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Enquiries
K Engel /
F Tomasek

Telephone
012 315 5508 /
012 422 5146

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**THE CHAIRPERSON OF THE
PORTFOLIO COMMITTEE ON FINANCE
(PCOF)**

RESPONSES TO WRITTEN REPRESENTATIONS BY ORGANISATIONS TO THE PORTFOLIO COMMITTEE ON FINANCE ON THE DRAFT REVENUE LAWS AMENDMENT BILL, 2006 (the Bill)

1 Introduction

As indicated to you during the hearings on the above-mentioned Bill on 18 and 20 October 2006, National Treasury and SARS wish to respond as follows to the various points raised by commentators in their submissions on the Bill.

Abbreviations used in this document:

BASA	Banking Association South Africa
BUSA	Business Unity South Africa
CMASA	Club Management Association of Southern Africa
LOA	Life Offices' Association of South Africa
NPC	Non-Profit Consortium
PWC	PricewaterhouseCoopers
SACBC	Southern African Catholic Bishops' Conference
SACC	South African Council of Churches
SAICA	South African Institute of Chartered Accountants

2 Consultation

The National Treasury and SARS placed the draft Revenue Laws Amendment Bill as well as a draft Explanatory Memorandum on the Bill on their websites on 29 September 2006. This was followed by a supplementary batch of legislation on 13 October 2006. The draft legislation and explanatory memoranda were submitted to your committee on 29 September and 12 October 2006. The Bill was, therefore, submitted more than 10 working days before the informal briefing on the Bill on 17 October 2006.

3 Responses to specific issues raised in representations by commentators to the PCOF

The responses will be dealt with under the following headings:

GENERAL ANTI-AVOIDANCE RULE

3.1 *General*

Before dealing with the specific comments made it is useful to review the process which has given rise to the GAAR proposal. The review of section 103, the GAAR in the Income Tax Act, was announced in the Budget Review 2005. A Discussion Paper in this regard was launched on 3 November 2005, setting out the scope of the problem, the mechanisms used by and common characteristics of impermissible tax avoidance, the international experience, a review of the existing provisions of section 103 and proposed changes. Commentators were given until 31 January 2006, later extended to 28 February 2006, to provide comments on the Discussion Paper. The intention of finalising legislative proposals in the latter half of 2006 was announced in the Budget Review 2006.

An Interim Response to the comments that had been received by 28 February 2006 was issued on 16 March 2006, when SARS and National Treasury briefed the Portfolio Committee on Finance on the Discussion Paper. The Interim Response summarised the comments that had been received, set out SARS' initial response, and requested further proposals with respect to certain issues that had been raised. While commentators did not agree with certain of the proposals, sometimes for diametrically opposed reasons, some of the comments recorded in the Interim Response bear repeating. These include the comments that section 103 had been "essentially emasculated" and "ceased to be the deterrent it once was" and that "SARS has done its homework, as the list [of factors] is a comprehensive description of the kind of stratagems that characterize many avoidance schemes." Three days of hearings followed on 22, 24 and 31 March 2006, with SARS providing a response on 31 March 2006 to the submissions that had been made.

SARS returned to the Portfolio Committee on 12 September 2006 to provide a report on the Revised Proposals that would be released later that week. The Revised Proposals were released on 15 September 2006. The revised proposals were then incorporated in the draft Revenue Laws Amendment Bill released on 29 September 2006, with further amendments that had been proposed during the ongoing consultative process.

In the light of the above it is clear that the GAAR proposal was not arrived at lightly, but was the product of extensive research and consultation.

The legislation is not required in the light of the substantial increases in revenue collections achieved by SARS.
(BUSA)

This comment is not accepted. Improvements in revenue collections are driven by economic factors, an enhanced compliance culture and SARS enforcement action. There is a fundamental responsibility to the taxpayers and practitioners that made this possible to provide a level playing field where everyone is paying their fair share. The proposed GAAR is intended to underpin the progress that has been made and ensure that it is not undermined by a new generation of schemes employed by aggressive taxpayers and practitioners. The estimates revenue loss of R10.7 billion over five years from known transactions in respect of just six types of tax avoidance arrangement, presented to the Portfolio Committee on Finance on 16 March 2006, serves a warning of magnitude of the problem confronting us.

3.2 *Impermissible tax avoidance arrangements – section 80A*

The legislation is too wide reaching. It is submitted that it

cannot be the intention of Parliament to tax a transaction in a manner other than as specifically provided for in terms of the Act merely because the alternative transaction chosen by the taxpayer has the result of yielding less tax to the fiscus. The proposed anti-avoidance legislation will result in too many legitimate business transactions being unjustly subject to an attack by SARS unless extreme caution is exercised in the course of carrying out such measures to avoid the effect that such legislation may have on legitimate business transactions.
(SAICA)

The proposed new GAAR assigns an 'avoidance badge' to transactions that are normal, but nevertheless have an avoidance outcome. It could be argued that the required objective could be attained by way of interpretation notes that deal with problem issues rather than changing section 103. The fact is that the efficacy of the current section 103 remains to be tested.
(BUSA)

These comments are not accepted. The proposed GAAR follows a tiered approach to determine whether or not a transaction constitutes impermissible tax avoidance, and may therefore be countered.

	Arrangement
+	Tax Benefit Effect
	Avoidance Arrangement
+	Main Purpose Tax Avoidance
+	Tainted Element
	Impermissible Tax Avoidance

Contrast this approach to, for example, that of the New Zealand GAAR, as set out in Annexure D to the Discussion Paper. Here the Commissioner may counter an arrangement if it has tax avoidance as its purpose *or* effect, *or* if it has tax avoidance as one of its purposes *or* effects, if that purpose or effect is not merely incidental. In effect, it is sufficient to only reach the first sub-total above to trigger the New Zealand GAAR.

Furthermore, it should be borne in mind that Interpretation Notes, while useful to communicate SARS' views on the interpretation of law are not binding on SARS, unless issued as binding general rulings, and are never binding on taxpayers.

Finally, as comments recorded in the Interim Response noted and SARS experience has confirmed, section 103 is not a consistent and effective deterrent against impermissible tax avoidance.

There is an overwhelming sense of concern over the move towards a novel yet untested concept that assigns autocratic powers to the tax administration and the associated uncertainty

that it imposes upon taxpayers. There can be no doubt that the tax system is working efficiently and there appears no justification for assigning autocratic powers to the tax authority under ill-defined descriptive phrases such as 'commercial substance' and 'frustrate the purpose of'. BUSA would argue in favour of maintaining the as yet insufficiently tested existing Section 103 provisions.
(BUSA)

It of great concern that the proposed measures:

- **characterise a vast number of everyday transactions as impermissible tax avoidance, and**
- **have the effect of transferring a significant amount of power governing tax law from the Legislature and Judiciary to the Executive.**

(BASA)

These comments are not accepted. As noted above the proposed GAAR follows a tiered approach to determine whether or not impermissible tax avoidance has occurred. The concern that the proposed GAAR would circumscribe the judiciary was raised in the March hearings and now by BASA. In the March hearings this concern was raised with respect to the proposal that tax avoidance intention with respect to a transaction be objectively determined. While this approach is common internationally, the concern was expressed that it would reduce the Courts' role in determining such intention by excluding a taxpayer's *ipse dixit* or own testimony. This concern was addressed in the Revised Proposals in section 80G(1). BASA's current concern appears to relate to the provisions of section 80C(1). In this regard see 3.4. below.

The presumption exists that the onus rests on the Commissioner to prove that the abnormal manner, the commercial substance, the abnormal rights and obligations and the "frustrate" tests apply. This should be expressly stated in the proposed legislation, to ensure that this is clearly understood.

(BASA)

This comment is not accepted. This is the effect of existing case law.

Many of the proposed changes have addressed the concerns raised in BUSA's original submission in January. Yet the revision introduces a fundamental, if novel, concept which surely increases rather than reduces uncertainty.
(BUSA)

The test "frustrate the purpose of any provision of [the Income Tax] Act" is too wide.
(BUSA, PWC)

The "frustrate" test is considered to be illogical and problematic. For the "frustrate" provision to apply it requires that an arrangement simultaneously wholly complies and frustrates the provisions of the Act. The suggested solution is that the "frustrate test be removed from the draft.
(BASA)

These comments are partially accepted. The test of "would frustrate the purpose of any provision of this Act" has been replaced with "would result directly or indirectly in the misuse or abuse of the provisions of this Act". This alternative formulation has precedent in other jurisdictions and was suggested by several commentators.

3.3 *Tax consequences of impermissible tax avoidance - section 80B*

The Commissioner will be empowered able to recharacterise an arrangement as he sees fit even though this may not be in accordance with the taxpayer's or a court's view.
(SAICA)

It is unsatisfactory to give the Commissioner the power to override the independent legal status of independent statutory entities. The powers granted to the Commissioner under this section should be limited to transactions between connected persons.
(SAICA)

These comments are not accepted. The powers granted the Commissioner are a codification of the Commissioner's existing powers to "determine the liability for any tax, duty or levy imposed by this Act, *and* the amount thereof, as if the transaction, operation or scheme had not been entered into or carried out, *or* in such manner as in the circumstances of the case he deems appropriate for the prevention or diminution of such avoidance, postponement or reduction."

Should "impermissible avoidance" clearly be present (as held by the Courts) the Commissioner's remedial action (including his actions taken in terms of discretionary powers) should be consistent and symmetrical. The application of the provisions should not allow the Commissioner to collect more taxation (from all parties to the arrangement) that would have been collected had the arrangement not been entered into.

(BASA)

Replace the words “may” with “must”.
(BUSA)

These comments are partially accepted. The proposed section 80B(2) has been amended to require that “the Commissioner must make compensating adjustments that he or she is satisfied are necessary and appropriate to ensure the consistent treatment of all parties to the impermissible avoidance arrangement.”

