



THE SUPREME COURT OF APPEAL OF SOUTH AFRICA
JUDGMENT

Reportable

Case No: 927/2017

In the matter between:

**COMMISSIONER FOR THE SOUTH
AFRICAN REVENUE SERVICE**

APPELLANT

and

DIGICALL SOLUTIONS (PTY) LTD

RESPONDENT

Neutral citation: *Commissioner for the South African Revenue Service v Digicall Solutions (Pty) Ltd* (927/2017) [2018] ZASCA 137 (28 September 2018)

Coram: Navsa, Majiedt, Swain and Zondi JJA and Mokgohloa AJA

Heard: 21 August 2018

Delivered: 28 September 2018

Summary: Income Tax Act 58 of 1962 – s 103(2) – taxpayer company – successive changes in shareholding in consecutive tax years – sole purpose from time of first change in shareholding to preserve and utilise assessed loss for set-off against future income – assessed loss carried over to next tax year – second acquisition of shares – income thereafter received by taxpayer – income indirect result of first acquisition of shares – set-off of assessed loss against income disallowed.

ORDER

On appeal from: Western Cape Division of the High Court, Cape Town (Cloete J with Yekiso and Nuku JJ concurring, sitting as court of appeal):

- 1 The appeal succeeds with costs, including the costs of two counsel.
- 2 The order of the court a quo is set aside and replaced with the following order:
'(a) The appeal succeeds with costs, including the costs of two counsel.
(b) The order of the tax court is set aside and replaced with the following order:
"The appeal is dismissed and the assessments which form the subject of this appeal are confirmed".'

JUDGMENT

Swain JA (Navsa, Majiedt and Zondi JJA and Mokgohloa AJA concurring):

[1] The appellant, the Commissioner for the South African Revenue Service (the Commissioner), issued additional assessments against the respondent, Digicall Solutions (Pty) Ltd (the taxpayer), during November 2010 in respect of the 2005-2008 income tax periods, disallowing the utilisation by the taxpayer of certain assessed losses during these periods, in terms of s 103(2)(b)(A)(aa) of the Income Tax Act 58 of 1962 (the Act).

[2] Aggrieved at the additional assessments, the taxpayer lodged an objection which was dismissed by the Commissioner. The taxpayer then successfully appealed to the tax court which granted an order setting aside the assessments and referred the matter back to the Commissioner for reassessment on the ground that the taxpayer was entitled to set-off the assessed loss against its income during the relevant years. The Commissioner then appealed to the full court of the Western

Cape Division of the High Court, which dismissed the appeal with costs on the ground, inter alia, that the requirements of s 103(2) of the Act were not satisfied. Special leave to appeal was thereafter granted by this Court.

[3] The relevant portions of s 103(2) of the Act read as follows:

'Whenever the Commissioner is satisfied that—

- (a) any agreement affecting any company or trust; or
- (b) **any** change in—
 - (i) the shareholding in **any** company; or
 - (ii) the members' interests in any company which is a close corporation; or
 - (iii) the trustees or beneficiaries of any trust,

as a *direct or indirect* result of which—

(A) income has been received by or has accrued to that company or trust during **any** year of assessment; or

(B) any proceeds received by or accrued to or deemed to have been received by or to have accrued to that company or trust in consequence of the disposal of any asset, as contemplated in the Eighth Schedule, result in a capital gain during any year of assessment, has at **any** time been entered into or effected by **any** person *solely or mainly* for the purpose of utilizing **any** assessed loss, **any** balance of assessed loss, **any** capital loss or **any** assessed capital loss, as the case may be, incurred by the company or trust, in order to avoid liability on the part of that company or trust or **any** other person for the payment of **any** tax, duty or levy on income, or to reduce the amount thereof—

(aa) the set-off of **any** such assessed loss or balance of assessed loss against **any** such income shall be disallowed. . . .' (Emphasis added.)

[4] In terms of s 103(2) of the Act the Commissioner had to be 'satisfied' that three requirements were fulfilled to justify the disallowance of the assessed loss, namely:

4.1 A change in the shareholding of the taxpayer had been effected; and

4.2 The change in the shareholding resulted directly or indirectly in income being received by, or accruing to the taxpayer, during any year of assessment, and;

4.3. The change in the shareholding was a transaction concluded for the sole or main purpose of utilising the taxpayers assessed loss, in order to avoid liability for the payment of tax on income.

[5] The distinctive feature in the present case is that two changes in the shareholding of the taxpayer occurred in successive tax years. The first sale of shares took place on 5 March 2003, during the taxpayer's 2003 year of assessment, when they were purchased by Selldirect Marketing (Pty) Ltd (SDM). The second, on 25 November 2003, during the taxpayer's 2004 year of assessment, when they were purchased from SDM by a company called Glasfit, which thereafter nominated Nutbridge Investments (Pty) Ltd (Nutbridge) as the purchaser. A portion of the consolidated assessed loss in question was set-off against the taxpayer's income during the 2004 year of assessment, after the shares had been acquired by Nutbridge. The balance was thereafter set-off against the income of the taxpayer during the 2005-2008 income tax periods. As stated earlier, these amounts were subsequently disallowed by the Commissioner. The assessment for the 2004 income tax period was not adjusted, because this was precluded by the lapse of time in terms of s 79 of the Act, as it then stood.

