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TAX & EXCHANGE CONTROL ALERT

IN THIS ISSUE

BUYING A HOUSE AND PAYING TRANSFER DUTY – SEPARATE RIGHTS EQUALS SEPARATE OBLIGATIONS

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AMENDMENT IN RESPECT OF FOREIGN EMPLOYMENT INCOME EXEMPTION

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CLIFFE DEKKER HOFMEYR

BUYING A HOUSE AND PAYING TRANSFER DUTY – SEPARATE RIGHTS EQUALS SEPARATE OBLIGATIONS

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SARS argued that the written sale agreement failed to make provision for separate considerations of the two distinct rights and as such deemed the contract indivisible.

Facts

The Taxpayers are life partners and entered into a written sale agreement on 7 August 2007, in terms of which they purchased a sectional title unit together with two parking bays (Property) from the seller. In terms of the sale agreement, Mr B would acquire the right of "habitatio" and Ms A would acquire the "bare dominium" for a total purchase price of R4.2 million. The agreement also stated that the Taxpayers would acquire "the rights of habitatio and the bare dominium respectively but jointly". The Taxpayers each filed separate transfer duty declarations (TD2 declaration) with SARS. Ms A indicated in her TD2 declaration form that transfer duty was payable on an amount of R2,869,103.40 and Mr B indicated an amount of R1,330,896.60, which, together, totaled R4.2 million. Based on these declarations, the Taxpayers owed transfer duty in the amount of R225,998.49, but SARS argued that transfer duty must be calculated on the total purchase price of R4.2 million, in which case the transfer duty would be R281,000 and about R55,000 more than the transfer duty calculated by the Taxpayers. The Taxpayers paid the amount of R281,000, but appealed against SARS's decision.

Arguments raised by the parties

The main basis of the Taxpayers' appeal was that on a proper reading of the sale agreement, they acquired two separate real rights, namely the right to habitatio and the right to bare dominium, and therefore transfer duty should be payable on two distinct and divisible transactions and not on the full amount of R4.2 million recorded in the sale agreement. Mr B testified that the sole reason for structuring the transaction in the manner which they did was to protect the Property against his potential creditors, who could hold him personally liable as he was a director of a law firm.

On the other hand, SARS argued that the written sale agreement failed to make provision for separate considerations of the two distinct rights and as such deemed the contract indivisible. It argued that more than one "property" was acquired in one transaction with one composite consideration being the amount of R4.2 million. SARS conceded that if the amounts reflected in the TD2 declarations had been apportioned in the agreement, the transfer duty that was payable according to the Taxpayers would have been correct.

Judgments

The Tax Court first considered the legal scheme of the Transfer Duty Act, No 40 of 1949 (Act). Section 1 of the Act defines "property" as land in South Africa and any fixtures thereon, including any real right in land, but excluding any right under a mortgage bond or a lease of property other than a lease for the right to minerals or to mine minerals. Section 2 of the Act states that transfer duty is levied on the value of

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CONTINUED

The Tax Court therefore upheld the Taxpayers' appeal and found that they only had to pay transfer duty as calculated in their TD2 declarations.

any property acquired by any person after the date of commencement of the Act and that the value must be determined with reference to s5, s6 and s7 of the Act. Section 3(1) of the Act states that transfer duty is payable by the purchaser within six months from the date of acquisition. With regard to determining the value of the Property, the Tax Court referred to s5 of the Act, which states that where consideration is payable by the purchaser, the transfer duty is payable on the amount of the consideration.

The Tax Court held that to determine whether a contract, as in the present instance, is divisible or not for the purpose of paying transfer duty, it is necessary to interpret the contract. With reference to previous case law on the issue, the Tax Court held that one must look at whether the contract provides for separate considerations (amounts). Where the parties have not divided the consideration and there is nothing to show what consideration should go to each portion, the contract would normally be regarded as indivisible. The Tax Court relied on the decision in *Natal Joint Municipal Pension Fund v Endumeni Municipality* 2012 (4) SA 593 (SCA), where the Supreme Court of Appeal held, amongst other things, that in interpreting a contract one must look at the language of the provision, read in context and having regard to the purpose of the provision, and the background to the preparation and production of the document. The Tax Court rejected SARS's argument that the sale of the rights of habitatio and bare dominium in the contract were indivisible and found it to be misguided. It held that when viewed objectively and having regard to the purpose of the provision and the background to the preparation of the document, two different persons acquired two different forms of property distinct from each other. This was despite the agreement referring to one composite amount of R4.2 million. It was not in dispute that the value of the right to habitatio was correctly computed by the parties.

SARS also tried to argue that the agreement was indivisible because the Taxpayers would have to act together if they wanted to cancel the agreement and because they could only sue for the composite purchase price (R4.2 million) and not for two separate considerations. The Tax Court rejected this argument and held that the purchase price can only be regarded as a guideline for the purposes of paying transfer duty. Furthermore, it held that if either of the purchasers wanted to sue the seller to enforce the provisions of the agreement, they could only sue the seller for the rights to which they were entitled in terms of the agreement. If the seller wanted to sue Ms A or Mr B, it could only claim the proportionate amount, which each of them stipulated in their TD2 declarations.

