How are professional football player transfers taxed in South Africa?

CHAPTER 1 – INTRODUCTION

1.1 Introduction

Professional football has developed into a lucrative industry which commands high value financial transactions. Among the most prevalent financial transactions is the transfer of professional football player ("players") registration rights among professional football clubs ("clubs"). The quantum and frequency of these financial transactions begs an inquiry into their tax treatment.

The literature on the income tax treatment of player transfers in South Africa is lacking and that which has been published only concerns itself with permanent player transfers. An academic contribution which delves into the tax treatment of the prevalent conventional player transfer methods, and some unconventional, would be valuable to the development of the literature in this area. In its non-binding guidance publication entitled *Guide on the Taxation of Professional Sports Clubs and Players*, the South African Revenue Service ("SARS") states that it is unlikely that professional soccer clubs could be said to trade in player contracts, and accordingly, player transfers are unlikely to constitute revenue receipts or expenditure as anticipated by the Income Tax Act[1] ("Income Tax Act").

Accordingly, the primary objective in this mini-dissertation ("paper") is to critically evaluate SARS's assertion by providing a broader perspective of the income tax implications related to player transfers in South Africa with reference to applicable football regulations and well established common law principles, specifically from the perspective of a club acquiring the registration rights of a player ("acquiring club") and a club disposing of the registration rights of a player ("disposing club"). In this pursuit, the paper will use practical scenarios premised on combination of the following conventional transfer methods: (i) permanent; (ii) temporary; (iii) free. In addition, special variations of the conventional transfer methods shall be considered.

[1] Act 58 of 1962.

1.2 Research method and sources

I shall observe the doctrinal legal research methodology. Accordingly, I must compose a descriptive and detailed analysis of the tax treatment of player transfers with reference to the Income Tax Act and case law interpreting it. In addition to these sources, I shall rely on: -

I. global, regional and national football regulations (and commentary thereon) to contextualise the various player transfer methods;
II. SARS guide on the taxation of professional sports clubs and players;
III. academic and media articles; and
IV. case law.

An academic article entitled *Income tax implications from the transfer of football players in South Africa*[2], appears to be the leading authority on this topic. Notwithstanding its limited scope, it provides an adequate intellectual base from which to develop this paper. I intend to critically evaluate its contention that player registration rights generally constitute capital receipts or accruals.

1.3 Delineation and limitations

I shall limit this paper to the income tax analysis of South African player transfer fees and other ancillary fees; accordingly, it will not deal with tax implications that may arise from receipts or accruals related to sponsorships, prizes, ticket and merchandise sales, insurance premiums, and employment relationships.

Furthermore, this paper only deals with the income tax implications for acquiring and disposing clubs in accordance with the domestic football regulations - not players or player agents.

1.4 Chapter Overview

Chapter 2

This chapter provides the contextual background surrounding player transfers. In doing so, a general overview of the player transfer system with reference to global, regional, and national football regulations is advanced. Importantly, the scope of the

[2] S Makhaya and L Barnard "Income tax implications from the transfer of soccer players in South Africa" (2017) *Journal of Economic and Financial Sciences 10(1)*.

player registration rights are discussed.

This chapter also elaborates on the different player transfer methods and fees, which include: (i) permanent and temporary player transfers; (ii) free player transfers, (iii) training compensation; (iv) bridge player transfers; (v) buy-out clause player transfers; and (vi) buy-back player transfers.

Chapter 3

The third chapter describes the applicable principles of South African income tax with reference to case law. This chapter specifically contextualises the rules relating to gross income, allowable tax deductions, capital gains tax and anti-avoidance rules.

Chapter 4

The fourth chapter illustrates the tax treatment of the transfer fees generated from the various player transfers methods, using practical scenarios. I have selected these scenarios because some are common in football transfers and others demonstrate the extent to which football transfers have been convoluted.

Chapter 5

The final chapter summarises contents of the paper and advances the following suggestions: (i) SARS should issue a dedicated guideline for the tax treatment of transfer fees, given the commercialisation of football generally and player transfers in particular; and (ii) there is merit in amending the Income Tax Act to allow the limited tax exemption of training compensation.

CHAPTER 2 - CONTEXTUAL BACKGROUND

2.1. General

Understanding the workings of player transfers is essential for the accurate application of the tax principles. Accordingly, this chapter will provide a contextual overview of the origins of player transfers, stipulate the applicable football regulations, and discuss the various player transfer methods and fees related thereto.

2.2. Contextual overview

2.2.1 Foundations of the transfer market

The Football Association of England ("FA") pioneered the growth of football by being the first governing body, globally, to professionalise football.[3] This decision culminated in the formation of the English Football League ("EFL") in 1888.[4]The professionalisation of football meant that players could formally commoditise their talents but it also resulted in a need to introduce additional rules to regulate the legal relationships between players and their clubs.

Consequently, the FA adopted the 'player registration system' ("system").[5] In terms of the system, players were required to register to play for a club at the commencement of each football season, and once a player had done so, they were not permitted to register to play for another club, within the same season, without the FA's permission or the club they were registered with.[6] In addition to this, each player had to have an employment contract for the season concerned. Without the system, the FA ran the risk of players playing for multiple clubs within the same season, which would undermine the principle of fair competition.

Once a season concluded, however, a player was within their right to register for any club which sought their services for the following season. When players moved from one club to another, it was dubbed a 'player transfer'.[7] In practice, the system allowed clubs with superior financial resources to lure talented players from clubs with less

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[3] R Steen, J Novick and H Richards *The Cambridge Companion to Football* (2013) at 23.
[4] Ibid.
[5] D McArdle 'One Hundred Years of Servitude: Contractual Conflict in English Professional Football before Bosman' *Web Journal of Current Legal Issues* 2000, available at https://web.archive.org/web/20100301021524/http://webjcli.ncl.ac.uk/2000/issue2/mcardle2.html, accessed 23 October 2022. Under heading "The Football Association's player registration scheme and the Radford case".
[6] Ibid.
[7] Ibid.

financial resources because they could offer higher wages and other perks. Thus, the EFL's administration was concerned that a failure to intervene, could render professional football less competitive.

In response, the EFL administration adopted the retain-and-transfer system ("transfer system").[8] After the transfer system was introduced, a player was no longer free to register with a different club in a new season, without the approval of the club they had previously registered with.[9] This rule applied even if a player's employment contract had expired and/or the club had no intention to field a player in the upcoming football season. Thus, a player whose club refused to release their registration to a different club was likely to seek employment in other (often less lucrative) professional football leagues, which had not yet adopted the transfer system, or retire from football.[10]

Hereafter, disposing clubs began to leverage their authority to demand financial compensation from acquiring clubs, in exchange for their cooperation in player transfers. Henceforth, player registration rights were commoditised.[11] Clubs with less financial resources were content with the transfer system because it deterred financially endowed clubs from poaching their talent, and where they agreed to a player transfer, the option to demand compensation would provide the financial resources to replace the player or settle outstanding debts.[12]

Therefore, the transfer system placed the professional prospects of players in the hands of clubs. This led to disputes between clubs and players seeking a transfer to a club of their liking. Among other factors, player transfer disputes culminated in the establishment of an EFL players' union to advocate for the abolishment of the transfer system.[13]

2.2.2 Key legal developments

The transfer system was the subject of several legal challenges. In this section I shall deal with four notable cases which influenced the present-day transfer system.

2.2.2.1 Kingaby v Aston Villa Football Club

In 1906, Herbert Kingaby ("Kingaby") transferred from Clapton Orient Football Club to

[8] Ibid under the heading "The Football League's player registration scheme and the Kingaby case".
[9] Ibid.
[10] Ibid.
[11] Ibid.
[12] Ibid
[13] Ibid.

Aston Villa Football Club ("Aston Villa") for a sum of £300, on a one-year employment contract. After a brief period, Aston Villa tried to dispose of Kingaby, as they were not satisfied with his technical ability.[14] Their efforts were unsuccessful because interested clubs were not prepared to meet Aston Villa's asking price. Notwithstanding the expiration of Kingaby's employment contract (which they had no intention to renew), Aston Villa indicated their intention to retain his registration, unless their asking price was met, thus preventing him from registering with a different EFL club.[15]

With the financial assistance of the player's union, Kingaby initiated a legal challenge to set aside Aston Villa's decision to retain him on the ground that the decision was tantamount to an unlawful restraint of trade. Furthermore, he claimed damages from Aston Villa for breach of contract, maliciously procuring breaches of contract, and an injunction. Kingaby contended that by not releasing his registration, when they had no intention to use his services, Aston Villa maliciously used the transfer system to stunt his professional career.

The court dismissed Kingaby's application on the basis that he did not challenge the legality of the transfer system. Accordingly, the court stated that Aston Villa's motives were irrelevant because even malicious motives cannot render a lawful act unlawful.[16] This case effectively confirmed the lawfulness of the transfer system in the United Kingdom ("UK").

2.2.2.2 Eastham v Newcastle United Football Club[17]

By 1959, the transfer system had evolved. At that stage, a player who was nearing the end of his employment contract could confront one or a combination of the following scenarios:

I. re-register for the same club;

II. be offered a less favourable contractual terms (for instance a lower wage) by their current club, and if the player unsuccessfully appealed the decision to the FA, the club could retain the player indefinitely;

[14] Ibid under the heading "The Football League's player registration scheme and the Kingaby case". Kingaby was prevented from playing for EFL clubs, but he could and did, join professional clubs in other divisions. First, Fulham Football Club in the in the Southern League and then Leyton Orient in the English First Division. After, Southern League and the English First Division adopted the EFL's retain-and-transfer rule, however, this meant he could not play professional football anywhere in England.
[15] Ibid.
[16] Ibid.
[17] [1963] 3 All ER 139.

III. the club could place the player on its transfer list, which is circulated to other clubs, specifying their asking transfer fees; or

IV. the club could release the player for free, whereafter he could register to a different club.[18]

During 1959, George Eastham ("Eastham") was registered to Newcastle United Football Club ("Newcastle"). For several reasons he rejected Newcastle's offer to stay and indicated that he sought a transfer to another club. This was off course not possible without Newcastle's consent or a successful appeal to the FA. It so happened that Newcastle exercised their right to retain his registration, albeit without an employment contract, and he unsuccessfully appealed this decision to the FA. He was thus not free to join another club, up until Newcastle agreed to release his registration.

At the instance of the player's union, Eastham instituted legal proceedings to challenge the legality of the transfer system on the ground that it amounted to an unreasonable restraint of trade. The FA, which was joined as a defendant in the matter, argued that the transfer system was lawful because it served the legitimate purpose of maintaining fair competition among clubs and spectator interest because it deterred bigger clubs from unfairly poaching the best players.

In finding for Eastham, the court opined that any rule which limited the players right to seek alternative employment at a time he was not employed was in restraint of trade. The combination of a club's right to seek a transfer fee and/or to retain a player's registration, in most cases, unfairly restrained a player's right to seek employment where they were unemployed. And therefore, the legitimate interest to maintain competition and spectator interest did not justify the retention aspect of the transfer system.[19]

On the back of this case, the FA initiated two significant reforms to the transfer system. First, at the end of each football season, clubs were required to advise the FA if they sought to transfer any of its players at a fee, so that these players could be included on a transfer list circulated to other clubs. If a player was not placed on the transfer list, and the parties could not agree an extension of a players employment contract, the player would be entitled to a free transfer. Thus, it became easier for players to

[18] D McArdle op cit (n5) under the heading "The abolition of the maximum wage and the Eastham case".
[19] Ibid.

seek free transfers (with the intervention of the FA) after the expiry of their employment contracts.[20]

Second, the FA adopted new dispute mechanisms. One of these was an independent transfer tribunal which had authority to hear matters which involved disputes between players and their clubs This led to clubs having to grant players contracts which were favourable to a player, failing which players would be permitted a free transfer.[21]

Owing to the increased player autonomy brought about post the Eastham ruling, clubs veered away from the practice of offering one-year employment contracts to players, the duration of three-year employment contracts became the industry standard.[22]

2.2.2.3 Belgian Football Association v Bosman [23]

By the early 1990s, the transfer system developed by the FA was mandatory for all national football associations affiliated to the International Federation of Association Football ("FIFA"). At that stage, the transfer system still permitted clubs which held a player's registration to demand transfer fees even if a player's contract had expired.[24]

When Jean-Marc Bosman ("Bosman"), a Belgian player, refused to renew his employment contract with Belgian First Division side RC Liege, it placed him on its transfer list. But because RC Liege's desired transfer fee was too exorbitant for the interested French club Dunkerque to meet, and RC Liege were not prepared to release Bosman on free transfer, RC Liege denied Bosman the opportunity to join Dunkerque.[25]

Aggrieved by his circumstances, Bosman launched a legal challenge to the rule that disposing clubs could demand transfer fees from acquiring clubs in circumstances where a player's employment contract had expired. The court held that the right of disposing clubs to seek transfer fees in circumstances where a player's employment contract had expired unfairly limited the principle of freedom of movement.[26]

To give effect to the Bosman ruling, FIFA amended its transfer rules to permit a player to sign a pre-contract with a new club where the duration remaining on their

[20] D McArdle op cit (n5) under the heading "The post-Eastham reforms".
[21] Ibid.
[22] Ibid.
[23] (1995) C-415/93.
[24] M Marcen 'Bosman Ruling' n Marciano, A., Ramello, G.B. (eds) *Encyclopaedia of Law and Economics* (2019) Springer, New York at 144.
[25] Ibid.
[26] Ibid at 145.

employment contract with their current club was six months or less, without the requirement for the acquiring club to pay financial compensation to the disposing club. The reforms to the transfer system placed more power in the hands of players to join clubs of their liking.

2.2.2.4 Coetzee v Comitis [27]

Global developments to player transfer rules also impacted South African football, the Coetzee case was foundational in this regard. In 2000, injury-plagued 21-year-old, Andre Coetzee, sought to revive his professional career by requesting an extension of his employment contract with Ajax Cape Town Football Club ("Ajax"). After Ajax advised Coetzee that it no longer required his services, he sought to register with Hellenic Cape Town Football Club ("Hellenic").

In accordance with the National Soccer League ("NSL") rules at the time, Coetzee could not register with Hellenic, unless he obtained a clearance certificate from Ajax. Ajax were, however, not prepared to issue a clearance certificate without receiving compensation from Hellenic. And because Ajax and Hellenic could not agree on an amount of compensation, the rules stipulated that Coetzee could not register with Hellenic (or any other club) for at least 30 months from the end of the season in which his Ajax employment contract expired, or until compensation was independently determined by an arbitrator.[28]

Aggrieved by his circumstances, Coetzee instituted legal proceedings wherein he contended that the compensation regime in the NSL rules, violated the fundamental constitutional rights of players and were thus unlawful and contrary to public policy. In finding for Coetzee the court *inter alia* opined that the compensation regime, in the context of players whose employment contracts have expired, constituted a restraint of trade which was unreasonable and against public policy because it unjustifiably restricted a player's right to freedom of movement, freely choose a profession or occupation and human dignity. Accordingly, the court issued a suspended declaration of the invalidity to allow the NSL to remedy the constitutional inconsistency of their rules.[29]

[27] 2001 (4) BCLR 323 (C).
[28] *Coetzee* supra note 27 21.8.
[29] Ibid 41 and 42.

