Answers

Note: The ACCA does not require candidates to quote section numbers or other statutory or case references as part of their answers. Where such references are shown below [in square brackets] they are given for information purposes only.

1 Medical partnership and Dr Silwa

XYZ Tax consultants
[Firm's address]

Drs Badroodien and Saxe
[Client's address]

6 June 2011

Dear Drs Badroodien and Saxe,

Further to our recent meeting, I set out below information on Dr Silwa's tax position.

(i) Employee or independent contractor of the partnership

The portion of the patient billings received by Dr Silwa is remuneration unless such receipts can be excluded as income of an independent contractor.

There are two statutory tests to be applied in the definition of remuneration [see paragraph 1 of the 4th Schedule to the Income Tax Act]. A positive result for either test would result in Dr Silwa being deemed to be an employee and not an independent contractor. Furthermore, if either test has a positive result causing the deeming provision to apply, the common law tests are rendered irrelevant.

'The tests provide for a deeming provision that a person shall *not* carry on a trade independently if the services or duties are required to be performed mainly at the premises of the client and

– the worker is subject to the **control** of any other person as to the manner in which the worker's duties are or will be performed, or as to the hours of work […]; *or*

– the worker is subject to the **supervision** of any other person as to the manner in which the worker's duties are or will be performed, or as to the hours of work […]' [extract drawn from Interpretation Note 17 (Issue 3 – 31 March 2010)].

These tests must be applied to the facts to determine an outcome. The facts must also be assessed on a balance of probabilities.

The first test is that of 'control'. Control refers to the manner in which the work is done. From the facts supplied, it is apparent that the partnership does not control the hours worked (i.e. have no control over the productive capacity of Dr Silwa). In addition, the partnership does not require Dr Silwa to use certain equipment or medicines as she has to obtain those medicines and equipment she intends to use in her consulting room herself. It would seem that this first test fails.

The second test is that of 'supervision'. It is apparent from the facts that there is no system of performance evaluation or monitoring of the associates. While the patients seen by the associates are billed by the partnership, it would seem that the associates are free to expand the patient list. It would seem further that the partners are not involved in any way with an associate's patients. Again, it would seem that this statutory test fails.

Based on the statutory tests, Dr Silwa remains an independent contractor.

The common law test assesses a person based on a 'dominant impression'. The indicators for such 'dominant impression' can be effectively split into three categories, being:

– Near conclusive indicators (including control of the manner of working; payment regime; the person to render the service; nature of obligation to work; client base; risk of profit/loss)
– Persuasive indicators (including supervision; reports; training and productive time)
– Indicators 'resonant' of an employer/employee relationship (such as supply of tools, machinery and stationery; usual premises; duration of relationship; hierarchy structure; employee benefits etc).

Many of these indicators are inter-related but all serve to derive a dominant impression of the relationship between the persons involved.

Key facts emerge from the scenario supplied, namely there is no control over the manner in which the work is performed or supervision of that work (as per the statutory tests above as well). The associates must maintain their own medicine stocks and acquire their own furniture for their consulting rooms. The risk of an associate bearing a loss is small, as the associates are guaranteed to receive 60% of their billings to patients, although this could happen if the expenses of medicine and furniture exceed this amount. The hours worked are decided by the associates themselves and there is no apparent hierarchical structure.

It would seem that the common law test indicates that Dr Silwa is an independent contractor.

(ii) Gross income for yourselves and Dr Silwa

Gross income comprises the following criteria:

– An amount
– Is received or accrued
– In cash or otherwise
– That is not of a capital nature.

It is accepted that the patient billings are for services rendered and as such are amounts not of a capital nature. Furthermore, there is clearly an amount (the amount invoiced) and that receipt would be in the form of cash. However, the amount that is received by or accrued to Dr Silwa needs analysis.

The partnership retains 40% of such billings for 'overhead' costs. For an amount to have accrued to Dr Silwa, she must be 'unconditionally entitled' to such amount [see the cases of *Lategan* or *People's Stores*]. It is submitted that Dr Silwa has no entitlement to the 40% of her patient billings as the partnership deducts such amount before payment to her. The associate agreement does not permit the payment of a higher amount.

Dr Silwa's gross income is therefore 60% of her patient billings.

