TAX ADMINISTRATION ACT ONE YEAR AFTER IMPLEMENTATION

VAT AND THE PRINCIPLES OF AGENCY

SARS’ NEW SINGLE REGISTRATION SYSTEM WHAT YOU NEED TO KNOW

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Famous tax dodgers
Recently many tax practitioners were unable to file IR12 and IT14 electronically on behalf of their clients. Essentially, SARS prohibited tax practitioners from rendering tax services to clients/taxpayers. This practice must be viewed as an attempt by SARS to prohibit illegal tax practitioners from continuing to ply their trade, implying that it is only tax practitioners affiliated with a professional body and registered with SARS who are eligible to perform the function of a tax practitioner.

Once a tax practitioner has registered with SARS and informed SARS of their preferred professional body, such as SAIPA-CoTE, then it is the responsibility of the professional bodies, such as SAIPA-CoTE, to confirm that the Tax practitioner is a member of SAIPA-CoTE. Essentially, the current downloading/uploading of members’ details is an electronic means of confirming membership with SAIPA-CoTE. Verification of membership to a professional body is a two-legged process. Firstly, a member has to inform SARS which professional body he/she is a member of, and secondly, SAIPA-CoTE has to confirm that the Tax practitioner is a member. The latter may only be done electronically on a platform, provided by SARS, for professional bodies to download members’ details.

The downloading/uploading of members’ information on the SARS platform is not the end of the process. The downloaded information by SAIPA must correspond exactly with the members’ detail already supplied by the tax practitioner to SARS when registering as a tax practitioner. If the membership information corresponds with SARS’ database and the information confirmed by SAIPA, then SARS database will recognise and register the Tax practitioner.

The following are the reasons why the information downloaded by SAIPA may not correspond to the information already on the SARS database:

- Some tax practitioners had their ID numbers changed a few years ago but did not inform SARS and/or SAIPA-CoTE of changed ID numbers. Hence SAIPA will have an ID number different from SARS for the same Tax practitioner.
- Many female tax practitioners have had their surname changed as a result of a change of marital status but simply forgot to inform either SARS or SAIPA-CoTE of the changed surnames. Once again, the same tax practitioner will have a different surname between SARS and SAIPA.
- Some tax practitioners (natural persons) have registered their businesses as tax practitioners and expect to use the tax practitioners’ numbers allocated to their business for their individual tax practitioners status.

Therefore, the tax unit of SAIPA-CoTE makes a strong appeal to members to double-check whether the information supplied to SARS corresponds with the information supplied to SAIPA-CoTE.

If a member has not been downloaded as yet on the SARS platform and is still unable to file tax returns on behalf of clients, then such members should send an email to either of the following SAIPA staff members, requesting the Manual Upload form.

- Aysha Naino: anaino@saipa.co.za, or
- Chantal Klaasen: temp@saipa.co.za

SAIPA-CoTE is doing everything within their control to upload all SAIPA registered tax practitioners with SARS and will continue to do so until all our members are successfully uploaded and able to operate their businesses.

We thank you for your patience and wish you well during this filing season.

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Since the Tax Administration Act was implemented a year ago, SAIPA has been working hard to register and verify members under its tax designation.

“There has been a 207% growth in member registration since the law kicked in,” says Mahomed Kamdar, Tax Advisor at the Centre of Tax Excellence (CoTE), the tax division of SAIPA.

“Also, there has been a 1340% increase in member verifications via the SAIPA website since 1 July 2013, which means that business owners are taking it seriously that their accountants must be registered with a controlling professional body that is recognised by SARS.”

Tax professionals play a critical role in the lives of both individual and company taxpayers, enabling them to successfully apply the tax legislations. But are all tax professionals equally qualified to fulfil this important role? Not so, says Kamdar. “The only way to ensure that you’re receiving the best, most reliable advice is to check that your tax professional is registered with a recognised professional body like SAIPA.”

Individual tax season started 1 July
One of the benefits of engaging the services of a registered tax advisor, especially as the individual tax season began on 1 July, is that such a tax professional knows about key changes in the law that are likely to have an impact on a client’s affairs.
Government backs retirement saving

One such development is the new law concerning the contribution to retirement funds. “Not everyone knows about this, but government will soon be offering a very generous benefit to individual taxpayers rapidly approaching retirement by covering the bulk of the costs of saving for their retirement,” says Kamdar. “Government is showing a commitment to its expectation that people should fund their own income in retirement. We must pay serious attention to this.”

Under the law, which kicks in on 1 March 2015, individual taxpayers will be able to recoup as a rebate up to 27% of what they earn if they pay this amount into any retirement savings vehicle, whether it is a provident fund, pension scheme or retirement annuity. “That means you could receive up to R350 000 per year back as a rebate if you save the maximum amount as prescribed by the law,” he says.

Although the benefits will only be realised from March 2016, as a tax professional himself, Kamdar says it is worth upping one’s retirement savings now. “It’s a fact that most people aren’t saving as much as they ought to in order to prepare for their rapidly approaching retirement,” he says. “So, having consulted with your tax professional, you should exhaust the current limits now, while awaiting the greater benefit in 2015.”

Draft legislation

“Talk to your tax professional and you’ll find that there is some concern over the newly released draft Taxation Laws Amendment bill, which is expected to be passed into law by November this year.”

According to Kamdar, there is a chance that the individual tax liability will increase as government is planning to tax employers’ contributions to a Defined Benefit Fund. In terms of a Defined Benefit Fund, the notional employer contribution is made in order to ensure that the retiree receives the contribution that was promised. “Now, Treasury is thinking about making this contribution taxable in the hands of the employee, which clearly has enormous implications for an individual’s tax liability,” says Kamdar. “It is not yet clear how the formula will evolve, but SAIPA is currently scrutinising the draft law in order to give input into its formulation, for the benefit of individual taxpayers in South Africa.”

Increased tax burden?

“It is understandable that taxpayers begin to fear an increased tax burden when the South African Revenue Service (SARS) makes statements predicting a 10% annual increase in total tax revenue over the next three years to around R1.3 trillion by the end of March 2017,” says Kamdar.

“However, people are misunderstanding the fact that this also implies that they will be earning more over time, particularly as government’s investments in building schools, hospitals and roads translate into increased opportunities for people to earn more money,” he says. Although the tax community has consistently predicted an increase in the tax rate over the past few years, this has not materialised. “Instead, I believe that SARS is following the approach of benignly encouraging all taxpayers to disclose all of their income.”

“Better disclosure of taxable income is becoming a reality as the law enforces tax professionals to declare their clients’ entire income or they risk losing their professional status.”

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“Better disclosure of taxable income is becoming a reality as the law forces tax professionals to declare their clients’ entire income or they risk losing their professional status,” says Kamdar. In addition, there are moves to unearth the underground economy and bring more of South Africa’s taxable earnings into the tax net. “It is becoming more difficult for taxpayers to hide their income, even abroad, for example, as tax authorities are now communicating much more than they used to.”

There are also provisions in the Tax Administration Act that compel third parties who hold income on behalf of taxpayers – such as lawyers collecting rental monies on behalf of clients – to disclose that income. Moreover, SARS is applying entire ‘machinery’ and innovative ideas to catch tax dodgers – even, for example, noting the number plates on luxury cars in order to check on the owner’s tax situation.

