REPUBLIC OF SOUTH AFRICA

EXPLANATORY MEMORANDUM

ON THE

INCOME TAX BILL, 1977

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INTRODUCTION

The Bill fixes rates of normal tax payable by individuals and companies and introduces amendments to the Income Tax Act, 1962 (Act No. 58 of 1962), hereinafter referred to as the principal Act.

CLAUSE 1 AND THE SCHEDULE

Rates of Normal Tax.

Rates of normal tax are enacted by clause 1 and the Schedule to the Bill.

Individuals.

The rates for persons (other than companies) apply in respect of the year of assessment ending on 28 February 1978, or 30 June 1978, and are provided for in paragraph 1 (*a*) of the Schedule. To the basic tax determined in accordance with the tables in paragraph 1 (*a*) of the Schedule are added a surcharge of 10 per cent of such basic tax (see the proviso to paragraph 1 (*a*) of the Schedule) and a loan portion of 10 per cent of such basic tax (see paragraph 1 (*h*) of the Schedule). The surcharge and the loan portion are not payable where the basic tax is less than R150 nor in the case of a natural person who is over 60 years of age on the last day of the year of assessment and whose taxable income for that year is R5 000 or less (see the proviso to paragraph 1 (*a*) of the Schedule, paragraph 1 (*h*) of the Schedule and, as regards the loan portion, paragraph 2 (4) of the Fifth Schedule to the principal Act).

The basic tax is calculated on the taxable amount, i.e. the amount remaining after deducting from taxable income the abatements provided for in section 5A of the principal Act.

Companies.

The rates for companies apply in respect of years of assessment, i.e. financial years, ending during the twelve-month period from 1 April 1977 to 31 March 1978, and are provided for in paragraph 1 (*b*) to (*g*), inclusive, and paragraph 1 (*i*) of the Schedule. Those rates, which apply in respect of taxable income derived in South West Africa and taxable income derived in the Republic, are as follows:—

(*a*) Taxable income derived otherwise than from mining—

(i) where derived in South West Africa: 35 cents per R1 (paragraph 1 (*b*) (i) of the Schedule);

(ii) where derived elsewhere than in South West Africa, i.e. in the Republic: 40 cents per R1 (paragraph 1 (*b*) (ii) of the Schedule).

To the tax determined as above is added a surcharge of 7½ per cent of such tax (proviso to paragraph 1 (*b*)) and a loan portion of 15 per cent of such tax (paragraph 1 (*i*)).

(*b*) Taxable income derived from gold mining—

(i) by any mine other than a post-1966 gold mine: an amount determined in accordance with one of the formulae provided for in paragraph 1 (*c*) of the Schedule plus a surcharge (which

is not payable in the case of certain assisted gold mines) equal to 10 per cent of the said amount (third proviso to the said paragraph 1 (*c*)) and a loan portion equal to 15 per cent of the said amount (paragraph 1 (*i*) of the Schedule);

(ii) by a post-1966 gold mine: an amount determined in accordance with one of the formulae provided for in paragraph 1 (*d*) of the Schedule, plus a surcharge of 10 per cent of the said amount (second proviso to the said paragraph 1 (*d*)) and a loan portion of 15 per cent of the said amount (paragraph 1 (*i*) of the Schedule).

(*c*) Taxable income in the form of "recoupments" of capital expenditure accruing to companies which are or have been gold mining companies: the average rate of tax, as determined in accordance with paragraph 2 (2) of the Schedule, or 35 cents per R1, whichever is higher (paragraph 1 (*e*) of the Schedule).

(*d*) Taxable income from diamond mining: a basic tax of 45 cents per R1, plus a surcharge equal to 10 per cent of the basic tax (paragraph 1 (*f*) of the Schedule) plus a loan portion equal to 15 per cent of the basic tax (paragraph 1 (*i*) of the Schedule).

(*e*) Taxable income from mining operations (other than mining for gold or diamonds)—

(i) where derived in South West Africa: 35 cents per R1 (paragraph 1 (*g*) (i) of the Schedule);

(ii) where derived elsewhere than in South West Africa, i.e. in the Republic: 40 cents per R1 (paragraph 1 (*g*) (ii) of the Schedule).

To the tax determined as above is added a surcharge of 7½ per cent of such tax (proviso to subparagraph (*g*)) and a loan portion of 15 per cent of such tax (paragraph 1 (*i*)). (These rates apply also to taxable income from oil mining. A further levy, by way of additional normal tax, is provided for in respect of such taxable income in terms of the amendment to section 5 (2A) of the principal Act introduced by clause 5 (*b*)).

CLAUSE 2

Accrual to the Revenue Fund of South West Africa of a Portion of the Normal Tax Payable by Certain Companies.

In terms of this clause a portion of the normal tax payable by companies on taxable income (other than taxable income from mining operations) derived in South West Africa will accrue for the benefit of the Revenue Fund of that territory and will be paid into that fund in the manner prescribed in section 22 (2) (*c*) of the South West Africa Affairs Act, 1969 (Act No. 25 of 1969). The portion so accruing will be one-seventh of the basic normal tax payable before the addition of the surcharge or the loan portion. This is equivalent to 5 cents for every R1 of the taxable income on which the tax is payable. No portion of the normal tax which is payable by any private company and has to be paid into the Rehoboth Revenue Fund in terms of section 25 (2) (*a*) (ii) of the Rehoboth Self-Government Act, No. 56 of 1976, will, however, accrue for the benefit of the Revenue Fund of South West Africa.

CLAUSE 3

The Loan Portion of the Normal Tax.

In terms of this clause the portion of the normal tax determined in accordance with the provisions of paragraph 1 (*h*) or (*i*) of the Schedule

is a loan portion of that tax. The loan portion is repayable to taxpayers in accordance with the provisions of section 5 (2B) of the principal Act and the Fifth Schedule to that Act.

CLAUSE 4

Definitions: Amendments to section 1 of the principal Act.