While the partnership bills the associates' patients, the partnership is not entitled to the full amount received (60% being immediately due to the associate). The associate agreement also prevents the partnership from being entitled to the full amount (net of VAT). The gross income for the partners in the partnership from associate billings is 40% (net of VAT) of such billings split according to the profit sharing arrangement in the partnership agreement.

(iii) Value added tax (VAT) implications if Dr Silwa is regarded as an independent contractor

If Dr Silwa is an independent contractor and not an employee, she would have to register as a VAT vendor if she, independently, met the compulsory turnover requirements.

It is clear from the scenario given that over a 12-month period, Dr Silwa bills (excluding VAT) a total of R1,200,000. These taxable supplies constitute her turnover figure, with the result that Dr Silwa must register for VAT in her personal capacity.

The implications of such registration would be as follows:

While the partnership can continue to bill Dr Silwa's patients including VAT, Dr Silwa must bill the partnership for 60% of the net invoice before adding VAT. This can be demonstrated numerically as follows:

Patient billed R100 for the service plus VAT of R14 by the partnership. Dr Silwa bills the partnership R60 plus VAT of R8·40 for the service rendered.

As a result, the partnership has a VAT output of R14 and input (from Dr Silwa's invoice) of R8·40. Dr Silwa has an output VAT of R8·40.

In addition, Dr Silwa could claim the VAT on purchases from other vendors (for example for the medicines purchased).

Such treatment would also match the gross income implications for income tax as identified in (ii) above.

Should you require any further assistance with regards to the above, please contact me.

Yours sincerely

Tax consultant

2 Global Products Ltd

(a) Memorandum

TO: Audit Manager
FROM: Tax assistant
RE: Income tax effects selected transactions
Date: 6 June 2011

This memorandum concerns the tax effects of the loan granted by Foreign Holdings LLC and the tax effects of the purchase and sale of trading stock denominated in foreign currency.

(1) Loan from Foreign Holdings LLC

As Foreign Holdings LLC holds more than 20% of the equity share of Global Products Ltd and no other shareholder holds the majority of the shares, it is connected to Global Products Ltd.

The South African tax system [s.31] requires that international transactions with connected persons be based on the arm's length principle. The provision of financial assistance (which includes the granting of a loan) by a non-resident is such an international transaction. The arm's length principle is applied in two ways: firstly to the ratio of debt capital to equity capital (thin capitalisation) and secondly, to the terms of any loan.

Tutorial note: *Section 31 is amended with effect for years of assessment commencing on or after 1 October 2011 and is therefore not of application to this solution.*

The first test to be applied to the financial assistance granted by Foreign Holdings LLC is that of thin capitalisation. Unless exceptional circumstances exist, the allowed debt to equity ratio for a non-resident lender may not exceed 3:1. The weighted average of the debt provided by Foreign Holdings LLC for the year of assessment ended 31 March 2011 must be tested against three times the fixed capital. Fixed capital (in this scenario) is represented by share capital; accumulated profits but excludes reserves arising from the revaluation of assets. The fixed capital is therefore: 40% x (10 million plus 25 million) = R14 million. The weighted average debt granted by Foreign Holdings LLC must therefore not exceed three times R14 million (being R42 million).

The weighted average debt for the year ended 31 March 2011 would be R52·5 million (50 million x 9/12 plus 60 million x 3/12).

Tutorial note: *The weighting should (in terms of the Practice Note) be performed using days. However the exam instructions permit the use of months and so both methods are accepted.*

As the weighted average debt exceeds three times the fixed capital, the interest payable on such excess would not be permitted as a deduction. Furthermore, Secondary Tax on Companies (STC) would be charged (at 10%) on such excess.

Whether or not thin capitalisation was applied, the high rate of interest must be tested against the arm's length principle in terms of the transfer pricing practice. The interest rate for financial assistance is considered to be excessive (in terms of the South African Revenue Service practice) where the rate of interest is greater than 200 basis points above the South African prime lending rate, i.e. for Global Products Ltd, the acceptable rate of interest would be 12% (10% prime lending rate plus 2%).

As all the interest on the loan has exceeded three times the fixed capital, and it has been disallowed, the transfer pricing limitations only apply to the 'acceptable' debt of R42 million. Only the rate of 12% on such amount will be permitted as a deduction and the remainder will be disallowed. The disallowed portion will also be subject to STC at 10%.

