A comparative study of the complexity of trust tax legislation in selected Southern African Development Community countries

by

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ABSTRACT

For many years tax jurisdictions have encountered challenges with the concept of the taxation of trusts. The trust concept itself conjures up thoughts of complexity. The development of the trust as a structure and the subsequent colonial influence on the development of trusts in Africa, resulted in different applications of the common law trust principle in tax legislation. This study explores the complexity of the trust tax legislation by way of a comparison of the legislation in selected Southern African Development Community (SADC) countries.

The study applies a qualitative approach to compare the trust tax legislation of the selected SADC tax jurisdictions in an effort to assess the complexity involved in the taxation of trusts. The research methodology employed is doctrinal (black letter law) and includes an analysis of the legislation of the selected jurisdictions.

The study reveals substantial similarities in the terminology used in the taxation of trusts in the selected jurisdictions. In comparing the legislation of the jurisdictions that make provision for the flow through principle with those of the jurisdictions that do not make provision for the flow through principle, a larger element of complexity in the legislation becomes apparent with wider legislative design differences. Additionally, jurisdictions that make provision for the flow through principle also introduce anti-avoidance legislation to curb the misuse of income attributed to the beneficiaries of trusts. This anti-avoidance legislation creates additional complexity in the legislation.

Key terms

Complexity, flow through principle, SADC, tax, taxation, tax legislation, trusts.

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LIST OF ABBREVIATIONS AND ACRONYMS

Table 1: Abbreviations and acronyms used in the study

Abbreviation/Acronym	Meaning
AICPA	The American Institute of Certified Public Accountants
Botswana ITA	Botswana Income Tax Act, Cap 52:01
DTC	South African Tax Review Committee or Davis Tax Committee
Eswatini ITO	Eswatini Income Tax Order in Council No 21 of 1975
Franzen Commission	Commission of Enquiry into Fiscal and Monetary Policy in South Africa
Katz Commission	Commission of Inquiry into Certain Aspects of the Tax Structure of South Africa
Lesotho ITA	Lesotho Income Tax Act No 9 of 1993
Malawi TA	Malawi Taxation Act Chapter 41:01
Margo Commission	Commission of Inquiry into the Tax Structure of the Republic of South Africa
Mauritius ITA	Mauritius Income Tax Act of 1995
Namibia ITA	Namibia Income Tax Act 24 of 1981
SADC	Southern African Development Community
SARS	South African Revenue Service
South African ITA	South Africa Income Tax Act No 58 of 1962
Steyn Committee	Committee of Enquiry into the Income Tax Act
Tanzania ITA	Tanzania Income Tax Act of 2004, Chapter 332
TPCA	Trust Property Control Act, 57 of 1988
UK	United Kingdom
USA	United States of America
Zambia ITA	Zambia Income Tax Act No 3 of 1997, Chapter 323
Zimbabwe ITA	Zimbabwe Income Tax Act Chapter 23:06

CHAPTER 1: INTRODUCTION

1.1. BACKGROUND

“If we don't do something to simplify the tax system, we're going to end up with a national police force of internal revenue agents” (Leon Panetta, Former White House Chief of Staff in James, 2018).

Modern-day tax systems are inclined to become highly complex over a period of time, transpiring from accumulated accretions of statutes, regulations, administrative practices, bureaucratic conventions and evolving societal norms (Steyn & Stiglingh, 2016:157; World Bank, 2009:11). Since historical times, evidence can be found of complaints by taxpayers who deemed tax systems to be complex. It is also evident from the literature that tax complexity has been a popular focus area for research and tax reform activities (Budak & James, 2016:430; Pollack, 1993:341, McCaffery, 1990:1267, Burton & Karlinsky, 2016:61-66).

Adam Smith, a Scottish philosopher credited as the founder of modern-day public economics, formulated the widely recognised principles of a good tax system (Mizuta & Sugiyama, 2016:vii). These principles are tax equity (also known as tax fairness), tax certainty, convenience of paying tax and economical tax collection (Smith, 1776:644). A complex tax system can be viewed as one of the main enemies of the noble tax principles advocated by Smith (Tanzi, 2013:14). In relation to tax equity, a complex tax system may obscure an objective assessment of the effectiveness of a tax system towards reaching horizontal and vertical equity (Tanzi, 2013:14). Tax certainty and convenience objectives are essentially destroyed by complex tax systems, which may create an additional economic burden for taxpayers through increased costs of compliance and tax administration (Tanzi, 2013:14-15).

These consequences of a complex tax system may culminate in taxpayers’ perceptions on the fairness of the tax burden and finally vest in their decision to be tax compliant or not (Tanzi, 2013:16). The fairness principle of an efficient tax system and its relationship to tax

compliance has enjoyed much attention in research (Alm, 2019:366,369; Slemrod, 2007:39,41; Braithwaite, 2003:279; Atawodi & Ojeka, 2012; Rosid, Evans & Tran-Nam, 2019; James & Alley, 2002:33,36; Engida & Baisa, 2014:433-436). In this context, it is necessary to understand the concept of tax compliance. Randlane (2016:9) defines tax compliance by a taxpayer as the voluntary declaration, submission and payment of the calculated tax obligation (provided that the tax obligation is calculated according to the relevant tax legislation). Randlane continues, stating that compliance does not necessarily refer to the willingness of a taxpayer to comply, but to the fact that the taxpayer does actually comply – whether voluntary or due to enforcement actions by the tax authority. James and Alley (2002:29) state that the most basic definition of compliance may be described as the degree of conformity with which the taxpayer adheres to the tax legislation. They also state that tax compliance may more accurately be described as a consecution of definitions that include contributions from other disciplines including economics, behavioural science and law enforcement (James & Alley, 2002:29). In other words, tax compliance encapsulates characteristics from various fields of study including law, economics and behavioural science.

Research performed in the field of tax compliance mainly emanates from two perspectives (Alm, 2019:254). Firstly, from an economic perspective, Allingham and Sandmo (1972) utilise Becker's Economics-of-Crime Theory to formulate their Rational Choice Theory (also known as the Expected Utility Theory or the Allingham and Sandmo Model) (Alm, 2019:254; Slemrod, 2007:35). Secondly, from a behavioural perspective, the Moral Sentiments Theory finds application in the research of tax compliance (Alm & Sheffrin, 2017:9). These theories are discussed in more detail below.

The Rational Choice Theory is based on the economic impact of a decision to avoid or evade tax, as opposed to the value of full compliance (Güzel, Őzer & Őzcan, 2019:81). In other words, this theory explains the economic impact of a decision by a taxpayer to either comply or not to comply with his tax obligation. The theory thus considers the financial implication between the costs of detecting non-compliance (combined with the probability of detection) as opposed to the cost of full compliance.

From a behavioural perspective, the Moral Sentiments Theory determines that tax compliance by taxpayers is influenced by non-economic factors including tax morality, demographic characteristics, impression of tax justice, trust in the government and religious beliefs (Güzel, Őzer & Őzcan, 2019:81). This theory entails that taxpayers may be more likely to voluntarily comply when the factors mentioned above influence the decision to comply with the tax obligation.

In summarising the different compliance theories, the economic perspective on tax compliance proposes that financial punitive measures may be instituted against non-compliant taxpayers, whereas the Behavioural Perspective Theory on tax compliance endorses a voluntary or unforced approach to compliance by taxpayers.

Notwithstanding the above, the level of tax compliance has a significant impact on revenue collected by governments (Güzel, Őzer & Őzcan, 2019:81). Variables influencing taxpayer compliance levels include taxpayers' perceptions of role players, including government, authorities, tax practitioners and other taxpayers. Information on these variables may assist governments in formulating and improving tax policies and strategies to create a more efficient tax system (Güzel, Őzer & Őzcan, 2019:81).

Alley and Bentley (2005:586-588) tabulate the principles of an efficient tax system as highlighted in various reports, guides, articles and research papers. The authors identify that simplicity became a prominent characteristic in the design of a tax system from as early as 1966.

The pursuit of tax simplification is a result of the growing worldwide complexity of tax systems (Fleming, 2015:232; James, Sawyer & Wallschutzky, 2015:283; McCaffery, 1990:1267; Krever, 2003:468; Laffer, Winegarden & Childs, 2011:21). This pursuit of tax simplification requires a clear understanding of what the tax complexity consists of, the ultimate goal of the simplification and achieving a balance between simplification and policy goals (James, Sawyer & Wallschutzky, 2015:299). The aim of simplifying a tax system is to move towards increased levels of compliance, whilst reducing costs in the context of economic and social objectives (World Bank, 2009:6). A simplified tax system is achieved when a taxpayer can comply by easily calculating, filing and paying his/her tax

liability with limited costs, while allowing for tax administrators to easily verify the taxpayer's information and confirm that the correct amount of tax was calculated (World Bank, 2009:6).

The present study considers tax simplification from a South African perspective. The simplification of tax legislation in itself is a complicated process, as tax legislation may often be the product of numerous changes made to the legislation over an extended period (Steyn & Stiglingh, 2016:157). In South Africa the tax system became complex over numerous years (Steyn & Stiglingh, 2016:157). This is mainly the result of periodic amendments and additions to the original South African Income Tax Act (No 58 of 1962) (South African ITA), changes in administrative processes and changes in the South African politics and society (Steyn & Stiglingh, 2016:157). The next section provides a brief historical perspective on tax system complexity in South Africa from which the rationale of this study is extracted and clarified.

1.2. RATIONALE FOR THE STUDY

The perception that the South African tax system is complex is confirmed by numerous research studies (Lubbe & Nienaber, 2012:698; Oberholzer & Stack, 2014:237; Steyn & Stiglingh, 2016:157; Surtees, 2001:68). Lubbe and Nienaber (2012:698) found the number of small businesses that make use of professional tax practitioners in South Africa indicative of the complexity of the South African tax legislation. The South African Revenue Service (SARS) indicated in 2004 that as many as 95% of small businesses make use of professional tax practitioners (Lubbe & Nienaber, 2012:698). Another study identified that the compliance related to small business tax concessions was so complex that it was not worth the effort as reported by the respondents (Smulders, 2014:35).

Prior to the studies mentioned above, the South African Government had, from as early as 1910, appointed numerous tax commissions and committees to consider different tax issues. Some of the more notable committees are the following:

- A *Committee of Enquiry into the Income Tax* Act, the Steyn Committee, was commissioned in 1949 and was the first committee to focus on the South African tax legislation as a whole (Lavine, 1952:135). This committee investigated all aspects

related to tax in the Union of South Africa and its provinces (Lavine, 1952:135). The committee was mandated to make recommendations to consolidate the existing acts into a single income tax act for the Union (Steyn & Stiglingh, 2016:3). Even though none of the recommendations of the Steyn Committee were implemented, this may be seen as the first acknowledgement for the need to simplify the South African tax legislation (Steyn & Stiglingh, 2016:3).

- A *Commission of Enquiry into Fiscal and Monetary Policy in South Africa* (the Franzen Commission) was appointed by the South African State President on 24 November 1967 to inquire into the overall tax system in South Africa (Van Niekerk, 1969:108). The Franzen Commission issued three reports during 1969 and 1970 and amongst other findings, reported that the current tax system inhibited economic growth within the country and made specific recommendations in this regard (Steenekamp, 2012:277). These recommendations included reducing the progressiveness of the direct taxing system, a move towards the use of indirect taxes, the dissolution of the source base of taxation and redefining the tax base in an effort to broaden it (Koch, Schoeman & van Tonder, 2005:194). A significant change recommended by the Franzen Commission was the termination of the right of provinces within the Republic of South Africa to levy personal and company income tax (Heyns, 1999:65). Simplification of the tax system was achieved by consolidating the tax systems of all the provinces.

- During 1984 a *Commission of Inquiry into the Tax Structure of the Republic of South Africa*, the Margo Commission, was appointed (Steyn & Stiglingh, 2016:4). Some of the recommendations made by the Margo Commission contributed to the simplification of the South African Tax system (Steyn & Stiglingh, 2016:4). These recommendations included the abolishment of the joint taxing of a husband and wife in favour of taxing the individual, the replacement of general sales tax (GST) with the much simpler value added tax (VAT) system, and reducing income tax by using income tax tables with less tax brackets (Steenekamp, 2012:278). The Margo Commission was the first commission to consider some of the basic principles of taxation that include fairness, neutrality, simplicity, certainty, administrative

efficiency, cost effectiveness, flexibility, stability, distributional effectiveness and a fair balance between direct and indirect taxes (Steyn & Stiglingh, 2016:4).

- During 1994 the *Commission of Inquiry into Certain Aspects of the Tax Structure of South Africa* (M. Katz, Chair), (the Katz Commission) was formed (Steyn & Stiglingh, 2016:5). The Katz Commission was provided with a broad mandate to investigate all aspects of taxation, with a specific focus on the new political dispensation of the post-apartheid era (Steyn & Stiglingh, 2016:5). Nine reports were issued during the life span of the Katz Commission from 1994 to 1999 which focused on simplification of the tax system, reduction of tax rates and the broadening of the tax base (National Treasury, 2006:iii). The reforms introduced into the tax system resulted in a robust and efficient tax system for South Africa, which compared favourably with other developed and developing economies, whilst setting a basis for the new political dispensation (Steyn & Stiglingh, 2016:5).

- During the 2013 budget speech, the South African Minister of Finance introduced the *South African Tax Review* Committee (under the leadership of Judge Dennis Davis), commonly known as the Davis Tax Committee (DTC) (Steyn & Stiglingh, 2016:6). This committee was appointed as an advisory committee that engaged in a consultative process to address specific tax issues. The terms of reference of the DTC were to assess the South African tax policy framework and its role in supporting the objectives of inclusive growth, employment, development and fiscal sustainability (Davis Tax Committee, 2013). The DTC issued 25 reports during its lifespan of four and a half years. A move towards a simpler and more certain tax system was recommended to encourage local and foreign direct investment (Davis Tax Committee, 2018:15). This committee made recommendations for significant changes to the taxation of trusts (Davis Tax Committee, 2018:10).

As is evident from the discussion above, the original focus of the appointed committees and commissions was to consolidate the fragmented tax legislation of South Africa. Admittedly, these processes facilitated a simplification of the overall tax legislation and in later committees and commissions simplification of the tax legislation became a bigger focus area. However, it was only the DTC that specifically identified trusts and their taxation as a focus area.

Within the context of what has been stated above, one notable study was obtained which compared the way in which income is taxed within trusts in selected SADC countries. The study by du Plessis (2018) considered the taxation of trusts in SADC member states. However, this study did not consider the relevance of the complexity of trust tax legislation across SADC countries. The study by du Plessis (2018) considered the way in which trusts are taxed within the selected SADC jurisdictions. To the knowledge of the researcher, no comparative research that considers the complexity of trust tax legislation within the SADC countries had been undertaken at the time of this study. In Section 1.5, the scope of the study and the relevance of using the SADC countries as a comparative basis is discussed.

1.3. GOAL OR PURPOSE OF THE RESEARCH

This study aims to investigate the complexity of trust tax legislation using the DTC Report as its point of origin, with specific focus directed towards the simplification of trust tax legislation within the context of the SADC countries. The study will serve as a foundation for future research activities directed towards the identification and isolation of core concepts in tax legislation that may cause complexity in the trust tax legislation. Tax authorities may use the results of this initial study as guidance in efforts to simplify the complex tax legislation within the trust environment.

The purpose of the research is to compare the tax legislation of selected SADC countries to identify and explore complexities related to trusts included in the tax legislation.

1.4. RESEARCH OBJECTIVE

The research objectives pursued in addressing the goal of the research are:

1. to analyse and describe the characteristics of the constructs of tax complexity and trusts, and
2. to analyse and compare the complex characteristics in the trust tax legislation of the selected SADC jurisdictions.

The scope of the research as described in the goal or purpose of the research and research objectives are limited to specific jurisdictions. The justification for the inclusion of the selected jurisdictions is discussed below.

1.5. SCOPE OF THE STUDY

The study is confined to the jurisdictions of Botswana, Eswatini (Swaziland), Lesotho, Malawi, Mauritius, Namibia, Seychelles, South Africa, Tanzania, Zambia and Zimbabwe. These jurisdictions were selected based on an initial criterion of being a member state of SADC. South Africa became a SADC member and signatory of the SADC Treaty (1992) in 1994 (Amos, 2010:124). The shared objectives of the SADC jurisdictions allow for cross jurisdictional analysis to be performed. The objectives of SADC, as stated in Article 5 of the SADC Treaty (1992) are to:

- "Achieve development and economic growth, alleviate poverty, enhance the standard and quality of life of the people of Southern Africa and support the socially disadvantaged through Regional Integration;
- Evolve common political values, systems and institutions;
- Promote and defend peace and security;
- Promote self-sustaining development on the basis of collective self-reliance, and the inter-dependence of Member States;
- Achieve complementarity between national and regional strategies and programmes;
- Promote and maximise productive employment and utilisation of resources of the region;
- Achieve sustainable utilisation of natural resources and effective protection of the environment;
- Strengthen and consolidate the long-standing historical, social and cultural affinities and links among the people of the Region" (SADC, 2012).

In light of the above, it is evident that these objectives include a diverse range of themes and focus not only on economic cooperation, but a wider variety of social, political and

economic areas. The diversity of the objectives and relationship of almost 30 years illustrate the importance of the SADC countries as trade partners. SADC comprises sixteen members, eleven of which are included in this study.

A second criterion used as a justification for the inclusion of the selected jurisdictions is that all these countries are current or past members of the Commonwealth. The Commonwealth was founded in 1965 with the purpose of improving the well-being of all its citizens and to advance their shared interests globally (Commonwealth Secretariat, 2019). Zimbabwe withdrew as a member of the Commonwealth in 2003, but has subsequently re-applied for membership. Four SADC countries were excluded based on this criterion, namely Angola, the Comores, the Democratic Republic of the Congo and Madagascar.

In addition to the above, South Africa shares a rich colonial background with the majority of SADC countries selected for this study. Victor Thuronyi, of the International Monetary Fund, classified countries into various tax law families (Thuronyi, 1998:xxiv). This classification provides insight into the historical background of the legal system found in the various countries. The “Commonwealth Family” includes countries that were influenced by the United Kingdom (UK) legal system due to the colonial background of these countries.

The final criterion used was language and only those jurisdictions in which the legislation was available in English were selected. Based on this criterion, Mozambique was also excluded from the scope of this study, which resulted in eleven countries forming part of the study.

After selecting the eleven SADC countries based on the criteria mentioned above, the scope of the study was further limited to only consider the income tax legislation of these countries as far as they impact on the general trust concepts and not relating to specific application trusts. Specific application trusts include collective investment schemes/unit trusts, special trusts, land rehabilitation trusts, public benefit organisation trusts, personal service providers, share incentive trusts and Black Economic Empowerment trusts. Furthermore, this study excludes the provisions relating to capital gains tax.

An additional limitation may be the number of trusts registered in the different jurisdictions as this may influence the development of tax legislation and case law related to trusts. Furthermore, there may be subjectivity inherent to the interpretation of legislation. The impact of these limitations on the study is discussed in chapter 5.3.

The next section briefly explains the research design and methodology adopted in this study.

1.6. RESEARCH DESIGN AND METHODOLOGY

The purpose of the research is to compare the trust tax legislation in the selected SADC countries to determine which aspects (if any) contain complexity. The research methodology applied may be described as doctrinal or "black letter law" and is concerned with the formulation of legal doctrines through the analysis of legal rules (Hutchinson, 2015:130). This methodology is selected to critically analyse documentary data to compare and reach conclusions that inform the research objectives. This qualitative research methodology is adopted as it is based on documentary data that does not involve statistical analysis (McKerchar, 2008:18-19).

The study commences with a review of the relevant literature to establish and clarify the theoretical underpinnings of the research. This is followed by a critical analysis of the sections in the legislation of the different SADC countries pertaining to trusts. A comparison of these sections will be made and tabulated after which a conclusion will be drawn.

The research is exploratory in nature; it compares data collected from the legislation of different countries and the results may be informative in nature. This methodology provides a review of the rules governing a particular legal category, analyses the relationships between the rules and explains areas of difficulty and ambiguity in the rules (Pearce, Campbell & Harding, 1987; McKerchar, 2008). The aims of the study are to encourage debate and further research around trust tax legislation and the potential for its simplification, as well as to inform policy makers and legislators.

For the purpose of this study, the documentary data used are the income tax legislation of the selected SADC jurisdictions. Additional sources include government publications, books and peer reviewed academic articles. In addition, case law, books, journals, articles and websites that inform the literature review and constructs of the study are examined and applied. The documentary data used for this research is publicly available, therefore there were no ethical or confidentiality considerations relating to its use.

Based on the literature review and specifically the constructs of tax complexity and trusts, the data will be analysed with the aim to ascertain the design complexity contained within the tax legislation of the selected jurisdictions. This design complexity will be tabulated and compared to identify sections and definitions within the legislation that may indicate complexity. This tabulated data will form the basis for identifying the trust taxation principles applied to the trust tax legislation by the different jurisdictions.

The research design and methodology are discussed in more detail in Chapter 3 of this study.