Specific provision should be made for corresponding adjustments where the counter party has already been assessed and the assessment has prescribed.
(PWC)

This comment is not accepted. Corresponding adjustments may require both additional and reduced assessments for other parties to the impermissible avoidance arrangement. Disturbing prescription under these circumstances is not a step to be taken lightly.

3.4 *Lack of commercial substance - section 80C*

The concepts “substantial effect”, “beneficial ownership” and “significant effect” should be defined.
(SAICA)

This comment is partially accepted. The concept “substantial effect” appeared in the Revised Proposals but was replaced by “significant effect” in the draft Revenue Laws Amendment Bill, as consultations had indicated that the second term was better supported in South African case law. As the question of what is significant with respect to a particular transaction and taxpayer is a question of facts and circumstances, no definition of the term is proposed. The concept of “beneficial ownership” has been deleted.

The provisions seem to be attempting to influence or limit a Court considering alleged tax avoidance, instead of allowing the court to consider the circumstances totally objectively. This is particularly problematic in numerous and obvious occasions. To automatically characterize the lower-risk transactions as lacking commercial substance is patently absurd. Secondly, a great number of everyday transactions involve minimal effect on net cash flows. Thirdly, the test of a significant effect on beneficial ownership of an asset is similarly flawed and ignores the obvious fact that transactions involving services do not involve the ownership of assets. This section should be deleted.

(BASA)

These comments are partially accepted. The proposed section 80C(1) has been amended to clarify the provision by testing for a significant tax benefit without a significant effect upon either the business risks or net cash flows of the taxpayer. The reference to beneficial ownership was restricted to assets involved in an avoidance arrangement but has been deleted for other reasons.

The factors indicative of a lack of commercial substance are by no means exhaustive. The factors may taint perfectly legitimate transactions as impermissible avoidance arrangements.
(SAICA)

The concept of "lack of commercial substance" is ill defined in the context of business operations. Oppose the codification of "commercial substance".
(BUSA)

This is a presumptive provision that must allow for a rebuttal opportunity.
(BUSA)

These comments are noted. It is true that the factors are not exhaustive. They cannot be exhaustive given the variety of business transactions in existence. To the extent that the factors may be present in legitimate transactions, they are not decisive but merely indicative and their presence may be defended by the taxpayer when SARS gives notice of its intention to apply the GAAR, as well as through objection and appeal should the GAAR be applied.

3.5 *Round trip financing - section 80D*

The definition of "avoidance arrangement" read together with this section is so broad that any loan and subsequent repayment thereof appear to fall within this section. This is exacerbated by the fact that the timing and sequence or manner in which round–tripping occurs is ignored.
(SAICA)

Many commercial transactions require what would now be deemed to be round tripping. Certain transactions within the group relief provisions actually necessitate this practice. Furthermore, the use of this sophisticated cash management system by many corporate taxpayers would probably be disallowed as it might be considered to fall within the ambit of this provision.
(BUSA)

These comments are not accepted. Legitimate loans and repayments, as well as cash management systems, would generally not result in a tax benefit *and* reduce risk. In as far as certain transactions with respect to the corporate rules are concerned, this factor may be present but this in of itself is not decisive in determining whether impermissible tax avoidance is present. The sole or main purpose of the transactions must also be to obtain a tax benefit.

3.6 *Accommodating or tax-indifferent parties – section 80E*

Reference is made to "the amount of tax imposed by another country". This implies that the amount in question must not only be subject to tax in another country at a rate of at least two-thirds the amount of normal tax which would have been payable had the amount been subject to tax under the Act, but it must actually have been *taxed*. This is contrary to our understanding of the normal application of international double tax treaties. The wording should refer to the amount of tax that "may" or "could" be imposed by the other country.
(SAICA)

This comment is not accepted. While the principle enunciated by SAICA has its place, it is not absolute even in the tax treaty context and is certainly not when dealing with anti-avoidance legislation. As an example, tax treaties do not provide for a credit for tax that was not imposed, unless an explicit tax sparing clause is present.

A number of commercial transactions require tax-indifferent parties for pure commercial reasons. Its adoption will undoubtedly create uncertainty which is unnecessarily counterproductive to the business environment.
(BUSA)

This comment is noted. If the tax indifferent party is present for purely commercial reasons the taxpayer will be able to make its case in this respect. Furthermore, the sole or main purpose of such a transaction will presumably not be tax avoidance, so the GAAR will not apply. Taxpayers will also be able to obtain greater certainty for legitimate transactions through the advance tax rulings system that was introduced on 2 October 2006.

In many financial trading transactions, margins of 0,5% or less are common. On the face of it expenditure of 99,5% or more of the related income would seem to be "substantial", but it is clearly absurd that routine financial transactions can result in a party to an arrangement being regarded as accommodating or tax-indifferent. It is suggested that the "substantial offset" test be qualified along the lines of the following: "substantially offset

to an extent unusual in the context of the transaction in question."
(BASA)

This comment is not accepted. As was noted in the Discussion Paper, the concept of abnormality is the Achilles heel of the existing section 103 and this proposal would re-introduce it in another form and place in the proposed GAAR. If the tax indifferent party is present for purely commercial reasons the taxpayer will be able to make its case in this regard.

3.7 *Treatment of connected persons and accommodating or tax indifferent parties – section 80F*

SARS has now been granted, in the relevant circumstances, the power to override the advantages to be gained by having separate taxpayers in a group, without giving away any of the disadvantages to the *fiscus* of group taxation. If the advantages of separate taxpayers in a group are, to this extent, being removed, then it behoves the *fiscus*, as a matter of some urgency, to introduce group taxation.
(SAICA)

The Commissioner can totally disregard arms'-length commercial transactions between connected persons in a group of companies. He is given the same powers in relation to so-called "accommodating or tax-indifferent parties". There is no requirement that there be anything unusual about the transactions in question.
(BASA)

The issue of group taxation is an area still to be developed and it would be inadvisable to introduce a concept that has a bearing on Group Taxation into the GAAR. It merely generates further uncertainty.
(BUSA)

These comments are not accepted. The combination of connected persons and accommodating or tax indifferent parties takes place in a limited context, namely the determination of whether there is a lack of commercial substance to a transaction or whether a tax benefit exists. It is necessary in this context to prevent the addition of such entities as a mechanism to circumvent the Income Tax Act's provisions or add so called "structural fog". The advantages of having separate taxpayers in a group remain outside this context, be they for tax purposes or commercial purposes.

3.8 *Presumption of purpose - section 80G*

The right of the taxpayer to structure his affairs in the most efficient manner should be recognised, provided that his overriding purpose is not a tax one. Businesses are in existence first and foremost to make profits.

The "presumption of purpose" provision allows the Commissioner to presume a purpose of obtaining a tax benefit in any arrangement, even where no tax liability is necessarily being avoided or postponed.
(SAICA)

This comment is not accepted. SAICA appears to have overlooked that the presumption in section 80G(1) only applies to an "avoidance arrangement". Thus an arrangement must give rise to a tax benefit before the presumption applies. (See the definition of "avoidance arrangement".)

3.9 *Application to steps or parts of an arrangement – section 80H*

Parliament intends taxpayers to be attracted to enacted measures that confer favourable tax circumstances. In many circumstances, an attempt to make legitimate use of these tax measures will fall foul of the new proposals. For example, the sole purpose of the step of selecting one building above another to be upgraded and expanded is to obtain a tax benefit. The transaction is deemed to lack commercial substance as it has no effect at all on the beneficial ownership of the asset. The arrangement is thus automatically an "impermissible avoidance arrangement". The above example is not a rare circumstance.
(BASA)

This comment is noted. However, with respect to the example cited, the concept of beneficial ownership has been deleted from the provisions dealing with commercial substance. Furthermore, the selection of a particular building to be upgraded is generally a factor to be considered when considering the main purpose of the upgrade, rather than a separate part of a transaction.

3.10 *Notice – section 80J*

The 30 day period to submit reasons for the non-application of GAAR should be extended to at least 90 days as, given the complexity of this legislation, the taxpayer would have to seek professional assistance in formulating its response to SARS. This request must also be considered in light of the fact that there is no corresponding time deadline for the Commissioner to respond to the submission made by the taxpayer and the

Commissioner may automatically issue an assessment if he is not satisfied with the reasons furnished by the taxpayer.
(SAICA)

It is suggested that some degree of reciprocity be introduced, with time limits also applicable to SARS in the same way as is applied for objection and appeal procedures.
(PWC)

A taxpayer must be afforded at least 180 days to revert to SARS as to why the section should not apply. A statutory obligation should revert upon SARS to progress matters within 180 days, failing which the challenge should lapse.
(BUSA)

These comments are partially accepted. The period for the taxpayer to reply has been extended to 60 days or such longer period as SARS may allow. SARS is required to respond to the taxpayer's reply within 180 days. When considering these timeframes it should be borne in mind that SARS intends issuing notices as early as is practical in its investigations to limit the commitment of resources on either side in cases where the GAAR is not applicable. As stated in the presentation to the Portfolio Committee on Finance on 16 March 2006, impermissible avoidance schemes may take years to unravel.

The Commissioner should be given the power to revoke a notice if, upon enquiry, he is satisfied that it is no longer appropriate.
(PWC)

This comment is accepted.

3.11 *Definitions – section 80L*

The question is raised how an understanding that is not enforceable could constitute an arrangement and whether this is an attempt to codify existing law on simulated transactions. It is submitted that the courts will not give effect to this and the Zandberg and Randles Brothers cases are cited.
(SAICA)

To a large extent the definition merely incorporates the practical approach that has been adopted by the Courts. The reference to "(whether enforceable or not) is intended to cater for "gentlemen's agreements", "letters of wishes", and the like.

