorthodox and outside of the mainstream approaches.

[106] As the conclusion of his testimony the court asked him if the WTP methodology had been used previously in a transfer pricing case. Dr Slate said he was not aware if it had been used in any litigation although he said he had used the technique for many years in dealing with tax authorities. He also cited its usage by the United Kingdom's then regulator the Competition Commission.[16] But to be clear, the usage by a competition regulator is for market definition not to deal with a transfer pricing problem. Dr John remarked in his report that the Competition Commission has "…no authority in transfer pricing compliance".

[107] Dr Slate remarked that he had been using WTP for fifteen years in dealings with tax authorities who had accepted it. I accept that this may be so but given that the technique has not to our knowledge been used in litigation before, in a transfer pricing case, we must approach its usage with caution. The methodology employed as well as the survey questions have been justifiably criticised. In the well-known United States Supreme Court case of *Daubert,* where the court deals with the admissibility of expert testimony in a jury trial the following test was developed to consider whether an expert's methodology was valid:

a. Whether the technique or theory in question can be, and has been tested;

b. Whether it has been subjected to publication and peer review;

c. Its known or potential error rate;

d. The existence and maintenance of standards controlling its operation; and

e. Whether it has attracted widespread acceptance within a relevant scientific community.[17]

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[16] In a report emanating from consultants employed by the Competition Commission to review the Willingness to pay survey, dated April 2010, the following is stated:

> "The Competition Commission (CC) frequently uses surveys when conducting competition investigations and the evidence from these surveys are an important component of its findings. Survey evidence is also proving to be useful in remedies work. Such surveys are undertaken in a wide range of sectors which has included, for example, personal banking, gaming, betting, retail, travel, packaging, advertising and storecards. They are commissioned to fill in gaps in knowledge such as customer response to price changes, customer switching behaviour if there are changes in the market and the value that customers put on alternatives and their attributes. Such research can inform market definition and the analysis of competitive effects."

[17] *Daubert v. Merrell Dow Pharmaceuticals Inc.,* 509 U.S. 579 (1993). *Daubert* has often been referred to in judgments of South African courts. See for instance, *SMD Telecommunications CC v Mutual & Federal Insurance Company Ltd* [2009] JOL 24577 (WCC) at paragraph 57; *Bee v Road Accident Fund* [2018] JOL 40197 (SCA) at paragraph 25; and *Member of the Executive Council for Health, Limpopo Provincial Government v LWM obo DM (Member of the Executive Council for Health, Eastern Cape as Amicus Curiae)* [2022] JOL 56067 (SCA) at paragraph 51.

[108] While the *Daubert* test is used by US courts to decide whether expert evidence should be admitted in a jury trial, which is not what we are dealing with here, it is nevertheless a useful test to apply when considering the weight which should be given to the acceptance of a novel methodology over the acceptance of a more conventional one.

[109] On that test, the fact that the WTP methodology has been used by a competition regulator for one purpose does not signify widespread acceptance by the transfer pricing community for its purposes. Given that this community is an active one, regularly preparing and updating guidelines one might have expected this technique to gain some mention if it was accepted. It has not. The Competition Commission's report on this technique is dated 2010.Nor was there any evidence of its acceptance by courts or peer review by the academic community for its use as a technique in transfer pricing cases. Nor does it tick the boxes of the other factors set up in the *Daubert* test.

[110] Perhaps the WTP survey may prove useful as a benchmark when a taxpayer is negotiating with an authority. But in contested litigation the current survey and application of the WTP method has not yet been shown to be a reliable foundation for the application of the TPSM.

[111] By way of contrast the Cyprus CUP, has of all three models presented to us, proved the most persuasive. The Guidelines suggest that this is the preferred method when it can be used. The facts of this case bolster that proposition. Despite two applications of the TPSM method relying on different methodologies (ROBI by Brine for ABD) and WTP by Slate, each has been shown to have yielded widely different outcomes. The Cyprus CUP most closely resembles what would be achieved in a market-based arm's length negotiation. Whilst there are criticisms of its application, they are not conclusive. They amount to saying that certain factors such as exclusivity, duration and territory might have led to a different outcome. But these are speculative not conclusive criticisms. Speculation does not amount to refutation. By contrast the criticism of Dr Slate's approach has a solid factual basis. Its assumptions, legal, economic, and accounting have been dismantled. If this were not enough it is an untested methodology for use in litigation in transfer pricing cases.

