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TAX AND EXCHANGE CONTROL ALERT

IN THIS ISSUE

TAX CONSEQUENCES OF WAIVER OF CONTRACTUAL RIGHTS

Capital gains tax (CGT) is levied on the disposal of an asset. The terms "disposal" and "asset" are defined widely in the Eighth Schedule to the Income Tax Act, No 58 of 1962 (Act). The term "disposal" includes "the forfeiture, termination, redemption, cancellation, surrender, discharge, relinquishment, release, waiver, renunciation, expiry or abandonment of an asset" (see paragraph 11(1)(b) of the Eighth Schedule to the Act (Eighth Schedule)).

CUSTOMS AND EXCISE HIGHLIGHTS

This week's selected highlights in the Customs and Excise environment since our last instalment.

CDH

CLIFFE DEKKER HOFMEYR

TAX CONSEQUENCES OF WAIVER OF CONTRACTUAL RIGHTS

Paragraph 38 of the Eighth Schedule applies when a person disposes of an asset by way of a donation, or to a person who is a connected person in relation to the person disposing of the asset for a consideration that is below an arm's length price.

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It is encouraging to see that SARS continues to rule that commercial transactions in the ordinary course do not give rise to donations tax.

Paragraph 38 of the Eighth Schedule applies when a person disposes of an asset by way of a donation, or to a person who is a connected person in relation to the person disposing of the asset for a consideration that is below an arm's length price. In such a case, the asset is deemed to have been disposed of for a market-related consideration.

The reduction of a debt for inadequate consideration can give rise to either income tax (under s19 of the Act), or to CGT (under paragraph 12A of the Eighth Schedule) in the hands of a creditor. The tax depends on the way that the debtor applied the debt funding.

Donations tax is levied on the value of property disposed of under a donation. The term "donation" includes "any *gratuitous* waiver or renunciation of a right" (s55 of the Act – emphasis added).

The provisions above were the subject of Binding Private Ruling 273 (Ruling) issued by the South African Revenue Service (SARS) on 2 May 2017. The facts were as follows: two companies (Co A and Co B) were both wholly-owned subsidiaries of another company. Co A had the right to receive from Co B "an annual quantity of produce" determined under a prescribed formula. Co A unilaterally waived the right against Co B.

Unfortunately, the further details of the arrangement between the parties and circumstances surrounding the waiver of the right are not set out in the Ruling.

Notably, it is not clear how Co A could unilaterally waive its right. Presumably, if Co A had a right it would have arisen under some contractual arrangement with Co B. If so, Co A would not have had the power to waive the right; the right would have had to have been terminated by mutual agreement between the parties. If that was the case, there would have been no question of a donation or disposal of the asset by waiver for tax purposes.

Nevertheless, SARS ruled that the waiver did not give rise to donations tax. Assuming that there had been a unilateral waiver of the right, it is unclear why donations tax was at issue in the Ruling at all. As noted above, for a disposal to amount to a donation, there must be an element of gratuity. It is doubtful that the element of gratuity would have been present in the context of what appears to have been a commercial transaction. Nevertheless, it is encouraging to see that SARS continues to rule that commercial transactions in the ordinary course do not give rise to donations tax (see also, for example, Binding Private Ruling 252 dated 10 October 2016 and Binding Private Ruling 253 dated 19 October 2016).

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TAX CONSEQUENCES OF WAIVER OF CONTRACTUAL RIGHTS

CONTINUED

SARS ruled that the waiver of the right to the produce for no consideration did not trigger the application of s10(4) of the Value-Added Tax Act, No 89 of 1991 to deem the value of the supply of the service to be at open market value.

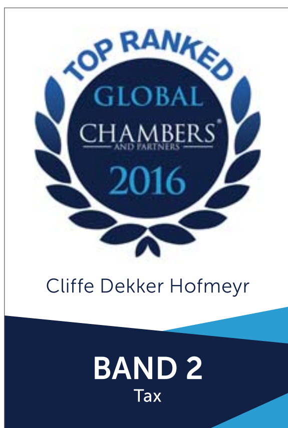
Co A and Co B were "connected persons" in relation to each other. However, SARS nevertheless ruled that the waiver of the right for no consideration did not trigger paragraph 38 of the Eighth Schedule. Again, it is not clear why that provision was at issue. The provision applies if there is a disposal to a person. If the right was simply waived, could it be said that there was a disposal of the right to Co B? (See, for example, *Income Tax Case No 1859* 74 SATC 213.)

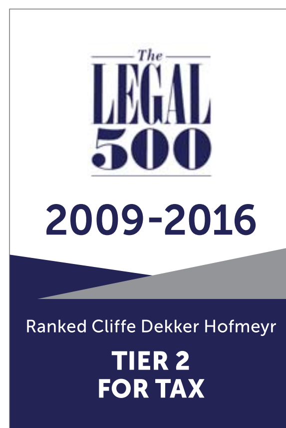
SARS also ruled that neither s19 of the Act, nor paragraph 12A of the Eighth Schedule applied to the waiver. Those provisions apply where a debt owed is waived. It is not clear that the obligation to provide the produce annually actually was a debt owed at the time of the waiver.

