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REAL ESTATE

NOMINATION CLAUSES AND TAX IMPLICATIONS

A nomination clause in a sale agreement of property often seems like a very good idea in complex business structures but unwanted consequences may stem from the Transfer Duty Act 40 of 1949 ('Act'). Notwithstanding the VAT status of an entity, it is possible that a sale of property transaction is subject to transfer duty and not VAT, due to either the seller not being a registered VAT-vendor, or due to the sale of property not being in the seller's ordinary course of business, thus attracting transfer duty. It is within this context that we shall have a look at some of the unwanted consequences and possible solutions arising from the use of nomination clauses.

An agent's duty to disclose

Section 16 of the Act states that:

> *"(1) Where property is sold to a person who is acting as an agent for some other person, the person so acting as agent shall disclose to the seller or his or her agent the name and address of the principal for whom he or she acts, and furnish the seller or his or her agent with a copy of the documents appointing him or her as agent-*
>
> *(i) if the sale is by auction, on the day of acceptance by the auctioneer of his or her offer; or*
>
> *(ii) if the sale is otherwise than by auction, on the day of conclusion of the agreement of sale.*
>
> *(2) Any person who has been appointed as an agent, but fails to furnish the documents contemplated in subsection (1) and the name of the person on whose behalf he or she is acting to the seller or his or her agent on the date specified in subsection (1) shall, for the purpose of the payment of the duty payable in respect of the acquisition of the property in question, be presumed, unless the contrary is proved, to have acquired the property for himself or herself."*

Presumption that the agent is the purchaser

Section 16 of the Act effectively forces an agent to make a nomination by midnight on the same day of the sale, by disclosing details and providing documents of the principal to the seller, failing which the property in question is presumed to have been acquired by the person who entered into the sale agreement of property.

The implication of this presumption is that if an agent is acting on behalf of a principal with the ultimate intention to transfer the property to the principal (ie a company, trust or other entity), there would be two transactions for transfer duty purposes. The first being to the agent (first purchaser) and the second being to the principal that is now seen as a successive purchaser and not an alternative purchaser. However, this is a rebuttable presumption, which means that the agent and principal bear the burden of proving to the Commissioner of the South African Revenue Service that the requirements in s16 of the Act have been met, and that consequently, the presumption is incorrect.

Nominating a principal

The three essentials for a sale agreement of property are: the clear identification of the property, an agreed purchase price and the identities of the parties. Accordingly, once an agent has signed and presuming that the other two elements have been met, the sale agreement has effectively been concluded and is binding on the parties thereto. A verbal nomination will not have an effect on the sale agreement of property as more fully discussed in *Du Toit Group (Pty) Ltd v Van Breda and Others* (3128/08) [2009] ZAWCHC 152 (16 October 2009).

The common law prescribes that the principal must exist when the agent concludes the juristic act. Thus, a party cannot be said to be an agent if the ultimate purchaser is found only after the conclusion of the sale agreement. Therefore it is not permitted to nominate a trust as the principal unless the trust is already registered. It is however possible to enter into a sale agreement of property with a company in the process of formation, so long as the board of directors ratify the agreement. Such an agreement is seen as a pre-incorporation contract and should the board of directors choose not to ratify the agreement, the person who entered into the pre-incorporation contract is personally liable on a joint and several basis with "any other such person" (if there is another person) for any liabilities created while acting in this capacity. If the board of directors fails to take any action within three months from the date of formation, the company is deemed to have ratified the pre-incorporation contract.

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When does liability for transfer duty arise?

In terms of s5(2)(a) of the Act, "if a transaction whereby property has been acquired, is, before registration of the acquisition in a deeds registry, cancelled, or dissolved by the operation of a resolutive condition, duty shall be payable only on that part of the consideration which has been or is paid to and retained by the seller and on any consideration payable by the buyer for or in respect of the cancellation thereof, provided that on cancellation or dissolution of that transaction, such property completely reverts to the seller and the original buyer has relinquished all rights and has not received nor will receive any consideration arising from such cancellation or dissolution." This means that notwithstanding the termination of a sale agreement, transfer duty is still payable on that portion of consideration which has been paid to and retained by the seller.

Escaping the unwanted consequences of nomination clauses

In order to overcome the possibility of "double-tax", a substitution clause can be used instead of a nomination clause. Such a clause provides that should the principal wish to enter into the sale agreement of property, the sale agreement of property is to be cancelled by written request of the purchaser (agent) before the purchase price is secured and on condition there is no default of any obligation by the purchaser. In such instances, s5(2)(a) will also be applicable. To avoid any delays the conclusion of the new sale agreement must coincide with the cancellation of the previous sale agreement.

Where an agreement refers to a cession and assignment or benefit for a third party clause, double-tax consequences are still possible. In these circumstances we would suggest the insertion of a substitution clause, subject to the above considerations.

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