

TAX & EXCHANGE CONTROL ALERT

IN THIS ISSUE

RESIDENTIAL PROPERTY DEVELOPERS FACE CASH FLOW CRUNCH DUE TO VAT ON TEMPORARY LETTING OF UNITS

Many residential property developers will kick off 2018 with a major cash flow challenge as a result of a substantial value added tax liability which they may face in respect of the temporary letting of residential units which have been developed for resale.

CONSECUTIVE ASSET-FOR-SHARE TRANSACTIONS

Section 42 of the Income Tax Act, No 58 of 1962 allows taxpayers to transfer assets to a company free of immediate tax consequences, provided certain requirements are met; there is a "roll-over" for tax purposes. However, certain anti-avoidance provisions may be triggered if the company that acquired the assets, disposes of the assets within 18 months of acquisition.

CUSTOMS HIGHLIGHTS

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

RESIDENTIAL PROPERTY DEVELOPERS FACE CASH FLOW CRUNCH DUE TO VAT ON TEMPORARY LETTING OF UNITS

The moment the developer lets the unit, VAT becomes payable on the open market value of the unit at that time.

The temporary relief was initially provided until 1 January 2015 but was subsequently extended to 1 January 2018.

Many residential property developers will kick off 2018 with a major cash flow challenge as a result of a substantial value added tax (VAT) liability which they may face in respect of the temporary letting of residential units which have been developed for resale.

When a property developer develops residential properties for resale, the developer is entitled to deduct the VAT incurred on the development cost as input tax. The developer is then obliged to levy VAT on the sales consideration when the residential units are sold. If the developer experiences difficulty in finding buyers for the units due to adverse market or economic conditions, the developer may instead let them until the property market improves. However, the moment the developer lets the unit, VAT becomes payable on the open market value of the unit at that time. This is because the South African Revenue Service (SARS) is of the view that the temporary letting of residential units developed for resale comprises a 'change in use' from making taxable supplies to exempt supplies, since the letting of residential accommodation is exempt from VAT.

The Minister of Finance at the time, Mr Pravin Gordhan, stated in his budget review on 17 February 2010 that this situation is disproportionate to the exempt income received by the owners of the properties and that options will have to be investigated to determine a more reasonable method in dealing with the temporary letting of residential properties developed for resale.

Section 18B of the Value-Added Tax Act, No 89 of 1991 (VAT Act) was introduced with effect from 10 January 2012 under which residential property developers enjoyed temporary relief from the payment of VAT. Section 18B allowed developers to temporarily let the residential units for a period of up to 36 months before the VAT thereon became payable. The temporary relief was initially provided until 1 January 2015 but was subsequently extended to

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

Gerhard Badenhorst ranked by CHAMBERS GLOBAL 2014 - 2017 in Band 1: Tax: Indirect 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.



RESIDENTIAL PROPERTY DEVELOPERS FACE CASH FLOW CRUNCH DUE TO VAT ON TEMPORARY LETTING OF UNITS

CONTINUED

The temporary relief provided for under s18B has not been extended any further and ceased to apply on 1 January 2018.



1 January 2018. The relief did not apply where the property was let beyond a 36-month period, or when the property was applied permanently for letting as a dwelling or for purposes other than making taxable supplies.

The temporary relief provided for under s18B has not been extended any further and ceased to apply on 1 January 2018.

Consequently, residential property developers are now faced with the dilemma that they are required to account for VAT to SARS in the January 2018 tax period on the open market value of all the unsold residential units which they temporarily let as dwellings. The VAT is payable even though some of the units may not have been let for a full 36 months.

When the temporary relief measures were first introduced, it was recognised in the Explanatory Memorandum on the Taxation Laws Amendment Bill, 2011 that the VAT payments due upon the temporary letting of the residential units undercut the cash-flow gains otherwise associated with temporary letting and may even force certain developers into insolvency. It was further stated that s18B was introduced as a short-term measure to address the cash flow problem faced by developers, whilst a more permanent solution was being sought. However, it seems that during the six years that the temporary relief under s18B applied, no effort was made to find a permanent solution to the problem, and we merely revert back to the VAT position prior to the introduction of the temporary relief measures.