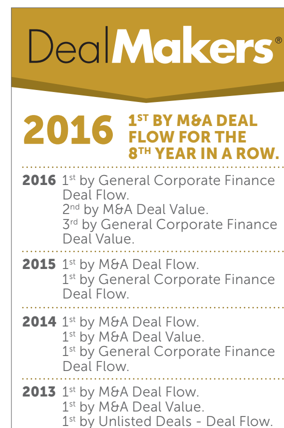
Finally, as to value-added tax, SARS ruled that the waiver of the right to the produce for no consideration did not trigger the application of s10(4) of the Value-Added Tax Act, No 89 of 1991 to deem the value of the supply of the service to be at open market value.

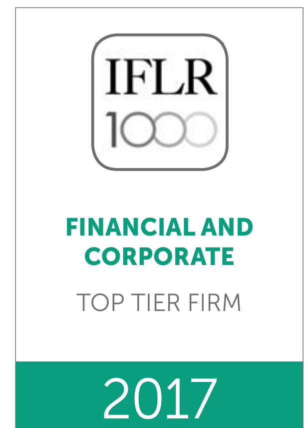
Taxpayers should welcome the Ruling. But, unfortunately, as the Ruling does not set out the facts in detail, and as the Ruling does not set out SARS's reasoning, taxpayers should take care in similar transactions.

Ben Strauss









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CUSTOMS AND EXCISE HIGHLIGHTS

Please note that this is not intended to be a comprehensive study or list of the amendments, changes and the like in the Customs and Excise environment, but merely selected highlights which may be of interest.

In the event that specific advice is required, kindly contact our Customs and Excise specialist, Director, Petr Erasmus.

This week's selected highlights in the Customs and Excise environment since our last instalment:

1. The official launch of the South African Revenue Service's Customs Preferred Trader Programme occurred on 8 May 2017. This journey began in 2011 and was set up under the World Trade Organisation's internationally recognised Authorised Economic Operator programme.

   Generally, the Preferred Trader Programme is aimed to be a relationship between a Customs client and SARS Customs in order to:

   - Achieve benefits for both parties;
   - Stamp out misconduct and fraudulent activities;
   - Obtain and maintain a high level of compliance; and
   - Promote legitimate trade facilitation.

   Some of the benefits to trade should include:

   - The appointment of a Customs Relationship Manager tasked with facilitating the relationship between the client and Customs;
   - Reduction of the amount of security required for compliance with a Customs procedure;
   - Fewer routine documentary and physical inspections;
   - Prioritising a request for tariff and valuation determinations; and
   - Prioritising access to non-intrusive inspection techniques when goods are stopped or detained for inspection.

   A specialised Preferred Trader team has been set up by SARS to handle applications and audits, while an Accreditation Review Customs Committee at SARS's head office makes a final decision on all accreditation submissions. All importers and exporters may apply for Preferred Trader status if they meet certain compliance criteria.

   For more information, interested parties can email preferredtrader@sars.gov.za or go to the SARS website: www.sars.gov.za.

   Note, however, that SARS will likely conduct a thorough audit on applicants and the risk of potential discovery of (inadvertent) contraventions of the Customs & Excise Act, No 91 of 1964 (Act) and subsequent retrospective demands in duties, VAT, penalties, interest and so on, is prevalent.

2 Draft technical amendments to Schedule 1, 2 and 6 to the Act. We quote from the SARS media release:

   > The draft amendments in Parts 1, 2A and 3E of Schedule No. 1, Part 1 of Schedule No. 2 as well as Part 1C of Schedule No. 6 to the Customs and Excise Act, 1964 (the Act), are technical in nature and will have no effect on the duty structure.

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CUSTOMS AND EXCISE HIGHLIGHTS

CONTINUED

Primary products that are made from virgin material as opposed to recycled material for plastics classifiable in Chapter 39.

The amendments are mostly due to requests received from industry or other government agencies but there are also some consequential amendments to the HS 2017 that were omitted from the Publication for 1 January 2017 that is now rectified.

These relate to:

2.1 Schedule 1 Part 1:

- 2.1.1 Mixed portions of bone in cuts of chicken under tariff subheading 0207.14.9;
- 2.1.2 Primary products that are made from virgin material as opposed to recycled material for plastics classifiable in Chapter 39;
- 2.1.3 Aluminium waste and scrap of heading 76.02;
- 2.1.4 The creation of separate tariff subheadings for substances that contribute to the depletion of the ozone layer and global warming, of Chapters 29 and 38;
- 2.1.5 The creation of 8-digit tariff subheadings for screw studding classifiable in heading 73.18; and
- 2.1.6 Providing for road wheels and rims fitted with tyres separately under certain categories for parts included in Part 3E for Chapter 87.

2.2 Schedule 1P2A: Heading 2206.00 amended to include saké;

2.3 Schedule 1P3A: Providing for road wheels and rims fitted with tyres separately under certain categories;

2.4 Schedule 2: Anti-dumping item 201.02/0207.14.92/01.08 is inserted as a consequence to the insertion of 8-digit tariff subheading for mixed portions in Part 1 of Schedule No. 1; and

2.5 Schedule 6: With the implementation of HS 2017 provisions were inserted for wine in containers holding more than 2 litres but not more than 10 litres.

Petr Erasmus

CHAMBERS GLOBAL 2011 - 2017 ranks our Tax and Exchange Control practice in Band 2: Tax.

Emil Brincker ranked by CHAMBERS GLOBAL 2003 - 2017 in Band 1: Tax.

Mark Linington ranked by CHAMBERS GLOBAL 2017 in Band 1: Tax.

Ludwig Smith ranked by CHAMBERS GLOBAL 2017 in Band 3: Tax.

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