2.3 Player Transfer Regulatory Framework

2.3.1 Global Framework

FIFA is the international governing body for football, its statutes and regulations ("FIFA rules") are universally applicable. The FIFA rules regulate the rights and obligations of its member associations and the practices which all stakeholders must observe in relation to organised football. The FIFA rules are, however, drafted with an appreciation of the autonomy of its member associations, therefore specific matters are left to member associations to regulate and enforce.[30]

Player transfers is one of the matters which FIFA has sought to establish global uniformity. This, they contend, protects the sanctity and rights of players, clubs, and association football. In this pursuit, FIFA rules provide for a 'three-tier' scope to the regulation of player transfers.[31]

The first of the three is the 'international tier', in terms of which the FIFA rules are universally applicable and binding on player transfers between clubs belonging to different member associations, i.e., international transfers.[32]

Second is the 'prescribed national tier'. These rules limit the freedom of member associations to independently draft rules relating to player transfers among clubs affiliated to the same member association. For the sake of uniformity, some FIFA rules are automatically incorporated into every member association's national rules, without modifications. These rules include the player registration process, the status of players and their eligibility to participate in organised football, and the ban of third-party ownership of players' economic rights. FIFA contend that these rules prevent unfair sporting disparities between clubs belonging to different member associations, brought about by varying regulatory approaches.[33]

FIFA does, however, recognise that member associations are better placed to grasp their socioeconomic landscape, and have accordingly provided for a 'flexible national tier'. In terms thereof, the FIFA rules broadly reference principles which member associations must incorporate into their national rules; however, the member

[30] International Federation of Association Football Edition 2021 'Commentary on the Regulation of the Status of and Transfer of Players' (2021) at 16.
[31] Ibid at 13.
[32] Ibid at 14.
[33] Ibid at 14 and 15.

associations are at liberty to determine the particulars. For instance, member associations must have a mechanism to compensate clubs for training young players that graduate to professional footballers, but the structure and details are determined by each member association.[34]

2.3.2 National framework

2.3.2.1 The South African Football Association ("SAFA")

SAFA, a member association of FIFA, is responsible for the administration of South African football. SAFA's constitution and statutes ("SAFA rules") govern the affairs of its members associations. Owing to its affiliation to FIFA, SAFA incorporated specific provisions of the FIFA rules into its national rules.

Like FIFA, SAFA has opted for a tiered approach to its regulation of player transfers. The primary tier stipulates binding rules concerning the status of players, their eligibility to participate in organised football, and player transfers between clubs within the SAFA's jurisdiction, belonging to different associations.[35] The second tier rules permit a degree of flexibility for individual associations to formulate their own rules for player transfers between clubs within the association, provided that such rules provide for mechanisms to resolve disputes between clubs and players, a compensation scheme for clubs which train young players to reach professional status, and that the compulsory rules prescribed by FIFA are included without modification.[36]

2.3.2.2 The NSL

The NSL is a special member of SAFA, it is thus the only body recognised by SAFA to administer professional football in South Africa. The NSL is responsible for governing the premier soccer league ("PSL") and the national first division ("NFD"), within the confines of FIFA and SAFA rules. The NSL has published a handbook[37] ("Handbook") which incorporates its constitution and rules which deal with the status of players, the registration of players and player transfers among its member clubs. The material provisions in the Handbook relating to player transfers are as follows:

I. **player status:** a professional player is someone who has a written employment contract with a member club, in terms of which they derive remuneration from

[34] Ibid at 16.
[35] South African Football Association 'Regulations on the Status and Transfer of Players' (2011) at 3.
[36] Ibid.
[37] The National Soccer League 'The National Soccer League Handbook' (2022).

their football activity which exceeds the expenses they effectively incur from playing football;[38]

II. **player eligibility:** a player is not eligible to be registered by an NSL club unless they: (a) have never been registered with a club affiliated to any national association recognised by FIFA, (b) the registration of a player has been transferred from a club affiliated to SAFA to an NSL club, (c) the registration of a player has been transferred from one NSL club to another, (d) the registration of a player has been transferred in accordance with FIFA rules, SAFA rules, and the Handbook from a club affiliated to another national association, (e) a player's employment contract has expired or has been terminated, (f) the player has been declared a free agent, or (g) the FIFA Players' status committee has granted the player temporary eligibility to be registered by the NSL club in question;[39]

III. **player registration:** a player is not permitted to *inter alia*: (a) play for a club unless they have been registered by an NSL club in accordance with the Handbook[40], and (b) be registered with more than one NSL club or an NSL club and any other club[41];

IV. **transfers of professional players within South Africa:** the prescribed process for permanent and temporary transfer of players within the NSL is dealt with in the Handbook and described in more detail, hereunder;

V. **professional player contracts:** every NSL club employing a player must enter into a written contract with the player, and the player is only permitted to enter into the contract if: (a) they have never previously concluded an employment contract with an NSL club or any other club, (b) their previous employment contract with an NSL club has expired by effluxion of time, (c) their current contract is due to expire within six months, (d) their previous contract of employment by mutual agreement with an NSL club or any other club, (e) their previous contract of employment has been lawfully terminated; or (f) the player has been declared a free agent;[42]and

[38] Ibid rule 29.1.2.
[39] Ibid rule 30.1.
[40] Ibid rule 31.1.
[41] Ibid rule 31.4.
[42] Ibid rule 41.10.

VI. **compensation for training, development and educating of young players:** the Handbook provides for the circumstances and process under which clubs which have developed young players are due to be compensated, this is detailed further hereunder.

2.4 Types of Transfers and Fees

Thus far, I have demonstrated the progressive development of the transfer system. There have been substantial changes to the initial rules established by the FA to arrive at the modern-day transfer system. The commercial structure of player transfers has also developed, within the ambit of the transfer system, clubs have developed various structures to secure the services of players. Hereunder I shall describe the conventional player transfers structures, and special variations thereof, with reference to the applicable player transfer rules.

2.4.1 Conventional player transfers and fees

2.4.1.1 Permanent player transfers

The most prevalent player transfer entails a player permanently moving from one club to another, in exchange for a transfer fee. the Handbook stipulates that an acquiring club must approach the disposing club, before approaching the player to negotiate an employment contract, to agree the terms of the transfer.[43] If the clubs agree, they must enter into a written transfer agreement which the player must countersign. Thereafter the parties must forward the executed transfer agreement, along with the application for the transfer of the players registration, to the NSL for it to review compliance with the Handbook.[44]

Transfer agreements are typically conditional on a player passing a medical examination conducted by the acquiring club's medical personnel. The medical examination is a method of mitigating the acquiring club's risk of spending financial resources on a player who cannot fulfil the requirements of their employment contract. If a player fails the medical examination, the transfer agreement will usually fall through.[45]

Additionally, disposing clubs tend to include bonus clauses in the transfer agreement.

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[43] Ibid rule 38.1.
[44] Ibid rule 38.3.
[45] S Shah, 'What happens in a football medical' *BBC News*, 1 December 2014, available at https://www.bbc.com/news/uk-30269991 accessed on 15 November 2022.

A bonus clause typically triggers the obligation of an acquiring club to pay the disposing club a stipulated sum if a player reaches a career milestone.[46] Some examples of milestones included in transfer agreements are related to a player:

I. reaching a stipulated goal tally;

II. earning a stipulated number of appearances for their national team; or

III. winning certain individual awards or championships.

2.4.1.2 Temporary player transfers

At times, young players earn minimal playing time for their clubs due to the competitive nature of football. This can stunt a players footballing development. Accordingly, clubs often allow young players to temporarily join other clubs for an agreed, often brief, amount of time.[47]

The Handbook refers to this as a "loan transfer" and prescribes the maximum duration permitted and a process to execute these transfers.[48]To effect a loan transfer, the clubs concerned must enter into a written loan agreement which a player must countersign, and the loaning club must issue a loan certificate which must be forwarded, along with the executed loan agreement and the loan registration form, to the NSL for it to review the transaction for compliance with the Handbook.[49]

2.4.2 Special Variations

2.4.2.1 Free transfer: training compensation and solidarity contribution

On the back of the Bosman ruling, players were free to join a different club, after the expiration of their employment contract with a club, without the exchange of a transfer fee. The negative consequence of this was that clubs (specifically in Europe) were disincentivised to commit financial resources for the development and training of young player to become professionals, because they were less likely to recoup their investment.[50]

Consequently, in 2001, FIFA adopted training compensation and solidarity

[46] D Sheldon 'Transfer add-ons: What are they and why are they used' *The Athletic*,30 August 2022, available at: https://theathletic.com/3544623/2022/08/30/transfer-add-ons-what-are-they/ accessed on 15 November 2022.
[47] International Federation of Association op cit (n30) at 78.
[48]National Soccer League op cite (n37) rule 39.
[49]Ibid rule 39.3.
[50] J Douvis and T Billionis "Implications and consequences of the Bosman ruling: the case of the Greek basketball league" (2005) 40 *Turkish Journal of Sports Medicine* 4 at 160.

contribution mechanisms to incentivise clubs which develop young players. Training compensation and solidarity contributions form part of FIFA's "flexible national tier". Accordingly, SAFA adopted its own variation of training compensation and solidarity contribution which the Handbook reflects.

The Handbook stipulates that any club which registers a player between ages 12 and 21, qualifies as a training club. Training clubs are eligible to receive training compensation when a player signs their first professional contract and, when a player is a professional, on each occasion the player transfers to another club up until the player reaches age 23.[51]An acquiring club must pay training compensation whether a player transfers during or after their employment contract expires. The value of the training compensation due is a fixed amount depending on the category of the club and the amounts are determined in relation to the actual costs borne by a club to produce a player.[52]

On the other hand, and in addition to any training compensation payable, any club which registered a player between ages 12 and 23 shall receive a percentage of any transfer fee paid for the player in future transactions. The solidarity contribution is therefore not contingent on actual costs expended by a training club to develop the player, instead it ensures that every acquiring clubs compensates a training club for its early investment in a player for the duration of the player's professional career. Unlike training compensation, qualifying training clubs share the solidarity contribution on a pro-rata basis.[53]

2.4.2.2 Bridge transfers

FIFA is concerned about the growing prevalence of bridge transfers. A bridge transfer entails: (i) the transfer (permanently or temporarily) of a player on at least two occasions within a condensed timeframe; and (ii) the player not (or seldomly) playing for the club(s) which are not the first or final club in the transfer sequence. The club(s) in the middle of the transfer sequence are referred to as 'bridge clubs'.[54]

The intention behind bridge transfers is for a player to move from the first club to the final club, without the bridge club(s) deriving any sporting value from the transfer

[51] National Soccer League op cite (n37) rule 46.2.
[52] Ibid rule 48.
[53] International Federation of Association op cit (n30) at 334.
[54] Ibid at 42.

arrangement. FIFA contends that bridge transfers undermine the 'integrity and fairness of organised football'.[55] Additionally, it has also held that that bridge transfers should be forbidden because they are tantamount to an 'unlawful practice'.[56] FIFA notes that the broader objectives behind bridge transfers include:

I. **tax avoidance**: many member associations, or their revenue authorities, impose a special levy or tax on transfer fees. To entirely avoid (or reduce) the imposition thereof, the parties agree to first transfer the player to the jurisdiction of a member association where no (or significantly lower) transfer levy or tax is payable. Almost immediately thereafter, the parties transfer the player from a bridge club to the final club;[57] and

II. **avoiding the sanction on third party ownership of players' economic rights**: within the prescribed national tier, FIFA banned players or clubs from entering any agreement which entitles third-party persons (natural or juristic) to share in the compensation received for current or future transfers of players. Clubs are, however, not included in definition of a third party. Accordingly, some variations of bridge transfers entail a player joining a bridge club and thereafter immediately joining the final club upon the payment of a transfer fee. The intention is to ensure the owner of the bridge club shares in any compensation which could be payable for future transfers of the player.[58] In response to these concerns, FIFA has prescribed national tier rules which prohibit bridge transfers and incorporate a legal basis to sanction clubs and players involved in these unlawful mechanisms. FIFA has accordingly clarified that that every player transfer must be underpinned by a legitimate sporting purpose and these rules are applicable in South Africa.

2.4.2.3 Buyout provisions in a player's employment contract

The Handbook stipulates that every player must have a written employment contract with their club which adheres to 'South African Law, the Handbook, the Statues of SAFA and FIFA, and may not exceed the period of 5 (five) years, inclusive of any option to renew, from its effective date'.[59] A player and a club are therefore free to

[55] Ibid.
[56] Ibid at 43.
[57] Ibid.
[58] Ibid.
[59] South African Football Association op cite (n35) article 41.2.

agree additional terms within this regulatory framework. Accordingly, a club may incorporate a 'buyout clause'' in a player's employment contract.

A buyout clause generally stipulates the amount a club or player must pay to the disposing club as compensation for early termination of a player's employment contract. The buyout amounts are often exorbitant to deter other clubs from activating it, yet it also ensures that if a party pays the amount, a club cannot frustrate the professional ambitions of a player should a different club wish to acquire their services on better terms. Accordingly, when a party triggers a players buyout clause, the employment contract terminates (in accordance with its terms) and the player is free to register and sign an employment contract with a different club.[60]

2.4.2.4 Buyback provisions in transfer agreements

A buyback clause is a mechanism incorporated in a transfer agreement to allow a disposing club to re-acquire a player from the acquiring club. A buy-back clause takes one (or a combination) of the following forms:

I. **option to purchase**: the clubs agree a pre-determined transfer fee which the disposing club must pay at a predetermined future date. Once the clause is triggered, the player is free to negotiate an employment contract with their former club;[61] and

II. **right of first refusal**: if the acquiring club accepts a transfer bid for the player from another club in future, the acquiring club must accept the disposing clubs transfer bid if it matches the offer. Thereafter, the disposing club is granted the right to negotiate an employment contract for the player to re-join them.[62]

[60] M Tatraeva ''Buyout-out clauses in football contracts' *iLaw*, available at: https://www.ilaw.co.uk/news/buy-out-clauses-in-football-contracts , accessed on 15 November 2022.
[61] D Geey "Football Transfers: Buy-Back Clauses Explained" *The Final Score on Football Law*, available at: https://www.danielgeey.com/post/football-transfers-buy-back-clauses-explained/ , accessed on 17 November 2022.
[62] Ibid.

CHAPTER 3 - PRINCIPLES A SOUTH AFRICAN TAX LAW SYSTEM

3.1 Contextual Background

3.1.1 General

The South African government requires financial resources to fulfil its mandate to provide public services and promote economic growth. In the main, government generate their budget through imposing taxes on natural and juristic persons. In 2001, South Africa adopted the residence basis for taxation. In terms of this, resident taxpayers are taxed on their worldwide income, whilst non-resident taxpayers pay tax on income from or deemed to be sourced from South Africa.

This chapter includes legislative and case law references as are relevant to the analysis undertaken in Chapter 4. Chapters 3 and 4 have been structured in this way to allow a more short-hand analysis to be conducted in Chapter 4 given the word constraints of this dissertation.

3.1.2 Fundamental sources of tax law

Legislation and common law are fundamental sources of tax law. The Income Tax Act is the pillar of the fiscal legislative scheme. Over time, the courts have used their authority to interpret legislation, to supplement the Income Tax Act with common law principles. Accordingly, all taxpayers must afford meaning to the Income Tax Act with reference to common law principles.

3.1.3 Type of taxes considered

The Income Tax Act provides for the imposition of various taxes, this paper limits itself to the consideration of normal tax.[63] Normal taxes are determined annually in accordance with a calculation wherein the taxpayer must include into their gross income, the taxable portion of their capital gains and exclude allowable deductions and exempt receipts to arrive at their taxable income.

3.1.4 Interpretation of tax legislation

3.1.4.1 Approach to interpretation

The Constitution[64] mandates the legislature to pass legislation,[65] and where there is a

[63] "Normal tax" refers to the income tax imposed on all persons (natural and juristic) in accordance with the Income Tax Act. For the purpose of this paper it includes business income and capital gains/losses.
[64] The Constitution of the Republic of South Africa, 1996.
[65] Ibid section 44 (1)(a)(i).

dispute as to the meaning of a provision in the legislation, it authorises the courts to provide a binding interpretation of the meaning of the provisions before them.[66] Over decades South African courts have continuously refined their approach to statutory interpretation.

