Tutorial Letter 103/0/2017

Applied Taxation

TAX4862
NTA4862

Year module

Department of Financial Intelligence

This tutorial letter contains learning units 2 and 3 as well as self-assessment Assignment 01.
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I. INTRODUCTION

This tutorial letter is divided into two learning units. Learning unit 2 deals with donations tax and learning unit 3 deals with value-added tax. The goal of this tutorial letter is to assist you in making the most of the time available to master the topics in this tutorial letter. Follow the guidelines and try to keep to the time limitations. (Remember that these limitations are based on the fact that certain topics have already been covered in the first year of your postgraduate studies).

II. TIME FRAME

Your time should be divided into two parts:

- Obtaining the required knowledge (15 hours)
- Application of knowledge and revision of difficult concepts (15 hours)
  This would entail the completion of integrated and assignment questions (sections B and C of this tutorial letter). While obtaining the required knowledge (section A), you will, where we deem it necessary, be referred to specific questions in section C. After you have studied all the concepts and have completed all the questions, you will have time available to reflect on the knowledge obtained and to revisit any difficult concepts that you have difficulty understanding.

III. PROPOSED WORKING METHOD

Start by reading this tutorial letter. The tutorial letter will show you how to obtain the knowledge from the textbooks and the respective Acts. After you have obtained the knowledge, it should be easier to apply your knowledge when answering the questions.

IV. INSTRUCTION ICONS (LEGENDS)

In this tutorial letter, the following instruction icons will be used:

<table>
<thead>
<tr>
<th>Icon</th>
<th>Description</th>
</tr>
</thead>
<tbody>
<tr>
<td>Timer</td>
<td>Time allocation</td>
</tr>
<tr>
<td>Book</td>
<td>Work programme or Instruction or Activity</td>
</tr>
<tr>
<td>Information</td>
<td>Important or Additional information</td>
</tr>
<tr>
<td>Example</td>
<td>Examples or Exercises</td>
</tr>
</tbody>
</table>
Information about changes in legislation

Abbreviations used in the learning unit

Outcomes of the learning unit

The following abbreviations are used in this tutorial letter:

<table>
<thead>
<tr>
<th>Abbreviation</th>
<th>Meaning of abbreviation</th>
</tr>
</thead>
<tbody>
<tr>
<td>OMV</td>
<td>Open-market value</td>
</tr>
<tr>
<td>par</td>
<td>Paragraph</td>
</tr>
<tr>
<td>AQSAT</td>
<td>Advanced Questions on SA Tax 2017, Parsons, S. (Editor)</td>
</tr>
<tr>
<td>SAICA</td>
<td>The South African Institute of Chartered Accountants</td>
</tr>
<tr>
<td>LU</td>
<td>Learning unit</td>
</tr>
<tr>
<td>the Income Tax Act</td>
<td>the Income Tax Act No. 58 of 1962 (as amended)</td>
</tr>
<tr>
<td>the VAT Act</td>
<td>the Value-Added Tax Act No. 89 of 1991 (as amended)</td>
</tr>
<tr>
<td>TL</td>
<td>Tutorial letter</td>
</tr>
<tr>
<td>VAT</td>
<td>Value-added tax</td>
</tr>
</tbody>
</table>

V. WEEKLY STUDY PROGRAMME

<table>
<thead>
<tr>
<th>Day</th>
<th>Date</th>
<th>Activity</th>
</tr>
</thead>
<tbody>
<tr>
<td>Wednesday</td>
<td>15 February 2017</td>
<td>LU 1 in TL 102/2017 (30 minutes); donations tax; question 1 of self-assessment Assignment 01; and section C (2 hours and 30 minutes)</td>
</tr>
<tr>
<td>Thursday</td>
<td>16 February 2017</td>
<td>VAT (3 hours)</td>
</tr>
<tr>
<td>Friday</td>
<td>17 February 2017</td>
<td>VAT (3 hours)</td>
</tr>
<tr>
<td>Saturday</td>
<td>18 February 2017</td>
<td>VAT (6 hours) and section A – VAT; outcome of the Beancounter scenario (15 minutes); and section B: Integrated example (1 hour)</td>
</tr>
<tr>
<td>Sunday</td>
<td>19 February 2017</td>
<td>Section C: Self-assessment Assignment 01 (questions 2 – 23) (7 hours 45 minutes)</td>
</tr>
<tr>
<td>Monday</td>
<td>20 February 2017</td>
<td>Section C: self-assessment Assignment 01 (questions 2 – 23) (3 hours)</td>
</tr>
<tr>
<td>Tuesday</td>
<td>21 February 2017</td>
<td>Section C: Self-assessment Assignment 01 (questions 2 – 23) (3 hours)</td>
</tr>
</tbody>
</table>
VI. BEANCOUNTER SCENARIOS

Refer to TL 101/2017 to meet the Beancounter family.

VII. LECTURERS

The following lecturers compiled this tutorial letter:

Ms L Pienaar
Ms M Ungerer
Ms MS Vorster

Please contact any of the tax lecturers should you have questions regarding this tutorial letter. You may also send your queries (regarding administrative and academic matters) and comments via e-mail to TAX4862-17-Y1@unisa.ac.za. (Note that e-mail correspondence is the preferred method of communication – refer to TL 101/2017 in this regard.)

For queries regarding academic matters, you may call the administrative officer at +27 12 429 2947. The administrative officer will put you in touch with the relevant lecturer on duty or will take a message. The lecturer will contact you as soon as possible, or you may call the hunting line at +27 12 429 4135 (remember to let it ring so that the exchange can find a free extension).

VIII. IMPORTANT DATES FOR THIS TUTORIAL LETTER

Due date for self-assessment Assignment 01: 21 February 2017

Date of test 1: TUESDAY, 14 March 2017

(Covering both TL 103/2017 and TL 104/2017, as well as the relevant case law in TL 102/2017)

IX. UNISA’S OPEN-BOOK POLICY

VERY IMPORTANT

Please refer to TL 101/2017 and CASALL2/301/2017 for information on UNISA’s open-book policy (and calculator policy). It is very important to familiarise yourself with the policy, as you need to adhere to it strictly.

X. SYLLABUS FOR THIS MODULE

The content of this module is based on the SAICA Taxation Examinable Pronouncements. All provisions are either listed at a knowledge level of 3 or are excluded.

Knowledge level 3 (Advanced) is defined in the Competency Framework as follows:

At this level the candidate is required to acquire a thorough knowledge and rigorous understanding of the subject matter. This level of knowledge and understanding extends beyond a sound understanding of central issues, to include complexities and unusual / exceptional aspects associated with the subject matter.
Consequently the candidate is required to have a knowledge and understanding of –
- all content that is required to develop a thorough and rigorous understanding of the subject matter;
- complexities; and
- sufficient depth to clearly locate content in the general field of accountancy (as described by competencies II–VII) and to identify implications and relationships.

At this level the candidate should be equipped with a level of knowledge and understanding of the substance of the subject matter that enables him/her to perform tasks and solve problems with a high degree of rigour, exercising sound judgement.

| Interpretation and practice notes | Regulations, interpretation notes and binding general rulings included in the SAICA Student Handbook will be assessed on the same level as the applicable provision in the Act. |
SECTION A - GUIDELINES

REMEMBER
We assume that you have three hours of study time on a weekday/night and 15 hours over a weekend. We have based the work plan in this tutorial letter on this assumption.

WORK PLAN FOR WEDNESDAY, 15 FEBRUARY 2017

A total of 2 hours and 30 minutes of your study time has been allocated to LU 2 and 30 minutes to study the interpretation of legislation (LU 1 in TL 102/2017).

The following time allocation is recommended:

<table>
<thead>
<tr>
<th>Activity</th>
<th>Time</th>
</tr>
</thead>
<tbody>
<tr>
<td>Background and the interpretation of legislation (LU 1)</td>
<td>30 minutes</td>
</tr>
<tr>
<td>Revision of undergraduate knowledge of donations tax</td>
<td>135 minutes</td>
</tr>
<tr>
<td>Do question 1 in section C of this tutorial letter</td>
<td>15 minutes</td>
</tr>
<tr>
<td><strong>Total</strong></td>
<td><strong>180 minutes</strong></td>
</tr>
</tbody>
</table>

Note that this is much work to master in the allocated time, but most sections would have been covered in depth in your first year of postgraduate studies. You will probably not have time to study every section in detail again, but will have to rely on your prior knowledge. Where necessary, you should refresh your memory regarding sections you already know.

Start your studies of LU 1 and 2 by reading through notes 1 – 2.3.
1. **INTERPRETATION OF LEGISLATION**

Since this is your first academic tutorial letter for the year, we have decided to allocate the first 30 minutes of your study time this week to giving you some background information on the interpretation of legislation (LU 1, TL 102/2017). We feel that this is important before you start studying any specific legislation. After completing your study of the interpretation of legislation, we will first cover donations tax and then we will continue with the most important section of this tutorial letter, namely VAT.

Use the first 30 minutes of your study time today to familiarise yourself with LU 1: "Interpretation of legislation", which is contained in TL 102/2017. This should assist you in the optimal use of your Student Handbook.

2. **DONATIONS TAX**

2.1 **BACKGROUND**

Donations tax is a separate tax from income tax, but it is levied in terms of the Income Tax Act (Part V – sections 54 to 64). It is payable on the transfer of assets from one person (not necessarily a taxpayer) to another.

Take note that donations tax could also affect the calculation of capital gains tax, where an asset (as opposed to cash) is donated. You therefore also have to refer to the applicable paragraphs in the Eighth Schedule of the Income Tax Act.

2.2 **OUTCOMES OF THIS LEARNING UNIT**

After studying LU 2, you should be able to achieve the following outcomes:

- Achieve all the outcomes listed at the beginning of chapter 26 (Donations Tax) of SILKE.
- Explain and calculate the capital gains tax implications in terms of the Eighth Schedule of the Income Tax Act in the event of a donation.

2.2.1 **SAICA levels and references to the Income Tax Act**

The following table provides a summary of the sections of the Income Tax Act covered in LU 2:

> Although this table provides you with a summary of the sections of the Income Tax Act and the appropriate references to Silke covered in this learning unit, it should not be used in isolation to guide you through the study process. Proceed to the daily work programme and follow the specific study approach stated there.

Please note that at the time of completing this tutorial letter, we had to base our references to SILKE on the 2016 edition, since the 2017 edition was not yet available. Amendments to the legislation were also based on the available Bills. Should there be any differences, we will communicate them to you as soon as possible via myUnisa.
<table>
<thead>
<tr>
<th>Reference to the legislation</th>
<th>Topics</th>
<th>Reference to SILKE</th>
<th>SAICA level</th>
</tr>
</thead>
<tbody>
<tr>
<td>Sections 54 to 64</td>
<td>Donations tax</td>
<td></td>
<td></td>
</tr>
<tr>
<td>s 54</td>
<td>Levy of donations tax</td>
<td>26.1 – 26.2</td>
<td>*</td>
</tr>
<tr>
<td>s 55</td>
<td>Definitions for purposes of this part</td>
<td>26.3 – 26.4</td>
<td>*</td>
</tr>
<tr>
<td>s 56</td>
<td>Exemptions</td>
<td>26.7</td>
<td>*</td>
</tr>
<tr>
<td>s 57</td>
<td>Disposals by companies under donations at the instance of any person</td>
<td>26.9</td>
<td>*</td>
</tr>
<tr>
<td>s 57A</td>
<td>Donations by spouse married in community of</td>
<td></td>
<td></td>
</tr>
<tr>
<td>s 58</td>
<td>Property disposed of under certain transactions</td>
<td></td>
<td></td>
</tr>
<tr>
<td>s 59</td>
<td>Persons liable for the tax</td>
<td>26.10</td>
<td>*</td>
</tr>
<tr>
<td>s 60</td>
<td>Payment and assessment of the tax</td>
<td>26.10</td>
<td>*</td>
</tr>
<tr>
<td>s 61</td>
<td>Extension of scope of certain provisions of Act for purposes of donations tax</td>
<td></td>
<td></td>
</tr>
<tr>
<td>s 62(1)(a)–(c)</td>
<td>Value of property disposed of under donations (The value of limited interests in property will be given based on different life expectancies or a fixed period, and candidates should select relevant amount based on application of provisos)</td>
<td>26.11 – 26.11.1</td>
<td>*</td>
</tr>
<tr>
<td>s 64</td>
<td>Rate of donations tax</td>
<td>26.2</td>
<td>*</td>
</tr>
<tr>
<td>s 7C</td>
<td>Interest-free or low-interest loans to trusts (Effective 1 March 2017)</td>
<td>26.6</td>
<td>*</td>
</tr>
<tr>
<td>8th Schedule</td>
<td>Capital Gains Tax</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Disposals and acquisitions</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>par 11(1)</td>
<td>Disposals</td>
<td>28.7.1</td>
<td>*</td>
</tr>
<tr>
<td>Base cost</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>par 20</td>
<td>Base cost of asset</td>
<td>Only the basic principles 28.8.1 – 28.8.4</td>
<td>*</td>
</tr>
<tr>
<td>par 22</td>
<td>Amount of donations tax to be included in base</td>
<td>28.8.6</td>
<td>*</td>
</tr>
<tr>
<td>Proceeds</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>par 38</td>
<td>Disposals by way of donation, consideration not measurable in money and transactions between connected persons not at an arm's length price</td>
<td>28.9.7</td>
<td>*</td>
</tr>
<tr>
<td>Exclusions</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>par 62</td>
<td>Donations and bequests to public benefit organisations and exempt persons</td>
<td>28.10.2</td>
<td>*</td>
</tr>
<tr>
<td>Roll-overs</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>par 67</td>
<td>Transfer of asset between spouses</td>
<td>28.10.3.3</td>
<td>*</td>
</tr>
</tbody>
</table>
2.2.2 Sections in SILKE you may ignore

Note that regarding the calculation of the value of limited interests (SILKE – chapter 26.11.2 to 26.11.4) you need not know how to do the complex calculations (amounts will be provided in questions). You will be required to determine which value to use for the limited interests taking the provisos of section 62 into account. You must also be able to recognise and define the meaning of a fiduciary interest, usufruct and bare dominium, as described in the first few paragraphs of chapter 26.11.2. However, you may ignore the rest of chapter 26.11.2 (i.e. the steps to determine the value of a fiduciary, usufructuary or other like interest in property) as well as chapter 26.11.3 and 26.11.4.

2.2.3 Important law amendments

Every year, the proposed taxation law amendments are firstly published in the form of Bills. Only once the Bills have been passed through Parliament and once it is then assented to by the President, it is published as Acts. More information on this process is contained in Silke chapter 36.

The study material in this tutorial letter is based on amendments as proposed in the Bills. The two Bills which have been published on 26 October 2017 are Taxation Laws Amendment Bill 17 of 2016 and in the Tax Administration Laws Amendment Bill 18 of 2016. It is normally expected that the Bills will be enacted by early 2017.

An important proposed amendment which is applicable to this learning unit is contained in the Taxation Laws Amendment Bill (Bill 17 of 2016) as follows:

**PROPOSED LAW AMENDMENTS**

The Bill introduces a new section, section 7C, which stipulates that the interest (calculated as the difference between the interest that would have been charged at the official interest rate and the actual interest paid) on an interest-free or low interest rate loan made to a trust by a connected person who is a natural person or at the instance of a natural person will be a donation for donations tax purposes. This amendment only comes into operation on 1 March 2017 and is deemed to be a donation to the trust on the last day of the year of assessment of that trust. Refer to SILKE, chapter 26.6.

Before you start studying the detailed provisions of donations tax, you should first read the following scenario relating to the Beancounter family. As you study the applicable sections in the Income Tax Act, identify areas of concern that should be brought to the attention of the Beancounter family.
2.3 BEANCOUNTER SCENARIO

Barry Beancounter is married in community of property to Bizzie Beancounter. Barry is a very charitable person, as he made a number of donations during the year.

- He donated R40 000 cash to the Butterbean Family Trust, R20 000 cash to his lovely wife, Bizzie, and R20 000 cash to each of his children, Jelly and Soya Beancounter.

- He also donated R5 000 to the B.E.A.N. political party.

- Barry considers selling a property with a market value of R500 000 to the Butterbean Family Trust on an interest-free loan account. This property is excluded from Barry and Bizzie’s joint estate. The journal entry will be recorded as follows in the financial records of the trust:

<table>
<thead>
<tr>
<th>Dr Property</th>
<th>R500 000</th>
</tr>
</thead>
<tbody>
<tr>
<td>Cr Loan account: B Beancounter</td>
<td>R500 000</td>
</tr>
</tbody>
</table>

- He also considers making another donation to the trust utilising the rest of his R100 000 annual exemption. (Remember there is an existing loan [see above] that the trust owes Barry.)

- All cash donations (except for the donation to Bizzie) were made (and in future will be made) from funds available in an investment account. This investment is included in Barry and Bizzie’s joint estate.

Barry is, however, uncertain about the donations tax and capital gains tax implications (if any) that may arise from the above donations he made during the year, as well as those he considers making and he has therefore asked you to assist him.

Before attempting to assist Barry with his donations tax and capital gains tax query, you should first work through and master the applicable sections in the Income Tax Act relating to donations tax.

2.4 DISCUSSION OF DONATIONS TAX

You should now be ready to commence studying the calculation of donations tax. Work through note 2.4.1 in this tutorial letter. The framework provided in this note may be used as a mind map for donations tax and should be a useful study tool.
2.4.1 Framework for the calculation of donations tax

DID A RESIDENT DISPOSE OF THE PROPERTY?

YES

WAS THIS PROPERTY DISPOSED OF UNDER ANY DONATION OR DEEMED DONATION?

YES

IS THE DONATION EXEMPT FROM DONATIONS TAX?

NO

IS THE DONATION A REASONABLE CONTRIBUTION TO MAINTENANCE OF A PERSON?

NO

CALCULATE THE VALUE OF THE DONATION.

CALCULATE THE TAXABLE DONATION = VALUE OF DONATION LESS BALANCE OF EXEMPTION (not a natural person: R10 000 per annum; natural person: R100 000 per annum) (exemption applied in order that donations take effect)

NO DONATIONS TAX PAYABLE

CALCULATE DONATIONS TAX = TAXABLE DONATION x 20%

References to the Income Tax Act

Sections 1 and 54

Sections 54, 55 and 58

Section 56(1)

Section 56(2)

Section 62

Section 56(2) Section 60(2)

Section 64
Notes to the framework

1. Donations tax is payable on the fair market value of any property disposed of gratuitously or for less than the fair market value by a South African resident.

2. Donations tax must be calculated separately on each donation as and when the donation takes place and not at the end of the year of assessment as in the case of income tax. The R100 000 exemption, applicable to natural persons, and the R10 000, applicable to persons who are not natural persons, must therefore be applied in the order that the donations take place.

3. The R100 000 exemption, applicable to natural persons, applies to all property donated and is not apportioned where the period of assessment is less than a full year. The R10 000 exemption, on the other hand, applicable to a donor that is not a natural person, only applies to casual gifts and it must be apportioned where the period in question exceeds or is less than 12 months.

4. Donations tax is payable by the end of the month following the month during which the donation takes effect.

Example: Donations tax

On 20 January 2017, Petrus, married out of community of property, donated all his old furniture and Toyota Corolla to his younger sister. At this date, the furniture was worth R45 000 (he purchased it for R70 000 in 2013) and his Toyota Corolla had a book value (market value) of R90 000 (original cost was R140 000).

REQUIRED
Calculate and indicate whether the donation of the furniture and motor vehicle to Petrus’ sister will have donations tax implications for Petrus if

- he is an ordinary resident of the Republic of South Africa; or
- he is not a resident of the Republic.

Suggested solution

1) Resident

A resident is subject to donations tax (sections 1 and 54)

<p>| | |</p>
<table>
<thead>
<tr>
<th></th>
<th></th>
</tr>
</thead>
<tbody>
<tr>
<td>Furniture</td>
<td>R45 000</td>
</tr>
<tr>
<td>Toyota</td>
<td>R90 000</td>
</tr>
<tr>
<td><strong>Total</strong></td>
<td><strong>R135 000</strong></td>
</tr>
</tbody>
</table>

Less: Section 56(2)(b) exemption

<p>| | |</p>
<table>
<thead>
<tr>
<th></th>
<th></th>
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</thead>
<tbody>
<tr>
<td><strong>(100 000)</strong></td>
<td></td>
</tr>
<tr>
<td>x 20%</td>
<td></td>
</tr>
<tr>
<td><strong>Total</strong></td>
<td><strong>R35 000</strong></td>
</tr>
</tbody>
</table>

<p>| | |</p>
<table>
<thead>
<tr>
<th></th>
<th></th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>7 000</strong></td>
<td></td>
</tr>
</tbody>
</table>
2) Non-resident

Donations tax is not applicable to non-residents.

REMEMBER

Donations tax does not apply to non-residents, even if they donate South African assets. Donations tax is payable by the end of the month following the month during which the donation takes effect.

Read the definition of a resident in section 1 of the Income Tax Act (which will be dealt with in detail in TL 104/2017) and work through SILKE, chapter 26.1 to 26.11 (refer to par 2.2.2 of this tutorial letter and ignore the steps to determine the value of a fiduciary, usufructuary or other like interest in property under chapter 26.11.2, as well as chapter 26.11.3 and 26.11.4), together with the following additional notes 2.4.2 to 2.4.5 in this tutorial letter. Also, refer to sections 54 to 64 of the Income Tax Act. Although we will not refer you specifically to the Income Tax Act, we urge you to refer to it while working through chapter 26.

2.4.2 General

REMEMBER

Refer to paragraph 2.2.2 of this tutorial letter regarding your required knowledge of the value of limited interests (SILKE, chapter 26.11.2 – ignore the steps to determine the value of the limited interests and chapter 26.11.3–26.11.4). As noted under paragraph 2.2.2, you will be required to determine which value to use for the limited interests, taking the provisos of section 62 of the Income Tax Act into account. The provisos are discussed below.

A donor may donate either the bare dominium or the usufructuary of a property or he/she may donate the full ownership of the property. Remember that the value of a bare dominium (refer to SILKE, chapter 26.11.2) is the fair market value of a property less the value of the usufruct.

Provisos to section 62

When calculating the value of a fiduciary or a usufructuary, we first have to calculate the annual value of a fiduciary or usufructuary. This is done by multiplying the fair market value of the property by a rate of 12%. However, if the Commissioner is satisfied that the property cannot reasonably be expected to produce an annual yield equal to 12%, he may fix whatever sum may seem reasonable to him as representing the annual yield.

(Therefore, if a question provides the value of a fiduciary and usufructuary calculated by applying a rate of 12% and another value calculated by applying a rate accepted by the Commissioner as reasonable, you should use the value calculated by using the rate acceptable to the Commissioner.)

The annual value of books, pictures, statuary or other objects of art is determined as

- the average net receipts, if any
- derived by the person entitled to the right of enjoyment of the property
- during the three years immediately preceding the date at which the donation took effect
2.4.3 Donations in the same group of companies (section 56(1)(f) – SILKE 26.7.1)

Note that a “group of companies” refers to at least a 70% direct holding of equity shares (by the controlling group company) in at least one controlled group company in the same group of companies. In addition, the donating company must be a resident for this exemption to apply.

2.4.4 Capital gains tax consequences of a donation

Study SILKE, chapter 28.8.6 (par 22 of the Eighth Schedule), 28.9.7 (par 38 of the Eighth Schedule), and 28.10.2 (only the paragraph relating to par 62, which appears under the heading “(11) Public benefit organisations and other exempt bodies – exclusions (par 62)”) and 28.10.3.3 (par 67 of the Eighth Schedule) in order to understand that a donation can, in addition to donations tax, also have capital gains tax consequences. To be able to understand the capital gains tax consequences of a donation it is not necessary to have a detailed knowledge of capital gains tax. The knowledge obtained from your undergraduate studies should be sufficient.

2.4.5 Impact of donations on other taxes

Read SILKE, chapter 26.12.

Always remember that a donation may affect many more things than merely donations tax. You may be required to consider the capital gains tax or normal tax (including income tax and capital gains tax) implications of a donation.

Donations tax may therefore be combined/integrated with topics that will only be addressed in future tutorial letters, for example:

- Meaning of “resident” – TL 104/2017
- Capital gains tax – TL 104/2017 (see previous discussion)
- Trusts (sections 7(3) – 7(10)) – TL 105/2017.

**REMEMBER**

Do not confuse the section 18A deduction (donations to certain organisations) with the donations tax provisions! Even if no donations tax is payable on a specific donation, it does not mean that the specific donation may be deducted for normal tax purposes. Consider the provisions of section 18A to determine the deductibility for normal tax purposes.

You have now covered all the theory on donations tax. Attempt question 10.1 in AQSAT to see how the theory is applied in a practical question.
**SUGGESTED SOLUTION: Integrated example on donations tax (AQSAT 10.1)**

a)

<table>
<thead>
<tr>
<th>Date</th>
<th>Donee</th>
<th>Amount</th>
<th>Exempt portion</th>
<th>Taxable portion</th>
<th>Due @ 20%</th>
<th>Note</th>
</tr>
</thead>
<tbody>
<tr>
<td>20 March</td>
<td>Niece</td>
<td>40 000</td>
<td>(40 000) (s 56(2)(b))</td>
<td>-</td>
<td>-</td>
<td>2</td>
</tr>
<tr>
<td>1 April</td>
<td>SPCA</td>
<td>5 000</td>
<td>(5 000) (s 56(1)(h))</td>
<td>-</td>
<td>-</td>
<td></td>
</tr>
<tr>
<td>30 April</td>
<td>Husband</td>
<td>50 000</td>
<td>(50 000) (s 56(1)(b))</td>
<td>-</td>
<td>-</td>
<td>3</td>
</tr>
<tr>
<td>10 June</td>
<td>Son</td>
<td>70 000</td>
<td>(60 000) (s 56(2)(b))</td>
<td>10 000</td>
<td>2 000</td>
<td>4</td>
</tr>
<tr>
<td>1 October</td>
<td>Trust</td>
<td>-</td>
<td>-</td>
<td>-</td>
<td>-</td>
<td>5</td>
</tr>
<tr>
<td>20 December</td>
<td>Two children</td>
<td>10 million</td>
<td>(10 million) (s 56(1)(d))</td>
<td>-</td>
<td>-</td>
<td></td>
</tr>
<tr>
<td>10 January</td>
<td>Best friend</td>
<td>80 000</td>
<td>-</td>
<td>80 000</td>
<td>16 000</td>
<td>6</td>
</tr>
</tbody>
</table>

b) The donations tax is payable by Mrs Good by the end of the month following the month in which each separate donation takes effect (section 60(1)).

**Notes to the solution**

1. Payable by the end of the month following the month in which the specific donation takes effect.

2. Annual basic exemption from donations tax of R100 000, applied in the order that the donations take effect. The donation to the niece is R40 000; therefore, R60 000 as exemption is still left for other donations.

3. For the benefit of the donor’s spouse – thus it is exempt.

4. The balance of the section 56(2)(b) exemption applies, that is, a R60 000 balance of the exemption applied against the donation (see note 2). (It will not qualify for the bona fide maintenance exemption [section 56(2)(c)], since it was donated for investment purposes.)

5. The contributions to the trust are a settlement of her legal obligations under the divorce settlement and therefore do not comprise a donation.

6. In terms of section 58, the donation will be the amount by which the value of the motor car exceeds the selling price; thus R180 000 – R100 000 = R80 000.

Read the Beancounter scenario again and make a rough summary of what your solution would be. Now read the outcomes of the scenario to determine if your answer is correct.
2.5 OUTCOMES OF THE BEANCOUNTER SCENARIO

After you have studied donations tax, you should be able to answer Barry Beancounter’s query on donations tax. In formulating your advice, you should have considered the following:

- For persons married in community of property, it is important to establish if the property falls in the joint estate or if it is excluded from the joint estate. The effect is explained in section 57A (refer to SILKE, chapter 26.8).

- Section 56(1) exemptions from donations tax must be considered, for example, donations to the spouse (section 56(1)(b)) or to any political party (section 56(1)(h)).

- Barry may be taxed on some of the income from the trust (donations in terms of section 7 – refer to TL 105/2017).

- Also, note the order of donations in the case of multiple donations (section 60(2)).

Donations tax payable

<table>
<thead>
<tr>
<th>Description</th>
<th>Amount</th>
</tr>
</thead>
<tbody>
<tr>
<td>Donation of R40 000 to the Butterbean Family Trust (R100 000)</td>
<td></td>
</tr>
<tr>
<td>(section 56(2)(b) exemption) – R40 000 / 2 [donation out of joint estate]</td>
<td></td>
</tr>
<tr>
<td>R80 000 [remaining balance of exemption]</td>
<td></td>
</tr>
<tr>
<td>Donation to his wife, Bizzie – exempt (section 56(1)(b))</td>
<td></td>
</tr>
<tr>
<td>Donation of R20 000 to Jelly (R80 000 [balance of section 56(2)(b) exemption]</td>
<td></td>
</tr>
<tr>
<td>– R20 000/2 [donation out of joint estate] = R70 000 [new balance of exemption]</td>
<td></td>
</tr>
<tr>
<td>Donation of R20 000 to Soya (R70 000 [balance of section 56(2)(b) exemption]</td>
<td></td>
</tr>
<tr>
<td>– R20 000/2 [donation out of joint estate] = R60 000 [new balance of exemption]</td>
<td></td>
</tr>
<tr>
<td>Donation to B.E.A.N. political party – exempt (section 56(1)(h))</td>
<td></td>
</tr>
</tbody>
</table>

All of the above taxable donations will be exempt from donations tax, as the first R100 000 of donations made by a natural person during a tax year are exempt from donations tax (section 56(2)).

The R100 000 must be applied in the order that the donations take place, as donations tax must be calculated separately on each of the donations as and when they take place. Donations tax is payable by the end of the month following the month in which the donation takes effect.

- If Barry donates the property with a market value of R500 000 to the Butterbean Family Trust, no donations tax will be payable, as the donation will be reflected against Barry’s loan account in the trust. (Section 7 could however be applicable. This section will be dealt with in TL 105/2017.) An interest-free loan in itself is not a donation for donations tax purposes, but it is a continuing donation for purposes of section 7 only.

Take note that once the new section 7C (relating to interest-free loans made to trusts) comes into effect on 1 March 2017, it will need to be taken into account.
If Barry decides to make a donation to the trust, you will have to establish if he has made a cash donation or if he has waived a portion of the loan owed by the trust. Waiving part of a loan is often done by utilising the R100 000 (or portion thereof – R60 000 remaining balance, in this case) annual exemption from donations tax. If this is the case, the waiver of the loan will have capital gains tax implications for the trust (paragraph 12A of the Eighth Schedule), or it might have section 19 implications. Note that, if it constitutes a donation or a deemed donation, neither paragraph 12A of the Eighth Schedule nor section 19 of the Income Tax Act will be applicable. Capital gains tax will be discussed in TL 104/2017 and section 19 is dealt with in TL 106/2017. If he makes a cash donation, he can make a donation of R120 000 without paying any donations tax, as it will be paid out of the joint estate. Therefore, his donation will be R60 000 and he will still have a section 56(2)(b) exemption of R60 000 that he may utilise. Bizzie, on the other hand, might have to pay donations tax if she has no portion of the section 56(2)(b) exemption available.

REMEMBER

Whenever there is a “donation, settlement or other disposition” in terms of section 7, the subsections of section 7 will be applicable on the income received by or accrued to a beneficiary from a donated asset. This section will be dealt with in TL 105/2017.

An interest-free loan in itself is not a donation for donations tax purposes, but it is a continuing donation for purposes of section 7. (Also, take note of Commissioner, SARS v Brummeria Renaissance (Pty) Ltd [2007] SCA 99 (RSA), 69 SATC 205 – TL 102/2017.) From 1 March 2017, the interest-free portion of an interest-free or low interest rate loan made to a trust will be a donation for donations tax purposes.

To test your ability to apply your knowledge and comprehension of donations tax to practical problems, do question 1 of section C.

After completion of the above question, please use the outcomes at the beginning of this learning unit to identify areas for improvement.

You have now completed LU 2 ("Donations tax") and you should be ready to attempt LU 3 (VAT) tomorrow.
3. VALUE-ADDED TAX  
DETAILED WORK PLAN FOR VAT

A total of 27 hours of your study time this week has been allocated to the studying of VAT.

The following time allocation is recommended:

<table>
<thead>
<tr>
<th>Activity</th>
<th>Time</th>
</tr>
</thead>
<tbody>
<tr>
<td>Outcomes for this learning unit and the Beancounter scenario</td>
<td>45 minutes</td>
</tr>
<tr>
<td>Output tax (including types of supplies)</td>
<td>315 minutes</td>
</tr>
<tr>
<td>Time and value of supplies</td>
<td>60 minutes</td>
</tr>
<tr>
<td>Input tax (including denial of input tax and imports)</td>
<td>120 minutes</td>
</tr>
<tr>
<td>Special situations (including instalment credit agreements and fixed assets)</td>
<td>35 minutes</td>
</tr>
<tr>
<td>Adjustments</td>
<td>80 minutes</td>
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<td>Administrative issues</td>
<td>20 minutes</td>
</tr>
<tr>
<td>Comprehensive examples</td>
<td>45 minutes</td>
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<tr>
<td>Outcomes of the Beancounter scenario</td>
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<tr>
<td>Section B (Integrated example)</td>
<td>60 minutes</td>
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<tr>
<td>Section C (Self-assessment Assignment 01)</td>
<td>825 minutes</td>
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<tr>
<td><strong>Total</strong></td>
<td><strong>27 hours</strong></td>
</tr>
</tbody>
</table>

Start your studies of LU 3 by reading notes 3.1 and 3.2.
WORK PLAN FOR THURSDAY, 16 FEBRUARY 2017

Your three hours’ study time for today has been allocated to the studying of VAT. The following time allocation is recommended:

<table>
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<th>Outcomes for this learning unit and the Beancounter scenario</th>
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</tr>
</thead>
<tbody>
<tr>
<td>Output tax (including types of supplies)</td>
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<tr>
<td><strong>Total</strong></td>
<td><strong>180 minutes</strong></td>
</tr>
</tbody>
</table>

3.1 BACKGROUND

After the completion of the first year of your postgraduate studies, you should have a basic knowledge of VAT. In this learning unit, you should concentrate on those areas that were not covered in your previous studies and master complex issues. While studying, ensure that you can also apply the theory to a practical situation. When you plan your study time, bear in mind the required levels of knowledge, as indicated in the SAICA tax syllabus (reflected in the table under note 3.2 of this learning unit).

3.2 OUTCOMES OF THIS LEARNING UNIT

After studying LU 3, you should be able to meet all the outcomes listed at the beginning of chapter 32 of SILKE.

3.2.1 SAICA levels and references to the VAT Act

The following table provides a summary of the sections of the VAT Act covered in learning unit 3:

Although this table provides you with a summary of the sections of the Income Tax Act and the appropriate references to Silke covered in this learning unit, it should not be used in isolation to guide you through the study process. Proceed to the daily work programme and follow the specific study approach stated there.

Please note that at the time of completing this tutorial letter, we had to base our references to SILKE on the 2016 edition, since the 2017 edition was not yet available. Amendments to the legislation were also based on the available Bills. Should there be any differences, we will communicate them to you as soon as possible via myUnisa.
<table>
<thead>
<tr>
<th>Reference to the VAT Act</th>
<th>Topics</th>
<th>Reference to SILKE</th>
<th>SAICA levels</th>
</tr>
</thead>
<tbody>
<tr>
<td>s 1</td>
<td>All definitions, except for the following:</td>
<td>Various</td>
<td></td>
</tr>
<tr>
<td></td>
<td>Excluded: Lloyds, Road Accident Fund, constitutional institution, controller, customs-controlled area, customs-controlled area enterprise, customs and excise act, designated entity, part (d) of the definition of “exported”, inbound and tax-free shop, Industrial Development Zone (IDZ), IDZ operator, service enterprise and transitional metropolitan council</td>
<td></td>
<td>excluded</td>
</tr>
<tr>
<td></td>
<td>Note: It will be stated whether or not an 'imported service' qualifies as an 'electronic service'.</td>
<td></td>
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<tr>
<td>s 2</td>
<td>Financial services</td>
<td>32.11.1</td>
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<tr>
<td></td>
<td>Debt security (c), provision of credit (f) and the issue, allotment or transfer of ownership of an equity security (d)</td>
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<td></td>
<td>Rest of the section</td>
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<td>s 3</td>
<td>Determination of &quot;open market value&quot;</td>
<td>32.22</td>
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<tr>
<td>s 4</td>
<td>Administration of Act</td>
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<tr>
<td>s 5</td>
<td>Exercise of powers and performance of duties</td>
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<td>s 6</td>
<td>Secrecy</td>
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<td>s 7</td>
<td>Imposition of VAT</td>
<td>32.4 – 32.9</td>
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<tr>
<td>s 8</td>
<td>Certain supplies of goods or services deemed to be made or not made</td>
<td>32.12</td>
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<td>s 8(9)</td>
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<td>Supply of services</td>
<td>32.10.2 &amp; 32.12.3.1</td>
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<td>Reference to the VAT Act</td>
<td>Topics</td>
<td>Reference to SILKE</td>
<td>SAICA levels</td>
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**Important court decisions**

| TL102/2017 | South Atlantic Jazz Festival (Pty) Ltd v C: SARS (6 February 2015) | 32.18 |
| TL102/2017 | CSARS v British Airways PLC | 32.12.8 |
| TL102/2017 | Stellenbosch Farmers’ Winery Ltd v CSARS | 32.10.2.4 |
| TL102/2017 | Master Currency (Pty) Ltd v C: SARS (20 March 2013) | 32.10.2.4 |
| TL102/2017 | CSARS v De Beers Consolidated Mines Ltd | 32.9.1 |

**VAT Binding General Rulings**

Binding General Ruling (VAT): No. 6 (Issue 2), 19 June 2012 – Discounts, rebates and incentives in the fast moving | 32.19.2 | * |
### Reference to the VAT Act

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# 3.2.2 Sections in SILKE you may ignore

When working through chapter 32 in SILKE, you may IGNORE all paragraphs of the text with shaded headings. This learning unit of the tutorial letter will guide you through chapter 32 of SILKE. Follow the work plan provided in the learning unit, as we will clearly indicate any particular part of a paragraph in SILKE that are EXCLUDED from the SAICA syllabus and that should therefore not be studied.

# 3.2.3 Important law amendments

You need to take note of the following proposed amendments to the VAT Act contained in the Taxation Laws Amendment Bill 17 of 2016 and in the Tax Administration Laws Amendment Bill 18 of 2016.

**PROPOSED LAW AMENDMENTS**

- Subparagraph (ii) of the definition of “second-hand goods will be amended effective from 1 April 2017 and will in future read as follows:
  - (aa) goods consisting solely of gold unless acquired for the sole purpose of supplying such goods in the same state without any further processing;
  - (bb) gold coins contemplated in section 11(1)(k); or
  - (cc) any other goods containing gold unless those goods are acquired for the sole purpose of supplying those goods in the same or substantially the same state to another person.
The following amendments to the VAT Act, which were enacted in the Taxation Laws Amendment Act 25 of 2015 which contains amendments which is effective from either 1 April 2016 or 1 April 2017 as indicated at each amendment:

- Section 7(4) has been added and stipulates the following:
  If the Minister makes an announcement in the national annual budget, that the VAT rate specified in this section is to be altered, that alteration will be effective from a date determined by the Minister in that announcement, and continues to apply for a period of 12 months from that date subject to Parliament passing legislation giving effect to that announcement within that period of 12 months.

  This stipulation was inserted to provide for a possible increase in the VAT rate during the next fiscal year.

- Section 16(2)(g) has been replaced with the following:
  (i) a ruling requested no later than two months prior to the expiry of the five-year period referred to in subsection (3) and issued in terms of section 41B of this Act or Chapter 7 of the Tax Administration Act confirms that the document in the vendor’s possession is acceptable for the purpose of making a deduction; and
  (ii) the ruling and document are held by the vendor at the time a return in respect of the deduction is furnished: Provided that the Commissioner may only issue a ruling in terms of this paragraph if satisfied that—
    (aa) the vendor has taken reasonable steps to obtain a document required in terms of paragraph (a), (b), (c), (d), (dA), (e) or (f) and is unable to obtain such a document due to circumstances beyond the vendor’s control; and
    (bb) no other provision of this Act can be applied to satisfy the Commissioner that the document in the vendor’s possession is acceptable for purposes of making a deduction.

  This stipulation provides for situations where vendors cannot obtain valid tax invoices under specific circumstances.
LAW AMENDMENTS

- Commercial accommodation and enterprise (section 1(1) – amendment of definitions of commercial accommodation and enterprise)
  
  In terms of the previous definition of commercial accommodation the supply of commercial accommodation would only be deemed to be that of commercial accommodation if the annual total receipts from the supply of commercial accommodation exceeded or were reasonably expected to exceed R60 000 in a period of 12 months. In turn, proviso (ix) to the definition of enterprise stated that where these supplies of commercial accommodation did not exceed or could not reasonably be expected to exceed R60 000 in any 12 month period the supplies would not be deemed to be made in the course of an enterprise.

  In the 2015 law amendments reference to the monetary threshold of R60 000 in the definition of commercial accommodation was removed and in proviso (ix) to the definition of an enterprise the monetary threshold was increased to R120 000.

  Therefore, from 1 April 2016, a person that carries on or intends to carry on an enterprise or activity supplying commercial accommodation, as defined, is deemed to be carrying on an enterprise and will be able to register as a vendor for VAT purposes if the total value of taxable supplies made by that person in respect of that enterprise or activity exceeded R120 000 in the preceding period of 12 months or is reasonably expected to exceed R120 000 in a period of 12 months.

- Shareholder (section 1(1) – definition of shareholder)
  
  A definition for a shareholder was included into the VAT Act, effective from 1 April 2016. The definition reads as follows:
  
  (a) In relation to any company referred to in paragraph (a), (b) or (d) of the definition of 'company' in section 1(1) of the Income Tax Act, means the registered shareholder in respect of any share, except that where some person other than the registered shareholder is entitled, whether by virtue of any provision in the memorandum or articles of association of the company or under the terms of any agreement or contract, or otherwise, to all or part of the benefit of the rights of participation in the profits, income or capital attaching to the share so registered, that other person shall, to the extent that such person is entitled to such benefit, also be deemed to be a shareholder; or
  
  (b) in relation to any close corporation, means a member of such corporation; or
  
  (c) in relation to any co-operative, means a member of such co-operative.