[112] Both Dr John and Dr Slate were the subject of criticism that they were biased witnesses who refused to make concessions. Both of them were strong willed personalities who frequently embarked on a lecture when a short answer was all that was required. Despite this I see no reason to discredit either. As Zeffertt and Paizes remark in their textbook, when dealing with the value of expert evidence on conflicting opinions: *"The resolution of the conflict between such rivals will*

generally not depend on credibility, but rather in the reasoning inherent in them."[18] In this case the choice of the Cyprus CUP advanced by Dr John, and supported by Ms Sana, as opposed to the TPSM, based on the WTP method, advanced by Dr Slate has been based on the reasoning advanced, not the credibility of either expert.

[113] I conclude that the Cyprus CUP serves as a comparable internal CUP. The royalty in that agreement was 1%. On that basis the royalty of 1% charged by ABD to the other Opcos constitutes a reasonable arm's length royalty. That being the case there was no factual justification for the Commissioner to have adjusted the royalty in terms of the then section 31 of the Income Tax Act. The appeal succeeds. It is not necessary for this reason to consider the several other administrative law grounds and accounting issues raised by ABD in its appeal.[19]

[114] I appreciate that the outcome of this case will be of great disappointment to SARS which put into it extensive resources to create a precedent in this seldom litigated field of tax law. But this not only meant it running contrary to the opinions and approach of its initial expert (which meant effectively dispensing with his views without explanation and engaging a new expert) but fighting a case where there appeared to be no rationale for the taxpayer to have any motive to shortchange the South African fiscus as I mentioned earlier in this decision.

Costs

[115] Ordinarily ABD as the successful party would be entitled to its costs. But as the issue of costs in tax appeals is dealt with in terms of the TAA, a different costs regime applies. Section 130(1)(*a*) provides that the Tax court on appeal may on application by the aggrieved party grant an order for costs in favour of that party if the SARS grounds of assessment or decision were unreasonable.

[116] SARS argues that ABD has not made this showing. It is correct that in seeking costs ABD has not addressed itself to the requirements of this section. But in its administrative law arguments about what they termed 'SARS flip flop', referring to its switch in its reliance on Mr David to its reliance on Dr Slate, ABD has made out a case that the decision to change its approach and new seek the new higher assessment, based on an analysis that has not met the test of rigour is

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[18] D.T. Zeffertt and A.P. Paizes. *"The South African Law of Evidence"* (Lexis Nexis) Third edition, pages 341-2.

[19] ABD raised quantum issues in respect of three of the Opcos (Zambia, Congo, and Rwanda) and a Mutual Agreement Procedure (MAP) issue in respect of Rwanda and Uganda. It also appealed against the imposition of interest in terms of section 31 of the Income Tax Act.

unreasonable. However, this should only influence a cost award from the time of the first Dr Slate report in 2020.

[117] ABD asks for costs of two counsel. Given the complexity and length of the case this is justified. SARS also made use of two counsel. As far as experts are concerned given that the case succeeds based on the costs of the Cyprus CUP, I will allow for the costs of the experts who supported this opinion again after the period of the Dr Slate report. This means I will allow the qualifying fee of Dr John as well as half the costs of Ms Sana, since some of her testimony related to the ROBI method used in Mr Brine's TPSM analysis, which has not determined the outcome of the case.

ORDER

It is ordered that:

a. ABD's appeal in relation to the years 2009 – 2012 is upheld.

b. The additional assessments for 2009-2012 are set aside.

c. SARS is to pay ABD's costs, from the date of receipt of the first report by Dr Slate in October 2020, including costs of two counsel, and the qualifying fees of the following experts; Dr John and half of those of Ms Sana.

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MANOIM, J
JUDGE OF THE HIGH COURT

CONCUR:

Prof. Zeyn Mia: Accounting member

Prof. Leo Luvuno: Commercial member

Dates of Hearing: 24 October to 11 November 2022 and 18 to 19 September 2023

Date of Judgment: 14 February 2024