



*SOUTH AFRICAN REVENUE SERVICE*

**INTERPRETATION NOTE NO. 44**

DATE: 31 August 2007

**ACT : INCOME TAX ACT, 1962 (the Act)**  
**SECTION : PARAGRAPH 63A OF THE EIGHTH SCHEDULE**  
**SUBJECT : PUBLIC BENEFIT ORGANISATIONS (PBOs): CAPITAL GAINS TAX (CGT)**

**1 Purpose**

This Interpretation Note explains the CGT consequences for PBOs. It reflects the law as amended by the Revenue Laws Amendment Act, No. 20 of 2006 and the Taxation Laws Amendment Act, No. 8 of 2007. In particular the Note provides clarity on paragraph 63A which was introduced into the Eighth Schedule to address the disposal of capital assets by PBOs. This Note must be read with Interpretation Note No. 24 (Issue 2) *PBOs: Trading Rules - Partial Taxation of Trading Receipts*.

**Note:** Unless otherwise indicated, all references to paragraphs are to paragraphs in the Eighth Schedule to the Act and all references to sections are to sections in the Act.

**2 Background**

Up until years of assessment commencing on or after 1 April 2006, PBOs enjoyed complete exemption from income tax and CGT. In terms of paragraph 63 PBOs disregarded all capital gains or losses on the basis that their gross income of whatever nature was exempt from income tax in terms of section 10.

This changed with effect from years of assessment commencing on or after 1 April 2006 following the introduction by the Revenue Laws Amendment Act, No. 31 of 2005 of a system of partial taxation for PBOs. Under this system a PBO conducting trading activities in excess of prescribed limits is taxable on receipts and accruals derived from those activities, but retains exemption in respect of its public benefit activities (PBAs).

Since PBOs could hypothetically trade and thereby derive taxable income, they could no longer claim that all their receipts and accruals of whatever nature would

be exempt from tax. They therefore no longer qualified for exclusion from CGT under paragraph 63 and instead, were required to seek partial exemption under paragraph 64, which was amended by section 78(1) of the Revenue Laws Amendment Act, No. 31 of 2005. In terms of the amended paragraph 64, any capital gain or loss on disposal of an asset was to be disregarded by a PBO if –

- the asset is used solely to produce amounts which are exempt from normal tax in terms of section 10 (other than certain receipts and accruals from a foreign source, dividends on shares and income from collective investment schemes), or
- substantially the whole of the use of the asset from the valuation date is in the carrying on of a PBA.

Paragraph 64 proved problematic when applied to dual-use assets (PBA use and trade use) and assets undergoing a change in use (PBA use to trade use or *vice versa*). Another unintended consequence was that PBOs were no longer able to disregard capital gains and losses on disposal of shares and participatory interests in collective investment schemes.

To address these issues, PBOs were removed from paragraph 64 and now fall under paragraph 63A, a new provision inserted by section 53 of the Revenue Laws Amendment Act, No. 20 of 2006.

In terms of section 64(2) of the Taxation Laws Amendment Act, No. 8 of 2007, paragraph 63A is deemed to have come into operation on 1 April 2006 and applies in respect of any year of assessment commencing on or after that date.

In terms of paragraph 63A any capital gain or capital loss made on the disposal of an asset, substantially the whole of which has not been used in the carrying on of a PBA, will be taken into account for CGT purposes.

### 3 The law

#### **The Eighth Schedule Paragraph 1. Definitions. –**

“**asset**” includes –

- (a) property of whatever nature, whether movable or immovable, corporeal or incorporeal, excluding currency, but including any coin made mainly from gold or platinum; and
- (b) a right or interest of whatever nature to or in such property;

“**base cost**” means the amount to be determined in terms of Part V;

**“valuation date”** means –

- (a) in the case of any person who after 1 October 2001 ceases to be an exempt person for purposes of paragraph 63, the date on which such person ceases to be an exempt person; or
- (b) in any other case, 1 October 2001;

**Paragraph 29. Market value on valuation date. -**

(4) For the purposes of paragraphs 26(1)(a) and 27(3), a person may only adopt or determine the market value as the valuation date value of that asset if –

- (a) in the case where the valuation date is 1 October 2001 –
  - (i) to (iii)
- (b) in the case where the valuation date is after 1 October 2001 –
  - (i) that person has valued that asset within two years after valuation date; or
  - (ii) that asset is one contemplated in paragraph 31(1)(a) or (c)(i) and the market value of that asset on valuation date is determined in terms of one of those paragraphs.

