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The analysis of the requirements of the new General Anti Avoidance Rules as compared to the repealed section 103 (1)

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A research report submitted to the Faculty of Commerce, Law and Management in fulfilment of the requirements for the degree of Master of Commerce in the field of Taxation

The analysis of the requirements of the new General Anti Avoidance Rules as compared to the repealed section 103(1)

ABSTRACT

There is a constant struggle between the South African Revenue Services (SARS) and the taxpayer. SARS wants to collect as much money as possible from taxpayers; on the other hand, taxpayers want to pay as little tax as possible. The Government tries to implement new legislation and provisions in the Income Tax Act to make sure that taxpayers are restricted or limited in structuring their agreements in a way that reduces or limits their tax liabilities. On the other hand, taxpayers also try to find loopholes in the Income Tax Act that will work in their favour to reduce their tax liability. Most taxpayers structure their agreements in a way that ensures that they are still within the ambits of the provisions of the Income Tax Act but at the same time, mitigating their tax liability. It has been established over the years that taxpayers have a right to structure their financial affairs in a way that benefits them.

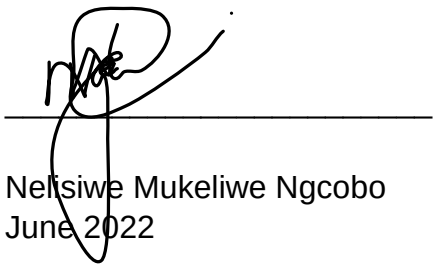
This research paper will be looking at the requirements of the new General Anti Avoidance Rules (section 80A – 80L), compared to the now repealed anti-tax avoidance provisions of the old section 103 (1) of the Income Tax Act, which made a huge impact on this topic as most court cases used the interpretation of this section to reach judgments. The new anti-avoidance provisions are based on the important elements of the old provisions. This research report will analyse the General Anti-Avoidance Rules (GAAR) under section 80A to 80L of the Income Tax Act 58 of 1962. The aim is to analyze and conclude on the developments and effectiveness of the new GAAR in curbing tax avoidance.

Key Words

Tax avoidance, tax evasion, tax planning, General Anti-Avoidance Rules (GAAR), Requirements, Transaction, operation or scheme, Tax effect, Abnormality, Purpose, Impermissible tax avoidance arrangement, tax benefit, Arrangement, Sole or main purpose, Lack of commercial substance, Business context, Business Purpose Test, Significant tax benefit, Substance over form, Onus of proof

DECLARATION

I declare that this research report is based on my own work, it has not been submitted by anyone else before. It is prepared and submitted as required for the degree of Master of Commerce at the University of Witwatersrand.



Nelisiwe Mukeliwe Ngcobo
June 2022

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More than anything I thank God for helping me through it ALL.

List of Abbreviations

CIR	Commission of Inland Revenue
Commissioner	Commissioner for South African Revenue Service
GAAR	General Anti-Avoidance Rules (used for old and new GAAR)
ITC	Income Tax Case
New GAAR	Refers to sections 80A to 80L of Part IIA of Chapter III of the Income Tax Act
OECD	Organisation for Economic Co-operation and Development
Old GAAR	Now-repealed s 103(1)
S	Section
South Africa	Republic of South Africa
s 103(1)	Section 103(1) of the Income Tax Act 58 of 1962
ss 80A-80L	new GAAR sections 80A to 80L of Part IIA of Chapter III of the Income Tax Act
SARS	South African Revenue Service
TAA	Tax Administration Act 28 of 2011
the Act	Income Tax Act 58 of 1962

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CHAPTER 1

1. INTRODUCTION

1.1 Introduction

Tax avoidance and tax evasion is a great concern for most tax authorities across the world and South Africa is no exception. The government gets most of its income from taxpayers and that makes it crucial for government to make sure that its tax policies are effective to enforce compliance from taxpayers.

The willingness of individuals to pay their taxes and comply with tax laws – is driven by several factors which work in combination to define whether people feel inclined or disinclined to contribute to the tax revenue of their country.[1]

Over the years tax avoidance arrangements have become more and more sophisticated, where taxpayers try to disguise transactions from their true nature with the ultimate goal of paying less tax than what they should actually pay. For decades tax authorities across the world, including SARS have implemented different strategies and mechanisms to combat tax avoidance and tax evasion. The introduction of the Organisation for Economic Co-operation and Development (OECD) is one of the means implemented to try to eradicate the disease of offshore tax evasion.

With taxpayers always looking to exploit the loopholes in the tax system, SARS revamped the now repealed GAAR (s 103(1)) and introduced the new GAAR as set out in ss 80A-80L. Throughout this research paper I will be mentioning the 'old GAAR' which refers to the now repealed s 103(1) and the 'new GAAR' which refers to ss 80A-80L. This piece of legislation comes with 12 new provisions that look to eradicate impermissible avoidance arrangements. South Africa has a long history of having a

[1] (SAIPA 2018)

GAAR in its tax legislation, dating back to 1941.[2] South Africa received a world-class new GAAR in 2006, which drew heavily on experiences of and provisions in other jurisdictions.[3]

These provisions are targeting avoidance arrangements that were created for the sole or main purpose of obtaining a tax benefit, which are impermissible avoidance arrangements as defined in s 80A of the Income Tax Act.

The courts have made it clear that the new GAAR may be applied as an alternative or additional basis for an assessment and that it may be applied to steps in or parts of a larger arrangement.[4]

One would be forgiven for thinking that a decade is long enough to have case law on a provision as important as the GAAR. However, to date, there is no major case on the GAAR which has shed light on the scope of the provision. This is not necessarily unique to South Africa. In Australia, when their GAAR in Part IVA of their Income Tax Assessment Act was introduced in 1981, a period of 13 years elapsed before their High Court handed down its first GAAR decision in *FCT v Peabody (1994 181 CLR 359)*[5]. Also, in Canada, it took 17 years for that country's Supreme Court to hand down a decision.[6]

Regardless of the existence of the GAAR or a doctrine that seeks to determine the true substance of the transaction, the plain fact is that a taxpayer can structure a transaction, operation or scheme which has the effect of avoiding tax, with a reasonable prospect of success in his endeavours provided there are sound commercial reasons for arranging

[2] (Kujinga 2017)
[3] (Kruger, Stein, Dachs & Davey 2012)
[4] (Liptak 2017)
[5] FCT v Peabody (1994 181 CLR 359)
[6] (Kujinga 2017)

the transaction in a particular manner – notwithstanding that structuring the transaction in a certain way will provide the taxpayer with a tax benefit.[7]

1.2 Purposes of the study

The purpose of this research report is to investigate and analyse the developments in the Anti-avoidance legislation in South Africa, comparing the old GAAR as set out in Section 103(1) to the new GAAR outlined in Sections 80A-80L of the Income Tax Act. To investigate the reasons why the old GAAR was repealed, the weaknesses of the old GAAR, who bears the onus of proof. The objective is to analyse and conclude on the effectiveness of the new GAAR in curbing tax avoidance.

- What is the difference between tax avoidance, tax evasion and tax planning?
- What is an impermissible tax avoidance arrangement?
- Why was the old GAAR s 103(1) repealed?
- What were the weaknesses in the old GAAR?
- Is the new GAAR ss 80A-80L effective?

1.3 Research methodology

This research report was prepared using the qualitative method, to be able to investigate and analyse the difference between the now repealed GAAR under section 103(1) and the new GAAR under sections 80A-80L of the Income Tax Act. This study will also analyse the requirements between these provisions and identify the weaknesses and why s 103(1) was repealed. Section 103(1) was relied upon and tested enormously by the courts, therefore some of the court cases will be applied accordingly to support or explain some of the requirements or concepts.

[7] (Kruger *et al.* 2012)

This research report will be prepared using data from books, journals, publications, court cases, the Income Tax Act, Tax Administration Act and articles and will be referenced accordingly.

The objective of this research paper will be achieved once the old GAAR and the new GAAR have been compared to be able to determine what developments have been put in place in the new GAAR that will assist SARS to minimise or curbing the tax avoidance and whether the new GAAR is effective as SARS anticipated it to be or not.

CHAPTER 2

2. DIFFERENCE BETWEEN TAX AVOIDANCE, TAX EVASION AND TAX PLANNING?

2.1 Introduction

This chapter will be looking at the differences between the tax avoidance, tax evasion and legitimate tax planning, which are important concepts to understand.

To what extent can you limit your tax liability by being creative with transactions and business structures, without running into trouble with the law? In order to answer this question, one needs to consider the difference between permissible tax avoidance arrangements and impermissible tax avoidance arrangements as well as the difference between tax avoidance and tax evasion.[8]

The impermissible tax avoidance has a wide scope to make sure that it covers as many different types of transactions as possible.

2.2 Tax Avoidance

Taxpayers are always looking for loopholes in the Income Tax Act that they can exploit to minimise their tax liability.

National Treasury defined Tax avoidance as occurring '(w)hen individuals or businesses legitimately use provisions in the tax law to reduce their tax liability.'[9]

The OECD defined avoidance as "A term that is difficult to define but which is generally used to describe the arrangement of a taxpayer's affairs that is intended to reduce his

[8] (South African Tax Guide)
[9] (National Treasury 2021)

tax liability and that although the arrangement could be strictly legal it is usually in contradiction with the intent of the law it purports to follow".[10]

In the past, it was established through different court cases that a taxpayer is allowed to structure their financial affairs in a way that will benefit them and result in a lesser tax liability, as indicated in the below court cases:

This principle is clearly brought out by the following extract from the judgment of Lord Tomlin in *Duke of Westminister v IRC (1953) (at 520*)[11]:

> Every man is entitled if he can to order his affairs so that the tax attaching under the appropriate Acts is less than it otherwise would be if he succeeds in ordering them so as to secure this result, then, however un-appreciative the Commissioner of Inland Revenue or his fellow-taxpayers may be of his ingenuity, he cannot be compelled to pay an increased tax.[12]

In *C: SARS v NWK Ltd*[13] *(supra)* the Supreme Court of Appeal, after having referred to *Erf 3183/1 Ladysmith (Pty) Ltd v CIR 1996 (3) SA 942 (A), Randles Brothers & Hudson Ltd, Commissioner of Customs and Excise v 1941 AD 369, 33 SATC 48* and *Conhage (Pty) Ltd (formerly Tycon (Pty) Ltd), CIR v 1999 (4) SA 1149 (SCA), 61 SATC 391*, stated that:

> "It is trite that a taxpayer may organise his financial affairs in such a way as to pay the least tax permissible. There is, in principle, nothing wrong with arrangements that are tax effective. But there is something wrong with dressing up or disguising a transaction to make it appear to be something that it is not, especially if that has a purpose of tax evasion or of the avoidance of a peremptory rule of law. However, as Hefer JA said in Ladysmith, one must

[10] (OECD)
[11] Duke of Westminster, IRC v [1936] AC 1
[12] (Stiglingh, Koekemoer, van Heerden, Wilcocks & van der Zwan 2021)
[13] C: SARS v NWK Ltd 2011 (2) SA 67 (SCA)

> distinguish between the principle that one may arrange one's affairs so as to 'remain outside the provisions of a particular statute', and the principle that a court 'will not be deceived by the form of the transaction: it will rend aside the veil in which the transaction is wrapped and examine its true nature and substance'".[14]

In Ensign Tankers (Leasing) Ltd v Stokes (Inspector of Taxes) [15]Lord Goff said

> 'Unacceptable tax avoidance typically involves the creation of complex artificial structures by which, as though by the wave of a magic wand, the taxpayer conjures out of the air a loss, or a gain, or expenditure, or whatever it may be, which otherwise would never have existed'.[16]

Some decisions have used the term 'tax avoidance' in a pejorative sense. In *CIR v Challenge Corp Ltd*[17], on appeal to the Privy Council, Lord Templeman took the view that tax avoidance connotes more than merely getting out of the way of an anticipated liability and said that

> 'Income tax is avoided and a tax advantage is derived for an arrangement when the taxpayer reduces his liability to tax without involving him [sic] in the loss or expenditure which entitles him to that reduction. The taxpayer engaged in tax avoidance does not reduce his income or suffer a loss or incur expenditure but nevertheless obtains a deduction in his liability as if he had. . .. In an arrangement of tax avoidance the financial position of the taxpayer is unaffected (save for the costs of devising and implementing the arrangement).[18]

[14] (Kruger *et al.* 2012)
[15] Ensign Tankers (Leasing) Ltd v Stokes (Inspector of Taxes) [1992] 2 All ER 275 (HL)
[16] (de Koker & Williams 2021)
[17] Challenge Corp Ltd, IR Comr v [1986] STC 548, [1987] AC 155
[18] (de Koker & Williams 2021)

In the case of *ITC 1625*[19] it was stated that in order to determine whether a scheme had the effect of the avoidance of tax, it had to be asked whether the taxpayer would "suffer a tax" were it not for the scheme.[20]

In *Smith v CIR*[21] it was held that the ordinary meaning of avoiding liability for a tax on income was 'to get out of the way of, escape or prevent an anticipated liability'.[22]

In *Hicklin v SIR*[23] the Appellate Division acknowledged that such liability may vary from 'an imminent, certain prospect to some vague, remote possibility' and Trollip JA said that

> 'it is unnecessary and hence inadvisable to decide here whether a vertical line should be drawn somewhere along that wide range of meanings in order to delimit the connotation of "an anticipated liability".'[24]

