# TAX & EXCHANGE CONTROL
## ALERT

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# Here we go again: The High Court gets a turn to weigh in on a protracted dispute

In the recent judgment of *SACS (Louis Trichardt) (Pty) Ltd v Commissioner for the South African Revenue Service* (Case No 40420/2020 and 17064/2021), which was handed down on 14 July 2022, the High Court was faced with two applications brought by the taxpayer after a litany of prior litigation spanning the course of over a decade.

## FACTS

The litigious history between the taxpayer in this case and the Commissioner for the South African Revenue Service (SARS) is protracted and cumbersome to wade through. The first dispute between the parties arose in 2007, in relation to the taxpayer's 2002–2004 years of assessment (YOAs), and subsequent disputes have arisen in respect of the taxpayer's 2005–2012 YOAs and its 2013–2017 YOAs.

The 2002–2004 YOAs dispute was brought to finality in the Supreme Court of Appeal (SCA) in 2014, after which the taxpayer requested that SARS compute its tax liabilities for the 2005–2012 YOAs in accordance with the outcome. However, SARS declined to do so on the basis that it had reconsidered the facts and relevant legal principles, as a consequence of which SARS included a substantial recoupment in the taxpayer's tax computation. Thus, the dispute in respect of the 2005–2012 YOAs arose.

Before this dispute was finalised, the taxpayer had to submit its tax returns for the 2013 and 2014 YOAs. This was done by adopting the same approach as was taken by the taxpayer in respect of the 2005–2012 YOAs. SARS rejected this approach and the parties engaged in dispute resolution proceedings in respect of the taxpayer's 2013 and 2014 YOAs.

In October 2016, the taxpayer and SARS entered into an agreement (Agreement) to extend the prescription period for the assessment of all tax liabilities for the 2013 and 2014 YOAs (in terms of section 99(2)(c) of the Tax Administration Act 28 of 2011 (TAA)) until the dispute relating to the 2005–2012 YOAs was finally determined. Importantly, the Agreement:

- noted that the outcome of the 2005–2012 YOA dispute (the "*Final Decision*" as referenced in the Agreement) would have an impact on the tax liability determination of subsequent YOAs: and
- the Final Decision would be given effect to by both parties in respect of the 2013–2014 YOAs.

The parties proceeded to litigate the 2005–2012 YOAs dispute. However, on the basis that SARS continuously failed to adhere to the prescribed deadlines, the taxpayer applied for default judgment in the tax court in 2017. SARS again failed to timeously submit the necessary documents in respect of the application for default judgment and as such, judgment was granted in favour of the taxpayer. This decision was not taken on appeal by SARS. Barring a few issues pertaining to the payment of interest by SARS to the taxpayer, the 2005–2012 dispute had been finalised.

The taxpayer then relied on the to attempt to persuade SARS that the outcome of the 2005–2012 dispute (being the Final Decision, which favoured the taxpayer) was to be applied in respect of the 2013–2014 YOAs. SARS declined,

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contending that the outcome of the 2005–2012 dispute did not constitute a "*Final Decision*" that would apply to the subsequent YOAs, as the merits of the dispute had not been judicially determined.

A year later, SARS extended its latest audit to include the taxpayer's 2013–2017 YOAs. The issues in dispute remained unchanged save for the additional YOAs that came under review.

Substantial litigation took place between the parties thereafter, including multiple applications by the taxpayer for default judgment on the basis that SARS failed to adhere to the prescribed tax court rules' deadlines.

In October 2020, another agreement (Agreement 2) to extend the prescription period in respect of the taxpayer's 2013–2016 YOAs was orally agreed to between the parties. However, this agreement was only signed by SARS in November 2020, whereas it was specified in the agreement that it had to be signed by October 2020. The taxpayer thus contended that Agreement 2 was invalid and that the 2013–2016 YOAs had prescribed, therefore precluding SARS from raising additional assessments in respect thereof.

Two applications were brought by the taxpayer in the present case.

## JUDGMENT

*The first application*

The first application brought by the taxpayer sought an order precluding SARS from assessing the taxpayer's tax liabilities for the 2013–2016 YOAs on a basis different to the outcome pertaining to the 2005–2012 YOAs.

As the 2005–2012 YOAs default judgment had not been taken on appeal by SARS, the taxpayer contended that the outcome thereof constituted a "*Final Decision*" in terms of the Agreement and that the parties were thus bound by that decision in respect of the subsequent YOAs. To this end, the taxpayer referred to section 100(1)(f) of the TAA, which provides that a final decision in respect of an assessment exists when "*the matter has been determined by the tax court and there is no right of further appeal*".

SARS, however, maintained its argument that the default judgment only addressed the issue of SARS' application for condonation for its failure to adhere to the tax court rules' time periods and that the merits of the dispute between the parties was not considered or pronounced on by the court in that case.

