Call for comment
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South African Revenue Service
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Dear Sirs

VALUE ADDED TAX (VAT): SECTION 8(25) READ WITH SECTION 11(1)(e) AND SECTIONS 42 TO 47 OF THE INCOME TAX ACT

Set out below please find SAICA submission regarding the above.

1. **Provisions of section 8(25) are in conflict with provisions of section 11(1)(e)**

   1.1. Section 11(1)(e) of the Value Added Tax Act No. 89 of 1991 (the VAT Act) provides for the zero rating of a supply of an enterprise as a going concern provided the enterprise is involved in rendering an income-earning activity on the date of transfer thereof (and certain other requirements are met). In effect, the purchaser must be in a position to carry on the enterprise being acquired.

   1.2. To illustrate our concerns, if we apply these requirements to land and buildings where the purchaser is also the tenant, the consequences would be that:

   - The disposal of land and buildings to the tenant (purchaser) will not be a supply of an enterprise as a going concern as the purchaser in these circumstances is not in a position to carry on the business operated by the seller (the rental business). This view has been confirmed by SARS in a general ruling (paragraph 2.4.1(c) of VAT Practice Note No 14).

   - The disposal of the land and buildings will (subject to what is said below in relation to the possible application of section 8(25) of the VAT Act), therefore be subject to VAT and the seller would have to account for output VAT on the transfer of the land and buildings.
The tenant would however be entitled to an input tax credit for the VAT paid on the acquisition of the land and buildings.

1.3. In the alternative, section 8(25) of the VAT Act would apply in these circumstances. That section in essence provides that where any goods or services are supplied by a vendor to another vendor and certain income tax corporate rules in terms of the Income Tax Act No 58 of 1962 (the Act), including sections 45 and 47, are complied with, then the two vendors are deemed to be one and the same person for VAT purposes. As the two vendors are deemed to be one and the same, no taxable supply arises and the provisions of section 11(1)(e) do not therefore apply. While in both instances, no VAT would in effect have been payable, the consequences that flow in relation to any VAT incurred in relation to the relevant transaction are different.

1.4. Had the transaction been treated as a taxable supply as a zero-rated transaction (section 11(1)(e)), any VAT incurred in respect of the transaction would have constituted “input tax” and would have been deductible by the recipient.

1.5. However, should the transaction be treated as a non-supply, any VAT incurred in respect of the supply would not constitute “input tax” and would not be deductible by the recipient.

2. Recommendation

It is accordingly apparent that the provisions of section 8(25) of the VAT Act are not addressing circumstances where the provisions of section 11(1)(e) of the VAT Act would have applied to the transaction. It is our understanding that section 8(25) was introduced to accommodate those transactions which, while tax neutral from an income tax and capital gains tax (CGT) perspective in terms of the corporate rules, did not qualify as the supply of a going concern as contemplated in section 11(1)(e) of the VAT Act. The provisions of section 8(25) of the VAT Act should perhaps therefore have been limited to situations where section 18A - Adjustments in consequence of acquisition of going concern wholly or partly for purposes other than making taxable supplies; of the VAT Act will apply, as it is perhaps necessary to provide relief where section 18A applies.

3. Transfer duty

It is further noted that a transfer duty exemption in terms of section 9(1)(15A) of the Transfer Duty Act No 40 of 1949 (the Transfer Duty Act) is provided for in circumstances where section 8(25) of the VAT Act and section 42 of the Act apply.

In terms of section 9(1)(1) of the Transfer Duty Act, exemption from transfer duty is provided for when sections 44, 45 and 47 of the Act apply. However, no similar exemption from transfer duty applies in respect of transactions qualifying for income tax and CGT relief in terms of section 43 (share-for-share) and 46 (unbundling) of the Act.
Please do not hesitate to contact me should you require further information.

Yours faithfully

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