Tutorial note: *As from 1 January 2013, the company would also have been liable to withhold 10% of the total interest paid to Foreign Holdings LLC in terms of the new withholdings tax on interest [ss.37L to 37M].*

(2) Purchase and sale of trading stock denominated in foreign currency

Purchase of the trading stock

On the purchase of the stock on 20 February 2011 (and the immediate shipping thereof), ownership has passed to Global Products Ltd. A deduction for income tax purposes may therefore be claimed for the acquisition of trading stock (which as an asset of working capital is not considered to be of a capital nature) [s.11(a)]. The value of the stock would be translated to Rands at the spot price on the transaction date of 20 February 2011, i.e. US$1,200,000 x 7·3 = R8,760,000. The full value is deducted despite the agreed payment schedule. The cost of the trading stock specifically excludes exchange differences [considered in terms of s.24I].

The customs and excise charges of R360,000 are considered to increase the cost of the trading stock and are therefore also claimed as a deduction for income tax purposes (but only when incurred on 15 March 2011).

Value added tax (VAT) is then charged to Global Products Ltd for the importation of goods. The import date is the same as that applied for the purposes of customs and excise [s.13(1) of the VAT Act] and the value on which VAT is charged is the same value as that used for customs and excise purposes. 14% is therefore charged on R9,060,000 = R1,268,400. As the VAT charged is claimed as a VAT input it does not add to the cost of the trading stock for income tax purposes.

The exchange losses on payments 1 and 2 would be tax deductible in the year ended 31 March 2011, and the subsequent exchange gain on payment three would be taxable in the year ended 31 March 2012.

Sale of the trading stock

As the sale of the trading stock represents an export, the sale is a zero-rated supply for value-added tax (VAT) purposes. VAT is therefore charged at 0%. This zero-rating permits the acquisition of the stock to be classified as goods acquired for the making of taxable supplies and allows the VAT input claim.

For income tax purposes, the sale is recognised on 15 March 2011. The gross income recognised is therefore £1,500,000 x 11·25 = R16,875,000. The exchange differences arising from the payment terms agreed with the customer are separately recognised. No exchange difference is recognised on the initial payment as it was paid on the date of sale.

The exchange loss on translation of the debt represented by the second instalment is tax deductible in the year ended 31 March 2011 and the further loss when the instalment was paid by the customer would be tax deductible in the year ended 31 March 2012.

(b) Joint Venture (JV) Company

(i) 'Residence' for non-natural persons in the context of the South African income tax act is achieved when the non-natural person (such as a company) is incorporated, formed, established or has its place of effective management in South Africa.

It is apparent from the scenario that the JV Company will be incorporated outside of South Africa. However, management will be sourced largely from Global Products Ltd. The key determinant in identifying the 'place of effective management' is usually where the key strategic decisions are made, usually by the board of directors. However, the South African

Revenue Service take the view that the 'place of effective management' is where the day-to-day management decisions are made.

It is submitted that despite Global Products Ltd supplying the majority of the management team, under both interpretations, the JV Company does not have a place of effective management in South Africa and is therefore non-resident for the purposes of the South African income tax act.

(ii) The existence of the JV Company must be tested against the 'basic permanent establishment (PE)' rule (as given). This rule can be broken into various factors, all of which must be present for a PE to exist.

(1) There must be a place of business: it is apparent from the scenario supplied that the JV Company will be renting premises in one or more jurisdictions outside of South Africa. This is sufficient to indicate that there is a place of business, as ownership is not a requirement.

(2) Such place of business must be fixed, either geographically or have a degree of permanence: whether or not the requisite 'permanence' exists is a purely factual test and would require further information as to the nature of the business undertaken by the JV Company.

(3) The business of the enterprise (Global Products Ltd) must be carried on through the place of business. This requirement also cannot be easily answered from the information supplied. While it is clear that Global Products Ltd will invest in this JV Company, it is not clear as to whether or not the business of the JV Company will be that of Global Products Ltd or a separate business. If separate, then no PE exists for Global Products Ltd as it would not be conducting its business through the JV Company.

