

**AN ANALYSIS OF THE GENERAL ANTI-AVOIDANCE
RULE IN SOUTH AFRICA AND A COMPARISON WITH
FOREIGN ANTI-AVOIDANCE PROVISIONS**

by

RUTENDO SATUMBA

Student Number: 26277086

Submitted in partial fulfilment of the requirement for the degree LLM

in the

FACULTY OF LAW

at the

UNIVERSITY OF PRETORIA

Prepared under the supervision of Adv Cornelius Louw

November 2011

DISCLAIMER

I, Rutendo Satumba, hereby declare that this dissertation is my own, unaided work. It is being submitted in partial fulfilment of the prerequisites for the degree of Master's in Tax Law at the University of Pretoria. It has not been submitted before for any degree or examination at any other University.

Rutendo Satumba

2011

ACKNOWLEDGEMENTS

The completion of this research would not have been possible without the presence of the spirit of God at work within me. I therefore would like to thank my Heavenly Father who gave me the strength to complete this project.

My supervisor Advocate C Louw was also instrumental in ensuring that this research comes to completion. To my parents, brothers and sisters who gave me words of encouragement and hope that stirred me up to put extra effort in my work, many thanks to you.

To my friends and colleagues who assisted me in formulating the structure of this research as well as finding sources; thumbs up to you.

The University of Pretoria's Law Library staff, how would I have found my sources without you? Thank you for assisting me in locating sources that were vital for my research.

To God be the glory.

ABBREVIATIONS USED IN THIS DOCUMENT

TERM/CONCEPT	SHALL MEAN
GAAR	General Anti-avoidance Rule
HMRC	Her Majesty's Revenue and Customs
ITA	Income Tax Act
ITAA	Income Tax Assessment Act
SARS	South African Revenue Services
PBL	Principles Based Legislation
TAAR(s)	Targeted Anti-Avoidance Rule

TABLE OF CONTENTS

DISCLAIMER	ii
ACKNOWLEDGEMENTS.....	iii
ABBREVIATIONS USED IN THIS DOCUMENT	iv
ABSTRACT	vii
CHAPTER 1. BACKGROUND TO THE RESEARCH.....	1
1.1. Research questions.....	5
1.2. Research objectives	5
1.3. Scope of study.....	6
1.4. Proposed methodology.....	6
1.5. Overview of chapters.....	6
CHAPTER 2. DISCUSSION OF TAX AVOIDANCE	8
2.1. Introduction	8
2.2. Tax planning.....	9
2.3. Tax avoidance	12
2.4. Problems caused by tax avoidance	15
2.5. Tax evasion.....	16
CHAPTER 3. OVERVIEW AND ANALYSIS OF SOUTH AFRICAN GAAR	18
3.1. Introduction	18
3.2. Requirements.....	18
3.3. Avoidance arrangement	20
3.3.1 <i>Transaction, operation, scheme, agreement or understanding</i>	<i>21</i>
3.3.2 <i>An arrangement includes all steps or parts therein</i>	<i>23</i>
3.3.3 <i>Sole/main purpose.....</i>	<i>25</i>

3.3.4	<i>Tax benefit</i>	33
3.3.5	<i>Requirement 4: The arrangement must contain an abnormality element</i> .	35
3.3.6	<i>In the context of business</i>	36
3.3.7	<i>Commercial substance test</i>	38
3.3.8	<i>Lack of commercial substance indicators</i>	42
3.3.9	<i>Substance over form</i>	42
3.3.10	<i>Round trip financing</i>	46
3.3.11	<i>Accommodating or tax –indifferent parties</i>	48
3.3.12	<i>Two thirds requirement</i>	49
3.3.13	<i>Elements that offset or cancel each other</i>	51
3.3.14	<i>Non-business context</i>	52
3.3.15	<i>In any other context</i>	53
CHAPTER 4. COMPARISONS WITH OTHER COUNTRIES		60
4.1.	Introduction	60
4.2.	Australia	60
4.2.1	<i>Requirements Part IVA</i> :.....	62
4.2.2	<i>Application to part/parts of an arrangement</i>	67
4.2.3	<i>The tax benefit requirement</i>	71
4.2.4	<i>Purpose to obtain a tax benefit requirement</i>	73
4.3.	United Kingdom.....	78
4.3.1	<i>Anti-avoidance techniques in the United Kingdom</i>	78
4.3.2	<i>GAAR v TAAR</i>	80
4.3.3	<i>GAAR v PBL</i>	81
4.3.4	<i>Canada</i>	82
4.3.5	<i>Avoidance transaction v avoidance arrangement</i>	83
4.3.6	<i>Series of transactions/events v all parts/steps therein</i>	84
4.3.7	<i>‘Tax Benefit’ requirement under both GAARs</i>	86
4.3.8	<i>Misuse or abuse concept</i>	87
CHAPTER 5. CONCLUSION		89
REFERENCES		94

ABSTRACT

The structure of the tax system is important in developing a workable environment capable of diminishing both the extent and the opportunities for tax avoidance and evasion. Generally, taxpayers dislike paying taxes, which results in them colluding against the government and this impacts negatively on the economy. Efforts by the legislature to curb tax avoidance with the introduction of various forms of anti-avoidance techniques have, however, contributed to the complexity of tax legislation. The complexity of tax legislation, as well as higher marginal tax rates, leads to higher incidences of tax avoidance, and at times, tax evasion. Uncertainty, complexity and confusion also provide the breeding ground for tax avoidance and evasion.

The South African GAAR is a concoction of GAARs from different parts of the world. This is in a bid to ensure that anti-avoidance techniques in South Africa are in line with international trends on anti-avoidance legislation. But has this purpose really been achieved? A comparative study of the South African anti-avoidance legislation with that of other countries is therefore necessary to determine how it stands on a global scale as a deterrent to tax avoidance. For the purposes of this paper, only the Canadian, Australian and United Kingdom GAARs will be discussed.

Unfortunately, it seems no jurisdiction has found a perfect solution, and the use of GAARs in varying forms has had mixed success.

CHAPTER 1. BACKGROUND TO THE RESEARCH

The sustainability of a tax system relies in part in reducing tax avoidance as far as possible.¹ Moreover, the very integrity of a tax system, necessary for its long-term sustainability, is threatened by tax avoidance.²

Tax avoidance has been defined as,

'...the process whereby an individual plans his or her finances so as to apply all exemptions and deductions provided by tax laws to reduce taxable income'.³

It has been noted that,

'... it cannot be said that there is anything like unanimity as to what constitutes tax avoidance, the reason in our view is that there is an inherent contradiction between specific provisions in terms of which certain things are allowable and general provisions which negate what the former allows'.⁴

Generally taxpayers dislike paying taxes, so tax avoidance is an eternally present feature. Tax avoidance impacts on the economy; both because it results in revenue loss and because it diverts people into devising, marketing and implementing avoidance arrangements, rather than engaging in economically productive activities.⁵

¹ Cassidy, J. (2009). The Holy Grail: The search for the optimal GAAR. *South African Law Journal*, vol. 126, issue 4.

² *Ibid.* (Some other effects of tax avoidance include short term revenue loss and severe damage to the tax system).

³ Investopedia. (2011). *Tax avoidance*. Available at http://www.investopedia.com/terms/t/tax_avoidance.asp.

⁴ The Taxpayer. (2007). General Anti-Avoidance Rule. *The Taxpayer*, vol. 56, No. 3.

⁵ *Ibid.*

Some other effects of tax avoidance include short-term revenue loss, and severe damage to the tax system. Further, impermissible tax avoidance has a tremendous impact upon the equity and fairness of the tax system, and at most basic level, it creates a form of subsidy from those paying their fair share of tax according to the intention of the law to those shirking their similar obligations.⁶

In the Budget Speech of 18 March 1985⁷, it was said that,

'It is regrettably true that there are those who consciously and wilfully evade taxation and those who cynically manipulate tax avoidance to such an extent that it cannot be construed as anything but evasion of taxation. A key element to the sustainability of a taxation system is finding a GAAR that fairly 'draws a line in the sand' between legitimate commercial transactions and tax avoidance strategies.'

However, efforts to curb tax avoidance through tax reform and accompanying legislative changes, coupled with detailed and precise legislation, have contributed to the complexity of tax legislation.⁸ In order to eliminate impermissible tax avoidance, the South African legislature implemented the GAAR in the form of s90,⁹ which was later amended to section 103, and later on to the current s80.¹⁰ It has been recognised that 'an appropriate general anti-avoidance regime is a prerequisite for an effective tax system'.¹¹

⁶ SARS Law Administration (2005). Discussion paper on tax avoidance and section 103 of the Income Tax Act 58 of 1962.

⁷ *Ibid.*

⁸ Freedman, J., Loomer, G. & Vella, J. (2008). *Alternatives to tax risks and tax avoidance: an analysis of a face to face corporate survey*. Available at http://www.sbs.ox.ac.uk.innopac.up.ac.za/centres/tax/Documents/working_papers/WP0814.pdf; at 2.

⁹ Income Tax Act, 31 of 1941.

¹⁰ Income Tax Act, 58 of 1962.

¹¹ SARS. (2006). *Tax Avoidance and Section 103 of the Income Tax Act, 1962: An Interim response*, at 31-2, quoting a submission by KPMG.

It was SARS's contention that,

*'In its current form the GAAR has proven to be an inconsistent and, at times, ineffective deterrent to the increasingly complex and sophisticated tax products that are being marketed by banks, boutiques structured finance firms, multinational accounting firms and law firms.'*¹²

A commentator noted that, 'for the past five or six years, the section has barely been a feature in tax planning and has ceased to be the deterrent it once was.'¹³

The new GAAR¹⁴ replaces the old s03 of the Income Tax Act¹⁵ and is spread over 12 new provisions of the Act; namely s80 A to s80L. The new GAAR consists of anti-avoidance measures compiled from tax legislations from across the globe and it has been described as difficult enough to perplex even the most impressive minds.¹⁶

Due to the complexity of the new GAAR, there is also the possibility that it may be restrictively interpreted by the courts, thus not giving the new GAAR its intended effect.¹⁷ It raises important questions as to whether the current anti-avoidance legislative techniques adopted in South Africa are effective in the fight against tax avoidance, or whether the complexity of tax legislation is the breeding ground for further tax avoidance opportunities.¹⁸

¹² SARS. (2006). Tax Avoidance and Section 103 of the Income Tax Act, 1962: An Interim response, at 31-2, quoting a submission by KPMG..

¹³ Mazansky, E. (2005). The Duke of Westminster still lives in South Africa (but is very careful when he crosses the road). *Bulletin for International Fiscal Documentation*, at 116.

¹⁴ Contained in a new Part II A of Chapter III of the Act.

¹⁵ Income Tax Act, 58 of 1962.

¹⁶ Drummond, B. (2006) A purposive approach to the drafting of tax legislation. *British Tax Review*, at 10-11.

¹⁷ *Ibid.*

¹⁸ Freedman, J., Loomer, G. & Vella, J. (2008). *Alternatives to tax risks and tax avoidance: an analysis of a face to face corporate survey*. Available at http://www.sbs.ox.ac.uk.innopac.up.ac.za/centres/tax/Documents/working_papers/WP0814.p

According to the Explanatory Memorandum to the Revenue Laws Amendment Bill 2006, the main reasons for the changes in the anti-avoidance rules were that the old s103 had proven to be ‘an ineffective deterrent against increasingly sophisticated forms of impermissible tax avoidance that certain advisers and financial institutions are putting forward’.¹⁹

The underlying concept of the new GAAR is not much different from s103 because certain elements still have to be present. These elements include the fact that there must be a transaction whose effect must be to obtain a tax benefit. The sole or main purpose of the transaction must be to obtain a tax benefit, and there must be certain abnormal rights or obligations or an abnormal means or manner adopted. Some have observed that the new enacted GAAR has added to the complexity of the already overburdened South African tax system.²⁰ This complexity creates certain difficulties with regards to how the GAAR would be interpreted by the courts and whether the courts would aid in giving effect to Parliament’s intentions or frustrate their intentions by erring towards a narrow interpretation.²¹

There is a thin line that separates permissible and impermissible tax avoidance. The distinction has been regarded as complex,²² but not always. Permissible tax avoidance is concerned with the organisation of a taxpayer’s affairs so that they give rise to the minimum tax liability. The GAAR does not, however, apply to the aforementioned scenario because the taxpayer’s main purpose would not be to obtain any tax benefit.

These new provisions apply only to transactions entered into or after 2 November, 2006.

df; at 25.

¹⁹ SARS. (2005). Discussion paper on Income Tax Act, 58 of 1962, November 2005.

²⁰ Drummond, B. (2006). A purposive approach to the drafting of tax legislation. *British Tax Review*. Available at <http://0-international.westlaw.com.innopac.up.ac.za>, at 10.

²¹ *Ibid*.

²² *Regina v Inland Revenue Commissioners ex parte Matrix-Securities Ltd* [1994] 1 WLR 334.

1.1. Research questions

The following are the research questions:

- Is the GAAR an effective deterrent against abuse of the tax system?
- Does the new GAAR²³ materially alter the position which existed under its predecessor, s103?
- Can the current GAAR be considered the ultimate anti-avoidance rule in South African fiscal laws or can one expect another GAAR?

1.2. Research objectives

The essence of this research topic is to test the feasibility of the current GAAR, compare it with other anti-avoidance rules in Canada, Australia and the United Kingdom, and highlight the prospects of its long-term success in the fiscal arena.

It seems that the GAAR is operating in a blast furnace because history shows us that some GAARs were doomed from the start, and others are just ticking time bombs. In Australia, the government decided to replace an existing GAAR, s260 of the ITAA, with part IVA of the ITAA, effective from 27 May 1981.²⁴ This is because s260 had proven to be ineffective in combating tax avoidance.

This is just one example of a failed GAAR; another is our own s103.²⁵ In this research I intend to highlight the possible lifespan of the South African GAAR in comparison with other GAARs in foreign jurisdictions which have been altered from time to time.

²³ As contained in sections 80A – L, Income Tax Act, 58 of 1962.

²⁴ Australian Income Tax Assessment Act, 1936 (Cth).

²⁵ Income Tax Act, 58 of 1962.

1.3. Scope of study

This research involves a critical analysis of the GAAR in the context of the South African Income Tax Act. I will also focus on foreign jurisdictions²⁶ whose tax legislation contains GAAR and compare the similarities and differences with the South African GAAR. I will critically analyse the Canadian GAAR²⁷ and the Australian GAAR.²⁸

1.4. Proposed methodology

The approach in this study will be analytical and comparative. I will employ the analytical approach by highlighting an overview and history of the GAAR in South African law, and also highlight the differences between permissible and impermissible tax avoidance.

A comparative approach will be employed, first of all by comparing the GAAR, as it is contained in s80,²⁹ with its predecessor in s103,³⁰ in an attempt to show the differences and similarities. I will also compare and contrast the South African GAAR with those of the United Kingdom and Australia.

1.5. Overview of chapters

Chapter 1: This chapter details the background to the problem, stating the research problem, the objectives of the research, and the scope of the study.

Chapter 2 comprises a general discussion of tax avoidance. I will identify and discuss

²⁶ Canadian and Australian.

²⁷ Subsection 245 (2) of the Canadian Income Tax Act.

²⁸ Part IV A of the Australian Income Tax Assessment Act, 1936 (Cth).

²⁹ Income Tax Act, 58 of 1962.

³⁰ *Ibid.*

the differences between permissible and impermissible tax avoidance schemes.

In Chapter 3 I will briefly examine the contents of s80 A – L of the Income Tax Act.³¹

Chapter 4 is a comparative analysis of the anti-avoidance techniques in South Africa with those of Australia, Canada and the USA.

Chapter 5 concludes this dissertation.

³¹ Income Tax Act, 58 of 1962.

CHAPTER 2. DISCUSSION OF TAX AVOIDANCE

2.1. Introduction

In this chapter I intend to engage in a general discussion of the concept of tax avoidance. It has been said that ‘the dynamics of tax avoidance are complex.’³² The analysis of this term is required in order to understand the challenges faced by tax policy makers in devising anti-avoidance techniques.

The discussion of tax avoidance often begins with an attempt to define and distinguish three broad concepts: 1) tax evasion, 2) impermissible tax avoidance, and 3) legitimate tax planning or ‘tax mitigation’.³³ SARS now clearly differentiates between legitimate tax planning at the one end of the scale and tax evasion at the other, with impermissible tax avoidance (which is the target of the GAAR) as the unacceptable category in-between.³⁴ In South Africa, however, there is no legal distinction between tax planning and tax avoidance.

The correct approach to tax avoidance, according to the SARS discussion paper on tax avoidance, is that implied by the extract from Practice Note No. 6 issued by the Commissioner for Inland Revenue on 1 April 1987 in connection with s105A of the Act:

‘A taxpayer who has carried out a legitimate tax avoidance scheme, i.e. who has arranged his affairs so as to minimise his tax liability, in a manner which does not involve fraud dishonesty, misrepresentation or other actions designed to mislead the Commissioner, will have met his duties and obligations under the Act if he fully and honestly completes his income tax return and fully and honestly answers any queries raised by the Commissioner.’

³² Bendel, E. (2006). Tax avoidance-is the party over? *Without Prejudice*, at 21.

³³ SARS Discussion paper on tax avoidance and section 103 of the Income Tax Act (Act No. 58 of 1962), Nov. 2005.

³⁴ SARS Draft comprehensive guide to the general anti-avoidance rule, at 2.

In practice, however, the lines between legitimate tax planning and tax avoidance are not always discernible.³⁵ SARS has also highlighted that the boundary lines between tax planning, tax avoidance and tax evasion are not always clear or constant, and are often left for the courts to categorise and define within their unique context.³⁶ However, 'the boundaries or guidelines established in the courts of law are bound to shift with the passing of time and changing social, legal and economic circumstances'.³⁷ This will result in uncertainty as to what can be regarded as tax avoidance.

I shall discuss the abovementioned concepts to highlight the broad distinction.

2.2. Tax planning

Tax planning is where the taxpayer takes advantage of a fiscally attractive option offered to him by the legislation and genuinely suffers the economic consequences that Parliament intended to be suffered by those taking advantage of the option.³⁸

In order to understand what tax planning entails, an analysis of what the courts regard and interpret it to be will be highlighted. The goal of the government is to balance legitimate commercial transactions against the need to combat tax avoidance arrangements.

³⁵ Wiese, I. (2006). Let the games (or pain?) begin. *Without Prejudice*, at 32.

³⁶ SARS Discussion paper on tax avoidance and section 103 of the Income Tax Act (Act No. 58 of 1962), Nov. 2005, at 5.

³⁷ Evans, C. (2007). *Barriers to avoidance: recent legislative and judicial developments in common law jurisdictions*. [Online] Available from:
<http://lawbepress.com.cgi/viewcontent.cgi?article=1014&context=unswwps>.

³⁸ CIR v Willoughby.

'Tax planning' is concerned with the organisation of a taxpayer's affairs (or the structuring of transactions) so that they give rise to the minimum tax liability within the law without resort to the sort of 'impermissible tax avoidance'.³⁹

Stiglitz⁴⁰ regards effective and acceptable tax planning as,

'... postponing taxes from the current period into future periods, arbitraging across different income streams facing different tax treatment (referred to as source based arbitrage), and transferring income from higher tax brackets to lower tax brackets (or rat-based arbitrage).⁴¹

The term tax mitigation has also been used,⁴² which is similar to tax planning. Tax planning is generally recognised as the legitimate and legal process of protecting one's property from unnecessary erosion by taxation. It has been said that 'legitimate tax planning is an essential feature of modern business life'.⁴³ Old United Kingdom (UK) case law is often referred to as authority for the notion that a South African taxpayer may arrange his or her tax matters in the most tax-efficient manner.⁴⁴ In *IRC v Duke of Westminster*⁴⁵ it was cited that:

'Every man is entitled if he can to order his affairs so that the tax attaching under the appropriate Acts is less than it otherwise would be. If he succeeds in ordering them so as to secure this result, then, however unappreciative the Commissioners of Inland Revenue or his fellow taxpayers may be of his

³⁹ SARS Discussion paper on tax avoidance and section 103 of the Income Tax Act (Act No. 58 of 1962), Nov. 2005.