An opinion has already been received by a practitioner that, in terms of the proposed provisions, delaying a decision to sell an asset till a future date gives rise to a tax benefit as it amounts to a postponement of a liability for tax. The definition of tax benefit

needs to be suitably limited.
(SAICA)

The term "avoidance arrangement" is defined as "any arrangement that results in a tax benefit". In turn, a "tax benefit" is defined there as including "any avoidance, postponement or reduction of tax". In order to clarify the term a comparator should be introduced. This might be achieved by comparing to the tax position that would have prevailed had the arrangement not have been entered into.
(BASA)

These comments are not accepted. The concept of a tax benefit as an avoidance, postponement or reduction of tax has existed in section 103 since its inception.

When BEE transactions are undertaken, some parties may indeed be "tax indifferent" and to some degree "circular" cash flows may be involved. There should be a qualification to the new proposals stating that arrangements that are specifically designed to implement the transactions envisaged in the "corporate rules" provisions should not inherently be regarded as conferring a "tax benefit".
(BASA)

This comment is not accepted. The corporate rules may be used as an integral part of an impermissible avoidance arrangement and should be subject to the same scrutiny that other transactions undergo.

3.12 *Effective date of new GAAR*

The commencement date for years ending on or after 1 January 2007 results in retroactive operation of the proposed provisions. It is suggested that the new provisions apply for arrangements concluded on or after a specified date. Signature date should not be determining as oral agreements must be respected.
(SAICA)

It should be made clear that the new provisions will only apply to affected arrangements entered into on or after the date of the commencement of the amending Act.
(BASA, BUSA, PWC)

These comments are accepted. The new GAAR will apply to transactions entered into on or after the effective date.

3.13 *Objection and appeal – section 3(4)*

The Commissioner also makes a decision under section 80F. This section should therefore also be inserted or, to simplify the wording, reference should simply be made to "Part IIA of Chapter III".
(SAICA)

This comment is not accepted. This decision may be challenged when the Commissioner invokes section 80B, which is subject to objection and appeal.

REPORTABLE ARRANGEMENTS

3.14 *General*

A number of commentators have suggested that the current provisions are overly broad, requiring large numbers of routine transactions to be reported. The concern that an excessive number of routine transactions would be caught up in the system was raised when the original reportable arrangements legislation was introduced. In the event only 55 transactions were reported. Nevertheless, the concern is recognised, so it is proposed that the effective date of the new legislation be postponed to a date to be determined by the President. This will allow industry to approach SARS with specific examples of routine transactions that may be affected and permit the Minister to extend the list of excluded transactions by regulation, as already provided for in the Bill.

3.15 *Reportable arrangements – section 80M*

The requirement that a tax benefit can be assumed to be delivered has absurd implications and even if no benefits are derived the transaction would still be a reportable arrangement.
(SAICA)

This comment is not accepted. As disclosure must take place early in the life of an arrangement, the tax benefits cannot await quantification at the end of that arrangement.

It is unreasonable to refer to the characteristics of an avoidance transaction that are indicative of a lack of commercial substance to determine whether an arrangement is reportable. The question whether the *indicia* are present is a matter of perception and interpretation and disregards the *bona fide* view taken on the legal and economic effects. A taxpayer is expected to be a witness against itself in applying the provisions correctly. The *indicia* in section 80C(2) is for the Commissioner to allege.
(SAICA)

Major concern is expressed about the proposals, the most important being that a substantial number of routine transactions will be caught. This, together with the magnitude of the penalty of non-reporting, is material.
(BASA)

The legislation provides for a set of disclosure requirements and does not as such attach any tax consequences to the transactions disclosed. Furthermore, specific provisions are included whereby identified routine transactions are excluded. Finally, provision is also made for the exclusion of further categories of routine transactions by way of regulation.

The question is whether accounting rules are to dictate taxation treatment? Many countries do in fact provide for exactly this in their tax laws, but South Africa does not. In the absence of such provisions, how can accounting treatment dictate tax disclosure, and create the potential for massive tax penalties?
(BASA)

Accounting rules do not dictate tax treatment, they merely provide a limited indicator of transactions that may be of interest to SARS. It is SARS' experience that a strong marketing point for an impermissible avoidance arrangement is that it will not impact significantly on profits reported for accounting purposes but will give rise to significant tax benefits.

It is SARS' experience that the accounting treatment is considered at the same time that the tax treatment is considered and in any event prior to inception of the transaction. Hence we do not expect this provision to be impractical in any manner.

The test relating to the specified indicative characteristics that are meant to denote lack of commercial substance is a flawed test because for tax avoidance transaction the factors are indicative but for RAs are prescriptive.
(BASA)

The characteristic that the legal or economic effect is inconsistent with the legal form of the individual steps is a vague test and can create significant problems with routine transactions. It is questioned why it is cause for suspicion that an individual step is inconsistent with the legal form of the individual steps.
(BASA)

"Round trip financing" is a new concept with an extremely complex definition that is difficult to interpret comprehensively,

in the short time that has been allowed. It would appear to cover a significant number of situations where borrowers or other counterparties lodge collateral security. Thus a conventional (and frequent) form of financial transaction has been "tainted" by these proposals, resulting in onerous reporting requirements.
(BASA)

These comments are not accepted. No substantive tax consequences flow from the fact that a transaction is reportable. This is a mere disclosure requirement and does not "taint" any transaction.

In many financial trading transactions, margins of 0,5% or less are common. On the face of it expenditure of 99,5% or more of the related income would seem to be "substantial", but it is clearly absurd that routine financial transactions can result in a party to an arrangement being regarded as accommodating or tax-indifferent.
(BASA)

The offsetting test will effectively condemn any arrangement that contains any element of security, no matter how trivial. Needless to say, this would involve a vast number of banking transactions.
(BASA)

It is not possible to comment on these assertions without detailed information with respect to these transactions. BASA is invited to provide SARS with this information by 31 January 2007.

It is unclear whether the "inconsistent" characterisation test is for accounting or tax purposes. In either case, this test is completely anomalous and totally unworkable. This follows because the characteristics of a transaction are frequently inherently inconsistent.
(BASA)

This comment is partially accepted. It is proposed that the test be withdrawn.

Transactions are reportable where there is no reasonable expectation of pre-tax profit. This measure turns on its head a substantial body of tax law, which holds that tax expenditures do not have to be laid out in the expectation of profit. Indeed, the number of transactions that have no such immediate intent is vast. This provision condemns all of these transactions with all of the onerous requirements that this entails.
(BASA)

The definitions of “participant” and “reportable arrangement” are circular.
(SAICA)

This comment is accepted and the circular reference is resolved by amending the definition of tax benefit to remove the reference to any participant.

3.16 *Excluded arrangements – section 80N*

It is not correct to require a determinable future date for a loan to be an excluded arrangement. Many vanilla loans will not be excluded.
(SAICA)

The wording proposed is based on an exclusion in the existing reportable arrangements legislation. SAICA is invited to provide SARS with detailed information as to why it believes this will be the case by 31 January 2007.

3.17 *Disclosure obligation – section 80O*

A reportable arrangement must be reported within 60 days of inception. However, at that time, the parties will not necessarily know if one or more of them will be disclosing the arrangement as a liability for accounting purposes. It may only be on finalisation of the audit that the accounting disclosure is finally determined.
(BASA)

This comment is not accepted. Ordinary ongoing transactions are generally well catered for by Generally Accepted Accounting Practice. With respect to more exotic arrangements, it is SARS’ experience that both the accounting treatment and tax benefits of these arrangements are considered when they are conceived.

3.18 *Penalties – section 80S*

The penalty of R1 million for failure to disclose is considered to be absurd. Even if the massive uncertainties raised are in some way clarified, this would result in businesses reporting thousands of transactions daily.
(BASA)

This comment is not accepted. As discussed above, steps will be taken to ensure that routine transactions are excluded. The penalty may be reduced both in the light of extenuating circumstances or if it is disproportionate to the assumed tax benefit. Finally, it will be clarified that SARS’ discretion in this regard is subject to objection and appeal.

RESEARCH AND DEVELOPMENT INCENTIVES

3.19 **R&D expenditure should including supporting expenditures. Operating supporting expenditures should accordingly include the employment of receptionists/secretaries to a researcher, research building maintenance and administration. In terms of capital expenditure, supporting expenditure should include meeting rooms, storerooms, canteens, workshops, vehicle parking, reception areas, secretary offices and ablution facilities (in addition to laboratories and computer room research offices).**
(SAICA)

The issue of whether an R&D expenditure is "direct" (thereby being eligible for the 150 per cent deduction) is essentially a question of fact that depends on the context. Issues of this kind are best left to interpretation.

3.20 **How does the new R&D rule apply to agricultural field land acquired for research? Also, how does the new R&D rule apply to land underneath an R&D building?**
(SAICA)

Land is never depreciable because land is not a wasting asset. The lack of depreciation for land is an across the board-tax-principle, not limited to R&D.

3.21 **How do the R&D rules apportion buildings that are partially used for R&D versus other uses? Is it area or time based? What happens if the building is used for R&D within the first 10 years and then the building is shifted to other uses?**
(SAICA)

The issue of apportionment of R&D versus other use is again a question of fact (that can arise whenever depreciation depends on use). However, the initial proposal failed to cover situations where use changes. Accordingly, under the final Bill, a recoupment rule exists for buildings that cease R&D activities within 10 years. No recoupment for change in use exists if the R&D use ceases after that date.

3.22 **The new R&D rules should apply to the acquisition of second-hand assets as long as the R&D is new.**
(SAICA)

The R&D rules do not apply solely to the acquisition of new assets. Taxpayers can obtain the incentive as long as the R&D concept is new (as requested in the comment).

