

DRAFT INTERPRETATION NOTE

DATE:

ACT : INCOME TAX ACT NO. 58 OF 1962

SECTION : SECTION 30(4)

SUBJECT : INCOME TAX: PUBLIC BENEFIT ORGANISATIONS: WRITTEN UNDERTAKING FURNISHED TO THE COMMISSIONER CONFIRMING COMPLIANCE WITH THE PRESCRIBED REQUIREMENTS

Preamble

In this Note unless the context indicates otherwise -

- "amendment" means an addition or alteration to the founding document;
- "fiduciary" means a person who holds a position of trust or responsibility including decision-making powers relating to the affairs of an organisation;
- "founding document" means the constitution, will or other written instrument under which an organisation is established and governed;
- "organisation" means an entity that has applied to the TEU for approval as a PBO;
- "PBA" means any public benefit activity listed in Part I of the Ninth Schedule;
- "PBO" means a "public benefit organisation" as defined in section 30(1);
- "prescribed requirements" means the formal conditions and requirements set out in section 30(3)(*b*);
- "section" means a section of the Act;
- **"TEU"** means the Tax Exemption Unit, a dedicated office within SARS dealing with all applications for approval or exemption from income tax on behalf of the Commissioner;
- "the Act" means the Income Tax Act No. 58 of 1962;
- "written instrument" means the founding document; and
- any word or expression bears the meaning ascribed to it in the Act.

1. Purpose

This Note provides guidance on the interpretation and application of section 30(4), which provides for a written undertaking to be submitted under certain circumstances before an organisation can be approved as a PBO by the TEU.

2. Background

Section 30(3)(b) prescribes specific requirements that have to be included in a founding document before an organisation can be approved as a PBO.

The founding document of an organisation may not comply with the requirements of section 30(3)(b) at the time the application is submitted to the TEU for approval. In these circumstances section 30(4) makes provision for the founding document to be deemed to comply with the requirements of section 30(3)(b), if the person responsible in a fiduciary capacity for the funds and assets of the organisation furnishes the Commissioner with a written undertaking that the organisation will be administered in compliance with the prescribed requirements.

In those circumstances in which it is possible to amend the founding document, the written undertaking is an interim measure, and the relevant requirements must subsequently be formally incorporated into the founding document within a specific timeframe.

3. The law

Section 30(4)

(4) Where the constitution, will or other written instrument does not comply with the provisions of subsection (3)(b), it shall be deemed to so comply

(a) (b)

if the person responsible in a fiduciary capacity for the funds and assets of such organisation furnishes the Commissioner with a written undertaking that such organisation will be administered in compliance with the provisions of this section.

4. Application of the law

4.1 Requirements under section 30(3)(*b*)

In order to be approved as a PBO the following specific requirements must be included in the founding document:

- At least three persons, who are not connected persons in relation to each other, must accept fiduciary responsibility for the organisation and no single person is permitted to directly or indirectly control the decision-making powers of the organisation.
- Funds must be used solely for the object for which the organisation is established and no funds may be directly or indirectly distributed to any person, unless this occurs in the course of undertaking an approved PBA.
- On dissolution, the remaining assets must be transferred to one or more of the following organisations that are required to use the assets solely for the purpose of carrying on approved PBAs:
 - > A PBO which has been approved under section 30(3).
 - An institution, board or body exempt from income tax under section 10(1)(cA)(i) that has as its sole or principal object the carrying on of any PBA.
 - The government of the Republic in the national, provincial or local sphere.
- A branch of a foreign exempt organisation must on termination of its activities in the Republic transfer the remaining assets to one or more of the

aforementioned entities, if more than 15% of the receipts and accruals of the branch is derived from a source within the Republic, during a period of three years preceding the termination of its activities.

- No donation may be accepted that may be revoked by the donor or when conditions are imposed that will entitle the donor or any connected person to obtain a direct or indirect benefit from that donation, or when there is any misrepresentation with regard to the tax deductibility of that donation under section 18A.
- A copy of all amendments to the founding document must be submitted to the Commissioner.

4.2 Written undertaking under section 30(4)

The term "written undertaking" is not defined in the Act. In the context of section 30 the written undertaking is regarded as a promise or commitment made by the person accepting fiduciary responsibility for the funds and assets of the organisation that, although the founding document does not meet the prescribed requirements necessary to obtain PBO approval, the organisation will be administered in compliance with these prescribed requirements.

The written undertaking is binding on the organisation and non-compliance with its terms will result in the same penalties and actions as if the prescribed requirements had been contained in the founding document (refer to **5**).