“SARS is not playing games,” concludes Kamdar, “And we would encourage taxpayers not to play games with them either. The time to engage the services of an experienced professional tax advisor is now.”
SARS’ NEW SINGLE REGISTRATION SYSTEM

Staff writer

As from May this year, SARS introduced changes to the registration processes for both individuals and companies and also across various tax types. The initial phase of changes implemented has been focused primarily on Income Tax (IT), Value-added Tax (VAT), Pay-As-You-Earn (PAYE), and to a limited degree, Customs and Excise.

Once the new system has been rolled out, all taxpayers, traders and tax practitioners will have a single interface with SARS for all of their registration, licensing and/or amendment needs. As a tax practitioner, this change will ultimately make the task of managing your client’s tax affairs much easier, as all your tax and customs products will be linked to your unique profile with SARS.

What is Single Registration?
The way in which taxpayers register for tax and customs and update their existing details has changed. SARS has now implemented a ‘Single Registration’ of taxpayers that applies across all taxes they pay and legal entities they are associated with. A taxpayer will only have to register once as a new taxpayer and thereafter only add or update their relevant details pertaining to the tax they are liable for. The new system also makes it easier for taxpayers to update their existing details.
The Single Registration process is being phased in, starting with:

- Single registration of taxpayers
- A simplified process to apply for: Corporate Income Tax (CIT), Income Tax (including Provisional Tax), Pay-As-You-Earn (PAYE), Value-Added Tax (VAT) and Customs and Excise

Why the change?
The cost of doing business in South Africa, especially for small entities, is very high. The Single Registration system will essentially remove the need for business to register for different tax types in separate application processes. When registering for the first time, businesses need to indicate which taxes they wish to register for. The details can be easily amended and updated at a later stage. The revised registration process will be far more cost-effective and save the taxpayer from having to go to a SARS branch numerous times with the required paperwork and documentation.

Another reason for the change in the taxpayer registration process is that SARS is increasing security around taxpayer identity. This forms part of government’s initiative to reduce red tape and cybercrimes such as identity theft. Changes are being implemented in co-operation with the Companies and Intellectual Property Commission (CIPC) and the Department of Home Affairs.

Third party data, information from the Department of Home Affairs and the CIPC will be used to verify registration particulars. For existing taxpayers and traders, SARS uses its current data that has passed through verification checks, and only in cases where there are discrepancies will clients be contacted to verify the information.

Registered representative
The registered representative of an entity has been identified as an area of risk for irregularities and fraud. One of the changes to be implemented is that this representative can no longer be a tax practitioner, and must be the public officer of the entity, who has been validated by SARS.

A public officer is the representative taxpayer for an entity and therefore serves as the face of the company for tax purposes. All actions carried out in their capacity as a public officer are deemed to have been undertaken by the entity. The public officer can allocate rights to additional people, such as tax practitioners acting on behalf of the entity. SARS’s new system requires that an authorised public officer must authenticate with SARS that a registered tax practitioner is mandated to act on behalf of the entity.

Benefits of Single Registration
The benefits of the new system, which according to SARS will be realised in the first phase, include a faster turnaround time for first-time registration applications, the introduction of additional registration channels, and simpler processes for official taxpayer representatives. For the first time, taxpayers or legal entities, such as Companies and Trusts, will be linked to their registered representative on the SARS system.

Taxpayers/registered representatives will now be able to:
- View all tax types registered for in a central place
- Manage all personal information centrally, either online or at a SARS branch
- Register for additional taxes (CIT, PAYE, VAT excluding Customs and Excise) online, provided the taxpayer is already registered with SARS for at least one tax

“The Single Registration solution provides a platform for improving various other functions and services in addition to automated tax registrations, including: the ability to obtain a Tax Clearance Status automatically based on the compliance of an entity across all tax types and the ability to perform account transactions across tax types (such as payment allocations),” said Marika Muller, Deputy Spokesperson at SARS.

How does it work?
The steps for first-time taxpayers (not already registered with SARS) are as follows:
- Go to nearest SARS branch
- Complete the applicable tax registration form
- Submit the required supporting documents

Provided there are no complications, the taxpayer will be registered and a profile created in real-time. The taxpayer will then receive an email notification confirming their tax-type registration.
The single registration system will enable registered taxpayers to log in to eFiling (if already a registered eFiler) and complete the Registration, Amendment and Verification form (RAV01) where all registered details excluding Name and ID/Registered name, company registration number and the nature of entity can be updated. If any details have changed, the taxpayer will need to go to their nearest SARS branch. The relevant supporting documents will be required to verify any new details, as a ‘physical authentication and visual inspection’ of documents by SARS is now compulsory.

**Challenges in the ‘first phase’**

Since the introduction of the new system, there have been some glitches experienced, particularly with existing registered tax practitioners. Some tax practitioners have not been recognised as practitioners of their existing clients on the eFiling system. Other tax practitioners have not been able to validate the public officers of the companies that they represent and maintain the details of the legal entity. Some tax practitioners have not been able to make changes to sensitive client information at SARS branch offices.

According to Muller, the most significant issue affecting tax practitioners is the need to resolve data conflicts and inaccuracies, which may result in visits to a SARS branch to rectify sensitive information that cannot be changed via eFiling.

In an effort to regulate tax practitioners, the Tax Administration Act introduced provisions stating that tax practitioners have to be registered with SARS and with one of the accredited regulatory bodies, such as SAIPA, verifying that they are registered with them and in good standing.

The process of getting all these names registered with SARS has not gone as smoothly as expected. “We did not anticipate the level of reaction to the new system and we dealt with it,” said Barry Hore, Chief Operating Officer of SARS. Manual processes to validate tax practitioners have also been put in place at SARS branch offices.

“It is the biggest change we have ever made — it is not simply about how you register an entity, but it covers every interaction with SARS that has to be checked. There are over 300 interfaces within SARS that had to be changed,” said Hore.

Keith Pietersen, Tax Manager at the Technical and Standards Department of SAIPA recommends that tax practitioners take the time to read and understand the guidelines provided by SARS on the new process. “[Some of] our members are confused because they did not take the time to read the guides SARS provided us. The guides are lengthy and members just do not have the time to go through all of the details. We have asked SARS to make a shorter guide available which will be much more simpler for members to use,” said Pietersen.

According to Pietersen, CoTE members that provided most of their information to SAIPA, such as tax clearances, income tax numbers and tax practitioner numbers, did not have difficulties and actually had pleasant experiences during the registration process.

**SAIPA’s involvement**

As a regulatory body, SAIPA needs to ensure that members are compliant in all aspects in order to portray their capability of managing the compliance and disciplines of their members.

“SARS will in all probability check whether the SAIPA members are up to date with CPD (continued professional development), legally compliant (tax clearances) and for the body, that the member has paid their fees to date,” said Pietersen.

**What to expect in the ‘second phase’**

“The implementation of the Single Registration solution is a journey rather than a single execution of a new system,” said Muller. “The initial solution laid the foundation for further enhancements to be performed, such as the ‘preparer’ functionality that was recently introduced for ITR12 submissions. Further enhancements during the course of the next year will include the implementation of the ‘merging’ function on eFiling, enhancements to the eFiling user registration, and the inclusion of additional tax types in the Single View.”

Many of the initial requirements imposed by the Single Registration process, such as rectifying any missing mandatory registration information and merging of taxes into a single entity, are once-off activities. SARS encourages all tax practitioners to address these as soon as possible.

SAIPA is appealing to all members to finalise their tax registrations as soon as possible. Members are also encouraged not to wait for the last days of the eFiling season to inform SAIPA of any difficulties experienced with the system, due to the member’s details not being activated by SAIPA-CoTE, the result of which will be a huge bottleneck at the tax department.
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From time to time the SAIPA-CoTE tax helpdesk receives questions on Personal Service Providers (PSPs). What are the tax implications of Personal Service Providers? The frequency of these questions makes it necessary to address in this edition, for quick reference purposes for members who may experience similar difficulties with a personal service provider in the future.

