

BINDING GENERAL RULING (INCOME TAX) 8 (Issue 3)

DATE: 12 May 2022

ACT : INCOME TAX ACT NO. 58 OF 1962
SECTION : SECTION 1(1), DEFINITION OF “GROSS INCOME”
**SUBJECT : APPLICATION OF THE PRINCIPLES ENUNCIATED BY THE
BRUMMERIA CASE**

Preamble

For the purposes of this ruling –

- “**BGR**” means a binding general ruling issued under section 89 of the Tax Administration Act, 2011;
- “**SCA**” means the Supreme Court of Appeal of South Africa;
- “**section**” means a section of the Act unless otherwise stated;
- “**TA Act**” means the Tax Administration Act No. 28 of 2011;
- “**the Act**” means the Income Tax Act No. 58 of 1962;
- “**the *Brummeria* case**” means the judgment handed down by the SCA in *Commissioner, SARS v Brummeria Renaissance (Pty) Ltd* 2007 (6) SA 601 (SCA), 69 SATC 205; and
- any other word or expression bears the meaning ascribed to it in the Act.

1. Purpose

This BGR prescribes in which year of assessment the right to use an interest-free loan should be included in the taxpayer’s gross income as well as the method to calculate the value of such right.

2. Background

Issue 1 of the BGR was issued on 30 June 2010 as a result of the judgment in the *Brummeria* case. Issue 2 of the BGR substituted references to section 76P with references to the TA Act and updated the dates in the examples and Issue 3 updates the dates and the weighted-average prime overdraft rates for banks relating to the relevant year of assessment in the examples. The principles dealt with in this BGR remain unchanged.

3. Ruling

Agreements in the retirement industry are frequently structured in such a way that one person (the owner of a unit) grants a lifelong right of occupation over that unit to another person (the life-right holder). As compensation the life-right holder advances the owner an interest-free loan for the duration of the period of occupation.

Only amounts received by or accrued to a taxpayer during a particular year of assessment must be included in that taxpayer's gross income for that year of assessment.¹ The value of a right that accrues to a taxpayer in a particular year of assessment must be determined in that year.²

In calculating the monetary value of the right to use an interest-free loan in the year in which it is granted, it should be taken into account that the owner of the unit has given something in exchange to the life-right holders. The *quid pro quo* is the granting of the lifelong right of occupation of the unit. The owner is therefore left only with the bare *dominium* of the unit for the full period of the loan. Only when the loan is repaid and the life right is re-united with the bare *dominium*, will the owner be in a position to deal freely with the complete ownership of the unit.

The value of this *quid pro quo* given by the owner of the unit to the life-right holder should therefore be determined and taken into account in the valuation of the right to use the interest-free loan.

The right to use an interest-free loan granted by an occupant in a retirement village to the owner of that unit in exchange for the granting of a life right of occupation in respect of that unit usually does not relate to a fixed period. Instead, the period over which the right to the use of the loan is to be enjoyed depends on the life expectancy of the life-right holder and certain other contractually agreed contingencies (such as the possibility that the life-right holder may cancel the loan before his or her death).

In view of the above, it may be accepted that the value of the right to use the interest-free loan should be calculated in the year that the loan is granted using the following formula

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

with reference to the following factors:

- A = The monetary value of the right of use of the interest-free loan which must be included in gross income
- B = The amount of the interest-free loan
- C = The present value of R1 a year over the life expectancy of the life-right holder*, or in the case of more than one life-right holder, the youngest of them
- D = The weighted-average prime overdraft rate for banks relating to the relevant year of assessment
- E = 93,1% (The percentage to be allocated to the monetary value of the life right of a unit, as opposed to the value of the complete ownership of the unit. This average percentage has been determined actuarially and is acceptable to SARS for all life rights granted.) SARS has accepted this method as a basis for calculating the amount to be included in gross income. This deduction compensates the owner of the unit who gives a right to occupy the unit as a *quid pro quo* for the right to use an interest-free loan.

¹ Definition of "gross income" in section 1(1).

² *CIR v People's Stores (Walvis Bay) (Pty) Ltd* 1990 (2) SA 353 (A), 52 SATC 9.

- * The life expectancy of the life-right holder and the present value of R1 a year for the life of the life-right holder may be determined by using the life-expectancy table issued under Government Notice No. R1942 of 23 September 1977 under section 29 of the Estate Duty Act No. 45 of 1955 (see **Annexure**).

