Legal & Policy

Income Tax

Guide to the Disposal of a Residence from a Company or Trust

(1 October 2010 to 31 December 2012)

(Issue 3)

South African Revenue Service

Guide to the disposal of a residence from a company or trust

Preface

This guide –

- deals with the window of opportunity covering the period 1 October 2010 to 31 December 2012 for the disposal of a residence from a company or trust into the hands of individuals free of transfer duty, capital gains tax, secondary tax on companies and dividends tax;
- seeks to provide general guidance on the interpretation of paragraph 51A and related exemption provisions and does not deal with every possible situation which can arise;
- is not a binding general ruling issued under section 89 of the Tax Administration Act 28 of 2011; and
- reflects the law as amended by the Taxation Laws Amendment Act 24 of 2011, which was promulgated on 10 January 2012. This version of the guide has also been updated to include references to the Rates and Monetary Amounts and Amendment of Revenue Laws Act 13 of 2012 (promulgated 9 October 2012) and the Tax Administration Act 28 of 2011 (effective 1 October 2012 except for certain provisions relating to interest).

Should you require additional information concerning any aspect of taxation you may –

- visit the SARS website at **www.sars.gov.za**;
- visit your nearest SARS branch;
- contact your own tax adviser or tax practitioner;
- if calling locally, contact the SARS Contact Centre on 0800 00 7277; or
- if calling from abroad, contact the SARS Contact Centre on +27 11 602 2093 (between 8am and 4pm South African time).

Comments on this guide may be sent to **policycomments@sars.gov.za**.

Prepared by

Legal and Policy Division
SOUTH AFRICAN REVENUE SERVICE

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Glossary

In this guide unless the context indicates otherwise –

- **"CGT"** means capital gains tax, namely, the normal tax attributable to the inclusion of a taxable capital gain in taxable income under section 26A of the Act;
- **"CIPC"** means the Companies and Intellectual Property Commission established under section 185 of the Companies Act 71 of 2008;
- **"company"** includes a close corporation;
- **"Eighth Schedule"** means the Eighth Schedule to the Act;
- **"IFRIC"** means the International Financial Reporting Interpretations Committee;
- **"paragraph"** means a paragraph of the Eighth Schedule;
- **"section"** means a section of the Act;
- **"STC"** means secondary tax on companies;
- **"the Act"** means the Income Tax Act 58 of 1962;
- **"the Transfer Duty Act"** means the Transfer Duty Act 40 of 1949; and
- any other word or expression bears the meaning ascribed to it in the Act.

1. Purpose

This guide deals with CGT, dividends tax, STC and transfer duty relief measures that apply to the acquisition by a natural person of a residence from a company or trust between 1 October 2010 and 31 December 2012. The donations tax and value-added tax consequences are also examined.

2. Background

Paragraph 45 provides that only a natural person (individual) or special trust is entitled to disregard the whole or a portion of the capital gain or capital loss on disposal of that person's primary residence. Subject to certain exceptions –

- the first R2 million[1] of the capital gain or capital loss must be disregarded, or
- if the proceeds are R2 million or less, the full amount of any capital gain must be disregarded.

Historically many individuals purchased their residences in companies or trusts for a variety of reasons, including protection from creditors, avoidance of transfer duty and estate duty and circumvention of the Group Areas Act 36 of 1966 (repealed). A window of opportunity was granted in 2002 which enabled these individuals to transfer their residences out of their companies or trusts into their own names without suffering any adverse CGT, STC or transfer duty consequences [see Appendix A of the *Comprehensive Guide to CGT* (Issue 4)].

[1] Section 10 of the Rates and Monetary Amounts and Amendment of Revenue Laws Act 13 of 2012 promulgated on 9 October 2012 increases the exclusion from R1,5 million to R2 million for the 2013 year of assessment.

Following the amendment of the Transfer Duty Act in 2002, it is no longer possible to avoid transfer duty by disposing of the shares or member's interest in a company holding residential property, or by substituting beneficiaries holding contingent interests in the residential property of a discretionary trust.

Before the amendments effected by the Revenue Laws Amendment Act 74 of 2002 the distribution of a capital profit in anticipation of or in the course of liquidation, winding up or deregistration of a company was exempt from STC. However, since the amendments, any capital profit derived by a company on or after 1 October 2001 is subject to STC, even if distributed in anticipation of or in the course of liquidation, winding up or deregistration. Furthermore, with effect from 1 January 2011 all capital profits, regardless of whether derived before or after 1 October 2001, are subject to STC. STC has been repealed with effect from 1 April 2012 but has been replaced by dividends tax under section 64E which also applies regardless of the capital or revenue nature of profits out of which a dividend is distributed. Dividends tax is levied at a rate of 15% compared to the previous STC rate of 10%.[2]

Outside the relief measures discussed in this guide, maintaining a residence in a company or trust has, amongst others, the following tax consequences:

- A natural person who holds an interest in a primary residence owned by a trust is not entitled to the primary residence exclusion except in the case of a lessee who is not a connected person in relation to the trust.[3]
- A company or trust is not entitled to the primary residence exclusion.[4]
- A company would potentially be liable for CGT at a rate of 14%[5] on any capital gain on a residence disposed of during years of assessment commencing before 1 March 2012 and at 18,65%[6] thereafter.
- A trust would potentially be liable for CGT at a rate of 20%[7] on any capital gain on the disposal of a residence before 1 March 2012 and at 26,64%[8] thereafter.
- A trust that vests a residence in a resident beneficiary must disregard any capital gain on such a disposal and the beneficiary must take it into account.[9] An individual's effective CGT rate is 0% to 10% up to 29 February 2012 and 0% to 13,32% thereafter.[10]

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2 Section 6 of the Rates and Monetary Amounts and Amendment of Revenue Laws Act 13 of 2012.

3 Definition of "an interest" in paragraph 44.

4 Under paragraph 45(1) the primary residence exclusion applies only to a natural person or a special trust.

5 28% × 50% = 14%.

6 28% × 66,6% = 18,65%. The increase in the inclusion rate from 50% to 66,6% was effected by the Rates and Monetary Amounts and Amendment of Revenue Laws Act 13 of 2012. It applies to years of assessment commencing on or after 1 March 2012.

7 40% × 50% = 20%.

8 40% × 66,6% = 26,64%. The increase in the inclusion rate from 50% to 66,6% was effected by the Rates and Monetary Amounts and Amendment of Revenue Laws Act 13 of 2012. It applies to years of assessment commencing on or after 1 March 2012.

9 Paragraph 80(1).

10 40% × 33,3% = 13,3%. The increase in the inclusion rate from 25% to 33,3% was effected by the Rates and Monetary Amounts and Amendment of Revenue Laws Act 13 of 2012.

- A natural person acquiring the residence will be subject to transfer duty on a sliding scale at a rate varying between 0 and 8%.[11]
- A company would potentially be liable for STC at a rate of 10% on the distribution of a residence as a dividend *in specie* before 1 April 2012. Thereafter it would potentially be liable for dividends tax at a rate of 15% on such a distribution *in specie*[12] unless the dividend was exempt[13] or qualified to be taxed at a reduced rate.[14]

Retaining a residence in a company or trust may carry other benefits (for example, a trust may provide estate duty savings and protection of assets from creditors). However, these advantages need to be weighed up against the loss of the primary residence exclusion (worth up to R266 400[15] in tax savings) and the higher rate of CGT in a company (18,65% v 13,32%) or trust (26,64% v 13,32%) and the imposition of dividends tax at 15%.

It has emerged that many individuals did not avail themselves of the 2002 opportunity, with the result that they now face the adverse tax consequences described above when disposing of a residential property from a company or trust.

Paragraph 51

A further window of opportunity in the form of paragraph 51 of the Eighth Schedule, which operated on a roll-over basis, was introduced by the Taxation Laws Amendment Act 17 of 2009. Paragraph 51 applies to the disposal of a residence by a company or trust on or after 11 February 2009 but no later than 30 September 2010. Thus paragraph 51 will apply to residences acquired under contracts signed on or before 30 September 2010 which are not subject to any suspensive conditions at that date. There is no time limit on the registration of the property in the deeds registry. In other words a property acquired unconditionally on or before 30 September 2010 which is registered after that date must still be dealt with under paragraph 51.

A disposal of a residence that is subject to suspensive conditions which are only fulfilled after 30 September 2010 must be addressed under paragraph 51A.

For guidance on paragraph 51, see Appendix B of the *Comprehensive Guide to CGT* (Issue 4).

Paragraph 51A

On 17 February 2010 it was announced in the 2010 Budget Tax Proposals that paragraph 51 was inadequate and that a

> "new, more flexible window period is proposed so that these residential property entities are to be liquidated or dissolved with limited compliance and enforcement effort."

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11 Transfer duty rates on a sliding scale also apply to legal persons (close corporations, companies and trusts) for properties acquired under purchase agreements concluded on or after 23 February 2011. For details see the SARS website under Tax Types/Transfer Duty.

12 Under section 64EA(*b*) a resident company distributing a dividend *in specie* is liable for dividends tax.

13 Section 64FA(1).

14 Section 64FA(2).

15 R2 000 000 × 33,3% × 40% (assuming the taxpayer is paying the maximum marginal rate of tax).

The Taxation Laws Amendment Act 7 of 2010, promulgated on 2 November 2010,[16] inserted paragraph 51A which widens the relief in a number of respects but also imposes new conditions. The revised relief measure came into operation on 1 October 2010 and applies to the disposal of a residence from a company or trust on or after that date and before 1 January 2013.

Further amendments to paragraph 51A have been made by the Taxation Laws Amendment Act 24 of 2011, most of which have been backdated to 1 October 2010. These amendments –

- extend the relief to qualifying holiday homes;
- clarify who may be an acquirer;
- confirm that the connected person relationship between the company or trust and the acquirer must be determined at the time of disposal;
- require a trust to be terminated rather than revoked; and
- effect a number of technical corrections.