(8) Where the valuation date of a person is after 1 October 2001 the provisions of subparagraphs (1)(a), (1)(b)(i), (2), (2A), (3), (5) and (6)(a) do not apply.

**Paragraph 30. Time-apportionment base cost. –** (Refer to the Eighth Schedule for detailed legislation)

*[For purposes of this Note the following has been extracted from paragraph 30]:*

(1) Subject to paragraph (3), the time-apportionment base cost of a pre-valuation date asset is determined in accordance with the formula –

$$Y = B + \frac{(P-B) \times N}{T + N}$$

where –

- (a) “Y” represents the amount to be determined;
- (b) “B” represents the amount of expenditure incurred prior to the valuation date in respect of that asset that is allowable before, on or after the valuation date in terms of paragraph 20;
- (c) “P” represents the proceeds as determined in terms of paragraph 35, in respect of the disposal of that asset, or where subparagraph (2) applies, the amount of the proceeds attributable to the expenditure in “B” as determined in accordance with subparagraph (2);
- (d) “N” represents the number of years determined from the date that the asset was acquired to the day before valuation date, which number of years may not exceed 20 in the case where the expenditure allowable in terms of paragraph 20 in respect of that asset was incurred in more than one year of assessment prior to the valuation date;
- (e) “T” represents the number of years determined from valuation date until the date the asset was disposed of after valuation date;

Provided that for purposes of items (d) and (e) a part of a year must be treated as a full year.

**Paragraph 63A. Public benefit organisations. –**

A public benefit organisation approved by the Commissioner in terms of section 30(3) must disregard any capital gain or capital loss determined in respect of the disposal of an asset if –

- (a) that public benefit organisation did not use that asset on or after valuation date in carrying on any business undertaking or trading activity; or
- (b) substantially the whole of the use of that asset by that public benefit organisation on and after valuation date was directed at –
  - (i) a purpose other than carrying on a business undertaking or trading activity; or
  - (ii) carrying on a business undertaking or trading activity contemplated in section 10(1)(cN)(ii)(aa), (bb) or (cc).

**Section 10(1)(cN) of the Act:**

**10. Exemptions. –** (1) There shall be exempt from normal tax –

- (cN) the receipts and accruals of any public benefit organisation approved by the Commissioner in terms of section 30(3) to the extent that the receipts and accruals are derived –
  - (i) otherwise than from any business undertaking or trading activity; or
  - (ii) from any business undertaking or trading activity –
    - (aa) if the undertaking or activity –
      - (A) is integral and directly related to the sole or principal object of that public benefit organisation as contemplated in paragraph (b) of the definition of 'public benefit organisation' in section 30;
      - (B) is carried out or conducted on a basis substantially the whole of which is directed towards the recovery of cost; and
      - (C) does not result in unfair competition in relation to taxable entities;
    - (bb) if the undertaking or activity is of an occasional nature and undertaken substantially with assistance on a voluntary basis without compensation;
    - (cc) if the undertaking or activity is approved by the Minister by notice in the *Gazette*, having regard to –
      - (A) the scope and benevolent nature of the undertaking or activity;
      - (B) the direct connection and interrelationship of the undertaking or activity with the sole or principal object of the public benefit organisation;
      - (C) the profitability of the undertaking or activity; and
      - (D) the level of economic distortion that may be caused by the tax exempt status of the public benefit organisation carrying out the undertaking or activity; or
    - (dd) other than an undertaking or activity in respect of which item (aa), (bb) or (cc) applies and do not exceed the greater of –
      - (i) 5 per cent of the total receipts and accruals of that public benefit organisation during relevant year of assessment; or
      - (ii) R100 000;

## 4 General meaning of certain terminology

**“Substantially the whole”** – This concept is regarded by SARS as being 90% or more. However, in order to conform with section 30 of the Act and to overcome certain practical difficulties, SARS will accept a percentage of not less than 85%. The percentage usage is determined using a method appropriate to the circumstances which may be based either on time or area.

