

INTERPRETATION NOTE: NO. 25 (Issue 3)

DATE: 12 March 2014

ACT : INCOME TAX ACT NO. 58 OF 1962
SECTION : SECTION 1(1)
SUBJECT : RESIDENT: DEFINITION IN RELATION TO A NATURAL PERSON – APPLICATION OF THE PHYSICAL PRESENCE TEST IN THE YEAR OF DEATH OR INSOLVENCY

Preamble

In this Note unless the context indicates otherwise –

- “**person**” means a natural person;
- “**section**” means a section of the Act;
- “**the Act**” means the Income Tax Act No. 58 of 1962; and
- any word or expression bears the meaning ascribed to it in the Act.

1. Purpose

This Note explains the application of the physical presence test in the year of assessment that a natural person, who is not ordinarily resident on the Republic, dies or becomes insolvent. The implications of a double taxation agreement have not been taken into account in this Note.

Issue 2 of this Note, dated 8 February 2006, is hereby replaced.

2. Background

Persons who are residents of the Republic of South Africa are subject to tax on their worldwide taxable income. A person is a “resident” as defined in section 1(1) if that person is –

- **ordinarily resident** in the Republic; or
- **physically present** in the Republic for a specified number of days during the relevant (current) year of assessment as well as during each of the five years of assessment immediately preceding the current year of assessment (the **physical presence test**).

This Note must also be read in conjunction with Interpretation Note No. 4 (Issue 4) dated 12 March 2014 “Resident: Definition in Relation to a Natural Person – Physical Presence Test” as well as Interpretation Note No. 8 (Issue 3) dated 28 August 2013 “Insolvent Estates of Natural Persons”.

3. The law

For ease of reference the relevant sections of the Act are quoted in the **Annexure**.

4. Income tax implications

4.1 The physical presence test

There are three requirements that must be met when applying the physical presence test before a natural person is regarded as a resident in the Republic for tax purposes under paragraph (a)(ii) of the definition of a “resident” in section 1(1). The three requirements are that the person must have been physically present in the Republic for –

- (i) more than 91 days in total during the current year of assessment;
- (ii) more than 91 days in total in each of the five years of assessment immediately preceding the current year of assessment; and
- (iii) more than 915 days in total during those five immediately preceding years of assessment.

All three of these requirements must be satisfied, or the person will not be a resident for the current year of assessment. Refer to Interpretation Note No. 4 (Issue 4) for a detailed discussion on the application of the physical presence test.

A person who dies or becomes insolvent will generally have a year of assessment of less than 12 months in the year of death or insolvency.

4.2 The year of assessment in which a person dies

Proviso (a) to section 66(13)(a), read with the definition of a “year of assessment” in section 1(1), provides that the year of assessment for a person who has died –

- commences on the first day of the year of assessment (usually 1 March unless the person was born during the year); and
- ends on the date of death.

The “more than 91 days” requirement in the physical presence test for the year of assessment during which a person dies, is applied in the normal way, and is not scaled down to account for the year of assessment being less than 365 or 366 days. For example, a person who dies on 30 April and that person was physically present in the Republic as from 1 March, will not meet the “more than 91 days” requirement during the current year of assessment because that person would have been physically present in the Republic for only 61 days (1 March to 30 April).

Proviso (A) to the definition of a “resident” in section 1(1) provides that, when calculating the number of days for purposes of the physical presence test, a day includes a part of a day. A person would have been alive, and therefore physically present, in the Republic for part of the day on which that person dies, and the day of death therefore counts towards the number of days of physical presence in South Africa.

Example 1 – Death*Facts:*

Y, a resident of Utopia (with which South Africa does not have an agreement for the avoidance of double taxation) is not ordinarily resident in the Republic. Y was physically present in the Republic for the following periods during the 2014 year of assessment:

- a) 2 June 2013 to 19 June 2013.
- b) Y arrived at Cape Town International Airport at 23:40 on 10 November 2013.
- c) Y passed away at 20:00 on 21 January 2014.

During the five preceding years of assessment Y was physically present in the Republic for the following number of days:

Year of assessment	Number of days
2009	155
2010	188
2011	201
2012	181
2013	<u>191</u>
	<u>916</u>

Result:

Y's year of assessment for 2014 runs from 1 March 2013 to 21 January 2014. During that period Y was physically present in the Republic for 91 days in aggregate, determined as follows:

Period	Number of days
2 June 2013 to 19 June 2013	18
10 November 2013 to 21 January 2014	<u>73</u>
Number of in aggregate	<u>91</u>

Since Y does not comply with the first requirement of the physical presence test, namely, that Y must be physically present in the Republic for a period or periods exceeding 91 days in aggregate during the year of assessment (1 March 2013 to 21 January 2014), Y is not regarded as a resident for income tax purposes in the 2014 year of assessment.

Example 2 – Death*Facts:*

The facts are the same as in Example 1, except that Y died 6 hours later, at 02:00 on 22 January 2014.