Subclause (1) (*a*) *and* (*b*) introduces amendments to the definition of "dividend". The amendments should be read with the amendments to section 27 of the principal Act introduced by clause 17, in terms of which bonuses distributed by agricultural co-operatives will in certain circumstances be deductible from the incomes of such co-operatives. In terms of the existing provisions of the said section 27 closed trading co-operatives may also within limits deduct from their incomes bonuses distributed to their members. To qualify for deduction any such bonus must *inter alia* be distributed within the specified period (see subclause (1) (*d*)) in relation to a particular year of assessment. Where this condition is not satisfied or where a distribution by a co-operative does not for some other reason qualify as a deduction from the income of the co-operative, the ordinary rule that will apply in terms of the said amendments is that the distribution will be treated as a dividend. The usual rules applicable to dividends declared by companies will then apply to the amount so treated as a dividend, e.g. if the recipient of the dividend is a person other than a company he may qualify for the deduction provided for in section 19 of the principal Act.

The amendments to the definition of "dividend" apply to amounts distributed on or after 1 April 1977. The "ordinary rule" mentioned above will not apply to a bonus distribution by a co-operative out of its profits for a year of assessment commencing before 1 April 1977, if such distribution is made within twelve months after the end of such year of assessment. Such a distribution will fall to be dealt with under the general provisions of the principal Act or section 27 (1) of that Act, if applicable, and not under the new provisions of subsection (2) or the succeeding subsections of that section. (See subclause (1) (*b*). This is a transitional provision).

A further exception to the "ordinary rule" mentioned above is made in respect of distributions out of the stabilisation fund referred to in section 27 (2) (*h*), i.e. a stabilisation fund created by the Ko-operatieve Wijnbouwers Vereniging van Zuid-Afrika, Beperkt—such distributions will not be treated as dividends.

In terms of *subclause* (2) the amendments effected by subclause (1) (*a*) and (*b*) will, as respects persons receiving distributions from co-operatives, apply from the commencement of years of assessment ending on or after 1 April 1977.

Subclause (1) (*c*). The amendment to the definition of "gross income" is consequential upon the amendment to paragraph 12 of Schedule 1 of the principal Act introduced by clause 24.

Subclause (1) (*d*) inserts in section 1 of the principal Act a definition of "specified period". This definition is required for the purposes of the amendments to section 27 of the principal Act introduced by clause 17 (see subsection (2) (*a*) of the said section and the definition of "bonus" in subsection (9) of that section). The definition in effect replaces a similar definition in section 49 of the principal Act which is deleted by clause 20.

CLAUSE 5

Rates of normal tax payable by oil-mining companies: Amendments to section 5 of the principal Act.

In terms of the amendment to subsection (2) of section 5 of the principal Act introduced by *paragraph (a)* of this clause the rates of normal tax payable by oil-mining companies will, subject to the provisions of subsection (2A) of the said section, have to be determined annually, as in the case of other companies. In terms of the amendments to subsection (2A) of the said section introduced by *paragraph (b)* of this clause a company deriving taxable income from mining for natural oil (excluding gas) will in addition to the ordinary tax determined at the rates applicable to base mineral mines (at present 40 per cent basic plus a 7½ per cent surcharge plus a loan levy of 15 per cent) be required to pay, by way of additional normal tax, an amount equal to 40 per cent of the amount remaining after deducting the normal tax from the said taxable income. The rate of 40 per cent is a maximum rate: provision is made for the taxes to be reduced to or by such an amount and on such conditions as the Minister of Mines, in consultation with the Minister of Finance, may determine. The ordinary rates of tax applicable to base mineral mines will be applicable in respect of taxable income derived from mining for natural oil in the form of gas, but the tax payable may be reduced, as in the case of tax on taxable income from natural oil (excluding gas). The reductions of tax applicable are normally provided for in the relevant prospecting leases, e.g. in the case of a first discoverer of oil or gas.

CLAUSE 6

Abatements: Amendments to section 5A of the principal Act.

In terms of the amendments to section 5A (3) (*d*) of the principal Act introduced by this clause the maximum abatement allowable in respect of insurance premiums, contributions to provident and benefit funds, contributions to an unemployment insurance fund established by law and medical expenses is, in the case of a married person or in the case of an unmarried person who is the sole or main supporter of a child or who is entitled to the R250 abatement in respect of a dependant, increased from R700 to R1 000, and, in any other case, from R600 to R750. In addition, provision is made for amounts of the nature described which are paid after the death of the taxpayer or his wife by his or her estate, to be taken into account for the abatement. (At present such amounts, not being paid by the taxpayer but by his or his wife's estate, do not qualify for the abatement).

CLAUSE 7

Inclusions in income or taxable income: Amendments to section 8 of the principal Act.

Subclause (1) (*a*) introduces an amendment to section 8 (4) (*a*) of the principal Act in terms of which any recoupment of any allowance granted to an agricultural co-operative under section 27 (2) (*b*) or (*d*)*—i.e. the annual allowance granted in respect of storage buildings and the initial allowance granted in respect of machinery or plant used for storing or packing agricultural products or for subjecting such products to a primary processs—will have to be included in the co-operative's income.

Subclause (1) (*b*) extends the provisions of section 8 (4) (*e*) of the principal Act, which at present apply to recoupments of allowances in respect of machinery or plant used in a process of manufacture or a similar process, to recoupments of allowances in respect of machinery or plant used by an agricultural co-operative for storing or packing agricultural products or for

* Introduced by Clause 17.

subjecting such products to a primary process. The effect of this amendment, read with the amendment to section 11 (*e*) of the principal Act introduced by Clause 9 (1) (*a*), is that where such machinery or plant is damaged or destroyed and, as a result thereof, wear and tear or initial allowances granted under various provisions of the principal Act (now also section 27 (2) (*d*)*), have been recouped, the recoupment may, instead of being included in the income of the taxpayer (in this case an agricultural co-operative), be set off against further machinery or plant acquired to replace the damaged machinery or plant, provided various conditions are met.

CLAUSE 8

Exemptions from normal tax: Amendments to section 10 *of the principal Act.*

In terms of the amendments introduced by this clause the maximum annual exemption in respect of Special Tax-Free Indefinite Period shares in building societies is increased from R750 to R800, and the permitted rate of interest (for the purposes of the exemption) is increased from 7½ to 8 per cent per annum. The amendments apply with effect from years of assessment ending on or after 28 February 1977.

CLAUSE 9

Deductions from income: Amendments to section 11 *of the principal Act.*

Subclause (1) (*a*). The amendment to paragraph (iv) of the proviso to section 11 (*e*) of the principal Act which is introduced by this subclause should be read with the amendment to section 8 (4) (*e*) of that Act which is introduced by clause 7 (1) (*b*), and is explained in the portion of this memorandum dealing with the last-mentioned amendment.

