TAX & EXCHANGE CONTROL

ALERT

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The term "*consideration*" is widely defined in section 1(1) of the Value-Added Tax Act 89 of 1991 (VAT Act) to mean any payment made or to be made, whether in money or otherwise, or any act or forbearance, in respect of, in response to, or for the inducement of, the supply of any goods or services, whether by that person or any other person.

Where a business is transferred as a going concern which qualifies for the zero rate in terms of section 11(1)(e) of the VAT Act, or if the business transferred falls outside the scope of VAT under section 8(25), it may not be considered important to determine whether the assumption of the liabilities forms part of the consideration payable. In this case, the VAT on the assumption of the liabilities as part of the business acquisition will generally follow the VAT status of the consideration payable for the business. However, it is critical to determine whether the assumption of the liabilities forms part of the consideration payable if the transaction does not qualify for zero rating, or for the exclusion under section 8(25).

The VAT consequences of the assumption of the more common types of liabilities which are generally assumed as part of a business acquisition are discussed below.

TRADE CREDITORS

The purchaser may agree with the seller that the purchaser will assume the seller's contractual liability to make payment of amounts owing to trade creditors at the date of the transfer of the business. The parties agree that the purchase price for the business payable to the seller will be reduced by the amount owing to the trade creditors. These liabilities exist independently of the business assets that are being disposed of.

The consideration paid for the business in this case comprises of two parts, (i) the consideration paid to the seller for the business and (ii) the amounts paid to the trade creditors to settle the amounts owing by the seller and to relieve the seller of its liabilities. The amount of consideration on which VAT is payable is the aggregate of the two, as they both form part of the monetary consideration payable in respect of the supply of the business.

WARRANTY CLAIMS

The purchaser and the seller may agree that the purchaser will honour the seller's warranty obligations for goods sold prior to the transfer of the business. In this case the amount payable by the purchaser is not known at the time the business is transferred. The parties agree that the purchase consideration will be reduced by an agreed amount, determined on some basis as an estimate of the warranty claims that are expected to be made.

The undertaking by the purchaser to settle the seller's warranty obligations that arise after the effective date of the transfer of the business comprises non-monetary consideration for the

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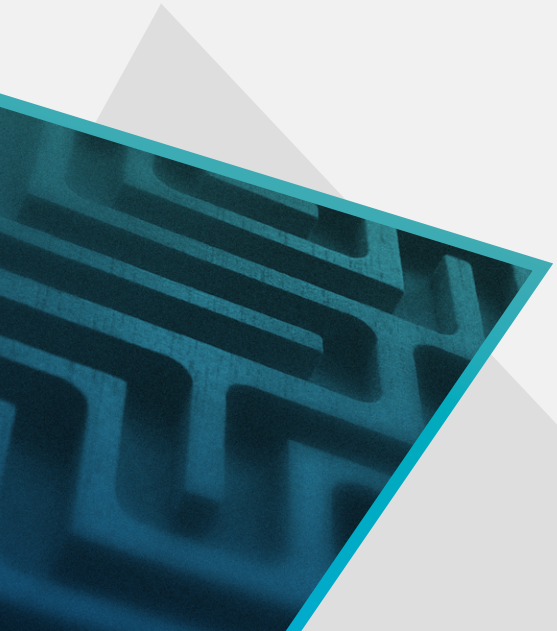

supply of the business. The value placed on this obligation by the parties acting at arm's length and by which the purchase price for the business is reduced, forms part of the consideration payable for the business. VAT is therefore payable on the actual amount paid by the purchaser to the seller plus the value placed on the warranty obligations assumed by the purchaser.

STATUTORY OBLIGATIONS

Certain liabilities may be imposed by statute, in which case the purchaser assumes the liability as a consequence of purchasing the business. Where a statute imposes an obligation on the owner of the business, the seller is released from the liability when the business is transferred, and the purchaser assumes the statutory liability.

