REPUBLIC OF SOUTH AFRICA

EXPLANATORY MEMORANDUM

ON THE

REVENUE LAWS AMENDMENT BILL, 1996

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INTRODUCTION

The Revenue Laws Amendment Bill, 1996, introduces amendments to the Marketable Securities Tax Act, 1948, the Transfer Duty Act, 1949, the Estate Duty Act, 1955, the Income Tax Act, 1962, the Stamp Duties Act, 1968, the Value-Added Tax Act, 1991, the Regional Industrial Development Act, 1993, the Taxation Laws Amendment Act, 1994, the Income Tax Act, 1996, and the Tax on Retirement Funds Act, 1996.

In this Explanatory Memorandum there are various references to the explanation with regard to *clause 14*. The reason therefor is as follows. In terms of the Revenue Laws Amendment Bill, the provisions in all the aforementioned Acts with regard to the search and seizure of information and documents have been amended to ensure that the provisions comply with the spirit and purpose of the Constitution. As the contents of the new provisions to be introduced in substitution of the existing provisions in the various Acts are all virtually the same, the introduction and the effect thereof have been explained only in the context of the amendments to the Income Tax Act as dealt with in *clause 14*. The explanation with regard to that clause should therefore be referred to for purposes of the similar amendments to the other Acts.

CLAUSE 1

Marketable securities tax: Amendment of section 1 of the Marketable Securities Tax Act, 1948

The definition of ''stockbroker'' in the Marketable Securities Tax Act is substituted to bring it into line with the definition of ''stockbroker'' as contemplated in the Stock Exchanges Control Act, 1985.

CLAUSE 2

General provisions with regard to information, documents or things: Substitution of section 9 of the Marketable Securities Tax Act, 1948

See the explanation with regard to *clause 14*.

CLAUSE 3

Penalties: Amendment of section 10 of the Marketable Securities Tax Act, 1948

The introduction, in terms of *clause 2* of this Bill, of revised provisions into the Marketable Securities Tax Act with regard to the—

- furnishing and production of any information, documents or things;
- search for and seizure of any information, documents or things; and
- making of inquiries,

necessitates the introduction of amendments to the provisions regulating the imposition of penalties where offences have been committed. The amendments introduced in terms of this clause are, therefore, consequential upon the introduction of such revised provisions.

CLAUSE 4

Powers of the Commissioner: Amendment of section 11 of the Transfer Duty Act, 1949

The introduction of the amendment proposed in terms of this clause, is consequential upon the introduction of revised measures into the Transfer Duty Act in terms of *clause 5* of the Bill, with regard to, *inter alia*, the furnishing of information, the production of documents and the questioning of persons for the purposes of the administration of the aforementioned Act.

CLAUSE 5

General provisions with regard to information, documents or things: Insertion of sections 11A, 11B, 11C, 11D and 11E in the Transfer Duty Act, 1949

See the explanation with regard to *clause 14*.

CLAUSE 6

Penalties: Amendment of section 17 of the Transfer Duty Act, 1949

The introduction, in terms of *clause 5* of this Bill, of revised provisions into the Transfer Duty Act with regard to the—

- furnishing and production of any information, documents or things;
- search for and seizure of any information, documents or things; and
- making of inquiries,

necessitates the introduction of amendments to the provisions regulating the imposition of penalties where offences have been committed. The amendments introduced in terms of this clause are, therefore, consequential upon the introduction of such revised provisions.

CLAUSE 7

General provisions with regard to information, documents or things: Substitution of section 8bis of the Estate Duty Act, 1955

See the explanation with regard to *clause 14*.

CLAUSE 8

Penalties: Amendment of section 28 of the Estate Duty Act, 1955

The introduction, in terms of *clause 7* of this Bill, of revised provisions into the Estate Duty Act with regard to the—

- furnishing and production of any information, documents or things;
- search for and seizure of any information, documents or things; and
- making of inquiries,

necessitates the introduction of amendments to the provisions regulating the imposition of penalties where offences have been committed. The amendments introduced in terms of this clause are, therefore, consequential upon the introduction of such revised provisions.

CLAUSE 9

Exemptions: Amendment of section 10 of the Income Tax Act, 1962

At present SAFTO (Pty) Ltd and the South African Special Risks Insurance Association (SASRIA) enjoy tax free status. In terms of the proposed amendment the exemption from normal tax which such institutions presently enjoy, is withdrawn.

CLAUSES 10 AND 11

Deduction in respect of certain machinery or plant: Amendment of section 12C of the Income Tax Act, 1962

Deduction in respect of buildings used in a process of manufacture: Amendment of section 13 of the Income Tax Act, 1962

On 14 June 1996 the Minister of Finance proposed a Macro-Economic Strategy to promote growth, employment and redistribution. One of the key elements of the economic package outlined by the Minister, encompasses certain tax incentives to stimulate growth. He announced that for a limited period the tax allowances in respect of certain machinery or plant and buildings will be granted on an accelerated basis.

Clause 10 introduces an amendment to section 12C of the Income Tax Act, 1962, to give effect to that proposal insofar as it relates to plant or machinery.

Generally speaking the accelerated wear and tear allowance will apply to machinery or plant which is new or unused and—

- acquired by the taxpayer; and
- brought into use for the first time by the taxpayer or the lessee, as the case may be, directly in a process of manufacture or in a process similar to manufacture,

during the period 1 July 1996 to 30 September 1999.

The expression ''acquired'' for the purposes of the above provisions means acquired in terms of an agreement, whether conditional or not, concluded during the said period.

However, where the plant or machinery has been acquired during the period 1 July 1996 to 30 September 1999, but brought into use during the period 1 October 1999 to 31 March 2000, such acquisition must have taken place in terms of a written agreement formally and finally signed by every party to the agreement. This will allow a taxpayer who purchased a large plant towards the end of the three year period ending on 30 September 1999, an additional period of 6 months within which the plant should be brought into use.

The effect of the accelerated wear and tear allowance is that the present allowance of 20 per cent per annum is increased to 33⅓ per cent per annum. Such allowance is determined on a straight-line basis.

Clause 11 introduces similar provisions in respect of buildings or improvements thereto, within which a process of manufacture or a similar process is carried on.