The courts have expressed disapproval of tax avoidance. In *COT v Ferera*[25], MacDonald JP said:

> 'I endorse the opinion expressed that the avoidance of tax is an evil. Not only does it mean that a taxpayer escapes the obligation of making his proper contribution to the fiscus, but the effect must necessarily be to cast an additional burden on taxpayers who, imbued with a greater sense of civic responsibility, make no attempt to escape or, lacking the financial means to obtain the advice and set up the necessary tax-avoidance machinery, fail to do so. Moreover, the nefarious practice of tax avoidance arms opponents of our capitalistic society

[19] ITC 1625 (1996) 59 SATC 383
[20] (Spence Attorneys, Notaries & Conveyancers 2020)
[21] Smith v CIR 1964 (1) SA 324 (A), 26 SATC 1
[22] (de Koker & Williams 2021)
[23] Hicklin v SIR 1980 1 SA 481 (A)
[24] (de Koker & Williams 2021)
[25] Ferera, COT v 1976 (2) SA 653 (RAD)

with potent arguments that it is only the rich, the astute and the ingenious who prosper in it and that “good citizens” will always fare badly.’[26]

A person who willfully issues an erroneous, incomplete or false document to SARS is guilty of an offence and is liable, upon conviction, to a fine or imprisonment for a period not exceeding two years...[27]

“Choice Principle”

There is a well-established principle known as the “choice principle” which was introduced into South African law by *CIR v Conhage 61 SATC 391* and was also referred to by the Supreme Court of Appeal in the *Sasol Oil* case. This principle is well-entrenched in South Africa’s constitutional democracy. The “choice principle” essentially provides that a taxpayer is entitled to structure a transaction in a manner which results in the least tax liability. If, for example, the same commercial result can be achieved in different ways, a taxpayer may enter into a transaction which does not attract tax or attracts the least amount of tax.[28]

In South Africa the Supreme Court of Appeal applied a version of the choice principle in *CIR v Conhage (Pty) Ltd (formerly Tycon (Pty) Ltd)* in a context where the Commissioner was arguing that s 103(1) was applicable. The court held that, where two alternative methods of achieving substantially the same commercial result are available to a taxpayer, his main purpose, as envisaged by s 103(1), is to secure the desired commercial result; by implication, therefore, the taxpayer’s purpose of securing the advantageous tax consequences was regarded as amounting to a subsidiary or incidental purpose which was not sufficient to bring s 103(1) into play.[29]

[26] (de Koker & Williams 2021)
[27] (Stiglingh *et al.* 2021)
[28] (ENSight)
[29] (de Koker & Williams 2021)

The choice principle may be explained as a particular application of the principle of statutory interpretation expressed in the *maxim generalia specialibus non derogant* which connotes that specific provisions of a statute are not to be read down by reason of contrary general provisions. The choice principle may also be implicitly based on a libertarian philosophy regarding the inherent rights of a taxpayer.[30]

2.3 Tax Evasion

Tax evasion is always a challenge because tax evaders benefit themselves at the expense of the country's resources.[31]

Tax Evasion refers to illegal entities deliberately (willfully) undertaken by a taxpayer to free himself from a tax burden. In an income tax context, it typically involves the non-payment of a tax that would properly be chargeable if a taxpayer made a full and true disclosure of income and allowable deductions. The fiscus requires the exercise of reasonable care by taxpayers in complying with the duties imposed on them.[32]

National Treasury defines Tax evasion as 'When individuals or businesses illegally reduce their tax liability.'[33]

The OECD defines evasion as "A term that is difficult to define but which is generally used to mean illegal arrangements where liability to tax is hidden or ignored, i.e. the taxpayer pays less tax than he is legally obligated to pay by hiding income or information from the tax authorities".[34]

[30] (de Koker & Williams 2021)
[31] (SAIPA 2018)
[32] (Stiglingh *et al.* 2021)
[33] (National Treasury 2021)
[34] (OECD)

Common examples of tax evasion include a deliberate (willful) failure by a person carrying on a 'cash' business to report the full amount of revenue received or the deliberate (willful) claiming of a deduction by a business for an expenditure it has neither incurred nor paid. A further example of a tax evasion is where a taxpayer omits income from his annual tax return.[35]

Tax evasion may also result from a bona fide attempt by the taxpayer to arrange his affairs so as to avoid or reduce his tax, which is later ruled by the court to be within the scope of the charging provisions of the tax legislation.

In *CIR v Challenge Corp Ltd* Lord Templeman said

> 'Evasion occurs when the Commissioner is not informed of all the facts relevant to an assessment of tax. Innocent evasion may lead to a reassessment. Fraudulent evasion may lead to a criminal prosecution as well as reassessment.'[36]

Tax evasion is a punishable crime.

Non-compliance with tax Acts as well as the evasion of tax with intent are criminal offences and are subject to severe penalties in terms of ss 234 and 235 of the Tax Administration Act.[37]

Section 235 of the TAA: Evasion of tax and obtaining undue refunds by fraud or theft – a person who with intent to evade or to assist another person to evade tax or to obtain an undue refund under a tax Act –

[35] (Stiglingh *et al.* 2021)
[36] (de Koker & Williams 2021)
[37] (Stiglingh *et al.* 2021)

- Makes or causes or allows to be any false statement or entry in a return or other document, or signs a statement, return or other document so submitted without reasonable grounds for believing the same to be true;
- Gives a false answer, whether orally or in writing, to a request for information made under this Act;
- Prepares, maintains or authorises the preparation or maintenance of false books of account or other records or falsifies or authorises the falsification of books of accounts or other records;
- Make use of, or authorises the use of, fraud or contrivance; or
- Makes any false statement for the purposes of obtaining any refund of or exemption from tax,

  Is guilty of an offence and, upon conviction, is subject to a fine or to imprisonment for a period not exceeding five years.[38]

Tax evasion is illegal and any taxpayer found guilty faces criminal charges which may result in imprisonment[39]

In instances of tax evasion, where taxpayers attempted to mislead SARS, the Commissioner is empowered to disregard the actual rights and obligations as created by a transaction and impose fines, imprisonment, or both. Furthermore, interest on the outstanding amount is payable, as well as an additional tax of up to 200% of the outstanding amount.[40]

The term ‘impermissible avoidance arrangement’, which is now central to the new GAAR contained in Part IIA of the Act, is intended to connote ‘arrangements that fall in

[38] (Professional Tax Handbook. 2020/2021)
[39] (SAIPA 2018)
[40] (South African Tax Guide)

the category between tax evasion, on the one hand, and legitimate tax-planning, on the other'.[41]

2.4 Tax Planning

Often the biggest mistake made by taxpayers is the lack of planning. One can't change the facts and nature of a transaction after it has been completed.[42]

In order to make educated decisions about your business, it's imperative to scope Tax Planning.[43]

"Tax planning" is concerned with the organisation of a taxpayer's affairs (or the structuring of transactions) so that they give rise to the minimum tax liability within the law without resort to the sort of "impermissible tax avoidance" just described. As used in this Discussion Paper, it is similar to the concept of "tax mitigation" described by Lord Templeman:

> "Income tax is mitigated by a taxpayer who reduces his income or incurs expenditure in circumstances which reduce his assessable income or entitle him to reduction in his tax liability. [The General Anti-Avoidance Rule] does not apply to tax mitigation because the taxpayer's advantage is not derived from an arrangement but from the reduction of income which he accepts or the expenditure which he incurs".[44]

The notion of tax planning captures the essence of the famous dictum by Lord Tomlin: "every man is entitled to order his affairs so that the tax attaching under the appropriate Acts is less than it otherwise would be". A GAAR, by its nature, operates in tension with this notion. It imposes limits upon the extent to which an "ordering of affairs" is to be

[41] (de Koker & Williams 2021)
[42] (South African Tax Guide)
[43] (Vorster)
[44] (SARS 2005)

respected for tax purposes. It thus helps to establish the boundary between legitimate tax planning and impermissible tax avoidance.[45]

In *Commissioner v Newman Justice Learned Hand*, in a dissenting opinion, said that

> 'Over and over again courts have said that there is nothing sinister in so arranging one's affairs as to keep taxes as low as possible. Everybody does so, rich or poor, and all do right, for nobody owes any public duty to pay more than the law demands: taxes are enforced exactions, not voluntary contributions. To demand more in the name of morals is mere cant.'[46]

In *Michau v Maize Board* our Supreme Court of Appeal said that

> '. . . parties are free to arrange their affairs so as to remain outside the provisions of a particular statute. Merely because those provisions would not have been avoided had the parties structured their transaction in a different and perhaps more convenient way does not render the transaction objectionable.'[47]

In *C: SARS v NWK Ltd* Lewis JA, giving the judgment of the court, said that

> 'It is trite that a taxpayer may organize his financial affairs in such a way as to pay the least tax permissible.'[48]

In *CIR v Sunnyside Centre (Pty) Ltd* the Appellate Division held that 'a taxpayer is entitled to order his affairs so as to pay the minimum of tax' and in *CIR v Conhage (Pty) Ltd* the Supreme Court of Appeal said that

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[45] (SARS 2005)
[46] (de Koker & Williams 2021) [47]
(de Koker & Williams 2021) [48]
(de Koker & Williams 2021)

> ‘Within the bounds of any anti-avoidance provisions in the relevant legislation, a taxpayer may minimise his tax liability by arranging his affairs in a suitable manner. If, for example, the same commercial result can be achieved in different ways, he may enter into the type of transaction which does not attract tax or attracts less tax.’[49]

The reality of tax planning and avoidance is that it all boils down to the management and planning of the following four elements:

- Timing (when the tax liability will be due);
- Gross income (tax liability is created by having an income);
- Income or capital (tax treatment of capital gains is different from that of revenue/ income); and
- Deductions (deductions against the gross income will reduce the taxable income).

Timing of a transaction is a key part of planning. Planning includes understanding the nature of a transaction and terms of the contract.[50]

2.5 Conclusion

Tax avoidance and evasion are economically costly.

These costs arise in a number of ways. At a basic level, to the extent that impermissible tax avoidance inevitably results in new amendments, more complex legislation and

[49] (de Koker & Williams 2021)
[50] (South African Tax Guide)

increasingly comprehensive and detailed reporting requirements, administrative costs and compliance burdens swell for both taxpayers and the government.[51]

It is crucial for taxpayer and tax advisers to be able to distinguish between tax avoidance and tax evasion as one is legal and the other is illegally; as explained above.

In the recent controversial judgment in *SARS v NWK Ltd (2010)*, the Supreme Court of Appeal seemingly used the words evasion and avoidance interchangeably.[52] This is incorrect because these terms have different meanings and the consequences are also different, tax evasion is a criminal offence whereas tax avoidance is not.

Proper planning beforehand will help understand the tax liability, the timing of the tax liability, disclosure requirements and, most importantly, possible options or alternatives.[53]

[51] (SARS 2005)
[52] (South African Tax Guide)
[53] (South African Tax Guide)

CHAPTER 3

3. REQUIREMENTS UNDER THE OLD GENERAL ANTI-AVOIDANCE RULES AS SET OUT IN SECTION 103(1)

3.1 Introduction and background

This is the third major revamp of section 103(1). In its first phase, section 103(1) lasted from its original enactment in 1978 to its amendment in 1996.

The second phase was effective from 1996 till 1 November 2006, then the third phase was introduced; and it became effective from 2 November 2006 to date.

GAAR is not a new concept in the South African tax system. Over the past years taxpayers became more and more creative in structuring their transactions, always looking for and utilising loopholes in the tax act with the purpose of paying less tax amounts. This forced SARS to also keep up, to strive to close the exploited loopholes.

The pre-1996 section 103(1)

In its pre-1996 format, section 103(1) distinguished between legitimate and illegitimate tax avoidance on the basis of four criteria, namely:

- the existence of a "transaction, operation or scheme";
- that had the effect of avoiding, postponing or reducing liability for tax;
- which was entered into in an abnormal means or manner or which created non-arm’s length rights or obligations between the parties; and
- which was entered into for the sole or main purpose of tax avoidance.

If all of these elements were simultaneously present, section 103(1) empowered the Commissioner to determine the parties tax liability as though the scheme had not been entered into or carried out, or in such other manner as he deemed appropriate to prevent or diminish the tax avoidance. In terms of section 103(4), if a transaction had

the effect of avoiding tax, it was rebuttably presumed that it had been entered into with the sole or main purpose of tax avoidance.[54]

The post-1996 section 103(1)

The second phase of section 103(1) lasted from its 1996 amendment to the coming into force of Part IIA of the Act. The reason for the 1996 amendment was that, from SARS's perspective, a major weakness of section 103(1) in its pre-1996 format was its "abnormality" criteria, for it was possible for taxpayers to argue that that it was not "abnormal" to structure a transaction so as to minimise liability for tax, because it is ordinary business practice to do so. The validity of this argument has never been determined by the courts.

The essence of the 1996 amendments to section 103 was as follows:

- In relation to a transaction, operation or scheme "in the context of business", the "abnormality" criteria were replaced by the criterion of whether the transaction had been entered into or carried out "in a manner which would not normally be employed for bona fide business purposes other than the obtaining of a tax benefit". Consequently, a transaction which was not abnormal in its means or manner or in its rights and obligations (and which would therefore have been outside the scope of section 103(1)) in its pre-1996 format) became vulnerable to the section in its post-1996 format if the transaction fell within the scope of this new formula.
- In relation to a transaction, operation or scheme which was not in the context of business, the Commissioner could invoke section 103(1) where it was entered into by means or in a manner which would not normally be employed in the entering into or carrying out of a transaction, operation or scheme of the nature of the transaction, operation or scheme in question. Transactions

[54] (SAICA March 2007)

which were not "in the context of business" probably included arrangements such as the creation and operation of family trusts, at least where the trust did not carry on a business.