Initially, the South African courts' approach to statutory interpretation was largely influenced by the English courts' approach of strictly adhering to the principle of parliamentary sovereignty. Accordingly, South African courts promoted a 'literal approach' when interpreting tax legislation, no matter the absurdity of the outcome.[67] To this end in *Cape Brandy Syndicate v Inland Revenue Commissioners*,[68], the court stated that:

> *'In a taxing Act one has to look merely at what is clearly said. There is no room for any intendment. There is no equity about a tax. There is no presumption as to a tax. Nothing is to be read in, nothing is to be implied'*[69]

As their English counterparts changed tact, so too the South African courts progressively embraced a contextual approach to interpreting legislation. In terms thereof, the courts only deviated from the literal approach where they believed not doing so would result in an outcome not intended by the legislature. When a court confronted these circumstances, the 'golden rule' was for it to apply a restrictive interpretation or to modify the words or phrase of a provision to give effect to the intention of the legislature.[70]

The courts have only recently veered from merely giving effect to the literal meaning of statutory provisions with reference to the intention of legislature, in favour of a 'purposive approach'. Although the purposive approach incorporates elements of the literal approach, it instructs courts to consider provisions of contracts and legislation in the context which they were concluded. In the case of *Natal Joint Municipality Pension Fund v Endumeni Municipality*,[71] the Supreme Court of Appeal (SCA) prescribed the following guide to statutory interpretation for courts:

I. statutory interpretation is an objective process for which the starting point is the text of the provision;

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[66] Ibid chapter 8.
[67] D French and R Stretch 'Income Tax in South Africa' (2022) *Lexis Nexis* at 2.1.
[68] [1921] 1 KB 64.
[69] Ibid at 71.
[70] D French and R Stretch op cite (n66) at 2.1.
[71] 2012 (4) SA 593.

II. the text of any provision must be interpreted within the context of the entire document and the circumstances of its conclusion, ordinary rules of grammar and syntax, the 'apparent' purpose and all the materials known to the drafter; and

III. the result of the interpretive process must not be unbusinesslike or undermine the 'apparent' purpose. [72]

In *Commissioner of for South African Revenue Service v Bosch*[73] the SCA confirmed that courts are required to follow the purposive approach when interpreting tax legislation. The dispute in this matter was about the interpretation of a provision in the Income Tax Act that provided that any gain made by a taxpayer from the exercise, cession, or release of any right to acquire a marketable security must be included in their taxable income. The question before the court was whether the provision was triggered when the taxpayer exercised the option to acquire shares or when payment and delivery were due. In finding for the taxpayer the court interpreted the purpose of the provision with reference to surrounding circumstances, which included the consideration of an explanatory memorandum for the subsequent amendment of the provision and the way SARS has previously interpreted the provision in question.[74]

3.1.4.2 SARS interpretation and practice notes ("Guides")

Periodically SARS publishes interpretation notes to give guidance to taxpayers on how it interprets specific tax provisions. Although these are not binding, courts have dubbed interpretation notes as a persuasive and useful reference in their process of interpreting tax legislation.[75]It appears, however, that the Constitutional Court have brought this practice to a halt. In the case of *Marshall v Commissioner for the South African Revenue Service,*[76] the Constitutional Court questioned the value of relying on the unilateral practice adopted by the executive arm of government in what is supposed to be an objective and independent interpretation of legislation by the

[72] Ibid at 18.
[73] [2015] 1 All SA 1 (SCA)
[74] E Brinker 'Interpretation of fiscal legislation' (2014) available at: https://www.cliffedekkerhofmeyr.com/en/news/publications/2014/tax/tax-alert-28-november-interpretation-of-fiscal-legislation.html , accessed on 17 November 2022.
[75] For instance, in the ITC1572 (1993) 56 SATC 175 at 186 the court stated that "*Departmental practice is not necessarily, of course, an indication of what the law means. However, it seems to me that the departmental practice is a very sensible approach to what should be done in this type of case. Plainly the procedure and the practice laid down by the Commissioner in that regard, is, if nothing else, commercial wisdom and good sense*"
[76] 2018 (7) BCLR 830 (CC).

judiciary.[77] It is not clear what effect this will have on the purposive approach in terms of which courts are encouraged to consider the historical context in which legislation was adopted, which may include the interpretation notes. It is nonetheless true that interpretation notes still have value for a taxpayer to have insight into SARS' reading of specific tax provisions.

3.2 Taxable Income: Gross Income

A company must calculate its taxable income in accordance with the Income Tax Act. This subsection shall discuss the components of the calculation applicable to this paper.

3.2.1 Gross Income

3.2.1.1 General

Determining gross income is the first step of the income tax calculation. Accordingly, this subsection stipulates the key requirements for a receipt to fall under the gross income definition in section 1 of the Income Tax Act. For convenience, the straightforward requirements are briefly dealt with in the list hereunder. The complex requirements, which require further elaboration as they constitute the basis of the analysis in chapter 4 of this paper, are dealt with in the following subsections.

The following components must be satisfied for a receipt to be included in a taxpayer's taxable income in terms of section 1 of the Income tax Act:

I. **an amount in cash or otherwise received in favour of a taxpayer within a defined period**: measurable monetary amounts, or receipts which have monetary value,[78] received or accrued within any year or period of assessment fall under gross income.

II. **resident**: if a person is tax resident in South Africa they are taxed on their worldwide income, if are they non-resident for tax purposes they are only liable to be taxed on income sourced or deemed to be sourced from South Africa. A Company is tax resident if incorporated in South Africa.

III. **received or accrued:** this requirement relates to the timing and is dealt with in detail hereunder.

IV. **non-capital receipts:** capital receipts, other than those specifically included, are excluded from gross income. With the introduction of Capital Gains Tax

[77] Ibid 10.

[78] *WH Lategan v Commissioner for Inland Revenue* (1926) SATC 16 at 19; this principle was also later confirmed in *Commissioner for Inland Revenue v Delfos* (1933) 6 SATC 92 at 99.

("CGT"), however, a certain portion of the taxable gain is included in a taxpayer's taxable income.[79]

3.2.1.2 Receipt and accrual basis

The amounts which must be in included in gross income are not necessarily synonymous with profits or gains, they are a statutory invention. In this regard the Income Tax Act provides that any amount received by or accrued to a taxpayer must be included in its gross income.

The receipts basis for the inclusion of amounts under gross income is straightforward. In the case of *Geldenhuys v Commissioner for Inland Revenue*[80] the court interpreted the words 'received by' to mean that any amount to be included under gross income must be 'received by the taxpayer on their own behalf for their own benefit'.[81]

On the other hand, the accrual basis for the inclusion of amounts under gross income is complex because it entails the tax consideration of an amount which the taxpayer is yet to receive, and only has a right to claim at a future date. Of course, this raises the question of the timing: should the taxpayer include the amount in their gross income when the right to claim the amount accrues or when it is due for payment. This question is complicated further when the right to claim an amount and the due date for payment arise in different years of assessment, or when a portion of the amount is paid in one year of assessment and the balance thereof in another.

In *WH Lategan*, the court interpreted the meaning of 'accrue to' to be the date when a taxpayer becomes entitled to claim an amount.[82] Accordingly, a taxpayer needed to declare the full amount in the year of assessment which it acquired the right to claim the amount, notwithstanding that the full amount or a portion thereof would be due for payment in a subsequent year of assessment. The legal principle established in *WH Lategan*, was settled law after the court in *Commissioner for Inland Revenue v People's Stores (Walvis Bay) (Pty) Ltd*[83] stated that:

> '*The pith of the supporting reasoning is that any right (of a non-capital nature) acquired by the taxpayer during the year of assessment and to which a money value can be attached, forms part of the 'gross income' irrespective of whether it is immediately enforceable or not.*'[84]

[79] Section 26A of the Income Tax Act.
[80] (1947)14 SATC 419.
[81] Ibid at 430.
[82] *WH Lategan* supra (n78) at 20.
[83] (1990) 52 SATC 9.
[84] Ibid at 22.

The *WH Lategan* principle faces difficulty, however, in a commercial context where contractual rights are at times contingent on the occurrence of an uncertain future event. Accordingly, in *Mooi v Secretary for Inland Revenue*,[85] the court held that a contingent right conditional upon the fulfilment of certain conditions does not constitute a taxable amount, even though it has a monetary value on receipt by or accrual to the taxpayer.[86] To this end the court in *Income Tax Case No 76*[87] distinguished a vested and contingent right as follows:

> *'A vested right was something substantial; something which could be measured in money; something which had a present value and could be attached. A contingent interest was merely a spes – an expectation which might never be realized. From its very nature it could not have a definite present value. In the income tax sense, therefore, a vested right was an accrued right.'*[88]

Accordingly, an amount accrues to a taxpayer if they are unconditionally entitled to claim it and it has not yet been received. However, if an amount is conditional on the occurrence of a future uncertain event, there is no accrual until the fulfilment of those conditions.

3.2.1.3 Capital or Revenue

In terms of the Income Tax Act, it is important to identify the nature of the any amount received by or accrued to a taxpayer because receipts which are capital in nature are generally excluded from gross income. And although the onus falls on the taxpayer to prove that an amount is of a capital nature, the Income Tax Act does not define the concept of a capital receipt. Accordingly, the courts have developed guidelines to distinguish revenue receipts (which are to be included under gross income) from capital receipts. One of the most authoritative yet simple guides given by the court was in the *Visser v Commissioner for Inland Revenue*[89] case, wherein the court opined that 'íncome is what capital produces, or something in the nature of a fruit as opposed to principal or tree.'[90]

The instances in which capital receipts must be distinguished from revenue receipts include when a taxpayer disposes an asset, receives compensation, employs capital

[85] (1972) 34 SATC 1.
[86] Ibid at 11.
[87] (1927) 3 SATC 68 (U).
[88] Ibid at 70.
[89] (1937) 8 SATC 271.
[90] Ibid at 276.

and or receives government grants. This paper limits itself to dealing with the instances where a taxpayer disposes an asset or receives compensation as these are relevant to preface the discussion under chapter 4.

3.2.1.3.1 Disposal of an asset

Where a taxpayer has sold an asset, the courts apply the 'intention test' to the determine the nature of the proceeds from the sale. This entails a court ascertaining whether a taxpayer sold its asset with the intention to realise a profit in a 'scheme of profit making' or whether they were merely realising a capital investment.[91] If the former is true, the amount constitutes a revenue receipt, and in the case of the latter being true, the amount constitutes a capital receipt.

To ascertain a company's intention a court will look to the intention of its directors, majority shareholders, management team and/or its investment committee.[92] In this pursuit, a court would typically look to documents such as board resolutions, company reports, correspondence, minutes of meetings, public statements, and memorandums of incorporation. Courts adopt a balanced approach when assessing a taxpayer's subjective evidence, because its prone to manipulation, by weighing it against objective considerations.[93]

Courts appreciate that its possible for a taxpayer to change their intention. For instance, a taxpayer could have acquired an asset as capital investment and subsequently sell the asset in a scheme of profit-making. To ascertain a change in intention, courts look at the taxpayer's intention with the asset wholistically. The cases discussed hereunder illustrate the prescribed approach:

I. **Commissioner of Inland Revenue v Stott:**[94] In this case the taxpayer purchased costal land for the purpose of constructing a private residence and a farm which was subject to a long-term lease. The taxpayer subsequently subdivided the properties into lots and sold them off at a profit over a 4-year period. The revenue authority included the proceeds from the sales in the taxpayer's gross income and the taxpayer unsuccessfully challenged the decision in the tax court. The court of appeal reversed the tax court's ruling and

[91] This principle is elaborated on when discussing the case of *Stott* case hereunder.
[92] *Commissioner for Inland Revenue v Richmond Estates (Pty) Ltd* (1956) 20 SATC 355 at 361; *Secretary for Inland Revenue v Trust Bank of Africa Ltd* (1975) 37 SATC 87 at 102.
[93] T Legwaila *Tax Law: an Introduction (2019)* 2 Juta and Company, Cape Town at 88.
[94] (1928) 3 SATC 253.

stated that merely subdividing the property and selling it off in lots was not sufficient to change the nature of the proceeds. Importantly, the court affirmed that every person is entitled to realise their asset to the best advantage and adapt to the fluctuations in the market, and that doing so was not necessarily embarking on a scheme of profit-making.[95] Accordingly, the court held that the proceeds were of a capital nature and cannot be included in the taxpayer's taxable income.

II. **Natal Estates v Secretary for Inland Revenue:**[96] In this case the taxpayer was a public company in the sugar business. Over the years it had acquired vast pieces of land and for varying reasons sold many of its properties over a five-year period. The revenue authority had included the proceeds from all the sales in the taxpayer's gross income. In dismissing the taxpayer's appeal and the revenue authority's cross-appeal, the court confirmed the ruling of the court-a-quo, importantly its decision to determine the tax treatment of each sale on its own merits. The court held as follows regarding each transaction:

    a. The first property was coastal land which the board of directors decided to develop into a township. In this pursuit, the company sought the services of skilled professionals whereafter it sold individual lots to members of the public and in bulk to property development companies. The taxpayer argued it was merely realizing the value of its capital assets to best advantage. The court disagreed and held that the taxpayer had "crossed the rubicon" because it had embarked on an expansive property business venture, and accordingly the proceeds generated were of a revenue nature.[97]

    b. The second property was a smaller area of land which the taxpayer subdivided and sold to members of the public, including the taxpayer's employees. The court confirmed the court-a-quo's finding that in the absence of sufficient evidence the proceeds constitute revenue receipts, because the taxpayer failed to satisfy its onus to prove the proceeds were of a capital nature.[98]

[95] Ibid at 261.
[96] (1975) 4 All SA 375 (A)
[97] Ibid at 393.
[98] Ibid at 394.

c. The third sale entailed the taxpayer selling inland properties after the government indicated its decision to expropriate the properties. The court distinguished these transactions from the sale of the first property because, because the taxpayer sold the properties for reasons beyond its control. Consequently, the court held these proceeds to be capital in nature.[99]

III. **John Bell & Co (Pty) Ltd v Secretary for Inland Revenue:**[100] In this case, the taxpayer conducted a business from an industrial property in Johannesburg. After it discontinued its business, the board of directors resolved to retain the property for the purpose of selling it at a large profit when the property market in the area had improved. When the taxpayer eventually sold the property, the revenue authority included the sale proceeds in the taxpayer's gross income. The tax court upheld this decision on the basis that the taxpayer had changed its intention when deciding to retain the property to realise a greater profit in future. The court of appeal reversed the decision and held that the mere fact that a taxpayer intentionally delays the sale of an asset because of unfavourable market conditions does not change the nature of the asset from a capital asset to stock in trade.[101] Accordingly, the court ordered the revenue authority to exclude the proceeds from the taxpayer's gross income.

The courts acknowledge that it is possible for a taxpayer to have more than one intention when selling an asset. Under these circumstances, a court must give preference to the taxpayer's dominant intention. To this end, in *African Life Investment Corporation (Pty) Ltd v Secretary for Inland Revenue*[102] the court stated that:

> *"Whether or not a purpose is dominant in the sense that another co-existing purpose may be effected at a profit without attracting liability for tax, is a matter of degree depending on the circumstances of the case. A purpose may be a main purpose without being dominant in this sense. I shall not attempt a precise definition of the distinction, but there would, I consider, be such a main purpose where there is a further purpose simultaneously pursued by way of an additional, albeit subsidiary activity calculated and intended to yield a profit."*[103]

Accordingly, the enquiry to identify the dominant purpose for the sale of asset is a

[99] Ibid at 400.
[100] (1976) 38 SATC 87.
[101] Ibid at 105.
[102] (1969) 4 All SA 243 (A)
[103] Ibid at 248.

matter of degree. Other motivations behind the sale, although material or contemplated by the taxpayer, should not be at the forefront of the taxpayer's mind. The mere fact that a taxpayer contemplates realising a profit through the sale of asset, should not tilt the scale in favour of treating proceeds received from the sale as a revenue receipt.

3.2.1.3.2 Compensation

3.2.1.3.2.1 General

When a taxpayer receives an amount for compensation in relation to their business, it should be asked whether such amount constitutes revenue or capital for tax purposes. To ascertain this one must take the following two-steps process:

I. Establish whether the compensation is intended to fill a hole in the taxpayer's capital assets or profits.[104] If the former applies the compensation would constitute capital asset, but if the latter applies it would constitute revenue receipt.