Subclause (1) (*b*) introduces an amendment to paragraph (vi) of the proviso to section 11 (*e*) of the principal Act. In terms of that paragraph where a wear and tear allowance is granted under section 11 (*e*) in respect of machinery, implements, utensils or articles used for the purposes of trade and an initial allowance has been granted under section 12 or 12A in respect of such machinery, implements, utensils or articles, the value thereof must for purposes of the wear and tear allowance be reduced by the amount of the initial allowance. The amendment extends this provision to include a reference to the initial allowance granted under section 27 (2) (*d*) (i.e. in respect of machinery or plant used by an agricultural co-operative for storing or packing agricultural products or for subjecting such products to a primary process—see clause 17).

Subclause (1) (*c*). Section 11 (*g*) of the principal Act provides for the deduction from a taxpayer's income of an allowance (spread over a period of years) in respect of expenditure incurred by him in pursuance of an obligation to effect improvements on land or to buildings under a lease agreement. Paragraph (iv) of the proviso to section 11 (*g*) limits the allowance where the taxpayer has also enjoyed an annual allowance in respect of such improvements (including any building erected) under the provisions of section 13 (1) or (4) (i.e. where the building is an industrial building or the improvements are effected to an industrial building). In terms of the amendment introduced by subclause (1) (*c*) the proviso is amplified by the inclusion of a reference to section 27 (2) (*b*). (Under section 27 (2) (*b*)—see clause 17—an annual allowance, similar to the allowance under section 13 (1), may be made to an agricultural co-operative in respect of the cost of certain buildings used as storage buildings or the cost of improvements thereto).

Subclause (1) (*d*) inserts in section 11 of the principal Act a paragraph numbered (*g*C). In terms of that paragraph an exporter may be allowed as

* Introduced by Clause 17.

a deduction from his income expenditure incurred in obtaining in any export country the registration or restoration of any patent or the registration of any design or trade mark or the extension of the term or registration period of, any patent, design or trade mark. Such expenditure may also qualify as marketing expenditure for the purposes of the exporters' allowance granted under section 11*bis* of the principal Act.

Subclause (1) (*e*). In terms of the amendments to section 11 (*k*) of the principal Act which are introduced by subclause (1) (*e*) the maximum amount allowable as a deduction from the income of a member of a pension fund not established by law or for the benefit of employees of a local authority, in respect of his current contributions is increased from R1 500 to R1 750 per annum, and provision is made for a deduction (in addition to the deduction for current contributions but not exceeding R1 000 in the year of assessment) of any sums paid by the member during the year of assessment in respect of any past period which is to be reckoned as pensionable service.

Subclause (1) (*f*). In terms of the amendments to section (11) (*n*) of the principal Act which are introduced by subclause (1) (*f*) the maximum amount allowable as a deduction from the income of a member of a retirement annuity fund, in respect of his current contributions is increased from R3 000 to R3 500 per annum, and provision is made for a deduction (in addition to the deduction for current contributions but not exceeding R1 000 in the year of assessment) of contributions made by the member under conditions prescribed in the rules of the fund whereby a member who has discontinued his contributions prematurely is entitled to be reinstated as a full member.

Subclause (1) (*g*). In terms of the amendment to section 11 (*o*) of the principal Act introduced by subclause (1) (*g*) the annual allowance made to an agricultural co-operative under section 27 (2) (*b*) of the principal Act in respect of a storage building or of improvements to such a building must, where the building is scrapped, be taken into account for the purposes of the scrapping allowance under the said section 11 (*o*), and the special machinery initial allowance made to such a co-operative under section 27 (2) (*d*) of that Act in respect of machinery or plant used for storage, packing or processing of products must, where the machinery or plant is scrapped, be taken into account for the purposes of the scrapping allowance.

Subclause (1) (*h*) introduces an amendment to section 11 (*t*) of the principal Act. In terms of section 11 (*t*) an employer who incurs expenditure in connection with the erection of a dwelling for an employee or who for the purpose of financing the erection of a dwelling for an employee, makes an advance or donation, may, subject to certain conditions, be granted an allowance as a deduction from his income of an amount equal to 25 per cent of the expenditure or advance or donation, as the case may be. The aggregate of the allowances in respect of any one dwelling is limited to R2 500. In terms of the amendment this amount is increased to R3 000.

CLAUSE 10

Exporters' Allowance: Amendments to section 11bis *of the principal Act.*

This clause introduces amendments to section 11*bis* of the principal Act. That section provides for an allowance to be granted to exporters in respect of marketing expenditure incurred. The amendments are as follows:

Subclause (1) (*a*) excludes from the definition of "goods" precious metals contemplated in the definition of "precious metals" in section 1 of the Mining Rights Act, No. 20 of 1967, in addition to the precious metals (i.e. specie, gold and similar bullion) already excluded. The precious metals now excluded include platinum and iridium and any other metals of the platinum group, other metals declared by the State President, with the approval, by resolution of the Senate and the House of Assembly, by proclamation in the *Gazette* to be precious metals for the purposes of the said Act, and the ores of any such metals.

Subclauses (1) (*b*) to (*k*), inclusive, introduce amendments varying the rules applicable to the determination of the marketing expenditure on which the exporters' allowance is calculated. The proposed changes are as follows:—

Subclause (1) (*b*) amends the wording of section 11*bis* (4) to make it clear that the special discounts to be included in marketing expenditure are confined to such amounts as have been determined by the Secretary for Commerce under section 11 *bis* (4E). See also subclause (1) (*m*).

Subclause (1) (*c*) (which amends section 11*bis* (4) (*a*)) deletes the provision whereby expenditure on research or the obtaining of information in regard to the marketing of goods in any export country is excluded from marketing expenditure if the exporter has received or become entitled to the payment of any cash grant in respect of such expenditure. It is also provided that expenditure of the nature described may qualify as marketing expenditure when it relates to the rendering of services or the supply of goods in the course of a trade recognized or defined as an export service industry. (A cash grant in respect of any expenditure qualifying as marketing expenditure will, in terms of the amendment introduced by subclause (1) (*k*), be deducted from the expenditure and any balance remaining may qualify as marketing expenditure).

