Transfer pricing and insurance structures in the BEPS Era

Author: Roxanna Nyiri, Director, BDO Tax.

Insurance in todays world is no longer limited to a single country and has over the last few decades seen interesting global developments. Reinsurance and cell captive insurance have become an integral part of enterprise risk management. Reinsurance and cell captive insurance not only provide business with tools to *manage their risk*, *limit their cost of insurance*, but also to *hedge against currency fluctuations*. These developments, of course, also have their own unique tax consequences, especially where they span jurisdictional borders. With the advent of the Organisation of Economic Cooperation and Developments (OECDs) Base Erosion and Profit Shifting (BEPS) initiatives, tax authorities across the globe are scrutinising insurance structures from a tax perspective, especially with regard to transfer pricing. This increased scrutiny often leads to the cross border pricing related to intercompany insurance related transactions being challenged.

Although South Africa has a well-developed financial services and insurance industry, it lags behind in certain respects when compared to some more favourable tax jurisdictions such as Mauritius. South African businesses often make use of inter-jurisdictional risk management opportunities which include reinsurance and cell captive arrangements. Tax free or low tax jurisdictions such as the Isle of Man, Bermuda, or Mauritius are often part of these arrangements. Reinsurance companies in these jurisdictions often reinsure part of the South African reinsurers risk. These arrangements could expose the local reinsurer to transfer pricing risk, where it can be demonstrated that the local reinsurer premiums or commissions paid to its foreign counterpart are in excess of what they would have been if charged between unrelated parties. Alternatively, South African businesses may opt to self-insure through a cell captive which, in turn, may reinsure with a foreign cell captive. Again, a transfer pricing risk could exist.

Transfer pricing is primary guided or informed by the arms length principle, which is based on the arms length standard. The arms length standard is an internationally accepted concept which requires the price of an intercompany transaction to be consistent with the price that would have been charged between unrelated parties. The OECD released its final report on its BEPS action plans on 5 October 2015. The report of Action 8-10 *Aligning Transfer Pricing Outcomes with Value Creation* equally applies to the insurance industry. The six-step risk framework is summarised below.

No	Step	Description
1	*Economically significant risks*	*Identify economically significant risks with specificity*

2	*Contractual risk allocation*	*Determine how each economically significant risk is contractually assumed under the terms of the contract*
3	*Functional analysis*	*Perform functional analysis of each economically significant risk. Attend to (i) control and risk mitigating functions (ii) risk actually borne by each enterprise and (iii) financial capability of each enterprise to bear the risk*
4	*Consistency between functional conduct and contract terms*	*Decide whether the contractual assumption of risk identified in step 2 is consistent with entities conduct identified in step 3*
5	*Risk allocation*	*Reallocate risk based on conduct established in step 3 if required*
6	*Transfer pricing analysis*	*Conduct transfer pricing risk analysis based on allocated risk from Step 5*

This framework adds the further complexity of supporting the substance of the reinsurance or cell captive operation. This requires that the reinsurance or cell captive operation has sufficient people, resources, and management expertise on the ground to manage risks. The capital infrastructure and financial capacity to bear the risk must also be evident. This needs to be evidenced in the day-to-day operational activities of the reinsurer or cell captive. Since no two insurance contracts are identical, to demonstrate arms length intercompany contract pricing can be a challenge. The Comparable Uncontrolled Price Method (CUP) is commonly used and is based on contract comparisons. In terms of CUP it needs to be established whether a comparable transaction exists in the open market between independent parties. If not, it would need to be considered whether the local insurance entity insures risk of third party unrelated entities, which are comparable to the intercompany transaction (referred to as *internal CUP*). Using the local insurance entitys reinsurance pricing model may be appropriate to determine a comparable price (internal CUP). An actuarial approach can also be followed to calculate the net present value (NPV) of future profits pre- and post-reinsurance. The difference may be attributable to a theoretical commission. The actuarial model is based on a number of key inputs and assumptions including premium income, cost of claims, payment patterns of premiums and claims (legacy data), acquisition and other costs, returns on investments, capital considerations, and applicable discount rates.

As the onus is on the taxpayer to ensure correct transfer pricing, it must ensure that it builds up relevant supporting documentation and price determination models. Robust transfer pricing documentation and relevant economic analyses and modelling can prevent costly pricing adjustments and penalties.