Result:

Y's year of assessment would have been for the period 1 March 2013 to 22 January 2014.

Y would have been physically present in the Republic for a period or periods **exceeding** 91 days in aggregate during the period of assessment in question, that is:

Period	Number of days
2 June 2013 to 19 June 2013	18
10 November 2013 to 22 January 2014	<u>74</u>
Number of days in aggregate	<u>92</u>

Y would therefore have been regarded as a resident because Y would have been physically present in the Republic for –

- more than 91 days in total during the current year of assessment;
- more than 91 days in total in each of the five years of assessment immediately preceding the current year of assessment; and
- more than 915 days in total during those five immediately preceding years of assessment.

4.3 The year of assessment in which a person is declared insolvent

The periods of assessment, when the estate of a natural person is sequestered, is determined, in the case of –

- (a) the insolvent person, for the period from 1 March up to the day before the date of sequestration;
- (b) the insolvent person, (a new taxpayer for tax purposes¹) for the period from the date of sequestration to the last day of February; and
- (c) the insolvent estate² (a new person for tax purposes³), from the date of sequestration to the last day of February.⁴

The insolvent person will be assessed as a natural person for the period before insolvency, as well as for the period subsequent to insolvency, should any income accrue to that person in his or her personal capacity.

The physical presence test must be applied each year of assessment. A year of assessment includes a period of assessment.⁵ In the case of a sequestration where there are two periods of assessment, the physical presence test must be applied to each of these periods of assessment. The first period (in (a) above) will be regarded as an immediately preceding year of assessment in relation to the second period ((b) above).

¹ The insolvent persons before and after sequestration are separate taxpayers but the same natural person. See also *ITC 349 (1936)* [9 SATC 66] at 69.

² Defined in section 1(1) to mean an “insolvent estate” as defined in section 2 of the Insolvency Act No. 24 of 1936.

³ A “person” as defined in section 1(1) specifically includes an insolvent estate.

⁴ The income tax treatment of insolvent estates is discussed in paragraph 3 of Interpretation Note No. 8 (Issue 3), and will not be discussed in this Note.

⁵ The definition of a “year of assessment” in section 1(1) refers to any year “*or other period*”.

The first period of assessment (referred to in (a) above) ends the day before the date of sequestration. In the case of –

- (i) a voluntary surrender of an estate, this is the date that the debtor's application for acceptance of the surrender is lodged with the High Court, if the court accepts the surrender; and
- (ii) a "compulsory" sequestration, being an application for sequestration of a debtor by a creditor, this is the date of the provisional order of sequestration, if the provisional order of sequestration is made final by the court.

The second period of assessment (referred to in (b) above) commences on the date of sequestration and ends on the last day of that year of assessment, which is the last day of February.

Example 3 – Insolvency

Facts:

Z, a resident of Utopia (with which South Africa does not have an agreement for the avoidance of double taxation) is ordinarily resident in the Republic. Z was physically present in the Republic for the following periods:

- a) 12 April 2013 to 25 June 2013.
- b) 31 July 2013 to 16 September 2013.
- c) 15 December 2013 to 15 March 2014.

On 2 September 2013 the court issued a provisional order placing Z's estate in sequestration. This order was later made final. As a result of the provisional order of sequestration issued on 2 September 2013, Z will have two periods of assessment, namely:

- *First period of assessment – Period before insolvency*

The period of assessment commenced on 1 March 2013 and ended on 1 September 2013, the day before the order of sequestration was issued.

- *Second period of assessment – Period from insolvency*

The period of assessment commenced on 2 September 2013 (the day on which the provisional order of sequestration was issued) and ended on the last day of February 2014.

During the five preceding years of assessment, Z was physically present in the Republic for the following number of days:

Year of assessment	Number of days
2009	110
2010	335
2011	185
2012	181
2013	<u>117</u>
	<u>928</u>

*Result:**Period of assessment before insolvency (1 March 2013 – 1 September 2013)*

Z was physically present in the Republic during the first period of assessment (1 March 2013 to 1 September 2013), as follows:

Period	Number of days
12 April 2013 to 25 June 2013	75
31 July 2013 to 1 September 2013	<u>31</u>
Number of days in aggregate	<u>106</u>

Z was resident in the Republic during the first period assessment because of the physical presence in the Republic for –

- more than 91 days in total during the current year (or period) of assessment;
- more than 91 days in total in each of the five years of assessment immediately preceding the current year of assessment; and
- more than 915 days in total during those five immediately preceding years of assessment.

Period of assessment from insolvency (2 September 2013 – 28 February 2014)

Z was physically present in the Republic during the second period of assessment (2 September 2013 – 28 February 2014), as follows:

Period	Number of days
2 September 2013 to 16 September 2013	15
15 December 2013 to 28 February 2014	<u>76</u>
Number of days in aggregate	<u>91</u>

Z does not meet the first requirement of the physical presence test during the second period (from insolvency) because Z is not physically present for a period exceeding 91 days in aggregate during that period of assessment.