This guide deals with the relief measures in paragraph 51A and related provisions.

3. Taxes qualifying for exemption

The relevant provisions offer exemption from –

- transfer duty on the acquisition of an interest in a residence contemplated in paragraph 51A [section 9(20) of the Transfer Duty Act];
- STC on any dividend declared before 1 April 2012 which constituted the disposal of an interest in a residence as contemplated in paragraph 51A [section 64B(5)(*k*A)];
- dividends tax (which replaced STC on 1 April 2012)[17] on a dividend *in specie* constituting a disposal as contemplated in paragraph 51A [section 64FA(1)(*c*)]; and
- CGT on any capital gain realised by the company or trust on disposal of an interest in a residence [paragraph 51A].

4. Modes of disposal

Paragraph 51A does not specify how the residence must be disposed of by the company or trust, for example, whether by way of a distribution or sale. Nevertheless, care should be exercised when a company disposes of a residence other than by way of a distribution *in specie*, since there could be adverse dividends tax, STC and donations tax consequences.

Set out below is a basic example which illustrates how a residence can be disposed of in order to access the relief under paragraph 51A without adverse tax consequences. The example is merely intended to serve as an introduction to the relief measures which will be explored in more detail later.

[16] *GG* 33726 of 2 November 2010.

[17] The effective date of 1 April 2012 was fixed by the Minister in GN 1073 *GG* 34873 of 20 December 2011.

Example 1 – Disposal of residence by close corporation

Facts:

Albert is the sole member of ABC CC which holds a residence which he has used as a holiday home from 11 February 2009 to 18 May 2012 when he acquired the residence from ABC CC. Immediately before the disposal of the residence ABC CC's balance sheet appeared as follows:

	R
Member's interest	100
Revaluation reserve (1 October 2001)	240 000
Member's loan	1 159 900
	1 400 000
Residence	1 400 000

The residence cost ABC CC R1 160 000 in 1998 and had a market value on 1 October 2001 of R1 400 000. The current market value of the residence is R2 million.

ABC CC used the residence to repay the member's interest and loan account with the balance being declared as a dividend *in specie*. By 30 September 2012 Albert had taken the necessary steps under section 41(4) to have ABC CC liquidated.

Result:

The repayment of the member's interest of R100 represents a return of contributed tax capital provided that Albert determines this before the distribution (see the definition of the term "contributed tax capital" in section 1(1)). The return of contributed tax capital has no tax implications for ABC CC. The amount will constitute proceeds in Albert's hands on disposal of his member's interest but nothing turns on this because he must in any event disregard any capital gain or capital loss on disposal of his member's interest under paragraph 51A(3) or (4).

The repayment of the member's loan account has been made for value and no capital gain arises under paragraph 12(5). From Albert's perspective the amount represents a recovery of the base cost of the loan which does not give rise to any capital gain or loss.

The current market value of the residence (R2 million) less the member's interest of R100 and loan of R1 159 900 represents a dividend *in specie* of R840 000 which is exempt from dividends tax under section 64FA(1)(*c*). The dividend therefore has no tax implications for ABC CC or Albert.

ABC CC must disregard any capital gain or capital loss on disposal of the residence under paragraph 51A(2).

The base cost of the residence in Albert's hands must be determined under paragraph 51A(3) or (4) depending on when he acquired the member's interest (that is, before or after the close corporation acquired the residence). This aspect is considered in more detail in **9.4** and **9.5**.

5. Assets other than a residence

The CGT, dividends tax, STC and transfer duty relief measures referred to in **3** above apply only to an interest in a residence. Paragraph 51A does not apply to any assets other than an interest in a residence which are disposed of by a company or trust.

6. The transfer duty exemption

The transfer duty exemption requirements are contained in section 9(20) of the Transfer Duty Act.

> **9. Exemptions from duty.—**
>
> (20) No duty shall be payable in respect of any acquisition of any interest in a residence as contemplated in paragraph 51 or 51A of the Eighth Schedule to the Income Tax Act, 1962 (Act No. 58 of 1962), where that acquisition takes place as a result of a transfer or disposal contemplated in either of those paragraphs.

Effective date

Under section 3(3) of the Taxation Laws Amendment Act 7 of 2010, section 9(20) comes into operation on 1 October 2010 and applies in respect of acquisitions taking place on or after that date and before 1 January 2013.

It might happen that a particular beneficiary of a trust will not qualify for the relief under section 9(20), for example, because he or she does not meet the domestic usage requirement in paragraph 51A(1)(*b*). It might nevertheless be possible to transfer the residence to the beneficiary free of transfer duty under section 9(4)(*b*) of the Transfer Duty Act. The latter provision applies when the beneficiary taking transfer is a "relative" as defined in the Estate Duty Act 45 of 1955 of the trust's founder and does not pay any consideration for the residence, whether directly or indirectly. CGT may nevertheless be payable.

When structuring these transactions sight should not be lost of section 20B of the Transfer Duty Act which applies to transactions, operations, schemes or understanding for obtaining an undue tax benefit.

7. The STC exemption

The STC exemption is contained in section 64B(5)(*k*A).

> (5) There shall be exempt from the secondary tax on companies—
>
> (*k*A) any dividend declared by a company which constitutes a disposal of an interest in a residence as contemplated in paragraph 51A of the Eighth Schedule; and

Effective date

Section 64B(5)(*k*A) came into operation on 1 October 2010 and applies in respect of disposals made on or after that date and before 1 January 2013.

Qualifying disposals

In order to qualify for an exemption from STC under section 64B(5)(*k*A) –

- the residence must comply with paragraph 51A;
- the dividend declared must comprise the disposal of a residence; and
- the dividend must be declared before 1 April 2012.

The *Oxford English Dictionary* provides, amongst others, the following meaning of the term "disposal":[18]

> "2. The action of disposing of, putting away, getting rid of, settling, or definitely dealing with."

A distribution *in specie* of a qualifying residence thus constitutes the "disposal" of a residence in the ordinary sense of the term and will meet the requirements in the second bullet point above.

A sale of the residence to a shareholder at less than market value will give rise to a dividend as defined in section 1(1), to the extent that it comprises –[19]

> "any amount transferred or applied by a company that is a resident for the benefit or on behalf of any person in respect of any share in that company".

Since the amount is a dividend as defined in section 1 it will by virtue of section 64C(4)(*a*) not comprise a deemed dividend under section 64C(2)(*a*).

Example 2 – Sale of an interest in a residence to a shareholder at less than market value

Facts:

A company holds a residence with a book value of R1 million and a market value of R1,5 million, which it disposes of to its sole shareholder on 15 March 2012 for R1 million. The shareholder has used the residence mainly for domestic purposes from 11 February 2009 to the date of disposal.

Result:

The sale gives rise to a dividend as defined in section 1 of R1 500 000 less R1 000 000 = R500 000, being the benefit to the shareholder in respect of that shareholder's shares in the company. The dividend of R500 000 is exempt from STC under section 64B(5)(*k*A) since it results directly from the disposal of the residence as contemplated in paragraph 51A.

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18 [OED Online] **http://dictionary.oed.com/ff** Oxford University Press [Accessed 21 February 2011].

19 Opening words of the definition of "dividend" in section 1.

A sale by a company of a residence at less than market value to a "connected person" as defined in section 1 in relation to a shareholder will, to the extent of the benefit, comprise a deemed dividend under section 64C(2)(*a*), which reads as follows:

> (2) For the purposes of section 64B, an amount shall, subject to the provisions of subsection (4), be deemed to be a dividend declared by a company to a shareholder, where—
>
> (*a*) any cash or asset is distributed or transferred by that company to or for the benefit of that shareholder or any connected person in relation to that shareholder;

The deemed dividend excludes any consideration paid for the residence [section 64C(4)(*b*A)(i)].

Such a deemed dividend will be exempt under section 64B(5)(*k*A) because it relates to the disposal of the residence by way of a sale. However, any amount returned to a shareholder after the sale of the residence, which comprises a dividend as defined in section 1, will not qualify for exemption from STC, since its distribution does not comprise the disposal of a residence.

A sale at less than market value may also carry donations tax consequences – see **10**.

The distribution of assets other than a residence will not qualify for the STC exemption in section 64B(5)(*k*A). Accordingly, a sale of the residence at market value and the subsequent distribution of cash or the resulting loan account will not qualify for exemption from STC under section 64B(5)(*k*A) because it does not constitute the disposal of a residence. However, in relation to the distribution of these other assets which occurred before 1 January 2011, an STC exemption may be available to the extent that there were pre-31 March 1993[20] profits or pre-1 October 2001 capital profits available for distribution [section 64B(5)(*c*)].[21]

8. The dividends tax exemption

The dividends tax exemption is contained in section 64FA(1)(*c*).

> **64FA. Exemption from and reduction of tax in respect of dividends *in specie*.—**(1) Where a company declares and pays a dividend that consists of a distribution of an asset in specie, that dividend is exempt from the dividends tax to the extent that it constitutes a distribution of an asset *in specie* if—
>
> (*a*) . . . (Not applicable)
>
> (*b*) . . . (Not applicable)
>
> (*c*) the dividend constitutes a disposal as contemplated in paragraph 51A of the Eighth Schedule.

[20] Profits derived during any year of assessment which ended not later than 31 March 1993.
[21] Section 64B(5)(*c*) was deleted with effect from 1 January 2011.

Effective date

Section 64FA comes into operation on 1 April 2012.[22]

A distribution of a qualifying residence *in specie* will constitute the disposal of a residence for the purposes of section 64FA(1)(*c*).

A sale of the residence to a person at less than market value will give rise to a dividend as defined in section 1(1), to the extent that it comprises –[23]

> "any amount transferred or applied by a company that is a resident for the benefit or on behalf of any person in respect of any share in that company".