- Domestic goods or services (section 1(1) – definition of domestic goods or services)
  
  Domestic goods and services are goods and services provided in any enterprise supplying commercial accommodation. The definition includes a list of items that are included in domestic goods and services. From 1 April 2016 water is included in the list of domestic goods and services.
**LAW AMENDMENTS**

- **Time of supply – connected persons (section 9(2) proviso to paragraph (a))**
  In terms of section 9(2)(a) the time of supply where the supplier and recipient are connected persons is:
  (i) in the case of a supply of goods which are to be removed, at the time of the removal; and
  (ii) in the case of a supply of goods which are not to be removed, at the time when they are made available to the recipient; and
  (iii) in the case of a supply of services, at the time the services are performed;
  Provided that in the case where an invoice is issued or any payment is made in respect of a supply on or before:
  - the day that the tax return for the tax period during which the supply was made is furnished, or
  - the last day that such a return may in terms of the VAT Act be furnished, section 9(2)(a) will not apply, the general timing rule in section 9(1), the earlier of the time an invoice is issued or the time any payment of consideration will apply.

  Effective from 1 April 2016, section 9(2)(a) does not apply if the recipient is a vendor that can claim the full input tax in respect of the supply and the whole of the consideration or part thereof for the supply of the goods or services cannot be determined at the time that the goods are removed or made available or at the time the services are performed. The general timing rule in section 9(1) will be applicable.

- **Value of supply – connected persons (section 10(4)(a))**
  In terms of section 10(4) if a supplier makes a supply to a recipient that is a connected person to the supplier and the supplier is either not a vendor or is a vendor that cannot claim the full input tax in respect of the supply, the consideration in money for the supply will be the open market value of the supply, if:
  - the supply is made for no consideration, or
  - for a consideration in money which is less than the open market value.

  Effective from 1 April 2016 the consideration in money is deemed to be the open market value if the consideration cannot be determined at the time of supply.

- **Zero-rating exported goods (section 11(1)(a)(ii))**
  Reference to an export incentive scheme referred to in paragraph (d) has been changed to reference to the regulation referred to in paragraph (d).

- **Exempt supplies - (section 12(h))**
  Section 12(h) provides for an exemption of a supply by a school, university, technikon or college solely or mainly for the benefit of its learners or students of goods or services necessary for and subordinate and incidental to the supply of educational services, if such goods or services are supplied for a consideration in the form of school fees, tuition fees or payment for board and lodging and effective from 1 April 2016 also for lodging (not just for board and lodging).

- **Accounting basis - (section 15))**
  As from 1 April 2016 the South African Broadcasting Corporation Limited contemplated in section 8A of the Broadcasting Act, 1999 was added to the list of vendors that may apply to the Commissioner in writing to account for tax payable on the payment basis.
LAW AMENDMENTS

- **Credit and debit notes - (section 21(6))**
  Reference to section 21(1)(e) was added to section 21(6). This amendment refers to a recipient, that is a vendor and has written or other notice or otherwise knows that a tax invoice is incorrect as a result of an error in stipulating the amount of consideration agreed upon for that supply. If the vendor deducted input tax in respect of that supply of goods or services, the excess amount of input tax claimed shall be deemed to be tax charged (output tax) in relation to a taxable supply in the tax period in which that notice or other knowledge was received or the amount of input tax for that tax period will be reduced with the excess input tax claimed.

- **Grants (section 1(1) – definition of grants)**
  From 1 April 2017 the definition of a grant will include a payment made to or on behalf of a vendor in terms of the national housing programme contemplated in the Housing Act, 1997 (Act No. 107 of 1997).

- **Zero-rating of grants (section 11(2)(c))**
  From 1 April 2017 the supply of goods and services in terms of the national housing programme contemplated in the Housing Act, 1997 and supplies to a public will no longer be zero-rated.

Before you start studying the detailed provisions of the VAT Act, read the following scenario relating to the Beancounter family. The scenario provided requires that you first carefully read the information provided. Then, as you study the different VAT provisions, identify areas of concern that should be brought to the attention of the Beancounter family.

### 3.3 BEANCOUNTER SCENARIO

Bizzie Beancounter has decided to start her own business venture. She has located the perfect premises that is currently available for letting. She will start a dry cleaning business in her own name (recognised as a process of manufacture by the Commissioner) on 1 March 2017 (with a February year-end). She will employ four permanent staff members (non-connected persons) and she herself will take care of the day-to-day management of the business. Bizzie will import two dry-cleaning machines from Europe, which will have arrived by 1 March 2017.

Bizzie has signed contracts with a few local restaurants to render dry-cleaning services to them with effect from March 2017. Her monthly turnover in terms of these agreements will be R85 000 for the first six months, increasing by 10% for every consecutive six-month-period.

However, Bizzie is uncertain about what (if any) VAT implications might arise from her business venture and she has asked you to identify all the VAT areas which may affect her business.

Six months have passed since your first meeting with Bizzie when she phones you to set a date for a second meeting. The dry-cleaning business is operating very successfully and Bizzie feels that it is time for one or two changes:
• The rented premises are no longer spacious enough for Bizzie's business venture and she wants to buy a house in Justice Mahomed Street, Pretoria, from where she will operate the business. She will buy the house from Ancient Eve, a 72-year-old woman who can no longer manage the old residence on her own (she is not a VAT vendor). The house has a separate, one-bedroom flat, which Ancient Eve wants to rent from Bizzie after the sale. The flat occupies 10% of the floor space of the residence.

• Bizzie wants to incorporate a collect-and-deliver dry-cleaning service into the business and she will need to buy a delivery truck for this purpose. Peter, the only man she currently employs, will do all the driving for business purposes. He will also be able to use the vehicle for private purposes during evenings and over weekends. All expenses relating to the delivery truck will be paid by the business.

Before attempting to assist Bizzie with her VAT query, you should work through and master the VAT Act. Work through notes 3.4, 3.4.1 and 3.4.2.

3.4 DISCUSSION OF VAT
It is very important to note that we will not continuously refer you back in this tutorial letter to the relevant sections of the VAT Act. You should ensure, however, that you keep your Act at hand and refer to it whenever a specific section is discussed.

3.4.1 Mind maps, definitions and output tax

In order to provide you with an overview of VAT and to use it as a useful study tool, we include a mind map of the output and input tax provisions in the VAT Act on the following page.
Mind map of output and input tax

Final consumer

NO

Person carrying on an enterprise

YES

Supply goods and services

Exempt supplies (sections 12 and 2)

Standard rated supplies (14%)
(sections 1 and 7)

Taxable supplies

Final consumer

YES

Supply goods and services

Exempt supplies (sections 12 and 2)

Standard rated supplies (14%)
(sections 1 and 7)

Taxable supplies

OUTPUT TAX
(section 7(1)(a))

Standard rated supplies (14%)
(sections 1 and 7)

Zero-rated supplies (0%)
(sections 11)

Deemed supplies
(sections 8 and 18(3))

OUTPUT TAX
(section 7(1)(a))

Standard rated supplies (14%)
(sections 1 and 7)

Zero-rated supplies (0%)
(sections 11)

Deemed supplies
(sections 8 and 18(3))

Adjusted supplies (sections 18(1), 18(2), 18A, 18B and 22(2) – 3A)

Adjusted supplies (sections 18(4), 18(5), 18(9), 16(3)(h), 22(1), 22(1A), 22(4) and 22(6))

Input tax deduction denied
(sections 7(1),(b), 13 & 14)

Notional input tax – second-hand goods (also fixed property)
(sections 1, definition of "input tax", sub-par (b))

Input tax deduction denied
(sections 7(1),(b), 13 & 14)

Notional input tax – second-hand goods (also fixed property)
(sections 1, definition of "input tax", sub-par (b))

Imported goods and services
(sections 7(1)(b), 13 & 14)

AMOUNT DUE TO OR BY SARS

Final consumer

NO

Person carrying on an enterprise

YES

Supply goods and services

Exempt supplies (sections 12 and 2)

Standard rated supplies (14%)
(sections 1 and 7)

Taxable supplies

OUTPUT TAX
(section 7(1)(a))

Standard rated supplies (14%)
(sections 1 and 7)

Zero-rated supplies (0%)
(sections 11)

Deemed supplies
(sections 8 and 18(3))

OUTPUT TAX
(section 7(1)(a))

Standard rated supplies (14%)
(sections 1 and 7)

Zero-rated supplies (0%)
(sections 11)

Deemed supplies
(sections 8 and 18(3))

Adjusted supplies (sections 18(1), 18(2), 18A, 18B and 22(2) – 3A)

Adjusted supplies (sections 18(4), 18(5), 18(9), 16(3)(h), 22(1), 22(1A), 22(4) and 22(6))

Input tax deduction denied
(sections 7(1),(b), 13 & 14)

Notional input tax – second-hand goods (also fixed property)
(sections 1, definition of "input tax", sub-par (b))

Input tax deduction denied
(sections 7(1),(b), 13 & 14)

Notional input tax – second-hand goods (also fixed property)
(sections 1, definition of "input tax", sub-par (b))

Imported goods and services
(sections 7(1)(b), 13 & 14)

AMOUNT DUE TO OR BY SARS
Study chapter 32.1 to 32.3.2 of SILKE. These sections will provide you with some clarity on the basics of VAT and a background on some administrative issues.

After studying the basics of VAT, you should now be ready to study the legislation regarding output tax. The following is a very basic mind map (an extract from the VAT mind map previously provided) of the supply of goods and services and therefore of output tax, which should assist you in studying the following sections on output tax.

Mind map of the supply of goods and services – OUTPUT TAX

Supply of goods and services by a vendor

- No output tax charged
- Exempt supplies (sections 12 and 2)
- Taxable supplies (sections 1 and 7)
- Standard rated supplies (14%) (section 7(1)(a))
- Zero-rated supplies (0%) (section 11)
- Deemed supplies (sections 8 and 18(3))
- Time and value of supplies (sections 9 and 10)
- Adjustments (sections 18(1), 18(2), 18A, 18B and 22(2)–(3A))

Study chapter 32.4, 32.5 and 32.6 to 32.6.2, all relating to output tax. After studying these sections of SILKE, read the following note to give you a better understanding of the definition of “services”.

OUTPUT TAX
(section 7(1)(a))
Additional notes to chapter 32.6.2.2 - Services

“Services”

The definition of services is very wide and the supply of services typically include (without being limited to) the following:

- royalties – granting the right to use intellectual property, that is, patents, trademarks and copyrights
- sale of intellectual property
- assignment, waiver or abandonment of a right to someone else, including the right of legal action
- acceptance of a restraint, including agreeing not to act or to act in a particular way
- acceptance of damages or compensation, including the cancellation of agreements
- provision of professional services, including construction, legal, accounting and other similar services
- provision of facilities by clubs, churches, charities and other non-profit organisations

Please note that this does not mean that all of the above services are taxable supplies; merely that they will constitute services for the purposes of the VAT Act.

The exclusion of “money” from the definitions of “goods” and “services” means that no VAT implications will arise in respect of its supply. This is important because it means that when goods are purchased from a vendor, the initial supply of the item will attract VAT, whereas the subsequent payment will not attract VAT.

Study chapter 32.6.3 (but not 32.6.3.3 – excluded from SAICA syllabus) and 32.7 relating to vendors and output tax matters relating to “in the course or furtherance of an enterprise”.

Summary of registration as a vendor

VAT registration (sections 23(1)(b), 23(3)(b), 24(5)(a) and 24(5)(b))

A person is liable to register if a person’s taxable supplies exceeded the R1 million threshold within the previous 12 months or if a person has a written contractual commitment to make taxable supplies exceeding R1 million within the next 12 months.

Furthermore, section 23(1A) deals with the compulsory registration of enterprises supplying “electronic services” from a place in an export country as soon as the value of its supply of electronic services to customers in South Africa exceeds R50 000.

In terms of section 23(3)(b), a person may register voluntarily if that person is carrying on an enterprise and the value of taxable supplies of all his enterprises is more than R50 000 (in the case of commercial accommodation the value of supplies must be R120 000 or more) for the preceding 12 months, or the total value of taxable supplies of the person has not exceeded R50 000, but can reasonably be expected to exceed R50 000 (R120 000 for commercial accommodation) within 12 months from the registration date. (Note that the person must register on the payments basis – refer to section 15(2B). Section 23(3)(d) provides for voluntary registration where a person continuously and regularly carries on an activity of a nature set out in any regulation made by the Minister in terms of the VAT Act and, in consequence of the nature of that activity, that person is likely to make taxable supplies only after a period of time.
Section 24(5) allows the Commissioner to cancel a vendor’s registration, as contemplated in section 23(1) (vendors that register under the compulsory registration regime) and 23(3) (voluntary registration) (section 24(5) (a)). The Commissioner can now also cancel the registration of a vendor where such vendor has failed to submit a return reflecting the information as required for the purposes of calculating VAT in terms of section 14 or 16 (s 24(5)(b)). Section 24(5) is subject to the proviso that, where a person lodges an objection against the Commissioner’s decision to cancel the registration, the cancellation shall not take effect until the Commissioner’s decision becomes final and conclusive.

A vendor registered in terms of section 23(3)(b)(ii), that is, where the total value of taxable supplies made or to be made has not exceeded R50 000, but it can reasonably be expected to exceed R50 000 within 12 months from the registration date, will be allowed to register on the payments basis. The vendor must account for VAT on the invoice basis from the commencement of the tax period following the tax period in which the total value of taxable supplies has exceeded R50 000 (proviso to section 15(2B)).

You have now studied some important definitions and must now continue your studies of taxable supplies by studying zero-rated supplies, contained in section 11 of the VAT Act.

3.4.2 Zero-rated supplies

We will start by looking at the basic principles of zero-rated supplies. You will then continue your studies by analysing the specific types of zero-rated supplies, the first being exports.

Study chapter 32.10 and 32.10.1, excluding any reference to the definition of “exported” as you do not need to study the definition of “exported”. A question will indicate whether goods are in fact “exported”.

Study Silke chapter 32.10.1.1 which deals with the zero rating of exports.

Silke par 32.10.1.2 to 32.10.1.4 which covers s 11(1)(c) – (d), including any reference to section 11(1)(a)(ii), as it is excluded from SAICA syllabus.

**REMEMBER**

Section 11(1)(a) does not apply to services

Study chapter 32.10.2. After studying these paragraphs, read the following additional notes and do the additional examples on the exporting of goods and services. Also, review the summaries of the CSARS v British Airways PLC and Stellenbosch Farmers’ Winery Ltd v CSARS court cases in TL102/2017 in this regard.

Additional notes to chapter 32.10.2 – Zero-rated supplies: exported services (section 11(2))

Although exported services have been dealt with in SILKE, we would like to focus your attention on the following exported service, which was not covered in SILKE:

- Services in respect of international transport of goods (section 11(2)(c))
  - Any supply of transport services (including ancillary transport services), which relate to goods that are transported from a place in the RSA to another place in the RSA, but which are performed by
the same supplier as part of the supply of the international carriage of passengers, will be zero rated as well.

Some of you may have difficulty in understanding what is meant by “ancillary transport services”. The term “ancillary transport services” is defined in section 1 of the VAT Act and means stevedoring (loading or unloading ships) services, lashing and securing services, cargo inspection services, preparation of customs documentation, container handling services and storage of transported goods or goods to be transported.

If a South African tour operator sells a tour to a foreign tour operator, the services are supplied to a non-resident, but if the actual tourists benefit from the services in South Africa, the supply cannot be zero rated – refer to Interpretation Note 42.

Examples of the exporting of goods and services

Example 1

An incorporated company, with its effective place of management in a country other than the Republic of South Africa, owns land with an office building thereon in the RSA. A local accountant attends to the submission of the VAT returns on behalf of this company.

Must the accountant (who is registered as a vendor) charge VAT at 14% or 0% in respect of his accounting services?

Suggested solution

The supply will be zero rated if section 11 of the VAT Act is applicable.

Section 11(2)(f) does not apply, as the land and improvements are not situated in an export country. Section 11(2)(f) might apply, as services are rendered to a non-resident. The zero-rating will fall away if section 11(2)(f)(i) is applicable. This is, however, not the case, as the services are not directly in connection with the property located in the RSA, but rather due to the foreign company carrying on an enterprise in the RSA. The supply by the accountant will therefore be zero rated. (The supply is not related to the immovable property, but rather to the service to a non-resident in RSA at the time of supply.)

Example 2

A resident from Mozambique, who is not a vendor in the RSA, regularly brings his personal vehicle to Nelspruit to have it serviced there. His family accompanies him and uses the time to do some shopping. Must the garage, which performs the service, charge VAT on the supply of this service at the rate of 0% or 14%?

Suggested solution

The supply will be zero rated if section 11 of the VAT Act is applicable; section 11(2)(f) might apply, as a service is rendered to a non-resident. The zero-rating will fall away if section 11(2)(f)(ii) is applicable. This is the case, as the service is supplied directly in connection with movable property that is situated in the RSA at the time the service is rendered. (Note that sections 11(2)(f)(ii)(aa) & (bb) are not applicable.) Thus, the supply must be at the standard rate of 14%. This is confirmed by the fact that the non-resident
is in the Republic when the service is rendered, and in terms of section 11(2)(i)(iii), the zero-rating then falls away.

### Example 3

Mr A buys wooden artwork (all movable items) from rural artists in the Republic of South Africa. He delivers it on a regular basis (every six months, when the ship docks in Durban) to a foreign-going ship for export to an art dealer in London.

None of the local, rural artists are registered as vendors; neither is Mr A. During the previous 12 months, his turnover amounted to R1 100 000 and he expects this to continue and increase in the future.

He is of the opinion that he does not have to register as a vendor because, according to him, there is no VAT on exports. Is he correct?

### Suggested solution

Mr A carries on an enterprise as envisaged in section 1 of the VAT Act. He continuously or regularly carries on an activity in the course or furtherance of which goods are supplied to any other person for a consideration.

The goods supplied are taxable supplies, as defined in section 1 of the VAT Act. Taxable supplies include a supply of goods at the rate of 0%.

The export of the wooden artwork to an export country constitutes a supply of goods (being movable goods) in terms of a sale agreement and, therefore, it should be charged with tax at the rate of zero per cent (refer to section 11(1)(a)).

As Mr A is a person who carries on an enterprise and the total value of the taxable supplies made by him at the end of a 12-month period has exceeded R1 000 000, he is liable to register as a vendor (refer to section 23).

Mr A must therefore apply to the Commissioner for registration and in fact, should have done so 21 days after becoming liable to do so (section 23(2)). (Take note that zero-rated supplies are still taxable supplies and therefore Mr A will be able to claim all input taxes levied on purchases.)

From 1 April 2015, electronic services physically rendered outside the Republic will not be zero-rated.

You have now completed your studies of the zero-rating of exported services and you will continue by studying the zero-rating of a going concern.

Study chapter 32.10.3 and 32.29. You will find that chapter 32.10.3.2 contains specific examples relating to going concerns. Ensure that you read these examples, as they will give you an understanding of what can be classified as a going concern. After completion of the above paragraphs, read the following additional note.
Additional note to chapter 32.10.3 and 32.29 – Zero-rated supply: the sale of a going concern (ss 11(1)(e) and 18A)

One requirement before the going concern criteria will be met is that both parties should be registered VAT vendors (section 11(1)(e)). Voluntary registration requirements cater for this situation, in that if a person intends carrying on a business from a specific date, which the person will purchase as a going concern and the total value of taxable supplies made by the supplier of the going concern has exceeded R50 000 during the previous 12 months, the person may apply for registration. Both parties can therefore register and the enterprise can be supplied as a going concern (section 23(3)(c)).

It is important to note, if a going concern is supplied to a vendor at the zero rate, but the recipient will use it partly (less than 95%) or wholly for purposes other than the making of taxable supplies, an adjustment to the recipient’s output tax must be made in terms of section 18A (discussed in detail in the textbook in chapter 32.29).

Study chapter 32.10.4. Before doing so, however, you should remember that some of the sections discussed in this paragraph are excluded for purposes of the SAICA syllabus. Consider this when studying these paragraphs in Silke.

Therefore, you must ignore the bullets under chapter 32.10.4, which refer to:
- Section 11(1)(g) that relates to goods and services used for farming purposes
- Section 11(1)(hA) that relates to certain crude oil products (ignore only the second part of this bullet and not the first part, as the first part relates to section 11(1)(h), which is on a level 3, as mentioned)
- Section 11(1)(m) and (mA), as it relates to goods supplied to customs-controlled areas or Industrial Development Zones
- Section 11(1)(n) that relates to controlled animals supplied to public authorities
- Section 11(1)(s) and (t) that relates to certain fixed property supplied that is zero rated
- Section 11(1)(a) relating to consideration subsidised in terms of the Provisions of Land and Assistance Act
- Section 11(2)(g) relating to land or movable goods situated in an export country, as these subsections are excluded from the SAICA syllabus.

You have now completed your studies of zero-rated supplies (section 11 and chapter 32.10). Your studies will start tomorrow with exempt supplies (section 12 and chapter 32.11).

WORK PLAN FOR FRIDAY, 17 FEBRUARY 2017

You will complete your studies of output tax today. First, you will study exempt supplies (SILKE 32.11) and then deemed supplies (SILKE 32.12).

Your three hours study time today has been allocated to the studying of VAT. The following time allocation is recommended:

<table>
<thead>
<tr>
<th></th>
<th>Minutes</th>
</tr>
</thead>
<tbody>
<tr>
<td>Output tax (including exempt and deemed supplies)</td>
<td>180</td>
</tr>
<tr>
<td>Total</td>
<td>180</td>
</tr>
</tbody>
</table>
3.4.3 Exempt supplies

You need to study chapter 32.11 relating to exempt supplies. Note that subsections (d), (e), (f), (k), (l) and (m) of section 12 are excluded from the SAICA syllabus.

You may therefore ignore the bullets under chapter 32.11.4, which refer to:
- section 12(d) that relates to letting of leasehold land
- section 12(e) that relates to the sale or letting of land situated outside South Africa
- section 12(f) that relates to the supply of services by a body corporate, share block company, housing development scheme or home owners associations
- section 12(l) that relates to supplies by a bargaining council to its members
- section 12(m) that relates to supplies by a political party to its members

As these sub-sections are excluded.

Take care when working through chapter 32.11.3, as this discussion not only covers the exempt supply of residential accommodation (under section 12(c)), but also the taxable supply of commercial accommodation. As students seem to find the differentiation between these two supplies difficult, ensure that you understand the difference between them and work through all the examples given.

After you have studied chapter 32.11, read the following additional note that relates to the transport of fare-paying passengers and their personal effects by road or rail.

Additional note to chapter 32.11.4 – Exempt supplies: other: Transport of fare-paying passengers and their personal effects by road or rail (s 12(g)).

Study section 12(g). Note that where transport services were taxed at 0% (in terms of section 11(2)(a)), this will take preference over the exemption (if it is transport by road or rail; transport by aircraft or boat is in any case a taxable supply).

For the exemption to apply, the following criteria must be met:

- Passengers must pay a fare.
- The supplier of the transport service must operate the vehicle himself.

These two requirements will be discussed in more detail.

Fare-paying passengers

Where the operator of the vehicle (in which passengers are transported) charges a consideration for the service, the passengers will be regarded as fare paying. The passengers themselves, or a third party, may pay a specified fare either on boarding the vehicle or on purchasing a ticket prior to travel.

The exemption does not apply where passengers are not charged a fare. If, for example, a mine were to provide transport by road for its miners from their lodgings to the mine, the mine would be entitled to claim the input tax paid in connection with the supply. This is because it will not constitute an exempt supply, as the miners do not pay a fee.

Operation of a transport business

In order to qualify for the exemption, the supplier of the transport service must be the operator of the vehicle in which the passengers are transported. The supplier need not necessarily be the owner of the vehicle or even the employer of the driver, but must be commercially responsible for the transporting of the passengers.
Where the supplier of the vehicle does not operate it himself, but rents or hires it to a third party, who uses it for the transport of passengers, the exemption does not apply. The reason for this is that the supply constitutes the hire of the vehicle and not that of a transport service, and is therefore standard rated. Should the supplier also provide the services of a driver, however, the supply will constitute an exempt supply in most cases, and not a standard-rated supply. Each situation must be judged on its own facts and the use of the words “hire” or “charter” in an agreement is not conclusive as to the nature of the transaction. The decisive factor in determining whether an exempt transport service or a taxable rental transaction is supplied will usually be to whom the driver is ultimately accountable.

If the driver were accountable to the owner of the vehicle, an exempt transport service would be supplied in the absence of factors to the contrary. By contrast, if the driver were accountable to the recipient, the supply would be taxable in most instances. In practice, SARS interprets this provision in a broad manner.

Examples of exempt transport services

- **Scheduled commuter bus services, intercity bus services and tourist bus transport** – The distance covered or duration of the service is irrelevant.
- **Ambulance services** – This is transport of patients in an ambulance for a consideration.
- **Tour buses or trains** – The transport of passengers by a tour operator, irrespective of whether a specific fee is charged for transport or whether it is incorporated into the total fee for the tour. In the latter case, the total fee will have to be apportioned between the taxable supplies and the exempt passenger transport service. If the fee is not apportioned, the full amount of the fee is subject to VAT at the standard rate.
- **Airport/hotel transfers** – This involves the transport of patrons to and from an airport by a hotel or equivalent supplier, provided a specific fee is charged for the service. Where, however, the service is provided as a courtesy to patrons without a specific amount being charged, the hotel will not be regarded as supplying exempt passenger transport.
- **Transport of employees or pupils** – This is the transport of employees or pupils on behalf of an employer or school, irrespective of whether the consideration charged by the operator is a fixed or variable amount based on the number of employees actually transported. This, however, does not include the case where the employer hires the vehicle and undertakes the transport of the employees himself, for no consideration.

Examples of taxable transport services (not exempt)

- Passenger transport by air or sea
- Courier services and the transportation of parcels by road, rail or sea
- Game viewing excursions
- Passenger transport, where no fare is charged, for example, where an employer provides transportation to and from the place of work to employees and no consideration is charged
- Passenger transport, where the transport fee is incorporated into the total charge for a composite supply and the total charge is not apportioned between taxable and exempt supplies
- Transport rental and hiring services, if the services of a driver are not included
- Zero-rated transport services, for example, passenger transport by road or rail to an export country

You have now completed your studies of exempt supplies (section 12). We will continue by studying **deemed supplies** (sections 8 and 18(3)).

### 3.4.4 Deemed supplies

Study chapter 32.12 and 32.12.1 that relate to deemed supplies, namely when a person ceases to be a vendor. After studying chapter 32.12.1 in the prescribed textbook, also read the following additional note.
Additional note to chapter 32.12.1 – Deemed supplies: Ceasing to be a vendor

If the delivery vehicle in the first example (Mr Phillip de Vos) in chapter 32.12.1.2 were used to make 40% taxable supplies, Phillip would only have claimed input tax on purchase of the delivery vehicle of R180 000 x 14/114 x 40% = R8 842. Phillip would still have to account for output tax, however, when ceasing to be a vendor on 100% of the lesser of cost (including VAT) (R180 000) or open-market value (R110 000), although the asset was only used 40% for taxable purposes, due to section 8(16) (see chapter 32.14). Section 8(16) provides that, if a vendor acquires goods only partly for the making of taxable supplies and then subsequently supplies the goods, the vendor will be deemed to make a 100% taxable supply of the goods. In the SILKE example, the output tax payable would thus be (R110 000 – R3 000) x 14/114 = R13 140, but the vendor would be able to make an input tax adjustment for the exempt portion under section 16(3)(h). Therefore, R110 000 (lower of adjusted cost and open-market value) x 14/114 x 60% = R8 105 input tax will be claimable.

If a person (who ceases to be a vendor) disposes of any goods or rights after the cancellation of his/her registration (and thus after the deemed supply has been accounted for), the person will not carry on an enterprise for VAT purposes and no VAT will be due on the supply of the goods or rights.

Where the assets, forming part of a vendor’s enterprise, are, prior to cessation of registration, distributed to shareholders as a dividend in specie, no VAT will be payable, as the supply will be made for no consideration. Should the recipient, however, be a connected person in respect of the vendor and not be entitled to a full input tax credit had VAT been payable, VAT will have to be levied on the open-market value of the dividend in specie (i.e. the value of supply rule for connected persons). The distribution of assets by a person in the form of a dividend in specie subsequent to the cessation of registration has no VAT implication, as the supply has not been made in the course or furtherance of an enterprise, the enterprise having ceased. The supply will therefore not be a taxable supply.

The general rules for deregistration (for VAT purposes) will not apply where a person ceases to be a vendor because of death or insolvency, provided the enterprise is thereafter continued by or on behalf of his/her executor or trustee.

REMEMBER

A deemed disposal for VAT purposes arises when a person ceases to be a VAT vendor (section 8(2)). Output tax is calculated by multiplying the lesser of the cost (including VAT) and the open-market value by the tax fraction. However, section 8(2)(v) provides that this shall not apply to assets where output tax has already been accounted for in terms of section 22(3).

In terms of section 22(3), when ceasing to be a vendor, outstanding creditor balances, on which input tax were claimed, are treated as follows:

- Outstanding for longer than 12 months: No adjustment for VAT on these balances is made when ceasing to be a vendor, since section 22(3) stipulates that a VAT vendor be required to account for output tax if he/she has not paid the full consideration for a supply within 12 months. This liability for output tax is therefore due to the non-payment of the creditor for 12 months and not because of the cessation of the enterprise. However, if the vendor has not yet accounted for the output tax on cessation, the adjustment should be made at that time.

- Outstanding for less than 12 months: At the date of the cessation of the enterprise, output tax is payable on outstanding creditor balances that are not older than 12 months. The value of these supplies is the outstanding balance of the creditor (section 22(3) (proviso (ii)(bb)).

Work through example 32.24 in SILKE, chapter 32, to make sure that you have mastered these principles.
Study SILKE, chapter 32.12.2, relating to indemnity payments, after which you should read the following additional note.

Additional note to chapter 32.12.2 – Deemed supply: indemnity payments

Note the following:

- Where the indemnity payment relates to the total reinstatement of goods stolen or damaged beyond economic repair AND the vendor was denied an input tax credit on its acquisition (for example, a motor car), no deemed supply will arise in the hands of the insured. A payout in respect of the repair of such an asset will thus give rise to a deemed supply (and output tax), since an input tax could be claimed on the repair expenses.

- Where the insurer replaces the damaged goods, the insured is not deemed to have made a supply to the insurer, as the replacement of goods does not constitute an indemnity payment. However, the insurer will have made a taxable supply of the replacement goods to the insured, but for an Rnil consideration. The insurer will be entitled to an input tax deduction on the acquisition of the replacement goods.

Study chapter 32.12.3 to 32.12.5 as well as 32.12.8, all relating to deemed supplies.

When studying fringe benefits, remember that the determined value of vehicles for VAT purposes is the cost excluding VAT, although the determined value for income tax purposes is the Retail Market Value (RMV)

Ignore chapter 32.12.6 and 32.12.7 that covers section 8A, as it is a specialist area (Islamic financing) and is excluded from the SAICA syllabus.

After studying chapter 32.12.8, read the following additional note that contains a practical example of the application of the provisions of section 8(15) (a single supply at both the standard and the zero rate).
Rent-a-Galop CC carries on an enterprise by providing motor vehicles for hire to clients. The agreement between the CC (who is also registered as a vendor) and its clients provides for two separate charges to be levied, the first for the actual rental of the vehicle and the second for insurance. In addition, the client is obliged to return the vehicle with a full tank. As this is often not possible, the CC is prepared to fill the tank up and recover this cost from the client.

An example of a tax invoice issued by Rent-a-Galop CC would be as follows:

<table>
<thead>
<tr>
<th>Unit price</th>
<th>VAT</th>
<th>VAT amount</th>
<th>Total</th>
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<tbody>
<tr>
<td>Rent of vehicle</td>
<td>100</td>
<td>14%</td>
<td>14</td>
</tr>
<tr>
<td>Insurance</td>
<td>50</td>
<td>14%</td>
<td>7</td>
</tr>
<tr>
<td>Fuel</td>
<td>69</td>
<td>0%</td>
<td>0</td>
</tr>
<tr>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
</tbody>
</table>

Study chapter 32.13 and 32.14 that relates to output tax.

Ensure that you understand the application of section 8(14) and 8(16), as well as section 8(15), discussed above. These are very important sections.

You will continue your studies of VAT tomorrow by studying the time and value of supplies and thereafter input tax.

Get a good night’s sleep!
WORK PLAN FOR SATURDAY, 18 FEBRUARY 2017

Today you will be spending six hours (of the allocated 7 hours and 15 minutes) of your study time on studying the time and value of supplies (SILKE, chapter 32.15 and 32.16), input tax, certain special situations (instalment credit agreements and fixed property) and VAT adjustments and administrative issues. You will then spend the last hour and 15 minutes of today’s study time by answering the questions relating to the Beancounter scenario and doing the integrated example under section B. This will assist you in assessing your knowledge of the VAT principles and legislation.

The following time allocation is recommended:

<table>
<thead>
<tr>
<th>Time and value of supplies</th>
<th>60 minutes</th>
</tr>
</thead>
<tbody>
<tr>
<td>Input tax</td>
<td>120 minutes</td>
</tr>
<tr>
<td>Special situations (including instalment credit agreements and fixed property)</td>
<td>35 minutes</td>
</tr>
<tr>
<td>Adjustments</td>
<td>80 minutes</td>
</tr>
<tr>
<td>Administrative issues</td>
<td>20 minutes</td>
</tr>
<tr>
<td>Comprehensive examples</td>
<td>45 minutes</td>
</tr>
<tr>
<td>Outcomes of the Beancounter Scenario</td>
<td>15 minutes</td>
</tr>
<tr>
<td>Section B (integrated example)</td>
<td>60 minutes</td>
</tr>
<tr>
<td><strong>Total</strong></td>
<td><strong>7 hours and 15 minutes</strong></td>
</tr>
</tbody>
</table>

3.4.5 Time and value of supplies

You may start by studying the **time of supply** (SILKE, chapter 32.15) and the **value of supply** (SILKE, chapter 32.16). Both these are very important parts of your studies, as they are the key components required in calculating VAT correctly and paying it timeously. After studying these paragraphs of the chapter, you should work through the following table, which provides you with a comprehensive summary of the different time and value of supply rules.

Limited time is available for studying the table, because the table is a summary of all the sections on time and value that are discussed in detail elsewhere in the chapter. It will be useful as a study tool to complement the discussion in the chapter and the relevant legislation.
Additional notes on SILKE, chapter 32.15 and 32.16 – Time and value of supply

The word “value” used in section 10 is confusing as the amount actually described in section 10 is “consideration”. It is important to understand the difference between value and consideration. Value excludes VAT. Consideration includes VAT. As the amount described in section 10 is actually consideration, the amount given in the table below should be multiplied by 14/114 in order to obtain the VAT amount.

Note that a separate table is provided later in this learning unit for the time and value of supply adjustments (section 18 and 18A).