### Example 1 – “Substantially the whole”

*Facts:* A home caring for orphaned children has a hall which is used for social and other functions for the residents. When the hall is not in use by the residents, it is let to outside persons. The hall is let for 48 days of the year.

*Result:* The 48 days during which the hall is let represents 13,2% of the total usage for the year ( $48/365 \times 100$ ). The balance of 86,8% represents the days when the hall is utilised for conducting PBAs. This means that substantially the whole of the hall, namely, more than 85%, is used to conduct PBAs.

## 5 Application of the law

### 5.1 Valuation date

In terms of paragraph (a) of the definition of “valuation date” in paragraph 1, the valuation date of a person who ceases to be an exempt person in terms of paragraph 63, is the date on which that person ceases to be an exempt person. Since all PBOs fall outside paragraph 63 with effect from the introduction of partial taxation of PBOs, it follows that the valuation date of PBOs in existence on 1 April 2006 will be the first day of their first year of assessment commencing on or after 1 April 2006. For example, a PBO with a March year end will have a valuation date of 1 April 2006, which is the commencement of its 2007 year of assessment.

The valuation date value of a pre-valuation date asset forms part of the base cost of that asset and ensures that any pre-valuation date growth or decline in value is disregarded for CGT purposes.

### 5.2 Base cost

The following methods of determining the base cost of an asset on valuation date are available:

- The market value of the asset on valuation date (paragraphs 26, 27, 29 and 31).
- Twenty percent (20%) of the proceeds from the disposal of the asset, after first deducting from the proceeds an amount equal to the expenditure

allowable as part of the base cost incurred on or after valuation date (paragraph 26).

- The time-apportionment base cost (TAB) of an asset as determined in terms of paragraph 30.
- The weighted average method under paragraph 32(3A). This is only available for the four categories of identical assets listed in paragraph 32(3A) (listed shares, participatory interests in collective investment schemes, gold and platinum coins whose prices are published in a newspaper, and listed section 24J instruments). This is unlikely to be of much relevance to a PBO in view of the exclusion of capital gains and losses on such assets in terms of paragraph 63A(a) discussed in **5.3.1** below.

### 5.2.1 Market value

In terms of paragraph 29(4)(b)(i), a PBO may not adopt or determine the market value of an asset unless it has valued the asset within two years from the valuation date. There is, however, no time limit for the valuation of financial instruments listed on a “recognised exchange” (as defined in paragraph 1) and participatory interests in South African collective investment schemes.

A PBO that comes into existence after 1 April 2006 does not need a valuation date since it will have acquired its assets at cost in terms of paragraph 20. The table below summarises the valuation dates for PBOs in existence on 1 April 2006 and the final date by which they must complete their valuations.

**Table 1** – Summary of valuation dates for PBOs in existence on 1 April 2006

<b>Tax year ending on the last day of</b>	<b>Valuation date</b>	<b>Final day for completion of valuation</b>
March	1 April 2006	31 March 2008
April	1 May 2006	30 April 2008
May	1 June 2006	31 May 2008
June	1 July 2006	30 June 2008
July	1 August 2006	31 July 2008
August	1 September 2006	31 August 2008
September	1 October 2006	30 September 2008
October	1 November 2006	31 October 2008
November	1 December 2006	30 November 2008
December	1 January 2007	31 December 2008
January	1 February 2007	31 January 2009
February	1 March 2007	28 February 2009

The two-year valuation period does not apply to the assets set out in the table below.