Subclause (1) (*d*) amends section 11*bis* (4) (*d*) so as to provide that expenditure incurred in bringing prospective customers (and not merely buyers) from any export country to the Republic may qualify as marketing expenditure, e.g. the customers of a taxpayer carrying on the trade of an export service industry.

Subclause (1) (*e*) amends section 11*bis* (4) (*e*) so as to provide for the inclusion in marketing expenditure of expenditure incurred in connection with the preparation or submission of tenders or quotations where such expenditure is incurred in connection with the rendering of services or the supply of goods to persons based in an export country if incurred in the course of a trade defined or recognized as an export service industry.

Subclause (1) (*f*) amends section 11*bis* (4) (*f*) so as to include in marketing expenditure any commissions or other remuneration incurred by an exporter in the course of carrying on a trade defined or recognized as an export service industry, in respect of orders for services or goods obtained from persons based in an export country.

Subclause (1) (*g*) inserts in section 11*bis* (4) a paragraph numbered (*f*A), providing for the inclusion in marketing expenditure of expenditure incurred in respect of the appointment of agents in any export country. (This expenditure has hitherto been provided for in paragraph (*f*) of the said section.)

Subclause (1) (*h*) deletes paragraph (*j*) of subsection (4) of section 11*bis*. That paragraph provided for the inclusion in marketing expenditure of expenditure incurred in conducting certain marketing operations.

Subclause (1) (*i*) deletes paragraph (*m*) of subsection (4) of section 11*bis*. That paragraph provided for the inclusion in marketing expenditure of expenditure incurred in packaging goods, to the extent that such expenditure exceeded the expenditure normally incurred in packaging similar goods for the South African market.

Subclause (1) (*j*) (which amends section 11*bis* (4) (*o*)) deletes the provision whereby expenditure incurred in maintaining any depot or warehouse in any export country used for storing exported goods is excluded from marketing expenditure if the exporter has received or become entitled to the payment of any cash grant in respect of

such expenditure. Such cash grant will be taken into account in terms of the general proviso added by subclause (1) (*k*).

Subclause (1) (*k*) adds to section 11*bis* (4) a general proviso providing that items of marketing expenditure which have been recovered or recouped in the current or a following year of assessment must be deducted from the marketing expenditure of the current year.

Subclause (1) (*l*) adds to the bodies referred to in section 11*bis* (4A) the South African Canned Fruit Export Board. This will enable producers of fruit for canning to receive the exporters' allowance in appropriate circumstances. A further provision is added to section 11*bis* (4A) the effect of which is that marketing expenditure incurred by an agricultural co-operative and in effect borne by producers shall for the purposes of the exporters' allowance be allowed only to the producers. The reference to the S.A. Wool Board is deleted as that board is now a control board established under the Marketing Act, 1968.

Subclause (1) (*m*). In terms of section 11*bis* (4E) (*a*) the Secretary for Commerce may determine the amounts of certain discounts to be included in marketing expenditure for the purposes of the exporters' allowance. In terms of the amendment applications for such determinations received after 30 June 1977 will not be considered.

Commencement of certain amendments. The amendments effected by subsection (1), except paragraphs (*a*), (*b*), (*h*), (*i*) and (*m*) thereof, are to apply with effect from years of assessment ending on or after 1 January 1977. The amendments effected by the said paragraphs (*a*), (*b*), (*h*) and (*i*) are to apply with effect from years of assessment ending on or after 1 January 1978, and the amendment effected by subclause (1) (*m*) is to take effect on 1 July 1977.

CLAUSE 11

Housing allowance in respect of employees of manufacturers in economic development areas: Amendments to section 11*quin of the principal Act.*

In terms of section 11*quin* of the principal Act if an industrialist carrying on a manufacturing or similar business in an economic development area incurs expenditure in connection with the erection or acquisition of any dwelling for the exclusive occupation of his employees an allowance by way of a deduction from income may, if the Minister of Finance so directs, be granted to the industrialist in respect of such expenditure. The allowance may, within certain limits, be spread over a period of 10 years. The allowance may also be granted to a housing company controlled by the industrialist. In terms of the amendments introduced by this clause the allowance may also be granted to any other person who is engaged in the provision of housing facilities for the industrialist's employees.

The allowance is terminated if the industrialist or housing company ceases to be the owner of the dwelling. In terms of the amendment introduced by subclause (1) (*b*), the rule is changed to apply where there is a cessation of control, whether the control is by virtue of ownership or under a lease.

CLAUSE 12

Bantu workers' training allowance: Amendments to section 11sept *of the principal Act.*

The amendments are of a textual nature.

CLAUSE 13

Allowances in respect of machinery and plant: Amendments to section 12 *of the principal Act.*

In terms of this clause the provisions of section 12 of the principal Act are amended to make it clear that the initial and investment allowances

are not available in respect of machinery or plant used for farming purposes, and that the allowances are not available to a person who does not as owner or lessee himself carry on the process of manufacture or a similar process in which the machinery or plant is used. This clause should be read with clause 24.

CLAUSE 14

Deduction of expenses incurred in appointing agents outside the Republic: Substitution of section 17 of the principal Act.

In terms of the new subsection (2) added to section 17 of the principal Act by this clause a person carrying on a trade defined or recognized under section 11*bis* (4B) of the principal Act as an export service industry will be allowed to deduct from his income expenditure actually incurred by him in appointing an agent in an export country for the obtaining of orders for the supply of services or goods supplied in the course of such trade. Such expenditure may also qualify for the exporters' allowance under section 11*bis*. The amendment applies in respect of years of assessment ending on or after 1 January 1977.

CLAUSE 15

Deduction in respect of married women's earnings: Amendments to section 20A of the principal Act.

In terms of section 20A of the principal Act a deduction not exceeding R750 is allowed in respect of the earnings of a married woman included in the income of her husband. "Earnings" is defined and excludes rents and royalties in respect of the use of patents, designs, trade marks or copyright. In terms of the amendment such royalties will be included in earnings if derived by a married woman in the course of any business, calling or occupation carried on by her. The amendment is to apply from the 1977 year of assessment.

CLAUSE 16

Development allowance: Amendment to section 21ter of the principal Act.

