

# Timing of immovable property transactions to determine the incidence of tax in South Africa

*Submitted to the University of Cape Town*

*In partial fulfilment of the requirement for the degree MCom(Taxation)*

*Faculty of Commerce*

*University of Cape Town*

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**Date: 19 September 2016**

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## ACKNOWLEDGEMENTS

I would like to extend my sincere gratitude to my supervisor Professor Jennifer Roeleveld, for her endless support, patience, helpful comments and encouragement.

Many thanks to my loving parents for their belief in me as well as their continual support and encouragement, especially when I thought I couldn't do it. Thank you for all the hours spent reading draft after draft. Thanks also to my son Ross who has believed in me and my abilities and who has and still does on a daily basis inspire me through his incredible determination and willpower.

## ABSTRACT

The main Acts applicable to the disposal of immovable property are the Alienation of Land Act 68 of 1981, the Deeds Registries Act 47 of 1937(DRA), the Sectional Titles Act 95 of 1986, the Subdivision of Agricultural Land Act 70 of 1970, the Transfer Duty Act 40 of 1949(TDA), the Value Added Tax Act 89 of 1991(VAT Act) and the Income Tax Act 58 of 1962(ITA). Apart from legislation there is also South African common law which is based on Roman-Dutch and English Law principles which also play an important role when dealing in immovable property.<sup>1</sup>

This dissertation focuses its review on the timing of immovable property transactions to determine the incidence of tax in South Africa and concentrates on the differences in the timing of ownership according to the ITA, VAT Act, TDA and DRA as well as common law principles.

International accounting standards have been reviewed and a comparison drawn between the accounting treatment of a disposal and the tax treatment as well as a comparison drawn up between South Africa and Australia with regards to how for tax purposes the disposal of immovable property is treated.

Statutory authority is necessary before taxes can be imposed and only the statute must be used in order to determine the liability for tax. Accounting or related principles are not taken into account when the tax liability is determined except in instances where the ITA specifically provides for it.<sup>2</sup>

The aim of this dissertation is to answer the question of whether there is a disconnect between the timing of the transfer of immovable property and the timing of the attendant taxation for the seller through analysing specifically the various Acts and laws which impact the transfer of immovable property.

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<sup>1</sup> Webbers Attorneys Notaries Conveyancers, Real Estate. [Online]. Available :<http://www.webberslaw.com/property-and-real-estate-2/> 21 April 2016

<sup>2</sup> University of South Africa, Tutorial Letter 102/0/2015 ADVANCED TAXATION 2015, Department of Financial Intelligence. [Online]. Available : [http://www.unisa.ac.za/contents/colleges/col\\_accounting\\_sciences/docs/cta/TAX4861\\_2015\\_TL\\_102\\_0\\_B.pdf](http://www.unisa.ac.za/contents/colleges/col_accounting_sciences/docs/cta/TAX4861_2015_TL_102_0_B.pdf) , 20 June 2016

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## ABBREVIATIONS

CGT	Capital Gains Tax
CIR	South African Revenue Service
DRA	Deeds Registries Act 47 of 1937
GAAP	Generally accepted accounting principles
IAS	International Accounting Standards
IFRS	International Financial Reporting Standards
ITA	Income Tax Act 58 of 1962
SA	South Africa
SARS	South African Revenue Service
SIR	South African Revenue Service
TDA	Transfer Duty Act 40 of 1949
VAT	Valued Added Tax Act 89 of 1991

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## 1.1 Background

'Immovable property' is not defined in the Income Tax Act 58 of 1962 (ITA) neither is it specifically defined in the Eighth Schedule.<sup>3</sup> In Notes to South African Income Tax, Haupt explains that if a word is not defined or is incompletely defined in the ITA the Interpretation Act must be referred to for a definition. If the word is not defined in the Interpretation Act, the word or phrase must be interpreted according to the ordinary meaning in the dictionary. Haupt goes on to say that "full effect must be given to all the words used in a provision. No word must be assumed to be superfluous. Where a provision does not make sense the courts have had to (of necessity) imply words or meanings." In the *Tax Case No. 12860* of 22 June 2012 Mbha J stated "It is accepted generally that the meaning of the words in a statute is derived from the common-law. The basic rule of interpretation is that the meaning must, unless it would result in an absurdity, be taken to be the ordinary meaning of the word which can now be found in a dictionary of established authority."<sup>4</sup>

Immovable property is not defined in the Interpretation Act 33 of 1957<sup>5</sup> and the ordinary dictionary meaning of 'immovable' indicates that it means not able to be moved or that it constitutes land, buildings, or other permanent items.<sup>6</sup> 'Property' is defined as a thing or things belonging to someone or a building or buildings and the land belonging to it or them.<sup>7</sup>

In 2013 a research study was conducted to determine the size of the immovable property market in South Africa. At that stage it was estimated to be worth in excess of R4.9 trillion. According to this study only 1% of land in South Africa is urban and residential, the rest is natural pasture, agriculture and nature reserves. Of the R4.9 trillion, R3 trillion is the estimated value of residentially owned property.<sup>8</sup>

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<sup>3</sup> Govender P, Does a mineral right constitute 'immovable property' for purposes of the Income Tax Act and double tax treaties? PG Tax Masters 28 February 2014, page 17

<sup>4</sup> Haupt P, Notes on South African Income Tax 2016, Thirty Fifth Edition, chapter 1, page 12

<sup>5</sup> Govender P, Does a mineral right constitute 'immovable property' for purposes of the Income Tax Act and double tax treaties? PG Tax Masters 28 February 2014, page 17

<sup>6</sup> Dictionary.com. [Online] Available: <http://www.dictionary.com/browse/immovable>, 7 September 2016

<sup>7</sup> Dictionary.com. [Online], Available: <http://www.dictionary.com/browse/property>, 7 September 2016

<sup>8</sup> SA Chamber of Commerce. How big is the property market in South Africa. [Online]. Available : <http://www.sa-chamber.co.za/how-big-is-the-property-sector-in-south-africa>, 22 April 2016

According to the Estate Agency Affairs Board of South Africa there are 5.8 million registered residential properties which make up about 86% of the immovable property industry in South Africa. The number of new registrations per year for residential properties are about 65 000.<sup>9</sup>

In terms of common law in South Africa the registered owner of immovable property is the owner of the land and all the buildings and other fixed improvements situated on that land. Up until 1971 when the first Sectional Title Act was promulgated it was not possible to separate ownership of a building or portion of a building from the immovable property, now this can be done.<sup>10</sup>

The main Acts applicable to the disposal of immovable property are the Alienation of Land Act 68 of 1981, the Deeds Registries Act 47 of 1937, the Sectional Titles Act 95 of 1986, the Subdivision of Agricultural Land Act 70 of 1970, the Transfer Duty Act 40 of 1949, the Value Added Tax Act 89 of 1991 and the Income Tax Act 58 of 1962. Apart from legislation there is also South African common law which is based on Roman-Dutch and English Law principles which also play an important role when dealing in immovable property.<sup>11</sup>

South Africa is seen to have one of the most sophisticated and reliable immovable property register systems in the world when it comes to defining the boundaries of properties and the positions of the rights affecting those properties.<sup>12</sup>

According to the provisions of section 16 of the Deeds Registries Act 47 of 1937 ownership of immovable property only takes place once the transfer of ownership has been registered in the deeds office.

The registration of immovable property **in the deeds office** will deem that the person concerned is the lawful owner of the right and that registration is regarded as a notice to the rest of the world of the validity of the right to the immovable property.<sup>13</sup>

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<sup>9</sup> Estate Agents Affairs Board of South Africa, The South African Residential Property Market : An Overview. [Online]. Available : <http://www.housingfinanceafrica.org/wp-content/uploads/2015/09/The-South-African-Housing-Market-Overview-2015.22>, April 2016

<sup>10</sup> Webbers Attorneys Notaries Conveyancers, Real Estate. [Online]. Available :<http://www.webberslaw.com/property-and-real-estate-2/> 21 April 2016

<sup>11</sup> Webbers Attorneys Notaries Conveyancers, Real Estate. [Online]. Available :<http://www.webberslaw.com/property-and-real-estate-2/> 21 April 2016

<sup>12</sup> Ibid

<sup>13</sup> Boshoff Dr D, Understanding the Basic Principles of Property Law in South Africa, Professional Skills Module No.8, Revised 30 August 2013, page 21

The ITA is however not aligned with the other Acts and common law principles and deems timing of ownership of immovable property, for tax purposes, to occur once all the suspensive conditions in the contract are met.

It is evident that there are a number of discrepancies between the various Acts as well as common law principles when it comes to the timing of when ownership in immovable property is deemed to take place. The Transfer Duty Act does not specifically mention when ownership takes place but does indicate that the acquisition of property is seen to be the date that the transaction was entered into. The VAT Act deems ownership to take place at the sooner of transfer or payment while the ITA deems ownership to take place once all suspensive conditions of the sale agreement has taken place. The Deeds Registries Act makes it clear that ownership will only pass once the immovable property has been registered in the Deeds Registries Office.

Differences in the timing of the passing of ownership and lack of clear consensus on what immovable property comprises results in transactions transferring ownership being treated differently for income tax, value added tax, capital gains tax and transfer duty purposes as to when taxes need to be declared and paid.

## **1.2 Research Objective**

This dissertation proposes to address the different timing issues surrounding the disposal of immovable property and when ownership is passed from the seller to the buyer. The dissertation therefore aims to answer the question of whether there is a disconnect between the timing of the transfer of immovable property and the timing of the attendant taxation for the buyer and the seller. The dissertation will analyse specifically, the various Acts and laws which impact the transfer of immovable property.

## **1.3 Research Method**

This dissertation is carried out in the area of legal interpretative research, specifically doctrinal research.

Doctrinal research is described by McKerchar: 2008 as “Research methodology which provides a systematic exposition of the rules governing a particular legal category, analyses the relationship between rules, explains areas of difficulty and, perhaps, predicts future developments.”

In this context in order to fulfil the research objectives of the dissertation an extended literary review as well as detailed study is undertaken of the relevant sections, paragraphs and articles in The South African Income Tax Act 58 of 1962 (ITA), Transfer Duty Act 40 of 1949, Value

Added Tax Act 89 of 1991 (VAT Act), Deeds Registries Act 47 of 1937, Common law principles of property in South Africa, and various articles and court decisions.

#### **1.4 Limitation of the scope**

The scope of this dissertation is on the disposal of immovable property and the timing issues which surround this. The study will be limited to the relevant sections, paragraphs and articles in the ITA, Transfer Duty Act, VAT Act, Deeds Registries Act, Principles of Property Law in South Africa, and the *SIR v Silverglen Investments (Pty) Ltd* [1969 (1) SA 365 (AD) 30 SATC 199] case which impact the ownership of immovable property. The tax treatment surrounding the timing of the disposal of immovable property in Australia is also compared to that of South Africa. Australia has been chosen for the comparison as there are a number of similarities between capital gains tax as well as other legislation in the two countries.

Only full ownership in immovable property with regards to residential and or commercial property will be considered and other types of limited interests in property, i.e. usufructs and fiduciary interests are excluded from the scope.

#### **1.5 Structure of the dissertation**

The Dissertation will take on the following structure:

- 1.5.1 Chapter 2: Identifying and defining relevant terminology relating to the disposal and ownership of immovable property.
- 1.5.2 Chapter 3: The process involved in the disposal and ownership of immovable property.
- 1.5.3 Chapter 4: Various Acts and paragraphs in the relevant Acts as well as laws surrounding the disposal of immovable property and when ownership is transferred.
- 1.5.4 Chapter 5: A comparison between the timing treatment of the disposal of immovable property for accounting and tax purposes.
- 1.5.5 Chapter 6: A comparison of the way in which Australia treats the disposal of immovable property for tax purposes compared to how it is treated in South Africa.
- 1.5.6 Chapter 7: Conclusion and recommendations.

**Chapter 2: Identifying and defining relevant terminology relating to the disposal and ownership of immovable property**

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## **2.1 Introduction**

Certain terminology will be used and referred to throughout the dissertation. For the sake of clarity these terms have been defined according to the various Acts in this chapter.

## **2.2 Relevant terminology defined**

### **2.2.1 Income Tax Act 58 of 1962**

**Gross income** “in relation to any year or period of assessment means –

(i) in the case of any resident, the total amount, in cash or otherwise, received by or accrued to or in favour of such resident; or

(ii) in the case of any person other than a resident, the total amount, in cash or otherwise, received by or accrued to or in favour of such person from a source within the Republic during such year or period of assessment, excluding receipts or accruals of a capital nature.....”

This definition is relevant for determining whether an inclusion in gross income is necessary. This would apply when an asset/ property is used in a business, allowances have been granted on the assets and the asset/property is subsequently sold giving rise to recoupments of previous allowances granted (section 8(4)(a). See discussion in chapter 4.

### **2.2.2 Eighth Schedule to the Income Tax Act 58 of 1962**

#### **Section 1**

**Asset** includes –

“(a) property of whatever nature, whether movable or immovable, corporeal or incorporeal, excluding any currency, but including any coin made mainly from gold or platinum; and

(b) a right or interest of whatever nature to or in such property.”

Therefore, immovable property falls under the definition of asset and has no further special selection under the Eighth Schedule. Disposal and the time of disposal (paragraph 13) of the Eighth Schedule are relevant and are defined below. The Eighth Schedule is discussed in Chapter 4.2.

**Disposal** means –

“An event, act, forbearance or operation of law envisaged in paragraph 11 or an event, act, forbearance or operation of law which in terms of this Schedule treated as the disposal of an asset, and “dispose: must be construed accordingly.”

“In terms of paragraph 11 a disposal includes-

(a) the sale, donation, expropriation, conversion, grant, cession, exchange or any other alienation or transfer of ownership of an asset .....

A disposal, whether an actual disposal or event treated as a disposal, is necessary before the provisions of the Eighth Schedule can apply. See discussion in Chapter 4.

**Suspensive conditions** according to the SARS Capital Gains Tax Guide refers –

“A suspensive condition suspends the full operation of the obligation under a contract and renders it dependent on an uncertain future event.”<sup>14</sup>

**Legal fiction** is defined by Prof Gerrie Swart in the SARS Guide as follows –

“A legal fiction is created, in other words, that the asset involved is transferred or delivered to the person entitled thereto on the date on which the unconditional right to claim such transfer or delivery arises, even though the actual transfer or delivery may be effected only at a later date (including a date falling in a later tax year, or which might, due to unforeseen circumstances, never occur). This artificial rule is of profound importance. By treating the transfer or change of ownership of an asset as taking place on the date on which and during the tax year in which the contract is concluded or becomes unconditional, the fictional change of ownership precedes the actual change of ownership. The rule therefore operates prospectively, with the result that the change of ownership is drawn back and recognized in the tax year in which the initial contractual right arises. The actual transfer or delivery of the asset in a later tax year is ignored as it does not qualify as a disposal in that year.”<sup>15</sup>

### **2.2.3 Deeds Registries Act 47 of 1937**

**Immovable property** includes -

“(a) .....[Para. (a) deleted by s. 53 of Act 24/2003]

(b) any registered lease of land which, when entered into, was for a period of not less than ten years or for the natural life of the lessee or any other person mentioned in the lease, or which is renewable from time to time at

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<sup>14</sup> South African Revenue Service, Comprehensive Guide to Capital Gains Tax (Issue 4), page 109

<sup>15</sup> South African Revenue Service, Comprehensive Guide to Capital Gains Tax (Issue 4), page 110-111

the will of the lessee indefinitely or for periods which together with the first period amount in all to not less than ten years;

(c) a registered right of leasehold; and

(d) a registered right of initial ownership contemplated in section 62 of the Development Facilitation Act, 1995;”

**Owner** means, in relation to -

“(a) immovable property, subject to paragraph (b), the person registered as the owner or holder thereof and includes the trustee in an insolvent estate, a liquidator or trustee elected or appointed under the Agricultural Credit Act, 1966 (Act 28 of 1966), the liquidator of a company or a close corporation which is an owner and the executor of any owner who has died or the representative recognized by law of any owner who is a minor or of unsound mind or is otherwise under disability, provided such trustee, liquidator, executor or legal representative is acting within the authority conferred on him or her by law; [Para. (a) substituted by s. 22 of Act 14/93 and s. 9 of Act 11/96]

(b) immovable property, real rights in immovable property and notarial bonds -

(i) which are registered in the name of both spouses in a marriage in community of property, either one or both of the spouses.”