1.7. STRUCTURE OF THE DISSERTATION

The outcomes of the study are presented in the form of a dissertation. The structure of the dissertation is set out below.

1.7.1. Chapter 1: Introduction

In this chapter the background and the rationale for the study are discussed. The importance of this study is addressed and the way forward for future studies in relation to the research subject, is paved. The scope of the study as well as the limitations and exclusions are outlined. The research design and research methodology are briefly discussed and the basic layout and structure of the dissertation are provided.

1.7.2. Chapter 2: Theoretical framework

Chapter 2 provides the theoretical background to the study in the form of a literature review. It introduces and explains the relevant concepts and constructs that form part of the background to the study. A detailed discussion on the history of taxation, tax

complexity, trusts and taxation of trusts (including trusts in SADC) are presented in this chapter. This chapter concludes with a brief discussion on the comparative foundation of the study.

1.7.3. Chapter 3: Research design and methodology

Chapter 3 considers the research design and methodology used in the study.

1.7.4. Chapter 4: Data analysis

In this chapter the core concepts included in the tax legislation of the selected SADC jurisdictions are analysed and compared. This analysis includes the sections pertaining to the trust concept, as found in the tax legislation of the selected SADC countries. The analysis also contains research on the definitions related to trusts included in the legislation, the inclusion/exclusion of the flow through principle found in trusts and anti-avoidance measures included in the legislation of the selected jurisdictions.

1.7.5. Chapter 5: Conclusion

Chapter 5 concludes on the research. This is done by considering and concluding on the findings of this study. The contribution of the study as well as the limitations thereof are also discussed, culminating in recommendations for future research.

CHAPTER 2: THEORETICAL FRAMEWORK

2.1. INTRODUCTION

The research objective of this study is to investigate tax legislation between selected SADC countries with the purpose to explore and compare tax legislative complexities related to trusts. While Chapter 1 of this study provided an introduction and a background to taxation, it also considered the principles of effective tax systems based on the original theories of Adam Smith and later theories of researchers and academics.

Chapter 2 provides further context and explores the history of taxation. The chapter considers the purpose of taxation and the complexity in tax systems as a worldwide phenomenon, and particularly the construct of complexity is discussed including its definitions, properties and sources of complexity. In addition to this, the construct of a trust is considered with a history and background of the trust that provides an understanding of and basis for the complexity of the trust concept. This is followed by a discussion on the taxation of trusts and an analysis of different models for the taxation of trusts. In particular, the development of trusts in the SADC region is examined, through a discussion on the colonial background and influences on the trust concept. This is illustrated by a review of the history and development of the trust in South Africa.

In pursuance of the first research objective, this chapter analyses the constructs of tax complexity and trusts, in order to lay a foundation for the complexities found in trust tax legislation. The underlying concepts and principles included in the discussion are the history of taxation, tax complexity and the history and concept of a trust. This analysis contributes to the comparative analysis that informs the research objectives and the conclusion of the study.

2.2. TAXATION IN CONTEXT

The purpose of taxation is to collect revenue to fund the majority of public sector activities managed by a government (Bird & Zolt, 2003:9). Taxation impacts on the finances (resources) of those charged with the payment of taxes, and as such, diminishes some of

the scarce resources that taxpayers have available (Dodge, 2016:528,540,554,557). Tax policy guides the distribution of the tax burden in such a manner that political and developmental goals of the country can be achieved (Bird & Zolt, 2003:9). Governments thus formulate policies to ensure that specific objectives or targets are met (Davis Tax Committee, 2018:2-3; Milliron, 1985:795-796). The design of tax policy is a complex process and numerous factors should be considered, including psychological, financial, legislative and economic elements (Alm, 2019:370-371).

In this context, it is understood that as early as in biblical times, reference is made to a taxman collecting tax on behalf of the Pharaoh. Joseph, a well-known character in the Bible, and at that time regarded as a wise man who was put in charge of planning for the famine in Egypt (Genesis 41:37-44), collected a 20% tax on behalf of the Pharaoh as a form of income tax (Jose & Moore, 1998:63). This may be seen as the first recorded account of taxation (Jose & Moore, 1998:67,69,72,73). Other early forms of taxation include those levied on travelling salesmen and other merchants (Bishop, 2000:[1]). This type of taxation had the advantage that it was levied on foreigners and not on local citizens (Bishop, 2000:[1]). During the 13th Century the British Parliament introduced the principle of 'tonnage and poundage' on consumables including wine, leather and wool (Bishop, 2000:[1]). This system of 'tonnage and poundage' was specifically focussed on levying taxes on Italian merchants. This simple taxation system was based on the weight of a specific item with the tax being calculated at a fixed rate per ton or per pound (Bishop, 2000:[1]). The basis for early taxation was the ease of measurement and calculation of taxes resulting in ease of assessment (Bishop, 2009:[1]).

The original forms of modern taxation did not necessarily include the payment of money to governments, but in fact were paid in kind. In ancient China, the citizens paid their taxes by way of pressed tea. In Europe, the Greeks and Romans paid their taxes by defending their country when at war, and during these wars the citizens had to provide their own weapons. Historically speaking, the origin of our modern tax systems can therefore be referenced back to prominent and wealthy citizens paying money in exchange for being pardoned from going to war (Bishop, 2000:[1-2]).

Later tax systems predominantly utilised tax revenue for the financing of war efforts in Europe (Bishop, 2000):[2]). In this regard, the first known personal income tax was levied in 1797 by the Dutch Batavian Government. Britain followed in 1799 and Prussia in 1808 (Bishop, 2000):[2]). After a peace agreement was reached, these taxes were no longer levied, to the extent that British Prime Minister, Henry Addington, vowed never to raise any personal income tax again (Bishop, 2000):[2-3]). However, in 1842, income tax was reinstated in Britain. These taxes were mainly earmarked in preparation for further war efforts and for social upliftment and the welfare of citizens (Bishop, 2000):[2]). Income tax systems were originally drafted to apply to a small number of subjects and the tax rates were low (Budak & Benk, 2016:209).

The focus of modern tax administrations changed from these early tax systems to a system where government expenditure is financed through the raising of tax revenue (Awasthi & Bayraktar, 2014:2). Taxation is a compulsory financial contribution imposed by a government to raise revenue for which the payers of tax receive nothing directly in return (Alley & Bentley, 2005:582). It can be defined as having three purposes:

- To provide revenue to finance necessary government expenditure (Awasthi & Bayraktar, 2014:2);
- To act as an instrument to achieve the economic aims of government (Alley & Bentley, 2005:583); and
- To redistribute income on a socially acceptable basis (Alley & Bentley, 2005:583).

In conclusion, this section focussed on the development of taxation from a basic, specific-purpose tax to the modern, complex, revenue generating tax system that governments require to finance their expenditure. Having considered the basic history of taxation, the section to follow will focus on the more specific constructs of this study. These constructs are tax complexity and the concept of trusts.

2.3. TAX COMPLEXITY AS CONSTRUCT

> "The complexity of our code in the main is not there because of some mischief. Most of it is there in the effort to do more perfect justice" (Pollack, 1993:319).

These words were spoken by Senator Russell Long, former Chairman of the United States Finance Committee (Pollack, 1993:319). This quote indicates that complexity may be the result of the pursuance of justice, as opposed to a mere co-incidence or as a result of improper planning. However, when a study of complexity in a tax system is undertaken, it is pertinent to understand exactly what is meant by tax complexity.

The complexity of tax systems is described by Burton & Karlinski (2016:21) as one of the most serious problems taxpayers and governments face. There are numerous reasons for the complexity of tax systems and there are various indicators of and classifications for tax complexity. In Tran-Nam & Evans (2014:367), the authors have identified indicators of tax complexity that include the following (Tran-Nam & Evans, 2014:350):

- Number of taxes;
- The length of the tax acts;
- The readability of tax acts;
- The dependence on tax practitioners to ensure taxpayer compliance;
- The operating costs (in this context, operating costs refer to the total of tax compliance costs and administration costs); and
- The magnitude of tax related disputes.

Complexity in the tax system obscures 'certainty' amongst taxpayers, as it results in unclear legislation (AICPA, 2001:11-12). The presence of the above indicators of complexity in tax legislation may confirm the necessity for simplification of tax systems. In

the sections to follow, the definitions, properties, sources and the consequences of tax complexity will be discussed.

2.3.1. Defining tax complexity

In an attempt to define the term tax complexity, the Committee on Tax Policy of the New York State Bar Association's Tax Section stated that complexity exists where:

> "(1) A reasonably certain conclusion cannot in some instances be determined despite diligent and expert research.
> (2) A reasonably certain conclusion can be determined in other instances only after an expenditure that is excessive in time and dollars" (Burton & Dirkis, 1995:208).

A further attempt at a definition was provided by Cooper (1993:424-425) when he defined a complex tax system as one:

> "…where neither taxpayers nor the revenue authority could identify a taxpayer's liability with an appropriate degree of certainty at a reasonable cost, nor could that liability be cheaply and easily satisfied, nor enforced".

Although both these definitions have highlighted critical components of tax complexity, it is agreed by researchers that the term 'complexity' cannot be defined by way of a single definition (Burton & Karlinski, 2016:63; Cooper, 1993:424; McCaffery, 1990:1269-1270; Richardson & Sawyer, 1997:326; Tran-Nam & Evans, 2014:341). A criticism against these definitions is that they do not identify from whose perspective the definitions were written or should be interpreted. For example, the definition by the New York State Bar Association's Tax Section may be assumed to be interpreted from the perspective of a tax practitioner and it does not leave scope for interpretation by a layman (Burton & Dirkis, 1995:208). The different perspectives include those of the taxpayer, tax practitioner or even the tax authority (McCaffery, 1990:1270).

A further shortcoming is that the definition of complexity itself is complex and applying the definition to a specific factual scenario may not provide a definite solution (Burton & Dirkis, 1995:208). This is as the terminology used in the definition is not definitive. For example

terms such as ‘reasonably certain’ and ‘excessive’ are used in the definition (Cooper, 1993:425). Numerous researchers agree that to get to a credible definition of the term complexity, it is necessary to consider the properties or sources of complexity in a holistic manner (Budak & Benk, 2016:209; Budak & James, 2018:24; Burton & Dirkis, 1995:199; Tran-Nam & Evans, 2014:345). These properties of complexity will be discussed in the next section.

2.3.2. The properties of tax complexity

Tax complexity is a multi-dimensional concept and factors influencing tax complexity would include government policy, tax administrative procedures and the perception and behavioural responses of taxpayers (Pollack, 1993:341). Tran-Nam and Evans (2014:345) confirm that it is difficult to define tax complexity or its inverse, tax simplification. Complexity in tax systems is a comparative concept that means a specific piece of legislation should be compared to similar legislation, for example: “the South African Income Tax Act is less complex than the Australian Income Tax Act” (Evans, Hasseldine, Lymer, Ricketts & Sandford, 2017:209). Tran-Nam and Evans (2014:345) indicate that the most appropriate way to define complexity may be by way of a combination of basic (fundamental) properties. These basic properties were identified by Slemrod (1989:157) and have been adopted in research by various authors (Budak & James, 2018:24; McCaffery, 1990:1276; Tran-Nam and Evans, 2014:346).

2.3.2.1. *Technical complexity*

The first property identified, is ‘**predictability**’ (Slemrod, 1989:157). ‘Predictability’ refers to the level of intellectual investment needed to interpret the tax legislation with clarity and certainty (McCaffery, 1990:1271). McCaffery (1990) refers to this type of complexity as ‘technical complexity’. Technical complexity indicates the ‘understandability’ of a section included in the legislation when that section is considered on its own (McCaffery, 1990:1271). McCaffery (1990:1271) argues that a reduction in technical complexity will assist taxpayers to understand, interpret and comply with the relevant section included in the legislation. From another perspective, ‘predictability’ can also be interpreted as the

ease of interpretation of the legislation. Legislation may be difficult to interpret from a grammatical perspective and this may result in perceived complexity (Paul, 1997:162).

2.3.2.2. *Structural complexity*

The second property, '**manipulability**' or '**structural complexity**', refers to the extent that the tax legislation lends itself to tax planning and tax manipulation (Slemrod, 1989:157). This 'manipulability' of the tax legislation may create uncertainty when the structure of the legislation allows for multiple interpretations, hence the legislation lends itself to varied interpretation in respect of the different tax treatment of similar transactions (McCaffery, 1990:1276).

2.3.2.3. *Compliance complexity from a tax authority perspective*

A further property identified by Slemrod (1989:157) is '**enforceability**'. 'Enforceability' refers to the administrative costs incurred by the tax authority in enforcing the tax legislation (Tran-Nam & Evans, 2014:345) and may also be referred to as 'administrative complexity'. 'Enforceability' and 'difficulty' (refer to Section 2.3.2.4) are combined by some researchers and referred to as '**compliance complexity**' (Evans *et al.,* 2017:213; McCaffery, 1990:1272).

2.3.2.4. *Compliance complexity from a taxpayer perspective*

The complexity related to the cost of complying with the tax legislation from a technical or interpretive perspective is referred to as '**difficulty'** or '**cost of compliance**' (Tran-Nam & Evans, 2014:345). This type of complexity relates to the costs incurred by the taxpayer to comply with the tax legislation. These requirements include the completing of forms, procedural red-tape and other administrative requirements (McCaffery, 1990:1272). As an example, a taxpayer may not be aware of certain procedures required during the compliance process, or may be aware of the procedures but may not understand how to comply with these procedures.

2.3.3. The stages of tax complexity

An alternative to the classification based on the properties of complexity may be to consider the stages where complexity occurs in the tax system. The stages of complexity identified and defined by Tran-Nam and Evans (2014:346) are policy-making, drafting of legislation (statutory), administration and compliance.

2.3.3.1. *Policy complexity*

Policy complexity is linked to the drafting of tax policy. This complexity relates to the specific policy choices made by government, including policies of a non-revenue generating nature, for example political or social considerations (Tran-Nam & Evans, 2014:367). Additionally, when policy makers attempt to apply tax legislation to achieve multiple goals, complexity may be increased (Pollack, 1993:321).

2.3.3.2. *Statutory complexity*

Statutory complexity may be the result of poorly drafted legislation. This may be caused when legislators use poor linguistics or grammar, or when the legislators apply a rules-based approach in legislation that is predominantly based on principles (or the inverse) (Tran-Nam & Evans, 2014:348). In other words, statutory complexity arises as a result of the drafting of the relevant tax legislation (Tran-Nam, 2016:15; Tran-Nam & Evans, 2014:367).

2.3.3.3. *Administrative complexity*

Administrative complexity is the complexity that is caused due to the administrative compliance requirements to enforce the stipulations within the legislation (Tran-Nam, 2016:15; Tran-Nam & Evans, 2014:367). In other words, administrative complexity is the result of the introduction of rules, processes and practices in an effort to ensure compliance (Tran-Nam & Evans, 2014:346). In this regard the tax authority may implement processes to reduce uncertainty regarding tax issues, should the benefit obtained outweigh the cost of implementation (Paul, 1997:174).

2.3.3.4. *Compliance complexity*

Compliance complexity is the complexity caused during the tax computation process and tax planning efforts by the taxpayer (Tran-Nam, 2016:15; Tran-Nam & Evans, 2014:367). A taxpayer may have to comply with the procedural requirements (including record-keeping and form-capturing processes), in addition to understanding the specific section of the tax legislation (McCaffery, 1990:1272).

2.3.4. The sources of tax complexity

The sources of tax complexity may be classified as governmental need to raise revenue, government objectives, fairness, certainty and judicial factors (Evans *et al.*, 2017:221; Tran-Nam, 2016:17; Vaillancourt & Bird, 2016:74; Budak & James, 2018:24-25; Paul, 1977:155; Borrego, Lopes & Ferreira, 2016:29). Each of these concepts is discussed below.

2.3.4.1. *Revenue source*

The first broad source of complexity stems from the '**governmental need to raise revenue'**. Governments have the responsibility to raise revenue for both fiscal and non-fiscal purposes (Budak and James, 2018:24). Therefore revenue raised by governments should be sufficient to effectively support these fiscal and non-fiscal goals, as provided for in the budget (Budak & James, 2018:24). This budget will be based on government policy and legislation drafted to meet governmental goals (Evans *et al*, 2017:222). However, the legislation should include sections dealing with or enacted to curb aggressive manipulation, avoidance or evasion by tax practitioners and taxpayers (Vaillancourt & Bird, 2016:74). In addition to this, government needs may also be driven by social and/or political goals (Evans *et al*, 2017:221). In this context, governments may allow certain interest groups or politicians to influence government spending, and these concessions inevitably lead to further (unintended) complexity (Budak & James, 2018:24; Cooper, 1993:453). A further consideration is the actual revenue raised by a specific tax type; the larger the amount of tax raised, the larger the focus on that tax type will become. This, in turn, may necessitate the revenue authority to provide clarification in the application of the tax type and may again result in further complexity (Evans *et al.*, 2017:221).

2.3.4.2. *Political*

The '**objectives of a government to be elected or re-elected'** may inherently be a source of complexity (Vaillancourt & Bird, 2016:74). For example, in an attempt to attract votes, governments or political parties may make promises to certain interest groups. Inevitably these promises may lead to tax complexity, as it may broaden the commitments from a budgetary perspective and may then cause more inequity in the budget (Vaillancourt & Bird, 2016:74). In light of this objective, legislation may tend to serve the purpose of the law makers, rather than the interest of the public (Paul 1997:156). Paul (1997:176) contends that the individual influence of those drafting the law may lead to their own legal approach finding effect in the legislation. An example mentioned is that American law makers, when drafting legislation, engage legal experts whose "taste" for legal complication may find its way into the legislation (Paul, 1997:176).

2.3.4.3. *Fairness*

The pursuit of **'fairness'** may be another broad source of complexity. At this point it may be necessary to consider that taxpayers may prefer more complex tax legislation that may be seen to be fair rather than a simpler tax legislation that is perceived to be unfair (Vaillancourt & Bird, 2016:74). In this context, governments that are committed to fairness and that align the tax legislation thereto, may inevitably cause tax complexity, as the desired tax effect and the actual tax effect will not be reconcilable (Paul, 1997:155, 165-166).

2.3.4.4. *Certainty*

In relation to **'certainty'** as a source of complexity, Benjamin Franklin, former President of the United States of America (USA), was reported as having said that nothing is certain but death and taxes (Vaillancourt & Bird, 2016:74). Although certainty in tax is sought after, it seems that a limited number of taxpayers are certain of their tax position (Vaillancourt & Bird, 2016:74). However, the rapidly changing world economy requires legislators to amend tax legislation to accommodate these changes (Vaillancourt & Bird, 2016:74). In turn, these changes in the legislation require more frequent interpretation that leads to further uncertainty (Alley, 2005:608). Post the 1950's, the taxation of multinational transactions and multinational companies changed significantly with expanding

international trade. This changing economic environment led to changes in tax legislation that contributed towards further complexity (Budak & James, 2018:24).

In the process of drafting policy and legislation, certain factors may contribute to complexity. Amongst these, the incompetence of law makers, narrow or limited advice provided by Treasury officials and poor or unclear drafting of the legislation are factors that contribute to complexity (Evans *et al.*, 2016:221). Additionally, the legal profession has a cultural tendency towards legal complexity in the drafting of legislation (Paul, 1997:180). Legal complexity may also cause uncertainty, as it may impede the appropriate comprehension of the legislation as it was intended (Budak & James, 2018:25). Further legal complexity may arise when the judiciary misapplies foreign legal interpretations to local tax legislation (Evans *et al.,* 2016:222). An example mentioned in Evans *et al.* (2016:222) is where doctrines from the UK are applied to Australian legislation, but have no or hardly any relevance in an Australian context (Evans *et al.*, 2016:221).

An alternative grouping or approach to the sources of complexity was suggested by Evans *et al.* (2016:222). This approach suggests that the role of government within the complexity debate should be more central (Evans *et al.,* 2016:222). The authors then continue to classify these sources of complexity as being within the control of government, partly under the control of government or outside government control. Each of these alternative groupings is discussed in more detail below:

2.3.5. The sources directly under the control of Government

2.3.5.1. *Protecting tax revenue*

Tax legislation may include a degree of complexity to ensure consistent tax revenue for government to meet its national budgetary requirements. An example of this complexity is the introduction of anti-avoidance measures into the legislation.

2.3.5.2. *Application of legislation for non-revenue purposes*

Tax legislation may be drafted to address non-revenue goals of governments. These would include the redistribution of wealth or meeting other socio-economic targets. An example would be the use of sin taxes or sugar taxes to curb unhealthy practices.

2.3.5.3. *Broadening the tax base*

The broadening of the tax base indicates an increase in the number of taxpayers within the tax system. This broadening of the tax base leads to complexity. An example is where efforts are made to broaden the tax base in a specific sector of the economy such as informal traders, where these informal traders will need to be policed by the tax authority to ensure the necessary compliance. This additional policing will create further complexity.

