REPUBLIC OF SOUTH AFRICA

EXPLANATORY MEMORANDUM

ON THE

INCOME TAX BILL, 1986

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INTRODUCTION

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

CLAUSE 1 AND THE SCHEDULE

Rates of Normal Tax

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

1. *Individuals*

The rates for persons other than companies apply in respect of the year of assessment ending on 28 February 1987 or 30 June 1987, and are provided for in paragraph 1 of the Schedule. While the basic rates of tax are the same as those which applied in the 1986 year of assessment, a discount of 5 per cent is granted. The discount is calculated on the amount of normal tax which remains after deducting the value of the rebates granted.

2. *Companies*

The rates for companies apply in respect of years of assessment, i.e. financial years, ending during the 12-month period from 1 April 1986 to 31 March 1987, and are provided for in paragraph 1 *(b)* to *(g)*, inclusive, of the Schedule. Those rates are as follows:

(a) Taxable income derived otherwise than from mining: 50 cents per R1 (paragraph 1 *(b)* of the Schedule).

(b) Taxable income derived from gold mining—

(i) by any mine other than a post-1966 gold mine: an amount determined in accordance with one of the formulae provided for in paragraph 1 *(c)* of the Schedule plus a surcharge equal to 25 per cent of the said amount (second proviso to the said paragraph 1 *(c)*);

(ii) by a post-1966 gold mine: an amount determined in accordance with one of the formulae provided for in paragraph 1 *(d)* of the Schedule, plus a surcharge of 25 per cent of the said amount (second proviso to the said paragraph 1 *(d)*).

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

(*d*) Taxable income from diamond mining: a basic tax of 45 cents per R1, plus a surcharge equal to 25 per cent of the basic tax (paragraph 1 *(f)* of the Schedule).

(*e*) Taxable income from mining operations (other than mining for gold or diamonds): 50 cents per R1 (paragraph 1 *(g)* of the Schedule). To the tax as calculated above a surcharge equal to 15 per cent of such tax is added (see proviso to subparagraph *(g)*). A further levy, by way of additional normal tax, is provided for in respect of taxable income from oil mining in terms of section 5 (2A) of the principal Act.

CLAUSE 2

Definitions: Amendment of section 1 of the principal Act

Subclause (1) (a): In terms of paragraph *(a)* of the definition of "benefit fund", a benefit fund includes *inter alia* a friendly society registered under the Friendly Societies Act, 1956, or any fund which is not so registered solely because the members do not make contributions to the fund. The latter provision has been subject to abuse, and an amendment is accordingly proposed in terms of which a fund established on or after 13 June 1986 will be recognised as a benefit fund under the said paragraph *(a)* only if it is in fact registered under the Friendly Societies Act. Non-contributory funds wishing to provide benefits similar to those provided by a friendly society will in future have to apply to the Commissioner for approval under paragraph *(c)* of the said definition.

Subclause (1) (b) proposes two amendments to paragraph *(d)* of the definition of "gross income", in terms of which any lump sum payment received by an employee on termination of service is included in his gross income.

Firstly, this paragraph excludes lump sum payments received from a pension fund, provident fund, retirement annuity fund or benefit fund. Such payments received from the first-mentioned three funds are taxable under paragraph *(e)* of the definition, but as benefit funds have traditionally paid only insignificant lump sum benefits, these have never been subject to tax. As it has now become clear that substantial tax avoidance can be achieved by the channelling of large lump sum payments through benefit funds, the exclusion of such funds has been deleted and, as a result, lump sum payments received on termination of service from a benefit fund will in future be taxable under this paragraph.

Secondly, it is common practice for employers to provide for the payment to employees on termination of service, or in the event of their prior death, to their nominated beneficiaries, of gratuities over and above what they may become entitled to under pension or provident funds. Where such a payment is made on death, it is at present taxed in the hands of the beneficiary to whom it is paid.

However, as the amount is payable as a result of services rendered by the employee, it is considered that it should more properly be taxed in his hands, as is at present the case with such payments emanating from a pension, provident or retirement annuity fund. The paragraph is accordingly amended so as to provide that such an amount which becomes payable by reason of or following upon the death of a person is deemed to have accrued to him immediately before his death. It should be mentioned that the first R30 000 of such a payment will be exempt from tax under section 10 (1) *(x)* of the principal Act, while any taxable portion will be subject to tax at average rate.

Subclauses (1) (c), (d) and (e): Pension funds, provident funds and retirement annuity funds are subject to the approval of both the Registrar of Financial Institutions and the Commissioner for Inland Revenue. This is necessary to ensure, firstly, that members' interests are adequately protected and, secondly, that the funds do not pay excessive untaxed benefits. To ensure that both these requirements are met, it is now proposed that any such fund must be registered with the Registrar of Financial Institutions before it may be approved for income tax purposes.

