Dizzy Chemicals (Pty) Ltd (‘Dizzy’) is a resident of the Republic of South Africa. It is a registered value-added tax (VAT) vendor with a 30 June financial year end.

Dizzy manufactures a variety of food colourants and additives. It manufactures these additives from raw materials sourced from within South Africa and abroad. It converts the raw materials to amongst others the trademark additive, TruBlu, in its factory situated near Port Elizabeth.

TruBlu is its biggest seller as it is made from natural ingredients only. It is sold in powder form and this powder must be carefully packaged to preserve the vivid shade of blue that customers desire. Excessive exposure to sunlight can cause the colour to fade. The powder also has a tendency to absorb moisture, which then impacts on its weight.

TruBlu is sold to customers throughout the world. Dizzy refuses to bear the transport risk of its exports and therefore ships all its goods free on board. As a courtesy to its customers, Dizzy will make the shipping arrangements, and it then bills its customers for the shipping costs.

When goods are exported they are accompanied by a goods delivery note. Upon arrival, customers send samples of the TruBlu they have received to a testing facility agreed to in the sales agreement. The testing facility performs two tests:

- The first test is to measure the shade of blue of the additive; and
- The second test is to determine its moisture content.

The results of these two tests are compared to ranges agreed to by Dizzy and its customer. If the results are within the required range, the final price of the product is determined by multiplying the weight of the product by the agreed price per kilogram of the trademark additive. Dizzy will then issue an invoice for this final price.

If the results fall outside the accepted range – in other words, if the powder is either too wet or the colour has faded too much – the customer is entitled to return the powder to Dizzy. Alternatively, the customer has the option of accepting the powder at a reduced price. This reduced price is negotiated at that time and is dependent on the extent of the degradation.

During Dizzy’s 2013 year of assessment it had amongst others the following transactions:

<table>
<thead>
<tr>
<th>Transaction 1</th>
</tr>
</thead>
<tbody>
<tr>
<td>On 1 June 2013 Dizzy shipped TruBlu at an expected selling price of R1 500 000 (1 000 kg at R1 500 per kg) to a customer in New Zealand. This TruBlu had cost Dizzy R800 000 (excluding VAT) to produce. All raw material purchases and production costs had been incurred during its 2013 year of assessment. The ship transporting this powder was delayed due to bad weather, and only arrived in New Zealand on 2 July 2013.</td>
</tr>
<tr>
<td>The agreed-upon testing procedures were completed on 14 July 2013. The shipping delay had a negative effect on the TruBlu powder, and its colour had faded to a level below the accepted range. Furthermore, the weight of the product had increased in transit to 1 200 kg due to additional moisture absorbed during the trip. Because the customer was desperate for the TruBlu, it agreed to purchase the powder for a total price of R600 000. After negotiations, an invoice was issued on 31 July 2013 at this price.</td>
</tr>
</tbody>
</table>
Transaction 2

Sweety Pie Ltd (‘Sweety Pie’), a loyal local customer of Dizzy, is introducing a new range of sweets that requires a bright red additive. Although Dizzy does not usually produce this additive, the company agreed to produce a red additive as a special order for Sweety Pie. Sweety Pie advanced, as a deposit, R400 000 of the expected invoice price to Dizzy before it commenced work on the new additive. The two parties agreed that this amount would be used to fund the production of the special red additive. Dizzy received the advance payment on 14 June 2013 and used the advance of R400 000 as well as R50 000 of its own funds to purchase the required raw materials on 3 July 2013.

Production commenced on 10 July 2013 and Dizzy delivered the additive to Sweety Pie on 31 July 2013. An invoice for R615 600 (including VAT) was sent to Sweety Pie on this date.

Transaction 3

Dizzy disposed of some of its shipping containers to Joe Shipping (Pty) Ltd (‘Joe Shipping’). These containers weighed 20 tonnes in total. Dizzy had originally paid R240 000 (excluding VAT) for the containers on 1 July 2005. The Commissioner of the South African Revenue Service agreed to a wear and tear allowance on the shipping containers calculated over a 12-year period.