In the present matter, the court took the view that the argument advanced by the taxpayer would pass muster only to the extent that the default judgment referred to by it constituted a final pronouncement on the substantive issues comprising the

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dispute between the parties. To this end, the court highlighted that the default judgment specifically stated that in that case, the court was "*not determining the merits of the disputed assessments*" because it had not been placed in a position to decide whether or not the prospects of success of SARS' case were good.

The court in the present case then reiterated that:

> *"The key component of the context of the [Agreement] was a joint recognition by the parties that their respective understandings of the interpretations and applications of [the relevant sections] of the ITA were not the same, and that the only way to resolve their differences was for the court to make a determination on these issues."*

The purpose and intention behind the Agreement was thus to allow the parties to seek a judgment from the tax court clarifying which of the understandings of the parties was correct. As such, even though the tax court's default judgment had not been appealed by SARS, the merits of the parties' respective cases remained alive and awaited judicial pronouncement.

Ultimately, the court concluded that only a pronouncement on the merits of the matter would constitute a "*Final Decision*" in terms of the Agreement that SARS would be bound to give effect to in respect of the taxpayer's subsequent YOAs.

The taxpayer raised a further argument in respect of a decision taken by SARS in 2007, whereby the tax treatment championed by the taxpayer in respect of the 2013–2014 YOAs dispute had been granted by SARS in respect of the taxpayers' 2001–2004 YOAs. In response, the court held as follows:

> *"It is correct that the exemption was granted in the 2001 to 2004 tax computations. But this does not mean that SARS has to grant the exemptions thereafter. It is clear from a comparison of what SARS said in its assessment for the 2001 to 2004 tax years – allowing the exemption – and what it said in its assessment for the 2005 to 2012 tax years – disallowing the exemption – that upon further analysis and reflection it had reassessed its understanding. There is nothing in law precluding it from doing so."*

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Ultimately, it was the court's finding that if SARS is of the view that its previous application or understanding of a tax provision was incorrect, it is not obliged to replicate that error in future assessments.

The court therefore dismissed the first application with costs.

*The second application*

In the second application, the taxpayer sought an order precluding SARS from raising additional assessments in respect of the 2013–2016 YOAs on the basis that Agreement 2 had not been properly executed in accordance with the requisite formalities and as such, these YOAs had prescribed.

It was common cause that Agreement 2 was only formally executed by SARS in November 2020, whereas the agreement had to be concluded before or on 16 October 2020 in order to extend the period of prescription (on the basis that the previous extension would have lapsed on 16 October 2020).

In terms of section 99(1)(c) of the TAA, the only way to extend the limitations period in respect of any YOA is for the parties to agree to do so. It was the taxpayer's argument that since Agreement 2 was only signed by SARS in November 2020, the parties had not agreed to extend the prescription period. On the other hand, SARS contended that prior to 16 October 2020, the parties had orally agreed to extend the prescription period and that the execution of Agreement 2 in November 2020 was merely a confirmation of what had been agreed.

Section 99(1)(c) of the TAA does not prescribe the method by which an extension should be agreed upon between SARS and a taxpayer. Of particular importance is that this section does not preclude an oral agreement extending the limitations period.

In light of the evidence presented by SARS that an oral agreement had been reached between the parties prior to 16 October 2020, the court held that the parties had in fact come to an agreement to extend the period of prescription in terms of the 2013–2016 YOAs such that the provisions of section 99(1)(c) of the TAA had been complied with.

The court therefore dismissed the second application with costs.

**LOUISE KOTZE**

# Rise of the electrical vehicle – A discussion on tax incentives and related tax considerations

**Recently, the South African private sector (and South Africa in general) has been boosted by the President's announcement regarding further relaxations to the existing legal framework applicable to private renewable energy generation.**

Aside from addressing the current electricity supply shortfall, this will also hopefully assist in boosting South Africa's electric vehicle market, including the infrastructure needed to increase the roll-out of electric vehicles and charging stations, with the ultimate goal of this taking South Africa closer to its goal of getting to net zero carbon emissions. At the same time, it is important to understand how tax laws encourage or discourage the use and purchase of electric vehicles.

It is a well-accepted principle that taxes can achieve several different purposes including increasing revenue for governments but also importantly encouraging or prohibiting certain behaviour. The Carbon Tax Policy published by National Treasury in May 2013 specifically recognised the important role that carbon taxes play in internalising the external costs of climate change and creating the correct incentives to stimulate changes in the behaviour of producers and consumers.

This article briefly discusses some of the potential applicable South African taxes that one should consider with reference to potentially changing behaviour and pursuing e-mobility more vigorously in light of some of the existing environmental taxes imposed on vehicles that cause carbon emissions, such as those using petrol and diesel.