A typical example of such an obligation is provided in Interpretation Note 94 (IN 94), citing a judgment by the Supreme Court of Canada, where the appellant disposed of its right to harvest timber and the buyer assumed the appellant's statutory obligation to reforest the land on which it had previously felled timber. The issue was whether the value of the assumed liabilities comprised part of the consideration received for the disposal of the right to timber. The court held that the reforestation obligation was simply a future cost tied to the forest tenures that depressed the value of the assets and was not a separate obligation, and therefore it did not comprise consideration for the sale.

Although IN 94 deals with the income tax implications of contingent liabilities assumed in the acquisition of a business, the same principles regarding statutory obligations equally apply in a VAT context. If a liability is imposed by a statute on the operator of the business, the liability reduces the value of the business. The liability assumed by the purchaser is embedded in the business acquired. In these circumstances the purchaser does not assume the liability in terms of a contractual arrangement between the supplier and the purchaser, but as a consequence of the operation of a particular statute. Accordingly, the assumption of a statutory obligation does not form part of the consideration paid to the supplier for acquiring the business.

PAYMENT MADE FOR ASSUMPTION OF A LIABILITY

The above scenarios must be distinguished from the situation where a person who has an existing or future liability pays another person to assume that liability. As an example, a company may have an existing

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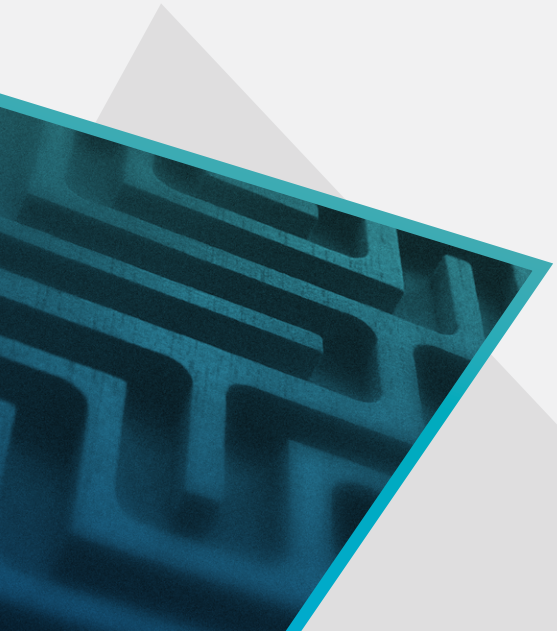

third-party claim against it, or have contingent warranty claims in respect of goods manufactured. The liability in this scenario comprises a "*debt security*", and the transfer thereof to another person is a financial service in terms of section 2(1)(c) of the VAT Act, which is exempt from VAT in terms of section 12(a). A "*debt security*" is defined in section 2(2)(iii) to include an obligation or liability to pay money that is or is to be owing by any person. It therefore includes current liabilities as well as liabilities that may arise in the future.

Consequently, a person who receives a payment as consideration for the assumption of another person's current or future liability is not liable to account for VAT on the payment, because it is exempt from VAT.

CONCLUSION

The VAT consequences of the assumption of liabilities depend on the nature of the specific liabilities and on the nature of the transaction under which the liabilities are assumed. In some instances, the assumption of liabilities is standard rated and sometimes it may form part of a zero-rated transaction. The assumption of certain liabilities may fall outside the scope of VAT, and in other instances it could be exempt from VAT. Each scenario must therefore be considered on its own merits and on the relevant facts.

TERSIA VAN SCHALKWYK AND GERHARD BADENHORST

May SARS widen its scope to investigate and seize? Yes, it's warranted!

In the case of *Bechan and Another v SARS Customs Investigations Unit and Others* (19626/2022) [2022] ZAGPPHC 259 (28 April 2022) the High Court was tasked with deciding whether the South African Revenue Service (SARS) acted unlawfully in searching motor vehicles parked outside of designated premises and whether the affected persons could demand the return of the seized items through the *mandament van spolie*.

On 28 March 2022, a warrant was issued in terms of sections 59 and 60 of the Tax Administration Act 28 of 2011 (TAA). The warrant authorised SARS to seize information and documentation at the premises of, and related to, a particular taxpayer (Taxpayer).