2.3.5.4. *Regular changes in tax legislation*

Frequent changes in tax legislation may increase complexity. Taxpayers and their tax practitioners will be required to maintain an updated knowledge of tax legislation and the application thereof.

2.3.5.5. *Drafting of legislation*

Government should ensure proper drafting of tax legislation. Poor drafting of the tax legislation will cause complexity as it will require clarification and interpretation.

2.3.5.6. *Managing tax revenue losses*

In an effort to minimise tax losses, tax administrators may implement administrative processes to compel taxpayers to comply. These additional administrative processes may lead to increased administrative complexity.

2.3.5.7. *Judicial traditions*

Complexity is caused when the legislature drafts legislation based on certain fixed principles or terminology (Krever, 2001:472). An example of this is the definition of ‘income’ where a more appropriate definition may have been ‘net profit’.

2.3.6. The sources of complexity only partly within the control of government:

2.3.6.1. *The established tax culture*

A culture of adversity between taxpayers and the tax authority may create complexity. An example is a society where a culture of aggressive tax planning exists and this requires of the tax authority to extensively audit these taxpayers who are involved (Evans *et al.,* 2016:222-223).

2.3.6.2. *The economy*

Tax complexity is caused by the growing global economy, increased multinational companies and complex business structures. A further complication is created due to a broader number of taxpayers owning equity investments. The factors mentioned may cause complexity as they require the tax authority to design and implement tax legislation to provide for complex transactions in the ever-growing global economy (Evans *et al.,* 2016:222-223).

2.3.7. The sources deemed to be outside of the control of government

2.3.7.1. *Taxpayer preference for minimisation of tax liability*

Taxpayers may prefer more complex tax legislation that provides for a lower rate of tax on certain transactions. An example is the use of a motor vehicle allowance that places a significant burden of proof on the taxpayer to claim the allowable deduction (Evans *et al.,* 2016:223).

2.3.7.2. *Tax practitioner preference for tax complexity*

Tax practitioners may prefer the tax legislation to be more complex. Complex legislation would require extensive research and preparation and this may result in additional chargeable hours (Evans *et al.,* 2016:223).

2.3.7.3. *Aggressive tax planning*

A culture of aggressive tax planning involving both taxpayers and tax practitioners may lead to tax complexity. An example of this type of complexity is where a tax authority

needs to implement extensive anti-avoidance measures to curb aggressive tax schemes (Evans *et al.,* 2016:223).

This section highlighted the sources of complexity from two different perspectives. However, even though the different approaches considered the sources of complexity from different viewpoints, both approaches encapsulated the same sources of complexity. The next section will consider the effect or consequences of tax complexity.

2.3.8. The consequences of tax complexity

The American Institute of Certified Public Accountants (AICPA) describes the effect of tax complexity on the basic principles of taxation and how this complexity erodes these basic principles (Laffer, Winegarden & Childs, 2011:10).

The principles of '**equity and fairness**' are threatened by complexity in tax legislation when taxpayers perceive tax legislation as unfair (Laffer, Winegarden & Childs, 2011:10). The complexity caused by regular changes to tax legislation and insufficient guidance on how to apply these changes threatens the principle of '**certainty**' (Laffer, Winegarden & Childs, 2011:10). Regular changes to tax legislation have a negative effect on the certainty that taxpayers may expect from tax legislation. According to the AICPA Report, complexity in the tax system obscures certainty amongst taxpayers as it results in unclear legislation (AICPA, 2001:11-12). Taxpayer uncertainty is further heightened by a lack of legislative and administrative guidance (Laffer, Winegarden & Childs, 2011:10).

Complexity in tax legislation may also threaten the principle of '**economy of collection**' by increasing the costs associated with the collection of government revenue. These costs may include additional administration costs related to the collection of revenue and additional dispute resolution costs (Laffer, Winegarden & Childs, 2011:10).

Complexity influences the '**neutrality**' of a tax system by causing inequity in the tax treatment of taxpayers who find themselves in a similar position (Alley, 2005:592; Laffer, Winegarden & Childs, 2011:10). An example occurs where a similar transaction yields different tax results, if the transaction is entered into making use of different business forms (the tax consequences of a trust may differ from that of a company for the same transaction).

In addition, complex tax legislation may also jeopardise '**economic growth and efficiency**'. A taxpayer may need to expend funds intended for investment purposes to finance tax compliance (Laffer, Winegarden & Childs, 2011:10).

Finally, complexity may also increase the '**tax gap**' as taxpayers become reluctant to comply (Laffer, Winegarden & Childs, 2011:10). In this regard the tax gap refers to the difference between the amount of tax that a government intended to collect and the actual taxes collected (Alley, 2005:618; Laffer, Winegarden & Childs, 2011:10).

A consequence of tax complexity that is not mentioned in the AICPA Report is '**tax evasion**' (Richardson & Dirkis 2006:164). Although researchers (Richardson & Dirkis 2006:164; Ulph, 2015:48), discuss the relationship between complexity and tax evasion, Richardson (2006:164) explains the interrelationship between complexity and other indicators of tax evasion. The indicators of tax evasion that are considered by Richardson (2006:164) are complexity, education, income source, fairness and tax morale. In performing the research, Richardson (2006:164) concluded that complexity is the major determinant of tax evasion. Interpreted differently, this means that a simpler tax system reduces or limits tax evasion. This view is supported by Brooks (1998:289) who, by way of example, mentions that a flat rate of taxation would simplify the tax system and reduce tax avoidance or evasion. Complexity may also lead to mistakes or confusion resulting in **misinterpretation** and even dishonesty by taxpayers (Richardson 2006:164). This may be as taxpayers may not understand complex legislation and thus decide not to comply or inadvertently submit incorrect information (Budak & James, 2018:25).

When considering the consequences of tax complexity, it is important to acknowledge that complexity may not mean the same thing to all people. Burton and Dirkis (1995:206) mention that a tax practitioner may read and understand a section of tax legislation easily and simply, but the "man on the street" may perceive the same section of the tax legislation as complicated and only accessible to an elite few. This illustrates that the consequences of tax complexity may have different implications for different role players.

Non-compliance as a consequence of tax complexity may be caused when the tax legislation is complex and to comply may become a **costly** exercise for the taxpayer (Budak & James, 2018:25). The taxpayer may need the services of expensive tax

practitioners to interpret the tax legislation (Burton & Dirkis, 1995:204). Complex tax legislation may lead to non-compliance, as taxpayers and tax practitioners may have multiple interpretations of a section of the tax legislation (Budak & James, 2018:25). The multiple interpretations may affect the **decision-making** process of taxpayers to such an extent that a taxpayer may decide not to enter into a transaction due to the uncertainty regarding the tax consequences of the transaction (Budak & James, 2018:25). An example of this type of uncertainty may be where a taxpayer has to decide on investing in two different jurisdictions. The decision to invest may be determined by the clarity that the taxpayer needs to ascertain the tax consequence related to the return on his investment. The economic result of a transaction may vary from one tax period to another, if the tax legislation is amended on a regular basis (Burton and Dirkis, 1995:204). This jeopardises the economic neutrality of a specific transaction, which in turn may dissuade a taxpayer from entering into the specific type of transaction (Burton & Dirkis, 1995:204).

An important consequence of complex tax legislation and the resultant non-compliance is that this inevitably leads to **higher tax rates** (Ulph, 2015:48). Avoidance by some taxpayers reduces total government revenues and decreases the base from which a revenue authority collects revenue (Ulph, 2015:48). This means that the total revenue required by the government will be collected from a smaller tax base.

From the perspective of government, a consequence of tax complexity may be that the **cost** involved in raising the tax revenue increases due to the additional resources required by the tax authority for interpretation or to enter into litigation (Budak & James. 2018:26). From a taxpayer’s perspective, professional assistance in the form of a tax practitioner may be required to interpret uncertainty in the tax legislation (Walpole, 2015:182). This assistance may increase the cost of compliance for the taxpayer (Ulph, 2015:48). It is likely that the tax practitioner will interpret the tax legislation in favour of the taxpayer. Similarly, should a taxpayer approach the Commissioner for a ruling, it is also likely that the Commissioner will rule in the best interest of the tax authority (Burton & Dirkis, 1995:205). Should the taxpayer disregard the ruling of the Commissioner, it would be likely that the taxpayer would be penalised in favour of the revenue authority (Burton & Dirkis, 1995:205). In addition, complexity of tax legislation may encourage disrespect for the ‘rule

of law' and may result in a reduction of voluntary compliance (Burton and Dirkis, 1995:205).

A positive consequence of simplifying complex tax legislation is that it may reduce the tendency towards **corruption** (World Bank, 2009:4). Simplified tax legislation may reduce the points of contact between the taxpayers and the tax authority, therefore minimising the opportunities for vested interest groups to seek bribes (World Bank, 2009:4). Simplified tax legislation may be seen as transparent in nature and a transparent tax system with fixed rules encourages investment (World Bank, 2009:4). Fixed rules facilitate a smoother decision-making process, as taxpayers do not have to negotiate with government on the technical interpretation of specific transactions (World Bank, 2009:4). Uncertainty around the tax treatment of a transaction may dissuade a taxpayer (investor) from entering into the transaction (World Bank, 2009:4).

A further consequence of tax complexity is that it may encourage incompetent tax practitioners and discourage thorough tax practitioners (Burton & Dirkis, 1995:205; Cooper, 1993:456). Complex tax legislation may require of a thorough tax practitioner to invest significant time and resources to interpret sections of the tax legislation (Burton & Dirkis, 1995:205). However, taxpayers may be reluctant to pay for such a significant investment of time, especially if it does not provide certainty on the outcome of the taxpayer's matter under consideration (Burton & Dirkis, 1995:205-206). In addition to the above, incompetent tax practitioners may interpret the same section in the tax legislation, spending less time and less resources, and may draft an opinion that is equally uncertain but at a much lower cost to the taxpayer (Burton & Dirkis, 1995:205-206). This phenomenon is known as Gresham's Law (Burton & Dirkis, 1995:206). A further consequence of tax complexity is so-called **creative compliance** (Walpole, 2015:182). Creative compliance occurs when taxpayers and tax practitioners exploit sections of the complex tax legislation for their own or their client's benefit (Cooper, 1993:456).

However, it is recognised that certain tax legislation is necessarily complex, as it deals with actual commercial transactions that are inherently complex in nature (Budak, James & Sawyer, 2016:351). These transactions are driven by economic design and not by tax legislation. In cases like these the taxation might be necessarily complex, and the tax rules

will thus also be complex (Budak, James & Sawyer, 2016:337-354). An example of this type of complexity may be found in the application of the flow through principle in the taxation of trusts.

In summary, this section considered the definition, properties, sources and consequences of complexity in the tax environment and how a certain degree of tax complexity may be necessary. The section that follows considers the construct of a trust by providing a background on trusts, followed by a discussion of the reasons why a trust is considered to be complex in nature.

2.4. TRUSTS

In this section the background of trusts is discussed, to gain an understanding of the complexity involved in the trust concept. To illustrate possible trust tax complexity, it is necessary to study the origin and history of trusts. This section is not aimed at providing a comprehensive discussion of the trust history, but rather at creating a foundation for the research that will be undertaken.

2.4.1. History of trusts

The concept of a trust, also known as the 'Use' in England, is commonly believed to have originated during the Middle Ages in England (Holdsworth, 1923:368). After the British invasion of South Africa, it was only natural that the concept of a trust found its way into the South African legal system (Honiball & Olivier, 2009:2). The development of trusts (as tax and estate planning instruments) and trust legislation within a South African context was founded on the same English colonial principles (Thévenoz, 2014:30). However, the South African courts, through their own interpretations, created a trust law specific to South Africa (Honiball & Olivier, 2009:10). From a legal perspective the formation of trusts in South Africa was formalised through the introduction of the Trust Property Control Act, 57 of 1988 (TPCA).

From a historical perspective, many scholars, jurists and historians credit the English Law as the founding law for the institution of the trust as we know it today (Honiball & Olivier, 2009:29). This contribution to international law is hailed as being the greatest contribution made by English jurists (Cameron, Honore & de Waal, 2002:24; Matthews, 2013:242).

In this context, the geographical location of the British Isles (that includes England) in relation to Europe has rendered it vulnerable to external influences and infiltration (Du Toit, 2001:15). In 1066 the Normans, under the leadership of William the Conqueror, invaded England (Du Toit, 2002:15). England was subsequently influenced by various Germanic cultural ideas, customs and institutions – this includes the medieval 'Opus' or 'Use' which found application through the so-called 'Treuhand' or 'Salman' principle (Du Toit, 2002:15; Holdsworth, 1923:368). The 'Treuhand' principle was a well-known custom of the Germanic tribes and bound a person to whom a property had been transferred with a duty to honour the obligation placed on him for the purposes of the 'Treuhand' (Du Toit, 2002:15). In practice the 'Treuhand' meant that Person A would transfer property to Person B who would manage the property for the benefit of Person C (Du Toit, 2002:15). This found application when crusaders left on extended journeys and needed to make provision for these extended absences (Cameron, de Waal, Wunsh, Solomon & Kahn, 2002:24). The person entrusted with the property was required to manage this property on behalf of the crusader for the benefit of his family for the duration of his absence (Du Toit, 2002:16). Upon his return, the person entrusted with the management of the property was required to transfer the property back to the crusader, but if the crusader did not return, the person entrusted with the property was required to transfer the property in line with the wishes of the crusader (Du Toit, 2002:16). This application of the 'Treuhand' was the predecessor of the 'Trust' or 'Use' (Du Toit, 2002:16). The 'Use' became popular in the middle-ages, as the legal application of the testament or will had not yet been conceptualised and was only instituted from the 12th Century (Cameron, de Waal, Wunsh, Solomon & Kahn, 2002:24-25; Du Toit, 2002:15).

From the 11th Century to the 13th Century the 'Treuhand' became a more popular form of transacting (Cameron, de Waal, Wunsh, Solomon & Kahn, 2002:24; Du Toit, 2002:16). An example of the 'Treuhand' in practice was evident in the 13th Century, where friars (who were sworn to poverty and were not allowed to own property) were provided with agricultural property on which they cultivated crops for the benefit of all (Du Toit, 2002:16; de Waal, 2000:553). These properties were not owned by the friars but held in 'Use'. Importantly, in 1279, Pope Nicholis III drafted the bull *Exiit qui seminat* (Holdsworth, 1923:371). On application of the bull (a formal document issued by the pope) it affirmed that the 'Use' held by the friars did not constitute property in their hands (Holdsworth,

1923:371). The bull affirmed that the legal owner was the executor for the beneficiary and this created the opportunity for the beneficiary to deal with the property easily or as he wished (Holdsworth, 1923:371).

During the Middle Ages the land law, which formed part of the common law, was the most developed law in England and the main application of the ‘Use’ was for the purpose of realty or land (Holdsworth, 1923:370). Other personal property in the Middle Ages, known as chattels, was made up of items of a consumable nature including cattle, books and armour (Holdsworth, 1923:370). It was not general practice for these chattels to be placed in ‘Use’ and this practice is still relevant today (Holdsworth, 1923:370; Perry, 1872:6).

However, in 1379 the English Parliament sourced the opinion of all the judges on the recognition of the ‘Use’ in common law (Holdsworth, 1923:371). The judges were unanimous in their rejection of the ‘Use’, unless it complied with the strict rules of the common law, and the ‘Use’ was consequently effectively banished (Holdsworth, 1923:371). However, the application of the ‘Use’ in the English society was at that time so widespread that it was nearly impossible for the practice to be eliminated, as the common law did not make provision for the treatment of property owned through the ‘Use’ (Holdsworth, 1923:371). To provide for this shortcoming it became practice from the 13th Century to approach the Chancellor (the chief advisor of the King) to clarify matters of uncertainty around the application of the common law (Holdsworth, 1923:371). The Chancellor provided the aggrieved party with a suitable remedy, and this practice resulted in a body of law known as ‘Equity’[1] that provided an alternative solution to the otherwise rigid body of common law (Cameron, de Waal, Wunsh, Solomon & Kahn, 2002:25; Du Toit, 2002:17). The influence of this ‘Equity’ in English law resulted in the creation of two separate courts, the one being the strict common law court, and the other the Court of Chancery dealing with matters of ‘Equity’ (Holdsworth, 1923:371).

A significant milestone in the history of the ‘Use’ occurred when the Statute of Uses was passed in 1535 (Du Toit, 2002:17; Holdsworth, 1923:367-368). The Statute was passed due to the abuse or questionable application of the ‘Use’, for instance for avoiding creditors (Du Toit, 2002:17). With the introduction of the Statute of Uses, the ownership of

[1] The term ‘Equity’ used in this context is not the same as the term ‘equity’ referred to in Adam Smith’s principles of a good tax system.

property in the 'Use' was effectively placed in the hands of the beneficiary (*cestui que use*) and no longer in the trustee (*feoffee*) (Du Toit, 2002:17). This meant that the 'Use' no longer had application in the law and the property transferred by a donor to a 'Use' (held by a trustee on behalf of a beneficiary) was negated as this ruling placed the property directly in the hands of the beneficiary. This regulation made it simpler for the application of common law on the property and effectively gave the common law courts authority over large numbers of 'Uses'. Unfortunately, this curbed the functionality or practicability of the 'Use' in the format in which it was originally intended, but that was overcome by legal creativity in the years to follow, recreating the original 'Use' principle (Du Toit, 2002:17). The *Statute of Uses* developed over the centuries to follow, overcoming challenges on the way, to result in the Trust Law as it is known in England today (Holdsworth, 1923:367, 375).

2.4.2. Characteristics of trusts

In the previous section a brief history and background of trusts was provided. This history creates a foundation of the underlying complexities imbedded in the trust concept. Complexities in trusts are caused by the unique characteristics of a trust. These characteristics are discussed below.

2.4.2.1. *Legal persona*

From a South African perspective the courts have refrained from granting a trust legal persona (Cameron, de Waal, Wunsh, Solomon & Kahn, 2002:67; Honiball & Olivier, 2009:9). The property of a trust vests in the trustees in a fiduciary capacity and thus they have no beneficial ownership of the assets (Honiball & Olivier, 2009:9).

2.4.2.2. *Flexibility of the trust*

The creation of a trust in South Africa by way of a trust deed is relatively simple with limited formalities (Honiball & Olivier, 2009:12). The founder may express his wishes freely and give utterance to these in the trust instrument (Honiball & Olivier, 2009:12). Amongst other determinations, the founder may include the number of trustees as well as the beneficiaries and the rights of these beneficiaries (Du Toit, 2002:60; Honiball & Olivier, 2009:12). Subsequent amendments to the trust instrument are in most instances simple,

provided that they are done in accordance with the trust instrument or with the approval of the founder (Du Toit, 2002:39-49; Honiball & Olivier, 2009:12).

2.4.2.3. *Transferability and protection of assets*

Property donated by the founder as well as any other property procured by the trust will be registered in the name of the trustees and will not form part of the estate of the founder, trustee or beneficiary, except to the extent that a trustee may also benefit as a beneficiary of the trust (Honiball & Olivier, 2009:13).

2.4.2.4. *Separation of formal ownership*

A further characteristic of a trust is that the trust property is held on behalf of the trust by the trustees in a fiduciary capacity (Honiball & Olivier, 2009:15). This unique ownership characteristic has the result that the ownership and enjoyment of the assets are separated (Cameron, de Waal, Wunsh, Solomon & Kahn, 2002:294; Nel, 2014:300). In other words, although the trustees, in form, own the property of the trust, they will not enjoy the fruits of these assets. The TPCA provides in section 12 that the property held by the trustee on behalf of the trust does not form part of the trustee's estate, should he be sequestrated.

2.4.2.5. *Tax transparency*

A common law principle of a trust is that a trust is a tax transparent entity (Honiball & Olivier, 2009:12). The income of a trust may either be taxed in the trust or may be attributable to either the donor or a beneficiary (Honiball & Olivier, 2009:12). This phenomenon is known as the flow through or conduit pipe principle. This unique characteristic of a trust provides the opportunity of income splitting to taxpayers (Honiball & Olivier, 2009:13).

2.4.2.6. *Lack of statutory directives*

The TPCA is not a codification of the law regulating trusts, and trusts are predominantly regulated by common law principles (Du Toit, 2002:45; Honiball & Olivier, 2009:10). The absence of a regulatory framework for trusts has certain benefits including that no formal format for the drafting and submission of a trust instrument is required; similarly no financial statements or audits of these financial statements are mandatory, except when specifically required in the trust instrument (Honiball & Olivier, 2009:10-11). There are no

limitations on who may act as trustees for the trust, although the Master of the High Court may require a suitably qualified financial person to be included as a trustee (Honiball & Olivier, 2009:11).

2.4.2.7. *Income retains its nature*

A unique characteristic of the flow through principle in trusts is that the income generated by a trust and attributed to a beneficiary retains its nature as was confirmed in *Armstrong v CIR* and SIR v Rosen (*Honiball & Olivier, 2009:72*). This means that an amount of interest earned by the trust and subsequently attributed to a beneficiary will retain its nature as interest. The result hereof is that the beneficiary will declare an amount of interest earned from the trust as interest in his tax return.