⁴⁰ Stiglitz, J.E. (1985). The General Theory of Tax Avoidance. *National Tax Journal*, 38 at 325, 337.

⁴¹ *Ibid.*

⁴² By Lord Templeman in *CIR v Challenge Corporation* (1987) AC 155, 'Income tax is mitigated by a taxpayer who reduces his income or incurs expenditure'.

⁴³ SARS. (2006). Tax Avoidance and Section 103 of the Income Tax Act, 1962: An Interim response (2006) 31-2, quoting a submission by KPMG, at 31.

⁴⁴ SARS Draft comprehensive guide, at 2.

⁴⁵ (1936) A.C 1 (HL).

*ingenuity, he cannot be compelled to pay an increased tax.*⁴⁶

SARS cautions that the right of taxpayers to minimise their tax affairs should be balanced against the role of taxation in modern society; namely, to secure the well-being of its citizens.⁴⁷

Also, in this regard, in *CIR v King*,⁴⁸ a taxpayer's freedom to structure his or her affairs so that they give rise to the minimum tax liability within the law without resorting to some sort of 'impermissible tax avoidance' was highlighted:

*'In a wide sense also the amount of a man's income tax can be reduced from what it was in previous years if he earns less income than in the previous years, but here again it is absurd to suppose that the legislature intended to impose a penalty upon a man who enters into a transaction which reduces the amount of his income from what it was in the previous years merely because his purpose was to reduce the amount of his income and consequently his tax. These two types of cases may be uncommon but there are many other ordinary and legitimate transactions and operations which, if a taxpayer carries them out, would have the effect of reducing the amount of his income to something less than it was in the past, or freeing himself from taxation of some part of his future income.'*⁴⁹

A more balanced approach to tax avoidance emerges from the 1983 decision of the Zimbabwean High Court in *R Ltd and K Ltd v COT*:⁵⁰

⁴⁶ (1936) 19 TC 40 at 520.

⁴⁷ SARS. (2005), at 15.

⁴⁸ 1947 2 SA 196 (A).

⁴⁹ *Ibid.*

⁵⁰ 38 SATC 70.

'Can it then be regarded as attracting a penalty for a taxpayer to avail himself of the assistance which the Act specifically allows him? In other words, is it avoidance of tax to arrange one's affairs in a way that will allow one to use an assessed loss as contemplated by the Act? I do not think that can possibly be so'.

It has always been a trite principle that business is entitled to order its affairs in such a way as to legitimately minimise the tax burden which it is legally required to bear. Legitimate tax savings are not hidden under mattresses, they are reinvested by businesses and put to work in profitable ways or returned to providers for capital who are an essential component necessary for the growth of our developing economy.⁵¹ 'The interest of the fiscus is only one side of the equation, on the other side are the interests of business. These two interests must not be seen as being in opposition.'⁵²

Even where tax avoidance is regarded as falling within the permissible limits of the law, the conduct itself may sometimes be viewed as immoral or otherwise unacceptable behaviour.

2.3. Tax avoidance

Lord Templeman offered the following definition in the Challenge Corporation⁵³ case:

'Income Tax is avoided and a tax advantage is derived from an arrangement when the taxpayer reduces his liability to tax without involving him in the loss or expenditure which entitles him to that reduction. The taxpayer engaged in tax avoidance does not reduce his income or suffer a loss or incur expenditure but nevertheless obtains a reduction in his liability to tax as if he had.'

⁵¹ Gad, R. (2005). Tax avoidance- another view, same conclusion. *Without Prejudice*.

⁵² *Ibid*.

⁵³ Challenge Corporation Ltd v Commissioner of Inland Revenue [1987] AC 155.

Tax avoidance involves using legitimate means and methods to structure one's affairs to pay less tax.⁵⁴ It has been described as the result of a never-ending struggle between the principles of legal certainty on the one hand, and the right to freedom of business activity on the other; that is, between the legal form of the business operation and the underlying motive of the taxpayer.⁵⁵

Impermissible tax avoidance has been a growing problem internationally during the past 10 years and Australia has repeatedly expressed concerns over tax avoidance and evasion.⁵⁶ The courts have often expressed their disapproval of the practice:

*'Tax avoidance is an evil, but it would be the beginning of much greater evils if the courts were to overstretch the language of the statute in order to subject to taxation people of whom they disapproved.'*⁵⁷

Before the inception of the GAAR, an impermissible avoidance arrangement was referred to as including,

*'... artificial or contrived arrangements, with little or no actual economic impact upon the taxpayer, that are usually designed to manipulate or exploit perceived 'loopholes' in the tax laws in order to achieve results that conflict with or defeat the intention of Parliament.'*⁵⁸

⁵⁴ Oguttu, A. (2007). *Curbing offshore tax avoidance: the case of South African companies and trusts*. Available at <http://0.uir.unisa.ac.za.innopac.up.ac.za/dspace/bidstream/10500/1929/1/thesis/pdf>.

⁵⁵ Gregg, M. (2008). *Avoidance and abus de droit: The European Approach in Tax Law*. Available at <http://www.austlii.edu.au/au/journals/eJTR/2008/2.html>, at 23.

⁵⁶ *Ibid.*

⁵⁷ *Vestey's (Lord) Executors & Another v Inland Revenue Commissioners* (1949). 1 AER, 1108 at 1120.

⁵⁸ SARS. (2006). *Tax Avoidance and Section 103 of the Income Tax Act, 1962: An Interim Response*.

The term certainly includes, but is not limited to, arrangements that embody the common characteristics of the abusive schemes discussed in the paper.⁵⁹ The term has also been described as,

*'... an attempt to defer or eliminate a potential liability by manipulating or exploiting perceived inconsistencies or discontinuities in the tax system through various tax arbitrage techniques'.*⁶⁰

Impermissible tax avoidance involves four basic goals:

- The deferral of a tax liability;
- The conversion of the character of an item (for example, from revenue to capital or, in more aggressive products, the conversion of a taxable item such as interest to an exempt one such as dividends);
- The permanent elimination of a tax liability; and
- The shifting of income (e.g. from a taxpayer subject to the highest marginal rates to taxpayer subject to a lower (or zero) rate of tax.

Impermissible avoidance arrangements are now statutorily defined as being solely and mainly tax driven, and being typically characterised by any one or more of the following in a business context:⁶¹

- A lack of commercial substance;

⁵⁹ SARS. (2006). Tax Avoidance and Section 103 of the Income Tax Act, 1962: An Interim Response.

⁶⁰ SARS Discussion paper, at 19.

⁶¹ S 80A.

- Abnormal features in terms of the manner entered into or carried out;
- Non-arms length rights or obligations;
- The misuse or abuse of the provisions of the Income Tax Act.

SARS, in the discussion paper,⁶² summarised the hallmarks of impermissible avoidance activity which include all or any of the following:

- The use of tax indifferent accommodating parties or special purpose entities;
- True nature of a scheme disguised in an overlay complex scheme or transaction;
- High transaction costs;
- Fee variation clauses or contingent fee provisions;
- Inconsistent treatment for tax and accounting purposes;
- Use of complex derivatives, hybrids and synthetic instruments which mimic traditional financial instruments, such as shares or debt without incurring the concomitant tax consequences; and
- The use of tax havens.

2.4. Problems caused by tax avoidance

One of the problems caused by tax avoidance is the negative effect on revenue

⁶² SARS Law Administration (2005). Discussion paper on tax avoidance and section 103 of the Income Tax Act 58 of 1962.

collections, resulting in short-term revenue loss.⁶³ Decreased tax revenues, as a result of tax avoidance, will result in failure to achieve the fiscal budget which is necessary for the discharge of governmental functions, whose purpose it is to work towards securing the economic and social well being of all its citizens. It weakens the ability of Parliament and National Treasury to set and implement economic policy.

Avoidance schemes seem to only be at the disposal of the rich, due to their expensive nature, therefore it results in unfairness in the tax system. This results in taxpayers being taxed at different rates on the same economic activity.⁶⁴ This perceived unfairness in the tax system may tend to discourage compliance among taxpayers who had previously not participated in tax avoidance activity.⁶⁵

2.5. Tax evasion

Tax evasion, an illegal offence resulting in severe penalties and possible imprisonment, involves the usage of fraud or deceit to reduce a tax liability through the non-disclosure of income and overstating deductions.⁶⁶ It has also been referred to as 'illegal arrangements through or by means of which liability to tax is hidden or ignored.'⁶⁷ Ulph⁶⁸ defines tax evasion as the '...deliberate concealment or misrepresentation of the taxpayers' affairs and the certain knowledge that this is illegal..

⁶³ *Ibid.*

⁶⁴ Ulph, D. (2009). *Avoidance policies: a new conceptual framework*. Oxford University Centre for Business Taxation, WP 09/22. Available from http://www.sbs.ox.ac.uk/centeres/tax/Documents/working_papers WP0922/.

⁶⁵ SARS Law Administration (2005). Discussion paper on tax avoidance and section 103 of the Income Tax Act 58 of 1962, at 10.

⁶⁶ Hauxham, K & Haupt, P. (2007). Notes on South African Income Tax. Cape Town: Hedron, at 350.

⁶⁷ OECD. International Tax Terms for the participants in the OECD Programme of Cooperation with Non-OECD Economies.

⁶⁸ Ulph, D. (2009). *Avoidance policies: a new conceptual framework*. Available from http://www.sbs.ox.ac.uk/centeres/tax/Documents/working_papers, at 5.

Examples of tax evasion include:

- Falsifying of financial statements;
- Not disclosing or misrepresenting relevant information in a tax return;
- Deliberate failure by a cash business to report the full amount of revenue received.⁶⁹

Taxpayers found guilty of tax evasion would face penalties as prescribed in the Income Tax Act⁷⁰ and possible imprisonment. In common law, the difference between tax avoidance and tax evasion is illustrated in *R v Mears*,⁷¹ where Gleeson CJ noted:

*'... the difference between the two is simple and clear. Tax avoidance involves using or attempting to use lawful means to reduce tax obligations. Tax evasion involves using unlawful means to escape payment of tax. Tax avoidance is lawful and tax evasion is unlawful.'*⁷²

⁶⁹ SARS Law Administration (2005). Discussion paper on tax avoidance and section 103 of the Income Tax Act 58 of 1962.

⁷⁰ Act 58 of 1962.

⁷¹ (1997) 37 ATR 321.

⁷² *Ibid.*

CHAPTER 3. OVERVIEW AND ANALYSIS OF SOUTH AFRICAN GAAR

3.1. Introduction

With the need to balance legitimate commercial transactions against the need to combat tax avoidance arrangements came the insertion of general anti-avoidance rules in tax legislation in order to monitor commercial transactions that have the possibility to frustrate the tax policies of governments.

In this chapter I intend to provide an overview of and critically analyse each of the relevant elements of the South African General Anti-avoidance Rule as it is contained in s80 A-L. The now repealed s103 (1) consisted of one section, whereas the new GAAR comprises 12 new sections, thus rendering it very broad in scope.

The new GAAR has been described as difficult enough to perplex even the most impressive minds.⁷³ Due to the complexity of the new GAAR, there is also the possibility that it may be restrictively interpreted by the courts, thus not giving the new GAAR its intended effect.⁷⁴ It has also been observed that the new GAAR has added to the complexity of the already over-burdened South African tax system.⁷⁵

3.2. Requirements

In order for the new GAAR to apply, four requirements have to be met:

⁷³ Drummond, B. (2006). A purposive approach to the drafting of tax legislation'. *British Tax Review* 6:669-676. Available at <http://international.westlaw.com.innopac.up.ac.za>.

⁷⁴ *Ibid.*

⁷⁵ *Ibid.*

1. There must be an avoidance arrangement.⁷⁶
2. The avoidance arrangement must have been entered into on or after 2nd November 2006.⁷⁷
3. The sole or main purpose of the taxpayer in entering into an avoidance arrangement must be to obtain a tax benefit.⁷⁸
4. The arrangement must include an abnormality element. The approach to determine abnormality is three fold and can be classified as a 'business context'⁷⁹ test, a 'non business context'⁸⁰ test and the 'any context'⁸¹ approach test. The predecessor to Part II A, subsection 103 (1), also included an abnormality test, but this was confined to business transactions. This abnormality test had, however, proven to be insufficient on its own to combat what might be viewed as blatant avoidance arrangements. Promoters of tax schemes commonly 'hijacked' features of legitimate normal commercial transactions to disguise their schemes.⁸² Promoters gave their tax avoidance schemes an aura of normality that would not be attacked under s103.⁸³

Under s80, the tainted elements that must be present in the arrangement will either be in a business context or in any other context. The avoidance arrangement will be impermissible in the business context if:

⁷⁶ S 80A (preamble).

⁷⁷ S 80 A (preamble).

⁷⁸ S 80 A(preamble).

⁷⁹ S 80 A (a).

⁸⁰ S 80 A (b).

⁸¹ S 80 A (c).

⁸² SARS Tax Avoidance and Section 103 of the Income Tax Act, 1962: Revised Proposals (2006) 16.

⁸³ *Ibid.*

- It was entered into or carried out in a manner which would not normally be employed for bona fide business purposes.⁸⁴
- It lacks commercial substance.⁸⁵

It will be impermissible in a context other than business if:

- It was entered into or carried out by an abnormal means or manner, not used for a bona fide business purpose other than obtaining a tax benefit.⁸⁶

In any context if:

- It would result in the misuse or abuse of the provisions of the Income Tax Act.⁸⁷

The first component of the definition of an 'arrangement' makes reference to a transaction, operation or scheme.

3.3. Avoidance arrangement

The Act defines an arrangement as:

*'Any transaction, operation, scheme, agreement or understanding (whether enforceable or not) including all steps therein or parts thereof, and includes any of the foregoing involving the alienation of property.'*⁸⁸

⁸⁴ S 80 A (a) (i).

⁸⁵ S 80 A (a) (ii).

⁸⁶ S 80 A (b).

⁸⁷ S 80 A (c) (ii).

⁸⁸ S 80 L definitions.

But, points out Price Waterhouse Coopers (PWC),⁸⁹ for all the detail in the new legislation, key concepts remain unclear. What, for example, does the word ‘arrangement’ mean? And asks PWC, can the new anti-avoidance provisions be applied where there was a tax avoidance ‘arrangement’ but the taxpayer was not a party to that arrangement.⁹⁰ The term ‘any’ indicates a wide application to arrangements that may be seemingly undertaken to avoid tax.

An ‘arrangement’ has been interpreted as requiring a conscious involvement of two or more participants who arrive at an understanding. It cannot exist in a vacuum and presupposes a meeting of minds, which embodies an expectation as to future conduct between the parties; that is, an expectation by each that the other will act in a particular way.⁹¹ On appeal it was held that an ‘arrangement’ did not require a meeting of minds, and it was therefore irrelevant that the taxpayer did not know about the dishonest inflating of the cost of the film.

3.3.1 *Transaction, operation, scheme, agreement or understanding*

The inclusion of this wide range of terms seems to be an attempt by the legislature to barricade almost all forms of arrangements. These same components were contained in the old GAAR, i.e. s103 (1).

- ‘Transaction’ can be defined as ‘the action of conducting business’.⁹²
- An ‘operation’ is ‘an organised activity involving a number of people’.⁹³

⁸⁹ Thersby, K. (2007). Exactly what is a tax avoidance arrangement? *Moneyweb’s Tax Breaks*, at 6.

⁹⁰ *Ibid.*

⁹¹ FCT v Newton (1958) 2 All ER 759 (PC).

⁹² Concise Oxford Dictionary.

⁹³ *Ibid.*

- A 'scheme' is considered as 'a large-scale systematic plan or arrangement for attaining some particular object or putting a particular idea into effect'.⁹⁴

It was said in *Meyerowitz v CIR*⁹⁵ that 'the word scheme is a wide term and I think that there can be little doubt that it is sufficiently wide to cover a series of transactions ...'. In *CIR v Louw*⁹⁶ it was held that 'scheme is wide enough to cover situations in which later steps in a course of action were left unresolved at the outset'.

Agreement and understanding basically connote the same meaning. One would presume that these newly inserted terms were borrowed from the Australian GAAR because in terms of s177(1) of the Australian Income Tax Act, the term 'scheme' includes the term 'agreement' and 'understanding', whether enforceable or not.

The term 'understanding' has not been defined in the Act but literally it means any gentleman's agreement, letter of wishes, or a verbal understanding. The SARS comprehensive guide to the GAAR⁹⁷ lists agreements which are not legally enforceable but which are considered as arrangements, viz.:

- An agreement between parties to agree in future on 'reasonable terms and condition' to effect a merger.
- The so-called gentleman's agreement 'heads of agreement' between parties which set out the intended result the parties wish to achieve but which is not necessarily legally binding at the time.
- An agreement binding in honour only in conscience, letter of intent and the like.

⁹⁴ *Ibid.*

⁹⁵ 1963 (3) SA 863 (A): 25 SATC 287 at 298.

⁹⁶ 1983 (3) SA 551 (A):45 SATC 113.

⁹⁷ SARS Guide to the GAAR.

An agreement may be reduced to writing or it may be an oral agreement, or merely an oral understanding.⁹⁸ In *Woods v Watters*⁹⁹ it was stated, ‘The broad rule is that writing is not essential to the validity of a contract. The consensus of the parties need not be so evidenced.’ Verbal agreements or understandings are difficult to prove and the Commissioner may find it difficult to identify a comprehensive listing of all the steps or parts of a verbal understanding to attack an assessment utilising the provisions of the GAAR.

The inclusion of the terms ‘whether enforceable or not’ leaves a lot to be desired. It seems to create uncertainty. Why would the GAAR be applied to an unenforceable agreement? My submission is that the Commissioner either has to justify the inclusion of such terms by issuing an Interpretation Note, or the terms could be deleted from the definition.

Also included in the definition of an arrangement is ‘alienation of property’. The reason for arrangements involving the alienation of property being explicitly included within the definition of arrangement is partly to counter the effect of the King judgement, and partly to cover the high prevalence of property-related transactions involving tax aggressive techniques.¹⁰⁰ The Explanatory Memorandum on the Income Tax Bill 1959 relating to s90 of the old Income Tax Act provided that the term ‘alienation of property’ is covered by the term ‘transaction’.¹⁰¹

3.3.2 An arrangement includes all steps or parts therein

The definition of an arrangement includes ‘all steps therein or parts thereof’. This deems all steps or parts of an arrangement to be an avoidance arrangement if they

⁹⁸ SARS Guide to the GAAR.

⁹⁹ 1921 AD 303.

¹⁰⁰ SARS Guide to the GAAR.

¹⁰¹ Mazansky, E, (2006). A new GAAR for South Africa-The Duke of Westminster is Struck a Blow. *Bulletin for International Fiscal Documentation*, 59, 3 at 125.

result in a tax benefit. This provision was non-existent before the emergence of the new GAAR. On one hand this section is useful to the taxpayer because it forces the Commissioner to formally disclose exactly which aspects of the arrangement he is attacking,¹⁰² but on the other hand, it would mean that the taxpayer will be uncertain as to which aspects of the arrangement exactly are prone to attack.

It was previously ruled in *CIR v Conhage*¹⁰³ that ‘the courts would look at the whole of the transaction as opposed to reviewing its individual steps to ascertain if tax avoidance has taken place’. This disposition would therefore render the previous disposition established in this case desolate.

Section 80H reiterates that the Commissioner may apply the GAAR to steps in or parts of an arrangement, and, s80G(2) provides that the purpose of a step or part of an avoidance arrangement may be different from a purpose attributable to the avoidance arrangement as a whole.