## BRIEF OVERVIEW OF ENVIRONMENTAL TAXES ON PETROL AND DIESEL MOTOR VEHICLES

### *Environmental levy on CO2 emissions on newly manufactured motor vehicles*

In terms of Schedule 1 Part 3D of South Africa's Customs and Excise Act 91 of 1964 (C&E Act), an environmental levy is payable on certain locally manufactured motor vehicles which are manufactured in a a special *ad valorem* manufacturing warehouse. Specifically, the environmental levy is imposed on vehicles, which use result in CO2 emissions. The environmental levy is imposed based on the CO2 emission level of the locally manufactured vehicle. While the customs legislation classifies vehicles with reference to the environmental levy item number and tariff subheading in which the vehicle falls, there are broadly speaking two categories of vehicles that are affected by the levy:

- Vehicles described as *"Other, double-cab, of a vehicle mass not exceeding 2 000 kg or a G.V.M. not exceeding 3 500 kg, or of a mass not exceeding 1 600 kg or a G.V.M. not exceeding 3 500 kg per chassis fitted"*. As of 1 April 2022, the environmental levy imposed on these vehicles is R176.00 per g/km CO2 emissions exceeding 175g/km. In other words, the environmental levy is only payable if the vehicle's CO2 emissions exceed 175g/km; and

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- All vehicles falling under the general description *"Other"*, which are subject to an environmental levy of R132.00 per g/km CO2 emissions exceeding 95g/km. In other words, the environmental levy is only payable if the vehicle's CO2 emissions exceed 95g/km.

*Carbon tax on petrol- and diesel-powered motor vehicles*

When the Carbon Tax Act 15 of 2019 was introduced in 2019, it made provision for the imposition of carbon tax on GHG (greenhouse gas) emissions arising from the use of petrol- and diesel-powered motor vehicles. However, in light of the fuel levy dispensation that already existed at the time under the C&E Act, it was decided that GHG emissions arising from the use of petrol and diesel in motor vehicles would be taxed through the fuel levy dispensation, by providing for a carbon fuel levy on petrol and diesel. This levy was increased to 9c/l for petrol and 10c/l for diesel from 6 April 2022 and is payable in addition to the general fuel levy and the road accident fund levy. In light of this approach, the formula in the Carbon Tax Act to calculate one's carbon tax liability (including from the use of petrol and diesel) was amended to prevent double taxation. In other words, carbon tax arising from the use of petrol and diesel in motor vehicles is only taxed under the fuel levy dispensation and not also under the Carbon Tax Act. To ensure fairness, the carbon fuel levy is also increased annually at by the same percentage as the carbon tax rate at which GHG emissions are taxed under the Carbon Tax Act.

## PETROL AND DIESEL MOTOR VEHICLES TO BE SCALED DOWN AND EVENTUALLY BANNED IN THE UK AND EU

Two of South Africa's (and Africa's) largest trading partners (particularly for motor vehicles) include the United Kingdom (UK) and Europe (EU). In April 2022, the UK Department of Transport published a paper titled: *"Outcome and government response to the green paper on a New Road Vehicle CO2 Emissions Regulatory Framework for the UK"* (UK Paper) which, amongst others, confirmed that the UK Government will introduce a zero-emission vehicle mandate setting targets requiring a percentage of manufacturers' new car and van sales to be zero emission each year from 2024.

Furthermore, the UK Government announced that it will continue to regulate the CO2 emissions of new non-zero emission cars and vans to limit their emissions until all new sales are zero emission at the exhaust. If not fully zero emission, it was stated that all new cars and vans sold between 2030 and 2035 must have significant zero emission capability (SZEC). The European Commission has similarly implemented various regulations and intends cutting carbon emissions from motor vehicles by 55% by 2030 with a 100% target by 2035.

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The impact of these measures will have a profound influence on Africa and South Africa as exports to those markets will be significantly impacted unless the local market starts to embrace the move towards *"net-zero"* and commences producing electric vehicles.

## SECTION 12R – SPECIAL ECONOMIC ZONE

In advancing its efforts towards promoting economic growth and industrial development, the South African government, via the Department of Trade and Industry, has established various special economic zones (SEZs) within designated areas in South Africa. Importantly there are a number of specific tax incentives including income tax, value-added tax (VAT), customs & excise and employees' tax incentives that a *"qualifying company"* in an SEZ (as defined), could potentially benefit from.