Section 21*ter* of the principal Act was amended in 1976 to empower the Minister of Finance to authorize the granting of a supplementary allowance to certain industrialists in economic development areas. The supplementary allowance was designed to confer on such industrialists benefits equivalent to those granted to other industrialists by way of the development allowance. The supplementary allowance was restricted to industrialists who had established or extended their industrial undertakings during the period 1 March 1961 to 1 January 1973. In terms of this clause the last-mentioned date is deleted as it has been found that in some cases industrialists who established or extended their undertakings after that date were not granted equivalent allowances.

CLAUSE 17

The taxation of agricultural co-operatives and their members: Amendment of section 27 of the principal Act.

Agricultural co-operatives have hitherto been exempt from normal tax except in respect of receipts or accruals derived from transactions with non-members. In terms of the amendments introduced by this clause the exemption is withdrawn with effect from years of assessment commencing on or after 1 April 1977. In the determination of the taxable incomes of agricultural co-operatives the deductions to be allowed will be those allowable in accordance with the general rules applicable under the principal Act and, in addition, the further deductions now provided for in the amendments to section 27 (2) of the principal Act

The *deductions from income* provided for in the amendments to section 27 (2) are as follows:—

(*a*) *Bonuses distributed.* In terms of *section* 27 (2) (*a*) an agricultural co-operative will be allowed to deduct from its income the amounts of any profits distributed by it by way of bonuses during the specified period (see definition in clause 4 (1) (*c*)) in relation to the year of assessment, to persons entitled to participate in such a distribution. "Bonus" is defined in section 27 (9). The total amount which may qualify for deduction under section 27 (2) (*a*) in any year of assessment will be restricted to a *calculated amount* equal to the co-operative's taxable income for such year, as calculated before deducting bonuses under section 27 (2) (*a*), the investment allowances provided for in section 27 (2) (*c*) and (*e*), loan repayments allowed under section 27 (2) (*f*), the exporters' allowance under section 11*bis*, the incentive allowances under section 11*ter*, 11*quat* and 11*quin*, the Bantu workers' training allowance under section 11*sept*, the investment allowances under sections 12 (2), 12A (3), 13 (5) and 13*bis* (7), the beneficiation allowance under section 15A and the development allowance under section 21*ter*, and before setting off any balance of assessed loss brought forward from a previous year of assessment. Distributions by an agricultural co-operative which do not qualify for deduction under section 27 (2) (*a*) will, with certain exceptions, constitute dividends (see clause 4 (1) (*a*) and (*b*)).

(*b*) An *annual allowance for storage buildings* and improvements thereto is provided for in section 27 (2) (*b*). "Storage building" and "improvements" are defined in section 27 (9). The rules laid down in regard to this allowance are somewhat similar to those applicable to the similar allowance for industrial buildings provided for in section 13 (1) of the principal Act. Section 27 (2) (*b*) should be read with the provisions of section 27 (3), (4) and (5) and in conjunction with the amendments introduced by clauses 7 (1) (*a*) and 9 (1) (*c*) and (*g*). The annual allowance is calculated at the rate of 2 per cent of the cost of the relevant storage building or improvements. The annual allowance is not granted if an allowance in respect of the building or improvements in question is granted under section 13 (1) of the principal Act.

(*c*) A *storage building investment allowance* is provided for in section 27 (2) (*c*). The allowance is similar to the investment allowance for industrial buildings provided for in section 13 (5) of the principal Act. The provisions of section 27 (2) (*c*) should be read with the provisions of section 27 (6) and (7) and the definitions of "improvements" and "storage building" in section 27 (9). The allowance is calculated at rates varying between 10 and 20 per cent of the cost to the co-operative of the relevant building or improvements, depending upon the date on which the erection of the building was commenced or the improvements were commenced. The enhanced investment allowance for industrial buildings in economic development areas does not apply to storage buildings. The storage building investment allowance applies only to a storage building the erection of which is commenced between 13 August 1970 and 30 June 1979 or improvements to such a building commenced between those dates and it is further provided that the allowance may not be granted if the building is brought into use or the improvements are completed after 30 June 1980. The allowance is not applicable to any storage building first used by an agricultural co-operative during any year of assessment commencing before 1 April 1977 or to improvements to any such building completed during any such year of assess-

ment. The storage building investment allowance is not granted if an investment allowance in respect of the building or improvements in question has been granted under section 13 (5) of the principal Act.

(*d*) A *special machinery initial allowance* is provided for in section 27 (2) (*d*). The allowance is calculated at the rate of 25 per cent of the cost of new or unused machinery or plant brought into use during any year of assessment commencing on or after 1 April 1977 and used by the agricultural co-operative directly for storing or packing pastoral, agricultural or other farm products of its members or for subjecting such products to a primary process. The allowance is not granted if an initial allowance in respect of the machinery or plant has been granted under section 12 (1) of the principal Act. "Primary process" is defined in section 27 (9).

(*e*) A *special machinery investment allowance* is provided for in section 27 (2) (*e*). It is granted in the same circumstances as the special machinery initial allowance; except that it is not available if the machinery or plant is brought into use after 30 June 1979. The allowance is not granted if an investment allowance in respect of the machinery or plant has been granted under section 12 (2) of the principal Act. The allowance is calculated at the rate of 30 per cent of the relevant cost.

(*f*) Provision is made in section 27 (2) (*f*) for a deduction in respect of *repayments or reductions of loans or advances* obtained and used in order to finance the cost of erecting any storage building or the cost of acquiring any storage building (excluding the cost of the land) or the cost of improvements (other than repairs) to any such storage building or the cost of acquiring immovable machinery or plant wholly or mainly used by the agricultural co-operative for storing or packing pastoral, agricultural or other farm products produced by its members or for subjecting such products to a primary process. "Storage building" and "primary process" are defined in section 27 (9). Various rules are laid down, which may be summarised as follows:

(i) A reduction or repayment of a loan or advance obtained by the co-operative from a company controlled by it does not qualify for the deduction. Where a loan or advance was obtained to finance the purchase of any building, plant or equipment from such a company any amount expended in the reduction or repayment of such loan or advance does not qualify for the deduction.

(ii) The aggregate of the deductions allowed in respect of repayments or reductions of loans or advances relating to any such building, improvements, machinery or plant is limited to the cost thereof, less any investment allowance granted in respect thereof under section 27 (2) (*c*) or (*e*) or section 12 (2) or section 13 (5) of the principal Act, and any amounts expended by the co-operative during years of assessment which commenced before 1 April 1977 in repayment or reduction of such loans or advances (see section 27 (2) (*f*) (i)).