**Table 2** – Assets which do not have to be valued within two years by PBOs

<b>Paragraph 31(1) of the Eighth Schedule</b>	<b>Description</b>	<b>Market value on valuation date</b>
(a)	Financial instrument listed on a recognised exchange for which a price was quoted on that exchange	Ruling price on last business day before valuation date
(c)(i)	<ul style="list-style-type: none"><li>• A participatory interest in a local collective investment scheme in securities</li><li>• A participatory interest in a local collective investment scheme in property</li></ul>	Price at which a participatory interest can be sold to the management company of the scheme on valuation date

Participatory interests in listed foreign collective investment schemes fall under paragraph 31(1)(a) in the above table. However, where they are unlisted the PBO must, in theory at least, establish their market value within two years of its valuation date in terms of paragraph 29(1)(b)(ii), namely -

- the last price published before valuation date at which a unit could be sold to the management company of the scheme, or
- where there is not a management company the price which could have been obtained upon a sale of the asset between a willing buyer and a willing seller dealing at arm's length in an open market on that date.

However, in practice a capital gain or capital loss arising from the disposal of an unlisted participatory interest in a foreign collective investment scheme is likely to be disregarded in terms of paragraph 63A(a). The failure by a PBO to value such an interest is therefore unlikely to have any adverse CGT consequences while the PBO remains approved by the Commissioner in terms of section 30(3).

The valuation submission requirements in respect of the high value assets listed in paragraph 29(5) do not apply where the valuation date is after 1 October 2001 (paragraph 29(8)). These requirements therefore do not apply to PBOs, which are simply required to lodge the valuation form (CGT 2L) with the tax return reflecting the disposal.

### **5.2.2 Time-apportionment base cost (TAB)**

It is beyond the scope of this Interpretation Note to explain the detailed workings of the TAB method. Reference should be made to the *Comprehensive Guide to CGT* on the SARS website where the method is explained in detail. Where a PBO

acquired an asset before valuation date for no consideration, it will have an acquisition cost of nil for the purposes of determining “B” in the TAB formula. This will result in a larger capital gain than would otherwise be the case. In these circumstances the market value method may well give a better result.

**Note:** Market valuation can only be used if the asset has been valued within the prescribed two-year period (see 5.2.1).

### 5.2.3 Twenty percent of proceeds method

This method, which is likely to be a method of last resort, is also explained in detail in the *Comprehensive Guide to CGT* to which reference should be made.

## 5.3 Exclusions

In terms of paragraph 63A a PBO approved by the Commissioner under section 30(3) must disregard a capital gain or capital loss arising on the disposal of three categories of assets as set out below.

### 5.3.1 Category 1: Non-trading assets (paragraph 63A(a))

This category applies to assets which have not been used by the PBO on or after valuation date in carrying on any business undertaking or trading activity. This includes assets which have been used exclusively for non-trade purposes such as carrying on a PBA. Only the usage of the asset on or after the valuation date is taken into account. Any trade usage before that date is ignored.

Also included in this non-trade category are assets which are not “used” but “held”. This includes investments in the nature of shares and participatory interests in collective investment schemes.

#### **Example 2 – Asset used exclusively on or after valuation date in carrying on a PBA**

*Facts:* A PBO whose year end is 30 April provides health care services to poor and needy persons. It acquired immovable property on 30 June 2003 from which it conducts its PBA, namely, the provision of health care services. During the period 30 June 2003 to 30 April 2006, 30% of the property was let to third parties while the remaining usage was in respect of PBAs. As from the valuation date the property was used exclusively in carrying on PBAs. The property is sold on 30 September 2006 resulting in a capital gain of R100 000.

*Result:* In terms of paragraph 63A(a) the capital gain of R100 000 must be disregarded as the asset was used exclusively on or after the valuation date (1 May 2006) to carry on PBAs. Any trade usage prior to valuation date is disregarded.



**Example 3 – Asset “held” not “used”**

*Facts:* An approved PBO conducts the sole activity of caring for homeless children. It has invested surplus funds in a collective investment scheme. The PBO disposes of its participatory interest in the collective investment scheme at a capital gain to fund the purchase of additional accommodation.

*Result:* The capital gain must be disregarded in terms of paragraph 63A(a), since the participatory interests were “held” by the PBO and are not “used” in carrying on a business undertaking or trading activity.