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3.23 **The definition of R&D should not exclude market research to the extent that research precedes the actual R&D. Otherwise, will the need for R&D be established without conducting market research (i.e. feasibility studies)?**
(SAICA)

Not accepted. The R&D incentive of 150 per cent will retain the current exclusion for market research. The goal is to enhance the development of new knowledge (which has positive externalities for the public as a whole). Standard feasibility studies may or may not have any public value. Therefore, only the normal 100 per cent deduction should apply to reflect actual cost.

3.24 **Government grants should not limit the 150% rate for two times government grants, only an amount equal to government grants.**
(SAICA)

The doubling rule reflects the concept of a matching grant. For instance, Government often contributes R100 with the expectation that the taxpayer will match the contribution with another R100. No reason exists to provide a 150 per cent deduction for the second R100 because the second R100 is already given an incentive via the grant (and the grant itself should not be given the incentive since that sum comes directly from Government).

3.25 **The concept of beneficial ownership should be removed as it is unknown in South African tax law.**
(SAICA)

Accepted. Moreover, the whole concept of required sole ownership of knowledge has been deleted to allow for R&D joint ventures.

3.26 **The amendments should apply to expenditure occurred on or after 2 November 2006 as the effective date to stimulate R&D as soon as possible.**
(SAICA)

Accepted. The effective date has been moved forward in the final Bill.

3.27 **How do the "election-out" rules of subsection (6) apply? Must taxpayers elect out of both the 150% operating expenditure and the capital expenditure for particular R&D, or must taxpayers elect out of both? When must this election be made – can it be made every year or the year an asset enters use?**
(PWC)

The "election-out" rules have been dropped in the final Bill as creating unnecessary complexity.

3.28 **The secrecy provisions do not bind the Minister of Science & Technology, only the persons employed by the Minister's department.**
(PWC)

Accepted. The Minister will be subject to the same secrecy provisions.

OIL AND GAS INCENTIVES

Incentives for Oil and gas exploration and production-Tenth Schedule (Section 26B)

3.29 **Paragraph 6(2) refers to "…any share outstanding…". This concept is not familiar in SA and should be replaced with appropriate wording such as "…any share issued…"**
(SAICA)

The thin capitalisation rules have been substantially revised. The concept of shares has been dropped in favour of "fixed capital", a more familiar South African tax concept.

RECREATIONAL CLUBS

Partial taxation of Recreational clubs - section 10(1)(cO)

3.30 **It is unreasonable to expect such clubs to separately account for the income and costs related to such occasional use of their facilities by members of the public. The section also appears to require the clubs to account separately for food and beverage income generated from members separately to that generated from non-members. The complexity required for such accounting is huge in relation to the immaterial gains to the *fiscus*.**
(SAICA)

This comment is partially accepted. Clubs cannot remain in a better tax position than Public Benefit Organisations, which are currently subject to partial taxation for business activities. Clubs should only be exempt to the extent they represent a sharing of member expenses (the "mutuality principle"). Investment income should not generally be exempt. Taxpayers cannot obtain exempt investment income merely because that income is directed toward a hobby. Therefore, why should such investment income be exempt merely because individual members have pooled their activities? However, as a matter of practicality, activities that are integral and directly related to a club's sole or principal object (and carried on substantially on a non-profit basis) will be exempt whether they relate to members or non-members.

3.31 **The taxation of all other income subject to a *de minimus* exemption is harsh and will have negative financial implications for many clubs. Can the approach taken for PBO's be adapted for Clubs? I.e. Clubs approved in terms of 30A should be allowed a tax-free *de minimis* amount of gross income derived from non-core business activities to the greater of 15% of the total receipts and accruals derived during the relevant year of assessment; or R300 000.**
(CMASA)

The general exemption of R20 000 per annum, which will have to be applied to investment income as well as other income such as hiring out facilities to non-members. In our view, the exemption of R20 000 is too low and will result in many recreational clubs facing substantial tax liabilities that could be the cause of their demise as these clubs are self-funding and are heavily reliant on alternative sources of income. We suggest that the rules which allow public benefit organisations a tax-free ceiling of the greater of R50 000 or 5% of gross income to recreational clubs.
(SAICA)

Both comments are partially accepted. The *de minimis* threshold will be adjusted to roughly match the *de minimis* threshold for Public Benefit Organisations. Hence, the test is changed to exempt the greater of: (i) 5 per cent of member contributions/subscription fees, or (ii) R50 000.

3.32 **If the gross receipts and accruals from other sources exceed R20 000 in any year of assessment, the full amount of receipts and accruals are taxed and not just that portion of the amount as exceeds R20 000. In our view this is unduly harsh in that if such receipts and accruals in any year for example amount to R20 100, we cannot see any reason why the first R20 000 should be taxed.**
(SAICA)

This comment is accepted. Tax will apply only to the extent amounts exceed the threshold (the all-or-nothing approach is dropped).

3.33 **The word 'solely' in definition of recreational club is a restriction not commonly found in the constitutions of clubs, as the latter allows visitors to accompany members and such permission to access is in line with international practice.**
(CMASA)

This comment is accepted. The "solely" concept was never intended to be viewed in this fashion. That said, the test will be changed for clarity (along with the "sole" object test used for Public Benefit Organisations). The final Bill accordingly adopts a "sole or principal" standard.

3.34 **Members entitled to a year membership place a legal obligation on clubs and which they will not be able to enforce. The right to terminate membership for non-payment of fees vests with the Clubs and furthermore, there are different periods of membership catering for the needs of membership base.**
(CMASA)

This comment is partially accepted. Membership of a reasonable duration is necessary to separate club activities from standard business activities (which are open to the public). However, the test has been relaxed to account for annual as well as season membership.

3.35 **Concern that the time period spanned between the implementation date of section 10(1)*(c*O*)* and the later deadline date in terms of section 30A (i.e. 31 March 2011) will result in administrative quirks in applying the legislation. What will happen if a club, having relied on the section 10(1)(cO) exemption in the 2008, 2009 and 2010 years of assessment, then fails to submit its application by 31 March 2011?**
(CMASA)

This comment is accepted. The closing date for existing clubs to apply for exemption has been brought forward to 31 March 2009.

3.36 **The time period set by SARS enabling the Commissioner to determine the period within which a club must rectify a contravention should take into account the administrative constraints faced by clubs and provision should be made for the clubs to apply for a longer period if necessary.**
(CMASA)

The time period will be based on the facts and circumstances. This period would generally account for administrative constraints as requested.

3.37 **A more reasonable period to arrange for the disposal of assets should be six or twelve months and the Commissioner should be granted the discretion to allow a longer period if necessary.**
(CMASA)

This comment is accepted. The three month time period (as initially proposed) will be increased to six months. A discretion to extend this period exists in the Bill and will be retained.

3.38 **The proposed amendment provides PBO's with relief from capital gains tax on disposals of assets not used for trade. Similar relief**

should be provided for disposals of assets by recreational clubs.
(CMASA)

PBOs receive exemption for both investment income as well as certain PBO directed income-producing activities. Self-sustaining funding is critical for this sector. Clubs operate on a different basis, as discussed above, and do not warrant this level of exemption – either in terms of income or capital gains. However, clubs can obtain exemption if a club-directed asset is sold to acquire a club-directed replacement asset. Hence, clubs can upgrade facilities without any tax charge.

3.39 **It is suggested that an apportionment should be provided for in the roll-over provision proposed, where an asset has been used partly for producing exempt income. Many assets used by recreational clubs would, at some stage during their useful lives, have been used to produce income that was not exempt in terms of section 10(1)*(c*O*).***
(CMASA)

This comment is partially accepted. The all-or-nothing rule will be retained for ease of administrative enforcement (and taxpayer compliance). Apportionment is easy in theory but hard to apply in practice. While apportionment can be justified in some cases (such as R&D), the club area requires a simpler level of enforcement/compliance. However, the requirement that the asset be solely used for club activities has been relaxed to permit incidental use that generates non-exempt income.

PUBLIC BENEFIT ORGANISATIONS

3.40 *Single tax rate for PBO trading activities*

We propose that the rate for taxation for all PBOs should be 29% and not 34% as proposed in the Bill. The proposal effectively increases the existing rate of taxation for voluntary associations and section 21 companies approved PBOs by 5%. The current rate of taxation for these kinds of organisations that are approved as PBOs is 29%. Only non-profit trusts that are approved as PBOs would pay a lesser rate of taxation from its current 40% rate. Secondary Tax on Companies is relevant to companies that distribute profits and declare dividends. Dividends are not declared by PBOs and there should be no reason for comparing for-profit companies to PBOs.
(NPC)

We agree that trusts should not bear a disproportionate tax burden. However, we fail to see why domestic PBOs should be

treated like branches of foreign companies. We question the assertion that PBO subsidiaries would necessarily be liable for secondary tax on companies, and we have grave doubts about the policy rationale underlying the entire effort to equalize PBO and corporate taxes. Our understanding is that unlike income tax, which is payable on all company profits, secondary tax is payable only on profits distributed to shareholders in the form of dividends. Thus, the effective tax rate experienced by companies (income tax + STC) would depend to some extent on what proportion of profits a company decided to distribute. Even if we accept that 34% is an accurate average, we do not believe that a PBO subsidiary would necessarily attract STC if it donated its post-tax profits to its PBO arm, rather than distributing them as dividends to shareholders.
(SACC)

There is no question of STC if the PBO is a section 21 company or trust. Impose tax at a rate of 29%.
(SACBC)

This comment is accepted. The initial proposal of a 34 per cent rate is dropped. All PBOs will be subject to a flat 29 per cent rate in terms of taxable business activities. The 29 per cent rate will apply to a PBO regardless of whether that PBO operates as a company, trust or association. This 29 per cent rate will also apply to taxable club activities.