ENDS

Kind regards,

Lee Moteetee

Senior Account Manager

Ogilvy Public Relations
The Brand Building | 15 Sloane Street Bryanston | Johannesburg
Private Bag X33 | Bryanston 2021
T +27 11 700 5408

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No tax relief in sight for home buyers

Author: Alistair Anderson (BDlive)

Given the state of the economy and the pressure on the fiscus in terms of tax revenue, there is unlikely to be any transfer duty tax relief in Wednesday’s budget for home buyers, especially at the upper end of the market.

“Last year saw a meaningful shift of the transfer duty tax burden from the lower to the upper and luxury end of the market, with buyers paying 11% per R1m where the purchase price for the property is above R2.25m. Surprisingly we saw very little impact, if any, on the market at the upper end as a result of the increase in transfer duties,” said Jawitz Properties CEO Herschel Jawitz on Friday.

Seeff Properties chairman Samuel Seeff said it was best for Treasury not to meddle with the transfer duty tax burden again.

“There is clear evidence that luxury buyers in top-end areas, such as Cape Town’s Atlantic Seaboard and City Bowl, as just one example, are staying put, opting to extend and renovate rather than sell,” he said.

“The legislated transaction costs are just too high. When you factor in the aspects that make up the costs of transacting – transfer costs, transfer duty and capital gains tax – sellers are in some instances having to fork out the equivalent of up to 20% of the value of the purchase price just in costs,” said Mr Seeff.

He said that on a R5m transaction, the additional transfer duty meant the buyer had to pay an extra R70,500, and on a

R10m transaction, an additional R220,500.

The Atlantic Seaboard and City Bowl generate about a third of the total annual sales turnover for the Cape metro. Last year’s sales, according to the Propstats estate agent database, amounted to nearly R7bn.

Almost 90% of this fell above the R2.25m price mark and, of that, about 40% was above the R10m mark.

“As you can see, it is quite a sizeable market which is already, before taking last year’s transfer duty hike into account, generating significant income for the fiscus,” Mr Seeff said.

Mr Jawitz said he was hoping there would rather be relief for entry-level home buyers.

“The other option would be for the threshold below which transfer duty is not payable to be increased in line with property price growth in 2015, which would mean an increase in the threshold from R750,000 to R800,000, as this threshold was increased by 25% from R600,000 to R750,000 last year,” said Mr Jawitz

Economist Colen Garrow said raising the lower threshold would encourage home ownership while the state struggled to deliver housing.

“Raising the transfer duty threshold may lose some money for the fiscus initially, but home ownership encourages economic activity elsewhere in the economy, (for example), in retail goods and services,” he said.

This article first appeared on bdlive.co.za.

Taxpayer's rights on SARS audits

The Tax Administration Act, Act 28 of 2011 (the TAA) came into effect on 1 October 2012. Its promulgation brought with it many changes to not only taxpayers' rights and obligations but the reciprocal rights and obligations on the part of the South African Revenue Service (SARS) in its continuous business of revenue collection. Some of the amendments and repeals of sections previously contained in the Income Tax Act No. 58 of 1962 (the Act) have seen a welcome improvement in taxpayers' rights. One of these improvements is contained in section 42 of the TAA.

Previously, the Act contained no obligation on SARS to keep the taxpayer informed during an audit, nor did it provide for a timeline on the time period SARS could take to complete an audit. The taxpayer could thus be left in limbo and be uncertain as to when an audit may be completed. This position was clearly not conducive to good commercial nor equitable practice and if the taxpayer were to enquire with SARS for the purpose of obtaining a status update on the audit or request that such an audit be completed within a reasonable time, SARS could merely state that it was under no statutory obligation to complete the audit within a certain timeframe and that complexities in conducting the audit required extensive use of resources.

Section 42 of the TAA, however, now provides that a SARS official involved in or responsible for an audit must, in the form and in the manner as may be prescribed by the Commissioner by public notice, provide the taxpayer with a report indicating the stage of the completion of the audit. SARS issued Public Notice No. 788 on 1 October 2012 in Government Gazette No. 35733 (the Public Notice) for this purpose.