(iii) The repayment or reduction of the loan or advance will not qualify for the deduction if it is financed out of other borrowed funds.

(iv) The aggregate of the deductions in respect of repayments or reductions of loans or advances may not for any year of assessment exceed the *calculated amount* referred to in paragraph

(*a*) above, less any deductions allowed in respect of bonuses under section 27 (2) (*a*). (See section 27 (2) (*f*) (ii).)

(v) The deductions under section 27 (2) (*f*) are, in terms of paragraph (iii) of the proviso thereto, permissible only in respect of the first year of assessment of an agricultural co-operative commencing on or after 1 April 1977 and the nine succeeding years of assessment. In terms of paragraph (iv) of that proviso the ten years of assessment will in the case of a new co-operative which has taken over an undertaking from another agricultural co-operative, whether by purchase or under an amalgamation, be determined as though the two co-operatives had been one co-operative. (A further rule in regard to amalgamations is provided for in section 27 (5). This is dealt with below.)

(*g*) An allowance is provided for in section 27 (2) (*g*) for losses suffered by an agricultural co-operative in consequence of physical damage to or deterioration of pastoral, agricultural and other farm products held by it on behalf of a control board. The allowance is made by way of a reserve which is to be re-calculated from year to year.

(*h*) In section 27 (2) (*h*) provision is made for an allowance to be granted to the Ko-öperatieve Wijnbouwers Vereniging van Zuid-Afrika, Beperkt, by way of a deduction from income, in respect of amounts transferred by the Vereniging from its profits to a price stabilisation fund. The allowance may not exceed such portion of the Vereniging's profits as the Secretary is satisfied was derived by the Vereniging in the exercise of its functions relating to the control and stabilisation of prices in the wine industry. The amount transferred must be distributed to members or wine growers within a period of five years. In terms of the definition of "bonus" in section 27 (9) any such distribution will be a bonus, and such bonus will, as at present, be treated as income and not as a dividend. (See also clause 4 (1) (*a*) and (*b*). Such a bonus distribution will not be deductible from the Vereniging's income (see section 27 (2) (*a*).)

Section 27 (3) provides that the aggregate of the annual allowances in respect of a building or improvements granted under section 27 (2) (*b*) or section 13 (1) of the principal Act may not exceed the cost (after the deduction of any amount set off in terms of subsection (4)) of the building or improvements.

Section 27 (4) provides that where any allowance granted under section 27 (2) (*b*) in respect of a building or improvements has been recouped, the amount recouped may, instead of being included in income, be set off against the cost of a further building if certain requirements are met.

Section 27 (5) provides in effect that where two or more agricultural co-operatives have amalgamated under section 94 of the Co-operative Societies Act, 1939, the new co-operative which comes into existence may in certain circumstances be granted the allowances under section 27 (2) (*b*) or (*f*) to which the formerly existing co-operatives would have been entitled. The relevant provisions are to be applied as though the formerly existing co-operatives and the new co-operative were one co-operative.

Section 27 (6) *and* (7). These provisions relate to the storage building investment allowance provided for in section 27 (2) (*c*). The more important aspects of this allowance are summarised in paragraph (*c*) above.

Section 27 (8) contains provisions relating to *the taxation of bonuses distributed by agricultural co-operatives*. In terms of *paragraph* (*a*) of that section the full amount of any such bonus will, to the extent that the bonus qualifies for deduction from the co-operative's income under section 27 (2) (*a*), be taxable in the hands of the persons entitled thereto and the date of

accrual of such bonus to such persons will be the date of the distribution thereof by the co-operative. In terms of *paragraph* (*b*) of the said section 27 (8) the amount of any bonus distributed by way of capitalisation shares or bonus debentures or securities will be the nominal value thereof. The expressions "capitalisation shares", "bonus debentures or securities" and "nominal value" are already defined in section 1 of the principal Act. "Bonus" is defined in section 27 (9).

Section 27 (9) defines various terms for the purposes of section 27.

The term *"agricultural co-operative"* comprises various societies or companies defined in the Co-operative Societies Act, 1939.

The word *"bonus"* means any amount distributed by any agricultural or trading co-operative out of its profits or surplus for any year of assessment (or by the Ko-operatieve Wijnbouwers Vereniging van Zuid-Afrika, Beperkt, out of its price stabilisation fund), whether the distribution is in cash or by way of a credit or an award of capitalisation shares or bonus debentures or securities, provided the bonus is divided among the persons entitled thereto in accordance with the value of the business transactions between the co-operative and its members and is distributed during the specified period in relation to the year of assessment or is distributed out of the aforementioned stabilisation fund. This definition is of particular importance in relation to the provisions of section 27 (2) (*a*) and (8) and the amendments to the definition of "dividend" introduced by clause 4 (1) (*a*) and (*b*).

The definition of *"improvements"* restricts that term to improvements (other than repairs) which are effected for the purpose of increasing the capacity of a storage building for storing or packing pastoral, agricultural or other farm products or for subjecting such products to a primary process. Allowances in respect of improvements are provided for in section 27 (2) (*b*), (*c*) and (*f*).

"Primary process" is a term used in section 27 (2) (*d*), (*e*) and (*f*) in relation to machinery or plant and in the definitions of "improvements" and "storage building". It is the first process to which any product produced in the course of pastoral, agricultural or other farming operations is subjected by an agricultural co-operative in order to render it marketable or to convert it into a marketable commodity. Further processes which are closely connected with the first process may, together with the first process, be regarded as one process if the further processes are necessary to convert the product into a marketable commodity.

Allowances in respect of a *"storage building"* are provided for in section 27 (2) (*b*), (*c*) and (*f*). It is a building which is wholly or mainly used by an agricultural co-operative for storing or packing pastoral, agricultural or other farm products produced by its members or for carrying on therein a primary process in respect of such products. The members of a central or federal agricultural co-operative are normally other agricultural co-operatives. The members of such other co-operatives will for the purposes of the definition be regarded as being members of such central or federal co-operative.

The amendments are to apply from the commencement of years of assessment commencing on or after 1 April 1977.

CLAUSE 18

Transfer of business undertaking by a foreign company to a South African subsidiary: Amendment of section 28bis.