[6] It is common cause that only the first change in shareholding is relevant to the determination of the appeal. Prior to the determination of the dispute before the tax court, the Commissioner applied to amend the grounds of assessment to include the second change in shareholding as justification for the disallowance of the assessed loss during the 2005-2008 income tax periods. The application was dismissed on the basis that the first change in shareholding was foundational to the Commissioner's disallowance of the use of the assessed loss. It was held that the fact that the Commissioner referred to and accepted that there had been a further change in shareholding did not, on a proper understanding and reading of the letter of assessment, disclose an intention to rely on the further change in shareholding for this purpose.

[7] The correct approach to the interpretation of s 103(2) of the Act, was described in *Glen Anil Development Corporation Ltd v Secretary for Inland Revenue* 1975 (4) SA 715 (A) at 727H-728A, as follows:

'Sec. 103 of the Act is clearly directed at defeating tax avoidance schemes. It does not impose a tax, nor does it relate to the tax imposed by the Act or to the liability therefor or to the incidence thereof, but rather to schemes designed for the avoidance of liability therefor. *It should, in my view, therefore, not be construed as a taxing measure but rather in such a way*

that it will advance the remedy provided by the section and suppress the mischief against which the section is directed. The discretionary powers conferred upon the Secretary should, therefore, not be restricted unnecessarily by interpretation.' (Authorities omitted and emphasis added.)

[8] In *Conshu (Pty) Ltd v Commissioner for Inland Revenue* 1994 (4) SA 603 (A) at 611E-612A, it was also pointed out that the intention 'to cast the net as wide as possible' in terms of the subsection could be perceived when regard was had to the use of the introductory 'whenever,' and that the provision was 'replete with the indefinite "any"', which appeared 13 times in s 103(2) of the Act, as indicated above. In addition, in *Commissioner for Inland Revenue v Ocean Manufacturing Ltd* 1990 (3) SA 610 (A) at 618H it was stated that 'any' was a word of wide and unqualified generality which may be restricted by the subject matter or the context, but prima facie was unlimited, and that;

'In regard to the subject-matter there is nothing in s 103(2) to suggest that the word *any* was used in a limited sense.'

[9] As regards the purpose of s 103(2), in *Conshu* at 610F-I, this Court quoted with approval the following statement by D M Stewart 'The Prohibition of Tax Avoidance: An Evaluation of s 103 of the South African Income Tax Act 58 of 1962' (1970) 3 CILSA 168 at 189:

'The reason for this subsection is that elsewhere in the Act (s 20) it is recognised that to divide a taxpayer's business up into separate yearly compartments is largely artificial, and, as a result, where in one year allowable deductions exceed income, the taxpayer may carry the balance of deductible excess forward as an "assessed loss". This loss may be deducted from income earned in the next or a subsequent year. As a result, certain taxpayers, whose businesses have failed to profit, build up large assessed losses. When these taxpayers are individuals the Revenue has nothing to fear for the assessed loss is not itself transferable, but where the taxpayer is a company, whose shares can readily change hands, new proprietors will attach themselves to the company and inject new income into it in order to exploit the assessed loss. It is this "trafficking" in the shares of companies with assessed losses which gave rise to the enactment of s 103(2).'

[10] The submissions by the taxpayer must therefore be assessed against a construction of the subsection that advances the remedy it provides and suppresses

the mischief against which it is directed. The taxpayer submitted that the first change in shareholding could not have been effected for the sole or main purpose of utilising the assessed loss, as there was no income during the taxpayer's 2003 year of assessment, against which the assessed loss could be offset. The purpose test had to be applied with reference to the person who 'effected' the 'change in the shareholding' that resulted in income, against which a set-off of the assessed loss was made. According to the taxpayer this was Glasfit / Nutbridge, the acquirer, pursuant to the second change in shareholding and not SDM, which did not utilise the assessed loss to satisfy the 'purpose' requirement, because of an absence of income by the taxpayer during that year of assessment.

[11] The subsection, however, expressly provides for 'the purpose of utilising *any* assessed loss' to avoid liability 'for the payment of any tax'. It also expressly disallows the set-off of 'any such assessed loss' against 'any such income'. Therefore, the set-off of any assessed loss against any income that is received directly or indirectly by the taxpayer company, as a result of the change in its shareholding, will be disallowed where the sole or main purpose in effecting the change in its shareholding, is to avoid liability for, or to reduce the amount of tax payable, by the taxpayer. The purpose requirement of the subsection may accordingly be satisfied by reference to any year of assessment in which income is received, whether directly or indirectly as a result of the change in shareholding of the taxpayer company, which was effected, whether solely or mainly, for the prohibited purpose. I shall in any event show that the first change in shareholding was directed at that ultimate purpose – utilisation of the assessed loss by the taxpayer.

[12] Before examining the evidence, the incidence of the onus of proof in these proceedings must be considered. The provisions of s 103(4) of the Act provide as follows:

'If in any objection and appeal proceedings relating to a decision under subsection (2) it is proved that the . . . change in shareholding . . . in question would result in the avoidance or the postponement of liability for payment of any tax . . . or in the reduction of the amount thereof, it shall be presumed, until the contrary is proved in the case of any such . . . change in shareholding . . . that it has been entered into or effected solely or mainly for the purpose

of utilising the assessed loss, balance of assessed loss, capital loss or assessed capital loss in question in order to avoid or postpone such liability or to reduce the amount thereof.'