II. If the compensation appears to constitute a capital asset, one must take the additional step of establishing the true nature of the capital asset in the taxpayers' hands.[105]

Furthermore, to ascertain the true nature of the compensation one must establish the intention of both the payer and recipient. It is important to note, however, that it is possible for the compensation to be of a capital nature in the hands of the recipient and a deductible revenue expenditure in the hands of the payer.[106]

3.2.1.3.2.2 Early termination of a contact

Compensation received for the early termination of a contract, is particularly relevant to preface the discussion in chapter 4 of this paper. The general legal position is that where compensation is received as an award for the termination of a contract, which composed a sizeable portion of the taxpayer's business structure, the amount would be capital in nature. However, if the amount was received as compensation for the loss of the taxpayer's future profits it will generally constitute revenue.[107]

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[104] *Burmah Steamship Co Ltd v Inland Revenue Commisioners* (1931) SC 156; *Taeuber and Corrsen (Pty) Ltd v Secretary for Inland Revenue* (1975) 37 SATC 129 at 136-7.
[105] *Estate AG Bourke v Commissioner for Inland Revenue* (1991) 4 All SA 94 (AD) at 98.
[106] *Income Tax Case 1310* (1979) 42 SATC 177 at 180.
[107] These principles are elaborated on in the cases discussed hereunder.

Determining the true nature of an amount paid in compensation for the termination of a contract is a question of circumstance and degree.[108] The following cases demonstrate this, and the nuances involved in this process:

I. **Income Tax Case 1259**: in this case a trust company providing *inter alia* property administration services received compensation from a client for the premature cancellation of a management contract. Ordinarily, amounts flowing from a contract of this nature (a commercial agreement intricately linked to a taxpayer's profit-generating activities) would be considered revenue in nature. In this matter, however, the court held that the compensation constituted capital in the hands of the taxpayer because it was intended to provide relief for their loss of a permanent and substantial part of its income-producing structure.[109]

II. **WJ Fourie Beleggings v Commissioner for the South African Revenue Service:**[110] in this case, the taxpayer (a hotelier) signed a contract in terms of which it agreed to reserve most of its hotel rooms for the exclusive use of a company, for a period of more than two years. The taxpayer anticipated generating R8.7 million from this deal. The company repudiated the contract, and the taxpayer received a settlement amount of R1.3 million as compensation for early termination thereof. In finding for SARS, the court held that the compensation was a revenue receipt because it stemmed from the taxpayer's usual income-earning activities.[111] The court's finding was premised on the distinction between contracts from which from the fundamental basis from which the taxpayer generated income and contracts directed by its performance towards making a profit.[112] Accordingly, the court concluded that the lease of the hotel and the use to which it was put was the taxpayers capital assets, however, this did not include contract in question.[113]

III. **Stellenbosch Farmers' Winery Ltd v Commissioner for the South African Revenue Service**[114]**:** in this case, the taxpayer, which carried on the business of producing and importing a range of liquor products, had signed a contract

[108] *Income Tax Case 1259* (1976) 39 SATC 65 at 68.
[109] Ibid at 71.
[110] (2009) JOL 23375 (SCA)
[111] Ibid at 13.
[112] Ibid at 11.
[113] Ibid at 13.
[114] (2012) 74 SATC 235.

with a company to attain the distribution rights for a foreign whiskey in South Africa. For commercial reasons, the company prematurely terminated the distribution contract (which was due to run for at least three more years), and the taxpayer consequently received R67 Million in compensation in terms of a termination agreement. In finding for the taxpayer the court held that the compensation was a capital receipt because it was an award for the closing down of a sizeable portion of the taxpayer's business.[115]

Accordingly, notwithstanding the factual similarities[116] of these cases, the outcomes were premised on the respective commercial circumstances. The taxpayers in *Stellenbosch Farmers'* and Income *Tax Case 259* relied on rights flowing from the contracts to realise new commercial opportunities, accordingly the compensation stemming from the early termination of the respective contracts was held to constitute capital. To the contrary, and notwithstanding the significance of its negative commercial impact on the taxpayer's business, the early termination of the contract in *WJ Fourie Beleggings*, did not decimate the taxpayer's right realise new commercial opportunities.

3.3 Taxable Income: Deductions

After a taxpayer has determined its gross income, the Income Tax Act allows for the deduction of qualifying expenses from taxable income. In this regard, section 11 (a) of the Income Tax Act provides for a general deductions formula. I deal with the requirements required to claim a deduction in terms of section 11 (a) of the Income Tax Act hereunder.

3.3.1. General deductions formula

Section 11 (a) of the Income Tax Act allows a taxpayer to deduct expenditure incurred in the production of the income, provided that such expenditure is not of a capital nature. I deal with each of the elements of this test hereunder.

3.3.1.1 Expenditure

The word 'expenditure' is not defined in the Income Tax Act. Accordingly, the courts have given meaning thereto. In the case of *Commissioner for the South African*

[115] Ibid at 248.
[116] In all these cases the taxpayers received monetary compensation for the substantial loss of future revenue, related to the early termination of a long-term contract.

Revenue Service v Labat Africa Ltd[117] the court opined that expenditure refers to the 'action of spending funds, disbursement, or consumption'.[118] Accordingly, to satisfy this leg of the test all that needs to be demonstrated is a reduction in the value of the taxpayers' assets.

3.3.1.2 Actually incurred

A taxpayer can only deduct expenditure which is incurred in the year of assessment. Whether the expenditure was objectively necessary or extravagant has no bearing in the enquiry, it must only be demonstrated that the amount was actually incurred. It is straightforward to demonstrate that an expense was incurred where a taxpayer pays for a good or service within the same year the deduction is claimed. Where goods or services are, however, acquired or rendered but not paid for within the same year of assessment, the matter is complex.

In *Port Elizabeth Electric Tramway Company Ltd v Commissioner for Inland Revenue*[119] the court interpreted the term 'actually incurred' as follows:

> *'But expenses "actually incurred" cannot mean that the taxpayer has actually paid the liability in question. So long as the taxpayer has an unconditional liability to incur the expenditure it will be deductible."*[120]

Accordingly, a taxpayer needs only to demonstrate that it has an unconditional liability, not that it was actually paid. For instance, in the case of *Nasionale Pers Bpk v Commissioner for Inland Revenue*,[121] the taxpayer's remuneration policy stipulated employees who were in the employ of the company on 31 October would qualify to receive a bonus on 30 September of the following financial year. The taxpayer claimed the bonuses as a deductible expense at the end of its financial year on 31 March. The revenue authority rejected the deduction of the bonus payments on the basis that a bonus was contingent on an employee being in the employ of the company on 31 October. The court upheld this decision on the ground that an uncertain future event that remains uncertain at year end meant that the expenditure was not 'actually incurred.'[122]But for the condition in the taxpayer's policy, the claim would have been allowed.

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[117] (2011) JOL 27986 (SCA).
[118] Ibid 12.
[119] (1936) 8 SATC 13.
[120] Ibid at 15.
[121] (1986) 48 SATC 55
[122] Ibid at 68.

3.3.1.3 In the Production of Income

A taxpayer can only claim a deduction if the expense is incurred to produce income. In the case of *Port Elizabeth* the court established a two-step enquiry to determine whether an expense is incurred in the production of income:

I. the business operation to which the expenditure is attached must be performed in the production of income. A business operation will be regarded as being performed in the production of income if it is performed *bona fide* for the purpose of carrying on the trade which earns the income; and

II. the expenditure must be so closely linked to the business operation that it can be regarded as part of the cost of performing it. If it is so closely linked, it does not matter if is necessary, if it is attached by chance, or *bona fide* incurred.[123]

In the case of *Port Elizabeth*, the taxpayer (which conducted a tramway business) had claimed a deduction for compensation paid to the widow of a driver who had died in a collision in the course of his employment. Applying the test above, the court allowed the deduction on the ground that the employment of drivers was inextricably linked to the taxpayer's business, and so too was the risk of potential liability to pay compensation for drivers injured in the course of their employment.[124] Accordingly, the payment for compensation was deemed to be in the production of income.

3.3.1.4 Not of a Capital Nature

3.3.1.4.1 General

In terms of section 11 (a) of the Income Tax Act, taxpayers are not permitted to deduct their taxable income by claiming capital expenses. Capital expenses are, however, not defined in the Income Tax Act. Accordingly, the courts have provided guidelines to distinguish capital expenses from revenue expenses. The guidelines are not always useful; therefore, each matter should be considered on its own merits. To this end, in the case of *New State Areas Ltd v Commissioner for Inland Revenue*[125] the court stated that:

> *'The conclusion to be drawn from all these cases seems to be that the true nature of each transaction must be enquired into in order to determine whether the expenditure attached to it is capital or revenue expenditure. Its true nature is a matter of fact and the purpose of the expenditure is the important factor; if it is incurred for the purpose of acquiring a capital asset for*

[123] *Port Elizabeth* supra note 119 at 16
[124] Ibid 18 and 19.
[125] (1946) AD 610.

the business it is capital expenditure even if it is paid in annual instalments; if on the other hand it is in truth no more than part of the cost incidental to the performance of the income producing operations, as distinguished from the equipment of the income producing machine then it is a revenue expenditure even if it is paid in a lump sum."[126]

Accordingly, to ascertain the nature of an expense one must first ascertain the taxpayer's motive for incurring the expense, and if such motive is closely linked to the income-producing structure of the taxpayer the expense should constitute a capital expense. Alternatively, if the motive for incurring the expense is closely linked to the income-producing operations the expense should constitute a revenue expense. Put differently, capital expenditure is directed at enhancing a taxpayer's profit-generating capacity, whilst revenue expenditure is directed at the taxpayer's day-to-day profit generating operations.

There are objective and subjective elements to the test. This is so because courts are required to consider both the purpose of the expenditure and then objectively assess the proximity of such expenditure to the taxpayer's income- producing structure and income-producing operations.

To ascertain the motives behind expenditure and their proximity to the taxpayer's income-producing structure, the courts have borrowed some tests devised in the UK. One of these is the 'enduring benefit' test.[127] In terms thereof, a court assesses whether the taxpayer incurred an expense for the purpose of acquiring an enduring asset or advantage. If so, the expenditure is deemed to be closely linked to its income-producing structure, and therefore a capital receipt.

3.3.1.4.2 Cases dealing with expenditure

The section above covered the general principles for the distinguishing capital expenditure. This section briefly illustrates how the courts have applied these principles in scenarios which are relevant for this Paper:

I. **contractual compensation:** where compensation is paid in accordance with a contract it is complex to identify if it constitutes capital or revenue expenditure. In *Nchanga* a mining company paid monthly compensation to another mining company (within the same group of companies), in accordance with a contractual clause, as consideration for the latter company ceasing production for a year. The court held that the amount did not constitute capital expenditure

[126] Ibid at 627.
[127] *Commissioner of Taxes v Nchanga Consolidated Copper Mines Ltd* (1964) 26 SATC 37 at 42.

because the taxpayer did not acquire a corresponding enduring right.[128] For instance, the company which paid the compensation did not inherit supply contracts for customers, they just ceased trading, accordingly the expenditure was held to have not altered the taxpayer's incoming-earning structure.[129]

II. **exclusive license fee (once-off):** In *Income Tax Case 1063*[130] the taxpayer claimed a tax deduction for several payments made to a foreign company to acquire exclusive distribution rights of gramophone records in South Africa, for a period of three years (with an option to renew for a further period of two years). The court upheld the revenue authority's decision to exclude the expense on the ground that the taxpayer incurred the expense with the motive to gain an enduring benefit, and it was therefore capital expense.[131]

III. **exclusive license fee (recurring):** In *Commissioner for South African Revenue Service v Kajadas Cosmetics (Pty) Ltd*[132] the taxpayer had acquired exclusive distribution rights of beauty products within South Africa, for a renewable period of five years. In exchange, the taxpayer paid an annual license fee. Notwithstanding the recurring nature of the taxpayer's payments, the court stated that the exclusive rights flowing from the distribution agreement created an 'income earning machine.'[133] Accordingly, the court held that the recuring payments constituted capital expenditure.

IV. **non-exclusive license (once-off and recurring):** In *Income Tax Case 1726*[134] a taxpayer was granted a non-exclusive license to construct, operate and maintain a nationwide cellular radio telephone service. The taxpayer claimed as a taxable deduction the initial payment made to obtain the renewable license of 15 years and the ongoing annual license fee payable. The court held that the upfront payment provided an enduring benefit and was incurred to enhance the taxpayer's income-earning structure, and therefore constituted capital expenditure. But, the court stated, the ongoing license fee was recurrent expenditure which the taxpayer incurred to keep the advantage of the initial

[128] Ibid at 44.
[129] Ibid at 46.
[130] (1964) 27 SATC 57.
[131] Ibid at 59.
[132] (2002) 64 SATC 200.
[133] Ibid 203.
[134] (2000) 64 SATC 236.

payment, and it was accordingly, revenue in nature.[135]

V. **non-exclusive license (once off):** In *Commissioner for South African Revenue Service v I-Net Bridge (Pty) Ltd*[136] the taxpayer, which conducted the business of distributing financial market information, acquired a five-year license to access an electronic content, data and information feed managed by a foreign company. The taxpayer claimed the license fee as a taxable deduction. Notwithstanding that the license fee was a once-off payment, the court held that the true nature of the expenditure was for the acquisition of data, being the taxpayer's 'trading stock,' and therefore revenue in nature.[137]

The cases mentioned above illustrate that the courts deal with each matter on its own merits. It matters not whether the expenditure is incurred in instalments or once-off, the material inquiry is the reason for the expenditure and nature thereof with reference to a taxpayer's business activities.

3.4. Taxable Income: Capital Gains Tax ("CGT")

3.4.1 General

Before 2001, taxpayers were not liable to pay tax on their capital receipts or accruals because they were specifically excluded from the definition of gross income in the Income Tax Act. However, in 2001 the Income Tax Act was amended to provide that the taxable income of a person must include any taxable capital gains for a year of assessment calculated in accordance with the Eighth Schedule of the Income Tax Act ("the Schedule"). The word 'capital' is not defined in the Income Tax Act and is thus defined in accordance with the basic income tax principles. Accordingly, the proceeds from the disposal of an asset can only be subject to CGT if deemed to be of a capital nature.

3.4.2 Prerequisite requirements

For a taxpayer for incur CGT it must dispose of an asset during the year of assessment. An 'asset' is defined to include property of whatever nature, including tangible and intangible, and rights or interests of whatever nature to or in such property.[138] Furthermore, a disposal is defined as any event, act, forbearance or

[135] Ibid at 242.
[136] (2010) 73 SATC 141.
[137] Ibid 147.
[138] Paragraph 1 of the Schedule.

operation of law that results in the creation, variation, transfer or extinction of an asset.[139] If a disposal is not subject to a suspensive condition, it is deemed to occur on the effective date of an agreement.[140] However, If the disposal is subject to a suspensive condition, it is deemed to occur on the date upon which the condition is fulfilled.[141]

3.3.3 Steps to calculate a company's CGT liability

The first step in the calculating CGT is to determine the proceeds from the disposal. An amount in cash or in kind received or accrued to a taxpayer, during a year of assessment, will constitute the proceeds received. An amount is deemed to have accrued to the taxpayer only if they have an absolute entitlement to receive it, notwithstanding that it is only due for payment in future.[142]

The following step is to deduct the base cost of the asset from the proceeds. The base cost composes of expenditure actually incurred in acquiring or creating the asset, or expenditure that is deemed to be incurred in acquiring the asset.[143] These include:

I. the purchase price for the asset;
II. professional fees; and
III. improvements or enhancements to the asset.[144]

Importantly, expenditure which a taxpayer claimed as a taxable deduction[145] and incurred for maintenance of an asset[146], are explicitly excluded from the base cost calculation.

After the base cost has been subtracted from the proceeds from the disposal, a taxpayer shall either arrive at a net capital gain or loss. If a taxpayer realises a capital gain it must be included their taxable income at 80 per cent of the value. If a taxpayer arrives at a net capital loss, the amount must be carried into the following year and can be set off against future capital gains.

