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Retrospective approval of apportionment methodology

In brief

The SCA handed down its decision in the case of Mukuru Africa (Pty) Ltd vs The Commissioner for SARS [Case no: 520/2020] where it was decided that proviso (iii) to section 17(1) of the VAT Act is applicable to the Appellant and that a method of apportionment can only be approved by the Commissioner from the year of assessment within which the taxpayer applied to SARS for approval of such method.

In detail

Background to the matter

Mukuru provides money-transfer services within Africa and bureau de change services. In conducting its enterprise, Mukuru makes both taxable and exempt supplies for VAT purposes and is therefore required to apportion the VAT incurred on its mixed expenses (that is, those expenses incurred for both taxable and non-taxable purposes).

In light of the above, Mukuru applied to SARS for approval to apply the Transaction Count-Based ("TCB") method of apportionment with effect from 1 February 2014. SARS approved the use of the requested method, however the approval was only granted prospectively and not for any tax periods prior to the year of assessment within which Mukuru applied for such approval. SARS referred Mukuru to the Standard Turnover-based method ("STB method") as approved and set out in Binding General Ruling No.16 ("BGR16") for the prior periods.

SARS placed reliance on the proviso (iii) to section 17(1) to justify its prospective approval of the TCB.

Let's talk

For a deeper discussion of how this issue might affect your business, please contact:

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Mukuru was of the view that the STB method is the only pre-approved apportionment method that may be used without specific prior written approval from the Commissioner. However, Mukuru was of the view that it could not apply the STB method due to the condition placed on the use of the STB method, that is, if the STB method produces an absurd result, proves impossible to use, or does not yield a fair result, the vendor must approach SARS to obtain approval to use an alternative method that yields a more accurate result.

Mukuru, being of the view that it did not have an approved method and therefore was not bound by the proviso (iii) to section 17(1) as it was not seeking to change an existing approved method, therefore objected to SARS decision refusing to "backdate" the methodology and eventually appealed to the Tax Court. The question at hand was therefore whether SARS was precluded by law, and more particularly by proviso (iii) to section 17(1) of the VAT Act, from approving the use by Mukuru of the TCB method in respect of historic tax periods.

The tax court found in favour of SARS (*Case No. 2063*) and stated that "*there is no reason why the legislature should not restrict the period of retrospective application of a private ruling having regard to the context and purpose of the provision and affording the provision a sensible and business-like interpretation to it."*

Mukuru appealed the matter to the SCA. Mukuru's arguments centred around the fact that BGR16 must be considered in its entirety and that the ruling made in BGR16 is immediately subject to internal limitations and restrictions. The effect of this is that the STB method could never have applied to Mukuru in the first place, due to the conditions imposed by BGR16. It further argued that section 17(1) as well as proviso (iii) thereto must be interpreted to apply to a specific vendor and cannot be regarded as a blanket section / approach for all vendors. As such, the approval of the method referred to in proviso (iii) to section 17(1) can only be a specific method approved for Mukuru and not a blanket approval for all vendors in general.

SARS argued that the STB method approved in terms of BGR16 is a method approved for all vendors. Whether a vendor can use it or not depends on its appropriateness. Therefore, a method was approved for Mukuru and cannot be 'changed' retrospectively (regardless of whether Mukuru can use such method or not).

The SCA handed down its judgment on 16 September 2021 and concluded that the STB method set out in BGR16 is an approved method for all vendors. That is *"the ratio in BGR16 thus applies to all vendors to whom section 17 finds application and who had not applied for and been granted an alternative ruling by the Commissioner."* The SCA further found that the conditions in BGR 16 *"are not conditions in the true sense and that they do not relate to the ratio referred to in section 17, but rather to the requirement to apply to SARS for an alternative ruling in the event that the STB method operates unfairly and unreasonably or is inappropriate. The condition, such as it is, cannot qualify section 17(1)."*

The SCA mentioned that *"the purpose served by the requirement that a vendor must make an application to the Commissioner, is to enable the latter to evaluate whether there is indeed any unfairness, unreasonableness or inappropriateness and if so, to approve an alternative method."*

It was concluded that on a proper understanding any further application for a method that is appropriate, is a request to change from the STB method.

Conclusion

Having regard to the judgment, the STB method is an approved method for any and all vendors and can only be changed with effect from a future date; that is from the year of assessment within which the vendor applies to SARS for the approval of the method. The condition contained in BGR16 that requires the method to be fair and reasonable before being applied, based on the SCA judgment, cannot operate to exclude the application of the STB method to a vendor even where such method is subsequently found by the Commissioner to be unfair, unreasonable or inappropriate.

Based on the above, it is clear that no alternative method can be approved by SARS retrospectively. That is, SARS can only approve a specific method for a vendor with effect from the year of assessment within which it applied for the ruling going forward.

What does this mean for vendors? Where a vendor does not have a specifically approved method for past tax periods (that is prior years of assessment), such vendor can only use the STB method to deduct input tax in those periods, regardless of whether it results in a more detrimental or beneficial position for the vendor. Therefore, if the vendor deducted input tax based on an unapproved method in the past or deducted input tax in full where it should have apportioned it, such vendor will be required to make the necessary adjustments in order to bring to account the input tax that was over-deducted in those periods by applying the STB method, noting that the vendor will also be liable for late payment penalties, understatement penalties and interest.

Vendors should accordingly consider the appropriate manner of correcting past non-compliance.

Vendors should also be aware of the importance of regularly analysing the nature and quantum of amounts received on an ongoing basis during the financial year to identify whether a requirement to apportion input tax arises, and where necessary, to apply to the Commissioner for SARS for an alternative method of apportionment prior to the financial year end where the STB method does not result in a fair and reasonable outcome.