Joe Shipping purchased the containers on 1 June 2013 and collected them from Dizzy on the same day. In terms of the sale agreement the price was based on the market price of scrap metal two months after delivery, that is, on 31 July 2013. On 1 June 2013 the market price of scrap metal was R1 700 per tonne (excluding VAT) and on 31 July 2013 the market price of scrap metal was R2 200 per tonne (excluding VAT).

Transaction 4

When collecting the shipping containers, the representative from Joe Shipping noticed a packaging machine that Dizzy was no longer using. This machine had been purchased for R150 000 (excluding VAT) ten years ago. Dizzy had been entitled to the section 11(e) allowance on this packaging machine and the write-off period was four years. Joe Shipping purchased this machine on the same conditions as the shipping containers (see transaction 3) on 1 June 2013. The machine, which weighed 5 tonnes, was collected by Joe Shipping at the same time as the shipping containers.

Transaction 5

Dizzy purchased and paid for raw materials from its offshore supplier, Cheapnnasty Plc (‘Cheapnnasty’). When Dizzy performed the usual spot checks on this purchase to ensure quality, it found that this particular shipment was contaminated with a pesticide. Dizzy had paid for this order in advance. Because Cheapnnasty refused to accept liability for the contaminated raw materials, Dizzy is suing Cheapnnasty for a refund. Dizzy appointed Mr Samson Shark, a local attorney, to recover the money. A first hearing of the matter took place on 1 May 2013, but it was postponed pending the outcome of independent laboratory testing of the raw materials. The results of these tests are only expected in January 2014. Dizzy paid Mr Shark a retaining fee of R300 000 (excluding VAT) before he commenced
work and he charges a daily rate of R10 000 (excluding VAT). He had invoiced Dizzy R30 000 (excluding VAT) for three days’ work by 30 June 2013. The balance of his fee is being kept in his attorney’s trust account. It is expected that Mr Shark will next invoice Dizzy only on 31 January 2014.

Transaction 6

Some of Dizzy’s employees failed to find accommodation near its factory due to the lack of residential accommodation in the area. A local builder, Mr Bob Bouwer, identified this as an opportunity and constructed a mixed-use building near Dizzy’s factory consisting of 150 one-bedroom flats as well as office space. Mr Bouwer then sold the property to Dizzy for R57 million (including VAT) on 1 June 2013. This price is made up as follows:

- Land: R5 700 000.
- Residential accommodation: R17 100 000.
- Commercial space: R34 200 000.

The Commissioner has ruled that 40% of the property is used for commercial purposes. Dizzy let the residential accommodation (all 150 flats) to its employees at a monthly market-related rental of R1 000 per flat from 1 June 2013. The finance and human resources divisions of Dizzy occupy the commercial space.

Because Dizzy did not have sufficient cash to pay for this property, Mr Bouwer agreed to accept equity shares in Dizzy instead of a cash payment. Dizzy accordingly issued 30 000 of its equity shares to Mr Bouwer on 1 June 2013. The market value of an equity share in Dizzy, as determined by an accredited valuation expert, was R1 900 at that date. In determining the value per share, the valuation expert took into account the value of Dizzy after the purchase of the property.

The accounting records of Mr Bouwer reflected the following items as costs of sales (excluding VAT):

<table>
<thead>
<tr>
<th>Item</th>
<th>R’000</th>
</tr>
</thead>
<tbody>
<tr>
<td>Building material</td>
<td>7 000</td>
</tr>
<tr>
<td>Salaries</td>
<td>13 000</td>
</tr>
<tr>
<td>Rental</td>
<td>8 000</td>
</tr>
<tr>
<td>Depreciation of machines and equipment</td>
<td>12 000</td>
</tr>
<tr>
<td>(tax allowances amounted to R15 million)</td>
<td></td>
</tr>
<tr>
<td>Other overheads (tax deductible)</td>
<td>5 000</td>
</tr>
<tr>
<td><strong>Total</strong></td>
<td>45 000</td>
</tr>
</tbody>
</table>

Transaction 7

On 1 July 2012 Dizzy advanced an interest-free loan of R180 000 to Ms Amber Fizzy (as a shareholder), a resident of the Republic. Ms Fizzy, who holds 25% of Dizzy’s equity shares, repaid the loan on 31 January 2013. The official interest rate for the period of the loan was 6%.