- The amended section 103(1) retained, as an alternative, one of the pre-1996 criteria, namely whether the transaction, operation or scheme "has created rights or obligations which would not normally be created between persons dealing at arm's length under a transaction, operation or scheme in the nature of the transaction, operation or scheme in question".
- A new expression "tax benefit" was introduced into the section and was defined as including any avoidance, postponement or reduction of any tax, duty or levy imposed by the Income Tax Act or any other law administered by the Commissioner.

The 1996 amendments did not abolish the requirement that the taxpayer must have entered into the transaction, operation or scheme solely or mainly for the purposes of obtaining (what was now called) a "tax benefit", and this requirement remained an overriding condition precedent to the application of s 103(1).[55]

A consequence of the way in which the 1996 amendments were drafted was that a taxpayer could, with impunity, enter into a transaction that was (objectively) abnormal, so long as he did not have a (subjective) sole or main purpose of tax avoidance. Conversely, a taxpayer could with impunity enter into a transaction with the (subjective) sole or main purpose of tax avoidance as long as it was not (objectively) abnormal.[56]

A subjective purpose is often not easy to prove and for this reason, once the dispute reaches the tax court or superior courts, the question of whether the Commissioner or the taxpayer bears the onus of proof is of vital concern. Litigation between SARS and

[55] (SAICA March 2007)
[56] (SAICA March 2007)

taxpayers (as with other litigation) is often decided on the basis that, on the evidence before the court, the party who bore the onus of proof has simply failed to discharge it.[57]

Part IIA of the Act

Part IIA of the Act came into operation on 2 November, 2006 and applies to any arrangement entered into on or after that date. The relatively concise provisions of section 103(1) and (3) have been replaced by twelve new complex sections, comprising sections 80A-80L, which together constitute a new Part IIA of the Act entitled "impermissible tax avoidance arrangements".[58]

An unwelcome aspect of the introduction of Part IIA is that it will take many years perhaps decades for the High Court and the Supreme Court of Appeal to rule on the interpretation of these new provisions, and the novel concepts such as "a lack of commercial substance", and whether a particular tax scheme "would result directly or indirectly in the misuse or abuse of the provisions of the Act.[59]

In the meantime, the business community and their professional tax advisers will have to endure prolonged uncertainty as to whether or not a proposed arrangement, or an arrangement which they have in fact entered into, will be found to have infringed Part IIA. This uncertainty will be particularly acute in relation to innovative methods of financing business deals, for it may be very difficult to determine whether or not a particular arrangement "lacks commercial substance" (as contemplated in section 80C) or involves "round trip financing" (as contemplated in section 80D).[60]

[57] (de Koker & Williams 2021)
[58] (SAICA March 2007)
[59] (SAICA March 2007)
[60] (SAICA March 2007)

3.2 The role of the GAAR

"[The GAAR] is perceived legislatively as an essential pillar of the tax system designed to protect the tax base and the general body of taxpayers from what are considered to be unacceptable tax avoidance devices. By contrast with specific anti-avoidance provisions which are directed to particular defined situations, the legislature through [the GAAR] has raised a general anti-avoidance yardstick by which the line between legitimate tax planning and improper tax avoidance is to be drawn. The function of [the GAAR] is to protect the liability for the income tax established under the other provisions of the legislation"[61]

It is equally important to emphasise what a GAAR is not. It is not a charging provision. While the application of the GAAR to impermissible tax avoidance may help to stem the tide of short-term revenue loss, the GAAR itself is not a revenue raising measure. It is intended to protect the tax base established by Parliament, not to expand it.[62]

In *Challenge Corp Ltd v CIR* Richardson J pointed out that the general anti-avoidance provision was never intended to strike down transactions merely because the taxpayer had been influenced by the prospect of obtaining a tax advantage, and, that in many cases, but for the anticipated availability of a tax benefit, the taxpayer would never have entered into the transaction at all.[63]

Issues with s 103(1)

Where the now-repealed s 103(1) applied, the Commissioner was empowered to determine tax liability 'as though the transaction, operation or scheme had not been entered into or carried out or in such manner as in the circumstances of the case he

[61] (SARS 2005)
[62] (SARS 2005)
[63] (de Koker & Williams 2021)

deems appropriate for the prevention or diminution of such avoidance, postponement or reduction [of tax]'.

The difficulty with the power to determine liability 'as though the transaction, operation or scheme had not been entered into or carried out' was that it was expressed as being purely annihilating – that is to say, it allowed the Commissioner to treat the transaction as never having come into existence but did not provide for anything to take its place. Consequently its invocation by the Commissioner might lead to the disallowance of a deduction, but as far as income was concerned, the annihilation of the transaction, operation or scheme would simply leave a vacuum, for the Act did not specify what set of facts or conclusion of law was deemed to take its place and in particular the Act did not provide for any deemed facts that would give rise to a tax liability.[64]

3.3 The four requirements

Under the previous law, before section 103 may be applied, the Commissioner must be satisfied that four elements exist. In the case of a transaction "in the context of business", these requirements may be summarised as follows –

- There must be a "transaction, operation or scheme" (the Scheme Requirement);
- The transaction must result in the avoidance, reduction or postponement of a tax (the Tax Effect Requirement);
- The transaction must have been entered into or carried out in a manner not normally employed for business purposes, other than obtaining a tax benefit, having regard to the circumstances (the Abnormality Requirement); and
- The transaction must have been entered into solely or mainly for the purpose of obtaining a tax benefit (the Purpose Requirement).[65]

[64] (de Koker & Williams 2021)
[65] (SARS 2005)

3.3.1 Transaction, operation or scheme requirement

There has been a growing recognition that many of the most abusive avoidance schemes share common attributes – what have sometimes been called the “hallmarks” or “badges” of avoidance. These characteristics include:

- **The lack of economic substance (usually resulting from pre-arranged circular or self-cancelling arrangements).**

  One of the most important characteristics of abusive avoidance schemes is the lack of economic substance. In many abusive avoidance schemes, the taxpayer purports to make a substantial investment. This investment, however, is largely an illusion. Through various devices, the taxpayer remains insulated from virtually all economic risk, while creating a carefully crafted impression to the contrary.

  In any investment, risk and return are related – the greater the risk, the greater the return. As a consequence, in so far as most abusive avoidance schemes typically involve little or no economic risk, they typically offer little or no opportunity for pre-tax gain. Rather, the “return” to the “investor” takes the form of the significant tax benefits promised by the arrangement. In this manner, “a negligible pre-tax profit is transformed into a significant after-tax return”. Indeed, the mismatch between a limited (or non-existent) potential for pre-tax profit and the promise of very significant tax benefits is often a good indicator of an abusive avoidance scheme.

- **The use of tax-indifferent accommodating parties or special purpose entities.**

  Most abusive avoidance schemes also involve the use of accommodating parties or special purpose entities. Thus, as Lord Diplock has observed: “The kinds of tax avoidance schemes that have occupied the attention of the courts in recent years . . . involve inter-connected transactions between artificial persons, limited companies, without minds of their own but directed

by a single master-mind". In the context of an abusive avoidance scheme, the accommodating party is typically "tax indifferent". Such parties may include foreign persons, partnerships, trusts, pension funds, and taxpayers that can either generate offsetting deductions to absorb any income they derive from their participation in a scheme or utilise existing assessed losses.

- **Unnecessary steps and complexity.**

  Abusive avoidance schemes are often mind-numbingly complex. There are several reasons for this. These schemes often require the completion of certain formalistic steps to claim the desired tax result. In so-called "bare dominium" schemes, for example, promissory notes evidencing future rental obligations are typically discounted through a tax indifferent party in order to enable the financing party to avoid tax on the full amounts received (while the borrower in the transaction continues to claim deductions for the full amount of the "rent"). Steps may also be inserted to prop up a claim of business purpose. Similarly, a complex structure maybe used to disguise the true nature of a scheme or "as a device to cloak the tax shelter transaction from detection". More cynically, promoters may even deliberately add complexity for its own sake in order to justify higher professional fees. The complexity of these schemes, coupled with the lack of any realistic possibility of a meaningful pre-tax profit, has led one expert to describe the typical abusive avoidance scheme as nothing more than a deal done by very smart people that, absent tax considerations, would be very stupid.

- **Inconsistent treatment for tax and financial accounting purposes.**

  There has been an increasing emphasis on keeping a company's reported effective tax rate (i.e., the ratio of its income tax liability to its profits for financial accounting purposes) low and in line with the rates reported by competitors. In order to do this, it is necessary to invent transactions in which the tax treatment varies from the financial accounting treatment.

Thus, “structuring a transaction that results in either a deduction [for tax purposes] without a financial accounting charge or financial accounting revenue without the concomitant imposition of tax can be viewed as a real coup by the tax manager”.

- **High transaction costs.**

  Given the Byzantine complexity of many abusive avoidance schemes and the development and marketing costs often incurred by promoters, it is not surprising that fees tend to be extremely high.

- **Fee variation clauses or contingent fee provisions.**

  In addition to the high fees, many promoters, particularly in the structured finance area, include fee variations clauses in their agreements in order to insulate themselves from any tax risk. Schemes possessing most, if not all, of these characteristics are referred to herein as “abusive avoidance schemes”.[66]

3.3.2 Tax effect requirement

It must be determined whether the transaction, operation or scheme has elements of ‘avoiding’, ‘postponing’ or ‘reducing’ the tax liability. None of these elements (terms) are defined in the income tax act, therefore it was the courts that decided if the transaction does have the tax effect.

A “tax benefit” includes “any avoidance, postponement or reduction of liability for payment of any tax, duty or levy imposed by this Act or by any other law administered by the Commissioner”. Once the Tax Effect Requirement is satisfied, a rebuttable presumption arises that the sole or main purpose of the transaction was to obtain a tax benefit. If a transaction falls within the ambit of section 103, the Commissioner is empowered to determine the liability for tax as if the transaction had not been entered

[66] (SARS 2005)

into or carried out, or, alternatively, “in such manner as in the circumstances of the case he deems appropriate for the prevention or diminution of such avoidance, postponement or reduction”.[67]

3.3.3 Abnormality requirement

Abnormality is not defined in the Act. One has to look at the case law.[68]

Trollip JA indicated that ‘the problem of normality or abnormality was mainly a factual question, and the Court could resolve it by taking judicial notice of relevant norms or standards or by means of the expert or other evidence adduced by either party’[69]

It is abnormal, within the meaning of s 103(1), for a person to arrange for the fruit of his labours to accrue to someone else. If this is done for the purpose of avoiding tax, it will infringe s 103(1).[70]

The Abnormality Requirement itself suffers from two fundamental weaknesses. First, the tax world is not neatly divided into two types of arrangements, one for “bona fide” business transactions and the other for impermissible tax avoidance schemes. To the contrary, scheme promoters routinely “hijack” techniques that were originally developed for bona fide business purposes. Thus, for example, in the film industry, cash strapped independent film makers developed deferred payment arrangements, pursuant to which service providers would agree to postpone payment for some or all of their services until the films generated revenue, as a way to help finance their productions. Scheme promoters then abused this concept to inflate the cost of films in order to maximise any applicable film allowance. Similarly, finance leases and the discounting of promissory notes are both accepted types of bona fide business arrangements. The problem arises when these components are put together in various schemes to create situations in

[67] (SARS 2005)
[68] (Haupt 2017)
[69] Hicklin v SIR 1980 1 SA 481 (A)
[70] (Williams 1995)

which the borrower/lessee seeks to claim a deduction for its full "rental" payments while the lender/lessor seek to include only the "interest" component of those same payments in its income.[71]

The second problem is closely related. Precisely because impermissible tax avoidance schemes hijack techniques that were originally developed for bona fide business transactions, it is relatively easy for promoters to "manufacture" plausible sounding "business purposes". Thus, for example, in various lease-in/lease out and "sale and buy-back" schemes, taxpayers have sought to achieve significant tax deferrals by accelerating payments in one leg of the transaction and deferring them in the other. Promoters would typically contend that these payment terms are "normal", with accelerated payments, for example, reflecting concerns about a borrower's creditworthiness and deferred payments reflecting perhaps a party's projected future cash flows. In most cases, however, there is little or no evidence that the creditworthiness of the borrower was ever a serious consideration or that the payment terms ever varied owing to a party's "projected cash flow profile".[72]

When the Margo Commission issued its report in 1986, it recognised that section 103 as it then stood suffered from serious deficiencies. In particular, its Report stated:

"The test of abnormality presents difficulties. If a particular form of transaction is widely used for tax avoidance purposes, it may gain a commercial acceptability to the extent that its utilization becomes normal. The concept of abnormality must therefore be qualified to this extent".[73]

[71] (SARS 2005)
[72] (SARS 2005)
[73] (SARS 2005)

In 1995, the Katz Commission again recognised that the abnormality requirement was the "Achilles heel" of section 103 and reiterated the concerns of the Margo Commission:

> "the test of abnormality presents difficulties for revenue in that if a particular form of transaction is widely used for tax avoidance purposes, it may gain a commercial acceptability to the extent that its utilisation becomes normal".[74]

The Katz Commission also identified a "further difficulty with the normality test" in that "there is ambiguity as to whether it is objective, that is whether there exists an objective test to be applied despite the context of specific circumstances". In order to remedy these problems, the Katz Commission recommended that "where a transaction occurs in the context of trade, a business purpose test should be substituted for the normality test".

