SARS South African Revenue Service

INTERPRETATION NOTE: NO. 8 (Issue 3)

DATE: 28 August 2013

ACT : INCOME TAX ACT NO. 58 OF 1962 (the Act)
SECTION : SECTION 25C AND RELATED PROVISIONS
SUBJECT : INSOLVENT ESTATES OF NATURAL PERSONS

Preamble

In this Note unless the context indicates otherwise –

- **"date of sequestration"** means –
  - the date of voluntary surrender of an estate, if accepted by the Court; or
  - the date of provisional sequestration of an estate, if a final order of sequestration is granted by the Court;[1]
- **"Schedule"** means a Schedule to the Act;
- **"section"** means a section of the Act;
- **"TA Act"** means the Tax Administration Act No. 28 of 2011; and
- any word or expression bears the meaning ascribed to it in the Act.

1. Purpose

This Note provides guidance on the tax treatment of insolvent estates including the application of section 25C of the Act. Issue 2 of this Note, issued on 22 March 2006, is hereby replaced.

2. Background

A person is said to be insolvent when their liabilities exceed their assets. Depending on the circumstances, a debtor (that is, the insolvent) or a creditor may apply to the court for sequestration of the debtor's estate. The effect of sequestration is, amongst others, to "divest the insolvent of his estate and to vest it in the Master until a trustee has been appointed, and, upon the appointment of a trustee, to vest the estate in him."[2]

Before 4 July 1997 it was SARS's practice to regard insolvent estates as taxable entities and to treat the trustees of these estates as representative taxpayers.

However, in the case of *Thorne & Molenaar NNO v Receiver of Revenue Cape Town*[3] the Supreme Court held that this practice was incorrect. The court had to decide whether a trustee of an insolvent estate was liable to pay income tax on

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[1] Section 1(1) and section 1 of the TA Act.
[2] Section 20(1)(a) of the Insolvency Act No. 24 of 1936.
[3] 1976 (2) SA 50(C) (38 SATC 1).

income accruing to an insolvent estate in the capacity of a representative taxpayer or any other capacity.

The court found that –

- the income derived by the trustees could not be said to be income of a person under a legal disability;
- merely because a person fell under the definition of a "trustee" as defined in section 1[4] of the Act did not necessarily mean the person was a representative taxpayer;
- the defined term "trustee" could not be regarded as correlative to the term "trust" and, for a trustee to be a representative taxpayer, he had to be a trustee of the income that was the subject of a trust; and
- as a result, the trustee of the insolvent estate was not liable for tax on any income accruing to the insolvent estate in his personal capacity or in his capacity as a representative taxpayer.

A number of amendments were subsequently enacted to ensure that income received by or accrued to an insolvent estate on or after 4 July 1997 is subject to tax.

3. Income Tax

3.1 Three separate entities exist for income tax purposes

The assets of a taxpayer, whose estate has been sequestrated, vest in the trustee or administrator who is appointed to take control of the administration and sequestration of the estate for the benefit of the creditors.

The effect of insolvency, from an income tax point of view, is to terminate the tax status of the taxpayer and to substitute, in that taxpayer's place, a new entity from the date of sequestration, that is, the insolvent estate.[5] In addition, the natural person receives a new taxpayer identity from the date of sequestration.

Three separate taxpayers will, therefore, be liable for tax, namely:

- The insolvent person for the period before insolvency (that is, up to the date preceding the date of sequestration);
- The insolvent estate (a new entity for tax purposes from the date of sequestration); and
- The insolvent person for the period on and after the date of sequestration.[6]

The insolvent person will be assessed as a natural person for the period before insolvency, as well as for the period subsequent to insolvency, should any income accrue to that person in his or her personal capacity. Given that the two periods of assessment are each less than 12 months, the rebates permitted for each period will only be allowed on a proportional basis.[7]

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[4] As it was at that time.
[5] ITC 349 (1936) 9 SATC 66 at 69.
[6] Although the insolvent person before and after sequestration is referred to as separate taxpayers, the insolvent person is technically the same natural person.
[7] Section 6(4).