3.5. Anti-Avoidance Rules

If a taxpayer's receipts or accruals fall outside the charging provisions of

[139] Paragraph 11 of the Schedule.
[140] Paragraph 13 (a)(ii) of the Schedule.
[141] Paragraph 13 (a)(i) of the Schedule.
[142] Paragraph 35 (4) of the Schedule.
[143] Paragraph 20 (1) (a).
[144] Paragraph 20 (1)(e).
[145] Paragraph 20 (3) (a) (i).
[146] Paragraph 20 (2) (b).

the Income Tax Act, no tax liability in relation thereto can be imposed. Some taxpayers strive to arrange their commercial transactions in a manner which escapes, reduces, or defers their tax liability, these actions are known as 'tax avoidance'. In the English case of *Duke of Westminster v Inland Revenue Commissioner*[147]the court famously stated that:

> "*Every man is entitled if he can to order his affairs so that the tax attaching under the appropriate Acts is less than it otherwise would be. If he succeeds in ordering them so as to secure this result, then, however unappreciative the Commissioners of Inland Revenue or his fellow-taxpayers may be of his ingenuity, he cannot be compelled to pay an increased tax*."[148]

Although legal, tax avoidance has attracted criticism because it reduces the resources flowing to the national fiscus. At times aggressive tax avoidance borders on tax evasion. Accordingly, the judiciary and the legislature have derived measures to counter tax avoidance. In this section I define tax avoidance and discuss the judicial and legislative measures to curb its effects.

3.5.1 Distinction between tax avoidance and tax evasion

It is important to distinguish the often-conflated concepts of tax avoidance and tax evasion. On the one hand, tax avoidance refers to *prima facie* lawful strategies to escape, reduce or defer tax liability.[149] On the other, tax evasion is the inherent unlawful methods of escaping tax liability such as simulated or disguised transactions. It is possible, however, for a taxpayer's tax avoidance strategy to be subsequently found to be unlawful. This tends to occur when taxpayers devise complex strategies to take advantage of loopholes in imperfectly drafted tax legislation.

3.5.2 Common law anti-avoidance methods

Before anti-avoidance provisions were incorporated to the Income Tax Act, the mitigation of unlawful tax avoidance was left to the courts. Although the courts endorsed a taxpayer's choice to arrange their affairs in manner which would reduce their tax burden, the endorsement was qualified by principle that any choice should be one anticipated by tax legislation. Accordingly, where unlawful tax avoidance was suspected, the courts first enquired whether the transaction was within the ambit of the tax legislation.

The courts uncover unlawful tax avoidance by assessing whether a transaction is

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[147] (1936) 19 TC 490.
[148] Ibid at 520.
[149] D French and R Stretch op cite (n66) at 26.1.

'simulated.' Simulated transactions conceal the true intentions of the parties through disguising it as something which it is not. Simulated transactions alter the tax consequences which should be attributed to the parties to the transactions. Describing simulated transactions, the court in *Zandberg v Van Zyl*[150] stated as follows:

> '*Now, as a general rule, the parties to a contract express themselves in language calculated without subterfuge or concealment to embody the agreement at which they have arrived. They intend the contract to be exactly what it purports; and the shape which it assumes is what they meant it should have. Not infrequently, however (either to secure some advantage which otherwise the law would not give, or to escape some disability which otherwise the law would impose), the parties to a transaction endeavor to conceal its real character. They call it by a name, or give it a shape, intended not to express but to disguise its true nature. And when a Court is asked to decide any rights under such an agreement, it can only do so by giving effect to what the transaction really is: not what in form it purports to be. The maxim then applies plus valet quod agitur quam quod simulate concipitur. But the words of the rule indicate its limitations. The Court must be satisfied that there is a real intention, definitely ascertainable, which differs from the simulated intention. For if the parties in fact mean that a contract shall have effect in accordance with its tenor, the circumstances that the same object might have been attained in another way will not necessarily make the arrangement other than it purports to be. The enquiry, therefore, is in each case one of fact, for the right solution of which no general rule can be laid down.'*[151]

In Commissioner for *South African Revenue Service v NWK Ltd*[152], however, the court went further to state that:

> '*the test to determine simulation cannot simply be whether there is an intention to give effect to a contract in accordance with its terms. Invariably where parties structure a transaction to achieve an objective other than the one ostensibly achieved they will intend to give effect to the transaction on the terms agreed. The test should thus go further, and require an examination of the commercial sense of the transaction: of its real substance and purpose. If the purpose of the transaction is only to achieve an object that allows the evasion of tax, or of a peremptory law, then it will be regarded as simulated. And the mere fact that parties do perform in terms of the contract does not show that it is not simulated: the charade of performance is generally meant to give credence to their simulation.*'[153]

Accordingly, simulated transactions are predicated on a lack genuineness and honesty. However, to decimate a simulated transaction, a court must be satisfied that there is an ascertainable true intention which differs from the simulated intention. The courts are thus required to take a global view of the transaction, including 'all

[150] 1910 AD 302.
[151] Ibid at 309.
[152] 2011 (2) SA 67(SCA).
[153] Ibid 55.

surrounding circumstances, any unusual features of the transaction and the manner in which the parties intend to implement it, before determining in any particular case whether a transaction is simulated'[154]. This a factual enquiry where each case must be dealt with on its own merits.

The common law test for simulation can be summarised as follows:

I. the substance of the transaction must have the effect to avoid tax (or other peremptory law).
II. if the first step is met, the simulation doctrine will apply if either:
    a. a subjective intention is present:
        i. to have presented the transaction in the disguised form; and
        ii. in all contracting parties; or
    b. The subjective purpose of any of the parties is to achieve a goal different from the one portrayed. [155]

If a court concludes a transaction is simulated, it is empowered to give effect to the true underlying intention and the tax consequences related thereto.

3.5.3 Legislative anti-avoidance methods

In 2006, the legislature introduced new general anti-avoidance rules which are contained in section 80A to section 80L of the Income Tax Act ("GAAR"). The GAAR co-exists with the common law principles described above. The application of the common law principles is, however, the first step to assess the lawfulness of tax avoidance. Only once the court is satisfied that the contract reflects the true, genuine intention of the parties can the GAAR be applied.

The GAAR enjoys wider application than the common law principles because, among other factors, it applies even in circumstances where tax avoidance scheme is genuine. The following elements must be satisfied to trigger the GAAR, namely:

I. there must be an avoidance arrangement as defined for which the sole or main purpose is to obtain a tax benefit;
II. the avoidance arrangement was abnormal, lacking in commercial substance or abusive of the provisions of the Act as set out in subparagraphs (a)-(c) of section 80A; and

[154] Ibid 37.
[155] A Marias "Simulation discussed: Tax avoidance in the common law" (2012) at 29.

III. the person whom the GAAR is invoked must have knowingly participated in the arrangement.

3.5.3.1 Avoidance arrangement

3.5.3.1.1 Arrangement

An avoidance arrangement is defined as 'any transaction, operation, scheme, agreement or understanding (whether enforceable or not), including all parts thereof, which results in a tax benefit'.[156] In the case of *Meyerowitz v Commissioner for Inland Revenue*[157] the court stated that the test to identify a scheme entails retrospectively evaluating each step and determining whether they were so connected with one another that they could ultimately lead to the avoidance of taxation.[158] Furthermore, the reference to an understanding encompasses both written and verbal agreements. Accordingly, it is wide enough to cover gentleman agreements.

3.5.3.1.2 Sole or main purpose to obtain a tax benefit

The Income Tax Act defines a tax benefit as the avoidance, postponement, or reduction of a person's tax liability.[159]Thus, SARS must demonstrate that but for the arrangement a taxpayer would have incurred tax liability, it would have incurred tax liability sooner, or it would have incurred a greater tax liability. Furthermore, SARS is burdened with the onus to demonstrate which other transaction would otherwise been entered into to produce the commercial consequences concerned with the greater tax burden.[160]

Once a tax benefit has been established, in accordance with section 80G (1) of the Income Tax Act, it is presumed that arrangement was entered into for the sole or main purpose of obtaining a tax benefit. Thus, the onus falls on the taxpayer to dispel the presumption by demonstrating an alternative motive for entering the transaction to satisfy the court that the tax benefit obtained was not its sole or main purpose. A court must evaluate a taxpayer's submissions in this regard, against the objective facts and circumstances, before deciding of the true purpose of the transaction.[161]

Importantly, if there are alternative methods of arriving at the same commercial outcome, the taxpayer is entitled to select the option which reduces their tax burden.

[156] Section 80L of the Income Tax Act.
[157] (1963) 4 All SA 148 (A).
[158] Ibid at 155.
[159] Section 80L of the Income Tax Act.
[160] D French and R Stretch op cite (n67) 26.3.2.
[161] Ibid.

In other words, selecting the option which incurs less tax liability, does not automatically promote the tax benefit to being the sole or main purpose for the transaction. This is in keeping with the recognition of the principle of 'choice' established by the courts.[162]

3.5.3.1.3 Abnormality test

Due to the limited scope of this paper and to preface the discussion in chapter 4 hereunder, I shall only deal with one of the additional requirements to identify an avoidance arrangement which will trigger section 80A of the Income Tax Act. This entails an enquiry into whether the arrangement has created rights or obligations that would not normally be created between persons dealing at arm's length.[163] This is a purely objective enquiry in terms of which a court would need to consider the way transactions of a similar nature would take place between unrelated persons.

[162] Ibid.
[163] Section 80A(c)(i).

CHAPTER 4 - TAXATION OF FOOTBALL TRANSFERS IN SOUTH AFRICA

4.1 General

The preceding chapters have provided a contextual background to the notion of the transfer system and relevant income tax principles. This chapter will deal with two matters. First, it will discuss preliminary issues to preface the application of the income tax principles. Second, it will apply the income tax principles to practical scenarios which incorporate the different player transfer methods.

4.2 Preliminary matters

4.2.1 Player registration rights

The Handbook stipulates that a club is not permitted to field a player in official games, unless the player is registered to it.[164] Accordingly, transfer fees paid by one club to another is not for the player themselves, but for the right to register and field the player in official games. Therefore, in the scenarios hereunder it is the transfer fees in relation to a player's registration rights which are the subject of tax consideration. One should therefore disregard references which imply that the player is the subject of the financial transactions in the scenarios.

4.2.2 Clubs as taxpayers

Professional football clubs in South Africa are incorporated entities, with a separate legal personality. Thus, in this paper, clubs are treated as resident taxpayers. The club's intentions are therefore ascertained in relation its owners, shareholders, or directors.

4.2.3 Special tax deductions

The Income Tax Act allows a taxpayer to claim certain special deductions from their taxable income. The relevant ones include capital allowances; deductions on expenditure to purchase patents, copyrights, and designs; and the notional deduction on trading stock. For reasons stipulated hereunder, I do not consider these deductions in the scenarios hereunder.

4.2.3.1 Capital Allowances

The general position is that capital expenditure is not deductible from taxable income, the Income Tax Act does, however, allow for certain exemptions. These include

[164] The National Soccer League op cite (n37) rule 31.1.

deductions for repairs and maintenance,[165] wear and tear of capital assets,[166] and building allowances[167] to mention a few. On an ordinary interpretation of the language of the provisions concerned, these deductions are only concerned with tangible assets. Accordingly, player registration rights, an intangible asset, cannot reasonably fall under any of these provisions. For this reason, I do not consider capital allowances in the scenarios hereunder.

4.2.3.2 Patents, copyrights, and designs

Section 11 (gC) of the Income Tax Act allows a taxpayer to claim a deduction of expenditure in connection with patents and similar rights from taxable income. These rights, like player registration rights, are intangible. This begs the question whether a club could claim a tax deduction for transfer fees incurred to acquire a player's registration rights. Put differently, are player registration rights 'property of a similar nature' to the rights stipulated under section 11(gC)? It's important to note that if there are at least two alternative reasonable interpretations of the provision, the benefit must in any event be read restrictively because it pertains to a privilege extended by the Income Tax Act.[168] On a purposive reading of the provision, however, I contend that they are not it is not possible that the right to field a player in official matches is akin to an extraordinary invention which constitutes intellectual property. Furthermore, the courts have provided that superficial similarities are not sufficient to be deemed a right of a similar nature.[169] Accordingly, I do not consider this deduction in the scenarios hereunder.

4.2.3.3 Trading stock

Section 22 of the Income Tax Act allows the notional deduction of the value of closing trading stock on account of damage, deterioration, change in fashion or any other reason satisfactory to SARS. Section 1 of the Income Tax Act defines 'trading stock' to include 'proceeds from the disposal of which forms or will form part of gross income'. In this paper I contend that, in certain instances, proceeds from a player transfer should form part of a club's gross income. Accordingly, in those circumstances, player

[165] Section 11(d) of the Income Tax Act.
[166] Ibid section 11 (e).
[167] Ibid section 13.
[168] *Burglers Post (Pty) Ltd v Secretary for Inland Revenue* 36 SATC 71 at 126.
[169] *Commissioner for South African Revenue Service v SA Silicone Products (Pty) Ltd* (2004) JOL 12536 (SCA) 18.

registration rights would loosely constitute trading stock. An enquiry into whether a club can claim this notional deduction for registration rights held on hand is, however, not practical, or useful in the context of player transfers. It is unlikely that a club has the intention to transfer all its players (they need them to conduct their trade) and thus it would not account for each player's registration rights as though it were a retail store selling shoes. Each player transfer has unique circumstances, and the nature of the transfer fees would be assessed retrospectively with reference to these circumstances.

4.2.4 Years of assessment

The scenarios hereunder do not expressly reference the respective years of assessment. Other than the fourth scenario, the reader should presume that the individual player transfers occur in successive years of assessment. The Income Tax Act and the common law are, however, consistently applied in the scenarios hereunder as they apply presently.

4.2.5 Solidarity contribution

The obligation to pay a solidarity contribution to training clubs does arise in the first, second and third scenarios. This obligation is, however, not stipulated in those scenarios, nor are the tax implications.

4.3 First scenario: conventional permanent transfer

4.3.1 Facts

Thandi Modise ("Thandi") is a 27-year-old player trained by FC Majita from age 12, up until they gave him his first professional contract at age 18. Thandi is renowned for his extraordinary ability to score goals but also his continuous battle with knee injuries. Notwithstanding this, Thandi progressed through the NSL ranks and has won league championships. Thandi has been the subject of three transfer deals.

First deal

After two seasons with FC Majita in the NFD, Thandi attracted the interest of several mid-table PSL clubs. FC Majita who are solely owned and managed by a former player- turned-businessman, Shakes Pilane ("Shakes"), were pleased with this as they are in the habit of developing young players and selling them off for profit. In television interviews and letters to fans, Shakes has consistently reiterated the club's focus of developing talent and to lead them to better opportunities at a premium. Accordingly,

FC Majita accepted Golden Stars' transfer bid of R2.8 million and Thandi signed a three-year employment contract with Golden Stars. Golden Stars are hoping that signing Thandi will take them a step closer to competing for the PSL championship, yet they are also aware that in due course bigger clubs will want to sign Thandi.

Second Deal

After playing two successful seasons with Golden Stars and being the top goal scorer in the league, Thandi submitted a transfer request to Golden Stars. The club chairperson accepted Thandi's request and advised him that the board were determined to get the highest possible transfer fee. Accordingly, when Langa Heat, the biggest club in the PSL, offered Golden Stars R15 million for Thandi, it was accepted. Langa Heat were willing to pay a large transfer fee because they believed Thandi would make them compete for the continental championship. The parties structured the transaction as follows:

I. Langa Heat pays R13 million upfront and the remaining balance of R2 million in equal instalments over two years;
II. Langa Heat would pay Golden Stars R1 million Rand if Thandi scores 50 goals for Langa Heat;
III. Langa Heat would pay Golden Stars R500 000 if Thandi earned 50 appearances for the South African National Team ("Bafana Bafana"); and
IV. If Langa Heat accepted a transfer bid for Thandi from a different club, Golden Stars will be given the opportunity to match the transfer bid and to approach Thandi to negotiate an employment contract.

Third Deal

In his third season with Langa Heat, Thandi scored his 50th goal for Langa Heat and earned his 50th appearance for Bafana Bafana. Due to a career-threatening knee injury however, he did not finish the season. Thandi's injury concerned Langa Heat's management and it was decided that the club would pay for Thandi to undergo specialist knee surgery and rehabilitation, whereafter he would be transferred to a different club. After concluding physical therapy, Thandi was placed on the transfer list which attracted interest from several clubs. Cape Warriors pounced on the opportunity by submitting a R4 million transfer bid, which Langa Heat accepted. Golden Stars were wary of Thandi's fitness and thus opted against exercising their right to match Cape Warriors' transfer bid. The parties made the transfer agreement conditional on Thandi passing a medical examination to be conducted by Cape Warriors' medical

team.[170] Unfortunately, Thandi failed the medical examination on account of his knee injury and the deal fell through. Thereafter, Langa Heat's medical team conducted its own medical examination and concluded that Thandi was no longer able to continue playing professional football. Accordingly, Langa Heat terminated Thandi's employment contract.