Following the Katz Commission Report, Parliament amended section 103 to read in pertinent part as follows:

1. Whenever the Commissioner is satisfied that any transaction, operation or scheme. having regard to the circumstances under which the transaction, operation or scheme –

   (i) was entered into or carried out –

   > (aa) in the case of a transaction, operation or scheme in the context of business, in a manner which would not normally be employed for bona fide business purposes, other than obtaining a tax benefit . . ."

This language continues to be in effect today.[75]

[74] (SARS 2005)
[75] (SARS 2005)

Section 103(1) does not come into operation unless a sole or main purpose of tax avoidance and abnormality are both present. Hence, if a taxpayer has a purpose of tax avoidance but the transaction was not abnormal, s 103(1) does not apply. Conversely, if the transaction was abnormal, but the taxpayer did not have a sole or main purpose of tax avoidance, s 103(1) does not apply.[76]

3.3.4 Purpose requirement

The problems under the Abnormality Requirement are exacerbated by the current Purpose Requirement. As a threshold matter, the Purpose Requirement can only be met if obtaining a tax benefit is the sole or main purpose of a transaction. The term "main" has generally been construed to mean predominant. In a simple example, if a transaction has both a tax and a commercial purpose, the Purpose Requirement can be satisfied only if it can be proven that the tax purpose was the predominant one. Since most transactions in a business context have at least a colourable commercial rationale, the Commissioner is placed in the difficult position of having to disprove a taxpayer's allegations through circumstantial evidence. In addition, under the current statute, following the Conhage case, taxpayers have frequently argued that a commercial purpose, such as raising capital, for an overall transaction is sufficient to "inoculate" each and every step in it from challenge.[77]

At the heart of s 103(1) were two inter-locking criteria: firstly, the subjective sole or main purpose of the taxpayer to avoid or reduce liability for tax; and, secondly, the objective normality or otherwise of the means or manner in which the transaction was entered into or carried out or of the rights and obligations thereby created.

[76] (Williams 1995)
[77] (SARS 2005)

For s 103(1) to apply to a ‘transaction, operation or scheme’ both the subjective intention and the objective abnormality had to be concurrently present.[78]

The difficulties encountered under the Purpose Requirement are compounded by the fact that it entails a subjective test – one that looks to the purpose the taxpayers purportedly intended to achieve when they carried out their scheme. Consequently, as RC Williams has observed:

> “In essence . . . a taxpayer could with impunity enter into a transaction with the (subjective) sole purpose of avoiding tax provided that there was no (objective) abnormality in the means or manner or in the rights and obligations which it created. Conversely, a taxpayer could with impunity enter into a transaction which was objectively ‘abnormal’ provided that he did not, subjectively, have the sole or main purpose of tax avoidance”.[79]

[78] (de Koker & Williams 2021)
[79] (SARS 2005)

CHAPTER 4

4. REQUIREMENTS UNDER THE NEW GENERAL ANTI-AVOIDANCE RULES AS SET OUT IN SECTION 80A-80L

4.1 Introduction of General Anti-Avoidance Rules

Section 103(1) contained a general anti-avoidance rule for a number of years. In SARS's view, this provision did contain certain inherent weaknesses and this resulted in new provisions on impermissible tax avoidance arrangements that were incorporated within the Act in Part IIA, ss 80A to 80L. These provisions apply to any arrangement, or any steps in or parts of an arrangement entered into on or after 2 November 2006.[80]

The new provisions of impermissible tax avoidance have retained some features of the previous regulations. The Amendment retains the sole or main purpose of obtaining a tax benefit, the abnormality test, and arm's length test. The Commissioner has the previous remedies to deal with a tax avoidance scheme, operation or transaction. He or she can treat the impermissible avoidance arrangement as if it had not been entered into or carried out. The Commissioner may also treat tax avoidance in such other manner in the circumstances of the case as he or she deems appropriate for the prevention or diminution of the relevant tax benefit.[81]

The most striking novel features of the Part IIA are:

- the criterion of "commercial substance" in an arrangement; (stated in section 80A(a)(ii) and expanded on in detail in section 80C);
- the criterion of whether the arrangement in issue "would result directly or indirectly to the misuse or abuse of the provisions of this [the Income Tax] Act" (including the provisions of section 80A(c)(ii));

[80] (Stiglingh *et al.* 2021)
[81] (Kanamugire 2013)

- new powers given to the Commissioner in relation to an "impermissible avoidance arrangement" (section 80B) and to determine whether parties are "accommodating or tax indifferent parties" (section 80E) and whether there has been a "tax benefit"(section 80F). [82]

One of the real benefits with the new GAAR is that SARS has stuck to a large extent to the wording that was used in the old section 103, precisely for the reason that the precedents in the law reports will still have value in a dispute between SARS and a taxpayer.[83]

Another interesting introduction to the rule is the provision of section 80A(c)(ii) which brings into the definition of impermissible avoidance arrangement an arrangement which has as its sole or main purpose the obtaining of a tax benefit and in any context it would abuse or misuse the provisions of the Act.[84]

4.2 Section 80A: Impermissible tax avoidance arrangement

Impermissible tax avoidance has been a growing problem internationally during the past ten years.[85]

Section 80A sets out the characteristics of an ‘avoidance arrangement’ (as defined in s 80L) which, if present, will cause such an arrangement to cross the threshold into the realm of an ‘impermissible avoidance arrangement’ (as defined in s 80L, read with s 80A) with the consequence that the Commissioner has the powers set out in s 80B to ‘determine the tax consequences’ under the Income Tax Act of that arrangement.[86]

[82] (SAICA March 2007)
[83] (SAICA February 2007)
[84] (SAICA February 2007)
[85] (SARS 2005)
[86] (de Koker & Williams 2021)

As a conceptual matter, it is difficult to draw a distinction between legitimate tax planning and impermissible tax avoidance arrangements.[87]

When this section is read with Section 80H, which allows the Commissioner to attack a part of an arrangement, it is clear that a single part of a composite avoidance arrangement can be attacked. The idea behind this is to ensure that taxpayers do not launder impermissible tax avoidance arrangements by placing them into wider and composite commercial schemes.[88]

SARS will often assess and challenge a purported impermissible tax avoidance arrangement on two bases, namely the "substance over form" or "simulation" doctrine, and in the alternative, the current GAAR reflected in sections 80A to 80J and 80L of the ITA.[89]

Four requirements must be met before the provision of ss 80A to 80L can be applied.

1. There must be an arrangement.
2. The arrangement results in a tax benefit and therefore constitutes an avoidance arrangement (s 80L, definition of 'tax' and 'avoidance arrangement')
3. The sole or main purpose of the avoidance arrangement was to obtain a tax benefit (Introduction to s 80A and s 80G).
4. If the avoidance arrangement is in the context of business, one of four requirements must be met, namely
    - Means or manner not normally employed (s 80A(a)(i))

[87] (South African Tax Guide)
[88] (Kujinga 2017)
[89] (ENSight)

- Rights or obligations not normally created (s 80A(c)(i))
- Lack of commercial substance (s 80A(a)(ii))
- Misuse or abuse of provisions of the Act (s 80A(c)(ii)).

If the avoidance arrangement is in a context other than business (therefore in a personal or private context), one of three requirements must be met, namely

- Means or manner not normally employed (s 80A(b))
- Rights or obligations not normally created (s 80A(c)(i))
- Misuse or abuse of provisions of the Act (s 80A(c)(ii)).[90]

Essential to the current GAAR are the “tax benefit” and “purpose” requirements.[91]

4.3 The four requirements

4.3.1 Requirement 1 (avoidance arrangements)

There must be an “arrangement”

‘Avoidance arrangement’ means any arrangement that, but for this Part, results in a tax benefit[92]

The word 'arrangement’ includes any of the following, and all steps therein or parts thereof:

- Any transaction
- Any operation
- Any scheme
- Any agreement
- Any understanding (whether enforceable or not)
- Any of the foregoing involving the alienation of property.

[90] (Stiglingh *et al.* 2021)
[91] (ENSight)
[92] (Professional Tax Handbook. 2020/2021)

The words ‘transaction, operation or scheme’ were also contained in the previous GAAR in s 103(1). In the case of *Meyerowitz v CIR (25 SATC 287)*[93] which dealt with s 103(1), it was held that the term ‘scheme’ is a wide term covering a series of transactions and that it is wide enough to cover situations in which later steps in a course of action were left unresolved at the outset. The terms ‘agreement’ and ‘understanding’ are new components and the meaning and scope of these terms must still be determined by the courts.[94]

In *Hicklin* it was indicated that it does not necessarily follow that, because a transaction, operation or scheme was aimed at and had the effect of avoiding an anticipated liability for tax, it is hit by the provisions of s 103(1). For they are inapplicable if that transaction, etc falls within the limits of normality of means, manner, rights, and obligations prescribed by s 103(1)(i) and (ii)…[95]

The criteria to determine what constitutes a ‘step in or part of’ an arrangement are not defined and it is suggested that each implies a distinct transactional element of the whole.[96]

The effect of s 80H is that SARS could potentially invoke a GAAR on a step of an ‘arrangement’ that seems driven by a tax benefit, irrespective of it being essential to the agreement as a whole, which lacks a main tax avoidance purpose. Clegg (*Income Tax in South Africa*) suggests correctly that the question should be whether the particular is commercially necessary in achieving the intended final commercial result, or whether it could be dispensed with or without affecting the commercial end result.

[93] Meyerowitz v CIR 1963 (3) SA 863 (A) [94] (Stiglingh *et al.* 2021)
[95] (Emslie, Davis, Hutton, & Olivier 2001)
[96] (Stiglingh *et al.* 2021)

A further implication of s 80H is that where a step in or part of an arrangement falls foul of the GAAR, the Commissioner may invoke his powers under s 80B in relation to the offending step or part, while the rest of the arrangement remains fiscally unaffected.[97]

It is submitted that an arrangement involving steps or parts carried out or brought into effect wholly or partly outside the Republic, which has a more than incidental purpose of avoiding tax, is caught by the GAAR.[98]

in *CIR v Louw*, the court found that the ultimate step in a scheme need not be in contemplation from the outset; it may be decided upon later but if there exists sufficient unity amongst the various steps, having regard to the ultimate objective, they may together be regarded as being part and parcel of a single scheme. Moreover, an act which did not form part of the scheme when it was entered into can become part and parcel of the scheme if it is later 'pressed into the service of the scheme'.[99]

In conclusion, the precise identification of the transaction, operation or scheme, agreement or understanding, or the steps or parts attacked by the Commissioner must be of vital importance to the taxpayer to avoid any misunderstanding in defending it. In this context, the obligation placed on the Commissioner to set out the reasons for his conclusion provides the necessary mechanism.[100]

4.3.2 Requirement 2 (Tax Benefit)

The arrangement must result in a tax benefit

[97] (Stiglingh *et al.* 2021)
[98] (de Koker & Williams 2021) [99]
(de Koker & Williams 2021) [100]
(de Koker & Williams 2021)

The word ‘tax benefit’ includes any avoidance, postponement or reduction of any liability for tax. The word ‘tax’ includes any tax, levy or duty imposed by the Act or any other law administered by the Commissioner. Examples of taxes imposed by other Acts are VAT, Estate Duty, Securities Transfer Tax and Transfer Duty. Any one of the avoidance, postponement or reduction of a liability for any of the aforementioned taxes constitutes a ‘tax benefit’. Thus, even though the arrangement concerned does no more than defer a tax payment, that deferral can be nullified through the Commissioner’s invocation of these provisions.[101]

Even though the word ‘tax’ includes various types of taxes, the GAAR will only be applied in relation to any tax under the Income Tax Act. This is because the introductory words of s 80A(1) allow the Commissioner to determine the tax consequences of any impermissible avoidance arrangement ‘under this Act’. It is submitted that the words ‘the relevant tax benefit’ in s 80A(*f*) refer to a tax benefit in terms of the Income Tax Act.[102]

The income tax Act does not provide a test to determine the existence of a tax benefit, but it was held by the court in *Copthorne Holdings Ltd v Canada* (2011 SCC 63), referring to *Canada Trustco Mortgage Co v Canada* (2005 SCC 54) that the existence of a tax benefit can be established by a comparison of the taxpayer’s situation with an alternative arrangement. If a comparison approach is used, the alternative arrangement must be the one that ‘might reasonably’ have been carried out but for the existence of the tax benefit. The ‘but for’ test simply ask whether, but for the existence of an arrangement, would tax have been suffered.[103]

Three interpretations of the term “tax benefit” have been used for the purposes of applying the current GAAR to the facts of the Sasol case:

[101] (Stiglingh *et al.* 2021)
[102] (Stiglingh *et al.* 2021)
[103] (Stiglingh *et al.* 2021)