3 Company M (Pty) Ltd and Company T (Pty) Ltd

(a) Tax implications for the year ended 31 March 2011 for Company M (Pty) Ltd ('Co M') and Company T (Pty) Ltd ('Co T')

All of the transactions fall within the so-called 'corporate rules'. Specifically, these transactions invoke the intra-group transaction provision of the Income Tax Act. While the companies may jointly elect for this provision to not apply, in the absence of such election the application of the intra-group effects is automatic. However, there are certain conditions that must exist for the intra-group provision to apply. These are discussed within the individual transactions below.

Disposal of manufacturing line at tax value (below market value)
As the manufacturing machinery, capital assets for Co M, will be used by the purchaser (Co T) as capital assets and the companies form part of the same group of companies, the intra-group provision applies.

Co M is deemed to have sold the manufacturing machinery for an amount equal to the machinery's base cost on the date of disposal, i.e. no capital gain or capital loss arises. Co T is deemed, on disposal of this machinery after an appropriate time (see (b) below), to be one and the same person as Co M. This means that Co T is deemed to have purchased the machinery at the same time and at the same price as Co M and used it for the same purpose.

Furthermore, being depreciable assets, Co M does not include a recoupment for the previous allowances granted on disposal to Co T. Co T merely continues the capital allowance or wear and tear deduction schedule begun by Co M and will recognise the full recoupment on disposal of such machinery.

Despite Co M and Co T being connected persons, it should be noted that this intra-group transaction provision overrides the other provisions of the Income Tax Act. For this reason, the determination of the cost of the asset for the purposes of capital allowances and the deemed disposal for capital gains tax (CGT) at market value are ignored.

In terms of the value added tax (VAT) Act, no VAT is applicable where the corporate rules have been applied. No VAT is therefore levied on the sale of the machinery from Co M to Co T irrespective of the consideration charged.

Disposal of raw materials for Product A to Co T
As for the disposal of the capital assets, the intra-group transaction provision overrides the other provisions of the Income Tax Act. In addition, VAT is not applied to this disposal of trading stock. For the intra-group provision to apply to the disposal of trading stock, the purchaser must also treat the asset as trading stock. As this will be the case, the intra-group provision applies.

Trading stock, as a revenue asset, is deemed to be disposed of at the cost deducted (if acquired in the same year) or the cost as determined for the purposes of the trading stock provision. The ultimate effect of such a deemed disposal value is that no revenue gain or loss is recognised by the disposing company (Co M).

Co T is deemed to be one and the same person as Co M for the future treatment of the trading stock acquired and will deduct the trading stock at the disposal value for Co M.

Disposal of finished goods for Product B to Co M
As both the raw materials (above) and finished goods represent 'trading stock', the effects for the disposal of finished goods by Co T to Co M of Product B are mirrored.

It is important to note that irrespective of the value placed on the transaction by the companies, the intra-group transaction provision determines the values for tax purposes where it is applied.

(b) Tax implications if Co T had to sell the machinery, acquired in terms of an intra-group transaction, in the next year of assessment

An anti-avoidance measure applies should Co T dispose of the machinery acquired through the intra-group transaction within a period of 18 months. The anti-avoidance measure will not apply if the disposal is involuntary (for example, destruction through fire; theft etc).

The effect of the anti-avoidance measure is that the capital gain, as would have arisen at the start of the 18-month period if Co M had sold the machinery to Co T at market value, is treated as a ring-fenced capital gain that must be immediately recognised (after applying the corporate inclusion rate of 50%). This ring-fenced capital gain may not be aggregated with Co T's other capital gains and capital losses, nor may the included ring-fenced capital gain be set-off against any assessed loss or balance of assessed loss that Co T may have available.

If disposal by Co M at market value at the start of the 18-month period would have resulted in a capital loss, such capital loss is ring-fenced in Co T's hands, i.e. may not be aggregated with any other capital gains or capital losses arising in Co T. Such capital loss may only be utilised against any capital gain arising from the disposal of any other asset acquired by Co T from Co M which qualified for treatment as an intra-group transaction.

Any capital gain or capital loss arising from the disposal (above that recognised in terms of the above anti-avoidance measure) is to be recognised in terms of the standard rules as contained in the Income Tax Act.

4 John Odis

Tax Consequences for John Odis

Residence
John is considered to be tax resident for the purposes of the Income Tax Act. This means that John is taxed on worldwide income and capital gains for that Act. However, for the purposes of Estate Duty, John is not a resident as the Estate Duty Act only considers resident those persons ordinarily resident in South Africa. Only those assets (and rights to those assets) within South Africa, for example immovable and moveable property, fall within the Estate Duty ambit.