**Definition of PSP**

Paragraph 1 of the Fourth Schedule of the Income Tax Act, as amended, defines a personal service provider (PSP) as follows:

**Personal service provider** means any company or trust, where any service rendered on behalf of such company or trust to a client of such company or trust is rendered personally by any person who is a connected person in relation to such company or trust, and

- Such person would be regarded as an employee of such client if such service was rendered by such person directly to such client, other than on behalf of such company or trust; or
- Where those duties must be performed mainly at the premises of the client, such person or such company or trust is subject to the control or supervision of such client as to the manner in which the duties are performed or are to be performed in rendering such service; or
- Where more than 80% of the income of such company or trust during the year of assessment, from services rendered, consists of or is likely to consist of amounts received directly or indirectly from any one client of
such company or trust, or any associated institution as defined in the Seventh Schedule to this Act, in relation to such client,

Except where such company or trust throughout the year of assessment employs three or more full-time employees who are on a full-time basis engaged in the business of such company or trust of rendering any such service, other than any employee who is a holder of a share in the company or member of the trust or is a connected person in relation to such person;

The aforementioned paragraph of the Fourth Schedule requires further clarification. A personal service provider, in other words, is defined as any company or trust where any service rendered on behalf of such company or trust to a client is rendered personally by a ‘connected person’ in relation to such a company or trust.

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The aforementioned paragraph of the Fourth Schedule requires further clarification. A personal service provider, in other words, is defined as any company or trust where any service rendered on behalf of such company or trust to a client is rendered personally by a ‘connected person’ in relation to such a company or trust. This definition is restrictive in the sense that natural persons practising as a sole proprietor or as individuals cannot be a personal service provider. Individuals will be employees anyway.

In addition to the above requirement any one of the following requirements must also be met:

- The ‘connected person’ would be regarded as an employee of the client, if such person receives remuneration as defined in the Fourth Schedule, and if the services were rendered by such person directly or indirectly to such client, other than on behalf of the company or trust
- If the service or duties are performed mainly at the premises of the client, such person, company or trust is subject to the control or supervision of the client in terms of the manner in which the duties are to be performed or the manner in which the services are rendered, the entity is a personal service provider.
- If more than 80% of the income of the company or trust during the year of assessment, results from services rendered, and consist of amounts received directly or indirectly from any one client of the company or trust then such an entity is a personal service provider.

However, if the company or trust, throughout the year of assessment employs three or more employees who are on a full-time basis engaged in the core business of that company or trust rendering the service, other than an employee who is a shareholder or a member of the company or trust or is a connected person in relation to that person, in these circumstances, the entity is not a personal service provider.

A gardener or the domestic cleaner is not considered to be engaged in the core business of a company and will not be considered in the minimum number of employees required in the aforementioned situation.

Tax practitioners and taxpayers are further reminded that a personal service provider cannot be a Small Business Corporation (SBC) in terms of s12E(4)(a), and consequently, cannot be eligible for SBC tax relief.

The responsibility of determining whether the recipient of remuneration is a personal service provider resides with the employer of the personal service provider. The employer will be held liable to SARS for failing to withhold employees’ tax on remuneration paid to the personal service provider if it is subsequently, irrefutably determined that the entity is a personal service provider.

It must be noted that the employer will not be required to determine whether more than 80% of a personal service provider’s income is from one client. The personal service provider has to give the employer an affidavit that it does not earn more than 80% of its income from one client.
Tax rate for PSPs
A personal service provider pays tax at a rate of 28% of taxable income for years of assessment commencing on or after 1 April 2012. The rate of tax on taxable income for years of assessment commencing on or after 1 March 2009 is 33%. Personal service providers who are companies will, in addition, pay dividends tax on any dividends declared.

It is crucial to bear in mind that the Fourth Schedule of the Income Tax Act defines a personal service provider (PSP) as an employee. Therefore, when payments are made to a personal service provider, employees’ tax at 28% must be withheld by the employer of the personal service provider unless a directive for a lower tax rate is provided to the employer. Consequently, an IRP5 is made out in favour of the entity recognised as an employee. The employees’ tax paid may be set off against the provisional tax payments or applied as a credit when the income tax liability of the personal service provider is calculated at the end of its year of assessment.

In the case of a trust that is regarded as a personal service provider, the tax rate is 40% of taxable income. Remuneration paid to a trust which is a personal service provider is paid net of employees’ tax of 40% unless a directive for a lower tax rate is provided to the employer.

“Remuneration paid to a trust which is a personal service provider is paid net of employees’ tax of 40% unless a directive for a lower tax rate is provided to the employer.”

Deductions available to personal service provider
Section 23(k) of the Income Tax Act limits the permissible tax deductions of a personal service provider to the following:
- An amount paid or payable to any employee of the personal service provider for services rendered by such employee, which is or will be taken into account in the determination of the taxable income of such employee
- Legal costs deductible under section 11(c)
- Irrecoverable debts deductible under section 11(i)
- Contributions made by the employer (PSP) for the benefit of employees to any pension fund, provident fund or benefit fund deductible under section 11(i);
- Refunds of salary (section 11 (nA) and the restraint of trade payments (section 11 (nB))
- Expenses in respect of premises, finance charges, insurance, repairs and fuel and maintenance in respect of assets, if such premises or assets are used wholly and exclusively for the purposes of trade.

Personal service providers are not permitted to deduct capital allowances such as wear and tear.

Conclusion
The taxation of a personal service provider was introduced largely to curtail tax schemes in which employees would resign from employment and subsequently, form a company or a trust (personal service provider) and thereafter offer the same services to former employers. These former employees, as a result would avoid paying employees’ tax on remuneration paid to them. They would be taxed at company rates instead of the higher marginal tax rates crafted for individual taxpayers. In addition, they would be able to claim deductions for personal expenses through the personal service provider which they were not able to claim if they were normal employees.
The state has demonstrated an important commitment to stimulate the level of employment in South Africa by enacting the Employment Tax Incentive Act 26 of 2013. This Act was promulgated on 18 December formalising the policy commitment of increasing youth employment. Employers consequently are well-placed to obtain tax benefit as a result of this new Act.

A synopsis of the Employment Tax Incentive Act 26 of 2013 is as follows:

- Signed into law on 18 December 2013 and will take effect on 1 January 2014
- Encourages private employers to employ young workers by providing a tax incentive to employers, with government sharing the costs of such employment
- The tax incentive can also be used to provide jobs to the many matriculants and other school leavers who will be entering the labour market;
- The incentive decreases the PAYE liability tax for every qualifying employee hired by the employer
- There are no changes in the wages that the employee receives
- The effective cost of hiring the employee will be lower, making it more attractive for companies and businesses to increase employment
- It is a temporary programme covering only the first two years of employment
- The Employment Tax Incentive (ETI) will be subject to continuous review of its effectiveness and impact to determine the extent to which its core objective of reducing unemployment is achieved
- The ETI will run from 1 January 2014 to 1 January 2017. It applies to qualifying employees employed on or after 1 October 2013 by eligible employers.
- Although the ETI is available for three years, an eligible employer can claim the incentives for a maximum period of 24 months per qualifying employee.