In terms of the Public Notice, a taxpayer is entitled to a status update of the audit within 90 days after commencement of the audit and within 90 day intervals thereafter. The definition of ‘day’ is currently an anomaly in our law, but for the sake of this note it suffices to say that ‘days’ indicate calendar days. The Public Notice goes on to provide the manner and form which the report should take:

“The report must include the following details as at the date of the report:

- A description of the current scope of the audit;
- The stage of completion of the audit;
- Relevant material still outstanding from the taxpayer”

This must be seen as a welcome development in South Africa’s tax law as it attempts to provide the taxpayer with greater certainty and provides suggested timeframes of completion of an audit and hence allows a better opportunity to put into place contingency plans for any eventualities. It is furthermore, in line with many overseas jurisdictions. However, despite this welcome development there are questions regarding its effect and usefulness in enforcing taxpayers’ rights.

Despite this new obligation on SARS to keep the taxpayer informed throughout the course of an audit, it is unfortunate that where SARS fails to abide by its legal obligations there is no sanction against SARS nor remedy for the taxpayer. In effect SARS could continue to issue such reports indefinitely, alternatively, could merely fail to issue the report as it will have no adverse effect on its ability to collect revenue in the long term.

Rule 26(5) of the Rules prescribing the procedures to be observed in lodging objections and noting appeals against assessments (the Rules) provides that where a party fails to comply with any requirement contained in the Rules, the Court may, upon application on notice by the other party, order the defaulting party to comply with that requirement within such time as the court deems appropriate. Rule 26(6) goes on to state that where the defaulting party fails to comply with such a court order in terms of Rule 26(5), then the court may upon application on notice by either party make an order which in effect either confirms the assessment or allows the objection. This remedy therefore ensures finality and certainty and is open to utilisation by both SARS and the taxpayer. It is unfortunate that it only applies to objections and appeals and not to the situation before SARS issues an assessment.

The question therefore remains – what are the remedies available to a taxpayer where SARS does not issue the report nor finalises the audit and the timeframe involved is extensive having regard to reasonability?

One possible solution may be to approach the civil courts for the purpose of granting a *mandamus* (mandatory interdict) against the relevant SARS official to carry out his obligations in terms of section 42 of the Act. The courts, may, however, be hesitant to grant such an order as it may be difficult to prove the requirements for an interdict, which include, *inter alia*, that there is a well-grounded apprehension of irreparable harm or that an injury has actually been committed or is reasonably apprehended.

The initiation of an audit does not necessarily mean that SARS will issue additional assessments against the taxpayer, and thus it is most certainly difficult to prove irreparable harm. An exception to this is perhaps the situation where a taxpayer requires a Tax Clearance Certificate (TCC) from SARS for business and commercial purposes, but where SARS refuses to issue such a certificate as a result of the pending audit or an audit which has not been finalised. Notwithstanding the fact that in the aforementioned situation, the taxpayer may be able to prove irreparable harm, litigation in the High Court is time and cost intensive and it seems unnecessarily burdensome taking into account the purpose of such an application.

An alternative could be to approach the High Court to take SARS on review for its failure to comply with section 33 of The Constitution of the Republic of South Africa, 1996 (the Constitution), as well as the Promotion of Administrative Justice Act, Act 3 of 2000 (PAJA). Again, the high costs of litigation involved in this process far outweigh the possible remedy the court may order. Furthermore, such applications are not financially viable for the majority of taxpayers and it could be too often a case of the taxpayer having to succumb to SARS' authority.

Unfortunately, at this stage there does not appear to be any further alternative remedies for the taxpayer or sanctions against SARS for not abiding by its legal obligations in terms of the TAA. It is always valuable to compare our position with overseas jurisdictions. However, in this instance it seems that although many foreign jurisdictions recognise the need and importance of keeping the taxpayer informed, there are neither sanctions on the revenue authorities nor reciprocal remedies for the taxpayer.

In the Irish Tax and Customs Code of Practice for Revenue Audit it states that it is in the best interests of everybody that the audit is concluded as quickly as possible and also provides that where the taxpayer has complied with all requests for information timeously, then Irish Revenue must advise of the status of the audit after the expiry of three months, and in so far as possible the estimated timeframe of completion thereof. The Code does not, however, provide for a sanction where the Irish authorities fail to adhere to these obligations.