Subclause (2) provides that the amendments to paragraph *(d)* of the definition of "gross income" relating to payments on termination of service, will apply to such payments received on or after 13 June 1986.

CLAUSE 3

Levy of normal tax: Amendment of section 5 of the principal Act

Certain abnormal receipts are, in terms of a formula contained in section 5 (10) of the principal Act, taxed at the taxpayer's average rate of tax applicable to his ordinary income. The granting of the 5 per cent discount (see *clause 1*) has necessitated a consequential amendment to this formula.

CLAUSE 4

Payments on termination of service: Amendment of section 7A of the principal Act

Gratuities payable to employees on termination of service may under certain circumstances be spread over a period of three years under section 7A (4), and under section 7A (4A) be taxed at the employee's average rate of tax applicable to his ordinary income for the year.

The amendment proposed by *subclause (1) (a)* provides that the three-year spreading provisions will not apply to a gratuity which becomes payable on death.

The concession to tax such amounts at average rate applies *inter alia* if the employee has attained the age of 55 years in the case of a male or 50 years in the case of a female, or where his services are terminated due to superannuation, ill-health or other infirmity. In terms of the amendment proposed by *subclause (1) (c)*, the concession can now also be applied to a gratuity received by a taxpayer under the aforesaid age who is dismissed as a result of his employer ceasing business, or who has become redundant under a staff reduction scheme. This amendment applies with retrospective effect to the 1986 year of assessment.

CLAUSE 5

Subsistence allowances: Amendment of section 8 of the principal Act

In terms of section 8 (1) *(a)* of the Act, any portion of a reimbursive allowance paid to an employee which is not actually expended by him, is included in his taxable income. It follows that any taxpayer who has received such an allowance must prove that he has spent the entire amount. Section 8 (1) *(c)* provides, however, that a subsistence allowance is deemed to have been fully expended if it is paid at a rate not exceeding R100 per day if the employee's accommodation is not supplied by his employer, or R50 per day if it is supplied by the employer. While these amounts are considered adequate in the case of local travel, they are clearly insufficient to cover the cost of overseas travel. To prevent employees

having to produce proof of all expenditure incurred on overseas trips, an amendment is proposed in terms of which the Commissioner for Inland Revenue is empowered to accept that larger allowances have been expended without production of proof.

CLAUSE 6

Income deemed to have been received from a source within the Republic: Amendment of section 9 of the principal Act

In terms of section 9 (2) of the Act, income received by a resident of the Republic from a deposit with, or shares in, a South African building society, is deemed to have been derived from a source within the Republic, even though the deposit may have been made to, or the shares subscribed for through, a branch of the building society situated outside the Republic. This deeming provision is now extended to include deposits or shares held by a South African resident in a building society or similar institution incorporated, established or formed in a country other than the Republic. The amendment is intended specifically to prevent the avoidance of tax through investments made in building societies established in the TBVC states.

CLAUSE 7

Exemptions: Amendment of section 10 of the principal Act

Subclause (a): Section 10 (1) *(c*C*)* of the Act provides for an exemption in favour of utility housing companies which comply with certain conditions, one of which is that at least one of the directors must be nominated by the Minister of Public Works and Land Affairs. The consequential amendment proposed by this subclause is necessitated by the fact that, as housing is an own affair, the nomination of such directors is now a function of the Minister responsible for housing matters in the relevant House of Parliament.

Subclause (b): The investment income derived by South African pension funds and retirement annuity funds is exempt from tax. Such funds established for the benefit of residents of the territory of South West Africa are, in view of the limited investment avenues available in the territory, obliged to invest in the Republic and consequently become liable for South African tax. In terms of the amendment proposed by this subclause, the exemption contained in section 10 (1) *(d*A*)* of the Act in favour of TBVC funds is now extended to South West African funds.

Subclauses (c) and (d): The first R250 of a taxpayer's income in the form of interest and building society dividends is exempt from tax. This amount is, in terms of the amendments proposed by this subclause and *clause 12*, increased to R500.

Subclause (e): When an employee is transferred from one station to another, certain costs arising out of his transfer may, under the exemption contained in section 10 (1) *(n*B*)*, be paid by his employer without giving rise to a taxable fringe benefit. This exemption is now extended to include costs incurred by the employee in selling his house at his old station.