In the light of these developments SAIP-CoTE has released its second Tax Guide for 2014 which can be obtained at the following link: http://www.saipa.co.za/resources/374586/employment-tax-incentive-act-no-26-2013-guide
TAX IMPLICATIONS OF FORMER SA RESIDENT WORKING ABROAD
Mahomed Kamdar, Tax Advisor, SAIPA

Citizen X, a client (taxpayer), recently relocated from South Africa to neighbouring Country Y. The following facts are given about above-mentioned former citizen X:

- Moved his home to neighbouring Country Y;
- Has a two-year work permit in neighbouring Country Y;
- Will apply for permanent residency in neighbouring Country Y;
- Is currently employed at a company based in neighbouring Country Y and pays employee’s tax in neighbouring Country Y;
- Sometimes travels to South Africa to work at service providers for the neighbouring Country Y company.

**Question**
What is the personal tax implication for client, Citizen X in South Africa? Is Citizen X’s income exempt in South Africa? What are the tax effects of frequent travelling to South Africa, if any?

**Answer**
There are many issues in this query that require attention. The most important issue is the question of residency. Although it is given that the client, Citizen X, has moved his home, has a two-year work permit, intends to apply for permanent residency, is employed by a foreign-based company, it is still not adequately convincing that the client, Citizen X, is not a resident of South Africa for income tax purposes. In addition, the client, Citizen X, has not revealed any steps taken which demonstrate an intention to permanently reside in Namibia. A taxpayer could be physically outside of SA but still a ‘resident’ for income tax purposes.

The definition of ‘resident’ in the Income Tax Act is crucial to this query. It reads as follows: Resident means any; natural person who is-

- Ordinarily resident in the Republic; or
- Not at any time during the relevant year of assessment ordinarily resident in the Republic, if that person was physically present in the Republic-
  - For a period or periods exceeding 91 days in aggregate during the relevant year of assessment, as well as for a period or periods exceeding 91 days in aggregate during each of the five years of assessment preceding such year of assessment; and
  - For a period or periods exceeding 915 days in aggregate during those five preceding years of assessment.

The sequence of the definition of resident is important. If a natural person is proven to be ordinarily a resident of SA, there would not be a
need to conduct a physical presence test as required by the second point above of the definition of resident as per the Income Tax Act.

The courts refer to the term ‘ordinarily resident’ as follows:

- Living in a place with some degree of continuity, apart from accidental or temporary absence. If it is a part of a person’s ordinary regular course of life to live in a particular place it is regarded with a degree of permanence.
- The place where the taxpayer’s belongings are stored is where the taxpayer’s permanent place of abode is.

It is, therefore, possible for a natural person to be a resident of SA, although the person was not physically present in SA during the relevant year of assessment. It is, therefore, necessary to determine the nature and intention of Citizen X’s (the taxpayer) absence in order to establish whether the taxpayer is still ordinarily resident in South Africa.

The following factors are relevant in establishing whether the taxpayer is ordinarily a resident:

- Most fixed and settled place of residence
- Habitual abode, i.e. present habits and mode of life
- Place of business and personal interest
- Status of individual in country, i.e. immigrant, work permit periods and conditions, etc.
- Location of personal belongings
- Nationality
- Family and social relations (schools, church, etc.)
- Political, cultural or other activities
- Application for permanent residence
- Period abroad; purpose and nature of visits
- Frequency of and reasons of visits

The above list is not intended to be exhaustive or specific, merely a guideline.

The circumstances of the person must be examined as a whole, and the personal acts of the individual must receive special attention. The courts ruled (ITC 1170) that one is entitled to look at the taxpayer's mode of life beyond the particular period under consideration. It is not possible to specify over what period the comparison must be made. The comparison must cover a sufficient period for it to be possible to determine whether Citizen X is 'ordinarily resident' in South Africa.

If the client, Citizen X, is unambiguously ordinarily resident in SA, then the client will be subject to income tax on the worldwide income – income derived from both within and outside SA. The resident is eligible for a foreign tax rebate. Section 6quat is the mechanism used to provide relief for foreign taxes proven to be payable on income derived from a foreign source that is included in a resident's taxable income.

A natural person, who is ordinarily resident, but spends time outside the Republic and who intends on returning to the Republic after his or her wanderings, is regarded as a resident, regardless of the period of time spent outside the Republic.

If evidence reveals that the client, Citizen X, is a non-resident, then the client would be liable on his/her taxable income arising from a source in South Africa. Another major concern in relation to this query relates to the neighbouring Country Y’s company. Not much information is provided about this company. It is possible for the company to have a branch in South Africa or a ‘permanent establishment’ – a term frequently used in international tax. Business profits are taxable where the permanent establishment is located even though the company may be resident in another country.

- A neighbouring Country Y company with a branch in SA would pay tax in SA on the profits of the SA branch. The reader is reminded that a permanent establishment excludes places used for storing goods for display or delivery. A non-resident who carries on business in SA is subject to tax in SA on the profits of the business if they are from a source in SA. Generally, the source of the business income is located where the business is conducted.
- If there is a Double Tax Treaty (DTA) between the two countries, such income will be taxed as per the provision of the relevant DTA. The DTAs are different for different countries. It is likely (depending on the DTA) that earnings will only be taxable in SA if it is earned by a permanent establishment of the non-resident located in South Africa. If the business is conducted through a permanent establishment it is necessary to determine how much of the non-resident’s income is attributed to the permanent establishment. Attached (p4) is a model OECD definition of permanent establishment.
- So if the client, Citizen X, an individual, is a non-resident, then the income earned from a permanent establishment could be taxable in SA. It is noted that source rules are applicable to a non-resident.

It is also possible that the neighbouring country Y’s company is also a non-resident branch of a South African resident company. If Citizen X is ordinarily a South African resident, then Section 10 (1) (o) (ii) of the Income Tax Act will apply.

The Tax Professional has written extensively on this subject. The reader is encouraged to refer to Quarter 3, 2012 (page 14 of the article or click on the following link: http://www.saipa.co.za/sites/saipa.co.za/files/Prof%20Acc%20Q3%20-%20%202012.pdf).
The SAIPA-CoTE helpdesk recently received a number of VAT-related questions.

Question 1: Vendor claiming input tax for assets
May a vendor claim input tax for assets purchased in the period prior to becoming a vendor? SAIPA-CoTE members expect a definitive ‘Yes’ or ‘No’ answer, but are frequently dissatisfied with the response they receive. The response from the Tax Help Desk is an instant ‘it depends’. The ambiguous response becomes clear on after a lengthy discussion of the relevant provisions of the VAT Act.

Question 2: VAT consequences of a purchase
On 1 March 201A (Year 1), a CC purchases a computer for business purposes for R7,980 (including VAT). The CC is not registered for VAT because the total value of taxable supplies is less than R1 million. A year later, on 1 March 201B (Year 2), the CC registers for VAT since the business has expanded and the total value of taxable supplies has exceeded R1 million.

From 1 March 201B, the computer is used wholly for enterprise purposes. The market value of the computer was R4,560 when the change of application was implemented. What are the VAT consequences for the purchase of the computer?

Question 3: VAT consequences of the purchase of property
A vendor acquires a residential property in July 201A for a consideration of R1,710,000 and pays transfer duty of R53,800. At the time of purchase, the property was used to supply residential accommodation. The vendor continued to rent out the property for residential purposes. Seven months
later, that is, in January 201B, the vendor renovates the property and converts it into office space. As a result the market value of the property increased to R3 million, and the property is rented out as office space. What are the VAT consequences for the purchase of the property?

Background information

Input tax is defined in the VAT Act (Section One), in relation to the purpose for which goods or services are acquired by a vendor.

