DLA CLIFFE DEKKER HOFMEYR

TAX

ALERT

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IN THIS ISSUE

SHUTTLEWORTH COULD HAVE 'SHUTTLED' HIS MONIES OUT OF SOUTH AFRICA WITHOUT THE PAYMENT OF A LEVY

In a far reaching judgment the Supreme Court of Appeal (SCA) held on 01 October 2014 that Mark Shuttleworth could have repatriated his funds out of South Africa without the imposition of a 10% exit levy that was imposed by the South African Reserve Bank (SARB) at that stage. In particular, it was indicated that the SARB had to repay such levy together with interest at the prescribed rate from 13 April 2012 to the date of payment.

The application that Mark Shuttleworth brought against the SARB pursuant to the exit levy that he had to pay on the repatriation of his funds outside South Africa has been the subject matter of much debate. The initial application (which was unsuccessful on the remission of the 10% levy) was worded quite widely and also sought that a number of the provisions of the Exchange Control Regulations (Regulations) had to be declared unconstitutional. He also criticised the so called 'closed door' policy of the SARB on the basis that applications had to be submitted through means of authorised dealer banks. Ultimately Shuttleworth emigrated from South Africa in order to free up his funds to invest outside South Africa on the basis that the exchange control system in South Africa was "severely restrictive and rendered investments outside" the South African borders prohibitive.

In the SCA the argument was confined to the appropriateness of the exit levy on the basis that the other relief sought by Shuttleworth did not impact upon his position directly. The argument of Shuttleworth was essentially that:

- the exit levy was levied on a generalised basis and no discretion was exercised in the deciding whether or not the exit levy should be applied; and

The SARB, in turn, contended that the levy was intended to constitute a disincentive to exit large amounts of capital and that it thus assisted to maintain the financial stability of the South African economy. For this the SARB relied upon regulation 10(1)(c) of the Regulations which provides that:

"No person shall, except with permission granted by the Treasury and in accordance with such conditions as Treasury may impose enter into any transaction whereby capital or any right to capital is directly or indirectly exported from [South Africa]".

It was accepted that the regulation serves a legitimate purpose and that the external balance of payments must be a continuing concern for National Treasury. However, the issue was whether such regulation could be used as a revenue raising mechanism and not whether there was merit in such prohibition.

Given the fact that the relevant procedure to raise the levy was not adopted in circumstances where the exit levy was held to constitute 'taxation', it was indicated by the SCA that one cannot levy taxation without representation and that the executive branch of Government should not be entitled to raise revenue. Rather, it should be dependent on the taxing power of Parliament which is the vehicle that is accountable to South Africa's taxpaying citizenry.

Reference was also made to the Constitution and specifically that a specific procedure must be adopted to the extent that so called 'money bills' are adopted. For instance a money bill cannot be introduced in the

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National Council of Provinces. The principle was thus confirmed that taxes cannot be levied by delegated legislation which is not specifically authorised in a money bill.

It was specifically indicated that the exit levy raised revenue for the Government in circumstances where the exit levy was paid into the National Revenue Fund (it appears that approximately R2,9 billion was paid in the form of exit levies during the time concerned).

Having held that the exit levy was unlawfully imposed, the SCA indicated that it would be inequitable for National Treasury to retain an amount "what it had no right to claim". Even though the exit levy was paid by Shuttleworth, it was paid under protest with a view to repatriate the monies concerned. There was no other mechanism available to Shuttleworth at the time. The payment under protest was thus involuntary and he was thus entitled to a repayment of the levy together with interest.

The SCA was at pains to emphasise that matters will not be heard in the abstract and without proper consideration for its effect on the exchange control regime and the South African economy as a whole. In other words, the relief that was sought by Shuttleworth in respect of the remaining exchange control provisions were not considered in circumstances where Shuttleworth acknowledged that he was acting in the public interest. Given the fact that a consideration of these other issues would have had no practical effect, the SCA refused to consider same. In particular, the SCA specifically did not consider the validity of the so called closed door policy of the SARB in circumstances where it has limited resources and that it cannot deal with a potential flood of applications.