Where the erection of any building, or any improvements to a building, commences during the period 1 July 1996 to 30 September 1999 and such building or improvements are—

- brought into use before 31 March 2000;
- used by the taxpayer or the lessee during the course of his trade; and
- used wholly or mainly for the purpose of carrying on therein a process of manufacture or a process of a similar nature,

the cost of such building or improvements will be written off at 10 per cent per annum on a straight-line basis over 10 years, instead of the present 5 per cent over a period of 20 years.

CLAUSE 12

Tax holiday scheme for certain companies: Insertion of section 37H in the Income Tax Act, 1962

Introduction

In his Macro-Economic Strategy Plan announced on 14 June 1996, the Minister of Finance announced a tax holiday scheme to be introduced to contribute to the achievement of South Africa's industrial development goals. The proposed section provides for the basic rules that will regulate the proposed scheme. It furthermore also introduces the necessary enabling legislation to enable the Minister of Trade

and Industry, in consultation with the Minister of Finance, to make regulations with regard to the guidelines to be followed by the Regional Industrial Development Board (the board) in evaluating and approving applications in terms of the scheme.

In essence the proposed scheme can be summarised as follows:

A project (being a specified manufacturing concern) may consist of one or more of three components, ie a spatial component, an industry component and a human resource component. A company incorporated on or after 1 October 1996, contemplating carrying on a project as its sole business, may apply to the Regional Industrial Development Board for the approval of its project. The board will consider the application in the light of the conditions and guidelines prescribed in the Bill and the aforementioned regulations. For each component certified by the board the company concerned will become entitled to tax holiday status for a continuous period of 2 years. A qualifying company may therefore become eligible for tax holiday status for a maximum period of 6 years, but the company shall not enjoy such status for a period longer than 10 years which period shall commence in the year in which the project was approved.

The aforementioned summary must, however, be construed in the light of the provisions governing the scheme, which provisions will come into operation on 1 October 1996.

Details of specific provisions

The following is an explanation of each of the subsections of the proposed section:

Subsection (1): This subsection provides for various definitions of words and expressions used in the proposed section.

(a) ''board'' — The board will be responsible for evaluating, approving and monitoring of projects. It is an existing body of persons established in terms of the Regional Industrial Development Act in 1993 and presently consists of members from the Departments of Trade and Industry, State Expenditure and Finance and 9 provincial representatives. However, to enable the board to fulfil its functions in this regard, it is proposed to introduce appropriate amendments to the aforementioned Act. For an explanation in this regard see *clauses 26 and 27.*

(b) ''commencement date'' — This definition prescribes 1 October 1996 as the date on or after which a qualifying company may commence carrying on a qualifying project.

(c) ''project'' — This definition restricts the ambit of a project to a project which in the board's opinion, represents a manufacturing process as described in the Standard Industrial Classification (SIC) code (5th Edition) issued by the Central Statistical Services in January 1993. The processes are restricted to those products and goods classified in Major Division 3: Manufacturing of the SIC code.

(d) ''qualifying company'' — In essence the definition prescribes four criteria with which a company has to comply in order to fall within the ambit of a qualifying company:

- The company (including a close corporation) must be incorporated on or after 1 October 1996.
- The project to be carried on by the company must have been approved by the board as a qualifying project. Such approval must take place before the commencement of the carrying on of the qualifying project. (In this regard see subsection (3)(b))
- The company must have commenced with the carrying on of the qualifying project for the first time on or after 1 October 1996.
- The sole object of the company must be the carrying on of only one qualifying project. The company may, therefore, not carry on any other trade.

The reason for restricting the provisions to a one entity/one project rule is to avoid the complications of ring-fencing the taxable income from each project and the regulation of different tax holiday status periods for different projects.

(e) ''qualifying project'' — Constitutes a manufacturing project which has been approved by the board.

(f) ''tax holiday status'' — Two types of tax holiday status are conferred. The first is merely a transitional measure and is based on a deduction rather than the application of a zero rate of normal tax. Such provisions will apply only to years of assessment ending on or before 31 March 1997. The reason for this special rule is that the Minister of Finance is only permitted to fix the rates of normal tax on an annual basis. As such rates have already been prescribed by the Minister in relation to companies whose years of assessment end during the period 1 April 1996 to 31 March 1997, an alternative method of reducing a qualifying company's normal tax liability to zero had to be introduced in relation to years of assessment ending during the aforementioned period.

The second type of status is that which is based on a determination of normal tax at a rate of zero per cent. This rate will be promulgated by means of a specific category for qualifying companies which will appear in the Schedule to the annual Income Tax Act, prescribing the rates of tax to be applied to taxable incomes and will apply to years of assessment of qualifying companies ending after 31 March 1997.

This subsection also defines ''goods'', ''services'', ''State'' and ''tax holiday scheme''.

Subsection (2): The powers and functions of the board which are granted in terms of the Regional Industrial Development Act, 1993, are extended by these provisions in order that the board may—

- evaluate and approve projects;
- investigate projects to ensure that a project qualifies, and in certain circumstances still qualifies, for the scheme;
- monitor the scheme as a whole;
- exclude the project from any other State assistance;
- require a relevant company to furnish it with information or documents; and

- perform ancillary functions in accordance with the provisions of the proposed section.

Subsection (3): These provisions prohibit the board from approving a project under certain circumstances.

Firstly, the project to be carried on may not be substantially the same as was previously or is currently carried on by any person within the Republic. This provision serves as an anti-avoidance measure to ensure that only new projects obtain a concession. The purpose of the tax holiday scheme is to encourage the establishment of new businesses in South Africa and it is, therefore, not desirable that an existing business be transferred into another entity in order to obtain the concession and thereby reduce the existing national normal tax base. In this regard see also the explanation with regard to subsection (14)(e).

The second circumstance under which a project may not be approved, is where the company has already commenced carrying on trade prior to the approval of the project by the board. See also the explanation with regard to subsection (14)(e).

The purpose of this section is to prohibit the approval of projects on a retroactive basis.

Subsection (4): All applications for approval of projects must be made directly to the board and will be in a form prescribed by the board. The approval of projects is, therefore, not a function of the South African Revenue Service.