Subclause (f): An employee who, after his retirement, continues to enjoy any fringe benefit granted by his former employer, is exempt from tax on that benefit. This exemption is granted primarily to avoid administrative problems. However, should a retired employee who continues to receive a benefit be re-employed on a part-time basis, for example, by be-

ing appointed to the board of directors, he would then again become liable for tax on the benefit, although the receipt of the benefit is not connected with his part-time employment. An exemption is proposed in such cases, subject to the conditions that the employee's part-time remuneration does not exceed R5 000 per annum, he retired from full-time employment after attaining the age of 60 years or because of ill-health, and that the benefit was granted before he retired.

CLAUSES 8 AND 9

Incentive allowances on machinery or plant and hotel equipment: Amendment of sections 12 and 12A of the principal Act

Sections 12 and 12A of the principal Act were amended in 1982 to provide that the incentive allowances which may be granted thereunder would not apply to lessors of such assets unless the assets were let for a minimum period of five years. These provisions were introduced to prevent a form of tax avoidance which was being achieved through the negotiation of short-term financial leases, but had the effect also of withholding the allowances from, for example, plant hire companies who by the nature of their business negotiate short-term letting contracts. An amendment is now proposed which will exclude genuine operating leases from these provisions. The expression "operating lease" is defined in section 23A of the principal Act, and an explanation of the definition will be found in the explanation of *clause 15.*

CLAUSE 10

Taxation of shipowners: Amendment of section 14 of the principal Act

South African shipowners are, by reason of the international political climate, frequently forced to own and operate their ships through foreign-registered subsidiary companies. Section 14 of the principal Act at present contains provisions in terms of which such subsidiaries may to a limited extent be taxed in conjunction with the parent company, i.e. losses incurred by the subsidiary may be deducted from the parent's income, and allowances granted to the parent in respect of a ship purchased by it are not affected if that ship is sold to a subsidiary.

These concessions still do not adequately cope with the peculiar conditions applying to shipping, and a new subsection, numbered (1D), is now added to section 14, in terms of which the parent company and any such subsidiaries which are engaged in shipping operations only, will for taxation purposes be regarded as one entity. Consequently, income derived by the subsidiary will be taxed in the hands of the parent, and expenditure incurred by the subsidiary will be allowed to the parent. Sales of ships and other assets between parent and subsidiary, or between fellow subsidiaries, will be ignored, as will dividends declared by a subsidiary to the parent.

CLAUSE 11

Sponsorship allowance: Insertion of section 18B in the principal Act

A new section 18B is inserted in the principal Act in terms of which a special allowance may be granted to sponsors of international events held in the Republic.

The term "international event" is defined as any cultural, educational or sporting event held in the Republic, which is approved by the Minister

of Finance. That Minister, in consultation with the Minister of National Education, must be satisfied—

(*a*) that the event is of a type in which international competition ordinarily takes place;

(*b*) that a substantial number of the participants in the event, or the key participants, are non-residents; and

(*c*) that the holding of the event will materially benefit cultural, educational or sporting activities in the Republic.

The allowance is granted in respect of "sponsorship expenditure", which is defined to include expenditure incurred in sponsoring the event and on advertising which is directly connected with the event. It is a requirement that both types of expenditure must be allowable as a deduction in the determination of the sponsor's taxable income. The allowance granted will be equal to 80 per cent of so much of the sponsorship expenditure actually incurred as the Minister of Finance directs. The Minister may therefore direct that the allowance be granted only on a specified maximum expenditure, or that it not be granted on a certain portion of the expenditure, for example, where some portion of the expenditure may be indirectly recovered by the sponsor by way of a percentage of ticket sales.

The total amount which may be allowed to a sponsor by way of the normal deduction under section 11 *(a)* of the principal Act and the sponsorship allowance, is 180 per cent of the expenditure incurred. This means that a company which pays tax at a rate of 50 per cent, will recover 90 per cent of its sponsorship expenditure.

The provision applies in respect of years of assessment ending on or after 1 July 1986.

CLAUSE 12

Dividends: Amendment of section 19 of the principal Act

See the explanation of *clause 7 (c) and (d)*.

CLAUSE 13

Deduction from the earnings of married women: Amendment of section 20A of the principal Act

Section 20A of the principal Act at present provides for a deduction of up to R1 600 from earnings derived by a married woman. "Earnings" is defined for this purpose as income derived by her from trade, but excluding, *inter alia*, a trade which is in any way connected with her husband's trade and salary received from a private company in which her husband is a principal shareholder.