The above definition covers below-market value sales to shareholders and other persons on behalf of shareholders (for example, a sale concluded at the instance of a shareholder).

The dividend would be equal to the difference between the market value of the residence and the selling price. Such a dividend will comprise a dividend in specie and will be covered by the exemption in section 64FA(1)(*c*).

A sale of the residence to a qualifying acquirer (see **9.8**) at market value will not give rise to a dividend but any resulting profit will be subject to dividends tax when distributed to a natural person shareholder since it does not comprise the distribution of a residence *in specie* and thus falls outside section 64FA(1)(*c*).

9. The CGT relief

Paragraph 51A deals with the following matters:

- Paragraph 51A(1) sets out the requirements for a qualifying disposal from a company or trust and makes provision for the termination of the company or trust holding the residence. It also identifies who qualifies as an acquirer of the residence when read with paragraph 51A(6).
- Paragraph 51A(2) provides for a disposal at base cost for the company or trust disposing of the residence.
- Paragraph 51A(3) determines the base cost of the residence in the hands of the shareholder. It applies when the shareholders acquired their shares in a company already holding the residence. The base cost of the residence is deemed to be the cost of the shares plus subsequent improvements.
- Paragraph 51A(4) determines the base cost of the residence for an acquirer from a company by means of a roll-over. It applies when the company acquired the residence in circumstances other than those in paragraph 51A(3) (for example, when the company acquired the residence after the shareholders acquired their shares).
- Paragraph 51A(5) determines the base cost of the residence for an acquirer from a trust by means of a roll-over.

[22] Section 79(2) of the Taxation Laws Amendment Act 24 of 2011 read with GN 1073 *GG* 34873 of 20 December 2011 (the latter notice established the date on which the dividends tax in Part VIII of Chapter II of the Act came into operation).

[23] Opening words of the definition of "dividend" in section 1(1).

- Paragraph 51A(6) deals with a multi-tier structure and confirms that an acquiring company or trust must on-distribute the residence and thereafter terminate its existence. It also confirms who may be a qualifying acquirer.
- Paragraph 51A(7) has been deleted with effect from 1 April 2012. It defined a "share" by reference to the definition of that term in paragraph 74.

9.1 The law

Paragraph 51A of Eighth Schedule

51A. Disposal of residence by company or trust and liquidation, winding up, deregistration or termination of company or trust.—(1) Subject to subparagraph (6), this paragraph applies where a company or trust disposes of an interest in a residence and—

(*a*) the disposal takes place on or before 31 December 2012;

(*b*) the residence to which that interest relates is mainly used for domestic purposes during the period commencing on 11 February 2009 and ending on the date of the disposal contemplated in item (*a*) by one or more natural persons who are connected persons in relation to the company or trust at the time of that disposal; and

(*c*) . . . .

(*d*) within a period of six months commencing on the date of the disposal contemplated in item (*a*)—

(i) in the case of a company making the disposal, that company has taken steps to liquidate, wind up or deregister as contemplated in section 41(4); or

(ii) in the case of a trust making the disposal, steps have been taken to terminate the trust.

(2) Where a company or a trust makes a disposal of an interest in a residence as contemplated in subparagraph (1), that company or trust must be deemed to have made that disposal for an amount equal to the base cost of that interest as at the date of that disposal.

(3) Where—

(*a*) an interest in a residence has been acquired by a person as a result of a disposal by a company of that interest to that person as contemplated in subparagraph (1);

(*b*) that person (together with all other persons holding shares in that company) acquired all the shares in the company subsequent to the date of acquisition by the company of that interest; and

(*c*) 90 per cent or more of the market value of the assets held by the company during the period commencing on 11 February 2009 and ending on the date of the disposal contemplated in subparagraph (1)(*a*) is attributable to that interest,

that person must—

(i) disregard the disposal of all shares held by that person in that company for purposes of determining his or her taxable income, assessed loss, aggregate capital gain or aggregate capital loss if that disposal is made in anticipation of or in the course of the liquidation, winding up or deregistration of that company; and

(ii) be deemed to have acquired that interest at a cost equal to the base cost of the shares contemplated in subitem (i) as at the date of the acquisition by the person of those shares plus the cost of any improvements effected in respect of that interest subsequent to that date of acquisition.

(4) Where an interest in a residence has been acquired by a person as a result of a disposal by a company of that interest to that person as contemplated in subparagraph (1) and where subparagraph (3) does not apply—

(*a*) that person must disregard the disposal of any share in that company for purposes of determining his or her taxable income, assessed loss, aggregate capital gain or aggregate capital loss if that disposal is made in anticipation of or in the course of the liquidation, winding up or deregistration of that company; and

(*b*) that person and that company must be deemed to be one and the same person with respect to—

(i) the date of acquisition of that interest by that company;

(ii) the amount and date of incurral by that company of any expenditure in respect of that interest allowable in terms of paragraph 20; and

(iii) any valuation of that interest effected by that company as contemplated in paragraph 29(4).

(5) Where an interest in a residence has been acquired by a person as a result of a disposal by a trust of that interest to that person as contemplated in subparagraph (1), that person and that trust must for purposes of determining any capital gain or capital loss in respect of the disposal by that person of that interest so acquired be deemed to be one and the same person with respect to—

(*a*) the date of acquisition of that interest by that trust;

(*b*) the amount and date of incurral by that trust of any expenditure in respect of that interest allowable in terms of paragraph 20; and

(*c*) any valuation of that interest effected by that trust as contemplated in paragraph 29(4).

(6) This paragraph does not apply to any disposal made to a person unless—

(*a*) within a period of six months commencing on the date of that disposal—

(i) where that person is a company, that company has taken steps to liquidate, wind up or deregister as contemplated in section 41(4); or

(ii) where that person is a trust, steps have been taken to terminate the trust;

(*b*) one or more natural persons contemplated in subparagraph (1)*(b)* acquire the residence contemplated in that subparagraph on or before 31 December 2012.

(7) . . . .[24]

Effective date

Paragraph 51A came into operation on 1 October 2010 and applies in respect of disposals made on or after that date and before 1 January 2013. With the exception of the deletion of paragraph 51A(7), which is effective from 1 April 2012, all the amendments made to paragraph 51A by the Taxation Laws Amendment Act 24 of 2011 are deemed to have come into operation on 1 October 2010 and apply in respect of disposals made on or after that date and before 1 January 2013.

[24] The deletion of paragraph 51A(7) which contained a definition of a “share” comes into operation on 1 April 2012 and applies in respect of disposals made on or after that date and before 1 January 2013.

9.2 Qualifying disposals

In order to qualify under paragraph 51A the disposal of a residence by a company or trust must meet the following requirements:

9.2.1 An interest in a residence must be disposed of

The terms “an interest” and “residence” are defined in paragraph 44 as follows:

> **“an interest”** means—
>
> (*a*) any real or statutory right; or
>
> (*b*) a share owned directly in a share block company as defined in the Share Blocks Control Act, 1980 (Act No. 59 of 1980) or a share or interest in a similar entity which is not a resident; or
>
> (*c*) a right of use or occupation,
>
> but excluding—
>
> (i) a right under a mortgage bond; or
>
> (ii) a right or interest of whatever nature in a trust or an asset of a trust, other than a right of a lessee who is not a connected person in relation to that trust;
>
> **“residence”** means any structure, including a boat, caravan or mobile home, which is used as a place of residence by a natural person, together with any appurtenance belonging thereto and enjoyed therewith.

Vacant land

Vacant land does not qualify for the relief under paragraph 51A since it does not contain a “residence” as defined above (that is, it does not contain a “structure”).

Land with appurtenances

It may happen that a trust or company holds two pieces of adjacent land, one of which contains the residence while the other contains “appurtenances” which are used and enjoyed together with the residence such as a swimming pool or tennis court. In such a case the land containing the appurtenances will also potentially qualify for the relief under paragraph 51A and related provisions when transferred with the land containing the residence since it meets the meaning of a “residence” as defined in paragraph 44.

Share block interests

A share in a share block company comprises an interest in a residence (paragraph (*b*) of the definition of “an interest” in paragraph 44). Thus a company or trust holding a share in a share block company can make use of paragraph 51A to dispose of that share to a qualifying acquirer.

While a company or trust may dispose of shares in a share block company under paragraph 51A, the transfer of a unit in a share block company to its members must be dealt with under paragraph 67B.

Size of land

Unlike paragraph 51 which contained a two-hectare limit, paragraph 51A contains no restriction on the size of land on which the residence is situated. It is considered that the common property associated with a sectional title unit or an interest in a share block company is not excluded from paragraph 51A.

Paragraph 51A refers only to the disposal of an interest in a residence, it does not specifically refer to the land on which the residence is situated. Nevertheless, under the common law principle of *accessio,* a residence accedes to the land on which it is situated. It is therefore considered that paragraph 51A does not extend only to the bricks and mortar of the residence but also the land on which it is situated. In a decision whether the residence and its land will qualify for the relief, paragraph 51A(1)(*b*) must be considered (see **9.2.3**), it requires that the residence be used *mainly* for domestic purposes. By implication this requirement also extends to the land on which the residence is situated. Accordingly, a three-hectare plot, with a residence on it, which is fully used for domestic purposes will qualify. Similarly, a residence on a three-hectare plot of which two-thirds is used for domestic purposes and one-third is used for trade purposes will qualify since it is mainly (that is, more than 50%) used for domestic purposes. However, the transfer of a residence situated on a commercial farm of 500 hectares of which only 1 hectare is used for domestic purposes will not qualify.