<table>
<thead>
<tr>
<th>Supply</th>
<th>Time</th>
<th>Amount of the consideration</th>
</tr>
</thead>
<tbody>
<tr>
<td>General rule</td>
<td>Invoice basis</td>
<td>Consideration = Value + VAT, or Value = Consideration – VAT</td>
</tr>
<tr>
<td>The earlier of</td>
<td></td>
<td>Consideration will be</td>
</tr>
<tr>
<td>• the date an invoice is issued, or</td>
<td></td>
<td>• consideration in money = money value</td>
</tr>
<tr>
<td>• the time of payment / consideration received by the supplier</td>
<td></td>
<td>• consideration not in money = open-market value</td>
</tr>
<tr>
<td>(section 9(1))</td>
<td></td>
<td>(section 10(2) &amp; (3))</td>
</tr>
<tr>
<td>Payment basis</td>
<td></td>
<td></td>
</tr>
<tr>
<td>The time of payment / consideration received by the supplier</td>
<td></td>
<td></td>
</tr>
<tr>
<td>(To claim an input tax deduction, the vendor must be in possession of a valid tax invoice – see SILKE, chapter 32.18.)</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Connected persons</td>
<td>Goods removed – time of removal</td>
<td>Open-market value</td>
</tr>
<tr>
<td>Goods not removed – time made available to recipient</td>
<td>if a supply is made by a vendor for no consideration or for consideration less than open-market value or if the whole of the consideration cannot be determined at the time of the supply and the recipient would not have been able to claim the full input tax deduction (fringe benefits excluded)</td>
<td></td>
</tr>
<tr>
<td>Services – time services performed</td>
<td>(section 10(4))</td>
<td></td>
</tr>
<tr>
<td>If</td>
<td></td>
<td></td>
</tr>
<tr>
<td>payment is received or an invoice is issued before the day on which a return is submitted for the tax period in which goods were removed, made available or services performed, the general rule (section 9(1)) will apply</td>
<td></td>
<td></td>
</tr>
<tr>
<td>(section 9(2)(a))</td>
<td></td>
<td></td>
</tr>
<tr>
<td>If</td>
<td></td>
<td></td>
</tr>
<tr>
<td>The recipient vendor would have been entitled to make a deduction of the full input tax in respect of that supply and the consideration cannot be determined at the time the supply is deemed to be made the general rule (section 9(1)) will apply and not section 9(2)(a).</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Supply</td>
<td>Time</td>
<td>Amount of the consideration</td>
</tr>
<tr>
<td>----------------------------------------------------------------------</td>
<td>----------------------------------------------------------------------</td>
<td>---------------------------------------------------------------------------------------------</td>
</tr>
<tr>
<td>Fringe benefits</td>
<td>The time at which the <strong>benefits become liable to employees’ tax</strong> in terms of the Income Tax Act (it is the month in which employees’ tax is payable on the benefit or the month that it is included as part of remuneration) (section 9(7))</td>
<td>The <strong>cash equivalent</strong> (which excludes finance charges and VAT) of the benefit, for normal tax purposes, except were the benefit is the right of use of a motor vehicle. Then: if input tax deduction was denied: <strong>0.3%</strong> of determined value (excluding VAT) of motor vehicle <strong>per month</strong> if input tax deduction was not denied: <strong>0.6%</strong> of determined value (excluding VAT) of motor vehicle <strong>per month</strong> (Refer to chapter 32.12.4.2 of SILKE for additional information.) (section 10(13) and Government Gazette 22 Nov 1991)</td>
</tr>
<tr>
<td>Game viewing vehicle or hearse, where input was claimed on conversion and then supplied or used for another purpose (section 8(14)(b) or 8(14A))</td>
<td>When <strong>supplied or utilised for another purpose</strong> (section 9(10))</td>
<td>Consideration in money equal to the <strong>open-market value</strong> (section 10(24))</td>
</tr>
<tr>
<td>Credit agreements</td>
<td>Day after the last day at which the recipient may exercise his right to terminate the agreement <em>(after cool-off period of 5 days)</em> <em>(section 9(2)(b))</em>*</td>
<td><strong>General rule</strong> <em>(section 10(2) &amp; (3))</em></td>
</tr>
</tbody>
</table>
| Instalment credit agreement *(suspensive sale agreement and a lease)* | Earlier of  
• time of **delivery**, or  
• time of **payment received** *(section 9(3)(c))* | **Cash value**, as defined in section 1 *(including VAT and excluding finance cost)* *(section 10(6))* |
| Rental agreement or services supplied under any agreement which provides for periodic payments | Deemed successive supplies  
Each successive supply deemed to take place at the earliest of when  
• payment becomes due, or  
• payment is received *(section 9(3)(a))* | **General rule** *(section 10(2) & (3))* |
<table>
<thead>
<tr>
<th>Supply</th>
<th>Time</th>
<th>Amount of the consideration</th>
</tr>
</thead>
<tbody>
<tr>
<td>Goods supplied progressively or periodically or directly in the</td>
<td>Deemed successive supplies Each successive supply deemed to take place at the</td>
<td>General rule (section 10(2) &amp; (3))</td>
</tr>
<tr>
<td>construction, repair, improvement, erection or manufacture under any</td>
<td>earliest of whenever</td>
<td></td>
</tr>
<tr>
<td>agreement where consideration is paid in instalments or</td>
<td>• any payment in respect of any supply becomes due and is received, or</td>
<td></td>
</tr>
<tr>
<td>periodically</td>
<td>• any invoice relating only to that payment is issued</td>
<td></td>
</tr>
<tr>
<td></td>
<td>(section (9(3)(b))</td>
<td></td>
</tr>
<tr>
<td>Instalment credit agreements, repossessions and surrender of</td>
<td>Day at which goods are repossessed or surrendered</td>
<td>Cash value of outstanding debts on goods repossessed or surrendered (excluding finance cost)</td>
</tr>
<tr>
<td>goods</td>
<td>(section 9(8))</td>
<td>(section 10(16))</td>
</tr>
<tr>
<td>Goods supplied under an agreement other than an instalment</td>
<td>Deemed successive supplies – Each successive supply deemed to take place at the</td>
<td>General rule (section 10(2) &amp; (3))</td>
</tr>
<tr>
<td>credit agreement or rental agreement and consideration is</td>
<td>earliest of when</td>
<td></td>
</tr>
<tr>
<td>contingent on a future event</td>
<td>• any payment in respect of the supply is due or received and claim to the extent that any</td>
<td></td>
</tr>
<tr>
<td></td>
<td>payment has been made, or</td>
<td></td>
</tr>
<tr>
<td></td>
<td>• an invoice relating to the supply is issued</td>
<td></td>
</tr>
<tr>
<td></td>
<td>(section (9(4)(a))</td>
<td></td>
</tr>
<tr>
<td>Services supplied under an agreement and consideration is</td>
<td>Deemed successive supplies – Each successive supply deemed to take place at the</td>
<td>General rule (section 10(2) &amp; (3))</td>
</tr>
<tr>
<td>contingent on future event</td>
<td>earliest of when</td>
<td></td>
</tr>
<tr>
<td></td>
<td>• any payment in respect of the supply is due or received and claim to the extent that any</td>
<td></td>
</tr>
<tr>
<td></td>
<td>payment has been made, or</td>
<td></td>
</tr>
<tr>
<td></td>
<td>• an invoice relating to the supply is issued</td>
<td></td>
</tr>
<tr>
<td></td>
<td>(section (9(4)(b))</td>
<td></td>
</tr>
<tr>
<td>Supply</td>
<td>Time</td>
<td>Amount of the consideration</td>
</tr>
<tr>
<td>-----------------------------------------------------</td>
<td>----------------------------------------------------------------------</td>
<td>---------------------------------------------------------------------------------------------</td>
</tr>
<tr>
<td>Supplies to foreign branches</td>
<td>Date at which goods are delivered to independent branch, or service is performed (section 9(2)(e))</td>
<td>Lesser of&lt;br&gt;• cost to vendor (including VAT) of acquisition, manufacture, assembly, construction or production, or&lt;br&gt;• open-market value of supply (section 10(5))</td>
</tr>
<tr>
<td>Ceases to be a vendor</td>
<td>Immediately before the person ceased to be a vendor (sections 8(2) and 9(5))</td>
<td>Lesser of&lt;br&gt;• cost to vendor (including VAT) of acquisition, manufacture, assembly, construction or production of goods or services, or&lt;br&gt;• open-market value of supply (section 10(5))</td>
</tr>
<tr>
<td>Indemnity payments</td>
<td>The date of receipt of payment by the vendor or date paid to another person (section 8(8))</td>
<td>Apply the tax fraction to consideration received in money (section 8(8))</td>
</tr>
<tr>
<td>Second-hand goods acquired from a vendor (excluding fixed property)</td>
<td>General rule (section 9(1))</td>
<td>General rule (section 10(2) &amp; (3))</td>
</tr>
<tr>
<td>Notional input tax in respect of second-hand goods (excluding fixed property) situated in the Republic of South Africa and acquired from a non-vendor</td>
<td>Claim to the extent that payment has been made (section 16(3)(a)(ii)(aa) &amp; 16(3)(b)(i))</td>
<td>The lesser of&lt;br&gt;• consideration in money, or&lt;br&gt;• open-market value (irrespective of whether the supply takes place at arm’s length or between connected persons) (section 1 – definition of input tax, sub-paragraph b(i))</td>
</tr>
<tr>
<td>Export of second-hand goods where a notional input tax had been claimed</td>
<td>General rule (section 9(1))</td>
<td>Consideration limited to the purchase price of the goods to the exporter. Note that the purchase price is not reduced by the notional input tax which has been claimed (section 10(12))</td>
</tr>
<tr>
<td>Supply</td>
<td>Time</td>
<td>Amount of the consideration</td>
</tr>
<tr>
<td>--------------------------------</td>
<td>----------------------------------------------------------------------</td>
<td>---------------------------------------------------------------------------------------------</td>
</tr>
<tr>
<td>Imports of goods</td>
<td>From 1 April 2015 vendors registered on the invoice or payment basis can only claim the input tax once the imported goods are released in terms of the Customs and Excise Act (thus, no longer at the date of payment). <em>(sections 16(3)(a)(iv) and 16(3)(b)(iii))</em></td>
<td><strong>Imports of goods from BLNS countries for home consumption</strong> Value for customs duty purposes</td>
</tr>
<tr>
<td></td>
<td>VAT charged and collected by Customs and Excise at designated border post (point of entry into the RSA. <em>(section 13(1))</em></td>
<td><strong>Imports from other countries for local consumption</strong> Value for customs duty purposes Plus: 10% of value for customs duty purposes Plus: Any duty levied in terms of the Customs and Excise Act</td>
</tr>
<tr>
<td></td>
<td>These amounts are the only ones in this table which represent &quot;VALUE&quot; and not &quot;CONSIDERATION&quot; and they should therefore be multiplied by 14% to get the VAT amount <em>(section 13(2))</em></td>
<td></td>
</tr>
<tr>
<td>Imported services</td>
<td>The imported service is deemed to take place at the earlier of</td>
<td>The greater of</td>
</tr>
<tr>
<td><em>(Services supplied by a director are excluded, as they entail remuneration and are not a supply.)</em></td>
<td>• the date at which an invoice is issued, or</td>
<td>• the value of the consideration, or</td>
</tr>
<tr>
<td></td>
<td>• when payment is made</td>
<td>• open-market value</td>
</tr>
<tr>
<td></td>
<td>The recipient must declare the imported service and pay the VAT to the Commissioner within 30 days of the receipt of the imported service. <em>(section 14(2))</em></td>
<td><em>(section 14(3))</em></td>
</tr>
<tr>
<td></td>
<td>Note that VAT is only payable on imported services if the imported service is made to a resident of RSA and only to the extent that such services are utilised or consumed otherwise than for the making of taxable supplies. No VAT is payable on exempt or zero-rated supplies or supplies where the value does not exceed R100 per invoice.</td>
<td></td>
</tr>
<tr>
<td>Fixed property acquired from a vendor</td>
<td>The earlier of the</td>
<td>General rule</td>
</tr>
<tr>
<td></td>
<td>• date of registration in the deeds office, or</td>
<td><em>(section 10(2) &amp; (3))</em></td>
</tr>
<tr>
<td></td>
<td>• date of any payment for supply</td>
<td>*(Input tax should only be accounted for to the extent that payment of the consideration has been made or received. <em>(section 16(3)(a)(iiA))</em></td>
</tr>
<tr>
<td></td>
<td><em>(section 9(3)(d))</em></td>
<td>*(Note: Output tax of the seller will also be limited to the extent of payment received <em>(section 16(4)(a)(ii)).)</em></td>
</tr>
<tr>
<td>Supply</td>
<td>Time</td>
<td>Amount of the consideration</td>
</tr>
<tr>
<td>--------</td>
<td>------</td>
<td>-----------------------------</td>
</tr>
<tr>
<td>Fixed property (second-hand goods) acquired from a non-vendor</td>
<td>The earlier of the • date of registration in the deeds office, or • date of any payment for supply <em>(section 9(3)(d))</em></td>
<td>Claim notional input tax by applying a tax fraction to the lesser of • consideration given in money, or • open-market value (x%) taxable supplies <em>(section 1 – definition of input tax, sub-paragraph (b))</em> However, notional input tax may only be claimed once the fixed property has been registered in the name of the vendor and it is then limited to the extent of payment of the purchase consideration. <em>(section 16(3)(a)(ii)(aa) read with section 16(3)(a)(ii)(bb)(A))</em></td>
</tr>
<tr>
<td>Commercial accommodation (Refer to chapter 32.11.3.2.)</td>
<td>General rule <em>(section 9(1))</em></td>
<td>Domestic goods and services supplied at an all-inclusive charge for an unbroken period exceeding 28 days attract VAT at 14% on 60% of the value of the supply. If the period is not more than 28 days, VAT is payable at 14% on the full value (100%). Domestic goods and services or other goods and services not included in the all-inclusive charge will attract VAT at 14% on the full value (100%) of the supply <em>(section 10(10)).</em></td>
</tr>
<tr>
<td>Supply</td>
<td>Time</td>
<td>Amount of the consideration</td>
</tr>
<tr>
<td>-------------------------------------------</td>
<td>-------------------------------------------</td>
<td>------------------------------------------------------------------------------------------------</td>
</tr>
<tr>
<td>Entertainment</td>
<td>General rule (section 9(1))</td>
<td>Where a vendor makes any supply of entertainment and an input tax deduction was denied in terms of section 17(2), the value of such supply shall be deemed nil. (section 10(21))</td>
</tr>
<tr>
<td>Nil-value supplies</td>
<td>General rule (section 9(1))</td>
<td>Where any supply is made for no consideration, the value of that supply shall be deemed nil. (section 10(22))</td>
</tr>
<tr>
<td>Excess payments received and not refunded within four months of receipt (section 8(27))</td>
<td>Deemed to be the last day of the tax period during which the four-month period ends. (section 8(27))</td>
<td>Output tax payable: Excess portion x 14/114 (section 10(26)) Note: If the excess payment is refunded at a date after the output tax has been accounted for, the vendor will become entitled to claim an additional input tax credit in the tax period refunded. (section 16(3)(m))</td>
</tr>
<tr>
<td>Prizes or winnings on betting transactions</td>
<td>The tax period in which the prize or winnings is paid out</td>
<td>The input tax claimable will be an amount equal to 14/114 x any amount paid as a prize or winnings. Note: If, however, the prize or winnings constitute goods or services, the input tax must be limited to the tax initially incurred when acquiring the goods or services. (section 16(3)(d) and 10(17))</td>
</tr>
</tbody>
</table>

If you are satisfied, after studying most of the sections that relate to the different types of supplies (output tax) and the time and value of supplies, that you have a clear understanding of the VAT principles relating to output tax, you may now continue by exploring the legislation relating to input tax.

### 3.4.6 Input tax

Before you start studying chapter 32.17, we recommend that you first read the following additional notes provided. The purpose of these additional notes is to provide you with additional background on input tax.

After reading the additional notes below, study chapter 32.17 up to 32.20. These sections deal with the basics of input tax, tax invoices, debit and credit notes and the determination of input tax.
Additional notes to chapter 32.17 in SILKE – Basics of input tax (section 17)

**Framework for input tax**

1. **WAS A VENDOR CHARGED WITH VAT ON THE SUPPLY OF GOODS OR SERVICES BY A SUPPLIER?**
   - NO
   - YES

2. **WILL THE GOODS OR SERVICES BE CONSUMED, USED OR SUPPLIED IN THE COURSE OF MAKING TAXABLE SUPPLIES?**
   - NO
   - YES

3. **IS THE DEDUCTION OF THE INPUT TAX DENIED?**
   - NO
   - YES

4. **IS THE PROPOSED CONSUMPTION, USE OR SUPPLY 100% IN THE COURSE OF MAKING TAXABLE SUPPLIES?**
   - NO
   - YES

5. **DETERMINE THE PORTION OF USE IN THE COURSE OF MAKING TAXABLE SUPPLIES.**

6. **IS ITS INTENDED USE TO MAKE TAXABLE SUPPLIES 95% OR MORE?**
   - NO
   - YES

**References to the VAT Act**

- Section 1
- Section 17(1)
- Section 17(2)
- Section 17(1)(i)

**Results:**
- **NO AMOUNT OF INPUT TAX MAY BE CLAIMED.**
- **APPORTION AND CLAIM ONLY THE AMOUNT OF INPUT TAX THAT RELATES TO INTENDED TAXABLE USE.**
- **CLAIM FULL AMOUNT OF INPUT TAX.**
Note that if a vendor intends to make taxable supplies of 95% or more, the vendor will be able to claim the FULL input tax and will NOT have to apportion the input tax. (For example, if vendor A makes taxable supplies of 97%, he will be able to claim 100% of the input tax and will not have to apportion the input tax.)

**General notes on input tax**

Study the definitions of “input tax” and “tax invoice” in section 1, section 16, section 17(1) and section 17(4).

- The input tax that may be deducted from output tax consists of the following:
  - VAT is charged in respect of
    - taxable supplies of goods or services (section 7(1)(a))
    - the importation of goods (section 7(1)(b))
    - the excise duty on certain manufactured goods and the environmental levy in certain circumstances (section 7(3)(a))
  - A notional amount of VAT in respect of an amount paid, not being a taxable supply (i.e. from a non-vendor) of second-hand goods
  - A notional amount equal to the tax fraction of the outstanding cash consideration in respect of goods repossessed or surrendered under an instalment credit agreement.

**The input tax deduction is also available when capital goods are acquired.**

- A person making only exempt supplies will not be able to register as a vendor, as no enterprise is carried on (refer to the definition of enterprise in section 1 of the VAT Act).
- A vendor is a person registered (or who is required to be registered) in terms of section 23. A non-vendor will not be entitled to any input tax deduction.
- Section 17(4) prevents the double deduction of input tax.

Remember that no input tax deduction will be available to a registered vendor on any supply if the vendor is not in possession of a valid tax invoice. (Tax invoices are optional for amounts of R50 and less [including VAT].) An abridged tax invoice may be issued where the consideration for the supply does not exceed R5 000. In terms of section 21(1)(e), a debit or credit note should be issued if the tax charged on a tax invoice is incorrect because of an error that occurred in stipulating the amount of consideration agreed upon for the supply or if the output tax stated on a VAT return is incorrect because of such error.

If a refund of input tax is not claimed in the applicable tax period, the input tax claim is not forfeited. The VAT Act allows a five-year period to claim a refund, starting from the tax period in which the transaction date falls (section 44(1)(i)).

You should now have a background of input tax. Your studies will continue with some more specialised issues regarding input tax, namely the denial of input tax, the deemed input on second-hand goods and then imports.

Study chapter 32.21 to 32.21.3 and then read the following additional notes relating to specific items on which input tax is denied.
Additional notes to chapter 32.21 of SILKE – Input tax: Denial of input tax (section 17(2))

**Goods or services acquired by a vendor for purposes of entertainment**

The following is a list of goods or services, which will be classified as being acquired for the purposes of entertainment (and therefore, an input tax deduction will be denied):

- staff refreshments such as tea, coffee, other beverages and snacks and the utensils related thereto (e.g. cups, teapots, water coolers, etc)
- food and other ingredients purchased in order to provide meals to staff, clients and business associates
- catering services acquired for staff canteens and dining rooms
- equipment and utensils used in the kitchen
- furniture and other equipment and utensils used in the canteen, staff room and dining rooms
- Christmas lunches and parties, including the hire of venues
- golf days for customers and clients
- entertainment of customers and clients in restaurants, theatres and night clubs

**REMEMBER**

An input tax deduction is allowed for all entertainment (as opposed to only meals or refreshments) supplied by a vendor on board of a ship or an aircraft (input tax will no longer be denied) if it is ancillary to the travel, supplied at no additional charge and the supply of the transport service is a taxable supply (refer to section 17(2)(a)(iii)).

**Motor cars (section 17(2)(c))**

A vendor is denied an input tax deduction on the supply of a motor car, as defined, in section 1 of the VAT Act, to the vendor. As repairs to a motor car or the insurance of a motor car is not the supply of a motor car to the vendor, an input tax deduction will not be denied in respect of the supply of the repairs to or the insurance of a motor car to a vendor making taxable supplies. When a motor car is rented it will constitute the supply of a motor car to the vendor and therefore the vendor will be denied an input tax deduction in respect of the rental of the motor car. Therefore, if a vehicle is rented at an airport for a short period for business travel purposes, it is still regarded as the supply of a motor car and input tax will be denied, even though the motor car is used for enterprise purposes.

**Medical or dental schemes (section 17(2)(d))**

This is an additional category, not mentioned in the prescribed textbook, where an input tax deduction will be denied.

Medical-aid societies may not charge VAT on any medical or dental goods or services supplied by them and they will not be entitled to claim any input tax in respect of any medical or dental goods or services acquired by them.
**REMEMBER**

Usually, if an input tax deduction in respect of the acquisition by the vendor of goods was denied in terms of section 17(2), the vendor will not have to account for output tax on a subsequent supply of these goods. The one exception to this rule is the supply of the right of use of an asset, as contemplated in paragraph (2)(b) of the Seventh Schedule of the Income Tax Act, which will constitute a supply for VAT purposes (for example, the right of use of a motor car).

Study SILKE, chapter 32.22 to 32.22.1 (Deemed input on second-hand goods).

Study the importation of goods and services. Start by studying chapter 32.8 to 32.8.2 and 32.9 to 32.9.3. Take note that, although these sections are treated under output tax in SILKE, it is a tax charged on the products, which is payable by the vendor. We therefore rather see it as part of input tax (being paid and claimed back by the vendor) than as part of output tax. We have therefore only included it in your studies at this point. Also, study the following additional note regarding the import of goods (chapter 32.8), after you have studied the applicable paragraphs in SILKE.

**Additional note to chapter 32.8 (Input tax: Importation of goods)**
(sections 7(1)(b) and 13))

The following is an example of the VAT payable on the importation of goods:

<table>
<thead>
<tr>
<th>OPTION A Entered other than from BLNS countries and entered for home (domestic) consumption</th>
<th>OPTION B Entered from BLNS countries</th>
</tr>
</thead>
<tbody>
<tr>
<td>Customs value</td>
<td>100</td>
</tr>
<tr>
<td>Customs/duties</td>
<td>10</td>
</tr>
<tr>
<td>Add-on (10% of customs value)</td>
<td>10</td>
</tr>
<tr>
<td>VAT</td>
<td>14% x R120 = R16,80</td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>OPTION B Entered from BLNS countries</th>
</tr>
</thead>
<tbody>
<tr>
<td>Customs value</td>
</tr>
<tr>
<td>Customs/duties</td>
</tr>
<tr>
<td>Add-on (10% of customs value)</td>
</tr>
<tr>
<td>VAT</td>
</tr>
</tbody>
</table>
A third option for the valuation of goods imported (OPTION C) has been added to the legislation. Note that section 13(2A) is excluded from your syllabus. We have only included this option (section 13(2A)) for the sake of completeness. This relates to goods which have been imported and entered for storage in a licensed customs and excise storage warehouse, but which have not been entered for home consumption.

The value of these goods for VAT purposes will be the greater of

- the value for customs duty purposes plus any duty levied in terms of the Customs and Excise Act plus 10% of the customs duty value (the same value as for OPTION A above), or

- the consideration paid in money (or if not in money, the open-market value [section 10(3)]) (section 13(2A)).

The VAT payable will be 14% of the value so determined. This ensures that, if a vendor acquires imported goods while they are held in a storage warehouse, the VAT will be payable on the greater of the imported value or the intra-warehouse sales value (which is usually a better reflection of the true arm’s length value). OPTION C was necessary because the VAT on importation is only levied and payable once the imported goods are entered for home consumption.

You have now covered most of the sections that relate to input tax. If you are satisfied that you have a clear understanding of the VAT principles relating to input tax, you may continue your studies by exploring the legislation relating to instalment credit agreements and fixed property.

3.4.7 Special situations – agents, instalment credit agreements and fixed property

Study SILKE, chapter 32.23 to 32.23.3 and 32.24 to 32.24.3. After completing your studies of chapter 32.24, read the following additional notes relating to fixed property.

Additional notes to chapter 32.24 in SILKE – special rules: fixed property

Chapter 32.24 summarises the situation where fixed property is bought as a taxable supply (VAT is charged). Chapter 32.24, however, also refers to a situation where fixed property is bought from a non-vendor (therefore, not a taxable supply – transfer duty is payable), but the purchaser is a registered vendor. The following illustration summarises the consequences if transfer duty is payable:
Fixed property transactions where transfer duty is payable

Is the supply in respect of fixed property?

YES

Should the supplier charge VAT?

(Is the supplier a VAT vendor?)

YES

NO

Refer to chapter 32.24.2 and 32.24.3.1

Transfer duty is payable by the purchaser based on the purchase price

Is the purchaser a registered vendor?

YES

NO

Will the purchaser be using the fixed property, either wholly or partially for the purposes of making taxable supplies?

YES

May not claim any input tax

NO

• The notional input tax, which the vendor may claim, is not limited to the transfer duty payable on the property. It will be calculated as 14/114 x the lesser of cost or open-market value of the fixed property (definition of “input tax” in section 1).

• The time of supply will be the earlier of any payment or date of registration of the property. Note however, that the notional input tax will only be claimable to the extent that payment has been made of the purchase consideration and then only if the fixed property has already been registered in the name of the vendor when the deduction of the notional input tax is made (section 16(3)(a)(ii)(aa), read together with section 16(3)(a)(ii)(bb)(A)).
REMEMBER

The purpose for which the fixed property is acquired determines whether input tax or notional input tax can be claimed on the acquisition of the property. If the property is acquired for the supply of residential accommodation under an agreement for the letting and hiring thereof (including residential accommodation for the employees, directors or shareholders of the company free of charge or at a rent charged to other tenants) no input tax can be claimed on the acquisition of the property as it was acquired to make exempt supplies (non-taxable supplies). If the property is acquired for the sale thereof or used for taxable enterprise activities, input tax will be deductible as the property was acquired for the making of taxable supplies.

If the property was acquired to make exempt supplies and it is thereafter supplied (sold) no output tax will be levied on supply as the supply is that of property that was used to make exempt supplies and exempt supplies are excluded from the definition of an enterprise. If the property was acquired to be sold it will be a taxable supply and output tax will be levied on the supply.

Study SILKE, chapter 32.31 which deals with agents. (Sections 54(1) and 54(3)). Also study sections 54(2A)(b) and 54(6) that applies if the principal is not a resident and not a vendor.

We will now explore the different types of VAT adjustments.

3.4.8 VAT adjustments and administrative issues

Study SILKE, chapter 32.25 to 32.29.3, which relate to all the different types of adjustments. After completing your studies of SILKE, read the following additional notes relating to the adjustments.

Additional notes to chapter 32.25 to 32.29 in SILKE – Adjustments arising from the changed use of goods or services

Since the change in use of goods or services appears to be problematic for some of you, we have summarised the relevant sections of the VAT Act in the following table. The table will also provide you with a reference to a relevant example of the application of that specific section.
<table>
<thead>
<tr>
<th>Section</th>
<th>Time</th>
<th>Calculation</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Section 18(1)</strong> (also refer to section 18B below for temporary change in use of fixed property) (100% or less taxable ➔ 0% taxable) Goods and services acquired wholly or partially for taxable supplies subsequently applied wholly for private, exempt or non-taxable supplies or for purposes where an input tax would be denied <em>(Example in chapter 32.25)</em></td>
<td>The time the goods are so applied <em>(section 9(6))</em></td>
<td>14/114 x open-market value <em>(section 10(7) or 10(8))</em></td>
</tr>
<tr>
<td><strong>Section 18(2)</strong> <em>(Capital goods ➔ taxable supplies, for example, 60%➔ 40%)</em> Reduction in the use of capital goods or services in the making of taxable supplies <em>(Examples in chapter 32.27)</em></td>
<td>The adjustment must be made on the last day of the year of assessment or on the last day of February, if not a taxpayer for income tax purposes <em>(section 18(6))</em></td>
<td>14/114 x the lesser of • adjusted cost (including VAT), or • open-market value on the last day of the year of assessment <em>(section 10(9))</em> x reduction in % taxable use <em>(No adjustment is required if the cost of the asset [excluding VAT] is less than R40 000, or if the decrease in apportionment ratio is 10% or less.)</em></td>
</tr>
<tr>
<td><strong>Section 18(3)</strong> <em>(Fringe benefits)</em> Vendor supplies an employee or office holder with a fringe benefit as contemplated in paragraph (i) of the gross income definition, read together with the Seventh Schedule of the Income Tax Act. (This section does not apply if the supply is an exempt or zero-rated supply or if it is the supply of entertainment) <em>(Examples in chapter 32.12.4)</em></td>
<td>The time at which the benefits are included as part of the employee's remuneration <em>(section 9(7))</em></td>
<td>14/114 x the cash equivalent of the benefit for normal tax purposes, except were the benefit is the right of use of a motor vehicle <em>(section 10(13))</em></td>
</tr>
</tbody>
</table>
## Adjustment to output tax – due to change in use (continued)

<table>
<thead>
<tr>
<th>Section</th>
<th>Time</th>
<th>Calculation</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Section 18A</strong></td>
<td>The <strong>tax period</strong> in which the <strong>enterprise was supplied</strong> to the purchaser (section 18A(3))</td>
<td>The part of the <strong>total cost</strong> to the vendor of acquiring the enterprise that is <strong>attributable to the intended non-taxable use</strong> (excluding any portion of the cost for which an input tax would have been denied in terms of section 17(2)) x 14% (section 18A(2))</td>
</tr>
<tr>
<td>The purchaser acquires an enterprise as a going concern (zero rated) wholly or partly for non-taxable supplies. (No adjustment if taxable supplies 95% or more) (Example in chapter 32.29)</td>
<td></td>
<td></td>
</tr>
</tbody>
</table>
| **Section 18B** | The **earlier of**  
  - 36 months after the conclusion of the rental agreement, or  
  - the date at which the vendor applies the fixed property permanently for a non-taxable purpose (section 18B(3)) | 14/114 x open-market value at the date at which this adjustment should be accounted for (section 10(7)) |
| Developer temporarily applies residential fixed property held for resale, for the supply of accommodation under an agreement for the letting or hiring thereof. (Example in chapter 32.25) |                                                                                   |
### Adjustments to input tax – due to change in use

<table>
<thead>
<tr>
<th>Section</th>
<th>Time</th>
<th>Calculation</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Section 18(4)</strong>&lt;br&gt;(100% non-taxable ➔ 100% or less taxable supplies)&lt;br&gt;Goods or services acquired for non-taxable purposes are subsequently wholly or partly applied for making taxable supplies (including second-hand goods where no notional input tax was claimed initially). (Example in chapter 32.26)&lt;br&gt;(Note that section 18(4) will also apply when a non-vendor becomes a vendor.)</td>
<td>The tax period in which the change takes place</td>
<td>14/114 x lesser of &lt;ul&gt;&lt;li&gt;adjusted cost (including VAT), or&lt;/li&gt;&lt;li&gt;open-market value at conversion date (section 18(4) &amp; 10(4))&lt;/li&gt;&lt;/ul&gt;x % taxable use x (in the case of second-hand goods) the ratio that the amount paid bears to the total consideration in money, expressed as a percentage (95% or more taxable use deemed to be 100% taxable use)</td>
</tr>
<tr>
<td><strong>Section 18(5)</strong>&lt;br&gt;(Capital goods ➔ taxable supplies, for example, 40% ➔ 60%)&lt;br&gt;Increase in the taxable use of capital goods or services (Examples included in chapter 32.27)</td>
<td>The adjustment must be made on the last day of the year of assessment or on the last day of February, if not a taxpayer for income tax purposes (section 18(6))</td>
<td>14/114 x the lesser of &lt;ul&gt;&lt;li&gt;adjusted cost (including VAT), or&lt;/li&gt;&lt;li&gt;open-market value on the last day of the year of assessment (section 18(5) &amp; 10(4))&lt;/li&gt;&lt;/ul&gt;x increase in % taxable use (No adjustment is required if the cost of the asset [excluding VAT] is less than R40 000, or the increase in apportionment ratio is 10% or less.)</td>
</tr>
<tr>
<td><strong>Section 18(9)</strong>&lt;br&gt;(Input tax denied on purchase or import of a motor car ➔ converted to a game-viewing vehicle or a hearse)&lt;br&gt;Motor car where input tax was denied in terms of section 17(2)(c) on acquisition or importation and subsequently converted to a game-viewing vehicle or hearse (Example in chapter 32.28)</td>
<td>The tax period in which conversion takes place (section 18(9))</td>
<td>14/114 x the lesser of &lt;ul&gt;&lt;li&gt;open-market value, or&lt;/li&gt;&lt;li&gt;adjusted cost inclusive of VAT of the motor car on the day before that conversion took place (section 18(9))&lt;/li&gt;&lt;/ul&gt;</td>
</tr>
<tr>
<td><strong>Section 16(3)(h)</strong>&lt;br&gt;(Less than 100% taxable supplies ➔ supplied or 100% non-taxable supplies)&lt;br&gt;Goods or services acquired partly for making taxable supplies, subsequently supplied by a vendor or applied wholly for non-taxable purposes (Example in chapter 32.25)</td>
<td>The date at which the goods are deemed to be supplied (section 9(6))</td>
<td>14/114 x the lesser of &lt;ul&gt;&lt;li&gt;open-market value, or&lt;/li&gt;&lt;li&gt;adjusted cost inclusive of VAT (section 16(3)(h))&lt;/li&gt;&lt;/ul&gt;x percentage use for non-taxable purposes for period before the adjustment</td>
</tr>
</tbody>
</table>
Study SILKE, chapter 32.30. This discussion relates to irrecoverable debts as far as debtors and creditors are concerned. After you have studied the paragraph in SILKE, read the additional note on irrecoverable debt.

Additional note to chapter 32.30 in SILKE – Adjustments: Irrecoverable debts (s 22)

Ensure that you are familiar with the following principles in respect of section 22, which will affect only group companies and specifically only groups where there is a 100% shareholding:

- If there is any outstanding debt between group companies that is irrecoverable, the debtor company will not be entitled to an input tax deduction on the irrecoverable debt. The input tax deduction will only be allowed at such time when the companies are no longer part of the same group of companies (section 22(1) and (6)).

- The general rule in section 22(3) that applies if a debt is outstanding for a period of 12 months, namely that the vendor has to account for output tax on the debt, will not be applicable to taxable supplies between group companies (section 22(3) and (3A)). The obligation to account for output tax will only apply to a vendor that was part of a group of companies, when the vendor and the creditor are no longer part of the same group of companies.

Complete your studies of VAT by studying chapters 32.35 (The influence of VAT on income tax calculations), 32.33 (Tax avoidance – s 73 and s 102 of the Tax Administration Act) and 32.34 (Chapter 18 of the Tax Administration Act). Chapter 32.32 (Rulings) is excluded from the SAICA syllabus.

You have now completed your VAT studies. In order to establish whether you understand the VAT concepts that you have studied and to reinforce the concepts that you have studied over the past few days, we will now do two comprehensive examples.

Do the two comprehensive examples in SILKE, chapter 32.36. The first example is a general VAT question, including the apportionment of input tax, while the second example requires you to provide journal entries for a series of transactions. This second example is very important, as you sometimes struggle to reconcile the VAT theory with the practical application of a journal entry for a VAT transaction – although this is what will be required in practice.

The completion of the two questions in SILKE, chapter 32.36, should assist you in solving the Beancounter scenario (refer to 3.5 below).
3.5 OUTCOMES OF THE BEANCounter SCENARIO

After you have studied this learning unit, you should be able to answer Bizzie Beancounter's queries.

You should now write down all the VAT implications relating to the Beancounter scenario. You need not provide detailed references to specific sections, but rather just a list of all the different provisions, which will have an effect on Bizzie Beancounter in starting her new dry-cleaning business.

First meeting

In formulating your advice, you should have to consider the following:

As Bizzie is starting a new business, she will not be registered for VAT. Therefore, the starting point will be to consider the possibility of VAT registration:

- As her monthly turnover is currently R85 000 (for the first 6 months) and will be R93 500 for the second six months of the year (in terms of her written contractual commitments), the total value of taxable supplies will exceed R1 000 000 in the next twelve months. Therefore, Bizzie will have to register as a VAT vendor in her own name (section 23).

- She needs to consider whether she wants to register on the invoice or the payments basis, which decision will be determined by her debtors and creditors policies (section 15). The payments basis will be beneficial if credit is granted to clients, as Bizzie will only have to pay output tax once payment from debtors is received. If Bizzie buys goods and services on credit, however, input tax may only be claimed once payment is made.

- She needs to register for a two-month tax period, period A or B.

- Bizzie needs to ensure that her accounting system can record the VAT implications of all transactions (section 55) and that proper documentation (sections 20 and 21), which adheres to the provisions of the VAT Act, is produced. She should also ensure that the accounting system could accommodate the payment of VAT on time to avoid penalties and interest (sections 28 and 39 (excluded from syllabus)).

- Bizzie should make a list of the type of supplies that she will make in order to classify them as taxable or non-taxable supplies (including exempt supplies) (sections 1, 2, 7 and 12).

- Bizzie should ensure that she complies with all the requirements in section 13 of the VAT Act on the importation of the two machines.

Second meeting

Buying of the residence

The residence will be bought from an individual who is not a VAT vendor and therefore transfer duty will be payable by Bizzie on the purchase. Bizzie may claim notional input tax, as she will be using the residence for business purposes (90%-10% rented out as residential accommodation, which is an exempt supply (section 12(c)). The notional input tax will be based on 14/114 x the lesser of the adjusted cost (excluding transfer duty) or open-market value. If the fixed property will be used partially for taxable supplies, as in this case, only 90% of the notional input tax may be claimed. If the percentage taxable
use increases or decreases in any subsequent period, Bizzie should account for or claim additional output or input tax (usually based on the lower of cost or open-market value at the time the change in use takes place (section 18)). The time of supply will be the earlier of any payment or date of registration of the property. Note, however, that the notional input tax will only be claimable to the extent that payment has been made of the purchase consideration and then only if the fixed property has already been registered in the name of Bizzie when the deduction of the notional input tax is made (section 16(3)(a)(ii)(aa), read together with section 16(3)(a)(ii)(bb)(A)).

No VAT will be charged on the rental payments received from Ancient Eve for the flat, as the letting of residential accommodation is an exempt supply in terms of section 12(c).

**Delivery truck**

Input tax may be claimed on the purchase price of the delivery truck, as it is not a “motor car” as defined in section 1. Since Peter will be able to use the vehicle for private purposes as well, a fringe benefit in terms of paragraph (i) of the gross income definition, read together with the Seventh Schedule of the Income Tax Act, is triggered for income tax purposes. In terms of section 18(3) of the VAT Act, Bizzie needs to pay deemed output tax on this fringe benefit. The output tax is calculated as 14/114 x the determined value (excluding VAT and any finance charges) x 0.6% (as an input tax could be claimed on the purchase of the vehicle) per month (Government Gazette 2835 of 22 November 1991). The time of supply will be when the benefit is included as part of Peter’s remuneration for income tax purposes (section 9(7)).

In order to test your ability to apply your knowledge and comprehension of VAT to practical problems, attempt the integrated question in section B. This question deals with VAT-related issues.
WORK PLAN FOR SUNDAY, MONDAY AND TUESDAY 19 - 21 FEBRUARY 2017

You will spend your study time during the next three days completing the self-assessment questions in section C. In completing these questions, you will be able to establish whether you have a clear understanding of the VAT principles and legislation. This formative assessment will be in the format of self-assessment exercises. You will therefore have to establish for yourself whether you have mastered the principles in a specific question, before continuing to the next one. Please revise the donations tax and VAT theory when you have identified areas for improvement, that is, if you have determined where your knowledge is lacking.

The following time allocation is recommended for answering section C: self-assessment Assignment 01 (Questions 2 - 23 – take note that you have already completed question 1):

<table>
<thead>
<tr>
<th>Date</th>
<th>Time Allocation</th>
</tr>
</thead>
<tbody>
<tr>
<td>19 February 2017</td>
<td>7 hours 45 minutes</td>
</tr>
<tr>
<td>20 February 2017</td>
<td>3 hours</td>
</tr>
<tr>
<td>21 February 2017</td>
<td>3 hours</td>
</tr>
<tr>
<td><strong>Total</strong></td>
<td><strong>13 hours 45 minutes</strong></td>
</tr>
</tbody>
</table>

After completing the above questions, please use the outcomes provided at the beginning of this learning unit to identify areas for improvement. If you have met all the outcomes stated, you have finished your studies of VAT.

You have now completed your studies of donations tax and value-added tax. Use any remainder of your study time to ensure that you have made adequate notes and summaries and that you have mastered all these topics, since there will not be time later in the year to study these topics in detail again.
SECTION B – INTEGRATED EXAMPLE

PURPOSE STATEMENT:
SECTION B contains an integrated example and is based on prior year’s examinations and test papers. The goals with this section are firstly to assist you to integrate knowledge and to vest a way of thinking in order for you to answer the questions in assignments, tests and exams and secondly to give you the opportunity to apply the assessment criteria stated in TL101 in order to prepare for the formative assessments (tests) and the final summative assessment (examination).

One hour has been allocated to work through this integrated example. We have included an integrated example on VAT only; donations tax has been sufficiently illustrated by way of the example contained in SU 2. This example will give you an indication at which level you need to apply your knowledge in tests and exams.

After completing the question in the time limit you should be able to:

- Demonstrate your competency to pass the formative assessments and summative assessment relating to VAT.
- Demonstrate your understanding of the frameworks and be able to illustrate the interaction between the different sections of the VAT Act.
- Identify your shortcomings in order to rectify it before the tests and examination for example:
  - Time management problems;
  - Shortcomings in your knowledge base;
  - Shortcomings in handling of data, for example: identifying the problem, distinguishing between relevant and irrelevant information, analysing data, integrating data, evaluating alternatives and the ability to propose practical solutions;
  - Problems with communicating your findings etc.
This integrated example illustrates the application of Value-Added Tax covered in this tutorial letter. We have, where applicable, added explanatory notes in the suggested solution. Before you attempt this question, read through our notes on exam technique (provided just before the suggested solution in these notes). You will gain the biggest benefit by attempting the question yourself (as opposed to the “oh-yes method”) before working through the suggested solution.

QUESTION
43 marks

Chong and Sing Woo inherited in equal shares a three-storey building, in desperate need of renovation, from the estate of their late father. Both their late father and his estate were not registered as vendors for value-added tax (VAT) purposes. The estate was finally wound-up during June 2016.

On 1 July 2016, the brothers incorporated a private company and voluntarily applied to have the company registered as a vendor. Each brother has a 50% interest in the company. The financial year of the company ends on 28/29 February.

On 1 July 2016, they sold the building to the newly formed company for R3,6 m (the open market value being R3,0 m). The company duly paid R288 000 transfer duty on 20 July 2016, but the purchase price remained due to the shareholders as a loan. The building was registered in the name of the company on 31 August 2016.

Together with the application for registration as a vendor, a business plan was submitted to the Commissioner, indicating the following (these operations commenced on 1 October 2016):

<table>
<thead>
<tr>
<th>Floor</th>
<th>Description</th>
<th>Amount</th>
</tr>
</thead>
<tbody>
<tr>
<td>Ground</td>
<td>rental income to be received in terms of rental contracts entered into for the letting of shops</td>
<td>R600 000</td>
</tr>
<tr>
<td>1st</td>
<td>estimated income from supplying overnight accommodation to street-walkers</td>
<td>R300 000</td>
</tr>
<tr>
<td></td>
<td>(These tenants will normally not stay for more than three nights. The rooms will be furnished and cleaned on a daily basis)</td>
<td></td>
</tr>
<tr>
<td>2nd</td>
<td>unfurnished apartments to be rented out for residential purposes in terms of a contract for a period of a minimum of twelve months</td>
<td>R300 000</td>
</tr>
<tr>
<td>TOTAL</td>
<td>EXPECTED RECEIPTS PER ANNUM</td>
<td>R1 200 000</td>
</tr>
</tbody>
</table>

(All of the above amounts exclude VAT)

PART A
24 marks

The company was registered as a VAT vendor with two-monthly tax periods, effective from 1 July 2016 and the first VAT period ended on 31 August 2016.

On 10 July 2016, the Woo brothers approached you for a consultation on various issues concerning their proposed enterprise.

Issue 1

What are the VAT consequences for the company following the purchase and renovation of the building by the company? The building must be renovated before they can commence trading.
### Issue 1

(a) Briefly explain, with reasons, whether the company will be entitled to claim an input tax deduction in respect of the cost of acquisition of the building and, if so, what is the amount that can be claimed and when will the company be entitled to claim such input tax. You can assume that the company will use the turnover method to apportion their input tax, if applicable.

(b) Briefly explain whether the company will be entitled to claim input tax in respect of the cost of renovating the building.

(c) Briefly explain to the Woo brothers whether or not they need to register as VAT vendors in their personal capacity on 1 July 2016, as they sold fixed property to a company for a purchase price exceeding the VAT registration threshold of R1 000 000.

<table>
<thead>
<tr>
<th>REQUIRED</th>
<th>Marks</th>
</tr>
</thead>
<tbody>
<tr>
<td>(a) Briefly explain, with reasons, whether the company will be entitled to claim an input tax deduction in respect of the cost of acquisition of the building and, if so, what is the amount that can be claimed and when will the company be entitled to claim such input tax. You can assume that the company will use the turnover method to apportion their input tax, if applicable.</td>
<td>10</td>
</tr>
<tr>
<td>(b) Briefly explain whether the company will be entitled to claim input tax in respect of the cost of renovating the building.</td>
<td>2</td>
</tr>
<tr>
<td>(c) Briefly explain to the Woo brothers whether or not they need to register as VAT vendors in their personal capacity on 1 July 2016, as they sold fixed property to a company for a purchase price exceeding the VAT registration threshold of R1 000 000.</td>
<td>3</td>
</tr>
</tbody>
</table>

### Issue 2

With effect from 1 October 2016, the company will employ cleaning staff for the first floor. These cleaning staff will be entitled to a monthly salary of R1 200 each plus a free lunch. To supply the free lunches the company will purchase a caravan that will be equipped as a canteen. One employee will prepare the lunches inside the caravan.

In respect of the above-mentioned, briefly indicate, with reasons, the input tax that the company may claim, the input tax adjustments (if any) that must be made, and the output (or deemed output) tax that must be accounted for.

<table>
<thead>
<tr>
<th>REQUIRED</th>
<th>Marks</th>
</tr>
</thead>
<tbody>
<tr>
<td>In respect of the above-mentioned, briefly indicate, with reasons, the input tax that the company may claim, the input tax adjustments (if any) that must be made, and the output (or deemed output) tax that must be accounted for.</td>
<td>5</td>
</tr>
</tbody>
</table>

### Issue 3

To equip the first floor for overnight residents, the company will purchase second-hand furniture from:

(a) Non-vendors by advertising in the local newspaper. All furniture must be delivered by 30 September 2016 and will be paid at the end of November 2016.

(b) Large furniture retailers (vendors for VAT purposes). This furniture will comprise of repossessed furniture and will be paid 90 days after the company takes delivery.

Indicate what the VAT implications will be for the company regarding the purchase of the furniture. Also, indicate when the company will be entitled to claim the input tax.

<table>
<thead>
<tr>
<th>REQUIRED</th>
<th>Marks</th>
</tr>
</thead>
<tbody>
<tr>
<td>Indicate what the VAT implications will be for the company regarding the purchase of the furniture. Also, indicate when the company will be entitled to claim the input tax.</td>
<td>4</td>
</tr>
</tbody>
</table>
On 15 January 2017, you were asked to conduct an interim VAT audit for your client (the company). The following facts came to light:

Cash stolen
All output tax was accounted for correctly, except when on 2 January 2017 the cashier disappeared with the cash collected from the overnight residents (R6 840). These collections were not recorded on the computer. A cheque for R3 000 was received from the insurance company on 10 January 2017. This was the maximum insured limit. The R3 000 was also not recorded on the computer.

Outsource and purchase of computer
The company purchased a computer on 1 October 2016 for R57 000 (including VAT) and correctly claimed the input tax.

The company decided that with effect from 1 January 2017, they would outsource the rental operations of the second floor (i.e. an outside agency will let the apartments and collect all the rentals). This computer had previously been used for all rent collections, but will now only be used for the ground and first floors. (The open market value of the computer on 1 January 2017 and 28 February 2017 was R45 000 and R42 000 respectively).