The day after obtaining the warrant, SARS arrived at the Taxpayer's premises in order to execute it. The premises were located within an office park, which was shared with a number of other companies. Access to the office park was controlled, and SARS was delayed in entering the premises. During the time of this delay, SARS officials noticed various people carrying items from the office premises to motor vehicles parked in the general parking area. When the SARS officials eventually gained access to the premises they encountered several of the Taxpayer's directors as well as the applicant in this case, Mr Bechan, who informed SARS that he was at the office park for business with a different company.

While executing the warrant, SARS investigated the vehicles parked in the general parking lot and noticed that several of these vehicles contained documents relating to the Taxpayer.

On SARS' version, when Mr Bechan was asked to open his motor vehicle he informed them that he did not have the keys. Considering the resistance SARS faced to execute its warrant, both the South African Police Service (SAPS) and the Hawks were called in to assist. SARS then procured the services of a locksmith to open Mr Bechan's vehicle and the other vehicles whose owners had refused to open them.

On Mr Bechan's version, he denied ever refusing to open his vehicle and claimed that he had immediately handed both his cell phone and his vehicle's keys to SARS. Despite the differing versions, once Mr Bechan's vehicle was opened, SARS removed certain items and took them into custody, duly inventoried.

MANDAMENT VAN SPOLIE APPLICATION

Mr Bechan then brought an application for a *mandament van spolie* order. This was an order to obtain the return of the items taken from his vehicle, which by the time the court heard the application, amounted to two laptops and two cell phones. SARS had returned all the other items beforehand.

The court relied on the principles stated in the Constitutional Court case of *Anale Ngqukumba v The Minister of Safety and Security* 2014 (5) SA 112 (CC) that the "*essence of the mandament van spolie is the restoration before all else of unlawfully deprived possession of the possessor*". Essentially, it is premised on the philosophy that no one should resort to self-help to obtain or regain possession and aims to preserve public order by restraining people from taking the law into their own hands and encouraging them to rather follow due process.

May SARS widen its scope to investigate and seize? Yes, it's warranted!

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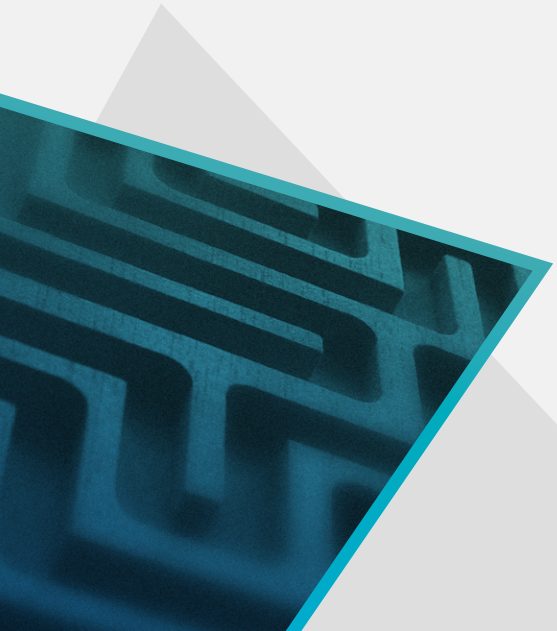

Mr Bechan's application was based on the contention that the items had been in his undisturbed possession and that SARS had unlawfully dispossessed him of them.

The court noted that on Mr Bechan's version of events, he had handed his vehicle keys to SARS upon request and so had voluntarily relinquished possession of his vehicle – which means that the fundamental requirements for the *mandament van spolie* would not be met.

However, the court considered SARS' version to be fundamentally more probable and that Mr Bechan did not relinquish possession of his vehicle, since SARS had involved both the SAPS and the Hawks and had experienced a delay of approximately 10 hours before the vehicle could be opened by a locksmith. This militated against Mr Bechan's version. As such, the court was in no doubt that Mr Bechan was deprived of possession by SARS.

The court noted that the man*dament van spolie* can only succeed where the dispossession was unlawful and so the next question was whether the deprivation was lawful or not. SARS submitted that although neither Mr Bechan nor his vehicle was specifically identified in the warrant, section 62(1) of the TAA applied in these circumstances.

