Among other things, it is a requirement that (i) the seller carries on an enterprise in relation to the property and (ii) the enterprise is an income-earning activity on the date of transfer of the enterprise.

The term ‘enterprise’ is defined widely in s1 of the VAT Act and it is trite that the leasing of commercial immovable property is an enterprise for purposes of the definition.

The South African Revenue Service (SARS) has issued Interpretation Note No 57 (IN 57) dealing with the sale of an enterprise as a going concern.

In IN 57, under the heading “Supply of an income-earning activity” SARS states the following:

“The purchaser must be placed in possession of a business which can be operated in that same form, without any further action on the part of the purchaser.

...Leasing activities generally consist of, amongst others:

■ an underlying asset that is the subject of a lease; and

■ a contract of lease.

Accordingly, a vendor who conducts a leasing activity in respect of fixed property and who intends to supply such leasing activity must make provision in the contract stating that the other aspects of the leasing activity are disposed of together with such fixed property in order to constitute an income-earning activity. In instances where the agreement does not provide for a property together with the lease agreements to be transferred, only the asset is sold and s11(1)(e) will not apply.

...An asset which is merely capable of being operated as a business does not constitute an income-earning activity. There must be an actual or current operation. For this reason, the agreement to dispose of a business yet to commence or a dormant business is not a going concern.

As the parties must agree that the enterprise will on the date of transfer thereof be an income-earning activity, the zero rate can apply where the seller is in terms of the contract obliged to start the business and ensure it is income-earning before transfer thereof. However, in instances where the purchaser takes possession of the enterprise before the date of transfer, and the enterprise is only income-earning after the date of transfer, the zero rate will not apply.”

In this regard the recent United Kingdom (UK) case of HMRC v Royal College of Paediatrics and Child health and another [2015] UKUT 38 (TCC) is interesting. Under UK VAT law – like our VAT Act – there is effectively no VAT if a business is transferred as a going concern and certain requirements are met.

Briefly the facts of the Royal College case were the following: A developer owned a commercial building in London. The building was vacant. The Royal College of Paediatrics and Child Health (Royal College) occupied other premises elsewhere in London. The Royal College also let part of those other premises to other organisations including the British Association of Perinatal Medicine (BAPM). The Royal College wished to buy the building from the developer. The BAPM and other tenants wished to move to the new building with the Royal College and remain its tenants.

continued
Before concluding the sale with the developer the Royal College instructed its advisers to achieve the most VAT efficient structure for the purchase. The advisors suggested that VAT could be saved if the sale was structured as the transfer of a going concern; if BAPM entered into an agreement for a lease with the developer before the Royal College agreed to buy the property then, since the developer was carrying on a business, the transfer would be one of a going concern.

The developer and BAPM entered into an agreement for a lease of a single room in the building for a premium of £1,000. The agreement was conditional on the developer concluding an unconditional contract for the sale of the property to Royal College. The premium would be repaid if this condition was not met or if completion of the lease with the Royal College had not happened by a certain date. Rent was only payable after completion. It appears as if the developer did not enter into a lease agreement with BAPM; they entered into an agreement to enter into a lease.

The Royal College granted a lease to BAPM after the sale. The court considered the relevant legislation and authorities and held as follows:

"It seems to me that a critical point arising...is that for a transfer to fall into the relevant class there are two things which have to be transferred. First of course an asset must be transferred. However something else has to be transferred as well. That further element is referred to variously as a business, an undertaking, or an economic activity (or part of such a thing). Merely transferring an asset on its own will never be enough to satisfy the test. In order to work out whether the necessary second element has been transferred, one needs to look at all the relevant circumstances. The test is one of substance not form. The circumstances can include the intentions of the parties."

The court accordingly ruled that there was no transfer of a going concern.

The attitude of the court was similar to that expressed in IN 57. Interestingly, in the Royal College case, the court held that there could be a going concern not only if the seller transferred an existing lease to the buyer but also if the seller transferred a lease agreement with a putative tenant.

In many cases in South Africa where owners of commercial properties wish to sell their properties, the properties are vacant. Without doing something further, the properties cannot be sold as going concerns and the transactions cannot be zero-rated for VAT purposes. Often parties in a transaction of this kind are tempted to create a lease between the seller and a third party simply for the purpose of creating a going concern. As the court in the Royal College case demonstrated, the substance and not the form of the transaction will be the deciding factor as to whether the rental enterprise is genuinely a going concern.

However, on the strength of the Royal College judgment, it appears that there may well be a case for a going concern if a seller, prior to the sale, concludes a lease agreement with a bona fide third party which will only take effect after the sale and which the purchaser will take over after transfer.

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IMPROVED TAX ALLOWANCE FOR PHOTO VOLTAIC POWER PLANTS

The 2015 Taxation Laws Amendment Bill (TLAB) proposes an amendment to s12B of the Income Tax Act, No 58 of 1962 (Act) in respect of the accelerated tax allowance available to photo voltaic (PV) power plants. The proposal, which comes into operation on 1 January 2016, allows for a 100% accelerated tax allowance in respect of embedded PV power plants, generating up to 1MW for self-consumption.

As a general principle and provided the requirements of s12B of the Act are met, a taxpayer is permitted to deduct the cost of qualifying assets (including structures of a permanent nature), used in the generation of electricity from renewable resources, on a 50 / 30 / 20 basis (i.e. over a three year period). As s12B of the Act currently stands, solar power is classified as a single concept without distinguishing between the sub-categories of photo voltaic and concentrated solar power (CSP). The TLAB proposes a split from the current ‘solar power’ reference in s12B of the Act to:

- PV solar energy exceeding 1MW;
- PV solar energy not exceeding 1MW; and
- CSP

In respect of embedded PV solar energy not exceeding 1MW, a new 100% accelerated tax allowance will be available in the year of assessment in which the asset is brought into use. This allowance is aimed at increasing the uptake in these projects. PV solar energy exceeding 1MW and CSP will, however, continue on the existing 50 / 30 / 20 write-off provisions.

Treasury states that the reason for the change is driven by the low environmental and water consumption impact, economies of scale and apparent historical experience within the PV solar energy industry. It is further stated that, unlike large-scale PV solar power projects (those exceeding 1MW), small-scale PV solar power projects do not necessarily require additional investment in supporting infrastructure, such as roads and transmission lines. This statement by Treasury appears counter-intuitive as investments in supporting infrastructure are just as crucial in certain aspects as the renewable energy projects themselves, especially in remote areas within South Africa.

However, the purpose of the change is clearly to promote self-consumption, i.e. where the power generated is not fed into the national grid. Should Treasury’s intended uptake indeed prove to be successful, you can expect the rooftops of corporate offices within South Africa to be adorned with small-scale PV solar plants.

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