The purpose of enabling the Commissioner to apply the GAAR provisions to any step or part of an arrangement, which in itself then constitutes the avoidance arrangement, is to overcome the established case law that s103(1) did not apply where the taxpayer could show that the overriding reason for entering into a composite arrangement was a non-tax reason.¹⁰⁴

This provision meets with criticism. It is my submission that if the GAAR is applied in isolation to individual steps within an agreement, there is likely to be confusion because an arrangement as a whole is intertwined. How consistently can the GAAR be applied to individual steps?

¹⁰² Broomberg, E.B. (2007). Then and Now II. *Tax Planning Corporate and Personal*, 21.

¹⁰³ 1999 (4) SA 1149 SCA, 61 SATC 391.

¹⁰⁴ SARS Draft comprehensive guide.

Broomberg¹⁰⁵ submits that ‘the new arrangement definition does not address problems that have arisen in the jurisdictions from which the wording of this new definition was borrowed’. He questions whether the Commissioner could apply the GAAR to a step or part in an arrangement where it loses its commercial substance as a result of being considered in isolation, and concludes that the answer to such question will have to await consideration in court.¹⁰⁶

It is my submission that the inclusion of ‘steps and parts’ in the definition of an ‘arrangement’ is not required and the position as it was before should still prevail.

3.3.3 *Sole/main purpose*

Part II A of the Act contains the purpose requirement in s80A and G. According to Meyerowitz, ‘a purpose arrangement is essential to any general anti-avoidance rule’.¹⁰⁷

In terms of s80A, ‘an avoidance arrangement is an impermissible avoidance arrangement if its sole or main purpose was to obtain a tax benefit’. The section refers to the purpose of an arrangement, as opposed to s103(1) (c) which referred to the purpose for which a transaction, operation or scheme was entered into or carried out.

In s80 G (1) lies a rebuttable presumption, in that an avoidance arrangement is presumed to have been entered into or carried out for the sole or main purpose of obtaining a tax benefit unless and until the party obtaining the tax benefit proves that, reasonably considered in the light of the relevant acts and circumstances, obtaining a tax benefit was not the sole or main purpose of the avoidance arrangement.

The tests under s80A and 80G are, respectively, ‘its sole or main purpose’ and ‘the sole or main purpose’.

¹⁰⁵ Broomberg, E.B. (2007). Then and Now-II. *Tax Planning Corporate and Personal*, 21.

¹⁰⁶ *Ibid.*

¹⁰⁷ Meyerowitz, D. (2005). What is tax avoidance? *The Taxpayer*, 205.

This requires the identification of a singular purpose, rather than one of a number of purposes.¹⁰⁸ Thus, it is significant that the legislation requires the ascertainment of ‘the’ rather than ‘a’ sole or main purpose.¹⁰⁹ Brinker¹¹⁰ reiterated that, ‘While a purpose may still be ‘a’ main purpose even though another purpose is more important, to be ‘the’ purpose it must supersede any other purpose.’

De Koker¹¹¹ submits that,

‘... to discharge the section 80G onus, a taxpayer is required to give affirmative evidence that satisfies a court, upon a preponderance of probability, that ‘reasonably considered in light of the relevant facts and circumstances’, the obtaining of the tax benefit was not the sole or main purpose.’

The purpose requirement also existed under the repealed s103, but of course not without flaws. It was originally proposed that the requirement would be the sole or ‘one of the main purposes’.¹¹² This was criticised, as it would potentially make it too easy for the GAAR to apply to legitimate business transactions that may have an insignificant tax-planning element.¹¹³

Under this section, the purpose of a scheme was established from the taxpayer’s *ipse dixit* which is a subjective inquiry. The intention of the taxpayer was weighed against the probabilities and inferences drawn from the surrounding circumstances and established facts.

¹⁰⁸ Cassidy, J. (2009). The Holy Grail: The search for the optimal GAAR. *South African Law Journal*, vol. 126, issue 4740, at 765.

¹⁰⁹ *Ibid.*

¹¹⁰ Brinker, E. (2001). The purpose requirement of the general anti-avoidance provision in South African fiscal law. *TSAR*, 158 at 164.

¹¹¹ De Koker, A.P. (2009). *Silke on South African Income Tax*. Durban: Lexus Nexus.

¹¹² The originally proposed section 103 (1) (a).

¹¹³ Ensor, L. & Tempkins, S. (2005). *SARS unveil plan to combat tax avoidance*. Business Day, 4 November at 2.

SARS listed the problems surrounding the purpose requirement under s103 (1) in the Discussion Paper on Tax Avoidance and Section 103 of the Income Tax Act No. 58 of 1962.

These problems are:

- The Commissioner is placed in the difficult position of having to disprove a taxpayer's allegations through circumstantial evidence since most transactions in a business context have at least a colourable commercial rationale;
- Taxpayers have frequently argued that a commercial purpose, such as raising capital, for an overall transaction is sufficient to 'inoculate' each and every step in it from challenge; and
- The purpose requirement entails a subjective test – it looks to the purpose the taxpayers purportedly intended to achieve when they carried out their scheme.

In light of these observations, SARS therefore proposed that the purpose requirement be amended to reflect an objective inquiry in accordance with the practice in other countries. Whether the new wording of the purpose requirement is clear enough to indicate that it now requires an objective enquiry, and not a subjective inquiry, as in s103 (1) is unsure.¹¹⁴

SARS indicated that the proposed amendments would change the purpose requirement to an objective test. In particular, the proposed arrangements would require the determination to be made objectively by reference to the relevant facts and circumstances.¹¹⁵

¹¹⁴ Van Schalkwyk, L. & Geldenhuys, B. (2010). The nature of the purpose requirement of an impermissible tax avoidance arrangement. *Journal for Juridical Science*, vol. 35 (1) at 72.

¹¹⁵ SARS Law Administration (2005). Discussion paper on tax avoidance and section 103 of the

In spite of this, SARS however, confirmed that it was never the intention of the original proposals to prevent a taxpayer's explanation of the reasons for an arrangement from being taken into account.

Rather, it was intended to ensure that a taxpayer's statements of intent be rigorously tested against the relevant facts and circumstances.¹¹⁶

Below is a synopsis of some of the judgements where the purpose requirement was considered, and in most of them it was found that a subjective inquiry should be considered in assessing the purpose of a transaction.

In *SIR v Geustyn, Forsyth and Joubert*¹¹⁷, Geustyn, Forsyth and Joubert all of whom were qualified civil engineers and members of the South African Association of Consulting Engineers, had practiced in partnership as consulting engineers. They formed an unlimited liability company in 1966 which bought the company for a goodwill consideration of R240 000, determined on the basis of an aggregate of three years profits. The partners were each employed by the company at an annual salary of R10 000. The Commissioner invoked s103(1) and taxed the profits of the company in the hands of the three partners. Ogilvie Thompson CJ stated with regard to the purpose requirement that:

'... while it may be that effect and result as respectively used in subsections (1) and (4) of section 103 of the Act have the same meaning it is clear that the former subsection distinguished between 'effect' and 'purpose'. The vital inquiry on this part of the case relates to the question of whether or not avoidance postponement or reduction of tax was 'the sole or one of the main purposes' of the conversion of the partnership into a company.

Income Tax Act 58 of 1962.

¹¹⁶ SARS Law Administration (2005). Discussion paper on tax avoidance and section 103 of the Income Tax Act 58 of 1962.

¹¹⁷ 33 SATC 113.

The intention or purpose with which any particular transaction is entered into is a question of fact...'

He also made a distinction between the words 'effect' and 'purpose'.

A rebuttable presumption is contained in s80G that the avoidance has been entered into or carried out solely or mainly to obtain a tax benefit. Therefore if a tax benefit is present, there is an immediate presumption that its sole or main purpose was to obtain a tax benefit.

Meyerowitz¹¹⁸ suggests that it would be logically impossible for a taxpayer to prove an objective purpose when at the same time the purpose is already presumed. The purpose requirement under s103 deviates from the new GAAR in the sense that the purpose of a transaction, operation or scheme was determined by applying a subjective test.

In *SIR v Gallagher* this principle was confirmed by Corbett JA. In his judgment, he held the following:

*'It is submitted in the heads of argument of appellant's counsel that in determining the purpose of a transaction, operation or scheme an 'objective' test should be applied. By an objective test in this context is evidently meant a test which has regard rather to the effect of the scheme, objectively viewed, as opposed to a 'subjective test' which takes as its criterion the purpose which those carrying out the scheme intend to achieve by means of the scheme... In the circumstances it is appropriate to state that, in my view, the test is undoubtedly a subjective one.'*¹¹⁹

¹¹⁸ Meyerowitz, D. (2005). What is tax avoidance? *The Taxpayer*, 205.

¹¹⁹ 1978(2) SA 463(A), 40 SATC 39.

Section 103 (1) draws a clear distinction between the effect of a scheme and the purpose thereof, and this virtually rules out an interpretation which seeks to give purpose an objective connotation and to equate it, more or less, to 'effect'. If the subjective approach be adopted (as it must), then it is obvious that of prime importance in determining the purpose of the scheme would be the evidence of respondent, i.e. the progenitor of the scheme, as to why it was carried out.

The new GAAR implements an objective approach to determine the existence of a tax benefit. Section 80A states that an avoidance arrangement is impermissible if its sole or main purpose was to obtain a tax benefit. So the focus under the new GAAR is on the purpose of the arrangement itself, not on the purpose of the individual.

A more objective approach was required to deviate from the subjective approach under s103. Therefore in *RC Williams*¹²⁰ it was noted that:

'In essence a taxpayer could with impunity enter into a transaction with the (subjectively) sole or main purpose of avoiding tax provided that there was no (objective) abnormality in the means or manner in the rights and obligations which is created. Conversely, a taxpayer could with impunity enter into a transaction which was objectively 'abnormal' provided that he did not, subjectively, have the sole or main purpose of tax avoidance.'

Broomberg¹²¹ elaborates that countries overseas have interpreted the legislation's purpose of an arrangement using an objective test. Broomberg is also unsure of where our law now stands with regards to the purpose requirement, but submits that the wording in s80G (1) suggests that an objective inquiry might be required.¹²²

¹²⁰ Williams, R.C. (1997). The 1996 amendments to the General Anti-Avoidance Section of the Income Tax Act. *SALJ*, vol, 114, 675.

¹²¹ Broomberg, E.B. (2007). *The new general anti-avoidance rule*. SAFA seminar, Cape Town.

¹²² *Ibid.*

There is no unanimous opinion amongst tax scholars regarding the test that should be applied under the purpose requirement. They vary between a subjective approach which takes into consideration the intention of the taxpayer, and an objective approach which does not consider the *ipse dixit* of the taxpayer.

Clegg and Stretch¹²³ advocate for an objective approach; they argue that the courts will, despite the changes to the purpose requirement, take an objective view of the facts and circumstances which include the *ipse dixit* of the taxpayer ‘in order to determine the purpose of the taxpayer.’

In the same line of thought is De Koker¹²⁴ who suggests that ‘section 80A refers to the purpose of the arrangement, and not of the taxpayer. The purpose as used in s80A of the Act is used in the sense of the ‘effect’ (objective enquiry) of the arrangement and not the intention (subjective enquiry) with which the arrangement was entered into by the taxpayer.’¹²⁵

Broomberg¹²⁶ also happens to be a proponent of the objective approach, and shares a similar approach with De Koker¹²⁷ in that s80A refers to the purpose of the arrangement. He also states that the phrase ‘the sole or main purpose’ in s80G has compelled the courts abroad to conclude that the test of purpose was objective.¹²⁸

Louw¹²⁹ argues that ‘the change in wording indicates that when applying the purpose requirement, regard must be had to the effect of the arrangement and not the purpose of the taxpayer’.

¹²³ Clegg, D. & Stretch, B. (2010). *Income Tax in South Africa*, at par 26.3.4.

¹²⁴ Koker, D.E. (2010). *Silke on South African Income Tax*, at par 19.6.

¹²⁵ *Ibid.*

¹²⁶ Broomberg, E.B. (2007). *The new general anti-avoidance rule*. SAFA seminar, Cape Town.

¹²⁷ Koker, D.E. (2010). *Silke on South African Income Tax*, at par 19.6.

¹²⁸ Broomberg, E.B. (2007). *The new general anti-avoidance rule*. SAFA seminar, Cape Town.

¹²⁹ Louw, I.D.P. (2007). *The New General Anti-Avoidance rule: A comprehensive discourse on this statute*, at p24. Available at lawspace.law.uct.ac.za/dspace/bitstream/2165/357/.../LWXIZA001.pdf.

He notes that such a change could result in our courts having to apply an objective test when determining the ‘purpose’ and ascertain from the relevant facts and circumstances if tax avoidance was the sole or main purpose of the arrangement.¹³⁰

Of those that advocate for the subjective interpretation to the purpose requirement are *inter alia*, Meyerowitz¹³¹ who indicates that it would become a logical impossibility for the taxpayer to prove an objective purpose when the purpose is to be presumed. He¹³² also quoted the words of Lord Devlin in *Chandler v Director of Public Prosecutions*:

‘I shall begin by considering the word purpose, for both sides have relied on this word in different senses. Broadly the appellants contended that it is to be given a subjective meaning and the crown an objective one. I have no doubt that it is subjective. A purpose must exist in the mind. It cannot exist anywhere else.’

Davies *et al.*¹³³ suggest that ‘the test with regards to the purpose of an arrangement; is still subjective, and according to them, *SIR v Gallagher* is still authoritative. They argue that a taxpayer’s *ipse dixit* will still be evaluated, within the context of objective facts so as to arrive at a conclusion of the true purpose.¹³⁴ They argue that the sole or main purpose remains a subjective one, to be decided with reference to the actual purpose of the participants in the arrangement under consideration.¹³⁵ This is so despite the fact that s80A refers to ‘its’, that is the avoidance arrangement’s sole or main purpose as distinct from the purpose of the participants in that arrangement. An arrangement can never of itself have a purpose.¹³⁶

¹³⁰ *Ibid.*

¹³¹ Meyerowitz, D. (2005). What is tax avoidance? *The Taxpayer*, 205.

¹³² As cited by Meyerowitz, D. (2005). What is tax avoidance? *The Taxpayer*, 205.

¹³³ Davies *et al.* (2007). *Juta’s Income Tax*, at 80A-7. Durban: Butterworths.

¹³⁴ Davies *et al.* (2009). The sole or main purpose test-subjective or objective?’ *The Taxpayer*, October at 181.

¹³⁵ *Ibid.*

¹³⁶ *Ibid.*

Louw¹³⁷ submits that,

'In the event that the taxpayer faces two commercially acceptable choices yielding the same result but with different tax benefits, the scenario which allows him to pay the least amount of tax should not fall foul of the Act'.

In *SBI v Lourens Erasmus (Edms) Bpk*¹³⁸ the term 'main' was considered and it was held to connote or mean 'a quantitative measure of more than 50%'. Literarily speaking, 'solely' would mean the only purpose of the taxpayer.

In *CIR v King*¹³⁹ it was established that 'the taxpayer's dominant purpose needs to be established.'

It is the writer's submission that using both the terms, 'solely' and 'mainly' is redundant, therefore one of terms would suffice, that is, 'mainly'. The South African courts have held that the time for testing the sole or main purpose under s103 is not necessarily when the purpose is first formulated, but rather when the arrangement is implemented.¹⁴⁰ It is my contention that this approach should be utilised under Part II A.

3.3.4 Tax benefit

The sole or main purpose of the arrangement must be to obtain a tax benefit. According to the SARS Draft Comprehensive Guide to the GAAR,¹⁴¹ the 'tax benefit' requirement operates at three levels:

¹³⁷ Louw, I.D.P. (2007). *The New General Anti-Avoidance rule: A comprehensive discourse on this statute*, at p24.

¹³⁸ 1966 (4) SA 434 (A), 28 SATC 233.

¹³⁹ *CIR v King* 1947 (2) SA 196 A.

¹⁴⁰ *Ovenstone v SIR* (1980) (2) SA 721 (A).42 SATC 55.

¹⁴¹ SARS. (2010). Draft Comprehensive Guide to the GAAR. Available at www.sars.gov.za.

- i) Firstly before any arrangement is considered an ‘avoidance arrangement’ as defined in s80 L, it must be established that a tax benefit is derived.
- ii) Secondly, once the existence of an avoidance arrangement is established, this forms the basis for enquiring whether an impermissible avoidance arrangement exists. To this end it must be established that, amongst other things, deriving such tax benefit is the sole or main purpose of the arrangement.
- iii) Thirdly, in the case of an arrangement entered into or carried out in a business context, if the lack of commercial substance is an issue’

In terms of s80L, a tax benefit includes ‘any avoidance, postponement or reduction of any liability for tax’. The term ‘any’ is an indication that the term ‘liability’ has a very wide meaning.

‘The definition of ‘tax benefit’ reflects an appreciation that tax benefits stem not only from the non-declaring of assessable income or manufacturing of deductions, but also making use of any concessions that might be provided under the legislative tax framework.’¹⁴²

‘It also recognises that advantages may be conferred through a mere deferral of liability.’¹⁴³ There is no formal test to determine the existence of a tax benefit. A possible approach would be for the Commissioner to identify income that might have otherwise accrued to the tax planner.

In ITC 1625, the judgment held that a possible test would be to determine if the taxpayer would have incurred taxation but for the transaction. What a tax payer could have done, however, is subjective.

¹⁴² Cassidy, J. (2009). The Holy Grail: The search for the optimal GAAR. *South African Law Journal*, vol. 126, issue 4740, at 740 -755.

¹⁴³ *Ibid.*

It was decided in *FCT v Peabody*¹⁴⁴that:

‘A reasonable expectation requires more than a possibility. It involves a prediction as to events which would have taken place if the relevant scheme had not been entered into or carried out and the prediction must be sufficiently reliable for it to be regarded as reasonable.’

The Commissioner bears the onus to prove that on a balance of probabilities a tax benefit was derived as a result of an arrangement being entered into or carried out.

In terms of s80C(1), ‘... the general presumptive commercial substance test, requires that a significant tax benefit is derived’. The term ‘significant’ is not defined in the Act and therefore its ordinary meaning must prevail. The term ‘significant tax benefit’ essentially encompasses any tax benefit which draws attention, not just in terms of its quantum, but also one which is of sufficient importance to merit the attention of the Commissioner in applying the presumptive or general commercial substance test.

In general, the focus is not upon the magnitude of the tax benefit *vis-à-vis* the amount of a party’s gross or taxable income, but upon the magnitude of that tax benefit *vis-à-vis* the actual economic expenditure or loss incurred by the party that gave rise to the tax benefit in question.

3.3.5 Requirement 4: The arrangement must contain an abnormality element

The last requirement that must be satisfied before the GAAR is implemented is that the arrangement must be abnormal.

The existence of the abnormality test is examined on three levels in the Act:

¹⁴⁴ (1994) 94 ATC 4663 at 4670.

3.3.6 *In the context of business*¹⁴⁵

It was entered into or carried out by means or in a manner which would not normally be employed for *bona fide* business purposes, other than obtaining a tax benefit, or it lacks commercial substance in whole or in part, taking into account the provisions of s80C.¹⁴⁶

The business purpose test in terms of the GAAR is not whether the scheme itself has a commercial purpose, but whether the manner in which the transaction is entered into or carried out in a manner which would normally be used for *bona fide* business purposes other than to obtain a tax benefit.¹⁴⁷

The phrase '*bona fide* business purpose' needs to be carefully analysed to establish exactly what the Act entails. There is no definition of the term '*bona fide*' in the Act. The term '*bona fide*' probably bears the established judicial interpretation of 'good faith'.¹⁴⁸ Clegg¹⁴⁹ is of the view that the phrase means that a transaction must be real and not imaginary.

