

VAT Alert

12 September 2011

Advisory services relating to share dealings

Imported services and input tax implications

The Tax Court recently held that advisory services obtained to perform statutory obligations are acquired for enterprise purposes. But the Court also found that other advice relating to share dealings are not incurred for making taxable supplies.

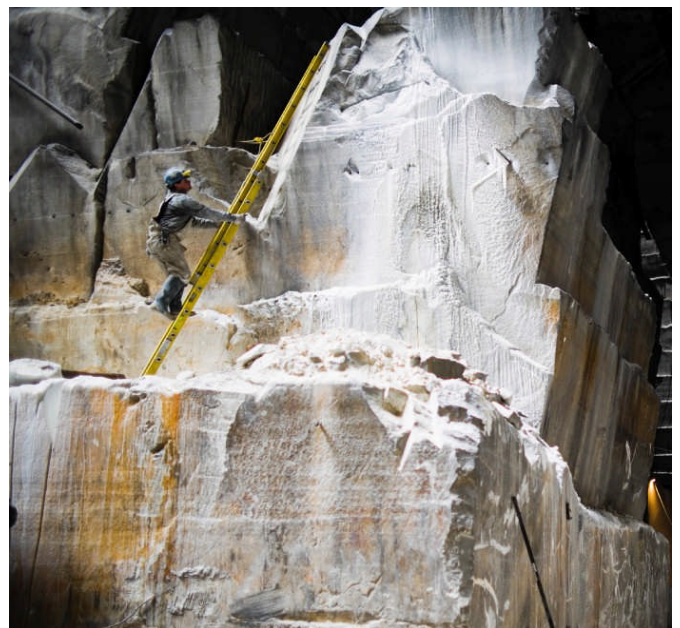
In Case VAT 382, a listed company, which is involved in the mining and selling of diamonds, received a proposal from a consortium of certain of its shareholders to acquire the shares of the remaining shareholders.

Due to a statutory obligation, the Company acquired the services of a UK adviser, in order to be able to advise its shareholders on the fairness and reasonableness of the consortium's offer. In addition, the Company acquired legal, accounting and financial services from local advisers.

The Company did not pay VAT on imported services, as it was of the view that the UK adviser's services were acquired for purposes of its diamond mining and selling business. For the same reason, the Company claimed the VAT incurred by it on the local advisory services as input tax. SARS, however, raised assessments for VAT payable on imported services and for VAT incorrectly claimed as input tax.

Foreign advisory services

The Tax Court held that the services provided by the foreign advisers do not constitute imported services because they were utilised and consumed for the purpose of making taxable supplies, in the course or furtherance of its enterprise of mining and selling diamonds. The Court was satisfied that the services are legally required of a listed company carrying on a



continuing enterprise, and in light of a statutory obligation of providing advice to the independent shareholders, which advice thus constituted an activity performed in the course or furtherance of the Company's enterprise.

The Court added that there was no justification in the language of the VAT Act to limit the concept 'enterprise' so as to apply it exclusively to assets which are used directly in the making of taxable supplies.

Local advisory services

The Tax Court accepted that some of the local advisory services related to the fiduciary obligations to give advice to the shareholders and therefore stands on a similar footing as the foreign advice. However, the Court found that the other portion of the local services were not incurred as a result of a statutory obligation, but merely in order to ensure the optimum transfer of shares and cash to independent unit holders.

Furthermore, the Court held that these advisory services, which related to the disposal of shares to non-residents, were not acquired to make zero-rated supplies. The Court agreed with SARS that when shares are held as an investment, it does not constitute an enterprise and thus the disposal of these shares are outside the scope of VAT and can be neither exempt (in the case of sales to residents) nor zero-rated (in the case of sales to non-residents).

As the ratio between the services relating to the statutory fiduciary obligation (which were acquired for purposes of taxable supplies) and services acquired for non-taxable supplies was not clear, the assessment was referred back to SARS for further investigation and issuing of a revised assessment.

The way forward

Based on the judgment, it can be assumed that expenses incurred on advice obtained as a result of a statutory obligation are used in the course or furtherance of the business activities and thus for purposes of making taxable supplies, even though the advice relates to share transactions.

However, SARS is likely to argue in future that if there is no statutory obligation to obtain the advice and the advice relates to the disposal of shares held as an investment, the disposal of the shares falls outside the scope of the VAT Act and can be neither an exempt supply (in the case of a sale to a resident), nor a zero-rated supply (in the case of a sale to a non-resident), but instead constitutes a 'non-supply', which means that input tax cannot be claimed.

The view is held that the approach that shares held as an investment is not an asset in an enterprise, and that the disposal of these shares does not constitute the 'supply' of services which would be subject to 14% VAT, had the supply not been listed as an exempt supply of a financial services, is incorrect.

While we understand that both parties have lodged appeals to the judgment, we would advise vendors to consider the potential impact of the judgment on their past and future liability for VAT on imported services and their input tax entitlement, especially in view of the fact that 31 October 2011, the last day for lodging applications for voluntary disclosure relief relating to any VAT defaults which occurred prior to 17 February 2010, is fast approaching.

We can assist you in determining your potential VAT liabilities, or entitlement to claim input tax for past tax periods. Please contact one of our indirect tax experts listed below.

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