The deduction is now increased to the greater of R1 800 or 20 per cent of her net earnings. "Net earnings" is defined as the taxable income derived from earnings, but without taking into account any deduction allowable under sections 11 *(k)* (pension fund contributions), 11 *(n)* (retirement annuity fund contributions), 18 (medical expenses), 18A (educational donations) and 21*quat* (physical disability expenditure). The deduction is limited to the amount of the net earnings and cannot, therefore, create a loss.

The present provision that the deduction is proportionately reduced where the period assessed is less than a full year, is deleted. The increased deduction is applicable with effect from the year of assessment ended on 28 February 1986.

EXAMPLE

Husband:	Business income	R60 000
	Business expenses	20 000
Wife:	Income from commission	30 000
	Travelling expenses	12 000
	Entertainment expenses	3 000
	Retirement annuity fund	2 000

Solution:

Calculation of "net earnings"—

Earnings		30 000
Deduct: Travelling	R12 000	
Entertainment	3 000	15 000
		R15 000

Determination of taxable income—

Income: Husband	R60 000
Wife	30 000
Total	R90 000

Deductions:

Husband:	Business expenses	R20 000	
Wife:	Travelling	12 000	
	Entertainment	3 000	
	Retirement annuity	2 000	
	20% of "net earnings"	3 000	40 000
TAXABLE INCOME			R50 000

CLAUSE 14

Valuation of trading stock: Amendment of section 22 of the principal Act

Subclause (1) (a) corrects a minor technical error.

Subclause (1) (b): Section 22 (5) of the principal Act was amended in 1984 so as to withdraw the concession to value trading stock on the LIFO basis. In view of the fact that the reversal of LIFO reductions made in past years would have had severe consequences for taxpayers who had been using this basis, provision was made for the creation of a reserve (known as the LIFO reserve) equal to the difference between the LIFO value of the stock and the correct value, which reserve may be carried forward indefinitely. This reserve represents a valuable concession to the taxpayers concerned.

A further amendment required taxpayers who were valuing their stock on the basis of bare cost, to include in future, in accordance with

generally accepted accounting practice, various overhead expenses. In this case, too, a concession was made, in that the difference between bare cost and the full cost was permitted to be phased in over four years.

Section 22 (5) *(d)* provides that where trading stock has been valued in accordance with subsection (5) *(a)*, i.e. the cost price thereof has been determined in accordance with LIFO principles, then the difference between that value and the cost price as determined without applying LIFO valuation principles, constitutes the LIFO reserve.

It has been contended that taxpayers' who had not previously included overhead expenses in the cost price of stock, may for the purposes of subsection (5) *(d)* exclude those expenses from their LIFO cost but include them in their non-LIFO cost. This procedure, if permitted, would artificially inflate the LIFO reserve and give taxpayers who had in the past used the bare cost method an unfair advantage over taxpayers who had correctly included overhead expenses.

It has further been suggested that the use of the word "value" in subsection (5) *(d)* entitles a taxpayer who has written down the cost of his stock on account of diminution in value under section 22 (1), to calculate his LIFO reserve on the difference between the written down LIFO value and the full non-LIFO cost.

Subsection (5) *(d)* is accordingly amended so as to make it clear that the LIFO reserve is to be calculated on the difference between LIFO cost and non-LIFO cost, and further that where the LIFO cost excludes overhead expenses, the non-LIFO cost must also exclude those expenses.

Subclause (1) (c): At the time of the withdrawal of the provision permitting trading stock to be valued on the LIFO basis, it was provided that where a business undertaking in respect of which that basis had been applied was taken over by one company from another before the commencement date of the 1984 Act, the LIFO reserve calculated in respect of the business could be transferred to the purchasing company. As it has been found that the potential loss of the LIFO reserve is inhibiting the rationalisation of business, it is now proposed that the transfer of the reserve also be permitted after the commencement of the aforesaid Act.

Subclause 2 makes the various amendments discussed above applicable as from the commencement of years of assessment ending on or after 1 April 1984.

CLAUSE 15

Limitation of allowances on machinery, plant or aircraft: Amendment of section 23A of the principal Act

Section 23A of the principal Act was introduced in 1984 to limit the deduction of allowances granted to lessors of machinery, plant or aircraft to the income derived by them from leasing. In terms of an amendment introduced in 1985, the letting of assets used by the lessor mainly in the course of a trade other than leasing was excluded from the provision.

A further amendment is now proposed in terms of which assets let under an operating lease are also excluded from the ambit of the section. The expression "operating lease" is defined as a lease of movable property concluded by a lessor other than a banker or financier, if—

(a) the property is available to be hired by members of the general public for short periods, i.e. a period of less than a month;

(*b*) the cost of maintenance and repairs occasioned by normal wear and tear is borne by the lessor; and

(*c*) the lessee does not assume liability for loss or destruction of the property, except where he has failed to take proper care thereof.