4.3.2 Application

4.3.2.1First transaction

4.3.2.1.1 Tax implications for FC Majita

In terms of the rule 46.2.2 of the Handbook, FC Majita qualifies as a training club and is accordingly due to receive an amount of R200 000 from Golden Stars for the eight years it trained Thandi. In addition to this, FC Majita received a transfer fee of R2.8 million. I deal with the tax consequences for each amount hereunder.

Training compensation

The training compensation appears to satisfy most of the requirements to be included in FC Majita's gross income. The contentious issues are whether the amount was received or accrued, and whether the training compensation is of a capital nature.

It matters not whether the training fees were actually received because the Handbook indicates that training compensation is due when 'the registration of the Player is transferred to another Member club while the Player retains his professional status',[171] accordingly, FC Majita is unconditionally entitled to receive the training compensation from Golden Stars, thus the training compensation has accrued to it.

The remaining issue is to determine whether the training compensation is intended to fill a hole in FC Majita's income-generating structure or to fill a hole in its future profits.[172] The training compensation due to FC Majita was not negotiated between the parties, it is imposed and calculated in accordance with the Handbook. FIFA has stated that training compensation is imposed to incentivise clubs to invest in the development of players, not to award them for the loss of assets from which they generate income. Furthermore, training compensation is uniformly calculated in relation to the approximate out-of-pocket costs a club incurs in relation to the development of a player.[173]These amounts are generally deductible in terms of the

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[170] The National Soccer League op cite (n37) rule 41.8 does not allow a players employment contract to be subject to a medical examination, but it is silent of the inclusion thereof in transfer agreements.
[171] Ibid rule 46.2.2.
[172] *Taeuber* supra note 104 at 136 and 137.
[173] These include fees such as: coaching, medical care, schooling, food, equipment, travel and lodge.

Income Tax Act because they are closely associated with the day-to-day running costs of the club and are therefore revenue in nature.

It follows therefore, that if training compensation is meant to reimburse the club for costs incurred, training compensation constitutes a revenue receipt. In this instance, the contention that the training compensation is revenue in nature is bolstered by the taxpayer's self-professed motive to develop and sell players in a scheme of profit-making. For the reasons above, the training compensation should be included in FC Majita's gross income.

Transfer Fee

FC Majita have received the transfer fee of R3.2 million, thus the contentious matter is whether the transfer fee is of a capital or revenue nature. Where a taxpayer sells an asset, to determine the nature of the receipt one must ascertain the intention of the taxpayer.[174] If FC Majita's motive for selling Thandi was to generate profit in a scheme of profit-making then the amount will be revenue. On the other hand, if FC Majita were merely realising their investment in Thandi, the transfer fees will constitute a capital receipt.[175]

To ascertain FC Majita's intention, one must look to the conduct of the persons in control of the club.[176] Shakes, effectively controls FC Majita's affairs, and he has publicly disclosed that the club is focused on developing and selling young players at a profit. Notwithstanding the extended duration Thandi spent with the club, it does not suggest that Thandi was a crucial component of the club's revenue-generating structure. To the contrary, Thandi is one of many 'products' which the club 'manufactures' and sells off as part of its revenue-generating activities. Accordingly, the transfer fee should be included in FC Majita's gross income.

4.3.2.1.2 Tax implications for Golden Stars

Training Compensation

In accordance with the Handbook, Golden Stars are unconditionally liable to pay R200 000 to FC Majita for training compensation, thus the expense is accrued. The issues which should determine whether the training compensation is deductible in terms of Section 11 (a) of the Income Tax Act, are whether the training compensation was incurred in the production of income and is of a revenue nature. The first issue is

[174] *Stott* supra note 94 at 262.
[175] Ibid at 261.
[176] *Richmond Estates* supra note 92 at 361.

straightforward, the training compensation was expended as part of the player transfer process, a process which is inextricably linked to the running of any professional football club. Accordingly, the training compensation is incurred in the production of income.

The contentious matter is whether the training compensation constitutes revenue expenditure from Golden Stars' perspective. To ascertain this one must establish the motive for the expenditure and if the motive is closely linked to the taxpayer's income-earning structure, it is of a capital nature.[177] Alternatively, if the expenditure is closely linked to the taxpayer's income-earning operations it is of a revenue nature.[178] The facts indicate that Golden Stars acquired Thandi to bolster their competitiveness, yet they were aware that they could command a greater transfer fee for him should he be sold in future. The latter motive is not material to the enquiry, because it is uncertain future event.[179] Thus, to me it appears that the training compensation represents a capital expense in the hands of Golden Stars because it is incurred as part of a transaction which is closely linked to the clubs' capital structure, and for which Golden Stars will acquire Thandi's registration rights for the duration of his employment contract, which is a corresponding enduring and exclusive benefit.[180] Accordingly, the training compensation should not be allowed as a tax deductible expenditure.

Transfer Fee

Golden Stars actually incurred a transfer fee cost of R2.8 million. Golden Stars can deduct the transfer fee from its taxable income in terms of section 11(a) of the Income Tax Act if it was incurred in the production of income and if the transfer fee constitutes revenue expenditure. Although the obligation to pay the transfer fee arises from the transfer agreement, as opposed to the Handbook like training compensation, it is closely linked to the business operation of player transfers. Accordingly, it is incurred in the production of income.

The contentious aspect is whether the transfer fee constitutes revenue expenditure. Golden Stars incurred the transfer fee to acquire Thandi's registration rights for the duration of his employment contract, a corresponding enduring and exclusive benefit, which is of a capital nature.[181] Accordingly, the transfer fee should also not be allowed

[177] *New State Areas* supra note 125 at 627.
[178] Ibid.
[179] *Nasionale Pers* supra note 121 at 15.
[180] *Income Tax Case 1063* supra note 130 at 59.
[181] Ibid.

as deductible expenditure in terms of section 11 (a) of the Income Tax Act.

4.3.2.2 Second Transaction

4.3.2.2.1 Tax implications for Golden Stars

Compensation

In terms of the Handbook, training compensation of R50 000 has accrued to Golden Stars for the one-year duration Thandi spent with the club before reaching age 21.[182] Training compensation is imposed to replenish Golden Stars' out-of-pocket costs for contributing to Thandi's training and development and is therefore closely linked to Golden Stars' income-generating operations and constitutes a revenue receipt. Accordingly, Golden Stars must include the training compensation in its gross income.

Transfer Fee

There are three financial components to Thandi's transfer from Golden Stars to Langa Heat. The first component is that Golden Stars must receive a total of R15 million from Langa Heat, of which an initial fee of R13 million was immediately paid and the remaining R2 million was payable in equal instalments over two years.

For convenience I shall deal with the tax implications of these amounts separately. The initial amount satisfies most of the requirements to be included in Golden Stars' gross income. The pertinent query is whether the initial amount constitutes revenue or capital to Golden Stars. This must of course be determined with reference to Golden Star's intention.[183] Golden Star's dominant intention when signing Thandi, was to increase its chances of winning the PSL. If the enquiry were to end there the transfer fees received should most likely be capital in nature. The pertinent question here, however, is whether it can be argued that Golden Stars' intention changed when the board expressed its determination to earn a substantial profit on the transfer, put differently: did Golden Stars 'cross the rubicon'[184] to embark on a scheme of profit-making?

A wholistic enquiry is required to determine whether there was a material change in Golden Stars' intention from when it signed Thandi up to the time of entering the transfer deal. The facts indicate that Thandi initiated the transfer, not Golden Stars, and only after this did Golden Stars' board take steps to prioritise its financial interests. Notwithstanding this, the courts have on several occasions affirmed a taxpayer's right

[182] The National Soccer League op cite (n37) rule 49.2.1 read with rule 48.1.1.
[183] *Stott* supra note 94 at 262.
[184] *Natal Estates* supra note 96 at 393.

to realise the value of its capital assets to its advantage.[185] Accordingly, Golden Stars earning a substantial profit on the transfer should not suffice to change the nature of the transfer fees to a revenue nature. Accordingly, the initial amount should not be included in gross income.

When considering the remaining R2 million payable, this balance is to be paid in instalments and will not be received in a single year of assessment. It must accordingly be determined whether this balance has accrued to Golden Stars. An amount is deemed to have accrued to the taxpayer if it payable in relation to a vested right.[186] In other words, accrual occurs when a taxpayer is unconditionally entitled to receive it, notwithstanding that it may only be received in a future financial year.[187] It follows therefore, that the balance has accrued to Golden Stars. For the same reasons attributed to the initial amount, however, the balance should not be included in Golden Stars' gross income because it constitutes a capital receipt.

The transfer deal will, however, trigger CGT liability for Golden Stars because the transfer deal constitutes an act that results in the transfer of an asset (Thandi's registration rights), which is a disposal as defined in paragraph 11(1)(a) the Schedule. Accordingly, the R15 million transfer fee must be included as proceeds received from the disposal, and the R2.8 million transfer fee and R200 000 training compensation paid to FC Majita must, in terms of paragraph 20 (1) (a) of the Schedule, be included in the base cost calculation. Golden Stars will thus realise a net capital gain of R13 million on the disposal.

The second component is the bonus conditions stipulated in the transfer agreement. In terms thereof, Langa Heat must pay Golden Stars certain amounts if Thandi scores 50 goals for Langa Heat and/or earns 50 appearances for Bafana Bafana. These bonus amounts have not been received nor, I contend, have they accrued to Golden Stars at the time of signing the transfer agreement because it is not unconditionally entitled to receive the amounts.[188] The bonus conditions are future uncertain events which may never occur and should thus not be included Golden Stars' gross income, up until they have been met.[189]

The third component is a right of first refusal in favour of Golden Stars, in terms of

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[185] *Stott* supra note 94 at 261.
[186] *Income Tax Case No 76* supra note 87 at 70.
[187] *WH Lategan* supra note 78 at 20.
[188] *Mooi* supra note 85 at 11.
[189] Ibid.

which Golden Stars has the option to match any transfer bid accepted by Langa Heat for Thandi in future. The enquiry here is whether Golden Stars can claim a deduction in terms of this clause. The expenditure is only incurred, and therefore deductible, if the taxpayer is unconditionally liable to pay an amount, not that it has actually paid an amount.[190] The facts indicate that no value is stipulated for a future transfer deal, and therefore the quantum of the expense cannot presently be ascertained. Notwithstanding this, it is uncertain whether the transfer will be concluded. For instance, Thandi could refuse to re-join Golden Stars or Golden Stars can cease its trade. Accordingly, no amount can be deducted at conclusion of the transfer deal, and therefore there are no tax implications arising from the right of first refusal.

4.3.2.2.2 Tax implications for Langa Heat

Training Compensation

In accordance with the Handbook, Langa Heat are unconditionally liable to pay R50 000 to Golden Stars for training compensation, thus the expense is accrued. The contentious issues, which should determine whether the training compensation is deductible in terms of section 11 (a) of the Income Tax Act, are whether it was incurred in the production of income and is of a revenue nature. The first issue is straightforward, the training compensation was expended as part of the player transfer process, a process which is inextricably linked to the running of any professional football club. Accordingly, the training compensation is incurred in the production of income.

The contentious matter is whether the training compensation constitutes revenue expenditure or capital expenditure from Langa Heats' perspective. The facts indicate that Langa Heat signed Thandi to bolster their chances of winning the continental championship, which would of course earn the club prize money, but it would also elevate the club's stature which would in turn create additional revenue streams. Thus, to me it appears that the training compensation represents a capital expense in the hands of Langa Heat because in exchange for paying it, Langa Heat receive Thandi's registration rights for the duration of his employment contact, a corresponding enduring and exclusive right.[191] Accordingly, the training compensation should not be allowed as a deductible expenditure.

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[190] *Port Elizabeth Electric* supra note 119 at 15.
[191] *Income Tax Case 1063* supra note 130 at 59.

Transfer Fee

Each of the financial aspects of the transfer must also be evaluated from Langa Heat's perspective. The first issue to be determined is whether Langa Heat can claim a tax deduction in terms of section 11 (a) of the Income Tax Act for the transfer fee. The contentious issue is whether the initial payment is of a capital or revenue nature. The facts indicate that Langa Heat signed Thandi to bolster their chances of winning the continental championship, which would of course earn the club prize money, but it would also elevate the club's stature which would in turn create additional revenue streams. The initial fee is therefore closely linked to Langa Heat's income earning-capacity, and it would accordingly be a non-deductible capital expense.

The same reasoning is applicable to the balance. The fact that expenditure is recurring does not automatically change its nature to revenue.[192] Furthermore, the fact that the expense will not be paid in a single year of assessment has no bearing because Langa Heat have accrued an unconditional liability to pay it.[193]

On the other hand, the bonus' payments due to Golden Stars if Thandi earns 50 appearances for Bafana Bafana and scores 50 goals for Langa Stars, should not be deducted from Langa Heat' taxable income. These bonus' are contingent on uncertain future events and the have therefore not actually been incurred.[194]

Finally, the right of first refusal in Golden Stars' favour should not trigger any tax liability for Langa Heat. Although it allows Golden Stars to match any future transfer bid for Thandi, the quantum of the transfer bid and whether the deal will go through, is uncertain.[195]

4.3.2.3 Third Transaction

4.3.2.3.1 Tax implications for Golden Stars

Subsequently, Thandi scored 50 goals for Langa Heat and earned his 50th appearance for Bafana Bafana, thus the bonus conditions in the transfer agreement were triggered. Accordingly, an amount of R1.5 million accrued to Golden Stars. Whether this bonus amount should be included in Golden Stars' gross income is contingent on whether it constitutes capital or revenue in its hands. Although the amount accrued well after the transfer deal, it emanates from it. Thus, the bonus amount should be treated equally

[192] *Kajadas Cosmetics* supra note 132 at 203.
[193] *Port Elizabeth Electric* supra note 119 at 15.
[194] Ibid.
[195] Ibid.

for tax purposes. Accordingly, the amount should not be included in gross income because is constitutes a capital receipt.

Furthermore, Golden Stars declined to exercise their right of refusal to re-acquire Thandi, and his employment contract with Langa Heat was terminated, therefore this clause shall never bring about tax consequences for Langa Heat because no amount was actually incurred.[196]

4.3.2.3.2 Tax implications for Langa Heat

Equally, the liability incurred by Langa Heat to pay the bonus amount to Golden Stars is not a stand-alone expense and must be evaluated in relation to the initial transfer expense. Thus, the bonus expenditure should constitute a non-deductible capital expense in terms of section 11 (a) of the Income Tax Act, as the transfer fee had.

The transfer fee agreed with Cape Warriors should not trigger any tax consequences. The transfer fee was not paid, but it had also not accrued because the receipt was conditional on Thandi passing a medical examination – a future uncertain event.[197] And in any event, Thandi failed the medical examination and the transfer deal fell through.

Finally, the termination of Thandi's employment contract (and by implication his registration rights) has CGT consequences. Paragraph 11 (1) (c) of the Schedule provides that a disposal includes the 'scrapping, loss or destruction' of an asset. I contend that Langa Heat's termination of Thandi's contract, due to his medical inability to play professional football, constitutes the scrapping of an asset. On the presumption that no compensation (such as insurance) was received for the disposal, Langa Heat's disposal is deemed to occur on the date of termination of the contract.[198] Furthermore, the proceeds received would amount to zero, but the initial transfer fees paid (including the bonus fees) should be included in the base cost in terms of paragraph 20 (1) (a) of the Schedule. The fees paid for surgery and rehabilitation, however, should not be included as amounts incurred because fees expended for maintenance of an asset are specifically excluded in terms of paragraph 20 (2) (b) of the Schedule. In addition, in terms of paragraph 20 (3)(a)(i) of the Schedule, an amount which was allowed as taxable deduction cannot be included under base costs, and medical costs qualify to be deducted from Langa Heat's taxable income. Accordingly, the termination of

[196] Ibid.
[197] Ibid.
[198] Paragraph 13 (1)(c)(ii) of the Schedule.