Property developers that find themselves in a cash flow squeeze as a result of s18B ceasing to apply, can approach SARS under s167 of the Tax Administration Act, No 28 of 2011 (TAA) to pay the VAT amount due in instalments over an agreed period. The

developer must, in terms of s168 of the TAA, be able to satisfy SARS that it has a cash flow problem and is unable to settle the VAT in a single payment, and that its financial position is likely to improve in the short term. SARS may also request the developer to provide suitable security before it agrees to the payment of the VAT in instalments.

If the developer has paid the VAT on an unsold unit which is temporarily let and it subsequently manages to sell the unit, then VAT is payable on the total sales consideration. SARS has stated in its VAT News 14 (March 2000) that the developer may then deduct the total VAT amount previously paid. SARS also subsequently stated in its Guide for Fixed Property and Construction (VAT 409 – 2011) that the developer is entitled to deduct the total amount of VAT previously paid on the unit let in the tax period in which the unit is sold, but this statement was not repeated in subsequent VAT 409 guides. However, allowing a full deduction of the VAT previously paid seems to be in contradiction with s18(4) of the VAT Act, which provides for a deduction to be made only on the lesser of the adjusted cost or the open market value of the unit.

We can only hope that SARS and National Treasury will urgently address the problems with regard to the VAT rules concerning the change in use adjustments for property developers, which problems have already been acknowledged by the Minister of Finance back in 2010, and that a permanent solution will be introduced soon. Both the New Zealand and Australian tax authorities have successfully addressed this issue, and guidance could be drawn from them to find a suitable solution in a South African context.

Gerhard Badenhorst

CONSECUTIVE ASSET-FOR-SHARE TRANSACTIONS

The South African Revenue Service has provided some guidance in its Binding Private Ruling: BPR 288 of 17 January 2018.

In BPR 288 the taxpayer sought a ruling from SARS on proposed transactions.



Section 42 of the Income Tax Act, No 58 of 1962 (Act) allows taxpayers to transfer assets to a company free of immediate tax consequences, provided certain requirements are met; there is a "roll-over" for tax purposes. However, certain anti-avoidance provisions may be triggered if the company that acquired the assets, disposes of the assets within 18 months of acquisition.

A question that has often been posed is whether the anti-avoidance provisions will apply if the company that acquired the asset, within 18 months of the acquisition, disposes of those assets to another company in terms of an asset-for-share transaction under s42 of the Act.

The South African Revenue Service (SARS) has provided some guidance in Binding Private Ruling 288 (BPR 288).

In BPR 288 the taxpayer sought a ruling from SARS on the following proposed transactions.

Company A is a local company. The shares in Company A are held (i) as to 89.8% by Company B, a foreign company, and (ii) as to 10.2% by the managing director (MD) of Company A.

A new shareholder (X) will buy 6.5% of the shares in Company A from Company B and the MD in proportion to their shareholding in Company A. The price will be market-related.

X will then transfer the shares it acquired in Company A to Company Q, a local company, in exchange for shares in Company Q.

Company B and the MD will then dispose of 19.5% of their shares in Company A to Company R in exchange for shares in Company R in quantities proportionate to their respective shareholding in Company A. Company B will transfer those shares as an asset-for-share transaction under s42 of the Act. Company R intends holding the shares in Company A on capital account.

The subsequent transaction is the tricky one: Company R will promptly transfer its shares in Company A to Company Q in exchange for shares in Company Q. Company R will transfer those shares in terms of an asset-for-share transaction under s42 of the Act. Company R will then hold 75% of the shares in Company Q. The remaining shares in Company Q will be held by X.

The rulings of SARS that are notable are the following:

- First, in the circumstances of the matter, Company R will be seen to hold the shares in Company A on capital account even though it will dispose of the shares in Company A to Company Q shortly after it acquired the shares.

CONSECUTIVE ASSET-FOR-SHARE TRANSACTIONS

CONTINUED

BPR 288 is not a licence for taxpayers to do successive asset-for-share transactions under s42 of the Act in all cases.