**5.3.2 Category 2: Minimal trading assets (paragraph 63A(b)(i))**

This category applies where substantially the whole of the use of the asset by the PBO on or after valuation date was directed at a purpose other than carrying on a business undertaking or trading activity. An example of such an asset is one that is used 10% of the time for trading purposes and 90% of the time to conduct PBAs. Of critical importance are the words “substantially the whole of the use”. As explained in paragraph 4, this is regarded to mean 90% or more. However SARS is prepared to accept a usage of not less than 85%. The assets referred to in this category are excluded from the first category (see 5.3.1) as they are used, albeit to a limited extent, in carrying on a business undertaking or trading activity.

The percentage of the asset used for trade or business purposes must be determined using a method appropriate to the circumstances, for example, one based on time or floor area.

**Example 4 – Determination of “substantially the whole of the use” on a time basis**

*Facts:* A religious institution has a year end of 30 April and has been approved as a PBO in terms of section 30. It acquired a manse in 1995 for occupation by its resident minister. The minister’s term of office ended on 30 June 2006 and the manse was let to a third party from 1 July 2006 to 31 July 2006. The newly-appointed minister took occupation on 1 August 2006. The manse was sold on 31 March 2007.

*Result:* The PBO’s valuation date is 1 May 2006, being the first day of its first year of assessment commencing on or after 1 April 2006. The asset was held for eleven months from valuation date to the date of sale (1 May 2006 to 31 March 2007). During this period the manse was utilised to carry on PBAs for ten months and let for one month. This represents a usage of 90.9% ( $10/11 \times 100$ ) for carrying on PBAs from the valuation date. This means that the PBO has utilised substantially the whole of the manse from the valuation date in carrying on its PBAs. Paragraph 63A(b)(i) is applicable and the PBO must accordingly disregard any capital gain or loss on the disposal of the manse.

### 5.3.3 Category 3: Permissible trading assets (paragraph 63A(b)(ii))

This category applies where substantially the whole of the use of the asset by the PBO on or after valuation date was directed at carrying on a business undertaking or trading activity which qualifies for exemption in terms of items (aa), (bb), or (cc) of section 10(1)(cN)(ii).

**Note:** Any capital gain or loss made on the disposal of an asset utilised in a trading activity or business undertaking as contemplated in the basic exemption rule described in item (dd) of section 10(1)(cN)(ii), will not be disregarded.

The permissible business undertakings or trading activities are as follows:

#### a) Related trade [section 10(1)(cN)(ii)(aa)]

In terms of this exclusion rule the receipts and accruals derived from a trading activity or business undertaking of a PBO will not be subject to income tax if the trading or business activity –

- is integral and directly related to the sole or principal object of the PBO,
- is carried out or conducted on a basis substantially the whole of which is directed towards the recovery of cost, and
- does not result in unfair competition with taxable entities.

#### **Example 5 – Asset used to carry on a permissible trading activity contemplated in section 10(1)(cN)(ii)(aa)**

*Facts:* An approved PBO conducts PBAs of providing facilities for the care of mentally disabled persons. As a therapeutic and remedial activity, the PBO has acquired land on which the disabled are taught to grow vegetables. The produce is primarily used for own consumption and any surplus is sold to a local home industry. All the labour is undertaken by the residents. The PBO disposes of the land on which the vegetable gardening takes place resulting in a capital gain.

*Result:* The vegetable gardening activity falls within the permissible trading rules of section 10(1)(cN)(ii)(aa) as it forms part of the PBA of caring for and providing training for the residents. The capital gain realised on the sale of the property is disregarded for CGT purposes.

#### b) Occasional trade [section 10(1)(cN)(ii)(bb)]

To qualify under this category the trading activity must –

- take place on an occasional basis, and

- be undertaken substantially with assistance on a voluntary basis without compensation.

**Example 6 – Asset used to carry on a permissible trading activity contemplated in section 10(1)(cN)(ii)(bb)**

*Facts:* A PBO conducts PBAs of caring for poor and needy persons 60 years and older. The PBO holds an annual fete as a fundraising event for which it has acquired a marquee. The fundraising event is undertaken with assistance from volunteers and the items which are sold were all donated.

*Result:* This event qualifies as an occasional trading activity which falls within the ambit of section 10(1)(cN)(ii)(bb). If the marquee is sold, any resulting capital gain or loss must be disregarded for CGT purposes.