3.41 *Trading by PBOs*

The concern about tax exemption for PBOs carrying on business or trade should be challenged. The unfair competition argument has not been tested by any survey and the erosion of the tax base has not been analysed by SARS. A moratorium should be declared for two years in order to monitor the reaction of the market to competition by PBOs and to establish the actual erosion of the tax base.
(SACBC)

This comment is not accepted. In theory, PBOs should not be given an unfair advantage over private operations in terms of business activities. That said, National Treasury and SARS will be engaging the PBO sector over the medium-term to better understand the factual permutations.

3.42 *De minimis exemption for trading*

Smaller PBOs which supplement donated income through trading and runs foul of the *de minimis* exemption should be assisted by setting an level of R1 million of non-trading receipts

before the trading prohibition kicks in.
(SACBC)

The *de minimis* exception for PBOs is outside the scope of this Bill. National Treasury and SARS will be engaging the PBO sector on an ongoing basis to discuss this and other issues.

3.43 *Foreign Established Charities*

We support this proposal, but in addition we propose that such foreign charities should be required to have at least one person who is authorised to accept service on behalf of that charity, to be resident in South Africa. Section 326 of the Companies Act is an example of how such requirement has been incorporated in South African corporate law and can be mirrored in the Income Tax Act.
(NPC)

We are amenable to this proposal. This issue will be addressed in 2007.

3.44 *Relaxing the rules for permissible PBO investments*

We support this proposal. However, we have the following concerns. After the removal of the bulk of the limitations on investments that a PBO is permitted to make what remains is a prohibition in investing in –"*any financial instrument issued by, or other property held by, a person that is not a resident*." This wording may prevent a PBO from investing any portion of its funds in foreign based shares or unit trusts ("collective investments"). Under the previous "prudent investment" dispensation as set out in Interpretation Note No. 32, foreign investments through a financial institution registered in South Africa or through a locally registered foreign unit trust were acceptable. Where a PBO has a substantial portfolio of investments it is prudent for it to spread its risk by having foreign as well as local investments. Concern expressed by SARS in this regard is that the rules of section 9D of the Income Tax Act regarding "controlled foreign companies" may be misused. If this is considered a real danger it is submitted that other wording should be used to satisfy SARS's fears rather than use wording that seems to impose a blanket prohibition on foreign investments.
(NPC)

The wording relating to the new prohibition is confusing. We can readily understand that the PBO is prohibited from investing funds in any financial instrument issued by a non-resident. We cannot understand what is contemplated by the prohibition from

the PBO investing funds in a property held by a non resident. How does one invest funds in a non-residents's property (whether movable or immovable). The Explanatory Memorandum states that PBOs "will not be allowed to hold instruments issued or held by foreign persons". Unfortunately, this is equally confusing. How can a South African PBO hold an instrument held by a non-resident, either the PBO holds it or the non-resident holds it? Should the real prohibition not be that the PBO is prohibited from acquiring property situated outside South Africa (including instruments issued by persons resident outside South Africa)?
(SAICA)

These comments are accepted. After further consideration, it was decided that all prohibitions against foreign investments should be dropped. PBOs can invest freely as desired as long as investments do not amount to an indirect distribution of profits.

3.45 *Streamlining the dual registration process*

We support this proposal, but in addition we propose that a requirement similar to that contained in section 17 of the Non-Profit Organisations Act, No. 71 of 1997, (NPO Act) be required for approval as part of the reporting requirements for PBOs. Therefore, the proposed section 3C should read; "….in respect of an organisation that *<u>has been convicted of an offence</u>* committed under that Act."
(NPC)

This comment is accepted. We always intended that this rule apply only upon conviction. The proposed wording will be adopted.

3.46 *Taxation of assets held by PBOs at market value*

We propose that this sub-section should be left unchanged. The proposed change which is motivated by administrative reasons may effectively result in organisations having to close down after PBO status has been withdrawn. The proposed amendment would have dire consequences for an organisation that has accumulated immovable property over the years and because of its non-compliance, will have to pay tax on all its assets. Section 30 of the Income Tax Act only came into operation in 2001 and would affect the assets of organisations that were owned prior to 2001. These assets may even have been acquired without the organisation having had income tax exemption. It would be an unfair result for the market value of those assets to be deemed taxable income. Although capital assets are excluded from the definition of gross income under the Income Tax Act, the proposed amendment to section 30 (7) refers to "*those assets*

***which have not been transferred*", which would naturally include capital assets. The administrative reason can be addressed in a manner that is less harsh as proposed in terms of the Bill. *Firstly*, section 30 (9) of the Income Tax Act requires PBOs to retain books of account, records or other documents relating to any approved PBO for a period of four years. *Secondly*, a similar requirement contained in section 17 of the NPO Act can be required from PBOs to secure the availability of financial requirements. In view of the given circumstances and the potentially crippling effect on PBOs of tax on the market value of its assets, it is submitted that this provision should be referred back for further consideration.**
(NPC)

The proposal is that the market value of the assets not transferred will be deemed to be taxable income. It cannot be the market value that is so deemed, but rather it should be an amount equal to the market value which is deemed to be taxable income. Secondly, it may be that at the time the PBO still has liabilities which would have to be discharged out of those assets. Therefore, the deemed taxable income should be an amount equal to the market value of those assets after deducting therefrom the aggregate of all liabilities of the PBO.
(SAICA)

This comment is partially accepted. The current taxation of recorded (realised and unrealised) profits is impractical. Many PBOs lack sufficient records to allow for a retroactive review of the PBO's history. However, it is agreed that taxation of gross assets is unfair. Deemed taxable income should instead be based on net asset value (gross assets less debts), which is essentially equivalent to the taxation of realised and unrealised reserves.

3.47 *Donations to the Government*

Currently, the activities listed in Part II of the Ninth Schedule do not cover some of the donations to Government, and hence no tax benefit is available in respect of these donations. We therefore suggest that the activities listed in Part II of the Ninth Schedule should be extended to include donations to Government made for purposes of building or improving public roads and for purposes of all public infrastructure. Such broadening would ensure that all donations to Government for purposes of improving public infrastructure would be treated equally from a tax perspective, as currently only a certain activities concerning public infrastructure (for example the building of schools and housing, clinics and creches for the poor) is covered in Part II of the Ninth Schedule.
(PWC)

This request is outside the scope of the Bill. Current law allows deductible donations to all three spheres of Government on the same playing field as payments to PBOs. Donations for infrastructure may not have a solely gratuitous intent. Infrastructure donations may yield an indirect benefit to the donor (such as informal regular use by the donor).

3.48 *Limitation of S18A benefits to domestic PBOs*

While it is understandable that SARS would wish to deny domestic tax credit for donations deployed outside of the Republic, it is likely that most donations to local branches of foreign charities would be used within the Republic. Indeed, it would make more sense to make the 18A status of any given donation conditional on the end use of that donation (e.g., to activities *occurring within the Republic* and listed in Part II of the Ninth Schedule) rather than on the national home of the mediating agency.
(SACC)

Many countries (such as the U.S. and the U.K.) do not allow for deductions in respect of donations made to foreign PBOs based on the theory that charity begins at home. Tracing the use of a donation by a PBO back to a single donor will be administratively challenging to say the least. However, in response to comments such as this one, foreign donations made to a qualifying South African branch or agency of a foreign PBO can be freely transferred outside South Africa if local PBO activities of that foreign PBO terminate.

It should be noted that foreign PBOs can actually obtain deductible local contributions if these foreign PBOs utilise the proper form. A foreign PBO can form a South African company or trust that operates as a local PBO. This local PBO can then collect deductible donations. This use of a local structure to obtain local deductions makes sense because the separation simplifies tracing.

3.49 *CGT on disposal of PBO assets*

Currently, PBOs are not be exempt from capital gains tax (CGT) on assets not directly used for public benefit activities. Concerns are raised regarding practical application of this provision. First, if CGT will be assessed on *all* assets not directly deployed in connection with public benefit activities, this would mean that PBOs would effectively be penalised for investing surplus funds in securities or any financial instrument. This would be a particular problem for PBOs engaged in the provision of funds and resources to other PBOs. Presumably their activities will be supported by a significant endowment which is

likely to be invested in shares and other assets. Taxing the returns on this investment will undermine their capacity to finance public beneifit activities and tend to frustrate the very objectives that the PBO tax regime was established to promote. Even if the assessment of CGT is limited to real assets (and the law is further amended to clarify this), there would still be practical problems with the assessment of CGT on assets that have a hybrid use or that undergo a change of use. We would urge Parliament to consider amending the legislation to give PBOs a two-year grace period in which to dispose of property that ceases to be uses primarily for public benefit activities. The period should also be calculated to the date of sale, rather than the date of transfer.
(SACC)

Practical application of this section is best left to interpretation given the inherently factual nature of these issues. Discussions are anticipated with the PBO sector on these and other issues.

Prudent investments should not be subject to CGT on realisation. Make it clear that financial assets are not taxed.
(SACBC)

This comment is accepted. The proposal completely eliminates any restrictions on investments unless operating as an indirect profit distribution.

3.50 *Advocacy for the non profit sector*

There should be a requirement that Treasury and SARS work with a structure that would be an official advocate for the non profit sector, e.g. similar to the Charities Commission in the UK.
(SACBC)

National Treasury and SARS engagement with the PBO sector cannot be legislated as a practical matter. However, discussions with the PBO sector have been ongoing, thereby resulting in the liberalised PBO regime announced in this Bill.