Income Tax on death
In the year of death, the year of assessment ends on the date of death. John's final year of assessment therefore runs from 1 March 2010 to 1 November 2010.

The event of death has a number of income tax implications arising from the information supplied:

The Trust:
The sale of assets to the Trust on interest free loan account represents a gratuitous disposition. Such gratuitous disposition triggers the attribution rules for income and capital gains. That the Trust is discretionary implies that beneficiaries only have a contingent right to the income and capital of the Trust. The right to income is effectively contingent on the Trustees exercising their discretion to vest income and/or capital.

John, through the sale of assets on interest free loan account, is the 'donor' of such contingent right. Effectively, until the Trustees exercise their discretion, the income generated by the assets sold to the Trust by John must be attributed to him for income tax purposes. Such attribution ceases on the date of death.

As the Trustees had not exercised their discretion for the year of assessment commencing 1 March 2010 to the date of John's death, the income earned by the Trust for that period would be attributed to John for his final year of assessment. However, in terms of case law [the *Woulidge* principle], the interest foregone on the loan account balance determines the maximum that can be attributed. As the loan balance remained at R2·3 million, the maximum notional interest foregone would amount to R153,333 (R2·3 million x 10% x 8/12).

To the date of John's death, the Trust earned rental of R120,000 (R180,000 x 8/12) and R80,000 of foreign interest (R120,000 x 8/12). This R200,000 potential attribution would have been limited to R153,333 (presumably on a pro-rata basis).

To the extent [as a result of the application of *Woulidge* – see above] that John had been taxed on the interest retained in the Trust in prior years, the distribution now received by him from the Trust out of the retained interest will have no tax consequences. That portion not previously taxed in John's hands would not have been taxed in South Africa as the interest is of a foreign source accruing to a non-resident Trust. Thus the portion not yet taxed would be deemed to be income in John's hands in the year of receipt (as John is resident for Income Tax purposes in South Africa).

Capital gains tax:
In terms of the Income Tax Act, the event of death triggers a deemed disposal of assets from John to the deceased estate on the date of death. As John is resident for Income Tax purposes, this deemed disposal considers his worldwide assets and not just those within South Africa.

The proceeds taken into account on the deemed sale of the properties in the Bahamas and in South Africa will not be reduced by the amounts of the outstanding mortgages on the properties. Any capital gain or capital loss on the life policies (both in the Bahamas and in South Africa) would be disregarded for capital gains tax purposes.

Tutorial note: *The application of the Long-term Insurance Act is not required, however, for noting is that 'policy' for the purposes of the capital gains tax disregarding provision refers to s.29A, which in turn refers to the Long-term Insurance Act. That Act defines a life policy as 'a contract in terms of which a person, in return for a premium, undertakes to—*

(a) provide policy benefits upon, and exclusively as a result of, a life event; or
(b) pay an annuity for a period,

and includes a reinsurance policy in respect of such a contract'. Thus it is submitted that foreign policies are also contemplated.

As John left the loan account to his wife, a roll-over takes place for capital gains tax purposes (unless his wife is considered non-resident in terms of the Income Tax Act). A roll-over results in John's wife receiving the loan account with the full history of John's dealings attached for tax purposes. This means that John's wife is considered (post-John's death) to have loaned the Trust the money.

Estate Duty on John's estate
As discussed under the heading of 'residence', John is not considered resident for the purposes of the Estate Duty Act. The market value of the property in South Africa plus the South African life insurance policy is considered 'property' for the purposes of Estate Duty. The amount owing on the South African property will qualify as a deduction against the property, as will the final income tax liability owed. Other miscellaneous deductions may also apply, such as executor fees, etc. The loan account (owed by the Trust) falls outside the Estate as it is unlikely that this debt is enforceable in South Africa against the Trust. The net value of the estate (being the property less applicable deductions) is further reduced by the abatement of R3·5 million and only to the extent that the net value of the estate exceeds such abatement will Estate Duty be levied at 20%.

5 Mr Thomas

(a) Taxation of pension annuities in terms of the South African income tax act

Mr Thomas, as a non-resident for South African tax purposes, may only be taxed in South Africa on income from a South African source. At the heart of this matter is the identification of the source of the pension annuity.