The monetary value of the right to use the interest-free loan in the year in which it is granted and paid must be determined by multiplying the amount of the loan by the present value of R1 a year for the lifetime of the life-right holder and the weighted-average prime overdraft rate determined for the relevant year of assessment. The amount so calculated is then reduced by 93,1%. **Note:** This is a once-off calculation of the amount to be included in the gross income of the borrower in the year of assessment in which the borrower becomes entitled to the right to use the loan. The amount is therefore not re-calculated and included in the borrower's gross income in each subsequent year until the loan is repaid.

Example 1 – Calculation of the monetary value to be included in gross income

Facts:

A retirement village is held under sectional title by the owner. The scheme is governed by the Housing Development Schemes for Retired Persons Act No. 65 of 1988. On 1 June 2020 the owner enters into an agreement, under which the owner grants a life right of occupation over a sectional title unit in the village to a person aged 75.

Under the agreement, the 75-year-old person and that person's spouse will be entitled to occupy the unit in exchange for the grant to the owner of the use of an interest-free loan of R400 000. The life-right holder advanced the loan on 1 July 2020.

The person turned 75 on 16 February 2020.

According to the life-expectancy table (see **Annexure**) the present value of R1 a year for the life of the 75-year-old male is 4,59354 (age next birthday = 76).

The interest-free loan is repayable by the owner of the village to –

- the life-right holder upon cancellation of the agreement under various circumstances, which include the life-right holder falling ill and requiring full-time medical care; or
- his or her estate when he or she dies.

The weighted-average prime overdraft rate for banks during the relevant year of assessment is 7,71%.

The financial year of the owner of the retirement village commences on 1 March 2020 and ends on 28 February 2021.

Result:

The monetary value of the right to the use of the interest-free loan is calculated as follows:

$$\begin{aligned}
 A &= (B \times C \times D) - E \times (B \times C \times D) \\
 &= (R400\,000 \times 4,59354 \times 7,71\%) - 93,1\% \times (R400\,000 \times 4,59354 \times 7,71\%) \\
 &= R141\,664,77 - R131\,748,23 \\
 &= R9\,916,54
 \end{aligned}$$

An owner that is obligated to refund only a portion of the loan on death or cancellation of the agreement must include the amount not refundable in gross income in the year of assessment in which the loan is granted and paid by the person acquiring the life right.

Example 2 – Full loan amount not refundable*Facts:*

The agreement between the owner and the life-right holder provides that only 80% of the interest-free loan of R900 000 is refundable on death.

Result:

The owner must include R180 000 (20% × R900 000) in gross income in the year of assessment in which the loan is granted and paid by the life-right holder.

In addition, an amount equal to the monetary value, calculated in respect of the right to use the interest-free loan, must be included in the owner's gross income in the year of assessment in which the loan is granted and paid.

Note: For purposes of calculating the monetary value, symbol "B" in the formula is 80% × R900 000 = R720 000.

In the case of an interest-free loan, the benefit to retain and use the interest-free loan will accrue to the owner on the date the loan has been granted and paid by the person acquiring the life right.

Example 3 – Date of accrual of an interest-free loan*Facts:*

B retired on 30 March 2020 and entered into an agreement with a retirement village owner. Under the agreement, B will be entitled to occupy a particular unit in exchange for the grant of the use of an interest-free loan of R400 000. The agreement is concluded on 15 February 2020. B undertook to pay the R400 000 on receipt of his lump sum benefit from his pension fund. He paid over the R400 000 to the retirement village owner on 12 June 2020. The year of assessment of the owner ends on 31 December 2020.

Result:

The date of accrual for purposes of calculating the monetary value of the right to use the interest-free loan is 12 June 2020.

4. Period for which this ruling is valid

This ruling is effective from the commencement of years of assessment ending on or after 31 December 2008 and will apply for an indefinite period.

Senior Manager

Leveraged Legal Products

SOUTH AFRICAN REVENUE SERVICE

Date of 1st issue : 11 April 2011

Date of 2nd issue : 4 October 2012

Annexure

**THE EXPECTATION OF LIFE AND THE PRESENT VALUE OF R1 PER ANNUM FOR LIFE CAPITALISED
AT 12 PER CENT OVER THE EXPECTATION OF LIFE OF MALES AND FEMALES OF VARIOUS AGES**