In terms of section 28*bis* of the principal Act where a foreign company has transferred a business undertaking carried on by it in the Republic to its wholly owned South African subsidiary, the two companies may be assessed for normal tax as though the foreign company had not discon-

tinued the business undertaking and the subsidiary had owned and carried on the undertaking prior to the transfer of the undertaking. One of the conditions laid down in this section is that at the time the arrangement is implemented all the issued shares of the subsidiary must be held for its own benefit by the foreign company or by another foreign company which is controlled by or controls the first-mentioned foreign company. In terms of the amendment introduced by this clause the said condition as to shareholding is relaxed where the arrangement was implemented in order to meet the requirements of section 3*quat* of the Insurance Act, No. 27 of 1943. In terms of that section, which was introduced in 1976, foreign non-mutual insurers are required within a period of 2 years to transfer their branch insurance businesses to domestic insurers. Such domestic insurer need not be a wholly-owned subsidiary.

CLAUSE 19

Exemptions from Non-Resident Shareholders Tax: Amendments to section 42 of the principal Act.

This clause introduces amendments to section 42 of the principal Act in terms of which exemptions from non-resident shareholders tax are provided in respect of dividends accruing to non-South African insurance companies in respect of shares held as assets of their insurance businesses in the Republic.

Subclause (1) (*a*) adds to section 42 (2), paragraphs numbered (*i*) and (*j*), in which the exemptions are provided.

Paragraph (*i*) relates to dividends derived by a *non-mutual insurance company.* The exemption is applicable if, in compliance with the provisions of section 3*quat* of the Insurance Act, No. 27 of 1943, a South African company has been formed to acquire the insurance business of the non-mutual insurance company in the Republic and has acquired all the assets and assumed all the liabilities of the non-mutual insurance company relating to such insurance business and the Secretary is satisfied that the dividends accrued for the benefit of such business and have not been remitted to any address outside the Republic. Provision is made for a partial exemption if the dividends have in part been remitted to such an address.

Paragraph (*j*) relates to dividends derived by a *mutual insurance company.* The procedure for the "domestication" of such a company under section 3*quat* of the Insurance Act, 1943, does not involve a transfer of assets to a separate subsidiary company. It is, however, as respects its insurance business in the Republic, deemed to be a juristic person for the purposes of the said Act when the registrar of insurance has issued a certificate in terms of section 3*quat* (3) of that Act. The proposed exemption applies to dividends accruing during the period before the date of "domestication" and to dividends accruing on or after that date. The exemption applies in respect of dividends accruing during the period before the date of domestication if the dividends accrue for the benefit of the company's South African business and have not before that date been remitted to any address outside the Republic. Provision is made for a partial exemption if such dividends have in part been remitted to such an address. As respects dividends accruing on or after the date of "domestication" the exemption applies if the dividends accrue for the benefit of the South African business and thus of the juristic person mentioned above. The exemption under paragraph (*j*) should be read with the provisions of section 42 (6) and (7), as introduced by subclause (1) (*b*).

Subclause (1) (*b*) adds subsections numbered (6) and (7) to section 42 of the principal Act. These subsections should be read with the provisions

of paragraph (*j*), as introduced by subclause (1) (*a*). Where a *mutual insurance company* has, after becoming a domestic insurer under the provisions of section 3*quat* of the Insurance Act, 1943, remitted any amount to any address outside the Republic, the amount so remitted (less so much thereof as the Secretary is satisfied does not consist of profits earned by the company), or a portion thereof, will be subject to non-resident shareholders tax. Any such tax will be payable on assessment.

The amendments are in terms of *subclause* (2) deemed to have taken effect on 31 March 1976.

CLAUSE 20

Definitions for the purposes of undistributed profits tax: Amendment of section 49 of the principal Act.

This clause deletes the definition of "specified period". A similar definition, inserted in section 1 of the principal Act by clause 4, will apply instead of the deleted definition.

CLAUSE 21

Donations tax exemptions: Amendment of section 56 of the principal Act.

In terms of section 56 (1) (*g*) donations tax is in certain circumstances not payable in respect of a donation of property situated outside the Republic. The exemption applies *inter alia* if the property was acquired by the donor by inheritance. In terms of the amendment the words "by inheritance" are qualified by the insertion of the words "from a person who at the date of his death was not ordinarily resident in the Republic". The exemption will thus not apply if the donor acquired the property by inheritance from a person ordinarily resident in the Republic.

CLAUSE 22

Exemptions from non-residents tax on interest: Amendment of section 64C of the principal Act.

In terms of the amendment introduced by this clause the requirement for the exemption from non-residents tax on interest in respect of dividends (treated as interest) on Special Tax-Free Indefinite Period shares in any building society, to the effect that the rate of the dividend shall not exceed $7\frac{1}{2}$ per cent per annum, is varied by the substitution for the rate of $7\frac{1}{2}$ per cent of a rate of 8 per cent. The amendment is in terms of subclause (2) deemed to have taken effect on 1 June 1976.

CLAUSE 23

Amendment of paragraph 7 of the First Schedule to the principal Act.

The amendment introduced by this clause is of a textual nature.

CLAUSE 24

Deduction in respect of expenditure on farm machinery, implements, utensils and articles: Amendments to paragraph 12 of the First Schedule to the principal Act.

Paragraph (*a*) of this clause adds to paragraph 12 (1) of the First Schedule to the principal Act an item numbered (*j*) in terms of which a farmer will be allowed to deduct from his income expenditure incurred by him in respect of the acquisition of machinery, implements, utensils and articles used by him for farming purposes, except motor vehicles the sole or primary function of which is the conveyance of persons or any caravan or any aircraft or any office furniture or equipment or anything the cost of which is otherwise deductible from the farmer's income. The new item will apply with effect from years of assessment ending on or after 1 January 1978.

Paragraph (*b*) of this clause inserts in the said paragraph 12 subparagraphs numbered (1A), (1B) and (1C), which are to the following effect:

Subparagraph (1*A*) provides for a deduction in respect of a portion of the cost of machinery, implements, utensils or articles held for farming purposes at the commencement of the year of assessment ending on 28 February 1978, other than motor vehicles, the sole or primary function of which is the conveyance of persons or any caravan or aircraft or office furniture or equipment. The deduction to be allowed for each of the 1978, 1979 and 1980 years of assessment will be one-third of the said cost, less any wear and tear allowances granted under section 11 (*e*) in respect of such machinery, implements etc.