Subsection (5): This subsection provides that the tax holiday scheme shall apply only to a project which has been approved by the board as a qualifying project in respect of an application for approval of a project which has been received by the board on or before the cut-off date of the tax holiday scheme, ie 30 September 1999.

Subsection (6): The provisions of this subsection provide that a project may consist of one or more of three components, ie a spatial component, an industry component and a human resource component. In this regard section 37H(14) provides that the Minister of Trade and Industry, in consultation with the Minister of Finance, may make regulations to define and describe such components having regard to the guidelines provided in the aforementioned section.

Subsection (7): In addition to satisfying itself that a project complies with the criteria relevant to the different components of a project, the board must also, in considering an application, have regard to the following soft-issues:

- financial viability of a project;
- effect on national competitiveness;
- utilisation of resources;
- utilisation of competitive technology; and
- commitment to the upgrading and training of local skills.

In this regard see also the explanation with regard to subsection (14)(g).

This subsection also provides that the board must analyse each component of the project and where it is satisfied that the component meets the necessary criteria, certify the component accordingly.

Subsection (8): The process of considering the soft-issues and certifying the components must be done on application of the project for approval. However, an exception to this rule is the human resource component. The nature of this component makes it difficult to finally approve it upfront. The final certification process is, therefore, delayed until 6 months after the end of the first year of assessment in which the qualifying project commences its tax holiday status where only the human resource component is present. Where the project consists of more than one component, one of which is a human resource component, the final approval is delayed until a date falling towards the end of the tax holiday period attributable to all the other components of the project. This will enable the board to ensure that the company is carrying out its proposed human resource policy.

Subsection (9): The provisions of this subsection specify the period of the tax holiday status. Such period is dependent upon the number of components out of which the project consists. For each component certified, tax holiday status is granted for a period of two consecutive years of assessment. This will have the effect that a qualifying company will be eligible for tax holiday status for a period of:

- two consecutive years of assessment where one component has been certified;
- four consecutive years of assessment where two components have been certified; and
- six consecutive years of assessment where three components have been certified.

Subsection (10): Where a project consists of a human resource component, the two year tax holiday status in respect of the human resource component will only commence after the expiration of the tax holiday status in respect of every other component. The purpose of this deeming provision is to allow the tax holiday status attributable to the spatial and/or industry component to run first so as to allow the board time to monitor the human resource component for final approval at a later stage.

Subsection (11): The tax holiday status of a qualifying company commences from the beginning of the first year of assessment during which the company derives a taxable income. In this regard see also the explanation with regard to subsection (13).

Subsection (12): The reason for the introduction of the provisions of this subsection is set out in the explanation of "tax holiday status". The measures are of a transitional nature by reason of the fact that the Minister of Finance has already fixed the rate of tax payable by companies with financial years which end on or before 31 March 1997.

The tax holiday status in respect of years of assessment ending on or before 31 March 1997 will be determined by allowing a deduction equal to the taxable income of such company before the application of the provisions of section 37H. Tax holiday status in respect of future years will be determined on the basis of applying a zero rate of normal tax.

Subsection (13): This subsection provides that a company must utilise its tax holiday status within 10 years from the commencement of the year of assessment during which the project was approved as a

qualifying project. As the tax holiday status commences only once the company has a taxable income, it is possible that if it is not profitable within 4, 6 or 8 years (depending on how many components the project consists of), it may have to forfeit a portion of its benefit. Only companies which are profitable will enjoy the full benefit of a tax holiday.

Example:

1. A project consisting of the spatial and industry components is approved and commences carrying on its project in the 1999 year of assessment. It makes losses for the first 3 years and thereafter has a taxable income. The financial year ends on 30 June. The tax position for the 10-year period will be as follows:

TAX YEAR	TAXABLE INCOME	TAX HOLIDAY
1999	(100 000)	N/A
2000	(300 000)	N/A
2001	(50 000)	N/A
2002	50 000	YES
2003	150 000	YES
2004	276 000	YES
2005	363 000	YES
2006	425 000	N/A
2007	550 000	N/A
2008	550 000	N/A

This company will, therefore, obtain the maximum benefit of the tax holiday status for 4 years.

2. A project consisting of all three components is approved and commences during the 1998 year of assessment. The company makes losses for the first 5 years and thereafter has a taxable income. The financial year ends on 31 March. The tax position for the 10-year period will be as follows:

TAX YEAR	TAXABLE INCOME	TAX HOLIDAY
1998	(100 000)	N/A
1999	(300 000)	N/A
2000	(350 000)	N/A
2001	(265 000)	N/A
2002	(45 000)	N/A
2003	76 000	YES
2004	168 000	YES
2005	257 000	YES
2006	350 000	YES
2007	475 000	YES

In this example the company will forfeit the sixth year of its tax holiday status, as it would not have utilised the benefit within the 10-year period.

Subsection (14): These provisions grant the power to the Minister of Trade and Industry to make regulations in consultation with the Minister of Finance. The regulations may—

(a) prescribe the investment requirements for any project regarding the amount of capital invested in land whereon and buildings wherein the process of manufacture will be carried on and machinery and plant to be used directly in the process of manufacture;

(b) provide for the demarcation of locations with an existing specialisation and advantage in manufacturing within which projects may be carried on (the spatial component), having regard to the—

- reinforcement of secondary cities;
- reinforcement of key urban nodes along development corridors;
- consolidation of emerging agglomeration areas where sufficient infrastructure exists; and
- diversification of local economies where sufficient appropriate infrastructure is available as a result of the restructuring of existing manufacturing activities;

(c) identify any manufacturing group contemplated in the SIC code which is likely to contribute most significantly to the achievement of sustainable economic growth and employment creation (industry component) having regard to—

- employment and output linkages throughout the economy;
- capital to human resource ratio;
- generation of increased output; and
- international demand for the group's products, goods, articles or other things;

(d) prescribe the necessary human resource remuneration as a ratio to value added (human resource component);

(e) prescribe criteria to determine for the purposes of—

- subsection (3)(a), whether the project which is to be carried on by a company is *substantially* the same manufacturing concern as was previously carried on by any other person within the Republic, having regard to the—
  - — scale and scope of the project;
  - — extent of the utilisation of machinery and plant or human resources;
  - — influence on the national normal tax base; and
  - — relationship between such company or its shareholders and any previous owner of the manufacturing concern; and
- subsection (3)(b), when the carrying on of a project commences;

(f) define any expression in subsection (14), if necessary;

(g) further describe and define the soft-issues which the board must consider when determining whether a project is a qualifying project;

(h) prescribe and define any other conditions for the evaluation, approval or monitoring of a project or the monitoring of the tax holiday scheme as the Minister may deem necessary.