A vendor may acquire the goods or services either wholly for the purpose of consumption, use or supply in the course of making taxable supplies or partly for such purposes. Consequently input tax may be claimed only to the extent that the goods or services concerned are acquired by the vendor for such purpose.

Moreover, these goods and services will form part of the VAT enterprise as long as the purpose for their acquisition does not change, and these goods and services will remain in the VAT enterprise until such time a formal decision is taken to change the purpose for which the goods or services have been acquired. Therefore, in practice, it is possible for a good or services, at some point, to be used for either exempt VAT activity or taxable activity. In the former situation, the transaction will fall outside the ambit of VAT. In the latter situation, it is likely that the transaction will reside within the VAT ambit since it is used for taxable purposes.

The discourse in VAT is widely exposed to the terms ‘exit provision’ and ‘entrance’ provision. The exit provision applies where the goods or services have been acquired for the purpose of consumption, use or supply in the course of making taxable supplies and are subsequently, used wholly for another non-VAT purpose. Exit provisions apply only when a conscious decision was made to change the intention for which the goods or services were originally acquired. A mere change in application is not necessarily a proof of a change in intention.

However, it is likely that the entrance provisions of the VAT Act are relevant to all three situations listed above. If an asset was originally acquired or applied wholly for exempt purposes and is subsequently applied partially or totally for taxable use, an input tax is deductible in the tax period in which the change of use has occurred.

If an asset is used for the taxpayers enterprise as defined in the VAT Act, the taxpayer may use Section 18 (4) of the VAT Act.

Section 18 (4) permits input tax deduction when an asset which was not used for ‘enterprising purposes’ is subsequently used for enterprising purposes.

The vendor is reminded that the input tax may be deducted only in the tax period when the asset is brought into enterprising use. The vendor has five years within which to claim the input tax from the date when the asset was brought into use.

“The ambiguous response becomes clear on after a lengthy discussion of the relevant provisions of the VAT Act.”

The value of the asset used to claim the input tax is the lesser of the adjusted cost or the market value.

- The adjusted cost (including any tax forming part of such adjusted cost) to the vendor of the acquisition, manufacture, construction or production of those goods or services. Finance charges would not form part of such costs.
- The open market value of the supply of those goods or services at the time when the supply is deemed to be made. Open market value refers to the consideration in money which the supply of those services or goods would generally fetch between persons who are not connected parties.

The tax fraction (14/114) must be used to determine the input tax deducted and the asset must be used wholly (100%) for enterprising purposes.

Answer 1

Yes! The vendor may claim the input tax provided that the asset is used for enterprising purposes as defined in the VAT Act. The value of the assets eligible for input tax is based on the aforementioned discussion.

Answer 2

In year 1 (201A), no input tax may be deducted as the CC was not a vendor. In year 2(201B), the CC now a vendor – may make an adjustment in terms of section 18 (4) (b) (i). The amount of the adjustment must be computed as follows: 14/114 X R4560 x 100%= R560.

Answer 3

In July 201A, there will be no VAT consequences. The property was used for exempt supply. In January 201B, the vendor will be entitled to an input tax deduction because this transaction is an ‘entry’ provision. The vendor will be entitled to the following input tax: 14 /114 X R 1, 710, 000 X 100% = R210, 000 (limited to Transfer duty which is R53 800). Where the change of use is fixed property, the adjustment is limited to the transfer duty in respect of this transaction. If the property was purchased in a tax period after 10 January 2012, the limitation will not apply and the deductible input tax will still be R210, 000.
The Value-Added Tax Act (‘the Act’) makes provision for an agent acting on behalf of a principal; the agent may obtain a tax invoice made out in the name of his agent. This would mean that the agent would be entitled to obtain a tax invoice in his name, and his VAT number (if the agent is registered for VAT), where he is acting on behalf of a principal. The principal may be entitled to claim the input tax.

Section 54(2) of the Act
“(2) For the purposes of this Act, where any vendor makes a taxable supply of goods or services to an agent who is acting on behalf of another person who is the principal for the purposes of that supply, that supply shall be deemed to be made to that principle and not to such agent: Provided that such agent may nevertheless request that he be provided with a tax invoice and the vendor may issue a tax invoice or a credit note or debit note as if the supply were made to such agent.”

SARS issued VAT News No.26 July 2005 and prescribes that “[w]here the principal may not be disclosed to the supplier for commercial reasons, the agent’s VAT number must appear on the tax invoice. If the agent for the undisclosed principle is not a vendor, the word ‘agent’ must appear on the tax invoice.

“Agents are required under the VAT law to provide the principal with a monthly statement of all supplies received on behalf of the principal. The statement must be issued within 21 days after the end of the calendar month, and must include at least the following information regarding the goods or services supplied:
- A full and proper description of the supplies;
- The quantity or volume involved; and
- The consideration and rate of VAT charged or where the rate of VAT is not shown, the amount of VAT included in the consideration must be indicated.

“The agent’s statement serves the purpose of a tax invoice, and it is required so that input tax may be claimed by the principle on the supplies acquired through the agent.”
To clearly distinguish when a person is acting as an agent, and the Act lacks the defining of an ‘agent’. The general law principles of agency will apply, and SARS express such in the following extract from the Guide for Vendors (VAT404):

“An agent is someone who acts on behalf or represents another person, his principal. In order for a principal-agent relationship to exist between two parties there must be consensus between them that the one party will act on behalf of, or represent, the other party in a particular transaction or series of transactions. The consensus (or agreement) between the parties may be expressed verbally, in writing, or may even be inferred from surrounding circumstances. The agent, when acting on his principal’s behalf, will sometimes disclose the identity of his principal but a failure to do so does not affect the fact that a principal-agent relationship exists.

“The principal/agent relationship may be expressly construed from the wording of a written agreement concluded by the parties. Where a written agreement does not exist, the onus of proof is on the person who seeks to bind the principal to show that the relationship was that of a principal or an agent.

“When a tax invoice or a credit or debit note has been issued by or to an agent in the circumstances described above, the agent must maintain sufficient records so that the name, address and VAT registration number of the principal can be ascertained. These records must be retained for at least five years.”

The differences between an agent and a principal can be summarised using the following table taken from SARS VAT409 guide:

<table>
<thead>
<tr>
<th></th>
<th>Agent</th>
<th>Principal</th>
</tr>
</thead>
<tbody>
<tr>
<td>a</td>
<td>The agent will not be the owner of any goods or services acquired on behalf of the principal.</td>
<td>The principal is the owner of the goods or services acquired on his/her behalf by the agent.</td>
</tr>
<tr>
<td>b</td>
<td>The agent will not alter the nature or value of the supplies made between the principal and third parties.</td>
<td>The principal may alter the nature or value of the supplies.</td>
</tr>
<tr>
<td>c</td>
<td>Transactions on behalf of the principal will not affect the agent’s turnover, except to the extent of the commission or fee earned on such transactions.</td>
<td>The total sales represent the principal’s turnover whereas the markup is the principal's profit percentage. The commission charged by agents forms part of the principal’s expenses.</td>
</tr>
</tbody>
</table>

“The principal declares gross sales as income for Income Tax purposes.

An agent only declares the commission for Income Tax and VAT purposes.

“In essence, the abovementioned differences indicate that a person who accepts the commercial risks associated with a transaction and is trading for his/her/its own account, when concluding a transaction, is the principal and not the agent.”