The Tax Court therefore upheld the Taxpayers' appeal and found that they only had to pay transfer duty as calculated in their TD2 declarations. It also awarded costs in their favour.

Louis Botha

Who's Who Legal

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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AMENDMENT IN RESPECT OF FOREIGN EMPLOYMENT INCOME EXEMPTION

In terms of the Bill, the Act will be amended to allow the first R1 million of foreign remuneration in respect of a year of assessment to be exempt from tax in South Africa.

Alongside the 2017 Medium Term Budget Policy Statements, National Treasury released the revised version of the Taxation Laws Amendment Bill 27 of 2017 (Bill) on 25 October 2017. The Bill contains those proposals that were accepted by National Treasury and which were communicated to Parliament's Standing Committee on Finance, during the report-back hearings.

Treasury stated that the introduction of the capped exemption should alleviate the increased taxation costs associated with employing South Africans abroad.

Initially in the draft Taxation Laws Amendment Bill, 2017 (Draft Bill), the proposal was to repeal the exemption on foreign employment income in terms of s10(1)(o)(ii) of the Income Tax Act, No 58 of 1962 (Act). National Treasury (Treasury) thereafter engaged in an extensive consultation process on the proposed amendments with various stakeholders.

In terms of the Bill, the Act will be amended to allow the first R1 million of foreign remuneration in respect of a year of assessment to be exempt from tax in South Africa if the person is outside of South Africa for more than 183 days and for a continuous period of longer than 60 days during a 12 month period. In its Draft Response Document dated 14 September 2017, Treasury stated that:

> The exemption threshold should reduce the impact of the amendment for lower to middle class South African tax residents who are earning remuneration abroad. The effect of the exemption will also be that South African tax residents in high income tax countries are unlikely to be required to pay any additional top up payments to SARS.

This was in response to comments that the tax will have a severely negative impact on finances and remittances to South Africa, especially for those on relatively lower incomes and that it would increase the cost of employment of South African tax residents who work abroad. Treasury stated that the introduction of the capped exemption should alleviate the increased taxation costs associated with employing South Africans abroad. One should note that the balance of the remuneration, being the amount in excess of R1 million, will be taxed in South Africa irrespective of the days spent outside of South Africa.

There were also a few other comments raised by stakeholders and addressed by Treasury during the consultation process:

- One of the comments received was that the cost of living in foreign countries is higher than in South Africa, and should be taken into account in the design of the tax. This comment was taken into account by Treasury in introducing the R1 million exemption, but Treasury also stated that the tax system does not usually cater for differences in the cost of living.

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.

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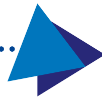
AMENDMENT IN RESPECT OF FOREIGN EMPLOYMENT INCOME EXEMPTION

CONTINUED

The Bill states that the amendment will come into operation on 1 March 2020 and will apply in respect of years of assessment commencing on or after that date.

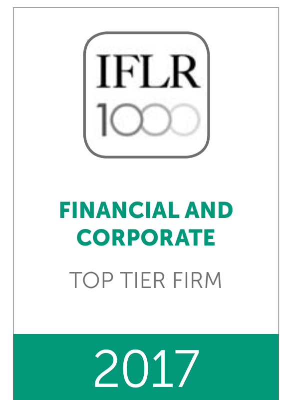


- Residency was also a big discussion point with views expressed that the amendment would lead to accelerated formal emigration from South Africa or breaking of residency. In response, Treasury reiterated that the proposal is not related to citizenship and should not lead to South Africans giving up their passports as the application rests solely on tax residency. However, it added that South African tax residents who left the country many years ago are encouraged to formalise their tax residency status.
- Another comment received was that the amendment will result in cash flow problems as the foreign tax credit (s6quat) can only be claimed on assessment. Treasury rejected this comment as employers are currently able to apply for a hardship directive from SARS, which would effectively take foreign employment taxes into account in determining employees' tax (PAYE).

Interestingly, in the Draft Bill released on 19 July 2017, Treasury cited the unequal treatment that had been created between public and private sector employees, as one of the reasons for the initially proposed repeal of s10(1)(o)(ii) (see our Tax and Exchange Control Alert dated 20 July 2017 – Foreign employment income – is this the end?). However, the revised amendment does not do away with this unequal treatment as the entire s10(1)(o)(ii) will still not apply to public sector employees.

The Bill states that the amendment will come into operation on 1 March 2020 and will apply in respect of years of assessment commencing on or after that date. Treasury has granted taxpayers leniency, as the Draft Bill proposed that the amendment come into effect on 1 March 2019. Treasury stated that this will also allow individuals time to adjust either their contracts or their circumstances and to finalise or formalise their tax residency status.

Nandipha Mzizi, overseen by Louis Botha



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