Subsection (15): The provisions contained in this subsection deal with the withdrawal of the tax holiday status under certain circumstances.

In terms of paragraph (a) the approval of a project as a qualifying project shall be withdrawn from the commencement of the year of assessment during which the approval was granted, if the company obtained the approval by fraudulent means or in consequence of misrepresentation or the non-disclosure of material facts.

In terms of paragraph (b) the certification of the human resource component shall be withdrawn by the board if it is satisfied that the human resource component does not comply with the prescribed ratio of human resource remuneration to value added.

Where the review was done in terms of—

- subsection (8)(b)(i), the certification shall be withdrawn from the date of commencement of the year of assessment wherein such review takes place; and
- subsection (8)(b)(ii), the certification shall be withdrawn from the date of the board's initial certification.

The certification will also be withdrawn where a spatial component or industry component no longer complies with the conditions of the spatial or industry components, eg it relocates to a location which does not meet the conditions set out in the regulations as at the time of the approval. Such withdrawal will, however, take place only from the commencement of the year in which the relevant component no longer constitutes a spatial component or industry component (as the case may be) as originally certified by the board.

The above withdrawals will be effected by the board.

Finally, the tax holiday status of a company will lapse, unless the Commissioner otherwise directs, where any company is involved in transfer pricing whereby the taxable income of the qualifying company is, for example, increased in order to take advantage of the provisions of this section. The tax holiday status will lapse from the commencement of the year of assessment during which the qualifying company enters into a transfer pricing transaction, operation or scheme.

Subsection (16): Where a company has been involved in fraud, misrepresentation or non-disclosure of any material fact, it could, in addition to forfeiting its tax holiday status, also be liable to pay additional tax (penalties) to the extent of twice the tax which would have been chargeable in respect of each of the years of assessment in which the tax holiday status was previously granted, but should not have applied.

Subsection (17): These provisions allow the Commissioner the discretion to remit the whole or portion of the additional tax chargeable in terms of subsection (16). Where the Commissioner and the company agree on the amount of the additional charge, the amount will not be subject to objection and appeal.

Subsection (18): Once the board has made a decision with regard to the approval of the project in terms of subsection (2), the non-approval in terms of subsection (3), the consideration of the soft-issues in terms of subsection (7), whether a company has obtained tax holiday status by reason of fraud, misrepresentation or the non-disclosure of any material fact as contemplated in subsection (15)(a) or that the project no longer complies with the criteria for the different components in terms of subsection (15)(b) or (c), it must advise both the company and the Commissioner accordingly. Such notification together with reasons for any decision must take place within 30 days after the approval of the minutes of the meeting whereat such decision was taken.

Subsection (19): In view of the fact that the board is entrusted with certain functions regarding for instance the approval of projects, it may be necessary for the Commissioner to disclose certain information regarding the relevant company's affairs to the board. At present section 4 of the Income Tax Act prohibits such an action and the provisions of this subsection override the provisions of section 4 to enable the Commissioner to disclose the necessary information.

Before the information is, however, disclosed, the company is afforded the opportunity to object thereto in writing.

Subsection (20): The provisions of this subsection ensure that information which is disclosed to the members of the board is not disclosed to any other person and requires the members to take an oath or make a solemn declaration of the preservation of secrecy. Any member of the board who contravenes these provisions is liable to a fine, imprisonment or both.

Subsection (21): The provisions of this subsection permit the Commissioner to raise additional assessments on the withdrawal of the certification of a component of a company or where the tax holiday status has lapsed, notwithstanding the three year limitation prescribed by section 79 of the Income Tax Act.

Subsection (22): Any decision of the Commissioner in terms of the section shall be subject to objection and appeal.

Subsection (23): A company which feels aggrieved by a decision of the board may refer the decision to the relevant division of the Supreme Court, which may review the decision on the following grounds—

- interest in the application, bias, malice or corruption on the part of any member of the board;
- gross irregularity in the proceedings; and
- exercise of its powers in an arbitrary, *mala fide* or unreasonable manner.

Subsection (24): Where the court reviews a decision and is satisfied that any grounds for review has been proved and the company has been substantially prejudiced by the decision, it may set aside the decision and order that the board must consider afresh the matter in respect of which the decision was made.

Subsection (25): A company which feels aggrieved by a decision of the board on a question of law, may appeal to the relevant division of the Supreme Court against the decision. Where the court is satisfied that the board misdirected itself, the court may set aside the decision and order that the board must consider afresh the matter in respect of which the decision was made.

The provisions of the proposed section 37H will come into operation on 1 October 1996.

CLAUSE 13

Levy and recovery of secondary tax on companies (STC): Amendment of section 64B of the Income Tax Act, 1962

Subclause (1)(a): This amendment is of a textual nature.

Subclause (1)(b): In terms of this amendment two further paragraphs are added to the exemptions from STC under section 64B(5) of the Income Tax Act, 1962. The first amendment (the addition of paragraph *(i)* to section 64B(5)) is consequential upon the introduction in terms of *clause 12* of this Bill, of the provisions regulating a tax holiday scheme for certain companies. In terms of the aforementioned provisions a qualifying company will be charged with normal tax at the rate of zero per cent. Although no tax will actually be payable, the company will still be required to compute a taxable income.

In addition to the above it is also proposed that such a company will not be liable for the payment of STC on dividends declared during the period ending 6 months after the end of the last year of assessment during which such company qualifies for tax holiday status. Furthermore, the STC exemption will be restricted to dividends declared out of profits derived during the period during which such company qualified for tax holiday status. The amendment introduced in terms of this subclause, gives effect to such proposal.