**Real right** “includes any right which becomes a real right upon registration.”

**Registrar** means “a registrar of deeds appointed under this Act, and, when used in relation to any deeds registry means the registrar in charge of that deeds registry; and when used in relation to a document means the registrar in charge of the deeds registry wherein that document is registered or registrable or intended to be used or filed.”

#### **2.2.4 Transfer Duty Act 40 of 1949**

**Property** means:

“ land in the Republic and any fixtures thereon, and includes –

(a) Any real right in land but excluding any right under a mortgage bond or lease of property other than a lease referred to in paragraph (c); .....

**Date of acquisition** means –

“(a) in the case of the acquisition of property (other than the acquisition of property contemplated in paragraph (b)) by way of a transaction, the date on which the transaction was entered into, irrespective of whether the transaction was conditional or not or was entered into on behalf of a company already registered or still to be registered and, in the case of the acquisition of property otherwise than by way of a transaction, the date upon which the person who so acquired the property became entitled thereto: provided that where property has been acquired by the exercise of an option to purchase or a right of pre-emption, the date of acquisition shall be the date upon which the option or right of pre-emption was exercised;

(b).....”

The Transfer Duty Act, therefore, only refers to ‘the date on which the transaction was entered into’. This is discussed in Chapter 4.5.

**Transaction** means –“(a) in relation to paragraphs (a) and (c) of the definition of “property”, an agreement whereby one party thereto agrees to sell, grant, waive, donate, cede, exchange, lease or otherwise dispose of property to another person or any act whereby any person renounces any right in or restriction in his or her favour upon the use or disposal of property; or .....

### 2.2.5 Land Survey Act 8 of 1997

**Owner** “in relation to land, means the person registered in a deeds registry as the owner of such land, and includes -

(a) the liquidator of a company or close corporation or the representative recognized by law of any owner who has died, become insolvent, assigned his or her estate, is a minor or of unsound mind or is otherwise under disability, provided that such liquidator or representative acts within the power conferred on him or her by law;

(b) the person in whom the ownership of the land is vested by statute, and the allottee of land held under provisional title and in process of alienation by the State;

(c) the lessee of land held under a lease for a period of 99 years registered in a deeds registry, and in the Province of KwaZulu-Natal a lease of land from the State for a period of 99 years; or

(d) or for the purposes of sections 19, 22, 23, 24, 25, 29, 31, 33, 34 and 36, the holder of a right to minerals in respect of such land; (ix)”

### 2.2.6 Basic principles of property law

**There are certain basic principles regarding property which are entrenched in property law.** These are presented below:

**Delivery of an Immovable** according to Zulman in Normans Law of Purchase and Sale in South Africa means “in the case of a sale, the delivery is effected by passing transfer of the immovable *coram lege loci* in accordance with the Deeds Registries Act 47 of 1937, as amended. In Normans Law it states that the seller will remain the owner until the immovable property has been registered in the name of the purchaser by the Registrar of Deeds in terms of the Act.”<sup>16</sup>

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<sup>16</sup> Zulman RH, Norman’s Law of Purchase and Sale in South Africa, 5<sup>th</sup> Edition 2005, page114

**Ownership** according to Dr Douw Boshoff in The South African Council for the Quantity Surveying Profession, Professional Skills Module No. 8, Understanding the Basic Principles of Property Law in South Africa is stated as:

“Ownership can be described as an abstract legal relationship, which implies that:

(a) a legal relationship exists between the owner and a thing (object) in terms of which the owner acquires certain entitlements, and

(b) a relationship exists between the owner and other legal subjects in terms of which the owner can require that others respect his entitlements regarding the object.

The relationship:

(c) consists of indeterminate entitlements in that they vary from time to time regarding the same relationship or regarding different relationships, and

(d) is limited by statutory measures, limited real rights, creditor’s rights of third parties and the interest of the community.”<sup>17</sup>

## **Property rights**

“Property rights are all rights that form the subject of the **law of property** and would include real rights, which is a right in something belonging to oneself; a limited real right, which is a right in something belonging to somebody else; or a creditor’s right, which is the right to claim something from another person, being a judicial person or a natural person. Sometimes it is difficult to distinguish if a right is a limited real right or a creditor’s right, but it is important to understand the main difference in that a limited real right is a right in the property of somebody else, and the right is transferred to a new owner should the property be alienated, while a creditor’s right is a right against a person, not a thing.”<sup>18</sup>

## **Real rights**

“Real rights usually deal with corporeal things and as it refers to rights in something belonging to oneself, it refers to ownership, which is the most comprehensive right that one can have in something. This right is however limited by the rights of others in one’s property. In the construction industry the following would be examples of real rights:

The land or construction site on which a building would be erected, which is the property of the employer.

The material, plant and equipment of the contractor, which is the property of the contractor.

Any material that is acquired on credit, which is the property of the material supplier.

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<sup>17</sup> Boshoff Dr D, The South African Council for the Quantity Surveying Profession, Professional Skills Module No. 8, Understanding the Basic Principles of Property Law in South Africa. Van der Walt, AJ & Pienaar, GJ 2009. Introduction to the Law of Property. Sixth Edition. Juta.

<sup>18</sup> Ibid

Any equipment, which is financed by way of a lease, which is the ownership of the financing institution.”<sup>19</sup>

### **2.2.7 Conclusion**

The definitions and principles described above will be used in the following chapters to address the main objective of this dissertation which is to consider the possible variances in the timing of ownership and sale of property transactions in terms of the rules. It is also necessary to outline the procedures involved in order to transfer ownership in property and these are first outlined in chapter 3 in order to inform the study further.

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<sup>19</sup> Boshoff Dr D, The South African Council for the Quantity Surveying Profession, Professional Skills Module No. 8, Understanding the Basic Principles of Property Law in South Africa, Revised 30August 2013, page9.

## **Chapter 3: The process involved in the disposal and ownership of immovable property**

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### **3.1 The procedure involved in the disposal and transfer of immovable property**

#### **Introduction**

The disposal of immovable property in South Africa is a complicated and sometimes lengthy process. There are many factors which play a role when disposing of immovable property and no two transactions are the same.<sup>20</sup> A comprehensive legal framework exists for the transfer of ownership in immovable property and it is underpinned by statute.<sup>21</sup> Below is a broad outline of the process involved in the disposal and transfer of immovable property. This is done in order to show that the timing of the disposal is not always easy to determine.

#### **Deed of Sale**

In order for there to be a sale of a property there must be a signed written deed of sale between the seller and the purchaser. Common law dictates that the contract must contain a full description of the property being sold, the purchase price and the manner in which the purchase price will be paid.<sup>22</sup>

#### **Estate Agent**

In most property sales the seller will appoint an estate agent to act on his/her behalf to find a buyer. The seller is liable for the commission which is payable to the estate agent. This becomes due once the agent has found a willing buyer for the property and therefore has fulfilled his mandate. The commission is usually added to the sellers' asking price so in effect the purchaser is actually paying the commission. An estate agent will use their own contract which is referred to as an "offer to purchase" which is in effect the same as a deed of sale. Once the seller has accepted the offer by signing the contract the result is a deed of sale as required by section 2(1) of the Alienation of Land Act 68 of 1981.

#### **Suspensive Conditions**

In many sales the purchaser will require a loan/mortgage to pay for the property. The deed of sale, in these situations, will therefore be made subject to the obtaining of this loan and should the purchaser not be able to obtain the necessary loan the deed of sale will lapse. If the loan is

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<sup>20</sup> Webbers Attorneys Notaries Conveyancers, Real Estate. [Online]. Available :<http://www.webberslaw.com/property-and-real-estate-2/> 1 May 2016. P5

<sup>21</sup> Bembridge, A. 8 May 2013. ENSight. The Real Estate Law Review, Second Edition – South Africa. [Online]. Available :<https://www.ensafrica.com/news/The-Real-Estate-Law-Review-Second-Edition-South-Africa>

<sup>22</sup> Webbers Attorneys Notaries Conveyancers, Real Estate. [Online]. Available :<http://www.webberslaw.com/property-and-real-estate-2/> 1 May 2016. P5

granted then the suspensive conditions of the deed of sale are met and the contract is now made complete. The transaction could also be made subject to the buyer being able to sell an existing property which will provide funds for the new purchase. This could also be a suspensive condition.

### **Transferring Attorney**

The transferring attorney will be the attorney appointed by the seller to legally execute the sale of the property. The transfer attorney is responsible for the registration of transfer of ownership of the immovable property from the seller to the purchaser. The purchaser is also entitled to appoint their own attorney.

Once the transfer attorney receives the instructions to start the transfer process a search will be done by the transfer attorney to verify the present owner, the description of the property, relevant title deed conditions and possible problems. If the buyer or seller is a company or close corporation the attorney will also verify company records.<sup>23</sup>

The Financial Intelligence Centre Act 38 of 2001 also requires that both the buyer and the seller provide the following documents to the transfer attorney in part 2 section 2:

- Copies of identity documents
- Proof of physical address
- Income tax and VAT registration numbers
- Marriage certificates if applicable
- Antenuptial contracts
- Divorce orders
- In the case of a company or close corporation incorporation documents or if a trust, the trust deed.<sup>24</sup>

The transferring attorney will also need the original existing title deed of the property being transferred.

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<sup>23</sup> Webbers Attorneys Notaries Conveyancers, Real Estate. [Online]. Available :<http://www.webberslaw.com/property-and-real-estate-2/> 1 May 2016. Page 6.

<sup>24</sup> Ibid page 7.

Once the transferring attorney has received all the necessary documents he can then proceed with the following steps:

1. Rates clearance certificate

A change in ownership may not take place until a certificate is lodged with the deeds office certifying that all rates, taxes and services are up to date for the last two years.<sup>25</sup>

2. Transfer duty receipt

Transfer duty is levied on every transfer of immovable property (not subject to value added tax (VAT)<sup>26</sup> and is payable by the purchaser. The receipt from the South African Revenue Service (SARS) for the payment of transfer duty must be lodged at the Deeds Office together with the other registration documents. In order for a certificate to be issued by SARS, a transfer duty declaration must be submitted to SARS in this declaration<sup>27</sup> SARS requires that all parties involved in the transaction, which include the estate agents, must supply their income tax and value added tax (VAT) registration numbers.

3. Levy Clearance Certificate

“According to the Sectional Titles Act, 95 of 1986

(3) The registrar shall not register a transfer of a unit or of an undivided share therein, unless there is produced to him-

(a) .....

(b) a clearance certificate from the local authority that all rates and moneys due to such local authority under any law in respect of the land and buildings of the scheme have been paid if-

(i) provision is made by law for the separate rating of units; or

(ii) the transfer will result in the establishment of a body corporate in terms of section 36;

(c) if the transferor is a developer, an affidavit by the developer in which it is declared whether the relevant unit is a unit to which the provisions of section 10 apply or not and, if those provisions so apply,

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<sup>25</sup> Webbers Attorneys Notaries Conveyancers, Real Estate. [Online]. Available :<http://www.webberslaw.com/property-and-real-estate-2/> 1 May 2016. Page 8

<sup>26</sup> If the seller is a registered VAT vendor then VAT will be levied on the proceeds of the sale. This means that no Transfer Duty will then be applicable.

<sup>27</sup> South African Revenue (SARS website) [online]. Available :<http://www.sars.gov.za/TaxTypes/TransferDuty/Pages/default.aspx>, 20 July 2016

that the transfer is effected in terms of a contract which is not contrary to any provision of that section.”<sup>28</sup>

Therefore if the property is a sectional title property the transferring attorney must obtain a clearance certificate from the body corporate certifying that all levies payable by the owners are fully up to date.<sup>29</sup>

#### 4. Transfer Documents

Once the transferring attorney has all the necessary documents he will prepare the transfer documents for the seller and purchaser to sign.

#### 5. Preparation for Lodgement

Once the transferring attorney has the above documents signed he will then wait for the following documents before being able to lodge the transfer at the Deeds Office:

Rates clearance certificate

Levies clearance certificate

Guarantees for the purchase price

Original title deed

Consent of cancellation of existing bond

Other relevant consent

Transfer duty receipt or exemption<sup>30</sup>

#### 6. Lodgement at the Deeds Office

All the documents for transfer of the property are now lodged at the Deeds Office.

#### 7. Examination and Preparation

The Deeds Office will examine the documents and this process will take approximately a week.

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<sup>28</sup> Sectional Titles Act, 95 of 1986

<sup>29</sup> Webbers Attorneys Notaries Conveyancers, Real Estate. [Online]. Available :<http://www.webberslaw.com/property-and-real-estate-2/> 1 May 2016. Page 9.

<sup>30</sup> Ibid Page 10.

## 8. Registration

If all the documents are in order they are registered. The transferring attorney and a designated Deeds Office official will sign the documents in a special room at the Deeds Office and staff of the Deeds Office will update their records.

## 9. Procedure after Registration

The seller and the buyer are now advised and all required payments are now made. The final account is now prepared by the transferring attorney.

## 10. Delivery of Registration Documents

Approximately a week after registration at the Deeds Office the registered documents will be returned to the transferring attorney and they will send the new title deed and mortgage bond to the relevant financial institution or where there is no bond then the title deeds will be handed over to the purchaser.<sup>31</sup>

### **3.2 How ownership in immovable property is determined**

South Africa is seen to have one of the most sophisticated and reliable real estate register systems in the world when it comes to defining the boundaries of properties and the positions of the rights affecting those properties.<sup>32</sup>

The term ownership can be found in common law and has been defined in South African case law. Ownership is defined as the *most complete real right that a legal subject can have regarding a thing or can be defined as the real right which gives the owner the most complete and absolute entitlement to a thing.*<sup>33</sup>

Ownership in South Africa can be acquired in two different ways, original acquisition and derivative acquisition of ownership. Derivative acquisition is where the owner cannot transfer more rights than he had himself, therefore there is a preceding owner that is transferring certain rights in the property to a new owner. Original acquisition of ownership is where there

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<sup>31</sup> Webbers Attorneys Notaries Conveyancers, Real Estate. [Online]. Available : <http://www.webberslaw.com/property-and-real-estate-2/> 1 May 2016. Page 11.