[13] The subsection provides that when it is proved that a change in shareholding has occurred which results in the avoidance, or the postponement of liability for payment of any tax, or its reduction, it will be presumed that the change in shareholding was entered into, or effected solely or mainly for the purpose of utilising the assessed loss, in order to avoid liability for the payment of any tax on income. In *Glen Anil* supra at 730F, it was held that the taxpayer therefore bore the onus in terms of the subsection, to rebut the presumption by proving that the change in shareholding was not effected solely or mainly for the prohibited purpose.

[14] The correct approach in assessing the evidence to determine whether the taxpayer discharged this onus, was described in ITC 1185 (1972) 35 SATC 122 (N) at 123, by Miller J in the following terms:

'It is necessary to bear in mind in that regard that the *ipse dixit* of the taxpayer as to his intent and purpose should not lightly be regarded as decisive. It is the function of the court to determine on an objective review of all the relevant facts and circumstances what the motive, purpose and intention of the taxpayer were . . . This is not to say that the court will give little or no weight to what the taxpayer says his intention was, as is sometimes contended in argument on behalf of the Secretary in cases of this nature. The taxpayer's evidence under oath and that of his witnesses must necessarily be given full consideration and the credibility of the witnesses must be assessed as in any other case which comes before the court. But direct evidence of intent and purpose must be weighed and tested against the probabilities and the inferences normally to be drawn from the established facts.'

[15] Central to a determination of the issue of whether the first change in shareholding was effected solely or mainly for the prohibited purpose, is an examination of the interaction between Mr Benatar, Mr Evans, Mr Kluever and Mr Allers during the period after SDM exercised the option to purchase the shares on 19 September 2002, their subsequent purchase by SDM on 5 March 2003 and their purchase by Glasfit from SDM on 25 November 2003. In order to place this crucial period in context, it is necessary to briefly examine the unsuccessful financial history of the taxpayer, before the first acquisition of the shares in the taxpayer by SDM.

[16] The name of the taxpayer on incorporation on 24 February 2000, was B Clear and Simple Telecommunications South Africa (Pty) Ltd (which later changed its name to that of the respondent) and its sole shareholder was an Australian company, B Digital Ltd. The taxpayer established a call centre facility in Cape Town, which sold MTN and Vodacom contracts, via the call centre to customers. A call centre, according to Mr Benatar, who was appointed as a director of the taxpayer in March 2000, was vital in terms of selling contracts to clients who did not have to come into a branch to do so. The other director of the taxpayer was Mr Lloyd. The taxpayer had an assessed loss in 2001 and in December 2001 it terminated its service provider contracts and disposed of its subscriber bases to MTN and Vodacom. At the beginning of 2002, B Digital Ltd wished to disinvest from South Africa and Mr Lloyd approached Global Capital, an investment company, with the intent that it purchase the taxpayer to provide services to a rival cellular provider, namely Cell C, with the object of making a profit.

[17] Mr Benatar, a chartered accountant who was also a fund manager at Global Capital, stated that the easiest way to effect the purchase was to sell the shares in the taxpayer, as opposed to selling the assets. According to Mr Benatar no mention was initially made of the assessed loss in the taxpayer, which in the 2001 tax assessment was reflected as R47 884 445, the sole purpose being to acquire a call centre to provide services to Cell C. He, however, was constrained to agree that the assessed loss would have appeared in the financial statements and would have been studied during the financial and legal due diligence exercise that Global Capital commissioned, in respect of the taxpayer. It was substantial and could not be ignored.

[18] The due diligence on the taxpayer revealed MTN had instituted proceedings against the taxpayer. According to Mr Benatar this meant Global Capital could not take over the company at that stage because of the continuing liability of an ongoing legal suit. In addition, B Digital wished to remain in control of the taxpayer during the litigation. He stated that Global Capital always wanted to buy the shares directly in the taxpayer and once the dispute with MTN was identified they decided to set up a new company for this purpose. A shelf company, Basfour 2544, was acquired and the name changed to SDM. The shareholders were Global Capital, Mr Lloyd, Mr

Benatar, Mr Nestadt and Mr Bloch. The directors were Mr Lloyd as the managing director, together with Mr Nestadt and Mr Bloch. The plan was for SDM to acquire the assets and the employees of the taxpayer immediately and take over the lease in respect of the call centre. It was to be granted an option to acquire the shares in the taxpayer, to be exercised once the legal dispute was resolved, to enable B Digital to retain control during the litigation.

[19] A written agreement was then concluded on 15 March 2002 between the taxpayer, which at that stage was still called B Clear and Simple Telecommunications, and Basfour 2544 (the name at that stage of SDM) and B Digital, in which the assets of the taxpayer were sold to Basfour 2544. Clause 12 provided that B Digital granted to the purchaser an option to purchase all of the shares in the taxpayer, which option endured for 18 months from the date of the agreement, the purchase price being the par value of the shares. Clause 7 recorded that as at the completion date the taxpayer would have ceased conducting the business.