One of the most beneficial tax incentives is that companies carrying on business within certain SEZs are subject to an annual income tax rate of 15% which is a significant benefit compared to the ordinary corporate income tax rate of 27%. In addition, qualifying companies can claim a special capital allowance of 10% per year on the costs of any new or unused building or improvement to such building. These incentives are provided for in sections 12R and 12S of the Income Tax Act, 58 of 1962 (ITA). One should appreciate that only companies operating in an SEZ approved by the Minister of Finance for purposes of section 12R can benefit from the incentive. Currently, only some of South Africa's SEZs are approved for purposes of section 12R.

Importantly, however, there are various requirements for an entity to commence business in an SEZ and benefit from the favourable tax incentives. Section 12R of the ITA sets out the various requirements, qualifications and exclusions. The definition of *"qualifying company"* in section 12R(1) is particularly instructive and requires that the company must be tax resident in South Africa and conducts an approved trade in the SEZ. Furthermore, not less than 90% of the income of that company must be derived from the trade carried on in the SEZ itself.

Para (e) of the definition of *"qualifying company"* furthermore requires that the trade carried on by the company must be either:

- Carried on before 1 January 2013 in a location that is subsequently approved as an SEZ in terms of section 12R(3) of the ITA; or

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- Commenced on or after 1 January 2013 in a location that is approved or subsequently approved as an SEZ in terms of section 12R(3) of the ITA and that trade was not previously carried on by that company (or a connected person in relation to that company) in South Africa; or
- Commenced on or after 1 January 2013 in a location that is approved or subsequently approved as an SEZ in terms of section 12R(3) of the ITA and that trade, either:
  - comprises the production of goods not previously produced by that company or any connected person in relation to that company in South Africa; or
  - utilises the use of new technology in that company's production processes; or
  - represents an increase in the production capacity of that company in South Africa.

Motor vehicle manufacturers (and their suppliers) should consider the section 12R SEZ tax regime and its applicability to the production of electric vehicles in South Africa given that such production of electric vehicles is either non-existent or negligible currently. The commercial impact of these incentives is very favourable, and it could be used as a key tool to adapt to the growing global shift towards net-zero motor vehicles.

The Tshwane Automotive Special Economic Zone (TASEZ) is located in South Africa's capital city. Although it is not currently an approved SEZ for purposes of section 12R, there is a possibility that it could be approved for this purpose in future. Therefore, it could certainly be considered a launching pad for manufacturers to commence producing electric vehicles within the precinct. At the very least, manufacturers operating in TASEZ can automatically benefit from the preferential value-added tax (VAT) provisions applicable to companies operating in SEZ's, with the section 12R income tax incentive also becoming available to them if the Minister of Finance approves TASEZ for purposes of section 12R. The sunset date for the section 12R incentive was also recently extended to 31 December 2030.

### SOUTH AFRICA'S POTENTIAL NEW *"DRIVING TAX"*

The South African National Department of Transport recently published the White Paper on National Transport Policy which, amongst others, proposed further investigations of additional and innovative funding strategies for traffic management functions. It was announced that a traffic-management levy to vehicle licence fees and fuel sales would be investigated. Interestingly, this potential new proposed levy may not impact electric vehicles especially if it is introduced with reference to fuel sales which could further encourage the uptake of electric vehicles in South Africa.

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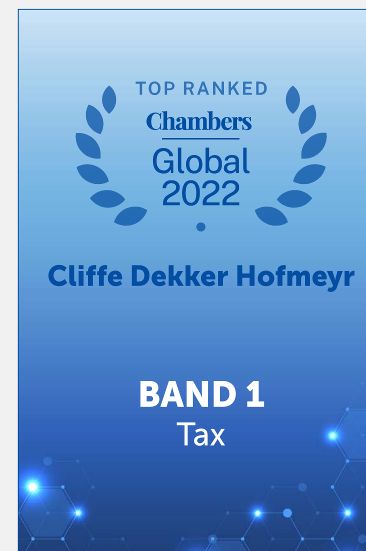
### FURTHER CARBON TAX PROPOSALS TO POTENTIALLY INCENTIVISE EV UPTAKE

In addition to the above, manufacturers and users of petrol and diesel vehicles must keep in mind that the taxes imposed as a result of the use of such vehicles is only likely to increase. This appears evident from the announcements in the recent 2022 Draft Taxation Laws Amendment Bill, which proposes, amongst other things, substantial increases in the annual carbon tax rate going forward. The likely effect of this is that each person in the petrol/diesel vehicle manufacturing supply chain, including the end-user, will potentially have to pay more for the vehicle and for the fuel necessary to use such a vehicle.

(This article is based on the South African section of CDH's E-Mobility In Africa publication, which is available here.)

JEROME BRINK AND LOUIS BOTHA



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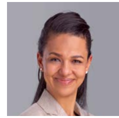

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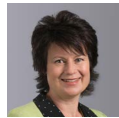

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Our BBBEE verification is one of several components of our transformation strategy and we continue to seek ways of improving it in a meaningful manner.

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