In the Australian Tax Office (ATO)'s guidelines on the conduct of complex audits, it sets out the auditor's obligations during the course of the audit, which includes, *inter alia*, to keep the taxpayer informed. Unfortunately there is no mention of a suitable remedy where the auditor abrogates from his obligations. The ATO, did however, recently introduce a system where it develops an ‘Aged Case Report’ showing all audits which have not been finalised within two years and the reasons behind the delays. This report is then forwarded to the ATO’s Deputy Commissioner: Large Business and International on a regular basis, for the purpose of determining any action required to speed up resolution of the audits.

It thus appears that, although the TAA went a long way to improving taxpayers’ rights and enhancing SARS administrative obligations, there are several issues which have arisen since its implementation. While it is accepted that the need for an efficiently functioning revenue authority is key for the success of the country’s economy and this goes hand in hand with the powers given to SARS in the new legislation, one must not lose sight of the fact that the sanctions imposed against the taxpayer for failing to comply with certain provisions are often harsh, whereas the reciprocal sanctions imposed on SARS are often not even catered for. Nevertheless, it is vitally important for all taxpayers to know their rights in these circumstances and to seek professional assistance where issues surrounding the interaction with SARS pertaining to requests for information, audits, objections and appeals arise.

Edward Nathan Sonnenbergs
TAA: Section 42
SARS Public Notice No. 788
SARS Rules for Objection and Appeal: Rules 26(5) and 26(6)
The Constitution of the Republic of South Africa: Section 33
PAJA

Conversion of a share block scheme into sectional title – exemption from transfer duty

With effect from 1 January 2013 transfer duty is no longer payable in respect of a transaction contemplated in item 8 of schedule 1 of the Share Blocks Control Act, No 59 of 1980, whereby a right to or interest in the use of immovable property conferred by virtue of the ownership of a share in a share block company is converted to ownership of the immovable property concerned.

The amendment of s9(19) of the Transfer Duty Act, No 40 of 1949 is contained in s1 of the Taxation Laws Amendment Act, No 22 of 2102.

The exemption from payment of transfer duty in such circumstances was previously restricted to a natural person and only applied if the initial acquisition of the share was subject to duty in terms of the Transfer Duty Act. The exemption now applies in respect of any such transaction concluded on or after 1 January 2013 irrespective of whether the holder of the share is a natural or juristic person, and whether or not the transaction relating to the initial acquisition of the share was subject to payment of transfer duty at that time.

The exemption is extended further to include the acquisition by any person of a part of the immovable property of the share block company where that person had a right of use of that part of the property that was conferred on him or her by reason of the ownership of a share held in the share block company.

Shuttleworth takes Reserve Bank to court

Pretoria – Billionaire IT entrepreneur and the first South African in space, Mark Shuttleworth, has turned to the Pretoria High Court in a bid to recover the 10 percent exit levy (more than R250 million) imposed on him by the South African Reserve Bank when he transferred more than R2 billion out of the country.
His legal team, headed by Gilbert Marcus SC, on Monday asked Judge Francis Legodi to set aside the decision by the Reserve Bank that he had to pay this amount – and he wants to be refunded.

Shuttleworth’s team said the levy was unconstitutional and invalid and the decision to impose it, unlawful.

Marcus said the levy decision was taken without affording Shuttleworth a fair hearing. In fact, the entire existing system of exchange control in South Africa was unconstitutional, he argued.

Shuttleworth was the founder of Thawte Consulting, which he sold in 1999 for $575m (R5.8bn).

He subsequently devoted his career to a range of entrepreneurial and philanthropic projects.

This required the investment of large amounts of capital across the world in high-risk entrepreneurial ventures.

Shuttleworth was forced to emigrate (to London) in 2001, because it was impossible to conduct these ventures within the existing exchange control in this country, the court was told.

Following his emigration, Shuttleworth left substantial assets in South Africa. Over the years he transferred some of them out of the country.

In 2009, he decided to transfer his remaining assets and was told by the Reserve Bank that he could only do that, provided he paid a 10 percent levy.

Although Shuttleworth questioned the validity of this decision, he paid it under protest and transferred his assets. Apart from wanting his money back, he is also asking for an order declaring the Reserve Bank's policy of refusing to deal directly with the public regarding its exchange control regulations, to be declared unconstitutional.

In terms of its rules, the Reserve Bank insists that the public communicate with it through the mediation of authorised dealer banks – a policy Shuttleworth referred to as "the closed door policy".

When Shuttleworth emigrated in February 2001, his assets – valued at an estimated R4.2bn – were blocked.