1. A tax benefit only arises if a taxpayer avoids an anticipated liability for tax (*Commissioner for Inland Revenue v King (1947) 14 SATC 184 (A)*). This may be contrasted with avoiding an existing liability for tax as this would constitute tax evasion and not tax avoidance (Pidduck, 2017, p. 81).
2. A tax benefit arises where the taxpayer has effectively stepped out of the way of, escaped or prevented an anticipated liability (*Smith v Commissioner for Inland Revenue (1964) 26 SATC 1 (A)*).
3. The "but for" test should be applied in determining whether a tax benefit exists and requires the following question to be asked: Would the taxpayer have suffered tax but for the transaction? *(Income Tax Case No. 1625 (1996) 59 SATC 383; Smith v Commissioner for Inland Revenue (1964) 26 SATC 1 (A); Commissioner for Inland Revenue v Louw (1983) 45 SATC 113 (A))*.[104]

For the Commissioner to be empowered to invoke the GAAR, it must be shown that the arrangement in question would result in a tax benefit – in other words that it was an 'avoidance arrangement' (as defined in s 80L) and that the sole or main purpose of the arrangement was to obtain such a benefit and that at least one of the elements of s 80A(a) to (c) was present – in other words, that it was an 'impermissible avoidance arrangement', as defined in s 80L.[105]

Clegg submits that, in order for the Commissioner to show that a tax benefit has arisen, it is necessary for him establish and show that transaction or arrangement would otherwise have been entered into or, possibly, that no transaction would otherwise have been entered into, to produce the commercial consequences concerned and the tax consequences thereof. It is not enough, he suggests, for the Commissioner simply to

[104] (Pidduck 2018)
[105] (de Koker & Williams 2021)

aver that a tax benefit has arisen – he must be sufficiently clear in his mind as to the nature of the alternative position in order to quantify the benefit.[106]

4.3.3 Requirement 3 (sole or main purpose)

The "avoidance arrangement" must have characteristics of abnormality and/or lack commercial substance

The introduction to s 80A states that an avoidance arrangement is an impermissible avoidance arrangement if its sole or main purpose was to obtain a tax benefit.[107]

As these words indicate, an indispensable constituent element of an 'impermissible avoidance arrangement' is a sole or main purpose of obtaining a tax benefit, coupled with at least one further element, introduced by the word and. It is thus clear that the requisite 'sole or main purpose' is a *sine qua non* for an 'impermissible avoidance arrangement', and the absence of such a purpose will mean that the GAAR is not applicable to the arrangement, even if it has given rise to a tax benefit.[108]

Clegg states that, in order to displace the presumption against him, not only must the taxpayer be able to point to some compelling reasons for the entering into of the arrangement, but a court be happy that 'reasonably considered in light of the relevant facts and circumstance' the tax benefit was not the sole or main purpose. It is clear, it is submitted, that the courts must take an objective view of the facts and circumstances – which include the *ipse dixit* of the taxpayer – in order to determine the actual purpose of the transaction.[109]

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[106] (Stiglingh *et al.* 2021)
[107] (Stiglingh *et al.* 2021)
[108] (de Koker & Williams 2021)
[109] (Stiglingh *et al.* 2021)

Section 80G(1), on the other hand, states that an avoidance arrangement is presumed to have been entered into or carried out with the sole or main purpose of obtaining a tax benefit (s 80G(1)). This will be presumed unless and until the party obtaining the tax benefit (not necessarily the taxpayer) proves that 'reasonably considered in light of the relevant facts and circumstance' obtaining a tax benefit was not the sole or main purpose of the avoidance arrangement.[110]

Section 80G(1) throws no light on what is encompassed by 'the relevant facts and circumstances' that may be laid before the court by the party attempting to rebut the presumption of purpose. Given that the operative purpose envisaged in s 80A is the objective purpose of the arrangement itself and not the subjective purpose of the taxpayer, a critical issue in any litigation between SARS and the taxpayer in relation to the GAAR will be what evidence, other than the terms of the arrangement itself (and also, according to Denning, 'the overt acts by which it was implemented') is admissible to rebut the presumption of a sole or main purpose of obtaining a tax benefit. Where the arrangement is not in writing, or not wholly in writing, but is oral or tacit, it seems that the terms of the arrangement will have to be laid before the court by way of oral testimony by the parties – but they will have to scrupulously avoid any reference to their subjective purpose in entering into the arrangement. Where the arrangement was in writing and was intended to be the exclusive memorial of the agreement, the common law parol evidence rule will bar any evidence being led to contradict the written agreement. All of this is going to lead to very fine lines being drawn in tax litigation in regard to evidentiary issues.[111]

…as a matter of litigation strategy, counsel for the taxpayer may deliberately leave the background to the arrangement shrouded in mystery and then, in closing argument, point to all the various ways in which (to use Lord Denning's phrase from *Newton v*

[110] (Stiglingh *et al.* 2021)
[111] (de Koker & Williams 2021)

FCT) the arrangement 'is capable of being explained' as being merely part of ordinary business or family dealing.

In short, when it comes to the evidentiary aspects of establishing the 'sole or main purpose' of an arrangement, the new GAAR opens up a playing field for the games lawyers love to play.[112]

…there is a critical difference between the now-repealed s 103(1) and s 80A of the new GAAR. In the context of s 103(1), 'purpose' referred to the subjective purpose of the taxpayer in entering into the transaction, operation or scheme whereas, in the new GAAR, 'purpose' refers to the purpose of the arrangement itself, objectively determined, and the subjective purpose of the taxpayer is irrelevant. The South African Revenue Service is on record as saying that under the new GAAR the standard is 'more objective' than it was under s 103(1), but this coyness is misplaced – the language of s 80A makes clear that the criterion is completely objective Indeed, it is doubtful whether the word 'objective', in this context, admits of degrees of comparison.[113]

In *Secretary for Inland Revenue v Gallagher* Corbett JA, as he then was, explained the distinction between an objective and a subjective test as follows:

> 'By an objective test in this context is evidently meant a test which has regard rather to the effect of the scheme, objectively viewed, as opposed to a "subjective" test which takes as its criterion the purpose which those carrying out the scheme intend to achieve by means of the scheme.'[114]

[112] (de Koker & Williams 2021)
[113] (de Koker & Williams 2021)
[114] (Stiglingh *et al.* 2021)

In giving content to the concept, novel in South African tax law, of the *objective* purpose of an 'arrangement', our courts will no doubt look for guidance to other fiscal jurisdictions which employ a similar objective criterion. The most influential explanation of how the objective purpose of an arrangement is to be determined is that articulated by Lord Denning in *Newton v FCT277* where he said, in regard to establishing the objective purpose of an arrangement in the context of Australia's GAAR, that

> 'In order to bring the arrangement within the section you must be able to predicate – by looking at the overt acts by which it was implemented – that it was implemented in that particular way so as to avoid tax. If you cannot so predicate, but have to acknowledge that the transactions are capable of explanation by reference to ordinary business or family dealing, without necessarily being labelled as a means to avoid tax, then the arrangement does not come within the section.'[115]

4.3.4 Requirement 4 (abnormality, commercial substance and misuse or abuse tests)

The "avoidance arrangement" must have had as its "sole" or "main purpose" the obtaining of a "tax benefit"

1. **In the context of business**
   - (i) it was entered into or carried out by means or in a manner which would not normally be employed for bona fide business purposes, other than obtaining a tax benefit; or
   - (ii) it lacks commercial substance, in whole or in part, taking into account the provisions of section 80C.'

Abnormality of means or manner

[115] (de Koker & Williams 2021)

The first limb, (s 80A(a)(i)), is posited on ‘abnormality’. It requires an objective determination whether the arrangement was entered into or carried out, by means or in a manner, which would not normally be employed for bona fide business purposes other than obtaining a tax benefit. It attaches the qualification ‘not normally . . . employed for bona fide business purposes’ to both the means (‘by means’) and the manner (‘in a manner’) in which the arrangement was entered into or in which it was carried out.[116]

if the taxpayer is assessed to tax on the basis of an abnormality as envisaged in s 80A (coupled with the requisite sole or main purpose) it seems that the onus is on the Commissioner to prove the abnormality.

In *Ben Nevis Forestry Ventures Ltd v CIR*; *Accent Management Ltd v CIR* the court, having pointed out that the statutory onus rests on the taxpayer, said that it is necessary for the appellants, on whom the burden of proof lies, to persuade the Court that the arrangement is not a tax avoidance arrangement.[117]

Business purpose Test

Section 80A provides no guidance as to what constitutes ‘bona fide business purposes’ save to say that, in this context, they do not include obtaining a tax benefit. By implication, therefore, every bona fide business purpose other than obtaining a tax benefit is included, and if there was also a purpose of obtaining a tax benefit, then the latter purpose must not have been the sole or main (objective) purpose of the transaction. The criterion of a ‘business purpose’ in s 80A must not be confused with the similarly named but very different business purpose test that prevails in the USA and which derives from the decision in Gregory v Helvering. In the latter version of the business purpose test, the taxpayer’s transaction is scrutinised to determine whether it was driven by commercial considerations rather than the prospective tax benefits, but

[116] (de Koker & Williams 2021)
[117] (de Koker & Williams 2021)

(unlike s 80A) the test does not entail a comparison between the taxpayer's transaction and the way in which that type of transaction would normally be carried out.[118]

Bona Fide

The Income Tax Act does not define the term '*bona fide*'.

The meaning of the term '*bona fide* purpose' is somewhat obscure. Presumably it requires the methodology employed by the taxpayer to achieve a personal, family or charitable result.[119]

Section 80C - Lack of commercial substance

The lack of commercial substance requirement is contained in section 80C of the Act. Broomberg and De Koker both indicate that section 80C of the Act could be described as the heart of the new general anti avoidance rule. Section 80C contains both a presumptive test and indicative test to determine whether a lack of commercial substance exists. Section 80C(1),the presumptive test, establishes a general rule for determining whether an avoidance arrangement lacks commercial substance, while section 80C(2) provides a non-exclusive set of characteristics that serve as indicators of a lack of commercial substance. (A Significant Tax Benefit)[120]

A 'lack of commercial substance' is now an important criterion in drawing the boundary between permissible and impermissible tax avoidance – because Part IIA of the Act

[118] (de Koker & Williams 2021)
[119] (de Koker & Williams 2021)
[120] (Geldenhuys 2010)

declares it to be so – though, even in that context, it is of no fiscal consequence unless it was coupled with a sole or main purpose of deriving a tax benefit.[121]

Lack of commercial substance

(1) For purposes of this Part, an avoidance arrangement lacks commercial substance if it would result in a significant tax benefit for a party, but does not have a significant effect upon either the business risks or net cash flows of that party apart from any effect attributable to the tax benefit that would be obtained but for the provisions of this Part.

(2) For purposes of this Part, characteristics of an avoidance arrangement that are indicative of a lack of commercial substance include but are not limited to-

(a) The legal substance or effects of the avoidance arrangement as a whole is inconsistent with, or differs significantly from, the legal form of its individual steps; or

(b) The inclusion or presence of-

(i) Round trip financing as described in Section 80D; or

(ii) An accommodating or tax indifferent party as described in Section 80E; or

(iii) Elements that have the effect of offsetting or cancelling each other.[122]

If an avoidance arrangement lacks commercial substance 'in whole or in part' and if, in addition, it had the requisite objective sole or main purpose of obtaining a tax benefit, it will be an 'impermissible avoidance arrangement'. Thus, a lack of commercial substance in 'part' of a composite avoidance arrangement suffices (if coupled with the requisite sole or main purpose) to taint the entire arrangement as an 'impermissible

[121] (de Koker & Williams 2021)
[122] (Professional Tax Handbook. 2020/2021)

avoidance arrangement', with the result that the Commissioner can exercise his powers under s 80B in relation to the entire arrangement and not merely in relation to the offending part.[123]

If the arrangement is such that it results in the inconsistent characterisation for tax purposes of the arrangement by any of the parties, it would also fall within this provision.[124]

'Significant tax benefit'

The GAAR gives no guidance as to what constitutes a 'significant' tax benefit. It is hardly satisfactory to brush this phrase aside as a mere de minimis rule, for that would surely be implied in any event. Particularly problematic is whether the quantum of a 'significant' tax benefit is not an absolute amount, but varies from taxpayer to taxpayer, such that what would be significant for a small business would be insignificant for a large one.[125]

Arguably, the benefit must be significant in the context of the taxpayer's annual net profit or his net assets or even his financial affairs in general. But such an interpretation, it is submitted, would discriminate between taxpayers in a manner that is constitutionally suspect. The same difficulty presents itself in determining what constitutes a 'significant effect' on net cash flow.[126]

[123] (de Koker & Williams 2021)
[124] (SAICA February 2007)
[125] (de Koker & Williams 2021)
[126] (de Koker & Williams 2021)

Substance over form: 'Legal substance or effect'

S 80(2)(a) highlights that an arrangement will lack commercial substance if legal substance or effects of the avoidance arrangement as a whole is inconsistent with, or differs significantly from, the legal form of its individual steps.