3.2 The insolvent estate is a "person" for income tax purposes

Section 5(1) requires every person to pay income tax on taxable income received or accrued during the year of assessment ending on, in the case of a person other than a company, the last day of February. A "person" specifically includes "an insolvent estate".[8]

The insolvent estate must register as a separate entity for income tax purposes. The requirements relating to the registration of taxpayers are regulated by Chapter 3 of the TA Act.

An "insolvent estate" is defined in section 1(1) as –

> "an insolvent estate as defined in section 2 of the Insolvency Act, 1936 (Act No. 24 of 1936)".

Section 2 of the Insolvency Act, 1936 defines an insolvent estate as –

> "an estate under sequestration".

An estate is only under sequestration if the court has issued an order accepting the surrender of or sequestration of the taxpayer's estate. The provisions relating to insolvency do not therefore apply to a taxpayer who merely assigns his or her assets for the benefit of his or her creditors in the absence of such a court order.

A partnership is not a separate entity for income tax purposes. However, from an insolvency law perspective, the estate of a partnership is separate to the estate of the individual partners. Section 13(1) of the Insolvency Act, 1936, provides that if the estate of a partnership is sequestrated, the estates of each partner, excluding a partner *en commandite* and certain special partners as defined, must generally be simultaneously sequestrated.[9]

The position is different if the personal estate of a partner is sequestrated as this does not necessarily result in the partnership or the estates of the other partners also being sequestrated.[10] The sequestration of a personal estate of a partner results in a dissolution of the partnership by virtue of the withdrawal of such partner's share in the partnership.[11] From the insolvent person's perspective there will be three entities to consider for income tax purposes (see **3.1**). From the other partners' perspective they will need to consider the impact of the dissolution of the partnership in their hands.

An insolvent estate is not a natural person. Accordingly, an insolvent estate does not, for example, qualify for the primary rebate as contemplated in section 6 or for the interest exemption in section 10(1)(*i*). These provisions are limited to natural persons.

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[8] Section 1(1), definition of a "person".

[9] Section 13(1) of the Insolvency Act, 1936; P M Meskin *et al Insolvency Law* [online] (LexisNexis: May 2012) in Chapter 3.1; JJ Henning and E Snyman-Van Deventer under 'Partnership / Dissolution of partnerships / Causes and formalities' 19 (Second Edition Volume) *LAWSA* [on-line] (*My LexisNexis*: 30 June 2006) in paragraph 310.

[10] JJ Henning and E Snyman-Van Deventer under 'Partnership / Liquidation and distribution of assets / General' 19 (Second Edition Volume) *LAWSA* [on-line] (*My LexisNexis*: 30 June 2006) in paragraph 316.

[11] JJ Henning and E Snyman-Van Deventer under 'Partnership / Dissolution of partnerships / Causes and formalities' 19 (Second Edition Volume) *LAWSA* [on-line] (*My LexisNexis*: 30 June 2006) in paragraph 310.

An insolvent estate is, however, taxed at the same rates of tax applicable to natural persons.[12]

3.3 The representative taxpayer of an insolvent estate

The definition of the term "representative taxpayer" in section 1(1) includes –

> "(*f*) in respect of the income received by or accrued to an insolvent estate, the trustee or administrator of such insolvent estate;".

Section 153(1) of the TA Act defines a "representative taxpayer" as –

> "a person who is responsible for paying the tax liability of another person as an agent, other than as a withholding agent, and includes a person who—
>
> (*a*) is a representative taxpayer in terms of the Income Tax Act;
>
> (*b*) is a representative employer in terms of the Fourth Schedule to the Income Tax Act; or
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> (*c*) is a representative vendor in terms of section 46 of the Value-Added Tax Act".