The second period is treated as a new year of assessment, and the “current year of assessment” for purposes of the physical presence test. The 106 days that Z was present in South Africa during the first period of assessment is considered as one of the five previous years of assessment for purposes of the second and third requirements of the physical presence test.

Separate tax returns are required to be submitted for both periods of assessment when a person is declared insolvent.⁶

⁶ Proviso (b) to section 66(13)(a) read with section 25 of the Tax Administration Act No. 28 of 2011.

The effect of the setting aside of an order of sequestration is to terminate the existence of the insolvent estate *ab initio*. The setting aside of the order of sequestration will mean that the first requirement of the physical presence test, namely, more than 91 days in the current year of assessment, will be determined in relation to the full year of assessment, that is, from the first day of March to the last day of February the following year.

5. Conclusion

In the event of death or sequestration, the first requirement of the physical presence test (namely, physical presence exceeding 91 days in total for the current year of assessment) is applied in the normal way, notwithstanding that the year of assessment is for a period covering less than a full calendar year. The first requirement is therefore not scaled down to account for the fact that the “year of assessment” is less than a full year.

An insolvent person will be assessed as a natural person for the period before insolvency, as well as for the period subsequent to insolvency, should any income accrue to that person in his or her personal capacity. The physical presence test must be applied to each of these two periods of assessment. The first period will be regarded as an immediately preceding year of assessment in relation to the second period.

Legal and Policy Division
SOUTH AFRICAN REVENUE SERVICE
Date of first issue: 26 March 2004
Date of second issue: 8 February 2006

Annexure – The law

Section 1(1) Definition of the term “date of sequestration”

“date of sequestration” means—

- (a) the date of voluntary surrender of an estate, if accepted by the Court; or
- (b) the date of provisional sequestration of an estate, if a final order of sequestration is granted by the Court;

Section 1(1) Definition of the term “resident”

“resident” means any—

- (a) natural person who is—
 - (i) ordinarily resident in the Republic; or
 - (ii) not at any time during the relevant year of assessment ordinarily resident in the Republic, if that person was physically present in the Republic—
 - (aa) for a period or periods exceeding 91 days in aggregate during the relevant year of assessment, as well as for a period or periods exceeding 91 days in aggregate during each of the five years of assessment preceding such year of assessment; and
 - (bb) for a period or periods exceeding 915 days in aggregate during those five preceding years of assessment,
 in which case that person will be a resident with effect from the first day of that relevant year of assessment: Provided that—
 - (A) a day shall include a part of a day, but shall not include any day that a person is in transit through the Republic between two places outside the Republic and that person does not formally enter the Republic through a “port of entry” as contemplated in section 9(1) of the Immigration Act, 2002 (Act No. 13 of 2002), or at any other place as may be permitted by the Director General of the Department of Home Affairs or the Minister of Home Affairs in terms of that Act; and
 - (B) where a person who is a resident in terms of this subparagraph is physically outside the Republic for a continuous period of at least 330 full days immediately after the day on which such person ceases to be physically present in the Republic, such person shall be deemed not to have been a resident from the day on which such person so ceased to be physically present in the Republic; or
- (b) person (other than a natural person) which is incorporated, established or formed in the Republic or which has its place of effective management in the Republic,

but does not include any person who is deemed to be exclusively a resident of another country for purposes of the application of any agreement entered into between the governments of the Republic and that other country for the avoidance of double taxation: Provided that where any person that is a resident ceases to be a resident during a year of assessment, that person must be regarded as not being a resident from the day on which that person ceases to be a resident.

Section 1(1) Definition of the term “year of assessment”

“**year of assessment**” means any year or other period in respect of which any tax or duty leviable under this Act is chargeable, and any reference in this Act to any year of assessment ending the last or the twenty-eighth or the twenty-ninth day of February shall, unless the context otherwise indicates, in the case of a company or a portfolio of a collective investment scheme in securities be construed as a reference to any financial year of that company or portfolio ending during the calendar year in question.

(2) Unless the context indicates otherwise, a word or expression to which a meaning has been assigned in the Tax Administration Act bears that meaning for purposes of this Act.

Section 66(13)**66. Notice by Commissioner requiring returns for assessment of normal tax under this Act.**

(13) The return for normal tax to be made by any person in respect of any year of assessment shall be a return—

- (a) in the case of a person (other than a company), for the whole period of twelve months ending upon the last day of the year of assessment under charge: Provided that where—
 - (a) a person dies, a return shall be made for the period commencing on the first day of that year of assessment and ending on the date of death;
 - (b) the estate of a person is sequestered, separate returns must be made for the periods—
 - (i) commencing on the first day of that year of assessment and ending on the date preceding the date of sequestration; and
 - (ii) commencing on the date of sequestration and ending on the last day of that year of assessment;