In ITC 1712,¹⁵⁰ the court accepted that the business purpose test encompasses a comparison between the transactions entered into versus a hypothetical enquiry of how the transaction should have taken place.

The terms 'business' and 'business context' have not been defined in the Act. The term 'business' has been included as part of the definition of the term 'trade' in s1 of

¹⁴⁵ S 80 A (a).

¹⁴⁶ S 80A (a) (i)-(ii).

¹⁴⁷ SARS. (2010). Draft Comprehensive Guide to the GAAR. Available at www.sars.gov.za, at p 24.

¹⁴⁸ Jarvis, J. (1996). Things are Seldom What They Scheme. *Juta's Business Law*, vol. 4 at 147-148

¹⁴⁹ Clegg, D. (2002). Business purpose test. *Tax Planning Corporate and Personal*, vol. 16.

¹⁵⁰ 63 SATC 499.

the Act, which is defined as including every profession, trade, business, employment, calling, occupation or venture, including the letting of any property and the use of or granting of permission to use certain other assets. This can be interpreted to mean that any 'business' is a 'trade' but a 'trade' is not necessarily a business.

In *Smith v Anderson*¹⁵¹ the court accepted that the word 'business' means anything which occupies the time and attention and labour of a man for the purpose of profit or improvement.

Beadle CJ in *Estate G v Commissioner of Taxes*¹⁵² was of the opinion that:

'The sensible approach, I think, is to look at the activities concerned as a whole, and then to ask the question: Are these the sort of activities which, in commercial life, would be regarded as carrying on business? The principal features of the activities which might be examined in order to determine this are their nature, their scope and magnitude, their object (whether to make a profit or not), the continuity of the activities concerned, if the acquisition of property is involved, the intention with which the property was acquired. This list of features does not purport to be exhaustive, nor is any one of these features necessarily decisive, nor is it possible to generalise and state which feature should carry most weight in determining the problem. Each case must depend on its own particular circumstances.'

The question as to whether a person is carrying on a business is a factual question. In *Modderfontein Deep Levels Ltd v Feinstein*,¹⁵³ Wessels J highlighted that,

¹⁵¹ (1880) 15 Chd 247 at 258.

¹⁵² 1964 (2) SA 701 SR, 26 SATC 168 at 173-174.

¹⁵³ 1920 TPD 288. 23.

'... to constitute a business there must either be a definite intention at the first act to carry on similar acts from time to time if opportunity offers , or the acts must be done not once or twice but successively with the intention of carrying it on , so long as it is thought desirable.'

'The factual character of the judicial doctrine of 'business purpose' is somewhat obscure. The wider statement of this rule is to the effect that if, in the context of business, an avoidance arrangement was entered into or carried out in a manner not normally employed for bona fide business purposes, it will be presumed that the avoidance of tax was the sole or one of the main purposes of the transaction. In other words, a transaction will not be given any effect for tax purposes unless it also achieves a valid business purpose.'

And saving of taxes alone is deemed not to constitute a valid business purpose'.¹⁵⁴

3.3.7 Commercial substance test

The commercial substance test contains two components:

- A general test,¹⁵⁵ and
- A list of indicators which indicate a lack of commercial substance.¹⁵⁶

¹⁵⁴ De Koker, A.P. (2009). *Silke on South African Income Tax*. Durban: Lexus Nexus.

¹⁵⁵ S 80 C (1).

¹⁵⁶ S 80 C (2).

General test

An arrangement lacks commercial substance if it would result in a significant tax benefit for a party (but for provisions of this part) but does not have a significant effect upon either the business risks or net cash flows of that party apart from any effect attributable to the tax benefit that would be obtained but for the provisions of this part.¹⁵⁷

This addresses that fact that tax avoidance schemes often create a façade of substantial investments which are largely illusory, and insulate the taxpayer from all economic risk, contrary to the overall impression.¹⁵⁸ A significant tax benefit must exist, therefore the existence of a mere tax benefit will not suffice.¹⁵⁹

Generally speaking, a commercial substance will be lacking where there is:

- A disproportionate relationship between the actual economic expenditure or loss incurred by a party and the value of the tax benefit that would have been obtained by that party and the value of the tax benefit that would have been obtained by that party but for the provisions of the GAAR; or
- A loss claimed for tax purposes that significantly exceeds a measurable reduction in the party's net worth.¹⁶⁰

The abovementioned section contains two parts. Firstly, the avoidance arrangement must result in a significant tax benefit, and secondly, it must not have a significant effect on the business risks or net cash flows of a party. What is 'significant' has not been defined in the Act and it leaves room for uncertainty for the taxpayer.

¹⁵⁷ S 80 C (1).

¹⁵⁸ Cassidy, J. (2009). The Holy Grail: The search for the optimal GAAR. *South African Law Journal*, vol. 126, issue 4740.

¹⁵⁹ *Ibid.*

¹⁶⁰ SARS. (2010). Draft Comprehensive Guide to the GAAR. Available at www.sars.gov.za.

Something 'significant' is something of relevance or importance. The courts will need to address how substantial the impact must be before it can be considered 'significant' within the context of each of prescribed limbs in subsection 80(1).¹⁶¹

It is the writer's submission that the legislature must consider amending the Act to the effect that a subparagraph is inserted with a list of factors to be considered when this subsection is applied. According to Broomberg,¹⁶² Part IIA was culled from the laws of many nations. These nations include, amongst others, Australia and the United Kingdom.

I shall examine case law in these countries as well as South Africa in order to deduce the meaning of 'a significant tax benefit'. In *Palser v Grinling*,¹⁶³ Viscount Simon indicated that,

"Substantial' in this connexion is not the same as 'not unsubstantial,' i.e., just enough to avoid the 'de minimis' principle. One of the primary meanings of the word is equivalent to considerable, solid, or big. It is in this sense that we speak of a substantial fortune, a substantial meal, a substantial man, a substantial argument or ground of defence. Applying the word in this sense, it must be left to the discretion of the judge of fact to decide as best he can according to the circumstances in each case'.

In *Tillmanns Butcheries Pty Ltd v Australasian Meat Industry Employees Union*,¹⁶⁴ the federal court of Australia elaborated on the meaning of 'substantial loss or damage'. It was cited by Brown CJ that the word 'substantial' requires a loss or damage that is more than trivial or minimal. He indicated that the word is quantitatively imprecise and that it cannot be said that it requires any specific level of loss or damage.

¹⁶¹ Cassidy, J. (2009). The Holy Grail: The search for the optimal GAAR. *South African Law Journal*, vol. 126, issue 4740, at 770-771.

¹⁶² Broomberg, E.B. (2007). *The new general anti-avoidance rule*. SAFA seminar, Cape Town.

¹⁶³ 1948 A.C 291.

¹⁶⁴ (1979) 42 FLR 331.

Dean J, in the same judgment, said ‘the word substantial is not only susceptible of ambiguity, but is a word calculated to conceal a lack of precision’. He indicated that the word can mean real or of substance, as distinct from ephemeral or nominal.

Various tax scholars have considered the term ‘significant tax benefit’. De Koker¹⁶⁵ indicates that a significant tax benefit, presumably implies that the tax benefit is significant in the context of the taxpayer’s annual net profit or his net assets, or even his financial affairs in general. According to Clegg and Stretch,¹⁶⁶ there is no indication of what would constitute a significant tax benefit.

They presume that the tax benefit will have to be significant in the context of the particular taxpayer’s financial affairs in general. Davis *et al.*¹⁶⁷ assert that a significant tax benefit implies a material or relevant tax benefit with the *de minimis* benefits being disregarded. A significant tax benefit could imply an essential, fundamental considerable, big, large, weighty, substantial, relevant or material tax benefit.

This section also provides that an avoidance arrangement lacks commercial substance if it does not affect the cash flows of that party. The term net cash flows has also not been defined in the Act. International Accounting Standard 7.6¹⁶⁸ defines ‘cash flows’ as ‘inflows and outflows of cash and cash equivalents’. Cash, is in turn defined as ‘cash on hand and demand deposits’.¹⁶⁹ ‘Cash equivalents’¹⁷⁰ are ‘short-term highly liquid investments that are readily convertible to known amounts of cash and are subject to an insignificant risk of changes in value’. The term ‘cash’ denotes money only. This would indicate that only if the taxpayer’s cash position is not affected, then only will the section apply.

¹⁶⁵ *Ibid*

¹⁶⁶ Clegg, D. & Stretch, B. (2010). *Income Tax in South Africa*. Durban: Lexus Nexus.

¹⁶⁷ Davies at al. (2009). The sole or main purpose test-subjective or objective? *The Taxpayer*, October at 181.

¹⁶⁸ IAS. (2011). *International Accounting Standards*. Available at www.iasplus.com/standard/standard.htm.

¹⁶⁹ *Ibid*.

¹⁷⁰ *Ibid*.

It was submitted by Olivier *et al.*¹⁷¹ that it would have been better for the fiscus if they had used the term ‘funds’, as defined in s80D(3), which includes money and it is worth widening the net to cover all forms of property. I concur with this submission because a taxpayer could derive a tax benefit from an arrangement that involves, for example, a transfer of property where a tax deduction may be allowed for the purposes of calculating income tax. In such a case the cash flows of the taxpayer may not be affected in any way but still the ‘lack of commercial substance’ test will not apply.

3.3.8 *Lack of commercial substance indicators*

If an arrangement falls outside the definition of commercial substance in this section but meets the requirements of s80C(2), and vice versa, this can possibly indicate that the term ‘commercial substance’ has different meanings and thus it creates confusion for taxpayers¹⁷². Subsection 80C(2) then sets out a non-exclusive¹⁷³ list of relevant factors that are indicative of arrangements that lack commercial substance.

3.3.9 *Substance over form*

Creating a legal façade that is contrary to the substance of the arrangement, in particular individual steps in a broader arrangement, is a common tool used in tax avoidance schemes.¹⁷⁴ This first indicia would appear to be aimed at those cases where unnecessary and artificial steps are inserted into the tax arrangements that are designed to disguise the true substance of the overall arrangement.¹⁷⁵

¹⁷¹ Olivier, L. & Davis, D.M. & Uruquhart, G. (2009). *Juta's Income Tax*, at 80C-1. Durban: Lexis Nexus.

¹⁷² Broomborg. E.B. (2008). Then and now- V. *Tax Planning Corporate and Personal*, vol. 22.

¹⁷³ The section states the determination is not limited to the listed factors.

¹⁷⁴ Cassidy, J. (2009). The Holy Grail: The search for the optimal GAAR. *South African Law Journal*, vol. 126, issue 4740, at 771.

¹⁷⁵ *Ibid.*

Standing alone, in isolation from the broader arrangement, these steps are often meaningless.¹⁷⁶

The traditional common law ‘substance over form’ doctrine has proven to be insufficient to combat many tax avoidance schemes because the underlying legal agreements are technically valid and thus not normally susceptible to challenge.¹⁷⁷

This saw the introduction of s80C(2)(a), providing that an arrangement lacks commercial substance if the legal substance or effect of the arrangement differs from the legal form of the steps. This indicia of lack of commercial substance ensures that a tax-driven step cannot be ‘camouflaged’ by the legitimate purpose of the arrangement as a whole.¹⁷⁸

The provision is seemingly confusing because the Act makes reference to the legal substance of the whole transaction against the legal form of the steps of the arrangement.

‘Firstly, the legal substance of the arrangement in respect of which SARS intends to apply the GAAR, must be compared to the legal form of the individual steps and any inconsistencies are indicative of lack of commercial substance.

*Secondly, the commercial, economic or practical effect of the arrangement on which SARS intends to apply the GAAR, must be compared to the legal form of the individual steps and any inconsistencies are indicative of lack of commercial substance.*¹⁷⁹

¹⁷⁶ *Ibid.*

¹⁷⁷ SARS Interim Response, at 92.

¹⁷⁸ SARS Explanatory Memorandum, at 65.

¹⁷⁹ SARS (2010). Draft Comprehensive Guide to the GAAR. Available at www.sars.gov.za.

It was submitted by Williams, and the writer agrees with this assertion, that,

'before invoking the principals of the new GAAR, the Commissioner should first attempt to fight any arrangement where the substance differed from the form of a transaction using common law principals and the principals of the new GAAR should only be considered if the common law principals are unable to reconcile a matter. The main reason provided is that the provisions of the GAAR are quite complex'.¹⁸⁰

Broomberg¹⁸¹ argues that the normal judicial parlance denotes that the term 'legal' is usually used in order to draw a contrast between, on the one hand, the legal effects of an arrangement and, on the other hand, its economic or commercial effect.

In March 1996 the first landmark ruling in favour of SARS with regard to substance over form was seen in the case of Erf 3183/1 Ladysmith (Pty) Ltd and Another vCIR¹⁸². In this case the Appellate division of the Supreme Court of Appeal found that a tax exempt entity was used to absorb the deemed taxable income arising out of a lessee's obligation to improve the property concerned. The Court drew a distinction between:

- Transactions in which the substance and form coincide – that is, the intended effects of the transaction are wholly in line with, and fully laid out in, the documentation; and
- Transactions which are never intended to have the effect that their documentation purports, or whose intended effect is different in some material way than their form would suggest. These are generally known as sham transactions.

¹⁸⁰ Williams, R.C. (2009). *Smoke and mirrors or genuine commercial venture?* PriceWaterHouseCoopers Synopsis, at 2-4. Available at www.pwc.co.za/en_ZA/za/assets/.../pwc-synopsis-september2009.pdf.

¹⁸¹ Broomberg, E.B. (2007). *The new general anti-avoidance rule*. SAFA seminar, Cape Town.

¹⁸² 1996 (3) SA 942 (A), 58 SATC 229.

Another ruling based on the substance over form doctrine was that of *Brummeria*¹⁸³ which was a case of the Supreme Court of Appeal. In this case the respondents were companies which developed retirement villages. They entered into written agreements with potential occupants of units still to be constructed in retirement villages. The features of the agreements included each company obtaining an interest-free loan from a potential occupant in order to finance the construction of a unit in a particular retirement village by the company in question.

In the recent judgement of *NWK v C SARS*,¹⁸⁴ NWK entered into a series of complicated commercial transactions with First National Bank (FNB). The effect of the structured series of transactions was that the amount of interest deducted economically included the capital amount of the loan intended to be advanced by FNB to NWK. SARS raised additional assessments on the basis that the agreements concluded between NWK, FNB and its subsidiary did not reflect the true substance of the transaction.

It was argued that if effect is given to the true intention of the parties, the parties entered into a loan agreement, and that the amount of this loan and resultant interest would be substantially lower than the amounts claimed. SARS also contended that some of the transactions had no commercial reality and that these were only entered into to disguise the true nature and amount of the loan transaction intended by the parties.

This *indicia* of lack of commercial substance ensures that a tax-driven step cannot be 'camouflaged' by the legitimate purpose of the arrangement as a whole.¹⁸⁵

¹⁸³ Commissioner for the South African Revenue Service v *Brummeria Renaissance (Pty) Ltd and Others* (391/06) [2007] ZASCA 99; [2007] SCA 99 (RSA) ; [2007] 4 All SA 1338 (SCA) ; 2007 (6) SA 601 (SCA) (13 September 2007).

¹⁸⁴ *CSARS v NWK* (27/10) [2010] ZASCA 168 (1. December 2010)

¹⁸⁵ SARS Explanatory Memorandum, at 65.

3.3.10 Round trip financing

Round trip financing is again a common feature of tax avoidance schemes.

Section 80C(2)(i) states that the presence of round trip financing, as defined by s80D, will indicate that an arrangement lacks commercial substance. In terms of s80D(1), round trip financing is present when funds are transferred between parties and the transfer of funds would;

- Result, directly or indirectly, in a tax benefit but for the provisions of the GAAR; and
- Significantly reduce, offset or eliminate any business risk incurred by any party in connection with the avoidance arrangement.

This practice ensures no money is actually paid, yet creates a façade of a (deductible) expense.¹⁸⁶ Money is simply re-routed through accommodating or tax-indifferent parties.¹⁸⁷

For purposes of s80D, 'funds' are defined as including any cash, cash equivalents or any right or obligation to receive or pay the same.

The issue of tax benefits and business risks is once again addressed in this section albeit with a slight twist. In s80C(1) discussed above, the avoidance arrangement must have resulted in a significant tax benefit for a party but should not have any significant effect on the business risks of the taxpayer. In s80D(b)(i) and (ii), the transfer of funds must have resulted in a tax benefit and must significantly reduce the business risks of the taxpayer.

¹⁸⁶ Cassidy, J. (2009). The Holy Grail: The search for the optimal GAAR. *South African Law Journal*, vol. 126, issue 4740.

¹⁸⁷ Interim response *ibid* at 11.

In the former section, therefore, no effect on the business risks of the taxpayer is required, yet in s80 D there must exist an effect on the business risks of the taxpayer, which is the elimination or reduction of the risks thereof.

Broomberg¹⁸⁸ contends that almost every single commercial arrangement between two or more parties will involve the transfer of funds, either physically or electronically. In light of Broomberg's¹⁸⁹ observation, this virtually means that every other commercial transaction that citizens of the Republic are involved in that result in some sort of tax benefit run the risk of being scrutinised by the Commissioner for fear of them falling foul of the general anti-avoidance rule.

It is the writer's contention that this provision might not be feasible to administer as we are living in a commercial world where funds are transferred on a daily basis between parties.

It has been suggested by Broomberg¹⁹⁰ that s80C(1) asks the question of whether round trip financing exists in relation to one particular taxpayer, whereas s80C(2) it makes an enquiry as to whether round trip financing exists in relation to the other parties to an arrangement. While the writer concurs with this observation, it seems quite skewed because the Commissioner will need to analyse the transaction as a whole, rather than looking at the impact it has on a single party. Furthermore, subsection 80D(2) provides that the section may apply to any round trip financing, whether or not the amounts can be traced to 'any party in connection with the avoidance arrangement', the 'timing or sequence' of the transfer of funds, or the 'means by or manner' of the transfer or receipt of the funds. Also, subsection 80D(3) recognises that the 'funds' may be cash equivalents, including the rights and obligations to receive cash.

¹⁸⁸ Broomberg, E.B. (2008). Then and now –VI. *Tax Planning Corporate and Personal*, vol. 22.

¹⁸⁹ *Ibid.*

¹⁹⁰ *Ibid.*

The last factor under s80 C is that the arrangement must have elements that off-set or cancel each other.

3.3.11 Accommodating or tax –indifferent parties

Section 80C(2)(b)(ii) states that the inclusion of an accommodating or tax indifferent party indicates a lack of commercial substance. A party to an avoidance arrangement is an accommodating or tax-indifferent party, as defined in s80E(1), if:

- (a) any amount derived by the party in connection with the avoidance arrangement is either: (i) not subject to normal tax; or (ii) significantly offset by either any expenditure or loss incurred by the party in connection with that avoidance arrangement or any assessed loss of that party;
- (b) and (b) either: (i) as a direct or indirect result of the participation of that party involves an amount that would have: (aa) been included in the gross income (including the recoupment of any amount) or receipts or accruals of a capital nature of another party would be included in the gross income or receipts and accruals of a capital nature of that party; (bb) constituted a non-deductible expenditure or loss in the hands of another party would be treated as a deductible expenditure by that other party; (cc) constituted revenue in the hands of another party would be treated as capital by that other party; or (dd) given rise to taxable income to another party would either be not included in gross income or be exempt from normal tax; or (ii) the participation of that party directly or indirectly involves a prepayment by any other party.

Section 80E(3) then discusses the various instances where an accommodating or tax indifferent party indicator may be ignored. These instances will be discussed below.

Section 80 contains the safe harbour provision that protects parties that would have otherwise be considered as accommodating or tax indifferent parties.

The Explanatory Memorandum indicates, ‘accommodating or tax-indifferent parties are often used to give the illusion of commercial substance in a specific entity and circumvent anti-avoidance rules’.¹⁹¹

In terms of s80F, the Commissioner is empowered to disregard accommodating or tax-indifferent parties, or to combine the transaction with another person to determine if a tax benefit exists.