TAXATION OF FOREIGN INCOME

3.51 *Rebate in respect of foreign taxes on income – section 6quat*

A rebate is denied for withholding taxes suffered in countries (with whom South Africa does not have a tax treaty) where the taxes relate to fees for services provided to the foreign country, on the basis that these fees have a South African source (Head office management fees and charges for technical services). This is wholly contrary to international interpretations or

legislation regarding similar instances. The requirement that the income must be from a foreign source for relief to be given should be removed.
(BASA)

This issue is wholly outside of the legislation proposed. Moreover, this issue is best left for tax treaties as opposed to domestic legislation. The commentator is essentially advising South Africa to provide foreign tax credits for activities that arise from local sources (in violation of internationally-accepted tax principles).

Allow foreign tax credits relating to CFCs to be carried forward where the related South African company is unable to utilise these credits because of domestic tax losses.
(BASA)

This comment is again outside the legislation proposed. It is also not entirely clear. Foreign tax credits can be carried forward for seven years if not utilised. It appears that the taxpayer is seeking to shift foreign tax credits within a group. Credit shifting, like loss shifting, within a group of related companies is not sanctioned.

3.52 *Definition of "foreign business establishment"- section 9D(1)*

CFCs can rely on employees of group companies within the same country of residence to satisfy the business establishment requirement

3.52.1 *Services to be rendered on a full time basis*

The requirement that the management and employees are required to render services on a fulltime basis for that business is unrealistic and impractical. Clearly, if employees in a group are working for more than one company, it cannot be fulltime for anyone of them, but will for all of them collectively. Also, it is unrealistic to require each foreign business establishment to be staffed by full time employees, especially if such employees are required to be of a managerial level.
(SAICA)

Also, the "full time" requirement and "purposes of conducting the primary operations of that business" seem to get confused in the current reading. It becomes unclear as to whether the activities of an individual looking after several businesses on a full time basis would constitute a foreign business establishment.
(SAICA)

In the context of the services company, it is not clear as to whose business is being referred to here? In other words is it the business of the CFC or the services company?
(SAICA)

We are concerned that the requirement for those employees to render their services on a full time basis could be implied to mean on a full time basis to the CFC seeking to establish its foreign business establishment. Often, where group services companies are used, their employees may render their services to a number of different group companies in that territory and cannot be said to do so to any one company on a full time basis. It is suggested that this requirement be relaxed to allow for the rendering of services on a full time basis for that business or the business of other group companies in the same country of residence. In this regard, we suggest that the explanatory memo be amended to state that the proposed amendments bring the legislation in line with the practice employed by SARS in terms of rulings they have issued previously.
(PWC)

The final Bill allows for a greater level of reliance on group companies for purposes of the general foreign place of business test under paragraph (a). CFCs can rely not just on full-time employees, but also equipment and facilities of a related group CFC. However, this reliance will require a SARS ruling in order to verify various aspects of the structure so as not to allow an unacceptable erosion of the tax base.

3.52.2 *Group company requirement*

The requirement that the exemption will only apply where the company providing the on-site managerial and operational employees forms part of the same group of companies as the controlled foreign company is restrictive. It is suggested that the exemption should apply to companies in the same group of companies where the reference to shareholding is more than 50% as opposed to at least 70% as is currently envisaged in the proposed definition of connected person in section 1 of the Act.
(SAICA)

Not accepted. Group treatment in the context of CFCs and onshore companies consistently requires a 70 per cent connection. The connected person standard is aimed largely at anti-avoidance (whereas, the 70% is intended to alleviate group transactions where the parties fully operate as a single economic unit).

3.52.3 *CFC must be suitably equipped and have proper facilities for business* *purposes*

The proposal that the place of business must be suitably equipped and have proper facilities is restrictive. No indication is given as to whether it would be acceptable if the equipment and those facilities were used on a shared basis together with other group of companies.
(SAICA)

Accepted. As discussed above, taxpayers can rely on equipment of a related group CFC via the SARS ruling process.

3.52.4 *Property Service Companies*

It is requested that further consideration be given to introduce a provision allowing the use of shared employees in respect of property service companies (paragraph (a)(ii)), as many groups hold their real estate investments in a territory through a single company which then on-charges the other companies in that territory for use of the property.
(PWC)

Accepted. As discussed above, reliance on group CFC employees will be allowed via the SARS rulings process.

3.52.5 *CFC international transport can satisfy the local foreign business requirement if the transport occurs wholly outside SA*

The proposed amendment requires that the vessel must be used "solely outside the Republic" for the purposes of transportation, etc. With regard to aircraft and vessels operating in and around Africa, it may happen that they are returned to South Africa for maintenance and repairs as there are very few places elsewhere in Africa where this can be done. It can be argued that if they are returned to South Africa for maintenance or repairs, it should not prejudice the existence of the business establishment, because this would not constitute use in South Africa for purposes of transportation or fishing or prospecting, etc. It is therefore proposed that the provision should be clarified to allow for occasional trips to South Africa for maintenance, repairs, refurbishment or the like.
(SAICA)

The initial proposal allows for this possibility. Ships and aircraft can return for non-transport purposes. This aspect of the test is clarified in the explanatory memorandum.

3.53 *Definition of "foreign financial instrument holding company" - section 9D(1)*

The reference to instrument as defined in section 24J(1) is inappropriate as this would exclude any interest free loans between group companies. The rationale for excluding amounts due between group companies holds also for interest free loans and the failure to exclude these as "financial instruments" would result from the proposed definition at odds to the approach currently taken.
(PWC)

The financial instrument test has been completely rewritten in the final Bill. The goal was to eliminate certain financial instruments from the financial instrument holding company tests for the company reorganisation provisions – no comparable change was intended for section 9D.

Diversionary Transaction Rules

3.54 *Services provided by a CFC to a connected SA resident – section 9D(9)(b)(ii)(cc)*

It would appear that the exclusion from the exemption in section 9D(9)(*b*)(ii)(*cc*) favours a CFC providing goods as opposed to services. If the provision of services relates to the creation of intangibles, the income received from such services is immediately tainted. This is despite the fact that there may be sound business reasons for having a CFC provide such services to a South African resident that is connected to a CFC. It is recommended that the exceptions provided in section 9D(9)(*b*)(ii)(*cc*) be expanded to allow for the foreign business exemption to apply where a CFC provides contract research and development services to a connected South African resident. As these services would be for the development of intellectual property which will be used by the connected resident in South Africa, it is not feasible to have a proviso that such services should be provided for intangibles which will be utilized by third parties in the CFCs country of residence. If a tax avoidance is considered necessary, it could be provided that the foreign business establishment exemption only apply if the research and development services are carried out on behalf of the South African connected party in the CFCs country of residence because such expertise is not available in South Africa or because the cost implications of carrying on such services in South Africa would be prohibitive for the South African resident.
(SAICA)

Not accepted. If a South African company makes deductible service payments to a CFC, a corresponding CFC inclusion is required for the service receipts by that CFC. On the other hand, no CFC inclusion will be required if the South African company is not entitled to a deduction for the payment. In the case of R&D, the South African will not be entitled to the 150 per cent deduction because the R&D is conducted offshore and the deduction may not be available at all if the amount is a capital expenditure. If the South African cannot take the deduction, no CFC inclusion is required (i.e. no deduction; no inclusion). Hence, the transaction should be tax neutral either way.

The proposed insertion of section 9D(9)(*b*)(ii)(*cc*)(C) and (D) is welcomed. We would be grateful if the explanatory memo would confirm that in instances where the South African resident taxpayer who is a party to the transaction themselves choose not to claim the related expenses on their tax return the exemption will apply.
(PWC)

The explanatory memorandum covers both provisions. It should be noted that the deduction for the South African company is not elective. The South African company is entitled to a deduction or not as provided by law. Whatever the outcome, section 9D(9)*(b)*(cc)(D) follows a matching principle.

3.55 *Clarification of the meaning of "delivery" – section 9D(9)(b)(ii)(bb)(C)&(D)*

The proposed requirement for physical delivery to the premises of clients situated within the country of residence of the CFC is far too strict, especially having regard to the fact that there are already both substance and arm's length test in place. It happens that a customer purchase goods and has them delivered elsewhere, e.g. to the customer of the purchaser for installation to another supplier of the customer for further processing or to a building site. We proposed that the amendment should include the following words "*or such other premises as instructed by any such customer".*
(SAICA)

The "delivery" rule is designed to ensure that the customer's economic activities arise in the same country as the CFC's country of residence. Allowing for the complete redirection of goods by the customer undermines this rule.

3.56 *Intra CFC exemption - sections 9D(2A)(c)and 9D(9)(fA)*

In order to make it clear that this exclusion applies equally to section 31 adjustments and section 24I exchange differences and not only to interest, rental, royalties or other income, it is suggested that the proposed amendment in section 9D(2A)(c)should read as follows "(*ii) that interest, royalties, rental*

or income of a similar nature paid or payable or deemed to be paid or payable by that company to any other controlled foreign company (including any similar amount adjusted in terms of section 31) or any exchange difference determined in terms of section 24I in respect of any exchange item to which that controlled foreign company and other foreign company are parties where that controlled foreign company and that other controlled foreign company form part of the same group of companies is included in the net income o that other controlled foreign company".
(SAICA)

The final Bill has been changed to cover section 31 adjustments and section 24I exchange differences.

3.57 *Exemption granted by Commissioner (rulings procedure) – section 9D(10)*

3.57.1 *General*

While the principle of the exemption is welcomed, however, in order to establish the exemption available, it is necessary to go through the whole calculation process as if the exemption was not available. This adds unnecessary compliance and administrative burden to both the taxpayer and SARS.
(SAICA)

Internationally, CFC taxation is often the most complex aspect of the Income Tax provisions due to the sophistication of multinational operations. Rough justice simplicity either results in unfairness for the taxpayer or avoidance to the detriment of the fiscus. The new ruling process proposed is designed to achieve the right result (admittedly at an added compliance cost).