The second amendment (the addition of paragraph (j) to section 64B(5)) deals with dividends declared by certain unit trust schemes. At present unit trust schemes in securities are liable for the payment of STC on the declaration of dividends to their unit holders. However, such schemes do not, in terms of ordinary rules, form part of the corporate sector as is the case with, for example, companies and close corporations. For the purposes of the Income Tax Act, such schemes were, however, specifically included in the definition of ''company''. The inclusion at the time was in order to exempt from tax, dividends received by such schemes and to reduce the tax liability of the ultimate investors in such schemes.

STC, on the other hand, was introduced partly to compensate the State for the loss of revenue arising from a reduction in the corporate tax rate and also to encourage companies to retain profits for investment purposes. As unit trust schemes are obliged to distribute all their income and are accordingly

not effectively liable to corporate tax, no direct benefit was derived by the unit trust schemes from the introduction of STC. An additional tax burden may, therefore, result as there is one area in which a potential STC liability could occur for a unit trust scheme and that is where notional income accruals are made upon the creation of units and such notional accruals are distributed as part of the dividend distributions.

Notional income accruals, which result in the major portion of a unit trust scheme's STC liability, occur whenever a unitholder acquires a unit. A portion of the price of the unit acquired represents income already earned by the unit trust scheme, but not yet distributed. In other words, a portion of the unit price will be redistributed to the unit holder at the time of the distribution subsequent to the purchase of the unit. As there is no corresponding dividend accrual, the unit trust scheme will be liable to pay STC on such notional income accruals.

The purpose of the amendments introduced in terms of this clause is, therefore, to exempt a unit trust scheme in securities from the payment of STC on any dividend declared by it.

CLAUSE 14

General provisions with regard to information, documents or things: Substitution of section 74 of the Income Tax Act, 1962

In terms of the Income Tax Act, 1962, as well as other Acts administered by the Commissioner for Inland Revenue, the Commissioner has wide powers with regard to the obtaining of information, in particular with regard to the search and seizure of information and documents. The adoption of the Interim Constitution, however, necessitated the reappraisal of these powers as it is generally believed that such powers may violate a person's fundamental right to privacy.

Certain shortcomings of the provisions with regard to the Commissioner's powers to search and seize documents were pointed out in the First Interim Report of the Katz Commission; and it was recommended that consideration be given to the following:

- where feasible, prior authorisation must be obtained in order to execute a valid search and seizure;
- authorisation must be granted by a neutral and impartial person capable of acting judicially; and
- the minimum standard requires that the person issuing a warrant must on reasonable and proper grounds established by information given under oath, believe that an offence has been committed and that evidence will be found at the place of the search.

The Commission furthermore pointed out that given the circumstances of the case, the purposes underlying the intrusion, the absence of any alternative method of obtaining the necessary evidence and the likelihood of accomplishing the goal as a result of the intrusion, exceptions can be made to the rule.

In the light of the abovementioned the provisions of section 74 of the Income Tax Act have been substituted by the proposed sections 74, 74A, 74B, 74C and 74D. Similar measures have also been introduced in virtually all other Acts administered by the Commissioner. Certain consequential

amendments are also proposed to the penalty provisions of the relevant Acts with regard to the committing of offences. The explanation with regard to the proposed measures to be introduced into the Income Tax Act, therefore also applies to the proposed measures to be introduced into the other Acts.

Proposed section 74: Definitions

The proposed section 74(1) introduces a number of definitions for the purposes of the proposed sections 74, 74A, 74B, 74C, 74D and 75. These new definitions are:

''administration of this Act'' — This expression is defined in order to identify the purposes for and circumstances under which the Commissioner may exercise his powers to obtain information, documents or things, or hold inquiries, or conduct a search and seizure exercise.

''authorisation letter'' refers to a written authorisation granted to officers to, for example, do ''field audits'' and allows for such letters to be issued by the Commissioner, or any chief director, receiver of revenue or chief revenue inspector under the direction and supervision of the Commissioner.

The expressions ''documents'', ''information'' and ''things'' have been defined in such a manner so as to cast the ambit thereof as wide as possible and are self-explanatory.

''judge'' includes a judge of the Supreme Court sitting in chambers, as it is envisaged that when an *ex parte* application in terms of section 74C or 74D is made, such application will be brought to a judge in chambers rather than a judge sitting in court.

''officer'' means an officer as contemplated in section 3(1) of the Income Tax Act.

''premises'' include any building, premises, aircraft, vehicle, vessel or place.

''warrant'' means an order granted by a judge to allow an officer to search for and seize information, documents or things, as contemplated in section 74D.

Subsection (2) provides that where information or documents are not in one of the official languages, the Commissioner may in such case require the taxpayer to furnish a translation thereof in one of the official languages. Should the taxpayer default in providing such translation, the Commissioner may require any other person to produce such translation. The Commissioner may also prescribe the language into which the information or document is to be translated.

Subsection (3) provides that the translation referred to above, shall be—

- produced at the time and place specified by the Commissioner; and
- prepared by a sworn translator or any other person approved for this purpose by the Commissioner.

Subsection (4) provides that the Commissioner may delegate his powers to authorise a person to conduct an inquiry as contemplated in section 74C or to apply for the issue of a search warrant as contemplated in section 74D.

Proposed section 74A: Furnishing of information, documents or things by any person

The proposed section 74A provides that the Commissioner may require any taxpayer to furnish such information (either in writing or orally), documents or things as he may require. The Commissioner's powers in this regard are, however, directed at the supply of information with regard to a specific taxpayer. In exercising such powers, the Commissioner may request the taxpayer himself or any other person to furnish such information, documents or things he may require for the purposes of the administration of the Act in relation to the tax affairs of such taxpayer.

Proposed section 74B: Obtaining of information, documents or things at certain premises

The proposed section 74B(1) provides that an officer authorised in terms of an authorisation letter should make arrangements with a taxpayer prior to carrying out an audit, inspection or examination giving the taxpayer reasonable notice of the intended audit, inspection or examination. Once again the examination or inspection should be directed at the affairs of a specific taxpayer and in this regard an officer may request the taxpayer, or any other person, to furnish, produce or make available such information, documents or things as the officer may wish to inspect, audit, examine or obtain for the purposes of the administration of the Act in relation to the taxpayer.