The principle that taxes cannot be levied without having adopted the appropriate procedures, is not only limited to the exit levy that was imposed by the SARB. It goes further and extends to a number of other areas where amounts or levies were applied in terms of delegated legislation or authorities other than Parliament. One such example in an income tax context related to the way in which transfer pricing provisions could have been applied by the Commissioner for the South African Revenue Service (Commissioner). In particular, these provisions provided that the Commissioner could adjust consideration so as to reflect an arm's length price for goods and services which effectively amounted to the imposition of a tax without the correct process having been adopted.

Emil Brincker

IMPROVEMENTS EFFECTED ON LAND NOT OWNED BY THE TAXPAYER

On 1 October 2014, the South African Revenue Service (SARS) released Binding Private Ruling 180 (Ruling) dealing with the question of whether a taxpayer, who is a party to a Public Private Partnership (PPP), would qualify for a deduction under s12N of the Income Tax Act, No 58 of 1962 (Act) in respect of improvements effected on land not owned by the taxpayer.

In respect of PPP's, Government often undertakes to provide underlying land to a private party for the construction of buildings or the improvement of the land, without parting with ownership of such land. Section 12N of the Act allows for private parties to a PPP to claim deductions in respect of improvements effected on land or buildings owned by Government, even though the private party only has a right of use or occupation of the land.

To qualify under s12N of the Act, a private party must:

- hold a right of use or occupation of the land or buildings;
- effect improvements on the land or buildings in terms of a PPP;
- incur expenditure to effect the improvements; and
- use or occupy the land or buildings for the production of income, or derive income from the land or buildings.

By way of background, a company incorporated in and a resident of South Africa (applicant) and a department of the National Government (department) entered into a PPP in terms of which it was agreed that under the proposed transaction, the applicant would:

- finance, design, construct, operate and maintain a new serviced head office building for the Department that is to be constructed on land owned by the Government; and
- assume the financial, technical and operational risk for the project.

The applicant would be able to use subcontractors to carry out its obligations for both the construction and the operational phases of the PPP. The PPP provided for a unitary payment to be made by the department to the applicant of the capital amount owed to the applicant, together with interest and service fees.

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Furthermore, during the construction phase, the applicant would be granted possession of and access to the project site to construct the serviced head office building. The operational phase would commence thereafter.

It is important to note that the applicant would not hold any right of use or occupation of the land or the serviced head office building by virtue of any term of the PPP. The applicant would only be given access to the new building exclusively for purposes of providing the services as described in the PPP.

The issue under consideration before SARS was whether the applicant qualified for any of the deductions referred to in s12N of the Act in respect of the improvements effected on land not owned by the taxpayer.

SARS ruled that the applicant did not comply with the requirements of s12N of the Act and therefore did not qualify for any deduction under any provision referred to in s12N of the Act.

The draft Taxation Laws Amendment Bill 2014 (draft Bill) was released by National Treasury on 17 July 2014. The explanatory memorandum to the draft Bill notes that under certain PPP arrangements a private party is not able to meet the criteria of s12N of the Act. Specifically, the private party will not necessarily have the right of use or occupation of the land or buildings. The private party could, for example, only have a right to access the land or building in order to perform under the PPP. As a result, the private party is not able to claim any deduction under section 12N and this has an effect on the overall pricing of the project.

The draft Bill proposes the insertion of s12NA into the Act, which addresses the above problem and will essentially allow a private party to claim a special capital allowance in respect of improvements to State-owned land and buildings where the Government has the right to use or occupy the land or buildings, and not the private party. In order to claim this special allowance, the private party must:

- be a party to a PPP agreement with Government; and
- incur expenditure of a capital nature.

The proposed insertion of s12NA to the Act will come into operation on 1 April 2015 and will apply in respect of expenditure incurred to effect improvements during any year of assessment commencing on or after that date.

It is evident that the insertion of s12NA to the Act will provide relief to those private parties to PPPs, who find themselves in a position similar to the applicant, where they do not have the right of use or occupation of land or buildings owned by the Government and to which improvements have been effected.

Gigi Nyanin (supervised by Heinrich Louw)

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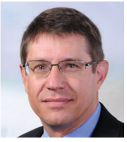

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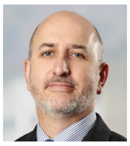

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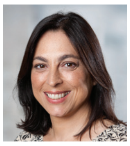

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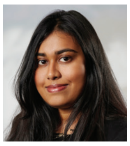

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