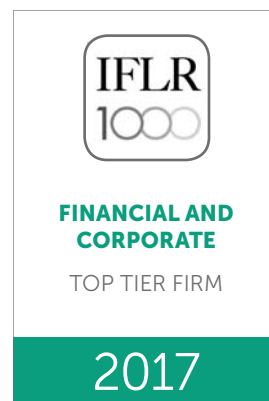
- Second, in principle, the 18-month anti-avoidance rule will apply to the disposal by Company R of its shares in Company A to Company Q. However, practically, no gain or loss will arise as the shares in Company A will be transferred at the cost at which they have been acquired.
- Third, the second asset-for-share transaction, that is, the transfer by Company R of its shares in Company A to Company Q, will qualify as an asset-for-share transaction under s42 of the Act.

What the ruling essentially says is this: if a taxpayer transfers a capital asset to a company in exchange for shares in that company and the requirements of s42 of the Act are met; and if the company then

promptly disposes of that capital asset to another company in exchange for shares in that other company and the requirements of s42 of the Act are met – then both transactions may qualify for tax “roll-over” relief.

A word of warning though: SARS made it very clear that the ruling in BPR 288 was specific to the facts in the matter. BPR 288 accordingly is not a licence for taxpayers to do successive asset-for-share transactions under s42 of the Act in all cases. Taxpayers would still in each case need to take specific advice from tax professionals before implementing such transactions.

Ben Strauss



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. Rule amendments (certain sections quoted from the SARS website):
 - 1.1 Draft rules under s8 of the Customs & Excise Act, No 91 of 1964 (Act), relating to the reporting of conveyances and goods (RCG), and intended to replace the current rules under s8 of the Act were published for public comment. The content of the proposed rules under s8 is, within the context of the Act, closely related to Chapter 3 of the Customs Control Act, No 31 of 2014. The proposed rules are intended to bring the RCG requirements under the Act closer to what will be required in terms of the Customs Control Act when that Act comes into effect.

Comments can be submitted to C&E_legislativecomments@sars.gov.za by 19 January 2018.
 - 1.2 Amendment to rules under s13, s46 and s49 relating to amendments of the various trade agreements and forms DA 185.4A7 and DA 185.4A2.
 - 1.3 Amendment to rules for the implementation of the REX system of self-certification of the origin of goods exported to Norway in terms of the Generalized System of Preferences.
2. Amendments to Schedules to the Act (certain sections quoted from the SARS website):
 - 2.1 Schedule 1:
 - 2.1.1 To implement the revised Tariff Rate Quota in terms of the Economic Partnership Agreement (EPA), with retrospective effect from 1 September 2017 up to and including 31 December 2017.
 - 2.1.2 To implement the revised Tariff Rate Quota in terms of the EPA, with effect from 1 January 2018.
 - 2.2 Schedule 1 Part 1:
 - 2.2.1 The substitution of tariff subheadings 1001.91 and 1001.99 as well as 1101.00.10 and 1101.00.90 to reduce the rate of customs duty on wheat and wheaten flour from 91c/kg and 136,50c/kg to 71,63c/kg and 107,45c/kg respectively.

CUSTOMS AND EXCISE HIGHLIGHTS

CONTINUED

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



2.2.2 Implementation of changes to the rates of customs duties in terms of the Economic Partnership Agreement between the European Union and the Southern African Development Community EPA States for 2018 and other miscellaneous amendments, with effect from 1 January 2018.

2.2.3 To increase the rate of customs duty on self-adhesive tape of subheading 3919.10.

2.2.4 The creation of subheading 7602.00.90 ("Aluminium waste and scrap"), with retrospective effect from 17 November 2017.

2.3 Schedule 2:

2.3.1 Item 260.03 – To create a temporary rebate provision on safeguard duty applicable to certain hot-rolled steel classifiable in tariff headings 72.08 and 72.25.

2.4 Schedule 3:

2.4.1 Deletion of rebate item 311.12/54.07/03.04 ("Woven fabrics of synthetic filament yarn").

2.5 Schedule 4:

2.5.1 Item 416.15 – To implement changes to the rates of customs duties in terms of the EPA between the European Union and the Southern African Development Community EPA States for 2018 and other miscellaneous amendments with effect from 1 January 2018.

2.5.2 Item 460.15 – The creation of a temporary rebate provision for the importation of certain stainless steel classifiable in tariff heading 73.18.

2.5.3 Item 460.15 – The creation of a temporary rebate provision for the importation of certain structural steel in the form of U, I, H and L sections, classifiable in tariff headings 7216.40 and 7228.70.