9.2.2 Disposed of on or after 1 October 2010 but no later than 31 December 2012 [paragraph 51A(1)(*a*)]

The residence must be disposed of on or after 1 October 2010[25] but no later than 31 December 2012.[26]

The time of disposal rules in paragraph 13 govern when a disposal takes place. Under paragraph 13(1)(*a*) the time of disposal of an asset by means of a change of ownership effected or to be effected from one person to another because of an event, act, forbearance or by operation of law is, in the case of –

- an agreement subject to a suspensive condition, the date on which the condition is satisfied [paragraph 13(1)(*a*)(i)];
- any agreement which is not subject to a suspensive condition, the date on which the agreement is concluded [paragraph 13(1)(*a*)(ii)];
- the distribution of an asset of a trust by a trustee to a beneficiary to the extent that the beneficiary has a vested interest in the asset, the date on which the interest vests [paragraph 13(1)(*a*)(iiA)]; and
- the expropriation of an asset, the date on which the person receives the full compensation agreed to or finally determined by a competent tribunal or court [paragraph 13(1)(*a*)(iv)].

The time of disposal for the distribution of an asset by a company to a shareholder,[27] is the date on which that asset is so distributed as contemplated in paragraph 75 [paragraph 13(1)(*e*)]. Under paragraph 75 the asset is distributed on the "date of distribution" as defined in paragraph 74. That definition reads as follows:

> **"date of distribution"**, in relation to any distribution, means the date of payment of the distribution—

25 Section 105(2) of the Taxation Laws Amendment Act 7 of 2010.
26 Paragraph 51A(1)(*a*).
27 For example, the distribution of an asset as a dividend *in specie*.

(*a*) by a company subject to the condition that it be payable to a shareholder of the company registered in that company's share register on a specified date, in which case it must be that date;

(*b*) by a company to a shareholder of that company otherwise than by way of a formal declaration of a dividend, in which case it must be the date on which the shareholder became entitled to that distribution; or

(*c*) by the liquidator of a company to a shareholder of that company in the course of the winding up or liquidation of that company, in which case it must be the date on which the shareholder became entitled to that distribution;

The time of disposal rules are important for at least two reasons. First, they will determine whether the disposal falls under paragraph 51 or 51A. Secondly, they will determine whether a residence has been disposed of before the cut off date of 31 December 2012. The time of disposal should not be confused with the time of registration in the deeds registry. Paragraph 51A does not lay down any time limit for registration of the property in the name of the acquirer.

For transfer duty purposes the "date of acquisition"[28] of property acquired under a transaction subject to a suspensive condition is the date on which the transaction was entered into. Nevertheless, that date is irrelevant for the purposes of determining whether paragraph 51 or 51A applies and as indicated above the determination must be done under paragraph 13.

Example 3 – Disposal of residence under an agreement not subject to any suspensive conditions

Facts:

On 30 September 2010 the XYZ Trust sold an interest in a residence to its founder. The sale was not subject to any suspensive conditions.

Result:

The sale falls under paragraph 51 since it occurred between 11 February 2009 and 30 September 2010. Paragraph 51A does not apply.

Example 4 – Disposal of residence under an agreement subject to a suspensive condition

Facts:

On 31 August 2010 the ABC Trust sold an interest in a residence to its trustee who was a relative of the trust beneficiaries. The sale agreement was subject to the trustee obtaining a bond from a bank. The trustee obtained the bond on 15 October 2010.

Result:

The disposal occurred on 15 October 2010 when the suspensive condition was satisfied [paragraph 13(1)(*a*)(i)]. It therefore falls within the qualifying period laid down by paragraph 51A.

[28] As defined in section 1(1) of the Transfer Duty Act.

Example 5 – Distribution *in specie* of residence to sole shareholder

Facts:

The directors of ABC (Pty) Ltd pass a resolution approving the payment of the distribution of the company's sole asset, a residence, as a dividend *in specie* to its sole shareholder as reflected in the company's share register on 31 December 2012. The residence is registered in the shareholder's name on 31 March 2013.

Result:

The time of disposal is the "date of distribution" as defined in paragraph 74. The date of distribution is 31 December 2012 because the resolution states that the distribution is payable to the company's shareholder as registered in the company's share register on 31 December 2012.

The disposal falls within the qualifying period laid down by paragraph 51A because the residence was disposed of before 1 January 2013.

9.2.3 The domestic use requirement [paragraph 51A(1)(*b*)]

A qualifying residence must be mainly used for domestic purposes by one or more natural persons during the period from 11 February 2009 to the date of disposal by the company or trust. In *SBI v Lourens Erasmus (Eiendoms) Bpk*[29] Botha JA held that the word "mainly" prescribed a purely quantitative standard of more than 50%. The measurement of the domestic usage will normally be determined on either a time basis or floor-area basis. Non-domestic use could be measured on a floor-area basis in the case of –

- the letting of a portion of the residence, for example, as a guesthouse;
- running a business from the premises; or
- using a portion of the residence as an office.

The time basis would be appropriate to, say, a holiday home which is made available for letting for a number of months during the period 11 February 2009 to the date of disposal.

Example 6 – Measurement of domestic usage of residence on a floor-area basis

Facts:

ABC (Pty) Ltd's sole asset is a double-storey house. From 11 February 2009 until the date of disposal of the residence by the company on 31 May 2012 the ground floor of the residence comprising 51% of the total floor area was used as a shop. The shareholder occupied the top floor as a residence.

Result:

The residence does not qualify under paragraph 51A since it was not used mainly (that is, > 50%) for domestic purposes.

[29] 1966 (4) SA 444 (A), 28 SATC 233 at 245.

Example 7 – Measurement of domestic usage of residence on a time basis

Facts:

XYZ CC's sole asset is a flat at the coast. Mr and Mrs X each hold a 50% interest in the CC. The flat was disposed of to Mr and Mrs X on 11 March 2012 as a distribution *in specie*. For six months during the period 11 February 2009 to 11 March 2012 the flat was let to holiday makers. During the remaining 30 months it was used as a holiday home by Mr and Mrs X.

Result:

Since the flat was used mainly (30/36 = 83%) for domestic purposes it will qualify under paragraph 51A(1)(*b*).

Occupation after 11 February 2009

A person who acquires an interest in a company or trust holding a residence after 11 February 2009 and commences using the residence mainly for domestic purposes thereafter is not a qualifying acquirer under paragraph 51A(1)(*b*) because the person would not have used the residence mainly for domestic purposes throughout the qualifying period. In other words, 11 February 2009 represents a cut-off date after which taxpayers are expected to acquire their residences in their own names if they wish to avoid the adverse tax consequences of owning residential property through a company or trust.

9.2.4 The connected-person requirement [paragraph 51A(1)(*b*)]

The natural persons who used the residence mainly for domestic purposes must be connected persons in relation to the company or trust at the time of disposal of the residence by the company or trust. The natural person need not be a connected person throughout the period from 11 February 2009 to the date of disposal of the residence by the company or trust. The natural person must, however, be a connected person at the time of disposal and have mainly used the residence for domestic purposes during the period 11 February 2009 to the date of disposal in order to qualify as an acquirer. For example, the natural person could become a connected person by acquiring additional shares in the company or by becoming a spouse of a shareholder.

The term "connected person" is defined in section 1(1). Some extracts from the definition are set out below.

"connected person" means—

(*a*) in relation to a natural person—

(i) any relative; and

(ii) any trust (other than a portfolio of a collective investment scheme in securities) of which such natural person or such relative is a beneficiary;

(*b*) in relation to a trust (other than a portfolio of a collective investment scheme in securities)—

(i) any beneficiary of such trust; and

(ii) any connected person in relation to such beneficiary;

(*b*A) in relation to a connected person in relation to a trust (other than a collective investment scheme in property shares managed or carried on by any company registered as a manager under section 42 of the Collective Investment Schemes Control Act, 2002, for purposes of Part V of that Act and other than a portfolio of a collective investment scheme in securities), includes any other person who is a connected person in relation to such trust;

(*c*) [relates to partnerships]

(*d*) in relation to a company—[30]

(i) any other company that would be part of the same group of companies as that company if the expression "at least 70 per cent of the equity shares of" in paragraphs (*a*) and (*b*) of the definition of "group of companies" in this section were replaced by the expression "more than 50 per cent of the equity shares of or voting rights in";

(ii) . . . . . .

(iii) . . . . . .

(iv) any person, other than a company as defined in section 1 of the Companies Act, 2008 (Act No. 71 of 2008), who individually or jointly with any connected person in relation to himself, holds, directly or indirectly, at least 20 per cent of—

(*aa*) the equity shares in the company; or

(*bb*) the voting rights in the company;

(v) any other company if at least 20 per cent of the equity shares of or voting rights in the company are held by that other company, and no shareholder holds the majority voting rights in the company;

(*v*A) any other company if such other company is managed or controlled by—

(*aa*) any person who or which is a connected person in relation to such company; or

(*bb*) any person who or which is a connected person in relation to a person contemplated in item (*aa*); and

(vi) where such company is a close corporation—

(*aa*) any member;

(*bb*) any relative of such member or any trust (other than a portfolio of a collective investment scheme in securities) which is a connected person in relation to such member; and

(*cc*) any other close corporation or company which is a connected person in relation to—

(i) any member contemplated in item (*aa*); or

(ii) the relative or trust contemplated in item (*bb*); and

(*e*) in relation to any person who is a connected person in relation to any other person in terms of the foregoing provisions of this definition, such other person:

[30] Paragraph (*d*)(i) and (v) amended by section 7(1)(*a*) of the Taxation Laws Amendment Act 24 of 2011 and deemed to come into operation on 1 January 2012.

In relation to a company (paragraph (*d*)(iv) of the definition of "connected person" in section 1)

A natural person will be a connected person in relation to a company if he or she individually or jointly with any connected person in relation to himself, holds, directly or indirectly, at least 20% of the company's equity shares or voting rights.

Example 8 – Connected person in relation to a company

Facts:

Jack and Jill, a married couple, own 50% and 49% respectively of the shares in ABC (Pty) Ltd, while Bruce, their minor child holds the remaining 1%.