2.4.2.8. *Perpetual succession*

A South African trust is not limited in terms of the number of years that it may exist, unless the trust instrument determines a specific duration (Du Toit, 2002:53; Honiball & Olivier, 2009:11). This has the advantage that the trust activities will not be interrupted by death or insolvency and makes it an excellent business form for estate planning purposes, as the trust has a continued existence over various generations (Honiball & Olivier, 2009:11). This perpetual nature of the South African trust is not that common in other tax jurisdictions where the trust may have a limited period of existence (Honiball & Olivier, 2009:11; Nel, 2014:312).

2.4.2.9. *Real subrogation*

The concept of real subrogation explains that when a trust owns property and this property is sold, the proceeds or the replacement property (should the proceeds be utilised to purchase new property) will remain an asset of the trust (De Waal, 2000:564).

2.4.2.10. *Trusteeship as an office*

This principle incorporates a public element to a trust that is not found in a normal contract (De Waal, 2000:566). This is evident when considering the powers of a court related to trusts as opposed to other contracts. A trustee acts in an official or a fiduciary capacity and should he fail or a position as trustee become vacant, the court may be required to remedy this situation (De Waal, 2000:565-566).

2.4.3. Trusts in the SADC region

This section provides an overview of the impact of colonisation on Africa and the influence thereof on the development of legal systems and trusts within the SADC region.

Law scholars have categorised countries into different families to highlight basic similarities in legal tradition (Evans *et al.*, 2017:11). During the 1990's Victor Thuronyi was the first to classify tax jurisdictions into different types of tax "families" (Evans *et al.*, 2017:11). Thuronyi based his classification on similar aspects in the legal tradition of different countries (Evans *et al.*, 2017:20). This classification provides clarity on the historic legal background of tax systems within different countries. Thuronyi also asserts that although a country may fall within a tax family, the influence of its own developments should not be underestimated; these developments will also be rooted in the same legal culture that the country has adopted (Evans *et al.*, 2017:20).

The SADC countries included in this study fall within the "Commonwealth" tax family (mainly influenced by the UK) (Evans *et al.*, 2017:13). The "Commonwealth" and "American" families are jointly known as "common law" countries where the development of tax legislation in these families is mainly guided by the courts (Evans *et al.*, 2017:13). A common characteristic of countries in the common law family is that the development of tax legislation is predominantly influenced by the courts; therefore case law plays a significant role in these jurisdictions (Evans *et al.*, 2017:13).

Although jurisdictions may fall into the same tax family, there may be substantial differences in their tax legislation (Evans *et al.*, 2017:14). Factors contributing to the tax legislative differences include the prevailing local business, and commercial and environmental influences (Frankema & van Waijenburg, 2014:392-393). An example of this influence is evident in Malawi where, in 1902, as a British Protectorate, Malawi was subject to the British Central Africa Order in Council (Mtonga, 2015:7). This effectively rendered Malawi subject to the British common law, statutes of general application and the principle of equity (Mtonga, 2015:7). This resulted in the inclusion of the common law trust in the legal system of Malawi (Mtonga, 2015:7).

In the next section the colonial influence on the development of tax legislation on the "Commonwealth family" is further illustrated by presenting a history of the development of trusts in South Africa.

In April 1652 Jan van Riebeeck arrived in the Cape of Good Hope (Southern tip of Africa) to set up a refreshment post for the Dutch when travelling to the East (Bain, 2018:1; Viljoen, 1997:320). Dutch influence was dominant in the Cape after 1652 and as a result Roman-Dutch law found its way into the legal system of the ever-expanding Cape Colony (Honiball & Olivier, 2009:2). In 1795 the first British occupation of the Cape took place, and in the early 1800's there was a second occupation of the Cape by the British (DuToit, 2002:18; Cameron, de Waal, Wunsh, Solomon & Kahn, 2002:21). Even though the Cape found itself under British rule, the British did not repeal the Roman-Dutch law, which had now entrenched itself over a period of approximately 150 years (Du Toit, 2002:18). However, it was inevitable that certain British concepts and laws (including the trust) found their way into the South African legal system (Cameron, de Waal, Wunsh, Solomon & Kahn, 2002:21; Du Toit, 2002:18**)**. In 1833 the first case involving a trust (Twentyman v Hewitt (1833) 1 Menz 156) was decided in the Cape. However, in this case the court rejected the trust as a legal instrument in South Africa (Cameron, de Waal, Wunsh, Solomon & Kahn, 2002:21).

During 1905 in the case of *Lucas Trustee (Lucas' Trustee v Ismail & Amod* 1905 TS 239) the court, for the first time, acknowledged the trust in South African law albeit that this case was that of a testamentary trust. In a landmark case in 1915 (Estate *Kemp v McDonald Trustee* 1915 AD 491) the Appellate Division held that the trust was not incompatible with South African law and the court indicated that the trustee was the owner of the property, while the beneficiary only had a personal right against the trust. This ruling is seen as the first judicial acceptance of the trust in South African courts (Honiball & Olivier, 2009:2; Du Toit, 2002:18-21).

Since the early 1900's the trust law in South Africa kept evolving and was highly influenced by court cases on different issues pertaining to the trust (*Lucas' Trustee v Ismail & Amod* (1905); *Estate Kemp v MacDonald's Trustee* (1915); *Armstrong v CIR* (1938)). In 1938 and in 1971, two cases (*Armstrong v CIR; SIR v Rosen)* confirmed the principle that the trust is

a mere conduit pipe (flow through principle) in relation to income earned by the trust. This means that an amount received by a trust and attributed to a beneficiary retains its nature (Horak, 2018:21). A further concept that was also settled through the courts was the attributes required for the ownership in *inter vivos* trusts (Du Toit, 2002:24). During the 1940's and 1950's the courts confirmed that the ownership trust is based on the principle of a contract and that the donor and the trustees enter into a contract for the benefit of the beneficiaries (Du Toit, 2002:23). In 1984, in the case of *Braun v Blann and Botha* (*Braun v Blann and Botha NNO* 1984 (2) SA 850 (A)), the question of the English trust again arose in the court and it was finally settled. The court concluded that the South African trust is a uniquely South African institution and that it evolved over time and is still evolving (Cameron, de Waal, Wunsh, Solomon & Kahn, 2002:22-24).

In South Africa and other countries, one of the applications of the trust is as an entity through which business is conducted (Honiball & Olivier, 2009:23). The popularity of trusts as a business type is attributed to the fact that a trust provides limited liability to trustees and has no expiration date (Honiball & Olivier, 2009:23). A further reason for the popularity of trusts lies in its flexibility to distribute or split income between beneficiaries; this allows for more effective tax planning (Freudenberg, Tran-Nam, Karlinsky & Gupta, 2012:29).

The presence of trusts in all the jurisdictions included in this study creates a foundation for the comparison of the tax complexity contained in the definitions and sections included in the tax legislation of the selected SADC jurisdictions.

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2.5. THE TAXATION OF TRUSTS

This section addresses general principles applied internationally (outside SADC) to the taxation of trusts and flow through entities. In this regard, Hin (2010) identifies five general models that may be applied in the taxation of trusts and this will be considered in this section.

In the UK, the government acknowledges the importance of the trust in society (Kessler, 2013:365). In this regard the government wishes to provide proper tax structures for the taxation of trusts and does not wish to create artificial incentives for the creation of trusts

(Kessler, 2013:365). In Australia, the trust is viewed as a legitimate structure through which its citizens may conduct their business and personal affairs and should not be viewed as a structure to assist in the avoidance of tax (Kessler, 2013:365). In the USA, the trust and flow through companies are only taxed once at the 'member' or 'beneficiary' level (Freudenberg, Tran-Nam, Karlinski & Gupta, 2012:684).

In Australia, the income of a trust is also taxed on the flow through basis (Freudenberg, Tran-Nam, Karlinski & Gupta, 2012:687). However, the Australian system is seen as a partial flow through system, as the income received by the trust may be vested in a beneficiary, but the vesting of a loss is not permitted and thus remains captured in the trust (Freudenberg, Tran-Nam, Karlinski & Gupta, 2012:687). In 2001 the Australian federal government proposed entity taxation for trusts similar to the tax system used for companies and other entities (Taylor-Sands, 2001:[1]). This proposal was subsequently amended with the entity taxation system only being applied to certain types of trusts (Taylor-Sands, 2001:[2]). The entity taxation system would mean that the trust would be taxed on all the revenue earned by the trust and would effectively end the flow through principle, as the trustees (on behalf of the trust) would be taxed on the gross amount earned by the trust and distributions to the beneficiaries would be taxed on a system similar to dividends tax (Taylor-Sands, 2001:[2]). All distributions to beneficiaries would be made from post-tax or retained earnings (Taylor-Sands, 2001:[2]). Subsequently various amendments and changes to the Australian legislation were proposed and introduced (Cooper, 2013:219, 224,227). Cooper (2013:235) comments that the vast number of changes and amendments to the trust legislation is unlikely to result in a uniform, coherent and consistent trust taxation system. He contends that the reason for this plethora of legislative amendments includes politics, industry pressure, interest group pressure and the contesting of well-known and accepted tax principles for the taxation of trusts by the tax authority (Cooper, 2013:235).

As is evident from the above, no standard model for the taxation of trusts is used in the tax jurisdictions discussed above. However, Hin (2010) has identified five models that may be applied to the taxation of trusts that are discussed in more detail below. He further contends that hybrids or a combination of these models may be used within different tax jurisdictions. These five models as described by Hin (2010) are:

2.5.1.1. *Trustee Taxation Model*

Under the Trustee Taxation Model the income of the trust will be taxed at the rates applicable to the trustee(s) (Hin, 2010:48). Beneficiaries will not be taxed on any income received from the trust, even though distributions of trust income may have been made to the beneficiaries, as all the income will only be taxed once (at the trustee level) (Hin, 2010:48).

2.5.1.2. *Imputation Model*

Under the Imputation Model the income of the trust will be taxed in the hands of the trustee based on the trustee's tax rate, as well as the tax sections relevant to the trustee (Hin, 2010:48). Income that is attributable to a beneficiary or that may accrue to the beneficiary will however be taxed at the rate applicable to the beneficiary, taking into consideration the beneficiary's tax rate and tax sections applicable (Hin, 2010:48). To prevent the same income being taxed twice, a tax credit will be given to the beneficiary for income already taxed in the trust at the trustee level (Hin, 2010:48).

2.5.1.3. *Modified Imputation Model*

Under the Modified Imputation Model the income of the trust will be taxed at the rate of the trustee based on the trustee's tax rate, as well as the tax sections relevant to the trustee (Hin, 2010:48). However, income attributable to the beneficiary will be taxed in the trust at the rate applicable to the beneficiary taking into consideration the beneficiary's tax rate and tax sections applicable. The result of this treatment of the beneficiary's portion of the income will have the effect that the tax calculated at the trustee level should match the actual amount payable on the income of the trust. This limits the additional administration required to calculate and provide a tax credit to the beneficiary (Hin, 2010:48).

2.5.1.4. *Direct Beneficiary Taxation Model*

Under the Direct Beneficiary Taxation Model (also known as the Flow Through Entity Model or the Tax Transparent Entity Model) the income of the trust is taxed directly in the hands of the beneficiary at the rate applicable and taking into consideration the tax sections applicable to the beneficiary (Hin, 2010:48). Effectively this model ignores the trust for tax purposes. A further characteristic of this model is that the nature of the income

that accrues to the trust is retained (flow through principle) and any tax benefits attributable to a specific type of income may then be utilised by the beneficiary. Any income that may not directly accrue to a beneficiary will however be taxed at the trustee level using either the Trustee Taxation Model or the Imputation Model. Alternatively, income not attributed to the beneficiary may be retained in the trust pending distribution to the beneficiaries at which time it will be taxed at the rate applicable to the beneficiaries as discussed above. This may however lead to the trust being used for tax deferral purposes (Hin, 2010:48).

2.5.1.5. *Indirect Beneficiary Taxation Model*

Under the Indirect Beneficiary Model the tax is calculated on a similar basis to the Direct Beneficiary Model (Hin, 2010:48). However, to ensure collection of the relevant tax on the amounts attributable to the beneficiaries, the tax on these amounts will be retained by the trust and paid to the revenue authority on behalf of and for the benefit of the beneficiaries. This is done to ensure actual collection, specifically in cases where amounts may be attributable to non-residents with limited presence in the relevant tax jurisdiction (Hin, 2010:48).

2.5.1.6. *Hybrid Models*

Under a Hybrid Model one or more of the above models are combined for application within a specific tax jurisdiction (Hin, 2010:48). This may be done to ensure a feasible model for a specific type of trust, or to meet with the policy objectives of the relevant tax jurisdiction (Hin, 2010:48).

Table 2 displays the models of the taxation of trusts as described by Hin (2010:48). The table illustrates the different options available to tax authorities in deciding on a policy to apply for the taxation of trusts. The decision by the tax authority will determine which entity - the trustees (on behalf of the trust) or the beneficiaries - will be taxed on the income of the trust (Hin, 2010:48). In practice, it is not uncommon that tax authorities apply Hybrid Models that integrate characteristics of more than one of the models listed below.

Table 2: Models of the taxation of trusts

	Trustee Taxation Model	Imputation Model	Direct Beneficiary Taxation Model	Indirect Beneficiary Taxation Model
TAXABLE ENTITY	Trustee	Trustee and beneficiary	Beneficiary	Beneficiary
EFFECTIVE TAX RATE				
- On income to which the beneficiary is *not* entitled	Trustee's effective tax rate	Trustee's effective tax rate	Not applicable	Not applicable
- On income to which the beneficiary is entitled or which is distributed to the beneficiary[1, 2]	Trustee's effective tax rate	Trustee's effective tax rate	Trustee's effective tax rate	General withholding tax rate or beneficiary's effective tax rate[3]
TIMING OF TAX CHARGE				
- On the trustee	When the income is derived by the trust	When the income is derived by the trust	Not applicable	Not applicable
- On the beneficiary	Not applicable	When the beneficiary becomes entitled to the income or when he receives the distribution[1]	When the beneficiary becomes entitled to the income	When the beneficiary becomes entitled to the income or when he receives the income[2]
Collection of tax	From trustee	From trustee[4]	From beneficiary	From trustee[5]

Notes:

1 Under the Imputation Model, the beneficiary may be taxed once he is entitled to the trust income or only when the income is distributed to him.

2 Under the Indirect Beneficiary Taxation Model, it is usual for the withholding tax to be triggered only when the trust income is distributed to the beneficiary.

3 This depends on whether the withholding tax represents the final or a non-final tax liability of the beneficiary.

4 Unless the Modified Imputation Model is used, a tax refund has to be made to the beneficiary if the gross tax payable on all of his income is lower than the tax credit for the tax imposed at the trustee level on his share of the trust income.

5 If the withholding tax is non-final, a tax refund may have to be made to the beneficiary if the gross tax payable on all of the income is lower than the tax withheld by the trustee on the distribution of the tax income.

2.6. COMPARATIVE FOUNDATION

The sections above considered the constructs of tax complexity and trusts as well as the different models that may be applied to the taxation of trusts. They analysed the constructs to identify the characteristics that contribute to the complexity that will be considered when assessing the complexity involved in the trust tax legislation of the selected SADC jurisdictions. The purpose of this section is to provide an orientation and basis for this comparative study.

Prior to assessing tax complexity, the question invariably arises as to what the goal is in assessing the complexity. There may be different reasons as to why tax complexity should be measured. A purely academic approach to measuring tax complexity may be to satisfy the requirements of comparing the tax complexity of one country to another country, or to merely measure tax complexity to compare it with an earlier measurement for the same country. A further consideration would be to develop an indicator that would confirm that complexity exists and furthermore that simplification efforts taken are effective (Ulph, 2015:51).

Ulph (2015:50) proposes that the primary reason for measuring tax complexity is to ascertain where to focus simplification efforts. He indicates that there are two main areas of complexity that may be measured. These areas are ‘design complexity’ and ‘operational complexity’. An example of a basis to measure ‘design complexity’ would be to measure the length of tax legislation and compare it to previous versions of this legislation to assess the extent of the impact of simplification on the tax legislation. Measuring ‘operational complexity’ may result in an index that would indicate the cost involved with compliance to the tax legislation. ‘Operational complexity’ comprises of two distinct categories, namely ‘compliance complexity’ and ‘transactional complexity’ (Ulph, 2015:47).

- ‘Compliance complexity’ refers to the record keeping activities involved in complying with the tax legislation (Pedersen, 2011:286). This denotes the actual calculation, submission (filing) and settlement of the tax debt.
- ‘Transactional complexity’ refers to additional processes or actions that the taxpayer may undertake to evaluate different options available when ambiguous tax

legislation allows for tax planning. Activities included are those required to investigate the different options available to the taxpayer (Pedersen, 2011:286).

In summary, ‘design complexity’ measures the complexity of the legislation itself, whereas ‘operational complexity’ measures the practical efficiency of the tax legislation.

For the purpose of this study the tax legislation of the selected SADC jurisdictions are analysed with the focus on the definitions and sections applicable to the taxation of trusts. The focus of the analysis is based on the ‘design complexity’ related to the characteristics identified earlier in this chapter. The critical analysis highlights the definitions and sections included in the tax legislation and also includes a comparison based on these characteristics.

2.7. SUMMARY

The purpose of this chapter was to provide a theoretical background for the study. It explored the history and purpose of taxation and then continued with a discussion on the construct of tax complexity with reference to the definitions, properties, sources and the consequences of complexity. The construct of a trust was then discussed with a review of the history and background of the trust. This history provided an understanding of and basis for the complexity of the trust concept. This was followed by a discussion on the taxation of trusts and an analysis of different models that may be applied in the taxation of trusts. The section that followed considered the development of trusts in the SADC region through a discussion on the colonial background and influences on the trust concept. This was illustrated by a review of the history and development of the trust in South Africa. Finally, the comparative foundation for the study, based on the literature review, was presented.

CHAPTER 3: RESEARCH DESIGN AND METHODOLOGY

3.1. INTRODUCTION

The research objective of this study is to investigate tax legislation between selected SADC countries with the purpose to explore and compare tax legislative complexities related to trusts. The purpose of this chapter is to clarify the research design and methodology selected to achieve this objective and to motivate the applicability of the research design and the methodology.

As stated in Chapter 1, the study is qualitative in nature within the field of tax legislation. In the context of the research objective, the trust tax legislation of the selected SADC countries is analysed and compared with the purpose, to determine the complexity in the trust tax legislation.

The chapter outlines the orientation of the research design and then proceeds to clarify the research methodology. This is followed by a discussion on the nature of the data and the method of collection. Lastly, the chapter includes a discussion of the validity and reliability of the data collected and analysed.

3.2. RESEARCH DESIGN

This section explains the adopted research design to provide clarity on the philosophical underpinning of the study, the nature of the study, the reasoning approach of the study, the study's time horizon, the unit of analysis in the study, and the nature and sources of the data relevant to this study.

3.2.1. Philosophical perspective of the study

The dominant perspective from which this study is approached is that of critical realism. Critical realism may be viewed as a research philosophy that falls in the middle ground between positivism and interpretivism (McKerchar, 200:7). In this regard the critical realist wishes to answer the questions of 'why' and 'how' (McKerchar, 200:8). Researchers who

ascribe to the critical realism philosophy is typically guided by the perpetual results of the research process, as opposed to a preconceived outcome (McKerchar, 200:8).

The philosophy of critical realism is based on what we experience in relation to the underlying reality (Thornhill, Saunders & Lewis, 2009:590). Critical realist researchers in the business and management environment comprehends what transpires in the social world subsequent to their comprehension of the structures that form the foundation of the social phenomenon (Thornhill, Saunders & Lewis, 2009:115). Critical realism views the world from a two-step approach. The first step is the occurrence of the event and the immediate impact thereof. The second step is the mental processing that follows the impact of the occurrence (Thornhill, Saunders & Lewis, 2009:115). McKerchar (2008:8) is of the opinion that the critical realism philosophy provides a suitable paradigm fit for researchers in the legal discipline.

3.2.2. The nature of the study

This study is exploratory in nature. The research is conducted by way of a study of the literature and is undertaken to review and interpret the legislation of the selected SADC countries.

Exploratory research is flexible and adaptable in nature and may result in a change in direction as the research progresses (Thornhill, Saunders & Lewis, 2009:140). Exploratory research initially has a broad focus on the literature that becomes progressively narrower as the study progresses (Saunders, Lewis & Thornhill, 2016:140).

3.2.3. Reasoning approach

Doctrinal research involves a meticulous analysis and original combination of legal principles, the identification of similarities and the extraction of similar principles (CALD, 2005:3). Doctrinal research can either follow a deductive reasoning approach, an inductive reasoning approach or a combination referred to as abductive reasoning (Bryman & Bell, 2007:11).

For the purpose of this study the legislation was collected, analysed, connections made and similar principles extracted. These similar principles were then analysed to identify

complexity contained in the legislation. This study is thus based on an inductive reasoning approach (Thornhill, Saunders & Lewis, 2009:41).