**c) Ministerial approval [section 10(1)(cN)(ii)(cc)]**

In terms of this category the Minister of Finance may approve a specific business undertaking or trading activity by notice in the *Gazette* having regard to factors such as –

- the scope and benevolent nature of the activity,
- its relationship with the sole or principal object of the PBO,
- its profitability, and
- the economic distortion that may result from the exemption.

To date the Minister has not approved any such undertakings or activities.

Any capital gain or capital loss made on the disposal of assets utilised in carrying on the specific trade or business as approved by the Minister must be disregarded.

## 6 Practical examples

**Example 7 – Determination of valuation date values (VDV)**

*Facts:*

- A PBO with a 31 March year end owns immovable property on which it carries on its PBAs.
- The property was acquired on 1 June 1996 at a cost of R40 000.
- With effect from 1 June 2006 the PBO let 20% of its property to a commercial business at an arm's length rental.

- No expenditure was incurred in respect of improvements to the property from date of acquisition.
- On 31 December 2011 the PBO disposed of the property for proceeds of R110 000.
- The PBO paid estate agent's commission of R7 000.
- The PBO determined that the market value of the property on 1 April 2006 was R80 000.

*Determine:*

The capital gain or loss on disposal of the property assuming that the valuation was performed on –

- 31 March 2008, or
- 31 August 2008

*Result:*

The valuation date of the PBO is 1 April 2006, namely, the first day of its first year of assessment commencing on or after 1 April 2006. If the PBO wishes to adopt the market value method for determining the valuation date value of the property, the valuation should be determined by 31 March 2008, namely, within two years of its valuation date. It follows that –

- where the valuation was performed on 31 March 2008, the market value was determined timeously and the PBO may adopt the market value of the property on 1 April 2006 as the valuation date value of the property. The PBO is also entitled to use the TAB or 20% of proceeds methods if it so chooses, and
- where the valuation was done on 31 August 2008, the market value was not determined timeously and the PBO must resort to the time-apportionment basis (TAB) or the 20% of proceeds method to determine the base cost of the property as at 1 April 2006.

**Time-apportionment basis (TAB)**

**Valuation date = 1 April 2006 (Note 1)**

**N = Number of years before valuation date (1 June 1996 to 31 March 2006), determined as follows:**

1 June 1996 to 31 May 2005 = 9 years

1 June 2005 to 31 March 2006 = 10 months (treated as a full year)

**N = 9 + 1 = 10**

**T = Number of years after valuation date (1 April 2006 to 31 December 2011)**

1 April 2006 to 31 March 2011 = 5 years

1 April 2011 to 31 December 2011 = 9 months (treated as a full year)

**T = 5 + 1 = 6**

$$\begin{aligned} P &= \text{Amount received or accrued reduced by selling expenses (Note 2)} \\ &= R110\,000 - R7\,000 = R103\,000 \end{aligned}$$

$$\begin{aligned} \text{TAB} &= B + [(P - B) \times N/(N + T)] \\ &= R40\,000 + [(R103\,000 - R40\,000) \times 10/(10 + 6)] \\ &= R40\,000 + (R63\,000 \times 10/16) \\ &= R40\,000 + R39\,375 \\ &= R79\,375 \end{aligned}$$

$$\begin{aligned} \text{Base cost} &= \text{TAB} + \text{post-valuation date costs} \\ &= R79\,375 + R7\,000 \\ &= R86\,375 \end{aligned}$$

$$\begin{aligned} \text{Capital gain} &= \text{Proceeds} - \text{base cost} \\ &= R110\,000 - R86\,375 \\ &= R23\,625 \end{aligned}$$

**Note:**

1. The TAB calculator on the SARS website cannot be used to determine TAB for a PBO as it assumes a valuation date of 1 October 2001. It will therefore give incorrect figures for 'N' and 'T' where, as in this example, the valuation date is after 1 October 2001.
2. This example assumes that no improvements were made on or after the valuation date. Had such improvements been made, the proceeds formula in paragraph 30(2) would have had to be applied to determine 'P'.