<sup>32</sup> Ibid Page 3.

<sup>33</sup> Boshoff Dr D, The South African Council for the Quantity Surveying Profession, Professional Skills Module No. 8, Understanding the Basic Principles of Property Law in South Africa, Revised 30 August 2013, page 11. See also the definition of real rights in property in chapter 2 of this dissertation.

is no previous owner that influences the entitlements of the new owner. In order for ownership to occur certain requirements must be met, in general the requirements are as follows:

- The item to be transferred must be negotiable
- The transferor must have contractual capacity over the property
- The transferor must be the owner of the property
- The transferee must have the contractual capacity to accept the transfer of ownership
- The ownership of the property must be accepted by the transferee
- Transfer of ownership of immovable property will only take place with delivery and with immovable property in the event of registration in the deeds office
- Registration of immovable property must take place with the intention of the transferor to transfer ownership and the intention of the transferee to accept ownership
- There must be a legal cause for transfer
- If ownership is transferred based on a contract of sale, transfer will only take place once the full purchase price has been paid.<sup>34</sup>

According to the Deeds Registries Act (DRA) ownership of immovable property only takes place once the transfer of ownership has been registered in the Deeds office. The fundamental principles of the DRA are as follows:

**“Section 13. When registration takes place**

(1) Deeds executed or attested by a registrar shall be deemed to be registered upon the affixing of the registrar’s signature thereto, and deeds, documents or powers of attorney lodged for registration shall be deemed to be registered when the deeds registry endorsement in respect of the registration thereof is signed: Provided that no such deed, document or power which is one of a batch of interdependent deeds, documents or powers of attorney intended for registration together, shall be deemed to be registered until all the deeds, documents or powers of attorney or the registration endorsements in respect thereof, as the case may be, have been signed by the registrar.

(2) If by inadvertence the registrar’s signature has not been affixed to a deed executed or attested by him, or to the registration endorsement in respect of the registration of a deed, document or power of attorney lodged for registration, at the time at which the signature should have been affixed in the

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<sup>34</sup> Boshoff Dr D, The South African Council for the Quantity Surveying Profession, Professional Skills Module No. 8, Understanding the Basic Principles of Property Law in South Africa, Revised 30 August 2013, page 21

ordinary course, the registrar may affix his signature thereto when the omission is discovered, and the deed, document or power of attorney shall thereupon be deemed to have been registered at the time aforesaid.

(Section 13(3): Decided cases)

(3) All endorsements or entries made on deeds, documents or powers of attorney or in registers, in connection with the registration of any deed, document or power of attorney, shall be deemed to have been effected simultaneously with the affixing of the signature of the registrar thereto in respect of deeds executed or attested by a registrar or with the signing of his registration endorsement in respect of deeds, documents or powers of attorney lodged for registration, although in fact they may have been made subsequent thereto.

(4) Any deed, document or endorsement which under this section is required to be signed by a registrar, may, if the registrar is not available to sign such deed, document or endorsement, be signed by the successor in office of the registrar or by any person acting in the place of the registrar, whereupon any reference in subsection (1) or (3) to the signature of the registrar shall be deemed to include a reference to the signature of such successor or person acting as registrar, as the case may be.”<sup>35</sup>

In terms of Section 16 of the DRA ownership of immovable property can only take place by means of a deed of transfer.

The registration of rights in immovable property will deem that the person concerned is the lawful owner of the right and that registration is regarded as a notice to the rest of the world of the validity of the right to the immovable property.<sup>36</sup>

### **3.3 VAT or Transfer Duty on the disposal of immovable property in South Africa**

If the seller is a registered VAT vendor, VAT will be payable on the transaction. The purchaser will not be liable to pay transfer duty in this case but will of course have to pay the full purchase price which will include VAT. If the seller is not a registered VAT vendor then transfer duty is payable by the purchaser on the transaction.

However in the case of residential property being sold, unless the seller is a property developer the transaction will be subject to transfer duty.<sup>37</sup> This is because the supply of residential accommodation is an exempt supply (section 12(c) of the VAT Act).

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<sup>35</sup> Deeds Registries Act 47 of 1937

<sup>36</sup> Boshoff Dr D, The South African Council for the Quantity Surveying Profession, Professional Skills Module No. 8, Understanding the Basic Principles of Property Law in South Africa, Revised 30<sup>th</sup> August 2013, page 21

<sup>37</sup> Davies, B. Vat or Transfer Duty On The Sale of Property in SA. [Online]. Available :<http://www.chaseveritt.co.za/vat-or-transfer-duty>, page 1, 1 May 2016

### **3.4 Conclusion**

By understanding the process involved in the disposal and transfer of immovable property it is clear that the timing of ownership and when this occurs is of relevance. Various Acts and Common Law principles surround the ownership and transfer of immovable property and will define the timing of ownership. The timing of ownership is of utmost importance especially from an income tax and VAT perspective as this will have a direct bearing on when the capital gain or income will need to be declared and taxes paid.

**Chapter 4: Various Acts and paragraphs in the relevant Acts as well as laws surrounding the disposal of immovable property and when ownership is transferred**

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## **4.1 Introduction**

There are a number of Acts as well as common law principles that are applicable when dealing with the disposal or acquisition of immovable property. Ownership of immovable property is evidenced by a title deed which is issued by the deeds registry. If ownership is not registered in the deeds registry it is more than likely that ownership of the property has not been passed.<sup>38</sup> The various Acts as well as common law principles with regards to the disposal of immovable property will be discussed below specifically dealing with the timing of the disposal of the property and when ownership is deemed to occur.

In respect of the ITA two specific areas need to be explored when dealing with the disposal of immovable property. This relates to the two main different reasons for holding/acquiring immovable property which are: acquiring the property for resale or acquiring the property as an investment. Where the property is acquired as an investment (capital intention), the sale of that property will have capital gains tax consequences and if acquired for resale (revenue intention), the sale of the property is dealt with as ordinary gross income. The timing of these transactions is dealt with below in order to determine when the gain or proceeds must be accounted for, for tax purposes.

## **4.2 Income Tax Act– Acquiring the immovable property as an investment**

The Eighth Schedule of the (ITA) deals specifically with the determination of a gain or loss for the purposes of including a taxable capital gain in income in terms of section 26A of the ITA. Paragraph 13 of the Eighth Schedule determines the time of disposal of an asset. An asset includes immovable property as noted in chapter 2.2.2.

According to paragraph 13(1)(a) of the Eighth Schedule, a change in ownership occurs between one person to another in an agreement on the date that all the suspensive conditions<sup>39</sup> are met. In the case where there is an agreement and there are no suspensive conditions it will then be on the date that such agreement is concluded.

When immovable property is held as an asset for investment purposes, the time of disposal is the factor which will determine when the capital gain or loss will need to be accounted for.<sup>40</sup>

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<sup>38</sup> Bembridge, A. 8 may 2013. ENSight. The Real Estate Law Review, Second Edition – South Africa. [Online]. Available :<https://www.ensafrica.com/news/The-Real-Estate-Law-Review-Second-Edition-South-Africa>, 13 April 2016

<sup>39</sup> See discussion in chapter 3 and definitions in chapter 2.2.2.

<sup>40</sup> South African Revenue Service, Comprehensive Guide to Capital Gains Tax (Issue 4), page 104

## Timing rules

In *SIR v Silverglen* [1969] (1) SA 365 (AD) 30 SATC 199 it was held that a contract is concluded at the stage when agreement is reached between the parties.<sup>41</sup> Even though the parties may have inserted an effective date in the contract, this will have no bearing on the time of the disposal as has been laid down in paragraph 13. The date of disposal will be the date that the agreement is concluded if there are no suspensive conditions or if there are suspensive conditions, the date when the suspensive conditions have been met.

A suspensive condition is a condition which will suspend all rights and obligations until a certain future event occurs. Once the future event has taken place the suspended part of the contract is brought to life and made effective. If on the other hand the suspensive condition is never fulfilled, the suspended rights and obligations will never come into existence and it will be as though they never existed.<sup>42</sup>

According to paragraph 13 of the Eighth Schedule a change of ownership will result in the disposal of an asset. The effect of the rule is that a legal fiction is created whereby the asset has been transferred or delivered on the date on which the agreement was concluded (contractual rights created)<sup>43</sup> which may precede actual ownership.

This type of “deemed” ownership is referred to as a legal fiction. The actual change in ownership will be at the date when the property is transferred from the buyer to the seller and registered in the deeds registry as discussed above in chapter 2.

Paragraph 13 deems ownership to take place once the agreement has been concluded. Even though ownership is deferred and requires performance on the part of the seller, this in itself does not make ownership a suspensive condition. Ownership is seen as a one of the terms of the contract and even if ownership does not occur this gives rise to ordinary contractual remedies of a compensatory nature.<sup>44</sup>

Therefore the actual transfer of the immovable property in a subsequent tax year is ignored and will not qualify as a disposal in that year. Even if there is a delay in actual transfer or deemed delivery of the immovable property, according to paragraph 13(1)(a)(ii) this will not

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<sup>41</sup> *SIR v Silverglen Investments (Pty) Ltd* (1969) 30 SATC 199, page 201.

<sup>42</sup> Norton Rose Fulbright, Publication July 2009, To be or not to be the effect of suspensive and resolutive conditions. [Online]. Available :<http://www.nortonrosefulbright.com/knowledge/publications/132562/to-be-or-not-to-be-the-effect-of-suspensive-and-resolutive-conditions>, 14 August 2016

<sup>43</sup> South African Revenue Service, Comprehensive Guide to Capital Gains Tax (Issue 4), page 110

<sup>44</sup> *Ibid* page 111.

delay the accrual of proceeds or the incurral of expenditure (for the buyer) for income tax purposes and deems delivery to occur on the conclusion of the contract.<sup>45</sup>

### **4.3 Income Tax Act– Acquiring the immovable property for resale**

The definition of ‘gross income’ according to the ITA specifically excludes receipts and accruals of a capital nature. The ITA does not define what is meant by capital however in *CIR v Visser* (1937 T) (at 276) Maritz J stated:

“Income is what capital produces, or something in the nature of interest or fruit as opposed to principal or tree. This economic distinction is a useful guide in matters of income tax, but its application is very often a matter of great difficulty, for what is principal or tree in the hands of one man may be interest or fruit in the hands of another. Law books in the hands of a lawyer are a capital asset; in the hands of a bookseller they are a trade asset. A farm owned by a farmer is a capital asset; in the hands of a land-jobber it becomes stock-in-trade.”<sup>46</sup>

If the proceeds from the sale of immovable property are acquired for the purpose of resale at a profit then the profits are made due to a normal operation of business, in the carrying out of a scheme of profit making and will be included in gross income.<sup>47</sup>

As was held by the majority judgment in *CIR v Pick n Pay Employee Share Purchase Trust* [1992] (4) SA 39 (A):

A distinction is drawn between carrying on of a business and the pursuance of a profit making scheme. The basis for such distinction is that it is more appropriate to refer to a profit making scheme where a single transaction is involved. I accept that a series of transactions is characteristic of the carrying on of a business. But irrespective of the number of transactions, whether the receipts that flow from the carrying on of a business are revenue still depends on whether the business was conducted with a profit-making purpose, i.e. as part of a profit making venture or scheme.”<sup>48</sup>

### **Timing rules**

As defined in chapter 2 the definition of gross income according to section 1 of the ITA means:

“(i) in the case of any resident, the total amount, in cash or otherwise, received by or accrued to or in favour of such resident; or

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<sup>45</sup> South African Revenue Service, Comprehensive Guide to Capital Gains Tax (Issue 4), page 111

<sup>46</sup> *CIR v Visser* 1937 TPD77 8 SATC 271

<sup>47</sup> Stiglingh M, assisted by Heyns A, Silke : South African Income Tax 2016, chapter 3, page 43.

<sup>48</sup> *CIR v Pick n Pay Employee Share Purchase Trust* [1992] (4) SA 39 (A) 46 SATC 34

(ii) in the case of any person other than a resident, the total amount, in cash or otherwise, received by or accrued to or in favour of such person from a source within the Republic .....

During such year or period of assessment, excluding receipts or accruals of a capital nature .....

From the definition it is clear that it applies both to receipts and accruals however the definition also establishes that an amount which has been taxed as an accrual cannot be taxed as a receipt again.<sup>49</sup>

When dealing with the disposal of immovable property it is the timing of 'received by or accrued to' which will determine when the amount must be included in gross income.

### **Accrued to**

From *Lategan v CIR* [1926] CPD 2 SATC 16 came the principle that the meaning of the word 'accrued' to means that once the taxpayer has become entitled to an amount, irrespective of the fact that the amount is due and payable in a later year of assessment, it will form part of gross income in that year of assessment.<sup>50</sup>

Judges De Villiers AJ and Stratford in *CIR v Delfos* [1933] AD 242; 6 SATC 92 contended that the concept 'accrued to' gives the Commissioner the right to tax all amounts received by the taxpayer or accrued to him in the year of assessment.<sup>51</sup>

In *CIR v Peoples Store (Walvis Bay) (Pty) Ltd* [1990] (2) SA 353 (A); 52 SATC 9 certain valuable principles emerged and it was held:

- "That income, although expressed as an 'amount' in the definition of 'gross income', need not be an actual amount of money but may be 'every form of property earned by the taxpayer, whether corporeal or incorporeal, which has a money value . . . including debts and rights of action'.
- That income in a form other than money must, in order to qualify for inclusion in 'gross income', be of such a nature that a value can be attached to it in money.
- That the fact that the valuation of the income may sometimes be a matter of considerable complexity does not detract from the principle that all income having a money value must be included.
- That no more is required for an accrual in terms of the definition of 'gross income' than that the person concerned has become entitled to the 'amount' in question.

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<sup>49</sup> De Koker AP, Williams RC, Silke on South African Income Tax, Last updated March 2016, Chapter 2.1

<sup>50</sup> De Koker AP, Williams RC, Silke on South African Income Tax, Last updated March 2016, Chapter 2.7

<sup>51</sup> De Koker AP, Williams RC, Silke on South African Income Tax, Last updated March 2016, Chapter 2.3

- 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, but that its value is affected if it is not immediately enforceable.
- That the decision in *Lategan v Commissioner for Inland Revenue* 1926 CPD 203, 2 SATC 16 reflects the law correctly.
- That the value of the instalments not yet payable nor paid at the tax year-end must be included in the taxpayer's gross income for that tax year.<sup>52</sup>

In *Silke: South African Income Tax*, the author uses the following example to demonstrate the meaning of accrual:

"Assume in each case that the 2014 year of assessment ends on the last day of February 2014.