In March 2008, he was given permission to transfer R1.5bn of his blocked assets.

In 2009, he decided to transfer the remaining blocked assets, which was granted, subject to the payment of a 10 percent levy. He instructed Standard Bank to do so, although under protest.

Marcus said if Shuttleworth had waited a year, he would not have had to paid the levy as this requirement fell away in 2010.

The Reserve Bank defended its actions by stating the levy was in accordance with its policy, as set out in a circular, based on a 2003 budget speech by then finance minister Trevor Manuel to Parliament.

Marcus on Monday told Judge Legodi that a circular is not regarded as law.

He said the system of exchange control in this country was not governed by laws, but by the dictates of an organ of State, which are not accessible to the public.

Marcus said the Reserve Bank understood itself to be bound to implement the then policy of the finance minister. But, he argued, this was a revenue-raising mechanism in terms of which R2.9bn was, since the exit levy was introduced and up to its termination in 2010, transferred to the fiscus.

When the Reserve Bank imposed the 10 percent levy on the transfer of Shuttleworth’s capital, it deprived him of his property and his client was entitled to get his R250m back, he argued.

Arguments on behalf of the Reserve Bank and the government will be presented today.

Pretoria News

Year in Review – 2012 Tax Developments in South Africa

During 2012 a number of significant amendments were made to the tax legislation in South Africa. This report provides a brief description of certain of these amendments which may be of interest to foreign companies that conduct business in South Africa as well as those seeking investment opportunities in South Africa.

Withholding Tax on Interest

From 1 July 2013, a new withholding tax on interest will be imposed in South Africa. The tax is a final withholding tax in respect of any interest paid by a South African resident to any foreign person. The tax is levied on the foreign person that receives or accrues interest from a South African source; however the South African payor has an obligation to withhold the tax on payment of the interest. A foreign person is broadly defined as any person that is not a resident for South Africa tax purposes. The withholding tax on interest will be imposed at a rate of 15%. The legislation caters for certain exemptions that apply when interest is paid to a foreign person by certain entities, for example the Government of South Africa, the South African Reserve Bank, a headquarter company or in respect of any debt that is listed on a recognised exchange. Further if the foreign person is physically present in South Africa for a period exceeding 183 days in a 12 month period or has a permanent establishment in South Africa, that interest paid to the foreign person will not be subject to withholding tax. It is important to note that South Africa has a vast network of double taxation agreements that have been concluded with other jurisdictions. As such, should the interest paid to a foreign person not be exempt from the withholding tax, the withholding tax rate may be reduced in terms of the application of a double taxation agreement where applicable.

Deductibility of Interest Expenses

Generally the deduction of interest expenditure incurred in respect debt financed share acquisitions is not allowed under South African tax law. The rationale for the interest expenditure being non-deductible is that the acquisition of shares produces exempt income. As such the deduction of interest incurred to acquire shares is disallowed on the basis that the expense is not incurred in the production of income.

However as and from 1 January 2013 a special deduction of interest expenses will be allowed in respect of debt used by a company to acquire a controlling interest in an operating company. The deduction does not take into account the general rules in order to claim a deduction, for instance the expense does not have to be incurred in the production of income or while conducting a trade. However there are certain other requirements that must be complied with in order to secure the deduction of the interest expenses. A company must acquire the equity shares in an operating company utilising debt finance. An operating company is defined as any company that carries on business continuously and in the course of that business provides goods or services for a consideration. The acquiring company must acquire a controlling interest in the operating company, which requires a 70 per cent acquisition of equity shares in the operating company.

Value-for-Value Principle involving Share Issues

Generally a company that issues shares for the acquisition of assets is deemed to have acquired the assets at the lesser value of either the market value of that asset immediately after the acquisition or the market value of the shares immediately after the acquisition. The taxpayer who has disposed of the asset is deemed to have disposed of that asset for an amount equal to the market value of the shares immediately after the acquisition.

The revenue authorities have noted that certain asset-for-share transactions did not occur on a value-for-value basis, which led to schemes with uneven exchanges without triggering the appropriate tax. As such, a “value-for-value principle” was introduced. Any value mismatches involving shares from 1 January 2013 will explicitly give rise to tax in the hands of the party receiving a benefit. The new rules relating to the value-for-value principle do not require the parties to be connected persons.