Thandi's employment contract would lead to a net capital loss of R15 million for Langa Heat. The capital loss has no consequences for Langa Heat's taxable income, but it can be used to offset against any other capital gains.

4.3.2.3.3 Tax implications for Cape Warriors

Notwithstanding that Cape Warriors had offered Langa Heat a transfer fee of R 4 million for Thandi, the deal was contingent on Thandi passing a medical examination. Thus, Cape Warriors had not actually incurred an unconditional liability which would trigger tax implications.[199] Furthermore, after Thandi failed the medical examination, the deal fell through and accordingly there are no tax implications for Cape Warriors in relation to the R 4 million transfer fee it offered to Langa Heat.

4.4. Second Scenario: conventional loan transfer

4.4.1 Facts

Langa Heat and Soweto Roses, an NFD club, are parties to an affiliation agreement. In terms of the affiliation agreement, Langa Heat are required to assist Soweto Roses with financial and other resources to develop young players. Some of the terms agreed include:

I. Langa Heat must loan at least three of its young players to Soweto Roses in each season;
II. they must pay 100 per cent of each loaned players' wages to Soweto Roses, who in turn distribute the wages to the loaned players;
III. Soweto Roses must provide continuous status reports on the players' development; and
IV. Soweto Roses must give Langa Heat preferential rates to sign any of its players.

Johnny Swart ("Johnny"), a 25-year-old player, was trained by Langa Heat. Unfortunately, he was not able to gain experience through playing regularly. Accordingly, Langa Heat opted to loan Johnny to Soweto Roses, in terms of the affiliation agreement.

After the first season, Soweto Roses indicated their interest to sign Johnny permanently so they could bolster their chances of winning the NFD. A transfer was not agreed, however, because Soweto Roses could not meet Langa Heat's asking

[199] Ibid.

transfer fee. Accordingly, the parties agreed that Johnny would join Soweto Roses on loan for an additional season. On this occasion, however, the clubs agreed the following terms:

I. Soweto Roses would pay an upfront loan fee of R 1 million;
II. Soweto Roses would cover 70 per cent of the Johnny's wages, and Langa Heat would cover the remaining 30 per cent; and
III. in the last month of the loan agreement, Soweto Roses could permanently sign Johnny if it paid a R5 million a transfer fee to Langa Heat.

4.4.2 Application

4.4.2.1 First Loan

4.4.2.1.1 Tax consequences for Langa Heat

In terms of the first loan agreement, Langa Heat were responsible for covering Johnny's wages. This is an expense which they actually incurred. Whether Johnny's wages are deductible is contingent on whether Langa Heat incurred them for the purposes of trade and whether they are revenue in nature. The facts indicate that the club had two motives for paying Johnny's wages, to honour the affiliation agreement and to ensure that Johnny gains the necessary experience. Both motives are for the purpose of Langa Heat's trade. A football club must develop its player's and acquire new players to function, paying Johnny's wages falls within these objectives.

Although Langa Heat may derive long-term commercial benefits from honouring the affiliation agreement, the expenditure for Johnny's wages is closely related to the day-to-day revenue activities of the club. Langa Heat's players must be remunerated for their services, even though the services are temporarily rendered to another club. Ultimately, Johnny's services are rendered to Soweto Roses at the behest of Langa Heat. Accordingly, Langa Heat can claim the Johnny's wages as a deductible expense in terms of section 11 (a) of the Income Tax Act.

4.4.2.1.2 Tax consequences for Soweto Roses

In the ordinary course, clubs are required to pay players for services rendered and, albeit temporarily, Soweto Roses enjoyed the right to use Johnny's services. Langa Heat's responsibility to pay Johnny's wages was undoubtedly financially beneficial to Soweto Roses because they did not have to incur an expense. It should therefore be considered, however, whether Johnny's wages, paid through Soweto Roses, is taxable in their hands. An amount must be included in a taxpayer's gross income if it

is received by the taxpayer on their own behalf for their own benefit.[200] In this regard, Johnny's wages should not be included in Soweto Roses' gross income because the amount was not received on its own behalf. Notwithstanding that Soweto Roses benefit from the arrangement, the wages are for services rendered by Johnny, and they are therefore received on his behalf.

4.4.2.2 Second Loan

4.4.2.2.1 Tax consequences for Langa Heat

The second loan agreement had three distinguishing factors. First, the Soweto Roses had to pay a loan fee. The facts indicate that Langa Heat's intention had changed, they were no longer adhering to the affiliation agreement but were taking active steps to facilitate Johnny's permanent transfer. This, however, has no bearing on the nature of the loan fee. A loan transfer does not entail a transfer of ownership of a player's registration rights, it is a subsidiary right of use. Indeed, the Handbook confirms that a club which loans a player does not have the right to transfer the player to any other club, without the written authorisation of the club that released the player on loan.[201] The loan fee, like rental income, is the income generated from the working of an asset. The loan fee is thus closely linked to Langa Heat's income-operations and constitutes a revenue receipt.

Second, Langa Heat was only required to pay 30 per cent of Johnny's wages. Although the fees are expended within a different context to the first loan, Johnny remained a Langa Heat player, and there was a possibility that he might return. Langa Heat incurred Johnny's Wages as a cost of working their capital asset, accordingly the wages were of a revenue nature. Langa Heat should therefore still be permitted to claim its 30 per cent contribution to Johnny's wages as a tax deduction in terms of section 11(a) of the Income Tax Act.

Third, although a future transfer fee had been agreed, Soweto Roses were not bound to sign Johnny, and Johnny was not obliged to agree to permanently join Soweto Roses. Accordingly, Langa Heat should not include the future transfer fee in their gross income because it is contingent on the occurrence of an uncertain event.[202]

4.4.2.2.1 Tax consequences for Soweto Roses

Once more, the second loan had three distinguishing factors. First, Soweto Roses paid

[200] *Geldenhuys* supra note 80 at 430.
[201] The National Soccer League op cite (n37) rule 39.7.
[202] *Mooi* supra note 85 at 11.

a loan fee. The loan fee payment brought about an enduring corresponding benefit (the right to field Johnny in official games), but the benefit was subject to the control of Langa Heat. There was no transfer of ownership of Johnny's registration, up until Soweto Roses paid a transfer fee. Accordingly, the loan fee is akin to rental fees and thus deductible in terms of section 11 (a) of the Income Tax Act from Soweto Roses' taxable income because it is closely linked to revenue-generating operations. Second, Soweto Roses was required to pay the greater portion of Johnny's wages. It has been noted that a player's wages are a running cost of a club, and accordingly constitute revenue expenditure. Soweto's contribution to Johnny's wages is thus a deductible tax expense in terms of section 11 (a) of the Income Tax Act.

Finally, although the future transfer fee has been agreed, Soweto Roses have not incurred an unconditional liability to pay it.[203] The clause is an option to purchase and therefore tax consequences shall only arise if the option is successfully exercised.

4.5 Third scenario: free transfer

Tim Sangweni ("Tim") was an academy player for NFD club, Hout Bay United. As an academy player he was yet to sign a professional contract, but as result of his extraordinary football talent, he received offers from many PSL clubs at age 19. Tim's family are ardent Gugulethu Bulls supporters and would have preferred that he take their offer, and while Hout Bay United wanted to promote him to their professional team, for financial reasons, his family decided that he would sign his first professional contract with Golden Stars. In terms of the Handbook, Golden Stars were required to paid training compensation of R175 000 to Hout Bay United. Thereafter, Tim was the subject of two further transfers.

First Transfer

In the last six months of his 3-year contract with Golden Stars, he rejected their offer for an extension and indicated his intention to leave on a free transfer to join a bigger club. Consequently, Tim signed a five-year contract with Langa Heat and received a signing bonus of R8 million. Notwithstanding the bonus and that Langa Heat was a successful club, Tim's father was concerned that the length of the contract could prevent him from moving to foreign clubs in the prime of his career. Tim's father communicated this concern to Langa Heat who responded by including an exorbitant R40 million buy-out clause in Tim's contract.

[203] *Port Elizabeth Electric* supra note 119 at 15.

Second Transfer

In Tim's second season with Langa Heat, Prime Sport (Pty) Ltd ("Prime Sport"), South Africa's largest sports broadcaster, acquired mid-table club Gugulethu Bulls. Historically, Gugulethu Bulls were Langa Heat's main rivals but were unable to meaningfully compete due to lacking financial resources. Prime Sport publicly announced their intention to re-build Gugulethu Bulls into the biggest club in South Africa. Accordingly, they invested significant resources into Gugulethu Bulls, including providing a large transfer budget to acquire players.

The newly appointed coach identified the acquisition of Tim as one of several players who could contribute to building the club, however, Gugulethu Bulls anticipated the following difficulties in concluding a transfer deal for Tim:

I. Langa Heat would be reluctant to transfer Tim to historical rivals; and
II. The value of the buy-out clause significantly exceeded the clubs transfer budget, allocated by the finance committee.

Accordingly, the Gugulethu Bulls management decided to forego the pursuit of Tim and signed another player within their allocated budget. Shortly thereafter, a financial executive from Prime Sport learned about the previous intention to sign Tim and instructed the Gugulethu Bulls' management the intention because signing Tim would assist to reduce the Prime Group's overall tax liability. To this end, a plan was devised and implemented in terms of which one of Prime Sports' subsidiary companies, Prime Finance (Pty) Ltd ("Prime Finance"), advanced a R35 million interest-free loan directly to Tim. Tim, used the loan amount, and R5 million of his savings, to activate the buy-out clause of his employment contract with Langa Heat. Accordingly, Tim's contract with Langa Heat was terminated and he was free to sign with Gugulethu Bulls. After signing with Gugulethu Bulls, Tim was given a signing bonus of R5 million. The way in which the transactions were structured resulted in less taxes payable by the Prime group companies, than if Gugulethu Bulls were to pay the transfer fee to Langa Heat directly.

4.5.1 Application

4.5.1.1 First Transfer

4.5.1.1.1 Tax consequences for Hout Bay United

In accordance with the Handbook, Hout Bay United is due to receive R175 000 from Golden Stars in training compensation. As stated previously, this amount is calculated

in accordance with the out-of-pocket costs required to develop a player. Although the facts indicate that Hout Bay United had intended to keep the player to develop further in their ranks, this should not change the nature of the receipt, it remains of a revenue nature. Accordingly, the training compensation should be included in Hout Bay United's gross income.

4.5.1.1.2 Tax consequences for Golden Stars

Training Compensation

The facts do not indicate that Golden Stars expended the training compensation in the scheme of profit-making Instead, Golden Stars paid the training compensation as a consequence of attaining Tim's registration rights for the duration of his employment contract, an exclusive and enduring right.[204] Accordingly, in terms of section 11(a) of the Income Tax Act, the training compensation constitutes non-deductible capital expenditure.

Signing Bonus

Golden Stars signed Tim as an unregistered player and therefore no transfer fee was paid to Hout Bay United. Golden Stars did, however, pay Tim a signing bonus. In a commercial context, a signing bonus fee is akin to a transfer fee, although a player receives it. Accordingly, one should ascertain Golden Star's motive for the expenditure. In terms of the Handbook, five years (including renewal periods) is maximum duration permitted for a player's contract. The fact that Golden Stars offered Tim the maximum possible duration in his employment contract, and that an exorbitant buyout clause to deter attempts to poach Tim was included in his employment contract, indicates that Golden Stars were intent on retaining Tim's registration rights for as long as possible, in other words, an enduring benefit.[205] Accordingly, the signing bonus is closely linked to Golden Stars' revenue-generating structure, and it should not be included in gross income as it constitutes a capital receipt.

4.5.1.2 Second Transfer

4.5.1.2.1 General

The second transfer entailed a series of transaction which culminated in Tim joining Gugulethu Bulls. When viewed as a composite whole it raises questions whether there was any unlawful tax avoidance. The first step to evaluate this is to

[204] *Nchanga Consolidated Copper Mines* supra note 127 at 42.
[205] Ibid.

apply the common law doctrines to ascertain whether this was a simulated transaction. The difficulty with the applying the common law doctrine is that the facts do not indicate any disingenuity among the parties, that the scheme was entered for the purpose of tax avoidance or other law, or that all parties were implicated. Indeed, the Gugulethu Bulls intended to acquire Tim and, its intention was not disguised, they merely followed a different yet valid path to achieve their intention. Therefore, the contract between the parties was genuine.

Accordingly, the next step must be to apply the GAAR. To invoke the GAAR the parties must have entered an impermissible avoidance arrangement in terms of section 80A of the Income Tax Act. I deal with each element in the following subsection.

4.5.1.2.2 GAAR

Arrangement

The definition of an avoidance arrangement in section 80 L of the Income Tax Act is broad, and it includes an understanding (whether enforceable or not), as well as all the steps in the understanding. The facts indicate that Gugulethu Bulls (through Prime Sport and Prime Finance) benefited from a series of transactions which entailed the transfer of property, after an understanding was reached with Tim. Although the understanding was not recorded or enforceable, the parties involved acted in accordance with the understanding. Accordingly, the first requirement is satisfied.

Sole or main purpose to obtain a tax benefit

The facts indicate that because of the arrangement the Prime Group avoided higher tax liability. Had Gugulethu Bulls paid the transfer fee directly to Langa Heat (which is what would occur in the ordinary course), Gugulethu Bulls (and by implication the Prime Group) would have incurred a higher tax liability. Accordingly, Gugulethu Bulls (and the Prime Group) obtained a tax benefit from the arrangement, and as a consequence, would be presumed to have entered into the arrangement for the sole and main purpose of obtaining the such tax benefit.[206] To dispel the notion that they did not enter into the arrangement for the sole or main purpose of obtaining a tax benefit, Gugulethu Bulls could rely on the 'choice principle'.[207] This would entail demonstrating that the underlying commercial rationale was to sign Tim and that they were entitled to choose an alternative course to affect their intention, even if it resulted

[206] Section 80G (1) of the Income Tax Act.
[207] D French and R Stretch op cite (n66) 26.3.2.

in lessening their tax burden. However, given that the facts indicate they had forgone this plan and only revived it once it was indicated that it would have tax benefits for the Prime Group. Therefore, the intervention of the financial executive would create difficulty which Gugulethu Bulls are unlikely to overcome.

Abnormality test

Now that it has been established that the avoidance arrangement was entered into for the sole or main purpose of obtaining a tax benefit, I shall apply the abnormality test. In terms thereof one must determine whether the avoidance arrangement has created rights or obligations which would not normally be created between parties dealing at arm's length.[208]

The parties of concern here are Gugulethu Bulls' and Tim. The elements in the facts which create unusual rights and obligations between a club and player dealing at arm's length are as follows:

I. In the ordinary course, a club is unlikely to arrange for an exorbitant interest-free loan of R35 million to be advanced to an unaffiliated player (who is little different from a complete outsider), so that they can buy themselves out of their employment contract; and
II. It is unlikely that a club and the player would enter an arrangement in terms of which a portion of the buy-out clause would be funded from a player's personal savings.

These elements indicate that the arrangement could be proven to be an impermissible avoidance arrangement as anticipated by section 80A of the Income Tax Act. If SARS successfully invokes the GAAR, the commissioner is empowered to disregard the impermissible avoidance arrangement as if it had not been entered into or carried out, or in such manner as the commissioner deems fit to prevent the prevention of the tax benefit.[209]If we are to assume that the commissioner would treat the arrangement as a direct transfer of Tim from Langa Heat to Gugulethu Bulls, the tax implications discussed in the following section would arise.

4.5.1.2.3 Tax consequences for Langa Heat

The facts indicate that Langa Heat was not party to the avoidance arrangement,

[208] Section 80A (c) (i) of the Income Tax Act.
[209] Section 80B(1)(f) of the Income Tax Act.

accordingly, the GAAR should not be invoked against it.[210] This means that the amount it received in terms of the buyout clause should be considered outside of the tax avoidance arrangement. The amount Langa Heat received for the early termination of Tim's employment contract represents contractual compensation. Accordingly, one must enquire whether the amount was received to fill a in Langa Heat's capital assets or profits.[211]To establish this one must also take note of nature of Tim's registration rights in the club's hands. At the time of termination, Tim formed a large part of Langa Heat's income-generating structure, this is demonstrated by the steps which they took to include an exorbitant buy-out clause in his employment contract to deter other clubs from signing him. They wanted to keep him at the club and benefit from his talent for an enduring period. Thus, there is nothing to suggest that the compensation was paid for the loss of revenue. Accordingly, the compensation received by Langa Heat was to fill a hole in its capital assets and constitutes a capital receipt which should not be included in its gross income.