The representative taxpayer of an insolvent estate is accordingly the trustee or administrator of the insolvent estate. Section 154 of the TA Act provides as follows with regard to the liability of a representative taxpayer:

> "(1) A representative taxpayer is, as regards—
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> (*a*) the income to which the representative taxpayer is entitled;
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> (*b*) moneys to which the representative taxpayer is entitled or has the management or control;
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> (*c*) transactions concluded by the representative taxpayer; and
>
> (*d*) anything else done by the representative taxpayer,
>
> in such capacity—
>
> (i) subject to the duties, responsibilities and liabilities of the taxpayer represented;
>
> (ii) entitled to any abatement, deduction, exemption, right to set off a loss, and other items that could be claimed by the person represented; and
>
> (iii) liable for the amount of tax specified by a tax Act.
>
> (2) A representative taxpayer may be assessed in respect of any tax under subsection (1), but such assessment is regarded as made upon the representative taxpayer in such capacity only."

Section 155 of the TA Act, furthermore, provides that the trustee or administrator of an insolvent estate will be personally liable for any tax payable in the representative taxpayer's representative capacity, if, while it remains unpaid, he or she –

- alienates, charges or disposes of the amounts on which the tax is chargeable; or
- disposes of any funds or money from which the tax could legally have been paid.

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[12] The relevant tax table is applicable to natural persons, deceased estates, insolvent estates and special trusts.

3.4 Person before sequestration and insolvent estate – the "one and the same person" rule

For the purposes of the Act (which includes the Eighth Schedule), and subject to any adjustments as may be necessary, section 25C deems the estate of the person before sequestration and that person's insolvent estate to be one and the same person for purposes of –

- the amount of any allowance, deduction or set-off to which the insolvent estate may be entitled;
- any amount which is recovered or recouped by or otherwise required to be included in the income of the insolvent estate; and
- any taxable capital gain or assessed capital loss of the insolvent estate.

This, amongst other things, means that:

- An assessed loss incurred by the insolvent person can be set off against the insolvent estate's income.
- Expenditure and allowances claimed by the insolvent person before the date of sequestration can be recouped in the insolvent estate, for example, depreciation allowances and bad debts previously written off as bad.
- Debts included in the income of the insolvent person before the date of sequestration can be claimed as bad debts by the insolvent estate.
- The write-off of assets and allowances can continue to be claimed in the insolvent estate.
- Closing stock taken into account in the insolvent person's last taxable income calculation may be taken into account as opening stock in the insolvent estate's first taxable income calculation.
- Any amount that would otherwise be required to be included in the income of the insolvent person may be included in the income of the insolvent estate, for example, the amount allowed as an allowance for doubtful debts or the allowance for future expenditure under section 24C.

  The reduction or cancellation of debt provisions in section 19 must be kept in mind if the insolvent estate reduces a debt by more than the amount of consideration given for that reduction, for example, in terms of a compromise with a creditor.

- A disposal does not take place when the insolvent person's assets pass from the insolvent person to the insolvent estate on sequestration.
- Capital gains and capital losses arising because of disposals by the insolvent estate to third parties will be included in the hands of the insolvent estate but will take into account events that occurred in the insolvent's hands, for example, previous depreciation allowances.
- An assessed capital loss incurred by the insolvent person before the date of sequestration may be set-off against capital gains arising in the insolvent estate.

3.5 Submission of returns

Section 25 of the TA Act, read together with section 66(13)(*a*)(*b*), prescribes that where the estate of a person is sequestrated, separate returns must be submitted for the periods commencing –

- on the first day of that year of assessment and ending on the date preceding the date of sequestration; and
- on the date of sequestration and ending on the last day of that year of assessment.

An insolvent estate's first period of assessment will commence on the date of sequestration and end on the last day of February. The second and subsequent years of assessment commence on 1 March and end on the last day of February, or on the date on which the estate is finally wound up. The individual whose estate is sequestrated must submit returns for the periods before sequestration and after the date of sequestration (see **3.1**).

3.6 Setting aside of the sequestration order

The effect of the setting aside of an order of sequestration[13] is to terminate the existence of the insolvent estate *ab initio*. Any transaction that took place in the insolvent estate while it was in existence must, therefore, be accounted for in the hands of the individual who has been released from sequestration.

