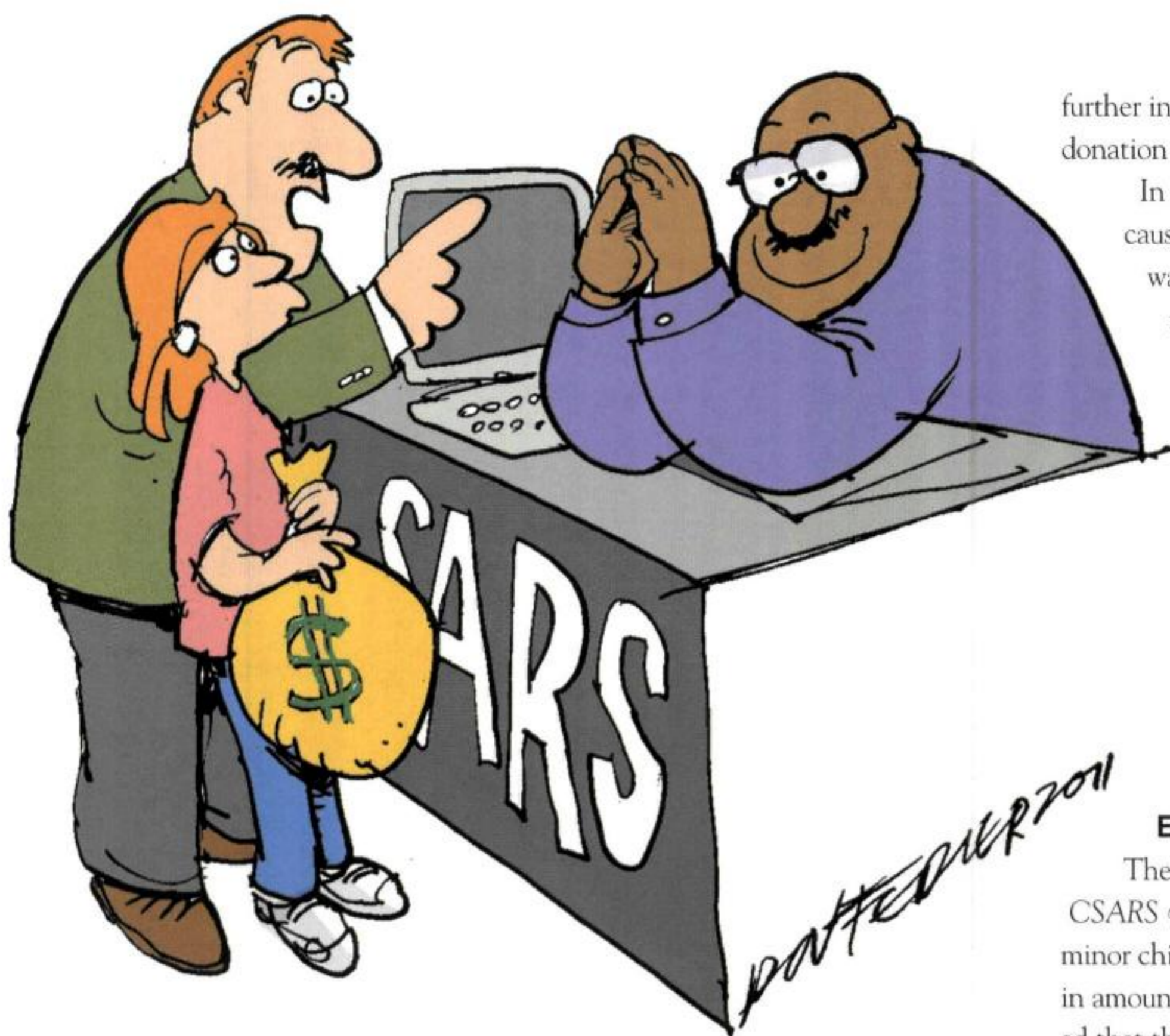


## Tax



to another. It held, however, that the use of these words in s7(3) and (4) indicates that it should have a more restricted meaning. It accordingly concluded that the words must be construed *eiusdem generis* (that is, of the same kind) as “donation” and that the phrase should therefore read “...donation, settlement or other similar disposition”. That would cover any disposal of property made completely gratuitously out of liberality or generosity, but would also cover disposals or settlements where some consideration was made but where there is still an appreciable element of gratuitousness and liberality. Any disposal of property that is wholly commercial would therefore be excluded from this phrase.