Sale and export
As a result of the advertisement for the purchase of second-hand furniture from non-vendors (see issue 3 above) the company purchased twenty extra beds (at a total cost of R16 000) from non-vendors. Originally the intention was to keep them for future use, but on 20 October 2016 they sold two beds to an employee for R300 (excluding VAT) each (the market value being R800 (excluding VAT) each).

The other eighteen beds were exported directly to a non-related buyer in China for a total consideration of R20 000 (also during October 2016). These transactions have not yet been recorded.

REQUIRED:

Discuss the VAT implications of each of the above three scenarios. Where applicable, show calculations and pay special attention to the tax period (time of supply) and the value of supplies.

<table>
<thead>
<tr>
<th>REQUIRED:</th>
<th>Marks</th>
</tr>
</thead>
<tbody>
<tr>
<td>Discuss the VAT implications of each of the above three scenarios. Where applicable, show calculations and pay special attention to the tax period (time of supply) and the value of supplies.</td>
<td>19</td>
</tr>
</tbody>
</table>

PROPOSED METHOD OF ANSWERING THE QUESTION (EXAM TECHNIQUE):

To make the most of the information provided in the allowable time (i.e. 60 minutes), you ought to follow a certain thinking pattern and working method:

1. **Reading the “required” part:**
   - This is a long question with various issues and problems based on the same set of facts.
   - The question addresses VAT only, which means that you can ignore all other types of taxes. However, in the case of fringe benefits that will give rise to a deemed supply, the income tax treatment (7th Schedule) is important. It is also important to be able to identify such deemed supplies from the information provided.
   - The verbs used (explain, discuss and indicate) tell you exactly what is required from you. You have to use words, but can support your views with calculations, where applicable. This is important as it will make your answer applicable to the specific set of facts.
2. **Evaluate and contemplate how to answer the question:**
   - This is a long question but has been broken down into 2 parts, namely part A and B. In each part, a few different issues are tested.
   - Start from the top and work through the question, as the facts obviously build up to a complete picture. For example, in part A issue 1, you can establish that the company will make both taxable and exempt supplies. Thus, input tax needs to be apportioned. This will impact on the rest of the question.
   - Bear in mind that the number of marks allocated for each part of the question is an indication of the length and detail required in your solution.

3. **Analyse and interpret the question as follows:**
   - The two Woo-brothers formed a company that is the vendor we are looking at.
   - The company acquires second-hand fixed property, which gives rise to a notional input tax deduction.
   - As mentioned above, input tax needs to be apportioned as the company makes both taxable and exempt supplies.
   - Various events with VAT consequences then take place, namely
     - the company renovates the building
     - the company employs cleaning staff and supplies them each with a free lunch which is prepared in an equipped caravan
     - the company purchases second-hand goods (furniture) from both vendors and non-vendors
     - the cashier embezzles cash
     - a change in taxable use of capital goods takes place
     - some second-hand goods acquired are exported; some are sold to an employee below market value
     - the VAT due is paid late.

4. **Communicate your answer**
   You now have to communicate the VAT consequences of the above by applying the principles of the VAT Act. Set out your answer in a logical sequence. Plan your answer to each issue before writing it down.
PART A

Issue 1

(a)  The building is a “second-hand good” as defined in section 1(1) and therefore the company is entitled to a notional input tax deduction. (1)

This is calculated by using the tax fraction and applying it to the lesser of consideration in money or open market value \( (\frac{14}{114} \times R3\ 000\ 000 = R368\ 421,05) \). (Section 1(1), par (b) of definition of input tax) (Although the transaction is between connected persons and the purchaser is not entitled to claim all the input tax (purchaser makes partly taxable and partly non-taxable supplies), section 10(4) is not applicable due to the fact that par (b) of the definition of input tax contains its own specific value rule. (2)

As the building is used to make both taxable and exempt supplies, input tax must be apportioned (section 17(1)). (1)

Based on rental income, the % to be used, is calculated as follows: (1)

Ground floor (50%): Taxable supply at standard rate (14%) (1)

First floor (25%): This constitutes “domestic goods and services” supplied at an all-inclusive charge by an enterprise supplying “commercial accommodation” as defined in section 1(1), thus a taxable supply. As it is not for an unbroken period of more than 28 days at a time, the full value of the supply is subject to VAT @ 14%. (2)

Second floor (25%): This does not constitute “domestic goods and services” as defined in section 1(1) (unfurnished), but the supply of a dwelling in terms of an agreement for the letting and hiring thereof (residential accommodation). This is therefore exempt supplies (section 12(c)). (1)

Thus based on turnover - 75% taxable supplies (ground and first floor).

The notional input tax that can be deducted is R368 421 x 75% = R276 316. (1)

The time of supply is the earlier of date of registration or the date that any payment of the consideration is received (section 9(3)(d)), but

The input tax can only be claimed on the date of registration of the building in the name of the company (section 16(3)(a)(ii)(bb)(A)) and is further limited to the extent that payment has been made (section 16(3)(a)(ii)(aa)). Input tax is therefore claimable on the date of registration (31 August 2016) but as no payment has been made by 31 August 2016 (purchase price outstanding on loan account) no input tax can be claimed. (1)

(b) All input tax paid on the costs incurred in renovating the ground floor (shops) and the first floor (overnight apartments) may be claimed as an input tax deduction as long as the company has valid tax invoices to support their claims. (1)

Input tax paid in renovating the second floor will be disallowed as an input tax credit, as it is used for the making of exempt supplies.

If the relevance of the expenditure cannot be directly established (directly attributable) - apportion it in the ratio mentioned above (75% deductible – section 17(1)). (1)
(c) The Woo brothers made a supply of goods exceeding the threshold of R1 000 000, but the sale of the property was not done in the course or furtherance of an enterprise as it is not an activity which is carried on continuously or regularly. (3)

Issue 2
The supply of overnight accommodation is a taxable supply as explained in issue 1 above.

Input tax
- The caravan is not a “motor car”, as defined (specifically excluded), but the input tax is denied because it is acquired for purposes of entertainment (section 17(2)). (1)
- Similarly - the input tax on all the ingredients acquired to prepare the meals will also be denied as it is for the purpose of entertainment (section 17(2)). (1)
- The rendering of services by an employee to an employer in the course of employment is not deemed to be the carrying on of an enterprise to the extent that remuneration (as contemplated in the Fourth Schedule) is paid. Therefore, no input tax consequences arise in respect of the salaries paid to the cleaning staff and the employee that prepares the lunches (definition of enterprise in section 1(1), proviso (iii)(aa)). (1)
- In terms of section 18(3) of the Act, where a vendor provides an employee with a benefit or advantage which falls into the employee’s gross income in terms of paragraph (i) of the gross income definition of the Income Tax Act, such benefit is deemed to be a taxable supply in the hands of the vendor. The free lunches will constitute a fringe benefit to employees, but with a Rnil value in terms of par 8(3)(a) of the Seventh Schedule. (1)
- However, the first proviso to section 18(3) provides that the section will not apply in respect of any benefit or advantage to the extent that it is the supply of entertainment. (1)
- The supply of free lunches in the caravan-canteen will therefore not give rise to a deemed supply in the hands of the company, as it constitutes entertainment, as defined. (1)

Issue 3
The furniture acquired from non-vendors is “second-hand goods” (as defined in section 1(1)) and the company will be entitled to a notional input tax deduction. (1)

This notional input tax will be calculated by applying the tax fraction (14/114) to the lesser of the consideration in money given or the open market value of the supply (section 1(1), definition of input tax, paragraph (b)). (1)

From the information given one can conclude that the amount paid will equal the open market value. Even though the company is registered on the invoice basis the notional input tax, with regard to the furniture, can only be claimed once payment has been made (November/December 2016 tax period) and only to the extent that payment has been made - section 16(3)(a)(ii)(aa). (1)

The furniture acquired from retailers, even though second-hand, is supplies by vendors and will be subject to VAT. In the tax period when the tax invoice is received the company may claim the input tax (section 9(1)). (1)
Part B

Cash stolen
The theft of the cash is an event that happened after the supply was made (amount had already been received “on own behalf and for own benefit” – Geldenhuys case). Therefore, output tax of R840 (14/114 x R6 840) should be declared on the rental income in the tax period ended 28 February 2017.

Deemed output tax of R368.42 (14/114 x R3 000) should be declared on the insurance payment received, in the tax period ended 28 February 2017, as this constitutes a deemed supply by the company (section 8(8)).

Outsource
No change of use occurred in respect of the building, as the second floor is still utilised for residential purposes (exempt supplies).

However, a change in the use of the computer took place. Previously, it was used to make taxable supplies of 75% and now it is used 100% for making taxable supplies. The increase of 25% exceeds the required 10% and as the computer is a capital asset with a cost of more than R40 000 (excluding VAT), an adjustment must be made in terms of section 18(5). The adjustment is made at year-end (28 February 2017) (section 18(6)).

To adjust input tax the tax fraction should be applied to the lesser of the adjusted cost (R57 000) and the open market value at 28 February 2017 (R42 000). The term ‘adjusted cost’ is defined in section 1(1) of the Act and means the original cost price including VAT, therefore R57 000. Therefore input tax of R1 289.47 (14/114 x R42 000 = R5 157.89 x 25%) can be claimed by the company in the tax period ending 28 February 2017.

Alternative solution based on a strict literal interpretation of the Act:

1/10/2016 – 31/12/2016 – 3 months at 75% taxable
1/1/2017 – 28/2/2017 – 2 months at 100% taxable
Therefore C in the formula is: (3 months x 75%) + (2 months x 100%) ÷ 5 months = 85%
D = previous taxable use = 75%
Therefore, change in use is ≤ 10%, therefore no adjustment as not > 10%. Adjustment may be made at 28 February 2018.

Sale and exports
Output tax of R84 (14% x (R300 x 2)) must be declared in the tax period ended 31 October 2016.

Selling two beds below market value to an employee, results in a fringe benefit (asset obtained at less than market value (R800)).

As this is a fringe benefit which falls into the employee’s gross income in terms of paragraph (i) of the gross income definition of the Income Tax Act and section 18(3) applies, there is no change in use adjustment under section 18(1).

The value of the fringe benefit is determined as the difference between the consideration paid (R600) and the market value (R800 x 2 = R1 600). A deemed output tax of R122,81 (14/114 x (R1 600 – R600)) must be paid by the company.
The above output tax should have been declared in the tax period ended 31 October 2016. Interest at the prescribed rate and a penalty of 10% of the amount is payable, as it will now only be paid in the tax period ending 28 February 2017 (section 39 and 45 (excluded from syllabus)).

Exports
Goods exported to an export country are zero-rated, except when it consists of second-hand goods and a deemed input tax was claimed, as in this case - section 11 (proviso to sub section (2)).

The value of the supply is based on the consideration paid for the goods by the exporter, namely R14 400 (R800 (R16 000/20 = R800) x 18). The company has to pay output tax of R1 768,42 (14/114 x R800 x 18 beds).
SECTION C – Self-assessment assignment 1/2017

PURPOSE STATEMENT:
In SECTION C, you will find the self-assessment assignment, which you have to mark yourself. You have to assess your own knowledge and competencies and take responsibility for your own learning experience.

Fourteen hours have been allocated to work through section C. You have already spent 15 minutes of this time to work through question 1. You therefore have 13 hours 45 minutes left for the rest of section C. We have provided you with a further 22 questions (15,25 hours) to work through.

After completing the questions in the self-assessment assignment in the time limits provided you should be able to:
- Identify if you have rectified the shortcomings identified in the previous sections;
- Demonstrate that you are competent to pass the formative assessments and summative assessment relating to the topics you have covered so far.

<table>
<thead>
<tr>
<th>Question</th>
<th>AQSAT / provided</th>
<th>TOPIC</th>
<th>Marks / Time</th>
</tr>
</thead>
</table>
| 1        | 10.2             | Donations tax  
  - the value of the annuity in note 1 = R327 099  
  - the value of the annuity in note 2 = R130 840  
  - the value of the usufruct in note 4 = R686 908  
Assume that all the donations were made in the 2017 year of assessment | 8/12 |
| 2        | 13.1             | VAT (calculation question on various VAT issues) (connected persons, deregistration, input tax and output tax)  
This question together with the solution is provided in AQSAT 2017 and therefore not reproduced in this tutorial letter. | 28/42 |
<table>
<thead>
<tr>
<th>Question</th>
<th>AQSAT / provided</th>
<th>TOPIC</th>
<th>Marks / Time</th>
</tr>
</thead>
<tbody>
<tr>
<td>3</td>
<td>13.3</td>
<td>VAT and accounting integration. In transaction 4 include both ABC Insurance and X Ltd in your answer. This question together with the solution is provided in AQSAT 2017 and therefore not reproduced in this tutorial letter.</td>
<td>39/59</td>
</tr>
<tr>
<td>4</td>
<td>13.4</td>
<td>VAT (calculation on various VAT issues) (Fringe benefits) This question together with the solution is provided in AQSAT 2017 and therefore not reproduced in this tutorial letter.</td>
<td>16/24</td>
</tr>
<tr>
<td>5</td>
<td>13.7</td>
<td>VAT (calculation on various VAT issues) (Input and output tax) (Solution provided)</td>
<td>30/45</td>
</tr>
<tr>
<td>6</td>
<td>13.8</td>
<td>VAT (Adjustments)</td>
<td>20/30</td>
</tr>
<tr>
<td>7</td>
<td>13.9</td>
<td>VAT (Supplies, deemed supplies, connected persons, instalment credit agreements)</td>
<td>24/36</td>
</tr>
<tr>
<td>8</td>
<td>provided</td>
<td>VAT (calculate with reasons) (Input and output tax)</td>
<td>24/36</td>
</tr>
<tr>
<td>9</td>
<td>provided</td>
<td>VAT (discussion question on various VAT issues and correcting journal entries) (Entertainment, motor car, fringe benefits, second hand goods (animals), game viewing vehicles, unpaid creditors, indemnity payment, fixed property)</td>
<td>50/75</td>
</tr>
<tr>
<td>10</td>
<td>provided</td>
<td>VAT (calculation, explain and advise question) (Various VAT issues)</td>
<td>40/60</td>
</tr>
<tr>
<td>11</td>
<td>provided</td>
<td>VAT (discussion question on various VAT issues and correcting journal entries) (Supply of training, entertainment, motor car, fringe benefits, exporting of second-hand goods, insurance premiums, indemnity payments, discounted transactions, commercial accommodation, partnerships, doubtful debts, bad debts, change in use adjustments, registering as VAT vendor, zero rated, exempt and standard rated supplies and fixed property)</td>
<td>40/60</td>
</tr>
<tr>
<td>12</td>
<td>provided</td>
<td>VAT (discussion question on connected persons and fixed property)</td>
<td>6/9</td>
</tr>
<tr>
<td>13</td>
<td>provided</td>
<td>VAT (calculation of VAT and discuss sale of residential house used partly for making taxable supplies and partly for residential purposes)</td>
<td>23/35</td>
</tr>
<tr>
<td>14</td>
<td>provided</td>
<td>VAT (discussion question on the purchase of a building, indemnity payments and fringe benefits) (QE 2007-question)</td>
<td>42/63</td>
</tr>
<tr>
<td>Question</td>
<td>AQSAT / provided</td>
<td>TOPIC</td>
<td>Marks / Time</td>
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<tr>
<td>15</td>
<td>provided</td>
<td>VAT and Donations tax (Calculation of VAT and donations tax) &lt;br&gt; (local and export sales, exportation of second-hand machine, imports, fringe benefit, donation (promotional items), transport of employees, change of use of capital asset (section 18(5)) and e-filing)</td>
<td>29/44</td>
</tr>
<tr>
<td>16</td>
<td>provided</td>
<td>VAT journals</td>
<td>29/44</td>
</tr>
<tr>
<td>17</td>
<td>provided</td>
<td>VAT and Donations tax (Calculation / Discussion on various VAT issues and calculation of donations tax) &lt;br&gt; (fixed property and conversion cost, fringe benefit, entertainment, advertising, over-payment and refund, second-hand goods, supply of assets used partly for taxable supplies (sections 8(16) and 16(3)(h)))</td>
<td>36/54</td>
</tr>
<tr>
<td>18</td>
<td>provided</td>
<td>VAT (Calculation / Discussion on various VAT issues) &lt;br&gt; (fixed property, going concern (sections 18A and 16(3)(h)), transport, company car and indemnity payments)</td>
<td>29/44</td>
</tr>
<tr>
<td>19</td>
<td>provided</td>
<td>VAT (Calculation / Discussion on various VAT issues) &lt;br&gt; (fixed property, going concern (sections 18B, 16(3)(h), and 8(2)))</td>
<td>20/30</td>
</tr>
<tr>
<td>20</td>
<td>provided</td>
<td>VAT (Discussion) &lt;br&gt; (registration, electronic services and imported services)</td>
<td>15/23</td>
</tr>
<tr>
<td>21</td>
<td>provided</td>
<td>VAT and Donations Tax (Calculation and discussion on fixed property transactions and VAT) &lt;br&gt; (VAT on fixed property transactions and donations tax calculation)</td>
<td>20/30</td>
</tr>
<tr>
<td>22</td>
<td>provided</td>
<td>VAT and Donations Tax</td>
<td>40/60</td>
</tr>
<tr>
<td>23</td>
<td>provided</td>
<td>VAT (Calculation and discussion on various VAT issues) &lt;br&gt; (fixed property, commercial rental and residential accommodation, fringe benefits, entertainment, going concern and zero-rated services (sections 16(3), 15(1), 12(1)(c), 18(3), 18A, 8(15), 7(1)(a), 11(2)(j), and 17(2)(a)).</td>
<td>20/30</td>
</tr>
</tbody>
</table>

Total marks / time: (628 marks/15.7 hours)

Remember:

1. In terms of the definition of open market value in section 1(1) of the VAT Act, open market value always includes VAT. Therefore, even if the question states that all amounts exclude VAT the open market value will always include VAT as open market value is defined in the VAT Act.

2. The amounts in the Trial Balance, Comprehensive Statement of Income (Income Statement) or Statement of Financial Position (Balance Sheet) of a vendor always exclude VAT in respect of items on which output tax were levied or in respect of items on which input tax were paid and could be claimed.
John Grove

<table>
<thead>
<tr>
<th>Donation</th>
<th>Value R</th>
<th>Exemption R</th>
<th>Taxable Donation R</th>
<th>Donations Tax @ 20% R</th>
</tr>
</thead>
<tbody>
<tr>
<td>1) R5 000 annuity to sister (s 62(1)(b))</td>
<td>327 099</td>
<td>(327 099)</td>
<td>-</td>
<td>-</td>
</tr>
<tr>
<td>Exemption is under section 56(2)(c) (if bona fide maintenance payments)</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Further annuity – not for maintenance; therefore (s 62(1)(b))</td>
<td>130 840</td>
<td>(100 000)</td>
<td>30 840</td>
<td>6 168</td>
</tr>
<tr>
<td>exemption under section 56(2)(b) relating to the R100 000 exemption permitted to each taxpayer annually</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>3) Proceeds from sale of shares – donated portion</td>
<td>100 000</td>
<td>(100 000)</td>
<td>-</td>
<td>-</td>
</tr>
<tr>
<td>As this donation arises from proceeds from the sale of a foreign asset inherited from a non-resident, the amount is exempt under section 56(1)(g)(iii)</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>4) Usufruct in farm to nephew (s 62(1)(a))</td>
<td>686 908</td>
<td>-</td>
<td>686 908</td>
<td>137 382</td>
</tr>
<tr>
<td>(R100 000 exemption (section 56(2)(b)) already used)</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>5) Donation exempt in terms of section 56(1)(d) – note no donation had taken place donee has not enjoyed any benefit – do not confuse with donation in contemplation of death (donatio mortis causa) (section 56(1)(c))</td>
<td>1 500 000</td>
<td>(1 500 000)</td>
<td>-</td>
<td>-</td>
</tr>
</tbody>
</table>

Note: The donee (Joe) will not obtain any benefit under the donation until the death of the donor (John). The deciding factor here is not the anticipation of death. Rather, the donor merely undertakes to donate an asset to the donee upon the donor's death. When John dies, the farm will be included in John's deceased estate for estate duty purposes, and is therefore not subject to donations tax.

6) Gifts | 10 000 | - | 10 000 | 2 000 | (1) |
| Do not confuse the R10 000 exemption granted to non-natural persons (s 56(2)(a)) with the R100 000 exemption to natural persons (s 56(2)(b)) R100 000 already utilised. | | | | |

7) Public Benefit Organisation | 10 000 | (10 000) | - | - | (1) |
| Exemption under section 56(1)(h) that refers to section 10(1)(cN) which in turn refers to section 30 (relating to public benefit organisations) | | | | |
QUESTION 1 - SUGGESTED SOLUTION (continued)

Note:

As donations tax is payable by the end of the month following the month in which the donation was made, donations tax should be calculated separately on each donation made.

QUESTION 2 – AQSAT 13.1  

Solution to question 13.1 in AQSAT is provided in AQSAT and therefore not reproduced in this tutorial letter.

QUESTION 3 – AQSAT 13.3  

Solution to question 13.3 in AQSAT is provided in AQSAT and therefore not reproduced in this tutorial letter.

Additional notes to the solution:

1. GB (Pty) Ltd

Debt reduction (section 19(5)) – trading stock not on hand is a recoupment (section 8(4)(a))

2. Company A

Local sales – amount provided in the question, excluded VAT, therefore the VAT should be R77 000 x 14% = R10 780

The Namibian branch: As the Namibian branch can be separately identified and an independent system of accounting is maintained, it is seen as as being a separate vendor from Company A. Therefore, trading stock sent to the Namibian branch is exported at 0%. (s 11(1)(i), s 8(9), proviso (ii) to the definition of enterprise).

The Botswana branch: As the Botswana branch does not maintain an independent accounting system, the branch is part of Company A’s enterprise. Therefore, the stock is only transferred to the branch (it is not a sale) and then sold at 0% to the Botswana customers.

3. Mr A

Bets received: The person with whom a bet is placed is deemed to supply a service (section 8(13)). The consideration for the supply is the amount received in respect of the debt (section 10(17)).

Winnings paid: An amount equal to the tax fraction (14/114) of the winnings paid out may be deducted as input tax, provided that if the winnings constitutes goods or services, the input tax will be limited to the amount of the input tax on the initial cost of acquiring those goods or services (section 16(3)(d)).

4. X Ltd

The full indemnity amount is a deemed supply (section 8(8)).

The cash received for the machine, will have a R3 509 recoupment (section 8(4)(a)) and output tax of R491 as a consequence. Once the R4 000 is received from the insurance company (Dr Bank account), R491 is accounted for as output tax and paid to SARS. Therefore, X Ltd has a R491 cash loss (R4 000 – R3 509 = R491) and it is submitted that it is deductible.
**QUESTION 4 – AQSAT 13.4**

Solution to question 13.4 in AQSAT is provided in AQSAT and therefore not reproduced in this tutorial letter.

**Additional note to point 6 of the solution:**
The supply of residential accommodation is an exempt supply in terms of section 12(c) of the VAT Act. Exempt supplies are excluded from the definition of an enterprise and are therefore not taxable supplies. Input tax can not be claimed in respect of the making of exempt supplies.

Section 18(3) also states that no deemed output tax need to be accounted for, for the supply of a fringe benefit that constitutes the supply of exempt supplies.
QUESTION 5 - SUGGESTED SOLUTION (AQSAT 13.7)

VAT effects

<table>
<thead>
<tr>
<th>Input</th>
<th>Output</th>
</tr>
</thead>
<tbody>
<tr>
<td>tax</td>
<td>tax</td>
</tr>
<tr>
<td>R</td>
<td>R</td>
</tr>
</tbody>
</table>

- **Purchases**: R410 400 \times \frac{14}{114} \quad 50 400 \quad (1)
- **Sales - local**
  - **- export**: (R700 000 - R10 000 (export)) \times 14\% \quad 96 600 \quad (1)
  - Zero-rated (section 11(1)(a)) \quad - \quad (1)
- **Interest income**: Financial services - exempt supply (section 12(a)) \quad - \quad (1)
- **Computers bought**: Input on lower of cost and open market value (section 1(1), definition of input tax sub paragraph (b)) - (R4 200 \times \frac{14}{114}) \times 3 \quad 1 547 \quad (2)
  - **from vendors**: (R5 000 \times \frac{14}{114}) \times 2 \quad 1 228 \quad (2)
  - **from non - vendors**: Second-hand goods rule applies \quad - \quad (1)
- **Motor car - VW Polo Playa purchased**: input tax denied (section 17(2)(c)) and definition of “motor car” in section 1(1) \quad - \quad (1)
- **Output tax on fringe benefit, use given to Bryce**: R130 000 \times \frac{100}{114} \times 0.3\% \times 14/114 \times 1 month \quad 42 \quad (3)
  - (deemed supply – section 18(3))
- **Delivery vehicle**: R87 500 \times \frac{14}{114} \quad 10 746 \quad (2)
  - (instalment credit agreement - VAT accounted for upfront on cash cost) (sections 9(8) and 10(16))
- **Petrol costs**: zero rated (section 11(h)) \quad - \quad (1)
- **Computer sold**: Connected person rule applies as New Found Glory is a connected person that cannot claim full input tax (non-vendor) and sale for less than open market value \quad (1)
  - Use open market value (section 10(4)) \quad (1)
  - R2 500 \times \frac{14}{114} \quad 307 \quad (1)
- **Rental agreement**: R8 000 \times \frac{14}{114} \times 6 \text{ months} (1 March 2016 to 31 August 2016) (sections 9(3)(a) and 10(2) and (3)) \quad 5 895 \quad (2)
- **Fixed property**: R200 000 (claim at earlier of payment or registration (section 9(3)(d)) but only to extent of payment) \quad 24 561 \quad (2)
  - (section 16(3)(a)(ii)(aa)) \times \frac{14}{114}
- **Repairs**: R21 000 \times \frac{14}{114} \quad 2 579 \quad (1)
QUESTION 5 - SUGGESTED SOLUTION (continued)

<table>
<thead>
<tr>
<th>Description</th>
<th>Amount</th>
<th>Note</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Insurance Receipt</strong></td>
<td><strong>R18 900 x ( \frac{14}{114} )</strong></td>
<td><strong>R 2 321</strong></td>
</tr>
<tr>
<td><strong>Doll donated to museum</strong></td>
<td><strong>R10 000 x ( \frac{14}{114} )</strong> (deemed supply in terms of section 18(1) at open market value as obtained for purposes of making taxable supplies now applied totally for another purpose – refer note 1).</td>
<td><strong>R 1 228</strong></td>
</tr>
<tr>
<td><strong>Salaries and wages</strong></td>
<td><strong>Employment not an enterprise (section 1(1), definition of an enterprise)</strong></td>
<td><strong>-</strong></td>
</tr>
<tr>
<td><strong>Yacht</strong></td>
<td><strong>The yacht was purchased for purposes of entertainment, the supply is thus one of entertainment, therefore no deemed supply arises in terms of section 18(3) proviso.</strong></td>
<td><strong>-</strong></td>
</tr>
<tr>
<td><strong>Alternatively if it was not used for entertainment but for holiday:</strong></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Value of deemed supply (section 18(3))</td>
<td></td>
<td></td>
</tr>
<tr>
<td><strong>R400 000 x 15% x ( \frac{104}{365} )</strong> = <strong>R17 096</strong></td>
<td></td>
<td></td>
</tr>
<tr>
<td><strong>Less:</strong> <strong>R10 000 paid by employee = R7 096</strong></td>
<td></td>
<td></td>
</tr>
<tr>
<td><strong>Output tax on taxable fringe benefit = R7 096 x ( \frac{14}{114} ) = R871</strong></td>
<td></td>
<td></td>
</tr>
</tbody>
</table>

**Note 1:**
Note that if the doll had been donated to a Public Benefit Organisation or if the company obtained any benefit by donating the doll (e.g. a marketing benefit) the supply would have had a nil value, refer to section 10(23).
1. In terms of s 8(16) of the VAT Act, a full output tax arises on the sale, although the mainframe was only used 25% for the making of taxable supplies, i.e.

\[ 100\% \times R1 \times 200 000 \times 14\% = 168 000 \]  

In terms of s16(3)(h), since goods have been supplied, an input tax adjustment is made to cater for the percentage of non-taxable use in accordance with the formula:

\[ A \times B \times C; \text{ where} \]

A = the tax fraction
B = the lesser of the adjusted cost (incl VAT) \( (R1 \times 500 000 \times 1.14 = R1 \times 710 000) \) and open market value \( (R1 \times 200 000 \times 1.14 = R1 \times 368 000) \) at the date of supply
C = the percentage of non-taxable use immediately before the supply

\[ \frac{14}{114} \times (R1 \times 200 000 \times \frac{114}{100} \times 75\%) = \frac{126 000}{1} \]

This input tax is claimable in the Bank's April tax return.

2. Since the use of the mainframe has changed such that the use for making taxable supplies has increased, an input tax adjustment is made in terms of s 18(5), in accordance with the formula:

\[ A \times B \times (C - D); \text{ where} \]

A = the tax fraction
B = the lesser of the adjusted cost (incl VAT) \( (R1 \times 500 000 \times 1.14 = R1 \times 710 000) \) and open market value \( (R1 \times 200 000 \times 1.14 = R1 \times 368 000) \) at the date of supply
C = the increased percentage of taxable use over the 12-month period ending on the last day of the vendor's year of assessment.
D = the previous percentage of taxable use

S 18(5) is applicable because the mainframe constitutes a capital good with a cost of R40 000 (excluding VAT) or more (refer to proviso (i)(aa) under s 18(5)) and the change in use is more than 10% (refer to proviso in definition of “C” under s 18(5)), from 75% 100%

\[ C = 100\% \]  
\[ D = 25\% \]

Therefore:

\[ \frac{14}{114} \times R1 \times 200 000 \times (100\% - 25\%) \]
\[ \frac{14}{114} \times R1 \times 200 000 \times 75\% \]

R110 526

Therefore, an input tax of R110 526 may be claimed in the April 2017 VAT return.

Even though the increase in taxable use occurred on 1 January 2017, the increase is only deemed to occur on 30 April 2017 (financial year-end) (s 18(6)).
**QUESTION 6 - SUGGESTED SOLUTION (continued)**

**Alternative solution based on a strict interpretation of the Act:**

2. Since the use of the mainframe has changed such that the use for making taxable supplies has increased, an input tax adjustment is made in terms of s18(5), in accordance with the formula.

\[ A \times B \times (C - D) \]

where

- \( A \) = the tax fraction
- \( B \) = The lesser of the adjusted cost (cost incl. VAT) and open market value on the last day of the Banks financial year – being 30 April 2016.
  - Cost = R1 500 000 x 1.14 = R1 710 000 (including VAT) and
  - OMV = R1 200 000, therefore use OMV of R1 200 000
- \( C \) = the increased percentage of taxable use over the 12 month period ending on the last day of the vendors year of assessment
  - = 25% for the first 4 months (1 Sep 2016 - 31 Dec 2016)
  - = 100% for the next 4 months (1 Jan 2017 - 30 April 2017)
  - = \((4 \times 25\% + 4 \times 100\%) / 8\)
  - = 62.5%
- \( D \) = the previous percentage of taxable use - 25%

S18(5) is applicable because the mainframe constitutes capital goods with a cost of R40 000 (excl. VAT) or more and the increase in taxable use is > 10%.

Therefore:

- \( C = 62.5\% \)
- \( D = 25\% \)

\[ \frac{14}{114} \times R1 200 000 \times (62.5\% - 25\%) \]
\[ \frac{14}{114} \times R1 200 000 \times 37.5\% \]

R55 263

Therefore an input of R55 263 may be claimed in the April 2017 VAT return.

Even though the increase in taxable use occurred on 1 January 2017, the increase is only deemed to occur on 30 April 2017, which is the end of the year of assessment, in terms of s18(6).

Assuming no further change in use, a second adjustment calculation will be performed on 30 April 2018, with the actual taxable usage \( C \) equal to 100% and the previously claimed usage equal to 62.5%. (25\% + 37.5\% + 37.5\% = 100%)
### QUESTION 7 - SUGGESTED SOLUTION (AQSAT 13.9)

**Argon Ltd**

<table>
<thead>
<tr>
<th></th>
<th>R</th>
<th>(Inputs) / Outputs</th>
</tr>
</thead>
<tbody>
<tr>
<td>1. Sales to vendors – (time of supply rule has been met)</td>
<td>100% x 2 300 000</td>
<td>x 14%</td>
</tr>
<tr>
<td>2. Sales to Xenon</td>
<td>30% x R1 400 000 =</td>
<td>420 000</td>
</tr>
<tr>
<td>(*refer note below)</td>
<td></td>
<td>cost =</td>
</tr>
<tr>
<td></td>
<td></td>
<td>=</td>
</tr>
<tr>
<td></td>
<td></td>
<td>cost + 50% =</td>
</tr>
<tr>
<td>Connected person (“CP”) who cannot claim full input tax (s 10(4))</td>
<td>CP rule VAT on</td>
<td>700 000 x 14%</td>
</tr>
<tr>
<td>Trade discounts - no VAT effects as output tax already reduced</td>
<td>-</td>
<td>-</td>
</tr>
<tr>
<td>Sales to other non-vendors:</td>
<td>70% x R1 400 000 =</td>
<td>980 000 x 14%</td>
</tr>
<tr>
<td>3. CP rule irrelevant (Neon can claim full input tax). (s 10(4) not applicable)</td>
<td>7 000 x 14%</td>
<td>980</td>
</tr>
<tr>
<td>4. Feb: Vendor to CP (Xenon can claim full input tax) – s 10(4) not applicable.</td>
<td>30 000 x 14%</td>
<td>4 200</td>
</tr>
<tr>
<td>Mar: Vendor (who cannot claim full input tax) (s 10(4))</td>
<td>40 000 x $^{14/114}$</td>
<td>4 912</td>
</tr>
<tr>
<td>5. S 8(8) Car – indemnity payment (This is a repair and not a total reinstatement, therefore – section 8(8) deemed supply.)</td>
<td>16 800 x $^{14/114}$</td>
<td>2 063</td>
</tr>
<tr>
<td>Trading Stock Purchases from vendors</td>
<td>1 850 000 x 14%</td>
<td>( 259 000)</td>
</tr>
<tr>
<td>Trading Stock Purchases from non-vendors (no VAT paid)</td>
<td>-</td>
<td>-</td>
</tr>
<tr>
<td>6. Rental agreement: time of supply – day rent becomes payable (Section 9(3)(a)), therefore:</td>
<td>50 000 x 14%</td>
<td>( 7 000)</td>
</tr>
<tr>
<td>February = 1 February, March = 1 March thus</td>
<td></td>
<td></td>
</tr>
<tr>
<td>7. The deposit is 'consideration', as it is applied in settlement of the debt. The agreement is an 'instalment credit agreement' (s 1, definition of 'instalment credit agreement'). Time of supply is 25 March 2017 (earlier of date of delivery or when any payment of 'consideration' is made). (Section 9(3)(c))</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Total payments</td>
<td>60 x R6 000 =</td>
<td>360 000</td>
</tr>
<tr>
<td>Less: finance charges</td>
<td>( 94 500)</td>
<td>(1)</td>
</tr>
<tr>
<td>Cash value =</td>
<td>265 500 x $^{14/114}$</td>
<td>( 32 605)</td>
</tr>
</tbody>
</table>
QUESTION 7 – SUGGESTED SOLUTION (continued)

8. Second-hand goods rule (purchased from non-vendor) (lower of consideration or open market value) (par (b) of “input tax” definition in section 1). Claim based on:
   R100 000 limited to extent of payment (Section 16(3)(a)(ii)(aa)).
   60 000 \times \frac{14}{114} = 7 368 \text{ (2)}

9. Erection of advertising boards - advertising
   Hire of box constitutes entertainment (R160 000 - R25 000) (input tax denied) (S 17(2)(a))
   The fact that the amount relates to an annual charge is irrelevant.
   25 000 \times 14\% = 3 500 \text{ (1)}

10. Input tax not denied, as this is not in respect of membership of a sporting, social or recreational club.
    3 600 \times 14\% = 504 \text{ (1)}

11. Trading stock on hand irrelevant.
    - \text{ (1)}
    \text{ (24)}

*Note to 2 above: Section 10(4) refers to “consideration” and “open market value”. Both these terms include VAT; however, you will note that the amounts in the question are exclusive of VAT. No adjustment was made to add VAT at 14% to the amounts calculated under 2 respectively, solely for the reason that the calculated open market value in the question is based on an amount exclusive of VAT.*
QUESTION 8

24 marks

Background:

Mr Alan Pane is the sole shareholder and director of Cape Panelbeaters (Pty) Ltd. Alan received his retrenchment package on 1 October 2016 at the early age of 50. Alan’s trade was that of a panelbeater.

On 1 November 2016, Cape Panelbeaters (Pty) Ltd began trading as panelbeaters (a process similar to manufacturing) in Cape Town. The company registered as a vendor for purposes of Value-Added Tax (VAT). The first tax period ended 31 December 2016 and the second period 28 February 2017. The financial year-end of the company is 28 February 2017.

The bookkeeper of Cape Panelbeaters is not sure how to account for the VAT on certain transactions that took place during the period January 2017 and February 2017. As the financial year-end is February 2017, Alan requested you as the auditor to assist with the VAT return of February. All amounts include VAT, where applicable.

Transaction 1: 2 marks

R Invoice issued to the Department of Defence on 28 February 2017 570 000

During February 2017 Cape Panelbeaters was awarded a tender for the repair of heavy duty military vehicles that were damaged in the course of training soldiers. A standard clause in the tender document stipulates that the vehicles will be delivered to the premises of Cape Panelbeaters during March 2017 and must be repaired within 90 days. Payment will be made after the inspection of the vehicles by military officials to ensure quality. As the financial year-end of all Government Departments is 30 April, they required a tax invoice to be issued by 28 February 2017 to prevent a budget cut for the next financial year.

REQUIRED Marks

Calculate the input and output tax on the above transaction for Cape Panelbeaters (Pty) Ltd. Provide brief reasons where no VAT is calculated. 2

Transaction 2: 2 marks

Sale of competition tickets

R 171 000

During December 2016, the company organized a competition in terms of which the lucky entrant would be awarded a motor car as a prize. Participants were required to purchase a ticket for R100 to enter the competition. The brand new car was purchased from a vendor for cash at a special discounted price of R205 200 in December 2016 (market value of the car was R228 000). Ticket sales during December 2016 was R114 000. The amount of R171 000 indicated above, was ticket sales during January and February 2017. The motor car was supplied as a prize on 28 February 2017.

REQUIRED Marks

Calculate the input and output tax on the above transaction. Provide brief reasons where no VAT is calculated. You may assume that the supply of the motor car is a deemed disposal in terms of section 8(13). 2
**QUESTION 8 (continued)**

**Transaction 3:**

11 marks

*Fringe benefit to employee*

The manager of the workshop is provided with the free use of a delivery truck (not a motor car) since 1 December 2016. The determined value (for VAT purposes) of the truck is R76 000. The employer (Cape Panelbeaters) pays for all fuel and maintenance to the vehicle, except when the manager is on holiday. During February 2017, the manager went on a three-week holiday with the truck (to tow his caravan). The manager used the company’s petrol card during the holiday. On his return he paid the company an amount of R750 consisting of R400 for the use of the truck and R350 for petrol.

**REQUIRED**

<table>
<thead>
<tr>
<th>Marks</th>
</tr>
</thead>
<tbody>
<tr>
<td>(a) Calculate the input and output tax on the above transaction. Provide brief reasons where no VAT is calculated; and</td>
</tr>
<tr>
<td>(b) Provide the journal entry (entries) to record the effect of the deemed output tax on the fringe benefit for income tax purposes.</td>
</tr>
</tbody>
</table>

**Transaction 4:**

4 marks

*Purchase of delivery van*

On 2 January 2017 Cape Panelbeaters (Pty) Ltd purchased a second-hand delivery van from Mr Phutie (a non-vendor) for R32 000 and paid the amount immediately. The company’s original intention was to use the van for deliveries, but it received an offer that the company could not reject from a client in Botswana to purchase the van for 69 000 pulas (equal to R60 000). They accepted the offer and on 6 January 2017, before they brought the van into use, they exported it to Botswana. Cape Panelbeaters recorded the transaction correctly as a debtor for R60 000, payable on 31 January 2017. By 15 February 2017, Cape Panelbeaters had still not received payment from the debtor. When they could not trace the debtor by 28 February 2017, they wrote the outstanding debt off as a bad debt.

**REQUIRED**

<table>
<thead>
<tr>
<th>Marks</th>
</tr>
</thead>
<tbody>
<tr>
<td>Calculate the input and output tax on the above transaction. Provide brief reasons where no VAT is calculated.</td>
</tr>
</tbody>
</table>

**Transaction 5:**

3 marks

*Purchase of assets*

During the beginning of January 2017, Cape Panelbeaters (Pty) Ltd acquired the following assets:

- A new oven to dry paint. They entered into a five-year financial lease agreement in terms of which the oven is leased at a monthly rental of R10 260. The oven could have been purchased for a cash amount of R456 000 (including VAT). The first lease payment was made on 31 January 2017 and the oven was brought into use on 1 March 2017.

- A welding plant. The plant was purchased (new) at a special discounted price of R91 200 (including VAT). The welding plant was brought into use on 1 February 2017.

**REQUIRED**

<table>
<thead>
<tr>
<th>Marks</th>
</tr>
</thead>
<tbody>
<tr>
<td>Calculate the input tax on the above transaction. Provide brief reasons where no VAT is calculated.</td>
</tr>
</tbody>
</table>
QUESTION 8 (continued)

Transaction 6: Destroyed welding plant

On 10 February 2017 the welding plant was totally destroyed by lightning (refer transaction 5). Cape Panelbeaters (Pty) Ltd would have lost a great deal of turnover, if they did not replace the plant as soon as possible. Their insurers paid them R110 000 for the damaged plant on 23 February 2017. A new welding plant was purchased for R115 000 (including installation cost) on the same day. Installation was completed on 28 February 2017 and the welding plant was brought into use on 1 March 2017.