**20% of proceeds method**

$$\begin{aligned} \text{Valuation date value} &= 20\% \times (\text{proceeds less post-valuation date expenditure}) \\ &= 20\% \times (R110\,000 - R7\,000) \\ &= 20\% \times R103\,000 \\ &= R20\,600 \end{aligned}$$

$$\begin{aligned} \text{Base cost} &= \text{VDV} + \text{post-valuation date expenditure} \\ &= R20\,600 + R7\,000 \\ &= R27\,600 \end{aligned}$$

$$\begin{aligned} \text{Capital gain} &= \text{Proceeds} - \text{base cost} \\ &= R110\,000 - R27\,600 \\ &= R82\,400 \end{aligned}$$

**Market value method (valuation done on or before 31 March 2008)**

$$\begin{aligned} \text{Base cost} &= \text{Market value on 1 April 2006} + \text{post-valuation date expenditure} \\ &= R80\,000 + R7\,000 \\ &= R87\,000 \end{aligned}$$

$$\begin{aligned} \text{Capital gain} &= \text{Proceeds} - \text{base cost} \\ &= R110\,000 - R87\,000 \\ &= R23\,000 \end{aligned}$$

**Example 8 – Determine “substantially the whole of the use” of the asset on area usage (paragraph 63A(b))**

*Facts:* An approved PBO provides counselling services to prisoners from a residential house which it owns. The PBO utilises only portion of the house for counseling services and lets the remaining rooms to third parties at a market-related rental. The area of the house is 210 sq metres. The area of the property which is let is 30 sq metres and the balance of 180 sq metres is used for PBAs. The financial year end of the PBO is 28 February. Valuation of the property took place on 1 March 2007. The property is sold on 30 June 2009 realising a capital gain.

*Result:* As from its first year of assessment commencing on or after 1 April 2006, the PBO is subject to the provisions of paragraph 63A in respect of assets disposed of. In order to determine whether the property was, from the valuation date substantially used to conduct PBAs, the area which was used for PBAs in relation to the whole property is taken into account, namely,  $180/210 \times 100 = 85.7\%$ . The capital gain made on the sale of the property must be disregarded as substantially the whole of the use of the property, more than 85%, was to carry on PBAs.

**Example 9 – Determination of “substantially the whole of the use” on an hourly usage basis (paragraph 63A(b))**

*Facts:* An educational institution that has been approved in terms of section 30 has acquired a separate property for purposes of development as sports grounds. Hockey fields and tennis courts were constructed. During school holidays and over periods when the facilities are not utilised by the PBO, they are let to outside sports clubs, coaches and other third parties at market-related rates on which the PBO is partially taxed with effect from the commencement of its financial year ending 31 December 2007. The PBO is obliged to dispose of the property on 8 March 2009 as a result of a commercial development on the adjoining properties and a capital gain is made on the transaction. Hourly usage of the property by third parties is 12%, with PBA usage being 88%.

*Result:* The PBO has utilised substantially the whole of the property from the valuation date in carrying out its PBAs. The capital gain on the disposal of the property must accordingly be disregarded in terms of paragraph 63A(b)(i).

**7 Donations or bequests to PBOs – paragraphs 40(1)(b) and 62(b)**

Any capital gain or capital loss determined in respect of an asset which has been donated or bequeathed to a PBO which has been approved by the Commissioner in terms of section 30(3) must be disregarded in the hands of the donor.

**8 Transfer duty**

A consequential effect on PBOs having to determine capital gains and capital losses on the disposal of fixed assets is the transfer duty implication. Where the asset (which qualified for transfer duty exemption) is subsequently not

substantially used for PBA purposes, transfer duty becomes payable at the time the property is used for any purpose other than for the purpose of carrying on one or more PBAs. For further information in this regard see Interpretation Note No. 22 dated 11 March 2004.

## **9 General**

Detailed information relating to CGT can be found in the various CGT Guides available on the SARS website.

## **10 Conclusion**

The information contained in this Interpretation Note provides broad principles in interpreting the legislation. As the facts and circumstances pertaining to specific PBOs may differ, each case must be considered on its own merits.

**Legal and Policy Division  
SOUTH AFRICAN REVENUE SERVICE**

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