One should be reminded that simulating a transaction merely to mask its true nature and purpose will not help, as the 'substance over form' rule is available to SARS, so that force will be given to the true transaction and not the simulated or sham transaction that the taxpayer professes it to be.[127]

In *IRC v Duke of Westminster* it was stated that:

> 'it is said that the substance of the transaction evidenced by the agreement must be looked at, and not its mere words.'[128]

The difficulty with this frankly ill-considered and ill-drafted provision is that it strings together a series of terms that the GAAR does not define and the meaning of which is far from clear. The phrase 'legal substance or effect', if dissected, is thoroughly confusing. What is 'legal substance'? How does it differs from 'commercial substance' which is a phrase used a few lines earlier in this provision? Does the adjective 'legal' in the phrase 'legal substance or effect' qualify both 'substance' and 'effect' – in which event what is a 'legal effect' and how does it differ from 'legal substance'. If 'legal' does not qualify 'effect', then what kind of 'effect' is being referred to? Why are 'substance and effect' spoken of in the same breath when they are surely different concepts? What is 'legal form' as distinct from 'legal substance' and does an inconsistency between legal substance and legal form equate to a 'disguised transaction' as envisaged in such

[127] (South African Tax Guide)
[128] (Clegg 1991)

decisions as *Erf 3183/1 Ladysmith (Pty) Ltd and Another v CIR and Relier (Pty) Ltd v CIR*?[129]

It is trite that the courts will have regard to the substance and not the form of a transaction. As Wessels ACJ said in Kilburn v Estate Kilburn:

> 'Courts of law will not be deceived by the form of a transaction; it will rend aside the veil in which the transaction is wrapped and examine its true nature and substance.'

Precisely how the 'substance' of a transaction is to be ascertained has been much debated. In *IRC v Duke of Westminster* Lord Tomlin warned that:

> 'This so-called doctrine of "the substance" seems to me to be no more than an attempt to make a man pay notwithstanding that he has so ordered his affairs that the amount of tax sought from him is not legally claimable.'

In the same case, Lord Russell said that

> 'If all that is meant by the doctrine [that substance prevails over form] is that having once ascertained the legal rights of the parties you may disregard mere nomenclature and decide the question of taxability or non-taxability in accordance with the legal rights, well and good . . . If on the other hand, the doctrine means that you may brush aside deeds, disregard the legal rights and liabilities arising under a contract between the parties, and decide the question of taxability or non-taxability upon the footing of the rights and liabilities of the parties being different from what in law they are, then I entirely dissent from such a doctrine.'[130]

In *Dadoo Ltd v Krugersdorp Municipal Council* 53 Innes CJ said,

[129] (de Koker & Williams 2021)
[130] (de Koker & Williams 2021)

> ‘a transaction is in *fraudem legis* when it is designedly disguised so as to escape the provisions of the law, but falls in truth within those provisions. Thus stated, the rule is merely a branch of the fundamental doctrine that the law regards the substance rather than the form of things . . .’[131]

The draft *Comprehensive Guide to the General Anti-Avoidance Rule* concedes that the term ‘legal substance or effect’ have been the subject of much debate and goes on to the say that the word effect includes ‘economic, commercial or practical effect’. From this it seems that the adjective ‘legal’ qualifies only ‘substance’ and not ‘effect’ and that ‘effect’ is concerned with ‘the economic, commercial or practical effect’, from which one may infer that ‘practical effect’ is something different from ‘economic or commercial effect’.[132]

The draft *Comprehensive Guide* goes on to say that, in essence, the test of ‘legal substance or effect’ consists of two sub-tests, as follows:

(1) ‘Firstly, the legal substance of the arrangement in respect of which SARS intends to apply the GAAR, must be compared to the legal form of the individual steps and any inconsistencies are indicative of lack of commercial substance.
(2) Secondly, the commercial, economic or practical effect of the arrangement on which SARS intends to apply the GAAR, must be compared to the legal form of the individual steps and any inconsistencies are indicative of lack of commercial substance.

If either one of these two sub-tests are met, subject thereto that the sole or main purpose of the arrangement is to derive a tax benefit and subject to the presumptive test

[131] (de Koker & Williams 2021)
[132] (de Koker & Williams 2021)

contained in section 80C(1) being satisfied, the arrangement is impermissible, and SARS will apply the remedy provisions to such arrangement.'[133]

Section 80D – Round trip financing

The second indicative characteristic of an avoidance arrangement that 'lacks commercial substance', as envisaged in s 80A(a)(i) read with s 80C, is the 'inclusion or presence' of round-trip financing, which is defined (or perhaps, more accurately 'explained') in s 80D**...**[134]

Round trip financing

(1) Round trip financing includes any avoidance arrangement in which-

(a) Funds are transferred between or amongst the parties (round trip amounts); and

(b) The transfer of the funds would-

(i) Result, directly or indirectly, in a tax benefit but for the provisions of this Part; and

(ii) Significantly reduce, offset or eliminate any business risk incurred by any party in connection with the avoidance arrangement.

(2) This section applies to any round tripped amounts without regard to-

(a) Whether or not the round tripped amounts can be traced to funds transferred to or received by any party in connection with the avoidance arrangement;

(b) The timing or sequence in which round tripped amounts are transferred or received;

[133] (de Koker & Williams 2021)
[134] (de Koker & Williams 2021)

(c) The means by or manner in which round tripped amounts are transferred or received.

(3) For the purposes of this section, the term “funds” includes any cash, cash equivalents or any right or obligation to receive or pay the same.[135]

In broad terms, it is easy to see what s 80D is driving at. It is saying, in essence, that a common characteristic of unacceptable tax avoidance is that it does not involve a genuine business arrangement, but merely tries to conjure up a tax benefit through sleight of hand. Money is made to appear to pass between the participants by way of a commercial consideration, but the funds simply travel in a circle and, when all is said and done, everyone is financially in the same position as they were in the beginning, save for the creation of a tax benefit and the payment of fees to the intermediaries.[136]

As Lord Templeman remarked in *CIR v Challenge Corp Ltd*, most tax avoidance involves a pretence, such as a pretended loss or a circular game in which the taxpayer and a few hired performers act out a play in which real documents or money may be exchanged, but nothing happens except that the Houdini taxpayer appears to escape from the manacles of tax, and in the end the financial position of the hired actors is the same as it was at the beginning, except that the taxpayer pays them for their services.[137]

The third characteristic, identified by s 80C(2)(b)(ii), that is ‘indicative of a lack of commercial substance’ in an avoidance arrangement is the inclusion or presence of an ‘accommodating or tax indifferent party’ as defined in s 80E(1).[138]

[135] (Professional Tax Handbook. 2020/2021)
[136] (de Koker & Williams 2021)
[137] (de Koker & Williams 2021)
[138] (de Koker & Williams 2021)

Section 80E

Accommodating or tax-indifferent parties

(1) A party to an avoidance arrangement is an accommodating or tax-indifferent party if-

(a) Any amount derived by the party in connection with the avoidance arrangement is ether-

(i) Not subject to normal tax; or

(ii) Significantly offset either by any expenditure or loss incurred by the party in connection with that avoidance arrangement or any assessed loss of that party; and

(b) Either-

(i) As a direct or indirect result of the participation of that party an amount that would have-

(ii) The participation of that party directly or indirectly involves a prepayment by any other party.

(aa) been included in the gross income (including the recoupment of any amount) or receipts or accruals of a capital nature of another party would be included in the gross income or receipts or accruals of a capital nature of that party; or

(bb) constituted of a non-deductible expenditure or loss in the hands of another party would be treated as a deductible expenditure by that other party; or

(cc) constituted revenue in the hands of another party would be treated as capital by that other party; or

(dd) given rise to taxable income to another party would either not be included in gross income or be exempt from normal tax; or

(2) a person may be an accommodating or tax-indifferent party whether or not that person is a connected person in relation to any party.

(3) the provisions of this section do not apply either

(a) the amounts derived by the party in question are cumulatively subject to income tax by one or more spheres of government of countries other than the Republic which is equal to at least two-thirds of the amount of normal tax which would have been payable in connection with those amounts had they been subject to tax under this Act; or

(b) the party in question continues to engage directly in substantive active trading activities in connection with the avoidance arrangement for a period of at least 18 months: Provided these activities must be attributable to a place of business, place, site, agricultural land, vessel, vehicle, rolling stock or aircraft that would constitute a foreign business establishment as defined in section 9D(1) if it were located outside the Republic and the party in question were a controlled foreign company.

(4) for the purposes of subsection (3)(a), the amount of tax imposed by another country must be determined after taking into account any applicable arrangement for the prevention of double taxation and any assessed loss, credit or rebate to which the party in question may be entitled or any other right of recovery to which that party or any connected person in relation to that party may be entitled.[139]

In the Challenge Corporation case Lord Templeman observed, “every tax avoidance scheme involves a trick and pretence”. In South Africa, the trick and pretence often involve a circular flow of funds and a step involving a tax indifferent party.[140]

Offsetting or cancelling elements

The fourth characteristic of an avoidance arrangement, which may be indicative of a lack of commercial substance (see s 80C(2)(b)(iii)), is the inclusion or presence of elements – the Act does not say they must be substantial elements – which need not be

[139] (Professional Tax Handbook. 2020/2021)
[140] (SARS 2005)

expressed in monetary terms, but could be off-setting rights or obligations and that have the effect of off-setting or cancelling each other.[141]

The self-neutralising criterion attempts to flush out intentionally misleading elements inserted into complex schemes, often involving complicated financial derivatives, in which rights or obligations created in one part of the scheme are seen, upon close scrutiny, to be extinguished in another part. The self-neutralising criterion is an 'indicative test' which leads back to the 'presumptive test' in s 80C(1) for a lack of commercial substance which, if coupled with the requisite sole or main purpose in s 80A, will trigger the GAAR.

In South Africa, an example of mutually 'off-setting or cancelling' elements would presumably be the extinction of rights and obligations by way of *confusio* that occurred in the factual matrix of *C: SARS v NWK Ltd*, although that case was decided in terms of common law principles and not a statutory GAAR.[142]

Section 80F

Treatment of connected persons and accommodating or tax indifferent parties

For the purposes of applying section 80C or determining whether or not a tax benefit exists for purposes of this Part, the Commissioner may-

(a) Treat parties who are connected persons in relation to each other as one and the same persons; or
(b) Disregard any accommodating or tax-indifferent party or treat any accommodating or tax-indifferent party and any other party as one and the same person.[143]

141 (de Koker & Williams 2021)
142 (de Koker & Williams 2021)
143 (Professional Tax Handbook. 2020/2021)

2. Arrangements in a context other than business

Section 80A(b) provides that an avoidance arrangement is an impermissible avoidance arrangement if its sole or main purpose was to obtain a tax benefit and

'in a context other than business, it was entered into or carried out by means or in a manner which would not normally be employed for a bona fide purpose, other than obtaining a tax benefit.**'**

Significantly, therefore, this provision speaks of a '*bona fide* purpose' rather than a '*bona fide* business purpose'. Consequently, any *bona fide* purpose other than obtaining a tax benefit will suffice.

Moreover, the absence of the requisite sole or main purpose envisaged in s 80A will render the GAAR inapplicable, no matter how abnormal the arrangement nor how great the tax benefit.[144]

The most obvious, though not the only, example of a non-business context is that of a domestic or family arrangement, such as one in which the taxpayer is putting in place a financial arrangement to ensure the maintenance of his dependants during his lifetime or after his death. Naturally, any astute breadwinner will seek to do so in a tax-effective manner, and if the sole or main purpose of the arrangement, objectively regarded, was to provide for dependants (or even friends) rather than to secure a tax benefit, then an essential element of an 'impermissible avoidance arrangement' will be lacking. Consequently, in terms of the criteria laid down in s 80A(b) no matter how substantial the tax benefit, nor how 'abnormal' the arrangement in the sense that such an arrangement would never be reached except between persons with bonds of family or friendship, it will not be an 'impermissible avoidance arrangement' as long as the one

[144] (de Koker & Williams 2021)

remaining hurdle is safely crossed, namely that it would not result in the misuse or abuse of the Income Tax Act.[145]

The meaning of the term 'bona fide purpose' is somewhat obscure. Presumably it requires the methodology employed by the taxpayer to achieve a personal, family or charitable result.

Part IIA of Chapter III creates no rebuttable presumption that the arrangement was entered into or carried out by means or in a manner not normally employed for a *bona fide* purpose and the Commissioner bears the burden of proving, on a balance of probability, the requisite abnormality…[146]

3. Arrangements in any context

An avoidance arrangement is an impermissible avoidance arrangement if its sole or main purpose was to obtain a tax benefit and

in any context—

(i) it has created rights or obligations that would not normally be created between persons dealing at arm's length; or

(ii) it would result directly or indirectly in the misuse or abuse of the provisions of this Act (including the provisions of this Part).'[147]

The phrase 'in any context' clearly means in all contexts, whether 'in the context of business' (s 80A(a)) or in 'a context other than business' (s 80A(b)). The criteria in s 80A(c) thus apply to all avoidance arrangements, including domestic and family arrangements, and any such arrangement (provided it has a sole or main purpose of

[145] (de Koker & Williams 2021)
[146] (de Koker & Williams 2021)
[147] (de Koker & Williams 2021)

obtaining a tax benefit) will be an impermissible avoidance arrangement if it falls foul of these criteria.[148]

Section 80G

The new GAAR contains a rebuttable presumption that an avoidance arrangement has a sole or main purpose of obtaining a tax benefit (s 80G(1)) but there is no statutory presumption that such an arrangement has created rights or obligations not normally created between persons dealing at arm's length.[149]

Presumption of purpose

(1) An avoidance arrangement is presumed to have been entered into or carried out for the sole or main purpose of obtaining a tax benefit unless or until the party obtaining the tax benefit proves that, reasonably considered in light of the relevant facts and circumstances, obtaining a tax benefit was not the sole or main purpose of the avoidance arrangement.