This amendment is effective from the date on which section 23A was enacted, i.e. years of assessment ended on or after 15 March 1984.

CLAUSE 16

Credit agreements: Amendment of section 24 of the principal Act

Section 24 of the principal Act provides that where any agreement for the sale of property is concluded subject to the condition that ownership of the property will not pass until the whole or a portion of the purchase price has been paid, the full purchase price is deemed to accrue to the seller when the agreement is concluded. An allowance is, however, granted to the seller in respect of any portion of the selling price which is still due at the end of his accounting period. In terms of an amendment introduced in 1985, this allowance may be granted only in cases where the passing of ownership of the property is suspended for a period of at least 12 months.

It is considered, however, that the allowance should be dependent on the credit period rather than the period in which passing of ownership is suspended, and an amendment is proposed in terms of which the allowance may be granted where at least 25 per cent of the purchase price under the agreement is payable at least 12 months after conclusion of the agreement.

A measure of relief is also proposed for taxpayers who previously qualified for the allowance under section 24, but do not so qualify under the amended provision. It is accordingly proposed that any allowance which was in accordance with generally prevailing practice granted in the taxpayer's last year of assessment ended before 1 January 1986 may be phased out over the succeeding four years. The amount which may be allowed under the phasing-out provisions in any year is a specified portion of the lesser of the allowance to which the taxpayer was entitled in his last year of assessment ended before 1 January 1986 and the allowance to which he would have been entitled in the relevant year had section 24 not been amended.

CLAUSE 17

Determination of taxable income of long-term insurers: Amendment of section 28 of the principal Act

Subclause (a) exempts from tax the investment income derived by a long-term insurer from business carried on by him with a South West African pension fund or retirement annuity fund. See also the amendment introduced by *clause 7 (b)*.

Subclause (b): In terms of section 12 (8) of the Regional Services Councils Act, 1985 (Act No. 109 of 1985), any levies paid by a taxpayer under that Act are deemed to be an operating expense which may be deducted in the determination of his taxable income for purposes of the principal Act. A long-term insurer, however, will derive no benefit from this provision, as his taxable income is determined under section 28 of the

principal Act at 40 per cent of his investment income, without regard to expenditure incurred. The amendment proposed by this clause will permit a long-term insurer to deduct such levies paid in respect of his taxable business from the taxable income determined under section 28.

CLAUSE 18

Non-residents tax on interest: Amendment of section 64C of the principal Act

Interest derived by a non-resident from an investment with *inter alia* a local authority, is exempt from non-residents tax on interest. This exemption, under section 64C *(a)*, is now extended to investments with the Local Authorities Loans Fund, a body established under the Local Authorities Loans Fund Act, No. 67 of 1984, for the specific purpose of obtaining loan financing for local authorities.

CLAUSE 19

Persons liable to render returns: Amendment of section 66 of the principal Act

In terms of the amendments introduced by *clauses 7 (c) and (d) and 12,* the first R500 of income derived by way of interest and building society dividends is exempt from tax. Section 66 of the principal Act is correspondingly amended, to provide that a person whose income consists solely of remuneration not exceeding an amount stated by the Commissioner and/or interest and building society dividends not exceeding R500, need not submit a return of income unless specifically required to do so.

CLAUSE 20

Interest on late payment of tax: Amendment of section 89 of the principal Act

The Commissioner is empowered under section 89 (1) of the principal Act to accept payment of tax in instalments. Under section 89 (2), interest is payable on any tax which is not paid within the period for payment specified on the notice of assessment, or any extension of that period which the Commissioner may grant.

In practice, the Commissioner will extend the period for payment only in exceptional circumstances, for example, where it is shown that the assessment was posted to an incorrect address. The Commissioner does, however, frequently accept payment of tax in instalments, subject to the payment of interest.

It has been contended that when the Commissioner agrees to accept payment of tax in instalments, this is tantamount to an extension of the period for payment, and that interest is thus not payable.

Subclause (1) proposes an amendment to section 89 (2) to make it clear that interest may be waived only where the Commissioner extends the period for payment and directs that interest shall not be paid. This direction will, as in the past, be given only in exceptional circumstances such as non-receipt of the assessment.

Subclause (2) provides that any interest which was paid or became payable in the past in accordance with the generally prevailing practice of the Commissioner is deemed to have been properly payable.