A developer sells a completed sectional title unit for R1 000 000 on 17 February 2014, subject to the condition that the purchaser obtains a bond on or before 15 March 2014. The bond is granted on the 10 March 2014. The purchase price accrues to the developer on 10 March 2014, upon fulfilment of the suspensive condition. The R1 000 000 will therefore not be included in the developers gross income for the 2014 year of assessment."<sup>53</sup>

### Entitled to

The date of accrual in terms of the principle established in *Lategan v CIR* is the date it becomes due; the date when the right to claim payment arises in terms of the contract, the date when the seller becomes entitled to the amount.<sup>54</sup>

The following example is illustrated in *Silke* where the principle in the determination of the date of accrual is the date when the taxpayer is entitled to the income:

A merchant sells goods for R100 on 17 February. In terms of the contract of sale he undertakes to deliver on 15 March. The R100 clearly accrues on 15 March when delivery takes place because, until that event takes place, the taxpayer is not entitled to the income. It has been held that the words of Watermeyer J in the *Lategan* case, 'he has not become entitled to a right to claim payment of the debt in the year of assessment but he acquired a right to claim payment of the debt in the future', seem to refer to a definite right *in praesenti* to claim payment *in futuro*, but in circumstances in which there is as yet no delivery, the right to claim payment does not arise until the delivery is made. A provision in an agreement that a right to claim payment arises on or after the day when delivery is made means that there can be no accrual of the purchase price for tax purposes until delivery has been made in terms of the agreement.<sup>55</sup>

<sup>52</sup> *Commissioner for Inland Revenue v People's Stores (Walvis Bay) (Pty) Ltd* [1990] 52 SATC 9, page 11

<sup>53</sup> Stiglingh M assisted by Heyns A, *Silke:South Africa Income Tax 2016*, chapter 2, page 23

<sup>54</sup> de Koker AP; Williams RC, *Silke on South African Income Last Updated: March 2016*, Examples illustrating the 'Lategan' principle Chapter 2.8

<sup>55</sup> de Koker AP; Williams RC, *Silke on South African Income Last Updated: March 2016*, Examples illustrating the 'Lategan' principle Chapter 2.8

However if the time of disposal rules are studied it becomes clear that the payment and the delivery of the property are the fulfilment of the obligations created by the agreement of sale. The time of disposal will be when the agreement is concluded even though the change of ownership of the property still needs to take place.<sup>56</sup>

Although the property is treated as a revenue asset and hence stock in trade for gross income purposes its nature as 'property' (refer to earlier definitions) is not changed and it is still an asset (refer earlier definitions) for capital gains tax purposes. Paragraph 13 of the Eighth Schedule sets out various rules for determining the time of disposal. Paragraph 13(1) provides as follows:

'The time of disposal of an asset by means of—

- (a) a change of ownership effected or to be effected from one person to another because of an event, act, forbearance or by operation of law is, . . .'

The time of disposal of an asset by means of a change of ownership from one person to another because of an event, act or forbearance or by operation of law will depend on whether the agreement for the disposal of the relevant asset is subject to a suspensive condition. The specific rules embodied in para 13(1)(a)(i) and (ii) provide that the time of disposal in the case of

'(i) an agreement subject to a suspensive condition, [is] the date on which the condition is satisfied;

(ii) any agreement which is not subject to a suspensive condition, [is] the date on which the agreement is concluded;'<sup>57</sup>

As stated above for the purposes of gross income as well as capital gains tax purposes an agreement can either be unconditional or be subject to a suspensive condition. If the agreement has a suspensive condition the time of disposal will be the date on which the agreement is concluded. Where an agreement is concluded unconditionally, but provides for delayed delivery of the property (a deferred delivery of the property), this results in the creation of two rights. The seller's right to payment and the purchaser's right to delivery. The created rights however cannot be regarded as separate events from the agreement of sale. The payment and the delivery of the property are the fulfilment of the obligations created by the agreement of sale. The time of disposal will be when the agreement is concluded even though the change of ownership of the property still needs to take place.<sup>58</sup>

## **Section 24(1)**

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<sup>56</sup> de Koker AC; Williams RC, Silke on South African Income Last Updated: March 2016, Examples illustrating the 'Lategan' principle Chapter 2.8

<sup>57</sup> de Koker AC; Williams RC, Silke on South African Income Last Updated: March 2016, Chapter 24.35

<sup>58</sup> de Koker AC; Williams RC, Silke on South African Income Last Updated: March 2016, Chapter 24.35

Section 24(1) of the ITA reads as follows -

“Credit agreements and debtors allowance. – (1) Subject to the provisions of section 24J, if any taxpayer has entered into any agreement with any other person in respect of any property the effect of which is that, in the case of movable property, the ownership shall pass or, in the case of immovable property, transfer shall be passed from the taxpayer to that other person, upon or after receipt by the taxpayer of the whole or a certain portion of the amount payable to the taxpayer, under the agreement, the whole of that amount shall for the purpose of this Act be deemed to have accrued to the taxpayer on the day on which the agreement was entered into.”

This section was relevant in *SIR v Silverglen Investments (Pty) Ltd*. Section 24(1) makes it very clear that the transfer of immovable property shall be deemed to accrue to the taxpayer on the date that the agreement was entered into.

### **Defining the timing of an agreement according to *SIR v Silverglen Investments (Pty) Ltd***

Section 24(1) of the ITA deals with credit agreements and debtor allowances, however, this provision makes it clear that the ownership of immovable property is transferred from the seller to the buyer on the date on which the agreement was entered into, which, will be the date that the amount payable under the agreement will be deemed to accrue for the purposes of the ITA for the seller.<sup>59</sup>

In *Silverglen Investments (Pty) Ltd* it was held that payments from the sale of immovable property will be deemed to accrue to the recipient at the date of the agreement. It is also clear from this case that there is no choice in which year a sale of immovable property can be assessed.<sup>60</sup>

The definition of ‘gross income’ refers to the total amount in cash or otherwise, received by or accrued to or in favour of the taxpayer during a year or period of assessment. This is interpreted as the total amount of both receipts and accruals.<sup>61</sup>

The *Silverglen case* is therefore of relevance and is discussed below as the case highlights when ownership of immovable property is deemed to take place.

### **Facts of the case**

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<sup>59</sup> Income Tax Act No 58 of 1962, section 24

<sup>60</sup> *SIR v Silverglen Investments (Pty) Ltd* [1969] 30 SATC 199, page 201.

<sup>61</sup> *Ibid* page 201.

The taxpayer was the owner of immovable property. This property was 'affected' property in terms of the Group Areas Development Act, 69 of 1955 in respect of which the Group Areas Development Board had certain pre-emptive rights if the property was put up for disposal.<sup>62</sup>

After notice had been given in terms of the Act to the Group Areas Development Board, the property was put up for sale and sold for an amount of R200 000.<sup>63</sup>

The property was auctioned off and sold on the 10 November 1962 to one E and the board was given notice of the sale.<sup>64</sup>

On the 10 December 1962 the Board notified the taxpayer that they intended to exercise their pre-emptive rights and take over the property at the price that it had been sold to one E.<sup>65</sup>

At that stage the Board also indicated that certain adjustments and payments would be made between the Board and the taxpayer in accordance with the conditions under which the sale had been 'affected'.<sup>66</sup>

Negotiations were finally concluded between the Board and the taxpayer on or about the 30 May 1963. Transfer was effected on the 7 August 1963 and the payment was made the next day to the taxpayer.<sup>67</sup>

The taxpayer claimed that in terms of section 24 of the ITA the amounts received by it on the 8 August 1963 must be deemed to accrue during the year ended 30 June 1963.<sup>68</sup>

The South African Revenue Service (SARS) said that the transaction between the Board and the taxpayer in terms of the Group Areas Development Act did not constitute an agreement in terms of section 24 of the ITA and that as the ITA levied tax on amounts received by or accrued to a taxpayer in any year of assessment and that SARS had the right to assess the amount in either the year of accrual or receipt if they occurred in different years.<sup>69</sup>

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<sup>62</sup> Ibid page 201.

<sup>63</sup> Ibid page 201.

<sup>64</sup> Ibid page 201.

<sup>65</sup> Ibid page 201.

<sup>66</sup> Ibid page 201.

<sup>67</sup> Ibid page 201.

<sup>68</sup> Ibid page 201.

<sup>69</sup> Ibid page 201.

The taxpayer was assessed in the following year of assessment. The taxpayer appealed against the assessment to the Special Court. The Special Court allowed the appeal holding that section 24 of the ITA did apply.<sup>70</sup>

SARS appealed against this decision saying that it had the right to elect in which year they were entitled to assess the amount.<sup>71</sup>

## Issues

The following questions were required to be answered in order for the court to reach a decision, the time which the disposal of the immovable property took place in relation to the tax year in which the disposal would be deemed to have accrued or received and whether SARS has the right to tax the disposal in whatever tax year it deems fit, either in the year of accrual or receipt?<sup>72</sup>

“In terms of section 24 of the ITA any amount received by a taxpayer in respect of a sale of immovable property in terms of an agreement which provides that transfer of such property shall be passed upon or after the receipt by the seller of the whole or part of the purchase price shall be deemed to have accrued to the seller on the date on which the agreement was entered into.”<sup>73</sup>

## Court findings

The court held that SARS does not have the right to elect the year in which to include an amount for assessment. SARS has a duty to assess all amounts received or accrued to a taxpayer in that year.<sup>74</sup>

The agreement clearly fell within the terms of section 24 of the ITA with the result that the amounts accrued to the taxpayer at the date of the agreement which was prior to 30 May 1963 and therefore fell in the tax year ending 30 June 1963.<sup>75</sup>

## Commentary

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<sup>70</sup> Ibid page 201.

<sup>71</sup> Ibid page 201.

<sup>72</sup> Ibid page 201.

<sup>73</sup> Ibid page 201.

<sup>74</sup> Ibid page 202.

<sup>75</sup> Ibid page 202.

Judge Steyn CJ commented that the accrual in the ordinary sense to the taxpayer could not have taken place before transfer of the property had taken place on the 7<sup>th</sup> of August 1963. However due to the provisions in section 24 of the ITA the accrual was deemed to have accrued to the taxpayer on the day on which the agreement was entered into. This date was therefore on the 10<sup>th</sup> of December 1962, the date the Board informed the taxpayer that they were to exercise their pre-emptive rights.<sup>76</sup>

As to the right to select in which tax year to include the amount, there is nothing in the ITA to support this. “The definition of gross income is clear and refers to the total amount in cash or otherwise, received by or accrued to or in favour of the taxpayer during a year or period of assessment. In *Commissioner for Inland Revenue v Delfos*, [1933] A.D. 24259 at 254, Wessels C.J. remarked:

“It was for the legislature to say how it wished to determine the taxable income of the citizen, and we cannot say that where in a definition it said “received by”, it did not mean to include everything that the taxpayer received in the year of assessment (not being something of a capital nature): nor can we say that when the legislature said disjunctively “received by or accrued to” it meant “received by and accrued to”.<sup>77</sup>

It can therefore be said that in the above context, received by or accrued to does not mean that income must both have been accrued and received in the same year of assessment to be included in that year but that whatever has accrued to the taxpayer during the year of assessment is part of gross income.<sup>78</sup>

De Villiers JA has pointed out that accrued to and received by in the definition of gross income is defined on two bases and that these bases are independent of each other. He said the following:

“that is to say that the Commissioner can claim to regard as gross income all amounts actually received during a tax year, whenever they may have originally accrued, and also all amounts accruing during a tax year”<sup>79</sup>

### **Conclusion of *SIR v Silverglen (Pty) Ltd***

Amounts which are payable under agreements are to be taxed in the year in which they are deemed to have accrued and not in any subsequent year of receipt or actual accrual when

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<sup>76</sup> Silverglen Investments page 208.

<sup>77</sup> Ibid page 208.

<sup>78</sup> Ibid page 208.

<sup>79</sup> Ibid page 208.

payments are made. The total amount receivable from the sale of immovable property will be deemed to accrue to the recipient at the date of the agreement.

### **Overall conclusion of the time rules when acquiring immovable property for resale**

From the principles above as well as taking section 24(1) into account, it is evident that for income tax purposes the legislature intended that when it comes to the sale of immovable property in a scheme of profit making as in the case of property developers, the sale of the immovable property will be included in gross income in the year in which the contract is concluded. The act specifically states that income will be included the earlier of receipt or accrual. Therefore irrespective of in which tax year the transfer of the property took place between the buyer and the seller the sale will be included for income tax purposes in the tax year in which the contract was concluded. The rules applicable for an inclusion in gross income will also be of relevance in the case of immovable property being disposed of for capital gains tax purposes as the Eighth Schedule is part of the ITA. The actual transfer of ownership of immovable property is seen to only take place with delivery and registration in the deeds office as previously discussed in chapter 3.3 above. The tax liability for income tax therefore precedes actual ownership in terms of the Deeds Registries Act.

### **4.4 Value Added Tax Act (VAT Act)**

The sale of immovable property is subject to value added tax (VAT) regardless of whether it was bought as an investment or bought for resale. The actual liability for VAT however would depend on whether the property is sold by a vendor and whether used for commercial or residential use.

Section 7 of the VAT Act states the following:

(1)“Subject to the exemptions, exceptions, deductions and adjustments provided for in this Act, there shall be levied and paid for the benefit of the National Revenue Fund a tax, to be known as the value-added tax –

(a)On the supply by any vendor of goods or services supplied by him on or after the commencement date in the course or furtherance of any enterprise carried on by him; .....”<sup>80</sup>

Fixed property is defined in the VAT Act to mean –

“Land (together with improvements affixed thereto), any unit as defined in section 1 of the Sectional Titles Act 1986 (Act No. 95 of 1986), any share in a share block company which confers a right to or interest in the use of immovable property, and, in relation to a property time-sharing scheme, any time-

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<sup>80</sup> Value-Added Tax Act No. 89 of 1991

sharing interest as defined in section 1 of the Property Time-sharing Control Act, 1983 (Act No. 75 of 1983); and any real right in such land, unit, share or time-sharing interest.”<sup>81</sup>

A sale is defined in section 1 as –

“An agreement of purchase and sale and includes any transaction or act whereby or in consequence of which ownership of goods passes or is to pass from one person to another;”

Where VAT is payable no transfer duty will be payable, this is in terms of section 9(15) of the Transfer Duty Act 40 of 1949, which is discussed below.<sup>82</sup>

A vendor will be liable for VAT on the sale of property if the vendor conducts business operations from fixed property. He can only be a registered VAT vendor if he is carrying on an enterprise. Where a vendor acquires a property for resale or for development he may claim an input tax deduction in respect of the VAT on his costs if he is a registered VAT vendor. When he then disposes of the property he will need to raise output VAT on the disposal.<sup>83</sup>

The purchase price of the immovable property for the buyer will be increased by the rate of VAT which is applicable at the time. The VAT and the purchase price of the immovable property are collected simultaneously and the VAT is paid over to SARS with the first VAT return submitted by the vendor after the property has been registered in the Deeds Registry.<sup>84</sup>

### **Timing rules**

According to the VAT Act the period in which the time of supply takes place will be determined when the VAT on the supply has to be accounted for.<sup>85</sup>

The supply of fixed property is dealt with in section 9(3)(d) of the VAT Act and states the following:-

“Time of supply. – (1) For the purpose of this Act a supply of goods or services shall, except as otherwise provided for in this Act, be deemed to take place at the time an invoice is issued by the supplier or the recipient in respect of that supply or the time any payment of consideration is received by the supplier in respect of that supply, whichever time is earlier.