[20] Mr Benatar accepted that at the time the agreement was concluded, SDM was aware of the loss of R47 884 445 in respect of the tax year ending 30 June 2001, which had not as yet been assessed. SDM was also aware that in terms of s 20 of the Act any assessed loss could only be carried forward to a future year of assessment, where the company in question traded. He acknowledged that this was something, he as a chartered accountant understood and that he knew at the time that if B Clear and Simple Telecommunications were to utilise this assessed loss, the company would, as it were, have to be brought back from the grave and start trading again in order to utilise the assessed loss. He was also aware at the time of the operation of s 103 of the Act.

[21] SDM then conducted the business in Cape Town and took over the lease from B Clear and Simple Telecommunications. However, only once it started, so they said, did they realise that they only needed 30 out of the 120 seats in the call centre. The success of the business of SDM depended substantially on deals being given to it by Cell C to sell contracts. However, the relationship between Mr Lloyd and the

head of marketing at Cell C allegedly soured, with the result that the business did not receive the deals it believed it would.

[22] Because the facilities in the call centre exceeded what they required and did not justify their cost, Mr Benatar stated they decided to sell the call centre and lease back 30 seats in the call centre from any purchaser. According to him this was the main reason they decided to sell the shares in the taxpayer, even before the shares had been purchased by SDM. He maintained the key strategy from the side of SDM was to reduce costs by selling the call centre, thereby reducing their rentals. He agreed, however, that they could have achieved this by just selling the assets. He also agreed by the time they exercised the option to purchase the shares, they already knew they only needed 30 of the 120 seats and nothing prevented them from looking for a buyer for the whole of the call centre.

[23] It is therefore clear that the taxpayer was not profitable from the outset and reflected a staggering assessed loss for the year of assessment ending 30 June 2001, of R47 884 445, which they all realised had a built-in tax advantage, with a concomitant commercial benefit. In December 2001 it terminated its service provider contracts and disposed of its subscriber bases to MTN and Vodacom, which were its main source of business. Messrs Benatar and Lloyd being directors of the taxpayer must have had intimate knowledge of the reasons for its abject failure. Nevertheless, the professed reason for selling the shares in the taxpayer to Global Capital was to provide services to a rival cellular provider namely Cell C, with the object of making a profit. No details were furnished of any business strategy to transform the taxpayer from an abject failure into a profitable entity, by selling services for Cell C in competition with its former suppliers.

[24] For a number of reasons it is improbable this was the true reason for selling the shares in the taxpayer. The success of the business depended substantially on deals being given to the taxpayer by Cell C, to sell contracts. According to Mr Benatar the reason this did not eventuate was simply because of a personal difference between Mr Lloyd and the head of marketing at Cell C. I find it grossly improbable that Global Capital having carried out a due diligence study, would have

purchased the taxpayer with the object of making a profit by selling contracts for Cell C, without having secured a prior commitment from Cell C to do so.

[25] I also find it grossly improbable that Mr Benatar and Mr Lloyd, who had intimate knowledge of the taxpayer's lack of success in selling contracts for MTN and Vodacom, would have been willing to be shareholders in SDM and acquire the business of the taxpayer with the sole object of making a profit, without a prior commitment from Cell C. In addition, Mr Benatar maintained that only once they started operating did they realise they only needed 30 out of the 120 seats in the call centre. Again it is improbable that Mr Benatar with his intimate knowledge of the history of the taxpayer, only came to this realisation after they restarted the business of the taxpayer.

[26] Such ill-informed conduct is only explicable on the basis that the purpose in acquiring the taxpayer was not to make a profit, but to ensure that it was trading, albeit at a loss, as at 30 June 2002. SDM was aware of the large assessed loss of R47 884 445 which could only be preserved and carried forward to the following tax year, if the taxpayer traded. The acknowledgement by Mr Benatar that if the assessed loss was to be utilised the taxpayer would as it were, have to be 'brought back from the grave' and start trading again, reveals their true purpose.

[27] Having ensured the taxpayer was trading as at 30 June 2002, the assessed loss was carried forward into the 2003 tax year and SDM then exercised the option to purchase the shares in the taxpayer, on 19 September 2002. Mr Benatar agreed by the time SDM exercised the option there was nothing left in the taxpayer, except the assessed loss. He also agreed that although their original intention was to acquire the shares in the taxpayer, they were not compelled to do so. He conceded there was nothing to be gained by SDM in acquiring the shares, because the business was dead in the hands of the taxpayer. However, if the taxpayer was revived and was conducting business the assessed loss gave it a value. These concessions together with the fact that a decision had been taken to sell the shares in the taxpayer even before they had been purchased by SDM, again reveals that their true purpose in acquiring the shares even at this early stage, must have been to utilise the assessed tax loss.

[28] According to Mr Benatar, once they had decided to sell the taxpayer and the call centre, Global Capital initiated the sale process. Mr Kluever was an auditor who audited the Global Capital group of companies and Mr Benatar asked him whether he had any clients looking to acquire a call centre. Mr Kluever stated that he had developed a close working relationship with Mr Benatar and Mr Allers, a director of Glasfit and like Mr Benatar and Mr Kluever, a chartered accountant. Mr Benatar stated he could not recall whether they had advised Mr Kluever of the assessed loss in the taxpayer. However, Mr Kluever confirmed Mr Benatar had told him at the outset of the assessed loss of approximately R90 million.