Result:

Jack, Jill and Bruce are connected persons in relation to ABC (Pty) Ltd. Jack and Jill individually hold more than 20% of the company's shares. Bruce is a connected person in relation to his parents (being a relative – paragraph (*a*)(i) of the definition of "connected person") and together with his parents holds at least 20% of the shares in ABC (Pty) Ltd (50% + 49% + 1% = 100%).

In relation to a close corporation (paragraph (*d*)(vi) of the definition of "connected person" in section 1(1))

The following persons are connected persons in relation to a close corporation:

- A member of that close corporation, no matter the size of that member's interest.
- A relative of a member.
- A trust (other than a portfolio of a collective investment scheme in securities) which is a connected person in relation to a member.
- A close corporation or company which is a connected person in relation to –
  - a member of the close corporation; or
  - any relative of a member of the close corporation; or
  - any trust which is a connected person in relation to a member of the close corporation.

The range of connected persons in relation to a close corporation is thus much wider than in relation to a company.

Example 9 – Connected person in relation to a close corporation

Facts:

Homer, Marge, Abe, Bart, Maggie and Thelma each hold 16,67% of the members' interest in ABC CC.

Result:

Homer, Marge, Abe, Bart, Maggie and Thelma are connected persons in relation to ABC CC. Every member of a close corporation is a connected person in relation to it irrespective of the size of the member's interest (paragraph (*d*)(vi) of the definition of "connected person" in section 1(1)).

In relation to a trust (paragraph (*b*)(i) and (ii) of the definition of "connected person" in section 1)

Every beneficiary is a connected person in relation to a trust. In addition, a person who is a connected person in relation to a beneficiary of a trust is a connected person in relation to a trust.

The term "beneficiary" is defined in section 1(1) as follows:

> **"beneficiary"** in relation to a trust means a person who has a vested or contingent interest in all or a portion of the receipts or accruals or the assets of that trust;

A founder or trustee of a trust may well be a connected person in relation to a trust if that person is, for example, a relative of a beneficiary.

9.2.5 The termination of the company or trust requirement [paragraph 51A(1)(*d*)]

Within six months of the date of disposal certain specified steps must be taken to terminate the existence of the company or trust holding the residence. This does not mean that the company or trust must actually be terminated within this period; rather it means that the required steps to initiate the process must have been taken.

Companies

The steps specified in section 41(4) must be taken to terminate the existence of a company. Since the procedures for liquidating or winding-up differ to deregistration, different steps are specified in section 41(4) for these termination procedures.

Care should be taken to ensure that the relevant steps laid down in section 41(4) are capable of being taken within the required six-month period before entering into the transactions.

Steps to liquidate or wind up

The table below sets out the required steps when a company is to be voluntarily wound up or liquidated.

Table 1 – Steps under voluntary winding-up or liquidation

Section 41(4)	Steps to be taken within six months of disposal of residence
(*a*)(i)(*aa*)	*Companies and close corporations* Lodge resolution under section 80(2) of the Companies Act 71 of 2008.
(*a*)(i)(*bb*)	*Co-operatives* – Not applicable.

Section 41(4)	Steps to be taken within six months of disposal of residence
(*a*)(i)(*cc*)	*Foreign companies* Comply with similar foreign law relating to liquidation of companies if that foreign law so requires.
(*a*)(ii)	Dispose of all assets and settle all liabilities except for assets required to satisfy any – • reasonably anticipated liabilities to any sphere of government of any country, and • costs of administration relating to the liquidation or winding-up.
(*c*)	Submit a copy of the resolution to SARS.
(*d*)	Submit all outstanding returns or information to SARS required under any law administered by the Commissioner or obtain the necessary extension from SARS. This must be done by the end of the six-month period.

Steps to deregister

The table below sets out the necessary steps to initiate the deregistration of a company.

Table 2 – Steps under deregistration

Section 41(4)	Steps to be taken within six months of disposal of residence
(*b*)(i)	*Companies and close corporations* Lodge a request for the company's deregistration in the prescribed manner and form to the CIPC under section 82(3)(*b*)(ii) of the Companies Act 71 of 2008.
(*b*)(ii)	Deleted.
(*b*)(iii)	*Foreign companies* Lodge a request for the company's deregistration in the prescribed manner and form with a person who, under any similar provision contained in any foreign law, exercises the powers and performs the duties assigned to the CIPC if such foreign law so requires.
(*c*)	Submit copy of the request to SARS.
(*d*)	Submit all outstanding returns or information to SARS required under any law administered by the Commissioner or obtain the necessary extension from SARS. This must be done by the end of the six-month period.

Trusts

Steps must have been taken to terminate the trust. Paragraph 51A is not prescriptive as to what steps must be taken as this will largely depend on the terms of the trust deed. Most trust deeds contain a termination clause which will set out what is required of the trustees.

9.3 No gain or loss treatment of the company or trust [paragraph 51A(2)]

If the requirements discussed in **9.2** are met, the company or trust is deemed to dispose of the interest in a residence at its base cost at the time of the disposal. As a result the company or trust will not make a capital gain nor a capital loss on the disposal. The "no gain / no loss" treatment is confined to an interest in a residence. Other assets which need to be disposed of before the company or trust can be terminated will trigger capital gains and losses in the normal way.

Paragraph 51A(2) applies only for CGT purposes. The sale of a residence held as trading stock will result in the consideration being included in the gross income of the company or trust and the possible application of section 22(8) if the consideration is not market-related. The distribution of such a residence as a dividend *in specie* will trigger a recoupment and consequent inclusion in income at market value under section 22(8)(*b*)(iii). In any event, a residence that was used mainly for domestic purposes by one or more natural persons would probably have ceased to be held as trading stock at the time it was first so used, thus triggering a recoupment at that time under section 22(8)(*b*)(v).

The disposal of a residence on which capital allowances have been claimed will also be subject to recoupment under section 8. In particular, see section 8(4)(*k*) which deems the disposal to take place at market value for the purposes of section 8(4)(*a*) when, for instance, an allowance asset is disposed of by a company to a shareholder or by a person to a connected person in relation to that person.

9.4 Base cost of residence acquired from a company – shares acquired in company already holding the residence [paragraph 51A(3)]

Paragraph 51A(3) applies when –

- an interest in a residence has been acquired by a person as a result of a disposal by a company of that interest to that person as contemplated in paragraph 51A(1);
- that person (together with all other persons holding shares in that company) acquired all the shares in the company after the date of acquisition by the company of that interest; and
- 90% or more of the market value of the assets held by the company during the period commencing on 11 February 2009 and ending on the date of disposal (which must be on or before 31 December 2012) is attributable to that interest.

The first bullet point confirms that the disposal must comply with paragraph 51A(1), for example, it must take place on or before 31 December 2012.

Under the second bullet point all the current shareholders must have acquired their shares in a company that already owned a residence. If any of them acquired their shares before the company acquired the residence, paragraph 51A(3) will not apply and the acquirer will have to establish a base cost for the residence under paragraph 51A(4) on a roll-over basis.

The third bullet point requires that 90% or more of the market value of the assets in the company must comprise an interest in a residence. This requirement applies throughout the period from 11 February 2009 until the date of disposal. The date of acquisition of the shares is not relevant when applying this 90% test. The 90% test is based on the market value of the assets, not on the company's net assets (that is, assets less liabilities).

Upon the above requirements being met the acquirer must –

- disregard the disposal of all shares held by that person in that company for purposes of determining his or her taxable income, assessed loss, aggregate capital gain or aggregate capital loss if that disposal is made in anticipation of or in the course of the liquidation, winding up or deregistration of that company; and
- be deemed to have acquired that interest at a cost equal to the base cost of the shares contemplated in the above bullet point as at the date of the acquisition by the person of those shares plus the cost of any improvements effected in respect of that interest subsequent to that date of acquisition.

Under the first bullet point above the acquirer disregards any capital gain or loss on disposal of the shares. The disposal must occur in anticipation of the deregistration or liquidation of the company or during the course of its winding up. Thus it covers a part-disposal of the shares that occurs before 1 April 2012 as a result of the receipt or accrual of a capital distribution under paragraph 76A and a full disposal of the shares under paragraph 77 (that is, on dissolution, deregistration or when a liquidator issues a certificate indicating that no reasonable grounds exist to believe that further distributions will occur).

Under the second bullet point above the acquirer is deemed to acquire the residence for an amount equal to the “base cost” of the shares on the date of their acquisition plus the cost of any improvements effected to the residence after the shares were acquired. The “base cost” of the shares in this context is the expenditure incurred under paragraph 20 in acquiring the shares. It is clearly not a base cost under paragraph 25 (valuation date value plus post-valuation date expenditure) since it must be determined at the date of acquisition of the shares. The implications of this provision in the context of shares acquired before 1 October 2001 are the following:

- The residence will also be a pre-valuation date asset since it takes its date of acquisition from the shares.
- It is therefore necessary to consider which methods may be used to determine the valuation date value of the residence.
- An acquirer of the residence will not be able to use any market value of the shares determined on 1 October 2001 for determining the valuation date value of the residence because no provision is made for the market value of the shares to be carried across to the residence.
- An acquirer of the residence will be able to use the “time-apportionment base cost” method or the “20% of proceeds” method in determining the base cost of the residence only when it is ultimately disposed of.
- Presumably any improvements made by the company after the acquisition of the shares must be treated as being made by the acquirer on the same date that those improvements were effected, though the provision is silent on this point. This is an important issue because the timing of the improvements can have a significant impact in determining the base cost of the residence. For example, “N” in the time-apportionment formula is limited to 20 when improvements occur in more than one year of assessment before the valuation date, while post-valuation date improvements trigger the proceeds formula in paragraph 30(2) and result in a greater proportion of the overall gain or loss forming part of the capital gain or capital loss.