Subparagraph (1*B*) provides that where any asset in respect of which a deduction has been allowed under subparagraph (1) or (1A) and which is or has become a movable asset, is disposed of, the amounts derived from the disposal shall be included in the farmer's income, except to the extent that such amounts exceed the expenditure allowed under subparagraph (1) or the original cost taken into account under subparagraph (1A). An adjustment is to be made where the asset is one in respect of which an allowance is made under subparagraph (1A), if the asset is disposed of during the 1978 or 1979 year of assessment: if, for example, the asset is disposed of during the 1978 year of assessment the allowances which would have been made in respect of such asset in the 1979 and 1980 years of assessment will not be made in those years, but an equivalent amount will be allowed in the 1978 year of assessment. The provisions of section 8 (4) (*a*) of the principal Act will not apply in respect of the recoupment of any allowance made under section 11 (*e*) of the principal Act in respect of any asset in respect of which an allowance has been made under subparagraph (1A) (*a*).

Subparagraph (1*C*). Where any asset in respect of which any deduction has been made under subparagraph (1) or (1A) and which is or has become a movable asset is disposed of by the farmer under a donation or for an inadequate consideration or for a consideration not readily capable of valuation, the farmer will be regarded as having received a consideration equal to the fair value of the asset, as determined by the Secretary and the person acquiring the asset (if he is a farmer) will be regarded as having paid such consideration. The amount determined by the Secretary may not, however, exceed the cost of the asset to the farmer who disposes of it.

Paragraph (*c*) of this clause introduces amendments to paragraph 12 (2) of the First Schedule to the principal Act which are of a consequential nature.

Paragraph (*d*) of this clause inserts in subparagraph (3) of paragraph 12 of the First Schedule to the principal Act references to item (*j*) of subparagraph (1) of the said paragraph and to subparagraph (1A) of the said paragraph. In practical terms this means that any assessed loss incurred by a farmer in respect of farming operations will be reduced to the extent that the loss is caused or increased by the deductions allowed under the said item (*j*) or the said subparagraph (1A). The amount by which the assessed loss is reduced is carried forward and is treated as expenditure incurred in the next succeeding year of assessment.

CLAUSE 25

Farmers: Excess profits in consequence of expropriations of farms: Amendment of paragraph 20 of First Schedule to the principal Act.

In terms of paragraph 20 of the First Schedule to the principal Act, where a farmer has wound up a farming undertaking in consequence of the acquisition of his farm by the State or a local authority or by a juristic person or body mentioned in section 3 (2) of the Expropriation Act, No. 63 of 1975,

any excess farming profits derived by him in winding up his undertaking may be subjected to normal tax at a rate lower than the rate which otherwise would be applicable. The concession is applicable in respect of the year of assessment during which the farm is acquired from the owner and the first and second succeeding years of assessment. The amendment introduced by this clause provides for the case where within the period of twelve months prior to the formal acquisition of the land the owner has accepted an offer to purchase the land and the farmer has commenced to wind up his farming undertaking in anticipation of such formal acquisition. In such case the farm will for the purposes of the concession be regarded as having been acquired from the owner on the date of acceptance of the offer to purchase.

CLAUSES 26 AND 27

Lump sum benefits from pension, provident and retirement annuity funds: Amendments to paragraphs 1 and 5 of the Second Schedule to the principal Act.

The Second Schedule to the principal Act provides rules for determining the amounts to be included in a person's gross income in respect of lump sum benefits derived from pension funds, provident funds and retirement annuity funds. From the gross amounts so derived certain deductions are made, some of which are, in the case of retirement and death benefits, determined in accordance with certain formulae, referred to as formula A and formula B.

Formula A, which applies in relation to a pension fund or a provident fund, takes into account the taxpayer's highest annual average salary actually earned by him during any five consecutive years of his service, but not exceeding an amount of R20 000. That amount is now increased to R22 500 (*clause* 26 (*a*)).

Formula B takes into account the fact that the taxpayer may be a member of more than one fund and places a limit of R40 000 on the amounts which (apart from certain contributions) may be deducted in respect of the various funds. This limit is now increased to R45 000 (*clause* 26 (*b*)).

Paragraph 5 (2) of the Second Schedule to the principal Act lays down that certain minimum amounts shall be deducted in certain circumstances under formula B. The minimum amounts which are as follows, are increased as indicated below:

(*a*) If the taxpayer is or was a member of a provident fund (other than a provident fund which has become a pension fund) from which any lump sum benefit was or may be derived in consequence of or following upon his retirement on or after 15 March 1961: R8 000, now increased to R9 000 (*clause* 27 (*a*)).

(*b*) In respect of death benefits: R20 000, now increased to R22 500 (*clause* 27 (*b*)). If the death benefits consist of or include benefits from any pension or provident fund the deduction may be increased to an amount equal to twice so much of the taxpayer's salary earned during the twelve months ending at his death as does not exceed R20 000. That amount is also increased to R22 500 (*clause* 27 (*b*)).

A minimum deduction is applicable in respect of death benefits from retirement annuity funds derived where death has occurred before retirement. That minimum amount is the amount (but not exceeding the lesser of R40 000 and the value of benefits) which the taxpayer could have derived in respect of the commutation of one-third of his annuities from the funds if he had retired on the day before the date of his death. The amount of R40 000 is increased to R45 000 (*clause* 27 (*c*)).

CLAUSES 28 AND 29

Amendments to paragraphs 2 and 13 of the Fourth Schedule to the principal Act.

The amendments introduced by these clauses are of a consequential or textual nature.

CLAUSE 30

Commencement of certain amendments.

For the purposes of assessments of normal tax and undistributed profits tax the amendments introduced by the Bill to the principal Act are, except where otherwise provided or the context otherwise indicates, to take effect from years of assessment ending on or after 1 January 1978.

CLAUSE 31

The Act is to apply also in South West Africa. This does not affect the liability for normal tax of persons (other than companies) in respect of income derived from sources in South West Africa, as such income is taxed under an ordinance of that territory.

CLAUSE 32

This clause gives the short title of the Act.

THE SCHEDULE

The provisions of the Schedule are dealt with in the portion of this Memorandum dealing with clause 1.

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