[29] Mr Kluever stated he thought the call centre in Cape Town might be of interest to Mr Allers. He contacted him and Mr Allers indicated Glasfit would be interested in acquiring the taxpayer. Mr Allers stated Mr Kluever had informed him in November 2002 that the taxpayer had made serious tax losses of approximately R90 million. The objective of Mr Allers was to set up a business process outsourcing venture (the venture) for Glasfit, together with a rival company PG Glass, which would require a call centre.

[30] Mr Allers therefore instructed Mr Kluever to gather information to enable an offer to be made to SDM, for the purchase of the taxpayer. On 4 December 2002 in a preliminary report which Mr Kluever prepared and discussed with Mr Allers, he stated the taxpayer had ceased trading after year end being June 2002 and its tax assessment reflected an assessed loss of R47 884 445.

[31] Mr Allers confirmed that Mr Kluever had reported this to him and he agreed that in December 2002, the board of Glasfit knew the taxpayer had ceased its operations and had an assessed loss. However, later in his evidence he sought to minimise this concession by maintaining the board would have queried this, because they wanted a company which was operating a call centre. The objective fact is the taxpayer was a dormant company with a very large tax loss and this was known by the board of Glasfit from the outset, when it discussed the proposed purchase of the shares from SDM.

[32] Mr Kluever stated as part of his due diligence study of the taxpayer, he visited the Cape Town call centre. He concluded it would be suitable for the venture envisaged by Mr Allers. He conveyed his views to Mr Allers but warned him the Commissioner could seek to apply s 103 of the Act to the intended acquisition by SDM of the shares in the taxpayer and the intended sale of the call centre back to the taxpayer. He also warned Mr Allers there was a risk the Commissioner may seek to prevent the carry forward of these losses against future income, if such income resulted directly or indirectly from the intended change in shareholding. He did not recommend that Glasfit should not proceed with the transaction because of this risk, but believed it should be taken into account in determining the value of the taxpayer. It is significant even at this early stage, when SDM had not yet acquired the shares in the taxpayer, the parties were concerned about s 103(2) of the Act being implicated.

[33] Mr Kluever nevertheless maintained that the main focus of the transaction in which Glasfit sought to acquire the shares in the taxpayer was the potential to utilise and conduct the call centre as a going concern, with the relevance of the assessed loss being minimised and with its value being relegated to a negligible factor. He, however, warned Mr Allers that the Commissioner might also seek to apply s 103 of the Act to this purchase of the shares in the taxpayer by Glasfit. His concern arose from the magnitude of the assessed loss and the inherent danger that any change in shareholding where a tax loss was involved, was at risk of being exposed to s 103 of the Act.

[34] The involvement of Mr Kluever and Mr Allers in the initial attempts by Glasfit to purchase the shares in the taxpayer, commencing in November 2002, must be examined in the context of their knowledge that the taxpayer had a large assessed loss of approximately R90 million and had ceased trading at the end of June 2002. It is also significant that these negotiations commenced after SDM had exercised its option to purchase the shares on 19 September 2002, but before it had purchased them on 5 March 2003.

[35] Various calculations were then made by Mr Kluever and Mr Allers to formulate an offer by Glasfit to purchase the shares in the taxpayer from SDM. That

Glasfit was extremely interested in purchasing the taxpayer, although it had not traded since the end of June 2002, is clear from the wide range of offers Glasfit made to SDM in the period between November and March 2003. In all of these offers, the largest percentage was allocated to the value of the potential tax shield. Offers were made of R2.2 million with a potential tax shield valued at R1.6 million, R4.8 million with a potential tax shield valued at R4 million and R10.726 million with a potential tax shield valued at R5 million. This clearly illustrates that the taxpayer's large assessed loss which SDM had conveniently carried over into the 2003 tax year, must have been of paramount importance to Glasfit.

[36] According to Mr Kluever, SDM did not accept these offers because SDM believed they substantially undervalued the taxpayer. Mr Allers stated the negotiations ceased in March 2003, because no progress was being made. However, on 27 February 2003 an email was sent by Mr Evans of B Digital, which recorded it was agreed that the sale of the shares in the taxpayer to SDM was to go ahead on the basis of the attached agreement and Mr Lloyd was planning to bring the business back into the taxpayer's 'company shell'. Mr Evans also recorded the taxpayer would be a going concern at the time the agreement was signed.

[37] Mr Benatar agreed that the significance of these statements lay in the application of s 20 of the Act, with the object of ensuring the assessed loss was carried over to the next tax year. That this was their objective, was confirmed in a further email from Mr Evans on 28 February 2003, in which he stated that the acquisition of the shares allowed SDM the opportunity to utilise approximately R16 million in assessed loss. Consequently, on the eve of negotiations apparently breaking down, steps were being taken by SDM to ensure the preservation of the assessed loss in the taxpayer. Mr Allers, however, maintained it was his interest in the call centre of the taxpayer in Cape Town that had not gone away after negotiations ceased in March 2003.

