

Interpreting court judgments

✘ The South Gauteng Tax Court has had to make a determination of the effect of a direction given in a judgment handed down by the Supreme Court of Appeal in referring an assessment back to the Commissioner for the South African Revenue Service (SARS) for correction.

The matter that was heard by the SCA (*C:SARS v South African Custodial Services (Pty) Ltd* [2012]74 SATC 61) had principally been concerned with whether improvements made to State property in terms of a public-private partnership constituted trading stock of the taxpayer. The costs incurred by the taxpayer had been claimed as a deduction on the basis that they were part of the cost of construction. Included in these costs were costs in respect of certain financial arrangements. In particular, the following were disputed by SARS: introduction fee, guarantee fees, consultation fees, financial advisory fee, margin fee and bid guarantee fee.

The various fees that were contested were listed in paragraphs [14] to [17] of the judgment, and comprised guarantee fees (paragraph [14]), introduction fee (paragraph [15]), financial advisory fee (paragraph [16]) and margin fee (paragraph [16]) – all of which were specifically quantified. Certain unquantified amounts were also referred to in paragraph [17] as follows:

“In addition, [the taxpayer] was obliged to pay a commitment fee and an initial fee to BoE Merchant Bank and First Rand Bank, administration fees to First Rand Bank and legal fees to its attorneys, Deneys Reitz. It also incurred interest on the loan facilities.”

In paragraph [47] of the judgment, the Court pointed out:

“In order to bid for the tender and to raise the loans that it required to finance the construction of the prison, SACS

incurred a number of fees payable to various parties. The individual fees, their purpose and the parties to whom they were paid have been set out above. [The taxpayer] also incurred interest on its loans. It claims to be entitled to a deduction in respect of the various fees and the interest in terms of section 11(bA) of the Act."

Thereafter, at paragraphs [49] to [50], the Court concluded:

"[49] The interest that [the taxpayer] has incurred is, in my view, deductible in terms of section 11 (bA): it has been 'actually incurred' by [the taxpayer] on its loans from BoE Merchant Bank and First Rand Bank to pay CGM for the construction of the prison. I am also of the view that the various fees are deductible in terms of section 11(bA): because of their close connection to the obtaining of the loans and the furtherance of [the taxpayer's] project, they qualify as 'related finance charges' for purposes of the section.

[50] Consequently, [the taxpayer] succeeds on this aspect. I consider it necessary, however, to refer the matter back to the Commissioner for a decision to be taken as to the precise quantum of the deduction in the light of the principle set out in Caltex Oil (SA) Ltd v Secretary for Inland Revenue [1975](1) SA 665 that the interest and fees had to have been actually incurred during the year of assessment in which the deduction was sought."

Taken at face value, the Court held that the various fees are deductible. It referred the matter back to the Commissioner to determine the amount of the interest and fees actually incurred in the year of assessment. The Commissioner was therefore limited to determining the amount of a deductible expense and not the principle whether the expense was deductible – deductibility had been determined by the Court.

SARS assessed the taxpayer on the basis that they should treat

as deductible only those amounts that the SCA had specifically noted in the judgment. On this basis they determined that an amount of R64 346 528, representing various amounts that had not been specifically referred to in the SCA judgment, was disallowable, apparently on the basis that the amounts were not incurred in the production of the income or were of a capital nature. These were labelled "other costs" and included bid expenses, developers' costs, legal fees, insurance, specialist advice fees and lenders' specialist advice fees.

The taxpayer contested this finding. The matter came before the Tax Court (*Case No. 13356*, judgment given 2 December 2013). The taxpayer's position was the following: the total costs it had incurred amounted to R464 376 824. The SCA had disallowed the deduction of R324 379 692 in relation to the construction and provisioning of the project. In its grounds of appeal, it had contended that, to the extent that the costs were not related to trading stock, all the costs incurred were deductible under either section 11(a) or 11(bA) of the Income Tax Act, No. 58 of 1962 (the Act). SARS had taken issue with the deductibility of the costs referred to specifically in the judgment, but the SCA had found these to be deductible, subject only to verification of the *quantum*. The SCA had not denied the appeal in relation to the remainder of the costs, and in any event they fell within the ambit of section 11(bA) of the Act, being closely related to the loan financing.

The Tax Court agreed with the taxpayer's contention. In so doing it stated the basis upon which a judgment should be interpreted.

Judgments must be interpreted in the same manner as any document (such as a contract or a statute) should be interpreted. The Court cited the statement of Wallis JA in *Natal Joint Municipal Pension Fund v Endumeni Municipality* [2012] (4) SA 593 (SCA) at paragraph [18], that:

"...consideration must be given to the language used in the

light of the ordinary rules of grammar and syntax; the context in which the provision appears; the apparent purpose to which it is directed and the material known to those responsible for its production. Where more than one meaning is possible each possibility must be weighed in the light of all these factors. The process is objective not subjective. A sensible meaning is to be preferred to one that leads to insensible or un-business like results or undermines the apparent purpose of the document. Judges must be alert to, and guard against, the temptation to substitute what they regard as reasonable, sensible or business like for the words actually used. To do so in regard to a statute or statutory instrument is to cross the divide between interpretation and legislation. In a contractual context it is to make a contract for the parties other than the one they in fact made. The inevitable point of departure is the language of the provision itself read in context and having regard to the purpose of the provision and the background to the preparation and production of the document.”

It was also clear that the Court could consider extrinsic evidence, such as the evidence before the court that made the judgment and the arguments made in the court.

The dispute centred around whether costs had been adjudicated generally in the course of the judgment given, or whether the deductibility of costs was confined to those specifically mentioned in paragraphs [14] to [17] of the SCA judgment.

The Tax Court came to the conclusion that the narrow interpretation urged by SARS was not tenable. In paragraphs [37] to [38] of his judgment, Victor J found:

“[37] To sum up, the Commissioner only emphasised the guarantee fee, introduction fee and other finance charges as a section 11(bA) issue. Ultimately the SCA provided for a wider range of fees as being deductible in terms of section 11(bA).

[38] It is correct that nowhere in the judgment is reference made to "further costs". The judgment goes much wider than guarantee fee, introduction fee and other finance charges. It refers to a range of other fees which were not highlighted in the disallowance document and the grounds of appeal document. The SCA, with respect, must have had in mind a broader approach to the proper application of section 11(bA)."

The guiding principle is crystallised in the following conclusion (at paragraphs [41] to [42]):

"[41] Principles emanating from judgments are meant to be applied to different facts; otherwise the law would be a static process. A sensible objective observer looking at the judgment in its entire context would note the import of the principles of allowing the deduction of a wide variety of fees and the like. The category 'further costs' is but a descriptive outline or a convenient label ... on the whole the items listed in 'further costs' are a 'close connection' to the furtherance of the project.

[42] Once that is so, in the absence of an express reference to disallowing 'further costs', I conclude that the judgment must be interpreted to include further costs."

One suspects that we have not heard the end of the dispute between this taxpayer and SARS, and we are faced with the mouth-watering prospect that the matter will again come before the SCA which will then have to interpret its own judgment.

(Refer to articles 2155 and 2269)

PwC

ITA: Sections 11(a) and 11(bA)

(Editorial comment: Section 11(bA) was deleted from the Income Tax Act with effect 1 January 2012. Refer to items 2155 and 2269).