3.2.4. Time horizon of the study

The time horizon of the study is cross-sectional, as the study looks at a particular data set at a particular time (Thornhill, Saunders & Lewis, 2009:155). This study is conducted in two distinct phases. The first phase of the study consists of the collection and analysis of the data and the second phase of the critical comparison and conclusion on the data.

3.2.5. Unit of analysis

The research is conducted on the tax legislation of the selected SADC jurisdictions with a specific focus on the sections that impact on trusts. The documentary data used for this study are the income taxing acts or similar legislation of the selected SADC jurisdictions. Additional sources include government publications, books and peer reviewed academic articles. The analysis is performed to create a background and to define and describe the constructs that underpin the study.

3.2.6. Nature and sources of data

The data collected is classified as secondary data. The tax legislation of the Republic of South Africa was obtained from LexisNexis, the official supplier of all legislation via their data bases to the South African Revenue Service. The tax legislation of all other selected SADC countries was obtained from the official government websites of these tax jurisdictions. In all cases the latest available version of the legislation was obtained to ensure that all amendments are included and considered.

All the data collected is available publicly therefore there are no confidentiality and ethical considerations relating to their use.

3.3. RESEARCH METHODOLOGY

This section clarifies the research methodology adopted in the study in terms of its methodological classification, research strategy and data collection technique.

3.3.1. Methodological classification

The methodological classification of the research is qualitative in nature. This type of research is based on non-numeric data and inferences are derived from meanings expressed through words (Thornhill, Saunders & Lewis, 2009:482). The collection process results in non-standardised data that is grouped into determined categories. The categorised data is analysed through conceptualisation that allows for rich or thorough description of the data and is then applied to formulate a specific theory (Thornhill, Saunders & Lewis, 2009:482).

The qualitative research methodology is selected as the data consists of doctrine in the form of words, sentences and paragraphs. This analysis of doctrine justifies the adoption of the doctrinal research strategy.

3.3.2. Doctrinal research

The doctrinal or “black letter law” research methodology is relevant in a study of aspects of the law (McKerchar, 2008:18). This methodology is applied when asking what the law is and how it was developed and applied (Hutchinson, 2015:130). Doctrinal research is pure theoretical research aimed at making inquiries to identify specific pieces of information relevant to the study (Ali, Yusoff & Ayub, 2017:493). This methodology is selected to critically analyse documentary data to reach conclusions and propose changes to the existing legislation, if and where appropriate (McKerchar, 2008:18-19).

The doctrinal research method is selected for this study and applied to critically analyse the data to compare and conclude thereon. The doctrinal research methodology is considered to be appropriate given the purpose of the research. In applying the doctrinal research strategy to the study the tax legislation of the selected SADC countries is analysed and sections relevant to the taxation of trusts are identified and interpreted. Components relevant to the objectives of the study are assessed, categorised and tabulated. The tabulated data is compared and assessed to identify aspects that may indicate the complexity involved in the legislation. Thereafter a critical analysis of the tabulated data is performed.

3.3.3. Data collection

In undertaking the research, the secondary data collected is the tax legislation of the selected SADC countries.

The data is analysed, tabulated and interpreted to achieve the research objectives, and takes the form of a critical review, supported by documentary evidence. To ensure the validity and reliability of the study the following criteria were applied:

- Placing greater weight on legislation;
- Considering credible and relevant sources;
- Considering opinions of acknowledged experts in the field;
- Concluding on the basis of credible evidence; and
- The rigour of the arguments.

The results of the data collected are presented in the next section.

3.4. SUMMARY OF INITIAL REVIEW OF DATA

This section provides a summarised overview of the data collected. The information collected for the data analysis was selected to inform the research objective of the study. The information was extracted from the tax legislation of the selected SADC jurisdictions. The tax legislation of each of the selected jurisdictions was analysed and the sections related to the taxation of trusts (in accordance with the demarcation of the study) were considered and extracted. The data extracted from the legislation and included in Table 3 are not meant to be the conclusion of the study, but rather to provide a basis on which conclusions may be made. In other words, the table includes relevant data from the tax legislation of the SADC jurisdictions that will be used to inform the conclusion of the study.

This information was categorised and tabulated under the following headings:

- **Jurisdiction –** introduces the selected SADC jurisdiction;

- **Legislation –** indicates the tax legislation of the selected SADC jurisdiction considered;

- **Trust inclusion –** indicates that a trust is provided for in the tax legislation of the selected SADC jurisdiction;

- **Trust definition –** indicates that the tax legislation of the selected SADC jurisdiction includes a definition of a trust;

- **Taxpayer definition –** indicates that the tax legislation includes a taxpayer definition (e.g. 'person') that includes a trust;

- **Trust tax section –** indicates that the tax legislation of the selected SADC jurisdiction includes a section that specifically deals with the taxation of trusts;

- **Taxation in the trust -** indicates that the tax legislation of the selected SADC jurisdiction provides for the taxation of all trust income in the trust (no attribution to beneficiaries);

- **Beneficiary attribution –** indicates that the tax legislation of the selected SADC jurisdiction makes provision for the attribution of income to a beneficiary; and

- **Anti-avoidance –** indicates that the tax legislation of the selected SADC jurisdiction includes anti-avoidance sections, e.g. attribution to the donor.

Table 3 summarises the results of the initial overview of the trust tax legislation of the selected jurisdictions. The results in Table 3 are arranged from the more basic definition of a trust and its inclusion in the definition of a taxpayer to the more complex concept of the attribution of trust income flowing through to the beneficiary, and finally attribution to a donor or other trust specific tax implications. Chapter 4 will consider the concepts used in the table in detail through the lens of complexity.

Table 3: Summary of initial overview *

Jurisdiction	Legislation	Trust inclusion	Trust definition	Taxpayer definition	Trust tax section	Taxation in the trust	Beneficiary attribution	Anti-avoidance
Botswana	Botswana Income Tax Act, Cap 52:01	✓	✓ Section 19(2)	✓ Section 2, 'person'	✓ Section 19(2)	✓ Section 19(1)	✗	✓ Section 13, Section 14, Section 15
Eswatini (Swaziland)	Eswatini (Swaziland) Income Tax Order in Council No 21 of 1975	✓	✗	✓ Section 2 'person'	✓ Sect 19*bis*	✗	✓ Section 19*bis*(1) and 19*bis*(3)	✓ Section 11
Lesotho	Lesotho Income Tax Act No 9 of 1993	✓	✓ Section 3	✗	✓ Section 4(1)	✗	✓ Section 81(1), 81(6) and Section 82	✓ Section 74(1)(e)
Malawi	Malawi Taxation Act Chapter 41:01	✓	✗	✓ Section 2, 'person'	✓ Section 2, Section 76	✗	✓ Section 2	✓ Section 72
Mauritius	Mauritius Income Tax Act of 1995	✓	✓ Section 2	✓ Section 2, 'person'	✓ Section 46	✓ Section 46	✗	✗
Namibia	Namibia Income Tax Act 24 of 1981	✓	✗	✓ Section 1, 'person'	✓ Section 5	✗**	✓**	✗

Jurisdiction	Legislation	Trust inclusion	Trust definition	Taxpayer definition	Trust tax section	Taxation in the trust	Beneficiary attribution	Anti-avoidance
Seychelles	Seychelles Business Tax Act No 28 of 2009	✓	✓ Section 2	✓ Section 2, 'person'	✓ Section 40	✗	✓ Section 40	✓ Section 56
South Africa	South Africa Income Tax Act No 58 of 1962	✓	✓ Section 1 (1)	✓ Section 1 (1), 'person'	✓ Section 25B	✗	✓ Section 25B	✓ Section 7, Section 7C
Tanzania	Tanzania Income Tax Act of 2004, Chapter 332	✓	✓ Section 3	✓ Section 3, "entity", 'person'	✓ Section 5	✓ Section 52	✗	✗
Zambia	Zambia Income Tax Act No 3 of 1997, Chapter 323	✓	✗	✓ Section 2, 'person'	✓ Section 27	✗	✓ Section 27(4), section 60(3)	✓ Section 19
Zimbabwe	Zimbabwe Income Tax Act Chapter 23:06	✓	✗	✓ Section 2, 'person'	✓ Section 6, Section 7	✗	✓ Section 2	✓ Section 10

Key:

✓ - included in the legislation

✗ - not included in the legislation

** Refer to Section 0

3.5. CONCLUSION

The purpose of this chapter was to clarify the research design and methodology applied to this study. The doctrinal research methodology was employed to identify specific strands of doctrines relevant to the study. The study was described as exploratory in nature using both inductive and deductive reasoning. This methodology was selected to critically analyse the documentary data to identify similarities and to reach conclusions based on the extracted data. The extracted data from the tax legislation (secondary data) of the SADC jurisdictions was tabulated to form the foundation of the detailed comparison in the following chapter.

CHAPTER 4: DATA ANALYSIS

4.1. INTRODUCTION

This chapter analyses the legislation in the selected jurisdictions to identify and understand the core concepts relevant to trust tax legislation in the various jurisdictions, in an effort to identify complex characteristics included therein. It is acknowledged that the various jurisdictions may apply different approaches to the design, construction and expression of the relevant trust tax sections. Based on an interpretation of the relevant legislation applicable to each jurisdiction, a categorisation is made based on the tax treatment of trusts and related complexities in the selected SADC jurisdictions.

4.2. THEMATIC DISCUSSION

The data of the study as presented in Table 3: Summary of initial overview (Section 3.4) is discussed in the context of complexity based on the following six recurring themes identified during the initial overview, namely:

- Trust inclusion (Does the tax legislation provide for trusts?)
- Trust definition (Is a trust defined in the tax legislation?)
- Taxpayer definition (Is a trust or trustee included in a taxpayer definition?)
- Taxation in the trust (Does the legislation provide for all of the income of a trust to be taxed in the trust?)
- Beneficiary flow through (Does the legislation make provision for the flow through of income to beneficiaries?)
- Anti-avoidance (Does the legislation make provision for anti-avoidance that may be applicable to trusts?)

The thematic perspective summarises the data from a cross-sectional view of the recurring underlying themes in the tax legislation; in other words recurring themes are used as a basis to extract similar provisions from the tax legislation.

The following sections consist of a discussion of each of these themes as they relate to the concepts of complexity discussed in Chapter 2.

4.2.1. Trust inclusion

The tax legislation of all the jurisdictions (Botswana, Eswatini, Lesotho, Malawi, Mauritius, Namibia, Seychelles, South Africa, Tanzania, Zambia and Zimbabwe) included in the study makes provision for the taxation of trusts, as is evident from the applicable sections listed in Table 3. The provision for the taxation of trusts in the legislation confirms that trusts are used in the relevant jurisdictions. In addition to this, the inclusion of tax legislation governing trusts may indicate that attempts have been made to provide certainty to taxpayers regarding the taxation of these entities. The individual components of the tax trust legislation are analysed in Sections 4.2.2 to 4.2.6 below.

4.2.2. Trust definition

Even though seven of the selected SADC jurisdictions (Botswana, Lesotho, Mauritius, Seychelles, South Africa and Tanzania) define a trust in the relevant tax legislation, it was found that complexity could be increased as a result of difficult terminology, reference to other acts or the lack of characteristics in defining a trust. In considering these definitions it is notable that there is little consistency in the structure of the definitions and the intricacies are pointed out after quoting the definition from the relevant acts below:

- Botswana ITA:

  > "In this section 'trust' includes-
  > (a) a will or other testamentary disposition; and
  > (*b*) a deed of donation, settlement or other disposition."

  In the Botswana ITA, although the definition is simple and concise, the inclusion of the term "a deed of donation, settlement or other disposition" in the definition may require

a higher level of understanding of the applicable section of the tax legislation, and may necessitate the assistance of a legal expert or tax practitioner to interpret the meaning. This type of complexity can be described as 'predictability' or 'technical complexity' (refer to Section 2.3.2.1). Similarly, the inclusion of these terms may also be considered an aspect of drafting complexity (Section 2.3.5.5) and statutory complexity (Section 2.3.3.2). The inclusion of the term "a deed of donation, settlement or other disposition" may also cause compliance complexity (difficulty), as the taxpayer may require the services of a legal expert or tax practitioner to assist with the interpretation of this terminology (refer to Section 2.3.2.4). A further complexity encountered in the Botswana ITA is the inclusion of the definition of a trust in Section 19 (taxation of trusts) and not in the terminology section of the legislation. This may impact the 'predictability' of the legislation and may require a higher level of intellectual investment needed to source and interpret the applicable section of the tax legislation (refer to Section 2.3.2.1). The definition of a trust in Section 19 creates additional technical complexity (refer to Section 2.3.2.1), as the definition merely states what is included under a trust and no characteristics of a trust are provided. Furthermore, the definition refers to its meaning in relation to Section 19 only. This implies that there may be a common understanding of the meaning of a trust, even though no other definition of a trust is included in the legislation.

- Lesotho ITA:

> "'trust' includes the estate of a deceased person, but does not include a grantor trust or qualified beneficiary trust described in section 80;"

In the Lesotho ITA a trust is included in Section 3 (relating to the terminology or interpretation section of the legislation). However, the 'definition' merely states what is included and excluded under a trust and no characteristics of a trust are included in this definition. The lack of characteristics may result in technical complexity (refer to Section 2.3.2.1). In addition to the lack of characteristics, the definition of a trust includes a "deceased estate", but excludes two specific types of trusts. These two exclusions deal with anti-avoidance and will be discussed in Section 4.2.6, but again result in what may be considered to be technical complexity (refer to Section 2.3.2.1). This lack of clarity in the legislation may lead to compliance complexity (refer to

Sections 2.3.2.4 and 2.3.3.4), as a taxpayer may need the assistance of a legal expert or tax practitioner to assist with the classification of the trust and the trust income.

- Mauritian ITA:

  "'trust' means a trust recognised under the laws of Mauritius;"

  This definition of a trust appears simple. However, in analysing the definition of a trust as defined in Section 2 of the Mauritian ITA, it requires the reader to familiarise himself with the concept of a trust as is recognised under the laws of Mauritius. The definition of a trust in Mauritius is found in the Mauritian Trusts Act of 2001 (du Plessis, 2018:280). This requirement may cause difficulty for taxpayers who wish to comply with the tax legislation, as the services of tax practitioners or legal experts may be required in recognising the characteristics of a trust in terms of the laws of Mauritius. This is an indication of the existence of compliance complexity (refer to Sections 2.3.2.4 and 2.3.3.4).

- Seychelles BTA:

  " a trust –
  (i) settled or established in Seychelles; or
  (ii) In respect of which a trustee of the trust is a resident person;"

  This definition of a trust creates a similar problem to that found in the Mauritian ITA. In Seychelles the definition of a trust includes a trust "established under the laws of equity" (Section 2). As the term "established under the laws of equity" is not defined in the Seychelles BTA, the services of a tax practitioner or a legal expert may be required to assist the taxpayer to comply with their tax obligation. This may cause compliance complexity (refer to Sections 2.3.2.4 and 2.3.3.4) as the tax authority will be required to ascertain whether the trust is established under the laws of equity in Seychelles. Additionally, compliance complexity (difficulty) is added to the definitions in referring to an additional piece of legislation, due to the assistance that may be required by the taxpayer (refer to Sections 2.3.2.4 and 2.3.3.4).

- South African ITA:

> "'trust' means any trust fund consisting of cash or other assets which are administered and controlled by a person acting in a fiduciary capacity, where such person is appointed under a deed of trust or by agreement or under the will of a deceased person;"

This definition of a trust may be difficult for a taxpayer to interpret and understand, as it includes terminology such as "trust fund", "fiduciary capacity" and "deed of trust or agreement". These terms may not be familiar to taxpayers and the services of a tax practitioner or a legal expert may be required in the interpretation of the definition. This may again cause compliance complexity (refer to Sections 2.3.2.4 and 2.3.3.4) that may have been avoided if all the terminology was defined in the tax legislation.

- Tanzanian ITA:

> "'trust' means an arrangement under which a trustee holds assets but excludes a partnership and a corporation;"

This definition of a trust may be considered simple and easy to interpret and understand, as there are no references to other legislation, the wording applied in the definition is simple and it includes terminology that is defined in the legislation.

While the majority of the jurisdictions analysed in this study did define a trust in their legislation, five of the jurisdictions (Eswatini, Namibia, Malawi, Zambia and Zimbabwe) do not define a trust in their tax legislation. Even though the inclusion of a definition may also result in complexity (as pointed out above), the lack of a definition of a trust creates uncertainty (refer to Section 2.3.4.4), as the taxpayer may not understand what is included in the term "trust". This uncertainty introduces an element of technical complexity (or predictability) for the taxpayer (refer to Section 2.3.2.1), as the level of intellectual investment needed to interpret the tax legislation with clarity and certainty is somewhat higher. This technical complexity (refer to Section 2.3.2.1) may have been averted if the legislature provided for clarity and certainty of the terminology in the process of drafting the legislation (refer to Sections 2.3.3.2 and 2.3.5.5). A further complexity caused by the lack of a definition of a trust is structural complexity or 'manipulability' (refer to Section

2.3.2.2). ‘Manipulability’ refers to the extent that the tax legislation lends itself towards tax planning and tax manipulation. The lack of a definition of a trust creates uncertainty on the taxation of the income of a trust and this may provide an opportunity for tax manipulation. This structural complexity may lead to multiple interpretations for similar transactions between taxpayers, trustees or trusts and should be avoided at a legislative level. In this context, compliance complexity (difficulty) may be caused, as taxpayers may be forced to consult with a tax practitioner or a legal expert to assist with the interpretation and application of the trust tax legislation related to the trust income of the taxpayer (refer to Sections 2.3.2.4 and 2.3.3.4).

Notwithstanding the above, each jurisdiction that does not include a definition of a trust and the related complexities are discussed below:

- In the Eswatini ITO, the Malawian TA and the Namibian ITA, while no specific definition of a trust is provided, the term “trustee” is defined. The fact that there is no definition of a trust but there is a definition of a “trustee” still creates uncertainty (refer to Section 2.3.4.4); hence a level of technical complexity or ‘predictability’ (as discussed in Section 2.3.2.1) and lack of clear interpretation may cause compliance complexity (‘difficulty’), as taxpayers may be uncertain as to the nature and treatment of a trust for tax purposes (refer to Sections 2.3.2.4 and 2.3.3.4).

- In Zambia, while no specific definition of a trust is included, the definition of a “settlement” includes a “disposition”, “trust”, “agreement”, “covenant”, “arrangement” or a “transfer of assets” (Zambian ITA Section 19(7)). This may be seen as a form of technical complexity (refer to Section 2.3.2.1). The reference to a trust in the definition of settlement may be considered statutory complexity caused during the process of drafting of the legislation (refer to Sections 2.3.3.2 and 2.3.5.5). This statutory complexity may increase the cost of compliance (‘difficulty’), as the taxpayer may again require the services of a tax practitioner or legal expert to clarify tax matters related to the inclusion of a trust for tax purposes (refer to Sections 2.3.2.4 and 2.3.3.4).

- In Zimbabwe, the terms “beneficiary with a vested right” and “income the subject of a trust to which no beneficiary is entitled” are defined in the legislation (Zimbabwean ITA

Section 2). Once again, this creates a level of technical complexity or ‘predictability’ as discussed in Sectinon 2.3.2.1. Similarly, the terminology used in the drafting of these definitions increases technical complexity, as this terminology may cause uncertainty from a grammatical perspective (refer to Section 2.3.2.1).

In conclusion, six of the eleven jurisdictions included a definition of a trust in the tax legislation while five did not. However, those jurisdictions that did not include a definition refer to trusts in other definitions or terminology. The presence of a definition of a trust may not necessarily have simplified the taxation of trusts, as various other aspects of complexity may have resulted from the definition itself or the location thereof in the legislation. In assessing the definitions it became apparent that the jurisdictions may have applied varying drafting styles that resulted in differences in the definitions of a trust. These differences in the definitions of a trust may also result in varying interpretations of the trust tax terminology in the different jurisdictions. In the jurisdictions that did not include a definition of a trust in their tax legislation, there may be an increased level of uncertainty in the interpretation of the trust tax legislation.

In the following section the inclusion of a trust in a taxpayer definition will be considered.

4.2.3. Taxpayer definition

Ten of the eleven jurisdictions (all jurisdictions, excluding Lesotho) included a trust or trustee in the definition of either a “person”, “entity” or “company”. These jurisdictions included these definitions of different taxpayers in the interpretation or terminology section of their respective tax legislation. The importance of a taxpayer definition in tax legislation is that it delineates the inclusion of different types of taxpayers into one specific definition. These taxpayer definitions simplify the taxing provisions in the legislation, as reference may only need to be made to one definition which includes multiple groups of taxpayers.

It is submitted that in this context the use of a definition of a taxpayer simplifies the tax legislation, as it may create more certainty amongst taxpayers (refer to Section 2.3.4.4). This reduces the technical complexity (‘predictability’) (refer to Section 2.3.2.1), as the taxpayer may read the legislation to ascertain the sections relevant to the taxpayer (trust) once he has ensured that a trust is included in a taxpayer definition. In addition, the use of

a taxpayer definition reduces the length of the legislation, as the number of words included in the legislation is limited to the taxpayer definition and may improve the readability of the legislation (refer to Section 2.3.2.1).