[38] The formal agreement (referred to by Mr Evans in his email) in which SDM acquired the shares in the taxpayer for a purchase price of R0,01, was signed on 5 March 2003. Although the shares had been acquired the business of the taxpayer was still located in SDM. A further agreement was therefore concluded on 7 May

2003 between SDM and the taxpayer, for the sale of the business back to the taxpayer for an amount of R1 million, being the amount paid by SDM to purchase the business in the first place. Mr Benatar agreed that after the implementation of the sale of the assets, over and above any value there was in the litigation with MTN (which in any event would only benefit B Digital), there was no value left in the taxpayer. The business had come to a standstill, it was deprived of its operating assets, no longer had premises from which to operate its business and there were no remaining employees.

[39] The purpose of SDM in acquiring the shares in the taxpayer and thereafter transferring the business back to the taxpayer, must therefore have been to ensure the taxpayer was a going concern as at the end of June 2003, in order to satisfy the requirements of s 20 of the Act. This goal having been achieved, the taxpayer again ceased trading at the end of June 2003, in the same manner and with the same goal as it had ceased trading at the end of June 2002. The result was that the assessed loss in the taxpayer was not only preserved by SDM, but was increased whilst under its control during the period 5 March 2003 to 30 September 2003, by R21 115 220.

[40] Of significance in this regard is that in March 2003 Mr Allers had no commitment from PG Glass to participate in the venture, although Glasfit and PG Glass had been in discussions for a long time. Consequently, a purchase by Glasfit of the shares in the taxpayer in March 2003 would have been premature and may have exposed Glasfit to proceeding on its own, when it was clear the participation of PG Glass was essential for the success of the venture. The relevant role players were all posturing with the objective of the utilisation of the assessed loss by the taxpayer.

[41] The negotiations between Glasfit and PG Glass continued and resulted in a memorandum of understanding being concluded between them on 3 September 2003, which provided for the venture. Both parties contemplated the formation of a new company and the establishment of a consolidated call centre from which the venture would be conducted, owned by the new company and operated from new premises.

[42] Mr Allers and Mr Kluever maintained that because the memorandum of understanding required a new company to be structured, this was the reason for their decision in September 2003 that discussions with SDM should be revived. The more probable reason was the commitment of PG Glass had been secured and the taxpayer with its large assessed loss was needed to house the venture. The reason for this conclusion is found in the evidence of Mr Kluever that the venture between Glasfit and PG Glass was an extremely ambitious undertaking, with great strategic and execution risk to Glasfit, which held the promise of significant profit if it could be completed successfully. It was a challenging and difficult project to complete and the participation of PG Glass was essential to its success. The large assessed loss would inevitably be a valuable safety net for the venture in the crucial early stages of its development, by the immunisation of any profits from tax when its success would be particularly vulnerable.

[43] Of particular significance is the fact that there was no evidence that SDM negotiated with any other parties for the sale of the shares in the taxpayer after the negotiations allegedly broke down, until they were resumed with Glasfit in November 2003. It is improbable that SDM would not have attempted to sell the taxpayer in the interim, if the negotiations with Glasfit had genuinely broken down. On the contrary, the conduct of SDM during this period was directed at preserving the assessed loss, by ensuring it was carried over to the following tax year. On the probabilities, the object in maintaining that negotiations had broken down must have been to prevent an inference being drawn that the conduct of SDM in preserving the assessed loss was to benefit Glasfit. This conclusion is supported by the improbability of Mr Allers being prepared to lose the opportunity of utilising the large assessed loss in the taxpayer, by allowing the negotiations to fail. Significantly, shortly after the negotiations were allegedly resumed in September 2003, agreement was reached between SDM and Glasfit for the sale of the shares in the taxpayer at a vastly reduced purchase price.

[44] The oft repeated evidence of Mr Allers and Mr Kluever that the purpose in buying the shares in the taxpayer was the acquisition of the Cape Town call centre, and not the opportunity to utilise the assessed loss to avoid liability for the payment of tax, is grossly improbable for several reasons. The first is that it is clear from the

minutes of the steering committee set up by Glasfit to manage the venture, that at no stage was the possibility of the consolidated call centre being located in Cape Town discussed. The attempt by Mr Allers and Mr De Clercq to suggest otherwise was disingenuous.

[45] The second reason is that Mr Allers agreed that in the memorandum of understanding the idea was to initially move the two separate call centres of Glasfit and PG Glass into one entity, in one location, which would have included staff who were all based in Johannesburg. He agreed that at the beginning of September 2003 the idea would have been to create the new premises in Johannesburg. This would be consistent with his concession that the views of PG Glass weighed heavily as to where the premises of the consolidated call centre would be located. In fact the view of PG Glass in this regard was recorded, albeit indirectly, in the minutes of the steering committee on 13 October 2003. PG Glass stated it was concerned about the distance and traffic problems for PG Glass staff, if Bryanston was to be the location of its new premises. It is therefore self-evident that PG Glass would never have agreed to the consolidated call centre being located in Cape Town and Mr Allers must have known this.