Is the exemption valid for a particular year of assessment or rather for a particular period of time? Does the exemption apply to a particular transaction i.e., a particular sale of goods or supply of services?
(SAICA)

The duration and scope of the exemption will depend on the ruling requested and the factual situation. Flexibility will be required for SARS (and the taxpayer) so the best result can be achieved.

The proposed relief only applies in very limited circumstances, where goods are sold or services are rendered to connected persons. This is of little value to multinational banking groups. This relief should be extended to circumstances where financial

institutions earn interest and related income in similar circumstances.
(BASA)

The rules for financial services are generally covered elsewhere in the CFC legislation. Those rules have also been liberalized, but related group payments remain a concern because these related group payments are the hallmark of a treasury operation, not a stand-alone banking operation.

3.57.2 *Subject to tax determination*

Is the application of "subject to tax determination" applied on a hypothetical basis? (i.e., if the amounts form part of the tax base of the foreign jurisdiction (in other words are not exempt) and are subject to tax at a rate of at least 2/3 of 29% then they would qualify), *OR* Is the determination to be made on an absolute basis? (i.e., having regard to the absolute amount of tax paid or payable in the foreign jurisdiction).
(SAICA)

The two-thirds test requires a comparison of the projected foreign tax calculation with a hypothetical South African tax calculation. This process is comparable to "high-taxed" CFC exceptions in other countries (such as the U.S. and the U.K.).

South African multinationals cannot take advantage of the low tax rates of intermediary jurisdictions as can the multi-nationals headquartered in the UK, Australia, Canada and most European countries. The 2/3 differential in is not substantial to make the use of an intermediary jurisdiction worthwhile.
(SAICA)

Not accepted. CFC legislation around the world is typically designed to prevent offshore incorporation in tax haven locations. Cases may exist where taxpayers can escape this regime, but this escape is often not intended by the tax authorities, especially if no substantive activity occurs in those tax haven locations.

We are concerned that the calculation in section 9D(10)(a)(i) is overly harsh in determining the foreign tax after use of assessed loss, credit or rebate. Where, for example, the foreign country has a system of group relief, the CFC in question may well have no foreign tax due to reasons entirely independent of transactions with SA residents. To deny the availability of the Commissioner's discretion in such instances is inappropriate.
(PWC)

Partially accepted. Assessed losses will not be taken into account for purposes of the two-thirds tax calculation.

3.57.3 Contiguous countries

The two contiguous countries exclusion is too narrow. For instance, Switzerland can no longer be used for trade with Belgium because the two countries are not contiguous. This will make South African headquartered multi-nationals uncompetitive in comparison and will increase the current trend of South Africans to headquarter their companies in countries other than South Africa, leading to a loss of revenue for the fiscus.
(SAICA)

The new rule represents a relaxation of the CFC regime, not a tightening. At some point CFC taxation is intended. Without knowing the facts, Switzerland may be used as a low tax location. Blanket exemptions in this area can often lead to the avoidance that CFC legislation was designed to target. The commentator must provide more facts on this issue.

What is envisaged by the term "contiguous countries". Would this encompass for example, the UK and Ireland separated as they are by the Irish Sea?
(PWC)

The contiguous country exception only covers countries connected via land.

3.57.4 Regional Hubs

In line with the manner in which many multinational groups operate, it is proposed that this discretion be available in respect of companies operating as regional hubs, in respect of that region.
(PWC)

The contiguous country exception proposed essentially allows for certain forms of regional hub activity.

3.57.5 Active royalties

The lack of any amendment to section 9D(9)(b) in respect of "active royalties" is sorely disappointing, particularly in light of information provided previously and the numerous discussions with both National Treasury and SARS on the matter. We urge that the amendments sought be introduced.
(PWC)

Partially accepted. "Active royalties" have been included in the rulings procedure.

3.58 *Definition of "foreign financial instrument holding company"* *(paragraph (b) - section 41(1)*

The insertion of the wording *"or influenced company as the case may be"* is considered necessary to clarify that there is no requirement for the influenced companies in relation to a company to conduct their business in the same jurisdiction as the influencing company.
(PWC)

Accepted. The wording has been changed as requested.

The new proviso states that the Commissioner "may disregard" business conducted in another country if attributable to a permanent establishment. Surely, this should be "must" as on what basis would the Commissioner be given a discretion? If the word "may" is to be retained, then the Commissioner's decision should be made subject to objection and appeal.
(SAICA)

The proviso has been deleted. Specifics requiring country of residence activity to be "more than any other country" in terms of financial services is generally applied without regard to Commissioner discretion. However, the Commissioner is given some discretion in the rulings process to provide relief upon taxpayer request.

3.59 *Definition of "foreign financial instrument holding company" (paragraph (i)(cc) - section 41(1)*

It would appear that the amendment renders the definition of foreign financial instrument holding company to be a nullity. With this amendment, the proviso states that there must be wholly disregarded any financial instrument other than an instrument defined in section 24J(1) with a term of less than 12 months. Thus all instruments of a longer term, as well as all shares, derivatives, collective investment scheme investments, and so on, will now be wholly disregarded in computing the prescribed proportion. Surely, this should read "with a term of more than 12 months"?
(SAICA)

The proposed amendments are entirely at odds to past practice. It disregards all financial instruments (including for example, portfolio shareholdings) other than instruments as defined in section 24J(1) with a term of less than 12 months. Clearly this cannot be intended. We would welcome the chance to discuss what exactly the intention is and how best to achieve this.
(PWC)

Not accepted. The goal was to remove cash and cash equivalents from the financial instrument holding company test. Short-term instruments of this nature typically do not give rise to intended trafficking of built-in gains and built-in losses via the company restructuring rules. It is the longer-term instruments that may give rise to the problem. The error which gave rise to the confusion has, however, been corrected.

PERSONAL SERVICE ENTITIES

Fourth Schedule

3.60 **Regular payment test for independent contractors should be deleted.**
(SAICA)

Outside scope of budget and not part of the RLAB.

3.61 **Reducing the required number of full time employees (not a connected person to the shareholder or company) from 4 to 3 does not go far enough. Proposal is to reduce the required number of employees to one.**
(SAICA)

Not accepted. One-person service operations do not differ substantially from service employees. The proposed change would reopen the very same tax avoidance giving rise to many of the personal service anti-avoidance rules.

3.62 **The 'good faith' requirement for a declaration by a contractor that it is not a PSE is difficult to apply. It is proposed that this requirement be eliminated.**
(SAICA)

Not accepted. Good faith reliance is a commonly accepted legal test. The new test allows clients to escape personal service withholding by relying on the contractor's statement in good faith.

3.63 **The requirement for a 34% withholding rate on payments to a PSE is too high and should be reduced.**
(SAICA)

Taxpayers can reduce the 34 per cent rate upon receipt of a directive from SARS. The directive process allows the rate to be reduced to level more in line with the final liability. Otherwise, the 34 per cent rate stands as viable proxy for standard employee withholding.

3.64 **Costs of fringe benefits should also be deductible for PSE**
(SAICA)

Not accepted. Fringe benefits are the precise area of concern in this area. PSEs should not receive tax benefits for fringe benefits that are not available to standard employees.

3.65 **Employee with separate business income should be allowed expenses related to that business against business income.** (SAICA)

Outside scope of budget and not part of the RLAB.

3.66 **Propose splitting of business activities for company doing both PSE/labour broking and other business activities. Currently expenses relating to business activities will be denied if disallowed in terms of PSE/labour broking provisions. Propose retroactivity to April 2000.**
(SAICA)

Retroactivity is generally rejected because retroactive legislation undermines administration. The splitting proposed is unclear and must be rejected at this stage due to time constraints.

Also proposal for splitting part year PSE/labour broker and part year independent contractor
(PWC)

The splitting proposed is unclear and must be rejected at this stage due to time constraints.

3.67 **Wear-and-tear allowance on assets used for trade purposes should be allowed for PSE.**
(SAICA)

The Bill does allow for wear and tear to be deducted. The amendment must be read in conjunction with the rest of the section.

3.68 **Reducing the required number of full time employees (not a connected person to the shareholder or company) from 4 to 3 does not go far enough. Proposal is to reduce the required number of employees to one.**
(SAICA)

Not accepted. One-person service operations do not differ substantially from service employees. The proposed change would reopen the very same tax avoidance giving rise to many of the personal service anti-avoidance rules.

3.69 **Wants explanatory memorandum on change to definition of 'investment income' that limits investment income to immovable property.**
(SAICA)

The request is accepted. The legislation now makes it clear that passive investment (generally falling outside the scope of small business status) does not include rental income from movable property. Hence, rentals from car hires are treated like any other active small business.

TAXATION OF RETIREMENT FUNDING

3.70 **Propose total revision of second schedule.**
(SAICA)

Outside scope of budget and not part of the RLAB.

3.71 **Propose special provisions dealing with SOI benefits:**

- **Definition of pension, provident and retirement annuity fund should be changed to allow SOI lump sum payments, and**
- **A portion of these payments should not be subject to withholding tax**

(LOA)

The comment is accepted. The final Bill reflects the changes made in consultation the industry to effectuate the Statement of Intent agreed upon earlier this year.

3.72 **Want Income Tax Act to allow "cooling off" period for RA's that are not underwritten.**
(LOA)

Current law presumably allows for a "cooling off" period in terms of locking in retirement annuity investments because the contract can already be unwound for non-tax purposes. However, the law makes this "cooling off" period explicit.