Subsection (2) provides that such an audit or inspection shall be carried out during the normal business hours of the taxpayer concerned, and at any premises as arranged with such taxpayer prior to the inspection or audit.

Subsection (3) requires the consent of the occupant before an officer may enter a dwelling-house or domestic premises. The limitation provided for in this subsection does, however, not apply to any part of such a dwelling-house or domestic premises occupied or used for the purposes of the taxpayer's trade.

Subsection (4) provides that any officer shall produce his written authorisation letter on demand during an inspection or audit.

Proposed section 74C: Inquiries

The proposed section 74C introduces new provisions with regard to formal inquiries made by the Commissioner.

Subsection (1) provides that the Commissioner, or an officer to whom he has delegated his powers under section 74(4), may authorise any person to make an inquiry. It is envisaged that, should the circumstances warrant it, persons other than officers, such as advocates or attorneys, be authorised in terms of this subsection to assist in the making of an inquiry.

Subsection (2) provides that the Commissioner, or an officer contemplated in section 74(4), may apply to a judge for an order designating a presiding officer before whom the inquiry will be conducted. This provision, therefore, introduces the important principle that an impartial person, namely a judge of the Supreme Court, appoints the person under whose guidance the inquiry will take place.

Subsection (3) provides that a judge may grant an order designating a person to act as presiding officer on *ex parte* application by the Commissioner and that such presiding officer shall be a person appointed by the Minister of Finance to act as a Chairman of the Special Board. The reimbursement of both the person appointed to conduct an inquiry and the person designated to act as presiding officer, will be dealt with in terms of current Treasury instructions regulating matters of this nature.

Subsection (4) provides that an application to the judge requesting an inquiry, must be supported by information under oath or solemn declaration, setting out the facts on which the application is based. The onus of proof to satisfy the judge that an order should be granted, therefore rests with the Commissioner.

Subsection (5) lists the requirements that a judge must satisfy himself have been complied with before he grants an order allowing an inquiry to be made. The judge must be satisfied that there are reasonable grounds to believe that—

- there has been non-compliance with the provisions of the Act or an offence under the Act has been committed;
- information, documents or things are likely to be revealed which may afford proof of such non-compliance or offence; and
- the inquiry in question is likely to reveal such information, documents or things.

Subsection (6) prescribes the information that should be contained in an order by a judge, namely:

- the name of the presiding officer;
- the alleged non-compliance or offence to be inquired into;
- the name of the person alleged to have failed to comply with the provisions of the Act or to have committed the offence; and
- a reasonably specific description of the ambit of the inquiry.

Subsection (7) provides that a presiding officer shall be a person appointed by the Minister of Finance in terms of section 83A(4) of the Income Tax Act.

Subsection (8) provides that the presiding officer shall—

- determine the proceedings of the inquiry as he thinks fit;
- have the same power to compel the attendance of witnesses and the giving of evidence or to submit evidential material, as is vested in the President of the Special Court for hearing Income Tax Appeals; and
- record the proceedings and evidence at an inquiry in the manner he thinks fit.

Subsection (9) provides that the presiding officer may issue a written notice to any person, requiring such person to appear at the inquiry and to give evidence at the inquiry. The proposed subsection also provides that evidence shall be given under oath or solemn declaration.

Subsection (10) provides that the notice issued by the presiding officer shall specify:

- the place where the inquiry will be held;
- the date and time of the inquiry; and
- the reasons for the inquiry.

Subsection (11) provides that the person whose affairs are investigated shall be entitled to be present throughout the inquiry, but grants the power to the presiding officer to exclude such person or his representative, or both of them, from the inquiry if the presiding officer deems their continued presence to be prejudicial to the effective conduct of the inquiry.

Subsection (12) provides that a person required to appear before a presiding officer, has the right to a representative of his choice.

Subsection (13) provides for the proceedings of the inquiry to be conducted *in camera*, in order to safeguard the interests of the person whose affairs are under investigation.

Subsection (14) allows for witnesses, including the person whose affairs are under investigation, to be compensated for reasonable expenses incurred in attending the inquiry, in accordance with the tariffs relating to compensation of witnesses prescribed in terms of section 51*bis* of the Magistrates' Courts Act, 1944.

Subsection (15) provides that where a person who is conducting the inquiry is not an officer, he shall be bound by the secrecy provisions of section 4.

Proposed section 74D: Search and seizure

The proposed section 74D regulates the Commissioner's powers with regard to the search and seizure of information, documents or things.

Subsection (1) provides that a judge may issue a warrant authorising a search and seizure, on the basis of an *ex parte* application by the Commissioner or an officer contemplated in subsection (4). The proposed subsection also regulates the Commissioner's powers in conducting a search for and seizure of information, documents or things. In this regard an officer may be authorised to—

- enter and search any premises;
- search any person on such premises, provided that the person being searched is of the same gender as the officer conducting the search;
- seize information, documents or things discovered during the search; and
- open, or cause to be opened or to be removed and opened, anything on the premises suspected of containing information, documents or things.

Subsection (2) provides that an application by the Commissioner shall be supported by an affidavit or solemn declaration which must contain the facts on which the application is based.

Subsection (3) lists the requirements that a judge must satisfy himself of having been complied with before he issues a warrant allowing a search. The judge must be satisfied that there are reasonable grounds to believe that—

- there has been non-compliance with the provisions of the Act or the committing of an offence;
- information, documents or things which may afford evidence of such non-Dcompliance or the committing of such offence are likely to be found; and
- the premises specified in the application are likely to contain such information, documents or things.

Subsection (4) prescribes the information that should be contained in the warrant, namely:

- a reference to the alleged non-compliance or offence referred to in the affidavit;
- the premises to be searched;
- the name of the person alleged to have failed to comply with the provisions of the Act or to have committed the offence; and
- a reasonably specific description of the information, documents or things to be searched for and seized.

Subsection (5) provides for an exception to the normal rule in the sense that where an officer named in a warrant has reasonable grounds to believe that—

- the relevant information, documents or things are at any premises not identified in the warrant;
- such information, documents or things are about to be removed or destroyed; and
- a warrant cannot be obtained timeously to prevent such removal or destruction,

the officer may search such other premises and exercise his powers in the same manner as if such premises have been identified in the relevant warrant.