REQUIRED

Calculate the input and output tax on the above transaction. Provide brief reasons where no VAT is calculated; and

<table>
<thead>
<tr>
<th>REQUIRED</th>
<th>Marks</th>
</tr>
</thead>
<tbody>
<tr>
<td>Calculate the input and output tax on the above transaction. Provide brief reasons where no VAT is calculated; and</td>
<td>2</td>
</tr>
</tbody>
</table>
QUESTION 8 – SUGGESTED SOLUTION

24 marks

Transaction 1:
Invoice supplied to the Department of Defence

Output tax
14/114 x R570 000 (earlier of payment or invoice)  70 000 (1)

Input tax
No input tax as no cost incurred as yet.  - (1)

Transaction 2:
Sale of competition tickets

Output tax
14/114 x R171 000  21 000 (1)
(A service was supplied – section 8(13))

Input tax
14/114 x R205 200  25 200 (1)
Although input on motor cars are generally denied, section 8(13) read with section 16(3)(d) and section 17(2)(c)(iii)(aa) permits a deduction in the tax period when the vehicle is deemed to be supplied as a prize – February)

Transaction 3:
Free use of delivery truck

Output tax
January 2017: Consideration 0.6% x R76 000 =  456 (1)

Output tax: 14/114 x R456 =  56,00 (1)

February 2017: Consideration 0.6% x R76 000 =  456

Less: paid by employee:
Petrol (zero-rated supply) - (1)
Consideration paid for use of truck (400) 56 (1)

Output tax: 14/114 x R56  6,88 (1)
Plus: VAT on consideration paid by employee
14/114 x R400  49,13  56,01 (1)

(Government Gazette 13651, Notice Number 2835, dated 22 November 1991)

Input tax
VAT on all cost (including maintenance) except fuel (zero-rated) can be claimed as an input tax deduction. (1)

Journal entries

Dr       Salaries (R56,00 + R6,88)  62,88 (1)
Cr       Output tax control  62,88 (1)
(output tax on fringe benefit)

Dr       Bank account  400,00
Cr       Output tax control  49,13 (1)
Cr       Consideration for use of truck (income)  350,87 (1)
(consideration paid for use of truck)
QUESTION 8 – SUGGESTED SOLUTION  (continued)

Transaction 4:
Purchase of delivery van

Output tax
Sale to Botswana – 14/114 (not zero-rated, export of second-hand goods and a notional input tax was claimed) x R32 000 (1)
(Value limited to original cost price) (section 10(12)) 3 929,82 (1)

Input tax
Claim notional input tax: 14/114 x R32 000 (section 1(1), definition of input tax, sub paragraph b) 3 929,82 (1)
VAT on bad debt: 14/114 x R60 000 limited to notional input tax (section 22(1)) 3 929,82 (1)

Transaction 5:
Purchase of assets:

- Oven
  Input tax
  14/114 x R456 000 (earlier of payment or delivery) 56 000 (2)
  (The fact that the oven was only brought into use in March 2017, has no bearing on claiming the input tax)

- Welding plant
  Input tax
  R91 200 x 14/114 11 200 (1)

Transaction 6:
Destroyed welding plant:

Output tax:
Indemnity payment: R110 000 x 14/114 (section 8(8)) 13 508,77 (1)

Input tax:
Purchase of new welding plant: R115 000 x 14/114 14 122,81 (1)

24
QUESTION 9

This question consists of two unrelated parts. Answer both parts.

PART 1

You are a tax consultant with a local firm of chartered accountants. You have received the following unrelated tax queries from various clients. All of the clients are registered VAT vendors with two-month tax periods.

Answer each query separately and round-off all amounts to the nearest Rand.

Query 1

Bellissimo (Pty) Limited is disposing of certain assets because it is moving to new premises. The financial manager would like to know whether Bellissimo (Pty) Limited is required to levy VAT on the selling price of the following assets:

(a) A pasta-cutting machine used in its pasta factory. The machine was acquired new by Bellissimo (Pty) Limited in 1990. No VAT was paid on the purchase of this machine as the VAT legislation applied only from 30 September 1991.

(b) A water-cooling machine located in the employees’ tearoom and used by the employees. The water cooler was acquired new from a vendor in 2012 and will be sold to a non-employee.

(c) A delivery van used to transport Bellissimo (Pty) Ltd’s products to its customers. The delivery van was acquired new from a vendor in 2013.

<table>
<thead>
<tr>
<th>REQUIRED</th>
<th>Marks</th>
</tr>
</thead>
<tbody>
<tr>
<td>Is Bellissimo (Pty) Limited required to charge VAT on these disposals? Provide reasons for your answer.</td>
<td>3</td>
</tr>
</tbody>
</table>

Query 2

Henry David, the new site supervisor of Buildex (Pty) Limited, a construction company, chose the free use of a motor cycle as part of his salary package. During February 2017, Buildex (Pty) Limited purchased a motor cycle for R182 400 (R160 000 plus VAT of R22 400) and granted the use of this motor cycle to Henry David from 1 March 2017. Henry David does not pay any consideration for the right to use this motor cycle. Buildex (Pty) Limited bears the full cost of repairs and maintenance of this motor cycle. (Applicable tax periods: February 2017 and March 2017.)

Up to 1 April 2017, no accounting entries had been made in the books of Buildex (Pty) Limited regarding the above transactions.

<table>
<thead>
<tr>
<th>REQUIRED</th>
<th>Marks</th>
</tr>
</thead>
<tbody>
<tr>
<td>Provide the accounting journal(s) that should be passed in the books of Buildex (Pty) Limited regarding the above transactions.</td>
<td>8</td>
</tr>
</tbody>
</table>
QUESTION 9  (continued)

Query 3

After a number of break-ins and thefts from its warehouse, SCP Limited increased the security at its warehouse by introducing guard dogs that patrol the premises each night. Five trained guard dogs were purchased at a cost of R900 each. They were purchased from a non-vendor. The journal entry recording the purchase was as follows:

Dr  Security expenditure  R 3 947
Dr  Input tax account ((R900 x 5) x 14/114)  553
Cr  Bank (R900 x 5)  4 500

Being guard dogs purchased to increase the security at the warehouse.

REQUIRED  Marks
State, with a brief reason, whether the above journal entry is correct, and if not, provide the correcting journal.  3

Query 4

Sardine Spotters (Pty) Limited operates a tourism business on the South Coast. During Winter many large schools of sardines (fish) are seen, and caught, along this coast. Sardine Spotters (Pty) Limited transports tourists to the beaches where they may observe, and catch, the sardines. The beaches do not qualify as a safari area.

Sardine Spotters (Pty) Limited purchased the following two motor vehicles:

- A “fourteen-seater” microbus that cost R171 000 (R150 000 plus VAT of R21 000). The microbus is used to transport tourists to and from the beaches.

- A one-ton single cab “bakkie” that cost R141 360 (R124 000 plus VAT of R17 360). Because the “bakkie” was purchased for the purpose of transporting more adventurous tourists onto the beaches, Sardine Spotters (Pty) Limited immediately spent R14 820 (R13 000 plus VAT of R1 820) to have three rows of comfortable seats built into the carriage area of the “bakkie”. As a result of this modification, ten guests can be transported on the back of the “bakkie” at any one time. This “bakkie” is used by Sardine Spotters (Pty) Limited exclusively for this purpose. The costs of modifying the “bakkie” were capitalised as part of the cost of the “bakkie”.

REQUIRED  Marks
Prepare a memorandum in which you advise whether Sardine Spotters (Pty) Limited will be entitled to input tax credits in respect of the purchase and modification of these two motor vehicles. Provide brief reasons to support your advice.  7
**QUESTION 9** (continued)

**Query 5**

In February 2016 Pedantic (Pty) Limited bought certain raw materials for R34 200 (R30 000 plus VAT of R4 200) from a local supplier. Pedantic (Pty) Limited claimed an input tax credit of R4 200 in its tax period 1 January 2016 to 28 February 2016. Pedantic (Pty) Limited encountered quality problems with these raw materials and paid the supplier only R27 360 (R24 000 plus VAT of R3 360) on 29 February 2016. The company refused to settle this account until the quality problems were resolved.

As at today (1 April 2017), R6 840 (R6 000 plus VAT of R840) is still outstanding despite numerous letters of demand having been received from the supplier.

**REQUIRED**

<table>
<thead>
<tr>
<th>Briefly discuss (supported by calculations) whether there are any VAT consequences that arise out of this account being outstanding for this long. In your answer, where relevant, also address the timing of the VAT consequences.</th>
<th>Marks</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>4</td>
</tr>
</tbody>
</table>

**Query 6**

New Look (Pty) Ltd sells slimming products to beauty salons and health spas. Ten months ago a newly appointed sales lady, employed to market a new range of fat burning products, disappeared along with a motor car (as defined) belonging to New Look (Pty) Ltd and a boot full of fat burning products. All attempts to trace this sales lady have failed. The insurance company finally decided to pay out R119 200, calculated as follows:

- R85 000 for the motor car and
- R34 200 for the fat burning products that were stolen.

These amounts comprise the full and final settlement of New Look (Pty) Ltd's claim in respect of the above.

**REQUIRED**

<table>
<thead>
<tr>
<th>Briefly discuss (with calculations where applicable) whether there are any VAT implications for New Look (Pty) Ltd on the R119 200 payment received from the insurance company. Where relevant, refer to the time of supply in your answer.</th>
<th>Marks</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>5</td>
</tr>
</tbody>
</table>
Wallis (Pty) Ltd (a vendor) makes 20% exempt supplies, 30% zero-rated supplies and 50% standard-rated supplies. On 1 March 2017 Wallis (Pty) Ltd signed a contract for the purchase of an administrative building from Ireland CC at its open market value of R1,500,000. No rental agreement relating to the building existed when the purchase contract was entered into.

A deposit equal to 10% of the purchase price was payable to the lawyers on the signing of the purchase contract; the remaining 90% of the purchase price was financed by way of a mortgage bond from ABC Bank. The full purchase price was paid over by the lawyers to Ireland CC upon registration of the property in Wallis (Pty) Ltd’s name. Since registration, capital amounting to R5,000 has been repaid to ABC Bank on the mortgage bond.

(All amounts include VAT where applicable.)

<table>
<thead>
<tr>
<th>REQUIRED</th>
<th>Marks</th>
</tr>
</thead>
<tbody>
<tr>
<td>(a) Discuss and calculate the VAT implications for both the buyer (Wallis (Pty) Ltd) and the seller (Ireland CC) if it is assumed that the seller is not registered for VAT purposes. Where applicable, specifically state in your answer when output tax must be declared and when input tax may be claimed.</td>
<td>6</td>
</tr>
<tr>
<td>(b) Discuss and calculate the VAT implications for both the buyer and the seller if the seller (Ireland CC) is a registered vendor, which makes taxable supplies only. In your answer, state when output tax must be declared and when input tax may be claimed.</td>
<td>5</td>
</tr>
<tr>
<td>(c) Assume that Ireland CC (the seller) is a registered vendor. Discuss and calculate the VAT implications for both the buyer and seller, if the seller (instead of ABC Bank) financed the loan (i.e. the buyer will pay the balance in monthly instalments of R5,000 (excluding finance charges). Only one instalment of R5,000 has been paid up to date). Where applicable, specifically state in your answer when output tax must be declared and when input tax may be claimed.</td>
<td>5</td>
</tr>
<tr>
<td>(d) Assume now that Ireland CC is a registered vendor, which makes 60% taxable supplies and 40% exempt supplies. Calculate and discuss the VAT implications (ignore the time of supply) for Ireland CC if the building had originally been purchased by it from a vendor for R900,000 (including VAT of R110,526). Ireland CC used 60% of the building for taxable supplies for a few years and is now selling it to Wallis (Pty) Ltd for R1,500,000 (including VAT).</td>
<td>4</td>
</tr>
</tbody>
</table>
QUESTION 9 – SUGGESTED SOLUTION

PART 1

Query 1

- **Pasta-cutting machine**
  Yes. Although this machine was purchased prior to the introduction of VAT, Bellissimo (Pty) Limited is still required to levy VAT on the selling price as it constitutes the supply of “goods” (as defined) by a vendor in the course or furtherance of its enterprise (the machine being an enterprise asset).

- **Water cooling machine**
  No. The water cooling machine constitutes the supply of “entertainment” to its employees and Bellissimo (Pty) Limited would not have been entitled to an input tax credit when it acquired the water cooler (section 17(2)(a)). In terms of section 8(14) Bellissimo (Pty) Limited is not required to levy VAT on the selling price when it disposes of the water cooler, because the input tax credit was denied on acquisition. This is referred to as a non-supply.

- **Delivery van**
  Yes. Bellissimo (Pty) Limited would have been entitled to an input tax credit when it acquired the delivery van as it is not a “motor car” (as defined). On the disposal of the delivery van Bellissimo (Pty) Limited is required to levy VAT on the selling price as it constitutes the supply of “goods” (as defined) by a vendor in the course or furtherance of its enterprise (the delivery van being an enterprise asset).

Query 2

**Journal Entry 1 – during February 2017**

<table>
<thead>
<tr>
<th>Dr</th>
<th>Amount</th>
<th>Cr</th>
<th>Amount</th>
</tr>
</thead>
<tbody>
<tr>
<td>Motor Cycle</td>
<td>R 160 000</td>
<td>Creditor / Bank</td>
<td>R 182 400</td>
</tr>
<tr>
<td>Input tax account</td>
<td>R 22 400</td>
<td></td>
<td></td>
</tr>
</tbody>
</table>

Being the purchase of a motor cycle.

Note that the motor cycle is not a “motor car” as defined because it only has two wheels (a “motor car” as defined must have three or more wheels). Therefore, Buildex (Pty) Limited is entitled to an input tax credit of R22 400 on purchasing the motor cycle, being acquired for the purpose of making taxable supplies.

**Journal Entry 2 – 31 March 2017**

<table>
<thead>
<tr>
<th>Dr</th>
<th>Amount</th>
<th>Cr</th>
<th>Amount</th>
</tr>
</thead>
<tbody>
<tr>
<td>Salaries and wages</td>
<td>R 118</td>
<td>Output tax account</td>
<td>R 118</td>
</tr>
</tbody>
</table>

Being the output tax on the deemed supply of the fringe benefit (free use of the motor cycle) provided to the site supervisor.

Note that the free use of the motor cycle by the site supervisor is a Seventh Schedule fringe benefit and a deemed supply arises in the hands of Buildex (Pty) Limited (section 18(3)). Buildex (Pty) Limited should account for output tax of R118 for each month that it provides this benefit.

\[(R182 400 \times 100/114 = R160 000 \times 0,6\% \times 14/114 \times 1 \text{ month}) = R118\]
**QUESTION 9 – SUGGESTED SOLUTION (continued)**

**Commentary:**

Note that a journal entry should have a date, debit and credit account(s) and a narrative. Furthermore, the journal entry should balance (total rand amount of debits should equal total credits). Note that the value of the deemed supply is based on the value per the Government Notice 2835 (that is excluding VAT). Note also that 0.6% is used as the input tax could be claimed on acquisition. When the input tax is denied on acquisition, 0.3% per month is used.

Query 3

The journal entry passed is incorrect. The correcting journal entry is:

<table>
<thead>
<tr>
<th>Date</th>
<th>Dr</th>
<th>Cr</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>Security expenditure</td>
<td>Input tax account</td>
</tr>
<tr>
<td></td>
<td>553 R</td>
<td>553 R</td>
</tr>
</tbody>
</table>

Being the reversal of the notional input tax credit incorrectly claimed on the purchase of the guard dogs.

The assumption is that the dogs were previously owned and used. The dogs were trained as they are ready to perform the duties as guard dogs.

A notional input tax credit cannot be claimed on the purchase of the watchdogs, as the definition of “second-hand goods” in section 1(1) of the VAT Act specifically excludes animals.

Query 4

**TO:** Sardine Spotters (Pty) Limited  
**FROM:** Myself  
**DATE:** 18 February 2017  
**RE:** Possible input tax credits (memorandum format)

The “fourteen-seater” microbus is a “motor car” as defined in section 1(1), because it is not suitable for carrying more than sixteen persons. The input tax credit of R21 000 can therefore not be claimed (section 17(2)(c)). (2)

Although the one-ton bakkie was not constructed wholly or mainly for the carriage of passengers, it was however immediately converted for this purpose. It therefore falls within the definition of a “motor car” (section 1(1), definition of motorcar). (1)

However, the definition of a “motor car” excludes a game viewing vehicle, which can transport seven or more passengers and is exclusively used for game viewing in national parks, game reserves, sanctuaries or safari areas. (1)

It would seem that sardine viewing (fish viewing) is not game viewing. It further seems that the South Coast would not be a qualifying area, not being a national park, game reserve, sanctuary or a safari area. It follows therefore that the converted “sardine-viewing bakkie” is not excluded from the definition of “motor car”. The input tax credits of R17 360 and R1 820 can therefore not be claimed (section 17(2)(c)). (3)
Commentary:
You were asked to provide your answer in memorandum format (to, from, date and subject). We recommend that you use a memorandum format whenever you are asked to advise a client, as this is what you would do in practice. Also, note that you had to advise the client with supporting reasons. This query tested the definition of “motor car”. The suggested solution illustrates the thought process you should follow in arriving at the answer. Ensure that you know this definition well.

Query 5

Your discussion should include the following:

- Pedantic (Pty) Ltd accounts for VAT on the invoice basis and originally claimed an input tax deduction of R4 200 in the tax period 1 January 2016 to 29 February 2016 as the goods would be used to make taxable supplies, but had not paid the full consideration by 28 February 2017 (being twelve months after the tax period in which the input tax was claimed), therefore output tax should be accounted for as follows: tax fraction of the unpaid consideration, being R6 840 x 14/114 = R840 in its 1 March 2017 to 30 April 2017 tax period (i.e. the tax period following the expiry of the twelve months) (section 22(3)).

Commentary:
The R27 360, which Pedantic (Pty) Limited had paid on 29 February 2016, included VAT of R3 360. VAT on the R6 840 unpaid consideration had to be recorded, namely R840 (being R4 200 – R3 360). Again you were asked to discuss the VAT consequences, supported by calculations where applicable. You therefore had to apply the theory to the set of facts. You were specifically asked to address the time of supply.

Query 6

The receipt of an indemnity payment under a contract of insurance is a deemed supply (section 8(8)) and output tax must be accounted for by the insured. However, in terms of the proviso to section 8(8) no deemed supply arises in respect of an indemnity payment received for the total reinstatement of goods stolen when an input tax deduction was denied on acquisition.

New Look (Pty) Ltd would have been denied an input tax deduction on the acquisition of the motor car (given that this is a “motor car” as defined). Thus, no deemed supply arises in respect of the R85 000 received for the motor car.

A deemed supply will arise in respect of the R34 200 received for the stolen merchandise. New Look (Pty) Ltd must account for output tax of R4 200 (14/114 x R34 200) in the tax period during which the indemnity payment is received.
Commentary:

No deemed supply arises in terms of section 8(8) when a payment is received for the total reinstatement of goods AND an input tax deduction was denied on acquisition. Note that both requirements must be satisfied.

Remember to address the time of supply!

PART 2

(a) **Seller**: (Ireland CC): No VAT implications (not a vendor for VAT purposes).

**Buyer**: (Wallis (Pty) Ltd): A notional input tax deduction may be claimed.

Input tax is claimable on the earlier of the date of registration or the date of payment of any consideration (section 9(3)(d)). However, the claim is limited to the extent of payment of the purchase price and then only if the fixed property has already been registered in the name of Wallis (Pty) Ltd.

The full consideration will be paid to the seller upon registration, being the 10% deposit paid to the lawyers and the remaining 90% financed by ABC Bank (section 16(3)(a)(ii)(aa) and (bb)).

The notional input tax is calculated as $\frac{14}{114}$ x lesser of cost price or open market value, thus $R1500000 \times \frac{14}{114} = R184211$.

However, the buyer makes both taxable (30% + 50% = 80%) and exempt (20%) supplies. Thus $R147369$ ($R184211 \times 80\%$) may be claimed by the buyer upon registration.

(b) **Seller**: $R1500000 \times \frac{14}{114} = R184211$ output tax.

The time of supply is the earlier of the date of registration in the deeds office or the date of any payment received for the supply (section 9(3)(d)), but output tax should only be accounted for to the extent that payment of the consideration has been received (section 16(4)(a)(ii)). The deposit paid to the lawyers ($R150000$) together with the remainder of the purchase price ($R1350000$) will be transferred to the seller upon registration, thus the seller must declare the output tax upon registration of the property in the buyer’s name.

**Buyer**: The buyer may in total only claim 80% (taxable supplies) of the output tax reflected by the seller: namely $R184211 \times 80\% = R147369$ (section 17(1)).

The input tax may be claimed to the extent that payment of the consideration has been made (section 16(3)(a)(ii)(aa)). The full consideration will be paid to the seller upon registration, being the 10% deposit paid to the lawyers and the remaining 90% financed by ABC Bank. Thus the full $R147369$ may be claimed by the buyer upon registration.

Note that the finance charges payable to ABC Bank carries no VAT as this relates to financial services (exempt supply (section 12(a))).

Please note that s 16(3)(a)(ii)(bb)(A) makes specific reference to fixed property where the provisions of section 9(3)(d) apply.
(c) As in (b) but, accounting for the output and input tax will occur in the tax period in which payment takes place (section 9(3)(d)) but only to the extent that payment takes place (sections 16(3)(a)(ii)(aa) and 16(4)(a)(ii)), namely:

- On payment of the deposit by the lawyers to Ireland CC: R150 000 x 14/114 = R18 421 (1)
  The 10% deposit was payable to the lawyer. The payment of the deposit is not regarded as a payment until the deposit is applied as part-payment or forfeited. The lawyers only paid the full purchase price over to Ireland upon registration.

- On capital repaid up until now: R5 000 x 14/114 = R614 (1)
  Thus, up until now, the seller must have accounted for output tax of (R18 421 + R614) R19 035, while the buyer may have claimed input tax amounting to R19 035 x 80% = R15 228. (1)
  Note that the finance charges levied by the seller, carries no VAT as this relates to financial services (exempt supply (section 12(a)). (1)

(d) Ireland CC must still account for output tax on the total selling price, namely 14/114 x R1 500 000 = R184 211 (section 8(16)). (1)
  A deemed input tax may be claimed in terms of section 16(3)(h) at the lesser of the adjusted cost and current open market value multiplied by the tax fraction. (1)
  Thus, use the original cost price including VAT (adjusted cost). Input tax of R900 000 x 14/114 x 40% (Note) = R44 210 may therefore be claimed. (See formula in section 16(3)(h): A x B x C.)
  On purchase only an input tax deduction of R66 316 (R900 000 x 14/114 x 60%) could have been claimed. (1)

Note: Use the non-taxable %. The reason for this is when the building was bought, only 60% input tax could have been claimed. But when the building is sold, output tax has to be raised on 100% of the selling price. But remember only 60% input was originally allowed, so now an adjustment for 40% in respect of the non-taxable supply portion that Ireland was never allowed as an input tax claim and they now have to raise output on it. (4)

Commentary:

This part of the question illustrated the VAT implications of fixed property transactions. Note that the building could not have been sold as a going concern as the question specifically states that no rental agreement existed at the date of the sale (thus not an income-earning activity).

Parts (b) and (c)
Although a time of supply rule exists (section 9(3)(d)), the input and output tax may only be accounted for to the extent that payment of the consideration has been made or received.

Part (d)
Remember:
- Section 8(16) that states that the sale of the building is fully (100%) taxable: and
- the section 16(3)(h) adjustment!

If s 8(16) is read, it states that the subsequent supply of any goods used partly for taxable supplies is deemed to be made wholly in the course or furtherance of this enterprise. Thus output VAT needs to be raised on the full R1 500 000. However, a deemed input tax may be claimed in terms of s 16(3)(h) - that is the 40% non-taxable supply portion. So the effect is as follows:

<table>
<thead>
<tr>
<th>Event</th>
<th>Formula</th>
</tr>
</thead>
<tbody>
<tr>
<td>when property was purchased</td>
<td>60% input tax claimable</td>
</tr>
<tr>
<td>when property sold</td>
<td>100% output tax payable</td>
</tr>
<tr>
<td>when property sold</td>
<td>40% input tax adjustment</td>
</tr>
</tbody>
</table>

Note: The non-taxable portion is taxed in the sale but allowed only 60% input tax in the purchase. Thus, when there is a deemed adjustment, a 40% input tax adjustment is allowed.
Luxurious Living (Pty) Ltd (“Luxurious Living”) is a private resident company and trades as a property developer. The company is registered on the invoice basis as a vendor for purposes of Value-Added Tax and has a 2-monthly tax period. The next tax period ends on 31 January 2017.

When developing properties, the company only trades with other VAT vendors, unless otherwise stated. Once a project is completed, the company moves all fixed assets (for example building equipment) to the next development as and when they decide on a new project.

Eighteen months ago, the company commenced with the development of a townhouse complex on the East Coast, consisting of 20 similar units. A sectional title register was opened in respect of the complex. The complex was completed in September 2016 at a cost of R12 million. The land was purchased from a non-vendor in 2013 for R1 million and the company paid transfer duty of R12 000 two months after they signed the purchase agreement.

In spite of an intensive marketing campaign during October and November 2016, they could not sell any of the units and on 1 December 2016, when the open market value of the town house complex was R20 million, decided to furnish 12 units and rent it to different tenants as holiday accommodation, for periods not exceeding three weeks at a time. The first unit was let on 15 December 2016. The letting of all units was done by a local estate agent. The remaining 8 units were let to local tenants with 12-month rental contracts (unfurnished). The decision to change the intention in respect of the use of the dwellings is permanent and not temporary of nature. Luxurious Living incurred the following expenses during December 2016 and January 2017:

(All amounts include VAT where applicable. SARS approved that, where necessary, input tax may be apportioned using the floor area as a basis.)

<table>
<thead>
<tr>
<th>Cost</th>
<th>R</th>
</tr>
</thead>
<tbody>
<tr>
<td>Cost of furnishing 12 units</td>
<td>912 000</td>
</tr>
<tr>
<td>Payment of rates and taxes</td>
<td>16 000</td>
</tr>
<tr>
<td>Legal cost for drafting contracts for permanent tenants</td>
<td>5 130</td>
</tr>
<tr>
<td>Hiring security from a security firm for the townhouse complex</td>
<td>3 648</td>
</tr>
<tr>
<td>Salaries of 3 permanent staff members to maintain the gardens</td>
<td>13 680</td>
</tr>
</tbody>
</table>

An amount of R15 000 was received from the insurance company in respect of the theft of furniture in one of the holiday apartments.

On 6 February 2017 Luxurious Living (Pty) Ltd received the following rent statement from the estate agent in respect of December 2016 and January 2017 (where applicable, amounts include VAT):

<table>
<thead>
<tr>
<th>Income</th>
<th>R</th>
</tr>
</thead>
<tbody>
<tr>
<td>Rent collected from holiday accommodation</td>
<td>239 400</td>
</tr>
<tr>
<td>Rent collected from permanent tenants</td>
<td>51 300</td>
</tr>
<tr>
<td><strong>Total Income</strong></td>
<td><strong>290 700</strong></td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>Expenses</th>
<th>R</th>
</tr>
</thead>
<tbody>
<tr>
<td>Collection commission – holiday accommodation</td>
<td>23 940</td>
</tr>
<tr>
<td>Collection commission – permanent tenants</td>
<td>5 130</td>
</tr>
<tr>
<td>Maintenance paid for 12 holiday units</td>
<td>4 104</td>
</tr>
<tr>
<td>Cleaning of holiday units (servants - wages)</td>
<td>60 000</td>
</tr>
<tr>
<td>Bank charges</td>
<td>1 140</td>
</tr>
<tr>
<td>Electricity and water (holiday accommodation)</td>
<td>15 960</td>
</tr>
<tr>
<td>Electricity and water for common property of the complex</td>
<td>13 680</td>
</tr>
<tr>
<td>Cheque returned as unpaid from the bank in respect of a holiday tenant that has since returned to Australia – address unknown. (It was decided to write the amount off as a bad debt.)</td>
<td>5 700</td>
</tr>
<tr>
<td><strong>Total Expenses</strong></td>
<td><strong>129 654</strong></td>
</tr>
</tbody>
</table>

Amount deposited in the bank account of Luxurious Living (R290 700 – R129 654) | 161 046
QUESTION 10 (continued)

REQUIRED | Marks
--- | ---
Calculate the VAT payable by Luxurious Living or to be refunded by SARS to the company for the tax period ended 31 January 2017. You must address each item separately and where no input tax credit is available or no output tax is payable, give a reason. You may assume that all VAT in respect of the tax periods ended before December 2016 was dealt with correctly. (Round off all amounts to the nearest Rand). | 20

PART B | 8 marks
For the month of February 2017, Luxurious Living (Pty) Ltd allowed the construction manager the free use of one of the holiday apartments. The apartment is normally rented out for R200 (including VAT) per day. The manager (normally stationed in Johannesburg) was permitted to use one of the motor cars, as defined in section 1(1) of the VAT Act, of the company to travel to the holiday apartment on the East Coast. He was also allowed to use the petrol card of the company, but only to purchase fuel, during his visit.

REQUIRED | Marks
--- | ---
In your capacity as accountant of Luxurious Living, advise the Managing Director of the VAT implications for the company regarding the free use of the apartment, the use of the company car and petrol card (no calculations are required). | 8

PART C | 12 marks
On 28 February 2017 (financial year-end), the abridged statement of financial position of Luxurious Living (Pty) Limited was as follows:

R

EQUITY AND LIABILITIES

200 Ordinary shares of R1 each | 200
Loan account of director | 14 800 000
Retained earnings | 88 203

14 888 403

ASSETS

Fixed property (residential) at cost (units 1-8) | 5 200 000
Fixed property (holiday units) at cost (units 9-20) | 7 800 000
Furniture (units 9 - 20) (at tax value) | 780 000
Building equipment and trucks (at tax value) | 561 403
Motor cars (as defined in section 1(1) of the VAT Act) (at tax value) | 547 000

14 888 403

On 1 March 2017 the company received an offer from AB Sulliman (not a VAT vendor) to purchase the shares and the loan account of the director for R26 million. A condition of the offer is that Mr Zee (majority shareholder of Luxurious Living (Pty) Ltd and not a VAT vendor) will purchase the furniture, building equipment, trucks and motor cars at their open market value. The transaction must be concluded by 31 March 2017. Mr Sulliman will continue to use the 20 units as before.
<table>
<thead>
<tr>
<th>REQUIRED</th>
<th>Marks</th>
</tr>
</thead>
<tbody>
<tr>
<td>1. Explain to Mr Sulliman (purchaser) the VAT implications for him regarding the purchase of the shares and loan account, should the offer be accepted.</td>
<td>2</td>
</tr>
<tr>
<td>2. Explain the VAT implications for Luxurious Living (Pty) Ltd should the offer be accepted.</td>
<td>4</td>
</tr>
<tr>
<td>3. Explain the VAT implications for Mr Zee regarding the offer.</td>
<td>1</td>
</tr>
<tr>
<td>4. Assume that Mr Sulliman registers as a VAT vendor prior to concluding the transaction and purchases all twenty units, including the furniture (not the shares and loan account) for R26 million. You may further assume that the transaction will comply with all the requirements of section 11(1)(e) of the VAT Act i.e. the purchase will be that of a going concern. The next two-monthly tax period of Mr Sulliman ends on 31 March 2017. After purchasing the twenty units Mr Sulliman will continue to use the property as was the case with Luxurious Living (Pty) Ltd. Mr Sulliman has no other business activities. Explain the VAT implications of the transaction for Mr Sulliman, also addressing the time of supply in your answer. Support your answer with calculations.</td>
<td>5</td>
</tr>
</tbody>
</table>
QUESTION 10 - (SUGGESTED SOLUTION)

PART A

Output tax

Rent collected from holiday accommodation (14/114 x R239 400 – section 1(1), definition of commercial accommodation)  
29 400 (1)
Rent collected from permanent tenants (residential accommodation – exempt – section 12(c))  
- (1)
Deemed output tax – insurance pay-out  
(14/114 x R15 000 – section 8(8))  
1 842 (1)
Section 18(1) change of use:  
Deemed output tax: (R20 million (OMV) x 40% (8/20 units)) x 14/114 (note )  
982 456 (2)  
1 013 698

Input tax

Cost of furnishing 12 units (14/114 x R912 000)  
112 000 (1)
Payment of rates and taxes (zero rated – section 11(2)(w))  
- (1)
Legal cost (applicable to residential accommodation which is an exempt supply, therefore not part of the enterprise – section 1(1), definition of enterprise, par (c)(iii)(v))  
- (2)
Hiring of security (60% (taxable supplies – holiday apartments) x 14/114 x R3 648)  
269 (1)
Salaries of garden staff (remuneration not part of an enterprise – section 1(1), definition of an enterprise, par c(iii)(v))  
- (1)
Collection commission – holiday accommodation (14/114 x R23 940)  
2 940 (1)
Collection commission – permanent tenants (residential)  
- (1)
Maintenance (14/114 x R4 104)  
504 (1)
Cleaning of holiday units (remuneration not part of an enterprise)  
- (1)
Bank charges (14/114 x R1 140 x 60% (12/20))  
84 (1)
Electricity and water (holiday accommodation) (14/114 x R15 960)  
1 960 (1)
Electricity and water (common property) (14/114 x R13 680 x 60%)  
1 008 (1)
Bad debt (14/114 x R5 700) (section 22(1))  
700 (1)

119 465

VAT payable (R1 013 698 – R119 465)  
894 233 (1)

Note:

The decision to change the intention in respect of the use of the dwellings is permanent and not temporary of nature, therefore section 18B is not applicable.

If the change of intention was temporary section 18B of the VAT Act would have been applicable, in which case a change of use would only have to be accounted for in terms of section 18B in respect of the 8 units supplied as accommodation in a dwelling under an agreement for the letting and hiring thereof at the earlier of:

- A period of 36 months after the conclusion of the rental agreement; or
- The date that the change becomes permanent.

Note that the 12 units used for holiday accommodation are still used to make taxable supplies, therefore no change in use arises in respect of the 12 holiday units.
QUESTION 10 - (SUGGESTED SOLUTION) (continued)

PART B

Holiday apartment
This is a fringe benefit, therefore section 18(3) applies. (1)
The free use of the apartment by the construction manager (an employee) will be considered as “enter-
tainment” (section 1(1), definition of entertainment). (1)
No “deemed” output tax is payable on the fringe benefit provided as the holiday accommodation consti-
tutes the supply of “entertainment” and is excluded from the “deemed” supply provisions of section 18(3). (1)

Free use of company car
The free use of a company car is a fringe benefit, therefore section 18(3) applies. (1)
The company must pay a deemed output tax at the end of the tax period (March 2017) based on the
determined value of the car (excluding VAT and finance charges) x 0,3% (input tax denied on motor
cars, as defined in section 1(1) of the VAT Act) (section 17(2)(c)) x 14/114 (tax fraction) for each month
or part of a month that the construction manager had the use of the company car, therefore one month.
(Section 18(3) and the Government Gazette no 2835 of November 1991). (3)

Petrol card
Deemed output tax is not payable on the use of the petrol card as petrol is zero-rated and therefore
excluded from the provisions of section 18(3). (1)

PART C

1. VAT implications for Mr Sulliman

The purchase of the shares and the loan account is an exempt financial service (sections 2(1)(c)
and (d) and section 12(a)) and therefore no VAT is payable by Mr Sulliman.
Had any VAT been payable, Mr Sulliman would not have been able to claim the input tax as he is not
a VAT vendor. (2)

2. VAT implications for Luxurious Living (Pty) Ltd

- Selling the building equipment, trucks and furniture to Mr Zee:

Luxurious Living and Mr Zee are connected persons. (1)
Section 10(4):
Where-
(a) a supply is made by a person for no consideration or for a consideration in money which is
less than the open market value of the supply; and
(b) the supplier and respondent are connected persons in relation to each other; and
(c) if a consideration for the supply equal to the open market value of the supply had been
paid by the recipient (Mr Zee), he would not have been entitled under section 16(3) to
claim an input tax deduction in respect of that supply,
the consideration in money for the supply shall be deemed to be the open market value of the
supply: Provided that this subsection shall not apply to the supply of a benefit or advantage of
employment contemplated in section 18(3).

As the building equipment, trucks and furniture were sold at open market value, the fact that
they are connected persons has no effect (section 10(4)).
The selling price must include VAT at 14%.
Thus 14% must be accounted for as output tax in the tax period ending 31 March 2017. (1)
QUESTION 10 - (SUGGESTED SOLUTION) (continued)

- **Selling the motor cars:** Input tax on motor cars, as defined in section 1(1) of the VAT Act, is prohibited in terms of section 17(2)(c) and therefore no output tax will be levied on the sale of the motor cars. (1)
- **Selling the shares and loan account:** Selling the shares and loan account is an exempt financial service (sections 2(1)(c) and (d) and section 12(a)) therefore no output tax will be levied. (1)

3. VAT implications for Mr Zee

- The purchase price of the building equipment, trucks and furniture includes VAT at 14%.
- Purchasing the motor vehicles has no VAT implications as no VAT is charged.
- Mr Zee will therefore only pay VAT on the purchase of the building equipment, trucks and furniture but as Mr Zee is not a VAT vendor, he will not be able to claim any input tax. (1)

4. Purchase of going concern

- As the purchase is that of a going concern it will be at zero rate, therefore input tax is paid at zero percent equaling Rnil, therefore no input tax credit claimed. (1)
- The supply of the property, which were applied partially for taxable and partially for non-taxable purposes is deemed to be made wholly (100%) in the course of the enterprise and is therefore fully taxable at zero rate – refer section 8(16).
- Mr Sullman will use the property partially for taxable and partially for non-taxable (exempt) supplies, therefore a section 18A adjustment must be accounted for as follows: (1)
  - Mr Sullman should account for a deemed output tax in respect of the 8 units purchased as residential units on R10 400 000 (R26 million x 40%). (1)
  - This should be done in the tax period ending on 31 March 2017. (1)
  - The deemed output tax should be calculated as:
    - 14% x (R26m x 40%) = R1 456 000 (1)

**Note:**
Refer to SILKE 32.29.2.
This explains the adjustments to the supplies of going concerns (section 18A) and there are specific rules relating to more than 50% or less than 50% taxable usage for the purpose of the supply of going concerns. Basically the purchaser must raise output tax in accordance with section 18A of the VAT Act, based on the percentage of the non-taxable use of the purchaser.
QUESTION 11

You are the senior tax partner in a local audit firm, with international ties. Once a month the firm publishes a newsletter, in which you have a tax column. In this column, you supply answers to various tax queries received from different clients. You have received the following queries during the month and have to answer the questions set to you.

Aero Limited

Aero Limited, a registered vendor, sent you the following query:

Aero Limited’s training division presented a one-day training session for the employees of Bar One Limited (not a connected person of Aero Limited). This training session was presented as a profit-making venture and a fee of R800 per delegate was charged (fifty delegates attended). A caterer provided early morning coffee, morning and afternoon teas and a luncheon. He was paid R3 420 (R3 000 plus R420 VAT) for his catering services. The following journal entries recorded these transactions in Aero Limited’s books:

Journal 1:
   Bar One Limited (debtor)                      R 40 000,00
   To Training income                           40 000,00
   Being fifty delegates on the training session at a fee of R800 each.

Journal 2:
   Catering expenses - training                3 420,00
   To Cash                                     3 420,00
   Being the catering expenses incurred in running the above training session.

REQUIRED

Indicate, with reasons, to Aero Limited whether these journal entries are correct or not and, if not, provide the correcting journal entries. Show all your calculations, where necessary.

New Look CC

New Look CC, a dealer in antiques, is registered for VAT purposes and it submits returns on a monthly basis. During March 2017, it purchased an antique pocket watch from Mrs Caravan (a resident of the Republic) for R11 400 cash. Mrs Caravan is not a registered VAT vendor. During May 2017 a dealer in the United Kingdom agreed to purchase the pocket watch for R14 000 from New Look CC and it was exported to London during this tax period.

REQUIRED

Indicate to New Look CC the VAT implications in respect of this export.
QUESTION 11  (continued)

Crunchie Limited

Crunchie Limited (a category A VAT vendor – tax periods end on the last day of January, March, May, etc.) bought a new manufacturing machine on 1 March 2017 for R239 400 (including VAT) and insured it on the same day with Excellent Insurance at a monthly premium of R6 156 (including VAT). Crunchie Limited is also insured against other risks relating to its business, and has been paying a monthly premium of R570 (including VAT) in this regard for the past year.

On 21 March 2017, the premises of Crunchie Limited were burgled and the new machine as well as a fax machine were stolen. Crunchie Limited submitted a claim to the insurance company, which on 31 March 2017 paid out R204 000 cash in respect of the new machine and replaced the fax machine with a similar model at a cost of R1 500 (including VAT).

REQUIRED

Discuss the VAT implications resulting from the above for Crunchie Limited (the company only makes taxable supplies) in respect of the tax period, which ended on 31 March 2017.

Marks

5

Lunch Bar (Pty) Limited

Lunch Bar (Pty) Limited, a registered VAT vendor, operates a bookshop. The company wishes to increase its turnover by selling its stock during the next month at a 10% discount.

REQUIRED

Indicate to Lunch Bar (Pty) Limited what the VAT consequences thereof will be. Support your answer by way of a journal entry (using a normal selling price of R68.40 (including VAT) before the discount).

Marks

3

Chartered Accountant Tex

Chartered Accountant Tex (a registered VAT vendor in Cape Town) went on a business trip to George. He spent a total of 45 days in the local Tempo hotel, which charged a fee of R400 (excluding VAT) per day (room only). He further enjoyed all his meals in the hotel and the total cost for meals during his stay amounted to R6 840 (including VAT). Chartered Accountant Tex is in possession of separate tax invoices in respect of all of these costs.

REQUIRED

Calculate the VAT input, which Chartered Accountant Tex would be able to claim in respect of the above mentioned business trip.

Marks

3

Smartie and Rascal Partnership

Mr Smartie and Mr Rascal (equal partners) sell manufacturing equipment at the standard rate of VAT (14%). The partnership is registered for VAT and accounts for VAT on a monthly basis by using the invoice basis. Previously there were three equal partners, but three months ago, Mr Jelly Tot decided to start his own business and left the partnership.
QUESTION 11 (continued)

At the end of their financial year (28 February 2017), the partnership made an accounting provision for doubtful debts of R11 400 and at the same time, they wrote off bad debts amounting to R5 700 for accounting purposes. The outstanding balances of these debts arose when Mr Jelly Tot was still a partner.