In eight of the eleven jurisdictions (Botswana, Eswatini, Malawi, Mauritius, Namibia, Seychelles, South Africa and Zambia), a trust or trustee is explicitly included in the definition of a "person". As discussed above this inclusion of a trust in the definition of a person simplifies the application of sections of the tax legislation that are relevant to trusts. This reduces technical complexity and improves readability of the tax legislation (refer to Section 2.3.2.1).

In the Mauritian ITA, however, a trust is also included in the definition of a "company" and this may be an indicator of technical complexity in the legislation (refer to Section 2.3.2.1). The inclusion of a trust in both the definition of a person and the definition of a company may lend the legislation to manipulability or structural complexity and aggressive tax planning (refer to Sections 2.3.2.2 and 2.3.7.3). Therefore, taxpayers may interpret similar transactions differently, as might the tax authority, depending on the definition applied to the transaction. This may lead to increased compliance complexity (refer to Sections 2.3.2.3 and 2.3.2.4), as both the taxpayer and the tax authority may need to incur costs to interpret or analyse the specific transaction and definition applicable. This complexity may create uncertainty in the interpretation of the legislation (refer to Section 2.3.4.4).

In the two remaining jurisdictions (Tanzania and Zimbabwe) a trust is either included in the definition of a person via another definition or the inclusion is conditional. In the Tanzanian ITA a trust is included in the definition of an 'entity' and an 'entity' is included in the definition of a 'person' (Tanzania ITA, Section 3) and in the Zimbabwean ITA the inclusion or exclusion of a trust in the definition of a person is dependent on the treatment of the income of the trust.

Considering the indirect inclusion in Tanzania, the definition of a person includes both an entity and a natural person. The definition of an entity also includes a corporation and a partnership. Specific rules applicable to a person and an entity are found throughout the Tanzanian ITA. As the Tanzanian ITA does not make provision for the attribution of income to a beneficiary, the effective inclusion of a trust in the definition of a person

suggests that a trust is taxed as a taxpayer in its own right with no amounts flowing through to a beneficiary. However, this may require taxpayers to familiarise themselves with all of the sections that refer to the term ‘entity’ and also to the term ‘person’, to identify those sections that are applicable to a trust. This inclusion of a trust in multiple definitions may cause compliance complexity (refer to Sections 2.3.2.4 and 2.3.3.4), as the taxpayer may require the services of a tax practitioner to assist with the tax calculation of the trust. The inclusion of a trust in the definition of a person through a further definition may indicate statutory complexity (refer to Sections 2.3.3.2 and 2.3.5.5). This complexity may have been averted by including the definition of a trust directly in the definition of a person.

In the Zimbabwean ITA the inclusion or exclusion of a trust in the definition of a person is conditional in the sense that it is dependent on the treatment of the income of the trust. When a trust generates “income that is subject of a trust to which no beneficiary is entitled”, then that trust is included in the definition of a “person”. This means that income attributable to a “beneficiary with a vested right” renders the trust outside the scope of the definition of a person (Zimbabwean ITA, Section 2). The implication of the above is that income retained in a trust (not vested in any beneficiary) falls within the definition of “income that is subject of a trust to which no beneficiary is entitled”. When income of a trust is included in this category, the trust is included in the definition of a person. This treatment of trust income to define the inclusion of a trust in the definition of a person requires a higher level of intellectual investment to interpret the legislation. This is an indicator of technical complexity (‘predictability’) (refer to Section 2.3.2.1). This definition of a person may create uncertainty in the interpretation of the legislation applicable to the taxation of a trust (refer to Section 2.3.4.4). Additionally, this definition of a person may indicate statutory complexity during the drafting process of the tax legislation (refer to Sections 2.3.3.2 and 2.3.5.5).

The only jurisdiction where a trust is not included in any taxpayer definition is Lesotho. The lack of a taxpayer definition that includes a trust may lead to compliance complexity, as the cost of compliance may increase due to the fact that the taxpayer may require the services of a tax practitioner or legal expert to assist with the calculation of the tax liability of the trust (refer to Sections 2.3.2.4 and 2.3.3.4). A tax practitioner or legal expert will

need to analyse the legislation to identify all sections in the legislation that are relevant in calculating the tax liability of the trust.

As discussed above, ten of the eleven jurisdictions (all jurisdictions, excluding Lesotho) included either a trust or a trustee in a taxpayer definition. Generally, this consistent treatment of a trust in SADC creates more certainty amongst taxpayers in the region. However, while there is some consistency (in comparison to other categories discussed in this study), the lack of a trust in a taxpayer definition (i.e. Lesotho) and the use of specific defined terminology in the definition of a taxpayer (i.e. Zimbabwe) both introduce aspects of complexity for different reasons. In light of this, it is submitted that neither of the two extremes are ideal and clarity in the legislation may reduce technical and compliance complexity (refer to Sections 2.3.2.1, 2.3.2.4 and 2.3.3.4).

4.2.4. Taxation in the trust

In three of the eleven jurisdictions (Botswana, Mauritius and Tanzania) no provision is made in the tax legislation for the taxation of the income of a trust in a person other than the trust. In other words, no attribution or vesting in a beneficiary in terms of the common law flow through principle is provided for in these jurisdictions. This treatment means that the income of the trust is taxed in the trust at the rate applicable to the trustee in his capacity as the trustee of the trust. In other words, the trust is treated as a separate entity for tax purposes and no deduction in relation to an amount vested in a beneficiary will be permissible. Two of the jurisdictions (Mauritius and Tanzania) apply the Trustee Taxation Model which may reduce the complexity related to manipulability and predictability, as all the income of the trust is taxed in one taxpayer and no attribution is made to beneficiaries or donors. The result is that the planning techniques associated with income splitting between different taxpayers may be curtailed. In addition, when the attribution rules do not apply, the 'understandability' of the legislation may be simplified. A discussion of the characteristics of these jurisdictions (Botswana, Mauritius and Tanzania) follows.

Botswana

Section 19(1) of the Botswana ITA determines that all income generated by a trust should be included in the gross income of that trust. The taxable income of the trust must be

charged to the trustee of the trust at the rate of the beneficiary who is entitled to the income. In other words, the trustee will be responsible for the payment of the tax, but the tax will be calculated at the rate applicable to the beneficiary, and no further tax is levied on amounts distributed from the trust to the beneficiaries. This treatment of trust income is classified by Hin (2010) as the Modified Imputation Model (refer to Section 2.5.1.3). In the Modified Imputation Model the tax is levied at the level of the trust. This differs from the flow through or Direct Beneficiary Taxation Model (refer to Section 2.5.1.4) where the income flows through the trust and is taxed at the beneficiary level. In other words the Direct Beneficiary Taxation Model taxes the beneficiary on income earned by the trust and vested in the beneficiary, whereas the Modified Imputation Model determines that the taxation should be paid by the trustee on the income earned by the trust based on the effective tax rate of the beneficiary. From a complexity perspective, uncertainty (Section 2.3.4.4) may be caused when the Modified Imputation Model is misinterpreted as the Direct Beneficiary Taxation Model (flow through model). This may be as a result of the fact that during the calculation of the tax payable by the trustee on the trust income that flows to the beneficiary, the income retains its nature (for example interest) and tax is calculated by taking this into consideration. In addition, the Modified Imputation Model may cause taxpayers to view the calculation and deduction of the taxation as a withholding tax, when it is in fact a final tax. This treatment of the income of a trust may cause compliance complexity (refer to Sections 2.3.2.4 and 2.3.3.4), as the trustee will be required to determine the amounts attributable to beneficiaries, as well as the tax rates of the beneficiaries, in order to calculate the tax payable by the trust. The trustees may furthermore require the services of a tax practitioner or legal expert to assist in the interpretation and calculation of the tax payable by the trust (including the tax payable on behalf of the beneficiaries).

Mauritius

In the Mauritian ITA, the income of a trust is also taxed in the trust (no provision for attribution to beneficiaries). However, all subsequent distributions made from the trust are classified as dividends in the hands of the beneficiary (Mauritius ITA, Section 46(4)). Although this treatment of the income of the trust may be perceived to be simple, the result is the application of a dividend tax to the distribution. This additional component (dividend tax) increases the scope of legislation applicable to the income, thereby increasing

technical complexity (refer to Section 2.3.2.1). Similarly, dividend tax requires an additional level of intellectual investment (application and interpretation) thereby increasing complexity. The application of dividend tax on the amounts distributed to the beneficiaries may also increase compliance complexity (refer to Sections 2.3.2.4 and 2.3.3.4), as the taxpayer may need the services of a tax practitioner or legal expert to assist with the calculation of the dividend tax applicable to the transaction.

Tanzania

In the Tanzanian ITA the income of a trust is taxed in the trust, and distributions made to beneficiaries by resident trusts are treated as exempt income in the hands of the beneficiary (Tanzania ITA, section 52(2)(a)). This treatment of the income and the wording in the legislation may be considered relatively simple and creates more certainty (than either its Botswanan or Mauritian counterparts) and thus less complexity for the taxpayer.

As discussed above, three of the jurisdictions (Botswana, Mauritius and Tanzania) tax all of the income of a trust in the trust. In general, the level of complexity related to this treatment of trust income seems to be simpler than legislation that provides for the attribution of income to beneficiaries. However, in contrast to Botswana, Mauritius and Tanzania, the Namibian ITA is silent on the attribution of the income of a trust to a beneficiary. When considered purely on the basis of the tax legislation, the inference may be drawn that Namibia does not provide for the attribution of trust income to beneficiaries. The treatment of such income is regulated by case law. The treatment of trust income in Namibia is discussed with the other seven jurisdictions that do provide for the attribution of income to beneficiaries in Section 4.2.5 below.

4.2.5. Beneficiary flow through

Eight of the eleven jurisdictions (Eswatini, Lesotho, Malawi, Namibia, Seychelles, South Africa, Zambia and Zimbabwe) make provision for the flow through or conduit pipe principle. The flow through principle determines that income earned in a trust may be attributed to a beneficiary (refer to Section 2.4.2.5). This means that income that is earned by a trust may either be taxed in the trust or in a beneficiary of the trust. When a beneficiary has a vested right to income or acquires a vested right through vesting by the

trustees of a trust, and the amount is distributed to the beneficiary, the beneficiary will be liable for the tax payable on the amount of income generated. This flow through principle may be directly included in the legislation (codified), or may stem from the application of case law relevant to the income of a trust, e.g. *Armstrong v CIR*, as applied in Namibia.

The flow through principle in taxation is a distinctive characteristic of trusts (refer to Section 2.4.2.5). It creates the opportunity to split income between taxpayers, whilst the income retains its nature. As an example, an amount of interest earned by a trust and attributed to a beneficiary will retain its nature and thus will still be classified as interest in the hands of the beneficiary. These distinctive characteristics of the trust may lead to different types of complexity.

The flow through principle provides the taxpayer with options when planning their tax affairs as the taxpayer may utilise the most tax effective option in the splitting of the income. In addition, the taxpayer may make use of exemptions or deductions that may decrease the effective tax rate for either the trust or beneficiary. These options that are created by the flow through principle may lead to complexity in the taxation of the income of a trust and its beneficiaries.

Not all jurisdictions make provision for the flow through principle in their legislation (refer to Section 4.2.4) and although this creates some complexity, it may be less complex than legislation with provision for attribution to beneficiaries or flow through of income. In addition to this, the inclusion of attribution rules may require the inclusion of anti-avoidance legislation (refer to Section 4.2.6).

The flow through principle may cause compliance complexity (refer to Sections 2.3.2.3 and 2.3.3.3), as the tax authority may need to provide for the attribution of income to beneficiaries in the returns of the trust and also include processes to verify compliance by the beneficiaries (should a trust vest amounts in beneficiaries). In consequence, the tax authority may also need to invest resources to engage the services of skilled employees to audit the accuracy and validity of these more complex returns. From the perspective of the taxpayer, the cost of compliance as a contributor to compliance complexity (refer to Sections 2.3.2.4 and 2.3.3.4), may necessitate the use of a tax practitioner or legal expert to interpret the tax legislation and to assist the taxpayer with the drafting of the financial

statements of the trust and the related assistance to ensure that the tax return is correctly completed. These complexities may result in significant additional costs to the taxpayer.

In the SADC countries providing for the flow through principle, certain of the jurisdictions include similar characteristics or features. For the purpose of this discussion the jurisdictions with similar characteristics will be discussed jointly based on these similarities. Three main groupings, namely 'codified in sections or subsections of the legislation', 'codified in definitions of the legislation' and 'case law application' will be used.

Codified in sections/subsections of the legislation

Five of the eight jurisdictions that make provision for the flow through principle (Eswatini, Lesotho, Seychelles, South Africa and Zambia) include a section or subsection in their legislation that provides for the attribution of income to a beneficiary of a trust. The sections in the legislation of these jurisdictions also regulate the treatment of the income that remains in the trust after the attribution to beneficiaries was made. An example of the codified attribution to a beneficiary from the Eswatini ITO is the following:

> "19*bis.* (1) Any income received by or accrued to or in favour of any person during the year of assessment in his capacity as a trustee of a trust, shall to the extent that such income has been derived for the immediate or future benefit of any ascertained beneficiary with a vested right to such income be included in the gross income of the beneficiary."

The intended tax consequences are clear in relation to the attribution of income to the beneficiary. Additionally, the Eswatini ITO includes the following subsection in relation to trust income:

> "[19*bis*] (6) The taxable income of a trust is so much of the income of the trust as is not included in the gross income of a beneficiary under subsection (1) or exempted under subsection (2)(a), less all deductions allowed in accordance with this Order for expenditure or losses incurred in deriving that income."

This subsection regulates the tax consequences of amounts not attributed to the beneficiaries but retained in the trust. In addition, it states that expenditure related to the

income may be deducted and that amounts attributed to beneficiaries may also be deducted prior to the taxation of the remainder of the income.

The subsections included in the above example illustrate the complexity that may be linked to the attribution or non-attribution of trust income. The attribution of income in the manner described above may be classified as a source of technical complexity (refer to Section 2.3.2.1), as the treatment of the income of the trust should be considered to determine which taxpayer will be responsible for the taxation of the income. In this regard a beneficiary may either have a vested right to income in terms of the trust deed or the trustees may vest income in the beneficiary. The determination (vesting in trust deed or at discretion of the trustees) falls outside the control of the tax legislation, but the legislation makes provision for either of these scenarios. In catering for both of these scenarios, it inherently leads to additional complexity as the tax authority will have to ascertain the nature of the distributions made to the beneficiaries. This type of complexity is known as compliance complexity (refer to Sections 2.3.2.3 and 2.3.3.3). Compliance complexity comprises of two distinct types of complexity, namely 'enforceability' and 'difficulty'. 'Enforceability' relates to the complexity involved for the revenue authority to enforce sections of the legislation. In this regard the tax authority may need to design processes and systems to ascertain the type of income that the taxpayer declares in their return. Should there be uncertainty in terms of the declared revenue of a trust or its beneficiary, the tax authority will have to invest in additional processes to ensure compliance by the taxpayers. 'Difficulty' (refer to Sections 2.3.2.4 and 2.3.3.4) as a source of complexity relates to the costs incurred by a taxpayer to ensure compliance with the relevant legislation. The services of a tax practitioner or a legal expert may also be required to comply with the trust tax legislation, as the taxpayer may not be familiar with the application of the sections applicable to the taxation of trusts. In addition, the taxpayer may need assistance with the calculation and declaration of the correct income and related taxation. The use of the attribution of income to beneficiaries may assist taxpayers with a preference for minimising their tax liability (refer to Section 2.3.7.1), as the attribution allows for the splitting of income between different taxpayers. This also allows for 'manipulability' (refer to Section 2.3.2.2) of the legislation.

As a consequence, the use of tax practitioners or legal experts may be an indicator of 'manipulability' or 'structural complexity' (refer to Section 2.3.2.2). Unclear legislation may

provide an opportunity for the tax practitioner or legal expert to interpret the legislation to the benefit of the taxpayer. Any uncertainty in the section on the taxation of trust income may similarly provide an opportunity to manipulate the legislation by the beneficiary or trust. This may be particularly relevant where the tax rates of beneficiaries and those of the trusts differ. In addition, the ability to split income between different taxpayers provides the opportunity to taxpayers to make use of lower tax rates when the tax is calculated based on incremental tax tables (progressive tax rates).

In addition to the above, the level of intellectual investment required in analysing this more complex legislation may be considered 'technical complexity' or 'predictability' (refer to Section 2.3.2.1). McCaffery (1990:1271) states that technical complexity is the ease of interpretation or 'understandability' of a section of the legislation, when considered on its own. The terminology and structure of the flow through section or subsection in the legislation may cause perceived complexity amongst taxpayers and may necessitate the use of a tax practitioner or legal expert to assist in the interpretation (refer to Sections 2.3.2.4 and 2.3.3.4).

The above discussion illustrates the extent of complexity that may be experienced when the flow through system of the treatment of the income of trusts are included in specific sections in the legislation. The complexity related to the inclusion of the flow through principle in definitions in the legislation is considered next.

Codified in definitions of the legislation

Two of the eight jurisdictions (Malawi and Zimbabwe) that provide for the flow through of trust income to a beneficiary include the provisions in the definitions of the legislation and not in separate sections. Definitions in the terminology section of the legislation provide for the attribution of income to a beneficiary as well as that related to the income remaining in the trust after attribution to the beneficiary was made.

An example of these definitions as codified in the Zimbabwean ITA is as follows:

> "'beneficiary with a vested right', in relation to income the subject of a trust created by a trust instrument, means a person named or identified in the trust instrument

who has at the time the income is derived an immediate certain right to the present or future enjoyment of the income."

"'income the subject of a trust to which no beneficiary is entitled' means income the subject of a trust created by a trust instrument which—

(*a*) is not paid to or applied to the benefit of—

(i) a beneficiary with a vested right; or

(ii) a person who would but for—

A. the conferment on the trustee by the trust instrument of a discretion so to pay or apply the income; and

B. the happening of some event stipulated in the trust instrument other than the exercise of that discretion;

be a beneficiary with a vested right; or

(*b*) is not income deemed by virtue of Section *Ten* to have been received or have accrued to or in favour of the person by whom the trust instrument was made; or

(*c*) is not accumulated in terms of the trust instrument for the future benefit of a beneficiary with a vested right."

The technical and design complexity related to these definitions are discussed in Section 4.2.3. The definitions pertaining to the treatment of the income of trusts are included in the definition or terminology sections of the legislation, but no formal section in the legislation deals with the treatment of the trust income. This lack of further statutory direction in the legislation may create complexity, as the taxpayer may require the services of a tax practitioner or legal expert for assistance. The inclusion of the flow through principle in the definition may therefore increase the cost of compliance to the taxpayer.

In addition to the increased cost of compliance to the taxpayer, the inclusion of the flow through principle for the treatment of trust income in these jurisdictions may increase the cost of the tax authority to enforce the legislation. An example of the increased cost to the tax authority may be the inclusion of a section in the tax return of trusts to assist the tax authority with the clarification of the declared amounts. Should the tax authority be unclear as to this treatment of the trust income by the taxpayer, the tax authority may have to

allocate additional resources to verify or audit the tax return of the trust. This source of complexity is classified as ‘enforceability’ or administrative cost of enforcement (refer to Sections 2.3.2.3 and 2.3.3.3).

Notwithstanding the above, additional structural complexity exists, as the uncertainty caused by the lack of statutory direction may leave these definitions vulnerable to manipulation or favourable interpretation by a taxpayer (refer to Sections 2.3.2.2 and 2.3.7.1). In other words, as a source of complexity this ‘manipulability’ may create an opportunity for a taxpayer to gain a tax benefit when the legislation creates the opportunity to do so.

The sections above discussed the complexity as a result of the codification of the flow through principle in the legislation. In the section that follows, the lack of codification in the legislation and the impact thereof on complexity is considered.

Case law application of the flow through principle

In the sections above the complexity related to the flow through principle in trusts (when the legislation makes provision for the flow through principle) was discussed. The remaining jurisdiction, Namibia, does not provide for the flow through principle in its legislation. However, the flow through principle may be applied to the income of trusts as a result of the application of case law.

In brief, upon the declaration of independence from South Africa, Namibia adopted a constitution that effectively retained the South African common law principles, as well as legislation applicable to Namibia at the time (provided it did not contradict the new Namibian Constitution) (du Plessis, 2018:282). Effectively this means that the South African common law trust principle, being the flow through principle, still finds application in Namibia. Therefore, income earned by the trust will flow through the trust and will be taxed in the hands of the beneficiary, provided that the income is attributed to the beneficiaries in the same year of assessment as it was earned. This principle was confirmed in *Armstrong v CIR* and *SIR v Rosen* (*Honiball & Olivier, 2009:72*).

