DLA CLIFFE DEKKER HOFMEYR

TAX ALERT

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IN THIS ISSUE

BINDING PRIVATE RULING 156 (BPR 156): PENSION BENEFITS ACCRUING TO A NON-RESIDENT FROM A RESIDENT PENSION FUND

BPR 156 dealt with the question of whether (or to what extent) a pension annuity and a retirement lump sum benefit will be taxable in South Africa, if it is received by or accrues to a person who is **not** a resident of South Africa, from a South African registered pension fund.

Prior to 2001, residents and non-residents were taxed based on the source of their income; essentially their income was taxed in South Africa (SA), if it originated in SA. Since 2001, SA has recognised the residence basis of taxation, which means that if a person is a resident in SA, he or she is taxed in SA on their worldwide income, regardless of its source. The source based system of taxation is, however, still applicable to non-residents in SA. Thus, persons who are not resident in SA, will only be subject to tax in SA on income sourced in this country. Double Tax Treaties (DTT's), which have been concluded by SA with various countries, regulate the taxation of income earned in one state and taxed in another, to ensure that double taxation is avoided.

Section 9 of the Income Tax Act, No 58 of 1962 (ITA) determines the source of various types of income. Specifically, s9(2)(i) treats an amount as being from a source in SA, if it is a pension or annuity and the services in respect of which that amount was received or accrues, were rendered within SA. Section 9(2)(i) further provides that the amount received or accruing, must be apportioned where the services were rendered partly inside and partly outside SA.

The facts in this instance were that the Applicant was employed by one company in a group of companies, which company was registered in SA. In 1999, the Applicant's employment with the latter company was terminated and he left SA to join a foreign company in the group, and then became ordinarily resident in that foreign country. The Applicant made contributions to a registered South African pension fund during his term of employment in SA and subsequently continued to contribute to this fund, despite having lost resident status in SA as a result of his move abroad.

Essentially, regarding the question submitted for ruling, SARS ruled based on s9(2)(i) of the ITA, providing that the portion of the pension annuity and retirement fund lump sum benefit received or accrued from a South African source (relating to services rendered in SA), would be included in the Applicant's gross income in SA in terms of paragraphs (a) and (e) of the 'gross income' definition. Therefore, the pension and retirement fund pay-out would have to be apportioned and only the portion relating to the time during which services were rendered by the Applicant in SA, will be taxed in SA. The remaining portion will be taxed based on its source.

Danielle Botha

SHARE TRADING - CONSIDERATION OF FACTORS INDICATIVE OF A BUSINESS BEING CONDUCTED

The issue of share trading and whether the profits or the losses derived therefrom should be treated on capital or revenue account for tax purposes, has been a contentious issue in South African tax law for quite some time.

For South African income tax purposes, the general rule in determining the nature of the proceeds or the losses derived from share market activities is to determine the intention with which the shares were acquired and held by the taxpayer.

Accordingly, South African tax law gives effect to the intention of the taxpayer in order to determine whether the proceeds or the losses derived from share market activities should be treated on capital or revenue account.

In the recent Australian case of *Hartley and Commissioner of Taxation [2013] AATA 601*, the Australian Administrative Appeals Tribunal (Appeals Tribunal) was asked to determine whether the applicant conducted the business of share trading in order to claim deductions for the relevant years of assessment or whether the applicant was in fact a share investor and accordingly did not carry on the business of share trading.

The facts of the case were that the applicant was, at all relevant times, a full-time employee of the council, a position which occupied him for 38 hours a week. For many years the applicant was also actively involved in the share market and according to his testimony, that activity occupied him for about 15 hours per week, which activity was mainly conducted during his ordinary working day.

Based on the applicant's assertion that his share market activities constituted a business for tax purposes, the applicant, through his tax agent, lodged income tax returns wherein he claimed significant amounts as deductions for each of the three tax years ending 30 June 2009, 2010 and 2011. These deductions were claimed by the applicant for the losses that he suffered as a result of his participation in the share market activities.

However, the Commissioner of Taxation (Commissioner) argued that the applicant was not entitled to claim the deductions for the losses suffered, due to the fact that the applicant was a share investor or possibly a speculator and therefore the shares should be treated as assets only for purposes of capital gains tax.

The Commissioner therefore conducted an audit on the tax affairs of the applicant for the three years in question and made a determination that the applicant was a share investor and was not carrying on the business of share trading. The Commissioner subsequently imposed an administrative penalty on the applicant for the 2009 year of assessment, based on a lack of reasonable care. The applicant lodged an objection against the notices of assessment and the shortfall penalty imposed by the Commisioner and the Commissioner subsequently issued the objection decision that allowed the objection in part by reducing the penalty shortfall to nil for the 2009 year of assessment.

Not being satisfied with the Commissioner's decision, the applicant applied to the Appeals Tribunal for a review of the objection decision.

The essential issue before the Appeals Tribunal was whether or not the applicant was carrying on the business of a share trader for income tax purposes.

In determining the issue at hand, the Appeals Tribunal held that the question as to whether someone is engaged in a business is a question of fact, the answer of which depends on the impression which the decision-maker forms having regard to all the surrounding circumstances.

The Appeals Tribunal further held that the more usual approach and the one adopted in the income tax context, is to consider a number of accepted factors which point in one direction or the other. In summarising the objective factors that should be considered in determining the existence of a business for income tax purposes, the Appeals Tribunal referred specifically to the factors as listed by the Deputy President Todd in *AAT Case 6, 297 (1990) 21 ATR 3747*, which was cited with approval in the case of *Shields and Deputy Commissioner of Taxation (1999) 41 ATR 1042 at 1048*. The factors to be considered are:

- The nature of the activities and whether they have the purpose of profit-making.

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- The complexity and magnitude of the undertaking.
- An intention to engage in trade regularly, routinely or systematically.
- Operating in a business-like manner and the degree of sophistication involved.
- Whether any profit/loss is regarded as arising from a discernible pattern of trading.
- The volume of the taxpayer's operations and the amount of capital employed by him.

In light of the factors set out above, the Appeals Tribunal held that the factors in favour of the applicant's argument was that the turnover in gross terms was quite large, particularly having regard to the applicant's salary which he received by virtue of his employment. The Appeals Tribunal further held that the applicant did in fact maintain an office specifically for the purpose of conducting his share purchase and sale transactions and further maintained records of transactions for the purpose of doing accounting and tax calculations.

On the other hand, the Appeals Tribunal held that there were also a number of factors in favour of the Commissioner's argument. In particular, the Appeals Tribunal held that looking at the totality of the evidence, it could not be said that the applicant's activities demonstrated an intention to trade regularly or routinely. Furthermore, the applicant was engaged in another full-time profession as a council employee and lastly, the operation of the applicant was very simple, lacked any real sophistication and was not consistent with the operation of a business.

The Appeals Tribunal concluded by stating that although the matter was finely balanced, those factors pointing against the existence of a share trading business were more significant than those pointing in favour of the existence of a share trading business.

Accordingly, the applicant's application for a review of the Commissioner's objection decision was dismissed and the Commissioner's objection decision was confirmed.

Based on the discussion set out above, it is clear that the Australian tax authorities, like the South African tax authorities, also determine the nature of proceeds derived from the sale of shares with reference to the taxpayer's intention. However, the factors considered by the Appeals Tribunal in this case, as well as the previously decided case law, is useful in determining the true intention of the taxpayer from an objective point of view.

It would be interesting to see whether the South African tax authorities would adopt a similar set of guidelines to enable one to determine the true intention of the taxpayer, insofar as share market activities are concerned.

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