2.6 Schedule 6:

2.6.1 Item 670.03 – Amendments to provide for refund provisions on distillate fuel for the manufacture of intermediate fuel oil with retrospective effect from 30 September 2015.

CUSTOMS AND EXCISE HIGHLIGHTS

CONTINUED

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



2.6.2 Item 623.14 –
Amendments to provide for refund provisions on distillate fuel for the manufacture of intermediate fuel oil with retrospective effect from 30 September 2015.

3. The International Trade Administration Commission has done the following (certain sections quoted from the notices):

3.1 Invited new importers to submit permit applications in terms of the rebate item 460.11/00.00/01.00 ("Used overcoats, car-coats, raincoats, anoraks, skijackets, duffle coats, mantles, three-quarter coats, greatcoats, hooded caps, trench coats, gabardines, padded waistcoats and parkas (but no other clothing articles) classifiable under tariff headings 61.01, 61.02, 62.01, 62.02 and 6309.00.13"), for 2018, within three (3) weeks from the date of the publication, being 5 January 2018.

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3.2 Issued a notice of initiation of the sunset review of the anti-dumping duty on glass frit originating in or imported from Brazil on 15 December 2017.

On 21 July 2017, the International Trade Administration Commission of South Africa notified the SACU industry through Notice No. 546 in the Government Gazette No. 40998, that unless a substantiated request is made by it indicating that the expiry of the anti-dumping duties on the subject product originating in or imported from Brazil would likely lead to the continuation or recurrence of dumping and injury, the antidumping duties on the subject product originating in or imported from Brazil will expire on 14 February 2018. A detailed response to the Commission's sunset review questionnaire was received.

The Applicant alleges that the expiry of the duty would likely lead to the recurrence of dumping and the recurrence of material injury. The Applicant submitted sufficient evidence and established a prima facie case to enable the Commission to arrive at a reasonable conclusion that a sunset review investigation of the anti-dumping duty on glass frit originating in or imported from Brazil be initiated.

Should you have any queries, please do not hesitate to contact the investigating officers Mr Busman Makakola at +27 12 394 3380 and Ms Charity Ramaposa at +27 12 394 1817 or at fax number +27 12 394 0518. Due date is 30 days from date of notice.

CUSTOMS AND EXCISE HIGHLIGHTS

CONTINUED

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



4. Government Gazette 41306 Notice 948 dated 8 December 2017 relating to Guidelines, Rules and Conditions pertaining to Permits issued under Rebate Item 460.17/87.03/04.04 for vintage and/or internationally collectable motor vehicles not imported for conventional/ Domestic Daily Transportation Use or Purposes Classifiable under Tariff Heading 87.03 has been published.

5. The Rates and Monetary Amounts and Amendment of Revenue Laws Act, 2017 was promulgated on 14 December 2017.

6. On 15 December 2017, the following was published (quoted from the media statement of the National Treasury):

Following the promulgation of the Rates and Monetary Amounts and Amendment of Revenue Laws Act, 2017 (Act, No 14 of 2017) (2017 Rates Act), the National Treasury and SARS today publish the 2017 Rates Act. The 2017 Rates Act deals with changes in tax rates and monetary thresholds, excise duties on alcohol

beverages and tobacco products as announced in the 2017 Budget Speech and 2017 Budget Review. Further, the 2017 Rates Act also introduces a Health Promotion Levy to be imposed on Sugary Beverages, effective from 1 April 2018.

7. The levies and fees payable on goods subject to compulsory specifications relating to the National Regulator for Compulsory Specifications (NRCS) have been increased per Department of Trade and Industry Notice 1413 dated 15 December 2017.

8. The tariff of fees charged for services rendered in terms of the Legal Metrology Act, No 9 of 2014 by the NRCS has increased per Department of Trade and Industry Notice 1412 dated 15 December 2017.

9. Please advise if additional information is required.

Petr Erasmus

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Emil Brincker has been named a leading lawyer by Who's Who Legal: Corporate Tax – Advisory and Who's Who Legal: Corporate Tax – Controversy for 2017.

Mark Linington has been named a leading lawyer by Who's Who Legal: Corporate Tax – Advisory for 2017.

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