‘This enables the Commissioner to ‘pierce the layers of “structural fog” in which certain promoters seek to cloak their schemes’.¹⁹²

3.3.12 Two thirds requirement

Firstly, it must be determined whether the amounts derived by the party in question are cumulatively subject to income tax by one or more spheres of government of countries other than the Republic, which is equal to at least two-thirds of the amount of normal tax which would have been payable in connection with those amounts had they been subject to tax under this Act.

The reasoning behind this safe harbour is that the comparable foreign tax would typically offset any tax benefit obtained in South Africa in respect of the avoidance arrangement in question.¹⁹³ This means that the taxpayer is then supposed to determine the tax liability of the other party as if they were a resident.

¹⁹¹ SARS Explanatory memorandum.

¹⁹² SARS Revised proposals.

¹⁹³ SARS Guide to the GAAR.

The second exclusion is that the party in question continues to engage directly in substantive active trading activities in connection with the avoidance arrangement for a period of at least 18 months. These activities must be attributable to a place of business, place, site, agricultural land, vessel, vehicle, rolling stock or aircraft that would constitute a foreign business establishment, as defined in s9D(1), if it were located outside the Republic and the party in question were a controlled foreign company. This exemption means that:

- There must be another party engaging in substantive active trading activities.
- The other party must be engaging with the taxpayer for the particular arrangement for at least eighteen months.
- These activities must be attributable to a business establishment and be considered a controlled foreign company.

Exactly what is 'substantive' has not been defined in the Act. A normal interpretation of the word means that it should be something material or relevant. It is submitted that what is considered as material or relevant to the taxpayer may not be so in the eyes of the Commissioner; a possible clarification of what constitutes 'substantive business activities' would shed more light and give clarity to the taxpayers.

The next requirement is that the other party had been engaging with the taxpayer for a period of at least 18 months.

The next requirement is that the other party needs to be classified as a controlled foreign company under s9D. In order for this component of the exemption to be satisfied, the taxpayer would need to obtain the names and nationalities of every shareholder of the other party and determine if the company is a controlled foreign company. This requirement sounds like a tedious process that the taxpayer must go through in order to qualify for the exemption.

Broomberg¹⁹⁴ indicates that the ‘foreign business establishment’ definition raises some of the most difficult factual issues in the Act, and the fact that the tax-indifferent party may be a stranger to the taxpayer makes the requirements absurd.

The first part of the definition of a foreign business establishment in relation to a controlled foreign company, as per s9D(c)(a), requires a place of business with an office, shop, factory, warehouse or other structure which is used or will continue to be used by that controlled foreign company for a period of not less than one year, whereby the business of such company is carried on. Therefore the CFC must have a fixed place of business in the Republic.

In terms of s9D(c)(a)(i), the foreign business establishment must be suitably staffed with on-site managerial and operational employees. According to s9D(c)(a)(ii), it must be suitably equipped and have proper facilities, and lastly, s9D(c)(a)(iii) requires that the foreign business establishment be located in a country other than the Republic for *bona fide* business purposes.

3.3.13 Elements that offset or cancel each other

In terms of s80C(2)(b)(iii), an arrangement entered into or carried on in the context of business will be an impermissible avoidance arrangement if a tax benefit is derived, the sole or main purpose of the arrangement is to derive the tax benefit, and the arrangement contains elements that have the effect of offsetting or cancelling each other.

The purpose of this provision has been summed up as follows:

¹⁹⁴ Broomberg, E.B. (2008). Then and Now –VII. *Tax Planning Corporate and Personal*, 22.

*‘The self-neutralising mechanism draws upon precedent in the United Kingdom and other jurisdictions that gave rise to the so-called fiscal nullity doctrine. It is targeted primarily at complex schemes, typically involving complex financial derivatives, which seek to exploit perceived loopholes in the law through transactions in which one leg generates a significant tax benefit while another effectively neutralises the first leg for non-tax purposes’.*¹⁹⁵

According to the Explanatory Memorandum,¹⁹⁶

‘... the last indicia in subsection 80C(2) draws on the United Kingdom’s judicially developed ‘doctrine of fiscal nullity’. The doctrine of fiscal nullity applies where there is a preordained composite transaction or series of transactions, and inserted into this is a step with no commercial business other than tax avoidance.’

The content of this doctrine will be discussed in more detail in the subsequent chapter. The Explanatory Memorandum¹⁹⁷ suggests, as further indicia, ‘the absence of a reasonable expectation of pre-tax profit or an expectation of pre-tax profit that is insignificant in comparison to the amount of the expected tax benefit’.

3.3.14 Non-business context

Section 80A(b) states that an avoidance arrangement is an impermissible avoidance arrangement if in a context other than business, it was entered into or carried out by a means or in a manner which would not be normally employed for a *bona fide* purpose other than obtaining a tax benefit.

¹⁹⁵ De Koker, A.P (2009). *Silke on South African Income Tax*, at 19.7.

¹⁹⁶ SARS Explanatory Memorandum.

¹⁹⁷ *Ibid.*

3.3.15 *In any other context*

Section 80A(c) states that in ‘any context’ an avoidance arrangement is an impermissible avoidance arrangement if:

- It has created rights or obligations that would not normally be created between persons dealing at arm’s length,¹⁹⁸ or
- It would result directly or indirectly in the misuse or abuse of the provisions of this Act (including the provisions of this part).¹⁹⁹

The provision is targeted at arrangements that frustrate the statutory purpose of any provision of the Act, including Part IIA.²⁰⁰ This is designed to ensure scheme promoters cannot misconstrue provisions in a bid to find unintended loopholes.²⁰¹

The use of the term in ‘any context’ implies that the provision has a wide application and it encapsulates every other arrangement that would not have been covered by the previous sections. While such tax avoidance schemes would fail either, or both, the abnormality or the commercial substance tests, in some cases the arrangements may less obviously be caught by these tests, and thus an alternative measure was needed.²⁰²

It was submitted by Cilliers²⁰³ that this section can be described as the heart of s80A as a result of it applying in any context.

¹⁹⁸ S 80 A (c) (i).

¹⁹⁹ S 80 A (c) (ii).

²⁰⁰ SARS Revised Proposals, at 15.

²⁰¹ *Ibid*, at 16.

²⁰² SARS Revised Proposals.

²⁰³ Cilliers, C. (2008a). Thou shalt not peep at thy neighbour’s wife: Section 80A(c) (ii) of the Income Tax Act and the abuse of rights. *The Taxpayer*, May, 85-92.

Previously the courts applied the literal approach to interpretation, and to combat this problem, this tainted element was introduced to discourage avoidance arrangements that rely on excessively literal interpretative techniques to defeat the intended purpose of the legislation²⁰⁴. The effectiveness of a GAAR is dependent on the content of the rule as well as the interpretative approach adopted by the courts.²⁰⁵ Moreover, in the course of the reform discussions it became apparent that s103 and the original proposals did not comply with international best practice as they failed to include any test that related to the purpose underlying the tax provision that was to be exploited or evaded.²⁰⁶

According to the SARS 2006 Revised Proposals on Tax Avoidance and Section 103 of the Income Tax Act 58 of 1962 (Revised Proposals), the rationale behind the insertion of s80A(c) (ii) was to reinforce the modern approach to the interpretation of tax statutes, 'in order to find the meaning that harmonises the wording, object, spirit and purpose of the provisions of the Income Tax Act'.

I shall briefly analyse the abovementioned rationale. The word 'reinforce' means to strengthen or support, especially with additional personnel or material.²⁰⁷ In light of this definition, it was submitted by Van Schalwyk and Geldenhuys²⁰⁸ that,

"Strengthening" is a much wider concept than "supporting": it involves an increase of an existing concept or structure as opposed to the mere maintenance thereof'.

²⁰⁴ SARS Revised Proposals.

²⁰⁵ Cassidy, J. (2009). The Holy Grail: The search for the optimal GAAR. *South African Law Journal*, vol. 126, issue 4.

²⁰⁶ *Ibid* at 15.

²⁰⁷ New Oxford Dictionary of English (2001:1565).

²⁰⁸ Section 80 A(c) (ii) of the Income Tax Act and the Interpretation of Tax Statutes in South Africa, at 169.

They also question whether s80A(c)(ii) will strengthen (increase) or merely support (maintain) the modern approach.²⁰⁹

Cilliers²¹⁰ indicates the following with regard to the meaning of the words 'misuse' and 'abuse':

'It is doubtful whether the words 'misuse' and 'abuse' have materially different meanings. In using both the words 'misuse' and 'abuse', the legislature probably acted ex abundanti cautela. This is a case in which one ought to disregard the presumption that each and every word in a statutory provision must be given an independent meaning and effect. The legislature did not wish to denote two distinct concepts, but tried instead to ensure that the concept being expressed would be clearly understood.'

There are different approaches to the interpretation of statutes in South Africa, literalism, intentionalism, purposivism and contextualism. According to literalism, the true meaning of a statutory provision is to be sought virtually exclusively in the very words used by the legislature.²¹¹ Intentionalism (also referred to as the subjective theory) holds that the meaning of a statutory provision is governed by what the legislature intended as disclosed by the wording of the provision²¹². Purposivism attributes meaning to a statutory provision in the light of the purpose it seeks to achieve.²¹³

²⁰⁹ Van Schalkwyk, L. & Geldenhuys, B. (2009). *Section 80A(c)(ii) of the Income Tax Act and the scope of Part II A. Accountancy SA*. Available at <http://www.accountancysa.org.za/resources/ShowItemArticle.asp?ArticleId=1792&Issue=1086>.

²¹⁰ Cilliers, C. (2008a). Thou shalt not peep at thy neighbour's wife: Section 80A(c) (ii) of the Income Tax Act and the abuse of rights. *The Taxpayer*, May, 87.

²¹¹ Cilliers, C. (2008a). Thou shalt not peep at thy neighbour's wife: Section 80A(c) (ii) of the Income Tax Act and the abuse of rights. *The Taxpayer*, May, 87.

²¹² Kellaway, E.A. (1995). *Principles of legal interpretation: statutes, contracts and wills*, at 63.

²¹³ Joubert, W.A. & Faris, J.A. (2001). *The law of South Africa*, vol. 25, part 1, at 285.

The meaning of a provision is often said to be determinable by reading its words in context or reading the language in context or reading the provision itself in context.²¹⁴

The accepted approach to interpretive legislation in South Africa is the purposive approach; abuse is in the eye of the beholder. It is dependent upon a particular view or understanding of the purpose of the legislation which is said to be abused. The misuse or abuse provision is new to the Income Tax Act as its origin is the Canadian Income Tax Act which employs a similar provision in conjunction with a business purpose test.

The relevant provision of the Canadian Income Tax Act is as follows: Section 245(2) states,

'Where a transaction is an avoidance transaction, the tax consequences to a person shall be determined as is reasonable in the circumstances in order to deny a tax benefit that, but for this section, would result, directly or indirectly, from that transaction or from a series of transactions that includes that transaction.' Subsection (2)(b) applies to a transaction only if it may reasonably be considered that the transaction would result directly or indirectly in an abuse, having regard to provisions of [the Income Tax Act] read as a whole.'

Although the concept derives from Canadian law, it is important to note that the test is nevertheless implemented somewhat differently in the context of the South African GAAR.²¹⁵

In Canada *Trustco* it was held that in considering misuse, the focus is on the specific legislative provisions relied on, and that the Court should not search for an overriding policy of the Canadian Income Tax Act that is based on a unified, textual, contextual and purposive interpretation of the specific provisions in question.

²¹⁴ *Ibid.*

²¹⁵ SARS Guide to the GAAR.

The above extract from the Canadian statute is written in a negative tone, and provides that s245(2) may not be applied when a transaction does not result in the misuse or abuse of the provisions of the statute.²¹⁶

It was also noted that in the same case that,

'The GAAR may be applied to deny a tax benefit only after it is determined that it was not reasonable to consider the tax benefit to be within the object, spirit or purpose of the provisions relied upon by the taxpayer. ...

[T]his means that a finding of abuse is only warranted where the opposite conclusion — that the avoidance transaction was consistent with the object, spirit or purpose of the provisions of the Act that are relied on by the taxpayer cannot be reasonably entertained. In other words, the abusive nature of the transaction must be clear.

The GAAR will not apply to deny a tax benefit where it may reasonably be considered that the transactions were carried out in a manner consistent with the object, spirit or purpose of the provisions of the Act, as interpreted textually, contextually and purposively.'

In Canada the misuse or abuse test involves a two-part inquiry.²¹⁷ The first is,

'...to interpret the provisions giving rise to the tax benefit to determine their object, spirit and purpose. The second is to examine the factual context of a case in order to determine whether the avoidance arrangement defeated the object, spirit or purpose of the provisions in issue.'

²¹⁶ Van Schalkwyk, L., Geldenhuys, B. (2009). Section 80A(c)(ii) of the Income Tax Act and the scope of Part II A. *Accountancy SA*, at 2.

²¹⁷ SARS Guide to the GAAR, at 39.

It has been identified that,

*'... the first problem relating to this provision is that it presupposes that all the other sections of the Income Tax Act have been appropriately applied and that all that needs to be determined is whether the arrangements of the taxpayer have the effect of misusing or abusing the statute.'*²¹⁸

The writer who made the above assertion further adduced that if a statute is clear and unambiguous, how can a taxpayer's arrangement then be considered for the misuse and abuse of the Act adopting a contextual, purposive and textual approach.²¹⁹

In South Africa the rules which require a court to have regard to the intention of the legislature are regarded as the 'purposive' or 'contextual' rules of interpretation. Now the misuse or abuse prerequisite of s80A requires a purposive approach to its interpretation and presupposes that there is some identifiable non-abusive use of each provision of the Act (and the Act as a whole), which can in some way be used as a yardstick against which to measure misuse or abuse.²²⁰

The introduction of the misuse or abuse concept is intended to reinforce the emerging trend in South Africa. The onus of proof rests on the Commissioner to prove on a balance of probabilities that a provision of the Income Tax Act was misused or abused by virtue of an avoidance arrangement.

The introduction of the misuse or abuse provision is specifically directed at ensuring that the remedy provided by the section is advanced and that the mischief against which the section is directed is suppressed.

²¹⁸ De Koker, A.P (2009). *Silke on South African Income Tax*, at 19.7.

²¹⁹ *Ibid.*

²²⁰ Clegg, D. (2007). Use it or abuse it. *Tax Planning*, vo.1 21 at 37.

As a result a mere literal interpretation of the provisions will no longer safeguard a taxpayer who applies the provisions in the Income Tax Act in a context or manner which is not intended by the Income Tax Act.²²¹

If an arrangement is carried out in a manner which is consistent with the spirit, object and purpose of the Act, as interpreted textually, contextually and purposively, the taxpayer's arrangement will not be considered to be a misuse or abuse of the provisions of the Income Tax Act.

²²¹ SARS Guide to GAAR, at 40.

CHAPTER 4. COMPARISONS WITH OTHER COUNTRIES

4.1. Introduction

This chapter contains a comparative analysis of the General Anti-avoidance Rule as contained in the Income Tax Act and the General Anti-avoidance rules as contained in foreign legislation *vis-à-vis* Australia, Canada and United Kingdom. The GAARs in South Africa, Canada and Australia interestingly have features that overlap each other, especially in light of the requirements that must be met before an arrangement is considered an avoidance arrangement.

These regimes, however, have features that are preferable, and thus the South African GAARs might be improved by incorporating aspects of other anti-avoidance models. The United Kingdom has chosen not to adopt a GAAR, but rather TAARs, which have their own advantages as compared with GAARs.

I shall provide synopsis of the general anti-avoidance rules in abovementioned states and compare them with the South African GAAR.

4.2. Australia

The Australian anti-avoidance rule was initially contained in s260,²²² and just like s103 of the South African Income Tax Act, it proved to be ineffective in combating tax avoidance.

²²² Section 260 of the ITAA 1936 was intended to render void, as against the Commissioner, any contracts, agreements or arrangements designed to evade or avoid tax. After a series of court decisions on tax avoidance schemes in the 1970s, a widely held view developed that section 260 of the ITAA 1936 was not operating as an effective GAAR.

This was largely due to the courts using an excessively literal interpretation of the provision, rather than a purposive test and legitimising arrangements structured to take advantage of the loopholes in s260.²²³

The following four particular problems with the way in which the courts interpreted s260 were identified:

- First, the courts would not invoke s260 merely because a taxpayer had chosen the most tax-effective legally available type of transaction. They had to find something more than this before they would hold that the taxpayer was cheating.
- Secondly, the courts had no power to look behind and examine the purpose or motive of a taxpayer in choosing a type of transaction. The courts would simply restrict their analysis to the legal effect of the transaction itself.
- Thirdly, s260 did not allow transactions to be declared partly void. It was an all-or-nothing provision which was not sufficiently flexible to deal with complex tax avoidance schemes.
- Finally, although s260 empowered a court to annul a dubious transaction, the section gave no remedial power to the courts so that they could reconstruct an annulled transaction and make it taxable after all (Explanatory Memorandum to the Income Tax Laws Amendment Bill (no. 2) 1981 (Cwlt, p.2).

It was concluded that s260 was of limited application and ineffective in combating the sophisticated tax avoidance schemes promoted by tax advisers.²²⁴ Section 260 was therefore replaced with Part IVA of the ITAA , which became effective on 27 May 1981.

²²³ Cassidy, J. (2009). The Holy Grail: The search for the optimal GAAR. *South African Law Journal*, vol. 126, at 744.

²²⁴ Grbich, Y. (1983). Problems of tax avoidance in Australia. In J G Head (ed.). *Tax Issues of the 1980s*. Australian Tax Research Foundation, at 413.

The Treasurer stated that Part IVA was introduced to,

‘... strike down blatant, artificial or contrived arrangements but not cast unnecessary inhibitions on normal commercial transactions by which taxpayers legitimately take advantage of opportunities available for the arrangement of their affairs.’²²⁵

However, the Treasurer added that Part IVA would,

‘... not cast unnecessary inhibitions on normal commercial transactions by which taxpayers legitimately take advantage of the opportunity available for the arrangement of their affairs.’²²⁶

In the same manner in South Africa, on 3 November 2005 the Minister of Finance launched a discussion paper on tax avoidance and s103 of the Income Tax Act and the proposed amendments. The proposals were revised and a new Part IIA of the Income Tax Act was enacted, which is applicable to any arrangement entered into on or after 2 November 2006.

4.2.1 Requirements Part IVA:

For Part IVA to apply there must be:

- a ‘scheme’ (defined in s 177A)
- that provides the ‘relevant taxpayer’ with a ‘tax benefit’ (defined primarily in s177C) and

²²⁵ Cassidy, J. (2008). The Holy Grail: The search for the optimal GAAR, quoting Second Reading Speech, Hansard, House of Representatives, 27 May 1981, 2683–4 at 744.

²²⁶ *Ibid.*

- a person must have entered into the scheme for the sole or dominant purpose of enabling the relevant taxpayer to obtain a tax benefit (s 177D).

Section 177A (1) defines a 'scheme' as:

- (i) any agreement, arrangement, understanding, promise or undertaking, whether express or implied and whether or not enforceable, or intended to be enforceable by legal proceedings and;
- (ii) any scheme, plan, proposal, action, course of action or course of conduct.

It must be noted that in Australia the word 'scheme' is used, as opposed to 'arrangement' in South Africa to highlight the requirements that must be met in order to deem an agreement an impermissible avoidance arrangement. It is Cassidy's contention that 'the South African use of the term 'arrangement' has much to commend it when compared to the Australian use of the term 'scheme' and the consequent uncertain judicial approach to this notion.'²²⁷

She says,

*'... first, the inclusion in the section 80L definition of an 'arrangement' of 'part' of an arrangement and the express statement in section 80H that the Commissioner can apply the legislation to 'any steps in or parts of an arrangement' eliminates the need to consider the difficult question under Part IVA whether the subject factual arrangement is a scheme or a mere sub-scheme.'*²²⁸

²²⁷ Cassidy, J. (2009). The Holy Grail: The search for the optimal GAAR. *South African Law Journal*, vol. 126, at 752.