The “20% of proceeds” method is applied by first deducting the post-valuation date improvements from the proceeds before multiplying the result by 20%.

The rule may not yield a satisfactory outcome in all cases. For example, if less than 90% of the market value of the company’s assets at the time of acquisition of the shares comprised a residence, the acquirer’s base cost would be unduly inflated. Conversely the rule ignores the fact that the shareholder’s interest may comprise shares and a substantial loan account. No account is taken of the loan account in determining the acquisition cost of the residence.

Example 10 – Shares acquired in company already owning a residence

Facts:

Husband and wife formed a company in 1995. The company purchased a house in the following year for R360 000. In 2004 the couple sold their shares in the company to an unrelated individual for R650 000. In 2011 the individual liquidated the company and transferred the house into the individual’s own name. In 2011 the house was worth R920 000. Improvements costing R25 000 were made to the house before the 2004 sale, and another R30 000 of improvements were made afterwards.

Result:

The transfer of the house during the liquidation process does not give rise to any CGT, transfer duty or STC in individual’s hands as the transaction is assumed to have met all the requirements of paragraph 51A(1). The individual’s base cost in the house is R680 000 (the purchase price of the shares in 2004 of R650 000 plus the R30 000 improvements undertaken after the acquisition).

9.5 Base cost of residence acquired from a company – residence acquired by company after the acquisition of its shares [paragraph 51A(4)]

Paragraph 51A(4) applies to the acquisition of a residence by a person from a company under circumstances other than those set out in paragraph 51A(3). This covers, for example, cases in which –

- the shareholders acquired their shares before the company acquired the residence;
- some of the shareholders acquired their shares before the company acquired the residence and others acquired them afterwards;
- the 90% test (see **9.4**) is not met; or
- the acquirer is not a shareholder but is still a connected person in relation to the company.

When paragraph 51A(4) applies –

- the acquirer of the residence must disregard the disposal of any share in that company for purposes of determining his or her taxable income, assessed loss, aggregate capital gain or aggregate capital loss if that disposal is made in anticipation of or in the course of the liquidation, winding up or deregistration of that company; and

- the acquirer and that company must be deemed to be one and the same person with respect to –
    - the date of acquisition of that interest by that company;
    - the amount and date of incurral by that company of any expenditure in respect of that interest allowable in terms of paragraph 20; and
    - any valuation of that interest effected by that company as contemplated in paragraph 29(4).

Unlike paragraph 51A(3), paragraph 51A(4) operates on a roll-over basis and the cost of the shares in the company is not taken into account for purposes of determining the acquirer's base cost. The acquirer "steps into the shoes" of the company for the purpose of applying the time-based apportionment, market value and "20% of proceeds" methods for determining the valuation date value of the residence and any post-valuation date costs.

Example 11 – Residence acquired by company after current shareholders acquire its shares

Facts:

Alan and Betty are spouses married in community of property. In 1995 they formed a company which purchased a house in the following year for R360 000. The company financed the acquisition of the residence using a mortgage bond secured over the property. The couple provided the bank with a guarantee and undertook to pay off the bond plus interest in exchange for a loan account with the company. The couple have stayed in the house with their children from the date that the company acquired the residence until the present time. By 2011, the company owed R200 000 to the bank and R420 000 to the couple. The house is worth R920 000. Improvements costing R50 000 were made to the house on 30 June 2005. On 1 March 2011 the company was placed into voluntary liquidation. The couple settled the outstanding bond and waived the amount owing to them on loan account. The house was distributed as a dividend *in specie* shortly afterwards to the couple and is registered in their names jointly.

Result:

The liquidation does not give rise to any CGT, transfer duty or STC. The initial R360 000 cost of the house (plus the R50 000 of improvements) is deemed to be incurred by the couple as if the couple incurred those costs directly (with the same 2001 CGT transition rules applying). The waiver of the shareholders' loans does not give rise to a capital gain in the company because of the exclusion contained in paragraph 12(5)(*a*)(*cc*). The couple must disregard the capital loss on waiver of their loan accounts under paragraph 56(1).

9.6 Base cost of residence acquired from a trust [paragraph 51A(5)]

Paragraph 51A(5) applies when a person acquires a residence from a trust. It does not identify who may be an acquirer of the residence – see **9.8**, but does confirm that the disposal must comply with paragraph 51A(1). Thus, for example, the disposal must take place on or before 31 December 2012.

When paragraph 51A(5) applies, the acquirer and the trust must for purposes of determining any capital gain or capital loss in respect of the disposal by that person of that interest so acquired be deemed to be one and the same person with respect to –

- the date of acquisition of that interest by that trust;
- the amount and date of incurral by that trust of any expenditure in respect of that interest allowable under paragraph 20; and
- any valuation of that interest effected by that trust as contemplated in paragraph 29(4).

Example 12 – Residence acquired from trust

Facts:

Founder formed a discretionary trust in 1995 for the benefit of Husband and Wife and their children. In the same year, the couple lent the trust R60 000 on loan account. Also in the same year, the trust obtained a mortgage bond from the bank of R300 000 and purchased a house for R360 000 using the funds from the bank and the couple. The couple guaranteed payment of the bond. The couple have resided in the house with their children from the date on which the trust acquired the residence until the present time. The interest on bond, rates and other expenses have been paid by the couple. By 1 March 2011, the bond was paid up and the house was worth R920 000. Improvements costing R50 000 were made to the house in 2004. On 31 August 2004, one month before the cut-off date of 30 September 2004 under paragraph 29(4), the trustees obtained a market valuation of the residence as at 1 October 2001 for CGT purposes.

On 31 March 2011 the house was sold to the couple for R920 000 and registered in their names jointly. In the process the couple's loan accounts totalling R410 000 (R60 000 + R300 000 + R50 000) were discharged. The balance of the purchase price of R510 000 (R920 000 – R410 000) was paid by the couple in cash.

The capital profit of R920 000 – R410 000 = R510 000 was vested by the trustee in the couple and their children in equal shares.

On 20 July 2011 the trustees took steps to terminate the trust.

Result:

The sale of the residence does not give rise to any CGT or transfer duty. The transaction meets the requirements of paragraph 51A and under paragraph 51A(2) the trust is deemed to have disposed of the residence at base cost so no capital gain arises in the trust. The distribution of the capital profit of R510 000 to the couple and their children accordingly does not represent the vesting of a capital gain under paragraph 11(1)(*d*) and there is therefore no capital gain to be attributed to the beneficiaries under paragraph 80(2). Since the loan accounts were discharged for full consideration there are no CGT implications under paragraph 12(5).

The initial cost of the house (R360 000) and the cost of improvements of R50 000 are deemed to be incurred by the couple under paragraph 51A(5)(*b*) as if they incurred those costs directly. Each spouse is therefore deemed to incur expenditure of R360 000/2 = R180 000 in 1995 and R50 000/2 = R25 000 in 2004. The actual consideration paid by the couple for the residence of R920 000 is disregarded for base cost purposes. The residence will be a pre-valuation date asset in the couple's hands, and they will have a choice of the time-based apportionment, market value and "20% of proceeds" methods available to them for the purpose of determining the valuation date value of the residence when they ultimately dispose of it.

9.7 Multi-tier structures [paragraph 51A(6)]

A residence may not be disposed of to a company or trust unless –

- within a period of six months commencing on the date of disposal of the residence –
  - in the case of a company, it has taken steps to liquidate, wind up or deregister as contemplated in section 41(4); or
  - in the case of a trust steps have been taken to terminate it

  [paragraph 51A(6)(*a*)]; and
- one or more natural persons contemplated in paragraph 51A(1)(*b*) acquire the residence contemplated in paragraph 51A(1) on or before 31 December 2012 [paragraph 51A(6)(*b*)].

Paragraph 51A(6) was introduced mainly to deal with the case in which a trust holds shares in a company which in turn holds a residence. But it also deals with a holding company which holds shares in a subsidiary which in turn owns a residence. There is no limit on how many companies or trusts can be in the chain, but all the companies or trusts in the chain will have to dispose of the residence on or before 31 December 2012 and take the steps discussed in **9.2.5** within six months of their respective disposals of the residence.

The CGT, dividends tax, STC and transfer duty relief does not extend to any other assets that may be held by the companies or trusts in the chain.

Paragraph 51A(6)(*b*) identifies the ultimate acquirers of the residence as the natural persons referred to in paragraph 51A(1)(*b*), namely, natural persons who –

- used the residence mainly for domestic purposes from 11 February 2009 until the date of acquisition by them of the residence; and
- are connected persons in relation to the company or trust at the time of disposal.

Example 13 – Multi-tier structure

Facts:

Angus and Brenda, a married couple, are contingent beneficiaries of the ABC Discretionary Trust. The trust holds all the shares in Propco (Pty) Ltd. In 1998 the company purchased a house in which the couple have resided ever since as their main residence. On 30 November 2010 the company distributed the house to the trust as a dividend in anticipation of its deregistration. By 31 March 2011 the company was deregistered.

On 1 April 2011 the trust distributed the house to the couple. On 12 April 2011 the trustees of the trust took steps to terminate the trust.

Result:

The disposal of the house from the company to the trust qualifies for the relief under paragraph 51A(2), (6)(*a*)(i) and (*b*). The distribution of the house from the trust to the couple also qualifies for the relief under paragraph 51A(2), (6)(*a*)(ii) and (*b*).

Sale by company directly to beneficiary of trust

In order to avoid terminating the trust in a multi-tier structure it has been contended that it is possible for the company to sell the residence directly to a beneficiary of the trust. In this way it is argued that only the company need be deregistered or liquidated because it is the only entity in the chain that has disposed of a residence. At issue is whether paragraph 51A(3) and (4) require that an acquirer of a residence from a company be a shareholder of that company. This is certainly the case with paragraph 51A(3) but the wording of paragraph 51A(4) does not appear to explicitly require that the acquirer be a shareholder. It applies –

- to the acquisition of a residence by a person as a result of a disposal by a company under paragraph 51A (note the use of the term "person" as opposed to "shareholder"); and
- when paragraph 51A(3) does not apply.