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<sup>81</sup> Ibid Section 1

<sup>82</sup> De Koker AP, Williams RC, Silke on South African Income Tax, Last updated March 2016, Chapter 10.15

<sup>83</sup> De Koker AP, Williams RC, Silke on South African Income Tax, Last updated March 2016, Chapter 11.5

<sup>84</sup> Green R, COX YEATS, Publication January 2008, VAT, Transfer Duty and Fixed Property. [Online]. Available :coxyeats.co.za/Roger Green, VAT, Transfer duty and Fixed Property, 21 April 2016

<sup>85</sup> De Koker AP, Williams RC, Silke on South African Income Tax, Last updated March 2016, Chapter 10.15

(2) Notwithstanding anything in subsection (1) or (2) of this section –

(a).....

(b) .....

(c) .....

(d) where goods consisting of fixed property or any real right therein are supplied under a sale, that supply shall be deemed to take place –

(i) ...

(ii) where registration or transfer of the goods is effected in a deeds registry, on the date of such registration; or

(iii) on the date on which any payment is made in respect of the consideration for such supply whichever date is earlier;

..... „<sup>86</sup>

A special timing rule applies in relation to immovable property which is supplied under a sale. The supply for VAT purposes is deemed to take place at the earlier of the date of registration of transfer and the date any payment is received.<sup>87</sup>

However the payment of “a deposit whether or not refundable will not constitute any payment until it is released, forfeited or applied as partial payment of the purchase price.”<sup>88</sup>

A supplier of immovable property who accounts for VAT on the invoice basis will in essence only account for the output tax once he receives the payment for the property disposed of.<sup>89</sup>

Therefore when dealing with immovable property the VAT will only become due once registration of transfer of the property has taken place which in essence means when the property has been registered in the deeds registry.

VAT, therefore, is not accounted for at the same time as the income tax liability is accounted for, for income tax.

The VAT Act was amended in 1993 to accommodate property developers, as according to the Explanatory Memorandum on the Taxation Laws Amendment Bill, 1993, the practical problem

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<sup>86</sup> Value-Added Tax Act No. 89 of 1991

<sup>87</sup> De Koker AP, Williams RC, Silke on South African Income Tax, Last updated March 2016, Chapter 10.15

<sup>88</sup> De Koker AP, Williams RC, Silke on South African Income Tax, Last updated March 2016, Chapter 10.15

<sup>89</sup> De Koker AP, Williams RC, Silke on South African Income Tax, Last updated March 2016, Chapter 10.15

that was being experienced by property developers was that development projects normally last longer than 6 months from the date on which the sale agreement is signed. The 6 month period therefore elapses before the property has been transferred in the deeds registries office resulting in the payment of the property not being received by the property developer.<sup>90</sup>

The VAT timing rule also ensures that the seller receives money with which to pay the VAT output liability.

#### **4.5 Transfer Duty Act No. 40 of 1949**

According to section 2 of the Transfer Duty Act (TDA), transfer duty is not payable on the transfer of property but is payable on the value of any property acquired by a person by means of a transaction (see chapter 2.2.4). Transfer duty is triggered on the acquisition of a right, that allows the person to acquire the property, to claim transfer. It must be taken into account that the actual transfer of the property is not necessary.<sup>91</sup>

Transfer duty will however not be payable in certain circumstances. According to section 15 of the TDA:

“(15) No duty shall be payable in respect of the acquisition of any property under any transaction which for purposes of the Value Added Tax Act, 1991, is a taxable supply of goods to the person acquiring such property if –

(a) the transferor of the property under such transaction, in a declaration in such form as the Commissioner may prescribe, certifies that value-added tax payable under the said Act has been paid to him in respect of the said supply by the transferee and has been accounted for by him in a relevant return required to be furnished by him under the said Act or will be so accounted for in such return within the time allowed under that Act for the rendering of such return, or where such supply was subject to the said tax at the rate of zero per cent, such information regarding such supply as the Commissioner may require has been furnished to him;

(b) .....

(c) .....”

Therefore it must be determined if a liability for transfer duty exists and if so when the duty must be paid.

#### **Timing rules**

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<sup>90</sup> Republic of South Africa, Explanatory Memorandum on the Taxation Laws Amendment Bill, 1993, Clause 25, page 11

<sup>91</sup> Hofmeyr CD, Transfer Duty, 2237. Acquisition of Property, September 2013 – Issue 168. [Online]. Available :[https://www.saica.co.za/integritax/2013/2237.\\_Aquisition\\_of\\_property.htm](https://www.saica.co.za/integritax/2013/2237._Aquisition_of_property.htm), 4 May 2016

According to section 1(1) of the TDA when property is acquired (refer to definition of date of acquisition in chapter 2) by way of a transaction the date on which the agreement was entered into is the date of acquisition of the property and from that date the person that is acquiring that property has 6 months in which to pay the transfer duty. If the transfer duty is not paid within the period allowed, interest will be payable in addition to the unpaid transfer duty.<sup>92</sup>

In *CIR v Freddie's Consolidated Mines Ltd* [1957 (1) SA 306 (A)] it was held that the word acquired meant the acquisition of a right to acquire ownership in property. It must be noted that it is not the transfer of property which gives rise to the transfer duty but it is the personal right which is acquired by the purchaser from the seller which gives rise to the obligation to pay the transfer duty.<sup>93</sup>

In *SIR v Hartzenberg* [1966 (1) SA 405 (A)], Botha JA confirms this view by stating (at 409A-B):

“Although the ordinary legal meaning of the word ‘acquire’ implies the acquisition of dominium, it is clear that in sec. 2 of the Act the word is used in its wider meaning and includes the acquisition of a jus in personam ad rem acquirendam... Transfer duty therefore becomes payable under sec. 2 upon the acquisition by a person of a personal right to obtain dominium in immovable property.”<sup>94</sup>

The “acquisition of property” refers to the acquisition of a personal right that entitles the person who is acquiring the property to claim transfer of that property. As there is a close association between the Deeds Office and the collection of transfer duty this may lead to the impression that the transfer duty liability arises at the same time as when the property is transferred in the Deeds Registry. According to the SARS guide on Transfer Duty, the date that the liability arises to pay transfer duty, is the date of acquisition regardless of whether the actual transfer of the property has been recorded in the Deeds Registry.<sup>95</sup>

The TDA makes no mention of ownership of immovable property or when ownership passes. The only reference is to acquisition of property and that date is seen to be the date that the transaction was entered into.<sup>96</sup>

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<sup>92</sup> South African Revenue Services (SARS) Website [Online]. Available : <http://www.sars.gov.za/AllDocs/OpsDocs/Guides/LAPD-TD-G01%20-%20Transfer%20Duty%20Guide%20-%20External%20Guide.pdf>, Page 41, 2 June 2016

<sup>93</sup> South African Revenue Services (SARS) Website [Online]. Available : <http://www.sars.gov.za/AllDocs/OpsDocs/Guides/LAPD-TD-G01%20-%20Transfer%20Duty%20Guide%20-%20External%20Guide.pdf>, Page 41, 2 June 2016

<sup>94</sup> *SIR v Hartzenberg* 1966 (1) SA 405 (A)

<sup>95</sup> South African Revenue Services (SARS) Website [Online]. Available : <http://www.sars.gov.za/AllDocs/OpsDocs/Guides/LAPD-TD-G01%20-%20Transfer%20Duty%20Guide%20-%20External%20Guide.pdf>, Page 33, 2 June 2016

<sup>96</sup> Haupt P, Notes of South African Income Tax 2016, Thirty Fifth Edition, Chapter 31 page 961.

Therefore to summarise, the liability for transfer duty arises on the date of the acquisition of the property and is the “date of acquisition” as defined in section 1(1).<sup>97</sup>

#### **4.6 Deeds Registries Act 47 of 1937**

South Africa has a very efficient registration of land title which is based on a land survey system. Each portion of land is determined by a diagram prepared by a surveyor and registered in the Surveyor General’s Office which gives rise to a certain and definite basis of registration of land.<sup>98</sup>

Various property registers exist in the various deeds registries in the different provinces of South Africa. The registers are properly indexed and are accessible electronically. All of the deeds registries are established under the relevant government department and all fall under a Chief Registrar of Deeds. The property registers are extremely accurate and all ownership of land is recorded in a deeds register.<sup>99</sup>

The law applicable to the transfer and registration of land is defined in the Deeds Registries Act 47 of 1937, together with its regulations. In South Africa there is no restriction on ownership of land and any natural person or juristic person may own land.<sup>100</sup>

#### **Timing rules**

According to the Deeds Registries Act (DRA) ownership of immovable property only takes place once the transfer of ownership has been registered in the Deeds office. The fundamental principles of the DRA are as follows:

##### **“Section 13. When registration takes place**

(1) Deeds executed or attested by a registrar shall be deemed to be registered upon the affixing of the registrar’s signature thereto, and deeds, documents or powers of attorney lodged for registration shall be deemed to be registered when the deeds registry endorsement in respect of the registration thereof is signed: Provided that no such deed, document or power which is one of a batch of interdependent deeds,

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<sup>97</sup> South African Revenue Services (SARS) Website [Online]. Available :<http://www.sars.gov.za/AllDocs/OpsDocs/Guides/LAPD-TD-G01%20-%20Transfer%20Duty%20Guide%20-%20External%20Guide.pdf>, Page 41, 2 June 2016

<sup>98</sup> Webbers Attorneys Notaries Conveyancers, Real Estate. [Online]. Available : <http://www.webberslaw.com/property-and-real-estate-2/> 1 May 2016. Page 3.

<sup>99</sup> Webbers Attorneys Notaries Conveyancers, Real Estate. [Online]. Available : <http://www.webberslaw.com/property-and-real-estate-2/> 1 May 2016. Page 2.

<sup>100</sup> Bembridge, A. 8 may 2013. ENSight. The Real Estate Law Review, Second Edition – South Africa. [Online]. Available :<https://www.ensafrica.com/news/The-Real-Estate-Law-Review-Second-Edition-South-Africa>, 4 May 2016

documents or powers of attorney intended for registration together, shall be deemed to be registered until all the deeds, documents or powers of attorney or the registration endorsements in respect thereof, as the case may be, have been signed by the registrar.

(2) If by inadvertence the registrar's signature has not been affixed to a deed executed or attested by him, or to the registration endorsement in respect of the registration of a deed, document or power of attorney lodged for registration, at the time at which the signature should have been affixed in the ordinary course, the registrar may affix his signature thereto when the omission is discovered, and the deed, document or power of attorney shall thereupon be deemed to have been registered at the time aforesaid.

(Section 13(3): Decided cases)

(3) All endorsements or entries made on deeds, documents or powers of attorney or in registers, in connection with the registration of any deed, document or power of attorney, shall be deemed to have been effected simultaneously with the affixing of the signature of the registrar thereto in respect of deeds executed or attested by a registrar or with the signing of his registration endorsement in respect of deeds, documents or powers of attorney lodged for registration, although in fact they may have been made subsequent thereto.

(4) Any deed, document or endorsement which under this section is required to be signed by a registrar, may, if the registrar is not available to sign such deed, document or endorsement, be signed by the successor in office of the registrar or by any person acting in the place of the registrar, whereupon any reference in subsection (1) or (3) to the signature of the registrar shall be deemed to include a reference to the signature of such successor or person acting as registrar, as the case may be."<sup>101</sup>

Therefore the Deeds Registries Act (DRA) is specific in that ownership of immovable property will only occur at the time that the transfer of ownership has been registered in the Deeds office. This is in contrast to the Income Tax Act which deems the tax liability to occur on conclusion of the contract which could mean that the seller has not yet divested himself of the property as it has not gone through the Deeds office.

#### **4.7 Common law principles in South Africa**

South African common law is drawn primarily from Roman-Dutch and English law. These common laws have been combined and adapted by the courts in a South Africans context. The South African law of property has been developed from these laws.<sup>102</sup>

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<sup>101</sup> Deeds Registries Act 47 of 1937

<sup>102</sup> Govender P, Does a mineral right constitute 'immovable property' for purposes of the Income Tax Act and double tax treaties? February 2014 Chapter 6.2.1 , Page 25-26

The most important classification of property is the division between movables and immovables.<sup>103</sup> This dissertation as mentioned above only focuses on the disposal of immovable property.

Immovable property is seen as land and those things which are attached to that land either naturally or by artificial means in such a manner that it cannot be detached from the land without being damaged and without losing its identity.<sup>104</sup> Refer to chapter 2.2.6.

The title to immovable property in South Africa will always vest in the owner of the property and a comprehensive legal framework for the ownership and transfer of immovable property is governed by statute.<sup>105</sup>

### **Timing rules**

According to common law the description of ownership is derived from South African case law, ownership is defined as the most complete real right that a legal subject can have regarding a thing, or as “the real right which gives the owner the most complete and absolute entitlement to a thing.”<sup>106</sup> The acquisition of ownership when it comes to immovable property is the transfer of ownership which is done by means of registration in the deeds office in accordance with the DRA.<sup>107</sup>

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<sup>103</sup> Ibid page 25-26.

<sup>104</sup> Ibid page 25-26.

<sup>105</sup> Bembridge, A. 8 may 2013. ENSight. The Real Estate Law Review, Second Edition – South Africa. [Online]. Available :<https://www.ensafrica.com/news/The-Real-Estate-Law-Review-Second-Edition-South-Africa>, 4 May 2016

<sup>106</sup> Boshoff Dr D, Understanding the Basic Principles of Property Law in South Africa, Professional Skills Module No. 8, page 11

<sup>107</sup> Boshoff Dr D, Understanding the Basic Principles of Property Law in South Africa, Professional Skills Module No. 8, page 20

#### 4.8 Summary in table form of the timing of ownership in immovable property

	Income Tax Act 58 of 1962	8 <sup>th</sup> Schedule of the Income Tax Act 58 of 1962	Value Added Tax Act 89 of 1991	Transfer Duty Act 40 of 1949	Deeds Registries Act No47 of 1937	Common Law Principles
The date on which the sales agreement is entered into will determine when the ownership in immovable property takes place.				✓		
The date on which all suspensive conditions of the sale agreement are met determines when the ownership in the immovable property takes place.	✓	✓				
The earlier of registration or payment of the purchase price will determine when the ownership in immovable property takes place.			✓			
The date on which the immovable property is registered in the Deeds Registries Office will determine that ownership has been transferred from the seller to the purchaser.					✓	✓

**4.9 Examples of when ownership in immovable property accrues according to the various acts and common law principles**

**Example no 1:**

A property developer sells a completed sectional title unit for R1 000 000 inclusive of VAT on 17 February 2014. The sale is conditional and subject to the purchaser obtaining a bond on or before 27 February 2014. The bond is granted to the purchaser on the 26 February 2014. On the 1 March 2014 the purchaser pays a 10% deposit to the transfer attorneys to secure the transaction. The deposit paid is placed in the attorneys trust account until such time that the transfer has taken place in the Deeds Registries Office. No transfer duty is payable by the purchaser as the transaction is subject to VAT. Transfer of ownership takes place in the Deeds Registries Office on the 30 June 2014. The purchaser is advised on the 30 June 2014 that the transfer of the property has taken place and that he is the new owner.

