30 November 2015

Group Executive: Interpretation & Rulings
SARS Legal & Policy Division
Khanyisa Building
Brooklyn
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BY E-MAIL: policycomments@sars.gov.za;

RE: COMMENT RESPONSE TO THE SARS DRAFT INTEPRETATION NOTE RELATING TO YEARS OF ASSESSMENT AND RELATED MATTERS

We refer to your request for comments on draft IN on the application of section 66(13C) and the discretionary power vested in the Commissioner to accept financial accounts of a company for a period ending on a day which differs from the last day of the company's financial year.

Under section 66(13C) the Commissioner can accept accounts drawn to a "fixed day" which is within ten days on either side of its financial year.

Attached are the comments associated with the draft IN for your consideration.

Sincerely

Piet Nel

Tax Technical Department

I. General Considerations

As a general matter, we largely agree with the draft interpretation note in terms of the law. The bigger issue is operational practice. Systems processes in terms of electronic filing and operational approvals make the process somewhat cumbersome. We also note that the impact of changes to year-ends needs to be integrated with provisional tax returns (Point V.)

II. Differences in Financial and Years of Assessment

A. Background Law

In terms of section 27 of the Companies Act "the first financial year of a company -

(a) begins on the date that the incorporation of the company is registered, as stated in its registration certificate; and

(b) ends on the date set out in the Notice of Incorporation, which may not be more than 15 months after the date contemplated in paragraph (a)."

The term "year of assessment" (as defined in section 1(1)) allows for the 'financial year' to differ from a period of 12 months. If a company is incorporated and its first financial year ends on a date more than 15 months after the date that the incorporation of the company was registered, it is then possible that its 'year of assessment' doesn't end on the last day of February immediately succeeding the date of incorporation. Similarly, if a company incorporated on 1 February 2015 adopts a financial year-end of the last day of February, the company could have a first financial year of one month.

B. Practical limitations

The problem in practice is that it is often not possible to submit two returns within a single financial year. If a year-end occurs on 31 March (as in Example 1 of the draft note), no practical issues arise. However, if the financial year falls in a different month (say April), system issues arise. The problem is that, when the year-end changes from April to December, the company would have two years of assessment that fall (in the current SARS view) in the same year of assessment. It would then only be able to file one return and the SARS solution to deal with this is to add the information to the next return. This is of course not correct and the system should be changed to allow for this (with a corresponding adjustment to the draft note). In essence, the SARS system needs to allow for multiple years of assessment within a single financial year.

III. Need for a Semi-Automatic Approval System

We agree that approvals for changes to years of assessment may require discretionary SARS intervention. Taxpayers should not be allowed to change years of assessment for tax benefits. One-off changes for staff shortages or special contracts are also a problem.

That said, the majority of year-end change requests stem from mergers and acquisitions. These changes are fully recognised in the draft interpretation note. In these instances, taxpayers should be allowed to automatic approval (via e-filing) if the cause of the change is to align year-ends with new controlling shareholders. SARS should then have right to override any tax benefit resulting from these changes if SARS subsequently determines that a significant tax benefit was realised from the change. Automatic approvals for year-end changes of this kind will ease compliance delays and reduce the administrative burden on SARS.

The draft note should also list further examples of valid possible reasons to allow for year-end changes on a discretionary basis. In our experience, we understand that there may be two additional common grounds for year-end changes:

- *Seasonal businesses:* Certain businesses operate based on the seasonal clientele. These business may entail holiday destinations (e.g. summer and winter hotel resorts) where business operates in mid-year peaks followed by inaction. At start, the business may have set the year without regards to these consideration – only to find that the year-end must adjust to this practical reality.

- *Retail businesses:* Certain business may find the press of year-end business too great for a proper accounting. For instance, retail business may find that the standard February year-end is preferable because accrued sales cannot be properly accounted for at 31 December given the Christmas rush.

Again, the above examples are just possible requests for year-end changes that would require discretionary approval.

IV. Technical Point: Paragraph 4.2 (Financial accounts drawn up for a period that differs from the financial year)

“For the purpose of section 66(13C),’ it is stated that “income” is interpreted as “profit” or “taxable income”. This interpretation is necessary to ensure that any deductions and allowances included in the financial accounts of a company are allocated to the correct year of assessment.” However, we don’t believe that word ‘profit’ is appropriate and suggest that only ‘taxable income’ be used because the ordinary common law meaning of the word “income”” may well exclude capital gains.

We agree that "any income falling after that fixed day in the financial accounts falls in the subsequent year of assessment" (and equally where the date is fixed after the year-end date). Again the term 'income' should instead be "taxable income", which includes a taxable capital gain arising after (or before) the fixed date.

The statement that "section 66(13C)(b) will thus also apply to an aggregate capital gain or aggregate capital loss" is therefore not fully correct. It is rather where the time of disposal falls within the '10 days before or after' period that section 66(13C)(b) will apply. Example 4 applies this principle correctly.

V. Impact of a change in financial year on provisional tax returns

We accept that a change to a year-end should be submitted before the last day of the applicable financial year. This is particularly important as the due dates of the provisional tax returns will then have to be amended accordingly. In other words, if the request is submitted by the company within a reasonable time and SARS only approves it after the current last day, the request creates problems for the submission of the provisional tax return on the correct date.

The proposed draft accordingly needs to address how changes in years of assessment impact provisional tax returns as both systems require integration. Operational and e-filing process should also be linked.