In the case where the market value of the asset disposed of exceeds the market value of the shares issued, the issuing company will be subject to capital gains tax in respect of the difference of the value asset and shares issued. On the other hand if the market value of the issued shares by a company has a greater value than the asset received, the excess amount will be deemed to give rise to dividend *in specie*. The issuing company of the shares will be liable for the Dividends Tax in respect of the dividend *in specie*.

Debt Reductions or Cancellations

From 1 January 2013 new rules were implemented regarding the tax treatment relating to the reduction or cancellation of any debt owed by a taxpayer. The tax treatment will depend upon the underlying cause that resulted in the debt being reduced or cancelled. As such a uniform system has been introduced to regulate the tax treatment of debt that is reduced or cancelled for less than the full consideration.

Debt can be reduced for a variety of reasons. If debt is reduced or cancelled such reduction or cancellation should be viewed as an indirect form of cash payment under the current tax principles. As such new ordering rules have been proposed, whereby the debt reduction or cancellation can be treated as a donation which will be subject to Donations Tax, as part of a bequest from an estate which is subject to Estate Duty or treated as a disguised salary payment which is subject to Employees Tax. Should the debt reduction or cancellation not fall within any of the above categories then income tax or a capital gains tax will be triggered depending on how the borrowed funds were utilised.

If the debt was used to fund deductible expenditure or allowances, the debt reduction or discharge will be taken into account in terms of the ordinary revenue rules. Should the revenue rules not apply then as a residual category the capital gains tax rules come into play.

If the debt was used to fund the acquisition of a depreciable asset and the taxpayer claimed depreciation allowances in respect of that asset, then the acquisition cost of that asset must be reduced by the depreciation allowances previously claimed in terms of the capital gains tax rules resulting in the base cost of that asset. The base cost of the asset is then reduced by the debt amount that has been reduced or cancelled. Should the base cost be reduced to nil any remaining amount that exceeds the base cost will be treated as ordinary revenue.

If the debt was used to fund the acquisition of capital assets, ie immovable property, any debt reduction or cancellation must be used to reduce the base cost of that asset to nil. Should the debt reduction or cancellation exceed the base cost, the remaining amount does not trigger any capital gain for the taxpayer. If the capital asset is no longer held by the taxpayer at the time when the debt is reduced or cancelled then the assessed capital loss of the taxpayer is reduced.

Hybrid Equity and Third-Party Backed Share

Hybrid equity shares are usually preference shares whose dividend yield is secured by debt-based instruments, which differs from equity shares whose yield is linked to the profitability of a company. Current rules deem the dividend arising from a hybrid equity share to be income and is accordingly taxed at the appropriate income tax rate. A third-party backed share is any preference share in respect of which the dividend yield from that share is guaranteed by an unconnected third party. Again the dividend yield of the third-party backed share is deemed to be income and subject to income tax.

As an anti-avoidance measure the rules relating to hybrid equity shares have been broadened to include any share whose dividend yield is based on one or more debt-bearing financial instruments of a third-party. Previously the rules merely required that the share be redeemed within three years from the date of issue. In respect of a third-party backed share, the holder of that share is looking to a third-party to either acquire that share from the holder or make payment in respect of that share. The dividend yields from a hybrid equity share and a third-party backed share will continue to be deemed as income and taxed accordingly. However an exception was introduced in respect of both hybrid equity shares and third-party backed shares, in which any dividend yield derived from these shares is ultimately applied to directly or indirectly to acquire a pure equity stake in an active operating company that dividend yield will not be deemed to be income.

New rules relating to hybrid debt instruments were also introduced in the initial draft taxation laws amendment bill in 2012; however these rules were later withdrawn. It is anticipated that the rules regulating hybrid debt instruments will be revised and reintroduced in the 2013 taxation laws amendment bill.

Depreciation of Supporting Structures in Energy Projects

South Africa has adopted certain tax measures that support the generation of electricity from renewable resources. As such, the cost of the plant and machinery used in relation to the generation of wind power, solar energy, hydro power and biomass are depreciable over a three year period at a ratio of 50:30:20 per cent.