CLAUSES 21 AND 29

*Payment of provisional tax by companies: Amendment of section 89*bis *of the principal Act and paragraph 27 of the Fourth Schedule to the principal Act*

A proviso was added to section 89*bis* (2) of the principal Act in 1984, in terms of which provisional tax paid by a company within 15 days after the end of the period prescribed for payment would be deemed to have been paid within that period. A similar provision was added to paragraph 27 of the Fourth Schedule as subparagraph (3).

The purpose of these provisions, which have not been brought into effect, was to relieve the banking sector by reducing deposit peaks on the last day of a month. It has been found that, for technical reasons, it will not be desirable to bring these provisions into operation, and their deletion is accordingly proposed.

CLAUSES 22, 27, 28 AND 30

*Provisional tax payments by companies and individuals: Amendment of section 89*quat *and paragraphs 23, 23A and 28 of the Fourth Schedule to the principal Act*

New requirements are proposed in relation to provisional tax payments by companies and individuals. These requirements will apply with effect from, in the case of companies, years of assessment ending on or after 28 February 1986, and in the case of individuals, years of assessment ending on or after 28 February 1987.

The provisions apply to companies whose taxable incomes exceed R20 000, and individuals whose taxable incomes exceed R50 000, in any year of assessment.

The provisions relating to the first and second payments, due after the first six months and on the last day of the accounting period, respectively, remain unchanged. The mandatory third payment by companies is no longer required, but both companies and individuals are permitted to make voluntary additional payments. If, in the case of a company whose taxable income exceeds R20 000 and an individual whose taxable income exceeds R50 000, the total amount paid for the year is less than the tax assessed, interest is payable by the taxpayer at the prescribed rate (currently 15 per cent per annum) on the shortfall, while if the total amount paid exceeds the tax assessed, interest is payable to the taxpayer at the prescribed rate on the amount overpaid. In either case, interest is calculated from six months after the close of the accounting period until the due date of the assessment or the date of refund, as the case may be.

Clause 22 amends section 89*quat* to provide for the payment of debit and credit interest. Subsection (1) defines two expressions, namely "credit amount" and "effective date".

"Credit amount" means the sum of the mandatory provisional tax payments made, any voluntary additional provisional tax payments made,

any employees tax deducted (in the case of an individual) and any other credits available to be set off against the assessment.

"Effective date" means a date falling six months after the last day of the taxpayer's accounting period.

Subsection (2) provides that if the normal tax assessed is less than the credit amount, interest is payable by the taxpayer from the effective date until the due date of the assessment. Subsection (3), however, authorises the Commissioner to waive interest on so much of the shortfall as he is satisfied was caused by an amount being taxed or expenditure being disallowed which the taxpayer genuinely believed would not be taxable or would be allowed, as the case may be.

Subsection (4) provides for the payment of interest to the taxpayer where the credit amount for the year exceeds the normal tax assessed.

Clause 27 deletes the requirement that a company must make a third payment of provisional tax.

Clause 28 amends paragraph 23A of the Fourth Schedule so as to permit both companies and individuals to make voluntary additional payments of provisional tax. However, any such payments which are made after the effective date, are deemed to be payments which were due on the effective date, and are subject to interest calculated from the effective date until the date of payment.

Clause 30: Paragraph 28 of the Fourth Schedule at present provides that in the case of a person other than a provisional taxpayer, any overpayment of employees tax is automatically refunded. In the case of a provisional taxpayer, however, a refund is made only where the Commissioner authorises one—in other cases, the credit is retained to be set off against subsequent provisional tax or assessed tax due. This paragraph is now amended to provide in all cases for the automatic refund of overpayments of employees tax and provisional tax.

CLAUSE 23

Reporting of unprofessional conduct: Insertion of section 105A in the principal Act

Section 4 of the principal Act prohibits the Commissioner from revealing to any person other than a taxpayer and his lawful representative, any matters in relation to the taxpayer which come to the Commissioner's knowledge in the exercise of his duties. Cases have arisen in the past where professional persons acting on behalf of taxpayers have committed unprofessional acts in relation to the preparation of the taxpayer's accounts and returns which would have rendered them liable to disciplinary action by their controlling bodies, but they have escaped such disciplinary action because the Commissioner has been prevented by section 4 from making a report to the controlling body concerned. Section 105A of the principal Act, the insertion of which is proposed by this clause, authorises the Commissioner to report such cases to the bodies concerned.

Subsection (1) defines a "controlling body" as any body, whether established voluntarily or by law, which has been established for the purpose of controlling the carrying on of any profession, calling or occupation, and which is empowered to take disciplinary steps against any person who contravenes any rules or code of conduct laid down by the body.

