Dr John Rentalittle is a retired university lecturer. His personal home, which includes a separate ‘granny flat’ (consisting of a bedroom, bathroom and living room), is situated near the University of Pretoria campus. In his 2013 year of assessment John built four low-cost residential units on the same property. This was the maximum number of units for which the local municipality gave permission. Each low-cost residential unit was erected at a cost of R195 000. On completion the units were let to students at a market-related rental.

John’s son, Richard, aged 22 years and a full-time student, occupies the ‘granny flat’. In the past Richard did not pay rental for this accommodation.

In order to qualify for the section 13sex capital allowance of the Income Tax Act, John entered into the following agreement with Richard:

Richard would no longer occupy the ‘granny flat’ rent free. Instead, he would rent it at a market-related rental of R1 500 per month. Since this meant that Richard had additional expenditure (the rental) of R1 500 per month, John increased the living allowance he grants Richard each month by R1 500.

As a result of this agreement John then owned five residential units in South Africa (the four being let to students and the ‘granny flat’ being let to Richard) which are used by him for the purpose of a trade carried on by him.

The Commissioner for the South African Revenue Service is of the opinion that the agreement between John and his son is an ‘impermissible avoidance arrangement’ in that he gives Richard an extra R1 500 per month, and then immediately recovers this same amount as rental from Richard.