Sections 54(1), (2) & (2A) stipulates that an agent may make or receive a supply of goods or services or import goods on behalf of any other person who is the principal of that agent, in which event the supply or importation is deemed to be made by or to the principal and not by or to the agent. In fact, it was held that an agent may never account for an amount of output or input tax relating to an agency transaction, except for some limited circumstances. On this basis any expenses incurred by the agent acting on behalf of the principal should be treated as disbursements, and no tax should be levied by the agent or principal when reimbursing these amounts (not a supply by the agent to the principal – the agent acted on behalf of the principal and the expenses incurred by the agent is deemed to be the expenses of the principal).

It is SARS’s current policy that an agency relationship, for purposes of VAT, does not automatically exist between an employer and employee. If the employer wishes to claim the input tax deduction for an expense the employee incurred on behalf of the employer, the employer needs to not only have the required supporting documentation (such as the tax invoice), but must also demonstrate that the employee acted as an agent for and on behalf of the employer. For this reason, some reimbursement of expenses will not support an input tax deduction, such as reimbursing the employee for cell phone costs.

The services are generally rendered by the cell phone provider to the employee, and the employer is not a party to the contract, nor is the contract entered into for and on behalf of the employer. Be mindful of claiming input tax deductions with regards employee reimbursements, as many still incorrectly claim input tax deductions!
It’s not uncommon for suppliers of goods or services to request that a deposit be paid on acceptance of a quote. It is important to distinguish between a deposit and a pre-payment. A deposit is generally considered to mark the conclusion of a contract between the parties, and to obviate some of the risks for the supplier. The deposit is not applied as payment for goods or services as yet. An example of a deposit is where a hotel requires a deposit to confirm a reservation, and the hotel will keep the relevant room for the guest. A pre-payment on the other hand is applied toward the consideration and is generally used to fund the provision of goods or services. An example is where a contractor requires a pre-payment in order to purchase the required materials for the building contract.

The general time of supply rule is that output tax is accounted for at the earlier payment received (payment of the ‘consideration’) or date of invoice issued (being the call for payment). Also, a ‘supply’ can only be such if there is a consideration. ‘Consideration’ broadly means anything that is received in return for the supply of goods or services.

The term ‘consideration’ has some specific exclusion. A ‘deposit’ received (whether refundable or not) in respect of a supply of goods or services
is not regarded as payment made for the supply (except for deposits on returnable containers) unless and until the supplier applies the deposit received as consideration for the supply, or the deposit received is forfeited.

This means that where a person pays a deposit to a vendor, which is to be held as security for the performance of an obligation, it is not treated as consideration for a supply, unless the time of supply has been triggered by the issuing of an invoice at that time. So, for an amount to be regarded as a true deposit as envisaged in the definition of ‘consideration’, the payment was not in respect of any invoice issued for the supply by the vendor, but rather some other document, such as a quote.

Remember, the issuing of an invoice (including ‘pro forma invoices’) would trigger the time of supply rule and output tax should be accounted for in that tax period. If a payment is in response to the issuing of the invoice, such payment will constitute a payment or pre-payment of the consideration (or part thereof) for the supply. A letter of terms, contract, quote, or notice claiming the deposit value would not trigger the liability for VAT if not an invoice, and it is clear from the terms and conditions that the payment is a deposit.

If the deposit received (or any part thereof) is later forfeited, the vendor will have to account for VAT at the time that the amount received is either forfeited (often deposits, or part thereof, is forfeited when the transaction/contract is cancelled); or the deposit received is applied as payment (or part-payment) of the consideration for a supply of goods or services. There is an argument to be made, with reference to European Court of Justice and Australian High Court judgements, and various positions taken by HMRC and New Zealand Tax Authority, that where a vendor cancels a contract as a consequence of the failure of a purchaser to perform the contract, the deposit retained by the vendor relates to compensation for the purchaser’s breach and not to any supply under the contract, which would not be subject to VAT.

However, we have a lack of case law in South Africa to support this position, and SARS’ current policy is that all deposit forfeiture is subject to VAT.

It should be noted that if the deposit was intended to be part-payment or pre-payment for the supply by the vendor, and not as a deposit, the time of supply will be triggered under the general time of supply rule, output tax must be recognised when payment is received (as invoice has not yet been issued), and a tax invoice must be issued within 21 days of the supply (as prescribed per section 20).

“A deposit is generally considered to mark the conclusion of a contract between the parties, and to obviate some of the risks for the supplier. The deposit is not applied as payment for goods or services as yet.”

SARS recognises the following as situations that do not constitute ‘consideration’ and therefore no output tax liability arises, when:

- Deposit is received where is not intended to lead to a taxable supply. For example, if a hotel charges a key deposit, the understanding is that the guest will use the key during that time that he/she is a guest at the establishment, and upon checking out and returning the key, the deposit will be refunded. Only if the guest fails to return the key will the deposit be simultaneously forfeited and treated as being consideration for a taxable supply.
- The deposit is vested with the vendor (being the supplier) for a supply which will take place in the future, but gives the person who paid the deposit the option to withdraw from the contract at no further cost, other than the forfeiture of all, or part, of the deposit received.

Be cautious not to make assumptions, merely because the amount payable is labelled ‘deposit’. If the contract or terms intend the up-front payment to be for part-payment of a supply, or an invoice is issued (even if intended to actually be a ‘deposit’), the supplier will be liable to account for the full output tax in that tax period. If an amount to be paid is intended to be a deposit, ensure that an invoice is not issued, and the terms of such deposit is clearly expressed.
Judgement was handed down in the case of Harding v Revenue and Customs Commissioners [2013] UKUT 575 (TCC) in the Upper Tribunal (Tax and Chancery Chamber) on 15 November 2013. The case revolved around the question of whether an omission by a tax payer of a severance payment in his tax return amounted to a ‘careless mistake’ in terms of the United Kingdom Finance Act, 2007 (UK Finance Act).

Background
The Appellant held a senior position in a company forming part of a leading accounting practice. He entered into a compromise agreement with his employer whereby his contract of employment was terminated and he received approximately £110,000 in severance payments (payment). The amount included performance-related bonuses in relation to his work. The Appellant omitted to include this payment in his tax return. However, his previous employer submitted a tax return to Her Majesty's Revenue and Customs (HMRC), which included the payment. Consequently, he was assessed by HMRC and penalty was imposed on him for careless inaccuracy in his return due to the understatement of his income.

First-tier Tribunal
The Appellant appealed against the penalty to the First-tier Tribunal (FTT) on the grounds that his failure to include the payment in his return was not careless, as he genuinely believed that the payment would not be subject to tax because it was made after the termination of his employment. The Appellant's employment was terminated on 31 October 2008 and his payment was only received later in November 2008. In support of his argument, the Appellant submitted evidence regarding an article from a tax website purportedly stating that severance payments such as the one received by him, were not taxable when they were paid after termination of employment.

The FTT dismissed the appeal stating that they were satisfied that the Appellant entertained considerable doubt as to whether the amount was in fact taxable, but failed to take steps to ascertain the correct position. Furthermore, there was no evidence that the Appellant took appropriate advice from an independent source or the HMRC.

Upper Tribunal
The Appellant subsequently appealed to the Upper Tribunal. The Upper Tribunal examined the article on which the Appellant relied as well as the compromise agreement entered into with his employer and found that:

- The compromise agreement contained a paragraph headed “Taxation” which provided that the first £30,000 of the payment was not subject to tax, but that any remaining balance shall be subject to deductions in respect of tax at the appropriate rate.
- The article made it clear that any payment received in connection with the termination of employment is taxable, but that in some circumstances the first £30,000 of such payment is tax free.
The Upper Tribunal consequently held that the decision of the FTT be upheld for the following reasons:

- The Appellant admitted that he considered that the payment was possibly subject to tax.
- The Appellant is an intelligent person, who held a senior position in a company forming part of an accountancy practice. It was not credible to propose that he could conclude that there was no possibility of the payment being taxable.
- The self-assessment the Appellant made contained an inaccuracy which led to an understatement of his liability to tax. That inaccuracy was careless, since it was due to the failure of the Appellant to take reasonable care.
- The Appellant failed to take reasonable care because he knew, or should reasonably have known, that there was at least a possibility that the payment was liable to tax.