Subsection (2) empowers the Commissioner to lodge a complaint with a controlling body if he is satisfied that any person subject to the control of that body has done or omitted to do anything which—

(a) was intended to enable or assist a taxpayer to avoid or unduly postpone the performance of a duty or obligation imposed on him under the principal Act, or by reason of negligence had the effect of avoiding or unduly postponing the performance of such duty or obligation; and

(b) constituted a contravention of a rule or code of conduct of the body and could result in disciplinary action being taken by it.

Subsection (3) *(a)* empowers the Commissioner, in lodging a complaint with the controlling body, to furnish that body with information the disclosure of which would otherwise be prohibited by section 4 of the principal Act.

Subsection (3) *(b)*, however, requires the Commissioner to furnish the taxpayer and the person concerned with details of the intended complaint, and subsection (3) *(c)* gives the taxpayer or the person concerned the right to object to the complaint being made.

Subsection (3) *(d)* empowers the Commissioner to lodge the proposed complaint where no objection is made within 30 days or, if an objection has been made, if the Commissioner considers that the objection should not be sustained.

Subsection (4) requires that the complaint be considered by the controlling body and dealt with by it in accordance with its rules. It is further provided that any hearing of the complaint may not be attended by any person whose attendance the body does not consider to be necessary for the proper consideration of the matter.

Subsection (5) requires the controlling body and its members to preserve secrecy in regard to the matter.

CLAUSES 24 AND 25

Lump sum benefits from pension, provident and retirement annuity funds: Amendment of the Second Schedule to the principal Act

The taxable portion of lump sum benefits from pension, provident and retirement annuity funds is determined in accordance with the Second Schedule. Paragraph 1 of that Schedule defines, *inter alia*, two formulae, viz "formula A" and "formula B". Formula A is applied separately to each lump sum derived on retirement from a pension or provident fund to determine the amount which may be deducted from such lump sum, and formula B is used to determine the cumulative maximum amount which may be deducted from the total of the lump sums derived from all pension, provident and retirement annuity funds.

Formula A is based on the length of membership of the fund and the average salary earned by the member. That average salary is, however, subject to a maximum, which at present is fixed at R40 000. *Clause 24 (a)* proposes that this maximum be increased to R60 000.

Clause 24 (b) effects a textual amendment to formula A.

The cumulative maximum deduction under formula B is at present the greater of R80 000 or R3 000 multiplied by the total number of years

membership of all funds. It is proposed in terms of *clause 24 (c)* that these amounts be increased to R120 000 and R4 500 respectively.

Paragraph 5 (2) of the Schedule provides for a minimum deduction in certain circumstances, namely R16 000 in the case of a retirement benefit from a provident fund, and the greater of R40 000 or twice the annual salary (not exceeding R40 000) in the case of death benefits from pension or provident funds. *Clause 25* proposes that these amounts all be increased by 50 per cent.

CLAUSE 26

Exemption from payment of provisional tax: Amendment of paragraph 18 of the Fourth Schedule to the principal Act

Paragraph 18 of the Fourth Schedule is amended to exempt from the payment of provisional tax any natural person over the age of 65 years (other than a director of a private company) if the taxpayer's taxable income for the year—

(a) does not exceed R20 000;

(b) is not derived from carrying on a business; and

(c) is not derived otherwise than from remuneration, interest, dividends or rental from the letting of fixed property.

CLAUSES 27 AND 28

See the explanation of *clause 22*.

CLAUSE 29

See the explanation of *clause 21*.

CLAUSE 30

See the explanation of *clause 22*.

CLAUSE 31

Gains under insurance policies: Amendment of paragraph 10 of the Sixth Schedule to the principal Act

The Sixth Schedule to the principal Act determines circumstances in which an insurance policy may be classified as a standard policy, and provides that any gain made under a policy which is not a standard policy, is subject to tax.

Subclause (1) (a) effects a textual amendment to make it clear that an insurance policy must provide at all times for the payment of a minimum benefit on the death of the life assured or, alternatively, it must provide

for the payment of such a benefit on the death of the life assured or his disablement, whichever occurs first.

In terms of an amendment introduced in 1985, an insurance policy must, to qualify as a standard policy, at all times be owned by a natural person. The amendment proposed by *subclause (1) (b)* provides that in the case of a policy held by a trustee on behalf of a trust, the trustee (whether he is a natural person or not) is deemed to be a natural person if all the beneficiaries under the trust are natural persons.

Subclause (2) provides that the amendment effected by *subclause (1) (b)* is deemed to have taken effect on 24 May 1985.