The early termination of Tim's contract is, however, a disposal of an asset in terms of the paragraph 11 (1) (a) of the Schedule and will trigger CGT. Accordingly, the R40 million compensation fee represents the proceeds received and the R8 million signing bonus paid to Tim should be included in the base cost calculation.[212] Langa Heat would therefore have realised net capital gain of R32 million.

4.5.1.2.4 Tax consequences for Gugulethu Bulls

After invoking the GAAR, SARS can disregard the impermissible arrangement culminating in Tim signing for Gugulethu Bulls, and attribute all the expenditure to it for income tax purposes. It would therefore be presumed that Gugulethu Bulls paid a R40 million transfer fee to Langa Heat. The facts indicate that Tim was one of the acquisitions which were perceived as a central aspect of Gugulethu Bulls growth plans. There is no indication that Tim was acquired as part of a scheme of profit- making. Thus, the enduring and exclusive right they have to utilise Tim relates to their income-generating structure, and the fees expended to attain this right must accordingly constitute a non-deductible capital expenditure in terms of section 11 (a) of the Income Tax Act.

4.6

[210] *Absa Bank Ltd v Commissioner for South African Revenue Service* (2021) 83 SATC 401. 43.
[211] *Taeuber* supra note 104 at 136-7.
[212] Paragraph 20 (1)(a) of the Schedule.

4.7 Scenario four: Bridge transfer

Jackson Mokoena's ("Jackson") football talent was discovered by his wealthy uncle, Thabo Mokoena ("Thabo"), at age 12. Thabo arranged for Jackson to join Golden Stars' football academy and made several large financial contributions to Jackson's family and lifestyle, up until Jackson signed his first professional employment contract with Golden Stars. Jackson is touted to grow into a world class player who will command exorbitant transfer fees in future. Thabo has since purchased his own NFD club, Caledon FC, from which he develops young players to transfer to European clubs at a profit.

Patrice Nxasana ("Patrice"), the chairperson of Golden Stars, has strong commercial acumen and is known for cutting corners to save money. He also enjoys a cordial relationship with Thabo, and if possible, wanted to ensure that Thabo realises some financial recognition for discovering Jackson's talent and investing in his family's upkeep. When English club, Manchester Boys, public indicated their interest to sign Jackson (and that they were in talks with Patrice), Patrice solicited the advice of a tax lawyer to structure the deal in manner that reduces his tax liability and could also reward Thabo (*via* Caledon FC) through a solidarity contribution. Accordingly, the transfer deal was structured as follows:

I. Golden Stars transferred Jackson to Caledon FC for a transfer fee of R1.5 million, on condition that Caledon FC pay a R1.5 million bonus to Golden Stars upon Jackson signing for an English club; and
II. After joining Caledon FC, Jackson was immediately loaned to Manchester Boys for one season on condition that Manchester Boys pay a R 3 million transfer fee to Caledon FC for Jackson's permanent transfer at the end of the season.

FIFA successfully challenged this arrangement on the ground that it is tantamount to a bridge transfer because Caledon FC did not derive any sporting benefit from the transfer. Accordingly, FIFA imposed fines of R1.5 million on Golden Stars and Caledon FC, respectively.

4.6.1 Application

4.6.1.1 General

The convoluted nature of the transaction lends itself to an enquiry into possible unlawful tax avoidance. It appears that the application of the common law doctrine

would not be possible because the facts do not indicate that the parties had a disguised or dishonest underlying intention, which ought to be given effect. The intention of the parties was to transfer Thabo, and although it was later proven to contravene football regulations, the transactions were honest. It follows therefore that it should be assessed whether the GAAR can be invoked.

4.6.1.2 GAAR

4.6.1.2.1 Arrangement

The facts indicate that the parties entered a series of transactions in terms of which Jackson was transferred to Manchester Boys on loan. The series of transactions would constitute, and arrangement as defined under Section 80L of the Income Tax Act because they relate to the alienation of property (Jackson's registration rights). Accordingly, the first step of the enquiry is satisfied.

4.6.1.2.2 Sole or main purpose of obtaining a tax benefit

In terms of the arrangement, Golden Stars deferred their tax liability on the R 1.5 million which would have certainly immediately accrued to them, had they not included Caledon FC in the transaction. In terms of section 80G (1) of the Income Tax Act it is presumed that an avoidance arrangement was entered into by Golden Stars for the sole and main purpose of obtaining the tax benefit. To rebut the presumption, Golden Stars could rely on the 'choice principle'[213] to argue that the sole or main purpose of the arrangement was not a tax benefit, but to realise a capital asset, and that they are entitled to choose any method which reduces their tax liability.[214] It is, however, doubtful whether this defence would succeed because in terms of section 80H, SARS is permitted to challenge individual steps within an arrangement, and it is likely that they would challenge the step wherein Jackson was briefly transferred to Caledon FC. Thus, it is unlikely that Golden Stars could justify the commercial rationale for this step in the context of the entire transfer arrangement and the fact that it was known that the deal with Manchester Boys was publicly known.

4.6.1.2.3 Abnormality test

I shall now consider whether in the ordinary course clubs dealing an arm's length would create the rights and obligations contained in the series of transfers.[215] But for

[213] D French and R Stretch op cite (n67) 26.3.2.
[214] Ibid.
[215] Section 80A(c)(i)

reduction of the tax liability and the cordial relationship between Thabo and Patrice, the transaction would not have been structured as it was. Clubs dealing at an arms-length do not usually include a third-party club in a series of transfers, so that the third-party club may gratuitously share in the future transfer fees. In the ordinary course, Jackson would have transferred directly from Golden Stars to Manchester Boys.

Accordingly, the series of transfers constitute an impermissible avoidance arrangement in terms of section 80A of the Income Tax Act. If the commissioner invokes their authority under Section 80B(1)(f) of the Income Tax Act, to treat the transaction as a transfer agreement between Golden Stars and Manchester Boys for the sum of R3 million, the following tax consequences would apply.

4.6.1.3 Tax implications for Golden Stars

Training Compensation

Notwithstanding the impermissible avoidance arrangement, in terms of the FIFA rules Manchester Boys are unconditionally liable to pay training compensation to Golden Stars. As described in previous scenarios, training compensation is imposed on acquiring clubs to reimburse training clubs for their out-of-pocket costs of developing a player. Accordingly, the training compensation is meant to plug a hole in the training club's revenue operations, and it must therefore be included in Golden Stars' gross income.

Transfer Fee

After the GAAR has been invoked, the R3 million transfer fee would be presumed to have accrued to Golden Stars, because Manchester Boys are unconditionally bound themselves to pay the amount.[216] The amount would however be excluded from gross income because the facts indicate that Jackson formed part of the club's capital structure and his disposal was merely a realisation of a capital asset.[217] Accordingly, in terms of the paragraph 11 (1) (a) of the Schedule, there would be CGT consequences for a disposal. Thus, the R3 million would constitute proceeds for the sale, and no amount can be included in the base cost. Therefore, Golden Stars would need to include R3 million as a net capital gain.

Fine

SAFA imposed R1.5 million fine on Golden Stars. Whether the fine is deductible from

[216] *Mooi* supra note 85 at 11.

[217]

Golden Stars' taxable income is contingent on whether the expense satisfies the requirements of section 11 (e) of the Income Tax Act, and that it does not fall under section 23 (o) of the Income Tax Act. Section 23 (o) of the Income Tax Act, prohibits the deduction of any penalties imposed on a taxpayer due to unlawful activities conducted in South Africa. An unlawful activity is generally understood to refer to conduct which is not authorised by law or a violation of a civil or criminal law. A contravention, of the FIFA rules, I contend is neither of these. The rules of a private association are not tantamount to legislation. Furthermore, the fine was incurred in relation to a player transfer, an activity closely linked to the taxpayer's business, therefore it was in relation to the taxpayers trade.[218] The transfer fee was, however, incurred for a purpose closely related to the taxpayer's income-generating structure and therefore it would constitute a capital expense and would not be deductible in terms of section 11 (a) of the Income Tax Act. It would, however, not trigger CGT consequences because there was no disposal in terms of paragraph 11 (1) of the Schedule.

4.6.1.4 Tax implications for FC Caledon

Transfer Fee

If the commissioner invokes Section 80B(1)(f) of the Income Tax Act the R1.5 million FC Caledon paid to Golden Stars and R1.5 million accrued from Manchester Boys would be disregarded for tax purposes. Accordingly, FC Caledon would not incur any tax liability from the transfer fees because no amount would have actually accrued to them in terms of section 1 of the Income Tax Act[219] nor would they have actually incurred an expense which could be deducted in terms of section 11 (a) of the Income Tax Act.[220]

Fine

The facts indicate that FC Caledon is club which specialises in the development and selling of players to foreign clubs in the scheme of profit-making. The fine incurred in relation to the bridge transfer was accordingly closely related with one of its revenue-generating activities and therefore the fine is of a revenue nature. SARS has stated that penalties incurred in commercial endeavours are deductible.[221] For this reason, I contend that it is likely that FC Caledon should be permitted to claim the fine as a tax

[218] *Port Elizabeth* supra note 119 at 16.
[219] *WH Lategan* supra note 84 at 20.
[220] *Port Elizabeth* supra note 119 at 15.
[221] AP de Koker and RC Williams 'Silke on South African Income Tax' (2022) *Lexis Nexis* at 7.30.

deduction in terms of Section 11 (a) of the Income Tax Act.

CHAPTER 5 - CONCLUSION

5.1 General

The private sector has grown to recognise the commercial potential of football. Over the last two decades, wealthy individuals and investment consortiums have mobilised their financial resources to purchase clubs, with the intention of building them into lucrative businesses. One can attribute to these developments the commercialisation of football, which in some instances, has led us to unfair competition and financial practices among clubs. A trend among well-endowed clubs is their aggressive pursuit to acquire the best players. In South Africa, for instance, Mamelodi Sundowns Football Club have confronted accusations of using its owners' wealth to acquire the best players to perpetually, and unfairly dominate the PSL.[222] The well-endowed clubs' scramble for talent, I contend, has created the conditions for smaller clubs to source and transfer players to them, in a scheme of profit-making.

FIFA, for instance, are concerned that a profit-driven transfer market has brought about bridge transfers, third-party ownership of player economic rights, the trafficking of minor players, and poaching practices which erode competition in football, and it has accordingly taken regulatory measures to supress these harmful practices. For these reasons, the UK government has published a report which recommends a player transfer tax for English premier league clubs, and for those resources to be allocated among grassroot clubs.[223]

If the transfer system has changed, so should the associated tax implications. Accordingly, SARS should take note of this and adapt their taxing strategy. In this pursuit, I contend that, among other measures, SARS should publish a guide dedicated to transfer fees and it should initiate an amendment to the Income Tax Act to allow for a limited tax exemption on training compensation receipts as motivated below.

5.2 Transfer fee guideline

5.2.1 General

SARS periodically publishes non-binding guides to assist taxpayers in the practical

[222] A Dithlobolo 'Mamelodi Sundowns weakening the PSL with big spending? – Motsepe hits back' (2022) available at: https://www.goal.com/en-za/news/mamelodi-sundowns-weakening-the-psl-with-big-spending-motsepe-hits-back/blt5a772852d602432c accessed on 19 November 2022.

[223] ESPN 'Premier League clubs urged to pay transfer tax in fan-led review of English football' (2021) available at: https://www.espn.com/soccer/english-premier-league/story/4530160/premier-league-clubs-urged-to-pay-transfer-tax-in-fan-led-review-of-english-football accessed on 19 November 2022.

interpretation of tax laws. In 2020, SARS published a Guide to explain the tax consequences for professional sports clubs and sports players in South Africa. Considering the commercialisation of football, I contend that SARS should publish a new guideline dedicated to transfer fees. The guideline should include the following:

I. tax implications for clubs in relation to permanent, temporary, and free transfers; and
II. examples of the application of anti-avoidance rules to bridge transfers, third-party ownership, and buyout clause transactions.

5.2.2 Tax implications of player transfers

In the Guide, SARS contend that 'it is unlikely that clubs could be said to be trading in players' contracts and the transfer fee will accordingly generally not be revenue in nature, but rather capital'.[224] The commercial developments in football and the practical scenarios illustrated in this paper, demonstrate that SARS' assertion is misguided. At an accelerating pace, clubs are engaging in speculative player transfer practices in the scheme of profit-making. For instance, the sole-owner, director, and coach of Jomo Cosmos (a club renowned for developing and selling players for large transfer fees) was once criticised by a former player for adopting a business model driven by selling players for profit. In response, the owner is quoted as having said: 'I do not sell players and then I go buy a Mercedes Benz or a Porsche. I take that money to run the club because I have to pay salaries'.[225] The owner essentially concedes that he perceives player transfers as a consistent revenue source. In these circumstances, I contend, the transfer fees received should constitute a revenue receipt.

Additionally, the Guide deals with permanent transfers, and to a small degree free transfers. The Guide does not take cognisance of loan transfers and that, in certain instances, an acquiring club will have to pay training compensation for free transfers, or a solidarity contribution for future transfers. These transfer methods are common in football and SARS should also deal with these.[226]

5.3 Training compensation

Training compensation is paid to clubs who invest in the training and education of young players who reach professional status. In essence, training clubs are rewarded

[224] SARS "Guide on the Taxation of Professional Sports Clubs and Players" (2020) at 6.
[225] S Ndebele "Yes, I sell players to run my club. What's the problem?" (2019) available at: https://www.sowetanlive.co.za/sport/soccer/2019-02-19-yes-i-sell-players-to-run-my-club-whats-the-problem-jomo-sono/ accessed on 15 November 2022.
[226] SARS op cite (n164) 7.

for investing in a public good. Section 10 of the Income Tax Act exempts certain income from taxation to encourage acts which advance social good. Examples of tax-exempt receipts include amounts received by employers from specific funds to train its employees and funds advanced for bursaries and scholarships.

I contend that training compensation is akin to the examples I have mentioned and thus SARS should initiate the amendment of the Income Tax Act to exempt training compensation received by training clubs. I am cognisant that if this suggestion were implemented, clubs which develop and sell players in the scheme of profit-making, could consequently receive large tax exemptions for receipts which should ordinarily flow to the national fiscus. Accordingly, I recommend that the tax exemption, like donations tax, should be capped to a value determined by SARS, after which the receipt would be taxed at a fixed rate. The limitation of this exemption would prevent clubs from engaging in exploitative practices harmful to minors.

I am also cognisant that the tariff for training compensation is calculated in relation to revenue expenditure which would have ordinarily been deductible from a club's taxable income in preceding years of assessment. It could be argued therefore that exempting training compensation from income tax would amount to a double tax benefit for clubs. Notwithstanding this, one must appreciate that clubs incur great financial risk when investing in the training and education of young players because very few reach professional status. Accordingly, this risk should be rewarded because it is an extraordinary contribution to South African football.

5.2.5 Concluding remarks

In this paper I have sought to critically evaluate SARS's assertion that clubs are unlikely to engage in player transfers in a scheme of profit-making. This was done by contextualising the origins of the transfer market and modern football regulations, the well-established common law tax principles, and applying these to practical scenarios. The practical scenarios incorporated a combination of transfer methods and demonstrated that the commercialisation of football has influenced the transfer market to the extent that clubs are increasingly engaging in speculative transfer practices. In other words, clubs are (at an accelerating rate) transferring players in a scheme of profit-making.

Accordingly, I concluded the paper by offering two recommendations. First, SARS must acknowledge these developments and publish a guideline in accordance thereto. The guideline should deal with:

I. tax treatment of permanent, temporary, and free transfers; and
II. include examples of the application of anti-avoidance rules to bridge transfers, third-party ownership, and buyout clause transactions.

Lastly, I propose the amendment of the Income Tax Act to provide for a limited tax exemption on training compensation received by clubs who train young players to become professionals, as the development of young players is social good which should be encouraged and rewarded.

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