FURTHER INCOME TAX AMENDMENTS

3.73 *Definition of "connected person – section 1*

This amendment may introduce unforeseen anomalies, particularly where one company sells assets on an arms'-length basis to a connected company. There is no clear need for this amendment, and that it should be scrapped, given its potential to result in anomalies.
(BASA)

This comment is not accepted. The proposed amendment maintains the most important aspect of the existing holding company / subsidiary provisions in the definition, which are being deleted in order to do away with the reference to the Companies Act, 1973.

3.74 *Subsistence allowance for foreign travel – section 8(1)*

Current payroll facilities do not cater for differentiation of subsistence allowance on the basis of different countries or regions. This would imply a manual process, which would be hugely onerous on larger payrolls to administrate. The implementation date should be gazetted to allow payroll administrators to liaise with SARS in sorting out practical difficulties, before implementation occurs.
(BASA)

This comment is partially accepted and the amendment will apply to tax years of individuals commencing 1 March 2007.

3.75 *Recovery and recoupment provisions - section 8(4)(k)*

We propose that a definition of disposal for purposes of the general provisions of the Act be introduced in section 1 of the Act so as to provide clarity as to what is meant by the disposal of an asset (other than for purposes of CGT).
(SAICA)

This comment is not accepted. The ordinary meaning of the word "dispose" applies.

3.76 *Interest exemption for non-residents – section 10(1)(h)*

Consideration should be given to extending the amendment to the provisions of section 8E of the Act dealing with hybrid equity instruments especially where the holder of the hybrid equity instrument is a non-resident.
(SAICA)

This comment is accepted and the legislation has been amended.

3.77 *Exemption of scholarship or bursary – section 10(1)(q)*

We can understand the motivation for keeping the salary level fairly low so that only lower-income employees can benefit from this exemption, but we would strongly recommend that the R60 000 and R2 000 amounts be increased as these monetary limits have not been amended since 2002. There is hardly a tertiary-level course that would qualify using the limit of R2 000.
(SAICA)

This comment is partially accepted and the R2 000 threshold is increased to R3 000. The income threshold of R60 000 is aligned with the SITE threshold of R60 000.

The requirement that the employee or relative agrees to repay the bursary to the employer if he fails is impractical to implement. Would the exemption be removed retrospectively if the employee does not reimburse the employer? This aspect should be clarified.
(SAICA)

This comment is partially accepted and the requirement that the bursary to the relative should be repaid if the relative fails has been withdrawn.

The wording of the proposed amendment and the explanatory memorandum s matter needs to be reconciled.
(BASA)

This comment is accepted and the Explanatory Memorandum will be aligned with the wording of the Bill.

3.78 *Payment of tax pending objection – section 88(1)*

The proposed amendment providing that payment is not suspended by an objection, is extremely prejudicial and inequitable to the taxpayer having regard to the way our tax system is administered. While it is accepted that the "pay now argue later" rule is part of our law, the way our law is administered, extending the rule in this manner ignores the prejudice that can be caused to taxpayers by the lack of resources in SARS. On what possible basis can SARS conceivably expect to be paid in respect of a clerical error, pending that error being sorted out at a later stage? Moreover, given the lack of resources which still prevail within SARS in most branch offices; it can still take up to 6 months for such an objection to be dealt with. To put the taxpayer in a position where the tax must be paid when objection is lodged, when only one official has been dealt with is grossly inequitable and unreasonable. We strongly suggest that a subsection be inserted to grant the Commissioner the discretion to extend the date for payment or delay payment entirely where the Commissioner is satisfied the taxes may not be payable.
(SAICA)

The amendment to section 88 has been withdrawn.

3.79 *Refunds-section 102*

The delaying of a refund to a taxpayer because of outstanding returns should take into account any extension of time that has been granted to the taxpayer by SARS. For example, if a taxpayer has not lodged a return but has an extension of time to submit such return by a future date, any refund of taxes overpaid should not be suspended until the return is lodged.
(SAICA)

The delay in the refund in this regard will only occur where the taxpayer has failed to furnish a return. Where an extension of time for submission of a return has been granted there would only be a failure to submit where the return is not submitted by the end of the period of extension.

3.80 *Current GAAR – section 103*

There is no effective date for the deletion of subsections (1) and (3). The effective date of the deletion cannot be made with effect from the date of the promulgation of the amending legislation as these sections should still be available to the Commissioner in respect of transactions entered into prior to the effective date of sections 80A to 80L.
(SAICA)

An effective date has been introduced which allows the current GAAR provisions to apply to transactions entered into before the effective date of the new GAAR.

3.81 *Definition of "remuneration – Fourth Schedule*

For consistency the definition of "remuneration" should be amended to exclude payments received by a person trading independently and who is not subject to supervision and control as to the manner in which and the hours during which duties are performed unless those duties are mainly performed at the premises of the client.
(PWC)

This comment is not accepted. The definition of remuneration does not contain other provisions that apply to personal service entities, so consistency would require a broader review and changes.

3.82 *Impact of currency hedging gains and losses on base cost – paragraph 20 of the Eighth Schedule*

In terms of the International Financial Reporting Standards (IFRS), where a company takes out foreign exchange cover for an

asset or liability of a group company, such company taking out the foreign exchange cover is required to account for any profit of loss on such foreign exchange contract in its own (company) income statement as such foreign exchange item is not a hedge. This means that the proposed amendment will not have any effect of not taxing any such gain. The amount will not appear in the group financial statements but we do not have group taxation and hence the group financial statements are irrelevant to SARS as there is no taxpayer being a group of companies.
(SAICA)

This comment is accepted and the amendment will have the effect that the consolidated income statement of the group financial statements will be evaluated to determine whether the base cost of the asset should be adjusted.

ESTATE DUTY

3.83 *Power to appoint agent – section 12A*

The appointed agent cannot be expected to be able to distinguish what amounts the executor holds in his/her capacity as the executor and which he/she owns in his/her personal capacity. The amendment should not be introduced.
(BASA)

This comment is not accepted. SARS is however willing to discuss the practical implementation of this provisions with BASA.

VALUE-ADDED TAX

3.84 *Deemed supply by an "IDZ operator" – section 8(24)*

The term "an IDZ operator" should be defined in the VAT Act.
(SAICA)

The term IDZ operator is defined in the VAT Act and refers to the definition in the Customs and Excise Act, 1964 (Act No. 91 of 1964).

3.85 *Deemed supply in respect of payments received in respect of taxable supplies of goods or services which exceed the consideration charged for that supply and which is not refunded within 3 months – section 8(27)*

Three months is too short a period for the refund of payment. SAICA suggests that it should preferably be six months.
(SAICA)

This statement is noted. The reason for granting the vendor a period of 3 months after the overpayment has been received is due to the fact that the vendor has collected VAT which is included in the overpayment, which should be paid over to SARS. In addition, the actual accounting of the VAT in respect of the overpayment will be reflected in the VAT return which will only be submitted in the 4th or 5th month (depending on the vendor's tax period) after the overpayment has been received by the vendor. In view of practical difficulties that may be experienced the period is extended to 4 months which will now require the declaration of the overpayment to be made 5 or 6 months (depending on the vendor's tax period) after the overpayment has been received by the vendor.

3.86 *Accounting for the adjustment where input tax was claimed and the creditor was not paid within 12 months – subparagraph (ii) of the proviso to section 22(3)*

It is believed that the removal of the reference to 12 months may lead to a double accounting for the adjustment.
(SAICA)

This proposal is accepted and the draft legislation has been amended.

3.87 *Advance Tax rulings - section 41A*

Section 41A revokes all rulings issued prior to 1 January 2007 and SAICA does not accept that all rulings issued prior to 1 January 2007 have no force and effect, as there will clearly be a period within which the taxpayer will be left with no ruling.
(SAICA)

This statement is noted. However, the proposed amendment to section 41*(c)* provides that although in effect the rulings will not be binding in terms of section 41*(c)* after 31 December 2006, the Commissioner has powers to extend the period of validity of the rulings beyond this date. In this regard, a general ruling as well as an interpretation note will be issued. In addition, where a ruling relates only to supplies which were made prior to 1 January 2007, the taxpayer will be able to rely on the ruling that was issued provided the current provisions of section 41*(c)* of the VAT Act have been met.

3.88 *Publishing of binding VAT rulings and binding VAT class rulings – section 41B*

SAICA disagrees with the proposal not to publish VAT rulings issued in terms of section 41B where the new rulings are the same or substantially similar to the VAT rulings already published.
(SAICA)

The purpose of the provision is to prevent multiple routine rulings having to be published on the same issue or problem. The intention is that if multiple private VAT rulings are requested on the same subject, a general ruling will be given.

General

3.89 The South African Institute of Chartered Accountants and PricewaterhouseCoopers proposed a number of amendments in respect of provisions which are outside the scope of the Bill currently under consideration by the PCOF. For that reason no responses are presented to those proposals at this time.

3.90 **If an existing shareholder of a company which transferred its business assets to a newly formed company holds more than 50% of the equity capital in the new company, the new company will not be allowed tax allowances on its cost of the qualifying assets but the tax allowances will be determined on the lower of the original cost to the selling company and the market value at date of sale to the new company. We understand the historical need for this anti-avoidance measure prior to the introduction of capital gains tax (CGT) but given the introduction of CGT and the better enforcement capability of SARS, we are of the view that there are more than sufficient measures in place to counteract any possible tax-avoidance in this area. There is no need for this "connected person" anti-avoidance provision, which has at its source the "connected persons" definition**.
(SAICA)

3.91 **CGT is triggered where corporate re-org. rule criteria (sections 42, 43 and 45) are not fully complied with (i.e. the 18-month holding period rule). Collective Investment Schemes are effectively exempt from paying CGT but not for purposes of this provision.**
(PWC)

3.92 *Process*

The Chairperson highlighted that a process should be implemented to ensure that there is no misunderstanding in respect of issues raised by commentators and that all concerns are taken on board.

Prepared by the National Treasury and SARS