A specimen written undertaking (form EI 2) can be found on the SARS website by selecting "Find a Form" under Useful Tools. The written undertaking must be submitted together with the application for approval as a PBO under section 30(3), unless the founding document meets the prescribed requirements of section 30(3)(b). A sample copy of form EI 2 has been included in **Annexure A** for ease of reference.

4.3 Person responsible in a fiduciary capacity

The written undertaking must be given by the person responsible in a fiduciary capacity for the funds and assets of the organisation. Section 30(3)(b)(i), however, requires the organisation to have at least three persons who are not connected persons in relation to each other to accept fiduciary responsibility for the organisation. SARS therefore requires that in addition to the person responsible in a fiduciary capacity for the funds and assets, any other two of the unconnected persons must sign the written undertaking.

4.4 Other instances in which the founding document may not comply

4.4.1 Branches of exempt foreign organisations

A branch established in the Republic by a company, association or trust that is incorporated, formed or established outside the Republic and which is exempt from income tax in its country of origin, may fall within the ambit of the definition of a PBO and may qualify for approval as a PBO provided it complies with the prescribed requirements of section 30(3)(b).

The branch of a foreign exempt organisation that does not have a separate founding document relating to its activities in the Republic, but operates and is governed in accordance with the founding document of the foreign organisation, which cannot be amended to incorporate the prescribed requirements of section 30(3)(b), may submit a written undertaking by the person responsible in a fiduciary capacity for the funds

and assets, that the branch in the Republic will be administered in compliance with the prescribed requirements of section 30(3)(b).

A specimen written undertaking for a branch of a foreign exempt organisation (form EI 2B) is available on the SARS website and must be submitted together with the application for approval as a PBO under section 30(3). A sample copy of form EI 2B has been included in **Annexure B** for ease of reference.

4.4.2 Testamentary trusts

A testamentary trust is created under the provisions of a will and its trustees can only apply for its approval as a PBO once it comes into existence after the death of the testator and commences to carry on approved PBAs.

The provisions of a will cannot be amended after the death of the testator and since the will may not include the prescribed requirements of section 30(3)(b) at the time when the trust comes into existence, the person responsible in a fiduciary capacity for the funds and assets of the testamentary trust, may submit a written undertaking, in order for the testamentary trust to qualify for approval as a PBO under section 30(3).

A testator may appoint, as a fiduciary of the testamentary trust, a trustee or manager of a financial institution or of a trust and asset management company as executor or trustee to administer the estate. The trustee or trust administrator may not have the authority in terms of the will to appoint additional trustees, in order to comply with the requirement of having three unconnected persons. Section 30(3)(b)(i) was amended by section 53(1)(b) of the Taxation Laws Amendment Act No. 7 of 2010 to provide that from the commencement of years of assessment ending on or after 1 January 2011 a testamentary trust is not required to comply with the requirement of having three unconnected persons. The written undertaking need therefore only be signed by the person accepting fiduciary responsibility for the funds and assets of the testamentary trust.

The written undertaking is binding on the person accepting fiduciary responsibility for the funds and assets of the testamentary trust and non-compliance with section 30(3)(b) will result in the same penalties and actions as if the prescribed requirements had been contained in the will (refer to **5**).

4.5 Interim measure

The written undertaking is an interim measure to enable an organisation to obtain approval as a PBO under section 30(3) despite its founding document not complying with the prescribed requirements of section 30(3)(b). Although an organisation may have submitted the required written undertaking and been granted PBO approval by the TEU, it must still incorporate the relevant requirements of section 30(3)(b) in its founding document.

SARS will require the organisation to amend its founding document within a reasonable period. A reasonable period will be regarded by SARS as 12 months from the date of the letter issued by the TEU confirming PBO approval or whenever any other amendment is effected to the founding document, whichever date occurs first.

Example – Amendment of the memorandum of incorporation to include the prescribed requirements of section 30(3)(b)

Facts:

ABC, a non-profit company, has been approved by the TEU as a PBO under section 30(3) and the three unconnected directors have signed a written undertaking, that ABC will be administered in compliance with the requirements of section 30(3)(b).

The letter confirming approval of ABC as a PBO under section 30(3) was issued by the TEU on 1 July 2013. The approval was granted subject to the condition that the memorandum of incorporation be amended to include the prescribed requirements of section 30(3)(b) within a period of 12 months from the date of the letter or whenever an amendment is effected to the memorandum of incorporation, whichever date occurs first.

Result:

ABC will be required to formally amend the memorandum of incorporation to include the prescribed requirements of section 30(3)(b) by no later than 1 July 2014.

However, should the company during the 12-month period from 1 July 2013 to 1 July 2014, make any other amendment to the memorandum of incorporation, it must include the prescribed requirements of section 30(3)(b) at the same time.