The source of services rendered is to be found (generally) where the service is rendered. Mr Thomas rendered all his employment services in South Africa. However, at the time of rendering the services, Mr Thomas was a South African tax resident and would have had to include the income from such employment in gross income irrespective of where he rendered the services.

It is submitted that the source of a pension is to be found where the service was originally rendered. Evidence for this submission may be found in the deemed source provision concerning pensions, which apportions a pension annuity for a non-resident on the basis of years of service in South Africa. As all of Mr Thomas' services were rendered in South Africa, the pension annuity would be exclusively of a South African source. Furthermore, as an annuity, the amount falls to be included in gross income by virtue of the special inclusion paragraph concerning annuities.

Mr Thomas would also not find relief in the exemption provision applicable to pension annuities as the provision is only applicable to residents, whereas he only received the pension annuity as a non-resident. Furthermore, the exemption provision only serves to exempt the foreign service portion of the annuity.

It can therefore be concluded that the annuity would have been gross income, being an amount received by or accrued to a non-resident from a source within South Africa and not of a capital nature, for Mr Thomas, despite his status as a non-resident.

Relief, if any, should be sought in the application of the Double Tax Agreement (DTA) with Australia.

(b) Double Tax Agreement with Australia

In analysing the pension article of this DTA, the term 'annuity' as contemplated would include the pension annuity from the pension fund [refer paragraph 3 of the supplied article]. Furthermore, the annuity was payable from the pension fund itself.

The first paragraph of the pension article may be read as follows:

'Pensions and annuities from sources in one Contracting State [South Africa] and paid to a resident of the other Contracting State [Australia] shall be exempt from tax in the first mentioned Contracting State [South Africa] *to the extent that such pensions and annuities are included in taxable income in the other State* [Australia]' (square bracketed inserts added for ease of reference and italics added for emphasis).

From this extract it is clear that the pension annuity from South Africa can only be exempt from South African tax to the extent that the annuity was included in Mr X's Australian tax. As the annuity was not included in Mr Thomas' Australian tax, the annuity remains taxable in South Africa. It is further submitted that the reference that the amounts 'are included' implies that failure to disclose such amounts in Australia would also render the provision inapplicable.

In addition, the DTA provision can only practically be of application if the taxpayer has notified the South African Revenue Service of the intent to apply the provision.

Tax, if levied in South Africa, could potentially be claimed as a tax credit in Australia in terms of Article 23 of that DTA.

In future, should Mr Thomas declare the annuity in Australia, he may be able to apply for relief from South African tax in terms of this DTA article.

			Marks Available	Marks Maximum
1	**(a)**	Independent Contractor versus employee		
		Receipt of remuneration (and employee) unless independent contractor	1	
		Positive test results indicate employee	1	
		Details of the two statutory tests explained	2	
		First test (control) and application to the facts	2	
		Second test (supervision) and application the facts	2	
		Failure of statutory tests and conclusion	2	
		Common law test requirements with explanations of the three categories	3	
		Application of the facts to the indicating factors	2	
		Overall conclusion	1	
			16	**13**
	(b)	Gross income		
		Identifying gross income definition criteria	1	
		Identifying criterion for critical consideration (the 40% deduction from associate's billings)	1	
		Accrual and unconditional entitlement principle	1	
		Application of unconditional entitlement principle to the facts	1	
		Application of unconditional entitlement principle to the partnership	1	
		Income split between the partners according to profit sharing ratio	1	
			6	**6**
	(c)	VAT implications		
		Application of VAT registration requirement to Dr Silwa	1	
		Applying compulsory registration requirements	1	
		Explanation of implications (with or without numerical example)	1	
		VAT input claims for associate once registered	1	
			4	**4**
	Format and presentation of the letter		1	
	Effectiveness of the communication		1	
			2	**2**
		Total		**25**