Paragraph 51A(4)(*a*) requires that the acquirer must disregard the disposal of "any share" in the company upon its termination but does not specifically require that the person must actually hold shares. Arguably this could be inferred. In view of the limited application of paragraph 51A and the fact that one of its purposes is to reduce the number of companies on register, SARS will accept that paragraph 51A(4) does not require a person acquiring a residence from a company to be a shareholder. Taxpayers who follow this route need to be mindful of the potential adverse donations tax (see **10**) and STC (see **7**) or dividends tax (see **8**) consequences.

9.8 Who qualifies as an ultimate acquirer?

A company or trust can be a temporary acquirer if it complies with paragraph 51A(6)(*a) – see **9.7***. An ultimate acquirer must, however, meet the requirements of paragraph 51A(6)(*b*).

Under paragraph 51A(6)(*b*), paragraph 51A will not apply unless one or more natural persons contemplated in paragraph 51A(1)(*b*) ultimately acquires the residence contemplated in that subparagraph on or before 31 December 2012. It is therefore clear that the ultimate qualifying acquirers of the residence must be –

- one or more natural persons who used the residence mainly for domestic purposes from 11 February 2009 until the date of disposal by the company or trust, and
- are connected persons in relation to the company or trust at the time of that disposal.

In the case of paragraph 51A(3) the acquirer must also be a shareholder. The implication is that a disposal of a residence to a person who is not a shareholder will not qualify for the relief under paragraph 51A(3) and consideration will have to be given whether the disposal by the company would qualify under paragraph 51A(4). While the natural person need not be a shareholder under paragraph 51A(4), he or she must still be a connected person in relation to the company and must have used the residence mainly for domestic purposes during the period from 11 February 2009 to date of disposal [paragraph 51A(1)(*b*)].

A deceased estate cannot be an acquirer because it is not a natural person. If a natural person acquires a residence from a company or trust under an unconditional agreement on or after 1 October 2010 but dies before the residence can be registered in his or her name, the relief will still apply since the residence was disposed of to a natural person at the time of disposal determined under paragraph 13.

An individual who inherits shares after 11 February 2009 in a company holding a residence can acquire that residence under paragraph 51A provided that individual is a connected person in relation to the company at the time of the disposal and used that residence mainly for domestic purposes from 11 February 2009 until the date of disposal.

Example 14 – Qualifying and non-qualifying persons

Facts:

A mother and son each hold a 50% member's interest in a close corporation which in turn owns a residence. The close corporation acquired the residence after the mother and her son had acquired their interests upon formation of the corporation. Only the son resided in the residence during the period 11 February 2009 until the date of disposal. The mother disposed of her member's interest to her son on 15 December 2010.

Result:

The mother will be subject to CGT on the disposal of her member's interest to her son. Under paragraph 38 the disposal must take place at market value since the mother and her son are connected persons in relation to each other. The son must pay transfer duty on the acquisition of the 50% member's interest from his mother. The duty is calculated on 50% of the fair market value of the full property. No account is taken of liabilities in the close corporation in determining the duty payable.

Once the son holds the 100% interest in the close corporation the residence can be distributed to him before 1 January 2013 free of CGT, dividends tax or STC and transfer duty. The son's base cost will then be determined on a roll-over basis under paragraph 51A(4) despite him having paid a market value consideration for the 50% interest he acquired from his mother. This can result in economic double taxation. Nevertheless, the son should at least be entitled to the primary residence exclusion in future.

Example 15 – Disposal by close corporation to relative of member

Facts:

A father holds 100% of the member's interest in XYZ CC (XYZ), which owns a residence. The father and his son have resided in the residence from 1 July 2002 to date. The close corporation's balance sheet appears as follows:

	R
Member's interest	100
Member's loan	100 000
	100 100

Residence – at cost (1 July 2002)	100 100

The father initially lent XYZ cash of R100 000 which it used to acquire the residence from a third party on 1 July 2002.

The residence has a current market value of R1 million.

The father waived his loan account and approved the sale of the residence to his son for R100 on 15 March 2012. The R100 is returned to the father as repayment of his member's interest and the close corporation is deregistered.

Result:

The son is a qualifying acquirer because –

- he has used the residence mainly for domestic purposes from 11 February 2009 to date, and
- being a relative of his father, is a connected person in relation to XYZ (paragraph (*d*)(vi)(*bb*) of the definition of "connected person" in section 1(1)).

The son is exempt from transfer duty under section 9(20) of the Transfer Duty Act.

Under paragraph 38 of the Eighth Schedule XYZ is deemed to dispose of the residence at market value. However, XYZ must disregard the capital gain of R1 000 000 – R100 100 = R899 900 on disposal of the residence under paragraph 51A(2).

The son is deemed to acquire the residence at a deemed cost of R100 100 on 1 July 2002 under paragraph 51A(4).

XYZ has declared a deemed dividend of R999 900 under section 64C(2)(*a*) because it has transferred an asset for the benefit of a connected person in relation to a member. This deemed dividend is exempt from STC under section 64B(5)(*k*A) because it comprises the disposal of an interest in a residence under paragraph 51A.

The waiver of the father's loan to XYZ gives rise to a capital gain in XYZ but this must be disregarded under paragraph 12(5)(*a*)(*cc*). The father must disregard the capital loss on waiver of the loan under paragraph 56(1).

XYZ has made a donation of R999 900 to the son at the instance of the father. The father is deemed to be the donor under section 57(1) and must therefore pay donations tax on R999 900 – R100 000 = R899 900 × 20% = R179 980. It is assumed that the father has not made any other donations during the year of assessment and that the full amount of the annual exemption of R100 000 under section 56(2)(*b*) is available to him.

9.9 Waiver of loan accounts [paragraph 12(5)]

A company making a disposal under paragraph 51A(1) will often have a liability in the form of a shareholder's loan account or mortgage bond.

Before such a company can be liquidated or deregistered it is necessary for its liabilities to be discharged. The waiver of a loan account for no consideration or for a consideration that is less than the face value of the loan account will normally give rise to a capital gain in the company under paragraph 12(5). Paragraph 12(5)(*a*)(*cc*) does, however, not apply to the waiver of a loan owed by a company provided that –

- the creditor is a connected person in relation to the company; and
- the loan is waived in the course or in anticipation of the liquidation, winding up, deregistration or final termination of the corporate existence of the company.

This exclusion from paragraph 12(5) applies only to the extent that the amount of the reduction or discharge did not exceed the amount of the creditor's expenditure contemplated in paragraph 20 of the debt at the time of that reduction or discharge. For example, if the creditor acquired a loan with a face value of R100 by cession from another creditor for R80, only R80 of the waiver of the loan will be excluded as a capital gain (assuming R100 is outstanding at the time of waiver).

The exclusion does not apply if –

- the company became a connected person in relation to the creditor after the debt or any replacement debt arose, and
- the transactions are part of a scheme to avoid any tax otherwise imposed by virtue of the Act.

Both the requirements of the last two bullet points must be met before the exclusion under paragraph 12(5)(*a*)(*cc*) is invalidated.

The creditor will forfeit any capital loss under paragraph 56(1) when this exclusion from paragraph 12(5) applies.

There is no specific CGT exclusion for loans waived in anticipation of the termination of a trust.

The waiver of a loan account can result in the reduction in the base cost of the residence under paragraph 20(3)(*b*) rather than in a capital gain under paragraph 12(5) under certain circumstances because paragraph 20(3) takes precedence over paragraph 12(5).[31] This could apply, for example, when the person from whom the residence was acquired waives the loan used to purchase the residence.[32]

In many cases it will be possible for a company to repay a shareholder's loan account by disposing of the residence to the shareholder and setting off the purchase price against the loan account (see Example 1). This will avoid the problems associated with the waiver of loan accounts described above.

10. Donations tax

The donations tax legislation is contained in sections 54 to 64 (Part V) of the Act.

No specific exemption from donations tax was introduced to deal with a donation which may arise in consequence of the disposal of a residence under paragraph 51A. Nevertheless, depending on the circumstances, the existing donations tax exemptions may apply.

31 Under paragraph 12(5)(*a*)(*aa*)(B) the provisions of paragraph 12(5) do not apply when the amount of the reduction or discharge has been taken into account under paragraph 20(3).

32 *Comprehensive Guide to CGT (Issue 4)* in paragraph 8.18.

Some donations tax consequences of the disposal of a residence under paragraph 51A are discussed below.

Exemption of distribution of a residence to a beneficiary

Under section 56(1)(*l*) donations tax is not payable on the value of any property which is disposed of under a donation –

> "if such property is disposed of under and in pursuance of any trust".

It is submitted that the above words mean that the donation by the trustees to a beneficiary will not be subject to donations tax if it is authorised by the trust deed. In *Abraham Krok Trust v C: SARS*[33] the court assumed in favour of SARS that this was the case but then found that the relevant donations were indeed in accordance with the trust deed and thus exempt from donations tax. While the court's assumption does not represent an interpretation of the words in question, the assumption is considered well founded given the wording of section 56(1)(*l*) which does not merely refer to a disposal by a trust but one under and in pursuance of any trust. The fact that such a donation is not authorised by the trust deed would not prevent it from being subjected to donations tax.[34]

Exemptions that may apply when a company disposes of a residence

A company that disposes of a residence to a qualifying acquirer (see **9.8**) for no consideration or for a consideration which is less than the market value of the residence will be making a donation for donations tax purposes under section 58 because the consideration would not be an "adequate consideration". Nevertheless, section 57(1) may deem the donor to be a person other than the company.