	<b>17 February 2014</b> a sales agreement is entered	On the <b>26 February 2014</b> all suspensive conditions of the sale agreement are met.	A <b>10% Deposit</b> is paid to the transfer attorney by the purchaser	On the <b>30 June 2014</b> the property is registered in the Deeds Registries office
<b>Income Tax Act 58 of 1962</b>		Ownership is deemed to take place once the agreement has been concluded and all suspensive conditions met. The disposal is now included in the taxpayers gross income for income tax purposes. (Refer chapter 4.3 above)		
<b>8<sup>th</sup> Schedule of the Income Tax Act 58 of 1962</b>	As the immovable property is held as trading stock and the income from the disposal will be included in the taxpayers gross income the capital gain will be zero. (Refer chapter 4.2)			
<b>Value Added Tax Act 89 of 1991</b>			As referred to in 4.4 above, a deposit whether or not refundable will not constitute any payment.	As referred to above in 4.4 the VAT and the purchase price of the immovable property are collected simultaneously and the VAT is paid over to SARS by the taxpayer

				with the first VAT return submitted by the vendor after the property has been registered in the Deeds Registry.
<b>Transfer Duty Act 40 of 1949</b>	Inclusive in the price of R1 000 000 for which the immovable property is disposed is 14% VAT. As the disposal is subject to VAT there is no transfer duty payable by the purchaser. (Refer to chapter 4.4)			
<b>Deeds Registries Act 47 of 1937</b>				As per Section 13 in the DRA ownership in property accrues once delivery has taken place. Delivery takes place once the property has been transferred into the name of the purchaser. (Refer to chapter 4.6)
<b>Common Law Principles</b>				Ownership in property accrues once delivery has taken place. Delivery takes place once the property has been transferred into the name of the purchaser. (Refer to chapter 4.7)

### **The tax year in which ownership is deemed to accrue**

For income tax purposes the sale of the property will need to be accrued for in the 2014 tax year. Even though transfer has only taken place in the Deeds Registries Office in the 2015 tax year this bears no relevance on when ownership for income tax purposes has been deemed to have accrued. The payment of the VAT is delayed until the earlier of payment or invoice, hence payable in the VAT period after 30 June 2014.

**Example no 2:**

A taxpayer who holds a residential property for investment purposes decides to sell the property for R1 000 000 on the 17 February 2014. The sale is conditional and subject to the purchaser obtaining a bond on or before 27 February 2014. The bond is granted to the purchaser on the 26 February 2014. On the 1 March 2014 the purchaser pays a 10% deposit to the transfer attorneys to secure the transaction. The deposit paid is placed in the attorneys trust account until such time that the transfer has taken place in the Deeds Registries Office. Transfer duty is payable by the purchaser before the deed of sale is lodged with the Deeds Registries Office. Transfer of ownership takes place in the Deeds Registries Office on the 30 June 2014. The purchaser is advised on the 30 June that the transfer of the property has taken place and that he is the new owner.

	<b>17 February 2014</b> a sales agreement is entered	On the <b>26 February 2014</b> all suspensive conditions of the sale agreement are met.	A <b>10% Deposit</b> is paid to the transfer attorney by the purchaser	On the <b>30 June 2014</b> the property is registered in the Deeds Registries office
<b>Income Tax Act 58 of 1962</b>	As the immovable property has been held for investment purposes, the property is not included in gross income but is subject to CGT. (Refer to chapter 4.2)			
<b>8<sup>th</sup> Schedule of the Income Tax Act 58 of 1962</b>		Ownership is deemed to take place once the agreement has been concluded. The disposal is raised as an accrual for capital gains tax purposes by the taxpayer. (Refer to chapter 4.2)		
<b>Value Added Tax Act 89 of 1991</b>	Residential property disposed of is exempt from vat unless being disposed of by a property developer who is a registered VAT vendor. (Refer chapter 4.4)			
<b>Transfer Duty Act 40 of 1949</b>	According to section 1(1) of the TDA when property is acquired by way of a transaction the date on which the agreement was entered into is the			

	date of acquisition of the property.(Refer chapter 4.5)			
<b>Deeds Registries Act 47 of 1937</b>				As per section 13 in the TDA ownership in property accrues once delivery has taken place. Delivery takes place once the property has been transferred into the name of the purchaser. (Refer chapter 4.6)
<b>Common Law Principles</b>				Ownership in property accrues once delivery has taken place. Delivery takes place once the property has been transferred into the name of the purchaser. (Refer chapter 4.7)

### **Income tax - the tax year in which the transaction will be accounted**

For capital gains tax purposes the seller of the property will need to declare the disposal of the property in the 2014 tax year. Ownership was deemed to have occurred to the purchaser on the 26 February 2014. Even though transfer has only taken place in the Deeds Registries Office in the 2015 tax year **this bears no relevance on when ownership has been deemed to accrue and be declared.**

With regards to the payment of transfer duty, the buyer of the property has 6 months in which to pay the transfer duty from the date on which the agreement was entered into. If the transfer duty is not paid within the period allowed interest will be payable in addition to the unpaid transfer duty.<sup>108</sup>

### **4.10 Conclusion**

<sup>108</sup> South African Revenue Services (SARS) Website [Online]. Available : <http://www.sars.gov.za/AllDocs/OpsDocs/Guides/LAPD-TD-G01%20-%20Transfer%20Duty%20Guide%20-%20External%20Guide.pdf>, Page 41, 2 June 2016

From the above tables and examples it is evident that there are a number of discrepancies between the various Acts as well as common law principles when it comes to the timing of when ownership in immovable property is deemed to take place. The Transfer Duties Act does not specifically mention when ownership takes place but indicates that the acquisition of property is seen to be the date that the transaction was entered into. The VAT Act deems ownership to take place at the sooner of transfer or payment while the Income Tax Act deems ownership to take place once all suspensive conditions of the sale agreement has taken place. The Deeds Registries Act makes it clear that ownership will only pass once the immovable property has been registered in the Deeds Registries Office. The VAT legislators have recognised that to pay VAT on proceeds not yet received causes hardship and is not practical when dealing with large and high value assets such as immovable property. The Income Tax Act, however, ignores this fact and sellers may have to pay income tax ( on gross income or capital gains) before any monies are received where the sale transaction occurs over two different years of assessment.

## Chapter 5: A comparison between the timing treatment of the disposal of immovable property for accounting and tax purposes

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## **5.1 Introduction**

International financial reporting standards (IFRS) represent a set of generally accepted accounting principles (GAAP) used by companies to prepare financial statements. The reports are used to understand the company's financial performance annually. Accounting Standards have been developed by an International Accounting Standards Board (IASB) and these accounting rules are currently followed by more than 100 countries of which South Africa is one. Due to the increase in globalisation of financial markets and of companies and making use of a set of financial reporting standards across countries is seen as having increased the comparability of financial statements across borders.<sup>109</sup>

International Accounting Standards (IAS) is defined as standards used for the preparation and presentation of financial statements.<sup>110</sup>

IAS used to record the disposal of immovable property for investment and resale purposes will be discussed in this chapter as well as whether there is a difference in the timing treatment of the disposal of immovable property for income tax and accounting purposes.

## **5.2 Accounting principles regarding the disposal of immovable property**

### **5.2.1 IAS 18 – Revenue**

The IAS for revenue outlines the requirements for when revenue must be recognised from the sale of goods, the rendering of services as well as for interest, dividends and royalties. Revenue is measured as the fair value of the consideration received or receivable and will be recognised when prescribed conditions are met which will depend on the nature of the revenue.<sup>111</sup>

The term recognition of revenue is defined to mean incorporating an item that meets the definition of revenue (as defined above) in the income statement and will be when the revenue meets the criteria of being able to be measured with reliability as well the likelihood that a future economic benefit will flow into the entity from it.<sup>112</sup>

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<sup>109</sup> Financial Times. Ft.com/lexicon. Definition of International Financial Reporting Standards IFRS. [Online]. Available :<http://lexicon.ft.com/Term?term=International-Financial-Reporting-Standards--IFRS>, 10 August 2016

<sup>110</sup> Financial Times. Ft.com/lexicon. Definition of International Financial Reporting Standards IFRS. [Online]. Available :<http://lexicon.ft.com/Term?term=International-Accounting-Standards--IAS>, 5 June 2016

<sup>111</sup> Ibid

<sup>112</sup> Ibid

IAS 18 has provided specific guidance for recognising the sale of goods as well as rendering of services.<sup>113</sup> As this dissertation only covers the disposal of immovable property, the recognising of revenue through the 'sale of goods' will be the focus.

### **Sale of goods**

According to IAS 18 the recognition of revenue arising from the sale of goods should only occur when all of the following criteria are met:

- “the seller has transferred to the buyer the significant risks and rewards of ownership
- the seller retains neither continuing managerial involvement to the degree usually associated with ownership nor effective control over the goods sold
- the amount of revenue can be measured reliably
- it is probable that the economic benefits associated with the transaction will flow to the seller, and
- the costs incurred or to be incurred in respect of the transaction can be measured reliably”<sup>114</sup>

Therefore in the case of disposing of immovable property revenue will only be recognised in the accounting records when the seller transfers all the risks and rewards of ownership to the purchaser, in other words when the property is transferred to the new owner in the Deeds Registries Office. The seller no longer has control over the property and once transfer of the property has taken place the revenue must be realised.

### **5.2.2 IAS 40 Investment Property**

IAS 40 applies to investment property (land and/or buildings) which are held to earn rental income or for capital appreciation (or both) and the way in which the property is accounted for. Investment properties are initially measured at cost price. Investment property is recognised as an asset when the future economic benefit is derived from the property.<sup>115</sup>

An investment property will be derecognised on disposal or when the asset is permanently withdrawn from use in the entity and there is no economic benefit which will be recognised

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<sup>113</sup> Ibid

<sup>114</sup> IAS Plus, IAS 18 – Revenue. [Online]. Available :<http://www.iasplus.com/en/standards/ias/ias18>, 10 August 2016

<sup>115</sup> Financial Times. Ft.com/lexicon. Definition of International Financial Reporting Standards IFRS. [Online]. Available :<http://lexicon.ft.com/Term?term=International-Accounting-Standards--IAS>, 5 June 2016

from it, except from the asset's disposal. Gains or losses arising from the disposal of property must be included in net profit or loss in the period in which they arise.<sup>116</sup>

Therefore once the immovable property is transferred from the seller to the purchaser in the Deeds Registries Office the investment property will be derecognised in the accounting records.

This means that income or gains or losses will be accounted for in the financial year that it is derecognised.

### **5.2.3 IAS 2 Inventories**

IAS 2 prescribes the accounting treatment for inventories. Inventory consists of assets which are held for resale in the ordinary course of business. IAS 2 also provides guidance on determining the cost of inventories<sup>117</sup> however this dissertation will not cover the costing of inventories. For the purpose of this dissertation inventory is immovable property held for resale purposes.

Inventory which is sold is recognised according to the accounting standards in the same period in which the related revenue is recognised.<sup>118</sup>

## **5.3 Timing rules for the disposal of immovable property for accounting purposes**

### **5.3.1 Immovable property as an investment**

An investment property will be derecognised on disposal or when the asset is permanently withdrawn from use in the entity and there is no economic benefit which will be recognised from it, except from the assets disposal. Gains or losses arising from the disposal of property must be included in net profit or loss in the period in **which they arise**.<sup>119</sup>

#### **Example:**

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<sup>116</sup> IFRS Website [Online]. Available :<http://www.ifrs.org/IFRSs/Documents/Technical-summaries-2014/IAS%2040.pdf>, 5 June 2016

<sup>117</sup> Financial Times. Ft.com/lexicon. Definition of International Financial Reporting Standards IFRS. [Online]. Available :<http://lexicon.ft.com/Term?term=International-Accounting-Standards--IAS>, 5 June 2016

<sup>118</sup> Financial Times. Ft.com/lexicon. Definition of International Financial Reporting Standards IFRS. [Online]. Available :<http://lexicon.ft.com/Term?term=International-Accounting-Standards--IAS>, 5 June 2016

<sup>119</sup> IFRS Website [Online]. Available :<http://www.ifrs.org/IFRSs/Documents/Technical-summaries-2014/IAS%2040.pdf>, 5 June 2016

A taxpayer who holds immovable properties for investment purposes decides to sell one of his properties for R1 000 000 on the 17 February 2014. The sale is conditional and subject to the purchaser obtaining a bond on or before 27 February 2014. The bond is granted to the purchaser on the 26 February 2014. Transfer of ownership takes place in the Deeds Registries Office on the 30 June 2014. The purchaser is advised on the 30 June that the transfer of the property has taken place and that he is the new owner.

**For the financial year ended 28 February 2014:**

Even though the property has been sold on the 17 February 2014 and the suspensive conditions of the sales agreement met on the 26 February 2014, the property has not yet been transferred in the Deeds Registries Office to the new owner as at 28 February 2014. The property will remain as an asset in the financial statements of the taxpayer. The significant risks and rewards have not yet been passed to the buyer.

**For the financial year ended 28 February 2015:**

Once transfer of the property goes through the Deeds Registries Office the purchaser will be the new owner according to the Deeds Registries Act (see chapter 4.6).

Once the purchaser is the new owner of the property the seller has no more managerial involvements nor control over the property as he no longer holds the title over the property.

The payment will be received by the seller once transfer has gone through in the Deeds Registries Office (see Chapter 3).

The revenue will be measurable as well as reliable as the appointed transfer attorneys will draw up a final account (see chapter 3).

Therefore as transfer of ownership takes place in the Deeds Registries Office on the 30 June 2014 the property disposed of will be derecognised as an asset in the financial statements and the income, gains or losses will be accounted for.

### **5.3.2 Immovable property held for resale**

Inventory sold will be recognised in the same period in which the related revenue is recognised.<sup>120</sup>

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<sup>120</sup> Financial Times. Ft.com/lexicon. Definition of International Financial Reporting Standards IFRS. [Online]. Available :<http://lexicon.ft.com/Term?term=International-Accounting-Standards--IAS>, 5 June 2016

According to IAS 18 the recognition of revenue arising from the sale of goods should only occur when the following criteria are met:

- “the seller has transferred to the buyer the significant risks and rewards of ownership
- The seller retains neither continuing managerial involvement to the degree usually associated with ownership nor effective control over the goods sold
- The amount of revenue can be measured reliably
- It is probable that the economic benefits associated with the transaction will flow to the seller, and
- The cost incurred or to be incurred in respect of the transaction can be measured reliably.”<sup>121</sup>

**Example:**

A property developer who has a February year end sells a completed sectional title unit for R1 000 000 inclusive of VAT on 17 February 2014. The sale is conditional and subject to the purchaser obtaining a bond on or before 27 February 2014. The bond is granted to the purchaser on the 26 February 2014. No transfer duty is payable by the purchaser as the transaction is subject to VAT. Transfer of ownership takes place in the Deeds Registries Office on the 30 June 2014. The purchaser is advised on the 30 June 2014 that the transfer of the property has taken place and that he is the new owner.

**For the financial year ended 28 February 2014:**

Even though the property has been sold on the 17 February 2014 and the suspensive conditions of the sales agreement met on the 26 February 2014, the property has not yet been transferred in the Deeds Registries Office to the new owner as at the 28 February 2014. The property will remain as an inventory item in the financial statements of the taxpayer.