The court held that the loans constituted a disposition that was partly commercial and partly gratuitous. The fact that the loans had to be repaid and that interest was charged made it partly commercial. The terms of the repayment were, however, vague and the taxpayer did not ask for security for the loans. In addition, the interest charged by him was less than the rate the bank would have charged the children and this convinced the court that it was also partly gratuitous and fell, therefore, into the expression “or other disposition”. It therefore dismissed the appeal.

### “By reason of”

The next step is to determine exactly what the phrase means. Once again there have been several court cases in this regard.

In *Kohler v CIR*<sup>5</sup> the court held that the words should be interpreted as referring to the proximate and not a remote cause. Where, for example, income is received by reason of a donation and the income is invested, the

further income earned from the investment is not “by reason of” the original donation since the causal connection was interrupted by the investment.

In *CIR v Widan*<sup>6</sup> the court also held that there must be some kind of causal relation between the donation and the income and held that it was necessary to look to the “real efficient” cause of the income being received.

Determining the real efficient cause is not always easy and each case has to be considered on its own merits by investigating the relevant facts and circumstances.

In *CIR v Berold (supra)* the court found that the donation by the parent (that is, the sale of his shares to the company with no interest payable on the outstanding purchase price) was the cause of the dividends being earned and the dividends were therefore held to have been received by the minor children by reason of the taxpayer’s donation and taxable in his hands in terms of s7(3).

### Extent of disposition

The question now raised is to what extent a disposition is taxable. In *CSARS v Woulidge*<sup>7</sup> the taxpayer sold his shares to two trusts of which his minor children were beneficiaries. The trusts had to settle the purchase price in amounts and at times mutually agreed upon. The sale agreement provided that the taxpayer could charge interest, but he didn’t do so. The Special Court held that the forsaken interest was taxable. On appeal to the Supreme Court of Appeal, the Court agreed and confirmed that the market related sale was a commercial transaction and outside the application of s7(3), but the forsaken interest was gratuitous and, therefore, fell squarely within the section.

The principle that has evolved from these decisions is that the amount by which interest charged at a market related rate exceeds the interest actually charged (if any) by the lender is the amount that is attributed to the lender.

### Conclusion

Mr X made an interest-free loan to his minor child to enable her to start a business. The money was used to construct a flat which was then rented out and rental income was earned.

It is clear that Mr X made a *donation, settlement or other disposition*. It is also evident that G earned income as a result of the donation as that is which enabled her to build the flat which she then rented out. Using the judgement in *Woulidge* it is probable that SARS will include, as deemed income in Mr X’s hands, the difference between a market related interest rate and the interest he actually charged (being zero).

Mr X may, in terms of s90, recover from G so much of the tax he paid as is due to the inclusion of the deemed income in his income. Alternatively, if he cannot pay the tax, he may, in terms of s91(4), recover the relevant amount from G’s assets. ♦

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<sup>1</sup> 58 of 1962.

<sup>2</sup> 1962 (3) SA 748 (A).

<sup>3</sup> 1980 (1) SA 674 (T).

<sup>4</sup> 1980 (2) SA 721 (A).

<sup>5</sup> 1949 (4) SA 1022 (T).

<sup>6</sup> 1955 (1) SA 226 (A).

<sup>7</sup> 2002 (1) SA 68 (SCA).