5. Non-compliance [section 30(5), 30(6), 30(7) and 30(11)]

The TEU may, after giving due notice, withdraw the approval of a PBO with effect from the beginning of the relevant year of assessment if the PBO has in any year of assessment in any material respect or on a continuous or repetitive manner failed to comply with the prescribed requirements.

Once the approval is withdrawn the organisation must transfer or take reasonable steps to transfer its remaining assets within six months from the date the approval is withdrawn (or any other period allowed by the TEU), to –

- another approved PBO;
- an institution, board or body that is exempt from income tax under section 10(1)(cA)(i) which has as its sole or principal object the carrying on of any PBA; or
- the government of the Republic in the national, provincial or local sphere.

Failure to transfer the remaining assets will result in an amount equal to the market value of the assets not transferred, less an amount equal to the *bona fide* liabilities of the PBO (net asset value), being deemed to be an amount of taxable income accruing to the PBO during the year of assessment in which the PBO approval is withdrawn.

Under section 30(11) any person in a fiduciary capacity responsible for the management or control of the income and assets of an approved PBO, who intentionally fails to comply with the prescribed requirements or the founding document under which the organisation is established to the extent that it relates to

the provisions of section 30, will be guilty of an offence and liable on conviction to a fine or imprisonment for a period not exceeding two years.

6. Conclusion

The TEU may grant an organisation approval as a PBO under section 30(3) if its founding document does not meet the prescribed requirements of section 30(3)(b) provided a written undertaking that the organisation will be administered in compliance with section 30(3)(b) is submitted by the person responsible in a fiduciary capacity for the funds and assets of the organisation.

Legal and Policy Division SOUTH AFRICAN REVENUE SERVICE

Annexure A – Form El 2 "Income Tax – Exemption – Public Benefit Organisation – Written Undertaking"

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Annexure B – Form El 2 B "Income Tax – Exemption – Foreign Branch approved as a Public Benefit Organisation – Written Undertaking"

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3.	At least 85% of such public benefit activity/activiti benefit of persons in the Republic of South Africa extent of donations received by that organisation f donations, receipts and accruals have not previou	 Provided that cost in from persons who are r 	curred for the benef not resident and rece	it of person ipts and ac	s outside the Republ cruals derived direct	ic shall be disr	egarded to th
4.	At least three persons, who accept fiduciary resp directly or indirectly controls the decision making p			ected perso	ns in relation to eac	n other, and no	single perso
5.	No funds will be directly or indirectly distributed to a	any person (other than	in the course of unde	rtaking any	public benefit activity	/).	
6.	The funds of the branch will be utilised solely for the	e objects for which the	branch was establisł	ned.			
7.	On termination of the activities of the branch in to -	the Republic of Sou	th Africa, the remai	ning assets	s of the South Africa	n branch will	be transferre
	 any public benefit organisation, which has bee any similar institution, board or body which is e principal object the carrying on of any public be any department of state or administration in t section 10(1)(a) or (b) of the Act; If more than 15% of the receipts and accruals source within South Africa. 	exempt from the payme enefit activity; he national or provinci	ent of income tax in t ial or local sphere of	erms of sec governmer	nt of the Republic of	South Africa, c	ontemplated i
8.	The branch will inform the Commissioner should t where it is established.	he off-shore charity no	longer qualify for ex	emption fro	m tax on income in te	rms of the laws	s of the countr
9.	No remuneration will be paid by the branch to any considered reasonable in the sector and in relation consistent with its objects.	employee, office bear to the service rendere	er, member or other ad and has not and w	person whi Il not econo	ch is excessive, havi mically benefit any p	ng regard to wh erson in a manr	nat is generall ner which is no
10.	Prohibited from accepting any donation which is re purposes and conditions of such donation. Provid or body which is exempt from tax in terms of section impose conditions which could enable such dona application of such donation.	ed that a donor (other t n 10 (1)(cA)(i), which h	han a donor which is as as its sole or princ	an approve ipal object	ed public benefit organ the carrying on of any	nisation or an ir public benefit a	stitution boar
11.	In the case where the branch provides funds or as: Act reasonable steps will be taken to ensure that the					1 of the Ninth S	chedule, of th
12.	The branch will not be a party or be used as pa postponement or avoidance of liability for any tax,		operation or scheme	of which t	he sole or main pur	oose is or was	the reduction
	Submit the required income tax returns.						
14.	No section 18A receipts will be issued to donors.						
Dec	laration						
Sig	ined at	on this		day of			20
	Full Name(s)	Si	gnature(s)		C	Capacity	