Practically this means that SARS must withdraw any assessment issued to the insolvent estate and must also withdraw the assessment which was issued to the insolvent person in the year the sequestration order was granted by the court (that is, from the beginning of that year to the date preceding the date of sequestration). This is done under section 98(1) of the TA Act which provides that SARS may withdraw an assessment if it was issued to the incorrect taxpayer or was issued for the incorrect tax period.

SARS must simultaneously issue assessments to the person who has been released from sequestration as if the sequestration never took place. Under section 98(2) of the TA Act a withdrawn assessment is regarded as not having been issued and accordingly SARS can issue assessments for the respective periods under Chapter 8 of the TA Act.

3.7 Paragraph 19(5)(*b*) of the First Schedule

Under paragraph 19(5) of the First Schedule any natural person who derives income from farming operations may elect that the normal tax chargeable on the taxable income from farming be determined in accordance with the rating formula as provided in section 5(10).

[13] This differs to the situation where a person has become rehabilitated through an application for rehabilitation (section 124 of the Insolvency Act 24 of 1936) or through the effluxion of time (section 127A of that Act). Although in the latter cases the sequestration comes to an end under section 129 of that Act, the original order remains a *fait accompli* and is not set aside.

The trustee of the insolvent estate of a natural person may also elect that the normal tax chargeable on the taxable income from farming be determined in accordance with the rating formula if –

- the farming operations commenced by the insolvent person were carried on by the insolvent estate in the period of assessment commencing immediately after insolvency (that is, commencing on the date of sequestration); and
- the election is made within three months after the end of such period of assessment or within such further period as the Commissioner may approve. In practice extensions will be granted up to a date before the raising of the assessment.

Once the election has been made it is binding on the insolvent estate for that period of assessment and all future periods of assessment and the insolvent estate will be taxed in accordance with the rating formula.

The average taxable income from farming will be calculated having regard to the figures determined for the insolvent person before the date of sequestration.

The insolvent estate should document the election in writing in the format specified in the ITR12 comprehensive guide (available on the SARS eFiling website **www.sarsefiling.co.za)**. The document must not be submitted with the annual tax return but must be retained as part of the taxpayer's records. Section 29 of the TA Act requires records to be kept for five years from the date of the submission of the return. In context, this means the document will have to be retained for five years from the date the last return was submitted in which the insolvent estate declared farming income.

3.8 Capital gains tax

On sequestration a person's assets pass to that person's insolvent estate. This change of ownership would normally trigger a disposal under paragraph 11 of the Eighth Schedule. However, the 'one and the same person' principle (see **3.4**) brings the two entities together and since a person cannot dispose of something to himself, there is no disposal of the individual's assets on the date of sequestration. Capital gains and losses are therefore determined in the hands of the insolvent estate when the assets are disposed of to third parties.

Under paragraph 83(1) of the Eighth Schedule the disposal of an asset by an insolvent estate is treated in the same manner as if the natural person whose estate has been sequestrated had disposed of that asset. This means that the insolvent estate is treated as a natural person and will be entitled to the same exemptions and exclusions the insolvent person would have been entitled to, had the person disposed of the assets. The purpose of this provision is to ensure that the insolvent estate will not be taxed on the disposal of the personal assets of the insolvent person such as that person's primary residence (to the maximum amount of the primary residence exclusion), furniture or private motor vehicles. It also confers the same 33,3% inclusion rate[14] and annual exclusion[15] on the insolvent estate.

[14] 33,3% (previously 25%) deemed to come into operation for disposals made on or after 1 March 2012 in accordance with the Taxation Laws Amendment Act No. 22 of 2012.

[15] Paragraph 5 of the Eighth Schedule.

The insolvent person before sequestration, the insolvent estate and the insolvent person on and after sequestration share the annual exclusion, in that order, in the year of sequestration. Therefore, to the extent that the insolvent person before sequestration has not used the annual exclusion during the applicable period of assessment (commencing on 1 March and ending on the date preceding the date of sequestration), the excess will be available for set-off against capital gains and capital losses arising firstly in the insolvent estate and secondly, if any excess remains, in the insolvent person on and after sequestration. In subsequent years, the insolvent estate and the insolvent person on or after sequestration will each be entitled to a full annual exclusion.