(2) The purpose of the step in or part of an avoidance arrangement may be different from a purpose attributable to the avoidance arrangement as a whole.[150]

Misuse or abuse of the provisions of the Act

The second criterion that s 80A(c) makes applicable 'in any context' and which makes an avoidance arrangement an 'impermissible avoidance arrangement' if it is coupled with the requisite sole or main purpose of obtaining a tax benefit, is fulfilled where the avoidance arrangement in question would result directly or indirectly in the 'misuse or abuse' of the provisions of the Act (including the provisions of the GAAR).[151]

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148 (de Koker & Williams 2021)
149 (de Koker & Williams 2021)
150 (Professional Tax Handbook. 2020/2021)
151 (de Koker & Williams 2021)

It is noteworthy, though, that the structure of s 80A is such that even if such a 'misuse or abuse' is established, it has no fiscal consequences unless the arrangement itself had a sole or main purpose of obtaining a tax benefit. The logic is astonishing – surely, the 'misuse or abuse' of the Act should be intolerable irrespective of the purpose of the arrangement?[152]

Section B: Tax consequences of impermissible tax avoidance:

The harms caused by impermissible tax avoidance are varied and pervasive. They include short-term revenue loss, growing disrespect for the tax system and the law, increasingly complex tax legislation, the uneconomic allocation of resources, an unfair shifting of the tax burden, and a weakening of the ability of Parliament and National Treasury to set and implement economic policy.[153]

The new GAAR has granted the Commissioner more power compared to the old GAAR. The Commissioner is fully equipped to deal with transactions that are said to be impermissible avoidance arrangements, the Commissioner is the one that decides the type of consequence to be issued to the taxpayer. Those consequences are listed in s 80H of the Income Tax Act.

The Commissioner may determine the tax consequence under this Act of any impermissible avoidance arrangement for any party by-

(a) Disregarding, combining or re-characterising any steps in or parts of the impermissible avoidance arrangement;
(b) Disregarding any accommodating or tax-indifferent party or treating any accommodating or tax-indifferent party and any other party as one and the same person;

[152] (de Koker & Williams 2021)
[153] (SARS 2005)

(c) Deeming persons who are connected persons in relation to each other to be one and the same person for purposes of determining the tax treatment of any amount;
(d) Reallocating any gross income, receipt or accrual of a capital nature, expenditure or rebate amongst the parties;
(e) Re-characterising any gross income, receipt or accrual of a capital nature or expenditure; or
(f) Treating the impermissible avoidance arrangement as if it had not been entered into or carried out, or in such other manner as in the circumstance of the case the Commissioner deems appropriate for the prevention or diminution of the relevant tax benefit.[154]

He is further empowered to make appropriate, compensating adjustments that are necessary to ensure the consistent treatment of all parties to the impermissible avoidance arrangement.[155]

4.4. Onus of proof

Section 82 of the Income Tax Act lays down a general rule regarding the incidence of the onus of proof – that is to say, the question as to who bears the onus of proof. The section provides that the burden of proving that any amount is exempt from or not liable to any tax chargeable under the Act, is subject to any deduction, abatement or set-off in terms of the Act, or is to be disregarded or excluded in terms of the Eighth Schedule, rests upon the person claiming the exemption, non-liability, deduction, abatement or set-off, or claiming that such amount must be disregarded or excluded.[156]

[154] (Professional Tax Handbook. 2020/2021)
[155] (SAICA February 2007)
[156] (de Koker & Williams 2021)

The taxpayer's first barricade therefore is to be able to demonstrate that the transaction did not result in a tax benefit. It is clear that the Commissioner cannot invoke the GAAR provisions unless the transaction has had the effect either of avoiding tax, or of postponing liability for tax, or of reducing the amount of tax on the part of the taxpayer. In practice the Commissioner tests for tax avoidance in the following manner: First, he ascertains how much tax would have been payable if the transaction had not been carried out at all. Then he determines how much tax, overall, is payable on the basis that the transaction is accepted at face value. If he finds that less tax is payable as a result of the implementation of the transaction, he considers that a tax benefit has been obtained as a result of the transaction.[157]

The second hurdle to overcome is to demonstrate that the avoidance arrangement (step or part) has not been entered into or carried out "solely or mainly for the purpose of obtaining a 'tax benefit'" (Section 80A of the Act).[158]

4.5. Powers of the Commissioner

Powers of the Commissioner Section 80J

The Commissioner's power to determine the taxpayer's liability as if the transaction had not been entered into or carried out or in such manner as in the circumstances of the case he deems appropriate may be exercised not only in respect of the year of assessment in which the transaction was entered into or carried out but also in respect of all subsequent years of assessment.[159]

Notice

(1) The Commissioner must, prior to determining any liability of a party for tax under section 80B, give the party notice that he or she believes that the provisions of

[157] (Kruger *et al.* 2012)
[158] (Kruger *et al.* 2012)
[159] (de Koker & Williams 2021)

this Part may apply in respect of an arrangement and must set out in the notice his or her reasons therefor.

(2) A party who receives notice in terms of subsection (1) may, within 60 days after the date of that notice or such longer period as the Commissioner may allow, submit reasons to the Commissioner why the provisions of this Part should not be applied.

(3) The Commissioner must within 180 days of receipt of the reasons or the expiry of the period contemplated in subsection (2)-

(a) Request additional information in order to determine whether or not this Part applies in respect of an arrangement;

(b) Give notice to the party that the notice in terms of subsection (1) has been withdrawn; or

(c) Determine the liability of that party for tax in terms of this Part.

(4) If at any state after giving notice to the party in terms of subsection (1), additional information comes to the knowledge of the Commissioner, he or she may revise or modify his or her reasons for applying this Part or, if the notice has been withdrawn, give notice in terms of subsection (1).[160]

The now-repealed s 103(1) was triggered where the Commissioner was 'satisfied' that all of its elements were simultaneously present, and his decision in this regard was subject to objection and appeal. The statutory requirement that he be so 'satisfied' rendered the provision vulnerable to technical arguments as to whether this (apparently) jurisdictional fact was present in the context of a given factual scenario. In order no doubt to forestall any such arguments, the new GAAR makes no mention of the Commissioner's having to be 'satisfied' in any respect; it simply defines (in s 80A) what constitutes an 'impermissible avoidance arrangement' and (in s 80B) gives the Commissioner the power to 'determine the tax consequences under this Act of any impermissible avoidance arrangement' by any of a specified range of actions 'for the

[160] (Professional Tax Handbook. 2020/2021)

prevention or diminution of the relevant tax benefit…..Moreover, the Commissioner's powers extend to any 'party' (as defined in s 80L) to the arrangement.[161]

[161] (de Koker & Williams 2021)

CHAPTER 5

5. THE REASON WHY SECTION 103(1) WAS REPLACED WITH THE NEW GAAR

5.1 Weaknesses identified in the old GAAR

A perceived weakness of s 103(1), from the point of view of SARS, was that the requisite sole or main purpose of tax avoidance had to be determined subjectively. In other words, the court was required to look into the mind of the taxpayer and determine, as best it could, on the evidence laid before it, and with due regard for the incidence of the onus of proof, whether the requisite purpose was present when he entered into the transaction, operation or scheme in question. Or, to be precise, if the transaction, operation or scheme had the result of avoiding or postponing tax, it was presumed that it had been entered into for the requisite purpose unless the taxpayer proved otherwise.[162]

A second perceived weakness in s 103(1) lay in the requirement that the transaction, operation or scheme had to be objectively 'abnormal' in the requisite sense. It seemed to be arguable that if a particular kind of transaction, operation or scheme became commercially commonplace, then would cease to be 'abnormal', as envisaged in s 103(1).[163]

Despite the on-going doubts and uncertainties about what 'normal' means in this context, the criterion of normality has been included in s 80A of the new GAAR, but with the addition of a new, alternative criterion of a 'lack of commercial substance'.[164]

A third perceived weakness in s 103(1) was uncertainty in regard to the extent of the powers of the Commissioner to act in relation to an offending transaction, operation or scheme in a way that would nullify the tax benefit. Section 103(1) said in this regard that

[162] (de Koker & Williams 2021)
[163] (de Koker & Williams 2021)
[164] (de Koker & Williams 2021)

where its provisions applied, the Commissioner was empowered to determine tax liability 'as though the transaction, operation or scheme had not been entered into or carried out or in such manner as in the circumstances of the case he deems appropriate for the prevention or diminution of such avoidance, postponement or reduction [of tax]'.[165]

Although the latter phrase was expressed in very broad terms, it was felt that, for greater clarity, the Commissioner's powers should be spelled out in specific as well as general terms. One of the features of the new GAAR is the detailed setting out in s 80B of the powers of the Commissioner in this regard.[166]

As with all litigation which turns on the credibility of a witness – particularly in regard to an attestation as to his subjective state of mind at a particular juncture – it was difficult to predict whether a court would, in all the circumstances and in the light of the evidence as a whole, conclude that the taxpayer was to be believed when he averred that he did or did not have the requisite sole or main purpose of avoiding or postponing tax liability when entering into the transaction, operation or scheme.

For this reason, when a new general anti-avoidance provision was on the drawing board, SARS was anxious that the subjective purpose, provided for in s 103(1), should, in the new GAAR, be replaced by an objective purpose, and this is indeed one of the major reforms of the new Part IIA of the Act.[167]

5.2 Difficulties with the implementation of the new GAAR

[165] (de Koker & Williams 2021)
[166] (de Koker & Williams 2021)
[167] (de Koker & Williams 2021)

The new GAAR is a long and complex piece of legislation, and considerable uncertainty followed its enactment. Unfortunately, for many years SARS and National Treasury did little or nothing to respond to these criticisms or to counter a growing impression that they lacked faith in or did not fully understand their own legislation.[168]

Perhaps the single biggest factor in undermining the potential effectiveness of the new GAAR has been SARS' reluctance to invoke it. Indeed, SARS seemingly did not issue its first notices under section 80J until 2012, some six years after the statute was enacted. With some justification, this has led to a widespread belief in the tax avoidance industry that SARS itself lacked faith in the legislation.[169]

5.3 The effectiveness of the new GAAR

Since its amendment in 2006, no cases have been brought before the courts to judicially clarify and test the efficacy of the current GAAR.[170]

The single biggest factor in undermining the potential effectiveness of the new GAAR has been SARS' reluctance to invoke it. Indeed, SARS seemingly did not issue its first notices under section 80J until 2012, some six years after the statute was enacted. With some justification, this has led to a widespread belief in the tax avoidance industry that SARS itself lacked faith in the legislation.[171]

The lack of certainty on the face of the new GAAR is essentially twofold. In the first place, the components of the operative provisions of the GAAR are extremely complex. Second, some of the new concepts appear to be based on the jurisprudence of

[168] (Liptak 2017)
[169] (Liptak 2017)
[170] (ENSight)
[171] (Liptak 2017)

countries such as Canada, the United Kingdom and the United States. These concepts may fit comfortably into the tax jurisprudence of these countries, but less so into South Africa's.[172]

The major weakness of the new provisions is that they do not mention or provide what constitutes a permissible tax avoidance, so that the taxpayer can arrange his or her affairs accordingly. Such a weakness is a significant drawback in the business activities of the taxpayer. The provisions tend to tell the persons how to organise their business. In the eyes of the taxpayers, the impermissible tax avoidance arrangement works against them.[173]

On 12 November 2020, the Tax Court had to consider the application of some of the provisions of the GAAR in the matter of *Mr X v Commissioner for the South African Revenue Service (Case No IT24502)* and *Mr Y v Commissioner for the South African Revenue Service (Case No IT24503)* (as yet unreported). The Tax Court held that to interpret the GAAR, one must adopt the well-known approach set out in Natal Joint Municipal Pension Fund v Endumeni Municipality 2012(4) SA 593 SCA. Pursuant to this, the Tax Court noted that it is clear from the provisions of the new GAAR that the legislature intended a departure from the provisions of the old GAAR, and to this end, specifically excluded as a jurisdictional requirement that SARS must be "satisfied".[174]

The Tax Court held that the question regarding the duty to begin must be determined with reference to who bears the onus to prove the four requirements for an "impermissible avoidance arrangement" as alluded to above. In other words, if SARS relies on the existence of an "avoidance arrangement", it bears the onus of proving it. As the existence of an "avoidance arrangement" is in dispute, SARS must commence

[172] (de Koker & Williams 2021)
[173] (Kanamugire 2013)
[174] (Cliffe Dekker Hofmeyr 2021)

leading evidence. The Tax Court ultimately found that SARS bore the duty lead evidence first and ordered SARS to pay the taxpayers' costs in respect of those applications.[175]

5.4 Conclusion

The effectiveness of the new GAAR will be established once the courts have put it to the test, until then 'impermissible avoidance arrangements' term continues to be an untested theory.

[175] (Cliffe Dekker Hofmeyr 2021)

CHAPTER 6

6. REPORTABLE ARRANGEMENTS

The provisions of ss 80A-80L of the Income Tax Act must be read in conjunction with section 34-39 of the TAA.