				Marks
2	**(a)**	(1)	Loan from Foreign Holdings LLC	
			Connected person application	1
			International transaction and the inclusion of financial assistance	1
			Identification of thin capitalisation as an issue	1
			Composition of fixed capital	1
			Disallowance of deduction	½
			Allowable debt to equity ratio	½
			Weighted average of debt tested against fixed capital	½
			Fixed capital excludes revaluation reserve	½
			Calculation of fixed capital	½
			Calculation of weighted debt	½
			STC chargeable on disallowed deduction amount for thin capitalisation	1
			Rate of interest for transfer pricing purposes	½
			Determination of acceptable rate of interest	1
			Application of acceptable rate	1
			STC chargeable on disallowed deduction amount for transfer pricing (excluding amount already disallowed for thin capitalisation)	½
				11
		(2)	Purchase of trading stock	
			Acquisition recognition date	½
			Claim of deduction	½
			Value of stock and translation	½
			Claim of customs and excise cost for income tax purposes	1
			VAT on importation	½
			Time of supply	½
			VAT charge and claim	½
			Exclusion of exchange differences from cost of trading stock	1
			Tax deductibility of exchange losses on instalments paid prior to year end	1
			Liability to tax on gain on year end translation of third instalment	1
				7
			Sale of trading stock	
			Export and zero rated supply	½
			Effect of zero rating	½
			Gross income (when and how much recognised)	1
			Exchange difference separately recognised	1
			No difference on sale date	½
			Translation of debtor at year end (and effect)	1
			Translation of debtor when final payment made	½
				5
				23
		Format and presentation of the memorandum		1
		Effectiveness of the communication		1
				2
	(b)	JV Company		
		Residence criteria		1
		Interpretation of place of effective management plus SARS interpretation		2
		Application of definition to facts		1
		Place of business and application		2
		Notion of ‘fixed’ and application		2
		Notion of ‘carrying on business through a PE’ and application of criteria to facts		2
				10
			Total	**35**

			Marks
3	(a)	Intra-group transaction (identified)	½
		Joint election out of section not applied	½
		Capital asset sold treated as capital asset by acquirer	1
		Capital asset sold at base cost	1
		Acquirer deemed to have purchased asset as same time and for the same purpose as disposer	1
		No recoupment for Co M	1
		Continuation of allowances for Co T	1
		Full recoupment on disposal by Co T	1
		Other provisions of the Income Tax Act do not apply (override by intra-group transaction provision)	1
		VAT does not apply where intra-group transaction applied	1
		For application of intra-group transaction, trading stock sold must be trading stock for acquirer	1
		Deemed disposal at tax carrying cost	1
		Co T treated as one and the same person as Co M	1
		Finished goods and raw materials both trading stock	1
		Consideration on sale determined with reference to intra-group transaction provision and not the values as agreed by the companies.	1
			14
	(b)	Sale of machinery acquired within 12 months	
		Anti-avoidance measure if sold within 18 months	½
		Does not apply where involuntary disposal of capital asset (plus example)	1
		Application where capital gain would have arisen	2
		Application where capital loss would have arisen	2
		Effect for remaining capital gain or capital loss	½
			6
		Total	**20**

4	Income tax – taxed on worldwide income and capital gains	1
	Estate Duty – only taxed on SA assets (plus examples) as not ordinarily resident	1½
	Final year of assessment runs to date of death	½
	Interest free loan is a gratuitous disposition	1
	Attribution rules apply	1
	Contingent rights and exercise of Trustee discretion	1
	Application of contingent right rule and effect of death	1
	Application on death	1
	Application of notional interest rule	1
	Demonstration of application	1
	Implications of receipt of distribution from retained income for John	1
	Application of notional interest rule to this distribution	1
	Deemed disposal for cgt of all assets on date of death	1
	Mortgages not considered	1
	Life policies disregarded	1
	Identifying roll-over event and effect	1½
	Property for Estate Duty and identification of such property	1½
	Deductions applicable	1
	Abatement and application of Estate Duty rate	1
	Total	**20**

			Marks
5	**(a)**	Non-resident taxed based on source	1
		For services source follows where the service is rendered and application	2
		Pension fund annuity source follows where the service was rendered	2
		Support for this principle	1½
		Annuity is South African source and included in gross income	1½
		No relief from exemption provision	1½
		Conclude that annuity is South African gross income	½
		Relief should be sought from DTA	1
			11
	(b)	'Annuity' as defined includes this pension annuity	1½
		Pension annuity is not a purchased annuity	1
		Application of paragraph 1	1½
		Meaning of 'are included'	1½
		Application of DTA provision – submission of intent	1½
		Potential to claim South African tax credit in Australia	1
		Future use of the pension article of the DTA	1
			9
		Total	**20**