Paragraph 83(2) of the Eighth Schedule provides that no person whose estate has been voluntarily or compulsorily sequestrated may carry forward any assessed capital loss incurred before the date of sequestration. In other words it may not be carried forward by the insolvent after the date of sequestration.

However, under section 25C's "one and the same person" rule in relation to determining any taxable capital gain or assessed capital loss of the insolvent estate, an assessed capital loss in the hands of the insolvent person before sequestration may be carried forward to the insolvent estate. Any assessed capital loss remaining in the insolvent estate at the time it is finally terminated will be forfeited.

The assessments raised on the insolvent person and the insolvent estate must be withdrawn and a new assessment issued as if the sequestration never took place (see **3.6**), when an order of sequestration is set aside. In that case any assessed capital loss must be determined *de novo.*

3.9 Taxes constitute costs of insolvency

Taxes and levies imposed on income accrued or business conducted from the date of sequestration qualify as a cost of administration under section 97(2)(*c*) of the Insolvency Act No. 24 of 1936.[16] There is no procedure for proving such claims,[17] which enjoy a higher degree of preference than claims for income tax in respect of the pre-liquidation period under section 101 of that Act. The representative taxpayer must simply lodge the relevant returns of income and settle the taxes owing before distributing any surplus to the preferent and concurrent creditors.

4. Value-added tax

Section 53 of the Value-Added Tax Act No. 89 of 1991 (the VAT Act) provides that after the sequestration of a vendor's estate, any enterprise previously carried on by the vendor –

- continues to be carried on by or on behalf of the trustee or administrator of the estate; or
- anything is done in connection with the termination of the enterprise,[18]

the insolvent estate, as represented by the trustee of the insolvent estate, will for the purposes of the VAT Act be deemed to be the vendor of the enterprise.

[16] *Van Zyl NO v CIR* 1997 (1) SA 883 (C), 59 SATC 105 at 113/114.

[17] E de la Rey *Mars: The Law of Insolvency in South Africa* 8 ed (1988) Juta & Co Ltd, Wetton in § 21.5 at 400.

[18] See section 8(2) of the VAT Act for further detail.

The vendor whose estate is sequestrated and the insolvent estate will, for purposes of the VAT Act, be deemed to be one and the same person. This means the insolvent estate does not have to be registered as a vendor under a new registration number. The representative vendor being the trustee or administrator of the insolvent estate will be liable to perform the duties as imposed by the VAT Act.

5. Employees' tax, skills development levies and unemployment insurance fund contributions

An insolvent estate that continues to carry on an enterprise previously carried on by the insolvent person and in so doing continues to employ people, will meet the definition of an employer for purposes of employees' tax,[19] skills development levies[20] and unemployment fund contributions[21] and will be subject to the duties, responsibilities and liabilities under those respective Acts.

Practically the insolvent estate does not have to register as a new employer and will continue to use the insolvent person's registration number.

The trustee or administrator of the insolvent estate will be required to withhold employees' tax and unemployment insurance fund contributions where the detailed requirements of those Acts are met and as such will be a withholding agent under section 156 of the TA Act. Under section 157 of the TA Act the trustee or administrator is personally liable for the tax withheld and not paid to SARS or the tax which should have been but was not withheld.

6. Illustrative example

Facts:

X's creditors applied for the sequestration of his estate on 15 September 2012. The court granted a provisional order of sequestration on 15 October 2012 and this was made final on 13 December 2012. X was the owner of a sports bar. The trustee of X's insolvent estate continued with the operation of the sports bar on behalf of the insolvent estate (and ultimately the benefit of the creditors) until 7 February 2013 when the estate was finally wound up.

During the period 1 March 2012 to 14 October 2012

- An assessed loss of R50 000 was brought forward from the 2012 year of assessment.
- Sports bar income of R301 998 was generated and allowable expenditure (before any allowances have been taken into account) amounted to R310 776.
- Interest income of R12 000 was received.
- A capital gain of R50 000 was made on the sale of listed shares on 31 July 2012.
- X purchased new furniture on 1 March 2012 for R180 000. The furniture is written off on the straight line method over 6 years.