In a South African context, in determining whether ‘reasonable care’ was taken, one would test the conduct in question against the objective criterion of the reasonable person. This means that conduct will be seen as negligent, or that reasonable care was not taken, if it is not in accordance with the conduct expected of the reasonable person who finds himself in the same situation. Conduct will be negligent where the reasonable person would have acted differently under the same circumstances, in that he would have reasonably foreseen the consequences of his actions, and taken steps to avoid such consequences. This test was laid down in Kruger v Coetzee 1966 (2) SA 428 (A).

If the facts in the Harding case were to be tested against the TAA, and the ‘reasonable person’ test was applied, then it is submitted that the South African Tax Court would likely have come to the same conclusion as that reached by the Upper Tribunal.

One could, however, speculate whether the same set of facts would be considered by the South African Revenue Service (SARS) to fall within the ambit of item (iv) of the penalty percentage table being ‘gross negligence’. Generally the ‘reasonable person’ test is also applied when testing for gross negligence; however, in terms of SARS’s Short Guide to the TAA, gross negligence calls for a disregard of the consequences of one’s actions and recklessness.

Conceivably, SARS could consider such an omission on a return as ‘intentional tax evasion’ in terms of item (v) of the penalty percentage table. However, the concept of intention generally requires a person to direct his will at achieving a particular result while being aware that the conduct in question is wrongful (Dantex Investment Holdings (Pty) Limited v Brenner 1989 (1) SA 390). SARS’s Short Guide to the TAA describes intention in terms of item (v) of the table as ‘acting wilfully or with a guilty mind’.

The relevance of the Harding case for South African taxpayers is that the fact that one genuinely believes that a particular tax position is correct will not absolve one from penalties where reasonable steps were not taken to make sure that the position taken is indeed correct. It is, therefore, crucial that taxpayers obtain the necessary tax advice, especially in circumstances where the facts raise some doubt.
Section 12P was introduced into the Income Tax Act to deal with government grants received by taxpayers and applies to years of assessment commencing on or 1 January 2013. As a result, taxpayers are now facing potentially complex rules that could have an adverse effect on their tax planning efforts.

Following the introduction of Section 12P, the Act no longer deals with:

- Grants or scrapped payments identified by the Minister of Finance;
- Amounts received by a registered exporter through a rebate or other assistance under an export incentive scheme; and
- State subsidies received in terms of the Critical Infrastructure Programme (CIP), or the Small/Medium Manufacturing Development Programme.

What are the tax implications for taxpayers?

Taxpayers that receive government grants that are either listed in the Eleventh Schedule to the Act or identified by the Minister of Finance by notice in the Government Gazette will be exempt for income tax purposes. However, no tax deductions will be allowed against such exempt grants and a comprehensive set of so-called “anti-double-dipping” rules will apply.

Examples of these rules are set out as follows.

- **Grants received to acquire, improve or reimburse expenses for trading stock**
  In such instances, the grant amount must be subtracted from the cost price of the trading stock. Any excess, i.e. if the grant exceeds the cost price of the trading stock, will result in a reduction of other tax deductible expenditure.

- **Grants received for the acquisition or improvement of an allowance asset or to fund expenditure in order to acquire or improve an allowance asset**
  The grant amount must be subtracted from the cost of the allowance asset. This means that the base cost of the asset will be reduced and as such, tax allowances claimed in respect of the asset will be limited to the reduced base cost. Furthermore, should the entire amount of a government grant not be used to acquire an allowance asset, any excess will be deemed to be a recoupment for income tax purposes. It is important to note that the grant will first reduce the cost of the asset, and any excess will then be regarded as a recoupment.

- **Grants used to fund the acquisition, creation or improvement of a “non-allowance” capital asset**
  In these circumstances, the base cost of the asset will be reduced by the grant received, which will then affect the capital gain if the asset is disposed of in the future. If the grant amount exceeds the cost of the asset, the base cost of the asset will be limited to zero. If none of these rules apply, a taxpayer will be required to reduce its other tax deductible expenditure.

Taxpayers should therefore be cognisant of the adverse tax implications associated with expenditure funded by government grants. As these rules could become complex it is recommended to speak to a tax advisor.
ARS issued a new draft Taxation Laws Amendment Bill, 2014 on 17 July 2014. The draft legislation gives effect to matters presented by the Minister of Finance in the Budget Review 2014, as tabled in Parliament earlier this year. The draft Taxation Laws Amendment Bill, proposed the scrapping of the ‘deemed loan’ secondary transfer pricing adjustment concept contained in section 31(3) of the Income Tax Act. It is to be replaced by a deemed dividend in specie paid by the South African taxpayer to the non-resident connected person. Therefore, where a South African subsidiary undercharges its foreign parent company, the shortfall will be deemed to be a dividend by the South African subsidiary to its foreign parent.

The explanatory memorandum provides us with two examples:

**Example 1**

**Facts:**
Foreign parent company pays R65 million for goods provided by the South African subsidiary. The South African subsidiary records taxable income based on the sale to its foreign parent. The arm’s length price for the goods is, in fact R100 million.

**Result:** A primary adjustment in terms of section 31 is effected, whereby the taxable income of the South African subsidiary is increased to reflect the arm’s length price of R100 million. The differential of R35 million constitutes a deemed in specie dividend paid by the South African subsidiary to its foreign parent.

**Example 2**

**Facts:**
Foreign sister company grants a R1 million loan to the taxpayer (a South African company). Foreign sister company charges interest at a rate of 10%, whereas the market related interest rate is 6%. South African company claims an interest deduction of R100 000.

**Result:** SARS effects a primary adjustment in terms of section 31, whereby interest allowable as a deduction is reduced to the market-related interest of R60 000. A secondary adjustment, in the form of a deemed dividend in specie paid to foreign sister company is triggered. Dividends tax is imposed on the R40 000 dividend deemed to have been paid by the South African company.

This amendment is to come into effect on 1 January 2015.
For anyone investing directly in the stock market, one of the most important things to consider is the tax implications. While a fund manager can buy and sell stocks in a portfolio without attracting any tax, this is not the case for individuals. There is some argument about whether this is fair or not, and if the South African Treasury shouldn’t reform the tax laws to allow the trading of shares within a portfolio as long as the value is retained. But for now anyone with an individual share portfolio needs to be aware of when their trades will be taxed, and how they will be taxed.

The first important factor is that individuals are only liable for tax on any profits that they have made. So if you buy a share for R10 and sell it down the line for R10, there is no profit and therefore no tax liability apart from the dividend withholding tax you would have paid in the interim on any dividends earned. But what happens when you buy a share for R10 and sell it later for R15?

“The intention of the taxpayer and length of time the shares are held is taken into account when determining whether the gain on shares sold is taxed as a capital or revenue profit,” explains Shelly Moreno, the head of tax at Harvard House. “Profits from shares held as part of a portfolio for long-term investment attract capital gains tax when sold, whereas shares held by a share dealer are treated as a revenue asset, so profit from the sale of these shares attracts income tax.”

Where time comes into the equation is that tax laws automatically consider any shares held for longer than three years to be a long-term investment.