²²⁸ *Ibid.*

*Secondly, explicit recognition in subsection 80G(2) that it suffices under the South African GAAR if one part of an arrangement has the requisite primary purpose of obtaining the tax benefit, rather than requiring that the scheme as a whole be so characterized, means that the issue of identifying the actual scheme is largely nugatory.*²²⁹

The writer concurs with this contention. Cassidy also added that,

*'... there is no need for the arrangement as a whole to be justified by a non-tax purpose, as long as each step/part of the arrangement in isolation is based on a bona fide non-tax purpose.'*²³⁰

There are, however, subtle differences in the way the two terms are defined in both legislations. Under subsection 177A(3), 'scheme' includes a 'unilateral scheme, plan, proposal, action, course of action or course of conduct'. In the same manner, an 'arrangement' is said to include any operation, transaction, scheme ...', highlighting the broad nature of the application of both requirements.

In *FCT v Peabody*²³¹ a further definition of scheme was introduced by requiring that the facts that constitute the alleged scheme must be capable of 'standing on their own without being "robbed of all practical meaning"'. As a consequence of this requirement, the narrower the factual arrangement that is the purported scheme, the less likely it will be capable of standing on its own within the High Court's test.²³² The writer concurs with this submission.

²²⁹ Cassidy, J. (2009). The Holy Grail: The search for the optimal GAAR. *South African Law Journal*, vol. 126, at 752.

²³⁰ *Ibid.*

²³¹ (1994) 94ATC4663 at 4670.

²³² Cassidy, J. (2009). The Holy Grail: The search for the optimal GAAR. *South African Law Journal*, vol. 126, at 752.

Cashmere,²³³ regarding this requirement, indicated that,

'This is a major limitation to the application of Part IV because the narrower the formulation of the scheme, the more likely that factual scenario will also satisfy the other elements of Part IVA.'

It is will be a question of fact in each case as to whether the particular circumstances are a scheme, as contemplated by the provisions of Part IVA. In deciding this issue, regard should be given to the characteristics of the arrangements, the relationship with surrounding events, and their apparent rationale.

Cooper J in *Spotless Services Ltd v FCT*²³⁴ asserted that the definition of a scheme,

'... requires that the parties to the scheme, insofar as they are known, must be identified and the terms or content of any agreement, arrangement, understanding, promise or undertaking and the steps or stages of any course of action or proposal insofar as they are relevant, be identified. In addition, the courts held that 'all the relevant facts had to be included in the relevant formulation before the factual scenario could be said to be capable of standing on its own and thus constituting a scheme.'

The 'capable of standing alone test' does not seem to be applicable to s80L although the section makes reference to Part IIA applying to part or parts of an arrangement. That part of an arrangement does not necessarily have to be a standalone arrangement.

²³³ Cashmere, M. (2003). The interrelation of scheme and purpose. *E-Journal of Tax Research*, 110, at 111 and 114.

²³⁴ (1995) 95ATC4775 at 4805.

The position in Australia regarding this test is now a grey area, in light of the decision in *FCT v Hart*.²³⁵ The counsel in this case had differing opinions regarding the relevance and applicability of the test. Gleeson CJ and McHugh J applied the ‘capable of standing on its own’ test.²³⁶ They asserted that ‘a broad formulation of the scheme, including all the facts, had to be adopted for the application of Part IVA’. They also concluded that it was inappropriate to ‘exclude the fact of borrowing from the putative scheme’.²³⁷

On the other hand, Callinan J stated that the ‘capable of standing alone’ test simply means that the Commissioner cannot,

‘... seize upon and isolate one event, or a series of events, which, standing alone may appear to have a complexion which it or they cannot truly bear when other relevant connected events are taken, as they should be, into account.’

Cassidy²³⁸ asserts that,

‘... even this interpretation of the ‘capable of standing alone’ test would appear inapplicable to section 80L as sections 80G, 80H and 80L make it clear that related facts do not have to be included in the subject arrangement.’

Gummow and Hayne JJ, in the same case²³⁹, rejected the proposition that ‘the reference to circumstances being ‘robbed of all practical meaning’ was a criterion for the application of Part IVA, asserting that it finds no support in the statutory language of Part IVA.

²³⁵ (2004) 2004ATC4599.

²³⁶ *Ibid* at 4603.

²³⁷ (2004) 2004ATC4599, at 4625.

²³⁸ Cassidy, J. (2009). The Holy Grail: The search for the optimal GAAR. *South African Law Journal*, vol. 126.

²³⁹ *FCT v Hart*, (2004) 2004ATC4599.

‘Arrangement’ is in turn defined in s80L as,

‘Any transaction, operation, scheme, agreement or understanding (whether enforceable or not), including all steps therein or parts thereof, and includes any of the foregoing involving the alienation of property.’

4.2.2 Application to part/parts of an arrangement

Part IIA of the Income Tax Act is applicable to part or parts of an arrangement or scheme. So therefore it can apply to the entire arrangement, or just a part of it. In different parts of s80 the terms ‘parts or steps of an arrangement’ are repeatedly used. Firstly, in s80 C(2), an avoidance arrangement is deemed to lack commercial substance if the legal substance or effect of the avoidance arrangement as a whole is inconsistent with, or differs significantly from the legal form of its individual steps.

Also, s80L states that an arrangement includes ‘all steps therein or parts thereof’. Furthermore, s80 G (2) provides that the ‘purpose of a step in or part of an avoidance arrangement may be different from a purpose attributable to the avoidance arrangement as a whole’. Thus, even if the overall arrangement has a legitimate purpose, this will not prevent Part IIA applying if part of an arrangement was entered into for the sole or main purpose of obtaining a tax benefit.²⁴⁰ The section is useful to the taxpayer because the Commissioner is obliged to formally disclose exactly which aspects of the arrangement he is attacking.

Part IVA, however, follows a different approach in this regard. It is the courts’ contention that it is insufficient if only a part of the scheme satisfies the elements of part IVA. Therefore, unlike the Income Tax Act, part IVA cannot be applied to an isolated aspect of the scheme but must rather be applied to the scheme as a whole.

²⁴⁰ Explanatory Memorandum.

This was highlighted by Hill J in *Peabody v FCT*²⁴¹ where he stated that,

'Where as a matter of fact a scheme consists of a course of action comprising several steps the Commissioner may not isolate out of that course of action one step and classify that as a scheme... [I]n a case where a series of steps constitutes a scheme, that whole series of steps is to be considered, the individual steps being seen as parts of the scheme rather than each step being capable of being seen as a scheme in itself.'

In relation to these elements, the dispute in *Peabody* raised, *inter alia*, five important issues²⁴²:

- The meaning of 'scheme';
- Did the Commissioner or the court identify the relevant scheme;
- Was it sufficient if tax avoidance tainted only a step in the scheme;
- How is a tax benefit identified under s177c; and

²⁴¹ (1992) 92 ATC 458 (1993) ATC 4104:(1994) 94 ATC 4663. The case involved a group of companies where two parties held the controlling interests i.e. TEP Holdings Pty Ltd (T Co) as trustee of the Peabody Family Trust (62%) and Mr Kleinschmidt (Mr K) and his associates (38%). The beneficiaries of the trust were the taxpayer (Mrs P) and her two children. The taxpayer and her husband (Mr P) were the sole shareholders and directors of T Co. Mr Peabody sought to purchase the interest of Mr Kleinschmidt to enable a public float of 50% of the group with the intention being that the 'Peabody interest' would retain the other 50%. Mr Kleinschmidt agreed to sell his interest but the transaction would be subject to considerable 'capital gains tax' under s 26AAA. To avoid the tax consequence a shelf company (Loftway Pty Ltd (L Co)), was created to purchase Mr Kleinschmidt's shares and then transforming those shares into a worthless class of shares. This would have the effect that the 'Peabody interests' in the corporate group effectively came to represent 100 per cent of the worth of the corporate group. Part IVA was held not to apply. The acquisition and conversion of the non-Peabody shares was held to be a sub-scheme, and thus Part IVA could not be applied to this narrow factual construct. It was held that 'the dominant purpose in relation to the scheme as a whole' was commercial in nature; namely, the floating of the company.

²⁴² Cassidy, J. (1995). *Peabody v FCT and Part IVA*. *Revenue Law Journal*, vol. 5 issue 2, at 199.

- How is the dominant purpose determined.

This approach adopted by the Australian courts might lead to unfair results on the part of the taxpayer. It creates uncertainty because the Commissioner could possibly attack individual steps which are interlinked with other steps and which are incapable of standing on their own.

On the other hand, if the Commissioner were to attack a taxpayer on a particular step in isolation, Broomberg²⁴³ questions whether the Commissioner would be successful if the step or part loses its commercial substance when considered in isolation.

The High Court in this case was again divided on the applicability of Part IVA to part of a scheme. Gleeson CJ and McHugh J asserted that Part IVA had to be applied to the whole facts. Callinan J quoted the statement in *FCT v Peabody* that 'Part IVA does not provide that a scheme includes part of a scheme'. It was also his contention that,

*'... the use of the singular, narrow words, proposal, action or course of action in subsection 177A (1)(b) in juxtaposition with, for example, agreement or arrangement in subsection 177A(1)(a) indicates that something done which is less than the whole of an arrangement or agreement may be capable of itself being a scheme'*²⁴⁴.

It is, however, the findings of Gummow and Hayne JJ that are generally accepted in Australia and are cited as 'relevant case law' in the ATO Practice Statement PS LA 2005/24. The statement notes that,

'these statements of law support the proposition that whether a scheme is wider or narrower should not be relevant in determining if the test in section 177D is met with respect to the scheme, as long as the tax benefit in question is

²⁴³ Broomberg, E.B. (2007). Then and Now-II. *Tax Planning Corporate and Personal*, 21.

²⁴⁴ (2004) 2004 ATC 4599 at 4612.

sufficiently connected with the scheme’.

Gummow and Hayne JJ said that s177A’s reference to ‘action’ ‘in the singular’ indicated that the ‘taking of but one step’ might constitute a scheme. They also noted that,

‘... subsection 177D(d), akin to subsection 80G(2), states that in determining the dominant purpose the legislation may be applied to any person entering into ‘any part of the scheme’.

They asserted that Part IVA could be applied to either the wider scheme (effectively all of the facts) or the narrower scheme (the tax effective aspect of the borrowing alone) or ‘any part of either scheme’.²⁴⁵ Cassidy²⁴⁶ made the following conclusion in relation to the use of the terms ‘arrangement’ in South Africa and ‘scheme’ in Australia:

‘The South African use of the term ‘arrangement’ has much to commend it when compared to the Australian use of the term ‘scheme’ and the consequent uncertain judicial approach to this notion. First, the inclusion in the section 80L definition of an ‘arrangement’ of ‘part’ of an arrangement and the express statement in section 80H that the Commissioner can apply the legislation to ‘any steps in or parts of an arrangement’ eliminates the need to consider the difficult question under Part IVA whether the subject factual arrangement is a scheme or a mere subscheme. Secondly, explicit recognition in subsection 80G(2) that it suffices under the South African GAAR if one part of an arrangement has the requisite primary purpose of obtaining the tax benefit, rather than requiring that the scheme as a whole be so characterised, means that the issue of identifying the actual scheme is largely nugatory.’

²⁴⁵ Peabody v FCT (1993) ATC 4104 at 4117.

²⁴⁶ Cassidy, J. (2009). The Holy Grail: The search for the optimal GAAR. *South African Law Journal*, vol. 126, at 752.

4.2.3 *The tax benefit requirement*

The definition of 'tax benefit' reflects an appreciation that tax benefits stem not only from the non-declaring of assessable income or manufacturing of deductions, but also making use of any concessions that might be provided under the legislative tax framework.²⁴⁷

'Tax benefit' is defined in s80L as including 'any avoidance, postponement or reduction of any liability for tax'. This definition of tax benefit focuses on any reduction of tax liability, instead of detailing specifically how a tax benefit might arise. 'Tax', is in turn, defined as including 'any tax, levy or duty imposed by this Act or any other law administered by the Commissioner'. This definition is exhaustive in nature and it encompasses any tax related benefit that might not have been covered by the specific terms used. The definition of 'tax' itself recognises that the benefit need not be a reduction of tax, but includes a reduction of any other levies, such as interest or penalties.

The original definition²⁴⁸ of 'tax benefit', was confined to the non-inclusion of an amount that would or might reasonably be expected to be included in the taxpayer's income, or the allowance of a deduction that would or might not have been expected to be allowable, but for the scheme.²⁴⁹

As this definition was exhaustive in nature, any other tax benefit, such as a rebate or credit, did not fall within the definition and thus was not subject to Part IVA. Amendments to the section were duly made, and in terms of s177C (4), a tax benefit applies to a scheme if:

²⁴⁷ Cassidy, J. (2009). The Holy Grail: The search for the optimal GAAR. *South African Law Journal*, vol. 126, at 755.

²⁴⁸ Under s177 C.

²⁴⁹ S177 C (1).

- An amount of income is not included in the assessable income of the taxpayer of a year of income; and
- An amount would have been included, or might reasonably be expected to have been included, in the assessable income if the scheme had not been entered into or carried out; and
- Instead, the taxpayer or any other taxpayer makes a discount capital gain.

The notion of a tax benefit in Australia also includes: a capital loss that would or might not have been reasonably expected to be incurred but for a scheme entered into after 3 pm on 29 April 1997; or a foreign tax credit that would or might not have reasonably been expected to be allowable but for a scheme entered into after 4 pm on 13 August 1998.

Clearly the South African approach, which defines ‘tax benefit’ in inclusionary, but also in expansive, terms is preferable to the approach in Part IVA.²⁵⁰ If one considers the way the two terms are interpreted in both GAARs, it can be concluded that the South African GAAR has a broader scope than its Australian counterpart.

In the ITAA there is a causal connection required between the scheme in question and the tax benefit. In s177C(1), the phrase ‘would or might not have been expected’ is used to highlight this causal link. ‘Tax benefit’ is defined in s177C as,

- ‘A capital loss that would or might not have been reasonably expected to be incurred, but for a scheme entered into after 3 pm 29 April 1997; or

²⁵⁰ Cassidy, J. (2009). The Holy Grail: The search for the optimal GAAR. *South African Law Journal*, vol. 126, at 752.

- A foreign tax credit that would or might not have reasonably been expected to be allowable but for a scheme entered into after 4 pm 13 August 1998’.

Peabody v FCT,²⁵¹ both the Full Court of the Federal Court and the High Court held that ‘section 177C(1)(a) requires a reasonable probability, not a mere possibility, that the taxpayer would have derived the income, but for the scheme.’²⁵² This test requires a prediction of the events that may have occurred if the scheme had not been entered into and the ‘predication must be sufficiently reliable for it to be regarded as reasonable’.²⁵³

There is no causal connection required under Part IIA, as long as there is a tax benefit, and the analysis then shifts to whether the sole or main purpose of the arrangement was to obtain that tax benefit. However, closely linked to s177C(1), is subsection 80E(1)(b)(i), which uses the phrase ‘would have’. The ‘would have’ test has nevertheless proven to be a significant limitation upon the applicability of Part IVA.²⁵⁴

4.2.4 *Purpose to obtain a tax benefit requirement*

It is not always clear when the taxpayer has overstepped the mark between acceptable and unacceptable behaviour. It is a requirement under both GAARs that the purpose underlying the scheme/arrangement was to obtain a tax benefit. Under s80A an ‘impermissible avoidance arrangement’ exists where, *inter alia*, the ‘sole or main’ purpose of the avoidance arrangement was to obtain a tax benefit.

²⁵¹ (1993) 93 ATC 4104 (1994) 94 ATC 4663.

²⁵² *Ibid*, at 4111-4112.

²⁵³ *Ibid*, at 4671.

²⁵⁴ Cassidy, J. (2009). The Holy Grail: The search for the optimal GAAR. *South African Law Journal*, vol. 126, issue 4, at 758.

In s80G(1), the party obtaining a tax benefit must prove that, ‘reasonably considered in light of the relevant facts and circumstances, obtaining a tax benefit was not the sole or main purpose of the avoidance arrangement’. Under s103 the onus of proving each of the elements of s103 lay with the Commissioner,²⁵⁵ and once he had established the presumption that the sole or main purpose was to obtain a tax benefit, the burden shifted to the taxpayer.

The shifting of the onus of proof under subsection 103(4) has been criticised on the basis that case law suggests that taxpayer’s *ipse dixit* may be insufficient to discharge the onus of proof.²⁵⁶ SARS asserts that the shifting of the onus to the taxpayer is valid given ‘taxpayers are the ones who have chosen their transactions (and the form in which they are cast) and have the most knowledge of and the greatest access to the facts’.²⁵⁷ The time for testing the purpose under Part IIA is when the arrangement is implemented. Under Part IVA, the time for testing the dominant purpose is generally the time at which the scheme was entered into or carried out, and by reference to the law as it then stood.²⁵⁸

In Part IVA, s177D requires that a person must have entered into the scheme with the ‘sole or dominant’ purpose of enabling the taxpayer to obtain a tax benefit. Subsection 177A (5) in turn provides that Part IVA may apply to a scheme involving more than one purpose where the ‘dominant’ purpose is the obtaining of a tax benefit. It has been asserted by the Australian courts that ‘dominant purpose’ is the ‘most influential and prevailing or ruling purpose’.²⁵⁹

²⁵⁵ The principle was established in *CIR v Conhage* (1999) 4 SA1149 (SCA), 61 SATC 391.

²⁵⁶ Brinker, E. (2001). The purpose requirement of the general anti-avoidance provision in South African fiscal law. *TSAR*, 158 at 160.

²⁵⁷ SARS Revised Proposals, at 20; SARS Interim Response, at 16.

²⁵⁸ *FCT v Spotlight Stores Pty Ltd* (2005) 2005 ATC 4001 at 4015; *FCT v Sleight* (2004) 2004ATC 4477 at 4511–12.

²⁵⁹ *FCT v Spotless Services Ltd* (1996) 96ATC 5201 at 5206 and 5210; *FCT v Spotlight Stores Pty Ltd* (2005) 2005ATC4001 at 4015.

The conclusion as to the dominant purpose under s177D must be reasonable to draw.²⁶⁰

Another point to be considered under both GAARs is the question of who is considered to have the purpose of obtaining a tax benefit. Under Part IIA the requirement is that 'its' sole or main purpose must be to obtain a tax benefit. The issue therefore is about the arrangement itself, and not any particular party. But then again the question arises as to whether an arrangement which is not a person can have a purpose on its own. Section 80G(1) also provides that 'the sole or main purpose of the avoidance arrangement...'. SARS has stressed that the purpose is to continually be determined objectively.²⁶¹

The South African provisions in this regard are said to be akin to the Australian GAAR.²⁶² The difference between the two is that in s177D, the requirement is that a person must have entered into the scheme with the sole or dominant purpose of enabling the taxpayer to obtain a tax benefit. The question posed by s177 D is directed at ascertaining the dominant purpose of the relevant person(s), not the dominant purpose of the scheme itself.²⁶³ The person that has the requisite purpose need not, however, be the taxpayer.²⁶⁴ It will suffice if the promoter of the scheme has a dominant purpose.²⁶⁵

²⁶⁰ Hart v FCT (2004) 2004 ATC 4599,4621.

²⁶¹ SARS Revised proposals, at 21.

²⁶² SARS Interim response, at 19.

²⁶³ Hart v FCT (2004) 2004 ATC 4599 at 4613; FCT v Spotlight Stores Pty Ltd (2005) 2005ATC4001 at 4015.