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[19] Section 1 of the Fourth Schedule – definition of the term "employer".
[20] Section 1 of the Skills Development Levies Act No. 9 of 1999 – definition of the term "employer".
[21] Section 1 of the Unemployment Insurance Contributions Act No. 4 of 2002 – definition of the term "employer".

During the period 15 October 2012 to 7 February 2013

- Sports bar income of R100 081 was generated and allowable expenditure (before any allowances have been taken into account) amounted to R98 660.
- Interest income of R1 500 was received.
- The sports bar was sold at an auction on 31 January 2013 for R400 000, of which R300 000 was paid for the business premises, R80 000 for the furniture and R20 000 for the kitchen equipment. The business premises of the sports bar were bought for R120 000 on 15 November 2011 (no allowances had been claimed for tax purposes). The kitchen equipment was bought on 1 March 2004 for R100 000 and was written off over a period of 6 years.
- X's primary residence which was bought on 2 November 2011 for R600 000 was also sold at the auction for R1 700 000.
- The trustee will elect the section 11(*o*) allowance wherever applicable.

Result:

	R	R
Tax impact of the disposal of furniture		
Section 8(4)(a) recoupment or section 11(o) allowance		
Purchase price of furniture		180 000
Less: Depreciation allowed 2013 – before insolvency R180 000 / 6 years x 228 / 365 days	(18 740)	
Depreciation allowed 2013 – insolvent estate R180 000 / 6 years x 116/365 days	(9 534)	(28 274)
Tax value on date of sale		151 726
Less: Proceeds		(80 000)
Section 11(*o*) allowance		71 726
Capital gain or (loss)		
Proceeds		80 000
Less: Base cost (R180 000 – R28 274 – R71 726)		(80 000)
Capital gain or (loss)		NIL
Tax impact of the disposal of kitchen equipment		
Section 8(4)(a) recoupment or section 11(o) allowance		
Proceeds		20 000
Tax value of kitchen equipment on 31/01/2013 (purchased in 2004 and written off over 6 years)		NIL
Section 8(4)(*a*) recoupment		20 000
Capital gain or (loss)		
Proceeds (sales price – recoupment)		NIL
Less: Base cost [purchase price – amounts claimed under section 11(e)]		NIL
Capital gain or (loss)		NIL

Tax impact of the disposal of business premises

Capital gain or (loss)

Proceeds	300 000
Less: Base cost	(120 000)
Capital gain or (loss)	180 000

Tax impact of the disposal of residence

Capital gain or (loss)

Proceeds	1 700 000
Less: Base cost	(600 000)
	1 100 000
Less: Primary residence exclusion	(2 000 000)
Capital gain or (loss)	NIL

Taxable income: insolvent person for the period before insolvency (1 March 2012 – 14 October 2012)

Income from sports bar	301 998
Less: Allowable expenditure	(310 776)
	(8 778)
Less: Depreciation – furniture	(18 740)
	(27 518)
Less: Assessed loss brought forward on 01/03/2012	(50 000)
Capital gain on sale of listed shares (R50 000 – R30 000 annual exclusion) x 33,3%	6 600
Assessed loss (to be carried forward to insolvent estate)	(70 918)

Note:

(1) The R12 000 interest received by the insolvent person (a natural person) before insolvency qualifies for the interest exemption under section 10(1)(*i*).

Taxable income: insolvent estate (15 October 2012 to 7 February 2013)

	R
Income from sports bar	100 081
Less: Allowable expenditure	(98 660)
	1 421
Less: Depreciation: furniture	(9 534)
	(8 113)
Section 8(4)(*a*) recoupment: kitchen equipment	20 000
Section 11(*o*) allowance: furniture	(71 726)
	(59 839)
Investment income	1 500
	(58 339)
Net capital gain = furniture + kitchen equipment + business premises + residence = (Nil +Nil + R180 000 + Nil) x 33,3%	59 940
	1 601
Less: Assessed loss for the period before insolvency brought forward	(70 918)
Assessed loss	(69 317)

Note:

(1) The insolvent person before sequestration and the person's insolvent estate *are regarded* to be one and the same person for purposes of the determination of *deductions or allowances*. The deduction for the depreciation of assets, therefore, continues in the insolvent estate.