**REQUIRED**

| Discuss the VAT implications of these two accounting entries for the Smartie and Rascal Partnership. | 3 |

**Kit Kat (Pty) Ltd**

Kit Kat (Pty) Ltd used to make taxable and exempt supplies. On 31 December 2014, it had purchased a computer system for R61 560 (including VAT). This computer system was used to maintain the records of the taxable (65%) and exempt (35%) supplies. The previous month they disposed of the portion of their business that made the exempt supplies and now only make taxable supplies (100%). This change of use of the computer system occurred at the end of Kit Kat (Pty) Ltd’s two-month period ending 31 December 2016. Its open market value at the time of change was R34 000. Its book and tax values at this date were R36 000. Kit Kat (Pty) Ltd’s year of assessment ends on the last day of February. The open market value of the computer system at 28 February 2017 was R30 000, while its book and tax values at this date were R33 000. Kit Kat (Pty) Ltd always ends its tax periods on the last day of the month.

**REQUIRED**

| Discuss the resulting VAT consequences now that the computer system is used solely to maintain the records of taxable supplies. | 5 |

**Milky Bar CC**

On 1 April 2017, Milky Bar CC signed the documents for the acquisition of a two-storey building from a non-registered person, which will be let to various tenants. The ground floor of the building will be let to two different tenants, one operating a petrol station (including sundry sales of motor vehicle related consumables) combined with a workshop, and the other acting as a greengrocer. The first floor consists of four residential flats that will be let as such to four different families.

The purchase price of the building was equal to its open market value of R3 990 000 and a deposit of R399 000 was payable (into a trust) to the attorneys of the seller (who would also handle the transfer of the property). On registration of the property into the name of the corporation (this was effected on 15 May 2017), an amount of R276 400 was payable by way of transfer duty. The outstanding balance of the purchase consideration is payable by way of six monthly instalments of R598 500 each, effective from the date of registration.

The financial director of the corporation did a calculation of the rentals that should be received from this property during the first year of trading: This calculation was done by referring to existing rental contracts.

<table>
<thead>
<tr>
<th>R</th>
</tr>
</thead>
<tbody>
<tr>
<td>Petrol station</td>
</tr>
<tr>
<td>Workshop</td>
</tr>
<tr>
<td>Greengrocer</td>
</tr>
<tr>
<td>Residential flats</td>
</tr>
</tbody>
</table>

1 180 000
QUESTION 11 (continued)

The Commissioner has indicated that he will accept the above turnover figures for the purposes of making any reasonable apportionment.

In the budgets, as prepared by the financial director, provision has also been made for interest payable on a loan that will be used to finance the acquisition of the property. Such amount of interest in respect of the first year of assessment will amount to R160 000.

<table>
<thead>
<tr>
<th>REQUIRED</th>
<th>Marks</th>
</tr>
</thead>
<tbody>
<tr>
<td>(a) Indicate, with reasons, whether Milky Bar CC is obliged to register as a VAT vendor.</td>
<td>1</td>
</tr>
<tr>
<td>(b) Indicate, with reasons, whether the respective tenants themselves are making standard rated, zero-rated or exempt supplies. Assume for this part of the question, that all the tenants are registered vendors where applicable.</td>
<td>3</td>
</tr>
<tr>
<td>(c) Indicate, with reasons, whether Milky Bar CC will be entitled to an input tax credit in respect of the acquisition of the property and, if so, indicate the extent (amount) thereof as well as the time of claiming such credit.</td>
<td>9</td>
</tr>
<tr>
<td>(d) Indicate, with reasons, whether Milky Bar CC will be entitled to an input tax credit in respect of the interest charged in this regard.</td>
<td>1</td>
</tr>
</tbody>
</table>
QUESTION 11 - SUGGESTED SOLUTION

Aero Limited

Query 1

Please note that the correct journal entry was not required - the correcting journal entry was required. This could have been done in two ways - either record the correction or reverse the incorrect entry and put through the correct journal entry.

Neither journal entries are correct since the Value-Added Tax relating to these transactions were not accounted for:

- the training fee charged by Aero Limited is a “taxable supply”, being the supply of a service in the course or furtherance of its enterprise. It is not the supply of an “educational service”. (1)
- although the catering costs have been incurred for the purposes of “entertainment”, Aero Limited is entitled to an input tax credit in terms of section 17(2)(a)(iv), being a meal or refreshment supplied by the client as the organiser of a seminar or training session where it will be consumed during such training session and the cost thereof will be covered by the fees charged. (1)

The correcting journal entries are as follows:

**Correcting journal 1:**

<table>
<thead>
<tr>
<th>Description</th>
<th>Amount</th>
</tr>
</thead>
<tbody>
<tr>
<td>Training income</td>
<td>R 4 912,28</td>
</tr>
<tr>
<td>Output tax account</td>
<td>R 4 912,28</td>
</tr>
<tr>
<td>Being output tax payable on training fees (14/114 x R40 000)</td>
<td>(1)</td>
</tr>
</tbody>
</table>

**Correcting journal 2:**

<table>
<thead>
<tr>
<th>Description</th>
<th>Amount</th>
</tr>
</thead>
<tbody>
<tr>
<td>Input tax account</td>
<td>R 420,00</td>
</tr>
<tr>
<td>Catering expenses – training</td>
<td>R 420,00</td>
</tr>
<tr>
<td>Being input tax claimable on catering costs incurred in presenting the training session. (14/114 x R3 420)</td>
<td>(1)</td>
</tr>
</tbody>
</table>

New Look CC

The question required you to indicate the VAT implications in respect of the antique pocket watch being exported. Although the word “indicate” is used, the requirement in this query is to supply an explanation or reasons (for which marks are awarded) for the VAT treatment since the word “indicate” is expanded on by the words “VAT implications”. The answer would also, of necessity, have to include two very important aspects, namely, the value of the consideration and the time or period in which the output tax must be accounted for or the input tax claimed.

There is no zero-rating for exported second-hand goods if purchased from a non-vendor (assuming that the notional input tax credit was claimed when the goods were paid for (March 2017)). (1)

The consideration for the supply is deemed to be equal to the purchase price of the goods to New Look CC (not the actual selling price). Thus, output tax of R1 400 (14/114 x R11 400) must be accounted for. (1)

The time of accounting for the output tax will be the tax period ending May 2017. (1)

Please note the following (for which no marks were awarded): The purchase of the pocket watch (second-hand goods) from a non-vendor means that New Look CC (registered as a vendor) should have claimed a notional input tax deduction of R1 400 (14/114 x R11 400) during March 2017 (when the goods were paid for). As the watch was purchased for cash, the full amount of R1 400 could have been
claimed immediately (section 16(3)(a)(ii)(aa) and the definition of “input tax”). Normally the export of goods would be zero-rated (if purchased from a vendor), but as a notional input tax deduction should have been claimed as the goods were purchased from a non-vendor, zero-rating does not apply and the standard rate of tax (14%) will be applied to the selling price, limited to the original purchase price.

Crunchie Limited

The same wording was used in the required section of this query as for New Look CC except that the word “indicate” is replaced with the word “discuss”. Since both words are expanded by the words “VAT implications”, the requirement is virtually the same. Therefore, the same general comments in this regard as to how the query should be answered (explanations/ reasons/ consideration/ time) applies as for the New Look CC query. However, there is a subtle difference in that the query only requires you to discuss the VAT implications for the tax period ended on 31 March 2017. Therefore, there is no necessity to mention the time when the VAT consequences are applicable - it is given in the question, namely February/March 2017.

Input tax of R29 400 (R239 400 x 14/114) will be claimable on the new machine purchased. (1)

It can further claim input tax on the insurance premiums paid (as not life insurance):

- Machine: R6 156 x 14/114 = R756 input tax. (1)
- Other insurance: (R570 x 2 months) x 14/114 = R140 input tax. (1)

Insurance claims:

- New machine: Deemed output on amount received (payment) from insurance claim, therefore output tax is R204 000 x 14/114 = R25 053. (1)
- Fax machine: Since the stolen asset was replaced (no payment received), no deemed output will have to be accounted for (section 8(8)). (1) 

Lunch Bar (Pty) Limited

There is no indication of the time when the transactions took place. Therefore, there is no necessity to mention the time aspect in your answer.

The correct journal entry in respect of the discounted transaction is as follows:

<table>
<thead>
<tr>
<th>Bank/Debtor (R68,40 – 10%)</th>
<th>R</th>
</tr>
</thead>
<tbody>
<tr>
<td>Sales</td>
<td>61,56</td>
</tr>
<tr>
<td>Output tax account</td>
<td>7,56</td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>R</th>
</tr>
</thead>
<tbody>
<tr>
<td>Sales</td>
</tr>
</tbody>
</table>

A supply of goods (or services) is subject to VAT calculated at 14% of the value of the supply (or 14/114 of the consideration thereof - unless exempt or zero-rated) and the discount is, therefore, not treated as a separate transaction. The VAT will therefore be based on the discounted price. (1)

Please note (no marks are awarded for this explanation) that if a customer were to buy a book at the full retail price, the output tax of Lunch Bar (Pty) Limited would be R8,40 (R68,40 x 14/114). By offering a 10% discount, the company is, in fact, supplying the book at a VAT inclusive price of R61,56 (R68,40 less 10%). The output tax is R7,56 (R61,56 x 14/114). (3)
Chartered Accountant Tex

You were only required to calculate the VAT input, which may be claimed. There was no necessity to explain or give reasons for your calculation. You were not required to indicate the tax period in which the input tax could be claimed.

Chartered Accountant Tex will be able to claim the following input tax (refer to section 10(10) and the definitions of “domestic goods and services” and “commercial accommodation”).

<table>
<thead>
<tr>
<th>Item</th>
<th>Cost</th>
<th>Calculation</th>
<th>Amount</th>
</tr>
</thead>
<tbody>
<tr>
<td>Hotel costs:</td>
<td>45 x R400 x 60% x 14%</td>
<td>R1 512</td>
<td>(2)</td>
</tr>
<tr>
<td>Meals:</td>
<td>R6 840 x 14/114</td>
<td>R840</td>
<td>(1)</td>
</tr>
<tr>
<td><strong>Total</strong></td>
<td></td>
<td></td>
<td><strong>R2 352</strong></td>
</tr>
</tbody>
</table>

If you had been asked to supply an explanation/reason for the input claim you would have had to mention that the VAT on the hotel accommodation should be calculated according to the value of supply rules applying to commercial accommodation which states that if the supply is for an unbroken period exceeding 28 days, VAT should be calculated on only 60% of the value of such supply.

Furthermore, the VAT on the meals could have been claimed as input tax as the meals were supplied during the course of a business trip away from the normal workplace for at least one night and are not regarded as “entertainment”. The meals and accommodation paid for by an employer for an employee when the employee is obliged to spend any night away from the employee’s usual place of residence by reason of his/her duties of employment is specifically allowed (not prohibited) in terms of the VAT Act, see section 17(2)(a)(ii).

Smartie and Rascal Partnership

You were required to discuss the VAT implications of the two accounting entries mentioned, namely, provision for bad debts and bad debts written off.

No mark is awarded for indicating that a partnership is a vendor separate from the partners thereof, and therefore, the change in partners will not affect its VAT registration or the claiming of an input tax credit since the query only requires that the VAT implications of the two accounting entries need to be discussed. However, it should have been mentioned in the discussion to show that you understand the principle relating to partners in VAT situations.

The provision for doubtful debts will have no effect on the claiming of an input tax credit - only when the debtor is actually written off will it have a VAT effect.

The debtors written-off will result in the claiming of a deemed input tax credit, since output tax on these amounts would already have been paid (on issuing the invoices) to SARS, but now these amounts turn out to be irrecoverable: R5 700 x 14/114 = R700 deemed input tax will be claimable (section 22(1)).

Kit Kat (Pty) Ltd

This question required explanations, reasons, time and value of input tax claimable, as it required you to “discuss the VAT implications”.

The computer is now being used 100% of the time for making “taxable” supplies as opposed to 65% of the time previously. Therefore, there has been a change of use of the computer - an increase of 35% in taxable use.

A change of use adjustment is available to Kit Kat (Pty) Ltd in terms of section 18(5), as the change in use is greater than 10% and the cost of the capital goods is more than R40 000 (excluding VAT).
The adjustment is based on the computer’s open market value at 28 February 2017 (section 18(5)) of R30 000 and not on its adjusted cost (R61 560) because the open market value is the lesser amount. (1)

This lesser value must then be adjusted by the change of use from 65% to 100%. The deductible input tax amount will thus be R1 289 (R30 000 x 14/114 x (100% - 65%)). The reason for the R30 000 is because “B” in the formula in section 18(5) states that you must use the OMV at the time the increase is deemed in section 18(6) to occur. Section 18(6) deems this increase to occur on the last day of the vendor’s year of assessment. (1)

The deduction will be granted in the tax period in which the end of Kit Kat (Pty) Ltd’s year of assessment falls (section 18(6)). Kit Kat (Pty) Ltd’s year of assessment ends on 28 February 2017 and this falls in its two-month tax period ending on 28 February 2017. (1)

Please note that when Kit Kat (Pty) Ltd purchased the computer it paid VAT of R7 560 (R61 560 x 14/114). As this computer was used 65% of the time for making “taxable” supplies and 35% of the time for making “exempt” supplies, only R4 914 (R7 560 x 65%) would have been allowed as an input tax deduction. No marks were allocated for mentioning this aspect as the query only related to the change in use.

### Alternative solution based on a strict literal interpretation of the Act:

<table>
<thead>
<tr>
<th>Date Range</th>
<th>Description</th>
</tr>
</thead>
<tbody>
<tr>
<td>1/3/2016 – 31/12/2016</td>
<td>10 months at 65% taxable</td>
</tr>
<tr>
<td>1/1/2017 – 29/2/2017</td>
<td>2 months at 100% taxable</td>
</tr>
</tbody>
</table>

C in the formula: (10 months x 65%) + (2 months x 100%) ÷ 12 months = 71%

D in the formula: 65%

Change in use = 6% (71% - 65%), which is <10%, therefore no adjustment.

### Milky Bar CC

**a)** The requirement is very specific - “a discussion with reasons”.

At the commencement of April 2017 it is anticipated that the total value of taxable supplies in terms of contractual obligations in writing to be made by the corporation (standard and zero-rated) is in excess of R1 000 000 for the following twelve-month period (R420 000 + R420 000 + R172 000 = R1 012 000) and the corporation will thus be obliged to register as a VAT vendor (section 23(1)(b)) as it is carrying on an enterprise as defined. (1)

**b)** The requirement for this part of the question is the same as for part (a).

The supply of fuel levy goods will be zero-rated (section 11(1)(h)) (taxable) while other motor vehicle related supplies will be standard-rated (taxable). (1)

The workshop will be making standard-rated (taxable) supplies while the greengrocer will be making zero-rated (taxable) supplies (basic foodstuff – section 11(1)(j)). (1)

The letting of flats for residential purposes constitute exempt supplies (section 12(1)(c)). (1)
c) You are required to indicate, with reasons. Additionally, you are specifically required to indicate the amount of the input tax as well as when it can be claimed.

Milky Bar CC will be able to claim a notional input tax credit in respect of the acquisition of the property since the corporation is carrying on an enterprise as defined and is obliged to register as a vendor for VAT purposes (see part (a) above).

However, the corporation is supplying both taxable services and exempt supplies. Therefore, the input tax that it may claim will have to be apportioned according to the turnover of the corporation. While no VAT is to be charged on the acquisition of the property (purchased from a non-vendor), such property will constitute “second-hand goods” as defined in section 1(1) and the corporation could, therefore, qualify to claim a notional input tax credit on the lower of the cost or its open market value. In this case, the notional input tax credit is $14/114 \times R3\,990\,000 = R490\,000$ (refer to section 16(3)(a)(ii)(bb) and the definition of “input tax” in section 1(1)).

Such notional input tax will, however, be subject to apportionment as mentioned above.

With regard to the amount of the input tax credit that may be claimed, the following calculation must be done:

As the building will be used 86% ($R1\,012\,000/R1\,180\,000 \times 100$) for the making of taxable supplies, only $86\% \times R490\,000 = R421\,400$ can be claimed. \(1\)

The time of supply is the earlier of date of registration of the building in the name of Milky Bar CC or the date of payment (section 9(3)(d)). \(1\)

Input tax that can be claimed is further limited to the extent of payment. And then only if the fixed property has already been registered in Milky Bar CC’s name (section 16(3)(a)(ii)(aa) and (bb)) \(1\)

Therefore:

On registration the attorney will pay the deposit of $R399\,000$ over to the seller (as part of consideration) and the first instalment of $R598\,500$ will be paid to the seller. Input tax of $(R399\,000 + R598\,500) \times 14/114 \times 86\% = R105\,350$ will be claimable on date of registration. \(3\)

Thereafter for five months on the date of payment of the instalments $R63\,210$ ($R598\,500 \times 14/114 \times 86\%$) will be claimable. \(2\)

\(9\)

d) No input tax can be claimed in respect of the interest charge as this relates to an exempt supply (a financial service) - sections 2 and 12(a). \(1\)

Total 40
Big Heart Limited and Prime Land (Pty) Limited are both registered VAT vendors and are further connected persons, as defined, for the purposes of the Value-Added Tax Act. In an effort to restructure the activities of the group at the commencement of their current years of assessment, it was decided to transfer a commercial property (shopping complex) from Big Heart Limited to Prime Land (Pty) Limited. It was resolved to effect such transfer at a value of R5,7 million (including VAT), which was lower than the property’s open market value of R6,84 million. The total cost of the property for Big Heart Limited amounted to R5,13 million (including VAT).

Prime Land (Pty) Limited did not have the required cash resources to finance the acquisition, while financial institutions were reluctant to provide these funds with the knowledge that only 15% of the floor space had at that stage been taken up by potential medium-term tenants. This negated any possibility of charging the transaction with VAT at the zero rate (not a supply of a going concern) and further meant that an interest-bearing loan (2% below prime rate) had to be advanced to this company by Big Heart Limited.

At the end of the year of assessment, Prime Land (Pty) Limited had only managed to repay R285 000 (more or less 5%) of the capital amount outstanding in respect of the loan. In addition to this, the total interest charge of R484 500 in respect of this same year had also been settled. Both companies solely make taxable supplies.

<table>
<thead>
<tr>
<th>REQUIRED</th>
<th>Marks</th>
</tr>
</thead>
<tbody>
<tr>
<td>Discuss all the VAT implications arising in the current year of assessment from the above restructuring exercise for both relevant companies.</td>
<td>6</td>
</tr>
</tbody>
</table>
QUESTION 12 – SUGGESTED SOLUTION

Big Heart Limited

This company will have to account for output tax on the supply of such property as it is a registered vendor (no transfer duty, as VAT will be levied). The fact that it relates to a transaction between connected persons for a consideration lower than open market value, will not affect the consideration in money to be used as the recipient (Prime Land (Pty) Limited) will be entitled to a full input tax deduction (section 10(4)) as it solely makes taxable supplies. The total output tax eventually to be accounted for will therefore be 14/114 x R5,7 million = R700 000.

Section 16(4)(a)(ii), however, prescribes that Big Heart Limited only has to account for output tax to the extent that payment of any consideration which has the effect of reducing or discharging any obligation, has been made. As only R285 000 of the loan has been repaid, the output tax for the year will amount to 14/114 x R285 000 = R35 000.

The interest relates to a financial service, which will be an exempt supply (section 12(a)) and no output tax needs to be accounted for in this regard.

Prime Land (Pty) Limited

The VAT implications for this company are a mirror image of the VAT implications for the supplier company. VAT will be levied on the supply of the property and there is thus no transfer duty payable, nor a deemed input tax credit to be claimed. The consideration in money will once again be the actual selling price (not the market value) and the total input tax credit eventually to be claimed amounts to R700 000.

Section 16(3)(a)(iiA) will limit the deduction of input tax to the extent that payment of any consideration which has the effect of reducing or discharging any obligation, has been made. As only R285 000 of the loan has been repaid, the input tax to be claimed for the year amounts to R35 000.

No VAT will be charged on the interest (financial service – exempt supply (section 12(a)) and, correspondingly, no input tax can be claimed.
You are a trainee accountant at an accounting and auditor’s firm. You are responsible for, *inter alia*, the tax affairs of Okohomo (Pty) Ltd.

Okohomo (Pty) Ltd owns a number of properties in South Africa. These properties are either rented out as offices or as residential accommodation. The company also trades in the buying and selling of new and second-hand office equipment. 30% of the turnover of the company is earned from the letting of office space, 20% from the letting of residential accommodation in terms of an agreement for a minimum period of 12 months and 50% is earned from the buying and selling of new and second-hand office equipment.

Okohomo (Pty) Ltd has a 28/29 February year-end and is registered as a VAT vendor. Okohomo (Pty) Ltd has a two-monthly VAT period.

Peggy Smith has been working as an accountant at Okohomo (Pty) Ltd since January 2017. As Peggy had been living abroad for a period of seven years before immigrating back to South Africa on 1 June 2016, she is unsure how to record the following VAT-related transactions that occurred during the company’s VAT period 1 January 2017 until 28 February 2017 and has requested your assistance.

All amounts *include VAT*, where applicable, and all transactions were entered into with VAT vendors, unless specifically stated otherwise. Tax invoices or other required documentation have been obtained, where necessary.

1. Okohomo (Pty) Ltd received an indemnity payment of R106 579 from the insurance company in respect of the total reinstatement of a delivery vehicle (a bakkie) that was stolen during December 2016. This vehicle was purchased on 1 November 2015 and was used solely to deliver office equipment to customers.

2. During January 2017 Okohomo (Pty) Ltd purchased new office equipment locally at a cost of R28 500 from a vendor and second-hand office equipment locally at a cost of R11 000 from a non-vendor. These purchases were paid for and taken into stock immediately. At the end of February 2017, 60% of this stock (new and second-hand office equipment) had not been sold. The 40% of the stock that has been sold was sold locally at a mark-up of 30% on cost.

3. During January 2017, Okohomo (Pty) Ltd imported and paid for office equipment purchased in the USA for the rand equivalent of R96 315. The office equipment had a customs duty value of R104 000 and the non-refundable duty levied and paid on importation when cleared and released for home consumption amounted to R7 520. The office equipment was purchased as trading stock.

4. A second-hand computer was purchased for R4 500 from a non-vendor during January 2017. The computer was purchased to be used for the processing of invoices for the letting of residential accommodation and office space as well as for the selling of office equipment. The purchase price was payable in 3 equal monthly instalments of R1 500 starting on 31 January 2017. Okohomo (Pty) Ltd has made all payments up to 28 February 2017 on time.

5. The following advertising and marketing expenses were incurred during January 2017:

   - 100 advertising boards were erected at a cost of R60 each. 40 of the boards will be used to advertise the letting of residential accommodation and 60 boards will be used to advertise the letting of office space.  
     - R
   - Cocktail party (food and drinks) to introduce a new photocopier range to potential clients
     - 3 500
     - 9 500
QUESTION 13 (continued)

6. A double cab bakkie was purchased on 1 February 2017 in terms of a 3-year finance lease (“instalment credit agreement” as defined) to replace the delivery vehicle that was stolen. The cash cost of this vehicle was R131 328. Instalments of R26 290 will be paid every six months from 31 July 2017. The exclusive right of use (private and business) of this vehicle was given to one of the sales representatives from the date of purchase. Okohomo (Pty) Ltd bears all expenses relating to the vehicle.

Okohomo (Pty) Ltd immediately entered into an insurance agreement in respect of the double cab bakkie. In terms of the agreement, the insurance is paid in advance three-monthly. The first payment of R1 920 (for the period 1 February 2017 to 30 April 2017) was paid on 1 February 2017.

7. Okohomo (Pty) Ltd has been trading from a residential house that they had purchased from a non-vendor for an amount of R1 200 000 on 1 October 2014. Transfer duty of R22 000 was paid in respect of the acquisition of this house. Okohomo (Pty) Ltd claimed the maximum possible input tax credit on the acquisition of this property. During January 2017, they sold the house to a vendor at the open market value of R1 650 000. Registration of the house in the name of the new owner took place on 25 February 2017. Okohomo (Pty) Ltd received the full consideration for the sale of the house on the date of registration in the name of the new owner.

REQUIRED

| Marks |
|-------------------------|---|
| (a) Calculate the VAT consequences of transactions 1 to 6. Clearly indicate if the amount calculated is classified as output tax or input tax. If any item has no VAT consequences provide a reason. Show all your workings and round each amount off to the nearest R1. | 16 |
| (b) Discuss, supported by calculations, the VAT implications in respect of transaction 7. In your discussion, pay special attention to the value and time of supply. Refer to VAT legislation. Round each amount off to the nearest R1. | 7 |
PART 1(a)

Letting of offices
Letting of residential accommodation (section 12(c))
Selling of new and second-hand equipment

<table>
<thead>
<tr>
<th>Exempt supplies %</th>
<th>Taxable supplies %</th>
</tr>
</thead>
<tbody>
<tr>
<td>20</td>
<td>30</td>
</tr>
<tr>
<td>20</td>
<td>50</td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>Input Tax R</th>
<th>Output Tax R</th>
</tr>
</thead>
<tbody>
<tr>
<td>R106 579 x 14/114</td>
<td>13 089 (1)</td>
</tr>
</tbody>
</table>

1. Indemnity payment: (R106 579 x 14/114)
   (The receipt of the indemnity payment is a deemed supply and output tax of R13 089 must be accounted for as Okohomo would have been entitled to an input tax deduction on the acquisition of the delivery vehicle (it is not a “motor car” as defined, the proviso to section 8(8) does not apply. The time of supply is the day on which the indemnity payment was received.)

2. Office equipment purchased – new office equipment
   (R28 500 x 14/114 = R3 500)
   Office equipment purchased – second-hand office equipment
   (section 1(1), def of input tax, par (b))
   (R11 000 x 14/114 = R1 351)
   Office equipment sold – new office equipment
   ((R28 500 x 100/114) x 40% x 130%) x 14% = R1 820
   Office equipment sold – second-hand office equipment
   ((R11 000 x 100/114) x 40% x 130%) x 14% = R702

3. Office equipment imported from a non-BLNS country.
   VAT is calculated as follows:
<table>
<thead>
<tr>
<th>R</th>
</tr>
</thead>
<tbody>
<tr>
<td>104 000</td>
</tr>
<tr>
<td>10% of customs duty value (R104 000 x 10%)</td>
</tr>
<tr>
<td>Customs duty</td>
</tr>
<tr>
<td>121 920</td>
</tr>
<tr>
<td>R121 920 x 14% (section 13(2))</td>
</tr>
</tbody>
</table>
QUESTION 13 - SUGGESTED SOLUTION (continued)

4. Second-hand computer purchased
   (A notional input tax can be claimed in respect of the second-hand computer. Input tax can only be claimed to the extent that payment has been made. Claim input tax only to the extent that the computer is used to make taxable supplies (section 17(1)), therefore 80%.)
   Thus: R4 500 x 14/114 x 80% x R3 000/R4 500 = R295; or ((R1 500 + R1 500) x 80% x 14/114)

5. Advertising
   • 100 advertising boards – (60 x R60 x 14/114 = R442)
     (Apportion and claim only to the extent that taxable supplies are made (section 17(1)))
     442 (1)
   • Cocktail party – input tax denied as this is entertainment (section 17(2))
     - (1)

6. Double cab bakkie
   (No input tax can be claimed on the acquisition of the double cab bakkie as it is a motor car as defined in section 1(1) (section 1(1) and 17(2)(c))
   Fringe benefit – free use of motorcar provided to sales representative (section 18(3)).
   Deemed supply - (R131 328 x 100/114 x 0.3% x 14/114 x 1 month = R42)
   42 (2)

Insurance premium
   (R1 920 x 14/114 = R236)
   (Section 17(2)(c) does not prohibit the claiming of input tax i.r.o. the running expenses of a “motor car”, only i.r.o. the acquisition.)
   236 (1)

Total
   16
PART 1(b)

Sale of house:

**Output tax:**
In terms of section 8(16)(a) of the VAT Act the supply of goods, held partly for the making of taxable supplies, will be deemed to be made wholly in the course or furtherance of the enterprise. VAT therefore has to be charged on the full selling price (no apportionment). The selling price of R1 650 000 thus includes output tax of R202 632 (R1 650 000 x 14/114) which has to be taken into account in the February VAT return.

**Input tax adjustment**
Okohomo could only claim 80% of the input tax on the acquisition of the house therefore the company will be able to claim additional input tax in terms of section 16(3)(h) of the VAT Act, calculated as follows:

\[
A \times B \times C
\]

A = tax fraction = 14/114
B = lesser of adjusted cost (R1 200 000) and the open market value at the time of the supply (R1 650 000), therefore R1 200 000
C = percentage of non-taxable supplies

Therefore:

\[
14/114 \times R1 200 000 \times 20\% = R29 474
\]

Thus:
A section 16(3)(h) input tax of R29 474 can be claimed in the February tax period being the tax period in which the sale took place.
QUESTION 14

You are a tax lecturer at an academic institution as well as a part time tax consultant registered as a tax practitioner with the South African Revenue Service (SARS). The following queries have been referred to you for advice:

Query 1

Advance Ltd, a registered VAT vendor, is considering the acquisition of two buildings for investment purposes.

The first building is owned by a non-vendor and the purchase consideration is R2 500 000. The three-storey building comprises shops and offices on the ground floor and residential flats on the other two storeys. SARS has accepted that on the basis of rental income, the building is intended to be used 40% for commercial letting activities.

The second building is owned by a registered VAT vendor. The purchase consideration is R2 850 000 (including VAT). The building comprises mainly shops and offices but 10% is let for residential purposes. If the company does purchase this building, it will convert the residential section so that it is suitable for commercial letting activities immediately upon acquisition.

Both buildings are fully occupied.

**REQUIRED**

<table>
<thead>
<tr>
<th>Discuss the VAT implications of the purchase of each of the buildings from the perspective of Advance Ltd.</th>
<th>Marks</th>
</tr>
</thead>
<tbody>
<tr>
<td>18</td>
<td></td>
</tr>
</tbody>
</table>

Query 2

Maluti (Pty) Ltd, a registered VAT vendor, which only makes taxable supplies, has a number of delivery trucks that it uses to transport products for clients. Recently one of its delivery trucks was hijacked. The delivery truck, which had originally cost R96 900 (including VAT) during 2014, was never recovered and Maluti (Pty) Ltd received an indemnity payment of R114 000 from its insurance company. The R114 000 comprises R68 400, being the market value of the truck, and R45 600 as compensation for client products which were in the truck when it was hijacked. The accounting carrying value and tax value of the delivery truck was R61 000. The indemnity payment was used to pay compensation of R40 000 to the client. No contract of insurance exists between the client and Maluti (Pty) Ltd.

**REQUIRED**

<table>
<thead>
<tr>
<th>Discuss the VAT implications of the following from the perspective of Maluti (Pty) Ltd:</th>
<th>Marks</th>
</tr>
</thead>
<tbody>
<tr>
<td>The indemnity payment received; and The compensation paid to the client.</td>
<td>5</td>
</tr>
</tbody>
</table>
The human resources manager of Rich Ltd has the following two queries on VAT issues:

The first query concerns a luxury motor car that is owned by Rich Ltd, which it acquired for R450 000 (including VAT) on 1 February 2014 and used from that date. The free use of the motor car was given to the managing director on 1 March 2016 as part of his employment package. The repair, maintenance, petrol and running costs, are borne by Rich Ltd.

The second query concerns one of the Rich Ltd salesmen, who lives in Johannesburg and flew to Cape Town on a two-day business trip. He is a full-time employee of the Johannesburg branch of Rich Ltd. For the first day he was away, the company awarded him the R372 a day subsistence allowance in terms of section 8(1)(c) of the Income Tax Act. The company paid for his airfare as well as for his accommodation and meals at a large hotel in Cape Town.

<table>
<thead>
<tr>
<th>REQUIRED</th>
<th>Marks</th>
</tr>
</thead>
<tbody>
<tr>
<td>Discuss the VAT implications of the two matters for the company.</td>
<td>19</td>
</tr>
</tbody>
</table>

Source: Qualifying Examination SAICA 2007 adapted
QUESTION 14 – SUGGESTED SOLUTION

Query 1

ACQUISITION FROM THE NON-VENDOR

The building is acquired from a non-vendor. Therefore, no VAT will be payable on the acquisition of the building. However, transfer duty will be payable. (1)

The building, however that is acquired from a non-vendor constitutes second-hand goods as it has previously been owned and used as defined in section 1(1) of the Value-Added Tax Act. (1)

Consequently, a notional/deemed input tax deduction may be claimed. (1)

The notional input tax deduction will be based on the:

• Application of the tax fraction of 14/114 (1)
• To the lower of
  o The consideration paid for the property of R2,5 million or
  o The open market value of the property. (1)

(1, definition of input tax, par (b))

Therefore, the notional input tax is 14/114 x R2,5 million = R307 018. (1)

The building is going to be used to make exempt supplies (residential accommodation) to the extent of 60%, thus the input tax deduction is limited to 40% of R307 018 = R122 807. (1)

Although the time of supply is the earlier of date of payment or registration in the name of the company (section 9(3)(d)) the notional input tax deduction will only be claimable on the date of registration in the name of Advance Ltd (section 16(3)(a)(ii)(bb)(A)) but can only be claimable to the extent that payment of the purchase price has been made (section 16(3)(a)(ii)(aa)). (1)

The asset must be acquired from a Republic resident and a copy of a letterhead or ID document retained in order to claim the notional input tax credits. (1)

ACQUISITION FROM THE VENDOR

As the second building is to be acquired from a vendor and VAT is payable on the transaction, no transfer duty is payable and input tax credits may be claimed. (1)

If the requirements of section 11(1)(e) of the VAT Act are complied with the sale will be zero-rated as it constitutes the sale of a going concern. (1)

For the sale of a going concern to be zero-rated, section 11(1)(e) requires the following to be met:

• The supply must be to a registered vendor (by implication by a registered vendor). (½)
• The enterprise or part of it must be capable of separate operation. (½)
• The supplier and recipient must agree in writing that the enterprise will be disposed of as a going concern. (½)
• The supplier and recipient must agree in writing that the enterprise is an income-earning activity on the date of the transaction. (½)
• The parties must agree in writing that the consideration agreed upon for the supply is inclusive of tax at the rate of zero percent. (½)
• The assets which are necessary for carrying on such enterprise are disposed of by the supplier to the recipient. (½)

Thus if it is a zero-rated sale, VAT is payable at 0%, and no input tax deduction is available to Advance Ltd. (1)

As the building is currently being used less than 95% to make taxable supplies, a section 18A adjustment to output tax would normally apply. (1)

However, as Advance Ltd is going to use the building exclusively to make taxable supplies no adjustment is required, as it is clearly stated in the question that Advance Ltd will convert the residential letting activities into commercial letting activities immediately upon acquisition. (1)
QUESTION 14 – SUGGESTED SOLUTION (continued)

If the acquisition is not structured as a going concern sale, VAT is payable on the acquisition of the building and Advance Ltd will be able to claim input tax credits on the acquisition of the building in total as the company will be converting and using the entire building for commercial letting purposes immediately upon acquisition. Therefore, R2,85 million x 14/114, being R350 000 may be claimed as input tax credits.

The input tax deduction will only be claimable on the earlier of date of any payment or the date of registration in the name of Advance Ltd (section 9(3)(d)) but can only be claimed to the extent that payment of the purchase price has been made (section 16(3)(a)(ii)(aa)). Input tax credits may be claimed when the vendor is in possession of a valid tax invoice.

Note:
If we look at the seller and the sale is not a going concern sale at zero-rate the following will apply:
As the seller used the building partly (10%) for the making of non-taxable supplies section 8(16) will apply. Therefore output tax will be levied on the full amount of consideration (R2 850 000). The seller will be entitled to claim an additional input tax in terms of section 16(3)(h) in respect of the 10% previously not claimed.

23

Query 2

The indemnity payment was received from the insurer under a contract of insurance.

Therefore, a deemed supply arises in terms of section 8(8) and output tax must be accounted for in the period when the payment is received.

As the vehicle is not a “motor car” as defined, the entire indemnity payment will constitute a deemed supply.

The output tax that Maluti (Pty) Ltd must account for is R14 000, being 14/114 x R114 000.

The payment to compensate the client is not an amount paid to indemnify another person in terms of a contract of insurance and therefore does not meet the criteria for an input tax deduction in respect of the tax fraction of the payment (section 16(3)(c)).

5

Query 3

Acquisition of motor car:

On the acquisition of the vehicle, input tax credits would have been denied, as the vehicle is a motor car as defined.

Free use of the motor car:

The free use of the luxury motor car given to the managing director is a Seventh Schedule taxable fringe benefit. The company is required to pay a deemed output tax over for the fringe benefit to the managing director in terms of section 18(3).
As the motor car was acquired two years before the use thereof was given to the managing director, the output tax per month is calculated as follows:

<table>
<thead>
<tr>
<th>Description</th>
<th>Amount</th>
</tr>
</thead>
<tbody>
<tr>
<td>Acquisition price less VAT: R450 000 x 100/114</td>
<td>R394 737</td>
</tr>
<tr>
<td>Less: 15% wear and tear on the reducing balance for each full year of use by the company prior to giving the use to the MD (2 years) for period 1/2/2014 to 31/1/2015</td>
<td>(59 211)</td>
</tr>
<tr>
<td>Less: for the period 1/2/2015 to 31/1/2016</td>
<td>(50 329)</td>
</tr>
<tr>
<td>x 0,3% as it is a motor car as defined and input tax credits denied</td>
<td>x 0,3%</td>
</tr>
<tr>
<td>Output tax per month</td>
<td>R105,07</td>
</tr>
</tbody>
</table>

The further indirect receipt of the running costs by the managing director does not constitute a further fringe benefit that has output tax consequences.

Rich Ltd will be able to claim input tax credits on the repair, maintenance and other running expenses for which it is in possession of valid tax invoices.

Petrol costs borne by Rich Ltd will not lead to the claiming of input tax credits as petrol is zero-rated under section 11.

**Subsistence allowance**
The company paid its salesman a R372 a day “no questions asked” subsistence allowance in terms of section 8(1)(c) of the Income Tax Act. Since the subsistence allowance is not a Seventh Schedule taxable benefit in terms of the Income Tax Act, no deemed supply in terms of section 18(3) arises for VAT purposes.

In addition no input tax credit is available to the company on the payment of the subsistence allowance to its salesman as the salesman is not making a taxable supply to it as the provision of services by an employee to an employer is excluded from the definition of an enterprise and consequently the salesman cannot register as a VAT vendor for that purpose. The subsistence allowance merely constitutes the supply of “money”.

**Business trip expenses**

**Output tax**
The airfare expense is a business expense to the company and it is not a fringe benefit to its salesman. Since the airfare expense is not a Seventh Schedule taxable benefit in terms of the Income Tax Act, no deemed supply in terms of Section 18(3) arises for VAT purposes.

The accommodation expense paid by the company is a Seventh Schedule taxable benefit in terms of the Income Tax Act being residential accommodation provided in terms of paragraph 2(d) of the Seventh Schedule. Although this a fringe benefit, section 18(3) excludes the supply of exempt supplies.

Note: The fringe benefit is, however, given a “nil” value being accommodation away from an employee’s usual place of residence provided by his employer while he is absent from his usual place of residence for the purposes of performing the duties of his employment. Therefore, if it had been a deemed supply, in terms of section 18(3) the value of the deemed supply would have been “Rnil” (14/114 x Rnil).
QUESTION 14 – SUGGESTED SOLUTION (continued)

The meal expenses paid by the company are a Seventh Schedule taxable benefit in terms of the Income Tax Act as provided for in paragraph 2(c) of the Seventh Schedule.

The fringe benefit is however, given an “Rnil” value as it is supplied to the recipient during extended working hours whilst away on a business trip. Therefore, the deemed supply will be “Rnil” (14/114 x nil).

Input tax
The company may claim back the input tax credits on the airfare as it was incurred in the course or furtherance of the enterprise.

Hotel accommodation and meal costs borne by the company constitutes entertainment as defined and input tax credits are generally denied upon the acquisition of entertainment.

However, as the salesman is away from his usual place of residence and his usual working place for at least one night, input tax credits will be claimable.

The input tax credits may be claimed on the valid business expenses when the vendor is in possession of a valid Tax invoice.
Paradise Birds (Pty) Limited is a company wholly owned by Adam Paradise and is located in Pretoria, South Africa. Paradise Birds (Pty) Limited is a registered VAT vendor (on the invoice basis and with two-monthly tax periods). The company’s primary business includes
- the purchase, breeding and sale of exotic (wild) birds and
- the manufacturing of bird cages, feeders and water containers.

Paradise Birds (Pty) Limited also manufactures, produces and distributes
- wild bird feed, vitamins and mineral supplements and
- wild bird remedy for the diagnosis and prevention of illnesses in exotic birds
(all above items qualify as goods used for agricultural or other farming purposes in terms of Schedule 2 of the VAT Act).

Paradise Birds (Pty) Limited has a February year-end. 98% of the company’s assets are used to make taxable supplies.

Birdie Howzit is the newly appointed accountant of Paradise Birds (Pty) Limited. She managed to register Paradise Birds (Pty) Limited with SARS on the e-filing system and wants to lodge the company’s VAT returns and make all payments to SARS via e-filing.

Birdie Howzit requested your assistance in calculating the VAT payable or receivable for the January/February 2017-tax period.

The following transactions occurred during January and February 2017 (all amounts include VAT where applicable):

1. Sales
   - Local sales – wild birds, cages, feeders and water containers $86,054
   - Local sales – wild bird feed, vitamins, minerals and remedy $38,109
   - Cages, feeders and water containers directly exported to the United Kingdom
     (all the necessary documentary proof that goods have been exported were obtained and all requirements regarding the export were met) $64,850

2. A second-hand machine used to manufacture bird feeders, was directly exported to the United Kingdom.
   Paradise Birds (Pty) Limited purchased this machine in September 2016 for R171,000 from Jack Black, a non-vendor who lives in Johannesburg, South Africa. Paradise Birds (Pty) Limited claimed a notional input tax deduction of R21,000 on this machine.

3. In December 2016, Adam Paradise purchased a new motor vehicle, a Start car (a “motor car” as defined in section 1(1) of the VAT Act), for R100,320 from Incredible Cars Limited (a registered VAT vendor). The car was registered in the name of Paradise Birds (Pty) Limited.
   On 1 January 2017 this car was made available to Birdie Howzit to enable her to run errands for Paradise Birds (Pty) Limited. As she had no other transport, Adam Paradise agreed that Birdie Howzit could use the Start car freely for private purposes as well.