[46] The third reason is that the facilities at the Cape Town call centre were not suitable for the venture envisaged by Mr Allers. Although Mr Kluever maintained that after visiting the Cape Town call centre at an early stage of his due diligence study of the taxpayer he concluded the call centre would be suitable for the venture, it was only on 19 November 2003 that it was ascertained that the computers at the Cape Town call centre did not have the required specifications and could not be used. In short, much of the existing equipment was technically obsolete. If the main focus from the outset was to acquire the Cape Town call centre for the venture, it is improbable this would only have been properly investigated and discovered at such a late stage.

[47] As pointed out above, shortly after the negotiations were allegedly resumed between SDM and Glasfit, SDM offered the sale of the shares in the taxpayer to Glasfit for R3.68 million which was accepted on 3 October 2003 and the sale agreement was concluded on 25 November 2003. There was no evidence that

during these negotiations any other offers were made and rejected, despite SDM rejecting the previous offer of R10 726 000 made on 14 January 2003 because SDM believed the offer substantially undervalued the taxpayer. In the light of the evidence of Mr Benatar that the value of the assets in the taxpayer were substantially higher than the purchase price, and the evidence of Mr Kluever that he regarded the sale price as a bargain, extensive negotiations must have preceded the conclusion of this agreement. The absence of any evidence on this issue, fortifies the conclusion that it is improbable the negotiations broke down in March 2003.

[48] The repeated attempts by Mr Allers and Mr Kluever to diminish the importance of the tax loss in the taxpayer, by steadfastly maintaining the assessed loss only affected the value to be offered for the taxpayer, were not only disingenuous, but were also cogent evidence of what their real purpose was in acquiring the shares in the taxpayer. Mr Kluever went so far as to claim there was essentially zero value in the assessed loss, but it was 'possible' it could be set-off against some future income. This statement was inconsistent with the concession made by Mr Allers, that the larger percentage of the offers made by Glasfit were allocated to the potential tax shield. It was also inconsistent with the evidence that prior to the approval of the sale by the board of Glasfit, Mr Kluever had advised the board that the taxpayer had an estimated tax loss of R100 million, which could provide a temporary tax shield for the business. In addition, Mr Kluever had on 27 October 2003 requested the annual financial statements for the taxpayer for the year ended 30 June 2003, in which the assessed loss was quantified. Mr Benatar agreed the production of these financial statements paved the way for the conclusion of the agreement, because they reflected what the accounting loss was.

[49] The justifiable concern of Mr Kluever that the Commissioner may seek to apply s 103 of the Act to the intended acquisition by SDM of the shares in the taxpayer, as well as any subsequent acquisition by Glasfit of these shares from SDM, did not, however, result in Glasfit being advised by him not to proceed with the transaction, despite the risk. Simply put, the huge benefit to Glasfit in utilising the loss in the taxpayer to avoid liability for the payment of tax, made the risk worthwhile.

[50] An objective review of all the relevant facts and circumstances is required in order to determine the motive, purpose and intention of SDM in acquiring the shares in the taxpayer. The direct evidence of Mr Benatar that the purpose of SDM in purchasing the shares in the taxpayer, was to provide services to the cellular provider Cell C with the object of making a profit, falls to be rejected when weighed and tested against the probabilities and inferences to be drawn from the established facts, set out above. For the same reasons the evidence of Mr Allers and Mr Kluever that the purpose of Glasfit in purchasing the shares in taxpayer, was to acquire the Cape Town call centre for the venture, also falls to be rejected. In both the first and second acquisition of the shares in the taxpayer, the sole or at the very least the main purpose of SDM and Glasfit respectively in purchasing the shares, was to utilise the assessed loss by setting it off against income to be received by the taxpayer in the ensuing tax years, in order to avoid liability for the payment of tax on such income. Mr Benatar, Mr Lloyd, Mr Kluever and Mr Allers were intimately involved in all the dealings from inception. All the related transactions were structured so as to enable the utilisation of the assessed loss ultimately by Glasfit or its nominee.

[51] The taxpayer therefore failed to discharge the onus of proving that the first change in shareholding when SDM purchased the shares in the taxpayer, was not effected solely or mainly for this prohibited purpose. The court a quo accordingly erred in directing its attention to the second acquisition of the shares in the taxpayer by Glasfit, in order to determine whether the purpose requirement of s 103(2) of the Act, had been satisfied.

[52] I turn to consider the further requirement of s 103(2) of the Act, namely whether the first change in shareholding in the taxpayer when SDM acquired the shares, had the direct or indirect result that income was received by, or accrued to the taxpayer, during any year of assessment.

[53] The taxpayer submitted that the income that was received by the taxpayer after the second change in shareholding when Glasfit purchased the shares in the taxpayer from SDM, was beyond the reach of s 103(2) of the Act, because this income did not result directly or indirectly from the first change in shareholding. The

income against which the assessed loss was set-off by the taxpayer in the 2004 to 2008 tax years, resulted directly or indirectly from the second change in shareholding, upon which the Commissioner could not rely. The Commissioner's response was that if this was so, taxpayer companies could simply artificially effect more than one change in shareholding to circumvent the provisions of s 103(2) of the Act. It was submitted that to permit this would be contrary to the principle that the subsection should be considered in a manner that advances the remedy and suppresses 'trafficking' in shares of companies, with assessed losses.