This is another leg to the SARSs anti-avoidance strategy. The legislation was introduced originally as section 76A of the Act. According to the SARS very few arrangements have been reported, and thus the legislation has been redrafted and broadened in its scope, and now has been placed in the Act immediately after the new General Anti-Avoidance Rules (GAAR), as Part IIB of Chapter III of the Act, being sections 80M to 80T.[176]

The new definition incorporates certain elements of the previous section, but now also has added some additional requirements or has changed some of the original requirements. As before, an arrangement will be reportable if it contains provisions in terms of which the calculation of interest (but now also finance costs, fees or other charges) is wholly or partly dependent on the assumptions relating to the tax treatment of the arrangement.[177]

An 'arrangement' is a 'reportable arrangement' if a person is a 'participant' in the 'arrangement' and the 'arrangement'-

- Contains provisions in terms of which the calculation of 'interest' as defined in section 24J of the Income Tax Act, finance costs, fees or any other charges is wholly or partly dependent on the assumptions relating to the tax treatment of that 'arrangement' (otherwise than by reason of any change in the provision of a tax Act);

[176] (SAICA May 2007)
[177] (SAICA May 2007)

- Has any of the characteristics contemplated in section 80C(2)(*b*) of the Income Tax Act, or substantially similar characteristics;
- Gives rise to an amount that is or will be disclosed by any 'participant' in any year of assessment or over the term of the 'arrangement' as-
    - A deduction for purposes of the Income Tax Act but not as an expense for purposes of 'financial reporting standard';
    - Revenue for purposes of 'financial reporting standards' but not as gross income for purposes of the Income Tax Act;
- Does not result in a reasonable expectation of a 'pre-tax profit' for any 'participant'; or
- Results in a reasonable expectation of a 'pre-tax profit' for any 'participant' that is less than the value of that 'tax benefit' to that 'participant' if both are discounted to a present value at the end of the first year of assessment when that 'tax benefit' is or will be derived or is assumed to be derived, using consistent assumptions and a reasonable discount rate for that 'participant'.[178]

The Commissioner determined in Notice 140 (3 February 2016) that the following arrangements have certain characteristics that may lead to an undue tax benefit and must therefore be reported.

- An arrangement that would have qualified as a 'hybrid equity instrument' as defined in s 8E, of the Income Tax Act, if the prescribed period had been 10 years. This does not include an instrument listed on a regulated exchange.
- An arrangement whereby a company buys back shares from one or more of its shareholders for an aggregate amount exceeding R10 million and the company issued or is required to issue shares within 12 months of entering into the arrangement or the date of any buy-back in terms of the arrangement.
- An arrangement where a resident makes a contribution or payment to a non-resident trust and has or acquires a beneficial interest in the trust and the

[178] Tax Administration Act, 28 of 2011

amount of all contributions or payments or the value of the interest exceeds or is reasonably expected to exceed R10 million. Contributions to a foreign collective investment scheme (as contemplated in par (*e*)(ii) of the definition of 'company' in s 1 of the Income Tax Act) or a foreign investment company (as defined in s 1 of the Income Tax Act) are excluded.

- An arrangement where one or more persons acquire the controlling interest in a company by means of acquiring shares, voting rights or a combination thereof and the company has a balance of assessed loss exceeding R50 million or is reasonably expected to have an assessed loss exceeding R50 million.
- An arrangement between a resident and a foreign insurer in terms of which
    - The aggregate amount that has been paid or is reasonably expected to be paid to a foreign insurer exceeds R5 million,
    - Any amount payable to beneficiaries in terms of the arrangement is determined mainly by reference to the value of particular assets or categories of assets held by or on behalf of the foreign insurer.
- An arrangement whereby a non-resident renders consultancy, construction, engineering installation, logistical, managerial, supervisory, technical or training services to a resident or to a non-resident's permanent establishment in South Africa. Such arrangement only qualifies as a reportable arrangement if
    - The non-resident is or was physically present in South Africa in connection with or for the purpose of rendering such services (or is anticipated to be present in South Africa for such purpose), and
    - The expenditure incurred or to be incurred on or after 3 February 2016 exceeds or is anticipated to exceed R10 million in aggregate. If the expenditure incurred in relation to this arrangement qualifies as remuneration for purposes of the Fourth Schedule to the Income Tax Act, the arrangement does not qualify as a reportable arrangement.[179]

[179] (Stiglingh *et al.* 2021)

The following arrangements are excluded arrangements:

- A debt in terms of which the borrower receives or will receive an amount of cash and agrees to repay at least the same amount of cash to the lender at a determinable future date; or the borrower receives or will receive a fungible asset and agrees to return an asset of the same kind and of the same or equivalent quantity and quality to the lender at a determinable future date
- A lease
- A transaction undertaken through an exchange regulated in terms of the Financial Markets Act 19 of 2012, or
- A transaction in participatory interests in a scheme regulated in terms of the Collective Investment Schemes Control Act 45 of 2002.[180]

Furthermore, an arrangement will only qualify as an excluded arrangement if

- The arrangement must be undertaken on a stand-alone basis, or
- The arrangement would have qualifies as having been undertaken on a stand-alone basis were it not for a connected arrangement entered into for security and no tax benefit is obtained or enhanced by virtue of that security arrangement.

However, an arrangement is not an excluded arrangement if it is entered into

- With the main purpose of obtaining or enhancing a tax benefit, or
- In a specific manner or form that enhances a tax benefit.

The Commissioner is given the power to decide that an arrangement is an excluded arrangement by notice in the *Government Gazette.*[181]

[180] (Stiglingh *et al.* 2021)
[181] (Stiglingh *et al.* 2021)

The taxpayer has a duty to submit relevant information to SARS in a prescribed form and manner, outlining the details of the transaction, as discussed below.

The following information in relation to a 'reportable arrangement' must be submitted in the prescribed form and manner and by the date specified:

- A detailed description of all the steps and key features, including, in the case of an 'arrangement' that is a step or part of a larger 'arrangement', all the steps and key features of the larger 'arrangement'
- A detailed description of the assumed tax benefits for all participants, including, but not limited to, tax deductions and deferred income
- The names, registration numbers, and registered addresses of all participants
- A list of all its agreements, and
- Any financial model that embodies its projected tax treatment
  The Commissioner must issue a reportable arrangement reference number to each participant for administrative purposes, after the receipt of the required information as mentioned in s 38 (s 39).[182]

Failure to comply with this section, will result in hefty repercussions for the parties involved.

Reportable arrangements — penalties

Sanctions may be imposed upon a participant for failure to disclose the required information or furnish oral or written information, documents or things, in which event he will be liable to a penalty of R1 million. But there is a safety net left to the Commissioner's discretion, which has been made subject to objection and appeal in terms of s 3(4). He may remit the additional charge or part thereof when he is satisfied that there are extenuating circumstances and the participant remedies the non- disclosure within a reasonable time or if it is disproportionate to the assumed tax

benefit (s 80S).[183]

[182] (Stiglingh *et al.* 2021)
[183] (de Koker & Williams 2021)

‘Disguised or Simulated Transactions’

Simulated/ sham transactions are so called because they are entered into in a manner calculated to mislead the tax authorities into and to conceal their true purpose or “true” transaction.[184]

In many situations, an arrangement that lacks commercial substance will also be a disguised or simulated transaction in which the court will, in terms of common law principles, disregard the ostensible arrangement and give effect to the real transaction. In this regard, the common law remedy for the mischief is more powerful than s 80A in that the common law principle applies even in the absence of a sole or main purpose of obtaining a tax benefit.[185]

In *Michau v Maize Board*, Scott J said that

> ‘What [taxpayers] may not do is conceal the true nature of their transaction or, in the words of Innes JA in *Zandberg’*s case . . . “call it by a name, or give it a shape, intended not to express but to disguise its true nature”. In such event a court will strip off its ostensible form and give effect to what the transaction really is.’[186]

The principle was restated by the Supreme Court of Appeal in *C: SARS v NWK Ltd* where Lewis JA, giving the judgment of the court, followed her affirmation that a taxpayer is free to arrange his affairs so as to minimise tax liability and that there is nothing wrong with arrangements that are tax-effective, with the qualification:

[184] (South African Tax Guide)
[185] (de Koker & Williams 2021)
[186] (de Koker & Williams 2021)

> ‘But there is something wrong with dressing up or disguising a transaction to make it appear be something that it is not . . .’[187]

It was held in *Zandberg v Van Zyl* that the criterion is whether the parties to the agreement in question intended that it was to ‘have effect in accordance with its tenor’ and that, if they did so intend, then the agreement was not ‘simulated’ or ‘disguised’. Moreover, for a court to hold that a particular agreement was disguised or simulated, ‘The Court must be satisfied that there is a real intention, definitely ascertainable, which differs from the simulated intention.’[188]

in *C: SARS v NWK Ltd* where Lewis JA, giving the judgment of the court, said that

> ‘In my view the test to determine simulation cannot simply be whether there is an intention to give effect to a contract in accordance with its terms. Invariably where parties structure a transaction to achieve an objective other than the one ostensibly achieved they will intend to give effect to the transaction on the terms agreed. The test should thus go further and require an examination of the commercial sense of the transaction: of its real substance and purpose. If the purpose of the transaction is only to achieve an object that allows the evasion of tax, or of a peremptory law, then it will be regarded as simulated. And the mere fact that parties do perform in terms of the contract does not show that it is not simulated: the charade of performance is generally meant to give credence to their simulation.’[189]

In *Roshcon (Pty) Limited v Anchor Auto Body Builders CC* Wallis JA cited the last-mentioned passage from *NWK* and said as follows:

[187] (de Koker & Williams 2021)
[188] (de Koker & Williams 2021)
[189] (de Koker & Williams 2021)

> ‘It appears that in some circles this, and particularly the statement that ‘If the purpose of the transaction is only to achieve an object that allows the evasion of tax, or of a peremptory law, then it will be regarded as simulated’, has been understood to condemn as simulated transactions any and all contractual arrangements that enable the parties to avoid tax or the operation of some law seen as adverse to their interests. But that fails to read this sentence in the context of both the particular paragraph in the judgment and the entire discussion of simulated transactions that precedes it. If it meant that whole categories of transactions were to be condemned without more, merely because they were motivated by a desire to avoid tax or the operation of some law, that would be contrary to what Innes J said in *Zandberg v Van Zyl* in the concluding sentence of the passage quoted above, namely that: ‘The inquiry, therefore, is in each case one of fact, for the right solution of which no general rule can be laid down.
>
> That was manifestly not Lewis JA’s intention.’

Wallis JA then went on to say

> ‘For those reasons the notion that *NWK* transforms our law in relation to simulated transactions, or requires more of a court faced with a contention that a transaction is simulated than a careful analysis of all matters surrounding the transaction, including its commercial purpose, if any, is incorrect. The position remains that the court examines the transaction as a whole, including all surrounding circumstances, any unusual features of the transaction and the manner in which the parties intend to implement it, before determining in any particular case whether a transaction is simulated.’[190]

[190] (de Koker & Williams 2021)

CHAPTER 7

7. CONCLUSION

From the above, it has been noted that there will always be a struggle between taxpayers and SARS (and other tax authorities), where taxpayers and their advisers are constantly trying to find loopholes in the Income Tax Act provisions, so they can utilize them to with an objective of paying lesser tax or no tax at all (as described above, with reference to transactions that lack commercial substance, that are tax indifferent, round trip etc).

The amendment of the requirements in the new GAAR comes with 12 provisions that have been placed to deal with impermissible avoidance arrangements, these requirements are more elaborate than the previous requirements in the old GAAR.

The Amendment has introduced new provisions to assist the Commissioner to combat or eliminate impermissible tax avoidance. It has extended the concept of the impermissible tax avoidance arrangement. An avoidance arrangement is an impermissible avoidance arrangement if its sole or main purpose was to obtain a tax benefit and in any context it has created rights or obligations that would not normally be created between persons dealing at arm's length; or it would result directly or indirectly in the misuse or abuse of the provisions of this Act (including the provisions of this Part). This provision encompasses every section of the Income Tax Act. The Commissioner is empowered to follow anyone whose activity amounts to an impermissible tax avoidance arrangement by using the entire Act and other legislation. Almost every activity may amount to an impermissible tax avoidance arrangement, with the result that the Commissioner will intervene to prevent it.[191]

[191] (Kanamugire 2013)

The Amendment has also increased the remedies available to the Commissioner to nullify an impermissible tax avoidance arrangement. He or she can disregard any steps in, or parts of, the impermissible tax avoidance arrangement; disregard any accommodating or tax-indifferent party; and reallocate or re-characterise any gross income. These new remedies assist the Commissioner to perform his or her duty to eliminate any impermissible tax arrangement. The Commissioner is in a better position than before to defeat impermissible tax avoidance.[192]

Misleading statements in returns and a lack of full disclosure are common features of many tax schemes and can come to light many years later. For this reason too, s 103(1) will remain a potential threat to taxpayers for many years to come – indeed there is no definitive 'sunset' date when s 103(1) can finally be consigned to history.[193]

A further reason why s 103(1) remains relevant despite its repeal is that the new GAAR has borrowed many terms of art from s 103(1). There is an extensive body of case law on the interpretation of those terms and it is inevitable that the courts, when they seek to interpret similar terms in the new GAAR, will turn to those decisions for guidance.

When Australia abandoned its 'old' GAAR that was contained in s 260 of the Income Tax Assessment Act of 2006 and replaced it with a new GAAR in Part IVA of the Act, the High Court of Australia warned that

> 'Part IVA is to be construed and applied according to its terms, not under the influence of "muffled echoes of old arguments" concerning other legislation.'

[192] (Kanamugire 2013)
[193] (de Koker & Williams 2021)

In South Africa, however, it seems unrealistic to expect that the new Part IIA of the Act can be interpreted *de novo* and free of the 'muffled echoes' of s 103(1), given the many aspects of the latter provision that have been incorporated into the new GAAR.[194]

[194] (de Koker & Williams 2021)

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