After the independence of Namibia, the new Namibian ITA was introduced, but it did not include a section or a definition that dealt with the taxation of trusts. Since 1981 the tax authority has not introduced any code amendments that deal with the taxation of the income of trusts. The effect is that Namibia treats the income of trusts based on the applications that were effective during the period when Namibia was a province of South Africa. Even though South Africa has subsequently codified the attribution rules in the legislation, the case law applied is still relevant to the treatment of trust income in Namibia. This application of South African case law to Namibian taxpayers creates a different type of complexity. Policy makers in Namibia decided not to introduce sections or definitions into the tax legislation. The reasons for this are unknown, but the result is that this creates policy complexity (refer to Section 2.3.5.5). Policy complexity is the complexity caused by decisions taken by policy makers (refer to Section 2.3.5).

The result of the decision not to codify the attribution of income is that there may be uncertainty amongst taxpayers (it may be unclear to a taxpayer that reads the legislation how the income of trust should be treated). As a source of complexity, this lack of statutory direction may cause difficulty (increased cost of compliance), as the taxpayer may require the assistance of a legal expert that is knowledgeable on South African case law to assist in the interpretation and application of the case law on the trust income in Namibia (refer to Sections 2.3.2.4 and 2.3.3.4). From the perspective of the tax authority this lack of statutory guidance may cause administrative complexity (refer to Sections 2.3.2.3 and 2.3.3.3), as the tax authority may need to employ or engage legal experts to ensure that the submissions and declarations of the taxpayer comply with the relevant case law. This complexity increases the cost of enforcement to the tax authority; and should the tax authority not agree with the interpretation of the taxpayer, it may lead to litigation and additional enforcement costs.

In summary this section considered the impact of the flow through principle on complexity in the taxation of trusts. It was found that, irrespective of the way that the flow through principle was applied in the taxation of trust income, complexity was experienced when the flow through principle was applied.

4.2.6. Anti-avoidance

The previous section considered the tax complexity involved in the flow through nature of the income of a trust. In this section the anti-avoidance legislation necessitated by the flow though is considered.

The flow through principle creates the opportunity for taxpayers to decide which taxpayer, the trust or the beneficiary, will be liable for the taxation of the income of the trust, as the trustees may vest income in a beneficiary or retain the amount of income in the trust. This creates the opportunity for the taxpayer to split income and reduce the effective amount of tax payable on the income. This splitting of income may be expected in jurisdictions where the income is taxed on a progressive table of taxation. This phenomenon has compelled tax authorities to introduce anti-avoidance legislation to curb the misuse or abuse of the flow through principle.

The anti-avoidance legislation is predominantly focused on ensuring that the tax authority does not suffer any prejudice when the income of a trust is attributed to a beneficiary (Kujinga, 2014:429-430). The legislative rules encountered in the majority of the jurisdictions are classified into three categories, namely attribution to a donor, limitation of losses and other anti-avoidance rules.

Attribution to the donor

In eight of the eleven jurisdictions (Botswana, Eswatini, Lesotho, Malawi, Seychelles, South Africa, Zambia and Zimbabwe) provision is made for the attribution of the income of a trust to a donor. For the purpose of this study, the donor referred to may either be the founder or settlor of a trust, or may be a person that donates property of any nature to a trust. Note that the definition of a donation may vary from jurisdiction to jurisdiction and may include fixed, movable, corporeal or incorporeal property, dependent on the interpretation in the relevant jurisdiction. While this category of anti-avoidance legislation differs between the jurisdictions, a number of main themes emerge. Firstly, the focus of this anti-avoidance legislation is to ensure that the person who is responsible for the donation to the trust does not create a tax benefit or tax advantage for himself, his family or close associates. As the flow through nature of trusts provides the donor with the opportunity to split income between the trust and the beneficiaries, the policy makers

introduced the anti-avoidance legislation to deter these donors from splitting income to gain a tax advantage (refer to Section 2.3.7.1). An example of an anti-avoidance inclusion in the legislation is Section 19 in the Zambian ITA, as follows:

> "(1) Where under the terms of any settlement and during the life of the settlor any income, or assets representing it, will or may become payable or applicable to or from the benefit of any child of the settlor and at the commencement of the charge year the child is unmarried and has not attained the age of 21 years, the income or assets representing it shall be deemed to be income of the settlor and not income of any other person."

This subsection determines that should an unmarried child, under the age of 21, "earn" an amount of income as a result of a donation (settlement) made by a donor (parent), then the donor will be taxed on the income and not the child. From a practical perspective, the child may receive the income but the donor will pay the tax thereon at the tax rate applicable to the donor. The reason for this rule is that the child may be in a lower tax category, whilst the donor (parent) may be in a higher tax category. Should the child then be taxed, the "family" will benefit from a tax perspective, as the nett tax payable will be lower.

The tax authorities in the mentioned jurisdictions have identified different anti-avoidance rules based on the efforts of taxpayers to avoid the payment of taxes. These anti-avoidance measures may be included in the legislation to protect the revenue of the tax authority (refer to Section 2.3.5.1). The Zambian example above relates to the attribution to the donor-parent of income earned by a minor child. The provisions in the eight jurisdictions where the 'attribution to a donor' rules apply are where:

- As a result of a donation, a spouse earns an amount of income (Lesotho, South Africa, Zambia);
- As a result of a donation, a minor child earns an amount of income (Lesotho, Malawi, South Africa, Zambia, Zimbabwe);
- A donor retains the right to revoke income to be earned by a beneficiary of a trust (Botswana, Malawi, South Africa, Zambia, Zimbabwe);

- A donor cedes income or an income generating asset to a trust (South Africa);
- A non-resident beneficiary earns income from a trust as a result of a donation (South Africa);
- The enjoyment of a benefit (income) is postponed based on the happening of a future event (Botswana, Malawi, South Africa and Zimbabwe).

In all of the scenarios mentioned above, the donor will be taxed on the income. It should also be noted that while there are differences in the detail contained in the legislation of these jurisdictions, the above scenarios are a generalisation of the provisions.

The anti-avoidance legislation discussed above creates substantial complexity for the taxpayer and revenue authority. The revenue authority may require the services of expensive legal experts during the original drafting process of the legislation. This type of complexity is defined as technical complexity (refer to Section 2.3.2.1). In addition to this, structural complexity is also evident, as the additional sections in the legislation may provide the opportunity for multiple interpretations of the same sections in the legislation by different taxpayers (refer to Section 2.3.2.2).

Notwithstanding the above, as discussed in Section 4.2.5, the introduction of the anti-avoidance legislation as a result of the flow through principle may cause compliance complexity to the revenue authority and the taxpayer:

- The revenue authority (refer to Section 2.3.2.3 and 2.3.3.3): there may be a need to engage experts to assist in the auditing and verification of information supplied by the taxpayers. These experts may need to analyse the financial statements of the trusts and may need to engage the taxpayers to ascertain the relationship between the different parties. In addition, these experts will need to understand and interpret the trust instruments of the trusts to compare the interpretation by taxpayers with those interpreted by the revenue authority.

- For the taxpayer (refer to Sections 2.3.2.4 and 2.3.3.4): compliance complexity is caused as the taxpayer may also need to engage legal experts during the drafting process of the trust instrument, as well as when decisions regarding donations, settlements or other dispositions in favour of the trust are made. These experts may

need to be engaged on an annual basis prior to the drafting of the financial statements, to explain the implications of decisions taken by the trustees. The taxpayer will also require a tax practitioner or legal expert to assist with the preparation and submission of the annual tax returns. Finally, should the revenue authority require clarification on tax matters of the trust, the trustees may have to engage these experts to assist with these queries. This may lead to substantial costs of compliance to the taxpayer.

Limitation of losses

Two of the eleven jurisdictions (Lesotho and South Africa) include a limitation of losses clause that is linked to the distribution of income to a beneficiary. An example of such a subsection is included in Section 80(3) of the Lesotho ITA:

> "(3) No beneficiary is allowed a deduction for a trust loss."

This subsection is included in the legislation to ensure that a trust may not distribute any losses to a beneficiary. Effectively this limits the amount of expenditure that may be off-set against the income that is attributed to a beneficiary. The minimum amount that may thus be distributed is the amount of income distributed less an equal amount of expenditure. For example: where the trustees vest a gross amount of $100 in a beneficiary and there is expenditure related to that income, the trust may only distribute expenses to the value of $100 (even if the trust incurred expenses of $120).

The limitation of losses subsection in the legislation may be considered compliance complexity (refer to Sections 2.3.2.4 and 2.3.3.4), as the taxpayer may have to engage the services of a tax practitioner or legal expert to assist in the calculation of the actual income of the trust to ensure that the limit is not contravened. Additionally, the experts may have to assist the taxpayer in the calculation of amounts to be vested in the beneficiaries, bearing in mind that the expenditure that follows the income may not exceed that income.

From the perspective of the revenue authority, additional costs may be incurred to ensure effective enforcement when considering the returns submitted by the trust. In this regard, the revenue authority my need to engage specialists to train and upskill the auditors and

verifiers in the compliance sections, and it may be necessary to employ legal experts to assist these employees. Additionally, the electronic processes within the revenue authority may need to be enhanced to ensure that the submissions made by taxpayers are automatically checked so that that income vested in and declared by a beneficiary meets the limitation of losses requirement. This type of complexity is known as administrative complexity or 'enforceability' (refer to Sections 2.3.2.3 and 2.3.3.3).

The tax legislation of Eswatini, Malawi, Namibia, Seychelles, Zambia and Zimbabwe is silent regarding the limitation of losses. This lack of guidance in the legislation (for the situation where expenditure exceeds the income) may cause uncertainty (refer to Section 2.3.4.4), and also lead to statutory complexity (refer to Section 2.3.3.2). This may furthermore cause compliance complexity as the taxpayer may need to engage the services of a tax practitioner or legal expert to assist with the tax treatment of the income and expenditure.

Other anti-avoidance provisions

The South African Government introduced section 7C as an anti-avoidance provision to discourage loans from connected persons to a trust where no revenue (interest) is generated on these capital amounts loaned to a trust (Stiglingh, Koekemoer, van Heerden,Wilcocks,de Swardt & van der Zwan, 2018: 910). In the South African ITA, a connected person to a trust is a beneficiary by definition, but may include certain trustees and founders or donors. This section determines that the amount of interest "lost" as a result of a 'low interest' or 'no interest' loan to a trust by a connected person should be calculated and deemed to be a donation with donations tax implications.

The inclusion of section 7C of the South African ITA may include an element of technical complexity. Technical complexity indicates the 'understandability' of a section included in the legislation, when that section is considered on its own (refer to Section 2.3.2.1). This specific section in the South African ITA includes various definitions and exclusions that need to be considered in the application thereof. Additionally, this section is included under the "normal tax" part of the South African ITA and not under the "donations tax" part, while no income tax is levied and the taxation levied is that of donations tax. Both of these concerns raised may cause uncertainty for a taxpayer (refer to Section 2.3.4.4). In addition

to the technical complexity, this section may also be considered to contain compliance complexity (refer to Sections 2.3.2.4 and 2.3.3.4), as the taxpayer may require the assistance of a tax practitioner or a legal expert to analyse and interpret the legislation to ascertain the applicability thereof. The taxpayer may also require the services of experts to ensure compliance with the section.

This section considered the six recurring themes in the context of complexity related to the taxation of trusts. It was found that all of the jurisdictions provided for the taxation of trusts in their legislation, but with varying terminology and treatment styles. It was notable that greater complexity was experienced in jurisdictions that make provision for the flow through of income from a trust to beneficiaries. In addition, anti-avoidance measures were introduced in the legislation of the jurisdictions that provide for the flow through principle in trusts. In the following section the different models of taxation in the jurisdictions are discussed as they relate to trusts.

4.3. INTO WHAT MODEL OF TAXATION DO THE SADC JURISDICTIONS FALL?

During the analysis of the legislation, the characteristics of the jurisdictions were assessed and these were used as a basis for the inclusion in the Hin Models of Taxation (refer to Section 2.5). The results are presented in Table 4 below.

Table 4: Models of the taxation of trusts applied to SADC jurisdictions

Jurisdiction	Trustee Taxation Model	Imputation Model	Modified Imputation Model	Direct Beneficiary Taxation Model	Indirect Beneficiary Taxation Model	Hybrid Model
Botswana			✓ S 19(1)			
Eswatini	✓ S 9*bis*(5)			✓ S 19*bis*(1); S 19*bis*(3)		✓*
Lesotho	✓ S 81(1)			✓ S 81(1) S 82(1)		✓*
Malawi	✓ S 2			✓ S 2		✓*
Mauritius	✓ S 46(1)					
Namibia	✓ Case law			✓ Case law		✓*
Seychelles	✓ S 40(1)			✓ S 40(1)		✓*
South Africa	✓ S 25B			✓ S 25B		✓*
Tanzania	✓ S 52					
Zambia	✓ S 27(4) S 60(3)			✓ S 27(4)		✓*
Zimbabwe	✓ S 2			✓ S 2		✓*

Key:

✓ - Model applied in the jurisdiction

* - The hybrid model includes more than one model (as indicated in the table) and refers to more than one section in the legislation (as indicated).

The taxation models identified by Hin (2010:48) consider five basic taxation models for the income of trusts. The Hin models consider the entity that is taxed (e.g. trust or beneficiary) and where the tax is levied and/or if the tax is retained and a tax credit provided to the beneficiary. These models are discussed in detail in Chapter 2 (refer to Section 2.5). The three jurisdictions discussed in Section 4.2.4 (Botswana, Mauritius and Tanzania) that do not provide for the attribution to beneficiaries and where the taxation is levied in the trust, all fall within the Trustee Taxation Model. This model provides for the taxation of the trust in the hands of the trustee (as the representative taxpayer of the trust).

The eight jurisdictions that provide for the attribution of income to a beneficiary (Eswatini, Lesotho, Malawi, Namibia, Seychelles, South Africa, Zambia and Zimbabwe) are all included in two of the models, namely the Trustee Taxation Model and the Direct Beneficiary Taxation Model. In analysing the Direct Beneficiary Taxation Model, the characteristics mentioned include the taxation of the income attributable to the beneficiary in the beneficiary’s hands. The taxation of the remainder of the trust income (that is retained in the trust) will be taxed in the hands of the trustee using either the Trustee Taxation Model or the Imputation Model. All eight of the jurisdictions apply the Trustee Taxation Model. From a purely theoretical perspective, these eight jurisdictions may be classified as Hybrid Models as described by Hin (2010:48), as more than one of the models identified by Hin are used in these eight jurisdictions. For the purpose of Table 4 the models that comprise the Hybrid Model are also indicated.

In light of the complexities identified in Sections 4.2.2, 4.2.3, 4.2.4, 4.2.5 and 4.2.6, the Trustee Taxation Model, the Imputation Model and the Modified Imputation Model are comparatively simpler than the Direct Beneficiary Taxation Model, the Indirect Beneficiary Taxation Model or Hybrid Models. This is due to the fact that the Trustee Taxation Model, the Imputation Model and the Modified Imputation Model do not provide for the attribution of income to a beneficiary, but do provide for the taxation of trust income in the hands of the trustee of the trust. It is therefore submitted that the model applied in a jurisdiction may inherently determine much of the complexity within the legislation.

4.4. DISCUSSION AND CONCLUSION

The aim of the study was to compare the trust tax legislation in the selected SADC countries to identify complexities of the trust tax legislation. Based on the results in Table 3 it was identified that nearly all of the jurisdictions included the definition of a trust in their legislation and also included a trust in a taxpayer definition (e.g. ‘person’).

The data analysed in Table 3 indicated that three of the jurisdictions (Lesotho, Mauritius and Tanzania) did not make use of the common law or legislative flow through (or conduit pipe) attribution of income to beneficiaries. It was notable that these sections were relatively more simple to read and, as indicated in Table 3, included limited or no anti-avoidance measures applicable to the taxation of trusts.

The remaining eight jurisdictions made provision for the flow through or conduit pipe principle in their tax legislation. Although the application and wording vary substantially from one jurisdiction to the other, the concept of the flow through system determines that either the beneficiary or the trust will be taxed on the income earned by the trust. When considering how the different tax jurisdictions construct the wording of the sections dealing with the flow through principle, it was clear that no uniform construction method was used in the design of the legislation. In considering the results from Table 3 it was also evident that jurisdictions that include the flow through principle in their tax legislation include anti-avoidance legislation. This seems to indicate that jurisdictions that include the flow through principle require a larger number of anti-avoidance measures in their legislation. In analysing the anti-avoidance sections included in the legislation, the focus of the legislation is predominantly on neutralising the effect of splitting of income. This indicates that the use of a trust, when allowing for the flow through principle to a beneficiary, facilitates the splitting of income, specifically between relatives and associates.

Table 5 presents a summary of the complexities (as described in Section 2.3) that were identified during the analysis of the various categories extracted from the legislation. This table is essentially a summary of the complexities identified in this chapter from Section 4.2.2 to Section 4.2.6 and summarises the various types of complexity experienced in the

different jurisdictions per identified category. This provides a birds-eye view of the complexity identified in the legislation of the selected SADC jurisdictions.

Table 5: Summary of complexities in trust legislation in SADC

Specific complexity	Trust definition (4.2.2)	Taxpayer definition (4.2.3)	Taxation in the trust (4.2.4)	Beneficiary flow through (4.2.5)	Anti-avoidance (donor attribution) (4.2.6)	Anti-avoidance (limitation of losses) (4.2.6)	Anti-avoidance (other) (4.2.6)
Technical complexity/ Predictability (2.3.2.1)	Botswana, Eswatini, Lesotho, Malawi, Namibia, Zambia, Zimbabwe	Lesotho, Mauritius, Zimbabwe	Mauritius	Eswatini, Lesotho, Malawi, Seychelles, South Africa, Zambia, Zimbabwe	Botswana, Eswatini, Lesotho, Malawi, Seychelles, South Africa, Zambia, Zimbabwe		South Africa (Section 7C)
Structural complexity/ Manipulability (2.3.2.2)	Eswatini, Malawi, Namibia, Zimbabwe	Mauritius		Eswatini, Lesotho, Malawi, Seychelles, South Africa, Zambia, Zimbabwe	Botswana, Eswatini, Lesotho, Malawi, Seychelles, South Africa, Zambia, Zimbabwe		

Specific complexity	Trust definition (4.2.2)	Taxpayer definition (4.2.3)	Taxation in the trust (4.2.4)	Beneficiary flow through (4.2.5)	Anti-avoidance (donor attribution) (4.2.6)	Anti-avoidance (limitation of losses) (4.2.6)	Anti-avoidance (other) (4.2.6)
Compliance complexity: Enforceability (2.3.2.3) or Administrative complexity (2.3.3.3)				Eswatini, Lesotho, Malawi, Namibia, Seychelles, South Africa, Zambia, Zimbabwe	Botswana, Eswatini, Lesotho, Malawi, Seychelles, South Africa, Zambia, Zimbabwe	Lesotho, South Africa	
Compliance complexity: Difficulty (2.3.2.4) or Cost of compliance (2.3.3.4)	Botswana, Eswatini, Lesotho, Malawi, Mauritius, Namibia, Seychelles, South Africa	Lesotho, Mauritius, Tanzania	Botswana, Mauritius	Eswatini, Lesotho, Malawi, Namibia, Seychelles, South Africa, Zambia, Zimbabwe	Botswana, Eswatini, Lesotho, Malawi, Seychelles, South Africa, Zambia, Zimbabwe	Lesotho, South Africa	South Africa (Section 7C)

Specific complexity	**Trust definition (4.2.2)**	**Taxpayer definition (4.2.3)**	**Taxation in the trust (4.2.4)**	**Beneficiary flow through (4.2.5)**	**Anti-avoidance (donor attribution) (4.2.6)**	**Anti-avoidance (limitation of losses) (4.2.6)**	**Anti-avoidance (other) (4.2.6)**
Statutory complexity (2.3.3.2) or Drafting complexity (2.3.5.5)	Botswana, Zambia	Tanzania, Zimbabwe	Botswana	Eswatini, Lesotho, Malawi, Namibia, Seychelles, South Africa, Zambia, Zimbabwe		Eswatini, Malawi, Namibia, Seychelles, Zambia, Zimbabwe	
Certainty (2.3.4.4)	Eswatini, Malawi, Namibia	Mauritius, Zimbabwe	Botswana			Eswatini, Malawi, Namibia, Seychelles, Zambia, Zimbabwe	South Africa (Section 7C)
Judicial traditions (2.3.5.7)	Zimbabwe						

Specific complexity	Trust definition (4.2.2)	Taxpayer definition (4.2.3)	Taxation in the trust (4.2.4)	Beneficiary flow through (4.2.5)	Anti-avoidance (donor attribution) (4.2.6)	Anti-avoidance (limitation of losses) (4.2.6)	Anti-avoidance (other) (4.2.6)
Aggressive tax planning (2.3.7.3)		Mauritius					
Taxpayer preference for minimization of tax liability (2.3.7.1)				Eswatini, Lesotho, Malawi, Seychelles, South Africa, Zambia, Zimbabwe	Botswana, Eswatini, Lesotho, Malawi, Seychelles, Zambia, Zimbabwe		
Protecting tax revenue (2.3.5.1)					Botswana, Eswatini, Lesotho, Malawi, Seychelles, Zambia, Zimbabwe		

In analysing the legislation of the selected SADC jurisdictions it was found that all of the eleven jurisdictions made provision for trusts in their tax legislation. This inclusion of trusts in tax legislation may indicate that attempts have been made to provide certainty to taxpayers regarding the taxation of these entities.