Age	Expectation of life		Present value of R1 per annum for life		Age
	Male	Female	Male	Female	
0	64,74	72,36	8,32791	8,33105	0
1	65,37	72,74	8,32828	8,33114	1
2	64,50	71,87	8,32776	8,33091	2
3	63,57	70,93	8,32714	8,33064	3
4	62,63	69,97	8,32644	8,33033	4
5	61,69	69,02	8,32567	8,32999	5
6	60,74	68,06	8,32480	8,32961	6
7	59,78	67,09	8,32381	8,32918	7
8	58,81	66,11	8,32271	8,32869	8
9	57,83	65,14	8,32146	8,32815	9
10	56,85	64,15	8,32007	8,32753	10
11	55,86	63,16	8,31849	8,32684	11
12	54,87	62,18	8,31673	8,32608	12
13	53,90	61,19	8,31480	8,32522	13
14	52,93	60,21	8,31265	8,32427	14
15	51,98	59,23	8,31029	8,32320	15
16	51,04	58,26	8,30770	8,32203	16
17	50,12	57,29	8,30489	8,32071	17
18	49,21	56,33	8,30180	8,31926	18
19	48,31	55,37	8,29841	8,31764	19
20	47,42	54,41	8,29471	8,31584	20
21	46,53	53,45	8,29061	8,31383	21
22	45,65	52,50	8,28613	8,31161	22
23	44,77	51,54	8,28117	8,30912	23
24	43,88	50,58	8,27564	8,30633	24
25	43,00	49,63	8,26959	8,30326	25
26	42,10	48,67	8,26274	8,29981	26
27	41,20	47,71	8,25516	8,29595	27
28	40,30	46,76	8,24677	8,29171	28
29	39,39	45,81	8,23737	8,28697	29
30	38,48	44,86	8,22694	8,28170	30
31	37,57	43,91	8,21538	8,27583	31
32	36,66	42,96	8,20257	8,26930	32
33	35,75	42,02	8,18836	8,26210	33
34	34,84	41,07	8,17262	8,25400	34
35	33,94	40,13	8,15536	8,24509	35
36	33,05	39,19	8,13647	8,23517	36
37	32,16	38,26	8,11558	8,22426	37
38	31,28	37,32	8,09274	8,21199	38
39	30,41	36,40	8,06781	8,19866	39
40	29,54	35,48	8,04030	8,18386	40
41	28,69	34,57	8,01067	8,16762	41
42	27,85	33,67	7,97844	8,14983	42
43	27,02	32,77	7,94344	8,13012	43
44	26,20	31,89	7,90547	8,10881	44
45	25,38	31,01	7,86380	8,08527	45

Age	Expectation of life		Present value of R1 per annum for life		Age
	Male	Female	Male	Female	
46	24,58	30,14	7,81924	8,05956	46
47	23,79	29,27	7,77109	8,03119	47
48	23,00	28,41	7,71843	8,00026	48
49	22,23	27,55	7,66236	7,96617	49
50	21,47	26,71	7,60201	7,92950	50
51	20,72	25,88	7,53713	7,88967	51
52	19,98	25,06	7,46748	7,84646	52
53	19,26	24,25	7,39387	7,79965	53
54	18,56	23,44	7,31631	7,74834	54
55	17,86	22,65	7,23234	7,69355	55
56	17,18	21,86	7,14414	7,63363	56
57	16,52	21,08	7,05178	7,56896	57
58	15,86	20,31	6,95225	7,49927	58
59	15,23	19,54	6,85004	7,42321	59
60	14,61	18,78	6,74206	7,34135	60
61	14,01	18,04	6,63010	7,25457	61
62	13,42	17,30	6,51232	7,16020	62
63	12,86	16,58	6,39301	7,06046	63
64	12,31	15,88	6,26822	6,95537	64
65	11,77	15,18	6,13789	6,84161	65
66	11,26	14,51	6,00726	6,72393	66
67	10,76	13,85	5,87165	6,59893	67
68	10,28	13,20	5,73403	6,46635	68
69	9,81	12,57	5,59182	6,32818	69
70	9,37	11,96	5,45165	6,18466	70
71	8,94	11,37	5,30775	6,03607	71
72	8,54	10,80	5,16744	5,88278	72
73	8,15	10,24	5,02437	5,72222	73
74	7,77	9,70	4,87876	5,55743	74
75	7,41	9,18	4,73490	5,38893	75
76	7,07	8,68	4,59354	5,21727	76
77	6,73	8,21	4,44663	5,04679	77
78	6,41	7,75	4,30309	4,87092	78
79	6,10	7,31	4,15898	4,69389	79
80	5,82	6,89	4,02440	4,51647	80
81	5,55	6,50	3,89051	4,34399	81
82	5,31	6,13	3,76802	4,17315	82
83	5,09	5,78	3,65276	4,00482	83
84	4,89	5,45	3,54546	3,83988	84
85	4,72	5,14	3,45232	3,67921	85
86	4,57	4,85	3,36864	3,52371	86
87	4,45	4,58	3,30066	3,37426	87
88	4,36	4,33	3,24907	3,23175	88
89	4,32	4,11	3,22597	3,10296	89
90	4,30	3,92	3,21438	2,98912	90