²⁶⁴ Cassidy, J. (2009). The Holy Grail: The search for the optimal GAAR. *South African Law Journal*, vol. 126, issue 4. at 767.

²⁶⁵ Vincent v FCT (2002) 2002 ATC 4490 at 4518–19; FCT v Sleight (2004) 2004 ATC 4477.

In some cases the actual parties to a scheme subjectively may not have any purpose, independent of that of a professional advisor, in relation to the scheme or part of the scheme, but that does not defeat the operation of s177D'.²⁶⁶

Section 177D requires an objective consideration, and thus is not based upon 'the fiscal awareness of a taxpayer'.²⁶⁷

The courts have held that s177D requires an,

'...objective conclusion to be drawn, having regard to the matters referred to in paragraph (b) of the section, but no other matters'. The actual subjective purpose of any relevant person is not a matter to which regard maybe had in drawing the conclusion'.

Subsection 80C(2) lists relevant factors that are indicative of arrangements that lack commercial substance:

- The legal substance of the avoidance arrangement as a whole is inconsistent with, or differs significantly from, the legal form of its individual steps;
- Round trip financing (as described in s80d);
- An accommodating or tax indifferent party (as described in s 80e); or
- Elements that have the effect of offsetting or cancelling each other.

Unlike the South African 'tainted elements', the factors that are indicative of a tax avoidance scheme are not additional to, but rather inter-connected with, the question whether the 'sole or dominant' purpose was to enable the taxpayer to obtain a tax

²⁶⁶ FCT v Consolidated Press Holdings Ltd(2001) 2001ATC4343 at 4360.

²⁶⁷ *Ibid.*

benefit.²⁶⁸

Subsection 177D (b) lists the following factors:

'(i) the manner in which the scheme was entered into or carried out;

(ii) the form and substance of the scheme;

(iii) the time at which the scheme was entered into and the length of the period during which the scheme was carried out;

(iv) the result in relation to the operation of this Act that, but for this Part, would be achieved by the scheme;

(v) any change in the financial position of the relevant taxpayer that has resulted, will result, or may reasonably be expected to result, from the scheme;

(vi) any change in the financial position of any person who has, or has had, any connection (whether of a business, family or other nature) with the relevant taxpayer, being a change that has resulted, will result or may reasonably be expected to result, from the scheme;

(vii) any other consequence for the relevant taxpayer, or for any person referred to in subparagraph (vi), of the scheme having been entered into or carried out; and the nature of any connection (whether of a business, family or other nature) between the relevant taxpayer and any person referred to in subparagraph (vi).'

²⁶⁸ Cassidy, J. (2009). The Holy Grail: The search for the optimal GAAR. *South African Law Journal*, vol. 126, issue 4, at 773.

Both sections identify common elements of tax avoidance schemes such as tax driven elements that lack commercial substance, non-arm's length transactions, and round trip financing. Section 177D of the ITAA requires an 'objective conclusion to be drawn, having regard to the matters referred to in paragraph (b) of the section, but no other matters'.²⁶⁹ Thus, unlike the South African 'tainted elements', the factors that are indicative of a tax avoidance scheme are not additional to, but rather inter-connected with, the question whether the 'sole or dominant' purpose was to enable the taxpayer to obtain a tax benefit.²⁷⁰

4.3. United Kingdom

The United Kingdom and South Africa both have anti-avoidance techniques that are meant to combat tax avoidance. In this segment I shall begin with an analysis of the anti-avoidance techniques employed in the United Kingdom, and thereafter I will compare and contrast the contents of anti-avoidance provisions in both states.

The anti-avoidance techniques in South Africa have been the subject of this research and have been discussed in detail above, therefore will not be repeated. It must be noted that complexity is a common aspect between the two legislations.

4.3.1 *Anti-avoidance techniques in the United Kingdom*

It has to be noted first that the United Kingdom does not have a GAAR and it relies on the judiciary to formulate anti-avoidance doctrines in the place of GAAR.

²⁶⁹ Peabody v FCT (1993) 93 ATC 4104 at 4113–14; Spotless Services Ltd v FCT (1993) 93 ATC 4397 at 4417; FCT v Sleight (2004) 2004 ATC 4477 at 4491–2,

²⁷⁰ Cassidy, J. (2009). The Holy Grail: The search for the optimal GAAR. *South African Law Journal*, vol. 126, issue 4, at 773.

GAAR has been rejected in the United Kingdom due to the uncertainty it creates regarding the operation of law.²⁷¹

As opposed to the general anti-avoidance provision in South African tax legislation, the United Kingdom has a set of alternative approaches to tax avoidance. Firstly, it has specific anti-avoidance rules that are designed to counter specific instances of tax avoidance. These specific rules are narrowly designed to prevent potential tax avoidance opportunities where taxpayers may attempt to frustrate the normal or expected operation of the law.²⁷² These rules have often been described as, ‘...smart bombs’ in contrast to ‘carpet bombs’ or ‘weapons of mass destruction’ that may be presented by general anti-avoidance provisions.²⁷³

To add on to the simplicity of anti-avoidance legislation, the United Kingdom also has targeted anti-avoidance rules (TAARS). They have been defined as a piece of anti-avoidance legislation designed to stop avoidance in a particular area of law. Typically a TAAR may be introduced to counter a wide spectrum of repeated avoidance in a particular area, where it is clear that existing legislative methods are not solving the problem. Alternatively, a TAAR may feature in a new area of law at the outset as a defence against potential exploitation. TAARs adopt a midway road between the application of the GAAR and detailed technical provisions aimed at countering every element of unacceptable tax avoidance.²⁷⁴

²⁷¹ Duff, D.G. & Alarie, B. (2008). The Legacy of UK Tax Concepts in Canadian Income UBC Faculty of Law. *British Tax Review*, vol. 2008, no. 3.

²⁷² Keating, M. (2008). GST tax avoidance: a New Zealand perspective on the application of div 165. *E-journal of tax research*, 8:64-69. Available from www.atax.unsw.edu.au/ejtr/content/issues/current/full_edition.pdf.

²⁷³ Evans, C. (2008). *Containing tax avoidance and anti-avoidance strategies*. [Online] Available from <http://lawbepress.com/cigiviewcontent.cgi?article=1115&context=unswwps>.

²⁷⁴ Freedman *et al.* (2008). *Alternatives to tax risks and tax avoidance: an analysis of a face to face corporate survey*. Oxford University centre for business taxation, WP 8/14, at 24. Available from http://www.sbs.ox.ac.uk/innopac.up.ac.za/centres/tax/Documents/working_papers/WP0814.pdf, at 16.

Lastly, the United Kingdom also adopted the principle-based legislation approach (PBL). PBL has been described as,

'... the principles-based approach to legislation seeks to include an expression of the policy intent behind the statute. Sometimes it is manifested in the form of 'purposive drafting' and is an approach which explicitly sets out the result the legislation is intended to achieve'.²⁷⁵

The PBL technique to drafting legislation can be used in anti-avoidance legislation to counter avoidance or to replace areas of the tax statute that have become too complex. Although the legislation is shorter than the legislation it replaces, the new legislation creates uncertainty as the principles upon which the legislation is based are not clear enough. The anti-avoidance legislations in both countries are *prima facie* complex.

4.3.2 GAAR v TAAR

TAARs are mini GAARs with the main difference being that GAARs are designed to be general and broad, thus aiming to capture a greater sphere of tax avoidance activity, whereas TAARs are more targeted and thus have a more narrow application.²⁷⁶

TAARs have the same aim as GAARs, i.e. to combat tax avoidance, but the nature of TAARs is narrower in scope than that of GAARs.

GAARs tend to be broad, and if a GAAR is too broadly designed, the judiciary have a tendency to adopt a narrow interpretation.²⁷⁷ In Australia, the wording of the GAAR was drawn up in very broad general terms and the courts adopted a narrow, literalistic approach to interpreting the GAAR provisions which rendered it largely ineffective

²⁷⁵ HMRC (2008) at 6. Available at <http://hmrc.gov.uk>.

²⁷⁶ Cashmere, M. (2003). The interrelation of scheme and purpose. *E-Journal of Tax Research*, at 1-44.

²⁷⁷ *Ibid* at 37.

deterrent to tax avoidance. It effectively made tax optional for those seeking out tax avoidance opportunities.²⁷⁸

Cashmere²⁷⁹ suggested that if the United Kingdom were to adopt a GAAR it has to be more targeted. He also suggested that if the content of the rule is more targeted, this would improve its chances of being applied as envisioned by Parliament.²⁸⁰ The HMRC has to be applauded for adopting TAARs as a means of reducing the complexity of anti-avoidance legislation. Some tax scholars are in support of a more targeted GAAR. Freedman²⁸¹ is of the view that a well drafted GAAR that encapsulates the intention of the legislature or Parliament will go a long way to aid the judiciary in interpreting GAAR by giving effect to the legislature's intention.

A more targeted approach will promote greater certainty in a tax system and this can be achieved²⁷⁸ by a GAAR, *inter alia*:

- Specifying specific objective criteria which targets types of tax avoidance activity which Parliament does not approve of; and
- Focusing on certain forms of behaviour and scheme characteristics that should be refrained from as a policy matter.

4.3.3 GAAR v PBL

The definition of PBL has been discussed previously. Certain differences and similarities are evident between these two anti-avoidance techniques. The main purpose of a GAAR is to preserve the outcomes intended by parliament.

²⁷⁸ *Ibid.*

²⁷⁹ *Ibid* at 39.

²⁸⁰ *Ibid.*

²⁸¹ Freedman, J. (2007). Interpreting tax statutes: tax avoidance and the intention of Parliament. *Law Quarterly Review*, at 20. [Online]. Available from <http://0international.westlaw.com.innopac.up.ac.za/result/default>.

Conversely, one of the main purposes of a PBL is to express the policy intent behind the legislation.

A consultation document was published in the United Kingdom December 2007²⁸² proposing a principle-based approach to avoidance involving financial products. The first form of principles-based drafting could more accurately be called ‘purpose-based drafting’.²⁸³ This is where it is sought to state Parliament’s intention in introducing legislation.²⁸⁴ The second form of principles-based drafting requires the tax rules themselves to be restated as principles.²⁸⁵ It is often very difficult to explain the principle underlying the tax provision.

A GAAR is restricted to the application of anti-avoidance transactions/schemes and is therefore not a charging provision; it is not designed to expand the tax base but to protect it.²⁸⁶ Conversely, a PBL can be incorporated in the formulation and drafting of charging provisions. Both techniques are, however, deemed to promote uncertainty and have therefore been criticised as anti-avoidance techniques. The GAAR has been criticised due to the uncertainty it creates pertaining to what constitutes legitimate tax planning and the difference between tax avoidance and tax planning.

4.3.4 Canada

Similar to South Africa, the legislature in Canada found its initial legislative attempts to combat tax avoidance ineffective. The South African GAAR seems to be a borrowed version of the Canadian GAAR in almost all respects.

²⁸² HM Treasury and HMRC. (2007). Principles-Based Approach to Financial Products Avoidance: A Consultation Document. Available at http://www.hm-treasury.gov.uk/consult_financialproducts_avoidance.htm.

²⁸³ Bowler, T. (2009). *Countering tax avoidance in the UK: which way forward?* Tax Law Review Committee Institute for Fiscal Studies, at 41.

²⁸⁴ *Ibid.*

²⁸⁵ *Ibid*, at 43.

²⁸⁶ SARS Explanatory Memorandum, at 6.

The requirements that must be met for a transaction to be considered as an avoidance transaction, as well as the wording under both GAARs, mirror one and the same thing.

The application of the GAAR in Canada involves three steps. It must be determined:

- (1) Whether there is a tax benefit arising from a transaction or series of transactions within the meaning of s245(1) and (2) of the Income Tax Act;
- (2) Whether the transaction is an avoidance transaction under s245(3), in the sense of not being 'arranged primarily for bona fide purposes other than to obtain the tax benefit';

and

- (3) Whether there was abusive tax avoidance under s254(4), in the sense that it cannot be reasonably concluded that a tax benefit would be consistent with the object, spirit or purpose of the provisions relied upon by the taxpayer. The burden is on the taxpayer to refute points (1) and (2), and on the Minister to establish point (3).

4.3.5 *Avoidance transaction v avoidance arrangement*

An 'avoidance transaction' is defined in s245(3) ITA as any transaction:

- (a) that, but for this section, would result, directly or indirectly, in a tax benefit, unless the transaction may reasonably be considered to have been undertaken or arranged primarily for bona fide purposes other than to obtain the tax benefit;

or

- (c) that is part of a series of transactions, which series, but for this section, would result, directly or indirectly, in a tax benefit, unless the transaction

may reasonably be considered to have been undertaken or arranged primarily for bona fide purposes other than to obtain the tax benefit.

This boils down to three elements that must be satisfied

- There must be a ‘transaction’ or a transaction that is ‘part of a series of transactions;’
- That transaction or a series would, but for the GAAR, result in a ‘tax benefit’,²⁸⁷ and
- It cannot reasonably be considered that the transaction (or a transaction in the series) was undertaken or arranged primarily for *bona fide* purposes other than to obtain the tax benefit.²⁸⁸

A ‘transaction’ is in turn defined as ‘an arrangement or event’ (s245(1) ITA). Under the South African GAAR the word ‘avoidance arrangement’ is used, as opposed to ‘transaction’ in Canada; but then under the definition of ‘avoidance arrangement’ a ‘transaction’ is included.

4.3.6 *Series of transactions/events v all parts/steps therein*

A ‘series of transactions or events’ is deemed under s248(10) ITA to ‘include any related transactions or events completed in contemplation of the series’. Thus if the factual scenario involves, for example, four transactions, each transaction in the series must be assessed to determine its underlying purpose.²⁸⁹

²⁸⁷ This is known as the ‘results test’.

²⁸⁸ This is known as the ‘purpose test’.

²⁸⁹ OSFC Holdings Ltd. v The Queen [2002] 2 EC. 288, [2001] 4 C.T.C. 82, 2001 D.T.C. 5471, 2001 FCA 260 [OSFC].

As long as the transactions are connected so as to be part of a series, it suffices if one transaction, one step, has the primary purpose of obtaining the tax benefit.²⁹⁰

Once one transaction is found to have that purpose, all the other transactions that are part of the series are tainted with the illegitimate purpose. Even if all other transactions in the series have a *bona fide* business or family purpose as their primary concern, or the series as a whole has as its primary purpose a *bona fide* concern, subsection 245(3) ITA will nevertheless be satisfied and each transaction will be an avoidance transaction.

This provision has, however, been subject to erroneous interpretation by the courts in Canada. One such court was in *Canadian Pacific Ltd. v The Queen*.²⁹¹ This case involved a weak-currency borrowing arrangement. The taxpayer borrowed funds in Australian dollars at a high interest rate and converted them into Canadian dollars (with a lower interest rate). The funds were to be used in its Canadian operations. Repayments were made pursuant to forward contracts that locked in the foreign exchange gains from an expected depreciation of the Australian dollar. Under Canadian tax laws, the taxpayer could obtain significant tax advantages through such weak-currency borrowings.²⁹²

This case involved what authors have described as a 'blatant tax avoidance scheme'²⁹³ that had been 'designed to obtain inflated interest deductions during the term of the loan and tax-preferred capital gains on repayment of the principal amount of the loan. The court was adamant that the GAAR did not apply to the arrangement.

²⁹⁰ *Ibid.*

²⁹¹ [2002] 3 F.C. 170.

²⁹² Duff, D.G. (2001). Weak-Currency Borrowings and the General Anti-Avoidance Rule in Canada: From Shell Canada to Canadian Pacific. *I.B.F.D.*, 233.

²⁹³ Duff, D.G. (2001). Weak-Currency Borrowings and the General Anti-Avoidance Rule in Canada: From Shell Canada to Canadian Pacific. *I.B.F.D.*, 233.

Bonner T CJ held that because the series as a whole had the *bona fide* purpose of borrowing capital to be used for business purposes, the GAAR could not apply, even though a transaction in the series was undertaken for tax reasons.²⁹⁴ He also concluded that ‘... [n]o transaction forming part of the series can be viewed as having been arranged for a purpose which differs from the overall purpose of the series.’

The Federal Court on appeal reiterated that the ‘words of the Act require consideration of a transaction in its entirety and it is not open to the Crown artificially to split off various aspects of it in order to create an avoidance transaction.’ In this case the overall purpose of borrowing was held to prevent the GAAR applying to the tax benefit arrangement, despite the extended definition of transaction.

A similar trend is evident in the South African GAAR that is closely linked to this provision. In South Africa, reference is made to ‘steps or parts of an arrangement’ which also recognises that an arrangement includes ‘all steps therein or parts thereof’. Broomberg²⁹⁵ submits that the new arrangement definition does not address problems that have arisen in the jurisdictions from which the wording of this new definition was borrowed. He questions whether the Commissioner could apply the GAAR to a step or part in an arrangement where it loses its commercial substance as a result of being considered in isolation, and concludes that the answer to such question will have to await consideration in court.²⁹⁶

4.3.7 ‘Tax Benefit’ requirement under both GAARs

A ‘tax benefit’ is broadly defined in s245(1) ITA as ‘a reduction, avoidance or deferral of tax or other amount payable under this Act or an increase in a refund of tax or other amount under this Act.’

²⁹⁴ *Ibid*, at para. 27.

²⁹⁵ Broomberg, E.B.(2007). Then and Now-II. *Tax Planning Corporate and Personal*, 21.

²⁹⁶ *Ibid*.

The definition reflects an appreciation that tax benefits stem not only from not declaring assessable income or claiming deductions that would not otherwise be available, but also making use of any concessions that might be provided under the legislative tax framework. The definition of 'tax benefit' in South Africa has been dealt with in the previous chapter. Both GAARs nonetheless provide appropriate and comprehensive definitions of the concept.

The mere existence of a tax benefit does not *per se* attract the Canadian GAAR. Coupled with the existence of a tax benefit must also be the requisite nexus between the tax benefit and the 'transaction/series of transactions'. The question will be 'but for' the GAAR, would a tax benefit directly or indirectly accrue to the taxpayer? (Subsections 245(2) and (3) ITA). This is known as a 'results test'. 'The results test' requires a determination of whether a transaction or series of transactions would, but for the GAAR, result in a tax benefit.

The determination is made through a process known as 'benchmarking'. Under this approach the court identifies a 'benchmark' transaction, 'a norm or standard,' that the taxpayer might otherwise reasonably have undertaken but for the tax benefit, and against this the existence of a tax benefit is determined. Under the South African GAAR there is no formal test to determine the existence of a tax benefit.

4.3.8 *Misuse or abuse concept*

The 'exception' to subsection 245(2) ITA is found in subsection 245(4) ITA. This states that subsection 245(2) ITA will not apply to a transaction where,

'...it may reasonably be considered that the transaction would not result directly or indirectly in a misuse of the provisions of this Act or an abuse having regard to the provisions of this Act, other than this section, read as a whole'.

Four key issues have arisen in regard to this provision in the Canadian jurisprudence.²⁹⁷

In *McNichol v. The Queen*,²⁹⁸ it was highlighted that the whole idea of subsection 245(4) ITA is clearly to consider the substance, not the legal form, of the avoidance transaction, to determine if there has been a misuse of the particular provision or an abuse of the Act as a whole. As the technical notes state,

*‘...a transaction structured to take advantage of technical provisions of the Act but which would be inconsistent with the overall purpose of these provisions would be seen as a misuse of these provisions.’*²⁹⁹

The section does not create an alternative test with regard to the definition of an avoidance transaction. Instead, it indicates the proper construction of s245 with respect to transactions that appear to be tax-motivated but that, arguably, do not produce tax results that frustrate the intention of Parliament. Thus, subsection 245(4) is a complement to the non-tax purpose test and is consistent with the general approach of a modern, as opposed to a literal, interpretation of the Act.³⁰⁰

The ambience within which the ‘misuse or abuse’ provision is used is different in the South African GAAR. From the above discussion it is evident that in Canada it is treated as an exception. The question whether a literal interpretation or a purposive approach be adopted when determining if there has been a misuse or abuse of a provision(s) of the Act has been dealt with extensively in Chapter 3.