Subsection (6) provides that an officer conducting a search may seize information, documents or things not referred to in the affidavit or solemn declaration referred to above, or set out or prescribed in the warrant, if such officer has reasonable grounds to believe that such other information, documents or things affords evidence of the non-Dcompliance with the Act or the committing of the offence, referred to in the warrant.

Subsection (7) provides that the officer exercising any of the powers under the proposed section 74D shall on demand produce the relevant warrant.

Subsection (8) provides that the Commissioner shall take reasonable care to ensure that the information, documents or things seized are preserved. In addition thereto, the information, documents or things may be retained until the conclusion of the investigation or until they are required in any legal proceedings, whichever occurs last.

Subsection (9) provides that any person may apply to the relevant division of the Supreme Court for the return of such information, documents or things and the Court may, on good cause shown, make such order as it deems fit.

Any person to whose affairs the information, documents or things relate, is in terms of the proposed subsection (10) entitled to—

- examine and make extracts therefrom; and
- obtain one copy thereof at the expense of the State.

The aforementioned will be allowed during normal business hours and under the control and supervision of the Commissioner.

CLAUSE 15

Penalty on default: Amendment of section 75 of the Income Tax Act, 1962

The introduction, in terms of *clause 14* of this Bill, of revised provisions into the Income Tax Act with regard to the—

- furnishing and production of any information, documents or things;
- search for and seizure of any information, documents or things; and
- making of inquiries,

necessitates the introduction of amendments to the provisions regulating the imposition of penalties where offences have been committed. The amendments introduced in terms of this clause are, therefore, consequential upon the introduction of such revised provisions.

CLAUSE 16

Offences in respect of supply and obtaining of information, documents or things, as well as inquiries and searches and seizures: Insertion of section 28B in the Stamp Duties Act, 1968

The introduction, in terms of *clause 18* of this Bill, of revised provisions into the Stamp Duties Act with regard to the—

- furnishing and production of any information, documents or things;
- search for and seizure of any information, documents or things; and
- making of inquiries,

necessitates the introduction of amendments to the provisions regulating the imposition of penalties where offences have been committed. The amendments introduced in terms of this clause are, therefore, consequential upon the introduction of such revised provisions.

CLAUSE 17

Powers of search for and seizure of forged stamps, etc: Repeal of section 29 of the Stamp Duties Act, 1968

The repeal of section 29 of the Stamp Duties Act in terms of this clause, is consequential upon the introduction of revised measures into the Stamp Duties Act with regard to, *inter alia*, the committing of offences.

CLAUSE 18

General provisions with regard to information, documents or things: Substitution of section 31 of the Stamp Duties Act, 1968

See the explanation with regard to *clause 14*.

CLAUSE 19

Stamp duty: Amendment of Item 15 of Schedule 1 to the Stamp Duties Act, 1968

At present the provisions of Item 15(3)(h) of Schedule 1 to the Stamp Duties Act, 1968, provides for an exemption from the payment of stamp duty on the registration of transfer of marketable securities from one pension fund registered in terms of the Pension Funds Act, 1956, to another, where such transfer is made in pursuance of a scheme referred to in section 14(1) of that Act. The lastmentioned section refers to the—

- amalgamation of any business carried on by a registered fund with any business carried on by any other person whether registered or not;
- transfer of any business from a registered fund to any other person; or
- transfer of any business from any other person to a registered fund.

In terms of the proposed amendment a further paragraph is inserted under the exemptions from the duty in respect of the registration of transfer of marketable securities. The effect thereof will be that any registration of transfer of any marketable security from—

- a pension fund established by law to a registered pension fund; and
- any previous fund to the Government Employees Pension Fund,

will be exempt from stamp duty.

A previous fund is a fund contemplated in section 14(5) of the Government Employees Pension Fund Law, 1996, and encompasses Government pension and superannuation funds of the former TBVC countries.

CLAUSE 20

Certain supplies of goods or services deemed to be made or not made: Amendment of section 8 of the Value-Added Tax Act, 1991

Section 8(13) provides that a person with whom a bet is placed (for instance a bookmaker) is deemed to supply a service to the person who places the bet with him. The bookmaker is, therefore, liable for output tax equal to the tax fraction of the amount that is received in respect of the bet. The bookmaker (a vendor) is in terms of section 16(3)(d) entitled to an input tax deduction equal to the tax fraction of any amounts paid out as a prize or winnings by him. In this way the amount retained by him, ie his value added, is taxed.

Where the bookmaker (A) in turn places a bet with another bookmaker (B) who is also a vendor, B will be liable for output tax in terms of section 8(13) and A will be entitled to an input tax deduction in terms of the normal provisions of section 16(3)(a)(i) and the definition of "input tax" as the services were acquired by A wholly for the purpose of consumption, use or supply in the course of making taxable supplies. This is a common practice with bookmakers to limit their losses where very big bets are placed on a particular horse.

When B pays out a prize or winnings he will, again, be entitled to a 16(3)(d) deduction, but as the law now reads there is no corresponding requirement that output tax be declared by bookmaker A who is a vendor. This results in a loss to the State.

To correct this situation, section 8(13A) is inserted whereby bookmaker A in the above illustration will be liable for a deemed output tax where he receives any amount as a prize or winnings in consequence of a bet he has placed with bookmaker B.

It should be noted that the provisions inserted by section 8(13A) are only applicable to vendors making taxable supplies of services as contemplated in section 8(13) — in other words mostly bookmakers.

The amendment to this clause should be read with the amendment discussed in *clauses 21 and 22*.

CLAUSE 21

Time of supply: Amendment of section 9 of the Value-Added Tax Act, 1991

The time at which the deemed supply in terms of the new section 8(13A) is deemed to take place, is whenever any amount is paid out as a prize or winnings by the supplier of the deemed section 8(13) services (bookmaker B in the illustration used in *clause 20*).

CLAUSE 22

Value of supply of goods or services: Amendment of section 10 of the Value-Added Tax Act, 1991

A valuation rule is introduced by subsection (17A) whereby the consideration in money for the deemed supply introduced by the new section 8(13A), is deemed to be the amount that is received as a prize or winnings. The amendment to this clause should be read with the amendment discussed in *clause 20*.