Six of the eleven jurisdictions included a **definition of a trust** in the tax legislation. The inclusion of a definition of a trust may not specifically have simplified the taxation of trusts, but may indicate the intention of the revenue authority to tax trusts. A summary of specific aspects that may have added to the complexity of the definition of a trust in the SADC jurisdictions is included below:

- The differences in the definitions of a trust in the different jurisdictions result in varying interpretations of the trust tax terminology across the SADC region. In this regard the use of specific wording or terminology may create complexity and reduce the 'understandability' of the legislation. For example, in Botswana and South Africa the references to "deed of donation, settlement or other disposition" may create additional complexity, as the terminology may require specific interpretation to assess the practical application thereof in each jurisdiction.

- Drafting complexity may be created in certain jurisdictions (i.e. Botswana) where the trust definition is included in Section 19 of the legislation, whereas the other jurisdictions include the definition of a trust in the terminology section. Similarly, in the Zambian ITA, a trust is included in the definition of a settlement that is discussed under Section 19 of the Zambia ITA. This inclusion of a trust in a settlement may cause statutory complexity.

- In certain jurisdictions (i.e. the Mauritian ITA and the Seychelles BTA), the legislation refers the taxpayer to consult the definition of a trust, as is defined in other legislation of the country. In other words, this requires of the taxpayer to consult legislation outside of the tax legislation, to interpret the trust definition and this may lead to additional technical complexity.

- Terminology used in the definition of a trust may create technical complexity from a grammatical perspective (i.e. Zimbabwean ITA). This is as the wording of the definitions is in itself complex and may be difficult to interpret by taxpayers.

- In the jurisdictions where no provision was made for the definition of a trust it is submitted that there may be an increased level of uncertainty in the interpretation of the trust tax legislation that may require expert knowledge and an increased reliance on tax practitioners. In addition, the lack of characteristics provided in the Lesotho ITA creates uncertainty to a taxpayer that may lead to further complexity.

Nevertheless, the inclusion of a trust or a trustee in a **taxpayer definition** in the majority (ten of the eleven) of the selected SADC jurisdictions creates greater certainty amongst taxpayers in the region. A summary of specific aspects that may have added to the complexity of the definition of a taxpayer in the SADC jurisdictions is included below:

- The inclusion of a trust in more than one location (i.e. the definition of a person as well as in the definition of a company, as is found in the Mauritian ITA), may create complexity as this provides the opportunity for taxpayers to structure their affairs for their own tax benefit. In addition, this may result in compliance complexity, as the taxpayer may require the services of a competent tax practitioner to provide clarity on the interpretation applicable to their situation.

- The lack of the inclusion of a trust in a taxpayer definition (as is the case in the Lesotho ITA) may create uncertainty and therefore introduce a form of technical complexity. However, the other extreme, where the legislation makes provision for a specifically defined inclusion or exclusion (as is evident in the Zimbabwean ITA), also creates technical complexity as the taxpayer will need to engage a tax practitioner or legal expert to clarify these specific definitions. It is submitted that neither of these two extremes is ideal.

In conclusion, clarity in terms of defining a trust or a trustee in a taxpayer definition may reduce both technical and compliance complexity and create greater certainty amongst taxpayers. This may then decrease the cost of compliance for the taxpayer.

The flow through principle is one of the distinctive characteristics of a trust (refer to Section 2.4.2.7). However, four of the jurisdictions (Botswana, Mauritius, Namibia and Tanzania) **do not provide for the attribution of income** (flow through) to beneficiaries in their tax legislation. Hence, all the income of a trust in these jurisdictions is taxed in the trust. However, note that although the Namibian ITA is silent on the attribution of the income of a trust to a beneficiary, the treatment of such income in Namibia is regulated by case law (and not by legislation) and therefore the flow through principle is applied in Namibia, similar to the other seven jurisdictions that do provide for the attribution of income to beneficiaries. In general, the level of complexity related to the attribution of income to a beneficiary is more complex than that of jurisdictions where the income of a trust is taxed in the trust (no flow through of income). A summary of specific aspects that may have added to the complexity where no provision is made for the flow through of income to a beneficiary in the SADC jurisdictions is included below:

- Additional complexity may be created where the distribution of amounts already taxed in the trust is subject to further taxation in the hands of the beneficiary. For example, the Mauritian ITA imposes dividends tax on amounts attributed to a beneficiary by a trust. This may result in technical complexity as the taxpayers may need to familiarise themselves with the implications of dividends tax.

- This further tax may also result in compliance complexity, as the taxpayer may have to engage the services of a legal expert or tax practitioner to assist with compliance.

- The flow through principle in taxation creates the opportunity to split income between taxpayers, whilst the income retains its nature. The flow through principle provides the taxpayer with options when planning their tax affairs, as the taxpayer may utilise the most tax effective option in the splitting of the income. In addition, the taxpayer may make use of exemptions or deductions that may decrease the effective tax rate for either the trust or beneficiary. These options that are created by the flow through principle may lead to complexity in the taxation of the income of a trust and its beneficiaries.

- Technical complexity may be caused by the inclusion of specific definitions and terminology related to the attribution of trust income to beneficiaries, but where no

specific section is included in the legislation that guides the treatment of trust income. An example is found in the Zimbabwean ITA where different trust definitions are included in the terminology section, but no section dealing with the treatment of trust income is included in the legislation.

As is evident from Table 5, the application of the **flow through principle** (attribution to beneficiaries) leads to four main types of complexity, namely enforceability, difficulty (both may be categorised as types of compliance complexity), technical complexity and structural complexity (or manipulability). A summary of specific aspects that may have added to the complexity of the flow through principle and attribution rules in the SADC jurisdictions is included below:

- The flow through principle may cause compliance complexity, as the tax authority may need to include processes to verify compliance by the trust as well as beneficiaries. Similarly, the tax authority may also need to invest financial resources to engage the services of skilled employees to audit the accuracy and validity of these more complex returns.

- From the taxpayer perspective, 'difficulty' as a source of complexity relates to the costs incurred by a taxpayer to ensure compliance with the relevant legislation. This is as the taxpayer may need to engage the services of a tax practitioner or a legal expert to comply with the trust tax legislation. In addition, the taxpayer may need assistance with the calculation and declaration of the correct income and the taxation thereon.

- The application of case law, as is applied in Namibia, leads to an additional type of complexity not present in the codified legislation, namely policy complexity.

- The level of intellectual investment required to analyse the more complex tax legislation (flow through and attribution to beneficiaries) may be described as technical complexity. The terminology and structure of the legislation may cause perceived complexity amongst taxpayers and may necessitate the use of a tax practitioner or legal expert to assist in the interpretation of these sections. The use of tax practitioners or legal experts may further be an indicator of 'structural complexity'.

- Ambiguous legislation may provide an opportunity for the tax practitioner or legal expert to unduly interpret the legislation to the benefit of the taxpayer. Any uncertainty in the section on the taxation of trust income may similarly provide an opportunity to manipulate the legislation. This may be particularly relevant where the tax rates of beneficiaries and those of the trusts differ.

The risk of manipulation of the legislation (particularly where tax rates differ) necessitated tax authorities to introduce anti-avoidance legislation to curb the misuse or abuse of the flow through principle to reduce the amount of tax payable on an amount of income. Anti-avoidance measures used by tax authorities to curb this exploitation of the flow through principle include the attribution of income to a donor (subject to certain conditions) where it is clear that the donor merely utilised the trust to gain a tax benefit.

The **anti-avoidance legislation** creates substantial complexity and the taxpayer and the revenue authority may require the services of expensive legal experts. In addition to the technical complexity, structural complexity also becomes evident as the additional sections in the legislation may provide the opportunity for multiple interpretations of the same sections in the legislation by different taxpayers. Notwithstanding the above, the introduction of the anti-avoidance legislation as a result of the flow through principle may also be a source of compliance complexity to the revenue authority and the taxpayer. A summary of specific aspects that may have added to the complexity of the anti-avoidance legislation in the SADC jurisdictions is included below:

- Those jurisdictions (Lesotho and South Africa) that provide for the attribution of income also include a limitation of losses clause that is linked to the distribution of income to a beneficiary. This subsection is included in the legislation to effectively limit the amount of expenditure that may be off-set against the income that is attributed to a beneficiary. The limitation of losses subsection in the legislation may be considered compliance complexity, as the taxpayer may have to engage the services of a tax practitioner or legal expert to assist in the calculation of the actual income of the trust to ensure that the limit is not contravened.
- Additionally, the experts may have to assist the taxpayer in the calculation of the distributions made to the beneficiaries, bearing in mind that the expenditure that follows the income may not exceed that income.

- Where the legislation is silent regarding the limitation of losses (i.e. Eswatini, Malawi, Namibia, Seychelles, Zambia and Zimbabwe), it may cause design complexity. This may once again cause compliance complexity, as the taxpayer may need to engage the services of a tax practitioner or legal expert to assist with the tax treatment of the income and expenditure.

It may be summarised that anti-avoidance measures were included in the legislation of the eight jurisdictions that provide for the flow through principle in trusts. The three jurisdictions that do not make provision for the flow through principle in their legislation and where the income of the trust is taxed in the trust do not require any anti-avoidance legislation. This indicates that the inclusion of the flow through principle in trust tax legislation creates additional complexity in the legislation.

This chapter provided a presentation and analysis of the data collected to inform the research objective of the study. The chapter concluded with a discussion and conclusion based on the analysed data. The next chapter will provide an overview of the study with a focus on the research objective and the conclusions drawn.

CHAPTER 5: CONCLUSION

5.1. INTRODUCTION

The purpose of this final chapter is to conclude on the study by providing a summarised overview and conclusion based on the research results, explaining the limitations of the study and making recommendations for future research. The aim of the research was to compare the tax legislation of selected SADC countries to identify and explore complexities related to trusts included in the tax legislation. As part of this study the phenomenon of tax complexity and the negative impact that this has on the principles of a good tax system have been researched. In the context of this study, the trust, as an entity that has developed over the last millennium, evolved into a complex structure. One unique characteristic resulting from the use of trusts is the flow through principle that has added to the complexity associated with the taxation of trusts.

In an effort to add to the body of knowledge of the taxation of trusts, this research was undertaken to compare the trust tax legislation in the selected SADC countries with the aim of adding value in the tax complexity debate. It is anticipated that the results of this study may inform the legislature in the SADC region on the complexity in the trust tax legislation, with the aim to contribute towards the simplification of the trust tax legislation in future. The research may also inspire future research into the subject that may contribute to the body of knowledge in both of these focus areas, namely tax complexity and taxation of trusts.

The research objectives pursued in addressing the goal of the research are:

1. to analyse and describe the characteristics of the constructs of tax complexity and trusts, and
2. to analyse and compare the complex characteristics in the trust tax legislation of the selected SADC jurisdictions.

In the next section a summary and conclusion based on the findings is provided.

5.2. SUMMARY OF FINDINGS AND CONCLUSIONS

Chapter 1 provided an introduction and a background to taxation and complexity in tax systems. It considered the principles of effective tax systems based on the original theories of Adam Smith and how this may impact on compliance. The rationale of the study included a discussion of the various initiatives by the South African Government aimed at finding solutions to the complexity within the tax system in South Africa.

Chapter 2 was presented in the form of a literature review. Firstly, it commenced with the history of taxation and how its purpose changed and it developed into complex modern tax systems. Secondly, tax complexity was analysed to establish the impact of tax complexity on the modern tax system. In this regard, the indicators and properties of tax complexity were analysed and summarised with the goal to examine its occurrence in and impact on the legislation of the selected SADC jurisdictions. The properties considered were 'predictability' (technical complexity), 'manipulability' (structural complexity), 'enforceability' (administrative complexity) and 'difficulty" (cost of compliance). In addition, a discussion on the consequences of tax complexity and its impact on a good tax system were provided. Thirdly, the concept of a trust and its compelling evolution over the last millennium was presented with a focus on the characteristics that render it complex in nature. In addition, the Hin Models of Taxation that are based on the general principles of the taxation of trusts were presented. Finally, the introduction of the trust into Africa as a result of the legal influences following colonisation was discussed.

Chapter 3 elaborated on the research design and methodology used to reach the research objectives of this study. The doctrinal or "black letter law" methodology was applied through the analysis of legal rules. This methodology was selected to critically analyse documentary data to compare and reach conclusions that inform the research objectives. A qualitative research approach was adopted, as it is based on documentary data that does not involve statistical analysis (McKerchar, 2008:18-19). The study was exploratory in nature with an inductive reasoning approach. This approach was followed to critically analyse the documentary data to identify similarities and to reach conclusions based on the extracted data. The extracted data from the tax legislation of the SADC jurisdictions was presented in Table 3 and forms the basis for the conclusion of the study.

The purpose of Chapter 4 was to analyse the data and present the results within the context of a comparative discussion. It provided an orientation of the data analysis technique and a presentation and discussion of the results. A summary of the complexities that were identified during the analysis of the various categories extracted from the legislation of the selected SADC jurisdictions was presented in Table 5. The categories used were based on recurring themes that emerged when analysing the tax legislation. These recurring themes were the inclusion of a trust in the legislation, the existence of a definition of a trust in the legislation, the inclusion of a trust in a taxpayer definition, the taxation of trust income in the trust, the existence of the flow through principle of income from a trust and the anti-avoidance legislation related to trusts in the legislation. In assessing the legislation of the selected SADC jurisdictions it was found that all of the eleven jurisdictions made provision for trusts in their tax legislation. This indicated that these jurisdictions have attempted to provide more certainty to taxpayers regarding the taxation of these entities.

Six of the eleven jurisdictions included a definition of a trust in the tax legislation. The inclusion of a definition of a trust indicates the intention of the revenue authority to tax trusts. The use of specific wording or terminology in the definition was found to create complexity and to reduce the 'understandability' of the legislation. In assessing the definitions of a trust in the different jurisdictions a number of technical and drafting complexity issues were discovered. These included a lack of characteristics to identify a trust (Lesotho), grammatical complexity in the terminology used (Zimbabwe) and a reference to other legislation when defining the trust in the tax legislation (Mauritius and Seychelles). Additional technical complexity was encountered where the definition of a trust was included in a definition of a settlement (Zambia) and where the definition of a trust was also included in the definition of a company (Mauritius). In Botswana the definition of a trust was not included in the terminology section, but rather in the body of the legislation, resulting in drafting complexity. In the five jurisdictions where no provision was made for the definition of a trust, there may be an increased level of uncertainty in the interpretation of the trust tax legislation that may require expert knowledge and an increased reliance on tax practitioners.

The inclusion of a trust or a trustee in a taxpayer definition (for example "person", "entity" or "company") in the majority of the selected SADC jurisdictions creates greater certainty amongst taxpayers in the region. However, the inclusion of a trust in both the definition of a person and a company (Mauritius) may create complexity, as this provides the opportunity for taxpayers to structure their affairs for their own tax benefit. Furthermore, the lack of inclusion of a trust in a taxpayer definition (Lesotho) may create uncertainty and thus was found to lead to complexity. However, the other extreme, where the legislation makes provision for a specific inclusion or exclusion in a taxpayer definition ("person") also creates complexity (Zimbabwe). It was submitted that neither of these two extremes is ideal. Undoubtedly, clarity in the legislation in terms of defining a trust or a trustee in a taxpayer definition reduces complexity.

The common law concept of the attribution of income to a beneficiary in the context of a trust determines that income earned by a trust may be attributed (vested) to a beneficiary whilst retaining its nature (flow through principle). Although this flow through principle is one of the distinctive characteristics of a trust, four of the jurisdictions do not provide for the attribution of income to beneficiaries in their tax legislation, with the result that all of the income of a trust is taxed in the trust. Namibia is included in the four jurisdictions that do not provide for the attribution of income to beneficiaries in its tax legislation. However, the flow through principle is provided for through the application of case law. Although less complexity was identified in jurisdictions where the flow through principle is not applied, the subsequent treatment of the income may cause additional complexity (for example dividends tax in Mauritius).

A variety of complexities arise as a result of the flow through principle and attribution rules. The application of the flow through principle and attribution rules creates the opportunity to split income between taxpayers, whilst the income retains its nature. It provides the taxpayer with options when planning their tax affairs as the taxpayer may utilise the most tax effective option in the splitting of the income. In addition, the taxpayer may make use of exemptions or deductions that may decrease the effective tax rate for either the trust or the beneficiary. All of these tax related matters add to the complexities of the taxation of trusts in the SADC jurisdictions. This may also be particularly relevant where the tax rates of the beneficiaries and those of the trusts differ. However, the differences in tax rates often necessitated tax authorities to introduce more complex anti-avoidance legislation to curb

the misuse or abuse of the flow through principle and at times include possible attribution of income to a donor (subject to certain conditions) where it is clear that the donor merely utilised the trust to gain a tax benefit. A further complex anti-avoidance measure is the limitation of losses that is linked to the distribution of income to a beneficiary. This measure is included in the legislation to effectively limit the amount of expenditure that may be off-set against the income that is attributed to a beneficiary.

Jurisdictions that do not make provision for the flow through principle in their legislation, and where the income of the trust is taxed in the trust, did not require anti-avoidance legislation. Therefore the inclusion of the flow through principle may create additional complexity in relation to the taxation of trusts.

Finally, during the analysis of the legislation, the characteristics of the jurisdictions were assessed and these were used as a basis for inclusion in the Hin Models of Taxation. The jurisdictions that do not provide for the flow through principle of income were included in the Trustee Taxation Model. The jurisdictions that do provide for the flow through principle of income in the trust were classified as Hybrid Models. Essentially, the Hybrid Models were a combination of the Trustee Taxation Model (in relation to amounts retained in the trust) and the Direct Beneficiary Taxation Model (in relation to income that flows through to the beneficiary). Botswana was the only jurisdiction that was included under the Modified Imputation Model. In light of the complexities discussed above, the Trustee Taxation Model (Mauritius and Tanzania), the Imputation Model and the Modified Imputation Model (Botswana) are comparatively simpler than the Direct Beneficiary Taxation Model, the Indirect Beneficiary Taxation Model or Hybrid Models (Eswatini, Lesotho, Malawi, Namibia, Seychelles, South Africa, Zambia and Zimbabwe). It is submitted that the model applied in a jurisdiction may inherently determine much of the complexity within the legislation.

5.3. LIMITATIONS OF THE STUDY

As highlighted in Section 1.5 there are certain limitations to this study.

Firstly, the scope of the study was limited to consider the income tax legislation of the selected SADC countries as far as they impact on the general trust concepts and not relating to specific application trusts (for collective investment schemes/unit trusts, special

trusts, land rehabilitation trusts, public benefit organisation trusts, personal service providers, share incentive trusts and Black Economic Empowerment trusts). Had these trusts been included in the study, this may have contributed to further complexity in the trust legislation. Therefore, the research is of limited use to those jurisdictions not selected for use in the study. Similarly it has limited (if any) application to specific application trusts in light of this scoping limitation.

Secondly, a disparity may arise from the number of trusts registered in the different tax jurisdictions. Although accurate figures are not available, the study by du Plessis (2018) indicated a significant difference in the number of trusts in the different jurisdictions. A country (for example South Africa) that has larger numbers of trusts registered for tax purposes may be subject to more regular influence from the courts that may impact amendments to legislation and may contribute to further tax complexity. Therefore, the value of the research may be limited where a smaller number of trusts exist in a certain SADC jurisdiction.

Lastly, the interpretation of legislation in the context of this study introduces possible subjectivity. However, this subjectivity is inherent to the interpretation of legislation, but by using a detailed literature review in the form of doctrinal research, the study provided insight into the intention of the legislation.

5.4. FUTURE RESEARCH

This research was exploratory in nature and the results were based on the structural complexity of the income tax sections dealing with trust tax legislation. Further research focusing on operational or compliance complexity may yield a more efficient method to determine the complexity in the selected tax jurisdictions.

Future research is required to:

- develop an effective measurement instrument to measure the structural complexity of trust tax legislation;
- compare the complexity of trust tax legislation between developed and developing countries;

- design a simplified and practical taxation model for the taxation of trusts;
- investigate the effect of case law on the complexity in trust tax legislation; and
- investigate the effect of policy decisions on the complexity in trust tax legislation.

5.5. CONCLUDING REMARKS

This study considered the complexities present in the trust tax legislation in the selected SADC countries. The study confirmed that structural complexity in tax legislation remains a source of concern to academics and legislators, in spite of the fact that the subject attracts significant worldwide attention. This fact is supported by the lack of a measurement instrument to assess this type of complexity. The study also revealed the lack of a body of knowledge in the area of the complexity related to trust tax legislation. It is the first to consider, from a comparative perspective, the complexity involved in trust tax legislation.

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