Under section 57(1) when –

- a company disposes of a residence at the instance of any person; and
- that disposal would have been treated as a donation had it been made by that person,

that residence is deemed to be disposed of under a donation by that person.

Typically the deemed donor will be a shareholder of the company. Such a shareholder will be exempt from donations tax if that shareholder is –

- not a resident (section 54 provides that donations tax applies only to a resident donor);
- the spouse of the person who acquired the residence (section 56(1)(*b*) exempts donations between spouses);
- a member of the same group of companies [section 56(1)(*r*)]; or
- a trust if the donation was authorised by the trust deed as discussed under the previous subheading [section 56(1)(*l*)].

In the multi-tier structure involving a trust holding the shares in a residential property company the conventional way of dealing with the matter would be for the company to

33 (2010) 73 SATC 105 (SCA) in [20].

34 In the *Abraham Krok* case above at [18] the court expressed the *obiter* view that the legislature did not intend section 54 to apply only to authorised donations.

distribute the residence to the trust which would in turn distribute it to the beneficiary (see **9.7**). This method does not usually carry any donations tax consequences because the distribution of a dividend under company law would not comprise a donation as it is not made gratuitously but under the terms of the company's memorandum of incorporation. Likewise, the distribution of the residence to the beneficiary should be exempt from donations tax under section 56(1)(*l*). In this scenario both the company and the trust must be terminated [paragraph 51A(1)(*d*) and (6)(*a*)].

The termination of a trust that holds other assets (see **5**) may carry adverse estate duty and CGT consequences for the trust and its beneficiaries in relation to those other assets. It is for this reason that the trustees may arrange for the company to dispose of the residence directly to the beneficiary at cost to the company.[35] The sale at below market value triggers a dividend as defined in section 1(1) but it is exempt from dividends tax under section 64FA(1)(*c*) – see **8**. The below market value sale by the company will result in a donation by the company to the beneficiary but the trust shareholder will be deemed to be the donor for donations tax purposes under section 57(1). In order to determine whether this deemed donation is exempt from donations tax under section 56(1)(*l*) it is necessary to make the following hypothetical enquiry: If the trust had owned the residence and donated it to the beneficiary, would the donation have been exempt from donations tax? If the answer is "yes" then the deemed disposal will be exempt from donations tax, and if "no" then donations tax will be payable. As noted above the determination whether donations tax is payable will depend on whether the hypothetical donation of the residence would have been authorised under the trust deed.

Example 16 – Disposal of residence by company to trust beneficiary

Facts:

The ABC Family Trust holds all the shares in a company which holds a residence which has been used by the trust's beneficiary mainly for domestic purposes from 11 February 2009 to the date of disposal of the residence by the company. The company disposes of the residence to the beneficiary at cost price of R200 000. The current market value of the residence is R1 million. Under the trust deed the trustees are authorised at their discretion to vest the capital of the trust in the beneficiary.

[35] The sale at cost price prevents a capital profit from arising in the company which would not qualify for the STC or dividends tax exemption upon its distribution. Such a distribution is not a dividend *in specie* and thus falls outside section 64B(5)(*k*A) and 64FA(1)(*c*).

Result:

Under paragraph 51A(1)(*b*) the beneficiary is a qualifying acquirer, being a connected person in relation to the company[36] and having used the residence mainly for domestic purposes from 11 February 2009 to date of disposal of the residence. The company will accordingly qualify for the relief from CGT under paragraph 51A. The beneficiary will also be exempt from transfer duty under section 9(20) of the Transfer Duty Act. The disposal of the residence at less than market value constitutes a dividend *in specie* of R800 000 (R1 000 000 – R200 000) since this represents a distribution on behalf of the company's shareholder.[37] This dividend is exempt from dividends tax under section 64FA(1)(*c*).

The trust deed authorises the trustees to dispose of the trust capital to the beneficiary. Thus, had the trust in reality disposed of the residence to the beneficiary the donation would have been "under and in pursuance of" the trust. The deemed donation of the residence to the beneficiary by the trust is accordingly exempt from donations tax under section 56(1)(*l*).

Waiver of shareholders' loan accounts

Before a company can be liquidated or deregistered it will be necessary for any shareholders' loans to be discharged. One way of doing this would be to capitalise the loans by issuing further shares at a premium. In such event there should be no donations tax consequences provided the shares are equal in value to the loan account discharged.

Alternatively, the shareholder could waive the loan for no consideration, and in this case the issue arises whether any donations tax is payable. The effect of a shareholder waiving a loan account should be to increase the value of that shareholder's shares. If the value of a shareholder's shares increases by an amount equal to the loan discharged by that shareholder, it will be accepted that the consideration given for the loan is adequate for the purposes of section 58 on the basis that the value of the shareholder's estate remains unchanged. This interpretation would not apply, for example, if there is more than one shareholder and the shareholders' loans are disproportional to their respective shareholdings.

Waiver of loans to trusts

The waiver of a loan by a founder to a trust will have donations tax implications for the founder.

A sale of the residence to the founder at market value with the purchase price being settled wholly or partly by set-off against the loan account will prevent a donation from arising and consequently no donations tax will become payable. In addition, no capital gain will arise on such a disposal under paragraph 51A(2) – see **9.3**. The proceeds from the disposal can then be distributed to the trust beneficiaries without any CGT implications under paragraph 80(2), since there is no capital gain to be attributed to them.

[36] The beneficiary is a connected person in relation to the company under paragraph (*b*A) of the definition of "connected person in section 1(1) because the beneficiary is connected to the trust [paragraph (*b*)(i)] and the trust is connected to the company [paragraph (*d*)(iv)].

[37] Definition of "dividend" in section 1(1).

Differential dividends

While it may have been possible for a company to legally distribute a dividend to a single shareholder as opposed to all shareholders within a particular class under the Companies Act 61 of 1973,[38] such an action in the context of paragraph 51A may well have resulted in donations tax becoming payable. For example, assume that A and B own 99% and 1% respectively of the shares in Company A, which owns a residence. The company distributes the residence to B at the instance of A. Generally in these circumstances it is clear that what has been dressed up as a dividend is in fact a donation by the company at the instance of A. In these circumstances A may be deemed to be the donor under section 57(1) and will be liable for donations tax. A's consent in this case would be required because the company will be disposing of the "whole or the greater part" of its assets and this would have required a special resolution under section 228 of the Companies Act, 1973.[39]

Under section 37(1) of the Companies Act 71 of 2008

> "[a]ll of the shares of any particular class authorised by a company have preferences, rights, limitations and other terms that are identical to those of other shares of the same class".

It is therefore not possible to declare a dividend to one shareholder to the exclusion of others in the same class under the Companies Act, 2008.

11. Value-Added tax

The Value-Added Tax Act 89 of 1991 contains no specific value-added tax relief measures relating to the disposal of a residence referred to in paragraph 51A. This is because the basis of the relief is that the residence held by a company or trust is used mainly for domestic purposes and not for the purposes of carrying on an enterprise. In these circumstances, the entity that owns the residence would not have been entitled to deduct input tax on the acquisition of the property, even if it was registered for value-added tax purposes in respect of any other taxable activities conducted by the enterprise. More specifically, input tax should not have been deducted because the private use of a residence ("dwelling") is not an "enterprise" activity and neither is the letting of a dwelling to another person.[40]

If input tax was erroneously deducted on a residence, the value-added tax position must be corrected by reversing the input tax in the tax period in which it was originally deducted. The amount incorrectly deducted would also have to be refunded to SARS together with penalties and interest. Alternatively, if the residence was used for taxable purposes in an enterprise and was subjected to a change in use from taxable to non-taxable (residential) purposes within the timeframes envisaged in paragraph 51A and before being transferred to a qualifying acquirer, the vendor would be required to make an output tax adjustment under

[38] P M Meskin, B Galgut, J A Kunst, P Delport and Q Vorster *Henochsberg on the Companies Act* [CD-ROM] (*My LexisNexis*: September 2009) LexisNexis Butterworths Durban in the commentary on section 90 of the Companies Act, 1973. According to the authors of this work such a discriminatory dividend is possible provided that it is sanctioned by the company's articles of association.

[39] The equivalent provision under the Companies Act 71 of 2008 is section 112 read with section 115, which also requires a special resolution.

[40] Section 12(*c*)(i) of the Value-Added Tax Act 89 of 1991. Under paragraph (v) of the proviso to the definition of "enterprise" in section 1(1) of the Value-Added Tax Act, any activity which involves the making of exempt supplies is not deemed to be the carrying on of an enterprise.

section 18(1) of the Value-Added Tax Act. The adjustment is based on the open market value of the residence and must be made in the tax period in which the change in use occurred, otherwise penalties and interest will be payable. As a practical matter, any incorrect value-added tax treatment will have to be rectified before any transfer duty exemption under section 9(20) of the Transfer Duty Act can be finalised.

12. Must the residence be disposed of at market value?

Paragraph 51A does not require that the residence be disposed of at market value. Although there are many rules in the Act which deem transactions to take place at market value, most of these are likely to be irrelevant because of the relief provided by paragraph 51A and related provisions.

It is, however, advisable to conduct transactions at market value in order to avoid unintended tax consequences such as the imposition of donations tax and to ensure that the correct tax is payable under provisions such as paragraph 12(5), section 8(4)(*k*) and section 22(8). Companies need to comply with generally accepted accounting practice. Under IFRIC 17 "Distributions of Non-cash Assets to Owners" an entity should measure a dividend *in specie* payable at the fair value of the net assets to be distributed. The interpretation is effective for annual periods beginning on or after 1 July 2009.

The STC and dividends tax exemptions in section 64B(5)(*k*A) and 64FA(1)(*c*) respectively apply only to the distribution of a residence and do not extend to the distribution of other assets. A sale of a residence by a company to a non-shareholder at cost price prevents any residual profit from arising which would not be covered by these exemptions.