CLAUSE 32

Circumstances in which insurance policies cease to be standard policies: Amendment of paragraph 14 of the Sixth Schedule to the principal Act

Under paragraph 13 (1) *(a)* of the Sixth Schedule, a policy may be deemed to be a standard policy if it provides for the payment of a benefit only on the death of the life assured. Under paragraph 14 (1) *(e)*, such a "deemed standard" policy will become non-standard if it is surrendered. Under paragraph (i) of the proviso to the latter provision, however, the policy will not become non-standard if the annual premiums payable thereunder do not exceed R4 000. These two provisions have been utilised to bypass the measures introduced last year to restrict the sale of pure endowment policies, in that pure endowment policies with annual premiums not exceeding R4 000, and which ostensibly provide for a payment on death only, are marketed on the understanding that they may be surrendered at any time.

In terms of the amendment proposed by this clause, any policy applied for on or after 13 June 1986 which qualifies as a standard policy only under paragraph 13 (1) *(a)*, will become non-standard if it is surrendered at any time.

CLAUSES 33 AND 40

"Official rate of interest": Amendment of paragraph 1 of the Seventh Schedule to the principal Act

Clause 33 confirms the reduction in the official rate of interest from 18 per cent to 15 per cent, as effected in terms of Government Notice No. R.2706 dated 29 November 1985, while *clause 40* withdraws that Notice.

CLAUSE 34

Occupation of residential accommodation: Amendment of paragraph 9 of the Seventh Schedule to the principal Act

The amendments proposed by this clause are of a textual nature.

CLAUSE 35

Benefits in respect of low-interest loans: Amendment of paragraph 11 of the Seventh Schedule to the principal Act

Paragraph 11 (2) of the Seventh Schedule at present determines the dates on which the taxable benefit arising from the granting of a low-inter-

est loan is deemed to accrue for employees tax purposes. *Subclause (1) (a)* proposes an amendment in terms of which such deemed dates of accrual will apply for assessment purposes as well.

Subclause (1) (b) adds a proviso to paragraph 11 (2), which makes it clear that where the official rate of interest is varied during a year of assessment, any interest benefit which is deemed to have accrued before the date of variation is to be determined using the previous rate of interest.

CLAUSE 36

Phasing in of benefits under approved housing schemes: Amendment of paragraph 14 of the Seventh Schedule to the principal Act

Subclause (1) (a) provides for the phasing in of the fringe benefit derived under a type of housing scheme where an employee whose repayments under his bond exceed 25 per cent of his salary, is granted a further loan each month to assist him in meeting his payments.

Subclause (1) (b): The phasing in of benefits derived under approved housing schemes is, in the case of loans granted on or after 1 March 1985, at present restricted to the benefit applicable to the first R50 000 of the loan. It has been found that this restriction causes unnecessary hardship in many cases, and it is accordingly deleted.

Subclause (2) makes the amendment effected by *subclause (1) (a)* applicable to the 1986 and subsequent years of assessment.

CLAUSE 37

Phasing in of benefits other than approved housing benefits: Amendment of paragraph 15 of the Seventh Schedule to the principal Act

Paragraph 15 of the Seventh Schedule is amended so as to provide for the phasing in of the benefit determined in respect of a subsidy granted on a loan used for purposes other than housing. This amendment is also applicable to the 1986 and subsequent years of assessment.

CLAUSE 38

Amendment of section 50 of the Income Tax Act, 1984

The definition of "retirement-funding employment" was amended in 1984 so as to exclude income not taken into account for the purposes of determining an employee's pension fund contributions. This amendment was inadvertently included in the list of fringe benefit provisions which in terms of section 50 (2) of the Income Tax Act, 1984, only came into operation in respect of the 1986 year of assessment. That section is now suitably amended.

CLAUSE 39

Amendment of section 6 of the Income Tax Act, 1985

Subclause (a) rectifies a drafting error in section 6 (1) *(a)* of the Income Tax Act, 1985.

Subclause (b): Section 10 (1) *(i)* (ii) of the principal Act was amended by section 6 (1) *(c)* of the Income Tax Act, 1985, so as to increase the

maximum tax-free investment in Post Office Savings Bank Certificates from R40 000 to R70 000. This amendment was made applicable with effect from the 1986 year of assessment. The increased limit was, however, approved with effect from the 1985 year of assessment, and the commencement date of the provision is amended accordingly.

CLAUSE 40

See the explanation of *clause 33*.

CLAUSE 41

Commencement of certain amendments

This clause provides that the amendments to the principal Act effected by the amending Act are to apply with effect from years of assessment ending on or after 1 January 1987, except where otherwise provided or the context otherwise indicates.

CLAUSE 42

This clause gives the short title of the amending Act.