CLAUSE 23

Information: Repeal of section 56 of the Value-Added Tax Act, 1991

This amendment is consequential upon the amendments introduced in terms of *clause 24* of this Bill. As the powers of the Commissioner in terms of section 56 of the Value-Added Tax Act (VAT Act) have now been incorporated in the proposed sections 57, 57A, 57B and 57C to be introduced into the VAT Act by the aforementioned clause, the provisions of section 56 of that Act have become obsolete and are, therefore, hereby repealed.

CLAUSE 24

General provisions with regard to information, documents or things: Substitution of section 57 of the Value-Added Tax Act, 1991

See the explanation with regard to *clause 14*.

CLAUSE 25

Offences: Amendment of section 58 of the Value-Added Tax Act, 1991

The introduction of the amendment proposed in terms of this clause, is consequential upon the introduction of revised measures into the VAT Act in terms of *clause 24* of this Bill, with regard to, *inter alia*, the furnishing of information, the production of documents or the questioning of persons for the purposes of the administration of the aforementioned Act.

CLAUSE 26

Establishment and composition of Board: Amendment of section 2 of the Regional Industrial Development Act, 1993

This amendment is consequential upon the introduction of the tax holiday scheme in terms of *clause 12* of the Bill. As mentioned in the explanation with regard to that clause, the evaluation and approval of projects will be done by an existing body of persons namely, the Regional Industrial Development Board established in terms of the Regional Industrial Development Act, 1993. As that board will also be responsible for the performance of certain functions in terms of the tax holiday scheme, it is necessary to extend the membership thereof as well as the powers and functions of the board. The measures introduced in terms of this clause effect an amendment to that Act whereby the membership of the board is extended to also include a member of the South African Revenue Service, while the amendment introduced in terms of *clause 27* extends the functions and powers of the board to enable it to administer the tax holiday scheme.

CLAUSE 27

Functions, powers and duties of Board: Amendment of section 5 of the Regional Industrial Development Act, 1993

See the explanation in respect of *clause 26.*

CLAUSE 28

Exemption from stamp duty or transfer duty relating to transfer of marketable securities or property or of rights or obligations under bonds under scheme for rationalisation of group of companies and assessment of companies in such group for income tax purposes in certain circumstances: Amendment of section 39 of the Taxation Laws Amendment Act, 1994

Section 39 of the Taxation Laws Amendment Act, 1994, was introduced to soften the tax impact on rationalisation schemes of groups of companies which are effected for commercial reasons. Limited exemption from transfer duty and stamp duty is granted and in addition the income tax effects of such rationalisations are regulated.

It is proposed that the definition of ''controlling company'' be amended to also include certain companies which are not listed companies as defined. The reason is that it has come to light that there is a need amongst groups of companies whose controlling companies are not necessarily listed companies, but the scope of activities and size of the group are comparable to the larger listed companies, to rationalise such groups. To accommodate such a restructuring, it is proposed that the definition of ''controlling company'' be widened to also include a ''holding company'' as defined.

A ''holding company'' is a company whose fixed capital (being share capital, share premium, accumulated profits, whether of a capital nature or not, or any other permanent owners' capital) amounted to more than R250 million as established at the end of the year of assessment immediately prior to the date on which the agreement referred to in the definition of ''rationalisation scheme'' has been concluded.

CLAUSE 29

Interest on underpayments and overpayments of provisional tax: Amendment of section 24 of the Income Tax Act, 1996

These amendments are consequential upon the amendments proposed in *clause 30.*

CLAUSE 30

Transactions, operations or schemes for purposes of avoiding or postponing liability for or reducing amounts of taxes on income: Amendment of section 29 of the Income Tax Act, 1996

Section 29 of the Income Tax Act, 1996, introduced, *inter alia*, a business purpose test into the anti-avoidance provisions of section 103 of the Income Tax Act, 1962, and limits the discretion granted

to the Commissioner in terms of section 89*quat*(3) and (3A), in terms of which he may direct that no interest shall be paid.

Such amendments came into operation on 3 July 1996 and are applicable to situations where the provisions of section 103 have been successfully applied in respect of transactions, operations or schemes entered into or carried out on or after that date.

It has been submitted, however, that such amendments may operate retrospectively in certain instances. It is, therefore, proposed that the provisions of sections 24(2) and 29(2), governing the date of commencement of the amendments to sections 89*quat* and 103 of the Income Tax Act, 1962, be amended to place it beyond any doubt that the relevant amendments will not apply on a retroactive basis, but will apply only in respect of any transaction, operation or scheme entered into or carried out or any agreement entered into or effected on or after 3 July 1996.

CLAUSE 31

Definition of ''retirement fund'': Amendment of section 1 of the Tax on Retirement Funds Act, 1996

The definition of ''retirement fund'' in section 1 of the Tax on Retirement Funds Act, 1996, identifies the funds in respect of which a taxable amount in terms of section 5 of such Act is to be determined. In order to preclude any possibility that income derived by a fund which is managed or controlled outside the Republic is taxed on the same amount under both the provisions of the Income Tax Act, 1962, as well as under the Tax on Retirement Funds Act, 1996, it is proposed that paragraph (b) of the definition of ''retirement fund'', referring to funds managed or controlled outside the Republic, be deleted.

CLAUSE 32

Determination of taxable amount of untaxed policyholder fund: Amendment of section 4 of the Tax on Retirement Funds Act, 1996

Section 4 of the Tax on Retirement Funds Act, 1996, was introduced to determine the taxable amount of an untaxed policyholder fund of an insurer for a tax period. The calculation is done by applying a prescribed formula. It has come to light that paragraph (f) of section 4 could possibly be interpreted that the taxable amount must be reduced on a proportionate basis by the income attributable to assets relating to pension, provident and retirement annuity funds. The effect thereof would be that such income must be taken into account twice in reducing the taxable income. It is, therefore, proposed that paragraph (f) of section 4 be amended to prevent a double reduction in respect of the same type of business conducted by an insurer.

CLAUSE 33

Short title

The short title of the amending Act is the Revenue Laws Amendment Act, 1996.