SEARCHING PREMISES NOT IDENTIFIED IN A WARRANT

Section 62 of the TAA, titled "*Search of premises not identified in warrant*", and section 62(1) in particular, essentially empowers a SARS official to enter and search premises not identified in a warrant, as if those premises had been identified in the warrant – subject to the qualifications in this section.

The court explained that with this section being applicable, SARS was entitled, in executing the warrant, to confirm whether Mr Bechan had in his possession or under his control any of the Taxpayer material specified in the warrant. Considering that SARS officials witnessed material being carried to motor vehicles, their decision to search Mr Bechan and his vehicle was not unreasonable.

In defending Mr Bechan's election to pursue restoration of the items under the *mandament van spolie*, SARS argued that the appropriate procedure to obtain the return of his property was in terms of section 66 of the TAA.

RETURNING SEIZED MATERIAL

Section 66, titled "*Application for return of seized relevant material or costs of damages*", essentially states that a person may request SARS to, among other things, return some or all of the seized material; if SARS refuses the request, the person may then apply to the High Court for the return of the seized material. The court may then, if good cause is shown, make the order it deems fit.

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Mr Bechan's counsel argued that the warrant had to be construed as narrowly as possible, including that since the TAA contained no definition of "*person*" (and should be read interchangeably with "*taxpayer*"), the proper interpretation of "*premises*" in section 62 ought to be read to mean the premises of the taxpayer in respect of whom the warrant had been issued. The contention being that since Mr Bechan parked in a general parking area – which was not on the premises of the Taxpayer – it was unlawful for SARS to open his vehicle and seize the items.

The court contemplated the following elements of the warrant: firstly, it provided for the seizure of material relevant to the Taxpayer at the specified premises; secondly, the warrant referred to the physical street address where the Taxpayer conducted business and where Mr Bechan found himself on the day in question; and finally, the description of the warrant of the address where it was to be executed together with the description of the material forming the subject of the warrant made it clear that SARS sought material relevant to the Taxpayer.

The court then held that:

- The warrant in its terms provided for the search anywhere on the premises identified in the warrant, which included vehicles parked on the premises.
- Interpreting the warrant as restrictively as argued by Mr Bechan's counsel would undermine its efficacy – which is the very situation SARS encountered when its entry to the premises was delayed.
- Even if it could be argued that the warrant was not sufficiently wide to include Mr Bechan's vehicle, the provisions of section 62 entitled SARS to open the vehicle and take possession of the Taxpayer information in it.

Consequently, the court dismissed the application.

OBSERVATION

The importance of this case lies in suggesting that SARS is not strictly limited in its execution of a warrant. Rather, in certain circumstances, it appears that SARS is empowered to investigate other premises with the purpose of seeking any relevant material related to the taxpayer in question. Furthermore, while a taxpayer is entitled to request the return of seized material, the judgment seems to indicate that a taxpayer should do so in terms of section 66 of the TAA and not the *mandament van spolie*.

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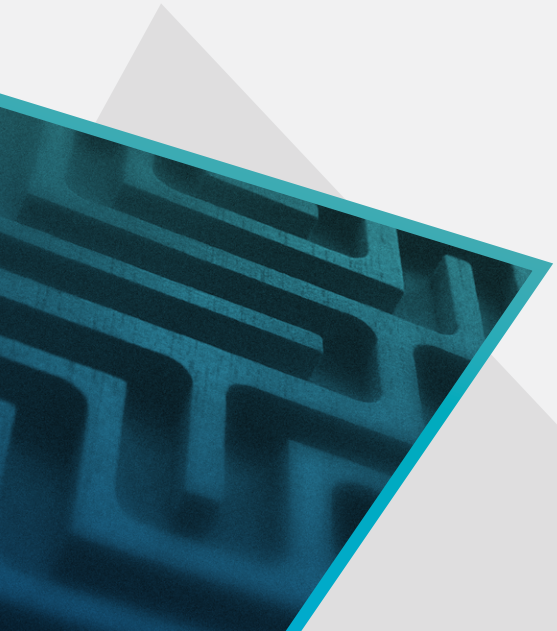

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Our BBBEE verification is one of several components of our transformation strategy and we continue to seek ways of improving it in a meaningful manner.

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