(2) The insolvent person before sequestration and the person's insolvent estate are *not regarded* to be one and the same person for purposes of determining any *exemption*. The insolvent estate is not a natural person and does not qualify for the interest exemption in section 10(1)(i). Accordingly, the interest of R1 500 received by the insolvent estate is fully taxable in the insolvent estate's hands.

(3) The estate of the person before sequestration and the person's insolvent estate *are regarded* to be one and the same person for purposes of the determination of *a capital gain or loss*. Paragraph 83(1) provides that the disposal of an asset by an insolvent estate shall be treated in the same manner as if disposed of by the insolvent person. The insolvent estate, therefore, enjoys the same exemptions and exclusions applicable to natural persons. Thus the insolvent estate qualifies for the primary residence exclusion of R2 million and an inclusion rate of 33,3%. The insolvent estate does not qualify for an annual exclusion in 2013 because the annual exclusion was fully used by the insolvent person.

(4) The balance of the assessed loss of R70 918 is forfeited and may not be used by the insolvent person for purposes of determining the person's tax liability for the period after sequestration. The balance of the assessed loss is, therefore, forfeited.

7. Conclusion

For income tax purposes, a new taxable entity comes into existence when a person's estate is sequestrated. In addition, the natural person receives a new taxpayer identity from the date of sequestration. Three separate taxpayers will, therefore, be liable for tax, namely –

- the insolvent person for the period before insolvency (that is, up to the date preceding the date of sequestration);
- the insolvent estate (a new entity from the date of sequestration); and
- the insolvent person for the period on and after the date of sequestration.

A separate tax return must be submitted for each of the periods identified above.

The estate of the person before sequestration and the person's insolvent estate are, however, deemed to be one and the same person for certain purposes, for example, the determination of the deductions and allowances the insolvent estate may be entitled to and the determination of a taxable capital gain or assessed capital loss in the insolvent estate. It also means there is no disposal for capital gains tax purposes when the assets pass from the insolvent to the insolvent estate.

Paragraph 83(1) and 83(2) of the Eighth Schedule provide that –

- the disposal of an asset by an insolvent estate is treated in the same manner as if the natural person whose estate has been sequestrated had disposed of that asset, and
- no person whose estate has been voluntarily or compulsorily sequestrated may carry forward any assessed capital loss incurred before the date of sequestration. In other words it may not be carried forward by the insolvent after the date of sequestration but it may be carried forward to the insolvent estate.

Similarly, an assessed loss prior to the date of insolvency may be carried forward to the insolvent estate.

The trustee or administrator of the insolvent estate is the representative taxpayer of an insolvent estate and, in that capacity, is subject to the duties, responsibilities and liabilities of the insolvent estate. In this capacity the trustee or administrator may, depending on the specific facts, elect that the normal tax chargeable on the taxable income from farming of the estate be determined in accordance with the rating formula specified in section 5(10).

The trustee or administrator may be held personally liable for the underlying taxes.

In circumstances where an order of sequestration is set aside SARS must withdraw any assessment issued to the insolvent estate and must also withdraw the assessment which was issued to the insolvent person in the year the sequestration order was granted by the court (that is, from the beginning of that year to the date preceding the date of sequestration). SARS must simultaneously issue assessments to the person who has been released from sequestration as if the sequestration never took place.

Taxes and levies imposed on income accrued or business conducted from the date of sequestration qualify as a cost of administration under section 97(2)(*c*) of the Insolvency Act No. 24 of 1936.

For purposes of value-added tax, employees' tax, skills development levies and unemployment insurance fund contributions, the insolvent estate and the person whose estate is sequestrated are regarded to be one and the same person. The trustee or administrator of the insolvent estate takes over the duties and responsibilities regarding these taxes, levies or contributions.

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