²⁹⁷ Cassidy J. (2006). To GAAR or not to GAAR. *Ottawa Law Review*, at 299.

²⁹⁸ [1997] 2 C.T.C. 2088, 97 D.T.C. 111.

²⁹⁹ SARS Explanatory Notes, at 432.

³⁰⁰ Dodge, D.A. (1988). A New and More Coherent Approach to Tax Avoidance. *Canadian Tax Journal*, 1, at 36.

CHAPTER 5. CONCLUSION

The prevalence of tax avoidance activity is a matter of utmost concern as it threatens to erode the tax base, promotes unfairness in the tax system, encourages non-compliant behaviour, and disregards the integrity of tax systems; thereby introducing a host of unwanted complexities to those systems.³⁰¹

Tax legislation has been modified in different parts of the world in a bid to counter tax avoidance. The Australian anti-avoidance rule was initially contained in s260 and it became ineffective in combating tax avoidance. This was largely due to the courts using an excessively literal interpretation of the provision, rather than a purposive test.

In a similar fashion, South Africa also repealed the ineffective s103 and replaced it with s80 A-L. In Canada it was concluded that the respective general avoidance provisions were of limited application and ineffective to combat the sophisticated tax avoidance schemes promoted by tax advisers. In the United Kingdom no GAAR exists, but rather they make use of TAARs and PBLs, which are more targeted and aim at specific transactions.

Therefore many loopholes and much uncertainty taints the success of these GAARs in curbing tax avoidance.

Though South Africa has recently enacted a new GAAR, it has arguably increased the complexity of South Africa's anti-avoidance legislation. Highly complex legislation does not necessarily achieve the purpose of stopping avoidance; the more detailed the rules, the more opportunity there may be for those so wishing to find and exploit loopholes.

³⁰¹Evans, C. (2008). *Containing tax avoidance and anti-avoidance strategies*. Available from <http://law.bepress.com/cgi/viewcontent.cgi?article=1115&context=unswpps>, at 13.

Efforts to curb tax avoidance through tax reform and accompanying legislative changes, coupled with detailed and precise legislation, have contributed to the complexity of tax legislation.³⁰² This observation fulfils the analysis and results that were made throughout this research. Given the complexity of tax avoidance schemes and the complicated manner in which many businesses operate, the complexity of tax systems appears to be a natural progression.³⁰³

Due to the complexity of tax laws on a global scale, brought about by the introduction of anti-avoidance legislation, it raises the question whether the current anti-avoidance legislative techniques in South Africa are effective in the fight against tax avoidance or whether the complexity of tax legislation is the breeding ground for further tax avoidance opportunities.³⁰⁴ A further challenge presents itself in the shortage of tax professionals required to manage the provisions of the new complex GAAR.³⁰⁵

From the above observations in this paper, we see that GAARs create uncertainty amongst taxpayers regarding legitimate tax benefits because they are more often than not too broadly worded. Freedman³⁰⁶ has warned that a GAAR that is too broad could ‘... start to remove the nature of the GAAR as a broad principle and turn it into a detailed set of rules which could damage its essence’.

It has been argued by some scholars that this element of uncertainty is deliberately present to act as a deterrent to tax avoidance.³⁰⁷

³⁰² Freedman, J. *et al.* (2008). *Alternatives to tax risks and tax avoidance: an analysis of a face to face corporate survey*. Oxford University centre for business taxation, WP 8/14, at 24.

³⁰³ Freedman, J. (2007). Interpreting tax statutes: tax avoidance and the intention of Parliament. *Law Quarterly review*, at 23.

³⁰⁴ Freedman, J. *et al.* (2008). *Alternatives to tax risks and tax avoidance: an analysis of a face to face corporate survey*. Oxford University centre for business taxation, WP 8/14, at 24.

³⁰⁵ Drummond, B. (2006). A purposive approach to the drafting of tax legislation. *British Tax Review*. Available at <http://0-international.westlaw.com.innopac.up.ac.za>.

³⁰⁶ Freedman, J. (2007). Interpreting tax statutes: tax avoidance and the intention of Parliament. *Law Quarterly review*, at 21.

³⁰⁷ Loutinsky, G. (2011). Gladwellian Taxation: Deterring Tax Abuse Through General Anti-

Some have argued that the element of uncertainty within a GAAR created by the use of broad and imprecise language is required so as to enable a GAAR to capture future tax avoidance arrangements in its anti-avoidance net.³⁰⁸ Freedman³⁰⁹ also concluded that ‘an element of uncertainty is necessary within an anti-avoidance regulatory framework, as the converse which is achieved by detailed prescriptive rules leads to avoidance or creative compliance. He also observed that general anti-avoidance principles, such as a GAAR, provide an opportunity to create a sensible regulatory framework to debate what is acceptable and foster an enhanced climate of understanding.’³¹⁰

It is the writer’s contention that South Africa should consider a more targeted GAAR to achieve the desired effectiveness of the current GAAR.

Widely drafted GAARs are also a dangerous tool in the hands of tax authorities, as it would empower them to override specific provisions of the Act. One tax scholar also concluded that ‘if a GAAR is too broadly designed, the judiciary have a tendency to adopt a narrow interpretation’.³¹¹

Although South Africa’s GAAR has been criticised as being excessively harsh, detailed and complex,³¹² it addresses the shortcomings of the old GAAR in s80G of the Income Tax Act. The onus of proving the existence of a tax benefit has now shifted from SARS to the taxpayer, in that the taxpayer must now prove that the sole or main purpose for entering into a transaction was other than to obtain a tax benefit.

Avoidance Rules. *Houston Business and Tax Law Journal*, Vol. 12, No. 1.

³⁰⁸ Keating, M. (2008). GST tax avoidance: a New Zealand perspective on the application of div 165. *E-journal of tax research*, at 67.

³⁰⁹ Freedman, J. (2007). Interpreting tax statutes: tax avoidance and the intention of Parliament. *Law Quarterly Review*, at 12.

³¹⁰ Freedman, J. *et al.* (2008). *Alternatives to tax risks and tax avoidance: an analysis of a face to face corporate survey*. Oxford University Centre for Business Taxation, WP 8/14, at 13.

³¹¹ Cashmere, M. (2008). A GAAR for the United Kingdom? The Australian experience. *British Tax Review*.

³¹² Drummond, B. (2006). A purposive approach to the drafting of tax legislation. *British Tax Review*. Available at <http://0-international.westlaw.com.innopac.up.ac.za>, at 10.

One scholar has concluded that 'the experience since the implementation of the new GAAR has been positive for SARS as taxpayers have backed away from schemes lacking commercial substance'.³¹³

It is unrealistic to expect any tax system to exist without tax avoidance. That should not be the aim of anti-avoidance measures. Instead, it is a case of finding the right balance so that taxpayers can carry on their business and lives without undue restriction (and at times can be incentivised by the tax system to act in a particular way) but also so that the need for government to raise sufficient revenues is met.³¹⁴

It is the writer's contention that adopting lengthy and complex tax legislation is not always ideal, but it would be acceptable if the result were a clear, efficient tax system where the line between what is within particular tax rules and what is not, is explained properly.

Most of the provisions in the South African GAAR were borrowed from other legislatures around the world. As noted, the GAARs in Australia and Canada had to be altered for the same reasons that the GAAR in South Africa was altered. This was largely due to the fact that the GAARs had also proved to be ineffective deterrents in curbing tax avoidance. Part IIA, when compared with anti-avoidance techniques in other legislatures, carries many positive aspects.

The review of the use of a GAAR leads to the conclusion that a GAAR on its own would not provide a solution. We have also seen that TAARs are not the solution on their own. However, where a particular avoidance can be clearly targeted, a TAAR may be the most appropriate solution.

³¹³ Liptak, E. (2008). Battling with boundaries: the South African GAAR experience. In J. Freedman J (ed.). *Beyond Boundaries*. UK: United Kingdom Oxford University Centre for Business Taxation, at 7.

³¹⁴ Bowler, T. (2008). *Tackling tax avoidance in the United Kingdom*. In J. Freedman (ed.). *Beyond Boundaries*. UK: Oxford University Centre for Business Taxation, at 2.

It is clear that no jurisdiction has found a perfect solution, and the use of GAARs in varying forms has had mixed success.³¹⁵

³¹⁵ Bowler, T. (2008). *Tackling tax avoidance in the United Kingdom*. In J. Freedman (ed.). *Beyond Boundaries*. UK: Oxford University Centre for Business Taxation, at 48.

REFERENCES

- Bendel, E. (2006). Tax avoidance-is the party over? *Without Prejudice*, at 21.
- Bernard, G. (2010). Section 80C (1): A Lack of commercial substance-an explanation of the phrase 'A significant tax benefit'. *Tax Talk*, November/December.
- Bowler, T. (2008). *Tackling tax avoidance in the United Kingdom*. In J. Freedman (ed.). *Beyond Boundaries*. United Kingdom: Oxford University Centre for Business Taxation.
- Bowler, T. (2009). *Countering tax avoidance in the UK: which way forward?* UK: Tax Law Review Committee Institute for Fiscal Studies.
- Brinker, E. (2001). The purpose requirement of the general anti-avoidance provision in South African fiscal law. *TSAR*, 158.
- Broomberg, E.B. (2007). Then and Now II. *Tax Planning Corporate and Personal*, 21.
- Broomberg, E.B. (2007). *The new general anti-avoidance rule*. SAFA seminar, Cape Town.
- Cashmere, M. (2003). The interrelation of scheme and purpose. *E-Journal of Tax Research*, 110.
- Cassidy, J. (1995). Peabody v FCT and Part IVA. *Revenue Law Journal*, vol. 5, issue 2.
- Cassidy J. (2006). To GAAR or not to GAAR. *Ottawa Law Review*, at 299.

Cassidy, J. (2009). The Holy Grail: The search for the optimal GAAR. *South African Law Journal*, vol. 126, issue 4740.

Cilliers, C. (2008). Thou shalt not peep at thy neighbour's wife: Section 80A(c)(ii) of the Income Tax Act and the abuse of rights. *The Taxpayer*, May, 85-92.

Clegg, D. (2002). Business purpose test. *Tax Planning Corporate and Personal*, 16.

Clegg, D. (2007). Use it or abuse it. *Tax Planning*, vol. 21.

Clegg, D. & Stretch, B. (2010). *Income Tax in South Africa*. Durban: LexisNexis.

Davies *et al.* (2007). *Juta's Income Tax*. Durban: Butterworths.

Davies *et al.* (2009). The sole or main purpose test-subjective or objective? *The Taxpayer*, October at 181.

De Koker, A.P. (2009). *Silke on South African Income Tax*. Durban: Lexus Nexus.

Dodge, D.A. (1988). A New and More Coherent Approach to Tax Avoidance. *Canadian Tax Journal*, 1.

Drummond, B. (2006). A purposive approach to the drafting of tax legislation. *British Tax Review*. Available at <http://0-international.westlaw.com.innopac.up.ac.za>.

Duff, D.G. (2001). Weak-Currency Borrowings and the General Anti-Avoidance Rule in Canada: From Shell Canada to Canadian Pacific. *I.B.F.D.*, 233.

Duff, D.G. & Alarie, B. (2008). The Legacy of UK Tax Concepts in Canadian Income UBC Faculty of Law. *British Tax Review*, vol. 2008, no. 3.

Ensor, L. & Tempkins, S. (2005). *SARS unveil plan to combat tax avoidance*. Business Day, 4 November.

Evans, C. (2008). *Containing tax avoidance and anti-avoidance strategies*. Available from <http://law.bepress.com/cgi/viewcontent.cgi?article=1115&context=unswwps>.

Freedman, J. (2007). Interpreting tax statutes: tax avoidance and the intention of Parliament. *Law Quarterly Review* [Online]. Available from <http://international.westlaw.com.innopac.up.ac.za/result/default>.

Freedman, J., Loomer, G. & Vella, J. (2008). *Alternatives to tax risks and tax avoidance: an analysis of a face to face corporate survey*. Available from http://www.sbs.ox.ac.uk.innopac.up.ac.za/centres/tax/Documents/working_papers/WP0814.pdf.

Gad, R. (2005). Tax avoidance- another view, same conclusion. *Without Prejudice*.

Grbich, Y. (1983) Problems of tax avoidance in Australia. In J.G. Head (ed.). *Tax Issues of the 1980s*. Australia: Australian Tax Research Foundation.

Greggy, M. (2008). Avoidance and *abus de droit*: The European Approach in Tax Law. Available at <http://www.austlii.edu.au/au/journals/eJTR/2008/2.html>.

Hauxham, K & Haupt, P. (2007). *Notes on South African Income Tax*. Cape Town: Hedron.

HMRC. (2008). Available at <http://hmrc.gov.uk>.

HM Treasury and HMRC. (2007). *Principles-Based Approach to Financial Products Avoidance: A Consultation Document*. Available at http://www.hm-treasury.gov.uk/consult_financialproducts_avoidance.htm.

IAS. (2011). *International Accounting Standards*. Available at

www.iasplus.com/standard/standard.htm.

Investopedia. (2011). *Tax Avoidance*. Available at http://www.investopedia.com/terms/t/tax_avoidance.asp.

Jarvis, J. (1996). Things are Seldom What They Scheme. *Juta's Business Law*, 4.

Joubert, W.A. & Faris, J.A. (2001). *The law of South Africa*. Vol. 25, part 1. Durban: Butterworths.

Keating, M. (2008). GST tax avoidance: a New Zealand perspective on the application of div 165. *e-Journal of Tax Research*, 8:64-69. [Online] Available from www.atax.unsw.edu.au/ejtr/content/issues/current/full_edition.pdf.

Kellaway, E.A. (1995). *Principles of legal interpretation: statutes, contracts and wills*. Durban: Butterworths.

Liptak, E. (2008). *Battling with boundaries: the South African GAAR experience*. In J. Freedman (ed.). *Beyond Boundaries*. UK: Oxford University Centre for Business Taxation.

Loutinsky, G. (2011). Gladwellian Taxation: Detering Tax Abuse Through General Anti-Avoidance Rules. *Houston Business and Tax Law Journal*, Vol. 12, No. 1.

Louw, I.D.P. (2007). The New General Anti-Avoidance rule: A comprehensive discourse on this statute, at p24. Available at lawspace.law.uct.ac.za/dspace/bitstream/2165/357/.../LWXIZA001.pdf.

Mazansky, E. (2006). A new GAAR for South Africa-The Duke of Westminster is Struck a Blow. *Bulletin for International Fiscal Documentation*, 59, 3.

Meyerowitz, D. (2005). What is tax avoidance? *The Taxpayer*.

OECD. *International Tax Terms for the participants in the OECD Programme of Cooperation with Non-OECD Economies*. Available at www.oecd.org.

Oguttu, A. (2007). *Curbing offshore tax avoidance: the case of South African companies and trusts*. Available at <http://0.uir.unisa.ac.za.innopac.up.ac.za/dspace/bidstream/10500/1929/1/thesis/pdf>.

Olivier, L. & Davis, D.M. & Uruquhart, G. (2009). *Juta's Income Tax*. Durban: Lexis Nexus.

SARS. (2005). *Discussion Paper on Tax Avoidance and Section 103 of the Income Tax Act 1962 (Act No 58 of 1962)*. Pretoria: SARS.

SARS. (2006). Explanatory Memorandum, Revenue Laws Amendment Bill 2006. Pretoria: SARS. Available at www.sars.gov.za.

SARS. (2006). *Revised Proposals on Tax Avoidance and Section 103 of the Income Tax Act, 1962*. Available at www.sars.gov.za.

SARS. (2006). *Tax Avoidance and Section 103 of the Income Tax Act, 1962: An Interim Response*. Available at www.sars.gov.za.

SARS. (2010). *Draft Comprehensive Guide to the GAAR*. Available at www.sars.gov.za.

South African Concise Oxford Dictionary. (2002). *Corporate*. Available at <http://www.ato.gov.au/corporate/content.aspx?doc=/content/75159.htm&page=122>.

Stiglitz, J.E. (1985). The General Theory of Tax Avoidance. *National Tax Journal*, 38 at 325, 337.

Thersby, K. (2007). *Exactly what is a tax avoidance arrangement?* Moneyweb's Tax Breaks. Available at <http://www.moneywebtax.co.za>.

Ulph, D. (2009). *Avoidance policies: a new conceptual framework*. Available from http://www.sbs.ox.ac.uk/centeres/tax/Documents/working_papers.

Van Schalkwyk, L. & Geldenhuys, B. (2009). Section 80A(c)(ii) of the Income Tax Act and the scope of Part II A. *Accountancy SA*. Available at <http://www.accountancysa.org.za/resources/ShowItemArticle.asp?ArticleId=1792&Issue=1086>.

Van Schalkwyk, L. & Geldenhuys, B. (2010). The Nature of the purpose requirement of an impermissible tax avoidance arrangement. *Journal for Juridical Science*, 35(1) 1:72-92.

Wiese, I. (2006). Let the games (or pain?) begin. *Without Prejudice*, at 32.

Williams, R.C. (1997). The 1996 amendments to the General Anti-Avoidance Section of the Income Tax Act. *SALJ*, vol, 114, 675.

Williams, R.C. (2009). *Smoke and mirrors or genuine commercial venture?* PriceWaterHouseCoopers Synopsis. Available at www.pwc.co.za/en_ZA/za/assets/.../pwc-synopsis-september2009.pdf.

Cases:

Canadian Pacific Ltd. v. The Queen [2002] 3 F.C. 170.

Challenge Corporation Ltd v. Commissioner of Inland Revenue [1987] AC 155.

CIR v Conhage (Pty) Ltd 1999 4 SA 1149 (SCA).

CIR v King 1947 2 SA 196 (A).

Commissioner for the South African Revenue Service v Brummeria Renaissance (Pty) Ltd and Others (391/06) [2007] ZASCA 99; [2007] SCA 99 (RSA); [2007] 4 All SA 1338 (SCA) ; 2007 (6) SA 601 (SCA) (13 September 2007).

CSARS v NWK (27/10) [2010] ZASCA 168 (1. December 2010)

Erf 3183/1 Ladysmith (Pty) Ltd v CIR 1996 3 SA 942 (A).

Estate G v Commissioner of Taxes 1964 (2) SA 701 SR,26 SATC 168 at 173-174.

FCT v Newton (1958) 2 All ER 759 (PC).

FCT v Peabody (1994) 94ATC 4663.

FCT v Spotlight Stores Pty Ltd (2005) 2005 ATC 4001.

Hart v FCT (2004) 2004 ATC 4599, 4621.

Meyerowitz v CIR 1963 3 SA 863 (A).

Modderfontein Deep Levels Ltd v Feinstein, 1920 TPD 288. 23

Ovenstone v SIR 1980 (2) SA 721(A), 42 SATC 55.

Palser v Grinling 1948 A.C 291.

Peabody v FCT(1992) 92 ATC 458 (1993) ATC 4104:(1994) 94 ATC 4663.

R Ltd and K Ltd v COT.

R v Mears(1997) 37 ATR 321.

SBI v Lourens Erasmus (Edms) Bpk 1966 (4) SA 434 (A), 28 SATC 233.

SIR v Gallagher 1978 (A) SA 463, 40 SATC 39.

SIR v Geustyn, Forsyth and Joubert 1971 3 SA 763 (A).

Spotless Services Ltd v FCT(1995) 95 ATC4775.

Tillmanns Butcheries Pty Ltd v Australasian Meat Industry Employees Union (1979) 42 FLR 331.

Vestey's (Lord) Executors & another v Inland Revenue Commissioners (1949) 1 AER, 1108.

Woods v Watters 1921 AD 303.