R 100,320
Paradise Birds (Pty) Limited incurred all the costs relating to the Start car for the 2 months. The costs were as follows:

- Fuel
- Insurance

4. Birdie Howzit purchased and then distributed samples of wild bird feed to customers for free. The cost price of these promotional items (purchased and distributed) amounted to R3 990.

5. Raw materials (to be used in the manufacturing process of taxable supplies) were imported from Mozambique by Paradise Birds (Pty) Limited during February 2017. The customs value of the goods amounted to R68 000 and the non-refundable duties and surcharges amounted to R15 200. The appropriate VAT was paid at the time of importation. These raw materials were entered for home consumption on 15 February 2017.

6. On 25 February 2017, Paradise Birds (Pty) Limited donated wild birds, cages, feeders and water containers (with a cost price of R111 720 and an open market value of R122 892), that was purchased on 1 February 2017, to Heavenly Paradise, an association not for gain, which provides tranquil gardens at hospices and other institutions for gravely ill patients. Heavenly Paradise is a public benefit organisation (PBO) for the purposes of the Income Tax Act and all the required documentation was received from Heavenly Paradise regarding the donation made.

Adam Paradise also made a cash donation of R30 000 on 25 February 2017 in the name of Paradise Birds (Pty) Limited to Patience Goodbuy. It was as a token of gratitude for the loving care that Patience Goodbuy, the director of Heavenly Paradise, provides to patients.

No other donations were made during the 2017 year of assessment.

7. Paradise Birds (Pty) Limited incurred bus, train & taxi expenses amounting to R2 565 for the two months in respect of the transport of the factory workers between their homes and their place of work. All these factory workers are fare-paying passengers and the transport cost is included in the workers’ remuneration.

8. On 1 September 2016, Adam Paradise purchased a computer in the name of Paradise Birds (Pty) Limited for R47 880. He claimed only 60% of the input tax in the September/October tax period as he used the computer for his private purposes as well. However, after Birdie Howzit joined the company, the taxable use of the computer increased to 100% on 1 January 2017. (The open market value of the computer on 1 January 2017 and 28 February 2017 was R42 000 and R39 000 respectively).
### QUESTION 15  (continued)

<table>
<thead>
<tr>
<th>REQUIRED</th>
<th>Marks</th>
</tr>
</thead>
<tbody>
<tr>
<td>(a) Calculate the VAT payable by Paradise Birds (Pty) Limited or refundable by SARS for the two-month tax period ending February 2017. Show all your calculations and motivate your answer (with a reason) where no VAT can be claimed, or where supplies are zero-rated or exempt.</td>
<td>23</td>
</tr>
<tr>
<td>(b) Indicate which day is the last day that Paradise Birds (Pty) Limited can submit its VAT return to SARS in respect of its January/February 2017 tax period.</td>
<td>1</td>
</tr>
<tr>
<td>(c) Calculate the donations tax payable by Paradise Birds (Pty) Limited (if any). Provide short reasons, if no donations tax is payable. Also, mention the date on which the donations tax should be paid to the Commissioner.</td>
<td>5</td>
</tr>
</tbody>
</table>
QUESTION 15 – SUGGESTED SOLUTION

(a) 

1. Sales:
   (a) Local sales – wild birds, cages, feeders and water containers
       • R86 054 x 14/114
           \[ \text{R} \times 10 568 \] (1)
   (b) Local sales – wild bird feed, vitamins, minerals and remedy
       • (qualifies as goods used for agricultural or other farming purposes – given) – zero-rated supply (section 11(1)(g))
           - (1)
   (c) Cages, feeders and water containers directly exported to the United Kingdom – zero-rated supply (section 11(1)(a))
           - (1)

2. Second-hand machine exported:
   Zero-rate does not apply to exports where a notional input tax deduction was claimed by the RSA vendor (proviso to section 11(1)).
   Output tax – consideration deemed to be equal to the purchase price (including notional input tax claimed by the RSA vendor)
   R171 000 x 14/114 – section 10(12)
   \[ \text{R} \times 21 000 \] (1)

3. The free use of the motor car – is a fringe benefit in terms of the 7th Schedule to the Income Tax Act.
   It is a deemed supply in terms of section 18(3) of the VAT Act and output tax must be accounted for:
   Determined value (excluding VAT) = R100 320 x 100/114 = R88 000
   R88 000 x 0.3% (input tax was denied on acquisition)
   x 2 months = R528
   Deemed output tax for Jan & Feb 2017 = R528 x 14/114
   \[ \text{R} \times 65 \] (1)
   Fuel – no input tax claimable – zero-rated supply (section 11(1)(h))
   - (1)
   Insurance – input tax claimed on R513 x 14/114
   \[ \text{R} \times 63 \] (1)

4. Free samples to customers:
   When a supply is made for no consideration, the value of the supply is deemed to be Rnil (section 10(23)) – no output tax (refer note at the bottom of the question).
   It is a taxable supply (even though the value is deemed to be Rnil) – input tax is claimed on R3 990 x 14/114
   \[ \text{R} \times 490 \] (1)

5. Imported goods customs value, duties and surcharges (section 13(2))
   \[ \text{R} \]
   Customs value
   68 000
   Plus: 10% of the customs value
   6 800 (1)
   Plus: All duties and surcharges
   15 200 (1)
   \[ \text{R} \times 90 000 \]
   Input tax of
   x 14% = \[ \text{R} \times 12 600 \] (1)
6. Donation of wild birds, cages, feeders and water containers to an association not for gain – excluded from the definition of “consideration” in section 1(1) of the VAT Act – thus no output tax
When a taxable supply of goods or services are made for no consideration, the value is deemed to be Rnil (sec 10(23)).
Since the supply is a taxable supply, a full input tax deduction may be claimed.
Input tax calculated on R111 720 x 14/114

\[ \text{Assumptions (Interpretation note no. 70):} \]
- The goods were not purchased in order to donate it. Nothing in the question suggests that. Therefore input tax may be claimed.
- No section 18(1) adjustment if goods donated for promotional purposes, corporate social responsibility (CSR) expenses and if a section 18A input tax adjustment could be claimed.
- Our interpretation is that due to the deductibility of the donation, no section 18(1) adjustment could be claimed.

Cash donation of R30 000 – not a supply of goods and services - “money” is specifically excluded from the definition of “goods” in section 1(1) of the VAT Act

7. Bus, train & taxi expenses in respect of fare-paying passengers:
- no output tax – not a deemed supply i.t.o. section 18(3) (exempt supply ito section 12(g))
- no input tax – exempt supply (section 12(g))

8. The computer is now being used 100% of the time for making “taxable” supplies as opposed to 60% of the time previously. There is a change of use of the computer - an increase of 40% in taxable use.

A change of use adjustment is available i.t.o. of section 18(5), as the change in use is greater than 10% and the cost of the capital goods is more than R40 000 (excluding VAT) (R47 880 x 100/114 = R42 000).

The adjustment is based on the computer’s open market value at 28 February 2017 (the end of the company’s year-end) (section 18(6)) of R39 000 and not on its cost (of R47 880) because the open market value is the lesser amount.

This lesser value must then be adjusted by the change of use from 60% to 100%. The input tax claimable will thus be R1 916 (R39 000 x 14 / 114 x (100% - 60%)) claimed in the Jan/Feb 2017-tax period.

\[ \text{VAT payable to SARS} \]
\[ \text{R} \]
\[ \text{2 844} \]
\[ \text{23} \]

(b)
As Paradise Birds (Pty) Limited is registered as an e-filing client, submission (and payment) must be made on the last working day of March 2017 (31 March 2017).
(c) Donation of wild birds, cages, feeders and water containers to a PBO – exempt in terms of section 56(1)(h)  
Cash donation of R30 000  
Less: Basic exemption – section 56(2)(a) for a company

\[
\begin{align*}
\text{Cash donation} & : \quad 30,000 \quad (1) \\
\text{Basic exemption} & : \quad 10,000 \quad (1) \\
\text{Net amount} & : \quad 20,000 \\
\end{align*}
\]

\[
\text{Less: Basic exemption} \times 20% \quad (1) \\
\quad 4,000 \\
\]

Donations tax is payable by the end of the month following the month during which the donation takes effect. In this case the donation was made on 25 February 2017, thus donations tax must be paid by 31 March 2017.

\[
\begin{align*}
\text{Donations tax: } & \quad 5 \\
\text{VAT (transaction 4): } & \quad \text{As the company is still supplying the samples for business purposes (therefore a taxable supply) no section 18(1) adjustment will be accounted for and the supply will be for Rnil consideration (section 10(23)).}
\end{align*}
\]
QUESTION 16  

Rent a Crock (Pty) Ltd is a resident company with a December year-end and is a registered category B VAT vendor (tax periods ending on February, April, June, etc.). All amounts in the question • exclude VAT (if applicable), and • all parties involved are registered VAT vendors unless specifically stated otherwise.

Information relating to Rent a Crock (Pty) Ltd

Rent a Crock (Pty) Ltd buys motor vehicles from Build a Crock (Pty) Ltd or other second-hand motor dealers and rents it to customers on a daily or weekly basis. Customers are invoiced for the rental of the vehicle, the petrol usage and for insurance.

The following transactions have not been recorded in the accounting records of Rent a Crock (Pty) Ltd on 31 December 2017:

1. On 1 November 2017 Rent a Crock (Pty) Ltd purchased two motor cars from Build a Crock (Pty) Ltd at their total market value of R141 360 (including VAT). 50% of the amount was paid immediately, while the other 50% of the amount will only be payable on 1 February 2018. The one car, a Volks-wagen Polo, was purchased for R63 510 (including VAT) and is used as one of the fleet of motor cars to be rented out to clients. The other car, a Honda Civic, was purchased for R77 850 (including VAT) and immediately given to the office manager for his exclusive use (private and business). Rent a Crock (Pty) Ltd bears all the expenses relating to the vehicle. The only expenses incurred in respect of these two vehicles during November 2017 and December 2017 were fuel costs of R5 500 (in total) on the Volkswagen Polo, and R700 (in total) in respect of the Honda Civic, as well as insurance of R350 per month per vehicle.

During November 2017 and December 2017, the Volkswagen was rented out to numerous customers. The income received on the rentals consists of:

<table>
<thead>
<tr>
<th>Description</th>
<th>Amount</th>
</tr>
</thead>
<tbody>
<tr>
<td>Rent</td>
<td>R 13 750</td>
</tr>
<tr>
<td>Fuel</td>
<td>R 5 500</td>
</tr>
<tr>
<td>Insurance</td>
<td>R 1 350</td>
</tr>
<tr>
<td><strong>Total</strong></td>
<td><strong>R 20 600</strong></td>
</tr>
</tbody>
</table>

On 1 December 2017, Rent a Crock (Pty) Ltd purchased a second-hand lawnmower for R5 400 from a non-vendor to mow the lawn outside the offices. The seller agreed to allow Rent a Crock (Pty) Ltd to settle the purchase price in two equal instalments of R2 700 payable on 31 December 2017 and 31 January 2018.

2. Instead of giving its employees cash to cover their transport expenses to and from work, Rent a Crock (Pty) Ltd purchases bus coupons (for cash) for all employees on a weekly basis. During November 2017 and December 2017, Rent a Crock (Pty) Ltd incurred R3 006 on purchasing bus coupons.

<table>
<thead>
<tr>
<th>REQUIRED</th>
<th>Marks</th>
</tr>
</thead>
<tbody>
<tr>
<td>Journalise the effect of the transactions in the books of Rent a Crock (Pty) Ltd for the year of assessment ended 31 December 2017. Ignore any journal descriptions but provide brief reasons to the treatment of the transactions. You do not have to provide any journal dates.</td>
<td>29</td>
</tr>
</tbody>
</table>
### QUESTION 16 - SUGGESTED SOLUTION

<table>
<thead>
<tr>
<th></th>
<th>Debit R</th>
<th>Credit R</th>
</tr>
</thead>
<tbody>
<tr>
<td>1</td>
<td>Motor vehicles (R63 510 x 100/114)</td>
<td>55 711</td>
</tr>
<tr>
<td></td>
<td>Motor vehicles</td>
<td>77 850</td>
</tr>
<tr>
<td></td>
<td>Input tax (R63 510 x 14/114)</td>
<td>7 799</td>
</tr>
<tr>
<td></td>
<td>Bank</td>
<td>70 680</td>
</tr>
<tr>
<td></td>
<td>Creditor – Build a Crock</td>
<td>70 680</td>
</tr>
<tr>
<td></td>
<td>(VAT is claimable in respect of the motor vehicle acquired as part of the rental fleet as it is an asset acquired for the making of taxable supplies. The motor vehicle acquired for use by the office manager qualifies as a motor car and input tax is denied in terms of section 17(2) of the VAT Act)</td>
<td>(1)</td>
</tr>
<tr>
<td></td>
<td>Salaries</td>
<td>50</td>
</tr>
<tr>
<td></td>
<td>Output Tax</td>
<td>50</td>
</tr>
<tr>
<td></td>
<td>(R 77 850 x 100/114 x 0.3% x 14/114 x 2)</td>
<td>(2)</td>
</tr>
<tr>
<td></td>
<td>(In terms of section 18(3) the vehicle acquired for use by the office manager constitutes a deemed supply.)</td>
<td>(1)</td>
</tr>
<tr>
<td></td>
<td>Fuel (zero-rated) (R5 500 + R700)</td>
<td>6 200</td>
</tr>
<tr>
<td></td>
<td>Insurance (R350 x 2 x 2 months)</td>
<td>1 400</td>
</tr>
<tr>
<td></td>
<td>Input tax (R1 400 x 14%)</td>
<td>196</td>
</tr>
<tr>
<td></td>
<td>Bank</td>
<td>7 796</td>
</tr>
<tr>
<td></td>
<td>Fuel and insurance paid on vehicles.</td>
<td></td>
</tr>
<tr>
<td></td>
<td>(No input tax claimed on fuel as it is zero-rated – section 11(h) of the VAT Act)</td>
<td>(1)</td>
</tr>
<tr>
<td></td>
<td>Bank</td>
<td>22 714</td>
</tr>
<tr>
<td></td>
<td>Fuel received (zero-rated)</td>
<td>5 500</td>
</tr>
<tr>
<td></td>
<td>Insurance received</td>
<td>1 350</td>
</tr>
<tr>
<td></td>
<td>Rent received</td>
<td>13 750</td>
</tr>
<tr>
<td></td>
<td>Output tax ((R1 350 + R13 750) x 14%)</td>
<td>2 114</td>
</tr>
<tr>
<td></td>
<td>(Income received on renting out the Volkswagen Polo. Fuel being zero-rated in terms of section 11(h) of the VAT Act, while rent and insurance are taxable supplies)</td>
<td>(1)</td>
</tr>
<tr>
<td></td>
<td>Salaries and wages</td>
<td>3 006</td>
</tr>
<tr>
<td></td>
<td>Bank</td>
<td>3 006</td>
</tr>
<tr>
<td></td>
<td>The supply of bus coupons constitutes a fringe benefit in terms of the Seventh Schedule, but as the supply of fee paying transport is an exempt supply in terms of section 12 of the VAT Act no deemed supply arises in terms of section 18(3).</td>
<td>(2)</td>
</tr>
<tr>
<td></td>
<td><strong>Note:</strong> There is no input tax as the cost of buying the bus coupons, does not include VAT (except supply) (section 12(g))</td>
<td></td>
</tr>
</tbody>
</table>

**Total marks 29**
QUESTION 17

This question consists of two related parts (part A and part B). In answering part A and part B you may assume that the same taxation legislation that is applicable to the 2017 year of assessment, will apply to the 2018 year of assessment.

Round-off all figures to the nearest R1.

PART A

John Dow recently qualified as a Chartered Accountant and registered with SAICA and IRBA to practice as a registered auditor. John registered an incorporated company, JD Incorporated, through which he plans to conduct his business. During March 2017, John registered JD Incorporated as a VAT vendor (on the invoice basis, with a two-monthly tax period). The first tax period will end on 30 April 2017.

Tax was never John's strong point. Certain transactions occurred during March and April 2017, which gave him a headache and he requested your assistance.

Transaction 1

John purchased a residential house, in the name of JD Incorporated, from a non-vendor for R1 200 000 and paid transfer duty of R48 000. The property was financed with a loan from the bank.

He converted 40% of the house into offices for his practice and uses the rest of the house to live in. John does not pay any consideration to the company for living in part of the house.

The cost of converting 40% of the house into a practice was as follows:

<table>
<thead>
<tr>
<th>Description</th>
<th>Cost</th>
</tr>
</thead>
<tbody>
<tr>
<td>Invoice received from Electrical and Plumbing (Pty) Ltd (a vendor):</td>
<td></td>
</tr>
<tr>
<td>Labour</td>
<td>R29 594</td>
</tr>
<tr>
<td>Material</td>
<td>R11 012</td>
</tr>
<tr>
<td>Total cost (including VAT where applicable)</td>
<td>R40 606</td>
</tr>
<tr>
<td>Other costs incurred (done on a “owner builder” basis by John – including VAT where applicable)</td>
<td></td>
</tr>
<tr>
<td>Labourers hired from the street</td>
<td>R15 000</td>
</tr>
<tr>
<td>Materials purchased from vendors</td>
<td>R76 000</td>
</tr>
<tr>
<td>TOTAL COST OF CONVERSION</td>
<td>R131 606</td>
</tr>
</tbody>
</table>

REQUIRED

| (a) Calculate the input tax credit that JD Incorporated may claim in respect of the purchase of the property and the conversion into offices. Where no VAT can be claimed, motivate your answer. | 5 |
| (b) Discuss whether the company will be liable for any output tax in respect of this transaction. | 2 |
QUESTION 17 (continued)

Transaction 2

On 5 April 2017, JD Incorporated held a function for all existing and potential clients as part of the opening of the new practice. The total cost of the function was R11 400 (including VAT). The company also purchased two huge banners. One banner was placed at the entrance to the venue, welcoming all the guests. The other banner was placed inside the venue, displaying all the services the company renders. The cost of purchasing the banners was R1 539 (including VAT) each.

REQUIRED | Marks
--- | ---
Calculate the input tax (if any) that JD Incorporated may claim. Where no input tax can be claimed, motivate your answer. | 3

Transaction 3

John had a consultation with a new client (not a vendor) on 2 March 2017. JD Incorporated invoiced the client for R2 052. The client immediately settled the account but tendered his cheque by mistake for R3 052. In the middle of July 2016, John read in the newspaper that the client had been murdered. The “excess” payment of R1 000 was posted by John (debited) to his drawings account.

REQUIRED | Marks
--- | ---
Explain, with calculations, the VAT implications of the excess payment received by the company from the client. Also, explain what will happen should the executor of the client’s estate request during September 2017 that the amount of R1 000 be refunded and the company refunds the R1 000. Also, address the time of supply in your answer. | 5

Transaction 4

When JD Incorporated commenced trading, John sold the following assets (his own) to the company at a fair market value:

- **Office furniture**: R25 000
- **A bakkie (for deliveries)**: R46 000
- **Total purchase price**: R71 000

On 1 March 2017 the company paid John an amount of R25 000 in respect of the furniture and R6 000 of the purchase price of the bakkie. The outstanding balance of R40 000 will be settled later.

REQUIRED | Marks
--- | ---
(a) Calculate the VAT implications for JD Incorporated of the above transactions for the tax period ended 30 April 2017. | 3
(b) Discuss, supported by calculation, the VAT implication if JD Incorporated should sell the bakkie to a second-hand dealer for R48 000 (cash) on 10 May 2017 and then use the R48 000 to repay the outstanding balance of R40 000 on the bakkie on the following day. Also, refer to the time of supply in your answer. | 3
QUESTION 17 (continued)

Transaction 5

<table>
<thead>
<tr>
<th>REQUIRED</th>
<th>Marks</th>
</tr>
</thead>
<tbody>
<tr>
<td>JD Incorporated received an offer to sell the house from which it operates (see details from transaction 1). The offer is for a total amount of R1 400 000. Explain, supported by calculations, the VAT implications should the company accept the offer. You may assume that for the purposes of your calculations, the adjusted cost of the house amounted to R1 250 000 at the date of the offer.</td>
<td>6</td>
</tr>
</tbody>
</table>

PART B 9 marks

During the period 1 March 2016 to 31 March 2017, John Dow was involved in the following transactions in his personal capacity:

March 2016 to February 2017:
John’s monthly contributions to the local church (a public benefit organisation approved in terms of section 30(3) of the Income Tax Act) amounted to R1 000.

June 2016
He donated R8 000 to Sandy, his niece, as a gift on her wedding day.

February 2017:
John sold his existing sectional title unit to his mother when he decided to purchase the house (see part A) in the name of JD Incorporated. The market value of the unit was R400 000 on the date of the sale. The selling price of the unit he sold to his mother was R250 000 and the payment terms were as follows:
- His mother took over the balance of R150 000 that he (John) still owed on the unit.
- For the balance of R100 000 he granted an unsecured interest-free loan to his mother. The loan has to be repaid on the death of his mother (a claim against her estate).

March 2017:
- After John received the free use of a Toyota Fortuner from JD Incorporated he donated his Honda Civic to his wife Erica to whom he is married out of community of property. The market value of the Honda Civic was R142 000 on the date of the donation.
- Some years ago John inherited original paintings from his grandmother (at that stage the market value of the paintings for estate duty purposes was R150 000). John donated the paintings (market value at the date of the donation was R180 000) to JD Incorporated.

<table>
<thead>
<tr>
<th>REQUIRED</th>
<th>Marks</th>
</tr>
</thead>
<tbody>
<tr>
<td>Calculate the Donations Tax that John should pay on each of the above transactions. Provide reasons if no Donations Tax is payable on any of the transactions.</td>
<td>9</td>
</tr>
</tbody>
</table>
**QUESTION 17 – SUGGESTED SOLUTION**

**PART A**

**Transaction 1** (Purchase of property)

(a) **Input tax**

- The property was purchased from a non-vendor, therefore the company paid transfer duty of R48 000 and no VAT.

  Using the property partly for residential purposes (60%) and partly for the business (practice – 40%) the company can claim a notional input tax credit as follows:

  \[
  \frac{14}{114} \times R1200\,000 = R147\,368 \quad \text{(section 1(1), definition of input tax, par (b))}
  \]

  Limited to: \[ R147\,368 \times 40\% = R58\,947 \quad \text{(section 17(1))} \]

- Conversion cost (expended only on office portion)

  An input tax credit can be claimed on the conversion cost (100%) as follows:

  Electrical and Plumbing (Pty) Ltd: \[ \frac{14}{114} \times R406\,406 = 4\,987 \quad \text{(1)} \]

  Other cost: - Labour (not part of definition of an “enterprise” in section 1(1) (refer to note 1 at the end of the solution of Part A)

  - Material \( \frac{14}{114} \times R76\,000 = 9\,333 \quad \text{(1)} \)

  \[ 73\,267 \quad \text{(5)} \]

(b) **Output tax**

- The free use of the company’s house results in a fringe benefit in terms of the Seventh Schedule to the Income Tax Act. This could be a deemed supply under section 18(3) for VAT purposes. This is, however, the supply of residential accommodation that is exempt in terms of section 12(c) of the VAT Act and section 18(3) does not apply to exempt supplies (proviso to section 18(3)). Therefore, no output tax has to be accounted for.

  \[ - \quad \text{(2)} \]

**Transaction 2** (Function)

(a) **Input tax**

- Function – input tax denied – refer to section 1(1) of the VAT Act, the definition of “entertainment” (for example the provision of any food, beverage and accommodation) and section 17(2).

  \[ - \quad \text{(1)} \]

- Banner at entrance – input tax denied as it is part of entertainment (section 17(2))

  \[ - \quad \text{(1)} \]

- Banner inside – claim input tax, as it is advertising: \[ \frac{14}{114} \times R1\,539 = 189 \quad \text{(1)} \]

  \[ 189 \quad \text{(3)} \]

**Transaction 3** (Excess payment)

(a) If the company does not refund the R1 000 within four months of receipt thereof, it must account for deemed output tax of \[ \frac{14}{114} \times R1\,000 = R123 \] (section 8(27) and section 10(26)) - which is 2 July 2017, thus the August 2017 tax period.

  \[ 123 \quad \text{(3)} \]

(b) When the amount is refunded during September 2017 (the October 2017 tax period), an adjustment equal to the tax fraction of the overpayment is allowed: \[ \frac{14}{114} \times R1\,000 = R123 \] to be claimed as input tax (section 16(3)(m))

  \[ 123 \quad \text{(2)} \]

  \[ 5 \]
QUESTION 17 – SUGGESTED SOLUTION (continued)

Transaction 4 (Second-hand goods)

(a) Input tax

Although John is a connected person, the sale took place at fair market value and the company can claim a full input tax credit. Section 10(4) is therefore not applicable.

Purchase of second-hand furniture

Notional input tax – second-hand goods: 14/114 x R25 000 = R3 070 (Paragraph (b) of the definition of “input tax” in section 1(1))

Purchase of bakkie (paid only R6 000 and may only claim notional input tax on second hand goods to the extent that payment has been effected – section 16(3)(a)(i) and 16(3)(b)(i)):

14/114 x R6 000 = R737

Total 3 807

(b) Output tax will be accounted for on the sale of the bakkie as follows: 14/114 x R48 000. The time of supply will be 10 May 2017, on the earliest of the issue of an invoice or payment received, therefore, the tax period ending June 2017 (refer to note 2 at the end of the solution of Part A).

Input tax in regard of the purchase of the bakkie will be deductible in the tax period ending June 2017 (time of supply for the acquisition of second hand goods being when and to the extent that payment is received – sections 16(3)(a)(ii)(aa) and 16(3)(b)(i)). Therefore input tax claim in respect of the bakkie will be R40 000 x 14/114 = R4 912

Total 4 912

Transaction 5 (General)

• Although the house was only used 40% for the making of taxable supplies, the company must levy 14% output tax on 100% of the selling price of the house (section 8(16) – goods acquired partly for use in the course of making taxable supplies and thereafter supplied shall be deemed to be made wholly in the course of his enterprise).

∴ Output tax = 14/114 x R1 400 000

171 930

• The company may however claim input tax in terms of section 16(3)(h) equal to the tax fraction (14/114) multiplied by the lesser of the adjusted cost (R1 250 000) or open market value at the date it is deemed to be supplied (R1 400 000) x % non-taxable supplies (before the current supply was made).

Claim: 14/114 x R1 250 000 x 60% = R92 105

Total 92 105

Note 1:
The labour included in the invoice from Electrical Plumbing (Pty) Ltd will attract VAT, as it is part of a service, as defined in section 1(1), supplied by one company to another. The labour expenses that JD Incorporated paid directly to casuals or labourers hired from the street, will not have any VAT implications, as the labourers are not carrying on an “enterprise” as defined in section 1(1).
Note 2:
The output tax payable on the second-hand bakkie will be payable on the full consideration, as it will only be calculated on the original purchase price if the second-hand goods on which a notional input tax was claimed, is later exported (see section 10(12)).

PART B

(a)  

<table>
<thead>
<tr>
<th>2017 Year of assessment</th>
<th>R Total amount</th>
<th>R Exempt</th>
<th>R Taxable</th>
<th>R Donations tax @ 20%</th>
</tr>
</thead>
<tbody>
<tr>
<td>March 2016 – February 2017</td>
<td>Contributions to church (R1000 x 12) – exempt i.t.o. section 56(1)(h)</td>
<td>12 000</td>
<td>(12 000)</td>
<td>-</td>
</tr>
<tr>
<td>June 2016</td>
<td>Wedding gift to Sandy – use part of section 56(2)(b) exemption of R100 000 per annum</td>
<td>8 000</td>
<td>(8 000)</td>
<td>-</td>
</tr>
<tr>
<td>February 2017</td>
<td>Sale of house to mother (R400 000 – R250 000) - use section 56(2)(b) exemption (R100 000 – R8 000)</td>
<td>150 000</td>
<td>(92 000)</td>
<td>58 000</td>
</tr>
<tr>
<td></td>
<td>R100 000 interest-free loan not a donation for donations tax (only for section 7) (interest-free loan not to a trust)</td>
<td>-</td>
<td>-</td>
<td>-</td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>2018 Year of assessment</th>
<th>R Total amount</th>
<th>R Exempt</th>
<th>R Taxable</th>
<th>R Donations tax @ 20%</th>
</tr>
</thead>
<tbody>
<tr>
<td>March 2017</td>
<td>Donation to wife (exempt in terms of section 56(1)(b))</td>
<td>142 000</td>
<td>(142 000)</td>
<td>-</td>
</tr>
<tr>
<td></td>
<td>Paintings (first R100 000 per annum exempt – section 56(2)(b)) (Note 1)</td>
<td>180 000</td>
<td>(100 000)</td>
<td>80 000</td>
</tr>
</tbody>
</table>

Note 1:
Both the donations in March 2017 fall into the following (2018) year of assessment and the annual R100 000 section 56(2)(b) exemption is therefore once again available.
QUESTION 18

Value-Added Services (“VAS”), a small firm in Pretoria, specialises in tax-related services and consulting. You have been employed by VAS for the past three years as a manager and have been confronted with the following problems and queries (all amounts INCLUDE VAT (if applicable) and all parties are registered VAT vendors and South African residents, unless specifically stated otherwise.)

QUERY 1

Flex Limited (“Flex”) is a resident company that manufactures multi-vitamins that is sold both locally and internationally. Flex has a June year-end and a one-month VAT-period.

Flex purchased a rent-producing property (situated in South Africa) from a non-vendor for cash at its market value of R3 250 000 during February 2015. Transfer duty of R177 000 was paid by Flex on 20 April 2015, the day that the property was registered in the company’s name.

The rent-producing property consists of commercial offices (60%) and residential flats (40%). SARS also accepts this ratio for VAT apportionment purposes.

Flex decided to sell the rent-producing property as a going concern to Echinea Limited (a registered vendor for VAT) for R4 500 000 (excluding VAT) on 30 April 2017. Echinea Limited will settle the full purchase consideration immediately and will continue to utilize the property as offices and flats in the same proportion as it was previously used by Flex.

**REQUIRED**

<table>
<thead>
<tr>
<th>Marks</th>
</tr>
</thead>
<tbody>
<tr>
<td>(a) Calculate, supported by references to legislation, the input tax that Flex could claim on the original purchase of the rent-producing property in 2015.</td>
</tr>
<tr>
<td>(b) Discuss, supported by calculations, all the VAT implications (including time of supply) of the proposed sale of the property for both Flex and Echinea Limited. You may assume that the transaction will be classified as the sale of a going concern in terms of section 11(1)(e) of the VAT Act.</td>
</tr>
</tbody>
</table>

QUERY 2

Ballet (Pty) Ltd (“Ballet”) is a resident company that manufactures and sells leather ballet shoes both locally and internationally. Ballet has a two-month tax period (ending February, April, June, etc.) and makes only taxable supplies.

You have been requested to assist Ballet in calculating their VAT liability for the tax period ending June 2017. The net VAT liability due to SARS is R5 467 800, before the following transactions have been taken into account:
QUESTION 18  (continued)

- Direct export sales of ballet shoes to the United Kingdom  
  R  570 000

- Indemnity payment received
  A laptop, purchased in 2014 for R5 700 was stolen on 15 May 2017. The insurance company paid out an indemnity payment of R7 980 on 15 June 2017, on which date Ballet purchased a new laptop for R10 260.  
  R  10 260

- Interest on current account received  
  R  53 423

- Transport expenses incurred for business purposes, which consists of:  
  R  73 229
  - Air tickets for local flights  
    R  13 680
  - Air tickets for international flights  
    R  56 000
  - Car hire  
    R  2 003
  - The hire of the motor cars, as defined, include insurance of R114, maintenance expenses of R171 and petrol expenses of R350.
  - Taxi fares paid for sales persons (when on business) who do not own their own cars  
    R  1 546

- Depreciation written off for accounting purposes for May and June 2017  
  R  435 000

- Company car
  The managing director has the exclusive use of a Toyota Fortuner (a motor car as defined), which the company purchased 1 January 2017 for R304 950 from which date he used it. The managing director bears the full cost of maintaining the vehicle and also paid R450 to Ballet for fuel.

### REQUIRED

<table>
<thead>
<tr>
<th>Marks</th>
</tr>
</thead>
<tbody>
<tr>
<td>Calculate the VAT liability for Ballet for the tax period ending June 2017. Show all your calculations and round off all amounts to the nearest rand.</td>
</tr>
</tbody>
</table>
QUESTION 18 – SUGGESTED SOLUTION

QUERY 1

Part (a)

- The building is a “second-hand good” as defined, purchased from a non-vendor and therefore Flex was entitled to a notional input tax deduction at acquisition.
- The notional input tax is calculated by using the tax fraction and applying it to the lesser of consideration in money or market value \((14/114 \times R3\ 250\ 000 = R399\ 123)\). (Section 1(1), definition of input tax, sub-paragraph (b)).
- As the building is used to make both taxable (60%) and exempt supplies (40%), input tax must be apportioned (section 17(1)).
- The input tax that Flex could deduct in 2015 was \(R399\ 123 \times 60\% = R239\ 474\) (section 17(1)).
- The input tax could be claimed at the earlier of date of payment or registration (section 9(3)(d)), but input tax could only be claimed on the date of registration of the building in the name of the company (section 16(3)(a)(ii)(bb)(A)) and is further limited to the extent that the payment had been made (section 16(3)(a)(ii)(aa)). Therefore as the building was purchased for cash during February 2015 but registration only took place on 20 April 2015 and the full consideration had been paid during February 2015 the notional input of R239 474 could be claimed on 20 April 2015 (April 2015 tax period).

Part (b)

VAT implications for Flex

The sale of the property to Echinea Limited as a going concern is a zero-rated supply, as the property was used mainly (more than 50% (60% - renting of commercial offices, which is a taxable supply)) for taxable supplies. Thus, output tax is Rnil.

Flex will however be entitled to claim an additional input tax in terms of section 16(3)(h) of the VAT Act on the disposal, calculated as follows:

\[
A = \text{tax fraction} = 14/114 \\
B = \text{lesser of adjusted cost (R3 250 000) and the current open market value (R4 500 000).} \\
C = \text{percentage of non-taxable supplies = 40%}
\]

Therefore:
\[
14/114 \times R\ 3\ 250\ 000 \times 40\% = R159\ 649.
\]

Thus a section 16(3)(h)-input tax of R159 649 can be claimed in the April 2017 tax period in which the date of the disposal (30 April 2017), falls.
QUESTION 18 – SUGGESTED SOLUTION (continued)

Echinea Limited

Echinea Limited will not be able to claim any input tax on the purchase, as it was a zero-rated supply (no VAT was payable on the purchase). (Note that since the transaction was subject to VAT, even though at 0%, transfer duty will not be payable).

Echinea Limited will have to make a section 18A-adjustment to output tax, since the property was acquired as a 100% taxable supply at a rate of 0%, but it will be partly used for purposes other than making taxable supplies (40% used for exempt supply of dwellings for rentals (section 12(1)(c))).

The section 18A-adjustment will be made during the tax period (tax period in which 30 April 2017 falls) that the supply (purchase) was made.

The adjustment will be:

<table>
<thead>
<tr>
<th>Description</th>
<th>Amount</th>
</tr>
</thead>
<tbody>
<tr>
<td>Full cost of the going concern purchase</td>
<td>R 4 500 000</td>
</tr>
<tr>
<td>Less: % intended to be used for taxable supplies (commercial offices – 60%)</td>
<td>(2 700 000)</td>
</tr>
<tr>
<td>(or R 4 500 000 x 40%)</td>
<td>1 800 000</td>
</tr>
<tr>
<td>Section 18A-adjustment to output tax (14% thereof)</td>
<td>252 000</td>
</tr>
<tr>
<td>Total</td>
<td>13</td>
</tr>
<tr>
<td>Total for query 1</td>
<td>17</td>
</tr>
</tbody>
</table>

QUERY 2 12 marks

VAT liability for Ballet for the tax period ending 30 June 2017

<table>
<thead>
<tr>
<th>Description</th>
<th>Amount</th>
</tr>
</thead>
<tbody>
<tr>
<td>Net VAT liability due to SARS</td>
<td>R 5 467 800</td>
</tr>
<tr>
<td>Export Zero-rated (section 11(1)(a)(i))</td>
<td>- (1)</td>
</tr>
<tr>
<td>Indemnity payment – Deemed supply – R 7 980 x 14/114 (section 8(8))</td>
<td>980 (1)</td>
</tr>
<tr>
<td>Computer/laptop Purchase – R 10 260 x 14/114</td>
<td>(1 260) (1)</td>
</tr>
<tr>
<td>Interest Financial service and exempt supply (section 2(1)(f) read with section 12(a))</td>
<td>- (1)</td>
</tr>
<tr>
<td>Transport expenses</td>
<td></td>
</tr>
<tr>
<td>• Local air tickets – taxable supply – R 13 680 x 14/114</td>
<td>(1 680) (1)</td>
</tr>
<tr>
<td>• International flights – zero-rated (section 11(2)(a))</td>
<td>- (1)</td>
</tr>
<tr>
<td>• Car hire: input tax is denied i.t.o. section 17(2)(c)) – (R 2 003 - R 114 - R 171 - R 350) = R 1 368 (cost of car hire only)</td>
<td>- (1)</td>
</tr>
<tr>
<td>• Insurance – R 114 x 14/114</td>
<td>(14) (½)</td>
</tr>
<tr>
<td>• Maintenance – R 171 x 14/114</td>
<td>(21) (½)</td>
</tr>
<tr>
<td>• Petrol – zero-rated (section 11(1)(h))</td>
<td>- (½)</td>
</tr>
<tr>
<td>• Taxi fares – Exempt transport of fare-paying passengers (section 12(g))</td>
<td>- (1)</td>
</tr>
<tr>
<td>Description</td>
<td>Solution</td>
</tr>
<tr>
<td>----------------------</td>
<td>--------------------------------------------------------------------------</td>
</tr>
<tr>
<td>Depreciation</td>
<td>Not a taxable supply (accounting entry)</td>
</tr>
<tr>
<td>Company car</td>
<td>Fringe benefit i.t.o. section 18(3), thus a deemed supply:</td>
</tr>
<tr>
<td></td>
<td>( { (\text{R}304,950 \times \frac{100}{114} = \text{R}267,500 \text{ (determined value)} \times \frac{0.3}{100}) ) – R85 \text{ (maintenance)} } = \text{R}717.50 \times \frac{14}{114} \times 2 \text{ months}</td>
</tr>
<tr>
<td></td>
<td>( \text{Note: Petrol is not deducted as it is a zero-rated supply} )</td>
</tr>
</tbody>
</table>

\[ \text{R} \quad (\frac{1}{2}) \]

\[ \text{176 (2)} \]

\[ \frac{5,465,981}{12} \]
This question consists of two unrelated parts (PART A and PART B).

PART A

All taxpayers referred to are South African residents, unless stated otherwise. All amounts, where applicable, include VAT.

Building (Pty) Ltd (not a Small Business Corporation) continuously builds residential units for resale. The company has a 31 December year-end and is registered on the invoice basis as a vendor for VAT purposes with one monthly tax periods.

On 31 January 2016, Building (Pty) Ltd purchased a property, situated in South Africa, from a South African resident (a VAT vendor) at the market value of R3 500 000. Building (Pty) Ltd paid the purchase price on 29 February 2016, the day of registration of the property in the name of the company. The company claimed the correct amount of input tax.

The company purchased the property with the intention of developing ten residential units for resale. The residential units were completed on 30 August 2016, but the company was not able to sell them, because of a slump in the property market.

On 2 January 2017, Building (Pty) Ltd entered into agreements for the letting of the ten units until the company could find suitable buyers.

Assume that the company will be able to sell seven of these units on 2 January 2018, 16 months after their completion, at the open market value of R1 500 000 each, payable in two equal instalments on 31 January 2018 and 28 February 2018 respectively. Registration of the units in the name of the new owners will take place on 3 March 2018. The other 3 units will still be on hand at 31 December 2020.

REQURED

<table>
<thead>
<tr>
<th>REQUIRED</th>
<th>Marks</th>
</tr>
</thead>
<tbody>
<tr>
<td>1. Discuss whether Building (Pty) Ltd meets the requirements for the application of section 18B of the VAT Act in respect of entering into lease agreements with regard to the residential units instead of selling them.</td>
<td>2</td>
</tr>
<tr>
<td>2. Explain the difference in the VAT implications if:</td>
<td>2</td>
</tr>
<tr>
<td>- Building (Pty) Ltd elects to apply section 18B of the VAT Act, or</td>
<td></td>
</tr>
<tr>
<td>- if it does not elect to apply section 18B on the day that the lease agreements are entered into.</td>
<td></td>
</tr>
<tr>
<td>3. Calculate the input and/or output tax in respect of the sale of the seven units on 2 January 2018, and also discuss the time of supply and the tax period in which the VAT will be payable or claimable.</td>
<td>4</td>
</tr>
<tr>
<td>4. Discuss the VAT implications in respect of the units that are not sold on 2 January 2018.</td>
<td>2</td>
</tr>
</tbody>
</table>
QUESTION 19 (continued)

PART B 10 marks

Beauty, a sole trader trading as Beauty Interior Designs, was registered on the invoice basis for VAT purposes on a two-monthly basis, with tax periods ending on April, June, August, October, December and February of each year.

Beauty provided you with the following list of assets and liabilities of Beauty Interior Designs as at 10 January 2017:

<table>
<thead>
<tr>
<th>Note</th>
<th>Description</th>
<th>Cost (excluding VAT) R</th>
<th>Open market value R</th>
</tr>
</thead>
<tbody>
<tr>
<td>1</td>
<td>Rent-producing property</td>
<td>4 500 000</td>
<td>4 800 000</td>
</tr>
<tr>
<td>2</td>
<td>&quot;Motor car&quot;, as defined in the VAT Act – used solely for business purposes</td>
<td>220 000</td>
<td>160 000</td>
</tr>
<tr>
<td>3</td>
<td>Office furniture and equipment – used solely for business purposes</td>
<td>90 000</td>
<td>95 000</td>
</tr>
</tbody>
</table>

**Notes:**

1. Beauty purchased the rent-producing property (situated in South Africa) from a non-vendor at its market value of R4 500 000 during February 2016. Transfer duty of R332 500 was paid in respect of the purchase of the building. The rent-producing property consists of commercial offices (55%) and residential flats (45%). The South African Revenue Services accepted this ratio for VAT apportionment purposes.