**For the financial year ended 28 February 2015:**

As in the example above the same principles apply, once transfer of the property goes through the Deeds Registries Office the purchaser will be the new owner according to the Deeds Registries Act (see chapter 4.6).

Once the purchaser is the new owner of the property the seller has no more managerial involvements nor control over the property as he no longer holds the title over the property.

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<sup>121</sup> Financial Times. Ft.com/lexicon. Definition of International Financial Reporting Standards IFRS. [Online]. Available :<http://lexicon.ft.com/Term?term=International-Accounting-Standards--IAS>, 5 June 2016

The payment will be received by the seller once transfer has gone through in the Deeds Registries Office (see Chapter 3).

The revenue will be measurable as well as reliable as the appointed transfer attorneys will draw up a final account (see chapter 3).

As transfer of ownership takes place in the Deeds Registries Office on the 30 June 2014 the inventory (property) has now been sold and will be recognised as revenue in the accounting records of the Property Developer's accounts. As the Property Developer is a registered VAT vendor, VAT will be accounted for on the 30 June 2014 and the VAT account will be credited with the amount which has become due and payable. The Accounting and VAT treatment are therefore aligned in the same year.

## 5.4 A comparison between the Accounting and Tax treatment where there is a disposal of immovable property

### 5.4.1 Immovable property as an investment

A taxpayer who holds a residential property for investment purposes decides to sell the property for R1 000 000 on the 17 February 2014. The sale is conditional and subject to the purchaser obtaining a bond on or before 27 February 2014. The bond is granted to the purchaser on the 26 February 2014. Transfer duty is payable by the purchaser before the deed of sale is lodged with the Deeds Registries Office. Transfer of ownership takes place in the Deeds Registries Office on the 30 June 2014. The purchaser is advised on the 30 June that the transfer of the property has taken place and that he is the new owner.

	Accounting Treatment	8 <sup>th</sup> Schedule of the Income Tax Act No58 of 1962
<b>2014 Tax Year</b>		
On the <b>17 February 2014</b> a sales agreement is entered into between the property developer and the buyer. This is subject to a bond being obtained by the purchaser.		
On the <b>26 February 2014</b> all suspensive conditions of the sale agreement are met as the bond has been approved.		Ownership is deemed to take place once the agreement has been concluded and the disposal is raised as an accrual for capital gains tax purposes.
On the <b>28 February 2014</b> – year end	As at the 28 February 2014 the property has not yet been transferred in the Deeds Registries Office to the new owner of the property and will therefore remain as a fixed asset in the financial statements of the taxpayer.  According to IAS 18 the seller has to transfer the significant risks and rewards of ownership before the	When the IRP6 (provisional tax return) is completed and submitted for the second period of the 2014 tax year at 28 February 2014, the capital gain will need to be calculated on the disposal and this amount included in taxable income.  The capital gain made on the disposal will be included in the 2014 taxable income of the taxpayer.

	revenue can be taken into account.	
<b>2015 Tax Year</b>		
On the <b>30 June 2014</b> the property is registered in the Deeds Registries office and transfer has taken place.	As the seller has transferred the significant risks and rewards of ownership to the purchaser by means of the property being transferred in the Deeds Registries Office on the 30 June 2014, the property will now, according to IAS 40, be derecognised as a fixed asset in the accounting records.	As the disposal was deemed to take place in the 2014 tax year, no capital gain will be included in the taxpayers' 2015 taxable income.

#### 5.4.2 Immovable property held for resale

A property developer who has a February year end sells a completed sectional title unit for R1 000 000 inclusive of VAT on 17 February 2014. The sale is conditional and subject to the purchaser obtaining a bond on or before 27 February 2014. The bond is granted to the purchaser on the 26 February 2014. No transfer duty is payable by the purchaser as the transaction is subject to VAT. Transfer of ownership takes place in the Deeds Registries Office on the 30 June 2014. The purchaser is advised on the 30 June 2014 that the transfer of the property has taken place and that he is the new owner.

	Accounting Treatment	Income Tax Act No58 of 1962	Value Added Tax Act No89 of 1991
<b>2014 Tax Year</b>			
On the <b>17 February 2014</b> a sales agreement is entered into between the property developer and the buyer. This is subject to a bond being obtained by the purchaser.			
On the <b>26 February 2014</b> all suspensive		Ownership deemed to take place, disposal of property	Even though for Income Tax purposes ownership is

conditions of the sale agreement are met as the bond has been approved.		raised as an accrual for income tax purposes.	deemed to take place on the 26 February, for VAT purposes as stated above in chapter 4.4, where goods are supplied under a sale, that supply shall be deemed to take place where registration or transfer of the goods is effected in a deeds registry; or on the date on which any payment is made in respect of the consideration for such supply whichever date is earlier.
28 February 2014 – tax year end	<p>As at the 28 February 2014 the property has not yet been transferred in the Deeds Registries Office to the new owner the property will remain as inventory in the accounting records of the Property Developer – IAS 2.</p> <p>According to IAS 18 the seller has to transfer the significant risks and rewards of ownership before the revenue can be taken into account, therefore no revenue will be accounted for from the disposal of immovable property in the 2014 Annual Financial Statements.</p>	When calculating taxable income for the taxpayer for the 2014 tax year the R1 000 000 less the 14% vat from the disposal of immovable property will be included as part of revenue for income tax purposes even though for accounting purposes this is not accounted for as revenue.	
<b>2015 Tax Year</b>			
On the <b>30 June 2014</b> the property is registered in the	As the seller has transferred the significant risks and rewards of	As the R1 000 000 from the disposal of immovable property was accounted for	The VAT and the purchase price of the immovable property are collected

<p>Deeds Registries office and transfer has taken place.</p>	<p>ownership to the purchaser by the property being registered in the Deeds Registries Office on the 30 June 2014, the disposal of property will now according to IAS 18 be accounted for as revenue in the accounting records. The inventory (immovable property) which is recorded at the carrying amount of the property is recognised as an expense in the accounting records.</p> <p>As the taxpayer is a registered VAT vendor, VAT will be accounted for on the 30 June 2014 and the VAT account credited.</p>	<p>in the 2014 tax year the taxpayer will not account for the revenue again in the 2015 tax year even though for accounting purposes it will be included as part of revenue.</p>	<p>simultaneously and the VAT is paid over to SARS with the first VAT return submitted by the vendor after the property has been registered in the Deeds Registry.</p>
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**5.5 Conclusion**

When comparing the accounting treatment with the taxation treatment when there is a disposal of immovable property it is evident that the treatments are different resulting in a divergence between accounting profit and taxable income. The question needs to be asked as to whether for income tax purposes sellers are disclosing the disposal of immovable property correctly and in the correct year of assessment? There should be a deferred tax adjustment in the year the tax liability is determined. The income tax system in South Africa does not follow accounting principles, specifically in regard to the timing of transactions, therefore necessary care needs to be taken when doing the relevant taxation calculations, namely provisional tax and final tax liability.

**Chapter 6: A comparison of the way in which Australia treats the disposal of immovable property for tax purposes compared to how it is treated in South Africa.**

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## **6.1 Introduction**

As South Africa and Australia both have capital gains tax and because South African tax legislation is quite similar to that of Australia a comparison is done between the two countries to determine how each country accounts for the timing of immovable property transactions when determining the incidence of tax.

## **6.2 Date of contract according to Australian law**

According to common law in Australia the formation of a contract is only required to have the attributes prescribed by common law. A binding contract is therefore entered into where one party communicates unconditional acceptance of an offer made by the other party. The time at which the contract becomes binding is sometimes difficult to determine as a contract may be wholly or partly oral.<sup>122</sup>

There have been a number of cases which have tested on which date a contract has been formed. In *Gardiner v FC of T* 2000 ATC 2018 it was held that the property was acquired on the date on which the taxpayer had accepted the offer and not when the contract was formally exchanged two months later. In the case of *Mc Donald and Anor v Federal Commissioner of Taxation* (2001) 109 FCR 207; 2001 ATC 4146; (2001) 46 ATR 426, it was confirmed that the contract was made on the date and time on which the oral contract was entered into.<sup>123</sup>

A contractual relationship arises every time one enters into a business transaction. A contract is a promise or a set of promises between two or more people that is intended to be enforceable. In Australian law contracts may be done verbally or in writing. However insurance contracts and contracts for the sale of land must be in writing.<sup>124</sup>

According to the Government of South Australia website, there are six basic principles which need to be satisfied for a contract to be legally binding:

- “1. Agreement - where one party makes an offer and the other accepts it.
2. Consideration - where one party gives something in exchange for something from the other party.

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<sup>122</sup> Austax PBR, PBR 1011476855796 Edited version of private ruling. Year Ended 30 June 2010. Capital gains tax - acquisition of CGT asset – date of contract –disposal of CGT asset. [Online]. Available : [https://austaxpbr.com.au/document/PBR\\_1011476855796](https://austaxpbr.com.au/document/PBR_1011476855796), PBR 1011476855796 Edited version of private ruling. Capital gains tax - acquisition of CGT asset – date of contract –disposal of CGT asset, 20 May 2016

<sup>123</sup> Austax PBR, PBR 1011476855796 Edited version of private ruling. Year Ended 30 June 2010. Capital gains tax - acquisition of CGT asset – date of contract –disposal of CGT asset. [Online]. Available [https://austaxpbr.com.au/document/PBR\\_1011476855796](https://austaxpbr.com.au/document/PBR_1011476855796), PBR 1011476855796 Edited version of private ruling. Capital gains tax - acquisition of CGT asset – date of contract –disposal of CGT asset, 20 May 2016

<sup>124</sup> South Australia. Government of South Australia website. Contract law. [Online]. Available :<https://www.sa.gov.au/topics/crime-justice-and-the-law/contract-law>, 23 May 2016

3. Intention - where both parties intend to abide by the contract.
4. Capacity - where both parties are mentally capable of understanding the contract.
5. Genuine consent - where both parties agree to the contract of their own free will.
6. Legality - where all parts of the contract are legal.”<sup>125</sup>

Contract law in Australia is largely based upon common law principles and in many cases these principles have been modified or altered by legislation.<sup>126</sup>

If the contract entered into is done by means of a verbal contract the date for such a contract would be the date ascribed to it at common law. This means that there was an intention by both parties to be bound by it. The contract would in this case become binding when the asset is physically disposed of. If the asset is disposed of under a contract, the time at which the contract will become binding will be when the taxpayer enters into the contract.<sup>127</sup>

### **Timing rules**

In *McDonald and Anor v. Federal Commissioner of Taxation (2001) 109 FCR 207; 2001 ATC 4146; (2001) 46 ATR 426*, it was confirmed that when a written contract exists the signing and exchange of the written contract will be when the contract becomes binding and will also be the time of the capital gains tax event.<sup>128</sup>

### **6.3 Sale of immovable property held as a capital asset**

According to the Australian Taxation Office a capital gains tax event occurs when there is a disposal of a capital gains tax asset. The asset must have been acquired or have been deemed to be acquired on or after the 19 September 1985. A capital gain or loss will be disregarded for capital gains tax purposes if the asset was acquired prior to 20 September 1985. A disposal of a capital gains tax asset will occur when there is a change in the beneficial owner of that asset. A capital gains tax event occurs generally at the making of a contract which will subsequently lead

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<sup>125</sup> Ibid

<sup>126</sup> Ibid

<sup>127</sup> Austax PBR, PBR 1011476855796 Edited version of private ruling. Year Ended 30 June 2010. Capital gains tax - acquisition of CGT asset – date of contract –disposal of CGT asset. [Online]. Available [https://aust taxpbr.com.au/document/PBR\\_1011476855796](https://aust taxpbr.com.au/document/PBR_1011476855796), PBR 1011476855796 Edited version of private ruling. Capital gains tax - acquisition of CGT asset – date of contract –disposal of CGT asset, 20 May 2016

<sup>128</sup> [https://aust taxpbr.com.au/document/PBR\\_1011476855796](https://aust taxpbr.com.au/document/PBR_1011476855796), PBR 1011476855796 Edited version of private ruling. Capital gains tax - acquisition of CGT asset – date of contract –disposal of CGT asset, 20 May 2016

to a change in ownership of that asset. When there is no written contract in place, the timing of the capital gains tax event will occur when there is a change in the ownership.<sup>129</sup>

When land is sold in Australia, the Australian law requires a written contract to be drawn up. The signing and exchange of the written contract is the time of the capital gains tax event. The tax treatment of a disposal of immovable property for capital gains tax purposes will be the date on which the written contract is signed. This was confirmed in the case *Mcdonald & Anor v FC of T2001 ATC 4146*.<sup>130</sup>

#### **6.4 Example for income tax purposes of a sale of immovable property held as a capital asset**

An Australian taxpayer who holds immovable property as a capital asset sells the property under a contract on the 31 May 2013 for a capital gain of \$50 000. Transfer of the immovable property to the new owner only takes place on the 31 January 2014.

Australian tax years run from 1 July to 30 June of the next year.

As the contract was concluded on the 31 May 2013 the capital gain tax event occurred in the 2013 tax year. The \$50 000 capital gain will need to be declared and tax paid on the gain even though settlement and transfer of the property only took place in the 2014 tax year.<sup>131</sup>

#### **6.5 Sale of immovable property held as trading stock**

Income earned from the carrying out of a scheme of profit making as a general rule is derived on an accrual basis. However it has been accepted that business income earned through the sale of immovable property, i.e. land, by means of a conditional or instalment sale agreement is not derived until the date of settlement. This was confirmed in the case of *Gasparin v FC of T (1994) 28 ATR 130*.<sup>132</sup>

In this case it was also confirmed that the land was held as trading stock by the vendor up until the date that settlement was received as it is only at this stage that the vendor will lose all the

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<sup>129</sup> The Taxpayers Guide, Taxpayers Australia Inc 2013 & 2014, 25<sup>th</sup> Edition, The CGT events, Chapter 11.020, page 452

<sup>130</sup> Austax PBR, PBR 1011476855796 Edited version of private ruling. Year Ended 30 June 2010. Capital gains tax - acquisition of CGT asset – date of contract –disposal of CGT asset. [Online]. Available [https://austaxpbr.com.au/document/PBR\\_1011476855796](https://austaxpbr.com.au/document/PBR_1011476855796), PBR 1011476855796 Edited version of private ruling. Capital gains tax - acquisition of CGT asset – date of contract –disposal of CGT asset, 20 May 2016

<sup>131</sup> The Taxpayers Guide, Taxpayers Australia Inc 2013 & 2014, 25<sup>th</sup> Edition, The CGT events, Chapter 11.020, page 452

<sup>132</sup> The Taxpayers Guide, Taxpayers Australia Inc 2013 & 2014, 25<sup>th</sup> Edition, The CGT events, Chapter 10.780, page 435

rights over the land. This will also be the stage where any contingencies that may result in the sale being prevented cease to exist.<sup>133134</sup>

A tax ruling in relation to the *Gasparin Case* states:

“The derivation of income from the sale of goods should be contrasted with the derivation of income from the sale of real property. It was held in *Gasparin* that income from the sale of land was not derived until settlement had taken place. We do not think that von Doussa J’s decision was based on the fact that legal ownership in the land would not be transferred until settlement. The explanation for the judgement rather lies in the realisation that a vendor in a real property transaction will not have performed all that is needed to become entitled to a payment prior to settlement. At settlement, transfers are effected which put the purchaser in a position to become registered as owner. As such, the vendor does not earn the income from the sale until settlement.”<sup>135</sup>

Therefore the tax treatment for the transfer of immovable property from the vendor will first need to occur before the income from the disposal can be accounted for as a disposal, up until such time the property will remain part of trading stock of the vendor.<sup>136</sup>

## **6.6 Example for income tax purposes of a sale of immovable property held as trading stock**

The Australian taxpayer/ vendor whose business is trading in immovable property sells a commercial property under a contract on the 31 May 2013 for \$500 000. The contract is only settled on the 31 January 2014 when the transfer takes place.