[54] The tax court and the court a quo concluded that the first change in shareholding did not directly or indirectly result in income being received by, or accruing to the taxpayer. The tax court reasoned that the income was derived not from the first change in shareholding, but from a later intervening event, being the second change in shareholding and the income was not contemplated at the time when SDM acquired the shares. It noted that the breaking of the chain of causation was referred to in delictual cases as a *nova causa interveniens*. Accordingly, so it reasoned, the income was not the 'result' of the first change in shareholding. The court a quo was even more explicit in its reliance upon the delictual test of causation, concluding that although the first change in shareholding may have been the *sine qua non* of the receipt of income by the taxpayer, it was not the *causa causans*. It was the second change in shareholding that was the effective cause.

[55] In *Tuck v Commissioner for Inland Revenue* 1988 (3) SA 819 (A) at 833B, Corbett JA stated that:

'I am not sure that it is appropriate to apply the principles of causation, as developed particularly in the criminal law and the delictual field, when considering the problem as to how, from the income tax point of view, a taxpayer's receipt should be characterised, ie whether as income or as capital.'

Although the reservation was expressed in a different factual context it is equally applicable on the facts of the present case.

[56] The subsection provides that the change in shareholding must result, directly or indirectly, in income being received by, or accruing to the taxpayer, during *any* year of assessment. It is therefore clear that the direct or indirect receipt of income

by the taxpayer, does not have to occur in the same tax year as the change in shareholding of the taxpayer. It may occur in any year of assessment, provided it results directly or indirectly from the change in shareholding.

[57] In ITC 1123 (1968) 31 SATC 48 (T), it was held whether income has been received by, or accrued to a company 'as a direct or indirect result' of the change in shareholding, is a question of fact. Consequently, whether the second change in shareholding precludes a finding that the income received by the taxpayer resulted directly or indirectly from the first change in shareholding, is an issue of fact which will have to be resolved on a consideration of the evidence.

[58] As pointed out in *Conshu* supra at 610G-I, the subsection was enacted to prevent such 'trafficking' in the form of new proprietors attaching themselves to the company and injecting new income into it, in order to exploit the assessed loss. In my view, the second change in shareholding would preclude a finding that the income in question resulted directly from the first change in shareholding. It would not, however, preclude a finding that the income resulted indirectly from the first change in shareholding. The conclusion that SDM purchased the shares in the taxpayer with the sole, or at the very least, the main purpose, of utilising the assessed loss to avoid liability on the part of the taxpayer for the payment of tax in the following tax years, must have had as its objective, the enablement of Glasfit to utilise the assessed loss for the same prohibited purpose. On the unique facts of this case, it would be artificial to ignore this objective when determining whether this income received by the taxpayer, resulted indirectly from the first change in shareholding.

[59] As pointed out by the Commissioner, the extent to which Glasfit was able to 'attach' itself to the taxpayer and 'inject' income from the venture located in the consolidated call centre into the taxpayer, which would otherwise have been earned by and taxed in the hands of Glasfit, is graphically illustrated by the following table. In addition, it shows that the Cape Town call centre after the second acquisition of shares in the taxpayer by Glasfit, made a loss in the 2004 and 2006 years and in the remaining years only contributed a small part of the taxable income.

1	2	3	4	5	6	7
YEAR END	TAXABLE INCOME/(LOSS) GAUTENG & CAPE TOWN	GAUTENG PORTION	CAPE TOWN PORTION	ASSESSED LOSS BROUGHT FORWARD	TAXABLE INCOME UTILISING ASSESSED LOSS	TAX PAID
2003 SDM	(18,242,495)		(18,242,495)	67 208 019	0	0
2004 Glasfit group	11,733,145	12 608 893	(875 748)	85 450 514	0	0
2005	15,207,187	13 883 028	1 324 159	73 717 369	0	0
2006	16,022,433	17 302 774	(1 280 341)	58 510 182	0	0
2007	27,723,657	27 538 720	184 937	42 487 749	0	0
2008	28,570,709	27 334 773	1 235 936	14 764 092	13 806 617	3 865 852
Total	99 257 131	98 668 188	588 943		13 806 617	

[60] Column 3 shows that by 'attaching' itself to the taxpayer, Glasfit 'injected' a total sum of R98 668 188 into the taxpayer from 2004 to 2008, enabling it to utilise the existing R85 450 514 assessed loss in the taxpayer when Glasfit acquired the shares in the 2004 tax year. Column 4 shows that during the period 2004-2008, the Cape Town call centre only generated R588 943 taxable income.

[61] The first change in shareholding therefore resulted indirectly in income being received by or accruing to the taxpayer during the 2005 to 2008 years of assessment. The Commissioner was accordingly correct in concluding that the provisions of s 103(2) of the Act were satisfied and in disallowing the taxpayer's claim to set-off the assessed loss against such income, during these years of assessment. The appeal therefore succeeds.

[62] The following order is granted:

- 1 The appeal succeeds with costs, including the costs of two counsel.
- 2 The order of the court a quo is set aside and replaced with the following order:
 - ‘(a) The appeal succeeds with costs, including the costs of two counsel.
 - (b) The order of the tax court is set aside and replaced with the following order:
“The appeal is dismissed and the assessments which form the subject of this appeal are confirmed”.’

K G B Swain
Judge of Appeal

Appearances:

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