“In terms of these rules, if a taxpayer disposes of a share which he or she has held for at least three years, then the proceeds from such a sale are deemed to be of a capital nature and so capital gains tax and not income tax is payable,” explains Madeleine Schubert, tax and fiduciary specialist at Citadel. “This rule applies regardless of whether the taxpayer is a trader or not.”

So it is only if the shares have been held for under three years that the ‘golden rule’ of the tax payer’s intention comes into question. And here, things can get quite tricky. If the shares were bought with the intention to trade and then sold again as such, there is no argument. Any profit would be considered revenue and therefore fully taxed at the taxpayer’s marginal rate.
However, it might be possible that the shares were acquired with the intention of trading, but then sold for another purpose. This would then make them capital assets, although this would be very hard to prove, especially if the taxpayer has a history of trading. But it could be done if the facts supported this case.

“Profits from shares held as part of a portfolio for long-term investment attract capital gains tax when sold, whereas shares held by a share dealer are treated as a revenue asset, so profit from the sale of these shares attracts income tax.”

Another possible scenario is that the shares were bought with the intention of keeping them as an investment and were sold as such, even though they weren’t held for a full three years. Again, this would have to be proven and the taxpayer would have to show that the intention was never to make a short-term profit. This obviously becomes more difficult if, in fact, a high short-term gain was realised. “And it is important to note that the onus of proof rests with the taxpayer should SARS see you as a trader rather than a long-term investor,” Moreno emphasises.

In all cases, it is always in the taxpayer’s interest to incur capital gains rather than income tax. This is because only one-third of the capital gain is included in your taxable income, rather than the whole gain if it is deemed as income.

“Capital gains tax is definitely not the enemy,” Moreno emphasises. “An individual earning a capital gain of R1 million and no other income in the 2015 tax year will only pay tax of R58 324 if he or she is under 65.”

So engaging with a tax expert is a good idea to make sure you cover your bases. “Tax planners are entitled to structure their affairs to obtain a tax benefit from a commercial transaction,” Citadel’s Schubert says. “And the taxpayer’s business, personal and investment goals would inform what is an optimal tax plan.”

It’s also important to note that the implications of selling shares are the same, whatever your age. So if you have directly held shares in your retirement portfolio, you must consider what tax you will be paying on them when and if you need to sell them to fund your retirement.

“The capital gains annual exclusion of R30 000 per year remains unchanged whether you are retired or not,” explains Moreno from Harvard House. “The taxable capital gain is added to the rest of the taxpayer’s taxable income, and the total taxable income will then be taxed according to the tax rates in the tables. The higher age rebates will, however, give relief to taxpayers over 65 and further relief to taxpayers over the age of 75.”

It is, therefore, worth considering how you structure your affairs for retirement to reduce your tax burden. And Moreno has some good advice in this respect.

“One way to reduce the tax liability would be for married couples to build separate investment portfolios,” she advises. “As a husband and wife are treated as separate taxpayers, each of them will get the interest exemption, capital gain annual exclusion and age rebates.”

She gives the example of a husband and wife who are both over 75 years old in the 2015 tax year. In the first scenario, only the husband has an investment portfolio and earns a capital gain of R200 000 on the sale of his shares and earns interest of R300 000. In this case, he would pay tax amounting to R48 577.

However, if the couple had built separate investment portfolios they could be structured so that they each earned R100 000 capital gain and R150 000 interest. The tax that would be paid in this instance would only be R2 783 each, or R5 566 in total.

“The saving of R43 011 is because each taxpayer is entitled to the interest and capital gains exclusions as well as the age rebates,” Moreno explains. “So we do feel that it is important that investors structure their portfolios in such a way that they understand what tax they will generate.”

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TAX SNIPPETS

FAMOUS TAX DODGERS

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Laureyn Hill
In May 2013 the famous former Fugees band member who won a Grammy award with her solo career album The Miseducation of Lauryn Hill was sentenced to three months in federal prison and a further three months of home confinement for failing to pay taxes on more than $2 million in earnings during a five-year period. She had pleaded guilty to the charges in 2012. In all, federal prosecutors said Hill had earned approximately $2.3 million during the five years and had an unpaid tax total of $1,006,517. She told the court she had always meant to eventually pay her taxes but had been unable to since her career tanked.

Wesley Snipes
On 2 April 2013 American actor, film producer, and martial arts expert Wesley Snipes was released from jail after almost three years for failing to submit income tax returns. Snipes was convicted of three misdemeanour counts of failing to file tax returns in 2008. Between 1999 and 2001, Snipes avoided $7 million in taxes. One of Snipes’ original defences was that he had relied on the advice of his tax advisors, Eddie Ray Kahn and Douglas P. Rosile. They were convicted by the same jury of tax fraud and conspiracy and both got longer prison terms than Snipes.

Leona Helmsley
The hotel magnate famously is quoted as saying, “We don’t pay taxes. Only the little people pay taxes.” The judge ordered her prison sentence to begin on 15 April which is Tax Day in the USA.

Al Capone
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Ulrich Hoeness
Ulrich Hoeness, the German football legend and former Bayern Munich football club president was sentenced to three and a half years in prison after being convicted for tax fraud by a German court on Thursday 13 March 2014. Hoeness cheated the German state out of 27m Euros in unpaid tax. He said he would not appeal the verdict and he had resigned from his position as president and board chairman of the football club.

Source: www.sars.gov.za

Lionel Messi
Barcelona FC and Argentina’s soccer star Lionel Messi and his father Jorge Horacio have paid €10 million in back taxes to try and avoid being charged for tax evasion. The two were summoned to appear in a court near Barcelona in September 2013, relating to taxes owed for image rights income in 2010 and 2011. If convicted, they could face a sentence of six years in prison.

Dolce and Gabbana
The founders of the world-known Italian designer label Dolce & Gabbana - Domenico Dolce and Stefano Gabbana - were convicted of tax evasion by a Milan court in June 2013. Prosecutors alleged that the fashion designers failed to declare €200 million when two of the company’s main brands were sold to a Luxembourg-based holding company. Dolce and Gabbana were sentenced to one year and eight months in prison, suspended, and were ordered to pay a penalty of €500,000 to the Italian tax administration.

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THE NEW COMPLIANCE RISK MANAGEMENT PLAN (CRMP) WEBSITE IS NOW AVAILABLE AT WWW.CRMP.CO.ZA.

This project was spearheaded by the Compliance Institute Southern Africa in line with their Generally Accepted Compliance Practice framework.

The CRMPs are exclusively available to companies that employ members of the Compliance Institute Southern Africa, IoDSA, SAICA or SAIPA.

A CRMP is an invaluable compliance tool that will assist you to:

- Easily identify and assess applicable regulatory requirements;
- Analyse the objective of the requirement and how it applies to you;
- Identify the associated compliance risk;
- Record the control measures that are in place to mitigate this risk;
- Document any additional controls required; and
- Email additional controls and target dates to responsible person.

CRMPs currently available:

- Consumer Protection Act (Rights) and (Interactions) (2 Plans);
- FAIS Act suite (3 Plans);
- Financial Intelligence Centre Act;
- Occupational Health and Safety Act (Core duties) and (Offices) (2 Plans);
- Companies Act
  - Private companies (Governance) and (Authorisations) (2 Plans);
  - Public companies (Governance) and (Authorisations) (2 Plans); and
- Municipal Finance Management Act (Municipality accounts).

The site will continually be updated with new CRMPs as they become available.

Visit www.crmp.co.za and “take a tour” to learn more about features such as:

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