The Australian tax years run from the 1 July each year to the 30 June each year.

As the transfer of immovable property from the vendor will first need to occur before the income from the disposal can be accounted for as a disposal, the immovable property will

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<sup>133</sup> Ibid page 435.

<sup>134</sup> In delivering his judgement in the *Gasparin v F C of T (1994) 28 ATR 130*. case the judge was in agreement with the taxpayer’s argument in that income from the sale of land is not derived until settlement and stated the following:

“If the appellant’s approach is correct, the allotments remained trading stock on hand until each transaction progressed to the point where a debt accrued due from the purchaser i.e. at settlement. If before that point was reached, a contract of sale came to an end, the allotment remain as stock on hand and no accounting consequences would arise, save in respect of the deposit payment made by the purchaser which might, depending on the circumstances in which the contract of sale came to an end, be forfeited to the vendors and thereupon become an actual receipt at that time. On the other hand, if the Commissioner’s approach is correct so that the income is taken to be derived from a sale as soon as a contract of sale becomes unconditional, the Act does not readily provide a means for reversing the imputed derivation of income from the contract which later failed. The difficulty arises from the fact that there is until settlement no debt which can be brought to account as a bad debt under section 63.”

<sup>135</sup> ATO Interpretative Decision, ATO ID 2004/27, Income Tax, Derivation of income : residential properties instalment sales contracts – carrying on a business. [Online]. Available: <http://law.ato.gov.au/atolaw/view.htm?locid='AID/AID200427'>, 23 May 2016

<sup>136</sup> Ibid

remain part of trading stock of the vendor during the 2013 tax year. Once settlement has been received on the 31 January 2014 the income will be accounted for as a sale and taxable as part of income. The \$500 000 income earned from the sale of immovable property will be accounted for by the vendor in the 2014 tax year.

**6.7 Differences in timing of ownership in immovable property for income tax purposes between Australia and South Africa**

	<b>Sale of immovable property held for investment purposes</b>	<b>Sale of immovable property held as trading stock</b>
Australia	Date all suspensive conditions of the sale agreement are met. (Refer chapter 6.3)	Settlement has been received by the vendor and transfer has taken place. (Refer chapter 6.5)
South Africa	Date all suspensive conditions of the sale agreement are met. (Refer chapter 4.2 Timing Rules)	Date all suspensive conditions of the sale agreement are met. (Refer chapter 4.3 Timing Rules)

**6.8 VAT consequences**

With effect from the 1 July 2000 Australia has applied a 10% goods and services tax (GST) on the supply of most goods, services and anything else, which includes all imports. In South Africa we apply value added tax (VAT) at a rate of 14%.<sup>137</sup>

In South Africa when dealing with immovable property which is subject to VAT as discussed in chapter 4.4 above, the VAT will only become due once transfer or registration of the property has taken place which in essence means that the property has been registered in the deeds registry.

In Australia according to GSTR 2000/28 the taxable supply of land under a land contract which is subject to GST will only become payable in the period in which the settlement occurs, this is

<sup>137</sup> The Taxpayers Guide, Taxpayers Australia Inc 2013 & 2014, 25<sup>th</sup> Edition, The CGT events, Chapter 23.132, page 1146

irrespective of whether the cash or accrual basis is used. A deposit will not trigger attribution of GST either.<sup>138</sup>

Therefore the same rules apply both in South Africa and Australia when it comes to the timing of the payment of VAT and GST.

## **6.9 Conclusion**

For capital gains tax purposes South Africa and Australia treat the transactions in the same manner. Both South Africa and Australia see the time of disposal as the date when the contract has been concluded. Both countries tax the gain or loss in the year in which the contract was concluded and not when the transaction has been settled and transfer has taken place.

When immovable property is disposed of in South Africa and Australia as part of trading stock the transactions are treated differently. In Australia the accrual for income tax purposes will only be accounted for once transfer of ownership of the immovable property has taken place. In South Africa the accrual will take place once the contract has been concluded.

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<sup>138</sup> The Taxpayers Guide, Taxpayers Australia Inc 2013 & 2014, 25<sup>th</sup> Edition, The CGT events, Chapter 23.132, page 1146

**Chapter 7: Conclusion and recommendations**

7.1 Concluding remarks and recommendations.....	66
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## **7.1 Concluding remarks**

In the introduction it was mentioned that in 2013 a research study was conducted to determine how big the immovable property market in South Africa is. At that stage it was estimated to be worth in excess of R4.9 trillion and that according to the Estate Agency Affairs Board of South Africa the number of new registrations per year for residential properties are about 65 000.<sup>139</sup> The number of commercial property registrations taking place in a year was not able to be determined however the majority of property transfers done in the deeds office are residential properties.

The main Acts applicable to the disposal of immovable property are the Alienation of Land Act 68 of 1981, the Deeds Registries Act 47 of 1937(DRA), the Sectional Titles Act 95 of 1986, the Subdivision of Agricultural Land Act 70 of 1970, the Transfer Duty Act 40 of 1949(TDA), the Value Added Tax Act 89 of 1991(VAT Act) and the Income Tax Act 58 of 1962(ITA). Apart from legislation there is also South African common law which is based on Roman-Dutch and English Law principles which also play an important role when dealing in immovable property.<sup>140</sup>

As there are so many Acts applicable to the disposal of immovable property the dissertation focused its review on the differences in the timing of ownership according to the ITA, VAT Act, TDA and DRA as well as common law principles. International accounting standards were reviewed and a comparison drawn between the accounting treatment of a disposal and the tax treatment. A comparison was also made between South Africa and Australia with regards to how for tax purposes the disposal of immovable property is treated.

Statutory authority is necessary before taxes can be imposed and only the statute must be used in order to determine the liability for tax. Accounting or related principles are not taken into account when the tax liability is determined except in instances where the ITA specifically provides for it.<sup>141</sup>

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<sup>139</sup> Citymark, Centre for Affordable Housing In South Africa, The South African Housing Market Overview, February 2016. [Online], Available :<http://www.housingfinanceafrica.org/wp-content/uploads/2015/09/The-South-African-Housing-Market-Overview-2015.22> April 2016

<sup>140</sup> Webbers Attorneys Notaries Conveyancers, Real Estate. [Online]. Available :<http://www.webberslaw.com/property-and-real-estate-2/> 21 April 2016

<sup>141</sup> University of South Africa, Tutorial Letter 102/0/2015 ADVANCED TAXATION 2015, Department of Financial Intelligence. [Online]. Available : [http://www.unisa.ac.za/contents/colleges/col\\_accounting\\_sciences/docs/cta/TAX4861\\_2015\\_TL\\_102\\_0\\_B.pdf](http://www.unisa.ac.za/contents/colleges/col_accounting_sciences/docs/cta/TAX4861_2015_TL_102_0_B.pdf) , 20 June 2016

Legislation forms the main source of tax law however case law also constitutes an authoritative source. There are a number of provisions in the act which contain terms that are not defined and it is therefore necessary to refer to case law for guidance on the meaning of these terms.<sup>142</sup>

The principles which were confirmed in *SIR v Silverglen* and were discussed in chapter 4 need to be taken into consideration when determining the timing of the disposal of immovable property for income tax purposes.

According to *SIR v Silverglen* amounts which are payable under agreements are to be taxed in the year in which they are deemed to have accrued and not in any subsequent year of receipt or actual accrual when payments are made. The total amount receivable from the sale of immovable property will be deemed to accrue to the recipient at the date of the agreement.

Section 24(1) of the ITA was relevant in *SIR v Silverglen*, this section makes it very clear that the transfer of immovable property shall be deemed to accrue to the taxpayer on the date that the agreement was entered into.

Paragraph 13 of the Eighth schedule in the ITA deems delivery to take place once the agreement has been concluded. Even though delivery is deferred and requires performance on the part of the seller, this in itself does not make delivery a suspensive condition. Delivery is seen as a one of the terms of the contract and even if delivery does not occur this gives rise to ordinary contractual remedies of a compensatory nature.<sup>143</sup>

Under the VAT Act a special timing rule applies in relation to immovable property which is supplied under a sale. The supply for VAT purposes is deemed to take place at the earlier of the date of registration of transfer and the date any payment is received. A supplier of immovable property who accounts for VAT on the invoice basis will in essence only account for the output tax once he receives the payment for the property disposed of.<sup>144</sup> Therefore when dealing with immovable property the VAT will only become due once transfer or registration of the property has taken place which means that the property has been registered in the deeds registry office.

The TDA makes no mention as to ownership of immovable property or when ownership passes. The only reference is to acquisition of property and that date is seen to be the date that the transaction was entered into.<sup>145</sup>

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<sup>142</sup> University of South Africa, Tutorial Letter 102/0/2015 ADVANCED TAXATION 2015, Department of Financial Intelligence. [Online]. Available : [http://www.unisa.ac.za/contents/colleges/col\\_accounting\\_sciences/docs/cta/TAX4861\\_2015\\_TL\\_102\\_0\\_B.pdf](http://www.unisa.ac.za/contents/colleges/col_accounting_sciences/docs/cta/TAX4861_2015_TL_102_0_B.pdf) , 20 June 2016

<sup>143</sup> Ibid page 111.

<sup>144</sup> de Koker AP, Williams RC, Silke on South African Income Tax, Last updated March 2016, Chapter 10.15

<sup>145</sup> Haupt P, Notes of South African Income Tax 2016, Chapter 31 page 961.

According to the DRA ownership of immovable property only takes place once the transfer of ownership has been registered in the Deeds office.

According to common law the acquisition of ownership in immovable property is when the transfer of ownership is done by means of registration in the deeds office.<sup>146</sup>

If the international accounting standards are taken into account, immovable property is only derecognised in the accounting records once the property has been transferred to the new owner by means of registration in the deeds office even though an agreement of sale has been entered into.

According to the Australian common law if an asset is disposed of under a contract, the time at which the contract will become binding will be when the taxpayer enters into the contract.

In *McDonald and Anor v. Federal Commissioner of Taxation (2001) 109 FCR 207; 2001 ATC 4146; (2001) 46 ATR 426*, it was confirmed that when a written contract exists the signing and exchange of the written contract will be when the contract becomes binding and will also be the time of the capital gains tax event.<sup>147</sup>

In Australia the tax treatment of a disposal of immovable property held for investment purposes will be the date on which the written contract is signed. This was confirmed in the case *Mcdonald & Anor v FC of T2001 ATC 4146*.<sup>148</sup>

When income is earned from the disposal of immovable property as part of a scheme of profit making the general rule is that income is derived on an accrual basis. However it has been accepted in Australian tax law that business income earned through the sale of immovable property by means of a conditional or instalment sale agreement is not derived until the date of settlement.<sup>149</sup>

Therefore for capital gains tax purposes South Africa and Australia treat the transactions in the same manner. Both South Africa and Australia see the time of disposal as the date when the

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<sup>146</sup> Boshoff Dr D, The South African Council for the Quantity Surveying Profession, Professional Skills Module No. 8, Understanding the Basic Principles of Property Law in South Africa, Revised 30 August 2013, page 20.

<sup>147</sup> Austax PBR, PBR 1011476855796 Edited version of private ruling. Year Ended 30 June 2010. Capital gains tax - acquisition of CGT asset – date of contract –disposal of CGT asset. [Online]. Available [https://aust taxpbr.com.au/document/PBR\\_1011476855796](https://aust taxpbr.com.au/document/PBR_1011476855796), PBR 1011476855796 Edited version of private ruling. Capital gains tax - acquisition of CGT asset – date of contract –disposal of CGT asset, 20 May 2016

<sup>148</sup> Austax PBR, PBR 1011476855796 Edited version of private ruling. Year Ended 30 June 2010. Capital gains tax - acquisition of CGT asset – date of contract –disposal of CGT asset. [Online]. Available [https://aust taxpbr.com.au/document/PBR\\_1011476855796](https://aust taxpbr.com.au/document/PBR_1011476855796), PBR 1011476855796 Edited version of private ruling. Capital gains tax - acquisition of CGT asset – date of contract –disposal of CGT asset, 20 May 2016

<sup>149</sup> The Taxpayers Guide, Taxpayers Australia Inc 2013 & 2014, 25<sup>th</sup> Edition, The CGT events, Chapter 10.780, page 435

contract has been concluded. Both countries tax the gain or loss in the year in which the contract was concluded and not when the transaction has been settled and transfer has taken place.

However when immovable property is disposed of in South Africa and Australia as part of trading stock the transactions are treated differently. In Australia the accrual for income tax purposes will only be accounted for once transfer of ownership of the immovable property has taken place. In South Africa the accrual will take place once the contract has been concluded.

The aim of this dissertation was to answer the question of whether there is a disconnect between the timing of the transfer of immovable property and the timing of the attendant taxation for the seller through analysing specifically the various Acts and laws which impact the transfer of immovable property. It is evident that such a disconnect exists between the timing of the transfer of immovable property and the timing of the taxation.

From the Acts reviewed in the dissertation, the ITA is the only Act that deems the transfer of immovable property to accrue to the taxpayer on the date that the agreement was entered into, even the VAT Act states that VAT will only become due once transfer or registration of the property has taken place which in essence means that the property has been registered in the deeds registry office.

As discussed in chapter 4.4 above, the VAT Act was amended in 1993 to accommodate property developers, as it was understood that there is a practical problem which exists whereby the projects undertaken by property developers normally last longer to complete and will vary in time when transfer of the property is to take place in the deeds registry office. This resulted in the VAT Act being amended and deeming the payment of VAT to be able due and payable only once transfer or registration has taken place.<sup>150</sup>

The question that now follows is that as this disconnect does exist, is the ITA being complied with when there is a disposal of immovable property? Is the disposal being accounted for in the correct tax period? The ITA is very clear with regards to when the disposal of immovable property needs to be accounted for, for both properties held for investment and resale purposes. However this could be easily overcome by amending the legislation to be more in line with the VAT treatment of disposals of immovable property. From a practical perspective a large tax liability could exist prior to any money being received which can cause financial difficulty. Take for example the scenario of the second provisional tax calculation, the financial impact could be large as the disposal of the property would need to be accounted for during the period even though the funds from the disposal could not yet have been received. If the

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<sup>150</sup> Republic of South Africa, Explanatory Memorandum on the Taxation Laws Amendment Bill, 1993, Clause 25, page 11

disposal is not accounted for in the provisional tax calculation this will result in penalties and interest being levied on the under estimation. It was for these reasons that the VAT Act was changed to defer the VAT liability until some proceeds are received.

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