Beauty sold the rent-producing property as a going concern in terms of section 11(1)(e) of the VAT Act to Fashion (Pty) Ltd (a registered VAT vendor) at the open market value of the property of R4 800 000 on 10 January 2017. Fashion (Pty) Ltd settled the consideration immediately and continued to utilize the property as offices and flats in the same proportion as it was previously used by Beauty Interior Designs.

2. Immediately after the sale of the rent-producing property, on 12 January 2017, Beauty deregistered as a vendor for VAT purposes.

The following is the debtors’ age analysis on the services rendered on credit:

<table>
<thead>
<tr>
<th></th>
<th>30 days</th>
<th>60 days</th>
<th>90 days</th>
<th>Total</th>
</tr>
</thead>
<tbody>
<tr>
<td>Amount (R) including VAT</td>
<td>25 650</td>
<td>17 100</td>
<td>8 550</td>
<td>51 300</td>
</tr>
</tbody>
</table>

Beauty is of the opinion that the 90 days outstanding debtors in the amount of R8 550 will not be recoverable and consequently wrote it off on 11 January 2017. Beauty does not charge any interest on outstanding accounts.
QUESTION 19  (continued)

The following is the creditors’ age analysis:

<table>
<thead>
<tr>
<th></th>
<th>30 days</th>
<th>Older than 370 days</th>
<th>Total</th>
</tr>
</thead>
<tbody>
<tr>
<td>Amount (R) including VAT</td>
<td>19 665</td>
<td>6 555</td>
<td>26 220</td>
</tr>
</tbody>
</table>

All these creditors were vendors and the supplies were neither exempt nor zero-rated. The creditors older than 370 days are already outstanding for more than 12 months, but no VAT adjustment has yet been accounted for. None of the assets mentioned above were funded by these creditors.

3. After the deregistration Beauty sold the office furniture and equipment to Richie, a vendor for VAT purposes, for R90 000.

**REQUIRED**

<table>
<thead>
<tr>
<th>Calculate the input and output tax in respect of notes 1 to 3 in Part B with regards to Beauty. Do not calculate the input tax in respect of the purchase of the property in note 1.</th>
<th>Marks</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>10</td>
</tr>
</tbody>
</table>
QUESTION 19 - SUGGESTED SOLUTION

PART A

1. Building (Pty) Ltd meets all the requirements for the application of section 18B.
   - The company is a developer (section 18B(1)).
   - The company constructed the residential units solely for the making of taxable supplies (sale) (section 18B(2)(a)) and subsequently temporarily applied it for the supplying of accommodation in a dwelling under an agreement for the letting thereof (section 18B(2)(b)).

2. In the absence of section 18B, the change of use of the residential units from totally making taxable supplies to totally making exempt supplies (non-taxable) in terms of section 12(c) (the letting of a dwelling under an agreement) would have led to a change in use adjustment in terms of section 18(1).
   In terms of section 18B(2), the supply of the residential units for the letting thereof, will at the date of the change of use be deemed not to be a taxable supply in the course or furtherance of Building (Pty) Ltd’s enterprise – thus on 2 January 2017 no change in use has to be accounted for.
   If a developer lets the units he developed instead of selling it, he should have a deemed output as the units are no longer built to sell (taxable supply) but let for residential purposes (exempt). Section 18B provides relief in that he does not have to declare output if he only let the units for a period of time. This was necessary due to the downturn in the property market when developers could not sell their residential units which they developed and had to sell it. (Refer to SILKE page 1121)

3. Output tax
   \[(R1 \, 500 \, 000 \times 7) \times \frac{14}{114} = R \, 1 \, 289 \, 474\]  
   The time of supply is the earlier of the date of payment or the date of registration of the property in the deeds office (section 9(3)(d)), but limited to the extent that payment of the consideration has been received (section 16(4))
   Therefore R1 289 474 x 50% = R644 737 will be accounted for on 31 January 2018 (January 2018 tax period) and R644 737 will be accounted for on 28 February 2018 (February 2018 tax period).

4. The units not sold will be deemed to be supplied by way of a taxable supply 36 months after entering into the lease agreements for the letting thereof (thus 2 January 2019) or when permanently used for non-taxable supplies, thus 36 months from 2 January 2017, therfore 2 January 2020.

   The units will be deemed to be supplied at the open market value as on 2 January 2020 and the output tax liability will be 14/114 x open market value.
1. Going concern:

<table>
<thead>
<tr>
<th>Description</th>
<th>Output tax</th>
<th>Input tax</th>
</tr>
</thead>
<tbody>
<tr>
<td>R4 800 000 x 0% (zero rated)</td>
<td>-</td>
<td>(1)</td>
</tr>
<tr>
<td>Section 16(3)(h) – R4 500 000 (lower of cost or OMV) x 14/114 x 45%</td>
<td>-</td>
<td>248 684</td>
</tr>
</tbody>
</table>

2. Deemed supplies in terms of section 8(2) on ceasing to be a vendor:

- Motor car – input tax was denied on acquisition (section 17(2)(c)), therefore no deemed supply

- Office furniture and equipment – lower of cost or OMV (s 10(5))
  
  Cost = R90 000 x 114/100 = R102 600
  
  Thus R95 000 x 14/114 = 11 667

3. Sale of furniture and equipment

- Beauty is no longer a VAT vendor (after deregistration)

  - - (1)
QUESTION 20

You are a senior tax consultant in the VAT division of Phakwena Consulting (Pty) Ltd in Johannesburg, South Africa. Your client – Research.net – is a company situated in the United States of America. Research.net is a web-based company that provides e-books that can be downloaded and used by children when doing research on various school projects.

Research.net received 100,000 hits from South Africa during the period 1 April 2017 to 30 September 2017 and 2,000 e-books were downloaded as a result of this. All the downloads were paid by credit cards issued by South African Banks. The value of the e-books downloaded exceeded R50,000 on 25 August 2017. It is anticipated that the number of school children that will make use of Research.net will double during the period 1 October 2017 to 31 March 2018 with the value of e-books downloaded during the same period increasing to R120,000.

**REQUIRED**

<table>
<thead>
<tr>
<th></th>
<th>Marks</th>
</tr>
</thead>
<tbody>
<tr>
<td>1.1</td>
<td>Your client requested your opinion as to whether it will have to register as a vendor in South Africa and if so from which date. Please refer to all relevant provisions of the Value-Added Tax Act 89 of 1991 (as amended).</td>
</tr>
<tr>
<td>1.2</td>
<td>If it is assumed that Research.net is not liable to register as a vendor for VAT purposes in South Africa, please indicate, with reference to the VAT Act, whether any VAT is payable on the download of the e-books and who will be liable to pay the VAT, by when it should be paid and how the VAT should be calculated.</td>
</tr>
</tbody>
</table>
QUESTION 20 - SUGGESTED SOLUTION

1.1 To ascertain whether Research.net should register as a vendor in South Africa, it should firstly be determined whether Research.net is carrying on an enterprise in or partly in the Republic in terms of the definition of ‘enterprise’ in section 1(1) of the Act:

Included in the definition of enterprise (paragraph (b)(vi)) is the supply of electronic services by a person from a place in an export country where at least two of the following circumstances are present:

(aa) the recipient is a resident of the Republic; or
(bb) any payment was done via a Bank registered in terms of the Bank Act;
(cc) the recipient of those electronic services has a business or residential or postal address in the Republic where a tax invoice may be delivered.

As the activities of Research.net satisfy at least two of the above criteria of par (b)(vi) of the definition of enterprise, Research.net is carrying on an enterprise in the Republic.

Following this, it must be ascertained whether Research.net meets the threshold for compulsory registration as a VAT vendor:

In terms of section 23(1A) a person who carries on an enterprise in terms of para-(b)(vi) to the definition of an enterprise will be liable for registration at the end of the month when the total value of the taxable supplies exceeds R50 000.

Research.net will therefore be liable to register as a VAT vendor on 31 August 2017.

max [5]

1.2 The purchase and download of e-books via the internet in this case qualifies as an imported service in terms of the definition in section 1(1) as the services will not be consumed for the purpose of making taxable supplies.

In terms of section 7(1)(c) of the Act, VAT is payable at the standard rate of 14% on imported services as defined in section 1(1).

In terms of section 7(2) the VAT should be paid by the recipient of the imported service.

In terms of section 14(1), read with section 14(2), the VAT should be paid within 30 days from the earlier of the date of invoice issued by the supplier or the time any payment is made.

In terms of section 14(3) the value for the consideration of the supply will be the greater of where the consideration is in money, the amount of the money; where the consideration is not in money, the open market value of the supply.

max [10]
PART A

Fabulous Fashions (Pty) Ltd is a South African clothing retail company that is registered as a category B VAT vendor. The company has a February year-end. The company operates from various premises and has decided to sell one of its buildings, as it became too difficult to manage.

1. The property was sold to Simply Stunning CC, a (not connected) VAT vendor, at its open market value of R3 800 000 (of which R1 200 000 was for the land and R2 600 000 for the building) on 15 August 2016. The property was not sold as a going concern. The property was registered in the name of the new owner on 5 October 2016 and on this date the total purchase price was settled.

The property was originally purchased from a registered VAT vendor (not connected) on 1 March 2015 for R3 220 000, being R1 000 000 for the land and the balance for the building. The building consisted of three floors. Fabulous Fashions (Pty) Ltd used 70% of the square area of the entire property to conduct its clothing retail business, whereas the remaining 30% of the square area comprised residential flats, let to various tenants. The Commissioner approved the use of surface area as the apportionment method for purposes of claiming the input tax on acquisition of the building. Fabulous Fashions (Pty) Ltd claimed the full amount of input tax that was available to the company.

2. On 10 October 2016, Fabulous Fashions (Pty) Ltd purchased a second-hand property from Mr Wright (not connected), who used the property for residential purposes. Fabulous Fashions (Pty) Ltd bought the property for the purposes of its clothing retail business. The purchase price of the property for Fabulous Fashions (Pty) Ltd amounted to R1 800 000 (the open market value of the property was R2 million). Fabulous Fashions (Pty) Ltd paid a deposit of R200 000 to Mr Wright on 15 October 2016 as part payment of the purchase price. The outstanding balance is financed by a loan granted by Mr Wright. Interest is charged at the official interest rate. The property was registered in the name of Fabulous Fashions (Pty) Ltd on 10 December 2016. Transfer duty of R144 000 was paid by Fabulous Fashions (Pty) Ltd on the date of registration. The cost of the conversion of the building into offices amounted to R220 000 and was invoiced and paid on 31 January 2017.

At 28 February 2017, Fabulous Fashions (Pty) Ltd had made two payments of R200 000 each in respect of the loan. These payments were made on 1 January 2017 (R200 000) and 1 February 2017 (R200 000) respectively. Interest in respect of the loan has been paid up to 28 February 2017 and can be ignored.

<table>
<thead>
<tr>
<th>REQUIRED</th>
<th>Marks</th>
</tr>
</thead>
<tbody>
<tr>
<td>(a) Calculate the VAT consequences for Fabulous Fashions (Pty) Ltd in respect of the sale of the property during its 2017 year of assessment. No reference needs to be made to tax periods or time of supply.</td>
<td>3</td>
</tr>
<tr>
<td>(b) Discuss, with specific reference to the time and value of supply, the VAT implications for Fabulous Fashions (Pty) Ltd in respect of the fixed property that it purchased from Mr Wright. Refer to VAT legislation and address all payments in your discussion.</td>
<td>10</td>
</tr>
</tbody>
</table>
QUESTION 21 (continued)

<table>
<thead>
<tr>
<th>REQUIRED:</th>
<th>Marks</th>
</tr>
</thead>
<tbody>
<tr>
<td>(c) Calculate the VAT implications (ignore the time of supply) for Simply Stunning CC in respect of the purchase of the property for R3 800 000 under 1 above, if the sale transaction were to be classified as a going concern in terms of section 11(1)(e) of the VAT Act. Assume that Simply Stunning CC will continue to use the property for its clothing store and the letting of the flats for residential purposes, in the same proportion as previously used by Fabulous Fashions (Pty) Ltd. Support your calculation with reasons.</td>
<td>4</td>
</tr>
</tbody>
</table>

PART B 3 marks

On 20 January 2017, Fabulous Fashions (Pty) Ltd donated stock with a market value of R120 000 (cost price was R100 000) to its foreign subsidiary, Fashionable Trends Plc. Fashionable Trends Plc is wholly owned by Fabulous Fashions (Pty) Ltd and registered in the United Kingdom.

<table>
<thead>
<tr>
<th>REQUIRED</th>
<th>Marks</th>
</tr>
</thead>
<tbody>
<tr>
<td>Calculate Fabulous Fashions (Pty) Ltd’s donations tax liability, if any, in respect of the donation made to its wholly owned foreign subsidiary. Substantiate your calculation with reasons. Furthermore, if donations tax is payable, indicate when the donations tax is due to SARS. Assume that this was the only donation made by Fabulous Fashions (Pty) Ltd in respect of its 2017 year of assessment.</td>
<td>3</td>
</tr>
</tbody>
</table>

Source: Unisa TAX4862 Test 1 2014
QUESTION 21 – SUGGESTED SOLUTION

PART A

(a)
Sale of property:  
Account for output tax (section 7(1)(a) of R3 800 000 x 14/114  
In terms of section 8(16) of the VAT Act, the supply is deemed to be made wholly in  
the course of or in the furtherance of an enterprise, thus VAT charged on 100% of the  
selling price.  
Section 16(3)(h)  
Claim input tax of R3 220 000 (lesser of adjusted cost or open market value (R3 800  
000)) x 30% x 14/114  

(b)  
Note that category B VAT vendors have two month tax periods that end on the last day of  
February, April, June< August, October and December. 
Notional input tax can be claimed (although transfer duty was paid) in respect of the second-hand  
property purchased from a non-vendor (par (b) of the definition of input tax in section 1(1)).  
Input tax can be claimed on the lower of the cost of R1 800 000 or open market value of  
R2 000 000; thus, use R1 800 000 (par (b) of the definition of input tax in section 1(1))  
The tax fraction of 14/114 must be applied to the cost of R1 800 000 (par (b) of the definition of  
input tax in section 1(1)); thus, input tax of R1 800 000 x 14/114 = R221 053 can be claimed.  
In terms of section 9(3)(d), the time of supply of the fixed property is the earlier of date of regis  
tration or the date of any payment, but section 16(3)(a)(ii)(aa) determines that Fabulous Fashions  
(Pty) Ltd can only claim input tax to the extent that payment of the consideration has been effec  
ted.  
Furthermore, section 16(3)(a)(ii)(aa) is subject to the provisions of section 16(3)(a)(ii)(bb) and in  
terms of section 16(3)(a)(ii)(bb)(A), input tax may only be claimed once the transfer of the fixed  
property has been registered in the deeds registry.  
Therefore, the input tax in respect of the deposit of R200 000, which was paid on 15 October 2016,  
may be claimed in the December 2016 tax period (since the property was registered in Fabulous  
Fashions (Pty) Ltd’s name on 10 December 2016). The input tax claim is R200 000 x 14/114 =  
R24 561 (or R221 053 x 200 000/1 800 000 = R24 561).  
A further input tax of R49 123 (R400 000 x 14/114) in respect of the loan repayments may be  
claimed in the February 2017 tax period.  
In addition, input tax of R27 018 on the conversion cost (R220 000 x 14/114) can also be claimed  
in the February 2017 tax period.
QUESTION 21 - SUGGESTED SOLUTION (continued)

(c) Simply Stunning CC will not be able to claim any input tax on the purchase, although a taxable supply was made to the CC it was made at 0% (no VAT was payable on the purchase). (Note that since the transaction was subject to VAT, even though at 0%, transfer duty will not be payable).

Simply Stunning CC will have to make a section 18A-adjustment to output tax, since the property was acquired as a 100% taxable supply at a rate of 0%, but it will be partly used for purposes other than making taxable supplies (30% used for exempt supply of dwellings for rentals (section 12(1)(c))).

The adjustment will be:

<table>
<thead>
<tr>
<th>Description</th>
<th>Amount</th>
</tr>
</thead>
<tbody>
<tr>
<td>Full cost of the going concern purchase</td>
<td>R3 800 000</td>
</tr>
<tr>
<td>Less: % intended to be used for taxable supplies (commercial – 70%)</td>
<td>(2 660 000)</td>
</tr>
<tr>
<td>(or R3 800 000 x 30%)</td>
<td>1 140 000</td>
</tr>
<tr>
<td>Section 18A-adjustment to output tax (14% thereof)</td>
<td>159 600</td>
</tr>
</tbody>
</table>

PART B

Donation to foreign subsidiary (valued at market value – section 62(1)(d))

<table>
<thead>
<tr>
<th>Description</th>
<th>Amount</th>
</tr>
</thead>
<tbody>
<tr>
<td>No specific exemption applies (section 56(1)(r) cannot apply, as donee is non-resident), general exemption under section 56(2)(a) also not available, as not a casual gift</td>
<td>120 000</td>
</tr>
<tr>
<td>Donations tax at 20% (section 64)</td>
<td>24 000</td>
</tr>
</tbody>
</table>

Payable by the end of the month following the month during which a donation takes effect (section 60), thus not later than 28 February 2017.
QUESTION 22
PART A

Mr Molefe and Mr Ebrahim commenced a computer software maintenance business (Netsoft) in a 50:50 partnership on 1 November 2016. Netsoft concluded annual computer software maintenance contracts to maintain the computer software and networks of a number of large corporations. The total value of these annual contracts on 30 November 2016 amounted to R798 000 (including VAT). During January 2017, Netsoft concluded more contracts and by 31 January 2017 the total value of their annual contracts concluded (in writing) amounted to R1 368 000 (including VAT).

During the period 1 November 2016 until 28 February 2017, Netsoft entered into the following transactions (Netsoft purchases only from VAT vendors and all amounts include VAT, unless stated otherwise):

1. A residential property was purchased from a non-vendor for R1 800 000 during November 2016. Transfer duty amounted to R49 000 and was paid during January 2017. The purchase price of the property was paid on the date of registration of the property in the deeds office, i.e. 1 February 2017.

   The property consisted of a house together with a double garage. The double garage was converted into a garden flat and will be let as residential accommodation to a person not related to Netsoft. The total estimated rent receivable for the 12 month period from 1 February 2017 should amount to R48 000 (excluding VAT). The house was converted into offices for use by Netsoft, both for the administration of the software maintenance business and for the letting of the garden flat. Both of the conversions to the buildings were done during January 2017. The cost of converting the double garage into a garden flat amounted to R125 400 and the cost of converting the house into offices amounted to R319 200. Assume that an invoice will be received from the contractor in February 2017 and that both amounts will be paid in February 2017. The garden flat comprises 4% of the total floor space of the buildings on the property. You may assume that this ratio will be accepted by SARS as the method for any apportionment, if applicable.

2. A single cab Yotota LDV (“bakkie”) with a cash value of R239 400 was purchased in February 2017 and financed by way of a financial lease agreement. This agreement meets the requirements of the definition of an instalment credit agreement in the VAT Act. This vehicle is used exclusively for the computer software maintenance part of the business. The monthly lease payment amounts to R5 447. The February 2017 payment consists of finance charges of R2 593 and a R2 854 capital repayment.

   The following expenses were paid during February 2017 in respect of the bakkie:
   
   Fuel .................................................................................................................. R 2 870
   Purchase and installation of a canopy ................................................................. R 9 348

3. A number of computers were needed in the business (software maintenance and residential letting) and were consequently obtained at a cash cost of R160 000 (excluding VAT) and financed by way of a 3-year operating lease during February 2017. The operating lease meets the requirements of the definition of a rental agreement in the VAT Act. The monthly rental amount for February 2017 amounted to R6 146, of which R1 976 (excluding VAT) was for finance charges and R4 170 in respect of capital repayments.

   A local area network (LAN) as well as a wireless internet connection was set up and the computers were linked to these networks. Netsoft had to bear the cost of this installation, which amounted to R32 376. An invoice was issued on 15 February 2017. Assume that the amount will only be paid by Netsoft on 3 March 2017.
QUESTION 22 (continued)

4. Assume that on 18 February 2017, lightning caused severe damage to the LAN (network) due to the fact that the surge and lightning protection unit failed. The cost of repairing the network amounted to R9 804 and this amount was paid by Netsoft during February 2017. Netsoft claimed from its short-term insurer to be indemnified for this loss. Assume that the insurer paid R8 664 into Netsoft’s bank account on 24 February 2017, to indemnify the partnership for the loss suffered in repairing the network. Furthermore, assume that on 25 February 2017, the insurer replaced the faulty surge and lightning protection unit at a cost of R13 680.

5. Assume that the invoices issued (on 28 February 2017) to clients for computer software and network maintenance done by Netsoft during February 2017 amounted to R136 800. However, assume that one client paid an amount of R11 400 during February 2017 (before an invoice was issued by Netsoft) for services only to be rendered in March 2017.

REQUIRED:  

<table>
<thead>
<tr>
<th>Marks</th>
</tr>
</thead>
<tbody>
<tr>
<td>(a) Discuss whether Netsoft is liable to register as a vendor for VAT purposes in terms of sections 23 and 51 of the VAT Act. Motivate and support your answer with calculations.</td>
</tr>
<tr>
<td>3</td>
</tr>
<tr>
<td>(b) On the assumption that Netsoft has in fact registered as a category B VAT vendor on the invoice basis as from 1 February 2017, calculate the output tax and input tax relating to transactions 1 to 5 mentioned above.</td>
</tr>
<tr>
<td>30</td>
</tr>
</tbody>
</table>

| PART B | 7 marks |

Mr Zeelie has made the following donations during the year of assessment ended 28 February 2017:

1. His parents struggle financially and he consequently decided to contribute a monthly amount of R3 000 towards their maintenance. These payments were made monthly from 1 March 2016 to 28 February 2017. You may assume that SARS will regard these contributions as reasonable.

2. Mr Zeelie maintains his son (22 years), his only child, who is studying full-time at a university. The study fees, books and hostel fees amounted to R40 000 and were paid on 1 March 2016. He purchased a brand new sports car of R320 000 and gave it to his son on his 22\textsuperscript{nd} birthday on 25 March 2017.

REQUIRED:  

<table>
<thead>
<tr>
<th>Marks</th>
</tr>
</thead>
<tbody>
<tr>
<td>Calculate and discuss the Donations Tax implications of these donations. Provide reasons for your answers.</td>
</tr>
<tr>
<td>7</td>
</tr>
</tbody>
</table>
PART A

(a) Registration of Netsoft as a vendor for VAT purposes

The provision of software and network maintenance qualifies as services rendered, as it is not exempt supplies, but taxable supplies.  

(½)

Residential letting constitutes exempt supplies (transaction 1). (Section 12(1)(c))  

(½)

A partnership (an unincorporated body of persons) is included as a person for purposes of the VAT Act (s 51).  

(½)

In the facts under review, Netsoft is liable to register as a VAT vendor in terms of section 23(1)(b) on 1 February 2017 as the total value of its annual contracts concluded (in writing), amounted to R1 200 000 (excluding VAT) on 31 January 2017, which exceeds the R1 million limit.  

(1½)

The annual value of residential letting (R48 000) can be ignored as it relates to an exempt supply and not a taxable supply.

References to the VAT Act in part (a) of the solution are only included for teaching purposes, therefore no marks are awarded.

(b) Output and input tax implications of transactions

The partnership is registered as a category B VAT vendor. Therefore, it has tax periods of two months ending on February, April, June, August, October and December each year.

Transaction 1:

Fixed property purchased from non-vendor

Input tax - deemed (notional) input tax on second-hand goods (par (b) of definition of input tax) – claimable as the property will be used to make partly taxable supplies.  

(1)

Denied? – Input tax not denied.

Amount – lesser of consideration or open market value (par (b) of definition of input tax) = R1 800 000 x 14/114 = R221 053.  

(1)

Apportionment - this expense relates to both the software and network maintenance (taxable supplies) part of the business as well as to the residential letting (exempt supplies) and is therefore expended only partly to make taxable supplies, BUT the de minimus-rule (at least 95%) is applicable, as the garden flat comprises only 4%, thus less than 5% of the total floor space of the buildings on the property (section 17(1)(i)) – no apportionment.  

(2)

Time – second-hand fixed property purchased from a non-vendor – section 9(3)(d) is applicable, but can only claim input tax to the extent that actual payment is made (section 16(3)(a)(ii)(aa)) (thus, promissory notes and loan accounts do not qualify), furthermore, subject to registration of the property (section 16(3)(a)(ii)(bb)(A) - claimable in February 2017.  

(2)

Rent received

Output tax – exempt supply – residential accommodation (section 12(1)(c)) - no VAT, as exempt supplies excluded from definition of an enterprise in section 1.  

(1)
Conversion of double garage into garden flat

Input tax - but it is not claimable as the garden flat will be used to make exempt supplies. (section 12(1)(c))

Conversion of house into offices

Input tax – claimable as a deduction as the offices will be used to make partly taxable supplies. Denied? – not denied.

Amount – general rule (section 10(3)) - R319 200 x 14/114 = R39 200.

Apportionment – this expense relates to both the software maintenance (taxable supplies) part of the business as well as to the (administration of) residential letting (exempt supplies) and therefore is expended only partly to make taxable supplies, BUT the de minimus-rule (at least 95% - section 17(1)(i))) is applicable, as the garden flat comprises only 4% (< 5%) of the total floor space of the property – no apportionment.

Time – general rule – invoice basis – earlier of date that invoice is issued or payment made (section 9(1)) - claimable in February 2017.

Transaction 2:

Purchase of single cab Yotota LD

Input tax – claimable due to the fact that the vehicle will be used to make only taxable supplies. Denied? – input tax not denied in terms of section 17(2)(c) as a single cab LDV is not a motor car as defined in section 1.

Amount – cash value = R239 400 x 14/114 = R29 400 (section 10(6)). (ignore monthly lease payment)

Apportionment – the question specifically stated that this expense only relates to the computer software maintenance part of the business and is therefore expended fully in the course of making taxable supplies - no apportionment.

Time – A financial lease agreement is regarded as an instalment credit agreement by the VAT Act, the timing rule is the earlier of delivery or any payment (section 9(3)(c)). The VAT on the full purchase price is therefore claimable in February 2017.

Fuel

Input tax – no VAT paid as fuel is zero-rated (section 11(1)(h)) – no VAT claimable.

Purchase and installation of canopy

Input tax – claimable due to the fact that the vehicle will be used to make only taxable supplies. Denied? – not denied.

Amount – general rule - R9 348 x 14/114 = R1 148 (section 10(3)).

Apportionment – the question stated that this expense only relates to the computer software maintenance part of the business and is therefore expended fully in the course of making taxable supplies - no apportionment.

Time – general rule – invoice basis – earlier of date that invoice is issued or payment made (section 9(1)) – claimable in February 2017.
QUESTION 22 - SUGGESTED SOLUTION (continued)

Finance charges

Input tax – This relates to an exempt supply (being a financial service (section 12(a))) and thus no VAT is claimable.
Amount – Exempt supply Rnil.  

Transaction 3:

Computers

Input tax - claimable due to the fact that the computers will be used to make partly taxable supplies.
Denied? – not denied.
Amount – general rule (section 10(3)) – R6 146 x 14/114 = R755.  
Apportionment – this expense (the whole amount paid is for rent) relates to both the software maintenance (taxable supplies) part of the business as well as to the residential letting (exempt supplies) and is therefore expended only partly to make taxable supplies, BUT the de minimus-rule (at least 95%) is applicable, as the garden flat comprises only 4% (< 5%) of the total floor space of the property – no apportionment.
Time – a rental agreement is not regarded as an instalment credit agreement by the VAT Act, the payments are deemed as successive supplies. Each successive supply is deemed to take place at the earlier of whenever any payment is due or received (paid) (section 9(3)(a)). The input tax on the monthly rental payment is therefore claimable in February 2017.  

Installation of local area network (LAN)

Input tax - claimable due to the fact that the network will be used to make partly taxable supplies.
Denied? – not denied.
Amount – general rule (section 10(3)) – R32 376 x 14/114 = R3 976.  
Apportionment – same as for computers - de minimus-rule applicable - no apportionment (section 17(1)(i)).
Time – general rule (section 9(1)) – invoice basis – earlier of date that invoice is issued or payment made – claimable in February 2017.  

Transaction 4:

Cost of repair to the network

Input tax - claimable due to the fact that the network is used to make partly taxable supplies.
Denied? – not denied.
Amount – general rule (section 10(3)) – R9 804 x 14/114 = R1 204.  
Apportionment – same as for computers - de minimus-rule applicable - no apportionment (section 17(1)(i)).
Time – general rule (section 9(1)) – invoice basis – earlier of date that invoice is issued or payment made, but can only claim if in possession of a valid tax invoice – claimable in February 2017 if the partnership has a valid tax invoice.
QUESTION 22 - SUGGESTED SOLUTION (continued)

Indemnity payment received from insurer

Output tax – deemed supply (section 8(8)).
Time – date of receipt of payment (section 8(8)) – output tax must be accounted for in February 2017.
Amount – consideration received (section 8(8)) - R8 664 x 14/114 = R1 064.
Apportionment – no apportionment of deemed proceeds.

Replacement of unit by insurer

Replacement of an asset by an insurer is not a deemed supply in terms of section 8(8), as no payment is received – no need to account for output tax on the replacement.
No input tax can be claimed as the asset was not paid for by Netsoft.

Transaction 5:

Invoices issued for software and network maintenance and prepayment received

Output tax – taxable supplies – must account for output tax.
Time – Earlier of date of invoice issued OR date any payment is received (section 9(1)) – output tax will be accounted for during February 2017 for all amounts received and invoiced (whichever takes place first) - R136 800 + R11 400 = R148 200.
Amount – general rule (section 10(3)) – R136 800 14/114 = R16 800 and R11 400 x 14/114 = R1 440.

PART B

Donations Tax implications for Mr Zeelie

1. The monthly contribution towards his parents’ maintenance is bona fide and is regarded as reasonable and is exempt in terms of section 56(2)(c) of the Income Tax Act.
2. The monthly contribution to his local church congregation (PBO) is exempt in terms of section 56(1)(h).
3. The study fees, book and hostel fees paid on behalf of his son while studying full-time at a University, should also be exempt in terms of section 56(2)(c), as it could be argued that it is a bona fide and reasonable contribution towards the maintenance of another person.

The sports car given to the son as a gift will probably not be regarded as a bona fide contribution towards his maintenance and it is doubtful whether this will be seen to be reasonable. Donations Tax will therefore have to be paid on this donation.

R320 000 – R100 000 (exemption in terms of section 56(2)(b)) = R220 000 x 20% = R44 000.

The date of the payment of the Donations Tax was not required in the question, but take note that it is at the end of the month following the month that the donation takes effect.
QUESTION 22 - SUGGESTED SOLUTION (continued)

COMMENTS ON THE SOLUTION

PART A

1. When considering whether a person has to register for VAT purposes, the R1 million limit is tested against taxable supplies, excluding VAT and exempt supplies.

2. This vendor will be making mixed (taxable and exempt) supplies. This aspect should have been addressed and concluded with a statement that the de minimus-rule is applicable. There were two instances where an item was used solely to make taxable supplies. Students should have noticed this and made reference thereto in their answers.

3. Some of the scenarios in the question dealt with the different time and value of supply rules. The time and value of supply rules are important and need to be studied thoroughly.

4. Take note that output tax is charged on the supply of goods or services. Use of the correct terminology is important in answering questions in tests and the examination.

5. Take note of the difference between a financial lease agreement and a rental agreement. They are treated differently for VAT purposes.

6. The format of this question forces you to think about the reasons why a specific input tax is deductible or not. It also forces you to apply the value and time of supply rules to a transaction.
QUESTION 23

20 Marks

Background information:

Assume you are a tax consultant with a local firm of Chartered Accountants. You received the following tax queries from Daniël Spanner, one of the clients of the firm. Daniël Spanner is a registered vendor for Value-Added Tax (VAT) with two-month tax periods ending on the last business day of January, March, May, July, September and November, respectively.

Office building:

1. Daniël Spanner retired from full-time employment on 30 November 2015. He used his lump-sum that he received from a retirement fund to purchase a second-hand building, consisting of 10 similar offices. Daniël purchased the building at its market value of R1 000 000 (R100 000 for each office) for cash, from a non-vendor (for VAT purposes). The building was registered in Daniël’s name on 15 March 2016. The invoice received from the attorneys of the seller on 15 March 2016 reflected the following (inclusive of VAT, where applicable).

<table>
<thead>
<tr>
<th>Description</th>
<th>Amount</th>
</tr>
</thead>
<tbody>
<tr>
<td>FICA identification and verification fee</td>
<td>R342</td>
</tr>
<tr>
<td>Transfer fees</td>
<td>R10 260</td>
</tr>
<tr>
<td>Postage and courier fees</td>
<td>R912</td>
</tr>
<tr>
<td>Transfer duties</td>
<td>R80 000</td>
</tr>
<tr>
<td>Purchase price of building</td>
<td>R1 000 000</td>
</tr>
<tr>
<td>Received from purchaser on 10 March 2016</td>
<td>(1 090 514)</td>
</tr>
<tr>
<td>Balance due</td>
<td>NIL</td>
</tr>
</tbody>
</table>

2. Eight offices were let by Daniël Spanner for a total amount of R10 000 an office per month, payable in advance on the first of each month from 1 April 2016 to 30 September 2016. On 30 September 2016 (the date of sale of the building (refer note 4)) one tenant was in arrears for September 2016.

3. During June 2016 Daniël Spanner converted two of the offices (therefore 20% of the building), that were not let, into two bachelor flats at a cost of R57 000 (inclusive of VAT) each. From 1 July 2016 to 30 September 2016 the bookkeeper and the receptionist each occupied one of the two flats at no cost.

4. On 1 October 2016 Daniël Spanner sold the building as a going concern (all the requirements in terms of section 11(1)(e) of the VAT Act were met) to Arcinea Limited (a non-connected, registered vendor for VAT) for R1 300 000 (excluding VAT). On this date the open market value of the building was R1 600 000. Arcinea Limited settled the purchase consideration on 1 December 2016 (the date that the building was registered in the company’s name) and from this date used the building to make 80% taxable supplies and 20% exempt supplies.

Travel agency:

During March 2016 Daniël Spanner, as part of his business, opened a travel agency in South Africa. He received a booking for a tour in South Africa from an overseas client (Mr Spencer). In March 2016 Daniël Spanner issued an invoice to Mr Spencer that included the following services (excluding VAT):
Fee for services rendered to attending to Mr Spencer while on tour in South Africa 5 000
Fee for arranging the tour while Mr Spencer was still outside South Africa 1 000
6 000

**Motor boat:**

On 1 April 2016 Daniël Spanner purchased a 15-meter motor boat for R79 800 (including VAT). He uses the boat in his travel agency business to take guests for deep-sea fishing at no charge. From 1 April 2016 to 28 February 2017 he took 60 guests on deep-sea fishing trips. Each month he also took 2 employees deep-sea fishing as a reward for the rendering of excellent services. A market-related charge for a deep sea fishing trip is R550 per person per trip.

<table>
<thead>
<tr>
<th>REQUIRED:</th>
<th>Marks</th>
</tr>
</thead>
<tbody>
<tr>
<td>(a) In respect of the information provided in note 1 under the heading &quot;Office building&quot;, calculate the input tax that Daniël Spanner could have claimed and discuss the specific date when the input tax could have been claimed (only mentioning the tax period is not sufficient). Indicate if any part of the information has no VAT consequences.</td>
<td>6</td>
</tr>
<tr>
<td>(b) Calculate the input and/or output tax in respect of the information provided in notes 2 and 3 under the heading &quot;Office building&quot;. Clearly indicate whether any amount calculated is input or output tax. If no input or output tax is applicable, provide a reason. Note that no change in use should be accounted for in respect of the conversion of the offices to residential accommodation as the building was sold before the end of the year of assessment (the time of supply in respect of the change of use of capital goods (section 18(2) read with section 18(6))).</td>
<td>3</td>
</tr>
<tr>
<td>(c) Calculate the input and output tax in respect of note 4 under the heading &quot;Office building&quot; for both Daniël Spanner and Arcinea Limited. If no input or output tax is applicable, provide a reason or a calculation.</td>
<td>5</td>
</tr>
<tr>
<td>(d) Calculate, supported with a reason and reference to VAT legislation, the output tax in respect of the information provided under the heading “Travel agency”.</td>
<td>3</td>
</tr>
<tr>
<td>(e) Discuss the input and output tax implications in respect of the free deep-sea fishing trips provided to the employees.</td>
<td>3</td>
</tr>
<tr>
<td><strong>Total</strong></td>
<td>20</td>
</tr>
</tbody>
</table>

Source: Unisa TAX4862 Test 1 2016
QUESTION 23 - SUGGESTED SOLUTION

(a) **Office building**

**Purchase of offices:**

The offices were purchased from a non-vendor, therefore a notional input tax can be claimed of 14/114 x with the lower of cost or open market value (section 1(1), par (b) of the definition of input tax).

Claim input tax of: R1000 000 x 14/114 = R122 807

The time of supply is the earlier of date of any payment (10 March 2016), or date of registration (15 March 2016) (section 9(3)(d)).

In terms of section 16(3)(a)(ii)(aa) the **input tax can only be claimed to the extent of payment** and in terms of section 16(3)(a)(ii)(bb)(A) only once registration in the name of Daniël Spanner has taken place.

Therefore the full input tax can be claimed on 15 March 2016 (March tax period)

**Note:** In terms of section 15(1) every vendor shall account for VAT on an invoice basis.

Section 15(2)(b) provides that a natural person whose taxable supplies has not exceeded R2,5 million or is not likely to exceed R2,5 million in the 12 month period may apply in writing to the Commissioner to account for VAT on the payments basis.

If Daniël had successfully applied to the Commissioner and was registered on the payment basis section 16(3)(a) would not have applied, section 16(3)(b) would have been applicable. The difference would be that Daniël would be able to claim input tax on the earlier of date of any payment (10 March 2016) or the date of registration (15 March 2016) (section 9(3)(d)) but in terms of section 16(3)(b) the input tax can only be claimed to the extent of payment, therefore the full input tax would have been claimable on 10 March 2016.

**Attorney’s invoice:**

The following input tax can be claimed at the earlier of the date of the invoice or the date of payment, provided that the vendor is in possession of a tax invoice, therefore on 15 March 2016 as this is the date that Daniël received the invoice.

FICA identification and verification fee – R342 x 14/114 = R42

Transfer fee – R10 260 x 14/114 = R1 260

Postage and courier fees - R912 x 14/114 = R1 12

Transfer duty – no VAT already a tax that is levied

(b) **Rent received**

R10 000 x 8 offices x 6 months x 14/114 = R58 947

**Conversion of offices**

No input tax can be claimed in respect of the conversion of the offices to residential accommodation as the supply of residential accommodation in terms of an agreement is an exempt supply (section 12(1)(c))

**Note:** No change in use should be accounted for in respect of the conversion of the offices to residential accommodation as the building was sold before the end of the year of assessment (the time of supply in respect of the change of use of capital goods (section 18(2) read with section 18(6)).
QUESTION 23 - SUGGESTED SOLUTION (continued)

Supply of free housing to employees
There will be no deemed output tax on the supply of the fringe benefits to the 2 employees (residential accommodation) as section 18(3) does not apply if the fringe benefit is in respect of an exempt supply. (1)

Sale of building as a going concern - Daniël Spanner
Daniël Spanner used 80% (more than 50%) of the building to make taxable supplies therefore the total sale (100%) will be at zero rate,
Thus: R1 300 000 x 0% Rnil

Note:
As Daniël has claimed the input tax on all 10 units there will be no section 16(3)(h) input tax claim. It can be argued that Daniël has not claimed the input tax on the conversion cost of the 2 offices into residential accommodation (R57 000 x 2) and that section 16(3)(h) should apply to the conversion cost. As the open market value contributable to the conversion was not available this calculation could not have been done. - (1)

(c) Sale of building as a going concern - Arcinea Limited
An amount of input tax can be claimed at 0% on the purchase of the building as input tax was paid at 0%.
Thus: Input tax – R1 300 000 x 0% = Rnil

Account for output tax in terms of section 18A adjustment:

\[
\begin{array}{ccc}
\text{R} & \\
\text{Full cost of going concern purchased} & 1 300 000 & (1) \\
\text{Less: % to be used to make taxable supplies (80%)} & 1 040 000 & (1) \\
\text{OR: R1 300 000 x 20%} & 260 000 & \\
\text{Output tax – R260 000 x 14% = R36 400} & 36 400 & (1) \\
\end{array}
\]

(d) Travel agency:
In terms of section 8(15) where a single supply of goods or services would, if separate consideration had been payable, been charged with tax in part at 14% and in part at zero rate, each part of the supply concerned shall be deemed to be a separate supply, THUS
Fee for services rendered to Mr Spencer while in SA – output tax will be accounted for at R5 000 x 14% - R700.
The supply will not be zero-rated in terms of section 11(2)(l) as the services are supplied while Mr Spencer is in South Africa and will be standard rated (s 7(1)(a)). (1)

The fee for arranging the tour will be zero-rated in terms of section 11(2)(l) as Mr Spencer was outside South Africa while the service was rendered; therefore R1 000 x 0% Rnil - (1)
(e) **Motor boat**

In terms of section 18(3) of the VAT Act, where a vendor provides an employee with a **benefit or advantage which falls into the employee’s gross income** in terms of paragraph (i) of the gross income definition of the Income Tax Act such benefit is deemed to be a **taxable supply in the hands of the vendor**.

The **supply of free fishing trips to employees** constitute the **supply of fringe benefits** to employees in terms of paragraph (i) of the gross income definition of the Income Tax Act.

Section 18(3) will not apply if the service supplied constitutes an exempt or zero-rated supply or the supply of entertainment. As the free trips are the **supply of entertainment**, section 18(3) is not applicable and therefore no taxable supply is made by Daniël Spanner to the employees.

**Note:**

Purchase of boat – **input tax** denied in terms of section 17(2)(a) as the motor boat was acquired for the purpose of supplying entertainment.

Supply of fishing trips to tourists – **no output tax levied** as it is the supply of entertainment. The vendor does not make taxable supplies of entertainment in the ordinary course of an enterprise; further the guests are not employees, therefore no fringe benefit arises.