However no deduction exists in respect of the supporting structures to the plant or machinery in the generation of electricity from renewable resources. From 1 January 2013 the cost of the supporting structures associated with machinery and plant that are used in the generation of electricity from renewable resources will be depreciable over a three year period at a 50:30:20 per cent. In order for these supporting structures to qualify for the deduction, certain requirements must be met. The plant or machinery must be owned by the taxpayer or acquired by the taxpayer in terms of an instalment credit agreement and the supporting structure must be brought into use for the first time by the taxpayer for the purpose of that trade. The supporting structure must be mounted or affixed to the plant or machinery and must be regarded as integrated to such a plant or machinery. The purpose of this amendment is to encourage investment in renewable energy projects.

Madonsela successfully challenges SARS

Public Protector Thuli Madonsela has successfully challenged the SA Revenue Service's (Sars) taxation of compensation paid to the estate of a deceased civil servant, her office said on Wednesday.

"In a landmark case… the collector of revenue agreed to refund the estate of the said official an amount of R110,903," the Protector's office said in a statement.

"The amount had been deducted, as income tax, from the department of correctional services' settlement offer of

R484,697, which was paid to the official’s estate.”

Madonsela found in 2011 that the process followed by the department in terminating the man’s services constituted maladministration.

“At the time, Minister [Nosiviwe] Mapisa-Nqakula accepted the remedial action, with her department agreeing to implement it fully,” Madonsela’s office said.

“Unfortunately, the official died before the remedial action could be implemented, prompting the department to pay the compensation to his estate.

“However, what then came into question was whether the settlement offer by the department constituted income in the hands of the taxpayer or his estate, and whether the benefits were therefore taxable in terms of the Income Tax Act,” it said.

Sars later agreed that the compensation could not be taxable.

Taxman tightens noose in cash hunt

Last year, SARS collected R12-billion less than its initial target.
New regulations to gather more “intelligence” from third parties are set to pull the noose tighter around tax-evaders and those who simply keep sloppy records.

People and companies with whom you do business, such as your lawyer, estate agent and medical fund, now have a duty to automatically submit information about you to SARS.

These powers were gazetted last month and follow provisions in last year’s Tax Administration Act that allow certain high-ranking SARS officials to authorise searching without a warrant.

“Ask anyone in the industry and they will tell you SARS is much more aggressive,” said Ettiene Retief, chairman of the national tax committee at the South African Institute of Professional Accountants.

“One of the biggest changes in the new Tax Administration Act is the broadening of the scope of the information that SARS can request,” he said.

This would include rental and investment income, interest payments, royalties, the proceeds of the sale of financial instruments, retirement income contributions, life insurance payouts and medical aid contributions.

Though these have to be filled in on an individual tax return, it was not easy to verify whether the taxpayer entered the correct numbers.

Where SARS had to request specific information relating to a particular taxpayer before, Retief said: “Now they can use ‘general specificity’ to request more general information; for example, a bank might be requested to submit a list of all SA residents with a balance in excess of a certain amount.”

SARS spokesman Adrian Lackay yesterday confirmed this.

“SARS can request any information from a bank account of a taxpayer as part of its third-party data verification,” he said.

He played down suggestions that it was aggressive and that changes to legislation and regulations were severe, calling it “evolutionary, rather than revolutionary”.

But SARS was “more focused”, said SA Institute of Tax

Practitioners CEO Stiaan Klue.

The taxman wa s increasingly using intelligence it had gathered through more than half a decade of eFiling to aggressively patch the holes in the tax net, said Klue.

Not only that, it also used a more direct approach and was going “for low-hanging fruit”, said Klue.

SARS and the National Treasury last week also showed their intention to spoil the multinationals’ party with proposed limits on tax deductions for interest.

“The reality is that the fiscus is under pressure to collect money,” said Retief.

The billions SARS collected below its initial target last year left South Africa with a budget deficit of 5.1%, according to the preliminary outcome for revenue collection released by SARS last month.

Finance Minister Pravin Gordhan said last month he anticipated the consolidated deficit to come in below 5%, piling on the pressure to get more money in.

SARS—Transfer Duty Guide

Today, Sars issued a new guide for transfer duty, it replaces the previous issue, Transfer Duty Handbook that was issued in March

The new guide contains a discussion of the application of the Transfer Duty Act 40 of 1949, in respect of transactions involving immovable property such as land, buildings and other real rights in connection with immovable property situated in

South Africa. Although fairly comprehensive, the guide does not deal with an analysis of all the legal detail which may sometimes be necessary when dealing with immovable property transactions. However, it has been necessary to include a certain amount of technical and legal terminology in explaining certain concepts which underpin the transfer duty legislation.

Transfer duty (originally referred to as the “40th penny” – because of a 2.5% tax rate at the time) was introduced in Holland in 1598. It was also introduced in the former Dutch colonies of Batavia (in 1623), Surinam (in 1684), Cape of Good Hope (in 1686) and Curaçau (in 1741). Transfer duty is one of the oldest taxes still levied in present-day South Africa and was modelled on the Dutch and Batavian examples.

Most of the SADC countries levy some form of property transfer tax on the acquisition of immovable property (also referred to as fixed property).

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SARS and your bank account

On 29 February 2012, the South African Revenue Service (SARS) issued a notice in Government Gazette No 35090 (Notice No 173) relating to the liability of certain institutions, most notably banks, to furnish SARS with financial information about taxpayers.

The notice was issued in terms of s69 of the Income Tax Act, No 58 of 1962, which section has been superseded by s26 of the Tax Administration Act, No 28 of 2011 (TAA).

In terms of the notice, banks are obliged to furnish financial information to SARS relating to the period 1 March 2012 to 28 February 2013, being the 2013 tax year for taxpayers who are natural persons.

Since natural person taxpayers are currently submitting their returns for the 2013 tax year, it means that SARS will, for the first time, have such financial information available for purposes of verifying information submitted in returns, or for other auditing purposes.

The specific information that banks will by now have had to report to SARS in terms of the notice, for both natural and juristic person
taxpayers, includes:

• Names, Surname, date of birth/Registered name if juristic person

• Address, identity number/registration number if juristic person, tax number

• Bank account number and dates account was opened/closed

• Closing balance of account at end of period

• Interest accrued

• Monthly totals of all credits and debits to the account

• FICA status of the taxpayer.

The said information has to be reported to SARS in electronic format.

Assuming that all banks have complied with the notice, SARS will by now have an enormous electronic database of financial information about taxpayers in respect of the 2013 tax year.

Perhaps one of the most striking pieces of information that banks have to report to SARS, is the monthly credit and debit totals on taxpayers' bank accounts (one step short of handing over a detailed statement).

It is however not entirely certain how SARS will be able to use all this information in a meaningful manner. At first glance one might assume that SARS will compare the aggregate credit totals of a taxpayer's bank accounts for a relevant period, with the income that the taxpayer has declared in his/her/its return, and that if there is a mismatch, the taxpayer will be seen as having under-declared his/her/its income.

However, on further consideration, it is quite evident that the aggregate credit totals of a taxpayer's bank accounts for a period will not necessarily equate to that taxpayer's gross income for the period, as defined in section 1 of the Income Tax Act No 58 of 1962.

Amounts reflected in credit totals could for instance be capital in nature, double counted, or held in trust for another. For example:

• Where a taxpayer has multiple accounts, receives money in one account (salary) and transfers an amount to another account (savings account), the same amount will be reflected in the credit totals of both accounts, and sufficient information will not be available in SARS's database to match the corresponding debit amount (only totals are reported).

• Where a taxpayer sells a capital asset (car or other business assets – assuming no recoupment) the amount reflected in the credit total will actually be capital in nature.

• Where a taxpayer receives money from a spouse to settle household expenses, the amount reflected in the taxpayer's credit total will arguably be an amount to be disbursed on behalf of another (the spouse).

• Even where a taxpayer receives a refund from SARS, the amount will arguably be capital in nature, and the credit total will be inaccurate for purposes of determining gross income.

For purposes of the 2014 tax year, a similar notice was published in terms of section 26 of the TAA (Government Gazette No 36346, Notice No 260, 5 April 2013). This notice requires banks to submit similar information in accordance with SARS’s IT3 data submission specification.

In addition to the above, s179 of the TAA gives SARS sweeping powers to instruct a taxpayer’s bank to transfer funds from that taxpayer’s account to SARS in circumstances where there is an alleged tax debt owed to SARS (whether disputed or not).

A taxpayer, whether a salaried natural person or a large corporate conducting business, may very well find itself with an empty bank account on any given day.

In light of the above, it will not be surprising to find that some taxpayers may be tempted to revert to a system of keeping their cash under the mattress, as opposed to handing it over to their banker.